



Project Information Document/ Integrated Safeguards Data Sheet (PID/ISDS)

Concept Stage | Date Prepared/Updated: 24-May-2017 | Report No: PIDISDSC21887



BASIC INFORMATION

A. Basic Project Data

| | | | |
|--|---|--------------------------------------|---|
| Country Sao Tome and Principe | Project ID P162129 | Parent Project ID (if any) | Project Name Sao Tome and Principe: Institutional Capacity Building Project (P162129) |
| Region AFRICA | Estimated Appraisal Date Nov 27, 2017 | Estimated Board Date Mar 20, 2018 | Practice Area (Lead) Finance & Markets |
| Financing Instrument Investment Project Financing | Borrower(s) Ministry of Finance, Trade and Blue Economy | Implementing Agency Central Bank | |

Proposed Development Objective(s)

To improve selected public institutions' capacity to perform their functions.

Financing (in USD Million)

| Financing Source | Amount |
|---------------------------|--------------|
| IDA Grant | 10.00 |
| Total Project Cost | 10.00 |

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|---|---|
| Environmental Assessment Category C-Not Required | Concept Review Decision Track II-The review did authorize the preparation to continue |
|---|---|

Other Decision (as needed)

B. Introduction and Context

Country Context

1. São Tomé and Príncipe is a lower middle income country with a population of nearly 200,000 located on two islands



off the western equatorial coast of Central Africa. Gross domestic product (GDP) per capita is USD 1,669. Around one-third of the population lives on less than USD 1.9 per day in purchasing power parity (PPP) terms and more than two-thirds of the population is poor using a poverty line of US\$3.1 PPP per day. It is highly dependent on external support—with 45 percent of its budget financed by development partners. Unemployment was at 13.6 percent in 2012 (last data available). Two sectors—agricultural and retail—generate 50 percent of all jobs in the country.

2. Economic growth has been stable, but it is heavily reliant on public spending and susceptible to fiscal, financial, and external shocks. STP has grown at an average rate of 4.5 percent from 2009 to 2016 with no recessions and little fluctuation. GDP growth in 2016 is provisionally estimated at 4 percent and has lost momentum during the year due to reduced public expenditure. Agricultural goods, especially cocoa, constitute the bulk of STP's exports. Tourism is an important area of economic activity, but STP is not a tourism-dependent economy. Oil exploration has taken place since 2013, but commercial activity is not expected before 2020. Few goods are produced locally, leaving STP dependent on imports, including the oil needed to generate power. Growth has not been pro-poor because the most vulnerable population lacks the skills to access economic opportunities. Social protection policies have not been able to alleviate poverty and provide a path for the vulnerable population to grow out of poverty.

3. Poverty reduction has been marginal despite solid economic growth and public investment. Urban poverty is higher than rural poverty due to limited employment opportunities, notably for youth. Human capital formation has steadily progressed in recent years, as health and education have improved. São Tomé and Príncipe had remarkable success in curbing infant mortality below sub-Saharan Africa averages in malaria control and maternal mortality. Between 1980 and 2014, its Human Development Index increased by about 23 percent, life expectancy at birth increased by 5.9 years, and mean years of schooling by 3 years. The Government is undertaking a new household survey to update information on poverty and social indicators, which will commence data collection in late May 2017 and is scheduled to be completed by October 2017.

4. Income generation is hindered by limited productive capabilities and low competitiveness. The currency peg to the euro, which was introduced in January 2010, provides an anchor for price stability and led to some limited real effective exchange rate appreciation. During 2010–15 the average current account deficit was 20 percent of GDP, which was financed by external assistance and FDI. From 2013–16, external grants were equivalent to 13 percent of GDP. São Tomé and Príncipe is at high risk of debt distress. Total external public debt was 75.5 percent of GDP in 2016, relative to 58.8 percent of GDP in 2015 according to the recent debt sustainability analysis. The increase in debt stock is mainly due to the incorporation of domestic arrears (17 percent of GDP). STP's main fiscal risks come from its inefficient SOE sector.

Sectoral and Institutional Context

Financial sector

5. São Tomé and Príncipe has one of the smallest independent financial systems in the world. Its financial sector is comprised of seven commercial banks that together control 98 percent of total sector assets, two insurance firms that specialize in property and casualty business, and four small consumer lenders. São Tomé and Príncipe liberalized its banking sector in the early 2000s, which grew rapidly as a result and in anticipation of oil income. Bank assets were equivalent to 58 percent of GDP in 2016 relative to 26 percent of GDP in 2001 (see Table 1 in Annex). Although there are 908 depositors per thousand adults (2015), access to basic savings and payment services is limited, as many of these accounts are inactive or non-resident. The central bank (Banco Central de São Tomé e Príncipe – BCSTP) supervises banks, insurance companies, and other financial institutions.



