

**Document of
The World Bank**

FOR OFFICIAL USE ONLY

Report No. 106725-GB

GUINEA-BISSAU

**TURNING CHALLENGES INTO OPPORTUNITIES FOR POVERTY
REDUCTION AND INCLUSIVE GROWTH**



SYSTEMATIC COUNTRY DIAGNOSTIC (SCD)

JUNE, 2016

International Development Association
Country Department AFCF1
Africa Region

International Finance Corporation
Sub-Saharan Africa Department

Multilateral Investment Guarantee Agency

ACKNOWLEDGEMENTS

We would like to thank the following colleagues who have contributed through invaluable inputs, comments or both: Vera Songwe, Marie-Chantal Uwanyiligira, Philip English, Greg Toulmin, Francisco Campos, Zenaida Hernandez, Raja Bentaouet, Paolo Zacchia, Eric Lancelot, Johannes G. Hoogeveen, Ambar Narayan, Neeta G. Sirur, Sudharshan Canagarajah, Edson Correia Araujo, Melissa Merchant, Philippe Auffret, Axel Gastambide, Audrey Ifeyinwa Achonu, Eric Mabushi, Jerome Cretegny, Faheen Allibhoy, Tanya Yudelman, Giovanni Ruta, Isabelle Huynh, Upulee Iresha Dasanayake, Anta Loum Lo, Arthur Foch, Vincent Floreani, Audrey Ifeyinwa Achonu, Daniel Kirkwood, Eric Brintet, Kjetil Hansen, Alexandre Marc, Asbjorn Haland, Simona Ross, Marina Temudo, Pervaiz Rashid, Rasmane Ouedraogo, Charl Jooste, Daniel Valderrama, Samuel Freije and John Elder.

We are especially thankful to Marcelo Leite Paiva who provided superb research assistance for the elaboration of this report.

We also thank the peer reviewers: Trang Van Nguyen, Sebastien Dessus and Nadia F. Piffaretti.

Marek Hanusch has also had a key role as co-Task Team Leader of the Concept Note and main author of the Country Economic Memorandum, both documents which have been central to the making of this Systematic Country Diagnostic.

LIST OF ABBREVIATIONS

AfDB	African Development Bank
APBG	Guinea-Bissau Port Authority
AU	African Union
BCEAO	Central Bank of West African States
BOAD or WADB	West African Development Bank
CCVI	Climate Change Vulnerability Index
CEM	Country Economic Memorandum
CPIA	Country Policy and Institutional Assessment
CPLP	Community of Portuguese Language Countries
DB	Doing Business Report
DEA	U.S. Drug Enforcement Administration
DGO	Directorate of the Budget
DTF	Distance to Frontier
DTIS	Diagnostic Trade Integration Study
EAGB	National Utility Company (<i>Empresa de Eletricidade e Águas de Guiné-Bissau</i>)
ECF	Extended Credit Facility
ECOMIB	ECOWAS Security Mission in Guinea-Bissau
ECOWAS	Economic Community of West African States
EI	Extractive Industries
EU	European Union
FAO	United Nations Food and Agriculture Organization
FAOSTAT	United Nations Food and Agriculture Organization Statistics
FCFA or CFA	West African Franc (Currency)
FCS	Fragile- or Conflict-Affected States
FDI	Foreign Direct Investment
FGM	Female Genital Mutilation
FUNPI	Fund to Promote Industrialization of Agricultural Products
GDP	Gross Domestic Product
GIC	Growth Incidence Curve
GNI	Gross National Income
HA	Hectare = 1,000 m ²
HHI	Herfindahl-Hirschmann Index
IBRD	International Bank for Reconstruction and Development (The World Bank)
ICT	Information and Communication Technologies
IDA	International Development Association
IFC	International Finance Corporation
ILAP	Household Survey (<i>Inquérito Ligeiro para a Avaliação da Pobreza</i>)
ILO	International Labour Organization
IMF	International Monetary Fund
INEC	National Institute of Statistics of Guinea-Bissau
IUCN	International Union for Conservation of Nature

LCD	Least-Developed Countries
MAB	UNESCO Man and the Biosphere Program
MCS	Monitoring, Control and Surveillance
MDGs	Millennium Development Goals
MFI	Micro Finance Institution
MICS	Multiple Indicator Cluster Survey
MTN	MTN Group, Telecommunications
NAPA	National Programme of Action of Adaptation to Negative Effects of Climate Changes
NGO	Non-Governmental Organization
NPL	Non-Performing Loan
OAF	One Acre Fund
ODA	Official Development Assistance
OECD	Organisation for Economic Co-Operation and Development
PAIGC	Party for the Independence of Guinea-Bissau and Cabo Verde
PEFA	Public Expenditure and Financial Accountability
PEMFAR	Public Expenditure Management and Financial Accountability Review
PFM	Public Financial Management
PPP	Purchasing Power Parity
R&D	Research and Development
SCD	Systematic Country Diagnostic
SDI	Service Delivery Indicators Survey
SE	Social Enterprises
SME	Small and Medium Enterprises
SPS	Social Protection Strategy
SSA	Sub-Saharan Africa
SSR	Security Sector Reform
TSA	Treasury Single Account
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
UNDC	United Nations Office on Drugs and Crime
UNDP	United Nations Development Program
UNESCO	United Nations Educational, Scientific & Cultural Organization
UNICEF	United Nations Children's Emergency Fund
VMS	Vessel Monitoring System
WAEMU	West African Economic and Monetary Union
WARFP	West Africa Regional Fisheries Program
WDI	World Development Indicator
WDR	World Development Report
WGB	World Bank Group
WGI	Worldwide Governance Indicator

Regional Vice President, IDA: Makhtar Diop
Vice President, IFC: Snezana Stoilkovic
Vice President, MIGA: Karin Finkelston
Country Director, IDA: Louise Cord
Regional Director, IFC: Vera Songwe
Senior Directors: Ana Revenga, Carlos Felipe Jaramillo
Practice Managers: Pablo Fajnzylber, Seynabou Sakho
Task Team Leaders: Javier E. Baez, Rohan Longmore

TABLE OF CONTENTS

1 INTRODUCTION	2
1.1 Guinea-Bissau is rich in natural resources and has opportunities to develop some sectors that can ignite growth	2
1.2 Economic growth, poverty reduction and shared prosperity performance have been disappointing	3
1.3 A vicious cycle of low assets, low productivity and lack of inclusiveness.....	3
1.4 An undiversified and vulnerable economic base and an unfriendly business climate	4
1.5 Cross-cutting challenges stemming from endemic fragility and a weak governance framework.....	5
1.6 Dark clouds on the horizon risk sustainability of growth, distribution and poverty reduction	8
1.7 Looking ahead, change in Guinea-Bissau will require major strategic efforts	8
1.8 Diagnostics framework	9
1.9 Scope and process	12
2 POVERTY, SHARED PROSPERITY AND EQUITY.....	14
2.1 Poverty in Guinea-Bissau is deep and entrenched	15
2.2 Inequality is particularly high and the poor are not able to capitalize on growth.....	20
2.3 The productive capacity of households is undermined by low human and physical capital, and an inefficient use of natural resources.....	23
2.4 Assets are not only low but also are used at suboptimal levels.....	33
2.5 Returns to assets are inadequate and undiversified.....	36
2.6 Private transfers provide modest support to household incomes	40
2.7 Household well-being is highly vulnerable to shocks.....	41
3 MACRO LEVEL COUNTRY CONTEXT.....	44
3.1 Growth has been low, largely due to a narrow economic base	46
3.2 Low productivity, savings and investments also underpin slow growth.....	51
3.3 Economic growth is fragile	53
3.4 Structural weaknesses constrain the effectiveness and equity of fiscal policy	55
3.5 An underdeveloped private sector and multiple supply-side constraints hinder actual and potential output	58
3.6 Untapped economic opportunities to spur shared growth.....	68
4 WEAK PUBLIC GOVERNANCE AND INSTITUTIONS ARE A CHALLENGE FOR SHARED PROSPERITY	75
4.1 Fragility, institution-building and economic development	76
4.2 Repeated cycles of fragility in Guinea-Bissau	78
4.3 A rentier economy	80
4.4 Rent extraction is facilitated by weak public governance.....	83
4.5 The way forward for stronger governance and less fragility	86

5 SUSTAINABILITY CHALLENGES.....	89
5.1 Structural issues and existing and emerging risks threaten economic sustainability	89
5.2 Risks to environmental sustainability are ultimately risks to long-term inclusive growth	92
5.3 Some drivers of fragility remain unaddressed.....	94
6 PRIORITIZATION OF CONSTRAINTS ON PROGRESS TOWARDS THE TWIN GOALS.....	98
6.1 Prioritization of development constraints in a challenging politically environment	98
6.2 Prioritization process.....	99
6.3 Binding constraints and prioritized policy actions.....	101

Annexes

Annex 1A. The Guinea-Bissau performance in development indicators compared to regional and global benchmarks	118
Annex 2A. Dissecting the drivers of negative growth in Guinea-Bissau with Recentered Influence Function (RIF) and Oaxaca-Blinder decompositions	121
Annex 2B. Mincerian Regressions	125
Annex 2C. Climate Change Impacts.....	126
Annex 3. Prioritization Worksheet	127
Annex Figure 1A.1. Guinea-Bissau exhibits significant gaps in development when compared to other Sub-Saharan African countries and the world.	119
Annex Figure 2A.1. Composition and endowment effects for the Guinea-Bissau growth incidence curve (2002-2010)	122
Annex Figure 2A.2. Panel A: Composition effects	123
Annex Figure 2A.3. Panel B: Structural effects	123
Annex Figure 2A.4. Returns to select variables (inputs).....	124
Annex Table 2B.1. Mincerian regressions for log of monthly earnings in poor and non-poor households (2010).....	125
Annex Table 2C.1. Guinea-Bissau's climate is changing in a number of ways.....	126

BIBLIOGRAPHY

List of Figures

Figure 1.1: Guinea-Bissau's growth performance has been hampered by political instability	7
Figure 1.2. Diagnostics framework to assess opportunities for poverty reduction and shared growth	11
Figure 2.1: Poverty in Guinea-Bissau is high and increased between 2002 and 2010	16
Figure 2.2: Poverty rate in Guinea-Bissau is above the rate in Sub-Saharan Africa (percent).....	16
Figure 2.3 Household per capita consumption has been systematically lower in rural areas.....	19
Figure 2.4: Poverty rates for most rural regions are above the national average.....	19
Figure 2.5: Despite moderate improvements, the endowment base for Guineans remains low...19	
Figure 2.6: Proxying chronic and transient poverty in Guinea-Bissau (2010)	20
Figure 2.7: Gini coefficients across countries in Africa (circa 2008-2012)	20
Figure 2.8: Consumption Growth was experienced by households in the top of the distribution	21
Figure 2.9: The lower quintiles are also the most deprived in asset ownership and access to basic services.....	22
Figure 2.10 . Educational outcomes in Guinea-Bissau are lower than the regional average.....	24
Figure 2.11. Gender inequities in educational outcomes are greater than regional average	25
Figure 2.12: Education outcomes are weaker for the lowest income quintiles	25
Figure 2.13. Poor access to improved water and sanitation and lower life expectancy (panel a)	27
Figure 2.13. Life expectancy at birth (panel b)	
Figure 2.14. Maternal health outcomes are weaker in Guinea-Bissau than in Sub-Saharan Africa	28
Figure 2.15. Child mortality is high even by regional standards	29
Figure 2.16. Malaria cases and malaria related deaths in Guinea-Bissau (2014)	29
Figure 2.17: Guinea-Bissau has considerable renewable and non-renewable resources.....	30
Figure 2.18:Resources accounting for the largest share of the country's total wealth	30
Figure 2.19. While labor participation is slightly above the average for neighboring countries, the gender gap is regionally high (2010)	33
Figure 2.20: The economically active population wants to work more hours... ..	36
Figure 2.21: Youth have higher unemployment	34
Figure 2.22. Guinea-Bissau's labor market is marked by informal employment.....	38
Figure 2.23. The share of salaried labor in Guinea-Bissau is lower than some of its neighbors (circa 2008-2012).....	38
Figure 2.24. Rice and cashew have had lower yields than the regional average	39
Figure 3.1. Guinea-Bissau has a history of low economic growth... ..	46
Figure 3.2: The primary sector is large in Guinea-Bissau.....	54
Figure 3.3: A major driver of economic growth	50
Figure 3.4: Both savings and investments are low in Guinea-Bissau	52

Figure 3.5: The cashew prices is an important determinant of the current account balance, savings, and investment	52
Figure 3.6: The international cashew price has been falling as global cashew exports increased.....	59
Figure 3.7: Guinea-Bissau's terms of trade have been deteriorating throughout the 2000s	53
Figure 3.8: Fiscal space is severely limited in Guinea-Bissau.....	56
Figure 3.9: Guinea-Bissau strongly relies on export taxes for domestic revenue	56
Figure 3.10. The size of the military is excessive by regional standards.....	57
Figure 3.11. Fiscal and macroeconomic management performance are relatively weak in Guinea-Bissau	58
Figure 3.12. Electricity access for households and businesses is low in Guinea-Bissau.....	60
Figure 3.13. Mobile phone coverage has increased in Guinea-Bissau but the internet revolution has not yet taken off.....	62
Figure 3.14: Guinea-Bissau's performance on Doing Business indicators is low, hindering the formation of capital in the country.....	63
Figure 3.15. The financial is sector is highly underdeveloped, constraining the business climate	64
Figure 3.16. Low bank penetration in Guinea-Bissau	65
Figure 3.17. Private sector Credit/GPD in WAEMU	65
Figure 3.18. Total Lending to the Guinea-Bissau Private-Sector (FCFA millions)	66
Figure 3.19. Median wages are relatively low in Guinea-Bissau... but, due to low productivity, unit labor costs are high	67
Figure 3.20. The Guinean labor market is relatively rigid.....	67
Figure 3.21. Firing costs are one disincentive for firms to hire into formal jobs	67
Figure 3.22 Guinea-Bissau is the fifth largest exporter of raw cashew worldwide, yet the country hardly produces processed cashew (kernel).....	70
Figure 3.23: Petroleum and cooper have respectively the second and third largest potential for export.....	77
Figure 4.1. Fragility is correlated with underperformance in multiple human development outcomes	77
Figure 4.2. Easier access to rents in associated with a higher incidence of military coups (LHS) and rent-seeking is associated with worse economic performance (RHS)	79
Figure 4.3. Corruption is endemic in Guinea-Bissau (percent of businesses)	81
Figure 4.4. Important differences appear between bilateral trade data reported by Guinea-Bissau and the one reported by its partners	82
Figure 4.5. Guinea-Bissau ranks among the bottom 10 percent globally on the quality of governance	83
Figure 5.1. Fluctuation in financial flows coincides with political events	90
Figure 5.2. Overall fiscal balance and public debt.....	96
Figure 5.3. Debt has declined to manageable levels	91
Figure 5.4. Gross and adjusted net savings (percent of GNI, 2010).....	93

Figure 5.5. In 2014, Guinea-Bissau was among the countries most likely to experience a coup.	95
Figure 6.1. Human capital base expansion, agricultural technology and risk-mitigation are top priorities to address low inclusiveness.....	105
Figure 6.2. Diversification, infrastructure and financial inclusions are top priorities	109
Figure 6.3. Inefficiencies in public spending, financial management systems, public sector capacity and the business regulation were considered top priorities to address fragility and weak governance	114

List of Tables

Table 2.1. The extreme poor have further deprivations when compared with the moderate poor	18
Table 2.2. Labor participation is lower among women and urban residents	34
Table 2.3: The level of welfare of female-headed households is influenced by transfers.....	40
Table 2.4: Approximately 70 percent of the population live in the coastal area	46
Table 3.1. Real per capita GDP in Guinea-Bissau and its peers, 1990-2014	47
Table 6.1. Ranking of mitigating actions to address constraints to lack of inclusiveness and low rural productivity	104
Table 6.2. Ranking of mitigating actions to address constraints to low and unstable growth....	108
Table 6.3. Ranking of mitigating actions to address constraints to fragility and weak governance	113

List of Boxes

Box 2.1. Female Genital Mutilation and HIV in Guinea-Bissau.....	28
Box 2.2. Women, Land and Productivity	32
Box 2.3. Opportunities and risks from future demographic changes in Guinea-Bissau	35
Box 2.4. The government policy on climate change	42
Box 3.1. “Terra Ranca” is the government reform agenda moving forward.....	46
Box 3.2. Economic Growth in Guinea-Bissau and Cabo Verde.....	49
Box 3.3. How much does Guinea-Bissau have to grow to catch up with the world?.....	51
Box 3.4. The 2015 Brussels Donor Roundtable	58
Box 4.1. Chronology of fragility in Guinea-Bissau.....	79
Box 4.2. Elites and the illegal economy in Guinea-Bissau.....	83
Box 4.3. Strengthening Public Sector Performance in Service Delivery through Partnership with Social Enterprises.....	87
Box Figure B2.3.1 The working age population will double by 2040	38
Box Figure B3.3.1 GDP Per Capita Projections for Guinea-Bissau at 9 percent growth.....	56

TURNING CHALLENGES INTO OPPORTUNITIES FOR POVERTY REDUCTION AND INCLUSIVE GROWTH

EXECUTIVE SUMMARY

COUNTRY CONTEXT

1. **Guinea-Bissau is fighting a battle against poverty, low growth, and political fragility. Each of these areas presents both a formidable challenge as well as an opportunity for serious, long-lasting and much-needed change.** With a Gross National Income (GNI) per capita of US\$570, Guinea-Bissau is the 12th poorest country in the world. Gross domestic product (GDP) growth averaged a mere 0.4 percent between 2000 and 2014, a rate that is symptomatic of a stagnating economy; this is roughly one-quarter the average performance of Sub-Saharan Africa (1.9 percent). The economy is dominated by agriculture, accounting for over 40 percent of GDP and employing about 80 percent of workers, high by regional standards. The production and export of raw cashews nuts constitute the main source of income for more than two thirds of the households (and for virtually all small farmers) and represent over 85 percent of the country's total export earnings. Little productivity growth across all sectors and low (public and private) savings and investment have undermined growth potential. The economy is characterized by a dual vulnerability to external developments stemming from a high dependence on a single export and a high susceptibility to international price shocks. Additionally, frequent bouts of political instability and shocks associated with adverse weather conditions impose large costs on economic and social development in the country.

2. **Poverty is entrenched, inequality is high and other human development outcomes are weak with many of the key indicators worsening over time.** In 2010, over two-thirds (67.1 percent) of the population survived on less than US\$1.9 per day (2011 PPP), which is well above the poverty rate in other Sub-Saharan African countries (42.7 percent) and noticeably high by global standards.¹ Additionally, poverty rose between 2002 and 2010, especially the extreme poverty rate. At 0.50, the Gini coefficient indicates that inequality in Guinea-Bissau is high, even in comparison to African and overall low-income country standards, and has worsened over time. Guinea-Bissau ranks 177th of 187 countries on the United Nations (UN) Human Development Index. The majority of the population, particularly the poor, have limited access to basic goods and services that directly influence the well-being of households. Consequently, a substantial number of households are trapped in a vicious cycle of low assets, low productivity, and low incomes.

3. **Fragility is intrinsically linked to low growth and lack of inclusiveness.** After independence in 1974, local elites quickly filled the power vacuum. The absence of strong local institutions meant that elites competed to capture the limited rents available, a feature which is still present in the country, leading to the constant threat of political upheaval. Over time there have

¹ See Annex 1A1 for a detailed discussion on the benchmarking exercise conducted for this report. The benchmarking methodology creates an algorithm to compare Guinea-Bissau against two groups of peers; its neighbors in sub-Saharan Africa and the world. Within these two groups, Guinea-Bissau is then benchmarked against the group's best performer, considering a normalized range within the sample of data for each indicator.

been several coup attempts including four realized, the highest number in the world. Instability has led to a weak State and institutions. Guinea-Bissau scores in the bottom 10th percentile on all indicators measuring public sector capacity in the World Bank's Worldwide Governance Indicator (WGI). Weak governance and elite capture have, in turn, created a patchy social compact, leading to weak provision of basic public goods and services, limited economic opportunities for the private sector and perversion of justice. Public sector management is also dysfunctional; public administration is undermined by a large bureaucracy, notably the overrepresentation of the military. Public institutions are geared toward providing private goods to elites—political and military—rather than public goods to citizens. Of course, instability has also been costly for the country. The most recent coup-imposed government mismanaged the 2012 and 2013 cashew campaigns, oversaw an increase in smuggling of natural resources, the suspension of donor programs, and halted public investment, which cut current expenditures and increased arrears. The economy contracted by 1.8 percent in 2012 and barely recovered in 2013, growing at 0.8 percent.

4. Nonetheless, the country has potential for unlocking income-generating opportunities for growth. Much of the country's rich endowment of natural capital comprising pristine national parks, forests, vast agricultural land, fisheries, as well as unexplored mineral fields, remain untapped. This is in spite of the of the country's advantageous geographical location which is conducive to maritime and inland waterway transport and trade. Agriculture, albeit pervasive, is mostly done through extensive subsistence farming, with little infusion of productivity-enhancing techniques and technologies. As a result, agricultural products are sold unprocessed. Much of the economy is not monetized, based instead on bartering, which may hamper incentives to exploit income-generating opportunities. The development of human and physical capital in agriculture can help farmers enter higher-value markets providing much needed boosts to the current cashew market and other cash crops, including revitalizing the tattered rice sector. Similarly, the development of landing capabilities and appropriate gear for fishermen can go a long way in bolstering value added in the fisheries sector. The extractive industry is small, with a large potential for the extraction of minerals such as bauxite and phosphates. There are also opportunities for timber production, processing and export. Additionally, the country's vast biodiversity is yet another underused source of high-value international tourism. Lastly, addressing deficiencies in the current system of land rights and titling should improve households' investment decisions inside and outside of the cashew sector. The central government's commitment is very important for this potential to flourish. Following elections in 2014, Guinea-Bissau released a strategy called *Terra Ranca*, which proposed investments in human development, infrastructure, business environment, urban development, biodiversity and natural capital, with an overarching theme of peace and governance.

5. The diagnostics framework of this Systematic Country Diagnostic (SCD) is based on three interrelated themes: inclusiveness of growth, overall economic growth and macro context, and sustainability risks, including the overarching issue of fragility. Broadly speaking, these three closely intertwined core building blocks lay at the foundations for inadequate levels of income and consumption in the population: 1) the inclusiveness of the economy (micro-determinants of household welfare), namely the availability of equitable opportunities, through asset accumulation and utilization, for all members of the society to contribute to and benefit from economic growth; 2) robust and sustained economic growth and cross-cutting economic services,

and fair, transparent and efficient governance and economic institutions; and 3) economic, social, political and environmental risks for the sustainability of the process of growth, distribution and poverty reduction (Figure 1.2). At the micro level, the inclusiveness of the economy is assessed by the assets households own, the intensity with which they are utilized and their returns. At the macro level, raising household incomes requires an enabling economic and institutional environment. The sustainability element examines whether the current economic, political, social and ecological systems and processes are dynamically sustainable in the medium and long term. Finally, as a cross-cutting theme, fragility and weak governance are considered and addressed at each step of the development process in Guinea-Bissau.

TRENDS IN POVERTY AND SHARED PROSPERITY

6. Poverty in Guinea Bissau is high and increased between 2002 and 2010, in particular the rate of extreme poverty. Nearly 1.2 million people (69.4 percent) were poor in 2010. One third of the population (33.1 percent) lived in extreme poverty, surviving on under US\$1 per adult equivalent per day (national extreme poverty line). Both absolute and extreme poverty rose between 2002 and 2010, the former by 3.7 percentage points and the latter by 11.5 percentage points. Rural standards of living are considerably lower than those in the capital, Bissau, reflecting lower rural human capital and low agricultural productivity. The difference in standard of living in rural and urban areas has widened over time. This has been accompanied by a similar shift over time toward employment in agriculture, further emphasizing the link between a sector plagued by low productivity and higher poverty rates. The higher levels of poverty seen outside of Bissau are further compounded by multiple deprivations in non-monetary dimensions, such as access to basic and social services, human capital, and levels of public infrastructure.

7. While the poor in Guinea-Bissau experience multiple deprivations, the extreme poor are further disadvantaged when compared even with the moderate poor. Household size among the extreme poor is substantially larger—on average over two more members- partly driven by a higher number of children which increases the dependency ratios (Table 2.1). School attainment—proxied by literacy rates and primary education for the head of household—is also lower. The extreme poor also have fewer household assets. Compared to the rest of the poor, their incomes are not only lower but also less diversified as nearly 90 percent of the extreme poor are employed in agriculture. When it comes to connectivity, the extreme poor are significantly more disadvantaged; on average farther from markets and schools and lacking access to electricity. General access to services, already low for the population in general, is even more critical for the extreme poor, with nearly half lacking safe drinking water and four-fifths lacking sanitation.

8. Between 2002 and 2010, consumption growth was on average only positive for the top 10 percent of the population and negative for the remaining households, highlighting poor households' limited ability to productively exploit assets. The greater consumption growth is associated with higher returns to assets for the non-poor, and is tightly linked to the ability of the elites to more efficiently capture the productive markets in Guinea-Bissau. The poorest of poor fared worse than the rest of the population since their consumption fell between 5 and 10 percent. Many other factors contribute to negative consumption growth among the poor, including significantly lower human capital, higher presence of those households in sectors plagued by low productivity such as agriculture, as well as a strong rural presence where markets are often non-

monetized (i.e. barter), disconnected (due to lack of infrastructure), and operating within a weak legal framework for land tenure and rights. Poor Bissau-Guinean households not only suffer from a paucity of human capital and physical assets, but their ability to productively exploit the assets they do possess is limited, adding another barrier to exiting poverty. The overall low returns to assets highlight the wide scope of the low-productivity and fragile economy equilibrium that characterizes Guinea-Bissau.

TAPPING INTO GROWTH OPPORTUNITIES

9. **The reality in Guinea Bissau is one where the country has lost decades without achieving significant growth and has been underperforming relative to most of its peers since independence.** The economy, which is dependent on the cultivation and export of unprocessed cashew nuts, has barely grown over the past twenty five years, recording average GDP per capita growth of about 0.7 percent significantly below peers. In fact, Guinea Bissau is one of the slowest growing economies in the continent. The country's inability to break out of the low growth, high poverty incidence trap can be attributable to its narrow economic base, low human capital and the absence of fiscal buffers which increases its susceptibility to shocks (including, but not limited to, terms of trade and unfavorable political events). There is a strong negative correlation between Guinea Bissau's growth performance and political developments. Institutional and political economy factors are major impediments to strengthening fiscal policy and management of public finances in the country; existing organizational structures have not supported the required fiscal discipline.

10. **The main engine of growth, agriculture, is constrained by several bottlenecks.** Productivity in the agriculture remains weak. Major constraints limiting the exploitation of the existing agricultural potential, include: (i) unclear land rights and poor land management system; (ii) lack of hydro-agricultural developments; (iii) limited access to inputs and technologies to support production; (iv) inadequate investment in agricultural research and development (R&D) and extension; (v) underdeveloped agribusiness value chains with low ratio of food processing to primary agriculture due to poor infrastructure (logistics, energy, storage, etc.); (vi) a lack of finance for agriculture; and (vii) unpredictable policy environment and dearth of market information. Within agriculture, in addition to cashew output, most of Bissau-Guinean products are essentially raw materials, which means the structure of the economy is concentrated in the first rung of the value ladder. Almost all of Bissau-Guinean exports are at the fringes of the product space, serving as raw inputs to more sophisticated value chains in other countries. This limits the ability of the economy to diversify into other products and create forward and backward linkages with other sectors. Cashew is the best example of a raw material with considerable potential to add value through processing.

11. **Nonetheless, Guinea Bissau's persistent low growth does not reflect its potential, given the country's abundant natural resources and advantageous geographical location.** Guinea Bissau possesses opportunities to grow much faster but the key to unlocking this potential will require action on several fronts including, *inter alia*, tapping multilateral agencies, regional institutions West African Economic and Monetary Union (WAEMU) and Economic Community of West African States (ECOWAS) and other stakeholders for technical and financial support to anchor critical interventions, while also introducing initiatives to directly address the underlined

weaknesses in the existing business environment and governance framework. The country has the opportunity to advance its development agenda by expanding its cashew value-chain, capitalizing on emerging green shoots in agriculture and other sectors by creating the environment for greater private sector participation in the economy, and by addressing some of the pressing infrastructure needs of the country. There is great potential in cashew processing, cultivation in rice and a diversified range of cereal, fruits and tubers. Fisheries and mining are also recognized as possible engines of growth. In spite of the country's significant natural beauty, the potential of the tourism sector remains largely untapped. Moving into higher value added activities in industry and services will be crucial to achieve the growth rates Guinea-Bissau will require to catch-up with other countries.

TREADING A FRAGILE POLITICAL ENVIRONMENT

12. Political instability has been continuously hampering economic growth, making recent efforts to capitalize on periods of stability critical for poverty reduction. Guinea-Bissau suffers repeated cycles of fragility with negative effects on economic, political and social systems. This has been induced by competition for power among the political and military elites, and enabled by weak institutions, meant to govern the country and provide public goods to the population. The country scores in the bottom 10th percentile on all indicators measuring public sector capacity in the World Bank's Worldwide Governance Indicator. Rooted in colonialism and continued by those who have governed after independence, weak governance has allowed a rentier economy to fester, effectively diverting much of public resources toward private gains. The main consequences have been low provision of services, faltering infrastructure, low access to education and health, and low-level household welfare equilibrium, to the low and unstable growth, inadequate private sector development, vulnerability to shocks and overall poor macroeconomic management. Moreover, there is growing consensus among both academics and policymakers that weak institutional capacity, governance and accountability are important in explaining why political instability and violence repeats in the same countries or subnational regions (WDR, 2011).

13. The business environment is skewed towards the interests of the elites, affecting all sectors and is particularly problematic in cashew production and trade where profits are concentrated. In Guinea Bissau, the business of the Government is often conducted through personal networks and political patronage. The tiny private sector remains controlled by few groups of elites, often political ones. The close-knit nature of this group encourages corruption and discourages transparency. An important source of rents is found in the agricultural sector, particularly in the production and export of cashews, where the elite benefits mainly as traders. Many smallholders do not capture the main benefits of cashew production and trade, and might benefit from diversifying their activities; nonetheless, they remain in agriculture due to a mix of low-liquidity, the low-risk nature of cashew cultivation, and the fear of land-grabbing (due to weak land rights) should they not keep the land busy year-round. Outside of agriculture, appropriation of budget and external resources through holding public office or being a public servant is another major source of rents. Likewise, illegal activities, especially around drug trade and illegal fishing and lumber exports are the third major source of rents in Guinea Bissau. Addressing the generally weak governance and institutional frameworks which enable elite capture is paramount for reducing poverty and promoting shared prosperity.

PRIORITIES IN TURNING CHALLENGES TO OPPORTUNITIES

14. **The Guinea-Bissau SCD is forward-looking and relies on a prioritization process to identify main binding constraints to poverty reduction and inclusive growth, and to guide future engagement with the country.** The analysis highlights entry points where policy intervention can contribute to breaking the current low-welfare, low-growth equilibrium, and the high-fragility environment in Guinea-Bissau. To address low inclusiveness and low rural productivity, households need to be propped up by better access to basic services, especially education, health and water and sanitation. Guinea-Bissau could benefit greatly from more reliable port, road, and utility infrastructure and which could help to strengthen the value-chain in cashew and other crops. Shocks can be potentially life threatening to the poor and extreme poor, hence social protection is another important part of this strategy moving forward. The low and unstable growth that has plagued the country is partly rooted in a low-equilibrium in its largest sector, agriculture, and in the undiversified nature of the economy. The cashew economy as central to agriculture can benefit from investments in developing and expanding its value chain (i.e. extension services, as well as storage and transportation infrastructure); other crops such as rice and sectors such as fisheries can also benefit from more investment. Financial inclusion can help poor households diversify their income by increasing the availability of credit through greater bank penetration and microfinance opportunities. Governance can be strengthened by improving public management systems and simplifying bureaucracies, particularly where transparency and accountability in expenditures are concerned. A more friendly business environment can also be constructive for the country, including streamlining import/export practices, and beginning to address property rights issues. Lastly, this SCD cannot overstate the importance of sustained political stability as a prerequisite to unlocking the country's limitless potential in many of the areas explored by this document.

1 INTRODUCTION

1.1 Guinea-Bissau is rich in natural resources and has opportunities to develop some sectors that can ignite growth

1. **Guinea-Bissau is a tropical country on West Africa's Atlantic coast. It has a population of 1.7 million and possesses rich cultural and religious diversity.** Guinea-Bissau shares borders with Senegal to the North and Guinea-Conakry to the East and South. Much of what is known about Guinea-Bissau dates back several centuries from its inclusion in the African kingdom of *Mandinka* under the Kabu Empire in the 12th century, to its transition to Portuguese rule in the 16th century, and to its full independence from Portugal in 1973 (recognized in 1974). Today, over 20 ethnicities, multitudes of religions, languages, and cultures are represented in Guinea-Bissau. The official language, Portuguese, is spoken by less than 20 percent of the population (mostly in the capital, Bissau), while Creole (a mix of Portuguese and native tongues) is the language spoken by the vast majority of people. The country has a large Muslim population and a Christian minority, with several other native African religions intertwined in between. Guinea-Bissau is a member of the Economic Community of West African States (ECOWAS) which provides the country access to regional markets and institutions through the promotion of interstate economic and political cooperation.²

2. **The country has rich biodiversity and ecosystems of both local and global significance.** This natural capital results from the country's unique geographic position: a coastal country lying in a transition zone between the Sub-Saharan arid savannah in the northwest, and humid tropical forest ecosystems in the south, which benefit from substantial rainfall and rivers. This unique region is characterized by a dense mesh of small river basins, as well as the Bijagos Archipelago. These areas are home to large diverse ecosystems and habitat habitats, including mangroves, sandbanks and mudflats, shallow estuarine waters, and sub-humid Guinean forests, all of which are known to be among the most diverse ecosystems on the West African coast. Inland, in the south and southeast areas of the country, a forest belt region comprised of dense and open patches of forest, interspersed with woodland savannahs, also hosts significant biodiversity.

3. **Guinea-Bissau has the potential for unlocking currently untapped income-generating opportunities for growth.** Natural-resource-based sectors are already the largest in Guinea-Bissau, in particular agriculture. Nevertheless, much of the country's rich endowment of natural capital, comprising pristine national parks, forests, vast agricultural land, fisheries, as well as unexplored mineral fields, remain untapped in spite of their advantageous geographical location, which is conducive to maritime and inland waterway transport and trade. Agriculture, albeit pervasive, is mostly done through extensive subsistence farming, with little infusion of technology. Much of the country's economic activities are based on a system of bartering, which hamper incentives to exploit income-generating opportunities. Nonetheless, the development of human and physical capital in agriculture can help farmers enter higher-value markets providing a much needed boost to the current cashew market and other cash crops, including revitalizing the tattered rice sector. Similarly, the development of landing capabilities and appropriate gear for fishermen can go a long way in boosting the value added in the fisheries sector. The extractive industry is

² ECOWAS is a 15-member regional group serving a population of approximately 300 million with a mandate of promoting economic integration in all fields of activity of the constituting countries.

small, with a large potential for the extraction of minerals such as bauxite and phosphates. There are also opportunities for timber production, processing, and export. Additionally, the country's vast biodiversity is yet another underused source of high-value international tourism. Lastly, addressing deficiencies in the current system of land rights and titling should improve households' investment decisions inside and outside of the cashew sector.

1.2 Economic growth, poverty reduction, and shared prosperity performance have been disappointing

4. Guinea-Bissau has a history of low and volatile economic growth. With a Gross National Income (GNI) per capita of US\$570, Guinea-Bissau is the 12th poorest country in the world. Between 1990 and 2014, Guinea-Bissau's real per capita Gross Domestic Product (GDP) fell by 12.3 percent. GDP growth averaged a mere 0.4 percent between 2000 and 2014, a rate that is symptomatic of a stagnating economy. This is roughly one-quarter of the average performance of Sub-Saharan Africa (SSA) (1.9 percent) and is well below the performance of some of the neighboring countries (1 percent in Senegal, 1.2 percent in Mali, 1.7 percent in Liberia, and 2.6 percent in Burkina Faso). The economy is dominated by agriculture, which accounts for over 40 percent of GDP and employs about 80 percent of workers, considered high by regional standards. The production and export of raw cashews nuts constitutes the main source of income for more than two-thirds of the households (and for virtually all small farmers) and represents over 85 percent of the country's total export earnings. Other agricultural activities include small-scale rice production and horticulture. Little productivity growth across all sectors and low (public and private) savings and investment have undermined growth potential. The economy is characterized by a dual vulnerability to external developments stemming from a high dependence on a single export and a high susceptibility to international price shocks. Additionally, frequent instances of political instability, and shocks associated with adverse weather conditions, impose large costs on economic and social development in the country.

5. Poverty is entrenched, inequality is high, and other human development outcomes are weak. In 2010, over two-thirds (67.1 percent) of the population survived on less than US\$1.9 per day (2011 purchasing power parity (PPP), which is well above the poverty rate in other Sub-Saharan African countries (42.7 percent) and noticeably high by global standards.³ Additionally, poverty rose between 2002 and 2010, especially the extreme poverty rate. At 0.50, the Gini coefficient indicates that inequality in Guinea-Bissau is high, even in comparison to both African and overall low-income country standards, and has worsened over time. Guinea-Bissau ranks 177th of 187 countries on the United Nations (UN) Human Development Index. The majority of the population, particularly the poor, have limited access to basic goods and services that directly influence the well-being of households. Consequently, a substantial number of households are trapped in a vicious cycle of low assets, low productivity, and low incomes.

1.3 A vicious cycle of low assets, low productivity and lack of inclusiveness

6. Faster economic growth alone will not be enough to bring significant improvements to the living standards of most Guineans. The evidence shows that even the modest economic

³ See Annex 1A for a detailed discussion on the benchmarking exercise conducted for this report. The benchmarking methodology creates an algorithm to compare Guinea-Bissau against two groups of peers; its neighbors in sub-Saharan Africa and the world. Within these two groups, Guinea-Bissau is then benchmarked against the group's best performer, considering a normalized range within the sample of data for each indicator.

growth recorded in the 2000s (assuming its distribution was neutral) would have reduced poverty by over 8 percentage points. Yet, in reality, since growth happened at the top, but consumption fell for the rest of the income distribution, poverty increased by 3.7 percentage points.

7. Several reinforcing mechanisms exist in Guinea-Bissau that, if unaddressed, will likely cause poverty and underdevelopment to persist. Most of the population, especially women, suffers from a paucity of endowments such as human capital, skills, and physical capital. Adults in the bottom 40 percent complete on average just two years of schooling, life expectancy is below the average for Sub-Saharan Africa, and most lack secure tenure rights. Inadequate nutrition, and a large burden of disease of adults and children limits the ability of individuals to work at full capacity and results in lasting effects across generations. Low access to basic services, such as clean water, sanitation, and electricity, coupled with failures in critical markets (for example, credit), poor public infrastructure, and pervasive fragility and natural resource depletion, limits economic opportunities and reduces returns to endowments differentially. In addition to material constraints, behavioral traps also appear to play a role because households' mental resources are overly focused on short-term basic needs, resulting in forgoing opportunities with higher returns in the middle and long term. Consequently, most households are stuck with cashew production, a stable yet low-investment, relatively lower-risk and low-productivity subsistence item. Nearly seven in ten individuals are below the poverty line, and over half of the population are deemed chronically poor. In contrast, the better-off population manages to benefit from modest but positive growth.

1.4 An undiversified and vulnerable economic base and an unfriendly business climate

8. In view of the narrow economic base and low productivity, economic growth is constrained and largely susceptible to external and internal shocks. The structure of Guinea-Bissau's economy has barely changed over the last two decades and remains largely agrarian. Growth performance is volatile, with the production and export of a single commodity (unprocessed cashew nuts) being the engine of growth. The production of cashews is concentrated in the first rung of the value ladder, serving as raw inputs to more sophisticated value chains in trading-partner economies. The high degree of concentration in one activity and the lack of safety nets, social insurance, or credit leaves the country subject to occasional trade shocks, harvest failures, and climatic events, undermining the stability of income of the poor. Increasing diversification and quality upgrading to levels observed in the WAEMU between 2001 and 2010 could have resulted in an increase in the average real growth rate for Guinea-Bissau by about 1 percentage point (International Monetary Fund (IMF) 2014a). Low and unpredictable public revenues, regressive and distortionary taxation, and poor quality of public expenditure, a part of which is related to the size of government, limits the effectiveness and equity of the fiscal policy to redistribute resources.

9. The potential of the economy to contribute more to output growth and prosperity is further constrained by a less than accommodating business environment. Guinea-Bissau is weakly integrated into global agricultural value chains, in particular due to an unfavorable business environment. The private sector depends heavily on the public sector's consumption and investments due to a small domestic market and very few export-oriented sectors. The business climate is not conducive to the generation of growth, employment, and productive capital. Guinea-Bissau ranks at the bottom of all the 10 Doing Business indicators. The challenges are

considerable, and range from a poor business and regulatory environment to limited access to finance, poor infrastructure, low productivity, and relatively high labor costs and political instability. Another central challenge is the complexity of the import and export environment, with many stakeholders controlling the port, and much of the institutional authority relying on informal dealings that decrease transparency, and encourage corruption and clientelism. In fact, Guinea-Bissau performs below Sub-Saharan Africa with regard to most of these business indicators. The lack of investments is an important pillar of a vicious circle of low productivity, low growth, lack of opportunities, and elite capture which then feeds back into low investments, suggesting the country is trapped in a low-growth equilibrium.

