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INTERNATIONAL DEVELOPMENT ASSOCIATION

PROJECT APPRAISAL DOCUMENT

ON A

PROPOSED CREDIT

IN THE AMOUNT OF (SDRXX) MILLION

US\$ 20 MILLION EQUIVALENT

TO

REPUBLIC OF CABO VERDE

FOR A

SOE RELATED FISCAL MANAGEMENT PROJECT

May 3, 2018

Governance Global Practice
Africa Region

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Currency Equivalents

(Exchange Rate Effective as of April 30, 2018)

Currency Unit = Cabo Verdean Escudo

US\$1.00 = CVEXXX

Weights and Measures

Metric System

Fiscal Year

January 1 – December 31

ABBREVIATIONS AND ACRONYMS

ASA	Airport Security Administration (<i>Agência de Segurança Aeroportuária</i>)
BCV	Central Bank of Cabo Verde (<i>Banco de Cabo Verde</i>)
BSG	Budget Support Group
CEM	Country Economic Memorandum
CVE	Cabo Verdean Escudos
DB	Doing Business
DGA	General Directorate of Environment
DNP	National Directorate of Planning (<i>Direção Nacional de Planejamento</i>)
EIA	Environmental Impact Assessment
ELECTRA	Public Water and Electricity Company (<i>Empresa de Electricidade e Água</i>)
ENAPOR	National Port Authority (<i>Empresa Nacional de Administração dos Portos</i>)
ESW	Economic and Sector Work
EU	European Union
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
GNI	Gross National Income
GPRSP	Growth and Poverty Reduction Strategy Paper
IATA	International Air Transport Association
IBRD	International Bank for Reconstruction and Development
IDA	International Development Association
IE	Road Management Agency (<i>Instituto de Estradas</i>)
IFH	Real Estate and Housing Fund (<i>Imobiliária Fundiária e Habitat</i>)
IFRS	International Financial Reporting Standards
IMF	International Monetary Fund
M&E	Monitoring and Evaluation
MDG	Millennium Development Goal
MoF	Ministry of Finance and Planning
MIC	Middle-income Country
MoU	Memorandum of Understanding
NIS	National Investment System
PBMC	Performance Based Management contract
PBMtC	Performance Based Maintenance contract

PDO	Program Development Objective
PEMFAR	Public Expenditure Management and Financial Accountability Review
PFM	Public Financial Management
PIP	Public Investment Program
PPP	Public Private Partnership
PRSC	Poverty Reduction Support Credit
SDR	Special Drawing Rights
SIGOF	Integrated Budget and Financial Management System (<i>Sistema Integrado de Gestão Orçamental e Financeira</i>)
SOE	State-Owned Enterprises
SPE	State Services Participation (<i>Serviço de Participações do Estado</i>)
TACV	Cabo Verde Airlines (<i>Transportes Aéreos de Cabo Verde</i>)
TBC	Tax Benefits Code
TVET	Technical and Vocational Education and Training
UASE	Unidade de Acompanhamento do Sector Empresarial do Estado
UGPE	Unidade de Gestão de Projectos Especiais
UN	United Nations
VAT	Value-Added Tax

Regional Vice President: **Makhtar Diop**
Country Director: **Louise Cord**
Senior Global Practice Director: **Deborah Wetzel**
Practice Manager: **Alexandre Arrobbio**
Task Team Leader(s): **Kjetil Hansen, Rohan Longmore**



Note to Task Teams: The following sections are system generated and can only be edited online in the Portal.

BASIC INFORMATION

Is this a regionally tagged project? No	Country(ies)	Financing Instrument Investment Project Financing
<input type="checkbox"/> Situations of Urgent Need of Assistance or Capacity Constraints <input type="checkbox"/> Financial Intermediaries <input type="checkbox"/> Series of Projects		
Approval Date 31-May-2018	Closing Date	Environmental Assessment Category C - Not Required
Bank/IFC Collaboration No		

Proposed Development Objective(s)

The Project Development Objective is to strengthen SOE related fiscal management.

Components

Component Name	Cost (US\$, millions)
Component 1: Results-Based Financing	16.00
Component 2: Technical Assistance	4.00

Organizations

Borrower :	Republic of Cabo Verde
Implementing Agency :	Ministry of Finance

PROJECT FINANCING DATA (US\$, Millions)

**The World Bank**

Cabo Verde SOE Related Fiscal Management Project (P160796)

<input type="checkbox"/> Counterpart Funding	<input type="checkbox"/> IBRD	<input checked="" type="checkbox"/> IDA Credit	<input type="checkbox"/> IDA Grant	<input type="checkbox"/> Trust Funds	<input type="checkbox"/> Parallel Financing
Total Project Cost: 20.00	Total Financing: 20.00		Financing Gap: 0.00		
	Of Which Bank Financing (IBRD/IDA): 20.00				

Financing (in US\$, millions)

Financing Source	Amount
International Development Association (IDA)	20.00
Total	20.00

Expected Disbursements (in US\$, millions)

Fiscal Year	2018	2019	2020	2021	2022	2023
Annual	14.40	1.30	1.30	1.00	1.00	1.00
Cumulative	14.40	15.70	17.00	18.00	19.00	20.00

INSTITUTIONAL DATA**Practice Area (Lead)**

Governance

Contributing Practice Areas

Macroeconomics, Trade and Investment

Transport & Digital Development

Social, Urban, Rural and Resilience Global Practice



Climate Change and Disaster Screening

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

Gender Tag

Does the project plan to undertake any of the following?

a. Analysis to identify Project-relevant gaps between males and females, especially in light of country gaps identified through SCD and CPF

No

b. Specific action(s) to address the gender gaps identified in (a) and/or to improve women or men's empowerment

No

c. Include Indicators in results framework to monitor outcomes from actions identified in (b)

No

SYSTEMATIC OPERATIONS RISK-RATING TOOL (SORT)

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

COMPLIANCE

Policy

Does the project depart from the CPF in content or in other significant respects?

Yes No



Does the project require any waivers of Bank policies?

Yes No

Safeguard Policies Triggered by the Project

Yes No

Environmental Assessment OP/BP 4.01		✓
Natural Habitats OP/BP 4.04		✓
Forests OP/BP 4.36		✓
Pest Management OP 4.09		✓
Physical Cultural Resources OP/BP 4.11		✓
Indigenous Peoples OP/BP 4.10		✓
Involuntary Resettlement OP/BP 4.12		✓
Safety of Dams OP/BP 4.37		✓
Projects on International Waterways OP/BP 7.50		✓
Projects in Disputed Areas OP/BP 7.60		✓

Legal Covenants

Conditions

PROJECT TEAM

Bank Staff

Name	Role	Specialization	Unit
Kjetil Hansen	Team Leader(ADM Responsible)		GGOAC
Rohan Longmore	Team Leader		GMTA2
Mamata Tiendrebeogo	Procurement Specialist(ADM Responsible)		GGOPF
Laurent Mehdi Brito	Procurement Specialist		GGOPF
Maimouna Mbow Fam	Financial Management Specialist		GGOAW



Alexandra C. Bezeredi	Social Safeguards Specialist		GSU01
Andre Herzog	Team Member		GSU13
Charles E. Schlumberger	Team Member		GTD08
Daniel P. Owen	Social Safeguards Specialist	Retrenchment	GSU01
Fanny Weiner	Peer Reviewer		GGOEP
Henri Fortin	Peer Reviewer		GGOAC
Herimpamonjy Mavoarisoa Ranaivoarivelo	Team Member		GGOAC
Mbaye Mbengue Faye	Social Safeguards Specialist		GSU07
Medou Lo	Environmental Safeguards Specialist		GEN07
Roland N. Clarke	Peer Reviewer		GGOLP
Sofia De Abreu Ferreira	Counsel		LEGEN
Yoko Kagawa	Team Member		GGOAW
Extended Team			
Name	Title	Organization	Location
Edson Medina	Consultant		Cabo Verde



CABO VERDE
CABO VERDE SOE REFORM PROJECT

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I. STRATEGIC CONTEXT

A. Country Context

1. **Cabo Verde has made substantial development progress since independence and is currently the 9th richest country in Sub-Saharan Africa (SSA).** In 2017 its gross national product per capita was US\$ 3277, almost six times what it was in 1982. Anchored in stable political institutions, the country's economic performance is attributable to significant investment in infrastructure linked to the promotion of the country as a tourist destination. Cabo Verde is renowned for its political freedom, rule of law, year-round attractive climate and rich culture. Diaspora remittances which approximated 11.0 percent of GDP in 2017, have been an important part of the success story providing a lifeline to segments of the population, and allowing the lower-middle income country to sustain its high consumption rate and to finance a large trade deficit. Cabo Verde has one of the highest Country Policy and Institutional Assessment score (3.7 in 2017) among IDA countries which shows the strength of its institutions.

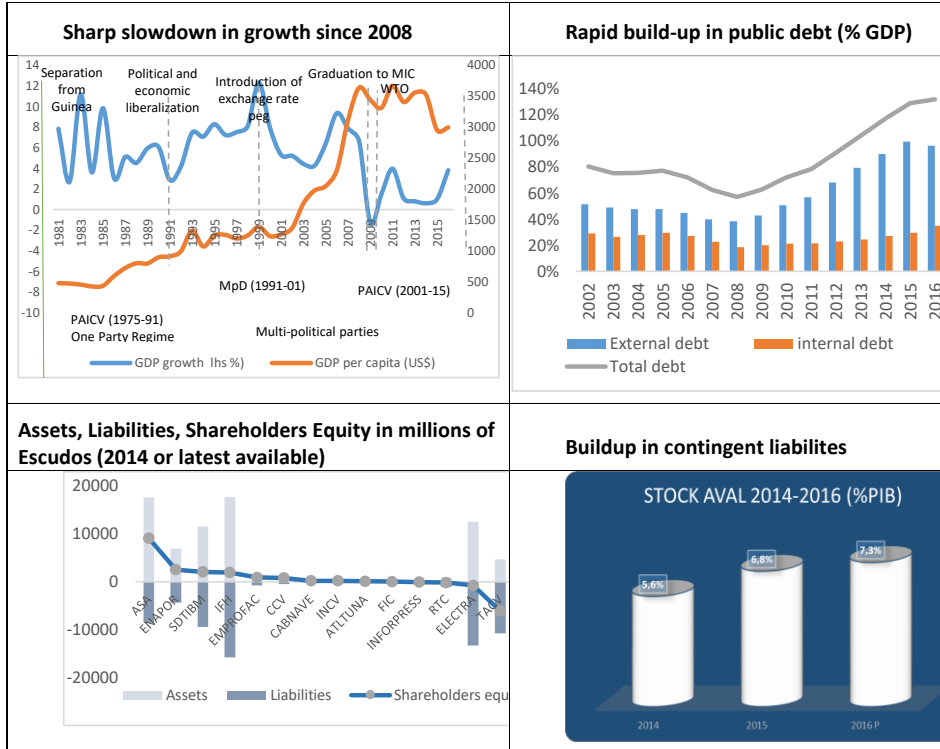
2. **The country also witnessed a sustained decline in the number of poor and has high human capital achievements.** The incidence of poverty fell from 58 percent in 2001 to 35 percent in 2015 while extreme poverty dropped from 30 percent to 10 percent during this period¹. Cabo Verde outperforms its peers on most non-monetary dimensions of poverty including life expectancy, maternal mortality, net primary school enrolment, and access to an improved water source. At 73, life expectancy at birth is – together with Mauritius and Seychelles - the highest of Sub-Saharan Africa. Solid performance has been demonstrated for different health indicators (infant mortality rate, proportion of births attended by skilled health staff - although Anemia prevalence is relatively high²), education (primary school completion), providing piped water to premises and expanding coverage of the electricity network. Access to electricity rose from around 50 percent of households in 1999 to 98 percent today.

3. **Growth has collapsed since 2008 as the economy was hit hard by the global financial and the European sovereign debt crises, and the associated fiscal response has led to a rapid build-up in debt.** Notwithstanding a pickup in growth in 2016 (3.8 percent), the economy struggled to reach average growth of 1.5 percent per annum between 2009 and 2016. The economy expanded at an annual rate of approximately 7 percent between 1990 and 2008. The deceleration in growth since 2008 was primarily attributed to lower private investments as capital spending by the government increased for the first 5 years after the crisis³. There was also a marked decline in the efficiency of investments. Taking advantage of available concessional financing, the government decided to increase public investments to create jobs, address infrastructure bottlenecks and lay the foundations for future growth. In this context, total public sector debt increased from 68 percent of GDP in 2008 to approximately 130 percent of GDP in 2016. The rise in debt is also closely linked to operations in the poorly performing state-owned enterprise sector (SOEs), which implemented a number of government projects.

¹ Extreme poverty, using PPP US\$ 1.9 per day, halved between 2001 and 2007 (from 16 to 8 percent in 2007). Preliminary estimates, using the 2015 household expenditure survey, suggest the extreme poverty rate based on PPP US\$ 1.9 per day is already below 3 percent (the benchmark for eradication).

² Anemia prevalence in 2011 was 61% among children under 5 children close to the average for SSA, higher than its structural peers (other lower middle income countries). No recent data for malnutrition are available.

³ Gross fixed capital formation dropped from 38.5 percent of GDP in 2009 to a low of 30 percent in 2013.



Source: Ministry of Finance and World Development Indicators

4. **Adjusting the country’s development model to restore fiscal sustainability requires urgent actions to address public sector imbalances and multiple public financial management issues.** The development model which underpinned the country’s remarkable growth run leading up to the crisis and the global circumstances are now much less favorable and subject to high downside risks. Productivity levels are falling and the country is at high risk of debt distress. Strains from the SOEs sector have become a burden on the fiscal, in particular key loss-making public enterprises. Although the government has undertaken several initiatives including the introduction of performance based contracts for selected SOEs to strengthen the management of these entities and ultimately safeguard overall public sector balances, several fundamental issues remain. This include, among other things, the need for right-sizing or rationalizing insolvent entities, reporting and proactively managing fiscal risks in the SOEs portfolio, improving budgeting processes and control over public expenditure and debt management reforms.

5. **A new administration took office in June 2016 and presented a plan which emphasized the gradual reduction of the budget deficit and a progressive decline in the debt-to-GDP ratio⁴ over the**

⁴ While the government undertook real efforts to contain expenditures (bringing the fiscal deficit to 3.5 percent), total financing needs scaled 7.5 percent in 2016, reflecting unprogrammed demands from the SOE sector. Preliminary information suggests that



medium-term as central to the country's development progress. The government's plan is also elaborated in the recently approved Strategic Plan for Sustainable Development (PEDs) 2017-2021. This is expected to be achieved through the implementation of an ambitious program of reforms structured around a few strategic pillars including: i) ensuring economic sustainability; ii) promoting fiscal efficiency and budget consolidation; and iii) accelerating the public-sector reform agenda. Accordingly, the government's program with the World Bank focuses on stabilizing the economy by reinforcing fiscal discipline, strengthening institutions that facilitate its capacity to manage and control the debt-generating process, as well as improving the environment for greater private sector participation in the economy.

B. Sectoral and Institutional Context

6. **The 2013 Country Economic Memorandum (CEM) concluded that there was an urgent need for the government of Cabo Verde to strengthen fiscal management.** This included recommendations for the adoption of a strong program of fiscal consolidation to curb increasing indebtedness. Significant indebtedness of the SOE sector has also become a significant source of fiscal risks, thereby exacerbating medium-term vulnerabilities. This has been further aggravated by relatively weak macro-fiscal and debt management practices. Accordingly, accelerating and deepening the process of fiscal risk management requires urgent reforms in the SOEs sector supported by institutional strengthening on macroeconomic management and SOE oversight.

