AFRICAN DEVELOPMENT BANK

POWER SECTOR REFORM SUPPORT PROGRAM (PSRSP)
COUNTRY: ANGOLA

Appraisal Report

ONEC / OSGE

April 2014

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CURRENCY EQUIVALENTS

As of March 2013

Angola Currency Unit = Angolan Kwanza (AON)

1 Unit of Account (UA)	=	AON 151.0301
1 Unit of Account (UA)	=	USD 1.54740
1 Unit of Account (UA)	=	EUR 1.12025
1 Unit of Account (UA)	=	GBP 0.927257
1 American Dollar (USD)	=	AON 105

Fiscal Year

January 1-December 31

WEIGHTS AND MEASURES

1 metric tonne	=	2204 pounds (lbs)
1 kilogramme (kg)	=	2.200 pounds (lbs)
1 metre (m)	=	3.28 feet (ft)
1 millimetre (mm)	=	0.03937 inch (“)
1 kilometre (km)	=	0.62 mile
1 hectare (ha)	=	2.471 acres

ACRONYMS AND ABREVIATIONS

ADB	African Development Bank
CSP	Country Strategy Paper
CPIA	Country Policy and Institutional Assessment
GDP	Gross Domestic Product
EDEL	Empresa de Distribuição de Electricidade
EIU	Economic Intelligence Unit
ENE	Empresa Nacional de Electricidade
ESIA	Environment and Social Impact Assessment
ESMP	Environmental and Social Management Plan
GAMECK	Gabinete de Aproveitamento do Médio Kwanza
GCI	Global Competitiveness Index
GoA	Government of Angola
GRB	Gender Responsive Budget
IFMIS	Integrated Public Financial Management
IPP	Independent Power Producers
IRSE	Instituto Regulador do Sector Electrico (Institute of Energy Sector Regulation)
MINEA	Ministerio da Energia e Aguas (Ministry of Energy and Water)
MTFF	Medium-term Fiscal Framework
MINFAMU	Ministry of Family and Promotion of Women
NAPA	National Action Plan for Climate Change Adaptation
NDP	National Development Plan
NESSP	National Energy Security Strategy and Policy
PBO	Program Based Operation
PCR	Project Completion Report
PEMSR	Public Expenditure Management and Fiduciary Systems Review
PFM	Public Financial Management
PIP	Project Investment Program
PRSP	Poverty Reduction Strategy Paper
PSRSP	Power Sector Reform Support Program
PTSE	Electricity Sector Transformation Program
QFO	Quasi-fiscal operations
SIGFE	Treasury Single Account, Automated Financial Management System (*Sistema Integrado de Gestão Financeira do Estado*)
Sonangol	Sociedade Nacional de Combustíveis de Angola (National petroleum company)
UA	Units of Account
UNFCCC	United Nations Framework Convention on Climate Change

LOAN INFORMATION

CLIENT'S INFORMATION

Borrower	Republic of Angola
Executing Agency	Ministry of Finance; and Ministry of Energy and Water

FINANCING PLAN 2014-2016

Source	Amount in USD	Instrument
African Development Bank (ADB)	1,000.0 million	Loan

ADB FINANCING INFORMATION

Loan currency	: United States Dollars (USD)
Type of Loan	: Enhanced Variable Spread Loan
Lending rate	: Base Rate (a) + Funding Cost Margin (b)+Lending Spread (c)
	a. Base Rate: Floating base rate based on 6-month LIBOR with a free option to fix the base rate
	b. Funding Cost Margin: the six months adjusted average of the difference between: (i) the refinancing rate of the Bank as to the borrowings linked to 6 month LIBOR and allocated to all its floating interest loans denominated in USD and (ii) 6-month LIBOR ending on 30 June and on 31 December. The Funding Cost Margin shall be determined twice per year on 1 January for the semester ending on 31 December and on 1 July for the semester ending on 30 June.
	c. Lending Spread: 60 basis points (0.60%)
Commitment Fee	: A graduated commitment fee ranging from 25 to 75 basis points, applicable to amounts non-disbursed within the timeframe negotiated in the loan disbursement calendar.
Maturity	: up to 20 years including a 5-year grace period.
Number of Tranches	: Two tranche disbursement of USD 600m in 2014 and USD 400m in 2015

TIME FRAME - MILESTONES

Concept Note Approval	March 2014
Appraisal	March 2014
Board approval	May 2014
First Tranche Disbursement	July 2014
Second Tranche Disbursement	July 2015
Project Completion	December 2015

PROGRAM EXECUTIVE SUMMARY

Paragraph	Topics to cover
Program Overview	Program Name: Angola – Power Sector Reform Support Program (PSRSP) Geographic Scope: Entire Nation Overall Timeframe: 2014-2015 Expected Outputs: The key outputs of the program are: (a) power sector restructuring completed; (b) improved power sector regulatory environment; (c) improved private sector participation in the power sector; (d) improved budget credibility and transparency; and (e) improved efficiency and value for money in procurement.
Program Outcomes	The expected outcomes of the program are (a) improved operational efficiency, competitiveness and sustainability of the electricity sector, and (b) strengthened transparency and efficiency of public financial management.
Program beneficiaries	The direct beneficiaries are Angola's key public institutions responsible for PFM, and ministries responsible for the delivery of energy infrastructure development. The indirect beneficiaries are the population of Angola in general, and private sector who will benefit from better access to reliable and affordable electricity supply as well as transparency and efficient management of public finance and procurement practices. The operation will have a positive social and gender impact. Reform in the energy sector is expected to expand access to electricity at affordable costs for the local population, particularly for the very poor who are concentrated in rural areas and make up 45.2% of the entire population out of which 72% are living in poverty
Needs Assessment	The Government has shown strong commitment to reform and increase public investment in transformational infrastructure development projects to support diversification and inclusive economic growth. The implementation of economic reform has registered progress in addressing the enormous challenges that arose from 27-year civil war. The Energy and Water Sector Action Plan for 2013-17 estimates financing needs of US$23billion to implement ambitious reform and investment in the power sector. Government's own resources will not be sufficient to meet the financing requirements. In addition, the Government's decision to approach the Bank for budget support also reflects its clear desire to adopt more transparent and modern budget financing instruments and a deliberate objective to move away from bilateral *Export Credit Lines* which are expensive and do not offer longer term financing.
Bank's Added Value	The Bank has a continent-wide experience and engagement in Africa, covering infrastructure development, institutional reforms at both the general and sector levels. The proposed budget support program builds on the Bank's experience in the power sector and PFM reforms and its position as a trusted partner. This allows it to promote dialogue on sensitive issues, and leveraging reforms in power sector governance and public finance, which are essential for economic diversification and competitiveness, and thus promoting inclusive and sustainable growth in Angola. The Bank has built a consistent track record in infrastructure development including power in RMCs and is scaling up its support through the new financing mechanisms such as Africa50. The Bank's support will bring expertise, knowledge and best practices to inform the government reform program, thus creating credibility, consistency and coherence in the reform process. Angola's determination to engage with the Bank in a sustained policy dialogue as a "trusted and preferred" partner, will send a powerful signal to the market and the international community that Angola is committed to doing business differently. The PSRSP will create the necessary platform for policy dialogue and advisory services.
Institutional development and Knowledge building	The program will contribute to consolidating available knowledge on the power sector. Building on the experience gained from other operations, the operation will be complemented by the ongoing PFM project and funds earmarked for capacity building to enhance the added value of the sector budget support instrument. The Bank will capture the knowledge from this program through careful monitoring and evaluation of program expected outputs and outcomes, joint government and Bank review missions, and the Project Completion Report (PCR).

RESULTS BASED LOGICAL FRAMEWORK

Country and project name: Angola Power Sector Reform Support Program (PSRSP)
Purpose of the project: Promote inclusive and sustainable growth by accelerating electricity sector reform and strengthened governance in public finance management[1]

RESULTS CHAIN		PERFORMANCE INDICATORS			MEANS OF VERIFICATION	RISKS/ MITIGATION MEASURES
		Indicator (including CSI)	Baseline	Target		
IMPACT	Contribute to inclusive and sustained growth by accelerating electricity sector reform and strengthened public finance management	GDP growth	4.1% (2013)	5.9% (2016)	IMF & budget report	**Macroeconomic risks due to volatility of the commodity prices /** oil price shocks. ***Mitigation***: Coordinated monitoring and dialogue around macroeconomic management to manage shocks, including IMF article IV consultations. Accelerate implementation of on-going structural reforms to increase the competitiveness of domestic production / diversification. Combination of continued investment in infrastructure and social services with prudent macroeconomic policies (e.g., conservative assumptions regarding oil price projections, sizeable reserve levels, effective management of the Sovereign Wealth Fund) **Fiduciary risk including corruption. *Mitigation***: A fiduciary risk assessment was carried out and set out mitigation measures to the identified risks. The mitigation measures include ongoing reforms to the budget process, procurement, and the Public Investment Program, all supported by the ongoing Bank's institutional support project; and the proposed operation through Component 3. **Implementation capacity risk.** Capacity constraints in Government could cause delays in the implementation of reforms.
		Access to "on-grid" electricity services	less 30% (2013)	42% (2016) and 60% by 2025	Annual Progress Report	
		Mo Ibrahim Index and CPIA Cluster D	41 (2013) and 3.18 (2012)	50 (2016) and 3.5 (2016)	Mo Ibrahim Index and CPIA	
		Global Gender Gap Index	87/135 (2011)	62 (2016)	WEF Gender Gap Report	
OUTCOMES	Outcome 1: Improved operational efficiency, competitiveness, and sustainability of the electricity sector	Electricity sector revenue collection (US$ millions)	90	108 by 2015 and 140 by 2016	Power sector reform monitoring report	
		% of Grid Customers metered	less than20%	40% by 2016		
		No. of IPP projects awarded in the electricity sector based on new regulations	0 (2013)	At least 6 contracts based on renewable energy (2016)		
		Distribution System Availability Index((ASAI[2]) in %	Less 60%	75% by 2016	ENDE Reports	
		% of women in board (utilities and IRSE) & % of women in Senior Management positions	a) 23% (2013) b) 23% (2013)	>30% by 2016 >30% by 2016	Companies annual report	
		Number of women who received professional training	1500 in 2012	Additional 1,200 in 2015 1,200 in 2016	MINFAMU annual report	
	Outcome 2: Strengthened transparency and efficiency of public finance	Increased execution rate of the PIP	50% (2013)	75% (2016)	PIP annual report	
		Variance between expenditure outturns and original budget	>25% (2013)	< 10% (2016)	Budget execution reports	
	Component 1: Restructuring the Power Sector & Improving Regulatory Environment					
OUTPUTS	Output 1.1 Power sector restructured	Unbundling of existing power utilities (into Generation, Transmission and Distribution companies)	Vertically integrated utilities	a) Presidential Decree establishing 3 utility companies signed by 2014	Presidential Decree	
		Revised General Electricity Law – Lei 14A/)96	Draft law	Draft revised General Electricity Law submitted to Cabinet *"Casa Civil"* by 2014	Letter from the Minister of Energy and Water	
		Establishment of a legal framework defining the contractual, commercial and operational relationships between the power utilities	None	Contractual Agreements (PPA etc.) signed between the three utility companies by 2015	Agreements	

[1] The operation aims at complementing and accelerating ongoing Government efforts to address public sector institutional weaknesses and infrastructure inadequacies that are a major bottleneck to competitiveness and diversification of the economy.
[2] Average Service Availability Index

Output 1.2: Improved sector regulatory environment, and enhanced environmental and social safeguards	Introduction of new tariff framework progressively oriented towards cost recovery and re-focusing subsidies to the most vulnerable Households	Outdated tariff framework	a) Submission of a tariff proposal to the Economic Commission by 2014 b) Adoption of a new tariff adjustment by 2015	Letter from Minister of Finance IRSE Reports	***Mitigation***: The operation includes a complementary capacity building component with the aim to strengthening capacity in areas supported by PBO.
	Reinforcing IRSE's mandate and independence as the sector power regulator	Draft Regulation	Amendment of the Presidential Decree establishing IRSE by 2015	Presidential Decree	
	No of staff (women and men) trained at various levels in the three utilities and IRSE	None	30 Directors/Management staff, 50 mid-level Managers and 433 operations staff by 2015 (>30% women)	Supervision and Reform progress reports	
Component 2: Fostering private sector investment in renewable energies					
Output 2.1: Improved incentives and business environment for private sector participation	Submission of a Renewable Energy White Paper	None	Renewable Energy White Paper submitted to Cabinet *"Casa Civil"* by 2014 and approved by 2015	*Letter from the Minister of Energy and Water*	
	Publication of Renewable Energy Resource Mapping	None	Renewable Energy Resource Mapping Published by 2014	Published RE Resource Map	
	Publication of Renewable Energy Regulations and Feed-In Tariff	None exists	Adoption of RE Regulation and launch of RE Feed-In Tariff by 2015	Published RE Regulation and IRSE reports	
Component 3: Enhancing efficiency and transparency in public finance to achieve value for money in public investment					
Output 3.1 Strengthened budget credibility and transparency and enhanced gender responsiveness	Publication of the 2014 "citizen" budget	None	2014 "citizen" budget published and posted in the MINFIN website by 2014	MINFIN website	
	Publication of 2013 Oil Revenue Reconciliation Report	Reports for 2011 and 2012	2013 Oil Revenue Reconciliation Report published and posted in the MINFIN website by 2014		
	Submission of the 2012 General State Accounts to the Court of Accounts, and Parliament	2011 accounts submitted	2012 General State Accounts submitted to the Court of Accounts, and Parliament by 2015	Court of Accounts reports	
	Adoption of Medium Term Reform Action Plan	PEMFSR diagnostic planned for 2014	PFM Reform Action Plan adopted by 2015	Action Plan	
	Evaluation of gender responsive expenditures in the financial reports	None	Evaluation report endorsed	Evaluation Report	
	Adoption of Gender Policy to mainstream gender in line ministries	None	Gender policy adopted by 2014, and Gender action plan rolled out by 2015	MINFAMU Progress Report	
Output 3.2 Improved efficiency and value for money in procurement	Approval of Public Procurement Action Plan	None	Public Procurement Action Plan approved by the MINFIN by 2014	Letter from MINFIN	
	Establishment of Procurement Portal	None	Procurement Portal online by 2014	Procurement Portal	
	Revision of Procurement Law, and adoption of procurement regulation and standard bidding documents (SBD)	Law enacted in 2010 Draft regulation 2013	a) A revised procurement bill adopted by 2015 b) Regulation adopted by 2015 b) SBD adopted by 2015	Legal texts	
Components					
Major activities under each component: Power sector regulatory framework review, drafting new legal frameworks, implementation of power sector reform action plan, change management, capacity building support, and public finance reform action plan implementation. Monitoring and supervision missions. Financing from AfDB (US$ 1,000 million). US$ 6 million will be earmarked for the Capacity building Program for the power sector and key Ministries involved in power sector development including the MINEA and MINFAMU					

REPORT AND RECOMMENDATIONS OF THE MANAGEMENT OF THE ADB GROUP TO THE BOARD OF DIRECTORS ON A PROPOSED LOAN TO ANGOLA FOR THE POWER SECTOR REFORM SUPPORT PROGRAM

I. THE PROPOSAL

1.1 **Management submits the following Report and Recommendation for a loan of USD 1,000 million to the Republic of Angola to finance the Power Sector Reform Support Program (PSRSP) over two years (2014 – 2015).** This is a two-tranche sector budget support operation and responds to a request from the Government of Angola (GoA) in November 2013. The program is aligned with Angola's National Development Plan (2013-2017), and the National Energy Security Strategy and Policy (NESSP) of September 2011. The operation supports the GoA's policy priorities and reform program, as set out in the Letter of Development Policy (Appendix 1). Program implementation will be further strengthened through the provision of complementary technical assistance and capacity building support.