1.5 Cross-cutting challenges stem from endemic fragility and a weak governance framework

10. Guinea-Bissau has a history of political and institutional fragility dating back to its independence.⁴ Understanding the country's fragility requires a look at its colonial period.⁵ Unlike other Portuguese colonies, Guinea-Bissau was not considered fit for settlement, and the colonial administration thus made no significant investments in the country beyond what was required to extract natural resources. Other than a small local elite, Guineans received virtually no provision of health care, education, or social services, and were unable to access—much less participate in—any aspect of the public administration. At the time of independence in 1974, Guinea-Bissau's literacy rate was 1 percent, and the country had only 60 kilometers of paved roads. The liberation war, which was one of the bloodiest on the African continent, did not automatically deliver improved livelihoods and peace. Instead, Guinea-Bissau has been beset by one experience of political instability after another, starting in 1980 when the first elected president was ousted in the country's first military coup - leading to the peaceful separation of Cabo Verde and Guinea-Bissau.

11. Guinea-Bissau is one of the most coup-prone and politically unstable countries in the world. Four successful coups have been recorded in independent Guinea-Bissau, with another 16 coups attempted, plotted, or alleged.⁶ Among the previous five chiefs of staff of the armed forces, three were murdered and one was forcibly exiled by rival officers. In recent years, the army has arguably become ever more powerful by drawing on financing from the international narcotics trade, which has led some observers to refer to Guinea-Bissau as Africa's first 'narco-state'. Military coups are just one manifestation of fragility. Frequent government turnover is another. Between 1999 and 2009, Guinea-Bissau experienced a government turnover each year. This was as much a consequence of military interference as it was of dismissals of the Government by the President, a constitutionally admissible process in the country's semi-presidential polity.

12. Fragility is largely the result of a rentier economy and the interlinked competition for rents among the elite. The functioning of product markets, for instance in agriculture, is often exposed to rent seeking through the weak country's business regulatory framework. Parts of the cashew business are controlled by powerful elites, which enjoy market power in the distribution and export channels. Another common form of rent extraction is the misappropriation and

⁴ Marshall, Monty and Benjamin R. Cole, *Global Report 2014: Conflict, Governance and State Fragility*, Center for Systemic Peace.

⁵ Advancing Stability and Reconciliation in Guinea-Bissau: Lessons from Africa's First Narco-State, O'Regan, Davin; Thompson, Peter, *Africa Center for Strategic Studies Special Reports*, 2013.

⁶ Center for Systemic Peace, Database of Coups d'Etat, 1946-2014. See also 2015 CEM and Fragility Assessment.

misallocation of public resources such as taxes, subsidies, funds from schemes created to increase access to finance and to promote the industrialization of the agricultural sector and wages of public officials. The appointment of civil servants is often based on patronage and corruption objectives rather than public administration needs or merit. Reviews of the country's public finance management system find discrepancies in amounts imported by other countries and exported by Guinea-Bissau implying potential corrupt practices (i.e. under reporting of exports) between traders and port officials. The amount of and competition for rents has increased in recent years with the intensification of the international drug trade, which uses Guinea-Bissau as a transshipment location. Civilian elites, too, compete for rents, supported by strong clientelist networks, further entrenching the country's fragility.

13. Rent extraction is the consequence (and likely also the cause) of weak public governance, which ultimately results in a broken social compact. Guinea-Bissau ranks in the bottom 10th percentile on all indicators measuring public sector capacity in the World Bank's Worldwide Governance Indicator (WGI). These institutional weaknesses translate into a weak public financial management framework manifested in insufficient internal and external controls, disconnect between the budget and the implementation of government programs and policies, an outdated tax framework and ineffective tax management. Public administration is undermined by a large bureaucracy, notably the overrepresentation of the military. Public institutions are geared toward providing private goods to elites –political and military ones– rather than public goods to citizens. The broken social contract is reflected in the low provision of basic public goods and services, limited economic opportunities for the private sector, and perversions of justice. Benchmarking analysis undertaken for the SCD shows that Guinea-Bissau ranks poorly (at the bottom 10-20 percent) with respect to regional averages in most, if not all, the indicators of human capital, physical capital, business climate, transparency, rule of law, and other quality of institutions.

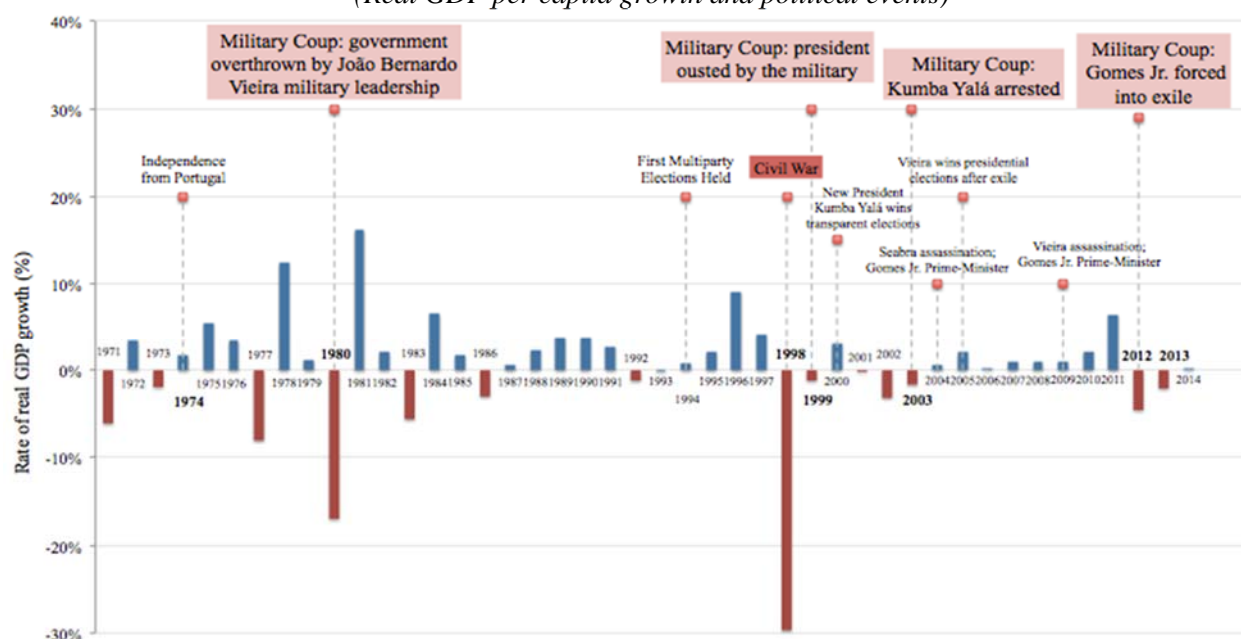
14. The cost of political and institutional fragility has been very large. The costs from the 2012 coup were severe. The military-backed government mismanaged the 2012 and 2013 cashew campaigns, aggravating the income losses of farmers and domestic traders due to a large drop in cashew prices. Smuggling of lumber increased when border controls softened, and corruption spread. The immediate suspension of donor programs in response to the coup dried up external financing. Public investment ground to a halt, current expenditures had to be cut, and arrears increased. This resulted in widespread strikes, the disruption of education and health services, and severe outages in both electricity and running water in Bissau. The economy contracted by 1.8 percent in 2012 and barely recovered in 2013, growing at 0.8 percent. Frequent political disruptions, such as the civil war and military coups, are the main culprits causing recessions in Guinea-Bissau because they unsettle economic activity from which the economy recovers only slowly (Figure 1.1). In the most recent Article IV assessment (July 2015), the IMF estimated that Guinea-Bissau's GDP per capita could have been 65-90 percent higher had it not been for its endemic fragility.

15. Elections restored democracy in 2014, and the new government embarked on ambitious reforms. Guinea-Bissau's largest political party, the Party for the Independence of Guinea-Bissau and Cabo Verde (PAIGC), won the elections held in early 2014, both at the parliamentary and the presidential level. The candidate of the main opposition party conceded

quickly, paving the way for the return of democracy. The new government, led by Prime Minister Domingos Simões Pereira, took important steps to curb military interference in politics, and developed an ambitious national development plan and strategy aimed at reigniting growth and poverty reduction (see Annex 1A). The plan is closely aligned with the World Bank Group (WBG) Country Economic Memorandum (CEM) that was finalized in January 2015. Early actions by the government included addressing macroeconomic issues in consultation with the IMF. The government also made considerable progress in restoring the orderly functioning of public finances, and started preparing a comprehensive plan to demobilize the military. Key public services were partially restored. A window of opportunity appeared to have opened, and the donor community rushed to help the country seize it by pledging US\$1.5 billion during a donor roundtable in March 2015. Growth rebounded in 2014 and 2015.

16. A short-lived period of political stability after the elections fostered important steps toward a set of reforms, including achieving stronger fiscal sustainability. Upon taking office in 2014, the leadership swiftly passed a retroactive budget for 2014 and prepared a 2015 budget in record time, both of which were unanimously adopted by parliament. It suspended the controversial and regressive 'FUNPI surcharge', an additional tax on export which the World Bank has estimated to have increased poverty by as much as 2 percentage points. The new government also successfully strengthened domestic revenue mobilization, significantly increasing non-tax revenues (especially through fishing licenses), while also raising customs and tax revenues by 39 percent and 9 percent year-on-year respectively. In addition, structural reforms were put in place that tightened control over fuel imports, reduced tax exemptions, rehabilitated customs posts and intensified tax audits of large taxpayers. Combined, these actions have given a much-needed boost to public revenues. The Government also succeeded in clearing all external arrears and a significant portion of domestic arrears.

Figure 1.1: Guinea-Bissau's growth performance has been hampered by political instability
(Real GDP per capita growth and political events)



Source: World Bank staff based on WDI, 2015

17. **However, a fresh round of political tensions emerged in mid-2015 and continues until today.** After the 2014 elections, the hope was that Guinea-Bissau had turned decisively away from a history of instability. Nonetheless, the country's underlying fragility was revealed by tensions between the President and the Prime Minister, reminiscent of the past experience of frequent government turnover and ushering in a new round of instability. President José Mario Vaz dismissed the Pereira Government on August 15, 2015, which resulted in two months of uncertainty and speculation before a new cabinet was sworn in on October 13, 2015. The new government was led by Carlos Correia until May 2016, when he was removed by the President in another bout of instability (albeit constitutional). The Correia Government had committed itself to the policies of its predecessor, particularly the development plan shared with donors and known as "Terra Ranca". Fortunately, the military has not intervened throughout the crisis and has declared itself neutral.

1.6 Dark clouds on the horizon risk sustainability of growth, distribution, and poverty reduction

18. **The structure of the economy in Guinea-Bissau, including the large dependency on its natural wealth to ignite and sustain growth, and the political settlement and interlinked elite competition for rents, subject the country to multiple economic, environmental, and political risks moving forward.** On the macroeconomic side, structural issues and existing and emerging risks threaten economic progress. Over time, the dependence on the cashew sector has grown, leaving the economy highly vulnerable to external, political, and natural shocks. While existing risks of fiscal distress are moderate, the sustainability of the fiscal accounts is dependent on grants from the international community, which in turn are unpredictable due to endemic fragility. Structural fiscal deficits are also a common feature of the economy.⁷ At the current rate of utilization of natural resources, Guinea-Bissau is depleting rather than building the value of its total wealth. Risks in the non-renewable sector such as depletion, environmental degradation, and mismanagement of rents, are also prevalent. Climate change will exacerbate many of these risks. Important drivers of fragility, the major source of political, economic, and social instability, remain unaddressed. The internal competition between politicians and the different arms of government is a major risk to the current reform agenda. Insofar, as elite capture and corruption, investment in the poor can contribute to promote inclusive growth but also stimulate demand for transparency and accountability. While interference of the military in political and economic spheres has lessened, the politicization of the security sector continues to create a series of severe imbalances. Reform of the security sector is crucial but bears its own risks. Impunity, a weak justice sector and a lack of effective conflict resolution systems fuel instability. Defining features of Guinea-Bissau's fragility, such as weak institutions and a rural-urban divide, also remain unaddressed.

1.7 Looking ahead, change in Guinea-Bissau will require major strategic efforts

19. **Considering fragility and weak governance as strong contextual factors, issues of inclusiveness, higher rural productivity, and overall growth are found to be key areas of binding constraints to poverty reduction and shared growth in Guinea-Bissau.** They follow from the analytical model applied in the SCD and from existing evidence because they reflect a context where the basic elements of well-being and economic opportunities are inadequate and

⁷ Structural fiscal deficit is the deficit that remains across the business cycle, and reflects the fact that the general level of government spending exceeds prevailing tax levels.

unequally distributed, and where economic growth, a key ingredient for poverty reduction, has been unsatisfactory and volatile. Cutting across most of the economic, social, and political structures of the country, the existence of fragility and weak governance, the third set of core constraints, represents major obstacles to improving the development outcomes of the country.

20. Results from the prioritization exercise highlight entry points where policy intervention can contribute to breaking the current low-welfare, low-growth equilibrium in Guinea-Bissau. In these areas of constraints, there is broad consensus resulting from the diagnostics and consultations that the selected policy actions contemplated are able to deliver the desired impact on poverty, with some actions even becoming entrenched. They include the urgent need to improve basic service delivery, raise productivity in agriculture, diversify the economy, strengthen market support services, and address allocative, technical, and regressive inefficiencies in public spending. With regard to addressing the constraint of fragility and weak governance, many of the more difficult reforms rate poorly on feasibility and traction, pointing to an unwillingness to break from the established order. This suggests that the gains from addressing the other constraints remain at risk.

21. Addressing the impediments to inclusive growth will require confronting the vicious cycle of fragility and elite capture by utilizing flexible strategies to engage directly with the elite and with other actors that can legitimately circumvent it. The challenges to poverty reduction and shared prosperity in Guinea-Bissau are self-reinforcing and well entrenched, requiring a massive and disruptive mix of measures to break with tradition and transform the economy. Marginal and stand-alone interventions, though feasible, may not be enough to break well-established norms that have kept the country in a high poverty, low growth fragility trap for the past three decades. Breaking the status quo will initially require strategies that yield benefits both to the poor and to the elite. This SCD points to a mixture of strategies that combine direct engagement of government with increased participation of other local, regional, and international actors to create a critical demand for transparency and accountability. Explicitly excluding the elite from the reform process may not be realistic or even effective in challenging elite domination. On the contrary, it can exacerbate rather than lessen fragility. Empowering the poor through increased demand for transparency and accountability, and through direct, more effective delivery of basic services, can be a major catalyst in the process of strengthening institutions and addressing behavioral norms in public and political spheres. This includes strengthening mechanisms to channel broad-based demands for improvements in public goods, and to achieve better performance by public officers. Working directly with beneficiaries, for instance, through community-driven programs implemented by Non-Governmental Organizations (NGO), can contribute to address urgent needs in basic services such as education, health, and water. International actors like WAEMU, ECOWAS, the African Union (AU) and the donor community can also harness forces to align incentives to bring about more transparency and stability.

1.8 Diagnostics framework

22. The diagnostics framework of this SCD is based on three interrelated themes: inclusiveness of growth, overall economic growth and macro context, and sustainability risks. Broadly speaking, these three closely intertwined core building blocks lie at the foundations for inadequate levels of income and consumption in the population: (1) the inclusiveness of the economy (micro-determinants of household welfare), namely the availability of equitable

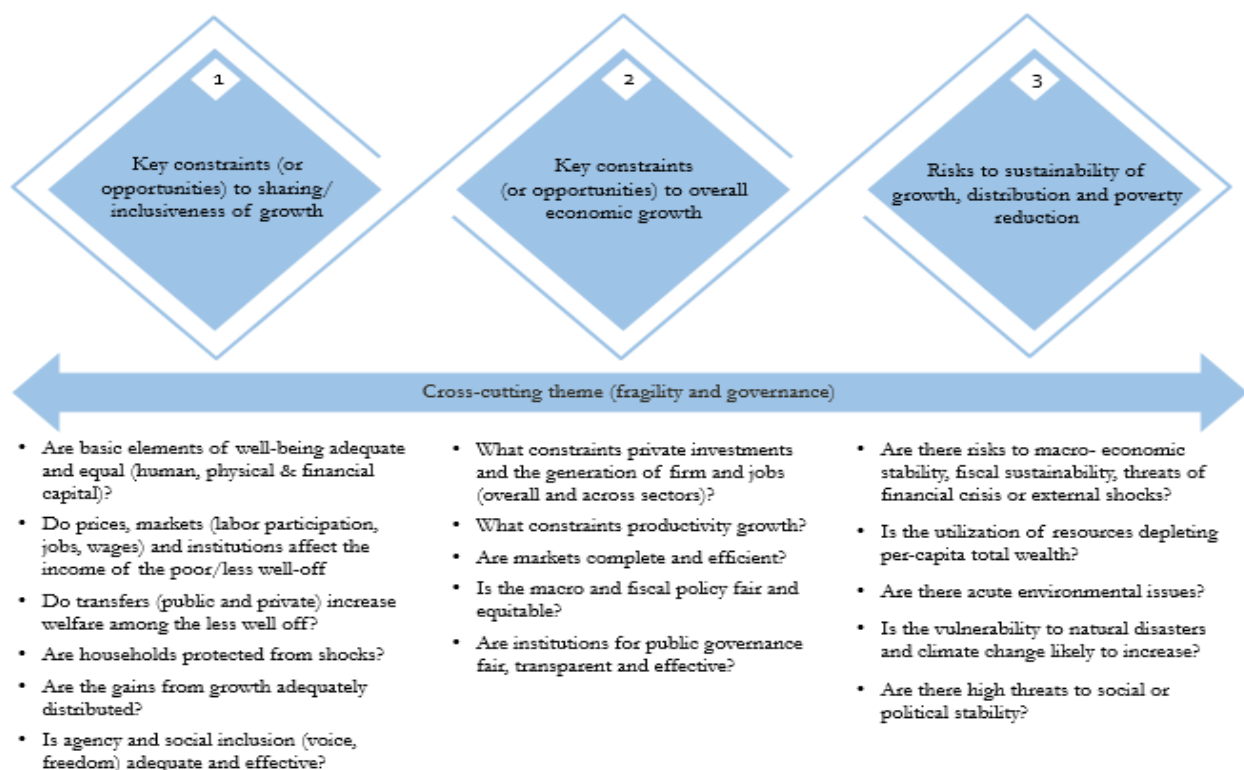
opportunities, through asset accumulation and utilization, for all members of the society to contribute to and benefit from economic growth; (2) robust and sustained economic growth and cross-cutting economic services, and fair, transparent, and efficient governance and economic institutions; and (3) economic, social, political and environmental risks for the sustainability of the process of growth, distribution and poverty reduction (Figure 1.2).

23. At the micro level, the inclusiveness of the economy is assessed by the assets households own, the intensity with which they are utilized, and their returns. The assets base is comprised of different forms of human, physical, natural, financial, and social capital. Intensity of factor usage is captured, for instance, by labor market participation (intensive and extensive margins, and formal and informal work shares) and by land utilization, among other uses. Returns can be measured by remuneration to labor factors or by returns in investments in human capital. Transfers (private and public) can complement household income. Risk management factors influence the household's ability (or inability) to hedge against losses due to shocks such as the variability of cashew prices, to climatic factors such as droughts or floods, or to idiosyncratic events, such as job losses or health shocks.⁸

24. At the macro level, raising household incomes requires an enabling economic and institutional environment. Core functions of the overarching macro and institutional environment include equitable and efficient fiscal policy, macro-stability, availability and quality of crosscutting economic services like finance, electricity, roads and telecommunications, a fair and transparent overall institutional environment, and well-functioning markets. This part of the framework allows for a systematic look at a number of interlinked economy-wide factors -- such as political instability, exogenous shocks, poor risk management and coping, a weak institutional, policy and regulatory environment, low private investment, imperfect markets, and a paucity of core public goods – which have a powerful bearing on households' incentives and ability to utilize productive assets.

⁸ This draws from the asset-based framework, previously presented in Attanasio and Székely (1999), Carter and Barrett (2006), and more recently Bussolo and Lopez-Calva (2014) as well as in the World Bank 'Risk Management Concept Note for Latin American and the Caribbean' (2015).

Figure 1.2. Diagnostics framework to assess opportunities for poverty reduction and shared growth



Source: World Bank, 2015.

25. The sustainability element examines whether the current economic, political, social and ecological systems and processes are dynamically sustainable in the medium- and long-term. This includes assessing what factors hinder the sustainability of policies to invest in more and better quality public goods and redistributive resources. It also looks at the factors that threaten political stability, such as rivalry and internal competition between politicians and the different arms of government, security sector reforms aimed to diminish the interference of the military in civil affairs, and unmet expectations from the civil society. Finally, sustaining and prudently managing the natural resource wealth is critical to ensuring environmental sustainability of the rich renewable and non-renewable natural capital base of the country.

26. Finally, as a cross-cutting theme, fragility and weak governance must be considered and addressed at each step of the development process in Guinea-Bissau. Inclusiveness, economic growth and sustainability factors will take place within the same Guinean context; one where fragility of institutions and weak governance may continue to erode improvements across the board and in any particular area. Historical hampering of economic growth due to political instability, concentration of rents at the top, and lack of transparency indicates that for the country to achieve significant and prolonged growth, it must address issues of national leadership tensions, rent-seeking, elite capture, military meddling, the culture of clientelism, transparency of national accounts, and increased fiscal responsibility and accountability, as well as achieving a stable transition of power between elected governments.

1.9 Scope and process

27. **The purpose of this SCD is to guide the WBG's future engagement in Guinea-Bissau by identifying key constraints and potential solutions to boosting growth, sustainably reducing poverty, and increasing shared prosperity.**⁹ In so doing, this SCD has drawn from available evidence, commissioned new analyses, including a joint World Bank-UN Fragility Assessment, and integrated country knowledge and expertise from across the WBG and other development partner institutions. The SCD also benefitted from in-country consultations (held in May 2015 and March 2016) with several stakeholders. The SCD was prepared in close collaboration with the entire Guinea-Bissau country team. It includes an in-depth discussion of the sources of growth, the drivers of poverty in Guinea-Bissau, and the constraints it faces in making growth inclusive and sustainable to improve the welfare of households, focusing especially on the most vulnerable population groups. Throughout the consultations, there was a broad consensus on the diagnosis of the challenges faced by Guinea-Bissau and on the priorities identified in this report.

28. **This SCD identifies three core interconnected areas of binding constraints.** These three core areas are: (1) lack of inclusiveness and low rural productivity; (2) low and unstable economic growth; and (3) fragility and weak governance. These constraints follow from the diagnostics framework in that they reflect the evidence that, under the current conditions, the gains from future growth will not be adequately shared due to the limited provision of public goods and opportunities and to the large barriers for households wanting to take up more profitable economic opportunities. Likewise, economic growth will likely continue to be low and volatile, and fragility and poor governance will undermine almost every economic, social, political environmental aspect of life in Guinea-Bissau. The SCD identifies priority policy areas and specific actions for each of the clusters of constraints for which a strong evidence base supports interventions in pursuit of the WBG's twin goals: reducing extreme poverty and promoting shared prosperity.

29. **While the main findings of the SCD are seemingly robust across the existing sources of quantitative and qualitative evidence, it is worth flagging key knowledge gaps that merit further research.** As expected for a diagnostic exercise that focuses on the development of a country as whole, the findings are often constrained by data limitations. This SCD has made an effort to go beyond the symptoms and identify the underlying constraints to faster and shared growth in Guinea-Bissau. However, economic, social, political, and environmental systems are intricately interconnected, making it a challenge to disentangle the root causes of development performance. Another important issue is the limited availability of quantitative data. When available, the data is sometimes outdated, patchy, or not fully reliable. The next poverty household survey is estimated to be finished by 2017. This will help to improve the quality of data and iterate the current picture of poverty in Guinea-Bissau. Other limitations hinge on qualitative data, which can be prone to limited external validity and subjective biases. This has left the following overall five critical areas that should guide further research and exploration:

A. In spite of the detailed account and research in this SCD, it is important to further understand how much of the poverty increase between 2002 and 2010 reflects cashew price trends versus

⁹ Reducing poverty means raising the proportion of the population living above a poverty threshold (for instance, US\$1.25 per day or less); boosting shared prosperity means raising the incomes of the poorest 40 percent of the population.

a structural shift in the ability of a large share of the population to generate income;

- B. The important interplay between risk management mechanisms and how they affect the production choices of rural households, especially the poor. This is to say how do households informal risk management influence their levels of welfare;
- C. This SCD offers many entry points for change. These include among other things the provision of services, better human capital, greater citizen engagement in the political process, expansion of agriculture and non-agricultural activities. Further analysis is needed to understand how much demand will follow an increase in supply and quality of these entry points for change.
- D. How can political constraints be sustainably addressed in Bissau? This means further understanding how to provide development support in the realistic context of potentially recurrent political instability and understanding how to maximize benefits while minimize risks of inconstant donor presence.
- E. Finally, the SCD makes an in-depth and meaningful attempt to identify ways to break the vicious cycle of elite capture, poor governance, weak social contract and fragility; nevertheless, further work should provide continuity to the exploration of these complex interlinkages, in particular looking for stronger causal links.

30. **In addition to the need for further research, capacities for statistic and analytical work in Guinea-Bissau need to be strengthened in areas of improved policy design and monitoring.** Timely high-quality macroeconomic and social data is key for evidence-based policy interventions across all sectors. On the macroeconomic front, consolidated fiscal data consistent with developments in the country is important for appropriately monitoring spending, especially in the context of the relatively low and volatile revenue flows. Frequent statistical surveys of social conditions will enable better analysis on poverty and growth, enabling the authorities to monitor progress and to appropriately adjust policy intervention. Improving existing monitoring and evaluation frameworks is necessary for promoting evidence-based and effective policy making. In this regard, investing in the national statistical system is critical.

31. **Following the structure of the diagnostics framework, the analysis of the SCD is organized into six chapters, one of which is devoted to the issue of fragility and weak governance, given its cross-cutting nature and relevance for the development of Guinea-Bissau.** After this introduction, Chapter 2 assess whether the minimum elements of well-being and personal opportunities are adequate and equal. Chapter 3 presents the growth patterns and the main factors driving and constraining economic growth in Guinea-Bissau. Chapter 4 zooms in on the political and institutional context of Guinea-Bissau to highlight the negative implications of fragility and weak governance for growth, poverty reduction, and shared prosperity. Chapter 5 discusses the main economic, fiscal, environmental, and political risks to boost and sustain inclusive growth in the medium and long term. Finally, Chapter 6 discusses the process and results of the prioritization analysis.

2 POVERTY, SHARED PROSPERITY AND EQUITY

- *As of 2010, 67.1 percent of Guineans are poor on the basis of the \$1.90/day (2011 PPP) poverty line. Poverty, especially the extreme poverty rate, increased between 2002 and 2010, and it is well above the average poverty rate of Sub-Saharan Africa. At 0.50, the Gini coefficient indicates that inequality in Guinea-Bissau is high, even in comparison to low-income country standards, and has worsened over time.*
- *Faster economic growth alone will not be enough to bring about poverty reduction in Guinea-Bissau. The modest economic growth recorded in the 2000s (assuming its distribution is neutral) would have reduced poverty. Yet, in reality, since growth happened only at the top, poverty increased by 3.7 percentage points. Assuming sustained political stability, the country has a chance to exploit both agricultural and non-agricultural sectors that can be pivotal in reducing extreme poverty and promoting shared prosperity.*
- *The assessment of the poverty, shared-prosperity and equity conditions reveals reinforcing mechanisms that lock most of the population in a persistent poverty trap. The low and unequal allocation of human and physical endowments (for instance, low school attainment, weak nutrition, a big burden of disease and low life expectancy) constraints the income generation capacity of households. Adults in the bottom 40 percent complete just two years of schooling, and their life expectancy is below the average for Sub-Saharan Africa. Weak nutrition and a big burden of disease among both adults and children limit the ability to escape poverty.*
- *Low access to basic services such as clean water, sanitation, and electricity, low access to primary-care in health and primary education, coupled with failures in critical markets (for example, credit and cashews), poor infrastructure, and natural resource depletion constrain economic opportunities, undermine asset utilization, and reduce asset returns. Poor infrastructure, in particular, renders potentially productive connections between markets more difficult. Certain groups, particularly women and the extreme poor, are disadvantaged in the allocation and utilization of resources. Each of these are areas urgently need interventions in order to unlock opportunities for Guinean households.*
- *Taken together, the low level of assets, the lack of an enabling context, and behavioral factors trap most households in cashew production, a stable yet low-investment, relatively low-risk and low-productivity subsistence equilibrium. In contrast, the rentier nature of the economy, the high concentration of the most important private and public rents, and a weak governance framework means that the better-off manage to benefit from modest but positive growth.*
- *Lack of inclusiveness and low rural productivity are each core areas of binding interconnected constraints for shared growth in Guinea-Bissau. Breaking the low equilibrium of welfare moving forward requires improving service delivery, enhancing market accessibility, reforming land tenure systems, improving agricultural technology and market support services, and reducing vulnerabilities of households to shocks. Yet, unlocking the underlying poverty trap is faced with challenges from systemically weak governance and institutional capacity, in spite of recent short-term advances in political stability.*

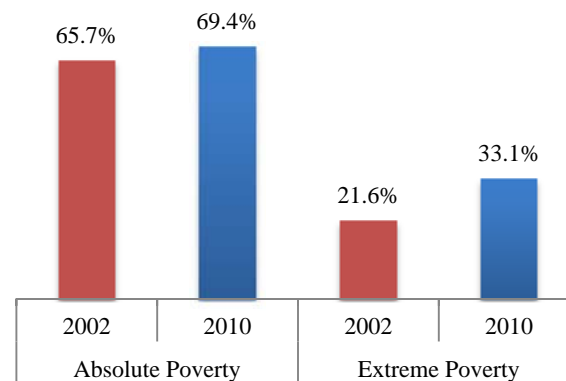
32. **The assessment of the poverty, shared-prosperity, and equity conditions for Guinea-Bissau carried out in Chapter 2 reveals several reinforcing mechanisms that cause poverty and underdevelopment to persist.** Most of the population, especially women, suffers from a paucity of endowments such as human capital, skills, and physical capital. Adults in the bottom 40 percent complete just two years of schooling on average. Their life expectancy is below the average for Sub-Saharan Africa, and households lack secure tenure rights. Weak nutrition and a big burden of disease among adults and children limit the ability of individuals to work at full capacity, and have lasting effects across generations. Low access to basic services such as clean water, sanitation, and electricity, coupled with failures in critical markets (for example, credit), poor public infrastructure, and pervasive fragility and natural resource depletion constrain economic opportunities and reduce returns to endowments differentially. Consequently, most households are stuck in cashew production, a stable yet low-investment, relatively low-risk and low-productivity subsistence equilibrium. In fact, nearly seven in ten individuals are below the poverty line, three in ten individuals are extremely poor, and more than half of the population are deemed chronically poor. In contrast, the better-off manage to benefit from modest but positive growth.

33. **Since growth alone will not be enough to bring about poverty reduction, breaking the low equilibrium of welfare moving forward requires improving service delivery and raising agricultural productivity to trigger a virtuous cycle of wealth accumulation at the household level.** As discussed in Chapters 3 and 4, conditions for more robust and diversified growth, political stability, and stronger governance are necessary but are not sufficient to create an enabling context for equitable growth and wealth accumulation. The increasing poverty trend in Guinea-Bissau is indicative that some kind of poverty trap is in operation. Most households are below a threshold that limits their ability to acquire enough wealth and to increase their future level of income and consumption. To improve the productive capacity of households, investments are needed in the delivery and reliability of basic services. Improving production practices in the cashew sector through extension services, increased access to enhanced inputs, and improved technology is expected to raise agricultural productivity in the most important economic activity of the country, which is the main employer of the poor, and potentially to generate opportunities for diversification in and outside of agriculture. The development of credit markets can also help to alleviate liquidity constraints which prevent these market managers from taking risks in the search of higher returns. Yet, unlocking the underlying poverty trap will be particularly challenging in the current context of fragility and limited institutional capacity.

2.1 Poverty in Guinea-Bissau is deep and entrenched

34. **Poverty in Guinea-Bissau is high and increased between 2002 and 2010.** Based on consumption data from the Poverty Evaluation Household Surveys (ILAP, *Inquérito Ligeiro para a Avaliação da Pobreza*, in Portuguese) conducted in 2002 and 2010, nearly 1.2 million people in 2010 (69.4 percent) are poor – that is, they live on less than \$2 per adult equivalent per day, which is the definition of the national poverty line. One third of the population (33.1 percent) lives in extreme poverty, surviving on under \$1 per adult equivalent per day (national extreme poverty line). Both absolute and extreme poverty rose between 2002 and 2010, the former by 3.7 percentage points and the latter by 11.5 percentage points (Figure 2.1).

Figure 2.1: Poverty in Guinea-Bissau is high and increased between 2002 and 2010

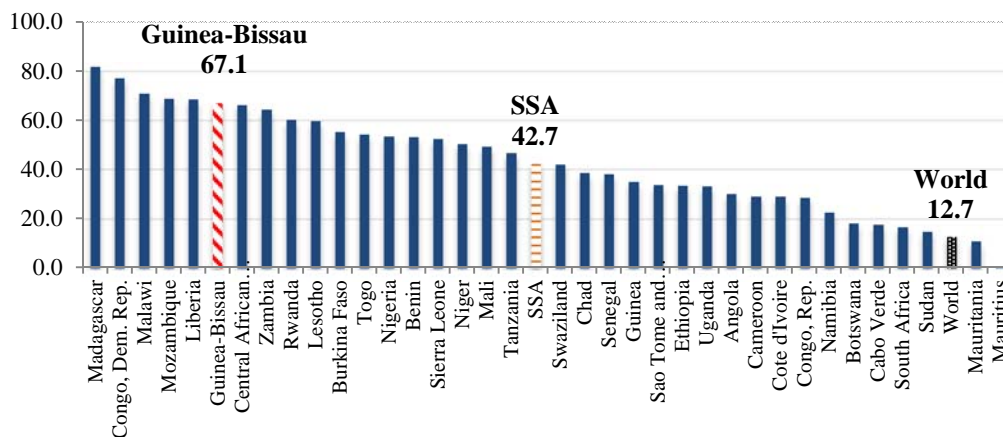


Note: National moderate poverty rate (US\$2 per day) and national extreme poverty rate (US\$1 per day)

Source: World Bank, 2015

35. **Poverty incidence in Guinea-Bissau measured using internationally comparable lines is equally high and lies above the average for Sub-Saharan Africa.** Extreme poverty, measured by the international line of US\$1.90/day (2011 PPP) was 67.1 percent in Guinea-Bissau in 2010 *versus* an average rate of 42.7 percent for Sub-Saharan Africa in 2012. Guinea-Bissau has a level of poverty only slightly lower than Liberia (68.6), one of its neighbors, but higher than most other neighboring countries in West Africa including Burkina Faso (55.3 percent), Togo (54.2 percent), Nigeria (53.5 percent), Benin (53.1 percent), Sierra Leone (52.3), Mali (49.3 percent), Senegal (38 percent), and Guinea (35.3 percent), as well as many other Sub-Saharan African countries (Figure 2.2).

Figure 2.2: Poverty rate in Guinea-Bissau is above the rate in Sub-Saharan Africa (percent)
Poverty at US\$1.90 (2011 PPP)



Source: World Bank with latest available data circa 2008-2012.

36. **Poverty in Guinea-Bissau is more prevalent in the rural areas, illustrating the connection between low growth, low agricultural productivity, and low inclusiveness.** The cumulative distribution function of consumption per capita shows that rural standards of living are considerably lower than those in the capital, Bissau, reflecting lower rural human capital and potentially lower agricultural productivity. As of 2010, the median consumption in rural Guinea-Bissau was US\$1.21 per capita per day, 38 percent less than in Bissau (US\$1.96 per capita per

day). As a result, poverty rates in 2010 were higher in rural Guinea-Bissau (75.6 percent) than in the capital (51.2 percent). Moreover, the difference in poverty between rural and urban areas widened over time (Figure 2.3). This has been accompanied by a similar shift over time toward employment in agriculture, further emphasizing the link between a sector plagued by low productivity and higher poverty rates. The higher levels of poverty seen outside of Bissau are further compounded by multiple deprivations in non-monetary dimensions, such as access to basic and social services, human capital, and levels of public infrastructure (explored further below).

37. **In some parts of the country, four out of every five households are poor.** The country is administratively divided into eight regions plus the capital city, Bissau. Poverty rates disaggregated at this level show substantial variation. In some geographical areas of the country, almost everyone is poor. Gabu and Cacheu –northern regions bordering Senegal– have the highest poverty rates (83.5 and 80.5 percent, respectively), whereas Bolama/Bijagos and Bissau have the lowest (47.2 and 51.2 percent, respectively) (Figure 2.4). The eight regions are themselves divided into 39 districts, 22 of which (all rural) have poverty rates (obtained from poverty mapping techniques) above 80 percent. There is also considerable spatial concentration of poverty among sectors within regions – for instance, within the Gabu region, the poverty headcount range from 90.2 percent in the Sonaco sector to 57.9 percent in the Boe sector. The concentration of extreme poor households (that is below the \$1/day national line) is higher in rural areas, particularly in the regions of Gabu (47.2 percent), Oio (45.6 percent), Cacheu (42.8 percent), and Quinara (41.1 percent). In contrast, at 13.2 percent, extreme poverty is substantially lower in Bissau.

38. **While in general all the poor in Guinea-Bissau experience multiple deprivations, the extreme poor are further disadvantaged when compared even with the moderate poor.** Household size among the extreme poor is substantially larger—on average over two more members. Part of this is driven by a higher number of children (that is, on average one additional child), increasing the dependency ratios (Table 2.1). School attainment—proxied by literacy rates and primary education for the head of household—is also lower. The extreme poor also have fewer household assets. Compared to the rest of the poor, their incomes are not only lower but are also less diversified with nearly 90 percent of the extreme poor employed in agriculture. When it comes to connectivity, the extreme poor are significantly more disadvantaged. On average they are more commonly far from markets and schools and lacking access to electricity. General access to services, already low for the population in general, is even more critical for the extreme poor, with nearly half lacking safe drinking water and four-fifths lacking sanitation. This is a further challenge to reducing poverty in Guinea-Bissau, and addressing the problems of the extreme poor.

Table 2.1. The extreme poor have further deprivations when compared with the moderate poor

Variable	Poor	Extreme Poor
Demographics		
Household size	11.2	13.3
Number of kids (total)	4.9	6
Number of kids (0-5)	2.2	2.8
Number of kids (6-14)	2.7	3.2
Age household head	50	53
Head lacks primary schooling	77%	86%
Literacy of household head	50%	36%
Assets		
Asset-based poor	91%	96%
Poor housing (Thatch Roof)	25%	40%
Has TV	19%	10%
Has bed	95%	91%
Has motorbike	11%	7%
Access to Services		
Lack drinking water	36%	43%
Child is out of school	54%	69%
Lack of sanitation	66%	78%
Lack of electricity	95%	97%
Far from market (60+ minutes on foot)	26%	41%
Far from school (60+ minutes on foot)	14%	20%
Economic Activities		
Agriculture	73.70%	90.10%
Industry	4.20%	2.30%
Services	22.10%	7.70%
Salaried Work	22.90%	11.40%

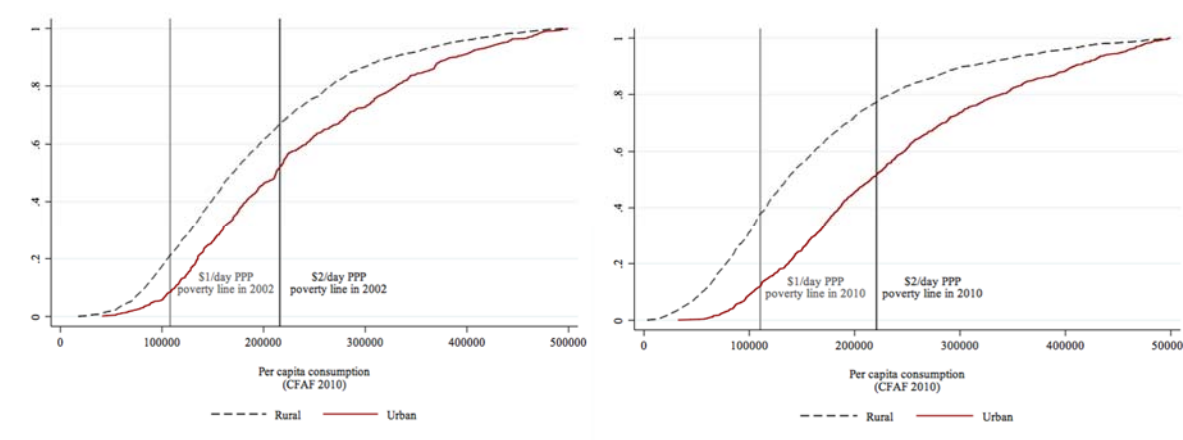
* All results significant at 90 percent confidence level.

Source: World Bank staff calculations using ILAP 2010.

39. **In spite of modest improvement between 2002 and 2010, low and unequal access to key basic and social services—especially in human capital—suggests that non-monetary poverty remains high holding back potential productivity gains and other economic opportunities.** Monetary measures alone cannot capture the various dimensions of household welfare or the deprivations suffered by individuals or households. Income and consumption challenges that poor people face are often related to factors such as access to vital services, as well as their ability to build human capital, one of several main pillars of higher productivity. An analysis of seven indicators – school attainment of the household head, children’s school attendance, housing quality (proxied by roofing material), household assets, and access to electricity, clean water, and sanitation services, based on ILAP data, shows that more than 87 percent of the population live with deprivations in at least three of the seven indicators, and over 70 percent with regard to four of the indicators (Figure 2.5). Furthermore, for one-third of the population (the extreme poor), these deprivations are even more profound (Table 2.1). Between

2002 and 2010 small gains were made in access to sanitation, water, and housing infrastructure, but little progress was achieved in the other dimensions.