7. **The SOEs sector in Cabo Verde has long been a source of high risk contingent liabilities for the government due to their generally weak commercial and financial performance.** There are thirty-two SOEs in the country with the state holding over 50 percent equity share in twenty-two, 20-30 percent share in three and 10 percent or less in the remaining seven entities⁵. These entities operate under the commercial code, their founding legislation and the 2016 framework SOE Law⁶. SOEs in Cabo Verde are tasked with the responsibility of providing many essential services, including in economically strategic areas such as transport, water, electricity and financial services. The largest SOEs by assets and turnover are ELECTRA (electricity utility), ASA (airports management), TACV (airline), ENAPOR (port), and IFH (housing). The five largest enterprises account for 80 percent of state-owned capital⁷ and hold assets equivalent to 40 percent of GDP as of end 2016. While the performance of SOEs vary, on aggregate, the portfolio has been loss-making and the stock of debt has increased. The biggest contributors to these losses in the last three years were TACV and IFH. In 2016, the state provided explicit guarantees for SOE commercial loans equal to 7.3 percent of GDP, up from 5.6 percent of GDP in 2014. The total debt stock for the three largest SOE reached 34 percent of GDP in 2016 (US\$550M), with the largest debt held by IFH (US\$225M), followed by ELECTRA (US\$192M) and TACV (US\$134M).

8. **Some SOEs have 'technically' defaulted on debt service obligations requiring government assistance through emergency loans and /or recapitalizations** (often through the conversion of direct payments on behalf of SOEs to some of their creditors). TACV is the most critical risk in the short term, given that it poses the largest burden on the budget and continues to need financial support from government. The latest report on contingent liabilities by the Treasury (2016) classifies debt held by TACV

debt levels (which were 130 percent at the end of 2016) have climbed to 136 percent of GDP in 2017, as pressures from the SOE sector remain elevated

⁵ See Annex 5 for the complete list of SOEs and detailed discussions on two large SOEs with the highest risk profile.

⁶ Law 47/VII/2009

⁷ The state's total capital share of these SOEs was CV12.1 billion in 2010 (9 percent of GDP), 70 percent of the enterprises total capital.



as high risk given its operational and financial performance and profitability prospects in the short to medium (Ministry of Finance 2017). IFH has also requested direct support from the authorities to deal with its cash flow problems⁸. Persistent losses for TACV and IFH are covered by financial transfers, guarantees and or accumulating arrears with providers. In some cases, the entities are also allowed to contract debt without guarantees. Therefore, the effective contingent liabilities generated are much higher than the SOE debt officially guaranteed by the state. The government simply does not have the capacity to continue bailing out loss making SOEs, and urgently need to put in place measures to improve their operational and financial performance to reduce their fiscal burden.

9. **The situation in the SOE portfolio is underpinned by a weak corporate governance environment.** While the authorities have introduced legislative⁹ and institutional changes to strengthen the role of the government in SOE management, significant weaknesses remain. This includes continued gaps in the legal/regulatory framework, and a lack of compliance with current laws. On the policy and legal framework side, there is room for further clarifying the objectives of state ownership, strengthening the disclosure and reporting obligations of SOEs through accompanying regulation. Enforcement of existing laws is weak and should be strengthened, starting with strengthening the state's capacity to act as an informed and proactive owner. Board and management practices could be strengthened to minimize political appointments in favor of bringing in needed technical expertise. Several of the large SOEs have signed performance contracts with the government. However, the challenge has been in ensuring timely reporting and evaluation of the agreements, and a lack of application of sanctions for non-performance. Despite an explicit requirement for companies to report regularly on their commitments and targets, such monitoring is sporadic, and companies do not face any consequences for non-compliance.

10. **Improving SOE monitoring and oversight has become a priority.** The unit assigned to the oversight of the SOEs within the Ministry of Finance (UASE) is also in charge of public private partnerships and privatization (PPPP). There is widespread deficiency in available monitoring instruments, such as updated SOE accounts, strategic plans, budgets and quarterly reports. The unit is currently receiving support through the World Bank transport project to improve its monitoring system. In order to strengthen the state as an owner, the unit also needs senior in-house technical expertise to provide independent and authoritative analytical advice on SOE business plans and performance. Limited capacity in government has meant that insolvent SOEs continue to operate, increasing their debt levels and demands on the budget. The situation reached a critical level in 2016, with two large SOEs becoming insolvent, requiring direct support from central government to cover operational cost (TACV and IFH). The challenge for the government is to gain some control of the situation and take urgent decisions on difficult but necessary SOE reforms to minimize the fiscal impact. For this to happen, the government needs to become a more active owner, with the capacity to form its own opinion of SOE performance and necessary reforms based on high quality technical analysis on SOE performance. On this basis, the

⁸ IFH manages a large social housing project (*Casa Para Todos*) financed out of a EUR 160 million credit line from Portugal.

⁹ The legal framework for SOEs was strengthened in early 2016, notably it (i) clarifies and broadens its scope of coverage to all categories of SOEs, including those owned by Municipalities; (ii) provides clearer guidance and limits on SOE debt, including the need for SOEs to outline debt plans as part of their annual budget and business planning process which is subject to approval by the authorities; (iii) calls for stronger sanctions for non-compliance with reporting obligations of the SOEs to the state, where failure to comply now provides justification for dismissal of senior management; (iv) introduces new articles (art. 33 and 34) on the Transformation/Fusion and Liquidation of SOEs. The reporting responsibilities of SOEs to the state have been slightly expanded beyond standard financial reporting to include detailed information on company corporate governance, including the frequency of board meetings and selection and remuneration of senior management and board members.



government needs to exercise its ownership in a more proactive manner in SOE boards and as ultimate shareholder of these companies.

11. **TACV has been identified as the SOE with the most urgent risk to the state from a contingent liability perspective.** Profitability has been a challenge since the end of the 1990s, and despite many attempts at restructuring and privatization, results continue to deteriorate. A number of studies and restructuring plans have been prepared but with recommendations only partially implemented, if not ignored or abandoned altogether. The latest round of studies, including work conducted and commissioned by the World Bank since early 2016. All studies concluded that TACV is insolvent and recommended that the authorities move quickly to cut costs and accelerate its search for suitable alternatives to eliminate the need for support from the budget. The financial situation of TACV has continued to deteriorate, culminating in the repossession of one of the two jet aircraft (B737) from the lessor in early 2016. The airline has posted losses in every year except in 2014 due to the one-off sale of its ground handling unit to ASA. The net loss for 2015 was close to US\$36.7 million (2.3 percent of GDP) and losses for 2016 and 2017 were just over US\$24 million in both years (1.3 percent of GDP). As a result of increasing debt and a reduction in assets from the sale and lease back of its planes, the net value (shareholders' equity) was negative and continued to decrease, reaching a negative US\$97 million as of end 2016.

12. Pressed by the deteriorating fiscal situation, the government has initiated an ambitious plan to restructure and possibly privatize TACV, based around three strategic priorities:

- (i) **Withdrawal from the domestic and regional airline market.** In November 2016, an MOU was signed with a local private sector company which resulted in the gradual withdrawal of TACV from the domestic and regional airline business. This took place between April and August, 2017 when the last of their two aircrafts was returned to the lessor. The staff associated with all domestic operations will be retrenched (207 staff – a close to half of total staff), and government has secured bridge funding for the cost of the retrenchment (US\$15 million). The withdrawal from local operations has led to substantial cost savings.
- (ii) **Restructuring and privatization of the remaining international business.** The Government of Cape Verde (GoCV) has signed a management contract with Icelandair, which includes the hiring of a CEO, the provision of two aircrafts under a long-term lease and the option for Icelandair to acquire 51 percent of TACV at a future date. The new CEO started working in August 2017, and a new business plan was prepared and approved by both boards of TACV and Icelandair in October 2017. The business plan includes establishing TACV as a hub operator in Cabo Verde, serving initially 25 destinations (Europe: 10, USA: 5, South America: 6, and West-Africa: 4). Icelandair has carried out a detailed route analysis and found that yields are strong enough to reach a positive cashflow and profitable operations by 2019. GoCV is now searching for a strategic partner to take on a majority stake in the airline by April 27, 2018, and is planning to gradually divest its shares entirely.
- (iii) **Debt restructuring:** the authorities have contracted external expertise to renegotiate and restructure the debt of TACV, which is currently estimated at €89 million (US\$103 million). The strategy consists primarily of creating a claim resolution company (CRC), backed by government guarantees, that would acquire most commercial debt of TACV from creditors at a discount.



13. **The first component of this strategy has already been achieved.** A private operator (*Binter Cabo Verde*) is now covering all islands and plans are advancing for the regional connections with Dakar and Bissau. The remaining two components are under implementation. A staff retrenchment plan has been prepared with support from the World Bank and was finalized in early March 2018. The viability of the privatization strategy or liquidation depends on TACV's ability to attract private investors. The government has announced that there will be no government support in the form of guarantees, subsidies or other types of contingent liabilities to finance the proposed business plan¹⁰. Debt restructuring, which is being supported by outside expertise, is already leading to a reduction in debt and liabilities.

C. Higher Level Objectives to which the Project Contributes

14. **The proposed support for strengthening SOEs and fiscal risks management mirrors the two complementary pillars of the Country Partnership Strategy (CPS) of the World Bank Group (WBG),** covering the years 2014-2017 (Report No. 92248-CV): (a) enhancing macro-fiscal stability, setting the foundations for renewed growth; and (b) improving competitiveness and private sector development. The proposed operation, which part of a broader program, supports the objectives of Pillar 1 which includes specific targets on reducing GoCV lending to SOEs (from 8.8 percent of GDP in 2013 to 6.7 percent in 2017) and increasing accountability for results in select SOEs. The operation is complemented by a Development Policy Financing (DPF) operation focused on policy reforms to improve fiscal management including key SOEs and debt management (Component 2) is specifically designed to build capacity in select reform areas targeted by the DPF operation.

15. **The operation is also consistent with the country's recently approved Strategic Plan for Sustainable Development (2017-2021).** The plan envisages improved monitoring of SOEs as well as a program of sustained fiscal consolidation including rationalization of government investments and entities either through divestiture, PPPs and or concession arrangements. The program also includes structural fiscal reforms focused on improving public financial management and the budget process as well as debt management. The associated spinoff from fiscal consolidation, including policy credibility and increased domestic resources could become available to help bolster growth over time.

16. **The Bank has a long history of support to SOE reform in Cabo Verde through numerous operations¹¹.** The recently concluded series of Poverty Reduction Credits VIII and IX (2013 to 2015) supported a number of SOE reforms including TACV, ELECTRA and ENAPOR as well as overall risk management of contingent liabilities by the Treasury. The ongoing Transport Project is providing technical assistance to strengthen transport sector SOEs and the Bank is also assisting with the preparation of a monitoring system for the SOE unit. Building on this past support, the proposed investment lending (IPF) operation will consolidate many of the reforms and take them further. It will also lay the ground for future budget support by the Bank and other donors who are currently unable to move ahead with their support due to concerns over elevated macroeconomic risks in the SOEs sector.

17. **The choice of an IPF with disbursement-linked indicators for the proposed operation can be justified** by the following expected benefits: (i) combining with the planned development policy financing operation to provide a meaningful incentive to undertake structural reforms by disbursing against agreed

¹⁰ The government has accepted to cover TACV's debts and liabilities stemming from activities prior to the approval of the new business plan (October 2017), including restructuring costs associated with retrenchment.

¹¹ See Annex 5 for a brief history of reforms in TACV and Electra



results, (ii) building on and reinforcing existing capacities in government to undertake politically sensitive reforms, particularly retrenchment and (iii) strengthening coordination with other development partners in supporting similar yet complementary programs and reforms in an area of recognized Bank comparative advantage. The choice of IPF with DLIs is also appropriate for a country which needs capacity strengthening to develop a well-defined results framework for its own SOE reform program, as it will help the government establish clear targets and mechanism to improve monitoring.

II. PROJECT DEVELOPMENT OBJECTIVES

A. PDO

The Project Development Objective is to strengthen SOE related fiscal management.

B. Project Beneficiaries

Direct beneficiaries of the project will be the Government of Cabo Verde through capacity strengthening for improved monitoring and reporting on SOE financial and operational performance. This increased capacity will empower the authorities and stimulate reforms to improve SOE performance and reduce the need for state support. Other beneficiaries include all users of public services as a result of possible improvement in the quality of services in targeted SOEs.

C. PDO-Level Results Indicators

PDO Indicator 1: Reduced public financing to SOEs (including budgeted and un-budgeted transfers and subsidies from the budget, capitalization and guarantees)

PDO Indicator 2: Improved operating margin of TACV

PDO Indicator 3: Increased public revenues from SOEs (tax payments, dividends concession payments and proceeds from divestment)

III. PROJECT DESCRIPTION

A. Project Components

18. The project consists of two complementary components: (i) Component 1: Results-Based Financing (US\$16 million) will provide incentives for achieving results in two distinct areas: staff retrenchment in the national airline (TACV); and reduced public financing for the airline's operations, and (ii) Component 2: Technical assistance (US\$4 million) to support the GoCV in several technical areas related to the reforms under Component 1. Component 1 will disburse against agreed eligible expenditure programs (EEPs) upon achievement of Disbursement Linked Indicators (DLIs).

19. **Component 1: Results-Based Financing (US\$16 million).** This component aims to support some critical reforms in TACV that are needed to improve performance and prepare the company for privatization and thereby eliminate their needs for public financing for their operations. The



component will also support the central SOE unit to improve their monitoring of the SOEs in their portfolio, including a closer assessment of financial and operational performance and SOE related fiscal risks. (for more details about activities and expected results see Annex 2).

- *Sub-component 1.1. TACV Restructuring and Reduced Public Financing:* This sub-component aims to reduce the financial bleeding of TACV through a series of restructuring actions including a company HR reconfiguration and retrenchment of 207 staff leading to an improvement in the company’s operating margin; and (ii) reduced public financing for TACVs operations in the form of guarantees, capital transfers or direct payments to creditors resulting from other cost cutting measures.
- *Sub-component 1.2. Fiscal Risk Assessment and Monitoring:* Preparation of comprehensive annual reports on the entire SOE portfolio by the central SOE unit, including analysis of company performance, contributions by SOEs to the economy through taxes and dividends and a complete overview of government support to SOEs through subsidies, guarantees, recapitalizations, loans, etc.;

Disbursement-Linked Indicators (DLIs) and Eligible Expenditure Programs (EEPs)

Target	Amount Allocated (million US\$)	Payment Schedule
DLI 1. Retrenchment plan approved and announced by TACV	3	July 15, 2018
DLI 2. Grievance mechanism established	3	July 15, 2018
DLI 3: Staff targeted by the retrenchment plan is retrenched	8	Scalable DLI
DLI 4: Detailed Annual SOE reports	2	Scalable DLI
	16	

1. **Eligible Expenditure Programs (EEPs).** A preliminary analysis of the program budget identified the following EEPs as suitable for project financing: salary, wages, retrenchment benefits, training, operating costs.



Identified EEPs						
EEP Budgets	Description	2018	2019	2020	2020	2021
<i>Sub-component 1.1. TACV Restructuring and Reduced Public Financing</i>	TACV: Salaries, Social Security Contributions, Retrenchment Packages, Training, Small Grants	14 US\$ Million				
<i>Sub-component 1.2. Fiscal Risk Assessment and Monitoring</i>	UASE: Salaries, TA, Operating costs, training	0.4 US\$ million	0.4 US\$ million	0.4 US\$ million	0.4 US\$ million	0.4 US\$ million
Total		14.4	0.4	0.4	0.4	0.4

Component 2: Technical Assistance (US\$4 million): This component will provide support for the preparation and implementation of the government SOE reform program and to strengthen the Ministry of Finance’s overall capacity for macro-fiscal monitoring and SOE oversight and monitoring. It aims to strengthen the GOCV’s capacity as an active and informed owner of SOEs, including its ability to independently analyze and assess SOE activities, operational and financial performance, business plans, audits, and to prepare comprehensive and in-depth analytical reports on the SOE portfolio under its purview and ability to increase private sector participation in SOEs. This set of actions is an essential element of the state’s ability to better manage the fiscal risk posed by SOEs from repeated ad-hoc requests for guarantees, recapitalizations and loans. Eligible expenditure under this component are consulting and non-consulting services, acquisition of goods and operating costs.