6. High asset impairment limits the availability of credit to the private sector. In 2016, non-performing loans (NPLs) represented 27 percent of gross credit (up from 15 percent in 2012) and 10 percent of assets. Provisions as a percent of non-performing loans were high at 87 percent at end-2016, albeit down from a peak of 165 percent in 2013. Growth of credit to the economy has slowed, mostly a result of capital preservation efforts, which are reflected in increased liquidity and holdings of foreign assets on banks' balance sheets. The sector also underwent some stress following the central bank's decision to resolve one of the largest banks in 2016 (the third bank to fail in São Tomé and Príncipe since 2010). In response, the authorities have initiated an ambitious program of financial sector reforms, underpinned by the Financial Sector Development Implementation Plan (FSDIP), and introduced a new framework for resolution of distressed banks and ordered capital raising by some of the weaker banks. The central bank still faces constraints in conducting effective on-site supervision, due to limitations in terms of staff and depth of technical skills available. There is also a need to understand the magnitude of the problem by conducting a detailed asset quality review (AQR).

7. Financial infrastructure is insufficient to meet the needs of a growing and modern economy. Banks' payment systems are not connected to international payment networks and the BCSTP maintains the only connection to SWIFT. The central bank's credit registry receives few lender inquiries, given data gaps, and does not provide consolidated credit concentration information by institution and borrowers, which is necessary for lenders to assess loan repayment capabilities of potential borrowers. There is no electronic registry for security interests in movable collateral.

Public financial management

8. Government effectiveness and regulatory quality is weak while low domestic revenue mobilization and poor expenditure control limits the state's capacity to provide needed services. Tax revenues represented only 13.5 percent of GDP on average between 2014-16, which is among the lowest in the world and below the minimum threshold needed for the provision of basic public services. Revenue shortfalls stem from fluctuation of oil prices and challenges to collect custom duties on fuel imports, lagging capacity in tax administration, and stalled efforts to widen the tax base. The Government has accumulated arrears, mainly to state-owned utility companies. A limited number of state-owned enterprises (SOEs) submit financial statements and regular reports to the Treasury, and there are no systematic routines for assessment and analysis of the fiscal risk linked to SOEs.

9. The credibility of public finances and expenditure forecasting is weak. There are significant variations between initial allocation and expenditure over-runs (more than 10 percent of budgeted expenditures) due to lack of predictability of external grants and optimistic domestic revenues projections. A 2013 Public Expenditure Financial Assessment (PEFA) showed progress in some areas of public financial management (PFM), particularly creation of a Treasury Single Account and the Integrated Financial Management System (IFMIS) instituted in 2009. It also highlighted challenges in expenditure control (including payroll), lack of oversight of fiscal risk from other public entities, inadequate auditing, low quality and infrequent annual financial statements, and poor tax administration.

10. Weak auditing and accounting standards reduce the prospects for transparent financial management and revenue collection, and make credit analysis difficult thereby constraining access to finance. A 2014 Accounting and Auditing Report on Observance of Standards and Codes (ROSC) identified minimal understanding of the role and contribution of the accountancy profession, lack of legislation stipulating auditing standards, and no official organization to establish and adopt accounting and auditing standards. The former has been addressed with the recent passage of a law establishing a professional accountancy organization (Ordem dos Técnicos Oficiais de Contas e Auditores – OTOCA), although they have yet to establish national accounting and auditing standards.

Systems for registering national statistical data and immovable property



11. São Tomé and Príncipe lacks some of the basic data required to inform economic and social policy. Timely data is absent, particularly on poverty, inequality, socio-economic issues, and agriculture. The latest poverty and inequality data is seven years old and only two poverty surveys have been implemented in the last 25 years (in 2000 and 2010). Despite progress, the National Statistical Institute (Instituto Nacional de Estatística [INE]) is not able to produce reliable statistics on a regular basis, fill data gaps, nor improve data quality. There is only one INE staff with experience in household surveys, who is close to retirement. In general, staff at INE and other ministries have limited analytical capacity to interpret economic data. São Tomé and Príncipe's lack of improvement in the World Bank's Statistical Capacity Indicator (score of 60 out of 100, the same as the Sub-Saharan Africa's average) is partly due to the lack of regular surveys to monitor key socio-economic indicators, an outdated base year for national accounts, and the inability to accurately report basic social statistics.