Figure 2.3: Household per capita consumption has been systematically lower in rural areas
2002 2010



Source: World Bank staff calculations using ILAP 2002 and ILAP 2010 data.

Figure 2.4: Poverty rates for most rural regions national average

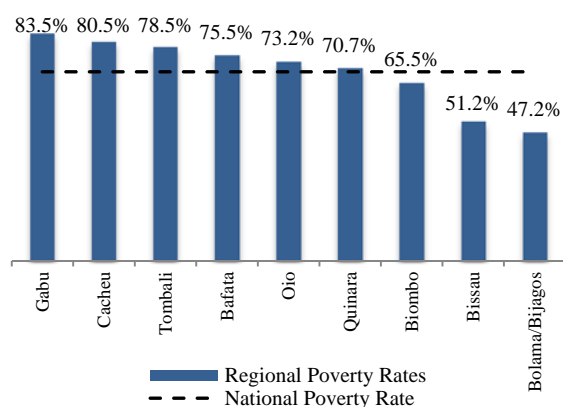
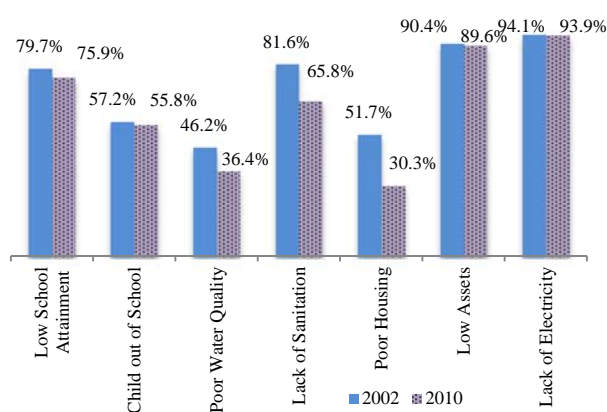


Figure 2.5: Despite moderate above are the improvements, the sendowment base for Guineans remains low

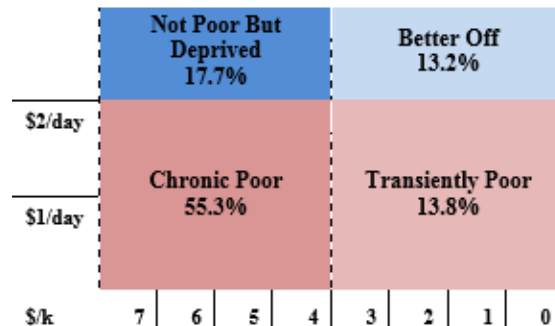


Source: World Bank staff calculations using ILAP 2010 data.

40. **Two-thirds of the population are poor in the monetary sense and over half in the non-monetary sense, pointing possibly to the existence of major poverty traps.** In the absence of longitudinal data, the intersection of non-monetary and monetary poverty allows for a proxy assessment of the temporality of poverty. In general terms, households living below the \$2/day national poverty line and experiencing, for instance, four or more non-monetary deprivations, are more likely to be exposed to long spells of poverty, this is, chronically poor. Under this rationale, 55 percent of the country's population (including the majority of the extreme poor) face the greatest challenges in moving out of poverty due both to low incomes as well as to severely-constrained human capital, access to services, and household assets. Only a small

share of the population (13 percent) can be considered non-poor in monetary or non-monetary terms (Figure 2.6).

Figure 2.6: Proxying chronic and transient poverty in Guinea-Bissau (2010)

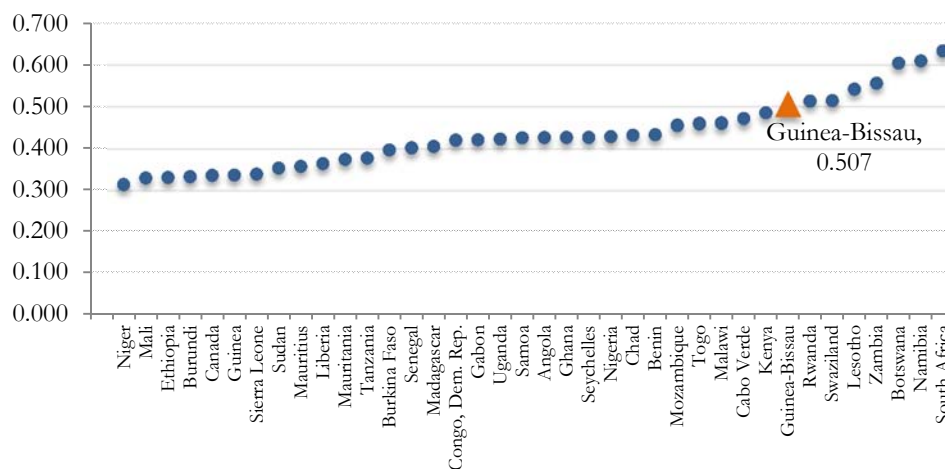


Source: World Bank staff calculations using ILAP 2010. A household is deemed multidimensional poor if k (the total number of deprivations) is greater or equal to four.

2.2 Inequality is particularly high and the poor are not able to capitalize on growth

41. **In addition to widespread poverty, inequality in Guinea-Bissau is also high, even in comparison to African and overall low-income country standards, and has worsened over time.** The increase in inequality in Guinea-Bissau is partly symptomatic of the rentier economy, which favors the long-standing business and political elites in the country. The Gini coefficient for Guinea-Bissau was 0.50 in 2010, which places it among the countries in the region with the highest levels of inequality (Figure 2.7). Inequality can also be measured through the ratio of consumption levels at two different points of the distribution. Expenditures for the top quartile is nine times higher than that of the bottom quartile. Similarly, average consumption at the top ten percent is 23 times higher than consumption at the bottom ten percent, and eleven times higher than the average consumption of the bottom 40. Inequality has worsened since 2002, when the Gini coefficient was 0.35.

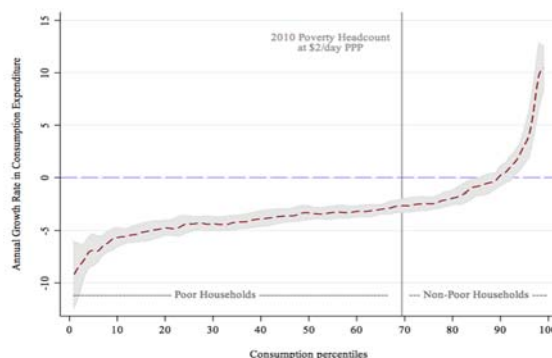
Figure 2.7: Gini coefficients across countries in Africa (circa 2008-2012)



Source: PovCalNet, World Bank. Gini coefficient for Guinea-Bissau calculated using ILAP 2010 data.

42. **A decomposition of poverty into growth and redistribution factors shows that while growth alone could have been sufficient to contribute to some poverty reduction, it did not, in fact, benefit the poor.** Rather, the observed increase in consumption inequality more than offset the potential poverty reduction effect of growth. Keeping the baseline income distribution constant, growth contributed to a decrease in poverty rates of approximately 8.2 percentage points. However, since growth happened at the top, the redistribution effect contributed to an increase in the poverty rate of about 11.9 percentage points. The net effect was an increase in poverty by 3.7 percentage points.
43. **Without strong human capital and access to services, the poor are unable to reach higher incomes. Overall, the trend between 2002 and 2010 was one of growth at the top and declining welfare for the rest of the population, which can explain the increase in poverty.** Growth incidence curves (GIC) plot the growth rate of a welfare measure (for instance, consumption or income) between two points in time for each percentile of the baseline distribution. GICs can be used to assess how the gains of economic growth (or the losses of economic stagnation) are distributed across the population. A GIC for Guinea-Bissau for the period 2002-2010 shows that positive consumption per capita growth was experienced only by the top 10 percent of the distribution (Figure 2.8). The rest of the distribution saw negative consumption growth, consistent with the increase in poverty recorded during this interval of time. Furthermore, the rate at which consumption falls per capita increases systematically as one moves from the top to the bottom of the distribution. Consequently, the poorest of poor fared worse than the rest of the population with their consumption falling between 5 and 10 percent. The breakdown by occupations corroborates the overall trend of wealth accumulation at the top consumption deciles, particularly for those in management positions (that is, public and private sector).

Figure 2.8: Consumption growth was experienced by households in the top of the distribution

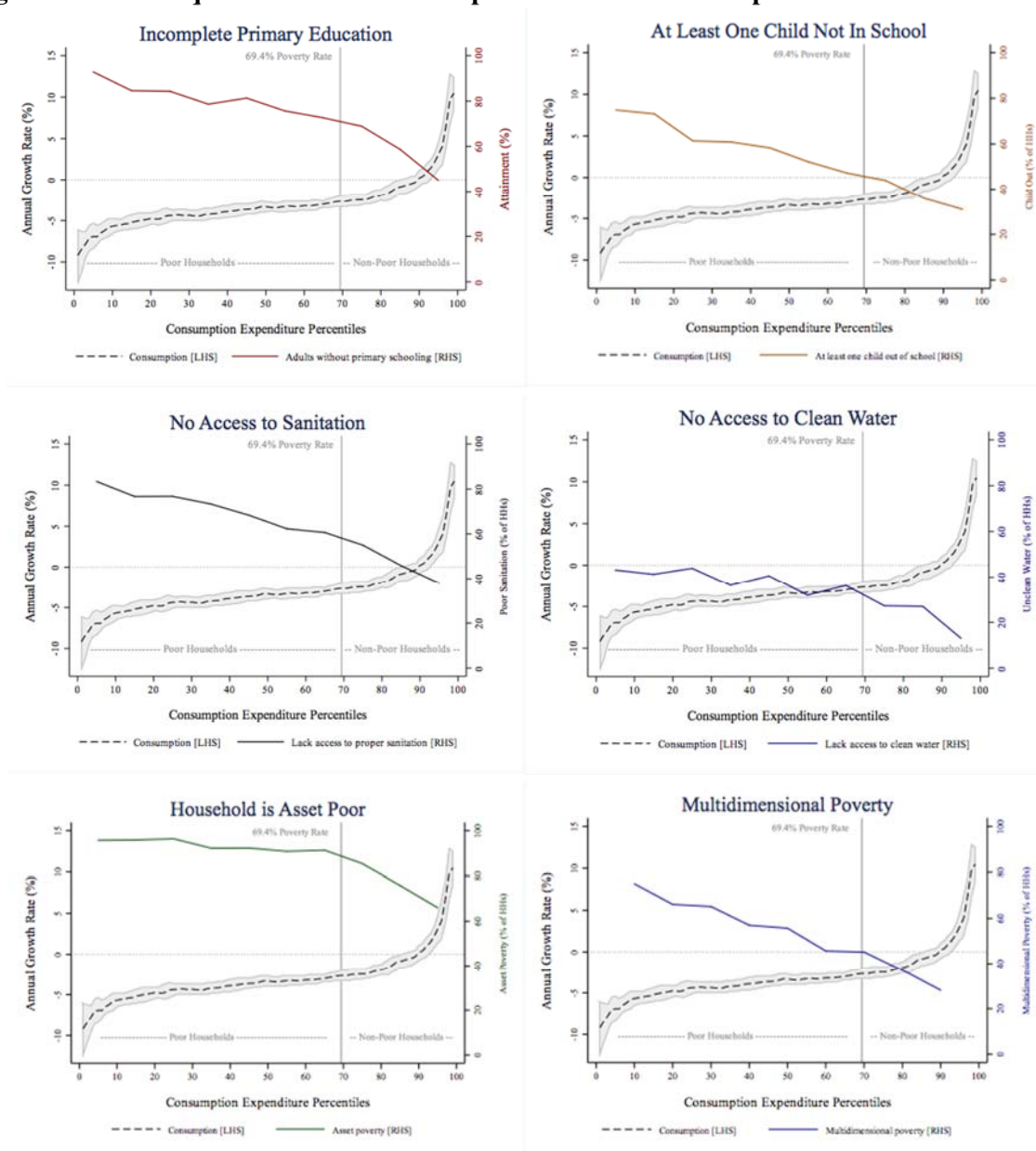


Source: World Bank staff calculations using ILAP 2002 and ILAP 2010 data.

44. **While a drop in cashew prices could partly explain the increase in poverty, the uneven allocation of endowments and economic opportunities structurally limits the inclusiveness of economic growth in Guinea-Bissau.** The increase in poverty between 2002 and 2010 may be associated with the fact that real cashew prices fell over the same period. Yet, the fact that some groups of people saw their consumption levels increase over the same period, and that this positive consumption growth was experienced solely by households at the top of the distribution, (which also derives part of their incomes from cashew) is indicative that structural inequality in opportunities constrain the inclusiveness of the economy. This emphasizes the focus on improving

returns for the poor, who are more prevalent in rural areas and more likely to earn a living from agriculture. The asset profile illustrates how households from the bottom 90 percent of the consumption distribution in 2002 had less ownership of, and access to, assets and services (schooling, sanitation, water, and so forth) that are central to seize opportunities for income growth. The pattern of deprivation is even more pronounced among the extreme poor for all the dimensions analyzed (Figure 2.9).

Figure 2.9: Lower quintiles are the most deprived in asset ownership and access to basic services



Note: Household is considered 'asset poor' if it does not have two of the following three items: clean-burning stove, refrigerator, or a radio. Household is considered 'Multidimensional Poor' if it is deprived in at least five of the following seven indicators: primary school attainment, school attendance for school-age children, basic sanitation, clean water, asset-wealth, non-thatch roofing, and access to electricity. *Source:* World Bank staff calculations using ILAP 2002 and ILAP 2010 data.

45. **The ability of the elites to widely dominate the few markets that exist in Guinea-Bissau is exemplified through the presence of much higher returns to assets among the better off, a major contributor to the skewed nature of consumption growth in Guinea-Bissau.** Using the Firpo et al (2007) framework to decompose the growth incidence curve into composition of endowments and returns to endowments shows that differences in household welfare are largely driven by the latter (Annex 2A). This is to say that non-poor households are better off due to having higher returns to the endowments they have, rather than the bigger stock of endowments itself, explaining the overall shape of the growth incidence curve. More specifically, the non-poor are able to derive higher returns to the allocation of assets, including education, work experience, other household assets, and to their work in agriculture. Returns to the accessibility to markets are more important to the poor, meaning that in a context of an unleveled playing field, ease of access to markets is an important channel for the poor to trade goods and ultimately increase their consumption. The composition effect (from how endowed a household is) is much less pronounced, and is driven upwards by the distribution of a household's asset-base¹⁰ and downwards by its distribution of demographics, especially the fact that poorer households are larger. As shown in Table 2.1, the poor and extreme poor are also less likely to work in non-agricultural sectors, which command higher returns.

46. **In what follows, the SCD documents in more detail the constraints that the population faces to raise their standards of living based on an exhaustive assessment of three major elements: (1) assets ownership; (2) intensity in which assets are utilized; and (3) returns earned on the factors of production.** This analytical framework is useful for understanding the micro-level factors underpinning the low levels of welfare across the country and across groups (especially women relative to men). The household *asset base* may be comprised of demographic endowments (the proportion of young and productive members of the household, implying a demographic dividend), human capital, natural capital, social capital, and financial capital. *Intensity of usage* is captured through labor market participation, its intensive and extensive margins, formal and informal work shares, and land use, among other uses elaborated below. Finally, *returns* are examined by the wages for labor factors. The assessment ends with a discussion of the extent to which private transfers¹¹ complement household income and the vulnerability of households to systemic and idiosyncratic shocks.

2.3 The productive capacity of households is undermined by low human and physical capital, and an inefficient use of natural resources

Human capital

47. **Low educational achievement, largely the result of a weak and inefficient education system, poses a major obstacle to improving labor productivity and generating income for the population.** While official statistics indicate that school attendance has improved over the past several years, Guinea-Bissau continues to have some of the lowest education results in the region. Primary net enrollment increased from 45 percent in 2000 to 67 percent in 2010. However, primary completion is low. A 2010 education sector analysis completed by the World Bank and

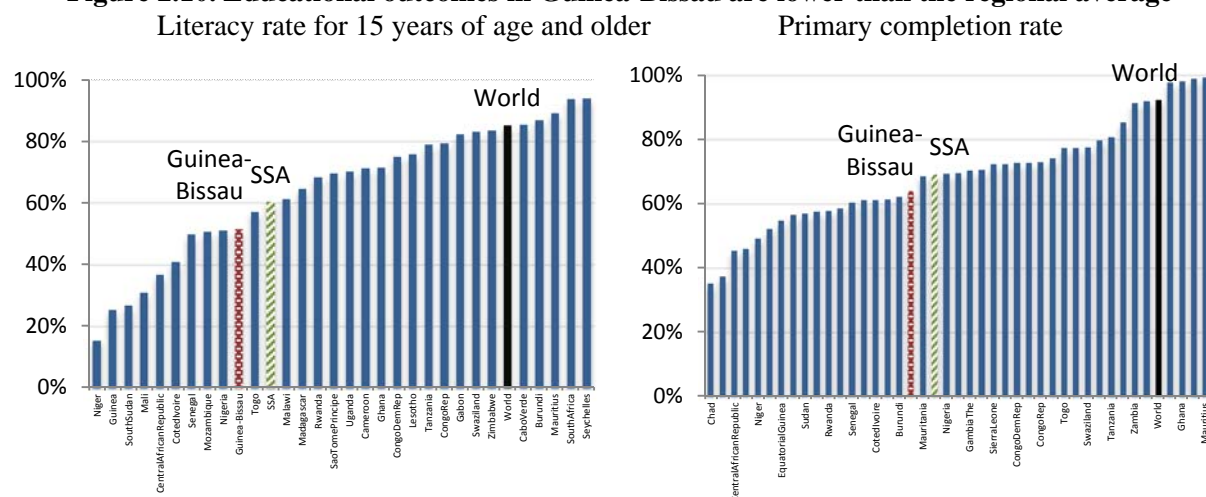
¹⁰ The asset-base is composed by education, experience and household assets (e.g. electricity, good roofing, and land ownership).

¹¹ While the standard assets-based model treats private transfers as independent of household income-earning assets, they—particularly international remittances—may be correlated with access to markets and the probability of households to migrate, factors themselves that determine the level of income of the population.

Pôle de Dakar found that out of 100 children starting the first year of primary, only 72 continued into the second year, and only 38 arrived at the sixth year. Overall, 64 percent of children complete primary education compared to 69 percent in Sub-Saharan Africa and 92 percent worldwide. At 51 percent, the literacy rate is also lower than the regional average of 60 percent (Figure 2.10). Inequities are found to remain between genders (Figure 2.11), rural/urban locations, and socioeconomic levels.

48. **While there is relative parity between girls and boys in enrollment at the primary school level, there is still a large gender gap at the secondary level.** The ratio of female to male enrollment is lower than for every West African neighbor, except Togo. Evidence suggests that pregnancy (17 percent) and early marriage (17.2 percent) are the most common reasons for girls to drop out of secondary school, while work is the most common reason for boys (38.6 percent) (Government of Bissau, 2012). Among women aged 20-49 years, 37 percent were married before the age of 18, and 7 percent were married before 15, according to the 2014 Multiple Indicator Cluster Survey (MICS). Early marriage is effectively promoted indirectly via a law, which sets the legal age at just 14 years for girls, compared to 16 for boys, and the international standard of 18 (AfDB, 2014). Lack of proper sanitary facilities and long distances to school are thought to be critical barriers to educational participation, especially for girls. Only 6 percent of secondary school teachers are females.

Figure 2.10. Educational outcomes in Guinea-Bissau are lower than the regional average

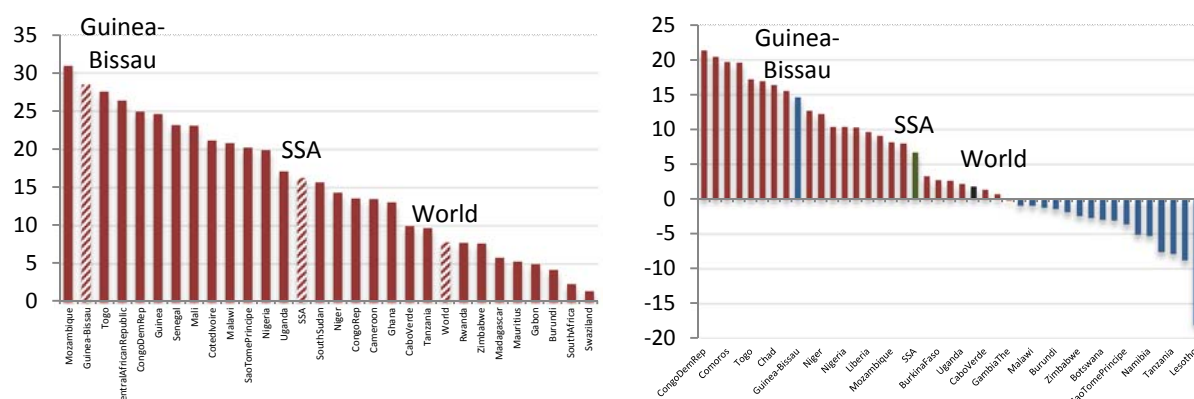


Source: World Development Indicators (2008-2012) and ILAP 2010 for Guinea-Bissau

Figure 2.11. Gender inequities in educational outcomes are greater than regional average

Literacy rate for 15 years of age and older
(Gender gap, p.p. men relative to women)

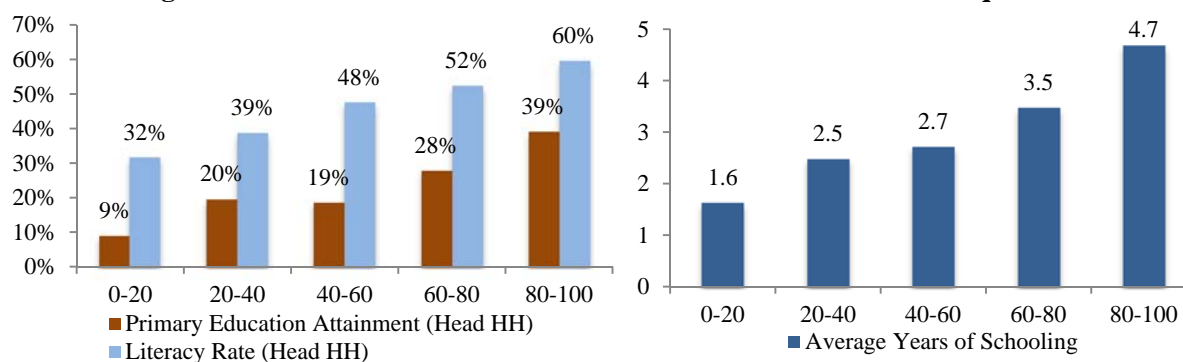
Primary completion rate
(Gender gap, p.p. boys relative to girls)



Source: World Development Indicators (2008-2012) and ILAP 2010 for Guinea-Bissau

49. **Low educational achievement more systematically affects the extreme poor, highlighting the deficient human capital causing lower returns for this group.** Data from ILAP shows that adults in the bottom 40 percent completed just two years of schooling on average, but that even for the top quintile, school attainment does not exceed five years (Figure 2.12). Overall, three-quarters of Guinean household heads had not completed primary education. Literacy rates were also lower among the extreme poor. Less than one-third of adults (aged 15 years and over) in the lowest consumption quintile reported an ability to read and write. Here again, there are significant differences by gender, with female educational achievement lagging significantly behind that of their male counterparts. Parental education is generally associated with better educational outcomes for children, and in Guinea-Bissau nearly 70 percent of households whose heads are illiterate have at least one school-aged child out of school, compared to about 40 percent for children of parents who are literate.

Figure 2.12: Education outcomes are weaker for the lowest income quintiles



Source: World Bank staff calculations based on ILAP 2010

50. **Substantial improvements in coverage, quality and institutional strengthening are needed in the education sector.** Recent tests of mathematics and Portuguese based on a 2014 evaluation reveal very low achievement levels. Less than 40 percent of teachers at the primary level are trained, many of whom are often appointed based on clientelist rather than education

sector objectives. High internal inefficiency has significant costs, with 47 percent of allocated resources wasted due to repetition and dropouts (Pole de Dakar, 2015). While achievement is low, access to schooling is also constrained, with only a quarter of schools offering all six primary grades. It is necessary to improve staffing, management, and training policies in the sector as well as to set mechanisms to control the hiring of teachers and ensure the sustainability of the cadre of teachers. Similarly, the lack of rules to address issues of absenteeism of teachers and children is a problem.

51. Health outcomes are equally poor, limiting the ability of individuals to work, and undermining their productivity. The poor general health of the population is encapsulated in the low average life expectancy in Guinea-Bissau: 54 years at birth, compared with sub-Saharan and world averages of 56 years and 71 years respectively. Poor health outcomes are closely related to the inadequacy of safe water and sanitation services. Even though indicators of access to clean water and sanitation show a modest improvement, more than a third of the population (36.4 percent) still lack access to safe water for drinking and bathing, and close to two-thirds have no access to modern sanitation (Figure 2.13, Panel a). Morbidity in adults is most commonly associated with lower respiratory tract infection, HIV/AIDS and malaria. Morbidity patterns, especially those associated with malaria, have serious implications for labor productivity and people's capacity to work over extended periods. In the 2010 ILAP, 78 percent of respondents (most of them poor) reported that they had missed at least one day of work due to illness during the four weeks before the survey was taken.

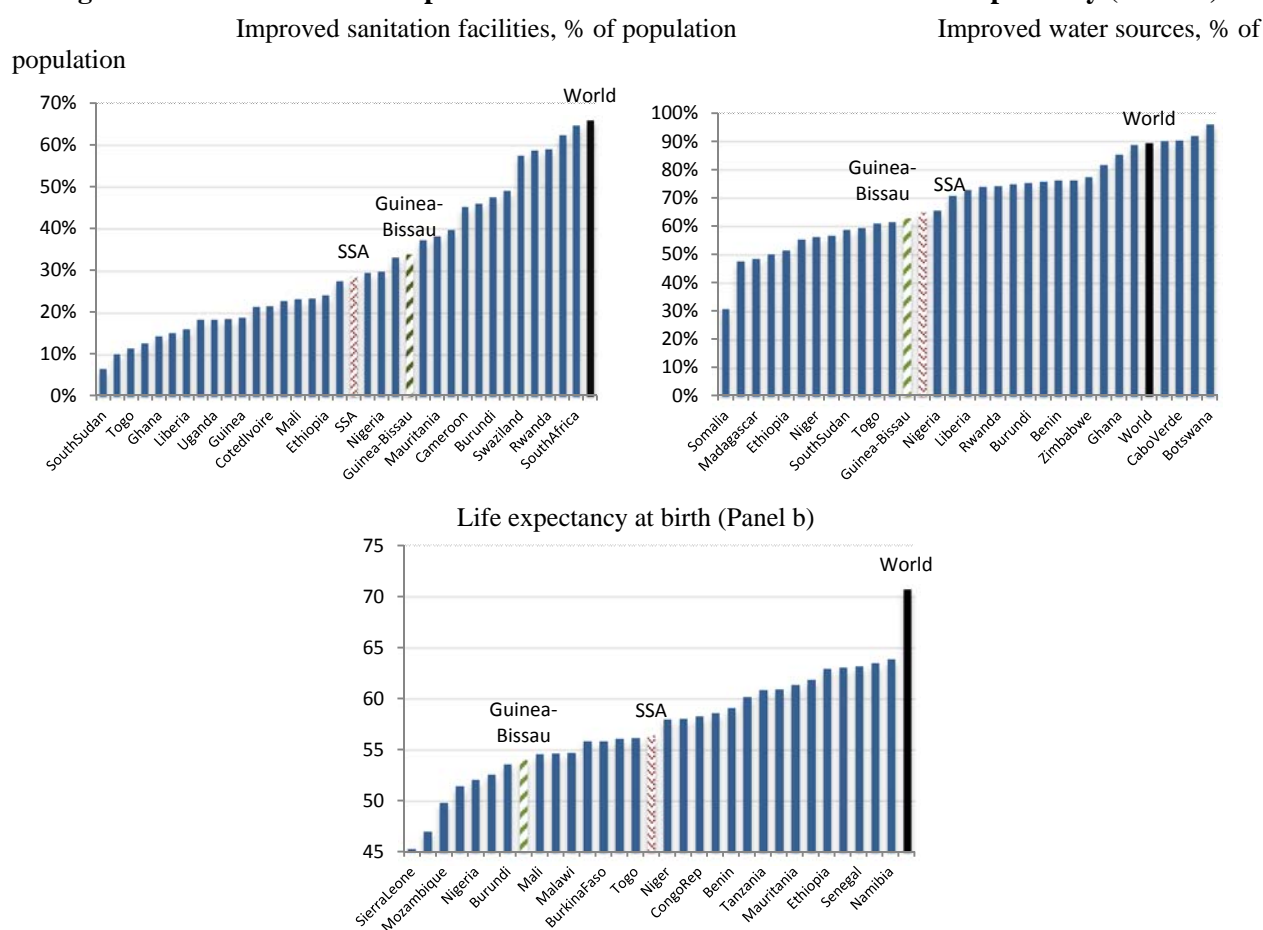
52. Health outcomes are particularly weak for women. The maternal mortality rate in Guinea-Bissau is one of the highest rates in all of Africa and appears to have increased since 2004. The latest national estimate suggests that there were 560 deaths per 100,000 live births in 2013 World Development Indicator (WDI), which made Guinea-Bissau the 13th highest in the world (WDI, 2013), well above the global rate (210) and higher than the level in Sub-Saharan Africa (510)¹² (Figure 2.13, Panel b). This means that among West African neighbors only Sierra Leone and Liberia have lower rates. Moreover, this figure is above the rate of 400 estimated in 2004, suggesting that maternal mortality has been on the rise. While coverage of pre-natal care is high at 93 percent, the high levels of maternal mortality indicate that the quality of care is low. Additionally, at just 43 percent, the proportion of births that are attended by a skilled health professional (one of the most important interventions for reducing maternal mortality) is lower than that of almost every West African neighbor. Fertility rates are also high, partly due to the low prevalence of contraception (14 percent among women ages 15-49), although that is rising slowly and is higher among the younger generation. However, it is not clear whether supply or demand factors drive the low use of contraceptives (see Box 2.1 on the practice of female genital mutilation).

53. Child health deprivations and food insecurity in Guinea-Bissau are high on regional and global scales. At 78 per 1,000 live births, infant mortality is 30 percent higher than the sub-Saharan average and more than double the world average. While under-five mortality has fallen over time (from 225 in 1990 to 88.8 per 1,000 live births in 2014), it is twice the global average (44 per 1,000 live births) (MICS5, 2015) (Figure 2.15). Almost two thirds of households in the bottom 40 percent experience frequent hunger, revealing a largely food insecure population.

¹² Mortality rates from MICS data for Guinea-Bissau show an increasing trend going from 349 in 2000, to 405 in 2005, to 900 in 2014.

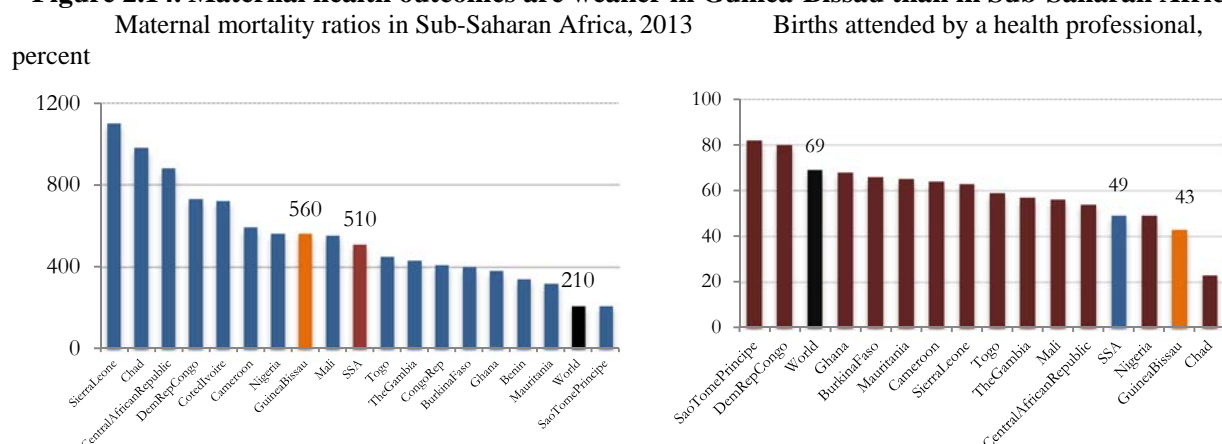
Nearly one-quarter of Guineans of all ages are undernourished, whereas almost one-third of children under five suffer from stunting (an indicator of chronic malnutrition) and one-fifth suffer from wasting (acute malnutrition, usually associated with illness). The high prevalence of undernourished children is further compounded by high rates of morbidity. According to ILAPII-2010, over 12 percent of children ages 0 to 5 years old (mostly from extreme poor households) were reported to be sick with diarrhea or malaria in the four weeks before the survey. The underinvestment in the human capital of children, largely driven by weak, under-budgeted, and inefficient education and health sectors, weakens the already difficult process of development in Guinea-Bissau by limiting their current and future productivity and contributing to the perpetuation of poverty across generations.

Figure 2.13. Poor access to improved water and sanitation and lower life expectancy (Panel a)



Source: World Development Indicators (circa 2008-2012).

Figure 2.14. Maternal health outcomes are weaker in Guinea-Bissau than in Sub-Saharan Africa



Source: World Development Indicators, MDGs 2013, and MICS (circa 2008-2012).

Box 2.1. Female Genital Mutilation and HIV in Guinea-Bissau

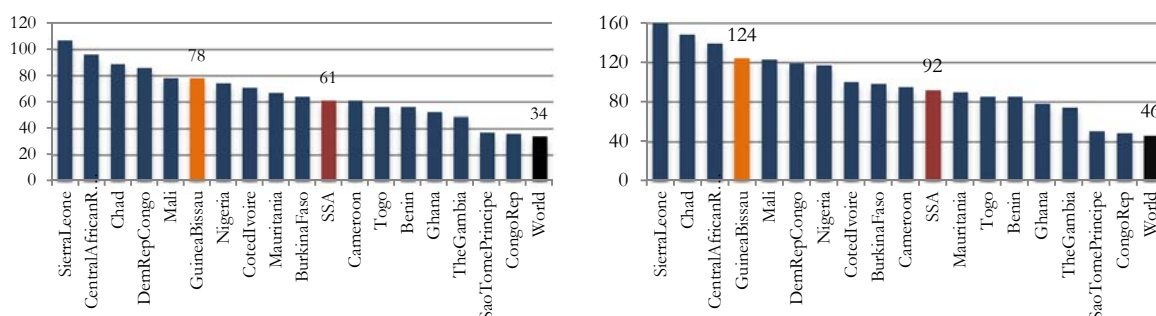
The practice of Female Genital Mutilation (FGM) is quite prevalent in Guinea-Bissau. Data from MICS5 (2014) suggest that 44.9 percent of women (aged 15-49 years) in the country have been subjected to FGM, though data from previous years suggests this could be as high as 95 percent for women of the two major Muslim ethnic groups (World Bank, 2009b). Data from the last MICS survey suggest that the practice is common across all wealth quintiles, but is less prevalent among women who have had some education (28 percent) than those who have had no education (65 percent). The parliament passed legislation against FGM in June 2011 (UN, 2011b). Given the importance of customary and religious law in Guinea-Bissau, it is encouraging that these formal efforts were backed up by the Guinea-Bissau National Islamic Council (African Development Bank (AfDB), 2014). On the ground, Muslim and Christian leaders have also worked to spread the message that FGM is not justified by religion and is harmful (AfDB, 2014). However, there are indications that these efforts have not been sufficient to have any real impact. In the region of Gabu, where FGM is universal, not a single case has been heard by the Regional Tribunal since the law was passed (AfDB, 2014). However, results from the latest MICS5 data suggest that FGM may be becoming less socially acceptable, with the share of women who stated that they think FGM should continue declining to just 13 percent, compared to 34 percent in MICS4.

The prevalence of HIV is higher than that found in neighboring countries, and women are more likely to contract it. In Guinea-Bissau, 3.7 percent of the population aged 15-49 are infected, compared to 1.7 percent in Guinea and 0.5 percent in Senegal. As in many countries, women make up a majority of those infected (59 percent). Moreover, prevalence is 1.9 times higher among young women than among young men (ages 15-24). The high rates of FGM may increase the chance of women becoming infected with HIV/AIDS.

54. **The incidence and mortality of malaria have gone down over the years, but the rate of malaria-related deaths remains relatively high.** The incidence of malaria is comparable to the levels recorded in Sub-Saharan Africa. This is positive for children because 78 percent of all malaria related deaths in Africa affect children under the age of five. Guinea-Bissau has one of the highest rates of coverage of children with a fever receiving anti-malarial treatment (Figure 2.16). Nevertheless, treatment still reaches only half of all children suspected of having malaria. Out of 47 African nations, Guinea-Bissau ranked 20th in the number of confirmed malaria cases, but 9th in number of malaria-related deaths per capita. This situation reported in 2014 is an improvement from the 2012 number of confirmed malaria-related cases and deaths by a decrease

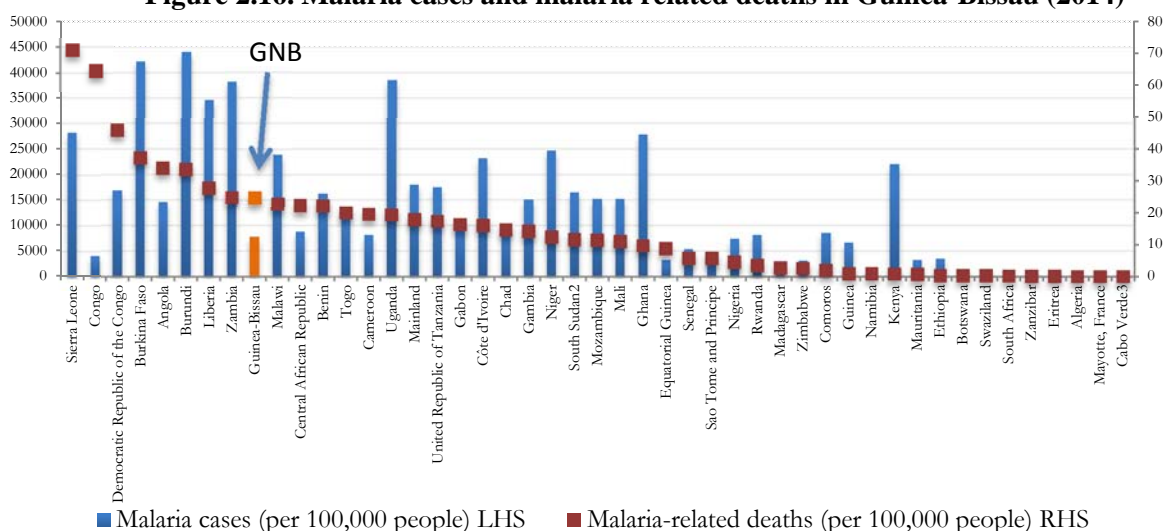
of roughly two-thirds. Overall, however, the country lacks robust health information systems, including disease surveillance capacity for early detection and response to disease outbreaks.

Figure 2.15. Child mortality is high even by regional standards
(Infant mortality rate, per 1,000 live births) (Mortality rate under five, per 1,000 live births)



Source: World Development Indicators, MDGs 2013, and MICS (circa 2008-2012).

Figure 2.16. Malaria cases and malaria related deaths in Guinea-Bissau (2014)



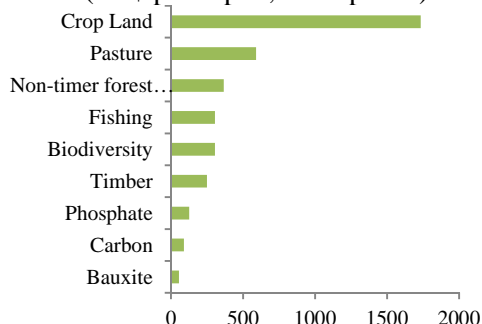
Source: World Malaria Report 2014, World Health Organization (WHO).

Natural resources and physical assets

55. **Aside from labor, the productive asset that is most available to Guinean households is land, to which they generally possess usufruct (rather than ownership) rights, in accordance with customary practices.** As noted in the January 2015 Guinea-Bissau CEM, wealth accounting methodologies suggest total natural wealth in Guinea-Bissau could be up to US\$3,874 per capita (Figure 2-17 and Figure 2-18). This natural resource base provides a multitude of goods and services, contributing directly to household incomes. As part of an effort to protect access to the country's natural wealth by the population, a statute was passed in 1975 prohibiting private ownership of land. The statute rules out freehold property rights for individuals, groups, businesses, and institutions, and underlines the responsibility of the state in safeguarding land resources as the mainstay of people's livelihoods. While this law is aimed at protecting the rights

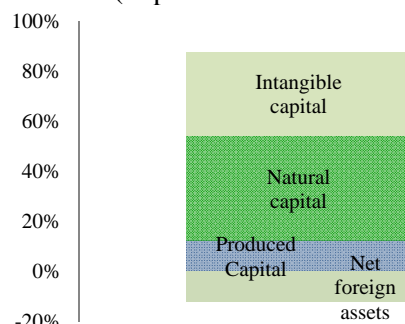
of the poor, it may have counter-productive effects by hampering potential benefits associated with land holding and title holding by households. In the context of the cashew economy, such benefits may include the ability to make longer-term and more diversified investments that do not chiefly hinge on keeping the land ‘busy’ with cashew trees (as further discussed below).