- *Sub-component 2.1. Improved SOE related fiscal management:*
 - Improve the technical capacity of the ownership unit (UASE) to closely monitor SOE financial and operational performance through the preparation of an analytical annual SOE report;
 - Training and development of tools for UASE staff with the objective of assessing the realism/quality of proposals and reports presented by SOEs (including business plans, performance agreements, HR restructuring plans), and to carry out SOE performance benchmarking with the objective to inform government decisions regarding approvals of recapitalizations, divestiture, etc;



- Carry out a review of the SOE sector including individual company valuations to identify possibilities for further divestment of the SOE portfolio;
 - Review of current ownership arrangements with a view to identify opportunities to further strengthen portfolio management;
 - Support to develop a communications strategy for SOE restructuring/reforms; and
 - Support to a long-term non-resident technical advisor in UASE
 - Technical assistance for improved macroeconomic monitoring, reporting and use of macroeconomic modelling and econometric tools;
 - Technical assistance to improve budget credibility through better revenue and expenditure forecasting; and
 - Technical assistance for a strengthened legal and debt management framework, including contingent liabilities.
 - Technical assistance to strengthen the Unit’s capacity to identify, launch and negotiate public private partnerships.
- *Sub-component 2.2. Improved corporate governance of SOEs:*
 - Technical assistance for the drafting of complementary regulations to the framework SOE legislation (law 47/2009);
 - Technical assistance for preparation of a SOE policy setting out the government’s objectives with regard to each sector and SOE operating in that sector, including minimum performance standards, dividend policy, subsidies, etc.;
 - Technical assistance for the development of guidance material and standards for board members, including a manual and tools for target setting, performance evaluation, etc; and
 - Training program for SOE board members based on good international practice and tools developed under above activity (ie training on financial analysis, role of board members, performance evaluation, etc).
 - *Sub-component 2.3: Project Management and Just-in-time Technical Assistance.* This sub-component would support project implementation needs including the financing of the project audit and independent verification agent. It will also finance some activities that are not included or anticipated in the original design of the project, but are necessary elements as the project unfolds. Providing flexibility, this sub-component will fill in the needs as related to the objective of the project, and to be adaptable in providing a continuous stream of support to the GoCV. It could include technical assistance to implement activities identified in ongoing or planned studies including fiscal risks associated with debts transferred from SOEs to municipalities, and or issues in debt or SOE management.

B. Project Cost and Financing

Project Components	Project cost	IBRD or IDA Financing	Trust Funds	Counterpart Funding
Total Costs				



Total Project Costs	20	20
Front End Fees		
Total Financing Required	20	20

C. Lessons Learned and Reflected in the Project Design

2. **Past efforts at fiscal consolidation and strengthening SOE management have only partly succeeded because of structural weaknesses inherent in public financial management policies and processes and the underlying political dynamics of public sector reforms in Cabo Verde.** The Government of Cabo Verde is aware of the limitations and is pursuing an ambitious reform program for strengthening SOEs oversight and management to support its overall public sector and fiscal management reform. The design of the proposed project reflects the lessons learned from previous and ongoing projects in Cabo Verde, particularly those from the Transport Sector Reform project, which includes a component for increased efficiency of transport SOEs. This project has a performance based component which has had a positive influence for the GOCV. The main lesson is to ensure clear and irreversible government reforms before providing any support, as such clarity and timeliness has reduced the necessity and urgency of difficult reforms in the past.

3. **Project ownership needs to be demonstrated.** Attempts to overhaul transport sector SOEs, including TACV, have faced many challenges mainly due to a difficult political economy context whereby reforms are faced strong opposition. While the project preparation provided rigorous diagnostics and analytical work necessary for a strategic approach, financial commitment was put on hold until the first phase of restructuring and possible privatization was achieved, e.g., TACV’s withdrawal from the domestic and regional air market.

4. **Better monitoring and motivating performance have long been primary goals of SOE reform.** This requires a strong unit, whose members are capable of analyzing SOE performance and forming their own opinions, which then can inform government about necessary reforms or changes to bring to SOE management and boards. The project will therefore focus on building the needed technical and institutional capacity of the unit responsible for the SOEs oversight at the MoF, which is a critical condition for the enhancement of the GoCV’s control over its SOEs and the reduction of fiscal risks associated to the SOEs financial performance. Technical assistance will also be provided to organize review meetings with relevant stakeholders to discuss the implications and findings in order to facilitate reform ideas or action plans.

5. **Workforce rightsizing is an important factor in delivering improved efficiency for TACV.** For the restructuring process to deliver its objectives of improving the efficiency of the company, it will be important to move forward in a fair and consistent way, with firm targets for employment rightsizing and adequate plans for the process and support to affected workers. Careful measures to mitigate any adverse effects associated with retrenchment is necessary. The Bank task team will collaborate with the UASE during the implementation phase and will provide support necessary to implement actions recommended by the PSIA.

6. **Overly broad and ambitious reform agendas on politically complex issues such as SOE reforms are risky and likely to fail.** The project therefore focuses on a few areas of impact for better targeting of



results. Particularly, linking the results with disbursements will foster difficult reforms which might be affected by vested interest. Additionally, the project activities include a communication strategy, geared towards both SOE employees and public at large.

7. **Lessons learned include the need for significant implementation support and advancing key preparatory activities to mitigate institutional capacity constraints.** This was undertaken as part of the extensive preparatory process involving several studies and technical assistance in the form of resident technical advisors to work with the government in terms of advancing with a plan to reform TACV. Preparation of the relevant social safeguard documents has followed a similar consultative approach, which has generated strong buy-in and support from key stakeholders.

IV. IMPLEMENTATION

A. Institutional and Implementation Arrangements

8. **UASE, established within the MoF in 2016, is the lead implementing agency.** The UASE will serve as the Project Implementation Unit (PIU), overseeing the day-to-day management of the project. It is responsible for technical inputs, coordination among participating entities, reporting on results and liaising with the World Bank. The UGPE, a central PIU which manages several other World Bank operations will be responsible for ensuring compliance with the Bank's financial management, procurement regulations and safeguard requirements, and reporting to the Bank on a timely manner.

9. **The UGPE's is managing several other World Bank projects and its capacity has been assessed adequate to assume its role as a PIU.** The financial management capacity developed under these projects is adequate to meet the World Bank's requirements. The UGPE FM staff comprises of an experienced financial management specialist and two accountants familiar with Bank fiduciary procedures. The overall performance of the ongoing projects management by UGPE is "Satisfactory". Staffing has remained adequate and proper books of accounts and supporting documents have been kept in respect of all expenditures. UGPE is familiar with the World Bank FM requirements

10. **Given the political importance of reforms in TACV the government has established a Privatization Team** which is inter-ministerial in nature and include members from ministries and institutions involved in the management of the planned reforms. The technical team is supported by the State Business Sector Monitoring Unit and answer to a small ministerial steering committee.

11. **Project Steering Committee (PSC).** To ensure proper coordination and supervision of the project, a PSC will be established to provide strategic guidance and oversight. The Minister of Finance or his designate will co-chair the PSC with the Minister of Economy, and including representatives from TACV and others as necessary (i.e. staff union SOEs, Regulatory agencies). The Project Director will serve as secretary to the committee. This committee will meet biannually and will review the annual progress report.

B. Results Monitoring and Evaluation

For the purposes of project monitoring, the Government and the World Bank have agreed on a Results Framework that comprises three Project Development Objectives and five Intermediate Results Indicators. The Results Framework defines the indicators and the institutional arrangements for data collection. The UASE has the overall responsibility and coordinating role in M&E of the program. The



Bank implementation support missions will undertake periodic evaluation of implementing M&E arrangements to verify that adequate systems are in place to generate the information needed for project reporting. The progress report will be submitted biannually in conjunction with the World Bank's implementation support missions.

12. **Four DLIs will be used to measure the achievement of agreed targets and will be the basis for disbursement of project financing.** The DLIs will be monitored as part of the overall project results monitoring arrangements by the UASE. To ensure independence of the verification process, the UASE will contract a third party to support the verification process, on terms of reference acceptable to the Bank.

C. Sustainability

13. **It is expected that the reforms supported by the project and the complementary DPF operation will have a lasting impact on the government's exposure to TACV liabilities.** While other SOEs have significant liabilities (notably IFH and Electra), dealing with TACV is a first-order priority given its poor performance and operational financing needs (which far surpasses the other SOEs in recent years--up to 2% of GDP in transfers to TACV whereas other SOEs have not required transfers for operational needs). The government's stated commitment to stop any further support to the airline for its operations is a strong indication that the supported activities will be sustainable. The sustainability of the impact on TACV's future operational costs are less certain, as these depends on the activities of any possible new private owners.

D. Role of Partners

14. **The Bank has an established a close coordination with other development partners in Cabo Verde, mainly through the budget support group (BSG).** The proposed activities to be supported through the project build on and is complementary to reforms supported by other development partners. The African Development Bank (AfDB) is currently supporting the PPP unit for its privatization program. In addition, both AfDB and the EU's budget support has prior actions/conditions related to SOE reforms. Several rounds of consultations with other donors suggest that SOE reforms is an area where development partners look to the Bank for leadership. Close continued collaboration with these partners during project preparation will ensure that various interventions are complementary and properly coordinated.

V. KEY RISKS

A. Overall Risk Rating and Explanation of Key Risks

15. The overall risk to the project is **Substantial**.

16. **Political risks are High:** The government in power since June 2016 has clearly indicated greater private sector involvement in the economy as a priority. This is also reflected in their political program. Prior to elections in May, 2016, they had identified several SOEs as targets for drastic reforms, including TACV, ELECTRA and IFH. However, well connected SOEs such as TACV have in the past been able to block or simply ignore important reforms and restructuring programs. Given this past history of failed reforms, political interference remains a substantial risk to the success of this operation. In order to mitigate this risk, the Bank has supported the authorities in developing a communication strategy and plan to clearly explain to the public and all stakeholders the rationale, objectives and scope for the planned restructurings.



17. **Macroeconomic risk is High.** Economic growth is picking up but the economy remains highly susceptible to shocks. Additionally, high public debt constrains the government's ability to respond to unforeseen events. The nascent recovery in growth is also likely to limit private sector participation in government divestment efforts which could have adverse implication for the project's development objectives. Macroeconomic imbalances could further reduce the risk appetite of potential investors. This risk is mitigated by the macroeconomic reform program undertaken by the government with support from its international development partners including the planned programmatic DPF series.

18. **Institutional Capacity for Implementation and Sustainability risks are Substantial:** These risks relate to the capacity of the SOE unit to proactively lead the reform process and engage the targeted SOEs to undertake agreed reforms in a timely manner. Low technical capacity and a lack of proactivity has let SOEs themselves set the pace for reforms in the past, but with the establishment of a relatively strong SOE unit there are signs of a modest change in the willingness of the PPPP/SOE unit to impose itself and set expectations. As noted above, the government has recently established a new SOE unit and strengthened the unit's status, which should help mitigate technical risks. In addition, the contracting of technical assistance will strengthen their capacity. The TA will be complemented by in-house Bank expertise to provide targeted support on Air transport, Housing, Macro-Fiscal and Debt Management.

19. **Environmental and Social Risks are Substantial:** The Program could experience social risks due to resistance from labor unions with respect to the initial retrenchment and possible full liquidation of TACV. Past efforts at staff reductions in TACV have been unsuccessful due to the lobbying and political power of the unions. These risks will be mitigated by dialogue with labor unions following national practices and legislation. Legal and HR expertise is being provided to the company, including in their dealings with unions.

20. **Stakeholder Risks are Substantial:** The key ministers in charge of the main SOEs targeted for reforms are fairly recent and are still in the learning phase, but have made clear commitments to the SOE reform agenda outlined above. TACV has a newly appointed management team and board in place and employees have been informed of the government's intentions. There is broad agreement between the World Bank and government, as well as within government, on the reforms necessary. Significant technical support has already been provided by the Bank in order to inform the reform options with strong involvement of the national counterparts. However, as with the political risks outlined above, stakeholder risks relate to the ability in the past of TACV to ignore, block or reverse reforms.

21. **Other risks related to Government M&E capacity are Substantial:** While government capacity to monitor risks related to SOE performance and contingent liabilities is relatively low, it has increased recently. The government now has a series of instruments at their disposal to facilitate monitoring – including existing performance agreements with agreed targets and sanctions for non-compliance. The main challenge related to ensuring sufficient follow up and monitoring is technical capacity, but this will be provided to the authorities through technical assistance. Another challenge is a cultural aversion to impose sanctions for non-compliance, although the presence of negotiated targets and agreed sanctions in performance agreements should help overcome this challenge.



VI. APPRAISAL SUMMARY

A. Economic and Financial Analysis

22. A costs-benefits analysis has been undertaken for the identified retrenchment of staff of TACV.

The reform of the cash strapped enterprise, which discontinued its ATR business in August 2017, is estimated at US\$15.2 million. A total of 207 staff will be retrenched. The economic costs and benefits of the project have been determined by comparing the economic impact of implementing the project to a situation without the project. To arrive at conservative overall economic evaluation of this component (85 percent of total retrenchment plan costs), it is assumed that the cost of staff to be retrenched under the TACV program would be the same irrespective of whether the project is implemented.

23. The economic benefit of the implementation of the operation is derived from the savings realized by having reduced the staff of TACV, and ultimately, reduced likelihood for support from the state budget.

This is also seen as an initial step towards restructuring the enterprise for an eventual privatization or liquidation. The costs to be covered by the project will be limited to cost of retrenchment of all categories of staff, retraining programs, access to social assistance where appropriate and associated fees¹². This is approximately US\$13.2 million. The economic results of the project are robust. The calculated internal return rate is 12 percent with the company generating a net benefit of US\$10 million over 10 years. Using a discount rate of 3 percent - which is a good proxy for the cost of capital in a country where credit is largely external and mostly at concessional terms - the Net Present Value (NPV) is US\$6.6 million. A sensitivity analysis was performed. A 20 percent increase in the cost of retrenchment and 20 percent decrease were evaluated. Under these assumptions, the project remains viable. In the case of higher costs, the internal rate of return falls to 7 percent and the NPV to US\$3.6 million. With lower costs, the rate of return and the NPV are 19 percent and US\$9.5 million, respectively. These results are very satisfactory, especially given the conservative basis on which they have been built.

24. In addition, there is significant additional value added in World Bank support to such a delicate and politically sensitive reform.

Specifically, the value added of a World Bank project in support of SOE Fiscal Risk management comes from several sources including (i) the significant technical knowledge of the World Bank related to SOE fiscal risks in general, and related TACV reforms, given the Bank's long history of engagement on this issue in Cabo Verde (ii) the confidence generated from the involvement of the World Bank in this process, and (iii) the convening and coordinating power of the World Bank, which has been important throughout the joint donor-government dialogue on SOE reforms over the last several years.

B. Technical

25. The government's SOE reform program has not been finalized, but some reforms have been agreed on as necessary to be implemented immediately, in particular, the strengthening of the government's capacity for SOE portfolio management and the cost cutting and restructuring of the national airline given that the latter has the most immediate impact on the government budget. These measures build on sound technical analysis and advice prepared over an extended period particularly related to the national airline and social housing where several studies have been carried out. Support in

¹² It is assumed that approximately 105 staff will benefit from training and an additional 130 individuals will have access to social assistance.



the Macro-Fiscal area builds on continuous World Bank engagement including recent AAA work (CEM, PEMFAR) and a recent PEFA.

26. **The World Bank's contribution is focused on a set of immediate short-term measures on which there is broad political and technical agreement to move forward, beginning with a retrenchment program of the national airline that will reduce staffing by approximately one half and generate significant savings.** The project aims to influence the evolving government program through supporting these immediate actions, setting the stage for more ambitious medium-term reforms through the technical support and accompanying dialogue with the government and SOE stakeholders. Movement on these reforms would open the door for further support from the bank and other donors once the government commits to move further on reforms and clearly communicate these decisions. The interventions supported by this project draw on lessons learned and international standards related to SOE monitoring and reforms as well as previous experience in Cabo Verde in these same areas.