1.2 **Angola's transition to the Bank's middle-income country (MIC) borrowing status and from ADF recipient to a contributor to the ADF-13 and a potential contributor to Africa50 fund reflects the GoA's strong economic performance as well as commitment to consolidate relationships with key strategic partners, in particular the Banks.** Angola has come a long way since the end of a 27-year civil war (1975-2002). The Government has been implementing governance and structural reforms primarily aimed at maintaining peace and stability, enhancing fiscal consolidation, and achieving macro-economic stabilization.. Once an agricultural based economy, the country is now the second leading oil-producer in Africa with a per capita GDP estimated at USD 5,706 in 2012, up from less than USD 1,000 in 2001. Angola has remained politically stable, with peaceful multi-party elections organized in 2008 and 2012, and achieved high levels of economic growth (over 10% on average since 2002). However, living standards remain low for most Angolans and infant mortality rate is among the worst in the world. Like in many resource-rich countries, income inequality represents a major challenge.

1.3 **Angola has made significant progress in rebuilding its economy and physical infrastructure which was severely damaged by the 27 years of civil war.** The GoA has been making substantial investments to restore and reconstruct the social and economic infrastructure that was destroyed during the civil war. But increased investments in infrastructure have not necessarily translated into inclusive growth. For example, only 30% of Angola's population benefits from access to power, lower than the 46% average for the nation's resource-rich African peers. Going forward, the operation seeks to support ongoing reforms aimed at addressing the power sector's structural weaknesses and increasing the level, efficiency and effectiveness of the sector's spending to support diversification and competitiveness of the economy.

1.4 This Program is the outcome of close and sustained dialogue between the Bank and the Angolan Authorities. In this dialogue, the Government showed its strong determination to accelerate and deepen ongoing reforms aimed at restructuring the power sector, and strengthening the PFM systems. To do so, it requires the support of its partners, with the Bank taking the lead. To this end, the Bank is working in synergy with the other partners active in Angola. The Bank's main value addition lies in the fact that, as a trusted partner it will bring the needed expertise and technical knowledge required for the successful implementation of the Government's investment program and play a catalytic role in creating a platform for policy dialogue between development partners and GoA.

1.5 **The operation is fully aligned with the objective of the Bank Group Ten Year Strategy (2013-2022), and Country Strategy Paper for Angola (2011-2015).** Further, it is consistent with the Bank Group's Energy Sector Policy, as well as the Governance Strategic Framework and Action Plan (GAP II, Draft 2014-2018). It is also in line with the PBO Policy.

1.6 **The overarching objective of the operation is focused on promoting inclusive growth by strengthening power sector reform, and greater transparency and efficiency in public finance.** The program is built around three areas of engagement in which the GoA intends to accelerate reform implementation: (i) restructuring the power sector, (ii) fostering private sector participation in the power sector, and (iii) enhancing transparency and efficiency in public financial management, to achieve value for money in public investment. The common theme across each of these areas is to increase efficiency and effectiveness of public spending in the power sector, which accounts for a considerable share of the national government's public investment program (US$ 4.6 billion per year), to boost its contribution to inclusive economic growth. To this end, the operation is designed to support GoA's efforts to enhance power sector governance and PFM system. The expected program outcomes are: (a) improved operational efficiency, competitiveness and sustainability of the power sector, and (b) strengthened transparency and efficiency of PFM. Ultimately, the operation is expected to contribute to enhancing the foundation for resilient and inclusive growth through broader access to reliable electricity supply. Improvement of the performance of the power sector is key to the GoA's efforts to (a) diversify the economy and improve economic competitiveness for job creation; and (b) scale up the provision, and access to public services (e.g. health, education) thereby raising the living standards of ordinary Angolans.

II. COUNTRY AND PROGRAM CONTEXT

2.1 Government overall development strategy and medium-term reform priorities

2.1.1 **Angola's long-term development strategy is outlined in the Vision 2025 and National Development Plan (NDP, 2013-2017)**. Building on the country's considerable resources, the Vision 2025 set out Angola's aspiration for equitable and inclusive development. NDP is anchored on key policy priorities (Box 1) and provides strategic direction to implement an ambitious program of reforms aimed at improving the well-being of all Angolans, , expanding youth employment, diversifying the economy and reducing extreme poverty. It includes far reaching reforms in key sectors of the economy, such as the power sector. Underpinning the NDP is a public expenditure management reform program that aims to increase the level of efficiency and effectiveness of public investment. The proposed operation seeks to support GoA's policy agenda to promote sustained and inclusive growth, through power sector and public finance management (PFM) reforms.

Box 1: National Development Priorities

- Macroeconomic stability;
- Modernization of public administration and public finance management;
- Entrepreneurship and private sector development;
- Accelerated infrastructure development (energy, water, roads, and railway);
- Job creation and economic diversification;
- Human development (education, science and technology, health, gender, rural development and housing); and
- Better natural resources management (agriculture, fisheries, oil, and mining).

Source: National Development Plan, 2013-2017

2.2 Recent developments, perspectives, constraints and challenges

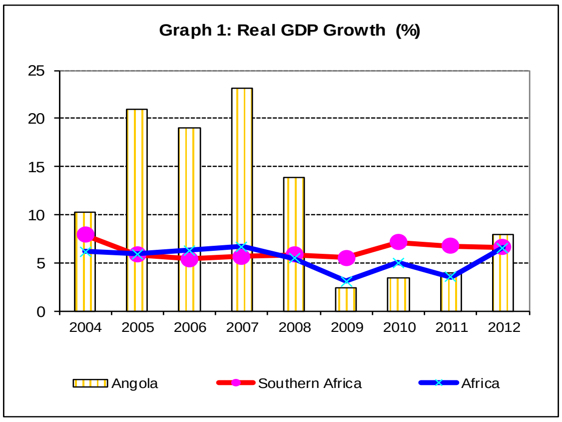
A. Political Context

2.2.1 **Angola's political environment is stable..** In 2002, the country ended a 27-year civil war that began soon after independence from Portugal in 1975. The war was fought mainly between the groups that had successfully fought for independence: the Popular Movement for the Liberation of Angola (Movimento Popular de Libertação de Angola, MPLA) and the National Union for the Liberation of Angola (União Nacional para a Independência Total de Angola, UNITA). The MPLA, obtained parliamentary majorities in the national elections held in 1992, 2008 and 2012. The new Constitution adopted in February 2010 established a presidential parliamentary system, allowing the leader of the party winning the most seats in Parliament to become President. The Constitution sets a limit of two five-year presidential terms effective from the 2012 election. Parliamentary elections, held under the new Constitution in August 2012, gave MPLA an absolute majority in parliament (175 out of 220 seats), while UNITA obtained 32 seats, with the remaining 13 seats divided among three other parties. The long-delayed first municipal elections and a new legislative election are expected in 2015 and 2016, respectively.

B. Economic Context

2.2.2 **Angola is the second largest crude-oil producer in sub-Saharan Africa after Nigeria.** Angola's economy is highly dependent on oil, which accounts for 47% of GDP, over 95% of exports and nearly 80% of government revenues. The government predominates in the oil sector through the state-owned oil company Sonangol, which is responsible for all oil-related operations in the country. Sonangol works together with foreign investors in exploration and production through joint-ventures and production-sharing agreements. Given its significant contribution to the budget and foreign exchange reserves, the performance of the oil sector and management of oil resources have been central to Angola's changing economic fortunes over the years.

2.2.3 **Angola has maintained robust economic growth rate that places it among the fastest growing economies in Africa.** Economic reform measures over the years was geared to support macroeconomic stability in the country, during which growth averaged 10%, mainly driven by the oil sector (Graph 1). Despite the economic slowdown since 2008, real GDP growth rose to 5.2 % in 2012.. In 2013, GDP growth is estimated to have decelerated to 4.1 %. Growth in the non-oil sector was constrained by the agricultural sector's slow recovery, due to a drought that affected large parts of the country in 2012. Inflation, after reaching single digits for the first time in decades at end-2012, further declined to 7.7% by end-2013, below the authorities' 9% target. Gross international reserves were US$ 33.2 billion at the end-of December 2013, equivalent to 6.9 months of projected 2014 imports.[3]



Source: AfDB Statistics Department, African Economic Outlook, March 2013

2.2.4 **In 2013, the government budget went into deficit for the first time since 2009.** According to the IMF, the fiscal surplus of 5.1% of GDP in 2012, is estimated to have turned into a deficit of 1.5% in 2013, due to GoA's ambitious infrastructure investment program. Oil revenues in 2013 fell to about 29.6% of GDP (compared to 37.3% of GDP in 2012), as a result of lower prices and declining export volumes. Non-oil tax revenue remained at 7.0% of GDP in 2013 (below the 9.2% budgeted) due to delays in adopting tax reform legislation. Current spending is estimated to have remained at its 2012 level (29% of GDP), while capital expenditure is estimated to have fallen to 10.6% of GDP, compared to a budgeted expansion of 13.8% of GDP.

2.2.5 **The pace of economic activity in 2014 is expected to increasegradually as public investment in infrastructure creates opportunities for non-oil sector growth.** The 2014 budget envisages a further increase in the overall fiscal deficit to 4.8% of GDP (compared to a deficit of 1.5% of GDP expected in 2013) to finance a sizeable expansion in public

[3] IMF Second Post-Program Monitoring, March 2014

investment needed to address infrastructure bottlenecks. Non-oil sector growth is expected to reach 6.4%, underpinned by expanded investment in infrastructure. The 2014 budget continues the precedent set in 2013 of using conservative oil price projections (price of US$ 98 per barrel), implying a more realistic budget. Capital spending as a share of total spending is projected to increase to 32%, up from 29% in 2012.

2.2.6 **The government policy agenda focuses on rebuilding and diversifying the economy.** Key policy priorities aim to accelerate reforms associated with the oil sector and infrastructure development with a view to diversifying the economy away from hydrocarbons and reducing the country's large income disparity. Thus far, the government has made significant progress in promoting macroeconomic stability and achieving high and sustained growth rates. Angola now has an improved fiscal position, exchange-rate stability, low level of debt, relatively low inflation and healthy reserves. However, a number of structural deficiencies remain. To address these deficiencies, plans are underway to improve the country's infrastructure ,deepen public sector reform, strengthen PFM, and promote rural and industrial development, as well as job creation.

2.2.7 **Angola's public debt has been declining in the past few years as a result of fiscal consolidation**. Public debt has reduced from over 49 percent of GDP in 2009 to an estimated 26.6 percent in 2013. External debt still accounts for the largest share of total public debt (17.3% of GDP), with domestic debt at 9.3% of GDP. The current level of public debt, which is quite low compared to other emerging countries, shows that Angola can absorb additional loans without jeopardizing debt sustainability. The composition of external debt also suggests fairly limited risks for debt sustainability. Going forward, the debt outlook is expected to remain sustainable, in spite of the Government's capital expenditure program.

Table 1: Selected Macroeconomic Indicators, 2012-2016

Indicators	2012 Act.	2013 Est.	2014 Proj.	2015 Proj.	2016 Proj.
Real GDP (%)	5.2	4.1	5.3	5.5	5.9
Consumer Price Index - end of period (%)	9	7.7	8	7.5	7.3
Overall fiscal balance, budget basis (% of GDP)	5.1	-1.5	-2	-2.6	-2.1
Total Revenue (% of GDP)	45.9	38.1	39.3	37.2	35.8
Total expenditure (% of GDP)	40.8	39.6	41.3	39.8	37.8
Current Account balance (% of GDP)	9.2	5	2.2	-0.4	-2.7
Gross official reserves (months of import cover)	7.5	7	6.9	6.8	6.8
External public debt(% of GDP)	19.3	17.3	18.7	19.9	21

Sources: *Angolan authorities and IMFstaff estimates and projections; March 2014*

2.2.8 **Medium-term Economic Outlook: Angola's growth prospects over the medium term remain positive (Table 1),** although its strength will depend on structural reforms aiming to loosen constraints to investment. According to the IMF, average GDP growth is projected at 5.4% in 2014-2016. Inflation is expected to remain at single digits, supported by a stable exchange rate and prudent monetary policy. The external current account is projected to deteriorate due to a rapid increase in imports linked to government-led capital investment and declining export revenue as oil prices weaken over the medium term. The current account surplus in % of GDP would contract from an estimated 5.0% in 2013 to 2.2% in 2014, becoming a deficit of 2.7% in 2016. Gross international reserves are expected to cover 6.8 months of imports in the medium term. . Despite its favourable outlook, Angola's reliance on oil revenues and consumer-goods imports leaves the economy highly vulnerable to external shocks, emphasizing the need for structural reforms to promote economic diversification.

C. Social Context

2.2.9 **The poverty headcount in Angola has decreased but inequality still remains high, with a Gini coefficient of 0.55.** The country has made reasonable progress in the areas of poverty reduction, health, primary education, and gender equality, but still ranks low in the Human Development Index (HDI) at 148th out of 187 countries in 2012. Despite progress made to reduce poverty from 68% in 2001 to 37% in 2009, unemployment remains high at 25%[4], in particular among the youth. Infant mortality was 84 deaths per 1,000 live births in 2012 which places Angola among the 10 countries with the highest infant mortality rates out of 221 countries.[5] In the same year, life expectancy increased to 51.5 years (52.98 for women and 50.02 for men), demonstrating a gradual improvement in the past decade.[6] The World Economic Forum ranked Angola 87th /135 countries in its 2011 Global Gender Gap Report compared to 106 out of 134 countries in 2009. Participation of women in political and business activities has increased in recent years and today, Angola has one of the highest shares of women MPs (36.4% in 2013[7]) in the region; nonetheless, the country's poor are predominantly women, especially in the rural areas. In order to further enhance gender equality, GoA approved a National Gender Equality Policy (Politica Nacional para Igualdade e Equidade de Genero) in 2013. GoA is also committed to increasing public investment in the social sector, to accelerate progress towards achieving the MDGs. In this regard, the 2010-2015 National Poverty Eradication Strategy (Estratégia de Combate à Pobreza), sets out the priorities and action plans for attaining the MDGs. GoA has also established an institutional framework for entrepreneurship development and employment creation. GoA is now developing a Social Assistance Strategy to create a system to support the extremely poor and vulnerable populations.[8]

D. Governance context

2.2.10 **The government has embarked on important reforms to improve governance and accountability but corruption remains a challenge.** Following Angola's civil conflict that damaged the institutions of governance and accountability, the country has experienced modest improvements in its governance indicators: the Mo Ibrahim Index of African Governance improved from 35 to 41/ 100 points from 2006 to 2013; the Bank's CPIA score from 3.33 in 2010 to 3.96 in 2012 (Cluster A-C), and Cluster D from 2.8 to 3.18 in 2012; the Transparency International CPI from 168th in 2011 to 153/178 countries surveyed in 2012; and the World Bank's Worldwide Governance Indicators in four out of six dimensions of governance improved between 2000 and 2012, especially in political stability, and voice and accountability. Nonetheless, the business institutions and infrastructure remain weak: Angola ranks 179/185 economies in the 2014 Doing Business Report; and 127th/130 countries (23rd/24 countries in the region) in the Intellectual property Rights 2012 Index; and 142/ 148 economies in the 2013-2014 Global Competitiveness Index (GCI), highlighting corruption, inefficient government bureaucracy, and an inadequate supply of infrastructure as the main challenges for doing business in the country. Measures are being taken to reduce opportunities for corruption, including the adoption of (a) a law strengthening the AML/CFT framework, in particular criminalizing money laundering and terrorist financing; and (b) the Public Probity Law (*Lei de Probidade Pública*) in March 2010, requiring all government officials to make a declaration of wealth and income in the country and abroad, and introducing criminal sanctions.