Figure 2-17: Guinea-Bissau has considerable renewable and non-renewable resources
(US\$ per capita, 2010 prices)



Source: Optimizing Guinea-Bissau’s Natural Wealth, 2014.

Figure 2-18: Resources accounting for the largest share of the country’s total wealth
(in percent of total wealth, 2010)



Source: Optimizing Guinea-Bissau’s Natural Wealth, 2014.

56. **Allocation of land and other renewable natural resources is largely determined by the diverse traditional customs of Guinea-Bissau’s twenty or more different ethnic groups.** Traditional land tenure systems vary by region, ethnicity, and the type of agricultural activity being pursued. Both customary practices and national laws generally protect the usufruct rights of individuals and households, although differences in traditional norms and modern land policies generate ambiguities. Inheritance norms, for example, vary significantly across ethnic groups, with some groups allowing inheritance by direct descendants (sons), while others require that use rights pass to nephews or other male relatives – dampening incentives to invest in land improvements. Land is exclusively administered by the male head of household/family clan, known as the *chefe de tabanca* or *regulado*. This makes women extremely vulnerable with respect to land rights since they are entirely dependent on the goodwill of the *regulado* in obtaining access to land. Use rights for women are usually acquired through birth in their family of descent or through marriage, and are usually only accorded for horticultural subsistence fields. In the event of conjugal separation, women generally lose their land rights, and separated women are rarely (if ever) granted land use rights in their family of descent (see Box 2.2 on women and land rights).

57. **Land tenure issues in Guinea Bissau are further complicated by a series of national laws passed between the mid-1970s and the mid-2000s, which attempted to modernize land policy and institutions, and which are overlaid on the mosaic of customary land practices.** In the colonial period, the traditional authorities covered the function of official community administrators. A 2006 Bank-commissioned study – *Land Tenure Issues and Policy Study* (Land Study) —showed that this formal link between the public administration and traditional leadership was not renewed in the post-independence period. Instead, the Government sought to establish a new system for land administration by establishing official land committees at national, regional, sector, and section levels. National land laws permit women to access land in their own right, and authorize the granting of land concessions for up to 90-year periods to private individuals and

enterprises as a means of promoting investment.¹³ Vast tracts of land have indeed been granted under this concession scheme, principally for cashew plantations and for achieving rice self-sufficiency. The criteria and process by which land is allocated to different groups is not clear, and concessionaires are not required to pay taxes on the concession land – limiting their value from the standpoint of strengthening public revenues, as well as raising questions about the transparency of these transactions. Overall, however, the majority of the rural areas continue to be administered by traditional authorities in accordance with traditional practices. State land laws are rarely implemented due to the weak capacity of state land institutions, including the cadastral service, to implement national policy.

58. In addition to profitability reasons, the notable increase in the cultivation of cashew has been partly driven by land customs that tend to increase security of tenure when land is planted with cashew. Guineans have increasingly sought to concentrate their labor and other resources in cashew production for a variety of reasons, not the least of which is obtaining returns on investment. However, incentives to shift to cashew are also strengthened by customary land tenure norms, which tend to protect investments in land. Since planting of cashew trees is seen as an improvement to the land (similar to investments in infrastructure), customary practice requires that the individual/household that planted them continues to hold that land as long as the trees remain on it. Households, therefore, have a strong incentive to produce cashew rather than seasonal crops since that helps guarantee longer security of tenure. Moreover, the ability to gain concessions for cashew outside of the household's own locality is a powerful incentive to cultivate cashew among ethnic groups which have inheritance rules that do not benefit direct descendants. Since the cashew concessions are acquired outside of the clan's area, they fall outside the traditional rules of inheritance and can be transferred to sons.¹⁴ In some regions, cashew production has encroached on traditionally managed communal forests, often without the consent of the local community – leading to societal tensions.

59. Existing land tenure and inheritance policies undermine agricultural productivity and inhibit a much needed structural change within and outside agriculture, likely perpetuating poverty and inequality. A major binding constraint to investment, for both smallholder and commercial agriculture, is the lack of secure tenure rights. The current mix of national and customary land usufruct, concessions, and inheritance rights constrains rural development in several ways. By concentrating land and labor on cashew production, farmers forego crop portfolio diversification and higher returns in higher-value agricultural activities; in other words, cashew may offer low short-term risk, but also below-potential returns. Sales and rental restrictions on agricultural land constrain investments in land and agricultural technology, employment transition across farm and to non-farm activities, and access to credit and insurance, and subsequently lead to lower agricultural productivity. By fear of losing the future income stream of land, insecurity of property rights limits migration. Moreover, these adverse incentives affect different groups, particularly women, disproportionately. Current land policies also have adverse impacts on sustainability via environmental or social impacts (conflict) and fiscal/revenue

¹³ However, the rights granted to women under the law are rarely implemented.

¹⁴ Revenues from cashew are principally invested in rice and other consumption goods. However, as a consequence of rapidly spreading cashew production, traditional rice-fields (*bolanhas*) have been increasingly neglected, –making usable rice fields increasingly scarce.

implications. A number of models have emerged elsewhere on the continent that would be illustrative for Guinea-Bissau.¹⁵

Box 2.2 Women, Land and Productivity

While statutory law provides equal land rights to men and women, in reality customary practices impede women's land rights, with women's access to land and other assets often dependent on their marital status. A study conducted for the United Nations Children's Emergency Fund (UNICEF) found that 63 percent of 80 localities visited had no justice services, with 58 percent of individuals stating that justice was determined by the community (AfDB, 2014). This is important given the discrimination that is apparent in many of the customs that are followed by the patriarchal communities of Guinea-Bissau. These customs mean that women largely access land through men. While this puts all women at a disadvantage and in a state of dependence, it results in particular vulnerability for single, widowed, and divorced women. Marriage is the institution through which men are allocated land by autochthonous kinship and domestic groups. Women generally only gain usage rights to such land, as well as the ability to hire labor, through their husbands. Women have no right to inherit property from their husbands or fathers, and if they are given any land as inheritance this is usually held in trust and inherited by sons once they marry. Single, widowed, and divorced women are often given inferior land and may have to re-negotiate access to land every year.

Women's agricultural productivity is constrained by their less secure access to land and reduced access to farm labor. Insecure land rights not only constrains women's participation in cash crops but may also reduce their overall agricultural productivity by reducing their incentives to invest in their land. For example, looking at the case of Ghana, Goldstein and Udry (2008) find that insecure access to land is associated with lower investments in land fertility. Part of the reason is that those with less secure access, such as women, feel less able to let their land lie fallow due to the greater risk that their land will be expropriated. This ultimately results in lower yields for women.

Women's agricultural productivity is also constrained by having less access to agricultural inputs. First, female household heads may find it difficult to access farm labor because they have fewer household members to draw from, due to various factors such as widowhood, migration of their husbands, or divorce. Secondly, emerging research suggests that women in SSA countries also find it more difficult to hire non-family farm labor and may achieve lower returns to that labor. Women can less afford to pay for the best workers and have less time to supervise workers due to their unequal responsibility for domestic chores. Evidence suggests that all other productive inputs, such as credit, materials, equipment, and training, are distributed according to the same patriarchal rules that provide men with an advantage in land access (Boubacar-Sid et al., 2007). Moreover, these customary rules are reflected in the Civil Code (article 1678) which states that a couple's assets belong to the husband.

Women's lower access to productive assets may also constrain their ability to improve their welfare outside of agriculture. The Civil Code contributes to the difficult environment women find themselves in, with article 1686 stating that a woman cannot operate a business without her husband's consent, unless she owns all of the household's property or if the couple has specifically chosen to have separate property (AfDB, 2014). It is not surprising that only 19.9 percent of businesses that took part in the World Bank's Enterprise Survey for Guinea-Bissau stated that they have female representation in their ownership, compared to a Sub-Saharan average of 33 percent (World Bank, 2006).

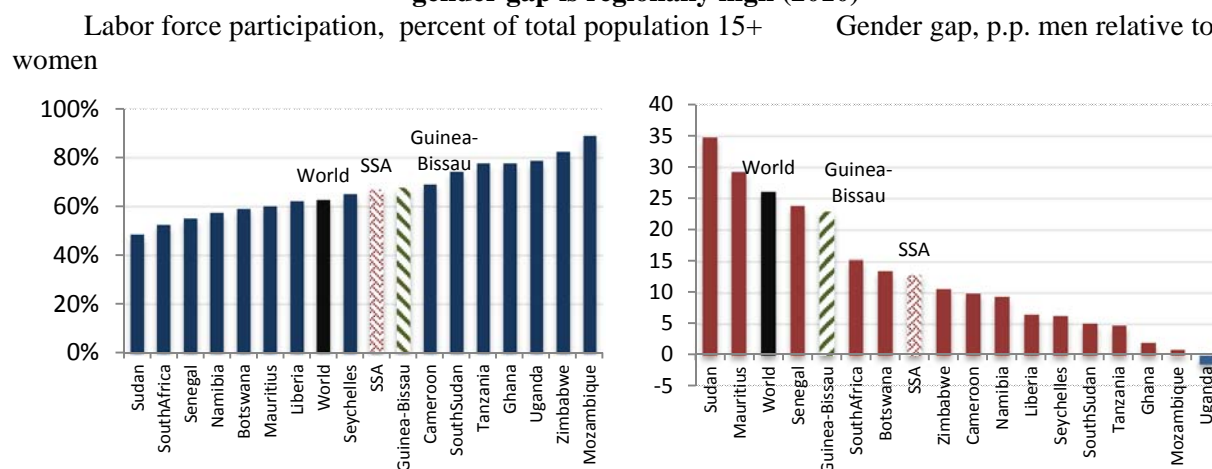
¹⁵ In Rwanda, a country equally small, government and civil society have successfully developed land laws and land administration systems for recognizing land rights for all citizens; elsewhere in former Portuguese Africa, Mozambique has adopted one of the most progressive land laws on the continent, and laws that allow the recognition of community land rights, and which clarify institutional authority across multiple sectors.

2.4 Assets are not only low but also are used at suboptimal levels

60. **Poorer Guinean households not only suffer from a paucity of human capital and physical assets, but their ability to productively exploit the assets they do possess is limited, adding another barrier to exiting poverty.** In 2010, labor force participation in Guinea-Bissau for the population over age 15 is estimated at 67.7 percent,¹⁶ comparable to the levels seen in other countries in the region (Figure 2.19). However, engagement in the labor market is much lower for some groups of the population. For instance, while over 70 percent of men are working or actively looking for a job, just over half of women are engaged in the labor market. These differences in labor participation by gender are higher than the regional average. Furthermore, engagement in labor activities in Bissau is low. One out of two of economically active individuals from the capital participate in the labor market compared to three out of four from rural areas (Table 2.2).

61. **Economically active women are disadvantaged in the labor market.** The formal sector is small, with salaried employees making up only 10 percent of the total workforce (AfDB, 2014). Women are less likely than men to work in the formal sector and, when they do, they are less likely than men to work in senior or skilled positions. Women make up only 26.5 percent of formal sector workers (GoGB, 2012). Data from the 2010 ILAP shows that only 4 percent of women report that their primary occupation pays them a salary, compared to 16 percent of men. Women are also less likely than men to report working in the private sector (4 percent versus 11 percent), which is significant because poverty rates are lower for those working in the private sector (World Bank, 2015).

Figure 2.19. While labor participation is slightly above the average for neighboring countries, the gender gap is regionally high (2010)



Source: World Development Indicators (2008-2012).

62. **The low intensity of labor utilization is also evident among young, urban men.** In 2010, 11.2 percent of male youth (ages 15-24) in Bissau were unemployed, compared to 6.9 percent of females. The overall unemployment rate for all adults (15+) is 7.3 percent. While unemployment rates are lower for rural citizens across all age groups and genders, these data might hide significant

¹⁶ The International Labor Organization's (ILO) definition of labor force participation is the one used here, and it is calculated as the ratio of the economically active population (employed and seeking employment) to the total working age population.

underemployment which is thought to be especially significant in rural areas (IMF/World Bank, 2011). Unlike men, many women may not even be actively looking for work. According to data from the 2010 ILAP, poor urban women are the least likely to be economically active (41 percent), followed by non-poor urban women (44 percent), and poor urban men (59 percent) (see Table 2.2). Indeed, while men are much more likely to mention the unavailability of jobs as a reason for not working, women are much more likely to cite domestic responsibilities.

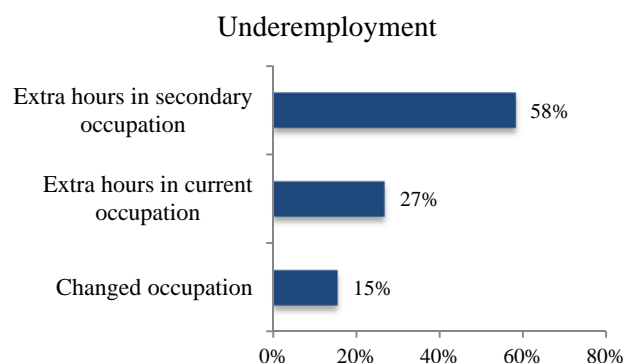
Table 2.2 Labor participation is lower among women and urban residents

	Urban		Rural	
	Women	Men	Women	Men
Non-Poor	43.8%	61.9%	68.9%	82.0%
Poor	40.6%	59.2%	66.7%	82.2%
Overall	42.2%	60.5%	67.2%	82.2%
Overall sample	67.70%			

Source: World Bank staff calculations using ILAP 2010 data.

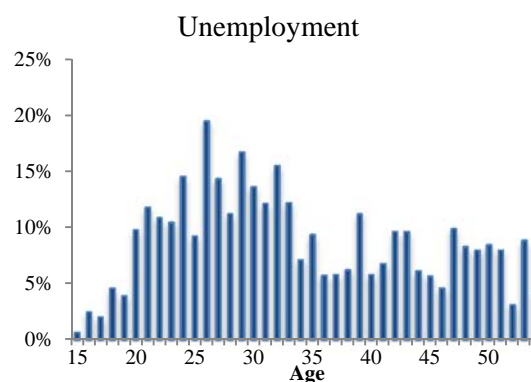
63. **The low demand for labor feeds into the low-level equilibrium in the Guinean economy.** An indication that the labor force is underutilized under current market conditions is the expressed desire of all of the economically active population to have an extra job or work more hours (Figures 2.20 and 2.21). Guinea-Bissau is affected with a potentially low intensive margin of labor. The vast majority (98 percent) of the active labor force has expressed availability to do more work, while 37.7 percent have sought out ways to further generate income. Within the latter group, over half report doing so by working extra hours in a secondary occupation, while 27 percent report working extra hours in their current occupation, and 15 percent report changing jobs to seek out higher returns. Further highlighting under-utilization of labor, 11 percent of the male working-age population that are neither working nor seeking work cite low demand for labor as a discouraging factor. As noted above, illness, hunger and disabilities impose further limitations on the ability of the population to provide their labor and increase productivity (see Box 2.3 on the impact of demographic changes on the labor market).

Figure 2.20: The economically active population wants to work more hours



Source: World Bank staff calculations using ILAP 2010 data.

Figure 2.21: ... Youth have higher unemployment



64. **Autonomous household activities are the main type of economic activity practiced in rural areas, especially among the poor.** The majority of rural households participate in autonomous household activities, ranging from agriculture to trade and crafts, and small businesses. A clearly visible, probably not surprising, pattern is that households in the lower income/consumption quartile tend to participate more in these autonomous economic activities. Transition from these potentially less-rewarding autonomous economic activities to private and public sector employment is limited among poor households. Only a 2 percentage points decline (from 89 to 87 percent) in the share of households participating in autonomous activity was recorded between 2002 and 2010 for households in the lower consumption quartile. On the other hand, a higher proportion of households in the upper two quartiles have moved to private and public sector employment, which is more rewarding.

65. **Utilization of natural resources is inefficient and hinders their sustainability.** Terrestrial and some sea-based resources are over-utilized. The Land Law (which rules out freehold property rights for individuals, groups, businesses, and institutions), multiple customary land practices, and an uncertain system of land concessions overlap to discourage utilization and investments in land. For instance, customary land tenure norms establish that households that plant cashews can hold the land as long as cashew trees remain. This incentivizes households to grow cashews extensively. Cashew trees grow easily, and planting them closely enough reduces the scope for invasive plants to develop between trees, thus reducing maintenance need and allowing larger areas to be colonized. As a result, natural resources such as forests are over-utilized (or simply lost) relative to the level that would allow sustainability.

Box 2.3. Opportunities and risks from future demographic changes in Guinea-Bissau

Demographic projections suggest that the working age population will increase relative to the total population. Based on the UN's fertility and mortality assumptions, Box Figure B2.3.1 maps out demographic projections for Guinea-Bissau. The figure shows that the population will grow rapidly, given the currently high fertility rates. By 2100, the population is estimated to quadruple. However, the composition of the age structure changes. As both fertility and mortality rates fall, the ratio of the working age population to dependents (that is, children and teenagers below the age of 15 and elderly people 65 years or older) is projected to rise from 54 to 65 percent.

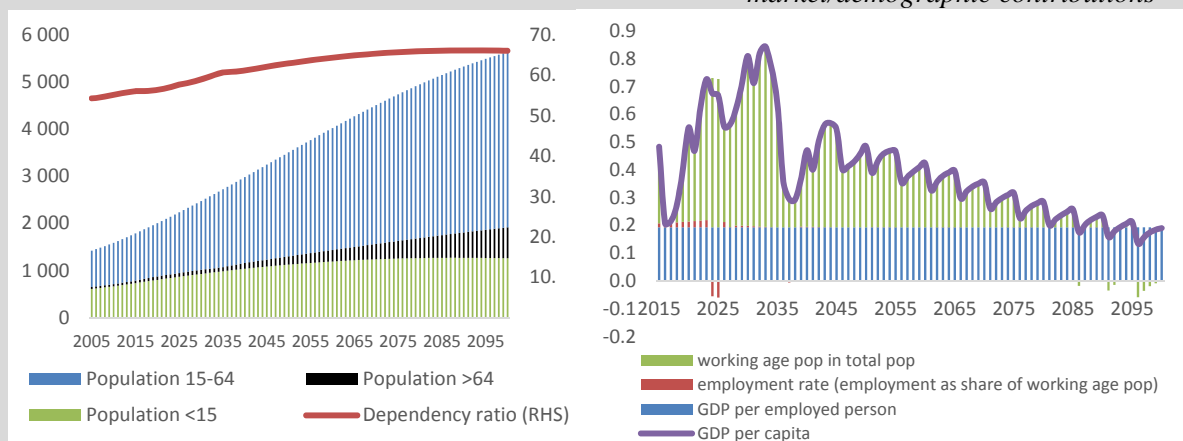
Improving dependency ratios can result in a 'demographic dividend'. World Bank simulations suggest that the increase in the working age population presents a considerable opportunity for Guinea-Bissau. Assuming that labor force participation rates are roughly constant (at 67 percent, according to the ILAP II), unemployment remains at about 8 percent (ILO estimate), and that labor productivity grows at its historical average of about 0.4 percent, the demographic change alone will raise GDP per capita by 20 percent in real terms comparing 2050 to 2015 levels. Additional improvements in the labor markets would result in further prosperity gains. For example, increasing the labor force participation rate gradually from 67 to 80 percent would boost real GDP per capita by a total of 39 percent. Raising labor productivity by 0.1 percentage point per year would more than double GDP per-capita levels.

Demographic change, however, also constitutes a major risk as new jobseekers put pressure on the labor market. A 'demographic dividend' can only occur when new labor market entrants find productive jobs. Given the current underemployment in Guinea-Bissau, the relatively low returns to labor, potentially diminishing returns in the cashew sector, and limited job opportunities outside cashew, the probability that the labor market will struggle to absorb incoming generations is relatively high. In this case, household income will fall as the younger generations will add little additional income to families. This would likely

translate into an increase in poverty. It may also be a source for social dissent which can be particularly perilous in a fragile state like Guinea-Bissau.

Box Figure B2.3.1: The working age population will double by 2040 yielding a more favorable dependency ratio (left) and Guinea-Bissau is going to benefit from a demographic dividend, assuming availability of jobs with constant productivity (right)

(Population by age group; dependency ratio (RHS) (GDP per capita growth, and labor market/demographic contributions



Source: World Bank staff calculations based on UN World Population Prospects and ILO unemployment data.

2.5 Returns to assets are inadequate and undiversified

66. **The overall low returns to assets highlights the wide scope of the low-productivity and fragile economy equilibrium that characterizes Guinea-Bissau.** Most poor households are engaged in agriculture, mainly in cashews, and subsist with lower returns. This is rooted in large differences in ownership of physical and human capital between the non-poor, and the poor and extreme poor. It is also a result of an economy that has been plagued by frequent bouts of instability, and a resulting short-term outlook in which the elite is better positioned to capitalize on short-term gains. It is also anchored in poor infrastructure (roads, ports and telecommunications), which disconnects farmers from markets and keeps transaction costs high. Symptoms of this underdeveloped and unstable labor economy include a high prevalence of informal jobs, low educational achievement, and a context where households are unable to make long-term, higher-risk investments in both the non-agricultural and agricultural sectors. This reality is even more prevalent among the extreme poor perpetuating overall high poverty rates and inequality.

67. **Generally, the effect of education on earnings is positive in Guinea-Bissau, but the highest returns to education are almost exclusively enjoyed by the better-off individuals, underscoring the high concentration of public and private rents.** Returns to schooling for Guinea-Bissau were obtained from the estimation of a standard Mincer earnings equation using ILAP-2010 data¹⁷ (see Annex 2B). The results are consistent with the notion that more education

¹⁷ Unfortunately, this dataset lacks information on individual earnings. For this reason, a synthetic individual was constructed, comprising the averaged values of all working individuals within a household, as a best approximation of individual returns to education. To ensure robustness and comparability, two sets of estimations were performed. Given that earnings were reported only at the household level, both sets of equations use the same values for the dependent variable (log of monthly earnings), but the latter (that is: i.e. synthetic) uses an averaged value for each of the explanatory variables in the equations.

contributes to higher earnings. The average return for a year of education is in the order of 5 percent. However, the average effect masks variations in returns across education levels. While returns to primary education are negligible—at least in a statistical sense—the wage premium is concentrated among workers that have completed secondary education (4 percent) or some years of or completed tertiary education (8 percent). These differential returns across education levels tend to exacerbate poverty and inequality due to the low level of school attainment of moderate and extreme poor households (Annex Table 2B.1). 1). In addition to formal education, the agricultural sector where most of the poor work, lacks extension services. Informality and low levels of education, already more prevalent among the rural poor, are coupled with a lack of extension services, which could disseminate off-the-shelf knowledge and help boost productivity.

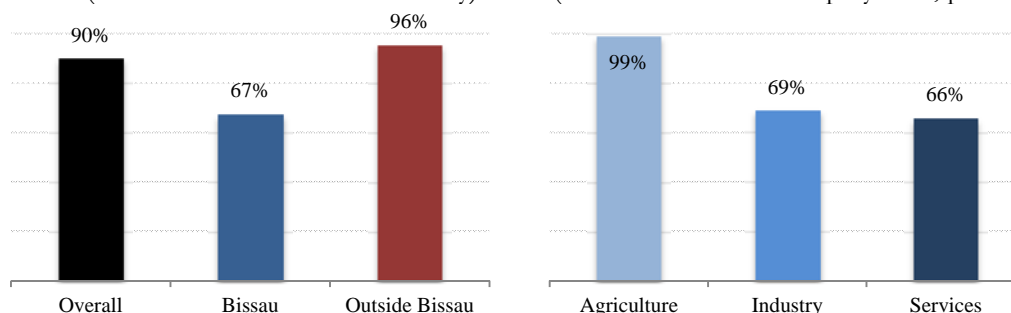
68. Even though poor and non-poor households benefit from accumulating secondary and tertiary education, the poor exhibit a relatively higher return, which points to underinvestment in education for this group of people. In the case of completed secondary education, the return among the poor is 52 percent higher than for the non-poor (5.3 percent compared to 3.4 percent). Along the same lines, on average poor households see a wage earnings increase 2.2 percentage points faster than their non-poor counterparts (8.4 percent compared to 6.2 percent) as they accumulate tertiary education (Annex Table 2B.1). These results suggests that increasing investments in the education of low income households would substantially raise the return that they can derive from their human capital. In reality, however, most people with secondary and tertiary education belong to better-off households.

69. Informality is highly prevalent in the labor market, due to the large reliance on agriculture and to informal contracts in other sectors of the economy. This translates into low labor productivity and low returns. Informal work is identified in this analysis with the type of remuneration, meaning informal pay is taken as a proxy for informality in the labor market. Within this definition, 90 percent of the labor force is employed in the informal economy in Guinea-Bissau; this is larger outside of the capital (96 percent) and smaller in Bissau (67 percent) (Figure 2.22). Looking across sectors, agriculture is nearly all informal, whereas industry and services house roughly two-thirds of informal persons within each sector. Figure 2.23 presents a breakdown for the type of remuneration in Guinea-Bissau. A large share of informal employment is associated with higher poverty and lower returns, as informal work tends to be marked by poor working conditions and an absence of legal identity, implying low job security and a lack of social protection mechanisms (International Labor Organization (ILO) 2015).

70. In the main economic sector (cashews), women do not benefit as much as men from the economic returns—even though about half of the cashew workforce is female. Cashews account for 26 percent of income (net of remittances) for female-headed households compared to 35 percent for male-headed households (ILAP, 2010). As with all agricultural production, women's roles in the cashew industry tend to be at the bottom of the value chain and they have little control over key productive inputs. In a sector where returns for poor farmers are already low compared to non-poor counterparts, men own most of the land on which cashews are grown (see Box 2.2 above dealing with land and productivity issue), they make the key decisions on whether and when to sell, and they take the lead selling the nuts to middlemen and processors, who also tend to be men (AfDB, 2014). Women, on the other hand, farm and harvest the cashews, peel and

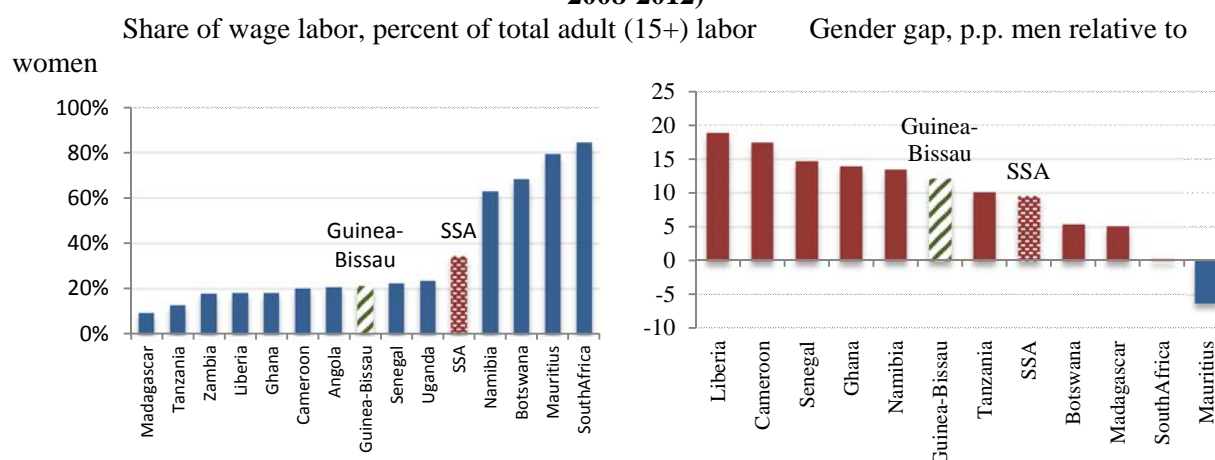
sort the nuts, and are involved in processing the cashew stem or fruit, which is much less valuable than the nuts, which are seen as belonging to men (AfDB, 2014).

Figure 2.22. Guinea-Bissau's labor market is marked by informal employment
(Share of informal labor economy) (Persons in informal employment, per sector)



Source: World Bank staff calculations using ILAP 2010.

Figure 2.23. The share of salaried labor in Guinea-Bissau is lower than some of its neighbors (circa 2008-2012)



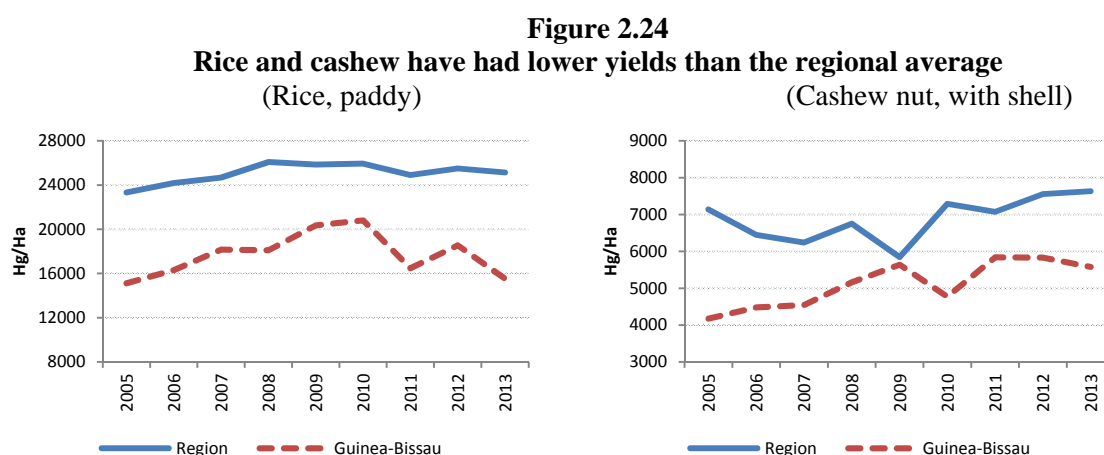
Source: World Development Indicators (2008-2012) and ILAP 2010 for Guinea-Bissau.

71. **Low returns are also evident among workers that have jobs thought to be more stable and of better quality.** Overall labor earnings are remarkably low across all types of jobs, yet having a salaried (often more formalized) job commands relatively higher wages. Poverty measured at US\$2 (national poverty line) is 56.7 percent for households whose heads are salaried and 71.8 percent for the unsalaried. The fact that more than half of the households whose household heads are employed in wage jobs are poor is indicative of a low-productivity, low-returns context, even in the sectors that are relatively more developed. This highlights that the general constraints to productivity, such as low human capital, infrastructure, and technology, are not only present in agriculture but permeate all aspects of the labor market, creating bottlenecks to growth.

72. **Returns are eroded by high transaction costs.** As noted above, weak connectivity to markets limits households' ability to diversify away from cashew and to benefit from higher prices when demand is high. For instance, trade and crafts contributed 11 percent of incomes of households that are less than half an hour commute (on foot) from markets, but their role declines

continuously to only 3 percent for those households that are located more than one hour walk from markets. Higher poverty rates for those with difficult access to basic infrastructure and remoteness from markets underscores potential transaction costs and lower farm gate prices, particularly in rural areas. According to data from 2010, households with easier access to local markets and public transit were less poor on average. Between those near (0-30 minutes) and far (more than one hour) from public transit and from a local market the difference in poverty rates was of 15 and 19 percentage points, respectively. In general, households within short commutes to markets have better diversified income sources.

73. **The largely agrarian economy has to cope with low returns to labor, capital, and ensuing low agricultural yields.** The large share of value added by agriculture in Guinea-Bissau (explored further in Section 3, below) implies that low productivity in this sector has deep economic implications. With the plethora of challenges facing rural households, including low human capital, market disconnect, and few systems to disseminate agricultural knowledge, the sector has not seen much technological advance over the years, with yields low when compared to the region (Figure 2.24). Rice yields are lower than the regional average and have been stagnant, while cashew yields have been below the regional average in spite of an upward trend.



Source: Food and Agriculture Organization Statistics, FAOSTAT (2015).

74. **In the agricultural sector, returns may also be inhibited by Guineans' heavy reliance on raw cashew production/exports, because the sector is often subject to political and climate shocks, and relative prices showed a declining trend in the 2000s.** Political turmoil derails economic activity, including the cashew sector. Indeed, cashew prices collapsed in 2012 in response to the military coup. Returns in the cashew sector are vulnerable to shocks from natural disasters, whether they are diseases or shocks from climate change. Moreover, the cashew price that Guinea-Bissau collects was falling (at least before 2014) in real terms with the exception of the increases observed during the commodity price shock of 2011 and the upward trend after 2014. At the same time, the rice price has risen modestly. Although rice is grown on a subsistence basis, rice imports have been increasing.¹⁸ Rising rice prices and falling cashew prices have driven a deterioration in the cashew-to-rice price. Finally, the high risk of political turmoil may keep

¹⁸ Per capita rice imports between 2008 and 2014 were twice the size of imported volumes between 2000 and 2007. Rice is the second most important import good for Guinea-Bissau, after fuel.

farmers from diversifying into other sources of agricultural and non-agricultural income, severely hampering long-term returns.

2.6 Private transfers provide modest support to household incomes

75. **While employment opportunities and incomes remain low in Guinea-Bissau, private transfers support household incomes and diversification.** Based on data from ILAP2, nearly one-fifth of Guinean households report receiving transfers. Perhaps due to easier access to financial services, infrastructure, and migratory connection, the proportion of households in Bissau receiving transfers such as remittances or internal transfers was closer to 25 percent compared to 15 percent elsewhere. The income share of private transfers is 7.3 percent for the whole population and 41 percent when looking exclusively at recipient households, indicating a significant support to household income.

76. **The highest rate of transfer receipt occurs in female-headed households located in Bissau, indicating a pattern of migration of male workers out of Bissau as well as frequent flows of internal transfers to support widows.** It is not uncommon for men to be more likely to migrate to look for work elsewhere, leaving households to be headed by female spouses. This pattern of migration is more evident in the capital city and helps explain why female-headed households are less poor than male-headed households. Almost half (42 percent) of female-headed households in Bissau were transfer-receiving households as opposed to 23 percent in other parts of the country. Consequently, the income share from transfers is more than three times higher in female-headed households compared to male-headed households—16.3 and 5 percent, respectively. At the same time, a large proportion of households whose head is a widow, particularly women, receive transfers, also suggesting that internal transfers between support communities and families are at play.

77. **Private transfers contribute moderately to alleviate poverty.** Poverty rates are lower for households receiving transfers both in urban and rural areas, although this difference is only statistically significant in rural areas. Simulation analysis suggests that the overall poverty rate would be 1.6 percentage points higher in the absence of private transfers (Table 2.3). As expected, the effects are more concentrated among female-headed households, for which the incidence of poverty would increase by 4.4 percentage points (from 65.4 to 69.9 percent). The modest overall effect of remittances on poverty is likely driven by the limited financial infrastructure of Guinea-Bissau and by liquidity constraints that limit the ability of low income households to migrate. Indeed, households in the bottom 40 percent are almost half as likely as those in the top quintile to be the recipient of a domestic or international transfer.

Table 2.3: The level of welfare of female-headed households is influenced by transfers

Poverty rates	Full Sample		Only Transfer-Receiving Households		
	Transfers	No Transfers	Transfers	No Transfers	
Female-Headed Households	65.4%	69.9%	56.0%	70.9%	**
Male-Headed Households	70.4%	71.2%	66.3%	72.4%	

Note: ** denotes that difference is statistical significant at the 5 percent level

Source: World Bank staff calculations using ILAP 2010

2.7 Household well-being is highly vulnerable to shocks

Risks from natural disasters and climate change

78. **There is already evidence that Guinea-Bissau's climate is changing in a number of ways.** These changes range from increasing rainfall variability, to late onset of the rainy season, to increases in temperature, and to a rise in sea level and tidal surges (see Annex 2C on climate change impacts). For instance, average yearly temperature has increased about 1°C over the past decades. Observations suggest a shortening of the cool season during the months of December-February. Trends show increased irregularity in precipitation, together with an overall trend of decreased mean annual precipitation and seasonal precipitation. Changes in rainfall patterns are leading to longer, hotter dry seasons, particularly in the northeastern interior, resulting in seasonal water shortages which directly affect access to water for the population's needs, as well as for agriculture, and livestock. Flooding events occur frequently in inland and coastal areas, causing severe impacts on infrastructure, agriculture, and public health. Approximately 70 percent of the population lives in the coastal area, making it highly vulnerable to rising tides and sea levels. Projections suggest that these trends are likely to be exacerbated going forward since Guinea-Bissau, while a low emission country, is highly vulnerable to the impact of global climate change, ranking second only to Bangladesh on the 2014 Climate Change Vulnerability Index (CCVI)¹⁹ (see Box 2.4 below on the Government policy on climate change).

79. **Climate stress, in conjunction with anthropogenic pressure (especially slash and burn agriculture, cashew plantation, and logging), has the potential to accelerate deforestation and degradation of forest cover as well as to affect a number of other sectors.** The country's terrestrial and mangrove forests are of critical importance to local livelihoods. Forests also have significant economic value both as a source of timber and carbon stocks, as an essential breeding and nursery ground for the country's fishing stock, and as an important defense against floods and saline intrusion from rising sea levels. These ecological services directly and indirectly underpin the well-being of the population. At the household level, non-timber forest resources provide, among other things, food, medicine, construction materials, shelter, and fuel. Fuel wood and charcoal, together with agricultural biomass, make up 80 percent of the country's energy consumption; the poor spend 15 to 20 percent of their income on energy alone. Changes in the quantity of both forest timber and non-timber resources will thus have direct impacts upon the subsistence livelihoods of the poor, and particularly on woman for whom the collection of fuel requires considerable time and effort. A number of other economic activities, ranging from fisheries to nature-based tourism, would also be adversely affected by climate change, and there will likely also be important impacts on infrastructure, urbanization, water supply, and health as well.

¹⁹ The CCVI ranks the climate related risks to the populations, business and governments of 67 countries over the next 30 years, down to a level of 22km² worldwide. It is based on three factors: (1) exposure to extreme climate-related events, including sea level rise and future changes in temperature, precipitation, and specific humidity; (2) the sensitivity of populations, in terms of health, education, agricultural dependence, and available infrastructure; and (3) the adaptive capacity of countries to combat the impacts of climate change, which encompasses, R&D, economic factors, resource security, and the effectiveness of government (Maplecroft CCVI 2015).

Box 2.4. The Government policy on climate change

Guinea-Bissau has signed and ratified the Framework Convention on Climate Changes and the Kyoto Protocol, and has undertaken a considerable amount of policy planning and analysis about climate change adaptation. It has prepared an initial and second National Communication on Climate Change (2004 and 2011, respectively), and prepared a National Programme of Action of Adaptation to Negative Effects of Climate Changes (NAPA, 2006). The NAPA assessed the country's vulnerability to climate change and proposed steps and priority activities to reduce and/or mitigate the negative effects of climate changes, and to implement early warning and forecasting measures enabling a response to future catastrophes.

The country's development strategy for 2015-2025 also addresses the climate change theme. Specifically, it calls for the implementation of the National Protected Areas Strategy, the preparation of an overarching National Sustainable Development Strategy, and the creation of a specific Climate Plan focused on increase resilience to climate change. The development strategy also highlights the intention to implement a coastal protection plan and an adaptation and mitigation plan to response to the physical and social risks posed by climate change. The State Secretariat of Environment is completing a detailed review and analysis of environmental governance as the first step towards the preparation of the National Sustainable Development Strategy.

As is the case for managing natural resources across the board, the country's capacity to address the challenges and risks of climate change is weak. Natural resource information and data is limited and of variable quality, as is the monitoring of climate parameters. Institutional capacity varies between the multiple sectors, but overall the capacity for on-the-ground implementation and enforcement is limited. Over the past few years, the country's increasing awareness of the importance of addressing these challenges has been demonstrated by the preparation and request for donor support for a growing number of climate-related projects (not all financed), such as: those aimed at improving the knowledge base, and implementing actions, to promote climate resilience and adaptation in the agricultural and water sectors as well as in the coastal zone; strengthening the climate early warning system; developing forest monitoring systems; and building institutional capacity, among others.

Risks stemming from other systemic and idiosyncratic shocks

80. **The well-being of households in Guinea-Bissau is also highly susceptible to other systemic shocks, such as military coups, civil strife, social upheaval, macroeconomic shocks, and harvest failures.** GDP per capita has fallen in Guinea-Bissau following the military coups and bouts of political instability that have affected the country (Figure 1.1). Moreover, the negative effects of growth collapse, changes in food prices, terms of trade shocks, and harvest failures are likely to disproportionately affect the poor, who lack effective formal and informal means to prepare ex ante for these risks, and to cope with their consequences as they materialize into major shocks. As result, households tend to rely on sub-optimal coping strategies, such as reducing consumption, cutting back on investments in the human capital of children, high-interest borrowing, or selling productive assets. In preparation to confront the effects of shocks, households may also smooth income ex ante by engaging in economic activities that allow the exchange of lower risks for lower returns. Opportunities for family and community risk-sharing are likely undermined by the covariant nature of the shocks.

81. **Households are also largely exposed to idiosyncratic shocks.** Mortality risks associated with childbearing, for instance, are high given the high rates of maternal mortality. At 560 deaths

per 100,000 live births, maternal mortality in Guinea-Bissau is among the highest in all Africa. Infant mortality rates are equally high. The most common causes of morbidity and death, such as respiratory infections, diarrhea, malaria, and HIV/AIDS are either preventable or treatable. Health shocks often result in over 40 percent of health care out-of-pocket payments, increasing the risk for affected household to fall further back into poverty.