C. Financial Management

27. **The financial management arrangements will be based on the existing arrangements under *Unidade de Gestão de Projetos Especiais (UGPE)*, which is implementing the following ongoing projects:** Competitiveness for Tourism Development Project (P146666); Recovery and Reform of the Electricity Sector Project (P115464); and Distributed Solar Energy Systems (P151979). The financial management capacity developed under these projects is adequate to meet the World Bank's requirements. The UGPE FM staff comprises of an experienced financial management specialist and two accountants familiar with Bank fiduciary procedures

28. **The overall performance of the ongoing projects management by UGPE is "Satisfactory".** Staffing has remained adequate and proper books of accounts and supporting documents have been kept in respect of all expenditures. UGPE is familiar with the World Bank FM requirements. The interim unaudited financial reports for the on-going project are also submitted on time and acceptable to IDA as well as the audited financial statements.

29. **In order to accommodate the project in the existing financial management system and ensure an adequate segregation of duties, the following measures should be taken three months after effectiveness:** (i) the update of the existing project implementation manual of UGPE including financial management procedures; (ii) the customization of the existing accounting software to include the bookkeeping of the project and generate interim financial reports and financial statements; (iii) the appointment of an additional accountant and (iv) the recruitment of an external auditor and an independent verification agent.

30. **A third party will be contracted to verify the EEP Spending and Results Reports.** The independent verification agent will issue an opinion on the accuracy and fair view of the information presented by the UASE on the EEP and DLIs. This certificate should be sent to the World Bank directly by the independent verification agent. In addition, the TACV's external audit reports together with Management Letter should be submitted to the World Bank within six months after the end of the TACV's each fiscal year

D. Procurement

31. **The Borrower will carry out procurement for the proposed project in accordance with the World Bank's "Procurement Regulations for IPF Borrowers" (Procurement Regulations) dated July 2016 under**



the “New Procurement Framework” (NPF), and the “Guidelines on Preventing and Combating Fraud and Corruption in Projects Financed by IBRD Loans and IDA Credits and Grants”, dated October 15, 2006 and revised in January 2011, and other provisions stipulated in the Financing Agreement.

32. **The *Unidade de Acompanhamento do Sector Empresarial do Estado* – (UASE), in charge of SOE Monitoring and Oversight Unit, shall carry out the procurement under the project.** It was created in 2016 with the merger of the Privatization and Public-private Partnership Unit and SOE Department. The former PPP Unit was financed by the Government of Cabo Verde, the African Development Bank, and Investment Climate Facility. With technical assistance from the AfDB and ICF, the Unit carried out international tenders for technical assistance in large transactions such as the process for the sub-concession of the main ports of Cabo Verde and the Cabnavé Shipyard. So, the Unit was responsible for managing all procurement processes, in accordance with national law, international best practices, and AfDB procurement guidelines, for all the projects in its pipeline. UASE and its staff have experience in preparing bidding documents such as Terms of References, Request for Proposals, and bid proposal evaluation reports as well as managing disbursement/payment processes.

Comentado [M/U/E-NMG1]: The UGPE shall carry out the Procurement under the Project

33. **However, this project will be implemented under the new Bank Regulations for Borrowers dated July 2016 and bring additional workload on the team.** There are risks of: i) Additional workload due to the proposed project; ii) The manual of procedures doesn't consider the project. The following measures are proposed to mitigate these risks and reduce their classification from substantial to moderate: i) hire a Procurement Specialist on a full-time basis and train the staff on the NPF; ii) update the manual of procedures to consider the project and develop Project Implementation Manual (PIM).

34. **As part of the preparation of the project, the Borrower prepared the Project Procurement Strategies for Development (PPSD) which describes how procurement activities will support project operations for the achievement of project development objectives and deliver Value for Money (VfM).** The procurement strategies are linked to the project implementation strategy and the state levels ensuring proper sequencing of activities. They consider institutional arrangements for procurement; roles and responsibilities; thresholds, procurement methods, and prior review; and the requirements for carrying out procurement. They also include a detailed assessment and description of state government capacity for carrying out procurement and managing contract implementation, within an acceptable governance structure and accountability framework. Other issues considered include the behaviors, trends and capabilities of the market (i.e. market analysis) to respond to the procurement plan.

35. The procuring entity, the bidders, and service providers (i.e. suppliers, contractors and consultants) shall observe the highest standard of ethics during the procurement and execution of contracts financed under the project in accordance with paragraph 3.32 and Annex IV of the Procurement Regulations. A detailed description of procurement and institutional arrangements can be found in Annex 3.

E. Social (including Safeguards)

36. **Retrenchment:** The most significant social issue relates to the workforce reduction in TACV. The target for retrenchment under the project is 207 workers, equivalent to just under one half of total employees (459). The project will finance eligible severance payments and associated measures to mitigate risks arising from loss of employment. The company has prepared an overall Retrenchment Plan to identify staff categories to be reduced and approximate costs for labor restructuring.



37. Workforce rightsizing is likely to have adverse distributional and social impacts in the short run, though the overall poverty impact is expected to be mitigated since compensation measures will be in place, comprising severance packages for retrenched workers.

38. The retrenchment process will comply with local labor regulations and respective Collective Agreements and their provisions for redundancy (severance) payments and formulas for calculation, established on the basis of negotiations with the unions. The TACV Retrenchment Plan has been drafted using as a basis of the aforementioned regulations and agreements, as well as good international practice guidance on responsible retrenchment aimed at ensuring a fair and transparent process and satisfactory mitigation measures. The Retrenchment Plan describes the retrenchment process to be followed, including the legal framework, retrenchment methods and procedures, management arrangements and monitoring, grievance redress mechanisms, the basis for calculation of benefits, associated mitigation measures such as training, alternative livelihood support, etc. and communication and M&E frameworks to be adopted. Clear principles for non-discriminatory processes for identifying redundancies and corresponding grievance redress mechanisms are described in the Retrenchment Plan.

39. The Retrenchment Plan is a living document that will be updated accordingly as necessary during implementation and identifies aspects of the retrenchment process and program that will be subject to monitoring and reporting for the Bank's due diligence purposes.

40. A **Poverty and Social Impact Analysis (PSIA)** has been prepared, to assess the social, economic and distributional impacts of the TACV restructuring and retrenchment. The analysis has assessed the loss of livelihoods and income-generating opportunities and the channels available to support alternative livelihood for retrenched workers, such as labor market reintegration, job transfer or retraining. It has also explored the indirect non-material losses associated with losing employment and the potential channels available for compensating these and addressing adverse welfare impacts of job shedding. The analysis has captured the characteristics of two categories of workers being made redundant – those assigned under pre-retirement and a second group classified around mutually agreed separation compacts. Potential disproportionate impact or targeting of women for dismissal has been included in the scope of the PSIA. The overall conclusion findings of the PSIA suggest that, with provision of suggested livelihood support interventions, the social and economic impacts of the retrenchment exercise is likely to be positive.

41. The PSIA methodology has been established around quantitative and qualitative research approaches, including focus group and key informant interviewing and will serve as a platform for Citizen Engagement outreach for the project. It is recommended that an update of the PSIA be carried out at the project mid-term.

F. Environment (including Safeguards)

42. **The project is classified as Category C.** The proposed project does not trigger any of the World Bank's safeguards polices. Since the project will primarily focus on building institutional capacity through TA and advisory support, the project will not require any social and environmental assessment.



G. Other Safeguard Policies (if applicable)

H. World Bank Grievance Redress

43. **Communities and individuals who believe that they are adversely affected as a result of a Bank supported operation, as defined by the applicable policy and procedures, may submit complaints to the existing program grievance redress mechanism or the WB's Grievance Redress Service (GRS).** The GRS ensures that complaints received are promptly reviewed in order to address pertinent concerns. Affected communities and individuals may submit their complaint to the WB's independent Inspection Panel which determines whether harm occurred, or could occur, as a result of WB non-compliance with its policies and procedures. Complaints may be submitted at any time after concerns have been brought directly to the World Bank's attention, and Bank Management has been given an opportunity to respond. For information on how to submit complaints to the World Bank's corporate Grievance Redress Service (GRS), please visit <http://www.worldbank.org/GRS>. For information on how to submit complaints to the World Bank Inspection Panel, please visit www.inspectionpanel.org.

44. Furthermore, within the aegis of the retrenchment plans incorporated under Component 1: Results-Based Financing, Sub-component 1.2. TACV Restructuring and Reduced Public Financing, design, organization and governance of a Grievance Redress Mechanism specifically oriented to the retrenchment process is included in the TACV Retrenchment Plan.



Note to Task Teams: The following sections are system generated and can only be edited online in the Portal.

Results Framework
COUNTRY : Cabo Verde
SOE Related Fiscal Management Project

Project Development Objectives

The Project Development Objective is to strengthen SOE related fiscal management.

Project Development Objective Indicators

Indicator Name	Core	Unit of Measure	Baseline	End Target	Frequency	Data Source/Methodology	Responsibility for Data Collection
Name: Reduced public financing to SOEs - including transfer from the budget and capitalization (in million USD)		Amount(USD)	30.00	0.00	Annually	Budget expenditure reports	UASE and Treasury
Description: Measured by transfers from the Government budget to SOEs for their operations, including subsidies, capital injections, loans, arrears, and any payments made on behalf of SOEs to creditors, and government guarantees for loans contracted by SOEs							
Name: Improved operating margin of TACV		Percentage	144.00	80.00	Annually	Financial Reports submitted by TACV	TACV and UASE



Indicator Name	Core	Unit of Measure	Baseline	End Target	Frequency	Data Source/Methodology	Responsibility for Data Collection
Description: Measured by the operational costs as a percentage of operating revenues as reported in audited annual financial statements by TACV							
Name: Annual public revenues from SOEs (Millions USD - in tax payments, dividends, concession payments, divestment proceeds)		Amount(USD)	5.00	10.00	Annually	Government budget execution reports	UASE and Treasury
Description: Measured by transfers and payments from SOE related activities to the government, such as taxes and dividends paid by SOEs, and proceeds from the sale or divestment of SOE shares or concession payments by private operators in areas previously controlled by SOEs (ports, airports)							

Intermediate Results Indicators

Indicator Name	Core	Unit of Measure	Baseline	End Target	Frequency	Data Source/Methodology	Responsibility for Data Collection
Name: IRI1: Comprehensive SOE policy adopted		Text	Current (2016) SOE framework law outlines general rules for corporate governance of SOEs and	The government adopts a policy on SOEs including clear performance targets and transparen	One Time	Ministry of Finance/Council of Ministers	UASE



Indicator Name	Core	Unit of Measure	Baseline	End Target	Frequency	Data Source/Methodology	Responsibility for Data Collection
			government oversight and reporting	cy obligations of SOEs			
<p>Description: A government policy document approved by the Council of Ministers. The policy should clearly outline the strategic objectives of individual SOEs, including any relevant performance targets, as well as clear corporate governance and transparency and reporting standards of SOEs as well as of government.</p>							
Name: IRI2: Implementation and utilization of the SOE financial database		Text	UASE operates general excel sheet with basic aggregated information on six (6) largest SOEs	Database with complete financial and operational performance information on the entire SOE portfolio	One Time	Ministry of Finance	UASE
<p>Description: The SOE financial database is a web-based monitoring tool that will permit the exchange of information between SOEs and UASE. The tool will allow SOEs themselves to upload or update information. Part of the website will also be made public.</p>							
Name: IRI3: Strengthened legal framework for debt management with a greater emphasis on contingent liabilities		Text	Fragmented debt management legislative	A clear legal framework that is respected	One Time	Ministry of Finance	UASE



Indicator Name	Core	Unit of Measure	Baseline	End Target	Frequency	Data Source/Methodology	Responsibility for Data Collection
			framework	by SOEs and Government			
Description: As measured by the delivery of draft regulations related to (i) the implementation of the SOE framework law and a draft law on (ii) debt management							
Name: IRI4: Review of SOE Portfolio and structuring oversight/holding of SOEs		Text	Some individual performance reviews carried out as part of performance agreement preparations	Greater clarity on SOEs that need to be restructured, sold or partially privatized	One Time	Ministry of Finance	UASE
Description: As measured by a review of the SOE portfolio with a view to identify companies to be restructured and/or sold. The review will also examine the institutional set up for SOE oversight and monitoring and make recommendations for strengthening the current arrangements							
Name: IRI5: Fiscal risk monitoring reports on SOE portfolio published		Text	Annual report on contingent liabilities from 6 largest SOEs with	Comprehensive reports on all SOEs published on MoF's web site including	Annually	UASE Annual SOE Report	UASE



Indicator Name	Core	Unit of Measure	Baseline	End Target	Frequency	Data Source/Methodology	Responsibility for Data Collection
			rudimental profit/loss information	analysis of financial and operational performance (including, benchmarking) and all financial transfers with the state (including all transfers, arrears, implicit subsidies, etc.)			
<p>Description: Measured by the number of annual reports on SOEs. Salient features of the SOE Annual reports include a complete overview of SOE net performance during the previous year, include net profit/loss, dividends paid, subsidies received, taxes paid, arrears and outstanding debt including contingent liabilities. Reports should be issued no later than one year after the period reported on.</p>							



Target Values

Project Development Objective Indicators

Indicator Name	Baseline	YR1	YR2	YR3	YR4	YR5	End Target
Reduced public financing to SOEs - including transfer from the budget and capitalization (in million USD)	30.00	15.00	10.00	5.00	2.00	0.00	0.00
Improved operating margin of TACV	144.00	120.00	100.00	90.00	80.00	80.00	80.00
Annual public revenues from SOEs (Millions USD - in tax payments, dividends, concession payments, divestment proceeds)	5.00	6.00	7.00	8.00	9.00	10.00	10.00

Intermediate Results Indicators

Indicator Name	Baseline	YR1	YR2	YR3	YR4	End Target
IR11: Comprehensive SOE policy adopted	Current (2016) SOE framework law outlines general rules for corporate governance of SOEs and government oversight and reporting	Draft SOE Policy Prepared	SOE Policy adopted by council of Ministers			The government adopts a policy on SOEs including clear performance targets and transparency obligations of SOEs



Indicator Name	Baseline	YR1	YR2	YR3	YR4	End Target
IRI2: Implementation and utilization of the SOE financial database	UASE operates general excel sheet with basic aggregated information on six (6) largest SOEs	Pilot database prepared and tested	Database finalized and rolled out to include all SOEs	Database used for SOE monitoring and preparation of annual report		Database with complete financial and operational performance information on the entire SOE portfolio
IRI3: Strengthened legal framework for debt management with a greater emphasis on contingent liabilities	Fragmented debt management legislative framework	Draft of consolidated debt management legislation submitted to Parliament	Debt management legislation approved	Associated regulations enacted		A clear legal framework that is respected by SOEs and Government
IRI4: Review of SOE Portfolio and structuring oversight/holding of SOEs	Some individual performance reviews carried out as part of performance agreement preparations	Review of selected SOEs	Restructuring and/or privatization plan prepared	Strategic review of SOE portfolio completed and agreement on entities to be privatized/liquidated identified		Greater clarity on SOEs that need to be restructured, sold or partially privatized
IRI5: Fiscal risk monitoring reports on SOE portfolio published	Annual report on contingent liabilities from 6 largest SOEs with rudimental profit/loss information	Consolidated report on 6 largest SOEs, including basic information on profit/loss, and all subsidies and transfers. The	Consolidated SOE report including at least 15 SOEs, and including more in-depth analysis of company financial and	Consolidated SOE report including all SOEs, and deeper analysis of financial and operational performance, including	Consolidated SOE report with elements of previous years and in line with OECD good practice. Report should be issued	Comprehensive reports on all SOEs published on MoF's web site including analysis of financial and operational



Indicator Name	Baseline	YR1	YR2	YR3	YR4	End Target
		report should also include an assessment of fiscal risk to government given SOE debt levels and government exposure through guarantees.	operational performance. Fiscal risk assessment as in previous year.	corporate governance elements such as board composition, selection and remuneration. Fiscal Risk assessment should be included.	within 12 months of the fiscal year covered by the report	performance (including, benchmarking) and all financial transfers with the state (including all transfers, arrears, implicit subsidies, etc.)

Note to Task Teams: End of system generated content, document is editable from here.