2.2.11 **GoA has been pursuing reforms to enhance governance and transparency in the management of oil revenue.** First, GoA's commitment to phase-out quasi-fiscal operations of Sonangol and to incorporate them into the fiscal account has been strong, and as of March 2014, those off-budget operations have been discontinued. Second, the GoA has made substantial progress on the reconciliation of oil revenue transfers from Sonangol to Treasury, to further promote budget transparency and predictability. This is essential for a proper

[4] http://www.tradingeconomics.com/angola/unemployment-rate
[5] http://www.indexmundi.com/g/r.aspx?c=ao&v=29
[6] http://countryeconomy.com/demography/life-expectancy/angola
[7] MINFEMU Relatorio do Balanco de Execução do Plano Nacional – 2013
[8] Ibid.

assessment of the fiscal policy stance and accuracy of oil revenue transfers. Third, the creation of the Sovereign Wealth Fund (SWF) in 2012, aimed at social and economic development, could serve as a pillar of macroeconomic stability by insulating the annual budget from volatile oil-revenue inflows.

Box 2: Angola's Sovereign Wealth Fund

In August 2012, the Government of Angola launched its Sovereign Wealth Fund, known as the Fundo Soberano de Angola (FSDEA). The mandate of the FSDEA is to "secure long-term sustainable financial returns to positively impact the lives of Angolans today and in the future." To do so, the FSDEA will invest in: (i) domestic investment projects that contribute to growth and economic diversification over the medium term; and (ii) financial assets abroad to save for future generations. FSDEA was established with an initial endowment of US$5 billion that had been held in the Oil for Infrastructure Fund, subsequently topped up by revenues from the sale of 100,000 barrels of oil per day, about US$3.5 billion per year at current prices.

2.2.12 **GoA has started to improve PFM but more international best practices need to be adopted.** The Bank's Fiduciary Risk Assessment (FRA) concluded that the overall risk level of PFM (financial management and procurement) is high, and the residual risk is substantial, in spite of the ongoing and planned reform initiatives and mitigation measures in the program. Additional fiduciary safeguards will be implemented under the program to strengthen PFM. To this end, measures have been proposed in the program to mitigate these risks including: the Government will submit quarterly Budget execution reports to the Bank during the program implementation period; the operations will be audited (covering the funds flow and the use of funds) by the Court of Auditors (*Tribunal de Contas*) or private audit firm; a consolidated annual state accounts for 2014 and 2015 will be submitted to the National Assembly and Court of Auditors for audit; implementation of procurement improvement action plan; building procurement capacity; review and adoption of new procurement law and regulations; technical assistance to carry out a Public Expenditure Management and Fiduciary Systems Review (PEMFSR) and preparation of PFM reform action plan drawing on the findings and recommendations of the PEMFSR. Monitoring and quarterly reports of the flow of funds will reinforce the control of the fiduciary risk. A detailed FRA and mitigation measures are also presented in Technical Annex 8. By focusing on PFM reform, the operation aims to support GoA's efforts to address existing weakness in this area. The program will be monitored through enhanced supervisions, regular follow-up by the Bank's Field Office (AOFO) and in consultation with all the other partners.

2.3 Energy Sector Review

2.3.1 **Infrastructure and Development**: The civil war had virtually destroyed Angola's infrastructure. However in just the past decade, strong government commitment propelled infrastructure development, buoyed by strong revenue streams from mineral exports and a peaceful environment that has attracted significant private sector investments. For example, by 2013, over 2,000 km of roads and 1,333 km of railway had been constructed or rehabilitated and the installed power generation rose from 830MW in 2002 to over 1,700 MW in 2013.

2.3.2 **Key participants in the Power Sector in Angola:** The Ministry of Energy and Water (MINEA) is responsible for the energy sector policy development, coordination and oversight. The main power utility company in Angola is the Empresa Nacional de Electricidade (ENE) which manages the transmission network and operates over 80% of power generation facilities and distribution system outside of Luanda. In the capital, power distribution is managed by the Empresa de Distribuição de Electricidade (EDEL). To facilitate design and development of large hydropower projects in the Kwanza river basin, MINEA established a Gabinete de Aproveitamento do Médio Kwanza (GAMEK) that currently owns hydropower plants totaling 520 MW and is implementing the 2,000MW Laúca Hydropower Project. The sector has a national regulatory agency, *Instituto Regulador* *do Sector Eléctrico* (IRSE) established in 2002. Sonangol is constructing a total of 900MW of combined cycle thermal power plant.

2.3.3 **Regional Grid Integration**: The GoA in collaboration with Government of Namibia is undertaking feasibility studies for the 600MW Baynes power project and a transmission line linking Angola power grid to Namibia, and by extension to the Southern Africa Power Pool. However, the current General Electricity Law does not provide for cross-border power exchange or transit power. The proposed revisions to the General Electricity Law provides clear definition of international transmission interconnectors, import, export and transit power, making it possible for Angola to implement regional grid interconnection projects and benefit from regional power trade while providing electricity wheeling services to neighbouring countries. Power Pool membership has many inherent advantages such as, sharing surplus cheap energy across borders, moderating the effect of climate change as countries are impacted differently by seasonal variations, and most importantly enhancing stability and security of electricity services. The policy advice under the PSRSP will include support for Regional Power Planning in line with the Bank's Regional Integration Strategy.

2.3.4 **Institutional setup and status of the power sector:** ENE, EDEL and GAMEK form a vertically integrated market structure, albeit with significant overlaps in their objectives and no contractual and commercial agreements (Technical Annex 4). The electricity infrastructure is characterized by: (i) inadequate generation capacity; (ii) very low levels of electricity access, averaging 30% nationwide and less than 9% in rural areas, posing major constraints to the delivery of social services; (iii) limited revenue collection, as over 80% of the consumers are not metered; (iv) technical and commercial losses that account for over 55% of the electricity energy supplied; and (v) a high cost of electricity production and distribution (approximately US$ 220/MWh), well above the average consumer tariff (US$ 38/MWh). The sector lacks a clear regulatory framework, capacity and skill to manage its operations effectively.

2.3.5 **Power Sector Development Plan and Rationale for Reforms**: GoA needs to urgently mobilize vast resources to address perennial power shortages, expand and modernize its electricity infrastructure, improve customer connection and metering, and reduce technical and commercial system losses. However, with ENE, EDEL and GAMEK operating as pseudo vertically integrated companies without any contractual obligations prevents effective sector re-capitalization and motivation for these companies to run efficiently and profitably. The Government's National Power Security Strategy and Policy (NESSP, 2011) was the first step in establishing and prioritizing the needed actions. The key priority actions recommended by the NESSP include: (a) restructure the sector and allow public-private partnerships (PPP) to become a viable business model, (b) promote contractual relationship among sector participants, (c) accelerate implementation of investment programs, and (d) promote empowerment of the IRSE. The NESSP also recommends the development of policies that allow the use of endogenous energy resources, ensuring the convergence between the principles addressing energy security, efficient technologies, efficient management and promotion of environmentally sustainable power development[9].

2.3.6 To convert the strategy document into implementable actions, the GoA adopted the **Electricity Sector Transformation Program (PTSE),** with key deliverables being the sector diagnostic study; submission of the optimum electricity market model; and a sector reform roadmap. The PTSE feasibility study recommended restructuring the market into a classic single-buyer model, unbundling the power utility into Generation, Transmission and Distribution core activities, establishing commercial contracts between the market

[9] Currently the installed grid generation is less than 33% hydro and the remainder comprising diesel power. The government objective is to rapidly eliminate the use of diesel based generation by 2025.

participants, and amending laws to improve regulations and attract PPP. The study further proposed four (4) reform phases, each with specific deliverables (Appendix T7): (i) Preparation Phase (2010-2013), for the design of a new market structure; (ii) Phase I (2014-2017), the stabilization phase following sector restructuring and unbundling of power utility; (iii) Phase II (2018-2021), the transition to efficient operation with limited use of IPPs, mainly in RE using RE Feed-In tariffs; and (iv) Phase III (2021-2025), the partial liberalization of the power market, introducing PPP and IPPs and limited concessions for the distribution system. The transmission system, a natural monopoly, will remain a public sector entity. To improve rural access to electricity services and efficiency, the distribution system will be further unbundled into 5 geographic regions, with a total of 18 business units.

2.3.7 The NESSP is aligned with the infrastructure development pillar of the National Development Plan 2013-2017.Together with the PTSE program, the NESSP underpins the US$ 23 billion investment program under the Energy and Water Action Plan 2013-17 of which the government has already mobilized from its own resources USD 5.3 billion for ongoing power infrastructure expansion, rehabilitation and modernisation (Appendix 7 and Technical Annex 4). The Plan aims to double electricity access from currently 30% to 60% by 2025, with a focus on the rural areas, and extensive exploitation of cleaner energy resources..

2.4 Bank Group Portfolio Status

2.4.1 **The overall performance of the Bank Group portfolio in Angola is satisfactory** (Technical Annex 1). As of 31st March 2014, the portfolio consists of 8 operations (7 national and one multinational project), totalling UA 74.920 million. The sector portfolio distribution comprises Agriculture (50%); Environment (16%); Multi-Sector (8%), Water and Sanitation (16%), Social (6%) and Transport (4%). The implementation progress rating is 2.18, and development objective rating 2.8, on a scale of 0 to 3. The percentage of Projects-at-Risk (PAR) is 10%, that is, under the Bank's current threshold of 18.99% but the Commitments-at-Risk is high at 50%. Thus, there is a need for greater monitoring, and the Angola Field Office has put in place plans to strengthen implementation capacity in government, enhance country dialogue, and improve portfolio follow-up and performance. The proposed program will complement ongoing projects through providing more fiscal space, enhancing reform implementation and efficiency in sector spending.

III. RATIONALE, KEY DESIGN ELEMENTS AND SUSTAINABILITY

3.1 Link with the Country Strategy Paper (CSP), country readiness assessment, and analytical works underpinnings

3.1.1 **The proposed operation is aligned with the Bank's CSP 2011-2015,** which is focused on two pillars: Stimulus to the competitiveness of the economy and Support to economic infrastructure development. The midterm review of the CSP envisages new financing instruments, including PBOs, to (a) strengthen ggovernance and PFM and (b) promote private sector and infrastructure development. The PSRSP is linked to the CSP's focus on energy infrastructure development, private sector development, and sound PFM (Table 3). By focusing on energy sector reform and public finance management, the proposed program is consistent with the Bank Group's Ten-Year Strategy in its support for infrastructure development, promotion of private sector participation, governance and accountability and skills development.. The operation is also aligned with the Bank's Energy Sector Policy in supporting Angola's efforts to scale-up access to modern, affordable, reliable, socially and environmentally sustainable energy services. In addition, it is well aligned with the Banks's Governance Strategic Framework and Action Plan[10] by helping to address shortcomings in PFM. The program is also anchored in the country's National Development Plan (NDP, 2013-2017) and National Energy Security Strategy and Policy (NESSP, 2011).

Table 3: Linkage of the PSRSP with the NDP and CSP

National Development Plan	CSP	PSRSP
Strategic Objective: Aims at improving the quality of life of Angolans, reducing poverty, expanding employment opportunities and diversifying the economy.	*Strategic Objective:* Support Angola's development plan with emphasis to economic diversification, fostering entrepreneurship and private sector development, and sound PFM system essential for inclusive economic growth	*Operational objective:* Promote inclusive and sustainable growth through energy sector reform and strengthened public finance management
Priorities (i) Macroeconomic stability (ii) Public administration and public finance management (iii) Private sector development; (iv) Infrastructure development (e.g. energy); (v) Job creation and economic diversification; (vi) Human development (vii) Natural resources management (fisheries, oil, and mining).	*Pillars/priorities* (i) Stimulus to the competitiveness of the economy through capacity building, climate change and environment management, public expenditure and financial management reviews, policy dialogue and diagnostic work. (ii) Support to economic infrastructure development including power	*Program components* (i) Restructuring the power sector & Improving Regulatory Environment (ii) Fostering private sector investment (iii) Enhancing efficiency and transparency in public finance to achieve value for money in public investment

3.1.2 **The proposed operation meets the Bank's eligibility criteria for PBOs** (Appendix 2). The country enjoys overall political and macro-economic stability (see Section 2.2.1); GoA's commitment to reform in the two main areas supported by this operation (i.e., power sector and PFM) is strong and grounded in the GoA's Vision 2025 and National Development Plan, which prioritize inclusive growth and poverty reduction. The proposed operation has been prepared in consultation and coordination with other development partners (DPs) active in the power sector; and a Fiduciary Risk Assessment (FRA) carried out for this operation has identified a positive trend, manifested in several ongoing or planned reform initiatives, as well as specific mitigation measures for certain persisting risks.

3.1.3 **Program Rationale**: Since 2008, the Government has been implementing major structural reforms supported under the IMF stand-by arrangement. These reforms have resulted in significant progress as confirmed by the IMF post program monitoring reports. Despite progress, Angola still continues to face challenges and constraints, mainly (a) inadequate supply of infrastructure, especially power, (b) inefficient government bureaucracy and a challenging business environment, and (c) weak institutional capacity and governance. The power infrastructure in Angola is underdeveloped, access to electricity is low and unequal, and supply is often unreliable due to insufficient investment in maintenance and refurbishment. In addition, the state-owned companies perform poorly due to weak governance and lack of competition. So far, the Government has demonstrated its strong commitment to implement the reforms. For this reason, it requires the support and assistance of its principal partners, with the Bank at the forefront. The PSRSP is set in this context, and aims to support Government efforts to address the country's development challenges relating to the energy sector through complementary structural, regulatory and governance reforms to improve efficiency, transparency and competition in the sector.

[10] Governance Strategic Framework and Action Plan II for 2014-2018 sets the priorities into (a) public sector and economic management, (b) sector governance with emphasis to infrastructure and natural resource management, and (c) investment and business climate.

3.1.4 **The successful implementation of the bold power sector reforms needs to be underpinned by a strong governance framework** that facilitates efficient utilization of public resources. Meanwhile, reforms supported by the IMF stand-by arrangement have started to bear fruits and significant progress has been confirmed by the IMF post-program monitoring reports. Notably, macroeconomic stabilization has been achieved and Angola is now on a path of rapid economic growth with single digit inflation, a strong international reserves position, and a stable exchange rate (see Table 1). To sustain this progress, reforms need to be intensified especially to address weaknesses in PFM systems and to improve the business enabling environment. These reforms are necessary to improve the quality of public expenditures and attract the needed foreign investment for infrastructure development (including in the power sector), so as to enhance fiscal sustainability and close the fiscal gap. Government is committed to pursuing reforms which it has already started implementing and needs the expertise, knowledge base and best practices of the Bank to support this process. It is on this basis that the GoA has approached the Bank for support as a "trusted and preferred" partner. This will enhance the credibility of the GOA's reform agenda and provide the bases for implementation monitoring.

3.1.5 Further the Bank's intervention is justified for the following reasons. (a) the reform of the power sector has taken into account national circumstances, international experience and good practices tailored to national conditions; (b) the power sector's ability to meet demand for electricity is a critical driver of Angola's economic growth and business environment; (c) this first sector reform provides a model for other utility and infrastructure sectors; (d) the operation is an effective way for the GoA and Bank to intensify the partnership and dialogue on energy sector reform, and (e) the GoA has decided to diversify its financing sources to fund infrastructure program as indicated in Appendix 7 and Technical Annex 4. To this end, the Government has taken several measures from the time the Bank initiated dialogue with the Government on PSRSP, and the following main measures have been implemented (Table 4).