Public and private mechanisms for risk mitigation are weak

82. Public risk management and coping mechanisms basically do not exist, exposing the population to great risks from even common life events. Limited fiscal space means that there is limited room for the Government to mitigate shocks, whether they are from the local economy or from natural events. Low capacity also limits the ability of the government to develop disaster management plans or to prepare adaptation strategies for climate change. The government's limited presence in rural areas means that these areas are particularly vulnerable to shocks. As the 2015 CEM illustrates, the country lacks social security and social assistance programs to protect against these income shocks, help smooth consumption over the life cycle, reduce poverty, and promote greater human development. Similarly, risks from old age remain uncovered, because there are no formal pension systems that protect the elderly except for a few particular schemes with similar objectives catering to some civil servants and the military. Simulations suggest that a well-targeted cash transfer scheme equivalent to 1.5 percent of GDP could reduce extreme poverty by up to 10 percentage points.

83. In view of the underdeveloped financial sector and poor investment climate, private risk management is also limited in Guinea-Bissau. The financial sector is shallow in Guinea-Bissau, as explained further below. This also means that there are few insurance companies (including micro-insurance) that could offer products to consumers to hedge their risks. Partly, this is linked to the country's poor investment climate. Risk management, especially for the poor, takes two forms: (1) private transfers, whether they are remittances or social transfers within communities, such as to the elderly or to widows, and (2) diversified agricultural production. However, the dependence of households on cashews has risen, reinforced by the nature of cashew production which only allows very limited intercropping.²⁰ As a consequence, the increase in cashew production in the absence of formal risk management and coping systems has come at the expense of limiting risk mitigation through agricultural diversification.

²⁰ For example, the juice of cashew apples is poisonous to many other crops.

3 MACRO LEVEL COUNTRY CONTEXT

- *Growth in Guinea-Bissau has been systematically low. GDP per capita grew by 0.7 percent annually between 2003 and 2014, less than half the average recorded for the Sub-Saharan region (1.5 percent) during the same period.*
- *The structure of Guinea-Bissau's economy has barely changed over the last two decades. Growth performance is volatile, with the production and export of a single commodity as the engine of growth. The production of cashews is concentrated in the first rung of the value ladder and engages 75 percent of small farmers, underscoring the tight connection between incomes and movements in farm gate prices or production levels, especially for the poor.*
- *The existing economic structure limits its resilience to mitigate the impact of shocks (terms of trade, political, and natural) and the intense competition for rents among the elite undermines the maximization of additional economic opportunities (cashew processing, rice, fisheries, mining, and tourism).*
- *Low and unpredictable public revenues, regressive and distortionary taxation, and poor quality of public expenditure limits the effectiveness and equity of the fiscal policy.*
- *The current business climate is not conducive to the generation of growth, employment, and productive capital. Financial inclusion is among the lowest in Sub-Saharan Africa, and infrastructure is in a woeful state, from the port to roads, to access to electricity, to potable water, and to telephone and the Internet. Guinea-Bissau is at the bottom for all of the 10 Doing Business indicators. The improvement of the business climate is an important prerequisite to increasing the inflow of private investments, which can boost non-agricultural activities, helping to diversify incomes. It will also provide opportunities to help leverage the existing agricultural activities, mainly in cashew production and processing.*
- *Low investments is an important pillar of a vicious circle of low productivity, low growth, lack of opportunities, and elite capture which then feeds back into low investments, suggesting that the country is trapped in a low-growth equilibrium. Nevertheless, there are emerging opportunities to support more consistent growth, particularly drawing on electricity cooperation across West Africa, telecommunications permeability through mobile services, and improvement of cashew-related country infrastructure.*
- *Low and unstable growth constitutes the second core area of binding constraints for poverty reduction and shared prosperity in Guinea-Bissau. To overcome this challenge, while capitalizing on emerging green shoots in the economy to boost poverty reduction and shared prosperity, Guinea-Bissau will need to implement policy actions geared towards diversifying the economy, improving cross-cutting economic and production support services, increasing financial inclusion, increasing flexibility of the labor market, enhancing fiscal discipline and public revenue collection and efficiency, and capitalizing on regional integration of markets and infrastructure. Participation in regional and international organizations could provide added policy discipline.*

84. **Guinea-Bissau has lost decades without achieving significant growth, underperforming relative to most of its peers since independence.** The economy, which is dependent on the cultivation and export of unprocessed cashew nuts, has barely grown over the past twenty-five years, recording average GDP per capita growth of about 0.7 percent significantly below peers. In fact, Guinea-Bissau is one of the slowest growing economies in the continent. The country's inability to break out of the low growth, high poverty incidence trap can be attributable to its narrow economic base, low human capital, and the absence of fiscal buffers, which increases its susceptibility to shocks. There is a strong negative correlation between Guinea-Bissau's growth performance and political developments. This is further compounded by weak budget management practices and fiscal policies which distort the allocation of capital and lower investment productivity. The wage bill accounts for a significant part of fiscal revenues, thereby reducing the fiscal space available for productivity-enhancing public spending, including public investment which is complementary to private investment and expenditures on education and health. As Chapter 4 will show, institutional and political economy factors are major impediments to strengthening fiscal policy and management of public finances in the country. Existing organizational structures have not supported the required fiscal discipline. The country has also been unable to raise productivity levels in the context of relatively low investments, poor infrastructure, inadequate human resources, limited access to finance, unaccommodating business and regulatory environments, coupled with weak linkages across sectors, and low technological infusion into productive activities.

85. **The analysis described in this chapter shows that Guinea-Bissau's persistent low growth does not reflect its potential, in view of the country's abundant natural resources and its advantageous geographical location.** Guinea-Bissau possesses opportunities to grow much faster, but the key to unlocking this potential will require action on several fronts including, *among others*, obtaining assistance from multilateral agencies, regional institutions such as the WAEMU and ECOWAS, and other stakeholders for technical and financial support to anchor critical interventions, while also introducing initiatives to directly address the underlined weaknesses in the existing business environment and governance framework (see Chapter 4 for a more detailed discussion, and Box 3.1 below for a discussion of the Government reform agenda). It has been empirically shown that improving fiscal institutions and boosting fiscal space through raising tax revenue and containing current spending, as well as through lower military spending and, to some extent, higher social expenditures, are significantly and robustly associated with building resilience. The commitment to an IMF program suggests a willingness on the part of the Government to start tackling some of these issues. While these are difficult reforms and may take time, the country has the opportunity to advance its development agenda by capitalizing on emerging green shoots in agriculture and other sectors by creating an environment for greater private sector participation in the economy. The country has been producing groundnuts with some degree of success, and the Government has also initiated steps to encourage sesame production. There is also potential in cashew processing, cultivation in rice, and a diversified range of efforts involving cereal, fruits and tubers. Fisheries and mining are also recognized as possible engines of growth. While the country possesses significant natural beauty, the potential of the tourism sector remains largely untapped. Moving into higher value-added activities in industry and services will be crucial for achieving the growth rates Guinea-Bissau will require to catch-up with other countries.

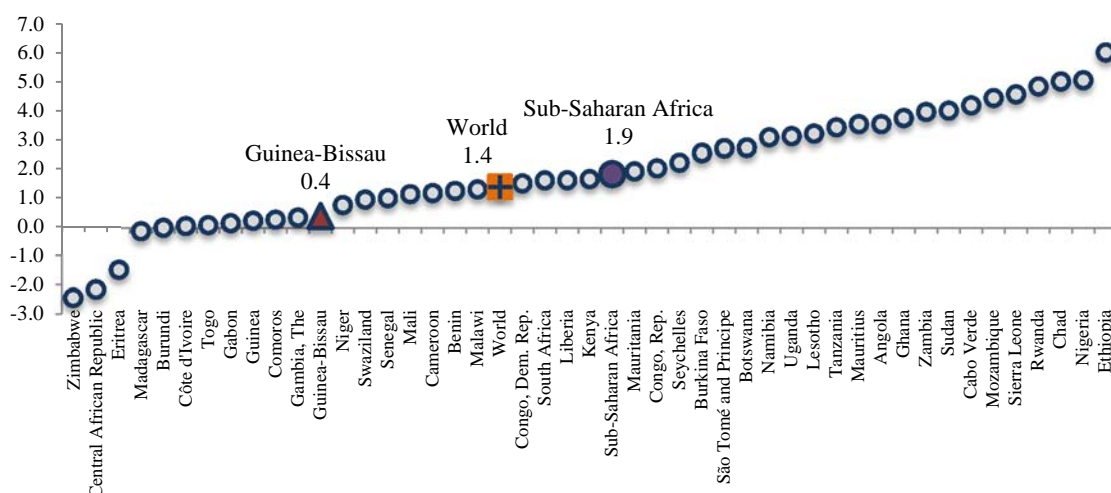
Box 3.1. “Terra Ranca” is the Government reform agenda moving forward

The Government elected in 2014 has committed to an ambitious reform agenda in order to turn the vicious cycle between fragility and poverty into a virtuous one of stability and prosperity. The plan’s vision for 2025 is “a positive Guinea-Bissau, politically stable through inclusive development, good governance, and preservation of its biodiversity.” The operational plan—with which the 2015 CEM was closely aligned—underpinning specific planned investments is based on six strategic axes: (1) governance and peace; (2) infrastructures; (3) industrialization; (4) urban development; (5) human development; and (6) biodiversity. The strategy identifies four growth sectors, agriculture/agribusiness, fisheries, tourism, and mining, which are framed by major investments to upgrade the electricity and Information and Communications Technologies (ICT) sectors. The implementation of the operational plan is expected to bring significant short-term economic benefits, especially in the construction and retail sectors. The plan was presented to the donor community at the pledging conference in March 2015, when US\$1.5bn were mobilized over five years. Box Figure B3.3.1 illustrates the intended distribution for these investments across the strategic axes and growth sectors respectively.

3.1 Growth has been low, largely due to a narrow economic base

86. **Growth in Guinea-Bissau has been low, especially when compared to the economic performance of the region (Figure 3.1).** Real activities expanded at an annual average rate of 0.4 percent per year in per capita terms between 2000 and 2014, significantly below the average 1.9 percent recorded for the Sub-Saharan region during the same period. This occurred in the context of extreme political instability, and recovery from these disruptions has often been slow. More recently, in 2010 and 2011, stronger and positive growth was recorded (2.1 percent and 6.5 percent, respectively), influenced by a sharp rise in the global price for cashews (as a consequence of the global commodity disruption in supplies from Cote d’Ivoire due to civil war). This stability was, however, short-lived as a result of the major coup in 2012, which was followed by other bouts of instability in 2015 and 2016. Growth turned negative to -1.8 percent in 2012 before gradually recovering to approximately 5 percent in 2015 from 2.9 percent and 0.8 percent in 2014 and 2013, respectively.

Figure 3.1. Guinea-Bissau has a history of low economic growth...



Note: Annualized GDP growth rate 2000-2014 for Sub-Saharan African countries – constant 2005 US Dollars
Source: World Development Indicators (WDI)

87. **In per capita terms, Guinea-Bissau has also fallen behind many of its peers.** Comparing Guinea-Bissau with its closest 19 African peers in per capita GDP in 1990 shows that the country has lost ground. Between 1990 and 2014, Guinea-Bissau's real per capita GDP declined by 12.3 percent falling from 10th to 18th in this group of 20 countries (see Table 3.1). Notably, only Congo and Central African Republic performed worse than Guinea-Bissau. Neighbors, Senegal and Guinea-Conakry, not included in the list of twenty closest peer countries in per capita terms, both recorded growth in income over the period.

Table 3.1. Real per capita GDP in Guinea-Bissau and its peers, 1990-2014

	1990		2014	% change
1 Zimbabwe	677	1 Equatorial Guinea	12272	3038.4
2 Comoros	670	2 Nigeria	1098	86.1
3 Mauritania	658	3 Zambia	1033	60.7
4 Zambia	643	4 Lesotho	988	93.5
5 Nigeria	590	5 Sudan	973	121.4
6 Kenya	555	6 Mauritania	877	33.3
7 Lesotho	511	7 Chad	766	87.5
8 Congo, Dem. Rep.	505	8 Ghana	764	102.9
9 Benin	505	9 Benin	671	33.0
10 Guinea-Bissau	479	10 Kenya	659	18.6
11 Sudan	439	11 Comoros	597	-11.0
12 Togo	426	12 Tanzania	588	64.4
13 Gambia, The	425	13 Sierra Leone	513	36.4
14 Chad	409	14 Mali	458	39.2
15 Equatorial Guinea	391	15 Zimbabwe	458	-32.3
16 Ghana	377	16 Gambia, The	446	5.0
17 Sierra Leone	376	17 Togo	430	1.0
18 Central African Republic	374	18 Guinea-Bissau	420	-12.3
19 Tanzania	358	19 Congo, Dem. Rep.	283	-43.9
20 Mali	329	20 Central African Republic	226	-39.4

Source: World Development Indicators (WDI)

88. **The structure of the economy has barely changed over the last two decades, contrary to developments in broader Sub-Saharan Africa (see the comparison between Guinea-Bissau and Cabo Verde in Box 3.2).** A breakdown of the Guinean output shows that the composition across sectors has remained fairly constant between 1987 and 2013. The contribution of agriculture to total value added has oscillated about 43 percent. Industries contribute 16 percent of GDP, while services make up roughly 41 percent. This is a contrast to the Sub-Saharan African average where both service and industry account for the major part of GDP, and where agriculture, though important, has a relatively small share. The share of services has progressively increased in the region from 45 to 58 percent, whereas the role of agriculture declined from 20.5 percent and 14.5

percent.²¹ In contrast, this shift from the primary to the tertiary sector is not observed in Guinea-Bissau. The service sector is concentrated in Bissau and is mostly informal. Almost 76 percent of workers in the capital are engaged in informal businesses, such as the sales of handicrafts and other street vendor items, and in restaurants and hotels.

89. **Guinea-Bissau's economy is largely agrarian.** Production in the country is closely linked to the products of the soil, which is dominated by cashew cultivation but which also includes a few other activities, such as small scale rice production and horticulture. It is estimated that the country produces about 200,000 metric tons of cashew nuts per year. Agriculture is mostly a family activity, a large portion of it which is unpaid due to alternatives such as subsistence or bartering. About 80 percent of workers are employed in the sector, most with low levels of human capital. Virtually all small farmers are engaged in growing at least some cashew, underscoring the tight connection between incomes and movements in farm gate prices or production levels, especially for the poor. A small proportion of cashew nuts is consumed domestically and there is also limited processing of cashew apples into juice and wine for domestic consumption. Given the high dependence on cashew nuts, Guinea-Bissau's economy is largely undiversified and, hence, highly vulnerable to demand, supply and price shocks (Figure 3.2).

90. **The dominance of cashews is also evident in the balance of payments.** Guinea-Bissau is a relatively open economy with exports and imports approximating 70 percent of GDP. Unprocessed cashew nuts are also the main export, accounting for 85 to 99 percent of the country's total exports (see Figure 3.3.). While almost all unprocessed cashews are exported through the port of Bissau, a part of the production is smuggled through Senegal and the Gambia. The country's main market for its cashew nuts is India, where the raw nuts are further processed for local consumption and re-exported to Asian and other developed countries.²² Other sources of external earnings are remittances (an estimated 7–8 percent of GDP in recent years) and donor flows. The main imports are fuel and food—the two items being equivalent to about 60 percent of total imports. However, this share has fluctuated in recent years due to variation in world prices for both oil and grains, among other reasons. Foreign Direct Investment (FDI) has been relatively low, at about 2 percent of GDP over the past 10 years.

²¹ Economic performance of other sectors have been modestly satisfactory but they make up for a small fraction of the economy. Of the 16 economic subsectors, construction (20 percent), mining (20 percent) and financial services (17 percent) were the fastest growing between 2007 and 2013. However, these three sectors combined account for less than 5 percent of GDP. The most important sectors - agriculture and wholesale/retail trade - grew at annual average rates of 3 percent and 4 percent, respectively.

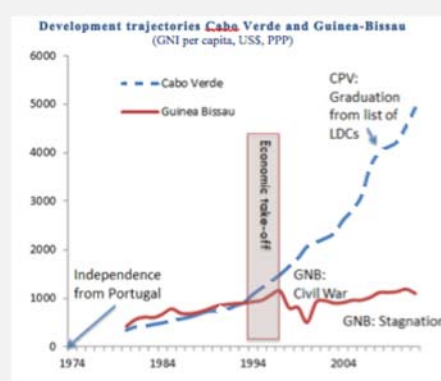
²² The recent CEM also confirms that the country has a large fishing sector though fish exports do not show up in the official export statistics. EU vessels have fishing rights in Guinea-Bissau, paid for under an EU fisheries agreement, with receipts classified as a transfer in balance of payments statistics, and a government revenue.

Box 3.2. Economic Growth in Guinea-Bissau and Cabo Verde

The Portuguese colonies of Guinea-Bissau and Cabo Verde achieved independence in 1974, following a liberation struggle that lasted almost 20 years. The path to independence is often described as having been one of the longest and bloodiest on the continent. Following a military coup in 1981, which saw Luís Cabral—an ethnic Cabo Verdean—being deposed from the presidency, Guinea-Bissau and Cabo Verde separated and went down independent development paths. Starting out at roughly equal levels of gross national income (GNI) per capita (in purchasing power parity [PPP] terms), Cabo Verde has grown rapidly, graduating from the United Nations (UN) list of Least-Developed Countries (LDCs) in 2007 and now enjoys income levels four times that of Guinea-Bissau. Guinea-Bissau, however, remains one of the poorest countries in the world, with a GNI per capita of US\$ 590 (Atlas method).

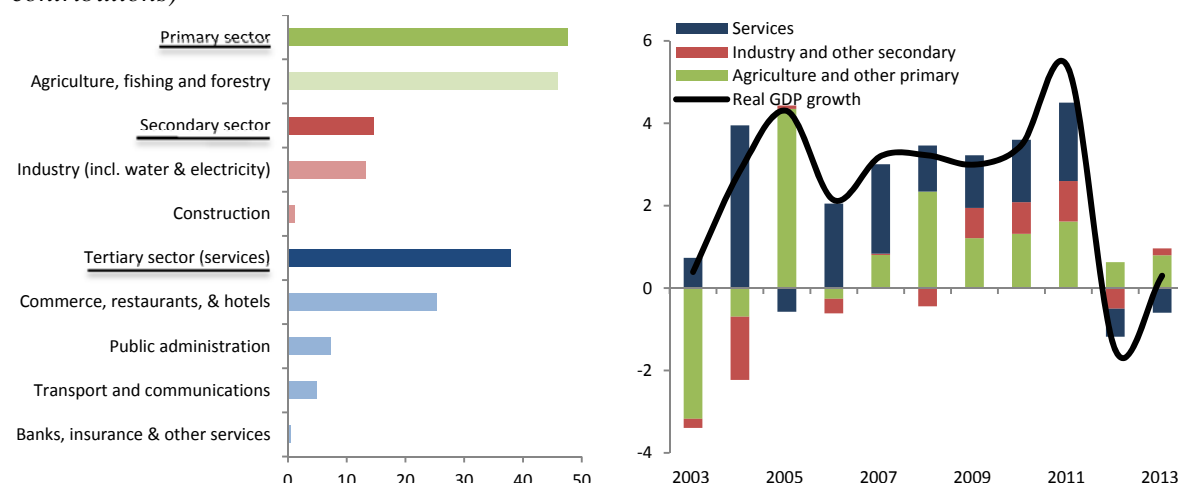
The difference in the growth outturn between both countries has been largely attributed to the interruptions caused by frequent coups and other political upheavals in Guinea-Bissau. Both Cabo Verde and Guinea-Bissau embarked on a process of democratic transition in the 1990s which gave birth to a period of growth. In Guinea-Bissau, however, growth came to a sudden halt in 1998 when civil war erupted. Although peace returned in 1999, economic dynamism did not, and fragility continued to mark the Guinean landscape. A period of relative calm began after the assassination of Guinean strongman Nino Vieira in 2009. In spite of occasional incidents in the wake of this event, the country experienced a rare period of stability and economic resurgence. But another intervention by the army during the run-off of presidential elections in April 2012 stifled optimism yet again and derailed a hopeful period of cautious progress.

Another important explanation for the divergence in growth performance relates to the fact that unlike Guinea-Bissau, Cabo Verde had better organized institutional and policy frameworks which made it possible for the country to capitalize on early incentives to promote Foreign Direct Investment (FDI). Investments in human capital created a better-educated workforce, which afforded Cabo Verde a literacy rate of 62 percent at the time of its independence, the region's highest. In this context, the country was generally better prepared to meet the challenges of independence, and thus enjoyed more favorable growth prospects.



91. **Trade with regional neighbors is almost non-existent in spite of its advantageous position, pointing to medium- and long-run benefits of investment in infrastructure.** Many of Guinea-Bissau's neighbors are landlocked, requiring good roads and, where possible, rail networks in linking these countries to both regional and global markets. Cashew is also produced in some of the neighboring countries, although on a more limited scale. Non-tariff barriers associated with the high transactions costs hinders progress. These costs are due to inadequate transport infrastructure, inefficiencies in customs procedures, and poor quality and costly logistics deriving from weak competition among service providers. The existing road network, the primary, basic artery of economic activity, is very deficient, particularly feeder roads which stem from main roads connecting producers with processors and other markets.

Figure 3.2: The primary sector is large in Guinea-Bissau... **Figure 3.3:** A major driver of economic growth
(Percent of nominal GDP at factor prices in 2013) (Real GDP growth and its sectoral contributions)



Note: Contributions to GDP (bars) at factor prices; real GDP growth (line) at market prices. Difference is due to indirect taxation.

Source: CEM 2015.

92. **The potential for agriculture to contribute to output growth and economic prosperity in Guinea-Bissau is constrained by several bottlenecks.** Productivity in the sector remains weak. For instance, yields for rice (about 1.7T/ha) and millet and sorghum (0.8T/ha) are well below the standards for countries with similar agro-climatic conditions. Major constraints limiting the use of the existing agricultural potential, include: (1) unclear land rights and poor land management systems; (2) lack of hydro-agricultural developments; (3) limited access to inputs and technologies to support production; (4) inadequate investment in R&D and extension; (5) underdeveloped agribusiness value chains with low ratios of food processing to primary agriculture due to poor infrastructure (logistics, energy, storage, and so forth), (6) a lack of finance for agriculture; and (7) an unpredictable policy environment and a dearth of market information. The deteriorated state of rural road networks and the lack of a sufficient power supply network increases costs for farmers and agro-business, lowering their productivity and competitiveness. Political instability has also slowed agri-processing investments.²³ In this context, Guinea-Bissau is weakly integrated into regional and global agricultural value chains, in particular due to an unfavorable business environment and a lack of infrastructure to support production and trade.

93. **The high reliance on agriculture also translates into very little economic diversification and concentration in low value-added sectors.** The structure of the economy in Guinea-Bissau is very basic. In addition to cashew output, most of Guinean products are concentrated in the first rung of the value ladder. Almost all of Guinean exports serve as raw inputs to more sophisticated value chains in other countries. This limits the ability of the economy to diversify into other products and to create forward and backward linkages with other sectors. Cashew is the best example of a raw material with considerable potential to add value through processing (see discussion of potential growth factors for Guinea-Bissau in Box 3.3).

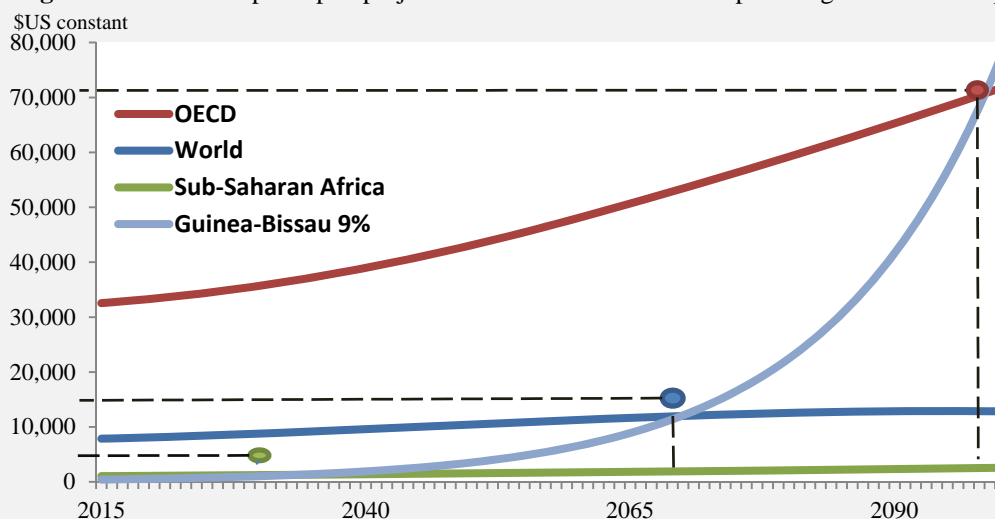
²³ There are only a few isolated cases of foreign investors, mainly involved in rice cultivation (production and processing) and in horticulture in the Bafatá region.

Box 3.3. How much does Guinea-Bissau have to grow to catch up with the world?

Guinea-Bissau continues to lag behind global growth and GDP per capita levels, as well as those of Sub-Saharan Africa. A considerable growth spurt will be required to catch up. GDP per capita in Guinea-Bissau stood at just under US\$570, compared to US\$1,057 for all of Sub-Saharan Africa, US\$7,857 for the world and almost US\$32,400 in the best regional performer — the Organization for Economic Co-Operation and Development (OECD) economies. Even if Guinea-Bissau grew by 9 percent on average, as assumed in the government's development strategy, it would take the country over 50 years to catch up with the rest of the world. Box Figure B3.3.1 uses UN population projections and assumes historical GDP growth for Sub-Saharan Africa, the world average, and OECD, the club of the world's richest economies. Even when growing at such a breakneck pace, it would take Guinea-Bissau 16 years to catch up with the 2014 GDP per capita of Sub-Saharan Africa; in the same vein, it would take 48 years to catch up with the world and 71 years to catch up with the OECD. Assuming that these other regions continue to grow at their average growth rates, it will take even longer to catch up: 22 years with Sub-Saharan Africa, 53 years with the world, and 76 years with the OECD.

More conservative growth estimates for Guinea-Bissau increase the amount of time necessary to catch up with comparator regions and the world average. If Guinea-Bissau continues to grow at its historical average of about 3 percent per annum, it would take the country 187 years to catch up with Sub-Saharan African GDP per capita of 2014, and 262 years assuming historical growth in the region. Catching up with the world or the OECD would virtually be impossible. Assuming a more realistic 5 percent average growth rate, Guinea-Bissau could catch up with Sub-Saharan Africa in 55 years; yet it would still take over 100 years to catch up with the world.

Box Figure B3.3.1: GDP per capita projections for Guinea-Bissau at 9 percent growth and comparators



Source: UN World Population Prospects: The 2012 Revision, World Development Indicators (WDI), and World Bank staff calculations.

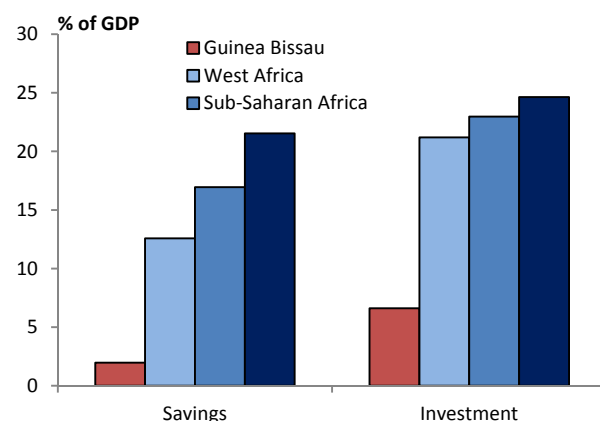
3.2 Low productivity, savings and investments also underpin slow growth

94. **Low GDP per capita is largely a consequence of weak growth in labor productivity.** Between 2000 and 2014, average GDP growth of 3 percent per annum exceeded population growth by a mere 0.4 percentage points, resulting in low average GDP per capita growth of 0.4 percent.

About half of GDP per capita growth can be attributed to demographic change, where the population of working age grew faster than the population as a whole (a so-called ‘demographic dividend’). This suggests that labor productivity grew no faster than 0.4 percent on average during that period.

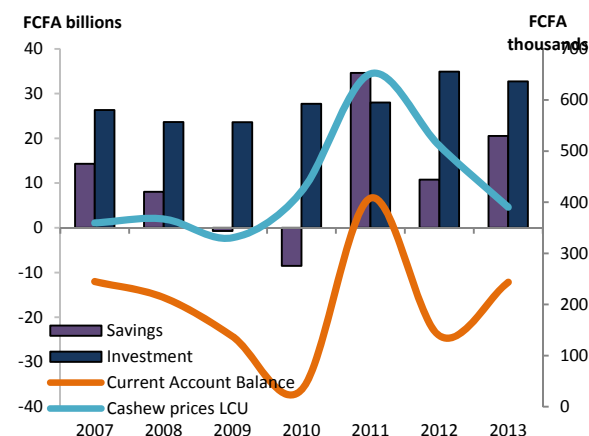
Figure 3.4: Both savings and investments are low in Guinea-Bissau

(Savings and investment in percent of GDP, 2004-2013 average)



Source: IMF, World Economic Outlook, April 2015.

Figure 3.5: The cashew prices is an important determinant of the current account balance, savings, and investment
(Savings, investment, current account balance and cashew prices in local currency (RHS))



Source: INEC, IMF, and World Bank.

Note: 1) The current account balance equals savings minus investment. 2) Investment in 2012 and 2013 was significantly driven by the build-up of inventories.

Source: WDI, 2015

95. **Weak labor productivity, in turn, is driven by low levels of savings and investment, even by regional standards.** Cross-country regressions show that savings are positively associated with productivity growth, especially in poor countries (Aghion, et al. 2009). Yet, at 1.9 and 6.6 percent of GDP, respectively, savings and investment in Guinea-Bissau are significantly low and many times less than the rates observed in West Africa and Sub-Saharan Africa (Figure 3.4). Savings are closely linked to the cashew price, the main driver of the economy, external trade, and in turn the country’s current account. Strong cashew prices tend to improve the trade balance and translate into higher national savings (Figure 3.5). With the exception of the global commodity price boom in 2010 and 2011, the cashew price has been falling in real terms. These adverse price developments can partly explain low savings in Guinea-Bissau. Low savings, in turn, translate into feeble domestic investment, especially given an underdeveloped financial sector that limits financial intermediation. About 40 percent of domestic investment is government-financed, almost exclusively with donor support. Foreign Direct Investment (FDI) is miniscule, not least as a consequence of political instability but also due to high unit labor costs and an unfavorable business climate.²⁴

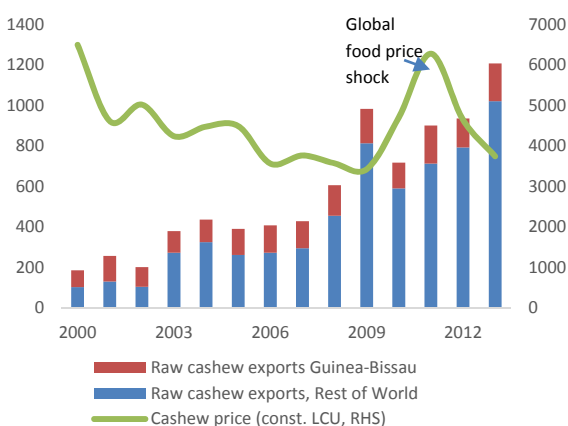
²⁴2015 CEM, Chapter 3.

3.3 Economic growth is fragile

96. **Given the narrow economic base, the economy is vulnerable to incidences of trade shocks, particularly negative shocks to cashew prices.** Between 2000 and 2013, global raw cashew exports rose six-fold (Figure 3.6). As supply expanded, the price of the commodity fell. Indeed, with the exception of 2011, cashew prices have been trailing general global food prices more broadly. Weaker cashew prices have been worsening the terms of trade, especially given the country's high reliance on rice imports. Rice is Guinea-Bissau's main staple food and families barter it for cashew. Although Guinea-Bissau cultivated rice for export in the distant past, it is now mostly grown on a subsistence basis. Yet given falling real cashew prices and somewhat increasing rice prices, the ratio of cashew to rice prices—the most meaningful interpretation of the terms of trade in Guinea-Bissau—has fallen (Figure 3.7). Falling cashew prices and rising rice prices are reinforcing shocks to the poor, undermining income from their main, monetized economic activity while eroding their purchasing power.

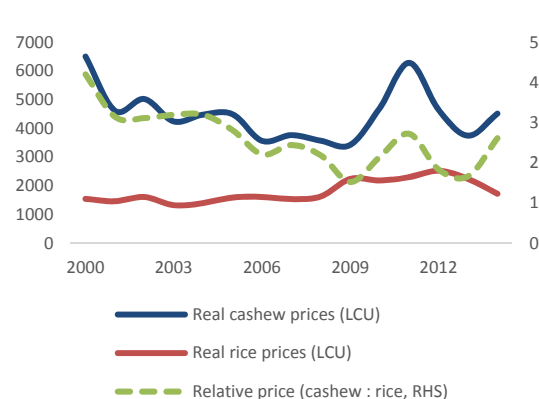
97. **Political instability has been continuously hampering economic growth, making efforts to capitalize on periods of stability critical for poverty reduction.** There is ample evidence showing that economic growth is lower in countries with a high propensity of government collapse through lower rates of productivity growth and physical and human capital accumulation (Aisen and Veiga, 2010, Jong-a-Pin 2009, Alesina and Perotti 1996 and Barro 1991). As shown in Figure 1.1, this is the case in Guinea-Bissau, where growth rates systematically fall following instances of political instability. In the most recent Article IV assessment (July 2015), the IMF estimates that Guinea-Bissau's GDP per capita could have been 65-90 percent higher had it not been for fragility. The uncertainty associated with political instability increases risk aversion of local entrepreneurs and foreign investors alike, and pushes donors to withdraw their support. For this reason, sustained periods of constitutional order provide important opportunities, which should be used to attract investments and bolster economic growth.

Figure 3.6: The international cashew price has been falling as global cashew exports increased. (Cashew exports in thousand tons, cashew price in constant local currency (RHS))



Source: COMTRADE, IMF, and World Bank staff calculations, (2000 -2013).

Figure 3.7: Guinea-Bissau's terms of trade have been deteriorating throughout the 2000s (Rice and cashew prices in constant local currency, cashew to rice price ratio (RHS))



Source: World Bank (Prospects Group). Note: Rice price is chosen for lower quality rice ('Thai 25 percent'), 2013.

98. **The latest coup in 2012 provides examples of the high economic cost of political instability.** The favorable cashew campaigns in 2012 and 2013 were overshadowed by mismanagement of the military-backed government, aggravating income losses to farmers and domestic traders from a large global drop in cashew prices. Smuggling increased as border controls softened and corruption spread, further undermining fiscal discipline. Plundering of natural resources, especially timber, and embezzled resources from fishing licenses, reduced national wealth. In addition, the immediate suspension of donor programs in response to the coup meant that external financing dried up. Public investment ground to a halt, current expenditures had to be cut, and arrears increased. This resulted in widespread strikes, the disruption of education and health services, and increasing public health concerns as both electricity and running water in Bissau experienced severe outages. The economy contracted by 1.8 percent in 2012 and barely recovered in 2013, growing at only 0.8 percent. In response, nonperforming loans in the banking sector soared, leaving some commercial banks with a need to recapitalize. The World Food Program estimates that food insecurity also doubled from 20 to 40 percent between 2011 and 2013.

99. **More recently, the macroeconomic policy agenda in Guinea-Bissau has been broadly tied to an IMF program aimed at addressing balance of payments and other macroeconomic imbalances.** The Government's program has been geared toward consolidating the fiscal position through efforts to boost revenue mobilization while improving expenditure management, the impact of which has been seen in 2014 (see Annex 3A). This is being addressed through initiatives to deepen institutional reforms - strengthening budgetary transparency as well as public investment and debt management. The thrust of the program is consistent with the findings of an IMF paper which suggest relatively high returns from focusing on building sound fiscal institutions in fragile states. In particular, the paper found that improving fiscal institutions and boosting fiscal space, through raising tax revenue and containing current spending, as well as lower military spending and, to some extent, higher social expenditure, are significantly and fairly robustly associated with building resilience.²⁵ The IMF program is ongoing but suffered significant setbacks in the context of political instability.

100. **One source of macroeconomic stability is WAEMU membership, which has kept inflation low; nonetheless it still leaves addressing idiosyncratic shocks to fiscal policy.** WAEMU membership means that monetary policy in Guinea-Bissau is governed by a competent, independent central bank, BCEAO, which is largely insulated from the country's fragility. It has succeeded in keeping inflation low. Yet, as in any currency union, giving up monetary autonomy limits the ability of monetary policy to help absorb country specific shocks. Empirical evidence suggests that shocks to WAEMU member countries tend to be idiosyncratic and the BCEAO thus cannot respond to individual country needs adequately, potentially at the expense of other WAEMU member states.²⁶ While there are obvious advantages to Guinea-Bissau retaining its membership in WAEMU, shock absorption will largely have to be shouldered by fiscal policy, which itself suffers from multiple constraints, as further explained below.

²⁵ See IMF Working Paper, "Exiting from fragility in sub-Saharan Africa: The role of fiscal policies and fiscal institutions". <http://www.imf.org/external/pubs/ft/wp/2015/wp15268.pdf>.

²⁶ Xiaodan Zhao and Yoonbai Kim (2009) 'Is the CFA Franc Zone an Optimum Currency Area?' *World Development* 37(12)1877-1886.

3.4 Structural weaknesses constrain the effectiveness and equity of fiscal policy

101. **Overall, public resources are low and variable.** Tax revenues to GDP in Guinea-Bissau, which are at about 10 percent, are among the lowest in the region, while the average for Sub-Saharan Africa is about 18 percent. Public revenues have traditionally been supplemented by donor grants, raising total general government revenue to about 15 percent of GDP (Figure 3.8). Akin to the broader economy, the fiscal accounts are highly vulnerable to incidences of trade shocks as a result of their high reliance on cashew taxes (about 15 percent of revenue). They are also vulnerable to political shocks and decisions on foreign aid. When donors collectively suspended their programs in response to the military coup in 2012, the public investment program collapsed. In addition, domestic revenue collections fell, current expenditures had to be cut sharply, and wage arrears increased.

102. **In terms of tax incidence, Guinea-Bissau's reliance on taxes from cashew exports means that the poor bear a considerable share of the tax burden.** Taxes on international trade in Guinea-Bissau are unusually high by global comparison with the cashew sector most affected (Figure 3.9). This, in part, stems from the prominence of the sector, as well as, the fact that most of the cashew produced is exported, thereby, making collections at the port very easy. Cashew farmers bear the brunt of the cashew tax burden—highlighting the regressive structure of public revenue generation. Cashew taxes are set at about 11 percent of the government's reference price for exports. Simulation analysis indicates that cashew farmers, mostly poor, absorb about 80 percent of the tax, while exporters absorb 13 percent and traders take up the remaining 7 percent. This translates into a reduction of nearly 12 percent in the incomes of the farmers.²⁷ Indirect taxation is distortionary as the main tax (Tax on General Sales) is cumulative and the tax basis is concentrated on a few formal activities in urban areas. The dependence on trade taxes could negatively affect the country's competitiveness. Income taxation is very limited due to precarious tax administration capacities. Corporate taxes are collected on presumed profits and its tax base is very small. Property taxes are almost nonexistent and are regulated by legislation dated back in 1920 and 1966. A reform of tax administration has been ongoing for one year (including refurbishment of the offices, excess unqualified staff made redundant, and recruitment of skilled new staff).

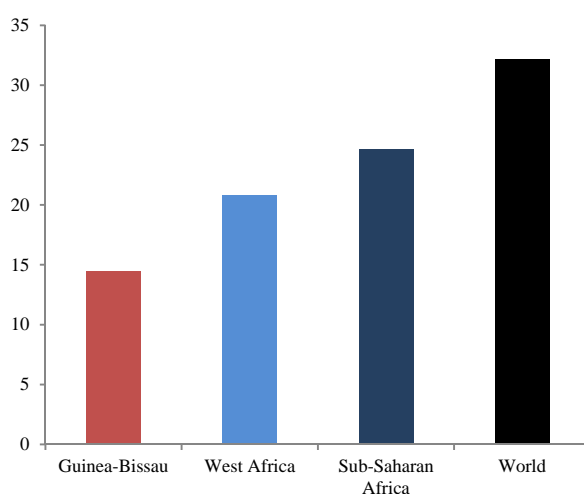
103. **Capital expenditure is dependent on donor financing, and there is limited capacity for project appraisal.** Almost all of Guinea-Bissau's capital expenditure is financed by donors. Public investment can be significant, up to 7 percent of GDP in good years, as was the case in 2011. However, donor financing is pro-cyclical as it tends to dry up and aggravate recessions during episodes of political turmoil. Frequent interruptions in public investment threaten the quality of investments, as do the shifting priorities of frequently changing governments. The quality of public investment is further undermined by weak project appraisal systems. This means that—especially given its limited resources—Guinea-Bissau is ill-positioned to identify the areas where public investment would yield the 'biggest bang for the buck', that is be truly transformative to enable growth and poverty reduction. This leaves considerable room for spending preferences

²⁷ See Walter Cont and Guido Porto, "Measuring the Impact of a Change in the Price of Cashew Received by Exporters on Farmgate Prices and Poverty in Guinea-Bissau", World Bank Policy Research Working Paper, N. 7036, September 2014.

for the incumbent government, which as explained further below, are often motivated more by clientelist loyalties rather than national welfare.