ANNEX 1: DETAILED PROJECT DESCRIPTION

COUNTRY : Cabo Verde
Cabo Verde SOE Reform Project

Overall approach: The proposed project design combines three key critical and interrelated elements: (i) eligible expenditure programs against which credit proceeds can be disbursed; (ii) a set of disbursement conditions that provide a performance framework to advance the reform agenda and contribute to the development objectives supported by the operation; and (iii) a technical assistance component to support the achievement of the agreed results.

Project Description.

The Project Development Objective is to strengthen fiscal risk and SOE monitoring and to reduce the operational financing needs of selected SOEs.

The project consists of two complementary components: **Component 1. Results-Based Financing (US\$ 15 million)** will provide incentives for achieving results in two distinct areas: staff retrenchment in the national airline (TACV); and further cost cutting measures in the airline and **Component 2: Technical assistance (US\$ 5 million)** to support the GoCV in a number of technical areas including those related to the reforms under component 1. Component 1 will disburse against agreed eligible expenditure programs (EEPs) upon achievement of Disbursement Linked Indicators (DLIs).

Component 1: Results-Based Financing (US\$ 16 million). This component aims to support increased monitoring of the SOE portfolio and critical reforms in TACV with a view to decrease their needs for public financing to support their operations (for more details about activities and expected results see Annex 2).

Sub-component 1.1. Fiscal Risk Monitoring: The objective is to support the new SOE unit (UASE) to become a more effective institution and to strengthen the government's role as an active owner of the companies in which they are shareholders. Until now, SOEs themselves has been technically stronger and better informed, and therefore able to influence the reform agenda to their advantage. Support in this area aims to change this dynamic and provide the state with the tools to hold SOEs to account for their performance and to make informed decisions regarding SOE restructuring, privatizations and divestments.

In particular, results focus on increased reporting compliance by SOEs to government. This is complemented by improvement in the capacity of the central SOE unit to use the available information to carry out sound performance analysis of the companies in their portfolio, including benchmarking on financial and operational performance, and regular interactions between portfolio managers on the government side and management of SOEs. At the end of this process, UASE portfolio managers should have a comprehensive and complete knowledge of the companies in their portfolio and be able to better advise and inform government in their relations with SOEs.

Increased transparency and accountability to the public will be increased through the preparation and publication of annual comprehensive reports on the entire SOE portfolio, including analysis of company performance, contributions by SOEs to the economy through taxes and dividends and a complete overview of government support to SOEs through guarantees, recapitalizations, loans, etc;



Sub-component 1.2. SOE Restructuring and reduced public financing: this sub-component aims to reduce the financial losses of TACV through an implementation of an immediate short-term cost-cutting plan focusing on HR reconfiguration and the retrenchment of 207 staff, which is equivalent to just over half of total employees (459). The company has prepared an overall Retrenchment Plan which identifies staff categories to be reduced and approximate costs and savings for these cuts, process to be followed, including the legal framework, retrenchment methods and procedures, management arrangements and monitoring, grievance mechanisms, the basis for calculation of benefits, and other options/benefits such as training, etc. The plan has been discussed and approved by the board in general and has been communicated to staff.

The retrenchment and other cost cutting measures including the sale of the company's maintenance department, phasing out of domestic operations and the return of 2 aircraft to the lessor and a second round of retrenchment would lead to reduced public financing for TACVs operations in the form of guarantees, capital transfers or direct payments to creditors. The third DLI therefore captures these other planned reforms taking place in a later phase of the project and will disburse against these results.

Component 2: Technical Assistance (US\$ 4 million): This component will provide technical assistance to support the implementation of the government SOE reform program and to strengthen their overall capacity for macro-fiscal monitoring. In particular, it aims to strengthen the government's capacity as an active and informed owner of SOEs, including their ability to independently analyze and assess SOE activities, operational and financial performance, business plans, audits, and to prepare comprehensive and in-depth analytical reports on the SOE portfolio under their purview and their ability to increase private sector participation in SOEs. This set of actions is an essential element of the state's ability to better manage the fiscal risk posed by SOEs from repeated ad-hoc requests for guarantees, recapitalizations and loans. Eligible expenditure under this component are consulting and non-consulting services, acquisition of goods and operating costs.

Sub-component 2.1. Improved monitoring, oversight and advice on the SOE portfolio:

- Improve the technical capacity of the ownership unit (DSPE) to closely monitor SOE financial and operational performance, assessing the realism/quality of proposals and reports presented by SOEs (including business plans, performance agreements, HR restructuring plans), and to carry out SOE performance benchmarking with the objective to inform government decisions regarding approvals of recapitalizations, divestiture, etc.;
- Carry out a review of the SOE sector including if necessary individual company valuations to identify possibilities for further divestment of the SOE portfolio;
- Review of current ownership arrangements with a view to identify opportunities to further strengthen portfolio management. The review will involve detailed assessment of UASE unit staff skills, existing tools and time use
- Support to a long-term non-resident technical advisor in UASE. The non-resident advisor will be a senior practitioner with significant operational experience related to SOE monitoring and oversight. The expert will be visit Cabo Verde at regular intervals and will work directly with UASE staff, providing staff training and support the development of practical tools for the unit. The expert will also provide advice and inputs to TORs for various other activities listed under this component.
- Technical assistance for improved macroeconomic monitoring, reporting and use of macroeconomic modelling and econometric tools. This includes strengthening issues of



consistency among different aspects of macro policy formulation; strengthening of internal capacity to undertake analysis of macro fiscal risks and fiscal sustainability analysis.

- Technical assistance to improve budget credibility through better revenue and expenditure forecasting. This will be done by contracting a technical advisor that can provide targeted training on the use of various forecasting models and practical advice on the ministry of finance's current forecasting practices.
- Strengthening public debt management and fiscal responsibility including broadening the coverage of contingent liabilities. Improving the legislative framework underpinning the budget and debt management are essential. The production of annual debt sustainability analysis (with consideration given to contingent liabilities), and medium-term debt management strategy will also be important to engender greater budgetary certainty and less fiscal risk. Developing a sound annual borrowing plan to operationalize the strategy and increase communication with investors and other stakeholders (rating agencies etc.); Developing and annual report with risk management focus and which reports on the compliance with the strategy; Undertake a strategic review of the existing institutional structure which supports macro-fiscal policy formulation in the country. This includes: i) exploring issues of consistency among different aspects of macro policy formulation; ii) designing a program of support to restructure key areas - process and workflow, strengthen analytical capacity (through the introduction of new tools and procedures), and to assist with the implementation; iii) assist with the design of a macro policy statement; iv) establish framework to improve the production and dissemination of public sector statistics; v) strengthening of internal capacity to undertake analysis of macro fiscal risks and fiscal sustainability analysis; and, vi) establish mechanisms to strengthen the link with other key departments within the ministry, including treasury and budget departments.
- Technical assistance to strengthen the Unit's capacity to identify, launch and negotiate public private partnerships. This will include specific targeted training on PPPs and as necessary financing for technical/ transactions advisers on specific PPP initiatives

Sub-component 2.2. Improved corporate governance of SOEs

- Technical assistance for the drafting of complementary regulations to the framework SOE legislation (law 47/2009);
- Technical assistance for preparation of a SOE policy setting out the government's objectives with regard to each sector and SOE operating in that sector, including minimum performance standards, dividend policy, subsidies, etc.
- Technical assistance for the development of guidance material and standards for board members, including a practical manual and tools for target setting, performance evaluation, etc.
- Training program for SOE board members based on good international practice and tools developed under above activity (i.e., training on financial analysis, role of board members, performance evaluation, etc).

Sub-component 2.3: Just in time Technical Assistance. This flexible component will be used to finance activities that are directly related to the Project Development Objective but which are not yet identified or agreed on with the authorities. It could include technical assistance to implement activities identified in ongoing or planned studies such as for example the debt management reforms, SOE specific reviews, or others. It may include targeted technical assessments of SOEs or programs managed by SOEs that may



The World Bank

Cabo Verde SOE Reform Project (P160796)

have an impact on the government budget.



ANNEX 2: Results Framework and Monitoring

Country: Cabo Verde

Project Name: SOE Reform Project (P160796)

Project Development Objectives

PDO Statement

The Project Development Objective (PDO) is to strengthen fiscal risk and monitoring of SOEs and to reduce the operational financing needs of selected SOEs.

These results are at Project Level

Project Development Objective Indicators

Indicator Name	Baseline	Cumulative Target Values			
		YR1	YR2	YR3	End Target
PDO1: Public financing to SOEs (including transfer from the budget and capitalization)	30 million US\$US\$ (2016)	15 million US\$US\$ (2017)	5 million US\$US\$ (2018)	1 million US\$US\$ (2019)	0 US\$US\$
PDO2: Operating margin of TACV	144% (2017)	120%	100%	90%	80%
PDO3: Annual Public revenues from SOEs (taxes, dividends, concession payments, divestment proceeds)	5 million US\$ (2017)	7 million US\$	9 million US\$	10 million US\$	10 million US\$

Intermediate Outcome Indicators

Indicator Name	Baseline	Cumulative Target Values			
		YR1	YR2	YR3	End Target
IRI1: Comprehensive SOE policy adopted	Current (2016) SOE framework law outlines general rules for corporate governance of	Draft SOE Policy Prepared	SOE Policy adopted by council of Ministers		The government adopts a policy on SOEs including clear performance targets and transparency obligations of SOEs



<p>IRI2: Implementation of the updated SOE financial database</p>	<p>SOEs and government oversight and reporting</p> <p>UASE operates general excel sheet with basic aggregated information on six (6) largest SOEs</p>	<p>Pilot database prepared and tested</p>	<p>Database finalized and rolled out to include all SOEs</p>	<p>Database used for SOE monitoring and preparation of annual report</p>	<p>Database with complete financial and operational performance information on the entire SOE portfolio</p>
<p>IRI3: Strengthened legal framework for debt management with a greater emphasis on contingent liabilities</p>	<p>Fragmented debt management legislative framework</p>	<p>Draft of consolidated debt management legislation submitted to Parliament</p>	<p>Debt management legislation approved</p>	<p>Associated regulations enacted</p>	<p>A clear legal framework that is respected by SOEs and Government</p>
<p>IRI4: Review of SOE Portfolio and structuring oversight/holding of SOEs</p>	<p>Some individual performance reviews carried out as part of performance agreement preparations</p>	<p>Review of selected SOEs</p>	<p>Restructuring and/or privatization plan prepared</p>	<p>Strategic review of SOE portfolio completed and agreement on entities to be privatized/liquidated identified</p>	<p>Greater clarity on SOEs that need to be restructured, sold or partially privatized.</p>



Indicator Description

Project Development Objective Indicators

Indicator Name	Description (indicator definition etc.)	Frequency	Data Source / Methodology	Responsibility for Data Collection
Fiscal risk monitoring reports on SOE portfolio published	Measured by the number of annual reports on SOEs. Salient features of the SOE Annual reports include a complete overview of SOE net performance during the previous year, include net profit/loss, dividends paid, subsidies received, taxes paid, arrears and outstanding debt including contingent liabilities. Reports should be issued no later than one year after the period reported on.	Annually	MoF Website	MoF/UASE
Operating margin of TACV	Measured by the operational costs as a percentage of operating revenues as reported in audited annual financial statements by TACV	Annually	TACV and UASE	UASE
Reduced public financing to SOEs	Measured by transfers from the Government budget to SOEs for their operations, including subsidies, capital injections, loans, arrears, and any payments made on behalf of SOEs to creditors, and government guarantees for loans contracted by SOEs	Annually	Treasury Reports	UASE
Public revenues from SOEs	Measured by transfers and payments from SOE related activities to the government, such as taxes and dividends paid by SOEs, and proceeds from the sale or divestment of SOE shares or concession payments by private operators in areas previously controlled by SOEs (ports, airports)	Annually	Treasury Reports	UASE
Comprehensive SOE policy adopted	A government policy document approved by the Council of Ministers. The policy should clearly outline the strategic objectives of individual SOEs, including any relevant performance targets, as well as clear corporate governance and transparency and reporting standards of SOEs as well as of government.	One time	Ministry of Finance/Council of Ministers	UASE
Implementation of the updated SOE financial database	The SOE financial database is a web-based monitoring tool that will permit the exchange of information between SOEs	One time	Ministry of Finance	UASE



	and UASE. The tool will allow SOEs themselves to upload or update information. Part of the website will also be made public.			
Strengthened legal framework for debt management with a greater emphasis on contingent liabilities	As measured by the delivery of draft regulations related to (i) the implementation of the SOE framework law and a draft law on (ii) debt management	One time	Ministry of Finance	UASE
Review of SOE Portfolio and structuring oversight/holding of SOEs	As measured by a review of the SOE portfolio with a view to identify companies to be restructured and/or sold. The review will also examine the institutional set up for SOE oversight and monitoring and make recommendations for strengthening the current arrangements	One time	Ministry of Finance	UASE



ANNEX 3: IMPLEMENTATION ARRANGEMENTS

COUNTRY : Cabo Verde Cabo Verde SOE Reform Project

Project Institutional and Implementation Arrangements

The UASE, established within the MoF is the lead implementing agency. The UASE will serve as the Project Implementation Unit (PIU), overseeing the day-to-day management of the project. It is responsible for technical inputs, coordination among participating entities and liaising with the World Bank. The UASE will rely on the on the Unit of Special Projects Unit (*Unidade de Gestão de Projetos Especiais*—UGPE) for the fiduciary tasks. The UGPE is also established within the Ministry of Finance and is managing the entire portfolio of the Bank-financed projects in Cabo Verde. It will also be responsible for ensuring compliance with the Bank’s financial management, procurement regulations and safeguard requirements, and reporting to the Bank on a timely manner. The head of UASE will be the Project Director.

The UASE’s capacity has been assessed adequate to assume its role as a PIU. Established in November, 2016, the UASE as the result of the merger of the Privatization and Public Private Partnership (PPP) units, has some track record of implementation experience as an institution. However, the members of the project team with relevant project experience is limited. Overall, the UASE has adequate staff capacity to carry out the proposed project. . In addition, technical assistance financed during preparation (by PPA) and over the lifetime of the project will ensure the adequacy of implementation capacity.

Given the political importance of reforms in TACV the government has established a Privatization Team which is inter-ministerial in nature and include members from all ministries and institutions involved in the management of the planned reforms. The technical team is supported by the State Business Sector Monitoring Unit and answer to a small ministerial steering committee.

Project Steering Committee (PSC). To ensure proper coordination and supervision of the project, a PSC will be established to provide strategic guidance and oversight. The Minister of Finance will co-chair the PSC with the Minister of Economy, and including representatives from TACV and others as necessary (i.e. staff union). The Project Director will serve as secretary to the committee. This committee will meet biannually and will review the annual progress report.

Financial Management

UGPE’s financial management arrangements in place satisfy the Bank’s minimum requirements. The government will rely on that existing financial management system for the implementation of the project. The UGPE has FM staff comprised of an experienced financial management specialist and two accountants familiar with Bank fiduciary procedures. In order to accommodate the project in the existing financial management system and ensure an adequate segregation of duties, the following measures should be taken three months



after effectiveness: (i) the update of the existing project implementation manual of UGPE including result-based financing procedures; (ii) the customization of the existing accounting software to include the bookkeeping of the project and generate interim financial reports and financial statements; (iii) the appointment of an additional accountant and (iv) the recruitment of an external auditor and an independent verification agent.

Budgeting: Annual budgets will be derived from this project disbursement plan and will be updated as needed to reflect implementation progress. UGPE will prepare in consultation with UASE a detailed annual work plan and a budget, which should be approved by the Project Steering committee. UGPE will submit the approved annual work plan and budget to the Bank, for no objection, before the end of previous calendar year.

Accounting and reporting. Project accounts will be maintained on a cash basis, supported with appropriate records and procedures to track commitments and to safeguard assets. Annual financial statements will be prepared by the UGPE in accordance with the Cabo Verde accounting requirements but considering specificities related to external financed investment projects. Accounting and control procedures will be documented in the UGPE's Fiduciary Manual. Every quarter, and within 45 days of the end of the reporting period, the UGPE will submit a withdrawal application for IDA grant along with IFRs and DLI results report to the World Bank for disbursements and documentation of expenditure. The template of IFRs will be agreed and will be used to document advances and actual project expenditure incurred against the eligible expenditure supported by the World Bank under the program. The UGPE will customized the existing accounting software for the bookkeeping of the project.