Table 4: Main Measures Taken since the Bank Engaged in Dialogue with the Government on the Program

1	Amendment to the Organic Budget Law and Budget Execution Rules to strengthen budget institutions and reduce the recurrence of Government Domestic Arrears
2	Publication of the 2014 "Citizen budget".
3	Publication of the 2013 Oil Revenue Reconciliation Report.
4	The approval of the Public Procurement Action Plan by the Ministry of Finance.
5	The establishment of Technical Procurement Agency (UTN) by the presidential decree 169/13.
6	The establishment of a Task Force to initiate and coordinate the Public Expenditure Management and Fiduciary Systems Review (PEMFSR) and preparation of PFM reform action plan drawing on the findings and recommendations of the PEMFSR
7	Submission of a tariff proposal to the Economic Commission

3.1.6 **The design of this operation is guided by various analytical diagnostic works (Technical Annex 2),** including the: 2005 Public Expenditure Management and Financial Accountability Review (PEMFAR); National Energy Security Strategy and Policy (2011); Energy and Water Sector Action Plan for 2013-2017; Energy Sector Challenges and Opportunities (USAID; 2012); Electricity Sector Transformation Program (2013-2017) feasibility study; IMF Second Post-Program Monitoring (March 2014); Economic Update (World Bank; 2012); 2011 Bank's National Competitive Bidding Assessment Report; Bank's Country Strategy Paper Midterm Review; Country Portfolio Performance Review (2013); and AfDB Country Gender Profile (2008). Recommendations from these documents are reflected in the program. The design of the operation has also benefited from the Bank's Power Sector

Analytical Review, and the Bank's Fiduciary Risk Assessment (FRA).[11] Stakeholder consultations and a workshop were carried out during the appraisal mission.

3.2 Collaboration and coordination with other donors

3.2.1 **In preparing the operation, the Bank has consulted key DPs[12].** Average ODA disbursements represented less than 2% of GDP during 2010-2013, and DPs' development coordination has been limited. Their activities are concentrated in institutional capacity building, health, education, water and sanitation. The Bank has organised a multi-stakeholder workshop in collaboration with GoA and DPs to enhance collaboration and leverage its support by working in partnership with various stakeholders (parliamentarians, private sector and civil society organizations). The program was informed by the outcome of the consultation workshop.

3.2.2 Furthermore, PSRSP complements the IMF post program monitoring and consultations. Consultation with the other partners regarding this operation reveals that, on the whole, they support the idea of supporting power sector reform as key driver of economic diversification and transformation. Joint discussions have already been initiated and the Bank intends to play a key role in creating the platform for dialogue among DPs and between DPs and GoA. Against this backdrop, the PSRSP policy matrix (Appendix 5) provides the mechanisms through which the Bank intends to play a driving role in creating the platform for policy dialogue. The Bank's Angola Field Office (AOFO) is taking the lead and had already initiated policy dialogue between the GoA and DPs.

3.3 Outcome of Past and On-going Similar Operations and Lessons

3.3.1 **The design of this operation has benefitted from lessons learnt from past Bank-supported budget support operations, CSP midterm review and other Bank funded operations in Angola.** Table 5 summarises the main lessons and how they have been incorporated into the proposed operation.

Table 5: Lessons learned from past Bank-supported program based operations and CSP Mid-term review

Lessons learned	Actions taken to integrate lessons into the PAR
(i) Flexibility in responding to the country's evolving development challenges including the use of new financing instruments	The program responds to the GoA's desire to reorient cooperation with the Bank towards large-size transformative projects, as opposed to small-scale interventions. It provides predictability and flexibility to disburse the loan in line with the country's budget calendar, and financing needs.
(ii) The significance of country ownership and the need to anchor the program on the country's development strategy to ensure effective program implementation.	The proposed operation is based on the country's reform agenda in particular the power sector reform plan and the ongoing PFM initiatives, both of which identify critical measures essential for the delivery of the objectives of the National Development Plan.
(iii) Importance of focusing on few but crucial reform priorities and performance indicators for monitoring results. Disbursement triggers should be realistic, giving consideration to the policy environment and the feasibility of legal changes.	The proposed operation has been designed with the objective of consolidating the progress made so far in connection with its main components (power sector restructuring, private sector participation, and PFM reform). The streamlined conditions for disbursement are considered critical to the success of the government-led reforms in the power sector and public finance. They have been carefully selected from upstream dialogue with the two key ministries of the Government of Angola.
(iv) Need to address capacity constraints in program implementation.	A complementary capacity building component is incorporated into the program to strengthen implementation capacity, thus enhancing the prospects of program development outcomes. The capacity building program will also allow key ministries to play a stronger role in addressing gender issues and promoting gender awareness at all levels of government and civil society, with a focus on budget, planning and policy.

[11] FRA undertaken as part of the PBO preparation and appraisal missions in February and March 2014
[12] Including the World Bank, IMF, EU, USAID, Norway, and Sweden.

(v) Effectiveness of program based operations is enhanced if combined with policy dialogue and capacity building interventions	The program complements the ongoing country dialogue led by the AOFO and technical assistance project funded by development partners including the Bank (ongoing projects supporting PFM and PIP). It is also included a strategic technical assistance and change management support
(vi) Need to deepen and scale up the governance reform process in the areas of PFM, and sector governance	The PSRSP components have been selected and focused on key PFM reforms (budget, and procurement) that would improve transparency, efficiency and value for money in public spending. Furthermore, the program addresses critical policy changes in the energy sector

3.4 Relationship to on-going Bank's operations

3.4.1 **This operation has a strong relationship with the other Bank Group funded operations in Angola (Technical Annex 1).** The PSRSP will positively impact the Bank's operations through three channels. First, the program will contribute towards strengthening the GoA's procurement and financial management systems. Second, it will provide an incentive to MINEA to pursue urgent reform in the sector, including in water services. Third, the proposed program will complement projects in water and sanitation, agriculture, environment and climate change, and financial governance, including capacity building in public investment programs. The program's focus on PFM and energy sector reforms will provide synergy in the execution, development and sustainability of Bank-funded projects and infrastructure development. The 2014 PEMFSR exercise, financed under the Bank's Angola Financial Management Support Project (PAGEF) will serve as a monitoring tool for the program and for fiduciary risk.

3.5 Bank's Comparative Advantages and Added Value

3.5.1 **The operation will build on the Bank's vast experience and engagement in Africa, covering infrastructure development, institutional reforms at both the general and sector levels, and capacity building.** The Bank's comparative advantage in supporting the program derives importantly from (i) being an African premier multilateral development institution with a deep knowledge of the African socio-economic setting; and (ii) scaling up its engagement and reorientation of its policy and institutional actions to respond to challenges in infrastructure and economic governance in Africa. The Bank's experience gained from participation and leading sectoral and governance reforms in several regional member countries puts it in an advantageous position in bringing expertise, knowledge and best practices into Angola's reform agenda, and the successful management of the operation. Thus the Bank's support will bring credibility, consistency and coherence to policy reform process in Angola. This will send a powerful signal to the market and the international community that Angola is committed to doing business differently by engaging with the Bank in a sustained policy dialogue as a "trusted partner". The PSRSP will create a catalytic platform for policy dialogue and advisory services in Angola. The Bank's field presence in Angola will facilitate close supervision of the operation and enhance the policy dialogue process. In this context, the Bank will continue to work in synergy with the other Development Partners active in Angola.`. Unless met, the vast infrastructure needs would weaken the business environment and imped economic diversification and inclusion. In this regard, the loan is important for closing the infrastructure gap and further reducing cost of electricity and improving business environment. The size of the loan (USD 1.0 billion) is also justified on the basis of the huge government fiscal deficit estimated at AON 630 billion (equivalent to USD 6.45 billion) in 2014 and AON 360 billion (equivalent to USD 3.68 billion) in 2015. The huge planned investment in the energy sector, estimated at USD 4.6 million per year over the next five years is an additional justification for the size of the loan.

3.6 Application of Good Practice Principles on Conditionality

3.6.1 **The program design incorporates good practice principles on conditionality (Technical Annex 3)** through: (a) aligning the program policy matrix with the country's energy sector reform plan and PFM reform process; (b) selecting reform actions critical to the success of the program and for achieving results as a condition for disbursement; and (c) streamlining the conditions to improve predictability and facilitate disbursement as required by the GoA, accompanied by policy dialogue and technical assistance. The Bank is processing this program in time so as to improve alignment with budget cycle and financing needs.

IV. THE PROPOSED PROGRAM

4.1 Program's Goal and Purpose: The overarching objective is promoting inclusive economic growth by improving efficiency in the energy sector and consolidating PFM reforms. The reforms envisaged in the program will support and facilitate the implementation of the government's ongoing and future investments in the power sector, which will create employment opportunities and extend access to electricity to a larger share of the population, in particular the most vulnerable ones.

4.2 Program Components, Operational Objectives and Expected Results

4.2.1 **Operational Objectives.** The operational policy objective is to support ongoing Government effort to improve operational efficiency, competitiveness and sustainability of the energy sector as well as greater transparency and efficiency in PFM.

4.2.2 **Program Components:** The program has four components: (a) restructuring the energy sector and improving its regulatory environment; (b) fostering private sector investment in the energy sector; (c) enhancing transparency and efficiency in PFM; and (d) capacity building and change management support. The rationale for the choice of these components is based on the complementarity between power sector reforms and the promotion of an enabling environment for private sector investment, skills as well as PFM reforms. Weaknesses in PFM have an impact on energy sector development in terms of investment planning, procurement, budget execution, and value for money. These weaknesses lead to an increase in the fiduciary risk associated with increased public spending in energy infrastructure development. Conversely, improved PFM will increase the level, efficiency and effectiveness of public investment in the energy sector.

Component 1: Restructuring the power sector and improving the regulatory environment.

4.2.3 **Challenges and constraints:** Inadequate infrastructure is one of the key constraints to private sector development in Angola. Evidence suggests that the costs resulting from unreliable energy supplies constitute a major constraint for the competitiveness of Angolan businesses and thus a major barrier to the creation and expansion of businesses, and economic diversification. Importantly, two-thirds of Angolan businesses are estimated to rely on their own generators in Luanda,[13] jumping to over 90% outside the city. Mostly diesel-based, costs can run as high as $0.40 per kWh, roughly double ENE's production and distribution costs.[14] A 2010 study estimated that Angolan firms lose roughly 13% of their annual turnover due to the impact of unreliable power supply (more than 40% downtime), almost three times more than in 2007 (5%).[15] Finally, Angola ranks 170th/189 economies for the "Getting Electricity" indicator of the 2014 Doing Business Report (DBR). Nonetheless, Angola's 7 different procedures and 145 days for an SME located in Luanda to obtain an electricity connection are not too different from the sub-Saharan African averages of 5 and

[13] AfDB, Angola Private Sector Country Profile, October 2012. A recent survey carried out by the Norwegian cooperation agency indicates that the average monthly expenditure in fuel for generators among the sample of small businesses surveyed (e.g., shops, small offices) is about USD 110.
[14] Angola's Infrastructure: A Continental Perspective, World Bank Policy Research Working Paper, No. 5814, September 2011.
[15] World Bank, 2010 Angola Enterprise Survey.

141, respectively. Power sector reform can therefore have a significant impact on private sector development and competitiveness and, more specifically, SMEs, where women entrepreneurs play a prominent role, thus enhancing inclusiveness. In addition to hurting competitiveness and the investment climate, inadequate power supply is a major constraint for public services such as education and health as well as on overall reduction in the quality of life.

4.2.4 **Recent Government Action:** GoA has commenced restructuring the power sector by addressing the institutional weaknesses and constraints summarized in Section 2.3 and detailed in Appendix 7 and Technical Annex 4. The power sector reform program aims at improving the institutional and regulatory frameworks, restructuring and unbundling the utilities, reviewing the current tariffs and subsidies, improving the efficiency of utilities, strengthening the capacity of the sector's regulator, promoting development of Renewable Energy and attracting private investment. To date, the Government has completed a number of studies detailing the specific arrangements for the unbundling and held stakeholder consultations on the draft revised General Electricity Law.

4.2.5 **Program Activities:** The proposed program will support the Government in its effort to implement the structural and regulatory reform measures under Phase I of the PTSE (see 2.3.6). The specific policy actions supported by the program include two complementary priorities: (a) power sector restructuring, and (b) improving the regulatory environment.

- The Power Sector Restructuring policy action focuses on the unbundling of the generation, transmission and distribution systems and the establishment, by Presidential Decree, of three new utility companies: (a) Empresa Pública de Produção de Electricidade (PRODEL) dealing with power production, (b) Rede Nacional de Transporte de Electricidade (RNT) as the national transmission company and Single Buyer of electricity, and (c) Empresa Nacional de Distribuição de Electricidade (ENDE) as the national distribution company. This policy action also supports (i) the approval of General Electricity Law by Cabinet, (ii) the establishment of contractual agreements (PPAs) between the three established utility companies; and (iii) the adoption of the by-laws ("estatutos"). Consistent with the national objective of integrating women at decision making levels, the program will promote gender equality in the appointment of the board and top management in the utility companies. The revised General Electricity Law will establish the basic principles for regulating the role of stakeholders in the production, transport, distribution, supply and marketing of electricity, and will define for the first time the Angolan *"Electricity Market*". It will also enhances the autonomy of the sector regulator and confer on IRSE the responsibility to approve electricity market rules, develop tariff methodologies, and approve concessions and licenses for electricity services[16]. The revised law will promote an energy mix composed of renewable energy resources and less polluting combined-cycle thermal power plants. To ensure financial sustainability of the power sector, the revised law will also strengthens Pre-Payment of electricity services and power project assessment based on least cost planning. This will speed up the implementation of the Government's roll-out of the pre-paid electricity metering program which had stalled. Regional power grid integration, power trade and energy wheeling is an integral part of the Angola's medium-term power development strategy. The GoA has therefore ensured that clarity of definition of the concept of export, import and transit power is addressed in the proposed revision of the General Electricity Law.
- The "Improving the Regulatory Environment" policy action supports government efforts to strengthen the sector's regulatory environment by enhancing business efficiency and

[16] This is limited to 10MW plant capacities and distribution services for up to 50,000 inhabitants.

productivity through amendment of the Presidential Decree establishing IRSE. The proposed amendment aims to give IRSE greater autonomy regarding sector operations, approve and publish Network Access and Connection regulations, establish and publish performance criteria for Quality of Service, design the tariff structure, and monitor commercial relations between the sector operators. It will include a funding mechanism based on fees and other payments from the sector, further boosted by the adoption of a Tariff Adjustment Proposal. The first step in tariff adjustment is aimed at compensating for annual inflation since 2006 (the last time tariffs were adjusted) as an initial financial remedy for the sector. A tariff methodology is being proposed that would ensure a social safety net for vulnerable consumers while providing for a gradual adjustment towards cost-covering tariffs by 2021.

4.2.6 **Expected Results:** The combined effect of the above reforms will be a drastic improvement in the operational efficiency of the new utilities in the form of increased revenue collection and improved service delivery (through increased availability). Ultimately, reforms will aim at ensuring the long-term financial sustainability of the sector and expanded reliable access to electricity in line with the NESSP. In addition, a gender approach will be mainstreamed into sector restructuring, as the operation provides support for an increased representation of women in senior management positions in the power sector.

<u>Component 2: Fostering private sector investment in the energy sector</u>

4.2.7 **Challenges and constraints:** Private sector participation in the energy sector is necessary to support the GoA's reform agenda in two main aspects: financing and skills. First, GoA has projected that, in order to double the country's electrification rate by 2025, total investment of about USD 23 billion will be needed between 2013 and 2017. It is highly unlikely that this can be achieved without a sizeable participation of private investors. Second, private investment, in particular FDI, can address the important skills gaps in the sector through knowledge and technology transfer. However, to date private sector investment in energy has been limited, mostly due to a deficient enabling environment. Indeed, as of 2013 private operators only accounted for 13% of installed capacity.

4.2.8 **Recent Government Action:** In recent years, GoA has adopted various reforms aimed at improving the business environment and attracting investment, including the recent adoption of the (a) Private Investment Law (Law 20/11 of May 20, 2011), which provides various incentives to foster FDI and identifies energy and water as priority areas; and (b) PPP Law (Law 2/2011, of March 14, 2011). At the sector level, the General Electricity Law of 1996 explicitly provides for privately-owned enterprises entering the generation and distribution areas of the electricity value chain. This law is currently under review. The 2011 National Energy Security Strategy and Policy, the Energy and Water Sector Action Plan (2013-2017), and the Electricity Sector Transformation Program (PTSE) all prioritize the attraction of private sector investment, in particular at the generation/production level with a special emphasis on renewable energies and isolated systems for rural electrification.