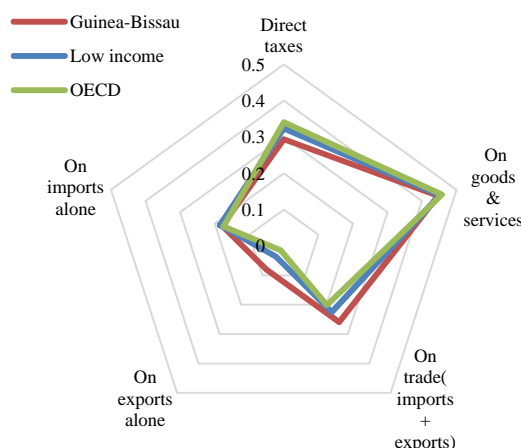
104. **Current spending is not well allocated across areas, with significant amounts spent on public sector workers and the army.** As the 2015 CEM illustrates, there are many inefficiencies in the Guinean civil service. Some areas are overstaffed (such as the military or customs), while others are understaffed (such as health and education). The armed forces and paramilitaries account for over a quarter of public employment, which is large by regional standards (Figure 3.10). Given the need to prioritize payments to soldiers to acquiesce the military, arrears are often accumulated in other sectors. Although the World Bank has supported the payment of teachers and health workers during the transition period after the military coup, strikes remain commonplace—as teachers claimed outstanding payments from previous years. However, even in education spending, there are signs of unions influencing public expenditures. In 2015, the Ministry of Education agreed to lower the number of hours taught per week from 32 to 24, and also to hire additional teachers in spite of shorter school days.

Figure 3.8: Fiscal space is severely limited in Guinea-Bissau
(General government revenue in percent of GDP, 2013)



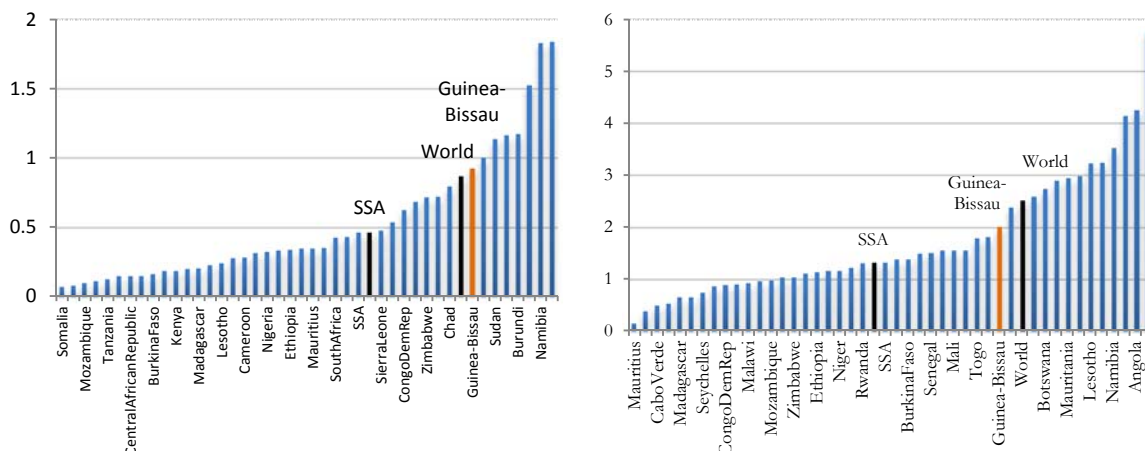
Source: 2015 CEM.

Figure 3.9: Guinea-Bissau strongly relies on export taxes for domestic revenue
(Shares of revenue as fraction of total domestic revenue)



Source: World Bank staff based on ECOPA report.

Figure 3.10 The size of the military is excessive by regional standards
 (Armed forces personnel [percent total labor force]) (Military expenditure [percent of GDP])



Source: World Development Indicators (2008-2012).

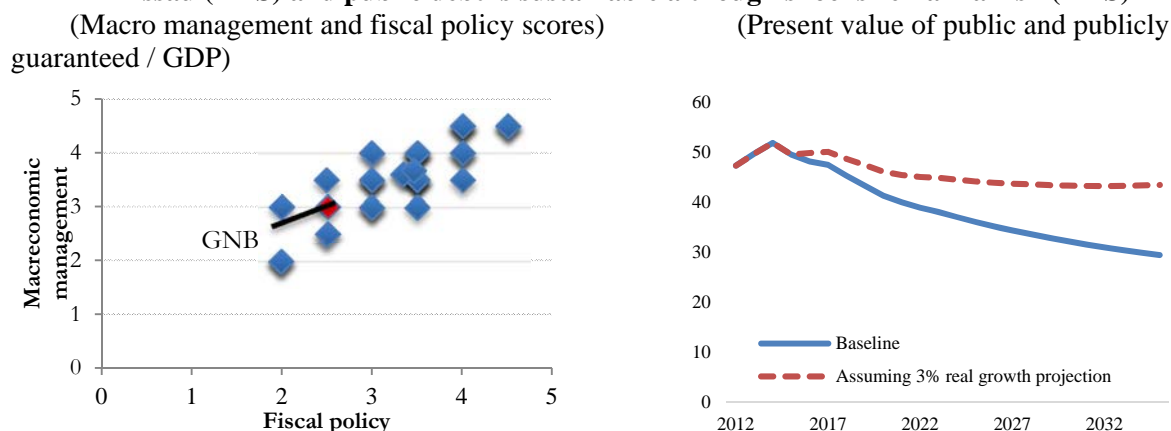
105. **Efficiency and quality of public expenditures in Guinea-Bissau are undermined by an incomplete and weak public financial management (PFM) framework.** A weak PFM system creates opportunities for the elites to extract rents from critical public resources. This is particularly damaging considering that fiscal revenue is already low, leaving even fewer resources for spending, and constraining the stability dimension of fiscal policy (Figure 3.12). The latest Public Expenditure and Financial Accountability (PEFA) report notes that some improvements on PFM strengthening undertaken between 2009 and 2010 had been reversed in the aftermath of the 2012 military coup. Guinea-Bissau has committed to the 2009 WAEMU PFM directives, but they have yet to be implemented.²⁸ A sign of progress toward better and more transparent budget execution was the government's establishment of a Treasury Committee under the Simoes Pereira's regime, which was convened relatively regularly (see 2015 CEM).

106. **Expected inflows of US\$1.5 billion in donor resources pledged over the next five years is as much a risk as it is an opportunity for fiscal policy.** These risks are both political and economic in nature (see Box 3.4 on the 2015 Brussels Donor Roundtable). Politically, the large influx of resources can further increase rent seeking, especially in a fragile state like Guinea-Bissau. Moreover, the population has high hopes of seeing results from this inflow of resources, increasing the risk that spending may be oriented toward short-term initiatives, rather than carefully identifying transformative investments that may only yield results in the future. This also represents an opportunity for the population to push for greater transparency in public spending. On the economic front, about 60 percent of the pledged resources are loans which will need to be serviced. The International Development Association (IDA)-IMF Debt Sustainability Analysis assumes economic annual growth rates of 5 percent per annum—in line with the government's baseline scenario and significantly below the government's optimistic scenario of 9 percent. Total public debt is currently projected to fall from its current relatively high level of about 50 percent

²⁸ This would involve the following: (1) improving the reliability and timeliness of macroeconomic forecasts for better annual and multi-year budgeting; (2) setting budget and financial controls to improve budget preparation, commitment management, control and accounting, as well as timely and accurate budget execution reports; and (3) improving payment management and controls, more timely and reliable in-year financial execution reports and their reconciliation with the budget execution reports published by the Directorate of the Budget.

of GDP—whereas lower growth would maintain public debt at relatively high levels (Figure 3.11). This would reduce fiscal space and thus limit the government’s ability to deliver important public goods and respond to shocks.

Figure 3.11. Fiscal and macroeconomic management performance are relatively weak in Guinea-Bissau (LHS) and public debt is sustainable although shocks remain a risk (RHS)



Source: LHS—World Bank Country Policy and Institutional Assessment (2008-2012); RHS—World Bank staff calculations based on IDA-IMF Debt Sustainability Analysis for Guinea-Bissau, 2015.

Box 3.4. The 2015 Brussels Donor Roundtable

The new government together with its international partners arranged a donor roundtable on March 25, 2015, in Brussels to mobilize international support for its development priorities. Guinea-Bissau’s international partners include international organizations, such as the WBG, UN, European Union (EU), AU, ECOWAS, AfDB, West African Development Bank (WADB), and Community of Portuguese Language Countries (CPLP), and also bilateral donors, such as the USA, Portugal, Brazil, Cabo Verde, East Timor, Guinea, UK, France, Spain, Canada and China.

The government’s strategic and operational plan (*Strategy Development Plan*) for 2015-2020 foresees over US\$560 million to invest in more than 200 development projects. The international community pledged to support the government with US\$1.5 billion, committed by WADB (US\$340 million.), UN (US\$300 million), WBG (US\$250 million), EU (US\$160 million), AfDB (US\$128 million), Portugal (US\$45 million), and other donors, although it remains unclear exactly how much of the pledges are for new activities and how much had already been committed beforehand.

3.5 An underdeveloped private sector and multiple supply-side constraints hinder actual and potential output

107. **The private sector in Guinea-Bissau is underdeveloped, and faces several challenges.** The economy is largely informal and is reliant on natural resources, principally agriculture and fisheries, with a considerable degree of subsistence farming and low productivity. Of the 30 percent of the labor force not engaged in agriculture, the majority is in services, mostly self-employed in commerce and transport. Only one in ten workers is in wage employment, half in small urban services, and half in the public sector. The private sector depends heavily on the public sector’s consumption and investments due to a small domestic market, and very few export-

oriented sectors. This form of economic structure discourages entrepreneurs from pursuing economic opportunities and from making investments that could create firms and generate jobs, resulting in little economic diversification. At the end of 2014, the taxpayer's registry included only 3,243 businesses, including individual entrepreneurs, although one third of those were classified as "inactive". The challenges to private sector development are considerable and range from poor infrastructure and a poor business and regulatory environment, to limited access to finance, low productivity, and relatively high labor costs and political instability.

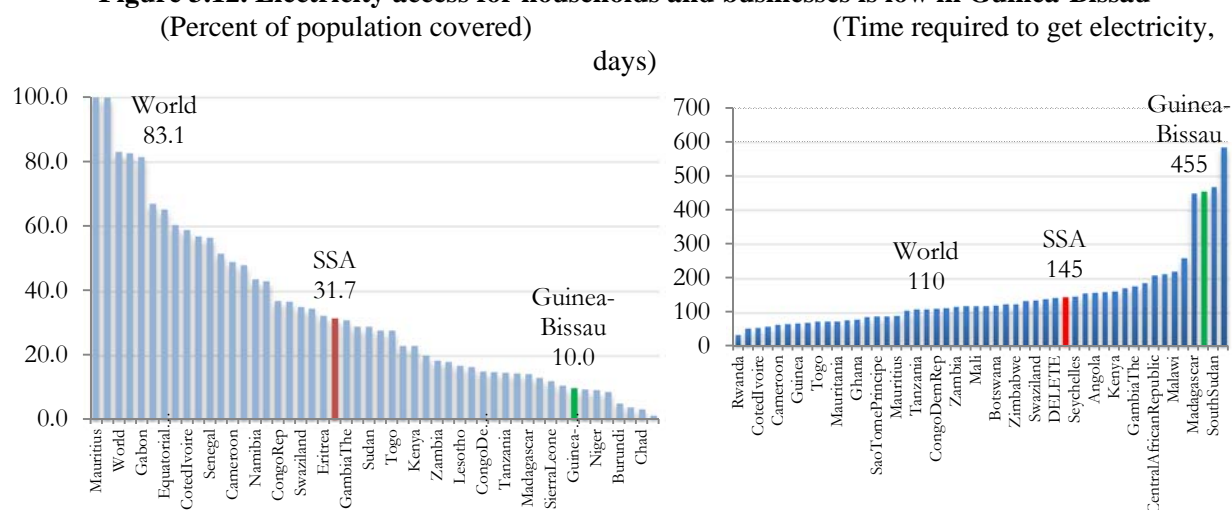
Poor infrastructure

108. The functioning of markets is undermined by the absence of public investments in fundamental economic services. Guinea-Bissau's infrastructure is in a woeful state, from the port to roads, to access to electricity, potable water, or the Internet.²⁹ The failure of Guinea-Bissau over several decades to provide these key public goods and services, either through direct public investments or through effective public-private partnerships, severely limits the ability of poor households to participate in economic activity, both through more productive autonomous activities, or through accessing employment opportunities that could be generated by a thriving private sector. Poor infrastructure also limits connectivity to markets, effectively reducing the scope and incentives for expansion of income-generating opportunities. Households often use cashew in bartering for rice or other staples, effectively reducing the scope for trading for both agricultural and other non-agricultural products with money, and lowering the returns and incentives to enter retail and services. This is particularly common in rural areas. Hence fostering better connections across the country can boost incomes by expanding economic activities and opening up the scope of local trade.

109. Under-provision of energy, due largely to weak governance in the sector, poses a critical constraint to the productivity of the economy, job creation, and household welfare. There is a severe electricity shortage, reducing most activities both for companies and households. ILAP data indicate that only about 6 percent of Bissau Guinean households have access to electricity -- primarily urban households in the higher consumption quintile. Other estimates place access to electricity at about 10 percent, one of the lowest in the world (Figure 3.12). Abysmally low coverage, especially in rural areas, obliges high outlays for alternative self-generated electricity, reducing most activities for both households and enterprises. Absence of, or high costs for, electricity also bars households from acquiring other physical --and welfare enhancing-- assets such as electrical stoves or cold storage. It takes on average 455 days for new businesses to get connected to the grid, almost three times longer than the regional average. The economic cost of these failures in electricity is very high -- pushing up production costs and ultimately dissuading investment and reducing competitiveness.

²⁹ See the 2015 CEM for a detailed analysis of the state of infrastructure in Guinea- Bissau

Figure 3.12. Electricity access for households and businesses is low in Guinea-Bissau



Source: World Development Indicators (2008-2012).

110. **The lack of generation capacity and the unreliability of power supply have technical, commercial, financial, institutional, and ultimately, policy roots.** The power system is well below the capacity needed. The level of technical and commercial losses is extremely high, having recently been estimated to occur with about 52 percent on average of energy produced. In the residential sector, losses could be as high as 60 percent. Non-payment, especially due to an ineffective billing system, is estimated to be high, and occurs among both public and private consumers. The prolonged electricity crisis and a decade of ineffective remedial measures have led to a vicious cycle of regular blackouts, overstaffing and high operating costs, poor billing and revenue collection, high incidence of electricity theft through illegal connections, and high retail tariffs in an (ultimately unsuccessful) attempt to cover these inefficiencies. Adding to the problem is the participation of public officials in theft of gasoil/diesel (for power generation) for resale, and for use in private cars and trucks. The sector imposes a significant fiscal burden through direct and indirect subsidies.

111. **A second key infrastructure constraint centers on the port of Bissau, which imposes high transaction costs on cashew and other (actual and potential) exports as well as on imports of key commodities such as rice.** In principle, Guinea-Bissau's position as a coastal country on the Atlantic Ocean should be an important asset, enabling the country to derive trade benefits from direct access to the Atlantic and proximity to the main shipping lanes linking the American and European continents. As a result, its port system could play a key role in the overall competitiveness of its economy. The port of Bissau is the country's main port, and it handles more than 85 percent of Bissau's recorded international trade, and is the window to the world for Guinea-Bissau's main export: cashew. At the present time, however, the port of Bissau is in a woeful state with a large number of deficiencies, including in critical areas such as maritime access, surfaces, warehousing, port buildings, and other infrastructure systems. Moreover, a number of shipwrecks are significantly hindering port operations. As a result, port costs are markedly high. The structure of terminal handling charges shows tariffs to be up to ten times higher than in other ports of the region, including those that are becoming competitors to the port of Bissau (for instance Dakar and Banjul) for trade into Guinea-Bissau and neighboring countries.

112. **Like most of the public goods in Guinea-Bissau, the port suffers from a host of managerial corporate governance problems and a poor regulatory context that impact not only the port's operational performance but also its financial viability.** The Guinea-Bissau Port Authority (APGB) must contend with both redundant and unqualified personnel, and there is no master port planning or port investment strategy to guide its efforts. More importantly, it is currently functioning outside a clear legal and regulatory framework and under an inadequate institutional arrangement. The existing framework, however, is all but simple, involving a large number of entities and reporting relations, and creating a complex web of stakeholder interests in the reform of the port. Failed concessions in the past, which were largely due to the unsettled institutional arrangement of APGB, the lack of progress on the reform front, political instability, and vested interests of the elite, have discouraged private investment in the port. Nevertheless, given that the port of Bissau is the only one in the country and is likely to remain a key piece in the country's infrastructure, addressing these issues will be paramount for the improvement of trade and development in the country.

113. **A third major constraint to productivity growth and the functioning of markets, especially for the rural economy, is the absence of adequate road transport.** The country is home to 1.7 million people, but has only 10 kilometers of paved roads per 100 square kilometers of land area. This road network coverage appears to be broadly in line with other Sub-Saharan African countries. However, the roads are in considerably poorer condition, especially secondary and tertiary roads, which are most important for rural dwellers. The poor road network hampers the efficient flow of goods and labor and creates high transaction costs. In fact, farmers report considerable constraints in marketing their goods, especially during the rainy season when roads are flooded or even washed away. Inadequate roads also inhibit people's ability to access basic services, including schools and hospitals. As noted in the inclusiveness section above, the poorest households and those that have less diversified incomes tend to reside farther away from roads, including secondary and tertiary roads, and thus are relatively more isolated from markets and other critical public goods and services, and economic opportunities.

114. **While the telecommunications sector has grown and generated positive impacts on the economy, it remains underdeveloped, representing another bottleneck to growth (Figure 3.13).** From 2004-2012, total private investment in telecoms approximated US\$134 million and accounted for 90 percent of total foreign direct investment. It is estimated that Orange Bissau and MTN (both telecommunications companies) have created about 300 direct jobs and 4,000 indirect jobs through their distribution networks.³⁰ Total revenues of the telecom sector increased by factor of six in the past 10 years and the sector's contribution to GDP has grown to almost 2 percent.³¹ However, it remains below the African average (7 percent), signaling ample room for growth.³² Landlines are almost nonexistent. Mobile telephony has grown rapidly and a high share of the population either have, or have close access to, a mobile phone.³³ Guinea-Bissau is the only country on the African coast not connected to a submarine cable. Consequently, internet usage remains low at 4 percent in 2015 compared to 19 percent in Gambia and 51 percent in Senegal.

³⁰ <http://www.sonatel.sn/guinee-bissau/>

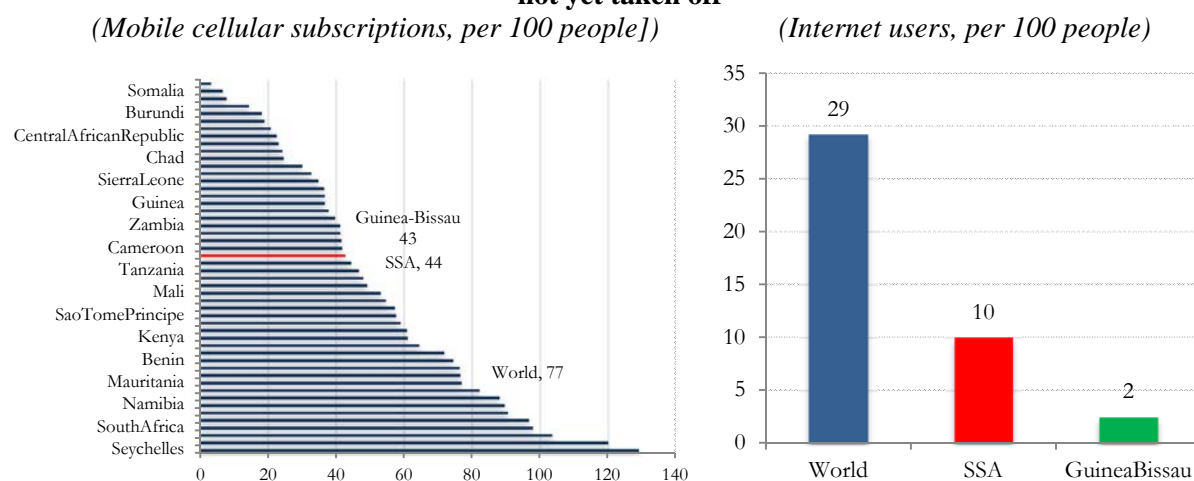
³¹ Total revenues of the telecom sector are only those of MTN and Orange and do not include that of the incumbent operator, for which there is a lack of available data.

³² In 2011, Orange Bissau alone contributed to 3 percent of the Government total tax revenue and its total revenues represented 22 percent of the Government total fiscal revenues. <http://www.sonatel.sn/guinee-bissau/>

³³ Mobile penetration as measured by number of SIM cards is 81 percent in 2015, but since the average number of cards per subscriber is 2.1, this suggests that only 41 percent of the population has a mobile phone.

The broadband market, concentrated in the capital, is nascent, with a penetration rate of about 0.9 percent of the population compared to 15 percent in Senegal and Morocco. Notwithstanding these issues, recent developments in the telecommunication sector hold much promise. An emerging body of research shows that reduction in communication costs associated with mobile phones has tangible economic benefits including improving agricultural (and labor market) efficiency, and fostering both producer and consumer welfare. In Senegal, the Manobi platform was created primarily to provide real-time information on agricultural prices in local and international markets, resulting in an increase in certain farmers' incomes by more than 40 percent.³⁴ For Guinea-Bissau, the Telco MTN is launching a mobile service allowing cashew nut merchants to improve access to market information and bypass intermediary agents.

Figure 3.13. Mobile phone coverage has increased in Guinea-Bissau but the Internet revolution has not yet taken off



Source: World Development Indicators (2008-2012).

115. In mobile telephony, Guinea-Bissau faces problems of access and affordability, although this is one of the more developed markets in the country. The country is currently facing a growing digital divide between the population living in the major urban areas and the remaining lagging regions. In fact, there are significant differences in terms of mobile coverage and mobile penetration between regions. Lack of fiber optic infrastructure, imperfect competition, weak regulation, and excessively high operational costs (caused mostly by critical electricity problems) lead to economic inefficiencies, high prices, and lower affordability. On average, a mobile subscriber in Guinea-Bissau spends more than 19 percent of his or her monthly income on mobile telecommunications services (voice and data), which is much higher than in other neighboring countries (14 percent in Côte d'Ivoire, 12 percent in Senegal, 9 percent in Ghana, and 4 percent in South Africa).

116. Limited connectivity and persistent economic inefficiencies in the sector mean that Guinea-Bissau is missing out on many of the economic, governance, and transparency benefits associated with modern telecommunications. There is abundant evidence showing that mobile phones connect market participants across distances (World Development Report (WDR),

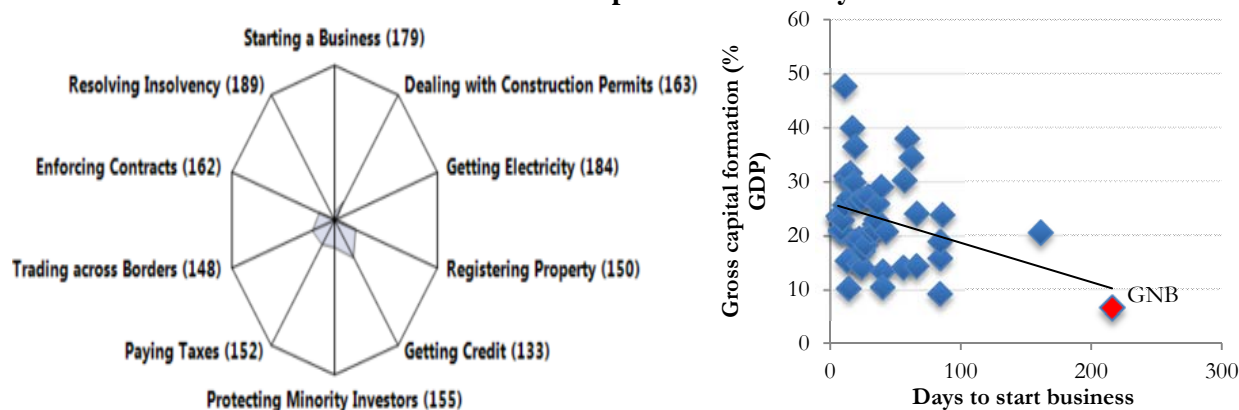
³⁴ Dalberg (2013). Impact of internet in Africa.

2016). They can improve access to financial services through mobile payment systems, mobile saving schemes, and even mobile banking, especially in a country with very low financial inclusion such as Guinea-Bissau.³⁵ Mobile phones are also increasingly used to channel cash to individuals through official cash transfer schemes or remittances, which reduces poverty and can boost the local economy through household demand and even investment stimuli. Limited broadband connectivity means that the country misses out on the benefits of broadband services, which are found to contribute directly to a country's productivity, competitiveness, and to its ability to attract foreign direct investment (FDI), reducing transaction costs and helping countries diversify into more sophisticated sectors. Within government, mobile phones are also used to track the delivery and quality of public services (for example, tracking teacher absenteeism). ICT can facilitate business within government, yet these benefits remains largely untapped. Guinea-Bissau ranks 182th out of 193 countries in the 2014 E-Government Development Index.³⁶

Weak business environment

117. **The business climate is not conducive to the generation of growth and employment.** The country's unstable political climate, which includes high levels of rent-seeking, is a formidable deterrent to private investment and growth. Furthermore, the regulatory framework for business remains precarious and inhospitable despite some efforts to improve it. This is illustrated by the country's performance in the Doing Business 2016 report (DB). With an overall rank of 178 out of 189 economies and a distance to frontier (DTF) score of 40.56 percentage points, Guinea-Bissau is at the bottom of the classification of "ease of doing business." While performance varies across topics (see Figure 3.14), the country does not rank in the top half of the classification in any of the 10 Doing Business areas included in the ranking. The multiple constraints that the business climate create for the generation of firms in Guinea-Bissau pose a big burden for the formation of productive capital.

Figure 3.14: Guinea-Bissau's performance on Doing Business indicators is low, hindering the formation of capital in the country



Source: Doing Business, World Development Indicators (circa 2008-2012) and World Bank staff

118. **As a result of the 'stop-go' policy environment, legal reforms are often incomplete or not applied in practice.** Legislation is sometimes approved, but the implementing regulations are

³⁵ In Guinea-Bissau, there is a great potential to develop the use of mobile money services since the two active telecom operators Orange and MTN already have a significant experience of in developing mobile money services in Africa.

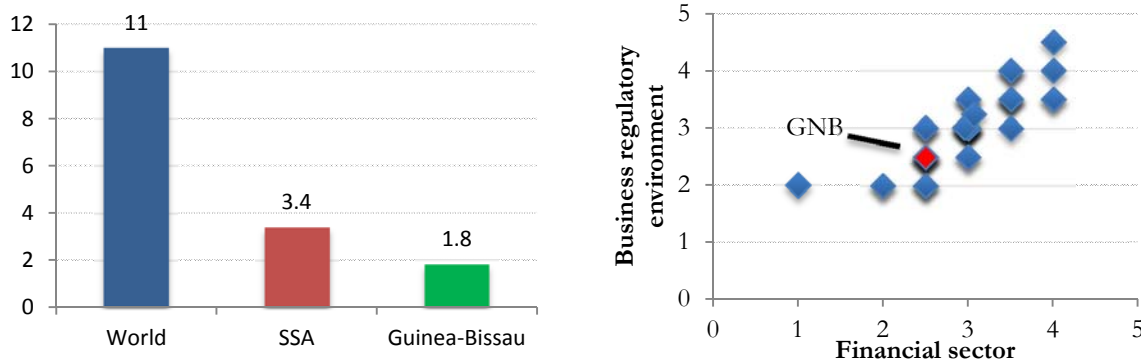
³⁶ Source: <http://unpan3.un.org/egovkb/en-us/Reports/UN-E-Government-Survey-2014>.

not developed and the necessary institutional arrangements to apply the law are not created. That was the case of the Land Law (Lei da Terra, Law 5/1998 of April 23), the 2011 Investment Code (Law 13/2011 of July 6), or the Decree 8/2011 on licensing reform. As a result, some regulations are partially applied, leaving room for interpretation. This is aggravated by insufficient knowledge of regulations among public officials, leading to inconsistent enforcement. Notwithstanding the creation of a commercial court, and the examples of good international practice for achieving more efficient resolution of commercial disputes that exist, enforcement of business law remains challenging. The general corruption and dysfunctional nature of the Guinean justice and law-enforcement system, where impunity is high, undermine the execution of decisions by the commercial court. Rent-seeking behavior by low-paid government officials further weakens the application of regulations. Interactions with the private sector are often seen as opportunities to extract additional earnings. The multiplicity of fees to be paid in the process of goods arrival and customs clearance at the port or land border is an example. Implementation of reforms that reduce opportunities for such rents, for example removing prior approvals and licenses or implementing transparent procedures, are met with resistance.

Limited access to finance is a significant constraint

119. **The financial sector is highly underdeveloped in Guinea-Bissau, with low access to formal banking services.** Guinea-Bissau has fewer banks than most other nations in Sub-Saharan Africa (Figure 3.15). Private sector credit to the economy plummeted to below 1 percent of GDP in 2003 (AfDB, 2014). Since then, overall credit to the private sector has been on the rise, reaching 13.8 percent of GDP in 2013, but still remains significantly below WAEMU countries. Despite rapid growth, the level of banking penetration remains very low. Between 2007 and 2013, the number of accounts increased from 27,725 to 60,096 (with a peak of 69,556 in 2012). However, only about 1 percent of the population is estimated to have a bank account (IMF 2013). This translates into 35 bank accounts per thousand adults, well below the average for WAEMU countries at 45. Equally, the banking network is very narrow with just 26 branch offices or “guichets”, of which only 7 are in rural areas. Low financial coverage is associated with low ratings in the Country Policy and Institutional Assessment (CPIA) for business environment.

Figure 3.15. The financial is sector is highly underdeveloped, constraining the business climate
(Commercial bank branches per 100,000 adults) (CPIA ratings for financial sector and business climate)



Source: World Development Indicators and World Bank Country Policy and Institutional Assessment (2008-2012).

120. **Overall, Guinea-Bissau's banking system is shallow and characterized by low intermediation.** (Figure 3.16) On average in 2011, African banks intermediated about 74 percent of their deposits, while the ratio was 109 percent in non-African banks (Beck et al., 2011). In Guinea-Bissau, although the trend has been on the increase, the ratio stood at just 60 percent in 2013, considerably lower than the 2011 regional average. The implication of this low ratio is that existing resources held by banks are not efficiently channeled to private sector activities, inhibiting business and employment growth. Most bank lending is short term, which carries high interest rates (fluctuating between 14 percent and 18 percent) and substantial collaterals to cover anticipated high risk. Moreover, more than 25 percent of bank lending is concentrated in the cashew sector in the context of pre- and post-cashew harvest financing, and also includes loans to small processing plants and trading advances to exporters. Working capital loans to Small and Medium Enterprises (SMEs) are very limited. The situation worsened after the 2012 military coup, when non-performing loans (NPL) reached approximately US\$50 million in the banks' portfolios from cashew sector activities. As a result, most SMEs and poor households are excluded from the credit market, further limiting their ability to invest in productive assets or to be able to exploit economic opportunities that could facilitate their exit from poverty. Furthermore, the absence of a capital market constrains the availability of risk hedging mechanisms, making businesses and households more susceptible to shocks and less efficient at managing them.

121. **The limited uses of financial instruments is constrained by several factors on the supply and demand sides of the market.** The supply of financial instruments is constrained by a risky business environment, gaps in credit information that prevent accurate pricing, weak debt recovery mechanisms, weak market and institutional financial infrastructures, including those for contract rights and enforcement and credit bureaus, and inadequate accounting and disclosure standards. Factors hindering the demand for credit include challenges in proving title over property, lack of collateral or high costs of registering it, weak capacity on the private sector to present bankable loan applications, and lack of proper accounting mechanisms (Figure 3.17).

Figure 3.16. Low bank penetration in Guinea-Bissau

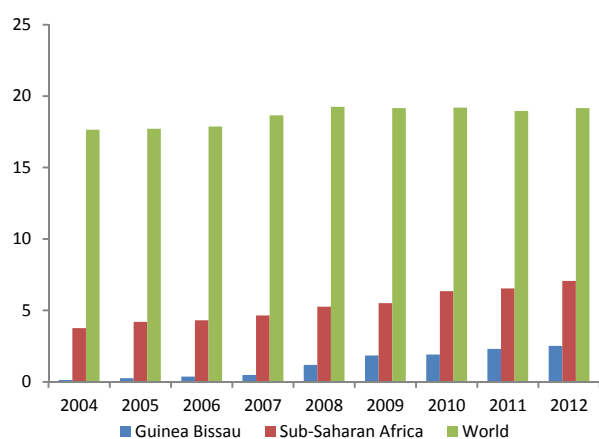
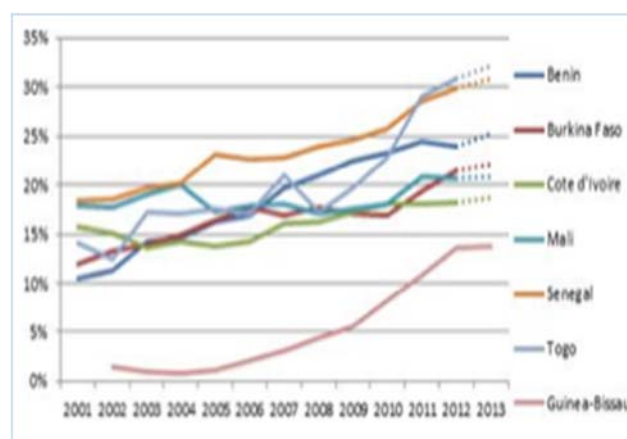
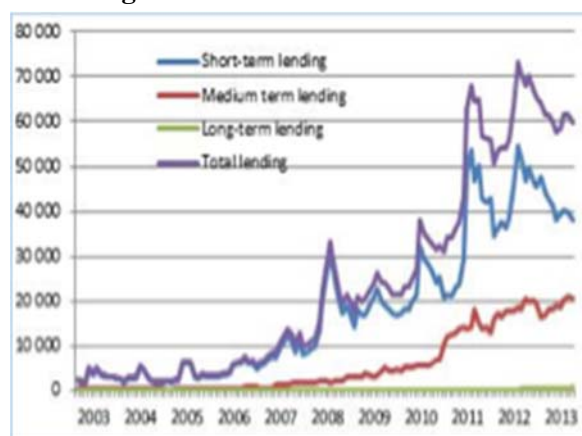


Figure 3.17. Private sector Credit/GPD in WAEMU (Growth - Commercial branches/100,000 people)



Source: CEM 2015, World Bank; BCEAO for Guinea-Bissau; 2013.

Figure 3.19. Total Lending to the Guinea-Bissau Private-Sector (FCFA millions)



Source: BCEAO, 2013.

122. **The microfinance sector, although underdeveloped, is necessary and could help smallholder and enterprises with diversification of credit options.** In Guinea-Bissau, microfinance institutions (MFI) represent very small volumes, contributing a meager 0.09 percent of GDP. Only six MFIs are currently active, with 19 service points for 16,210 members, and all are in the form of donor-financed cooperatives or projects with a credit component. Total deposits amounted to FCFA207 million (the lowest in Sub-Saharan Africa) and outstanding loans to 84 million CFA francs in 2014. Despite a 22 percent increase in deposits from 2010 to 2012, MFI loans actually fell by nearly 46 percent, due to donors' suspension of financing, resulting in an average rate of portfolio deterioration in 2012 of 61 percent, versus a norm of 5 percent (AEO, 2014) (Figure 3.19). Field inquiries show that lack of experience, poor management, and weak monitoring systems caused high NPLs and led to the collapse of the nascent microfinance sector in Guinea-Bissau. Other reasons for the low density of microfinance institutions are the high operating cost in Guinea-Bissau and the exclusion of microfinance institutions with licenses from other countries. A new regulatory framework is expected from the Government in the short- to medium-term to: (1) strengthen the institutional, legal, and regulatory environment so as to provide security for the sector; (2) initiate efforts to increase the professionalism of MFIs; and (3) promote partnerships among all stakeholders in order to provide MFIs with better access to sources of financing (AEO, 2014).

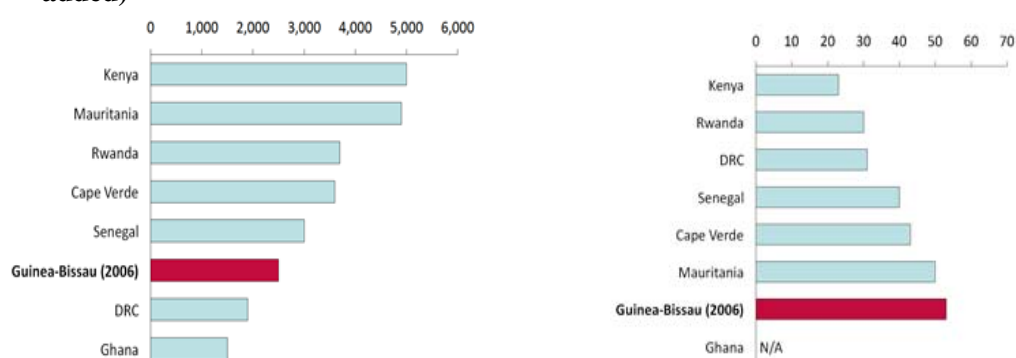
Labor costs are high relative to labor productivity

123. **Guinea-Bissau's labor market is characterized by low productivity and relatively high labor unit costs.** Despite relatively low absolute wage levels, unit labor costs (relative to value added) are high in Guinea-Bissau compared to similar countries (Figure 3.19). In fact, labor costs amount to as much as 54 percent of value added for the median firm in the country, a proportion higher than that observed in South Africa (41 percent) and much higher than levels observed in Kenya (24 percent) and the Democratic Republic of Congo (32 percent). This suggests that Guinea-Bissau is not competitive internationally in terms of labor costs, due to low value added per worker (see Figure 3.20 on labor market rigidity, and Figure 3.21 on firing costs affecting hiring decisions).

124. **Low productivity and the relatively high labor unit costs can also be explained by looking at the low skill level among workers.** As noted above in Chapter 2, education levels in Guinea-Bissau are low, and companies provide limited training. Data from ILAP shows that the average school attainment for adults in Guinea-Bissau is below 3 years and even less in the bottom two consumption quintiles. Overall, three-quarters of Guinean household heads did not have complete primary education. Only about 15 percent of workers have had any kind of technical or vocational training. These numbers are only based on the manufacturing sector; in agriculture, as depicted in Chapter 2 and where most Guineans work, education levels are much lower—less than 0.3 percent have higher education and only 3 percent have graduated high school.

Figure 3.19. Median wages are relatively low in Guinea-Bissau... but, due to low productivity, unit labor costs are high

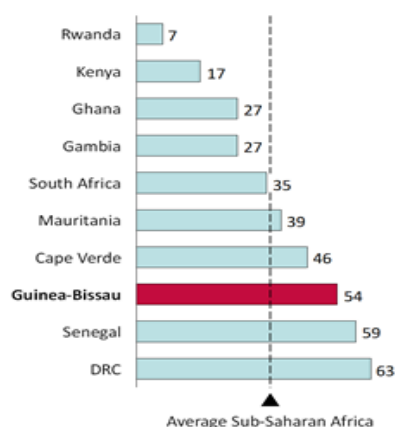
(Median wages per worker; in PPP terms) (Unit labor costs, ratio of wages to value added)



Source: CEM, 2015

Figure 3.20. The Guinea-Bissau labor market is relatively rigid

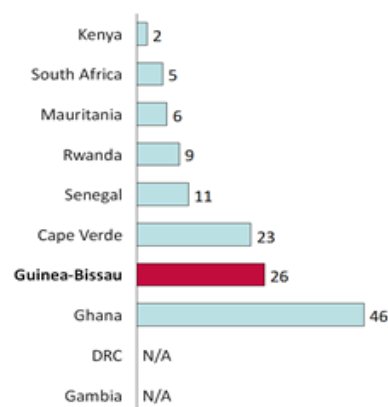
(Rigidity of employment index (higher is more rigid))



Source: CEM, 2015.

Figure 3.21. Firing costs are one disincentive for firms to hire into formal jobs

(Severance pay for redundancy dismissal, weeks of salary)



3.6 Untapped economic opportunities to spur shared growth

125. **There are several opportunities to foster stronger growth. However, this potential primarily rests on the ability of Guinea-Bissau to remove or at least ease the key growth obstacles identified in this chapter.** There is no silver bullet to solve all of Guinea-Bissau's problems, and neither is there any one binding constraint whose removal would by itself resolve all the other constraints. The challenge is not only about exploring new industries and sources of growth, but also about making traditional sectors and industries more competitive. In this regard, there is a need for concerted efforts to directly tackle the many constraints appropriately sequenced, where possible, capitalizing on low-hanging fruits, and embracing available technology. Importantly, this will have to be done in the context of limited fiscal space and a smaller public sector. Having lost decades of potential progress as a result of low and fragile growth, the government needs to move forward very efficiently, actions which call for urgent improvement in accountability and governance.

126. **Agricultural potential is significant because of favorable factors, such as climate and soil characteristics, and therefore agriculture should be pursued in the short- to medium term, if not also the long term, given that the majority of households stand to benefit from advances in this sector.** The 2015 CEM suggests, for instance, that improved farming techniques could increase cashew yields, and that much higher margins could be gained through processing cashew domestically. Thus far, however, the country has not managed to establish a cashew processing industry, a result attributed to the many aforementioned business climate constraints. There is some limited activity in other agricultural areas. Notably, Guinea-Bissau also produces groundnuts, which in 2015 was estimated to be 40,000 metric tons.³⁷ The Government has also initiated steps to encourage sesame production.³⁸ Rice is grown on a subsistence basis although the country was once a net exporter of the commodity in the 1970s.³⁹ There is also potential in a diversified range of cereal (rice, millet, sorghum, and so forth), fruit (mangoes, citrus fruit, papayas, and so forth) and pulse and tuber (cassava and sweet potatoes) crops. There is a fisheries sector but this is largely dominated by European fleets under licensing agreements with the Guinean Government.