Internal control and internal auditing arrangements. The UGPE's FM and administrative procedures will document the FM and disbursement arrangements, including internal controls, budget process, assets safeguards, and clarify roles and responsibilities of all the stakeholders.

Annual financial audit and DLI verification. An external independent and qualified private sector auditor will be recruited to carry out the audit of the project's financial statements. The auditor will express an opinion on the Annual Financial Statements and perform the audit in compliance with International Standards on Auditing. The auditor will be required to prepare a Management Letter detailing observations and comments, providing recommendations for improvements in the accounting system and the internal control environment. The audit report on the annual project financial statements and activities of the Designated Account (DA) will be submitted to IDA within six months after the end of each project fiscal year. The project will comply with the Bank disclosure policy of audit reports and place the information provided on the official website within one month of the report being accepted as final by the team

An Independent Verification Agent will be responsible for the regular verification of the EEP Spending and Results Reports, on a schedule to be agreed with the authorities. The agent will issue an opinion on the accuracy and fair view of the information presented by the UASE on the EEP and DLI. This certificate should be sent to the World Bank by the verification agent. Validation of results will be based on the verification protocol shown in table 2 below.

TABLE 2: DISBURSEMENT-LINKED INDICATORS (DLIS) VERIFICATION PROTOCOL



DLI	Verification Protocol Procedure
DLI 1. Retrenchment plan approved and announced by TACV	UASE with third party review of Retrenchment Plan formal approval process and evidence, including minutes from board meeting, management letter, or other.
DLI 2. Grievance mechanism established	UASE with third party review of all documentation relevant to grievance mechanism, including assigned personnel and processes for complaint receipt, treatment, recording, and follow up.
DLI 3: Staff targeted by the retrenchment plan is retrenched	UASE with third party review of relevant documents of severance packages, list of eligible TACV employees per the approved retrenchment plan Calculation: Number of Redundant TACV Employees receiving Redundancy Payments/Number of eligible Redundant TACV Employees receiving Redundancy Payments x100
DLI 4: Detailed Annual SOE reports	Third party review of UASE annual published SOE report. Quality criterion includes data comprehensiveness (# of SOEs covered; number of financial and operational indicators used) and quality of analysis (the use of data for analysis of performance, risk) in line with good international (OECD) practice for comprehensive SOE reporting

The TACV’s external audit reports together with Management Letters should be submitted to the World Bank within six months after the end of the TACV’s each fiscal year.

Disbursements

Table 1 summarizes the project’s disbursement arrangements.

Table 1. Project’s Disbursement Arrangements

Disbursement Categories	Amount of Credit (US\$, millions)	Percentage of Expenditure to be Financed	Disbursement Cycle	Disbursement Condition
(1) Eligible Expenditure Program (EEP)	16.0	100	Reimbursement of eligible expenditure based on certification of DLIs achieved and expenditure reported in bi-yearly EEP	Achievement of DLI targets
(2) Goods, Non-Consulting Services, Consultants’ Services, Incremental Operating Costs, Training and Workshops	4.0	100	Advance to Designated Accounts	None



TOTAL	20.0	—		
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Disbursements will be report-based. The World Bank will disburse loan proceeds to the Ministry of Finance into a Designated Account (DA) denominated in US dollars, maintained at the Central Bank of Cabo Verde for Category 2 (Component 2). Advances will be provided to the DA based on six-months forecast and subsequently quarterly IFRs will be used for documentation of expenditures. Retroactive financing of up to 20 percent of total project value is permitted, in line with standard World Bank rules. Other disbursement methods (reimbursement, direct payments, and special commitment) will be available for use. Overall disbursement arrangements will follow standard disbursement policies and procedures established in the Disbursement Guidelines for Investment Project Financing dated February 2017, and in the Disbursement Letter of the Project.

The disbursements for Component 1 (Category 1) will be made against achievement of DLIs targets. A certain amount of credit proceeds has been allocated to each DLI, referred to as the DLI allocation, which is the amount that the UASE can claim as disbursements against EEPs if that DLI has been achieved and verified. These EEPs are a part of recurrent expenses of the eligible activities, clearly identifiable in the MOF’s and TACV financial statements, and shall primarily comprise UASE or TACV staff salaries or other operational costs of the program. The price for each DLI has been agreed.

This mode of disbursement will mainly involve reimbursement of certified EEPs supported with achieved DLIs’ and other relevant documentation. The disbursements will be made against identified EEPs, and the triggers will be the actuals values of predefined DLIs. Decisions over compliance and disbursement against indicators will be made on the basis of reports prepared by the UASE and submitted to the Independent Verification Agent with necessary documentation assuring that they have been satisfied. The World Bank will receive the EEP spending and DLI assessment report by the end of March following each implementing year and will finally advise on the amount to be reimbursed to the Ministry of Finance which should not exceed the actual value of the EEPs that generate the results or DLI levels to be paid. Disbursements against EEPs and DLIs will flow to a special account to be opened.

Carryforward of amounts not disbursed. If the World Bank has received only partial evidence of compliance under the DLIs and/or the recipient has not presented enough eligible expenditures under the EEPs to disburse the full planned disbursement amounts, only part of the full planned amount will be disbursed. The World Bank may, at its discretion, authorize that the unwithdrawn portion of the financing resulting from this lack of evidence be carried forward to the subsequent withdrawals, provided that this occurs, the amount to be disbursed by the World Bank, in the aggregate under all subsequent withdrawals, shall not exceed 100 percent of the sum of the total amounts of EEPs incurred at that time.

Distribution of carried forward disbursements. The amounts carried forward for subsequent withdrawals because of the nonachievement of DLIs may be disbursed only if at the time of the subsequent withdrawal, (a) the applicable DLIs have subsequently been achieved and (b) the recipient has submitted documentation of eligible expenditures in the amount at least equal to the withdrawal amount requested. The amounts carried forward due to lack of documentation of eligible expenditures in the amount at least equal to the amount requested for withdrawal may be disbursed at the time of the subsequent withdrawal only if such amount of eligible expenditures is then submitted.

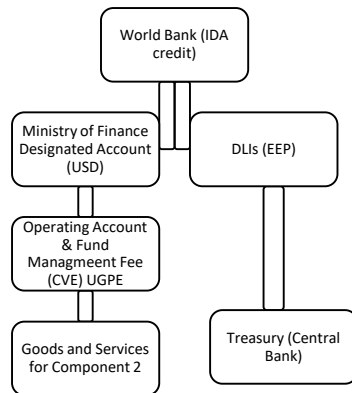
Final disbursement. If any amount allocated to Component 1 remains to be withdrawn from the loan balance due to partial evidence of compliance with the DLIs and/or lack of documentation of eligible expenditures, the Association may, at its discretion, authorize this remaining amount to be disbursed as an exceptional disbursement, before the



closing date, in accordance with the DLI formula, and provided the recipient has submitted documentation of eligible expenditures in the amount at least equal to the withdrawal amount requested.

A total of four DLIs will be financed from the US\$16 million allocated to EEPs. The tentative disbursement schedule is set out in Annex 6.

Figure .1. Flow of Funds



Procurement

The Borrower will carry out procurement under the proposed project in accordance with the World Bank’s “Procurement Regulations for IPF Borrowers” (Procurement Regulations) dated July 2016 under the “New Procurement Framework” (NPF), and the “Guidelines on Preventing and Combating Fraud and Corruption in Projects Financed by IBRD Loans and IDA Credits and Grants”, dated October 15, 2006 and revised in January 2011, and other provisions stipulated in the Financing Agreements.

The procuring entity, the bidders, and service providers (i.e. suppliers, contractors and consultants) shall observe the highest standard of ethics during the procurement and execution of contracts financed under the project in accordance with paragraph 3.32 and Annex IV of the Procurement Regulations.

The Borrower shall prepare and submit to the Bank a General Procurement Notice (GPN) and the Bank will arrange for publication of GPN in United Nations Development Business (UNDB) online and on the Bank’s external website. The Borrowers may also publish it in at least one national newspaper.

Comentado [M/U/PO-IB2]: GPN to be published before publication of a specific Procurement

The Borrower shall publish the Specific Procurement Notices (SPN) for all goods, non-consulting services, and the Requests for Expressions of Interest (REOIs) on their free-access websites, if available, and in at least one newspaper of national circulation in the Borrower’s country, and in the official gazette. For open



international procurement selection of consultants using an international shortlist, the Borrower shall also publish the SPN in UNDB online and, if possible, in an international newspaper of wide circulation; and the Bank arranges for the simultaneous publication of the SPN on its external website.

Institutional Arrangements for Procurement

Procurement Risk Assessment. An assessment was realized in March 2017 by the Procurement Specialist. The *Unidade de Acompanhamento do Sector Empresarial do Estado* – (UASE), in charge of SOE Monitoring and Oversight Unit, shall carry out the procurement under the project. was created in 2016 with the merger of the Privatization and Public-private Partnership Unit and SOE Department. The former PPP Unit was financed by the Government of Cabo Verde, the African Development Bank, and Investment Climate Facility UASE. With technical assistance from the AfDB and ICF, the Unit carried out international tenders for technical assistance in large transactions such as the process for the sub-concession of the main ports of Cabo Verde and the Cabnavé Shipyard.

The Unit was responsible for managing all procurement processes, in accordance with national law, international best practices, and AfDB procurement guidelines, for all the projects in its pipeline. The Unit and its staff have experience in preparing bidding documents such as Terms of References, Request for Proposals, and bid proposal evaluation reports as well as managing disbursement/payment processes.

However, this project will be implemented under the new Bank Regulations for Borrowers dated July 2016 and bring additional workload on the team. There are risks of: i) Additional workload due to the proposed project; ii) The manual of procedures doesn't take into account the project. The overall procurement risk without mitigation measures has been assessed to be substantial.

Mitigation measures: The following measures are proposed to mitigate these risks and reduce their classification from substantial to moderate: i) hire a Procurement Specialist on a full-time basis and train the staff on the NPF; ii) update the manual of procedures to take into account the project and develop Project Implementation Manual (PIM).

Procurement Manual: Procurement arrangements, roles and responsibilities, methods and requirements for carrying out procurement shall be elaborated in detail in the Procurement Manual which may be a section of the Project Implementation Manual (PIM). The PIM shall be prepared by the Borrower and agreed with the Bank not later than three months after the project effectiveness date.

Procurement methods. The Borrowers will use the procurement methods and market approach in accordance with the Procurement Regulations.

Open National Market Approach is a competitive bidding procedure normally used for public procurement in the country of the Borrower and may be used to procure goods, works, or non-consultant services provided it.

Operational costs financed by the project, if any, would be incremental expenses, including office supplies, communication costs, rental expenses, utilities expenses, consumables, transport and accommodation, per diem, supervision costs, and salaries of locally contracted support staff. Such service needs will be procured using the procurement procedures specified in the PIM accepted and approved by the Bank.

The Project Development Objective is to strengthen SOE related fiscal management. The market in Cabo Verde, with a population of around 550,000 inhabitants, is of a modest size. While the project will seek

Comentado [M/U/PO-IB3]: Procurement will be care out by UGPE



out qualified domestic consultants, it will have to procure services internationally.

Procurement Plan (PP). The PP was prepared (Annex 3) and submitted to the Bank and will be discussed and approved by the Bank during project negotiation. The PP will be updated by the procuring entity on an annual or as-needed basis to reflect actual project implementation needs. Updates of the PP will be submitted to the World Bank for No Objection and the PPSD updated accordingly.

Short lists composed entirely of national consultants: Short lists of consultants for services estimated to cost less than US\$300,000 equivalent per contract may be composed entirely of national consultants.

Environmental and Social (including safeguards)

Monitoring and Evaluation

For the purposes of project monitoring, the Government and World Bank have agreed on a Results Framework that comprises three Project Development Objectives and five Intermediate Results Indicators. The Results Framework defines the indicators and the institutional arrangements for data collection. The UASE has the overall responsibility and coordinating role in M&E of the program. The Bank implementation support missions will undertake periodic evaluation of implementing M&E arrangements to verify that adequate systems are in place to generate the information needed for project reporting.

Four DLIs will be used to measure the achievement of agreed targets and will be the basis for disbursement of project financing. The DLIs will be monitored as part of the overall project results monitoring arrangements by the UASE. To ensure independence of the verification process, the UASE will contract a third party to support the verification process.



ANNEX 3: PROCUREMENT PLAN

Comentado [M/U/PO-IB4]: Breakdown by activity

Ref. No.	Description of Assignment	Estimated Cost	Selection Method	Review by Bank (Prior / Post)	Expected Proposals Submission Date	Comments
1	Contract of Auditing/Consulting Firm/Independent Verification Agent	200,000	CQS	Post	5/15/2018	TOR ready
2	Technical Assistance Contract for: Training Program for UASE staff; development and preparation of tools for UASE; support review of legal and institutional framework including legal drafting; diagnosis of SOE portfolio; company specific assessments for select SOEs; preparation of privatization strategies for selected companies; business and assets valuation for 4 companies; transactions advisory services for the privatization of select companies.	3,600,000	ICB	Prior	7/10/2019	ToR in preparation
3	Contract of Auditing firm for the Project Financial Audit	50,000	CQS	Post	6/1/2019	TOR ready

Comentado [M/U/PO-IB5]: , due to this kind of service QCBS will allow to compare different methodology

Comentado [M/U/PO-IB7]: Consulting method QCBS?

Comentado [M/U/PO-IB6]: Breakdown by activity and with the estimated cost for each activity

Comentado [M/U/PO-IB8]: Normally is used the LCS – Least cost selection for this standard service



ANNEX 4: IMPLEMENTATION SUPPORT PLAN

COUNTRY : Cabo Verde
Cabo Verde SOE Reform Project

Strategy and Approach for Implementation Support

The strategy for implementation support has been developed based on the nature of the project and its risk profile. The aim is to make implementation support to the client more flexible and efficient by focusing on implementing the risk mitigation measures defined in the Systematic Operations Risk-rating Tool (SORT).

Implementation Support Plan and Resource Requirements

The World Bank Task Team Leaders (TTLs) will provide ongoing support by coordinating with the client and among World Bank staff who will provide implementation support on technical, fiduciary (FM and procurement), and safeguards aspects. The TTLs will be based in Washington DC, and implementation will be supported by task team members in the World Bank’s Washington, DC offices as well as selected field offices. Field missions can be organized quickly should the need arise and international expertise can be mobilized to provide global best practices. Specific technical expertise will be necessary on Airline Restructuring (Transport Specialist) and in particular staff retrenchment (Social Development Specialist). Formal monitoring missions will be carried out at least twice per year. Table 1 shows the expected skill requirements, timing and resource requirements for implementation support over the life of the project. The implementation support plan is flexible and open to adjustment throughout the project period.

In collaboration with government counterparts, the World Bank will monitor progress against the Disbursement Linked Indicators (DLIs) and monitoring indicators in the Results Framework. The World Bank will also monitor risks and update the risk assessment and risk management measures, as needed. A midterm review will involve a more in-depth stocktaking of performance under the project. Based on the assessment of progress at the midpoint, government counterparts and the World Bank will consider recommendations for improvements or changes. The World Bank team will also maintain close coordination with other development partners supporting SOE Reforms in Cabo Verde.