4.2.9 **Program Activities:** The program will support ongoing and planned initiatives to improve the business environment for private sector participation in the power sector. Some of the reforms supported under Component 1 are also instrumental in meeting the GoA's objective of attracting private sector investors into the power sector. In addition, the program will support policy actions to improve the enabling environment for private sector investment in energy generation, with an emphasis on the development of renewable energies.

4.2.10 In particular, the program will support the adoption of the White Paper on Renewable Energies as strategic for the development of renewable power production. The White Paper is expected to introduce a regulatory framework that fosters private sector investment in clean energy solutions as the preferred choice for rural electrification and isolated power systems, with a prominent role of small-scale privately-owned generation units in the hydro, wind, and solar segments. Furthermore, renewable energies is a tool for improving gender equality by supporting access to and control of renewable energy resources and providing women with knowledge (Technical Annex 5). The program will also support the completion of the renewable energy resource mapping, and the launching of a special Renewable Energy Feed-In Tariff (REFIT) scheme providing incentives for private investment into small green energy and rural electrification projects for isolated grids (below 10 MW), with a special focus on mini-hydro power plants.

4.2.11 **Expected Results:** It is expected that private investors will respond to the above reforms of the enabling environment by entering the sector as independent power producers (IPP), in particular in the renewables sub-sector, thereby contributing vital financial resources and knowledge transfer to meet the sector's sizeable investment needs.

Component 3: Enhancing transparency and efficiency in public finance management

4.2.12 **Challenges and constraints:** Progress has been made in several areas of PFM, including macroeconomic and debt management, budget formulation, accounting, and reporting. The budget and accounting functions were further improved with the adoption and roll-out of the Integrated Financial Management Information System – IFMIS (SIGFE). The adoption of Treasury Single Account, submission of financial statements (2011-2012) to the Court of Audit, and availability of fiscal information in the public domain also show important improvements. Nonetheless, an analysis of the Annual Financial Statements for the three years to 2011 reveals variances in terms of quality as well as shortcomings in expenditure control. Weaknesses include outdated regulatory frameworks, weak human resources capacity, and poor organizational arrangements in some of the key PFM institutions. Further, the Bank's FRA reveals capacity constraints and weaknesses in budget execution, expenditure control, and procurement. Also, the actual implementation of gender-responsive budgeting in sectors has not yet materialized.

4.2.13 **Recent Government Action:** The Ministry of Finance has placed PFM reform at the top of its reform agenda to ensure delivery of quality service and maximize the impact of the public investment program. The establishment of a Sovereign Wealth Fund represents a step in the right direction in terms of Angola's fiscal policy and expenditure planning. GoA has recently enacted important measures to increase transparency of oil revenues and reduce quasi-fiscal operations (QFOs) by state-owned enterprises. Incorporating these QFOs into the budget is an important step in consolidating the fiscal accounts. In addition, following the policy dialogue with the Bank, GoA has requested, and is in the process of receiving, TA support from the Bank to undertake a comprehensive PEMFSR to assess the strength of the PFM systems and produce a medium-term action plan to address persistent weaknesses. Further reform in PFM will help reduce the vulnerability of the budget and improve the efficiency of public spending.

4.2.14 **Program Activities:** The program will support policy measures in the areas of (a) budget credibility and transparency and (b) improving efficiency and value for money in public procurement. Under budget credibility and transparency, the key policy actions supported by the program are: (a) publication of the 2014 "Citizen budget" with the aim to improving citizen participation in the formulation and monitoring of the government's budget; (b) posting of the 2013 Oil Revenue Reconciliation Report; (c) adoption of a revised National Inspectorate of Finance Regulation; and (d) approval of a PFM action plan.

4.2.15 In addition, the Ministry of Finance has hired an auditing firm to verify outstanding domestic payment obligations incurred by ministries and provincial governments. The verification process is ongoing, with repayment of outstanding claims pending the completion of the verification process. The program will support measures to address the recurrence of government domestic arrears through an amendment of the budget law that will strengthen the enforcement of budget legislation and coverage of the budget monitoring system. The program also supports efforts to improve the collection and reporting of oil revenues and related transfers by completing a flow-of-funds report, which is expected to improve transparency and accountability in the management of oil revenues, as well as reducing the uncertainty of revenue flows from Sonangol.

4.2.16 The Inspectorate General of Finance (IGF) has a primary mandate over the financial administration of the GoA, offering technical support to the Minister of Finance. Since it is still operating under outdated regulations, limiting its scope to expenditure audits, a new regulation is being prepared[17]. The Program will support these efforts. In addition, the Public Expenditure Management and Fiduciary Systems Review (PEMFSR) action plan that will guide PFM reforms over the next 3-4 years will receive further support from the Bank. The operation also supports the adoption of a gender policy that will guide gender mainstreaming in line ministries. More specifically, the operation will provide a platform for policy dialogue with the government on sectoral programs that use gender-disaggregated data to ensure that both women and men benefit from public spending.

4.2.17 In light of the principle that procurement needs to ensure delivering value for money, the public procurement system is currently not providing sufficient benefit to the population. The Government needs to urgently revise procurement regulation, primarily by developing operational standard bidding documents and a manual consistent with international good practices. In this context, the program seeks to support the following policy actions: (a) adoption of a PFM Reform Action Plan based on the recommendations of the PEMFSR Review (to be completed in 2014); (b) establishment of a Technical Procurement Agency; (c) launching of a Procurement Portal; (d) adoption of a revised procurement law; and (e) adoption of procurement regulations, including Standard Bidding Documents.

4.2.18 **Expected Results:** The combined effect of the above reforms would strengthen transparency and efficiency of PFM. This will allow a more efficient execution of the PIP, which is of vital importance to address the country's infrastructure challenges. In addition, program-supported reforms will improve budget execution (measured by higher rates of budget execution) and internal and external controls (measured by a reduction of the stock of domestic arrears, one of the main challenges to GoA's fiscal discipline), and greater value for money in procurement.

4.2.19 Capacity building and change management support: The new market model to be implemented for the energy sector under Components 1 and 2 will require additional skills that do not exist in the sector today. To ensure the success of the reform program, GoA has developed a comprehensive capacity building plan with three broad objectives covering over 30 fields of specialization (Technical Annex 4): (i) develop leadership skills to manage the transition phase, (ii) enhance management capabilities needed for improving business and operational efficiencies, and (iii) acquire the new skills to manage new processes. Importantly, local universities, colleges and vocational institutions will help tailor courses to the sector's needs. The PSRSP supports strategic capacity building and change management for the transition and stabilization of the new market model. In this regard, GoA will earmark US$ 6 million over two years for training of board members, senior managers, mid-level technical and management staff, and system operators and support staff. The capacity building program will also strengthen the capacity of key ministries, such as MINEA and MINFAMU, to promote gender sensitive budgeting, planning and policy formulation. In addition, capacity building under Component 3 (PFM reforms) will be provided following the

[17] The IGF currently operates under a Decree passed in 1958, and there is need to align to among others the 2010 Constitution and the Presidential Decree No. 93/10 establishing the Ministry of Finance.

identification of needs under the PEMFSR. The Bank will consider additional instruments to support the Government in this respect, including a potential restructuring of the current ISP, based on the recommendations of the PEMFSR. In addition the Bank, through EADI, is preparing a tailored program for capacity development for the Ministry of Finance, including in the areas of statistics and public financial, and investment management.

4.3 Financing Needs and Arrangements

4.3.1 The proposed operation is part of the external financing sources that will help close the 2014-2015 financing gap. Table 6 presents the Government's financing needs for 2014-2015. For 2014, total revenues are projected at Kwanza 4,745 billion, while total expenditure are projected at Kwanza 5,375 billion. Revenues are projected to grow at above 8.4% per year in nominal terms. The budget envisages a significant increase in expenditure (10% compared to 2013) needed for rehabilitation of the country's infrastructure network. Capital expenditure as a share of total expenditure is projected to increase to 32% up from 29% in 2012. With the current fiscal policy, the overall fiscal deficit for 2014 and 2015 is projected as kwanza 990 billion, and of which 63.6% is required in 2014. Given the fact that the critical reform implementation is being implemented in 2014, the disbursement plan would contribute about 10.6% to the financing gaps.

Table 6: Projected Financing requirements and sources, 2014 and 2015 (in billions of Kwanza)

	2012 Actual	2013 Preliminary	2014 Budget	2015 Projection
Total Revenue	5,054	4,474	4,745	5,144
• Taxes	4,826	4,291	4,540	4,964
• Oil Revenue	4,103	3,472	3,313	3,844
• Non-oil revenue	723	819	1,227	1,120
Total Expenditure	4,490	4,647	5,375	5,504
Recurrent Expenditure	3,191	3,396	3,674	3,900
• *Of which:* Compensation of employees	1,031	1,125	1,369	1,620
• Use of goods and services	1,303	1,400	1,431	1,360
• Interest (domestic and foreign)	105	86	128	130
• Subsidies	548	563	394	580
Capital Expenditure	1,299	1,251	1,701	1,604
Overall fiscal surplus/deficit (-)	564	-173	-630	-360
• Domestic and external financing	0	173	567	318
• ADB	0	0	63	42
Residual Financing gap	0.00	0.00	0.00	0.00

Source: Angolan Authorities and IMF staff estimates and projections, March 2014.

4.3.2 The GoA does not intend to have recourse to the Sovereign Wealth Fund to finance the fiscal deficit. Furthermore, the Fund does not have stabilization mandate and as such its assets are not readily available to the treasury if needed in the event of a budget shortfall.

4.4 Beneficiaries of the Program

4.4.1 **The PSRSP is designed to assist the GoA in implementing its National Development Plan and reform priorities in the areas of PFM and Energy Sector.** The direct beneficiaries are Angola's key public institutions responsible for PFM and ministries responsible for the delivery of energy infrastructure development. The indirect beneficiaries are the population of Angola, with the private sector benefiting from better access to reliable and affordable electricity as well as transparency and efficient management of PFM, in particular procurement practices.

4.5 Social and Gender Impact

4.5.1 **The operation will have positive social and gender impacts**. Reform in the energy sector is expected to expand affordable access to electricity for the population, particularly for the very poor who are concentrated in rural areas and make up 45.2% of the 72% who are living in poverty.[18] The number of female-headed households is reported at 31% of all households and represents the majority of households living in extreme poverty.[19] Increased access to energy resources will positively impact the most vulnerable segments of the population, notably women. It will contribute to an increase in their productivity as women will have greater opportunities of employment through, for example, the development of new businesses. Furthermore, women and children will save time by avoiding trips for collecting or buying fuel, firewood, charcoal, etc. This will enable women and children to focus notably on education and income generating activities. Similarly, shifting to renewable energies will positively impact women's and children's health, mainly respiratory diseases, as they no longer have to be exposed to smoke and carbon monoxide from cooking indoors with wood and charcoal. Renewable energy also mitigates deforestation. There are other indirect impacts of this operation, specifically in the rural areas, which include improved access to piped water (contributing to e.g. cleaner water that reduces the incidence of water-borne diseases); better provision of maternal health services, contributing to reduced child and adult mortality and morbidity and improved newborn and maternal health; development of vocational training centers that rely on electricity that will allow increasing the number of women and youth attending evening classes; increased access to information (telecommunications, etc.); and boosted security (Annexes T5 and T6).

4.5.2 **Inclusive Infrastructure**: Improved energy efficiency and service will help the population in terms of income generation, as it will reduce household and business losses from power shortages. The reform includes changes to the existing subsidy framework, which may impact the price consumers pay for electricity. In that context, GoA has been encouraged to phase out fuel and utility subsidies (which account for 7.8% of GDP), and in fact GoA is preparing a new Social Assistance Strategy. To mitigate the adverse social impact on the most vulnerable population, GoA has prepared a 'pro-poor' tariff adjustment that is based on the consumption level of households. GoA is also in the process of preparing a communication plan in parallel with the tariff adjustments that will educate the consumer on billing, collection and energy savings (Technical Annex 6).

4.6 Environmental Impacts

4.6.1 **The PSRSP is classified as a category III impact, according to the Bank's procedure for environmental and social impact assessments.** The policy and institutional reforms supported by the operation are not expected to have any direct adverse impact on the environment. Improvements in policies and institutions for managing public resources, and improving sector governance in the energy sector as outlined above, cannot by themselves have a direct negative impact on the environment. Furthermore, GoA has put in place an Environmental Impact Assessment system that makes an EIA mandatory prior to the implementation of any project, private or public, to ensure compliance with environmental and social safeguard policies. In order to further strengthen the capacity of the energy sector in undertaking EIAs and assure that projects are screened in accordance with EIA guidelines, the operation supports the adoption of sectoral EIA guidelines, complementing the ongoing AfDB Support to the Environment Sector Project. The operation similarly supports Angola's transition to a greener pathway through key policies such as the Renewable Energy White Paper. This will ultimately lead to supporting legislation and institutional changes that

[18] IBEP 2013. Prefil da Pobreza. Relatorio Vol. III
[19] African Development Bank (2008) Angola Country Gender Profile

promote renewable energy technologies as the preferred choice for rural electrification and isolated systems in Angola (Technical Annex7).

V. IMPLEMENTATION, MONITORING AND EVALUATION

5.1 Implementation Arrangements

5.1.1 Implementation institutional framework**:** The Ministry of Finance (MOF), in collaboration with the Ministry of Energy and Water (MEW) and other agencies, will be responsible for implementing the reform programs supported by PSRSP. To further strengthen capacity the operation will be accompanied by a Capacity Building Program and Technical Assistance program as indicated in paragraph.

5.1.2 Disbursement Arrangements: The funds under the program will be disbursed in two tranches: USD 600 million in the first tranche and USD 400 million in the second tranche. Disbursement will be effected after fulfilment of conditions precedent. The proposed tranching is justified on the following grounds: (i) a number of critical reforms have already been implemented by GoA, as part of its dialogue with the Bank (see table 4). This confirms the GoA commitment to the reform program; (ii) a large number of critical measures of the program will be implemented in 2014; and (iii), the proposed tranching has been designed to take into account the Government's financing requirements (see Table 6).

5.1.3 The funds will be disbursed by the Bank into a foreign currency account to be opened in the Central Bank of Angola by the Ministry of Finance. In addition, a designated account in local currency will also be opened at the Central Bank and managed by the Ministry of Finance. Transfers will be made from the foreign currency account to the local currency account to meet local expenditures as required. The management of funds from these two accounts will be in accordance with GoA rules and procedures on budgeting, reporting and auditing.

5.1.4 Financial Management, Audit and Reporting Requirements: As indicated in paragraph 2.2.12, the fiduciary risk assessment revealed that the control environment and public finance management systems in Angola continue to present significant risks, in spite of the progress being achieved in PFM reforms. The proposed program is addressing fiduciary risks in two complementary ways: (i) including a specific component in the program (component 3) to support and monitor reforms to improve PFM systems and to reduce fiduciary risks. The envisaged reforms will introduce greater budget transparency, strengthen control systems and improve the procurement framework; and (ii) providing for specific disbursement and financial management arrangements for the funds of the proposed operation. In this respect, the program resources will be maintained in a dedicated account and centrally managed by the Debt and Aid Management Unit in the Ministry of Finance. This account will be subject to periodic audits by the Court of Accounts or an independent auditor. In addition, the Government will be required to submit to the Bank quarterly progress and funds flow reports to provide the requisite assurance on the expenditure of the resources. Also, an annual audit of fund flows and use of funds will be provided. The audit will be carried out by the Auditor General (Tribuno de Contras) or alternatively by an independent audit firm acceptable to the Bank. The audits will be performed in accordance with the Bank-approved Audit Terms of Reference and the audit reports will be submitted to the Bank within six months after the end of each respective financial year.