127. **There are also opportunities in other sectors.** The mining sector is in its very early stages of development. Guinea-Bissau has also more than 2 million hectares of forest, with considerable diversity in its fauna and ecosystem. In spite of the country's significant natural beauty, the potential of the tourism sector remains largely untapped.⁴⁰ Moving into higher value-added activities in industry and services will be crucial to achieve the growth rates that Guinea-Bissau will require to catch-up with other countries (Box 3.3).

Climbing the value chain in the cashew sector

128. **Cashew cultivation and exports have grown rapidly over time, and without new investments, the current status of the activity is reaching its productivity limits.** Cashew

³⁷ A consultant report commissioned for this SCD suggests that most of the production of groundnuts feeds a crushing plant in bordering Ziguinchor, Senegal.

³⁸ For discussions of the cashew, rice, fishing, and mining sectors, as well as tourism, see Chapters 8-12 respectively of the 2015 CEM.

³⁹ Favorable cashew prices since the mid-90s, led many farmers to disregard rice, and its more intensive labor requirements, in favor of cashew.

⁴⁰ See chapters 2, 3, and 12 of the 2015 CEM.

exports have been growing at almost 6 percent a year from 1994 to 2013, fueled by increased acreage under cultivation. This is related to availability of vast agricultural lands and the extremely low production requirements of cashews. Existing farming practices, however, represent a risk to productivity in the sector. Poor planting techniques result in lower yields per hectare. Processes such as revitalizing orchards by pruning current trees and replanting old ones with correct spacing are directly correlated with improved yields, but are not currently performed. Additionally, the development of a wider variety of cashew trees would help hedge against the risk of widespread plant disease. The current status of cashew production is geared toward raw nut export, with little focus on developing the internal value-chain. With little knowledge and bargaining power, farmers bear the costs of price volatility and cannot properly charge international prices. In 2013, farmers only received about 40 percent of the reference price of raw cashew nuts sold to exporters. Given the strong potential of the cashew sector in Guinea-Bissau, improvement of the production process should be leveraged by private sector involvement as well as by public-private cooperation. The cashew economy could benefit from several off-the-shelf solutions, both in knowledge (that is, planting techniques, and seed and fertilizer) and capital improvements (that is processing plants) that can boost and sustain higher productivity, helping Guineans to enter higher-value markets and raise efficiency in the production chain.

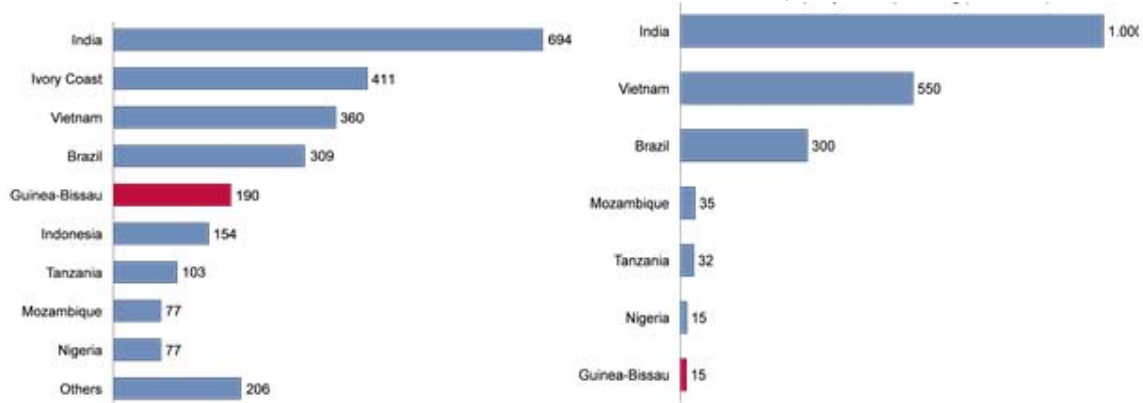
129. The next step in the value chain is the production of cashew kernels, but the processing capacity of the country is small. Guinea-Bissau is an important player in the production and export of raw cashew nuts, despite the country's small size. In 2012, it was the fifth-largest producer of raw cashew nuts, after India, Cote d'Ivoire, Vietnam, and Brazil. However, Guinea-Bissau exports consist of raw cashew nuts. There is little processing power at home, which means the country is an insignificant player in the production of cashew kernel.⁴¹ In 2010, the country had the capacity to process less than 15,000 tons of raw cashew nuts a year, making it far from the largest player in the sector (Figure 3.22). Additionally, capacity utilization remained low. In 2013, the country produced less than 250 tons of cashew kernels (<4 percent of capacity utilization), of which 55 percent were exported and the remainder still awaited a buyer. Developing a market for processed cashew, as well as complying with international standards, are important areas for development of the sector.

130. The country has the opportunity to develop a cashew processing industry and move up in the value chain if critical constraints are properly addressed. The conditions are favorable for Guinea-Bissau to develop a cashew processing industry. The country boast a plentiful supply of good quality raw cashew nuts, and labor is available. Nonetheless, significant challenges remain in place. The high cost of financing may pose the most significant constraint. Furthermore, the cashew harvest only lasts for three months, increasing the urgency for storage issues to be addressed. Another issue is an unsuccessful, albeit relevant, cashew-sector guarantee program that was established in 2013. Issues of low-credit volume and nontransparent allocation of funds both need to be addressed for the program to work. There are also minimum scale and quality requirements, such as achieving a consistent supply of container volume and cashew nut quality (that is, size). Infrastructure is a major obstacle due to the low availability and reliability of electricity and to the existence of poor roads (especially of secondary roads) and poor port infrastructure.

⁴¹ From 1994 to 2014, the country exported 95 percent of the raw cashew nuts it produced, mostly to India.

Figure 3.22. Guinea-Bissau is the fifth largest exporter of raw cashew worldwide, yet the country hardly produces processed cashew (kernel)

(Production of raw cashew nuts, thousand metric tons, 2012) (Installed capacity for cashew processing, thousand metric tons, 2012)



Source: CEM, 2015

131. **A cashew processing industry would bring sizable benefits to the economy.** The economy would be expected to grow, fueled by an increase in the size of the industry sector, and employment would increase. It is estimated that cashew-processing creates about one full-time job for every three tons of processed raw nuts. Processing 30,000 tons of nuts a year could therefore create about 10,000 jobs, mostly in rural areas. This increase in jobs would particularly benefit women, who make up the majority of factory workers. Organized communities and a better value chain could significantly raise incomes, address food security, and reduce poverty. It would also strengthen producer bargaining power, if they could guarantee a reliable supply to processors. Processors and exporters also would benefit, because the profit margin for enterprises would be greater for exporting kernel rather than raw cashew. Finally, the risks in the value chain could potentially be mitigated due to reduced dependence on the Indian market.

Reinvigorating the rice sector

132. **Rice constitutes the most important grain crop and staple food in the country, but over time several political and economic factors have adversely affected its cultivation.** Rice is the main staple food, grown largely for domestic auto-consumption. It is a crop with considerable potential to enhance food security and incomes, especially in poor, rural areas. Rice is also a major barter good for cashew growers. The cultivation of rice in the country started in the pre-colonial period over 500 years ago, but several conflicts caused production to undergo major changes. The colonial war of 1915 worsened the rice-growing situation. By the 1930's, migrants leaving the capital set up rice-growing systems in rural areas, resulting in production and export activities to make a comeback, until about 1960, when the national liberation war (which continued until 1973) caused rice production to again decline. Much of the infrastructure was destroyed during these several lengthy conflicts. The early years of independence were characterized by a program to re-launch agricultural production, which was one of the main pillars in the attempt to reach food self-sufficiency. This included expanding the area of mangrove swamp rice cultivation through the rehabilitation of sea dykes, construction of sluice gates, and creation of mangrove swamp rice perimeters. Rice production collapsed again during the civil war of 1998-1999, but it has rebounded since, although yields, by most standards, remain low.

133. **The topography of Guinea-Bissau is very suitable for all types of rice cultivation.** Rice is currently produced in three ecosystems: rain-fed uplands, lowlands (rain-fed and irrigated), and mangrove. Mangrove swamp rice is the most extensive system of rice cultivation in Guinea-Bissau and is widely practiced in coastal regions. The south is particularly suited for mangrove swamp rice, while the north has the potential for mangrove and lowland rice production and the east for irrigated rice. Traditionally, many of the ethnic groups comprising the majority of the population have been focused on rice cultivation, meaning that the human capital inherent in long-term cultivation of a crop is well developed. The Diagnostic Trade Integration Study (DTIS) for Guinea-Bissau, completed in 2010, shows that Guinea-Bissau has a significant comparative advantage in several aspects of rice production.

134. **Boosting rice production, interspersed with cashew or on a stand-alone basis, can increase incomes and reduce food security, but doing so requires interventions on several fronts.** Increasing rice production would enhance food security, boost incomes of rice farmers, hedge against monocrop risks, and diversify Guinea-Bissau's export base. The most immediate improvements can be promoted by better seed variety, and crop management that maximizes yield and land utilization. The sector would also benefit tremendously from better on-farm infrastructure, such as irrigation and drainage. Given the constraints on government capacity, NGOs with experience in performing knowledge transfer activities can step in to provide extension services. Public-private partnerships can also be formed to address on-farm infrastructure deficiencies, such as rehabilitating or constructing dikes for mangrove rice and drainage channels and anti-erosion banks for lowland rice, creating better irrigation and drainage in lowlands, and improving management. Nevertheless, even if rice productivity is improved, the rational decision at the household level might still be to plant cashew. This is due both to the role of cashew in securing land tenure and to its higher economic returns. This means that the interplay between rice and cashew should be leveraged when possible to maximize returns while enhancing household food security.

Increasing the rents from fisheries while ensuring ecological sustainability

135. **Fishing is one of the major economic activities undertaken in the western coast of Africa and has great potential in Guinea-Bissau.** The gross value of fisheries production in 2010 is estimated at US\$81.3 million, corresponding to 20 percent of the agricultural value added.⁴² This value, however, does not capture the higher potential revenue stream that the fisheries would generate in the long run. Guinea-Bissau has a relatively small coastline, 270 Km long (excluding oceanic islands), but the waters are rich in terms of abundance and diversity of fish species, sustained mainly by an influx of nutrients from the country's many estuaries which provide 3,400 km of mangrove cover, nearly 10 percent of the national territory. The geographical configuration and the humid tropical climate offer important productive fisheries conditions for demersals (that is bottom-dwellers) and small pelagics (that is offshore surface fish). The latest estimates confirm that the country has a fishing potential of 120,000 tons.

136. **Nonetheless, most of the current industry is exploited by foreign companies, with only a small share benefitting locals.** Fisheries resources are extracted by two main fishing industries:

⁴² Calculations based on figures reported in Optimizing Guinea-Bissau's Natural Wealth, 2014 and World Bank Development Indicators.

artisanal and industrial. The estimated total number of artisanal fishing boats operating in Guinea-Bissau in 2013 was 1,159, with about 40 percent of the fleet operated by foreign fishermen, while industrial fishing vessels totaled 106, through joint ventures and agreements. Almost 22,000 tons of fish were landed by the artisanal fishing sector in 2011, while the average annual catch is about 70,000 tons for industrial vessels.⁴³ Nonetheless, fish caught by industrial vessels are landed directly in foreign ports with very little contribution to national coffers; some estimates reveal that only about 25 percent of these revenues are captured at the national level. Overall, the contribution of fisheries to GDP –as estimated by the Sub-Regional Fisheries Commission– is less than 4 percent, despite the huge fishing potential of the country.

137. The sustainable contribution of fisheries could be much higher if appropriate governance and management structures were in place. The fishing industry is a highly unregulated activity, leading both to overexploitation and underperformance of the resource base. In Guinea-Bissau and in the West Africa region in general, marine fisheries resources are enduring excessive fishing pressure in an essentially unregulated environment. With a vast resource base, the fisheries sector of Guinea-Bissau has the potential to make a much greater contribution to the attainment of key development objectives, such as economic growth and poverty alleviation, but only if better managed to prevent overexploitation. The main challenges are insufficient governmental capacity both to regulate fishing and to prosecute and punish illegal activity, while at the same time most of the benefits to fishing are not accrued locally. Programs such as the West Africa Regional Fisheries Program (WARFP) have been introduced, and should be continued, with the objective of building the government's capacity to more sustainably govern the use of the marine fish resources, to reduce illegal fishing, and to increase local value added to fisheries products.

138. Guinea-Bissau has made progress against illegal fishing, which bodes well for commercial fishing to make a greater contribution and provide longer-term sustainability of the sector. In spite of major delays, Guinea-Bissau has achieved a substantial progress in the effort to monitor and control illegal fishing in the waters of Guinea-Bissau. The national registration system for industrial and artisanal fishing vessels has been designed and made operational, while the new regulation has resulted in a 100 percent utilization of VMS (Vessel Monitoring System) by vessels authorized to fish in Guinea-Bissau. With the recently-augmented patrol capacity, monitoring, control and surveillance (MCS) activities have successfully detected and controlled violations, and the percentage of fishing vessels committing offenses was well below the target for 2014 and 2015 both in the artisanal and industrial segments. In order to maintain the MCS activities and continue to reduce illegal fishing, the country needs support for further capacity building as well as financial sustainability of the MCS program. Stock assessment campaigns must continue to better evaluate the state of the stocks and determine appropriate levels of utilization. While these have generated an unprecedented amount of information regarding the fish stocks in the Guinean waters, continued assessment is essential to accurately evaluate the trend. Results of these campaigns also provide important data to estimate some key parameters for bioeconomic modeling, which would help determine possible paths towards sustainable management and utilization of the fish resources.

⁴³ Data unavailability may underestimate the local catch, while the estimated annual production does not include catches taken illegally from waters of Guinea-Bissau.

Tapping on nascent extractive industries

139. **Historically, the mining and petroleum sectors of Guinea-Bissau have been very small, mostly involving quarrying and a small amount of artisanal mining, but nevertheless, there is great potential in these sectors.** Currently, the only actively-producing extractive industries in Guinea-Bissau are small quarries for construction materials, such as granite, limestone, clay, and sand, although a relatively small mineral sands mine is near production in Varela, in the northwest section of the country. Recent interest of foreign investors in the extractive industries (EI) sector holds considerable promise. Petroleum and copper have respectively the second and third largest potential for export, after the cashew industry. Nevertheless, there are numerous examples of countries in which the large majority of the population not only did not benefit but was eventually left worse off after the discovery and exploitation of large oil or mineral deposits. By fostering local linkages with the economy, mining can support local incomes, while rents from the EI sector can support critical public investments.

140. **The resources closest to realizing their potential are phosphates and bauxite, but there also are good prospects for sands, gold, and petroleum.** Phosphate deposits were first identified by the United Nations Development Program (UNDP) in 1978. Since that time, several companies have started and then broken a lease for exploration due to a series of issues and mutual disagreements between the companies and the government. Plains Creek (also locally known as GB Minerals) is the latest company to sign a lease, in 2009, and it has more recently been successfully securing the funds to begin exploration in Farim (Oio Region). Bauxite deposits are another important resource, and five companies are closely situated to each another in Boe, in the southeast of the country. The latest lease, in 2007, was granted to Bauxite Angola. Other players include the Russian company Poto, which signed a contract in February 2014 for exploitation of 1 million m³ of sand, which is expected to result in about 119,000 tons of mineral sands (ilmenite, zircon, and rutile), while in the medium or long term, the prospects from gold could also be significant. In addition, there have been several finds from exploratory offshore drilling for petroleum in Guinea-Bissau, but to date no commercially viable discoveries.⁴⁴

141. **While laws governing the extractive industry exist, one of their main shortcomings has been the lack of clauses imposing social benefits to be derived from the vast resources to be potentially explored.** New legislation governing the mining and petroleum sectors have been in the process of being enacted for several years and is currently waiting for promulgation by Parliament.⁴⁵ However, the mining law does not contain provisions dealing with community development. For example, there is no provision requiring local or even regional employment in the mines or investments, or providing for the wellbeing of employees. The petroleum law, on the other hand, has those provisions, albeit in vague language. This is due to the nature of oil exploration. Because oil discoveries in Guinea-Bissau have all been offshore, the community development issues are not as complex as they are in hard rock mining, and the linkage opportunities are much fewer. Hence, overall there is still room to foster linkages with the local economy. Mining companies should be compelled to work with the Government to provide greater socio-economic benefits to Guinean communities. These projects, particularly in mining, often

⁴⁴ In the southern area, 14 blocks are licensed to six companies—Svenska (Sweden), Black Star Petroleum (UK), Supernova (Netherlands), Lime Petroleum (Norway), SHA (Angola), and Larsen Oil and Gas (Dubai).

⁴⁵ A new Mining Law (of 2010) is set to replace the Mining Law of 2000, and a new Petroleum Law (also of 2010) will replace the 1982 Petroleum Law, which has been amended several times through the years.

carry infrastructure benefits with them accruing to both society and other industries, while it can also help finance critical public investment programs, social assistance schemes aimed at alleviating poverty, and initiatives seeking to promote economic opportunities.

Sustainable tourism to give economic value to rich biodiversity

142. **Sustainable tourism and ecotourism in Guinea-Bissau has the potential to become a source of economic growth and employment.** Through tourism, protected areas and ecosystem can gain tangible economic value, helping to further preserve them. Guinea-Bissau is somewhat unique in that it is among the last countries in West Africa where development has had limited negative impact on the environment, and consequently, its biodiversity has not yet been significantly degraded. The country's ecosystems support a wealth of biodiversity. Several animal species found in Guinea-Bissau are globally significant and are identified on the International Union for Conservation of Nature's (IUCN) Red List as globally endangered or threatened. The Bolama-Bijagós Archipelago is a recognized United Nations Educational, Scientific & Cultural Organization (UNESCO) Man and the Biosphere Program (MAB) Reserve, due to its exceptional combination of biological and cultural assets. Recognizing the critical importance of these biodiversity, ecosystem, and cultural assets, the Government, together with national and international partners, has over the past 20 years worked to develop an institutional framework for their conservation and sustainable use.

143. **Guinea-Bissau's comparative advantage in tourism rests with its natural resources and cultural assets.** The rich biodiversity found throughout the country can be combined with strong cultural resources to create a unique tourism offering. Cultural resources in Guinea-Bissau include an interesting and diverse cuisine, many cultural festivals, traditional dance and music, and authentic handcrafts. In addition to its potential nature- and culture-based tourism products, the country is well positioned to receive tourists from Europe.⁴⁶ The country has already created an international image based on its natural environmental and ecosystems. However, opportunities remain largely untapped, mainly due to the country's history of instability. Tourism has a real potential to be a source of shared growth in Guinea-Bissau, positively impacting communities, especially if negative externalities are effectively managed. Most studies have pointed to three to five areas in Guinea-Bissau or *niches* where tourism seems to be emerging and, with one notable exception (Bissau), they are in and around the existing protected areas. These include the Bijagós Archipelago, the Cantanhez National Park, the Varela/São Domingos/Cachéu region and Bissau, the capital city. Dramatic shifts in community livelihoods can ensue from investment in tourism, helping to raise incomes, create new jobs, and add value to previously nonexistent activities.

⁴⁶ Guinea-Bissau is roughly in the same longitude as Europe so there are no changes in time zones and short flights. When direct flights are available from Lisbon, the travel time is just a little over four hours.

4 WEAK PUBLIC GOVERNANCE AND INSTITUTIONS ARE A CHALLENGE FOR SHARED PROSPERITY

- *Endemic fragility (military coups, political assassinations, and repeated unconstitutional takeovers of the Government) in Guinea-Bissau have undermined current development and, if unaddressed, may threaten future gains. With some stability, GDP per capita in Guinea-Bissau could have been 65-90 percent higher in the absence of this fragility.*
- *Fragility has largely been the result of a rentier economy and the interlinked competition for rents among the elite. The allocation of several sources of public resources often lacks transparency and accountability, limiting the availability of critical public goods to citizens.*
- *Weak institutions and governance are at the center of the rentier nature of the economy. Guinea-Bissau ranks in the bottom 10th percentile on all indicators measuring public sector capacity in the World Bank's Worldwide Governance Indicator (WGI).*
- *While instability and corruption are separate problems, both need to be addressed in order to achieve higher, more equitable economic growth, and to reduce poverty.*
- *The broken social contract is reflected in the poor provision of basic public goods and services, economic opportunities, and justice. Benchmarking analysis shows that Guinea-Bissau ranks in the bottom 10-20 percent with respect to regional and world averages in most of the human and physical capital, business climate, transparency, rule of law, and other quality of institution indicators.*
- *Fragility and weak governance constitute the third core area of binding constraints for shared growth in Guinea-Bissau. Looking ahead, mitigating actions include: improving public financial management systems; addressing allocative, technical, and regressive inefficiencies in public spending; aligning incentives in the public sector; building capacity; strengthening the business regulatory framework; reforming the management of natural resources; and reforming the political system.*
- *Democratic elections and the maintenance of constitutional order during periods of political turmoil suggest that things are changing in Guinea-Bissau. Breaking the vicious cycle of fragility and underdevelopment moving forward will require a flexible strategy to undertake approaches that engage directly with the elite and to balance those actions with others that work to enhance the livelihoods and voice of the poor.*

144. **Weak governance and fragility have undermined the country's development, and if unaddressed, threaten future gains.** Guinea-Bissau suffers repeated cycles of fragility with negative effects on economic, political, and social systems. This has been induced by competition for power among the political and military elites, over time undermining institutions meant to govern the country and to provide public goods to the population. The country ranks in the bottom 10th percentile on all indicators measuring public sector capacity in the World Bank's Worldwide Governance Indicator (WGI). Rooted in colonialism and perpetuated by those who have governed

after independence, weak governance has allowed a rentier economy to fester, effectively diverting much of the public resources toward private gain. As shown in Chapters 2 and 3, these power relationships and the resulting rentier economy undermined development outcomes across the board, ranging from the low provision of services, faltering infrastructure, low access to education and health, and low-level household welfare equilibrium, to low and unstable growth, inadequate private sector development, vulnerability to shocks, and overall poor macroeconomic management. Benchmarking analysis shows that Guinea-Bissau ranks poorly (at the bottom 10-20 percent) with respect to regional averages, let alone to world averages, in most of the human and physical capital, business climate, transparency, rule of law, and other quality of institution indicators.

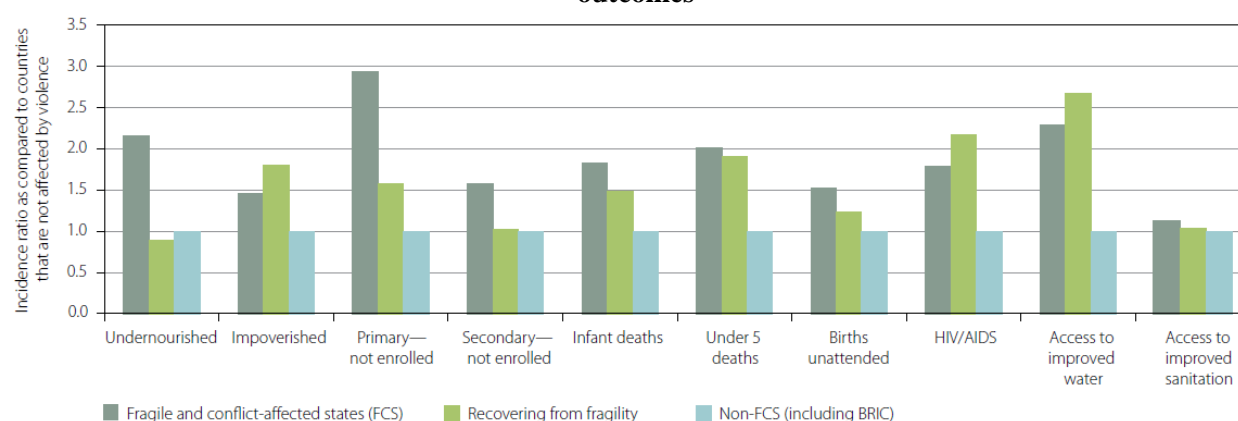
145. Breaking the vicious cycle of fragility and underdevelopment will require a flexible strategy to balance approaches that engage directly with the elite with other approaches that legitimately circumvent it to enhance the livelihoods and voice of the poor. A development agenda to move Guinea-Bissau away from the current high-poverty, low-growth, and high-fragility equilibrium will necessarily require engagement with the Government. Explicitly excluding the elite from the reform process may not be realistic and or even very effective in challenging elite domination. On the contrary, it can exacerbate rather than lessen fragility. Stability is a prerequisite for much-needed uninterrupted poverty reduction and growth. However, other strategies should be pursued in parallel to gradually start relaxing the existing political constraints. One approach is to encourage citizen engagement and demand for accountability and transparency in government performance. This includes deliberate policy efforts to increase access to and dissemination of information of general interest, and to strengthen mechanisms that channel broad-based demands for improvements in public goods, dissatisfaction with underperformance of public officers, and discontent with rigged politics. Another approach is working directly with beneficiaries, for instance through community-driven programs implemented by NGOs, to address urgent needs, such as water and sanitation, school and health services, nutrition programs, rural access roads, and micro-finance. International actors like WAEMU, ECOWAS, the African Union and the donor community can also harness forces and align incentives in favor of transparency and stability. International development institutions, in particular, can increase donor coordination and leverage their comparative advantage in data and diagnostics to improve the quality of political engagement.

4.1 Fragility, institution-building and economic development

146. Fragility constitutes a major challenge to economic development. There is fairly consistent evidence in the literature that shows a correlation between state fragility and low levels of economic development. Evidence synthesized for the 2011 World Development Report (“Conflict, Security and Development”) shows that most fragile or conflict-affected states (FCS) underperformed in a wide array of indicators with respect to other developing countries and were less likely to achieve the 2015 Millennium Development Goals (MDG). Children born in FCS are twice as likely to be undernourished, lack access to improved water, and die before their fifth birthday. Parents in FCSs are more than three times as likely to be unable to send their children to school. Countries affected by major instability between 1981 and 2005 showed on average poverty rates 21 percentage points higher than otherwise similar countries that saw no violence. This evidence is in line with the reality observed in Guinea-Bissau.

147. **Weak institutions and governance are at the center of repeated cycles of instability and violence, and are critical cross-cutting areas for addressing poverty reduction.** Kauffman et al. (2009) defined governance as the traditions and institutions by which authority in a country is exercised. This includes, among other things: (1) the process by which governments are selected, monitored, and replaced; (2) the capacity of the government to effectively formulate and implement sound policies; and (3) the respect of citizens and the state for the institutions that govern economic and social interactions among them (Figure 4.1). There is growing consensus among both academics and policymakers that weak institutional capacity, governance, and accountability are important factors in explaining why political instability and violence are repeated in the same countries or subnational regions (WDR, 2011). Different forms of instability are not one-off events but are rather ongoing and repeated. Nine out of ten civil wars in the 2000s took place in countries that had already had a civil war in the last 30 years. Repeated cycles of instability and violence exacerbate their negative human, social, and economic effects.

Figure 4.1. Fragility is correlated with underperformance in multiple human development outcomes



Source: World Development Indicators (2008-2012).

148. **The governance framework in Guinea-Bissau is found to be extremely fragile.** The country is known to have relatively weak institutions and traditions with limitations relevant to democratic participation, free media, freedom of expression, and political rights. Its elites use the public administration chiefly for their own gain with little responsiveness to the needs of the citizenry. This is consistent with the poor performance of Guinea-Bissau in the World Bank's Worldwide Governance Indicators and Enterprise Survey indicators. The country ranks in the bottom decile globally, scoring poorly on government effectiveness, the control of corruption, the quality of regulations, and the upholding and enforcement of the rule of law. Fragile and weak public institutions lend themselves to an environment of weak transparency and accountability in the use of public resources. Guinea-Bissau also has weak or non-existent systems in place for tracking government performance, public spending, and the proportion of budget allocations. This effectively blurs the revenue pathways and prevents a more efficient management of public finances.

149. **Fragility and resulting development challenges in Guinea-Bissau are rooted in the colonial history of the country.** Acemoglu, Johnson, and Robinson (2001 and 2012) in their research show that institutions in the developing countries are, more often than not, inherited from

colonial rulers.⁴⁷ In countries where colonial powers did not settle but only exploited their colonies' resources, wealth institutions were designed purely to extract rents. Newly-independent governments inherited the former colonial administration and the system of rent extraction, which were neither fair nor transparent, but the systems just served local elites instead of colonial ones. That was the case in the Portuguese colony of Guinea-Bissau. During colonial times, formally from the 19th century until the mid-1970s, Guinea-Bissau was a largely-neglected territory. Unlike the other Portuguese colonies of Cabo Verde, Angola, and Mozambique, Guinea-Bissau was not considered fit for large-scale settlement. No significant investment was made in physical infrastructure, human capital, or state institutions. Guineans were unable to access—much less participate in—any aspect of the public administration.

150. Fragility and the interlinked competition for rents among the elite have negatively influenced virtually every economic, social, and political dimension of the country. There is hardly a domain of economic, social, physical, or human development in Guinea-Bissau that does not bear the scars of a difficult legacy and the ongoing fragile political settlement. Political instability has been a defining feature for the country since independence in 1974. Continued competition among the elite has resulted in endemic political rivalry, frequent episodes of conflict such as military coups, political assassinations, and repeated unconstitutional takeovers of the government, weak public governance and institutions, clientelist political systems, and misappropriation of public rents. This vicious cycle of elite capture and fragility have ultimately undermined growth and service delivery to citizens.

151. Fragility, weak institutions and governance are pivotal underlying themes in development moving forward. Fragility, exemplified through the multiple destabilizing political events occurring throughout the country's history, has forced economic development into a start-and-stop pattern that resembles that of political power. Meanwhile, the weak governance framework has both precluded full representation of the government by the people, and encouraged those at the top to take advantage of the lack of accountability and massive disenfranchisement of society. The constraints imposed by fragility and weak governance cut across all areas explored in this document. Addressing them is one of the necessary pillars for shared prosperity and poverty reduction.

4.2 Repeated cycles of fragility in Guinea-Bissau

152. Fragility in Guinea-Bissau has translated into repeated cycles of political turmoil in the form of military coups, political assassinations, and repeated unconstitutional takeovers of the Government. In countries such as Guinea-Bissau, where the elites are fragmented and mechanisms limiting corruption are undeveloped, elites competing for rents will try to oust each other, including through violent means, such as military coups (Figure 4.2). Symptomatic of this context, the history of Guinea-Bissau was marked by regular attempted and successful military coups, political assassinations, and civil strife. All in all, four successful coups have been recorded in independent Guinea-Bissau, with another 16 coups attempted, plotted, or alleged.⁴⁸ Indeed,

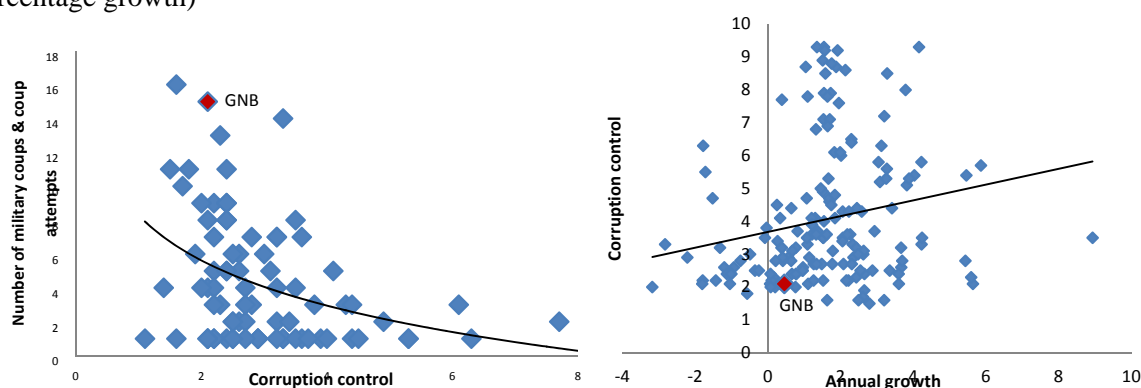
⁴⁷ D. Acemoglu, S. Johnson, and J. Robinson, "The Colonial Origins of Comparative Development: An Empirical Investigation," *The American Economic Review* 91(5):1369-1401 (2001); and D. Acemoglu, and J. Robinson, *Why Nations Fail: The Origins of Power, Prosperity, and Poverty* (Crown Publishers 2012). Further evidence corroborates that institutions play a primary role in development, for instance, D. Rodrik, A. Subramanian, and F. Trebbi, "Institutions Rule: The Primary of Institutions, Geography and Integration in Economic Development," *Journal of Economic Growth*, 9:131-165 (2004).

⁴⁸ Center for Systemic Peace, Database of Coups d'Etat, 1946-2014. See also 2015 CEM and Fragility Assessment.

together with Somalia, Guinea-Bissau has experienced the highest incidence of planned or actual coups in the world (see Box 4.1 for a chronology). This power struggle is evident among the army's past chiefs of staff (three were murdered and one forced into exile). Recently the relationship with the army has become more complex due to alleged funding from the international narcotics trade, leading some to label Guinea-Bissau Africa's first 'narco-state'.

153. Military coups are but one manifestation of fragility in Guinea-Bissau. Frequent government turnover is another. Conflicts between the Government and the President in the country's semi-presidential system also contribute to the fragility in Guinea-Bissau. Between 1999 and 2009, Guinea-Bissau experienced government turnover each year. This was as much a consequence of military interference as it was of dismissals of the Government by the President, a constitutionally admissible process in the country's semi-presidential polity. The recent dismissal of the Government of Prime Minister Domingos Simoes Pereira in August 2015 continued a cycle of annual government turn-over between the end of the civil war and 2009, after which a period of four years of stability ended with the military coup of April 2012.

Figure 4.2. Easier access to rents is associated with a higher incidence of military coups (LHS) and rent-seeking is associated with worse economic performance (RHS)
(Number of coups and corruptions control index) (Corruption control index and percentage growth)



Source: CEM, 2015

Box 4.1 Chronology of fragility in Guinea-Bissau

1974 – Independence from Portugal. Government led by Luis Cabral.
1980 – Coup by Nino Vieira. End of state unity with Cabo Verde.
1986 – Six military leaders, including Vice-President Paulo Correia sentenced to death for allegedly planning a coup against Vieira.
1994 – First multiparty elections with PAIGC and Vieira winning the legislative and presidential elections.
1998/99 – Political-military conflict opposing Vieira and General Mané.
2000 – Kumba Yalá elected President. Ansumane Mané, leader of the military junta murdered.
2003 – President Yalá deposed by Chief of Staff, Verissimo Seabra.
2009 – President Vieira assassinated.
2012 – President Malam Bacai Sanhá died. Coup d'état and formation of a transitional government.
2014 – Elections with President Jose Mario Vaz winning. Return of constitutional order.
2015 – Government dismissed by the president in August;

4.3 A rentier economy

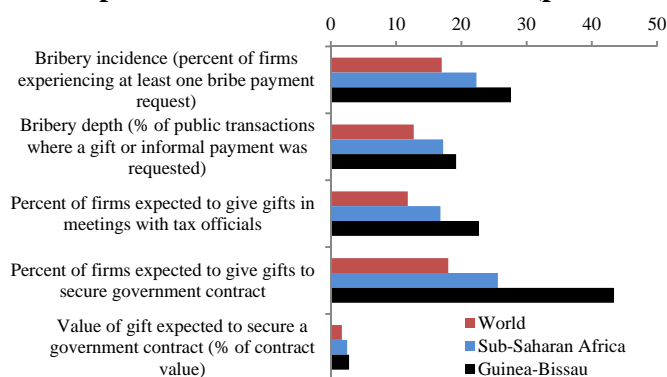
154. **Public office in Guinea-Bissau is associated with a personalized, clientelist model of rent extraction.** Weak public institutions enable the diversion of public goods toward private citizens—often political or military elites—undermining the social compact and poverty reduction. Appropriation of budget and external resources by those holding public office or being a public servant is another major source of rents. Likewise, illegal activities, especially involving the drug trade, illegal fishing, and lumber exports are the third major source of rents in Guinea-Bissau.

155. **The functioning of product markets, for instance, cashews in agriculture—is heavily exposed to rent seeking through the country’s weak business regulatory framework.** The cashew business is in many cases controlled by powerful elites, with the main issues being uncompetitive practices, distortionary and unfair taxation, port negligence, and general inefficiencies for smallholders. Background work for this SCD suggests that the quotas (number of licenses or amounts traded by license) established for cashew traders are a source for corruption, and also limit competition among traders, adversely affecting the bargaining ability of smallholders. The Guinea-Bissau cashew market has had roughly 50 exporters, but their market influence was equivalent to that of 20 exporters according to the Herfindahl–Hirschmann Index (HHI) which measures market concentration. It is also well documented that the Fund to Promote Industrialization of Agriculture Products (FUNPI) tax (suspended in 2015) burden fell most heavily on the producers (upwards of 80 percent), while groups with more influence and market share, such as brokers and traders, as well as exporters, collectively bear less than one-fifth of the extra costs—it also distorts prices, encourages smuggling, and its revenue has widely been misused (CEM 2015). Discrepancies in amounts imported by other countries and exported by Guinea-Bissau also imply potential corrupt practices between traders and port officials, and highlight the lack of a tracking system for merchandise at the country’s only port. Lastly, the fear of land grabbing by government elites is considered one reason why smallholders remain in cashew, so as to bolster their claims on land.⁴⁹

156. **The business environment is skewed towards the elite interests whereas the appointment of civil servants is often based on patronage and corruption objectives rather than on public administration needs or merit** (Figure 4.3). The close-knit nature of this group discourages transparency, and the fraudulent practice of hiring employees that are recorded in the payroll system but do not work in the public administration (“ghost workers”) is common. In 2009/2010, the Government completed, for the first time in recent memory, a full-fledged audit of its public administration, which identified 3,378 ghost workers, equivalent to 15.2 percent of the total employment for the Government of Guinea-Bissau, resulting in significant savings (CFAF 122 million per month). The country does not have an asset-recording and disclosure process for civil servants, government’s executives or members of parliament.

⁴⁹ See Temudo and Abrantes (2014).

Figure 4.3. Corruption is endemic in Guinea-Bissau (percent of businesses)



Note: 2009 for Guinea-Bissau, latest available data for all others.

Source: World Bank Enterprise Surveys and World Bank staff calculations.

157. **Another common form of rent extraction is the misappropriation and misallocation of public resources.** The last IMF technical assistance mission found that extra budgetary expenditures bypassing standard procedures still represent an estimated 25 percent of government spending. Political elites have been associated with embezzlement and misallocation of resources on many fronts. FUNPI, a fund created to increase access to finance and to promote the industrialization of the agricultural sector, has been heavily misused. There is evidence that a transport infrastructure tax that collects as much as CFAF 1 billion (US\$2 million) a year has been financing expenditures unrelated to roads (its original intended use). Part of the subsidies on gasoline and oil/diesel for power generation are stolen and used for private cars and trucks. In education, the money paid by parents of students in secondary school goes directly to schools via a local committee responsible for deploying the resources. These committees are not subject to proper accounting procedures. Health workers, equipment and supplies are illegally diverted from public health centers to private clinics to serve mostly the elite in the country. The military has also been reported to misappropriate public revenue.

158. **Illicit financial flows in and out of Guinea-Bissau constitute another sizable form of corruption.** Trade misinvoicing, analogous to trade-related money laundering, is an unlawful method for moving capital in and out of a country by misreporting the value of a commercial transaction on an invoice submitted to customs.⁵⁰ An evaluation of United Nations Conference on Trade and Development (UNCTAD) trade data reveals structural differences between Guinea-Bissau exports to its trading partners and its trading partners' records of imports from Guinea-Bissau (and vice versa) that are much larger than normal discrepancies that might be found in national accounts or from statistical errors.⁵¹ When Guinea-Bissau reports US\$150 million of exports to the world, the world reports importing more than US\$300 million of imports from Guinea-Bissau. Similarly, when Guinea-Bissau reports importing US\$200 million from the world, the world reports exporting more than US\$400 million to Guinea-Bissau (see Figure 4.4.). The

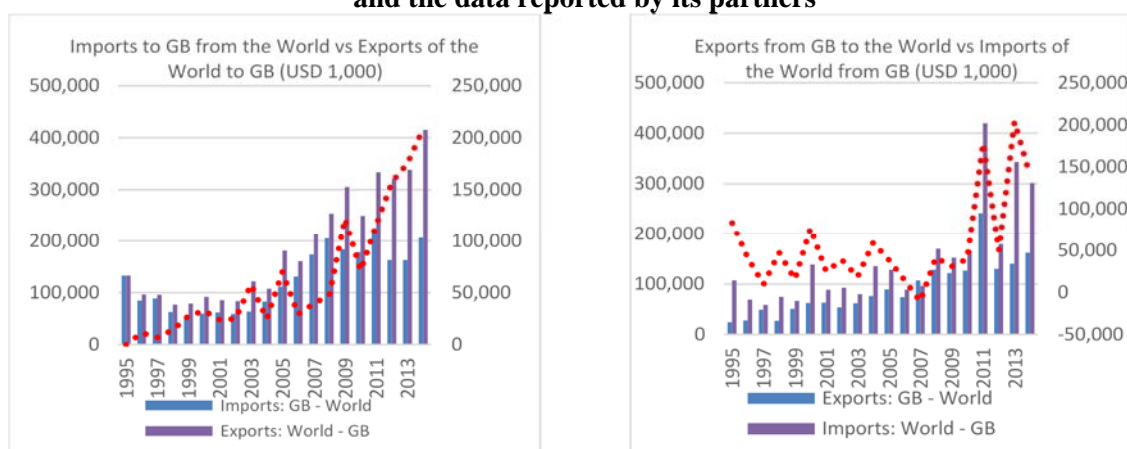
⁵⁰ See <http://www.gfintegrity.org/issue/trade-misinvoicing>. Trade misinvoicing is a method for moving money illicitly across borders which involves deliberately misreporting the value of a commercial transaction on an invoice submitted to customs. A form of trade-based money laundering, trade misinvoicing is the largest component of illicit financial outflows measured by Global Financial Integrity.