Implementation support skills mix

Skills Needed	Resource Estimate (Staff weeks/year)	
Task Team Leader (SOE Expert)	12	Based in HQ
Co-Task Team Leader (Country Economist)	10	Based in HQ
Procurement Specialist	6	Based in Dakar
Financial Management Specialist	6	Based in Dakar
Lead Transport Specialist (Airlines)	6	Based in HQ
Social Safeguards Specialist	4	Based in HQ
Environmental Safeguards Specialist	1	Based in HQ
Senior Legal Counsel	2	Based in HQ
Senior Finance Officer	2	Based in HQ



Note to Task Teams: What would be the main focus in terms of support to implementation during:

Time	Focus	Skills Needed	Resource Estimate	Partner Role
First twelve months	Smooth launch of the project, including the implementation of TACV retrenchment plan	SOE Expertise; Social Safety Operational and Fiduciary	30 weeks	
12-48 months	Capacity Building of UASA	SOE expertise, including specific industries	30 weeks	
Other				



ANNEX 5: THE SOE SECTOR IN CABO VERDE

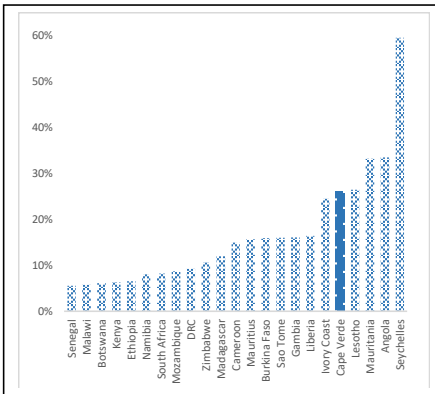
Sector size and composition

There are thirty-two SOEs in Cape Verde, providing essential services such as electricity, water, transportation and postal services. The state is sole owner of 17 companies and is a majority shareholder in another seven, and a minority owner in a further seven companies. Three SOEs are currently being liquidated, notably a fishing company (Atlantic Tuna – 60% share), a social housing fund (SOFHIS-GERE – 60% government share), and a partial risk guarantee fund (Promotora - 26% government share). The largest SOEs by sales and assets are ENACOL (oil imports and distribution), Electra (Electricity utility), ASA (Airports management), TACV (Airline), ENAPOR (Port), IFH (Housing), Telecoms (CVT) (Figure x.1). A new company (NOSI) was established in 2016. NOSI was formed by the former IT department in the ministry of finance, with a focus on providing software development services. A full list of companies is included at the end of this annex.

The analysis in this annex uses financial information for 21 SOEs as outlined in Table 1 below. The largest number of SOEs are in the Services sector. Companies include real estate development (IFH), investment promotion and special economic zone development (SGZ and FIC), Post Office (CCV), Pharmaceutical production (EMPROFAC), Software Development (NOSI), a Vocational Training School for the tourism sector (EHTCV), and Telecoms (CVT).

Table 1: Number of state owned enterprises (SOEs) by sector and size

Sector	# Companies	Sales/GDP	Debt/GDP	Assets/GDP
Communications	1	0.1%	0.2%	0.3%
Finance and Banking	2	0.5%	0.3%	0.8%
Industry	1	0.1%	0.1%	0.2%
Manufacturing	1	0.0%	0.0%	0.0%
Oil and Gas	1	6.0%	1.8%	4.3%
Services	8	5.1%	18.1%	25.6%
Transport	4	7.8%	15.7%	17.5%
Utilities	3	6.5%	14.8%	13.4%
Total	21	26%	51%	62%

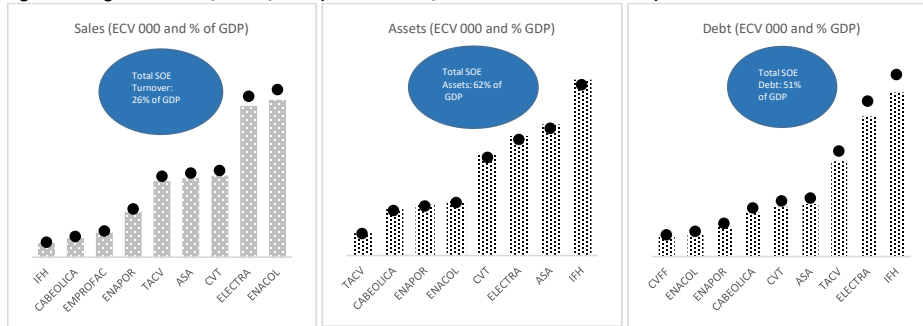




This is followed by Transport, including the national airline (TACV), ports (ENAPO), airports (ASA) and maritime transport (CVFF). Recently, the state has taken shares in another airline (Binter Cabo Verde – 30%). Utilities comes in third, led by the integrated water and electricity producer and distributor (Electra) where the state is a majority owner (78%), and including minority stakes in a privately owned water producer (APN - 10%) and energy producer (Cabeolica- 2%).

The weight of the SOEs in the Cabo Verdean economy is very significant, even when measured by global and regional standards. On average, SOEs in the Africa region contribute around 15 percent of GDP as measured by sales/turnover. In Cabo Verde, SOEs contributed 26 percent of GDP in sales in 2016, and they held assets worth over 60 percent of GDP and debts of 50 percent of GDP (Figure 1). The five largest SOEs make up nearly 80% of total sales, hold 75% of assets, and 78 percent of debt for the entire sector.

Figure 1: Largest SOE Sales, Assets, Debt (2016 numbers, ECV 000 and Percent of GDP)



Source: Ministry of Finance and authors calculations

SOE financial performance

The financial performance of SOEs vary, but the SOE portfolio has been loss-making on aggregate. The SOE portfolio lost US\$ 9.4 million in 2016 and just over US\$ 9 million in 2015, down from a net profit of US\$ 23 million in 2014¹³(Table 2). Sales have decreased from nearly 50 billion escudos (32 percent of GDP) to 42 billion escudos (26 percent of GDP) between 2013-2016, while value added increased slightly from 13.8 billion Escudos to 14.4 billion Escudos (Figure 2).

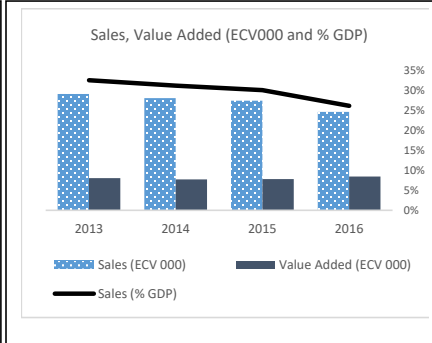
¹³ The net profit of 2014 is due to the sale/spin-off of TACV's ground handling services to ASA as part of a debt settlement agreement.



Table 2: Net result by sector (2014-16)

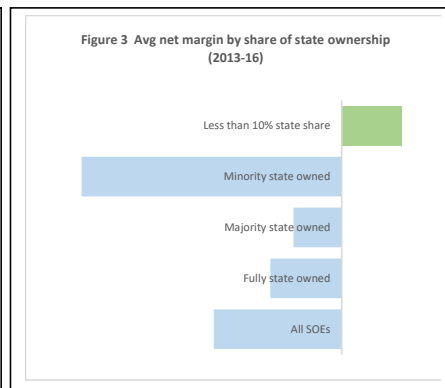
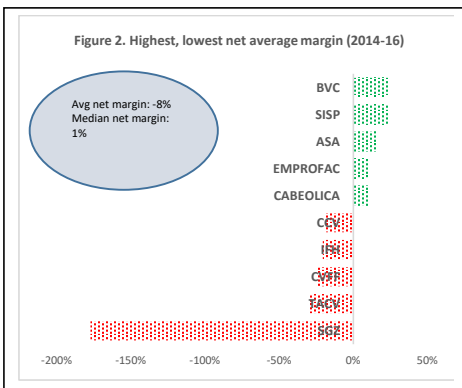
Net profit/loss (ECV 000)	2014	2015	2016
Communications		(6,286)	(5,170)
Finance and Banking	173,385	148,141	187,279
Industry	(21,355)	4,668	(25,908)
Manufacturing	6,302	5,247	1,486
Oil and Gas	136,566	68,341	525,984
Services	46,348	313,090	(77,649)
Transport	1,673,791	(2,160,944)	(1,517,366)
Utilities	298,213	717,274	(27,973)
Total	2,313,250	(910,469)	(939,317)

Figure 2: Sales, Value added (ECV 000 and % GDP)



Of the majority owned SOEs, the biggest contributors to losses over the last three years were the airline (TACV), regional development company (SDTIBM), real estate (IHF), maritime transport (CVFF) and postal service (CCV). The airports company (ASA) has been the most profitable, followed by the pharmaceutical import and distribution company (EMPROFAC), the energy and water utility (Electra) and ports (ENAPOR). Of the six companies in which government holds a minority share, only one has seen average losses over the period. The most profitable of these are telecoms (CVT), oil import and distribution (ENACOL) and the inter-bank payment system (SISP).

The average net margin for the group of 21 SOEs on which figures are available was -8.1 percent (Figure 2 and 3) while the median net margin was 1.3 percent. Fully state-owned companies had an average net margin of -4.5 percent, while majority owned had -3 percent and minority state owned companies saw the weakest results on average with -16.5 percent net margin. Only companies in which the state had less than 10 percent share had a positive net margin (3.8 percent).

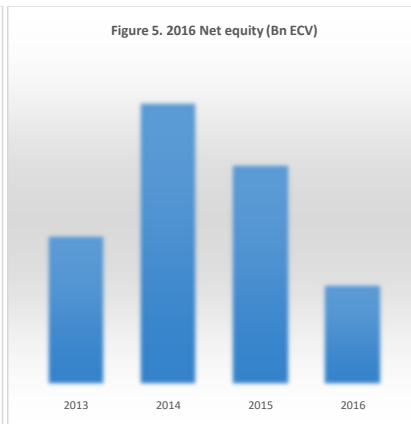
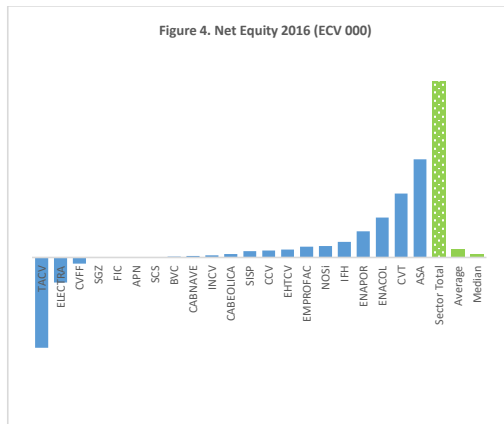


The stock of SOE debt has increased in recent years and many SOEs are in need of government



guarantees for their commercial debt. In 2017 the state is estimated to have provided explicit guarantees for SOE commercial loans equal to 7.4 percent of GDP up from 6.6 percent in 2016. The total debt stock for the three largest SOE reached 30 percent of GDP in 2014 (500 million USD). The largest debts are held by IFH (197 million USD), followed by Electra (188 million USD) and TACV (116 million USD). In 2013-14 the authorities set an annual limit of 7 bn ECV for government guarantees (just under five percent of GDP), while in 2015 this was lowered to 5 bn. Cabo Verde does not have a history of SOE debt defaults, and SOEs whose debt is guaranteed by the state have not defaulted and called on the guarantees provided by the state. However, in reality some SOEs have ‘technically’ defaulted since government has stepped in to provide emergency loans or recapitalizations in the past, and they are currently making direct payments on behalf of TACV to its creditors. IFH has also requested direct support from the authorities to deal with its cash flow problems while treasury is directly servicing the Portuguese credit line which finances the social housing program managed by IFH.

Overall, SOEs have more assets than liabilities, and the sector has a positive net value. Four companies have negative net worth, as measured by their equity, notably the airline (TACV), the energy and water utility (Electra), a maritime transport company (CVFF), and a special development zone (SGZ). The remaining companies have positive net equity (Figure 4). The sector total net equity is positive, as if the average and median. It has fluctuated slightly between 2013 and 2016, going from 19 billion escudos in 2013, then increasing to 21 billion in 2014 and decreasing again to just over 18 billion in 2016 (Figure 5). The challenge for government is to use these assets more productively, contributing to growth, wealth creation and improved public services.



Legal and institutional framework and corporate governance:

In Cabo Verde, the overall corporate governance environment for SOEs is generally acceptable, even though there are several areas in need of improvement. Corporate governance of SOEs refers to the rules and mechanisms under which they operate, including their internal governance structures, their relations with shareholders, the ability of the state to act as an informed owner, and their transparency and disclosure requirements. In particular, there is a room for clarifying the objectives of state ownership, strengthening the disclosure and reporting obligations of SOEs and the state, the strengthen state’s



capacity to act as an informed and proactive owner. In addition, board and management practices could be strengthened to minimize political appointments in favor of bringing in needed technical expertise.

SOEs operate under the commercial code, their own founding legislation and the 2016 framework SOE Law¹⁴ that consolidates the main SOE governance provisions. It includes rules related to reporting, disclosure, state oversight, and boards of directors. It subjects SOEs to the same rules of competition as all other companies in Cape Verde, and appoints the Minister of Finance as the shareholder representative. The legal framework for SOEs was strengthened in early 2016 with the passing of law 104/VIII/2016 on January 6, 2016, replacing the SOE framework law 47/VII/2009 of 7 December 2009. The new law has been strengthened in several areas, notably (i) it clarifies and broadens its scope of coverage to all categories of state owned corporate entities, including those owned by municipalities (ii) it includes clearer guidance and limits on SOE debt, including the need for SOEs to outline debt plans as part of their annual budget and business planning process which is subject to approval by the authorities (iii) it introduces stronger sanctions for non-compliance with reporting obligations of the SOEs to the state, where failure to comply now provides justification for dismissal of senior management (iv) it includes new articles (Article 33 and 34) on the Transformation/Fusion and Liquidation of SOEs. While the reporting responsibilities of SOEs to the state have been slightly expanded to include regular reporting on operational targets and shareholders, the reporting requirements of SOEs to the public remain limited to an annual publication in the official bulletin of the structure and composition of management, board, committees, etc. as well as their qualifications and their remuneration, as in the previous law. The council of ministers can request the publication of additional information.

The 2016 framework law consolidates the main provisions and rules related to SOE governance. It gives a definition of SOEs, confirms the subjection of SOEs to the commercial code, and includes extensive provisions related to governance requirements on control, reporting, disclosure, state oversight, and boards of directors. This legal framework provides a sound basis for SOE governance and oversight, but it suffers from uneven implementation. For example, the law clearly states that SOEs should be compensated for public service obligations (PSOs) and that the costs of PSOs should be calculated in a clear and transparent manner, yet in practice this has not been done. Further, the reporting obligations of SOEs to government go far beyond standard financial reporting to include detailed information on company corporate governance, including the frequency of board meetings and selection and remuneration of senior management and board. Currently, reporting happens on an irregular basis and is generally limited to audited financial reports. Closing this implementation gap requires stronger monitoring on compliance by the government as owner and regulator. In addition, and in line with evolving international practice, an ownership policy is an important instrument to lay out the rationale for state ownership and the specific objectives of companies, including public service obligations.

Government oversight and SOE monitoring

The institutional framework for monitoring SOEs is a dual system where the Ministry of Finance and line ministries share technical and financial oversight responsibilities. Treasury is the owner of SOE shares and is responsible for monitoring SOE debts and general financial performance, while technical ministries and regulatory agencies are involved in monitoring operational performance, including the setting of performance targets. In the past SOE oversight has been weak overall although it has improved

¹⁴ Law 47/VII/2009



significantly since the merger of the SOE unit (DNPE) and PPP unit in 2016 and the creation of the UASE.

However, the unit remains relatively weak technically. It lacks essential monitoring instruments, such as updated SOE accounts, strategic plans, budgets and quarterly reports. The unit is currently receiving support through the World Bank transport project to improve its monitoring system, and a web-based system has been developed and is being tested as of February 2018. In order to support the state as an owner, the unit also needs senior in-house technical expertise to provide independent and authoritative analytical advice on SOE business plans and performance. Currently, the SOEs have stronger technical and business knowledge than the Ministry of Finance, meaning that the authorities are unable to independently assess SOE proposals and reports and challenge SOE views and proposals when necessary.

Performance contracts are key instrument in the authorities' efforts to improve SOE monitoring. Agreement are all of good quality, prepared with the technical support of independent consulting companies with sector specific expertise. The challenges has been in ensuring timely reporting and evaluation of the agreements, and the lack of application of sanctions for non-performance. Despite an explicit requirement for companies to report regularly on their commitments and targets, such monitoring is sporadic.