5.1.5 Procurement: The procurement arrangements for the budget support program will be undertaken using country systems. The FRA concluded that the overall risk level of the country's procurement system is high, and the residual risk is rated substantial, taking into consideration of the ongoing and planned reform initiatives and mitigation measures. The program will support and monitor the implementation of key policy actions to reduce fiduciary risks related to procurement. The proposed procurement risk mitigation measures include but not limited to: (a) Approval and implementation of procurement improvement action plan, (b) ongoing Bank support to building procurement capacity, (c) review and adoption of new procurement law and regulations, and Standard Bidding Documents, (d) the launching of a Procurement Portal to improve information on public procurement, (e) the establishment of independent complaints and appeals mechanisms, and (f) the establishment of a Technical Procurement Agency (UTN) by the presidential decree 169/13 with the responsibility to manage all procurement transactions which requires approval at the level of the President (above US$ 10 million).

5.2 Monitoring and Evaluation Arrangements

5.2.1 Quantitative indicators have been agreed upon with the Government to monitor the implementation of the Program. These indicators are defined in the Results Based logical Framework. The Bank will monitor the implementation of the Program through enhanced supervision and close follow-up and oversight by the Angola Field Office, which will play an important role in this regard, particularly with respect to policy dialogue and monitoring of the program results and impact. To this end, the Bank plans to strengthen the Field Office with high caliber lusophone experts in the areas of energy and public financial management. This will enhance the capacity of the office to effectively engage in policy dialogue, provide advice and facilitate program implementation. The Government will be required to provide to the Bank quarterly progress reports on the implementation of the program. Upon its completion, a Program Completion Report (PCR) will evaluate progress against outputs and outcomes set out in the Results Based Logical Framework (RMF) to assess the program achievement and impact, and to draw lessons for follow-up operations.

VI. LEGAL DOCUMENTATION AND AUTHORITY

6.1 Legal documentation

Loan Agreement between the African Development Bank and the Republic of Angola.

6.2 Conditions associated with Bank Group intervention

6.2.1 **Conditions precedent to entry into force of the Loan Agreement:** The entry into force of the Loan Agreement shall be subject to the fulfilment by the Borrower of the provisions of Section 12.01 of the General Conditions Applicable to Loan Agreements of the Bank.

6.2.2 **Conditions precedent to disbursement of the first tranche of USD 600 million:** Disbursement of the first tranche of the loan shall be conditional upon the entry into force of the Loan Agreement, and the Borrower providing evidence of the fulfilment of the following conditions, in the form and substance satisfactory to the Bank:

Condition precedent to disbursement of first tranche	Evidence required
1. Opening of a foreign currency account at the Central Bank of Angola	1. A letter from the Ministry of Finance providing evidence of having opened a foreign currency account at the Central Bank of Angola dedicated to receiving the proceeds of the Loan
2. Presidential Decree establishing three utility companies. (¶4.2.5)	*2. Copy of the signed Presidential Decree*
3. Submission of draft revised General Electricity Law to Cabinet *"Casa Civil"*. (¶4.2.5)	*3. A letter from the Minister of Energy and Water confirming the submission of the draft revised general Electricity Law to Cabinet "Casa Civil".*
4. Submission of a Renewable Energy White Paper to Cabinet *"Casa Civil"*. (¶4.2.8)	*4. A letter from the Minister of Energy and Water confirming the* submission *of the Renewable Energy White Paper* to Cabinet *"Casa Civil" and copy of the White Paper*

6.2.3. **Conditions precedent to the disbursement of the second tranche of USD 400 million:** The obligations of the Bank to disburse the second tranche of the Loan shall be conditional upon the fulfilment of the following conditions, in the form and substance satisfactory to the Bank:

Conditions	***Evidence required***
1. Amendment of the Presidential Decree establishing IRSE(¶4.2.5).	*1. Copy of the signed Presidential Decree*
2. Adoption of the by-laws "estatutos" for the generation, transmission and distribution companies (¶4.2.5).	*2. Copy of the by-laws* ("estatutos") for the generation, transmission and distribution companies.
3. Adoption of a revised National Inspectorate of Finance Regulation (¶4.2.16).	*3. Copy of the signed Presidential Decree*
4. Adoption of the procurement regulation (¶4.2.17).	*4. Copy of the signed Presidential Decree*

6.3 Compliance with Bank Group policies

6.3.1 **This program complies with all applicable Bank Group policies and guidelines.** These include: (i) the 2012 Bank Policy on Program-Based Operations, (ii) the Bank Group Ten-Year Strategy (2013-2022); (iii) Governance Strategic Framework and Action Plan 2014-18, and (iii) the Energy Sector Policy of the Bank Group.

VII. RISK MANAGEMENT

7.1 The risks and mitigation measures for the program are presented in Appendix 4.

VIII. RECOMMENDATION

Management recommends that the Board of Directors approve an ADB loan not exceeding USD 1.00 billion to the Republic of Angola for the purposes, and subject to the conditions, stipulated in this report.

Appendix 1: Letter of Development Policy

REPUBLIC OF ANGOLA
MINISTRY OF FINANCE

1205

April 24, 2014

Dr. Donald Kaberuka
President
African Development Bank Group
B.P. 323, 1002 Tunis Belvedere
Tunisia

RE: LETTER OF DEVELOPMENT POLICY

1. On behalf of the Government of Angola, I hereby write to request the approval of the African Development Bank (ADB) loan of US$ 1 billion to finance strategic interventions and development priorities for the 2014 and 2015 fiscal years that would help address infrastructure bottlenecks and promote inclusive economic growth. More specifically, the loan would support efforts to implement the structural and regulatory reform in the power sector and enhance transparency and efficiency in public finance management.

2. This Letter of Development Policy presents the macroeconomic performance in Angola and sets out the actions that Government has already taken and will take over the medium term to implement its development agenda.

I. ECONOMIC PERFOMANCE

3. Angola's economic growth rate places it among the fastest growing economies in Africa. Economic reform measures over the last 10 years have improved macroeconomic stability and growth averaged about 8.3% in the past decade, mainly driven by the oil sector. Nonetheless, in recent years growth in the non-oil sector has been reduced by the agricultural sector's slow recovery from the 2012 drought. Inflation, after reaching single digits for the first time in decades at end-2012, fell further to 7.7% by end-2013, comfortably below our 9% target.

4. In 2013, preliminarily, the Government's budget produced a fiscal deficit below 1.1% (well below the 2012 GDP surplus of 6.7%) , due to government's ambitious infrastructure investment program. Oil revenue fell to 29.5% of GDP (37.7% of GDP in 2012), due to lower prices and declining export volumes. Non-oil tax revenue remained at 7.5% of GDP (9.4% was budgeted) due to delays in adopting tax reform legislation. Preliminary current expenditures recorded a slight decrease to 28.6% of GDP (29.3% of GDP in 2012), while capital expenditure showed a slight increase to 12.3% when compared to 10.5% of GDP in 2012 (14.1% of GDP was budgeted).

5. The pace of economic activity in 2014 is expected to accelerate reflecting public investment in infrastructure, resulting in a further increase in the budgeted overall fiscal deficit for 2014 to 4.9% of GDP. The 2014 budget, as in 2013, uses conservative oil price projections (US$ 98 per barrel), allowing a realistic increase in total expenditures (7% over

2013). Capital spending as a share of total spending (31.6%) is projected to experience a nominal increase of about 1.5% when compared to 2013 preliminary budget figures.

6. The medium-term fiscal framework 2014-17 aims at achieving fiscal balances consistent with macroeconomic stability. Average GDP growth is projected at 7.15% in 2014-2017. Inflation is expected to remain in single digits supported by a relatively stable exchange rate and prudent monetary policy. Further improvement in the quality of spending is being achieved through streamlining government procurement processes, evaluation of projects, and rigorous cost-benefit analyses. The Government is committed to strengthening these processes further.

II. POLICY PRIORITIES FOR 2014 AND 2015

8. The Government's National Power Security Strategy and Policy (NESSP, 2011) was the first step to establishing and prioritizing urgently needed actions in the power sector. To convert that strategy document into implementable actions, the Government commissioned the Electricity Sector Transformation Program (PTSE), with key deliverables being a sector diagnostic study, submission of the optimum design of the electricity market model, and development of the sector reform roadmap with clear milestones and goals.

9. With regard to governance and accountability, the Government has been pursuing reforms to enhance governance and transparency in PFM and the oil sector. First, the government is committed to phase out the quasi-fiscal operations of Sonangol; as of March 2014, these off-budget operations have been discontinued. Second, the Government has made substantial progress in reconciling oil revenue transfers from Sonangol to the Treasury. Third, the creation of the Sovereign Wealth Fund (SWF) in 2012 will boost macroeconomic stability by insulating the annual budget from volatile oil revenue inflows.

10. The requested loan would support key short-run policy measures in the energy sector and improve access to electricity and create an enabling environment for private sector participation in the medium to long run, as detailed below. Macroeconomic stability is a necessary condition for addressing the critical challenges in the energy sector, and the loan will also help consolidating PFM reforms. This will contribute to job creation and poverty alleviation.

III. Power Sector Reform Support Program

11. The program's overarching objective is promoting inclusive economic growth by improving efficiency in the energy sector and consolidating PFM reforms. It seeks to improve operational efficiency, competitiveness and sustainability of the energy sector as well as greater transparency and efficiency in PFM. The program has four components: (a) restructuring the energy sector and improving its regulatory environment; (b) fostering private sector investment in the energy sector; (c) enhancing transparency and efficiency in PFM; and (d) capacity building and change management support.

Component 1: Restructuring the power sector and improving the regulatory environment.

12. The Government has begun restructuring the power sector, aiming to improve the institutional and regulatory framework, restructuring and unbundling the existing utilities, reviewing the current tariff and subsidy frameworks, improving the efficiency of utilities, strengthening the capacity of the sector regulator, promoting Renewable Energy, and attracting private investment. The Government has completed a number of studies detailing the unbundling process and held stakeholder consultations on the draft revised General Electricity Law. The proposed program will support the Government in its effort to implement Phase I of the PTSE. The policy actions supported by the program include two complementary priorities: (a) power sector restructuring, and (b) improving the regulatory environment.

13. The Power Sector Restructuring priority focuses on the approval of the unbundling of the generation, transmission and distribution systems and the establishment, through Presidential Decree, of three new utility companies for those activities. The program also supports (i) the approval of General Electricity Law by Cabinet, (ii) the establishment of contractual agreements (PPAs) between the three existing utility companies; and (iii) the adoption of the by-laws ("estatutos") of the three utilities. Consistent with the national objective of integrating women at decision making levels, the program will promote gender equality in the appointment of the board and top management in the utility companies. To ensure financial sustainability of the power sector, the revised law strengthens Pre-Payment of electricity services and power project assessment along value for money considerations.

14. The "Improving the Regulatory Environment" priority supports the Government's efforts to improve the sector regulatory environment through amendment of the Presidential Decree establishing IRSE. This aims to give IRSE greater autonomy regarding sector operations, approve and publish Network Access and Connection regulations, establish and publish performance criteria for Quality of Service, redesign the tariff, and monitor the sector operators. It will also reinforce IRSE's regulatory functions and independence, including through a funding mechanism based on fees and other payments from the sector. The program seeks to support the adoption of a Tariff adjustment Proposal. The first step in tariff adjustment is aimed at compensating for annual inflation since 2006 as an initial financial remedy for the sector. A tariff methodology is being proposed with the aim to ensure a social safety net for vulnerable consumers while providing for a gradual adjustment towards cost-reflective tariffs by 2021.

Component 2: Fostering private sector investment in the energy sector

15. In recent years, the GoA has adopted various reforms aimed at improving the business environment and attracting investment, including the recent adoption of (a) the Private Investment Law that provides various incentives to foster FDI, identifying energy and water as a priority area; and (b) the PPP Law. At the sector level, the General Electricity Law of 1996 explicitly provides for the possibility of privately-owned enterprises entering the generation and the distribution areas of the electricity value chain. This law is currently under review. The 2011 National Energy Security Strategy and Policy, the Energy and Water Sector Action Plan (2013-2017), and the Electricity Sector Transformation Program (PTSE) all prioritize the attraction of private sector investment, in particular at the generation/production level with a special emphasis on renewable energies and isolated systems for rural electrification.

16. The program will support ongoing and planned initiatives to improve the business environment for private sector participation in the power sector. In particular, the program will support the adoption of the White Paper on Renewable Energies as strategic for the development of renewable power production sources. The White Paper will introduce a regulatory framework fostering private sector investment in clean energy solutions as the preferred choice for rural electrification and isolated power systems in the country with a prominent role of small-scale privately-owned generation units in the hydro, wind, and solar segments. The program will also support the completion of the Renewable energy resource mapping, and the launching of a special Renewable Energy Feed-In Tariff (REFIT) scheme providing incentives to attract private investment into small green energy and rural electrification projects for isolated grids (below 10 MW), with a special focus on mini-hydro power plants.

Component 3: Enhancing transparency and efficiency in public finance management

17. The Ministry of Finance has placed PFM reform at the top of its reform agenda to ensure delivery of quality service and maximize impact of public investment program. The

establishment of a Sovereign Wealth Fund represents a very important development in terms of Angola's fiscal policy and expenditure planning. Government has recently enacted important measures to increase transparency of oil revenues and reduce quasi-fiscal operations (QFOs) by state-owned enterprises. The Government also wishes to undertake a comprehensive PEMFSR to assess the strength of its PFM systems and produce a medium-term action plan to address persistent weaknesses. It acknowledges receiving technical assistance already from the Bank; further reforms of PFM will help to reduce the vulnerability of the budget. .

18. The program will support policy measures in the areas of (a) budget credibility and transparency, and (b) improving efficiency and value for money in public procurement. Under budget credibility and transparency, the key policy action supported by program are: (a) publication of the 2014 "Citizen budget" with the aim to improving citizen participation in the formulation and monitoring of the government's budget; (b) the 2013 EITI Oil Revenue Reconciliation Report; (c) Adoption of a revised National Inspectorate of Finance Regulation; and (d) approval of a PFM reform action plan based on the recommendations of the Public Expenditure Management and Fiduciary Systems Review which will be completed in 2014. In addition, the program will also support government efforts to improve the collection and reporting of oil revenues and related transfers by completing a flow-of-funds report, which is expected to improve transparency and accountability in the management of oil revenues, as well as reducing the uncertainty of revenue flows from Sonangol.

19. In order to improve efficiency and value for money in public procurement, the program will support key policy measures including: (a) adoption of a PFM Reform Action plan; (b) launching of a Procurement Portal; (c) a revision of the procurement law; (d) adoption of the procurement regulation; and (e) adoption of Standard Bidding Documents.

20. Finally, to ensure the success of the reform program, the Government has developed a comprehensive capacity building plan. It is seeking technical assistance and change management support for a successful implementation of the reform.

21. In conclusion, we would like to reiterate the commitment of the Government to all these reforms, and we trust that this request for your support for the implementation of our Development Agenda will receive your favorable consideration.