12. Despite recent progress, the existing land and property registries are inefficient. The existing registry is paper-based and procedures for consultation and registration are performed manually. As a result, registration of property is inefficient and expensive, which undermines the value of property as collateral for bank credit.

Relationship to CPF

13. The FY14-FY18 Country Partnership Strategy (CPS) supports São Tomé and Príncipe in promoting macroeconomic stability and competitiveness, and in reducing vulnerability and strengthening human capacity. The proposed project is aligned with both pillars and with the Performance and Learning Review under preparation. Key areas of the project are aligned with the second Development Policy Operation under preparation. The Government's goals for financial development are reflected in the 2016 Financial Sector Development Implementation Plan, which was commissioned by the central bank and completed with World Bank's technical support.

C. Proposed Development Objective(s)

14. To improve selected public institutions' capacity to perform their functions.

Key Results (From PCN)

15. Key results include enhanced institutional capacity in financial sector policy and regulation, public financial management and fiscal planning, statistical capacity, and property registration. Improving institutional capacity in these areas will result in: (i) a more stable, competitive, and inclusive financial system capable of providing affordable financial services and products, a precondition for economic development and poverty reduction; (ii) better revenue forecast, expenditure controls, and oversight of state-owned enterprises (SOEs), which will improve the credibility, accountability and transparency of public finances; (iii) timely and quality statistics to inform policy making; and (iv) more transparent and efficient property registration, which increases its potential to be used as collateral for bank lending.

D. Concept Description

16. The project will support institutional capacity building at the Central Bank, Ministry of Finance, National Statistics Institute, and the Property Registry.

SAFEGUARDS

A. Project location and salient physical characteristics relevant to the safeguard analysis (if known)



Technical assistance will be provided to the central bank and line ministries located in the city of Sao Tome.

B. Borrower’s Institutional Capacity for Safeguard Policies

To be determined

C. Environmental and Social Safeguards Specialists on the Team

Kristyna Bishop, Medou Lo

D. Policies that might apply

| Safeguard Policies | Triggered? | Explanation (Optional) |
|--|------------|--|
| Environmental Assessment OP/BP 4.01 | No | The project is designed to support the Central Bank, Ministry of Finance, National Statistics Institute, and the General Directorate for Registries and Notaries to improve their institutional capacity in the area of financial sector policy and regulation, public financial management and fiscal planning, statistical capacity, and property registration. The project is expected to have no adverse environmental and social impacts. |
| Natural Habitats OP/BP 4.04 | No | |
| Forests OP/BP 4.36 | No | |
| Pest Management OP 4.09 | No | |
| Physical Cultural Resources OP/BP 4.11 | No | |
| Indigenous Peoples OP/BP 4.10 | No | |
| Involuntary Resettlement OP/BP 4.12 | No | |
| Safety of Dams OP/BP 4.37 | No | |
| Projects on International Waterways OP/BP 7.50 | No | |
| Projects in Disputed Areas OP/BP 7.60 | No | |

E. Safeguard Preparation Plan

Tentative target date for preparing the Appraisal Stage PID/ISDS

Nov 13, 2017

Time frame for launching and completing the safeguard-related studies that may be needed. The specific studies and their timing should be specified in the Appraisal Stage PID/ISDS

Not applicable.



CONTACT POINT

World Bank

Julian Casal, Alvin Etang Ndip, Roberto O. Panzardi
Senior Financial Sector Economist

Borrower/Client/Recipient

Ministry of Finance, Trade and Blue Economy
Sandro Trigueiro
Advisor
sandrotrigueiros@gmail.com

Ministry of Finance, Trade and Blue Economy
Lindley Monteiro de Jesus
Advisor
linjesus@hotmail.com

Implementing Agencies

Central Bank
Dilson Tiny
Executive Director
dtiny@bcstp.st

FOR MORE INFORMATION CONTACT

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

APPROVAL

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| Task Team Leader(s): | Julian Casal, Alvin Etang Ndip, Roberto O. Panzardi |
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Approved By

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|---------------------------|----------------------------------|-------------|
| Safeguards Advisor: | Maman-Sani Issa | 23-May-2017 |
| Practice Manager/Manager: | Caroline Marie C. Cerruti Hailey | 24-May-2017 |
| Country Director: | Elisabeth Huybens | 24-May-2017 |

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