Limited capacity in government has meant that many SOEs have been able to continue to operate with continued losses, increasing their debt levels and their dependence on state support. The situation reached a critical level in 2016, with two large SOEs becoming technically insolvent and dependent on direct state support for their survival (TACV, IFH). The challenge for the government is to gain some control of the situation and take urgent decisions on difficult but necessary SOE reforms in order to minimize the fiscal impact. For this to happen, the government needs to become a more active owner, with the capacity to form its own opinion of SOE performance and necessary reforms based on high quality technical analysis on SOE performance. Based on the increased capacity, the government can exercise its ownership in a more proactive manner in SOE boards and as ultimate shareholder of these companies. Currently, the SOEs themselves are stronger technically, and they are; therefore, able to set the agenda for technical and financial discussions with the Government and Treasury.

Privatization and Public Private Partnerships:



Cabo Verde has undertaken several rounds of SOE reform. The first programs focused on privatization, and resulted in the sale of more than 27 SOEs between 1992-2004 resulting in a significantly reduced portfolio from 50 to 23 fully controlled holdings. Several large companies were privatized during this period, including Cabo Verde Telecom and Electra (Box 1), the electricity and water utility, and the two major commercial banks.

The second phase of reforms began after 2001 and focused on enhancing economic regulation, liberalizing sectors to spur competition, and improving the business and investment climate. A second privatization program was undertaken as part of a series of IMF-backed structural adjustments, but was largely unsuccessful. Many of the SOEs prepared for sale during that time (e.g. TACV, EMPROFAC, ENAPOR, CABNAVE) were never tendered.

Box 1: The failed privatization of Electra

To address the increasing needs of electricity services in the country and improve the performance of the state-owned utility, the government signed the contract for the privatization of ELECTRA (acquisition of 51% of the shares and a concession contract for a period of 50 years) with EDP - Electricity in Portugal, SA/IPE-ADP -Aguas de Portugal, SGPS, SA. in 1999¹.

EDP/IPE-ADP planned to invest ECV26 billion (260 million US\$) over the first 15 years of the concession to upgrade the power and water infrastructure, but conflicts regarding tariff increases, consumer dissatisfaction around tariff increases, and fundamental weaknesses in the concession agreement meant that these investments never fully materialized. The concessionaire/private operator was dissatisfied with the refusal of the regulator to allow for the contractually agreed tariff increases, which they felt were not granted for political reasons. The failure of the regulator to apply agreed tariff adjustments and the inability of both parties to reach a compromise was the main reason behind the privatization failure. That and other related issues of interpretation of the contract led to the abandonment of the concession by the private operator. The government renationalized Electra in 2007.

The government is currently pursuing an ambitious privatization and PPP program. As of early 2018 a total of 15 SOEs are in various stages of privatization. Substantial additional capacity will be required to ensure that PPP projects are bankable, tendered in a transparent, fully competitive way and implemented according to the terms of the agreement. As in many countries embarking on PPP programs, establishing a clear set of rules, guidelines and institutional authority for the process reduces risks and costs for all parties involved.



Transportes Aereos De Cabo Verde (TACV)¹⁵
A brief history of reforms

Transportes Aereos De Cabo Verde (TACV) was established on 27 December 1958 as the sole air operator for the islands of Cabo Verde. Its beginnings were small, carrying under 500 passengers in its first year and concentrating on inter-island traffic. However, in July 1975, following the independence of Cabo Verde, the airline was designated as the national carrier and became a state-owned company in 1983.

The airline experienced promising growth and developed into a small but modern carrier servicing just under 50,000 passengers in the year 2000 both in the domestic and in the international market. At the time, TACV dominated the domestic market as sole operator by transporting about two-thirds of its passengers, and had a lead position in the international market, contributing much to the more than doubling of tourist arrivals in the 1990s.

Restructuring and Privatization Efforts:

Despite its operational success during its first 30 years, profitability of the carrier became a challenge towards the end of the 1990s. In order to address the financial difficulties, the Government of Cabo Verde (GoCV) decided to include TACV into a privatization program, which aimed at spinning-off seven state-owned entities to the private sector. The World Bank supported the privatization program of the GoCV by including a component in the Structural Adjustment Credit (SAC) Credit No. 3587 approved on (Board date) of the International Development Association (IDA). The project supported the initiation of privatization of TACV, through the publication of a privatization Decree-Law, including a privatization action plan for TACV.

Following an initial analysis by the consulting firm SH&E in 2000 to evaluate the airline for privatization, another review by the same firm was done in 2002. The conclusion was that TACV was still not profitable, as many routes lost money, and a restructuring was necessary before privatization could be initiated. Management of TACV made some adjustments by discontinuing certain routes, and streamlining the fleet.

However, while the business volume of TACV grew, its profitability was not regained and losses started to amount. In order to further support the privatization process, it was decided in 2004 to engage a specialized firm, which would: (i) implement the TACV's operational and financial restructuring, (ii) develop a sound recovery and privatization strategy for the airline, (iii) identify international partners and networks for TACV, and (iv) initiate integration and privatization negotiations. Under the Privatization and Regulatory Capacity Building Project, Credit No. 3121 of IDA, the firm Sterling Merchant Finance Ltd was hired to execute the said mandate.

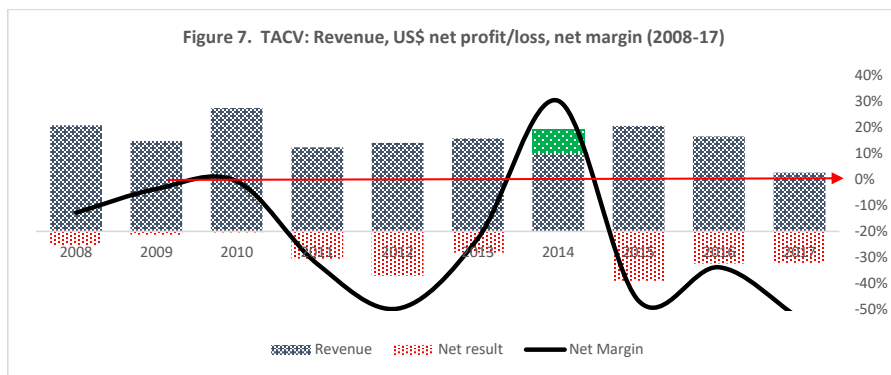
Sterling Merchant Finance Ltd "Sterling" performed a detailed analysis of TACV's business and operations. In 2007, Sterling presented a five-year business plan, which aimed, under the slogan "Vision 2012", to render the carrier highly profitable by 2011, achieving EUR 21 million profit with nine aircraft (two ATR42, two ATR72, two B757, and three A320). The business plan also foresaw an aggressive expansion of the

¹⁵ The following is a brief overview of the national airline, based on the 2016 assessment by a World Bank airline expert, a 2016 assessment by an independent Airlines Expert, and complemented by some recent performance information for 2017.



network and frequencies in Europe, South America, and West Africa, resulting in 1.2 million passengers on 18 international routes in 2011. Subsequently, Sterling engaged an experienced airline executive (Mr. Gilles Fillantreau) to manage the restructuring process at TACV. His mandate was to restructure TACV in accordance with Sterling’s business plan, and to identify an international partner to initiate integration and privatization negotiations.

Initially, the restructuring seemed to be successful, as management was able to reduce staff by 200, and streamline some operations. However, after the termination and nonrenewal of Sterling’s contract, many restructuring measures were stopped. As a result, the privatization of TACV became impossible, and losses started to increase rapidly again in 2011 and 2012 (Figure 7). Over the coming years, the GoCV had to support TACV by continuously injecting liquidity.



In 2013, the TACV mandated an individual consultant to perform a financial analysis to determine measures that would render cash flow positive. With the purpose of overcoming the company's difficult current financial situation and optimizing the utilization of its resources, together with the results obtained in the developed financial model, the consultant's recommendations were to temporarily discontinue nine routes, all of which had a negative financial contribution in the year 2011, and the continuation of 13 international routes. On the international network, TACV could generate a positive cash flow starting from the second year of the projected period, with an NPV of EUR 11 million (at 15% discount rate, 15 years operations, no perpetuity). With respect to the domestic route network, in order to make it financially viable, it had been calculated that an increase of 68% across all air fares would be necessary to assure a positive cash flow generation.

In 2014, TACV launched another study entitled “5 Year Strategic Business Plan”, which was prepared by the consulting firm InterVISTAS. The business plan suggested an aggressive expansion by opening several new routes to South America, Africa, and Europe, as well as a fleet increase from five to eleven aircraft. The business plan foresaw a more than doubling of passengers from 617,000 to 1,171,000 resulting in a total operating profit of about EUR 6 million in Year 5. The government presented this 5-year plan for financing under the PRSC series, and an adjusted two-year plan was eventually accepted in early 2015. The plan was never implemented, and the airline continued to see increased losses.



To yet again address the worsening situation, the GoCV mandated Brown Rudnick & Avisia Gulf in April 2016 to develop a restructuring strategy. The so called “Project Shine” proposed a set of measures, which downsize the company in terms of staffing levels and overhead, restructure debt, change the fleet, and privatize (or find new investors) to render the carrier profitable within two years. It was estimated, that the GoCV would need to finance USD 25 million in addition to USD 8 to 10 million for restructuring.

Recent Developments

Despite the numerous studies, business plans, and proposed measures for improvement, TACV never started to improve and gain profitability. In fact, between 2010 and 2015 income declined 44% while passengers carried declined 4%. In that period, every year resulted in losses, except 2014 where extraordinary income (sale of ground handling to ASA, write-off of debt) rendered the result positive. In 2016 and 2017 this poor performance continued, with net losses of 24.6 and 24.1 million USD respectively. In May 2016, the government requested support from the World Bank to assess the situation of TACV and propose a solution. A World Bank transport team visited Cabo Verde in June 2016 and carried out an assessment of the airline. The team looked at various options (Status Quo, Reduced Operations, Liquidation), and recommended a controlled winding down of operations given the very high costs of restructuring the airline and the low likelihood of success, combined with the government’s precarious fiscal position. The government questioned the conclusion and requested another opinion. The World Bank financed yet another assessment by an independent airlines specialist in the fall of 2016, which confirmed the findings of the Bank team, and recommended a partial liquidation and controlled winding down of operations with the sale of some assets.

Despite the findings and recommendations from these latest assessments, the government is making yet another attempt at restructuring and privatization. The strategy consists of (i) debt restructuring, (ii) TACV reorganization – including staff retrenchment (iii) a valuation of TACV, and (iii) the privatization transaction (sale of shares). As part of the business model, TACV has decided to move out of the domestic market and expand international operations with a view to create a regional hub in Cabo Verde. To this end, the authorities signed a management contract with Iceland Air in late 2017. The plan includes the hiring of a CEO, the provision of two B757-200 aircraft (leasing at market rate to arrive on 06NOV17), and the option for Icelandair to acquire 51% of TACV at a future date. The government is hoping that Iceland air will come in as an equity partner and invest in the company.

The most recent business plan, approved in late 2017, aims at establishing TACV as a hub operator in Cabo Verde serving initially 25 destinations (Europe: 10, USA: 5, South America: 6, and West-Africa: 4). The objective is to rapidly develop a new market between Europe, the US, South America, and Africa. This requires the aggressive expansion of the fleet, which will primarily be done with B757 aircraft.¹⁶ In 2018 the fleet will have four aircraft, six in 2019, and 11 by 2022 or 12. Management of Icelandair claims that a detailed route analysis was done, and that Yields were strong enough to reach a positive cashflow and profitable operations by 2019 in spite of aggressive fleet and market expansion. The cashflow projections forecast a cash need of US\$ 32 million in 2018, and US\$ 2,6 million in 2019, before operations become cashflow positive. Given the cash drain in 2017, it is estimated that TACV will need a working capital of US\$40 to 50 million to implement the said business plan.

¹⁶ Note that the last B757 was built in 2004. Most of the current fleet is 15 years or older, which suggests that by 2023 (end of projected business plan) most operators replaced the B757 (Icelandair is acquiring B737 MAX).



Table 3: List of SOEs (as of February 2018)

Nº	Company	State Share	Strategy	Timeline
1	ASA – Empresa Nacional de Aeroportos e Segurança Aérea, S.A	100.0%	Privatization/Concession	2019
2	ENAPOR – Empresa Nacional de Administração dos Portos, S.A	100.0%	Concession	2019
3	TACV – Transportes Aéreos de Cabo Verde, S.A	100.0%	Privatization	2018
4	CABNAVE - Estaleiros Navais	98.9%	Privatization	2019
5	IFH – Imobiliária, Fundiária e Habitat, S.A	100.0%	Restructuring	2018
6	LEC - Laboratório de Engenharia Civil, EPE	100.0%	Privatization	2019
7	CVFF - Cabo Verde Fast Ferry	53.2%	Privatization	2018
8	ELECTRA – Empresa de Electricidade e Águas, S.A	77.7%	Privatization/Concession	2019
9	CERMI - Centro de Energia Renováveis e Manutenção Industrial, EPE	100.0%	Restructuring	2018
10	ENACOL – Empresa Nacional de Combustíveis, S.A	2.1%	Privatization	2018
11	CABEOLICA, S.A	10.8%	Keep Public	N.A
12	APN - Águas de Porto Novo, S.A	10.0%	Privatization	2019
14	RTC – Rádio Televisão Cabo-verdiana, S.A	100.0%	Keep Public	N.A
15	INCV - Imprensa Nacional de Cabo Verde	100.0%	Keep Public	N.A
16	INFORPRESS – Agencia de Notícias de Cabo Verde, S.A	100.0%	Keep Public	N.A
17	CCV - Correios de Cabo Verde, S.A	100.0%	Privatization	2018
18	CVTELECOM – Cabo Verde Telecom (Shares)	3.4%	Privatization	2018
	CVTELECOM – Cabo Verde Telecom (Concession Contract)		Concession	2018
19	NOSI - Núcleo Operacional Sistema Informação, EPE	100.0%	Privatization	2019
20	SDTIBM – Sociedade de Desenvolvimento de Turismo Integrado das Ilhas de Boavista e Maio, S.A	51.0%	Privatization	2018
21	EHTCV - ESCOLA DE HOTELARIA E TURISMO, EPE	100.0%	Restructuring	N.A
22	Agro-Quibala - Sociedade Cabo-verdiana Agro-industrial de Quibala	100.0%	Privatization	2018
23	Atlantic Tuna – Sociedade Cabo-verdiana e Angolana de Pesca, S.A	60.0%	Liquidation	2018
24	EMPROFAC – Empresa Nacional de Produtos Farmacêuticos, S.A	100.0%	Privatization	2019
25	FIC – Feira Internacional de Cabo Verde, S.A	100.0%	Privatization	2018
26	SCS – Sociedade Caboverdiana de Sabões, S.A	68.9%	Privatization	2018
27	SONERF - Sociedade Nacional de Engenharia Rural e Florestas, EPE	100.0%	Privatization	2019
28	SGZ – Sociedade de Gestão de Lazareto, S.A	33.0%	Privatization	2019
29	BVC - Bolsa de Valores de Cabo Verde	100.0%	Privatization	2019
30	PROMOTORA – Sociedade de Capital de Risco, S.A	26.7%	Liquidation	N.A
31	SISP – Sociedade Interbancária de Sistemas de Pagamentos, S.A	27.0%	Keep Public	N.A
32	SOFHIS-GERE - Sociedade Gestora de Fundos de Habitação de Interesse Social	60.0%	Liquidation	N.A



ANNEX 6: DISBURSEMENT SCHEDULE

Target	Amount Allocated (million US\$)	Disbursement Schedule				
		2018	2019	2020	2021	2022
DLI 1. Retrenchment plan approved and announced by TACV	3	3 US\$ Million (July 2018 – retroactive financing)				
DLI 2. Grievance mechanism established	3	3 US\$ Million (Sep-Oct 2018)				
DLI 3: Staff targeted by the retrenchment plan is retrenched	8	8 US\$ Million (Sep-Oct 2018)				
DLI 4: Detailed Annual SOE reports	2	0.4 US\$ Million	0.4 US\$ Million	0.4 US\$ Million	0.4 US\$ Million	0.4 US\$ Million
	16	14.4	0.4	0.4	0.4	0.4