Yours sincerely,

Minister of Finance

Appendix 2: Assessment of Eligibility Criteria of PBO

Prerequisite	Comments on current situation
Government commitment to poverty reduction, and inclusive growth	The Government of Angola is committed to reducing poverty and improving the well-being of its population. This commitment is driven by the Government's long-term development agenda as outlined in its Vision 2025 for equitable and inclusive development for all Angolans. The strategic direction and operational priorities are articulated in the National Development Plan (2013-2017), and Poverty Reduction Plan (Estrategia de Combate a Pobreza, ECF, 2010-2015). This is also accompanied by the National Energy Security Strategy and Policy 2011; and Energy and Water Action Plan 2013-2017.
Macroeconomic stability	Angola has emerged from a more than four decades of war to become Africa's second largest oil exporter. During the oil price boom of 2003-2008 Angola began to rebuild infrastructure, the oil and non-oil sectors grew substantially, and per capita gross domestic product (GDP) reached middle-income levels. Nonetheless, the economy remained highly vulnerable to oil revenue volatility. With highly expansionary policies backing a full-steam reconstruction effort, Angola faced severe macroeconomic imbalances after the collapse in oil prices in 2008-09. In response, government put in place a stabilisation program accompanied by several reform measures towards regaining macroeconomic stability. The program was supported by the IMF Stand-By Arrangements. Under the program, considerable progress has been made, and Angola attained an improved fiscal position, a more comfortable level of international reserves, a stable exchange rate, and lower inflation. Large domestic arrears were settled, and progress was made in strengthening fiscal transparency and accountability. Macroeconomic conditions continued to improve in 2010 - 2013. Headline inflation declined to single digit, the overall fiscal surplus increased, mainly due to high oil price. The external current account improved, and international reserves rose to the equivalent of 6.9 months import cover. Based on the joint World Bank-IMF low-income country DSA, Angola remains at a low risk of debt distress. The outlook for 2014-2016 remains favorable, notwithstanding the recent decline in oil prices. The pace of the economic activities is expected to accelerate. The energy, transportation, and construction sectors are likely to benefit from a gradual scaling up of public investment program. However, agriculture and food prices are affected by a drought. Over the medium term the government is focusing on creating a fiscal space to support the scaling up of investment spending within reduced revenue envelop. Threats to the outlook include the risk of slowing of the global economy and declining oil prices. Government of Angola maintain its relation with the IMF, and the second post-program monitoring concluded successfully in March 2014 (see appendix 3).
Satisfactory fiduciary risk assessment	A fiduciary risk assessment was carried out as part of the program preparation. Angola has recorded steady progress in a number of aspects with in the PFM systems since the 2005 review of the PEMFAR. In addition to the legal framework, there has been an improvement in the budgeting and reporting process with the adoption and use of the IFMIS (SIGFE). The system was rolled out to all budget units to reinforce the budgetary mechanisms. The financial accounts have been subject to audit by the Court of Auditors for the years 2011 and 2012. Reform has been introduced to enhance transparency and accountability of oil revenue management. The quasi-fiscal operations undertaken by state owned oil company (Sonangol) were phased out. The 2013 and 14 budget preparation included a first-ever medium term macroeconomic framework (2013-2017). Although improving, capacity constraints and weakness exists in the areas of budget, procurement and audit. The assessment concluded that the fiduciary risk of Angola is high, and recommend the program to incorporate risk mitigation measures and fiduciary safeguard measures and indicators to monitor its implementation. To this end, measures have been proposed in the program to mitigate these risks including: the Government will submit quarterly Budget execution reports to the Bank during the program implementation period; the operations will be audited (covering the funds flow and the use of funds) by the Court of Auditors (*Tribunal de Contas*) or private audit firm; a consolidated annual state accounts for 2014 and 2015 will be submitted to the National Assembly and Court of Auditors; implementation of procurement improvement action plan; building procurement capacity; review and adoption of new procurement law and regulations; technical assistance to carry out a Public Expenditure Management and Fiduciary Systems Review (PEMFSR) and preparation of PFM reform action plan drawing on the findings and recommendations of the PEMFSR. It is also worth noting monitoring and quarterly reports of the flow of funds will reinforce the control of the fiduciary risk. The program will be also be monitored through enhanced supervision missions, regular local supervision by the Bank's Office (AOFO) and in consultation with all the other partners.
Political stability	Angola has maintained political stability since the end of the civil war in 2002. The new Constitution adopted in February 2010 established a presidential parliamentary system. Parliamentary elections were held under the new Constitution in August 2012. Movimento Popular de Libertação de Angola (MPLA) has an absolute majority in parliament, with 175 out of 220 seats. The long-delayed first municipal elections are expected to take place in 2015 and the next legislative election is scheduled for late 2016.

Harmonization	Average ODA disbursements in Angola represent less than 2.3% of GDP, and therefore donors' influence in development coordination has been limited. In the process of preparing the proposed sector budget support operation, the Bank consulted key development partners such as the World Bank, IMF, EU, Norway and USAID. During the appraisal mission, the Bank organised a multi-stakeholder workshop to discuss Bank's intervention in infrastructure and the power sector in particular. The Bank will continue to engage with cooperating partners to (a) develop a common understanding of the developing challenges facing Angola; and (b) promote dialogue, and partnership in infrastructure and other areas of interventions critical for economic diversification and job creation.

Appendix 3: IMF Country Relations Note

IMF Executive Board Concludes the Second Post-Program Monitoring with Angola
Press Release No. 14/110
March 19, 2014

IMF Executive Board Concludes the Second Post-Program Monitoring with Angola

On March 5, 2014, the Executive Board of the International Monetary Fund (IMF) concluded the Second Post-Program Monitoring with Angola.

Macroeconomic performance in 2013 reflected a marginal increase in oil production and a moderation of non-oil growth compared to previous years' growth rates. Overall real GDP growth is estimated to have decelerated to 4.1 %, down from 5.2 % in 2012. Growth in the non-oil sector was held down by the agricultural sector's slow recovery from the drought that affected large parts of the country in 2012, but is still expected to have reached 5.8 % in 2013 due to government spending bolstering performance in the construction and power sectors. Inflation, after reaching single digits for the first time in decades at end-2012, declined to 7.7 % by end-2013, comfortably below the authorities' 9 % target. The favorable inflation performance allowed the Monetary Policy Committee of the National Bank of Angola (BNA) to reduce its policy rate by 100 basis points cumulatively throughout 2013, a bit less than the decline in inflation. Gross international reserves stood at US$33.2 billion at end-December 2013, the equivalent of about 7 months of projected 2014 imports.

Preliminary fiscal data indicate that Angola returned to a fiscal deficit for the first time since 2009, reflecting a sharp decline in oil revenue, while non-oil revenue and investment expenditure fell short of their targets. The fiscal surplus, which had reached 5.1 % of GDP in 2012, is expected to have turned to a deficit of about 1½ % of GDP in 2013. To finance the deficit and pay down domestic arrears, Angola drew down its government deposits from the equivalent of about 5 months of domestically-financed government expenditure to around 4 months. As a result of arrears repayments, total public debt is estimated to have declined to about 27 % of GDP.

Three significant institutional reforms were introduced in 2013. First, a new oil-sector foreign exchange law was implemented. The law requires oil firms to channel payments through the domestic banking sector and to settle payments to resident suppliers in domestic currency. The legislation has helped deepen Angola's financial markets and aided with the de-dollarization process. The second was the launch of Angola's sovereign wealth fund, the Fundo Soberano de Angola (FSDEA), which will be funded from some of the proceeds previously allocated to the Oil for Infrastructure Fund. Part of the funds from FSDEA will be invested in infrastructure projects with the objective of reducing bottlenecks and supporting growth. The third was the legislative package which introduced, as part of the 2014 budget, a legal definition of arrears and a new procedure requiring the co-signature of the Ministry of Finance for authorizing investment expenditure. These measures, along with institutional capacity building efforts, are intended to address the recurrence of domestic arrears.

The pace of economic activity in 2014 is expected to accelerate gradually as public investment in infrastructure creates opportunities for non-oil sector growth. Non-oil sector growth is expected to reach 6.4 %, underpinned by expanded investment in the power sector and road construction. The 2014 budget, if fully implemented, implies a further relaxation of the fiscal balance, with a projected increase in the overall fiscal deficit to about 5 % of GDP to finance a sizeable expansion in public investment needed to address infrastructure bottlenecks. Efforts to ease infrastructure gaps, improve the business environment, and reform the financial sector are expected to support diversification and further non-oil sector growth. However, a rapid increase in government spending in 2014 may also contribute to renew price pressures, limiting the scope for further interest rate reductions.

Executive Board Discussion

Executive Directors commended the authorities for Angola's return to solid economic growth, with single-digit inflation, strong international reserves, and a stable exchange rate. However, they regretted the continued weaknesses in public financial management and called for decisive efforts to address arrears.

While recognizing the continued improvement in the non-oil primary deficit, Directors expressed concern that, based on preliminary data, the Angolan economy returned to an overall fiscal deficit in 2013. Directors stressed the importance of mobilizing domestic resources, especially non-oil revenue, and cautioned against permanent increases in government spending not accompanied by a broadening of the non-oil tax base, to avoid accumulation of debt. Directors also recommended replacing fuel subsidies with targeted transfers for the most vulnerable.

Directors commended the progress in reducing inflation, while advising continued readiness to address any inflationary pressures. They were encouraged by the decisive progress toward reform and better oversight of the financial system, in line with the recommendations of the Financial Sector Assessment (FSAP), as well as by the creation of a Financial Stability Committee. Directors noted that the implementation of the foreign exchange law has proceeded as planned, and underscored the need for continued careful monitoring, further strengthening of supervisory capacity, and enforcement of prudential rules. Directors saw merit in the creation of a sovereign wealth fund, but noted the need to clarify its objectives, integrate it into a broader asset-liability management strategy, and ensure an effective accountability and transparency framework. They commended efforts to improve compliance with international standards to combat money laundering and terrorist financing.

Directors underscored the importance of addressing key challenges for public financial management. They urged the authorities to strengthen their efforts to reconcile oil revenue data, ensure a timely and complete transfer of oil revenue to the treasury, and continue to make progress in integrating quasi-fiscal operations in the budget, including infrastructure expenditure undertaken by Sonangol. Directors noted the need to increase public investment in the context of enhanced efficiency of public expenditure and service delivery, while taking into account absorptive capacity. They encouraged the authorities to put in place reforms that will lead to higher, more inclusive, and diverse growth.

Directors expressed disappointment over the inaccurate reporting of data on domestic arrears during 2010 and accounts payable during 2011, which led to noncomplying disbursements and breach of obligations under Article VIII, Section 5. Directors noted that capacity constraints and the lack of a clear definition of arrears under Angola's legal framework were among the factors contributing to this inaccurate reporting. They took note of the authorities' corrective measures and new legislation clarifying the legal definition of arrears and requiring the co-signature of the Ministry of Finance on contracts for public investment projects. They underscored the need for resolute implementation of the corrective measures, firm commitment to ending recurrent domestic arrears, and further progress in strengthening public financial management, taking advantage of Fund technical assistance.

In view of the corrective actions taken by the authorities, the Executive Board decided to waive the non-observance of the performance criteria, the conditions for granting prior waivers for non-observance of performance criteria, and the prior action that gave rise to non-complying purchases by Angola following the second through sixth reviews under the 2009 Stand-By Arrangement, and determined that no further remedial action is required in connection with the breach of obligations under Article VIII, Section 5.

Appendix 4: Risks and Mitigation Measures

Risk	Probability/ Impact	Mitigation measures
Macroeconomic risks due to volatility of the commodity prices / oil price shocks	Medium probability/High impact	Coordinated monitoring and dialogue around macroeconomic management to manage shocks, including the IMF article IV consultations. Accelerate implementation of the ongoing structural reform to increase the competitiveness of domestic production / diversification. Effective Management of the Sovereign Wealth Fund to guarantee that the implementation of capital projects continues uninterrupted.
Fiduciary risk including corruption.	High probability/ High impact	A fiduciary risk assessment was carried out and identified mitigation measures to addresses the identified risks. The mitigation measures include but are not limited to: (a) Ongoing reforms to the budget process, procurement, and the Public Investment Program to appraise and manage capital projects, all supported by the ongoing Bank's capacity building project; and the proposed operation. (b) The PBO funds flow will be subjected to quarterly progress reporting and annual audits. (c) Bank's support to PEMFSR and its action plan. (d) Quarterly fiscal information (budget execution); and submission of annual audit reports (covering the funds flow and the use of funds) to the Bank. (e) Preparation of a consolidated annual state accounts and submission to the National Assembly and Court of Auditors (*Tribunal de Contas*) for audit. (f) Implementation of procurement improvement action plan, and building procurement capacity. (g) Review and adoption of new procurement law and regulations. (h) Technical assistance to carry out a Public Expenditure Management and Fiduciary Systems Review (PEMFSR) and preparation of PFM reform action plan drawing on the findings and recommendations of the PEMFSR. Monitoring and quarterly reports of the flow of funds will reinforce the control of the fiduciary risk. Details of the mitigation measures is presented in Technical Annex 8. The program will be also be monitored through enhanced supervision missions, regular local supervision by the Bank's Office (AOFO) and in consultation with all the other partners.
Implementation capacity risk. Capacity constraints in Government could cause delays in the implementation of reforms.	Medium probability/ medium impact	The operation will include a complementary capacity building component with the aim to strengthening capacity in areas supported by PBO. The ongoing two PFM projects will help strengthen the capacity of key institutions that are entrusted with the responsibility of ensuring transparency and efficiency in public finance

Appendix 5: Operations Policy Matrix
POWER SECTOR REFORM SUPPORT PROGRAM

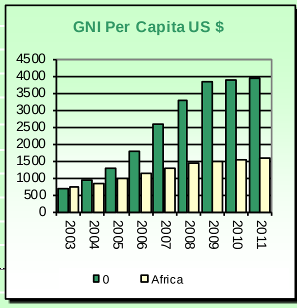
Medium term policy objectives	**Policy measures (2014)**	**Policy measures (2015) –**	**Outcomes (Monitoring indicators) 2016**	**CSP goals to which the program is contributing**
Pillar 1: Restructuring the power sector and Improving Regulatory Environment				
Restructuring the power sector	Presidential Decree establishing three utility companies signed. Evidence required: Copy of the signed Presidential Decree.	Contractual agreements (PPA etc.) between the three utility companies signed. Adoption of the by-laws "estatutos" for the generation, transmission and distribution companies.	Electricity sector revenue collection increased to USD 140 million (from USD 90 million in 2013) Distribution System Average Service Availability Index (ASAI)[20] of 75% (up from less than 60% in 2013) 40% of all customers metered (up from less than 20% in 2013) Board and senior Management positions of new power utilities and IRSE comprise at least 30% women. 1,120 members of staff trained, at least 30% women.	Pillar 2: Support to economic infrastructure development including power, water, transport etc
	Submission of draft revised General Electricity Law to Cabinet "Casa Civil". Evidence required: A letter from the Minister of Energy and Water confirming the submission of the draft revised general Electricity Law to Cabinet "Casa Civil".			
Improving the regulatory environment	Submission of a tariff proposal to the Economic Commission. Evidence required: A letter from the Minister of Finance confirming the submission of the Tariff Proposal to Economic Commission.	Amendment of the Presidential Decree establishing IRSE.		
		Adoption of a new Tariff Adjustment		
Pillar 2: Fostering private sector investment in the power sector				
Improved incentive and business environment for the private sector participation	Submission of a Renewable Energy White Paper to Cabinet "Casa Civil". Evidence required: A letter from the Minister of Energy and Water confirming the submission of the Renewable Energy White Paper to Cabinet "Casa Civil", together with a copy of the White Paper.	Renewable Energy Regulation including Feed-In Tariff (REFIT) adopted. Renewable Energy Resource Mapping Published.	At least 6 IPP RE contracts awarded based on REFIT	Pillar 1 - Stimulus to the competitiveness of the economy through capacity building of entrepreneurship, climate change and environment management, public expenditure and financial management reviews, policy dialogue and diagnostic work.
Pillar 3: Enhancing transparency and efficiency in public finance				
Maintaining budget credibility and transparency	The 2014 "Citizen budget" published and posted in the Ministry of Finance Website. Evidence required: Copy of the 2014 citizen budget and	Submission of the 2012 General State Budget to Tribunal Court of Account, and Parliament.	Variance between expenditure outturns and original budget reduced from over 25% (2013) to below 10%	Pillar 1 - Stimulus to the competitiveness of the economy through capacity

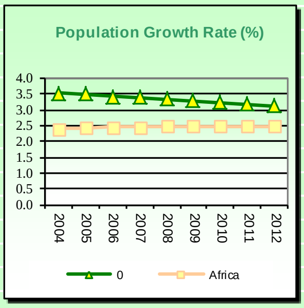
[20] Is the ratio of the total number of customer hours that service was available during a given time period to the total number of customer hours demanded.

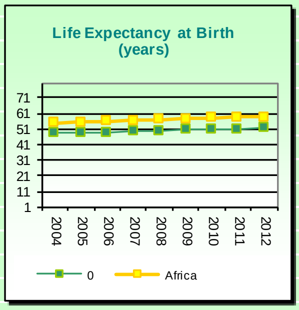
Medium term policy objectives	Policy measures (2014)	Policy measures (2015) –	Outcomes (Monitoring indicators) 2016	CSP goals to which the program is contributing
	print screen of the website		(2016)	building of entrepreneurship, climate change and environment management, public expenditure and financial management reviews, policy dialogue and diagnostic work.
	The 2013 Oil Revenue Reconciliation Report published and posted in the Ministry of Finance Website. Evidence required: Copy of the 2013 oil revenue reconciliation report and print screen of the website.	Adoption of a revised National Inspectorate of Finance Regulation.		
	Amendment to the Organic Budget Law and Budget Execution Rules to strengthen budget institutions and reduce the recurrence of Government Domestic Arrears. Evidence required: Copy of Presidential Decree 232/13.	A medium term PFM reform action plan adopted by the Ministry of Finance.	Stock of outstanding domestic arrears (USD 1.6 billion in 2013) reduced to 0 by 2016.	
Improved efficiency and value for money	Public Procurement Action Plan approved by the Ministry of Finance. Evidence required: A letter from the Ministry of Finance confirming the approval of the 2014-2016 Public Procurement Action Plan together with a copy of the Public Procurement Action Plan	Submission of a draft revised procurement law to Parliament. Adoption of the procurement regulation.	Execution rate of Public Investment Plan (PIP) increased from 50% (2013) to 75% (2016)	
	Establishment of Technical Procurement Agency (UTN). Evidence required: Copy of the Presidential Decree 169/13	Adoption of Standard Bidding Documents (SBD) by the Ministry of Finance.		
	Procurement Portal established. Evidence required: print screen of the Procurement Portal			
Pillar 4: Enhanced gender mainstreaming and environmental and social safeguards				
Improved gender mainstreaming in policy making	Adoption of Gender Policy to mainstream gender in main ministries	Implementation of gender action plan in main ministries for the roll out of the gender policy	Female representation in boards of utility companies increased from 23% in 2013 to at least 30% by 2016	Pillar 1 - Stimulus to the competitiveness of the economy through capacity building of entrepreneurship, climate change and environment management, public expenditure and financial management reviews, policy dialogue and diagnostic work.
Strengthened environmental and social safeguards in the power sector	New tariff proposal submitted to Economic Commission included a special tariff for most vulnerable households	Adoption and implementation of communications plan regarding tariff revision Adoption of Environmental Impact Assessment guidelines for the energy sector	100% of energy projects screened in accordance with EIA guidelines	

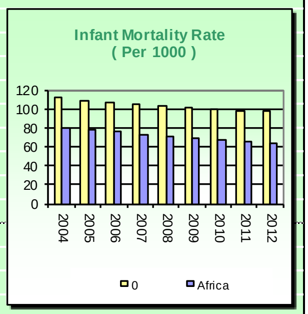
APPENDIX 6: ANGOLA: COMPARATIVE SOCIO-ECONOMIC INDICATORS

	Year	Angola	Africa	Develo-ping Countries	Develo-ped Countries
Basic Indicators					
Area ('000 Km²)	2011	1,247	30,323	98,458	35,811
Total Population (millions)	2012	20.8	1,070.1	5,830.9	1,249.2
Urban Population (% of Total)	2012	60.0	40.8	47.1	78.0
Population Density (per Km²)	2012	15.7	34.5	69.8	23.5
GNI per Capita (US $)	2012	4 580	1 604	3 795	37 653
Labor Force Participation - Total (%)	2011-2012	35.4	37.8	68.7	72.0
Labor Force Participation - Female (%)	2011-2012	45.8	42.5	38.9	44.5
Gender -Related Development Index Value	2005-2011	0.439	0.525	0.694	0.911
Human Develop. Index (Rank among 187 countrie	2008-2012	148	...	...	...
Popul. Living Below $ 1.25 a Day (% of Populatio	2009-2011	43.4	40.0	20.6	...
Demographic Indicators					
Population Growth Rate - Total (%)	2012	3.1	2.3	1.3	0.3
Population Growth Rate - Urban (%)	2012	4.4	3.4	2.6	0.7
Population < 15 years (%)	2012	47.7	40.0	28.5	16.4
Population >= 65 years (%)	2012	2.4	3.6	6.0	16.6
Dependency Ratio (%)	2012	93.9	77.3	52.6	49.2
Sex Ratio (per 100 female)	2012	98.3	100.0	103.3	94.3
Female Population 15-49 years (% of total populatic	2012	22.2	49.8	53.3	45.6
Life Expectancy at Birth - Total (years)	2012	51.5	58.1	68.2	77.7
Life Expectancy at Birth - Female (years)	2012	53.0	59.1	70.1	81.1
Crude Birth Rate (per 1,000)	2012	44.8	33.3	21.4	11.3
Crude Death Rate (per 1,000)	2012	14.2	10.9	7.6	10.3
Infant Mortality Rate (per 1,000)	2012	96.8	71.4	40.9	5.6
Child Mortality Rate (per 1,000)	2012	156.7	111.3	57.7	6.7
Total Fertility Rate (per woman)	2012	6.0	4.2	2.6	1.7
Maternal Mortality Rate (per 100,000)	2006-2010	450.0	415.3	240.0	16.0
Women Using Contraception (%)	2012	14.4	34.5	62.4	71.4
Health & Nutrition Indicators					
Physicians (per 100,000 people)	2004-2010	8.0	49.2	103.7	291.9
Nurses (per 100,000 people)*	2004-2009	135.0	133.0	168.7	734.3
Births attended by Trained Health Personnel (%)	2006-2010	47.3	53.7	64.3	...
Access to Safe Water (% of Population)	2011	53.4	67.8	86.5	99.1
Access to Health Services (% of Population)	2000	24.0	65.2	80.0	100.0
Access to Sanitation (% of Population)	2011	58.7	40.2	56.8	96.1
Percent. of Adults (aged 15-49) Living with HIV/AID	2011	2.1	4.6	0.9	0.5
Incidence of Tuberculosis (per 100,000)	2011	310.0	234.6	146.0	23.0
Child Immunization Against Tuberculosis (%)	2011	88.0	81.6	83.9	95.4
Child Immunization Against Measles (%)	2011	88.0	76.5	83.7	93.5
Underweight Children (% of children under 5 years	2007-2012	15.6	19.8	17.0	1.4
Daily Calorie Supply per Capita	2009	2 079	2 481	2 675	3 285
Public Expenditure on Health (as % of GDP)	2010-2011	2.2	5.9	2.9	7.4
Education Indicators					
Gross Enrolment Ratio (%)					
Primary School - Total	2009-2012	124.5	107.0	107.8	102.7
Primary School - Female	2009-2012	111.6	103.1	106.2	102.3
Secondary School - Total	2009-2012	31.3	46.3	66.4	100.4
Secondary School - Female	2009-2012	25.5	41.9	65.1	100.0
Primary School Female Teaching Staff (% of Total)	2009-2012	40.0	39.2	58.6	81.3
Adult literacy Rate - Total (%)	2011	70.4	71.5	80.2	...
Adult literacy Rate - Male (%)	2011	82.6	78.4	85.9	...
Adult literacy Rate - Female (%)	2011	58.6	64.9	74.8	...
Percentage of GDP Spent on Education	2008-2010	3.5	5.3	4.5	5.5
Environmental Indicators					
Land Use (Arable Land as % of Total Land Area)	2011	3.3	7.6	10.7	10.8
Annual Rate of Deforestation (%)	2000-2009	0.2	0.6	0.4	-0.2
Forest (As % of Land Area)	2011	46.8	23.0	28.7	40.4
Per Capita CO2 Emissions (metric tons)	2009	1.4	1.2	3.0	11.6









Sources : AfDB Statistics Department Databases; World Bank: World Development Indicators; last update : october 2013
UNAIDS; UNSD; WHO, UNICEF, WRI, UNDP; Country Reports.
Note : n.a. : Not Applicable ; … : Data Not Available.

Appendix 7: Rationale for Power Sector Reforms

With the end of civil war in 2002, Angola has remained on a fast growth path and recognizes that the status of the power sector characterized by electricity shortages and frequent outages is far below what is needed to support its economic development agenda. Aware of this reality, the Government prepared the ***National Energy Security Strategy and Policy (NESSP)*** **2011** paper to establish and prioritize the actions needed to address apparent institutional and infrastructure weaknesses, in particular the relationship between the various power utility entities and the need for mobilizing resources from the public and private sector to rehabilitate, expand and modernize the electricity network. The strategy recommended nine (9) priority Actions (Box 1) ranging from unbundling of the power utilities to empowering the regulatory agency, IRSE for better supervision of the electricity sector. In addition the NESSP also recommended development of polices that allow the use of endogenous energy resources, ensuring the convergence between the principles addressing energy security, efficient technologies, efficient management processes and promotion of environmentally sustainable power development[21].

Box1: National Energy Security Strategy & Policy (2011), Priority Actions

1. Conclude investment monitoring structure and begin regular progress monitoring;
2. Ensure implementation of the investment program and accelerate the launch of the projects on future energies (CCGT and hydro) as well as the transmission and distribution projects.
3. Implement the restructuring plan, and the public private participation framework in the sub-sector according to the business model and organization target, and strengthen internal capacities through recruitment/ training of skilled technicians;
4. Develop policy and regulatory framework for renewable energy;
5. Promote IRSE empowerment (roles and abilities strengthening) and undertake a revision of the regulatory framework;
6. Define a private investment attracting framework as well as its regulatory framework;
7. Propose a progressive tariffs evolution in order to ensure the reduction of subsidies to the final consumer tariffs and uniform prices all over the country;
8. Restructure and strengthen the public sector capacities and efficiency in the entire sub-sector.
9. Promote a contractual relationship among the sub-sector stakeholders in order to ensure the economic and financial sustainability throughout the value chain.

To convert the strategy document into implementable actions, the Government commissioned a detailed feasibility study, the **Electricity Sector Transformation Program (PTSE)** with key objective of undertaking a diagnostic study of the sector and submission of the most appropriate design of the electricity market model, and development of the sector reform roadmap. In its recommendations, the PTSE study proposed that power sector reform evolve through **four (4) phases** each with clear milestones and specific deliverables (Table 1). **Preparatory Phase** has three Stages. *Stage 1*, completed in September 2013 undertook diagnostic study and design. *Stage 2* is expected to be completed by April 2014 with the decree on unbundling of ENE, GAMEK and EDEL and establishing in their place three new power entities (Generation, Transmission, and Distribution), and strengthening of the IRSE. *Stage 3* expected to last until mid-2014 is the actual restructuring stage and introduction of best practices in utility management. **Phase 1,** runs from **2014 to 2017** and coincides with the end of the Energy and Water 2013-2017 Action Plan. This is the stabilization phase of the new power companies and has three stages starting with tariff and subsidy review and modelling. **Phase 2**, commencing from **2018 – 2021** introduces the concept of sector-wide operational efficiency with tariffs approaching cost of production and includes incentivized (Feed-In tariffs) participation of private sector in the Renewable Energy (RE) in rural areas.

[21] Currently the installed grid generation is less than 33% hydro and the remainder comprising diesel power. The objective is to eliminate the use of diesel based generation so that by 2025, combined cycle thermal power plants will account for 10% and hydropower will account for 90% of the total installed capacity of 8,742 MW.

Phase 3, 2021 – 2025 will introduce the concept of liberalization of the energy sector including full participation of Independent Power Producers at all levels and improvement of the energy mix with greater attention to RE and cleaner thermal based power plants. This stage will also see partial liberalization of distribution systems. To ensure sector sustainability and attract adequate private investment in power infrastructure development, tt is vitally important that at the time of market liberalization, tariff have reached cost reflective levels. This will depend on the overall pace of sector reforms, improvement of sector-wide operational and business efficiencies and the ability of the GoA to accelerate implementation of cheaper sources of energy. The proposed capacity building under this operation and close dialogue with Bank and other DPs on the reform process will be crucial for the sustainability of the reform and achievement of the set targets. .

The new market structure accepted by the Government is the classic Single-Buyer model which calls for unbundling the power utility into intrinsic core business areas (Generation, Transmission and Distribution), establishing commercial contracts between the market participants, and amending laws to improve market regulations, enhance sector efficiency and encourage participation of the private sector. The single-buyer model has inherent advantages such as (a) its simplicity which allows for gradual transition to competitive market for generation, (b) it enables the Government to efficiently re-capitalise the core business units and closely monitor their performance, (c) it provides for better balancing of supply and demand, and (d) it contributes to maintaining a stable power system in a rapidly evolving electricity market. It is worth noting that the Transmission system, as a natural monopoly, will remain a public sector entity. To address rural access to electricity services and enhance operational efficiency, the PTSE study proposed that the distribution be further unbundled into 5 geographic regions with a total of 18 business units.

Table 1 – PTSE Reform Phases – Actions and Goals

Prep Phase 2010-2013	Diagnostic and Design	Studies to determine the most appropriate restructuring model, amend applicable laws and develop other instrument required to support it.	Goal: Revision of General Electricity law; Decree on creation of 3 new utilities
Phase I 2014-2017	Stabilization	Stabilize; Reducing system & revenue losses; Develop Tariff model; Roll-out prepayment;	Goals: All points supply metered. Tariff adjustment towards cost-reflective value
Phase II 2018-2021	Transition to efficiency	Reduction of system losses; Setting the tariff model; Set regulatory model with efficiency incentives. Allow limited RE IPPs using RE-FIT	Goals: Regulatory model defined; Effective sector regulation by IRSE
Phase III 2021-2025	Partial Liberalization	Restructuring of the sector (PPPs, IPPs, Distribution system concessions); Reduction of system costs; coexistence of bilateral contracts & market competition	Goals: Sector sustainability, efficiency and high quality of supply

The NESSP is aligned with the infrastructure development pillar of the National Development Plan 2013-2017 and together with the PTSE program underpins the US$ 23 billion Energy and Water Action Plan 2013-17 that includes nearly 300 infrastructure projects on power generation (US$13.8 billion), transmission & distribution lines (US$5.9 billion), and electrification of 13 Municipalities (US$3.3 billion) adding over 800,000 new customers by 2017 with greater focus to the rural areas where access is less than 9% to stimulate socioeconomic activities in the rural areas and stem the flow of young people to cities where prospects for gainful employment are slim. In particular the Government has already committed USD 5.3 billion for several ongoing power infrastructure projects including construction of the first phase of Soyo 900 MW combined cycle gas power plant, upgrading of Cambambe hydropower plant to 700MW, extension of transmission lines, rehabilitation of the distribution system and installation of energy meters. Table 2 shows some indicative target figures.

Table 2 - Plan start point and objectives[22].

Designation	2012	2017	2025
Installed Power – Hydro and other Renewables	798MW	3832MW	7842MW
Installed Thermal based Power	1322MW	1868MW	900MW
Total Installed Capacity	2120MW	5700MW	8742MW
Total Estimated Electricity Energy Demand	8TWh	17TWh	33TWh
Grid Length	2.942 km	4,694 Km	5.500 km
Customers	752.000	1.500.000	2.500.000
Technical and Commercial energy losses[23]	24%	19%	9%
Electricity Access	30%	42%	60%

[22] PTSE Feasibility study

23 Billing not collected, not included (losses of 32%)

Appendix 8: Country Map