⁵¹ Trade data from other Sources are unavailable for the recent years for Guinea-Bissau. The data in this section are all from UNCTAD, as of January 2016.

relative stability of the amounts of the difference suggests that this is probably more related to trade misinvoicing rather than to glitches in measurement. At the product level, Guinea-Bissau reports twice less petroleum imports than its commercial partners' report they export to the country. On the exports side the differences are even more striking. While Guinea-Bissau reports exporting almost no fish or wood products to the World, its commercial partners report importing such goods in amounts equivalent to 30 percent of Guinea-Bissau exports.⁵²

159. **The amount of and competition for rents has increased in recent years with the intensification of the international drug trade, which uses Guinea-Bissau as a transshipment location.** In recent years, the international drug trade between Latin America and Europe took hold in Guinea-Bissau, with the West African nation serving as an entry point from which drugs are trafficked onwards by land and air. Estimates of trafficked narcotics volumes are difficult to obtain. Based on international seizures reported by the United Nations Office on Drugs and Crime (UNDC), trafficked cocaine in Guinea-Bissau could be valued above US\$16.9 million (3.4 percent of GDP) in 2005, and is likely to have increased considerably in value since that time. Cocaine flows surged in the aftermath of the 2012 military coup, and there is considerable evidence of military involvement in the drug trade (see Box 4.2).⁵³ Given the high value of the drug trade, it can be concluded that rents accruing from it to the armed forces are substantial.

Figure 4.4. Important differences appear between bilateral trade data reported by Guinea-Bissau and the data reported by its partners



Source: World Bank staff calculations based on UNCTAD data.

⁵² Looking at Guinea-Bissau's trading partners allows for the identification of the direction of potential trade misinvoicing, although it is difficult to underline any specific directions on the Guinea-Bissau export side.⁵² Such patterns are however clear on the Guinea-Bissau's import side, and some trade misinvoicing seem to occur with Portugal—the former colonizer- and Senegal –its biggest neighbor. Especially for Portugal, petroleum and oil products account for the main difference between the two recorded trade flows.

⁵³ D. O'Regan, and P. Thompson, "Advancing Stability and Reconciliation in Guinea-Bissau: Lessons from Africa's First Narco-State," Special Report (Africa Center for Strategic Studies 2013).

Box 4.2 Elites and the illegal economy in Guinea-Bissau

Guinean elites have a history of involvement in clandestine and illicit activities. There is indication that cocaine trafficking emerged in the mid-2000s, coinciding with President Lansana Conté of neighboring Guinea brokering a deal between the exiled Guinean president Nino Vieira and a number of key political and military figures in Guinea-Bissau to secure the former's safe return and successful election. Recently, an estimated 25 tons of cocaine transited through Guinea-Bissau between April and July of 2012 (O'Regan & Thompson, 2013). The arrest on charges of drugs trafficking by the United States Drug Enforcement Administration (DEA) of the former chief of staff of the navy, Rear Admiral José Américo Bubo Na Tchuto in a sting operation, and the subsequent indictment of the then chief of staff of the armed forces, General Indjai in April 2013, brought the trade to a temporary halt. It is suggested that it has since resumed, with small quantities flown by passengers (that is "mules") in commercial flights from Brazil, and more generally from Latin America. The Na Tchuto arrest may provide clues about the amounts of money involved, because the deal the Admiral had agreed to include a US\$1 million payment for every ton of cocaine passing through.

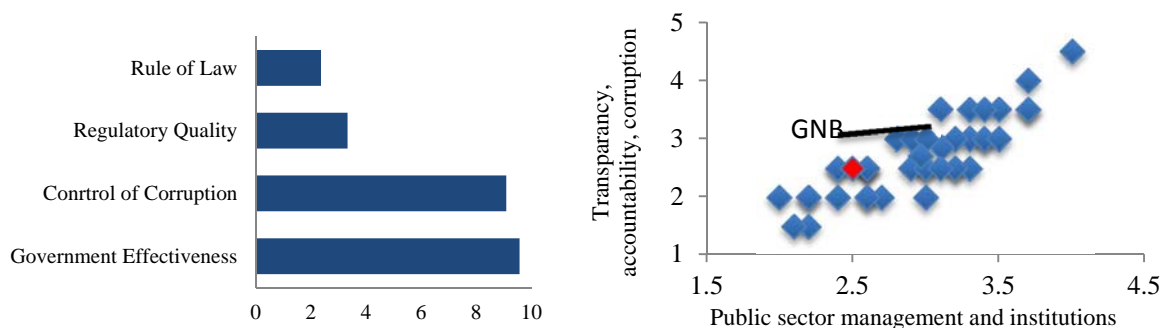
However, as long as the extension of state authority remains weak, Guinea-Bissau remains vulnerable to not only cocaine trafficking, but also to other illicit economic activities that can undermine development and stability. For the elites in the Guinean context, cocaine is just one of a variety of opportunistic items from a wide spectrum of activities varying from the legal to the criminal. Probably equally, and possibly more profitable, partly illicit opportunities include illegal fishing (or rent capturing from selling fishing licenses) or trade of precious, protected timber destined for China, which increased immensely as a consequence of the 2012 coup. On a smaller scale, the trafficking of illegal migrants, the sale of diplomatic passports, and weapon trafficking are equally worrisome.

Source: UNODC, 2013; ISS, 2013; <http://www.irinnews.org/report/84518/guinea-bissau-lowering-the-light-weapon-load>.

4.4 Rent extraction is facilitated by weak public governance

160. **Guinea-Bissau ranks poorly on most of the governance indicators.** Guinea-Bissau scores in the bottom 10th percentile on all indicators measuring public sector capacity in the World Bank's Worldwide Governance Indicator (WGI) (Figure 4.5). These indicators measure performance in control of corruption, government effectiveness, regulatory quality, and rule of law. On the latter two measurements, the country ranks as low as the 3rd percentile. Other rankings produce results along the same lines.

Figure 4.5. Guinea-Bissau ranks among the bottom 10 percent globally on the quality of governance
(Percentile rank, 0 worst, 100 best)



Source: CEM, 2015.

161. **The weak public financial management framework of Guinea-Bissau is one of the main areas where the lack of good governance is more evident, limiting the efficiency of public resources.** There are gaps in the existing PFM system which need to be addressed to enable the government to administer public resources while minimizing fiduciary concerns. The budget process lacks sufficient commitment controls, is plagued by significant off-budget expenditures, does not follow strict procurement, accounting, and reporting procedures, and lacks a credible set of internal and external controls. The overall legal and regulatory framework that governs the budget process is weak. A stronger process for budget execution, including fiduciary safeguards, will be necessary to administer both Official Development Assistance (ODA) and domestic revenue.

162. **Implementation of a credible budget process with sufficient internal and external controls remains a major challenge for Guinea-Bissau, after many systems were halted after the 2012 coup.** Both the 2009 Public Expenditure Management and Financial Accountability Review (PEMFAR) report and the 2013 Public Expenditure Financial Accountability (PEFA) assessment show that most of the modest gains recorded between 2009 and 2011 have subsequently been lost.⁵⁴ Whereas improvements had been made in budget credibility and reporting, and a new electronic PFM software system was mounted, these advances have largely stalled and some have been reversed, as PFM institutions have been regularly circumvented since the coup of 2012. Examples of items setback include preparation of quarterly budget reports for the National Assembly, attempts to strengthen budget preparation and execution through the use of the budgetary software system SIGFIP,⁵⁵ and the adoption of a budgetary nomenclature in line with WAEMU standards (CEM 2015).

163. **Consequently, the budget and the implementation of the government program and policies are disconnected.** It is a well-established norm that a budget is only useful as a policy tool if it is realistic and comprehensive, with clear lines to government priorities which can be closely monitored and enforced.⁵⁶ For Guinea-Bissau, the recent PEFA report shows that the budget exercise is generally an academic exercise, with ministries largely repeating prior years' allocations with only limited consideration of policies and government programs. Therefore, spending units and ministries often ignore the budget and find ways to implement their priorities through a variety of means, including off-budget sources of financing and unreported expenditures. This process undermines the usefulness of the budget and is prone to rent extraction.

164. **Existing systems of internal and external control are not functional, creating opportunities for misappropriation of rents in virtually every sector of the economy.** Unlike ex-post financial audits, internal controls are aimed at providing corrective action as the budget is being used. Yet, the few existing mechanisms of control are limited in scope, capacity, and independence. For instance, an inspection service exists within the Ministry of Finance (Inspectorate General of Finance) but it awaits the promulgation of new draft legislation, and its activities are limited and subject to ministerial and Council of Minister approvals. The Treasury Committee, which used to impose both cash-management and fiduciary controls, closed down in 2012. The procurement system has seen some improvements but remains underdeveloped; it is

⁵⁴ The 2009 PEMFAR and the 2013 PEFA reports describe at length many weaknesses in public financial management concerning all key areas.

⁵⁵ SIGFIP is a financial management information system (FMIS) software that is widely used in French-speaking Africa.

⁵⁶ This is a process which requires consultation with relevant stakeholders.

understaffed, with very weak capacity and limited operational means. There is a need to develop new procedures manuals, including national standard bidding documents for the procuring organizations, procurement performance review mechanisms, and electronic tools to monitor and report procurement transactions.

165. While Guinea-Bissau, in 2009, officially adopted WAEMU PFM directives, they are yet to be ratified as national law, thereby limiting the effectiveness of internal and external controls.⁵⁷ The directives adopted are intended to provide the basis for: (1) improving the reliability and timeliness of macroeconomic forecasts to better achieve annual and multi-year budgeting; (2) budget and financial control to improve budget preparation, commitment management, control and accounting, as well as timely and accurate budget execution reports; (3) improving payment management and control to produce more timely and reliable in-year financial execution reports, and to reconcile these reports with the budget execution reports published by the Directorate of the Budget (DGO). Special attention is required in the area of human resources and payroll system administration, including the incorporation into the system of the defense and security forces, which are not currently covered under the scope of the payroll application.

166. The tax framework is outdated and tax administration is highly ineffective. The low revenue intake has been the result of the narrow tax base and the existing weakness in tax policies, and also has been the result of poor administration. Improved business processes can increase total tax revenue without increasing the tax rate by more efficiently collecting actual tax payables. Reducing the burden associated with tax payments for companies will not only help the private sector grow but will also provide weaker incentives to avoid paying taxes. This would strengthen the collection effort (CEM, 2015). A functional Treasury single account (TSA), which could, among other things, help restore control over public resources for better service delivery is also not in place.

167. Public administration is also undermined by a large bureaucracy, notably the overrepresentation of the military. The size of the public sector in Guinea-Bissau is large and puts a strain on an already limited public sector resource base. In 2010, the public sector in Guinea-Bissau was 2.5 percent of the population, above that of Senegal (1.1 percent) and comparable to some of the largest in the region. Employment in the public sector has been increasing by 4 percent per year, faster than population and revenue growth, but due to “ghost workers”, this rate could be grossly understated.⁵⁸ General administration and education, and, to a lesser extent, the health sectors, were among the main beneficiaries. Nonetheless, the military and paramilitary sectors account for the largest share of overall public employment. There are also no systems in place to track civil servants’ time of duty in public administration, which undermines budget credibility, particularly since contingent liabilities related to labor are unknown. Salaries represented about 50 percent of current expenditures and about 35 percent of total expenditure in 2013 (or 5 percent

⁵⁷ In 2009, the West African Economic and Monetary Union (WAEMU) adopted six new public financial management (PFM) regulations (Directives) covering transparency in public finances, budget preparation and execution laws, government accounting, budget classifications, central government chart of accounts, and central government operations *tableau des opérations financières de l’Etat* (TOFE).

⁵⁸ The first public sector census completed in 2010 identified 3,378 ghost workers and double dippers, or 15.2 percent of the total employment for the government of Guinea-Bissau. Some public employees are not officially registered as civil servants but receive a bonus only, and are only paid occasionally.

of GDP), corresponding to about 60 percent of domestic revenue and 41 percent of revenue including grants, highlighting the importance of this problem in an environment of low revenues.

168. **Technical capacity in the public sector is low.** Human capital may be a binding constraint to efforts to improve the capacity of the public sector. The 2015 CEM demonstrates that Guinea-Bissau's civil service exhibits high capacity gaps and skills mismatches across line ministries. The latest civil service census confirmed that only 24 percent of total public sector workforce had six years of formal education or more, of which almost 50 percent held tertiary level qualifications. Another 15 percent had no mastery of basic numeracy and literacy skills.

4.5 The way forward for stronger governance and less fragility

169. **Repeated cycles of fragility and weak institutions have broken the social contract in Guinea-Bissau.** The vicious cycle of fragility and weak governance results in the neglect of the vast majority of the population, most of whom lack access to stable and reliable basic services and economic opportunities. Fragility and weak institutions are counter-productive and distortionary for growth more generally, creating significant barriers in the development of the private sector and competitive markets. Benchmarking analysis prepared for this SCD shows that Guineans fare worse than the regional and world averages on most economic, social, and institutional fronts, reiterating the country's complex yet much needed task of constructing the fundamentals for development through the strengthening of the social contract (Annex 1A). Among the main consequences of this loose social contact is widespread poverty.

170. **A new and inclusive strategy which capitalizes on short-term opportunities while addressing longer-term constraints will be needed to move Guinea-Bissau forward.** Donor pressure alone is unlikely to engender an environment for long-term change. At the same time, minimal pressure may legitimize weak governance and fragility. Instead, this report argues for a mixture of strategies that combine direct engagement of government with increased participation of other local, regional, and international actors to create a critical mass of demand for transparency and accountability and to increase political participation. A development agenda to move Guinea-Bissau away from the current high-poverty, low-growth and high-fragility equilibrium will necessarily require engagement with the Government. Explicitly excluding the elite from the reform process may not be realistic or even effective in challenging elite domination. On the contrary, it can exacerbate rather than lessen fragility. Stability is a prerequisite for much-needed uninterrupted poverty reduction and growth. However, other strategies should be pursued in parallel to gradually start relaxing the existing political constraints.

Box 4.3 Strengthening Public Sector Performance in Service Delivery through Partnership with Social Enterprises

Social Enterprises (SEs) provide innovative and cost-effective development solutions through combining business strategies to achieve social impact, rather than maximizing financial profits. They target areas where there are persistent gaps in the delivery of basic services that governments and markets have not adequately addressed, which includes working in areas such as education, maternal and child health, water and sanitation, and raising agriculture productivity. SEs manage to reach the poor by working closely with local communities, raising awareness, designing suitable, acceptable and easily available solutions, and providing value for money and financing solutions to fit the customers' needs and profiles. SEs can be valuable partners to governments, in particular those struggling to extend basic services to the unserved and underserved populations. By working with SEs, governments can harness the innovations and strategies that social enterprises have developed to reach the poor. Collaboration can take on many forms, including replicating the SE's model, encouraging SEs to expand, contracting directly with the SEs, or providing a supportive environment in which grassroots SEs can grow. Below are a couple of examples of the impact social enterprises have made in the region.

Replicating innovation for better educational outcomes. In Liberia, about 42 percent of children are out of school and the Government, strapped for resources, sought bold innovative solutions to address this problem. For this, they looked at Bridge International Academies (Bridge), a Social Enterprise in Kenya that provides low-cost private schooling in poor neighborhoods, at a cost of about US\$80 per year— or a quarter of the US\$318 cost for a Kenyan public school pupil. Bridge's low cost business model is based on using para-skilled teachers who deliver standardized curriculum provided on tablets, which also enables close tracking of the curriculum delivery and attendance. School management is centralized, further reducing overhead costs. Despite its lower costs, educational outcomes have proven to be higher—a Bridge child in a low income neighborhood had a 40 percent greater chance of passing the national exam than his public school counterpart. Since the first academy opened in 2009, Bridge currently operates over 450 schools, providing education to more than 110,000 low income students in Kenya, Uganda, and Nigeria. Under the Government of Liberia's Partnership Schools for Liberia program, Bridge will implement its model in about 50 Liberian public schools in a one-year pilot program. Schools will remain free public schools and be subject to the Ministry of Education's standards and expectations, but Bridge will be in charge of curriculum delivery and administration. The partnership seeks to replicate Bridge's previous successes to rapidly improve schooling quality and results in Liberia, and if successful could expand the program nationwide.

Increasing agricultural productivity and livelihoods. Agricultural productivity is another area where even moderate improvements can have significant impacts on the household income. One Acre Fund (OAF), a social enterprise working in Kenya, Tanzania, Burundi, and Rwanda, provides farmers with support throughout the value chain, including financing for farm inputs, distribution of seed and fertilizer, training on agricultural techniques, and market facilitation to maximize profits from harvest sales. OAF currently serves 305,000 farm families who have gained an average 55 percent (or US\$137) increase in annual income. The OAF model has also proved to be successful in the context of smaller, post-conflict countries. In collaboration with the Government of Rwanda, OAF entered the country in 2011 and currently serves 113,500 farmers who have experienced a 67 percent increase in annual income (corresponding to US\$99). Similarly, OAF entered Burundi in 2012 and has served 40,200 farmers whose income increased by 99 percent (or US\$67). There is further evidence of positive spillover effects in terms of increased agricultural productivity in farm fields neighboring OAF clients.

171. Empowering the poor through increased demand for transparency and accountability, and also through direct, more effective delivery of basic services, can be a major catalyst in the process of strengthening institutions and addressing behavioral norms

in public and political spheres. One approach is to encourage citizen engagement and demand for accountability and transparency in government performance. This includes deliberate policy efforts to increase access to and dissemination of information of general interest, and to strengthen mechanisms that channel broad-based demands for improvements in public goods, dissatisfaction with underperformance of public officers, and discontent with rigged politics. Another approach is working directly with beneficiaries, for instance through community-driven programs implemented by NGOs, to address urgent needs such as water and sanitation, school and health services, nutrition programs, rural access roads, and micro-finance (see Box 4.3 for examples of alternative service delivery mechanisms which have been used in some countries to raise income and productivity while circumventing the issues of fragility and elite competition.) Another approach involves promoting greater private sector participation – with support from reputable institutions such as the International Finance Corporation (IFC) and the Multilateral Investment Guarantee Agency (MIGA) – in the agriculture value chain and other sectors to spur confidence and leadership outside of the existing elites. International actors like WAEMU, ECOWAS, the African Union and the donor community can also harness forces and align incentives in favor of transparency and stability. International development institutions, in particular, can increase donor coordination and leverage their comparative advantage in data and diagnostics to improve the quality of political engagement.

172. The way forward should also involve combining stronger incentives and behavioral norms with capacity building. There is a need to improve the minimum level of public goods provided to citizens and to restore the ability of the State to efficiently collect and spend public funds. Public sector capacity needs to be improved through the creation of better standards for hiring of public servants, better training, and other capacity development measures. Public financial management systems are at the same time both archaic and cumbersome, requiring better and more simplified systems of internal and external control, such as better procurement, auditing, and inspection services more generally. Reallocation of expenditures from sectors such as the military toward those that build human, physical, and institutional capital is another way to address weak governance. Finally, a more business-friendly environment to accelerate investments and economic growth can be achieved through a better business regulatory environment, more competitive bidding, easier procedures for registering a business, and better contract-enforcement, and also by making regulatory bodies more independent. These measures can strengthen governance and improve the ability of the state to provide for its citizens, to restore the social contract, to reengage the common citizen, and to set forth a path for stable progress.

5 SUSTAINABILITY CHALLENGES

- *The structure of the economy in Guinea-Bissau subjects the country to multiple economic, environmental, and political risks moving forward, including an accelerated depletion of its natural wealth, a weak political settlement, and the interlinked elite competition for rents.*
- *Economic activities are extremely concentrated, limiting growth opportunities and leaving the economy vulnerable to external, political, and natural shocks. Reduced fiscal space and dependence on grants from the international community, which in turn are unpredictable due to endemic fragility, will continue limiting the ability of Guinea-Bissau to tackle its primary developmental challenges.*
- *The current manner of utilization of natural resources with misallocations of their associated rents results in Guinea-Bissau depleting rather than building its total net capital, undermining growth potential.*
- *Important drivers of fragility that remain unaddressed could fuel instability and should therefore be focused on moving forward. They include an unfinished political transformation, the existence of military interference in political and economic affairs, a weak justice system, a captured economy, weak institutions, and a strong rural-urban divide.*
- *Engendering sustainable growth and boosting shared prosperity in Guinea-Bissau is contingent on creating political stability and achieving the right mix of macroeconomic policy choices coupled with improved management of existing natural and environmental resources*

5.1 Structural issues and existing and emerging risks threaten economic sustainability

Limited diversification and internal and external sources of instability

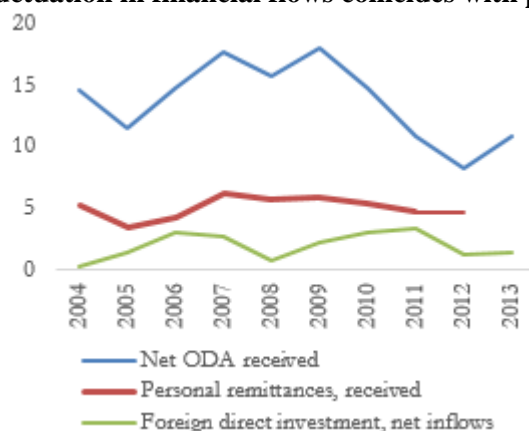
173. **Notwithstanding the importance of the cashew sector in economic life in Guinea-Bissau, economic activities are extremely concentrated, limiting growth potential in the future.** The dependence on raw cashews has grown overtime at the expense of other activities and sectors with higher valued added. A recent IMF report shows that both export diversification (product and partners) and quality of exports has been declining in Guinea-Bissau. In fact, the country has the least diversified export base in the WAEMU.⁵⁹ Increasing diversification and quality upgrading in Guinea-Bissau to levels observed in WAEMU between 2001 and 2010 could result in an increase in the average real growth rate by about 1 percentage point (IMF 2014a).

174. **The narrow economic base represents a major risk to external sustainability because it leaves the country vulnerable in terms of trade shocks.** While the recent trend in cashew prices on the international market has been favorable, a sudden reversal would have a deleterious impact on the country's external accounts. The same would also be true for oil prices, given the dependence on imported petroleum products. Frequent instances of political instability are also known to interrupt financial flows, undermining external stability (see Figure 5.1). Nevertheless, Guinea-Bissau's real effective exchange rate is assessed to be broadly in line with the country's

⁵⁹ See <http://www.imf.org/external/pubs/ft/scr/2015/cr15195.pdf>.

fundamentals, and the monetary policy framework in the WAEMU has produced substantial benefits in terms of price and exchange rate stability and convertibility of the CFA franc (Karas, 2006). At the same time, maintaining macroeconomic stability will be made more challenging if the business cycles of the member countries are not well synchronized and if stabilization mechanisms aimed at absorbing common and idiosyncratic shocks are absent or ineffective.

Figure 5.1. Fluctuation in financial flows coincides with political events



Source: WDI, 2015

175. Most indicators point to substantial stability risks in Guinea-Bissau's financial system. The financial system is shallow, informal, and extremely concentrated, and oversight is weak (IMF, 2015). Relative to other WAEMU countries, the banking sector which dominates Guinea-Bissau's financial sector is less liquid with higher non-performing loans. It is also undiversified, where 25 percent of bank lending is concentrated in the cashew sector. A poor judicial system, a heavy guarantee mechanism, and lack of operationability all incentivize informality. Compliance with key prudential benchmarks is also lower, which undermines the overall stability of the system.

Fiscal sustainability

176. Limited fiscal space will continue to hamper the ability of Guinea-Bissau to tackle many of the development challenges identified. As is the case in many fragile states, weak capacity is reflected in a limited scope of revenue collections. With a relatively narrow tax base, concentrated on a small number of revenue headings, which primarily cover duties on imports and cashew nut exports, public finances are significantly below the target of 17 percent required by the Convergence, Stability, Growth and Solidarity Pact of the WAEMU. There is an overreliance on donor grants, which represented 43 percent of government total revenue in 2014. On the expenditures side, the control of the wage bill is a big issue. Payroll expenditures represented 73 percent of tax revenue in 2014, well above the target of 35 percent for the WAEMU zone. Rigidities in compensation-related expenditures have traditionally limited public investments in social and public infrastructure, which increases the risk of accumulating domestic arrears linked to wages. In 2013, they represented nearly 52 percent of total domestic arrears.

177. Guinea-Bissau faces a moderate risk of fiscal distress, but the sustainability of its fiscal accounts is dependent on grants from the international community. With the relatively

low revenue base, which traditionally is outpaced by expenditures, the country has been accustomed to running deficits. In fact, the country suffered from fiscal stresses in the early 2000s with an overall fiscal deficit above 10 percent of GDP and with an overall public sector debt stock in excess of 400 percent of GDP. While the completion of the Heavily Indebted Poor Countries Initiative in 2010 helped to bring Guinea-Bissau's fiscal deficit and debt down to sustainable levels (see Figures 5.2 and 5.3), the gap between the actual and structural budget balances have started to deteriorate. The overall fiscal deficit increased to 2.2 percent of GDP in 2012, from 1.4 percent in 2011. To contain the risk of debt distress and ultimately support long-term debt sustainability Guinea-Bissau will, among other things, need to strengthen debt management practices, as well as implement necessary reforms for the economy to achieve higher rates of growth.

Figure 5.2. Overall fiscal balance and public debt manageable levels

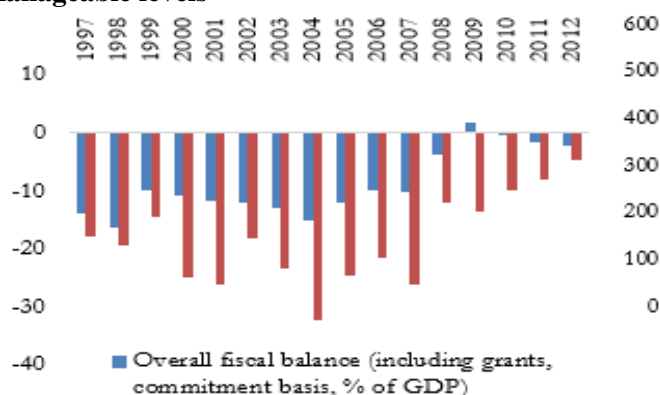
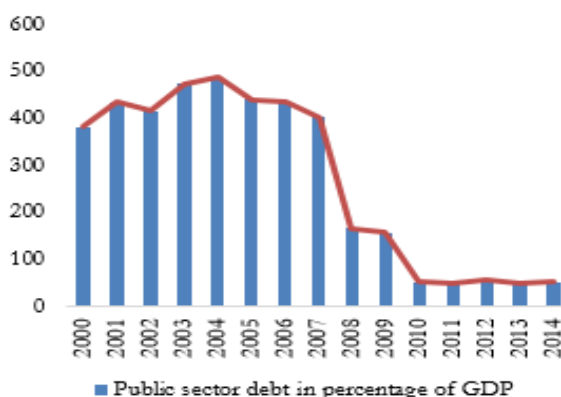


Figure 5.3. Debt has declined to manageable levels



Source: IMF (2015)

178. **Fiscal sustainability is anchored by the recent approval of a three-year program by the IMF under the Extended Credit Facility (ECF) program.** The program is intended to consolidate the country's fiscal position through better expenditure management and enhanced revenue mobilization, to strengthen institutional reforms, to mitigate vulnerabilities, and to develop private sector activities to support growth and job creation (IMF, 2015).⁶⁰ Notably, there is a focus on improving the policy framework by addressing governance and security issues, strengthening budgetary transparency as well as public investment and debt management, and improving the compilation of statistics. Efforts to improve budget execution and public financial management are expected to create a platform to tackle a number of governance-related issues, while enhancing revenue mobilization should help to build fiscal space for infrastructure and social spending (see Table 6.1). Effective debt management calls for a prompt upgrade of current practices and continued reliance on concessional borrowing.

⁶⁰ <http://www.imf.org/external/pubs/ft/scr/2015/cr15194.pdf>.

5.2 Risks to environmental sustainability are ultimately risks to long-term inclusive growth

179. **Most of Guinea-Bissau's wealth lies in its natural endowments, especially renewable natural resources which account for over 90 percent of this wealth.** Guinea-Bissau has the highest proportion of natural wealth per capita in the West African region, accounting for approximately 47 percent of the country's wealth. This includes agriculture land (crop and pasture land), fisheries, forests (timber, non-timber forest resources, carbon), and natural habitats and ecosystems protected in national parks. It is also among the few countries in West Africa where development has had limited negative impact on the environment. This may be rapidly changing: tree cover loss has resulted in a reduction of forest cover by 3.6 percent between 2010 and 2014. Forest cover had shrunk by 3.4 percent in the ten years before.

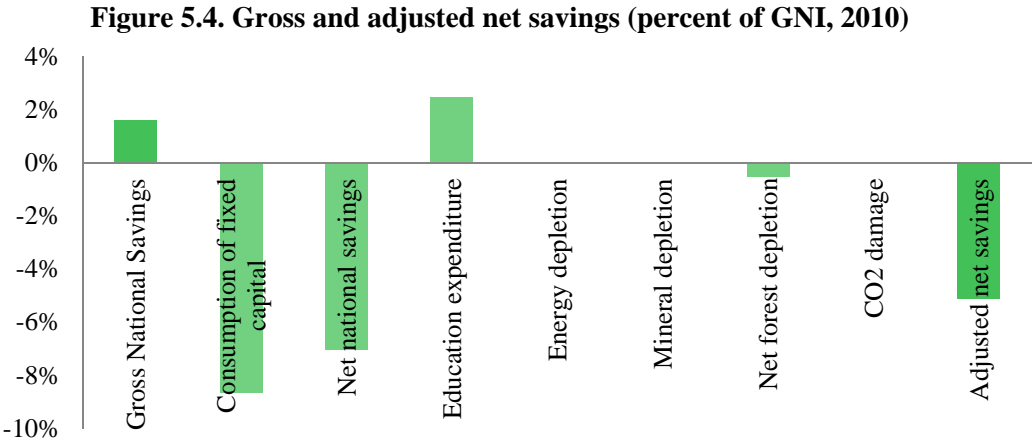
180. **The natural resource base of Guinea-Bissau is essential for the livelihoods of local communities, and for biodiversity and public revenue streams.** The country's ecosystems provide multiple services such as food, water, shelter, income, and resiliency to climate change. Forests help support hydrological cycles, preserve soil quality, and protect against erosion, which also serves as a buffer against desertification and a carbon sink. Mangrove forests provide neighboring villages with flood defense from rising sea levels, and act as an essential breeding and nursery ground for the fishing stock. The goods and services supported by the country's natural endowments also contribute to government finances. Exports of agricultural produce bring in much needed foreign exchange. Fishing licenses, on average, accounted for 15.5 percent of government revenue between 2009 and 2011. Improvements in forest governance and tax collection could result in greater tax revenue from the sales of timber and timber related products. Moreover, forests have the potential to provide the country with carbon credits to sell in international carbon markets.

181. **Sustainability of long-term growth is being mined by shrinking natural assets and a declining overall asset base.** Income, or GDP, results from the productive use of a country's assets. It can also occur from the depletion and monetization of certain assets such as timber and bauxite. To the extent that total wealth has decreased, largely as a result of mismanaged assets, prospects for nature-based growth will continue shrinking. Furthermore, considering the low investment in the physical and human capital of the country, the current mismanagement of natural resources means that Guinea-Bissau is depleting rather than building its total net capital. As noted above, at about 2 percent of GNI in 2010, savings and investments rates are exceptionally low in Guinea-Bissau. Estimates of natural capital show that natural-wealth adjusted net savings would be even more negative had current unsustainable resource exploitation rates in some sectors have been taken into account (for instance, logging and agricultural practices such as slash and burn techniques, and overgrazing of livestock). Poor management or mismanagement of mineral dividends such as phosphate, bauxite, and petroleum reserves pushed net savings rates down further (Figure 5.4).

182. **Weak capacity and governance as well as information gaps are largely responsible for the loss of valuable natural wealth.** Existing institutions for natural resource management are under resourced and face severe challenges, including lack of human resources and information, and data constraints. The Government is aware of the importance of the country's natural wealth, and since the early 1990s has put in place a number of agencies and plans to oversee the management of these resources. The initiatives are well placed, but not well financed. The lack

of approaches for natural capital accounting causes there to be limits on more explicit analyses of the costs and benefits of natural resource exploitation and management decisions. Resource management is largely dependent on official grants, and as a result of high fragility, aid flows have fluctuated widely. Weak governance leads to the indiscriminant felling of forests, which is taking a toll on the forest ecosystem. The poor state of the country’s energy infrastructure has increased the county’s reliance on basic fuels such as charcoal. Illegal fishing is widespread, and the weak institutional capacity to monitor and enforce licensing agreements is undermining the country’s marine fisheries. Some agricultural and forest-dwelling practices are hurting local ecosystems. Slash and burn techniques, and overgrazing of livestock, are not uncommon.

183. **Risks in the mining sector such as depletion, environmental degradation, and mismanagement of rents from mining are also high.** The supply of non-renewables is by definition limited, which means that depletion is unavoidable. Experience in other countries has shown that mineral resource extraction can lead to significant local environmental degradation (including, for instance, erosion, loss of biodiversity, and contamination of soil and bodies of water), to the detriment of local populations, particularly the poor who are the most directly dependent upon natural resources for daily subsistence, and the most vulnerable to experiencing negative impacts on their health and wellbeing from a degraded environment. Legal infrastructure has been built up to protect both the environment and the local communities that would be affected by mining interests in Guinea-Bissau. However, the capacity to enforce these laws and regulations is weak. Perhaps the biggest long-term risk to mining is posed by the limited capacity to absorb revenues and to transform them into other forms of wealth, or to directly transfer them to boost the incomes of the poorest members of society. Without effective and enforceable transparency arrangements, these economic rents can increase competition among the elite, which further increases fragility.



Source: World Bank (2014).

184. **Climate change adds extra pressure on the need to preserve natural habitats.** The country’s low lying coastal areas make up 61 percent of the country and are highly vulnerable to rising sea levels, stronger tides, and salinization of surface water and aquifers. These areas host approximately 80 percent of the population, the bulk of the country’s economic activity, and much of the country’s limited existing infrastructure. Increased risks of flooding and coastal erosion could lead to the disappearance of biodiversity reserves and agricultural land on which the local economy is based. Guinea-Bissau’s agriculture is also highly vulnerable to changes in rainfall

patterns. The recent NAPA (2011) identifies a reduction in rainfall of 11.7 percent by 2100 and increased irregularity of rainfall as the most serious climatic risks facing the country. Climate stress, in conjunction with anthropogenic pressure (especially slash and burn agriculture combined with cashew plantation and logging) has the potential to accelerate deforestation and degradation of mangrove and terrestrial forest cover.

185. Maximizing rents from natural resources in a sustainable manner requires managing important trade-offs. Mineral and petroleum extraction, plus the construction and operation of associated infrastructures, is likely to cause significant stress on national protected areas and their wildlife corridors, as well as on Bolama-Bijagos Biosphere Reserve. Policies to promote the expansion of lowland and bolhana rice cultivation, with a view to improving agricultural productivity and boosting food security, could come at the cost of mangrove forest. Carbon credits from REDD+ projects could bring many benefits in the long term (for instance, carbon sequestration, access to carbon credit revenues, and improved forest management) but could also result in restrictions on logging activities and timber revenues in the short term.

5.3 Some drivers of fragility remain unaddressed

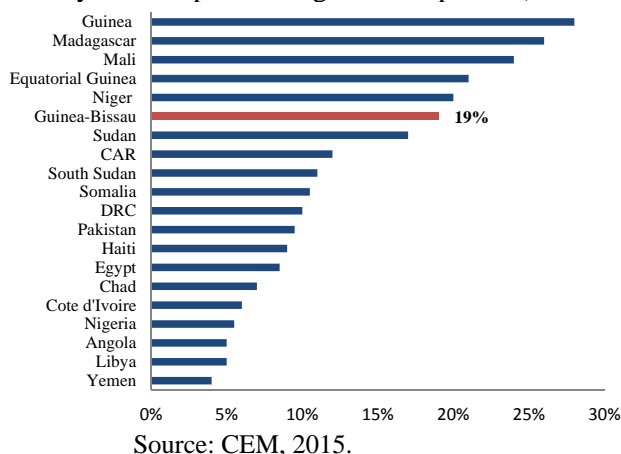
Unfinished political transformation

186. The country's history is marked by an unfinished political transformation driven by competition for rents. The constitution (adopted in 1991) is ambiguous about the division of labor between the offices of the president and the prime minister. This has created structural tensions between a president who is prevented by the constitution from serving as the president of a party, but at the same time has the right to dissolve the assembly and remove the prime minister; and a prime minister who hails from the majority party in the assembly, and can be strong as long as he controls the assembly through that party. In addition, factionalism is endemic. These factions are defined by shifting alliances among a small and exclusive elite made of security sector officials and politicians who are frequently also civil servants, businessmen, civil society, and NGO leaders, all in competition to secure access to segments of the Government. In Guinea-Bissau, the Government remains the primary tool for personal enrichment, whether through civil service positions, issuance of contracts to build public infrastructure and licenses to exploit natural resources (particularly for fishing and logging), access to loans (and protection from having to repay them), or profitable privatization opportunities. A government-toppling crisis is always a high latent risk in this context of elite capture and competition for rents. (Figure 5.5).

187. Internal competition between politicians and the different arms of government is a major risk to the current reform agenda. The current Government is undertaking a complex balancing act as it tries to mitigate a wide range of opinions, constituencies, and interests. Avoiding a political crisis is absolutely essential in the present circumstances in view of some of the very courageous but controversial reforms that the Government has initiated. This will require carefully calibrated support and a constant watch by the international community over political, economic, and security trends. The process of security sector reform (SSR) could trigger new instability if it happens or frustrations of unmet expectations if it does not take place. There is also a risk that the Government might be overstressing its ability if it moves ahead with too many difficult reforms in parallel. The Government is engaged in a careful balancing act between the need to maintain

the necessary alliances and compromises while at the same time promoting reforms that affect important vested interests within the military, political, and business establishment.

Figure 5.5. In 2014, Guinea-Bissau was among the countries most likely to experience a coup
(Probability of a coup occurring in 2014, percent)



Military interference in political and economic spheres

188. **The politicization of the security sector created a series of severe imbalances.** Since the end of the independence war, the Guinea-Bissau state has had difficulties handling the symbolic and financial weight of the armed forces. A formal merit-based system for career and rank attribution was never put in place. Instead, personal affiliation to certain politicians and military leaders and participation in political violence has been a necessity for career advancement. As such, the army is large compared to the size of the population and for a country that does not face significant external threats. Salaries for the army alone represents 30 percent of the total wages paid by the state. Despite the extensive demobilization campaigns over the years the troops-to-population ratio is still twice the West African average.

189. **Reform of the security sector is crucial but bears its own risks.** The army has been a source for rent-seeking and a key driver of the country's fragility. Reforming it by reducing its size and improving civilian oversight is crucial. Currently, the Government, with support of development partners, is developing a financial incentives system for soldiers in order to reduce the military's resistance to reform. So far, the focus has been on a special pension fund created to allow for the retirement and reintegration of more than 2,200 members of the defense and security forces. This was attempted in the past, but instead of army reform, the army became more demanding. If this were to happen again, the price for stability would be an increase in public payments to the military, posing large pressure on the fiscal accounts.

Impunity, weak justice sector, and lack of effective conflict resolution system

190. **Access to justice by all members of society, guaranteed by the constitution, is still far from real.** As with many other institutions in Guinea-Bissau, access to justice is often determined by social status, inclusion in a network of influence, and the availability of financial resources. The difficulty in obtaining proper adjudication is forcing people to depend on patrons with leverage, usually politicians or military, and thus reinforcing the patronage system at the expense

of a system based on meritocracy, equality, and rule of law. With such a dysfunctional legal system, hybrid forms of traditional and informal ways of justice administration and dispute resolution have emerged, particularly, but not exclusively, in the rural areas. This has its own challenges as vulnerable groups such as women and youth tend to have uneasy access to local authorities and their justice mechanisms. These judicial gaps can result in escalation to larger-scale communal violence.

191. **At the central level, Guinea-Bissau's justice sector faces great obstacles.** Cases of politicians suspected of embezzling public money, or members of the defense and security forces accused of involvement in violent crimes, if investigated at all, usually end up in judicial stand-offs. Judicial police and magistrates are often the targets of both corruption and intimidation, and the resulting impunity and the absence of rule of law have had a deleterious effect on judicial development beyond the criminal domain. For instance, the absence of mechanisms to enforce contracts and agreements has prevented investments in larger-scale agriculture and processing facilities. While natural resources are plentiful, the risks of such investments are significant in view of the weak regulatory framework and the lack of rule of law.

Rural-urban divide

192. **Lack of a government presence outside of Bissau is a defining feature of fragility, which has rendered the state illegitimate in the eyes of many.** Access to public services and possibilities to participate in public administration have been limited to the urban center. Unfavorable terms of trade persisted, with rural production used to subsidize imports benefiting the urbanized elites. The degradation of public institutions in the rural areas became even more evident after the 1998/99 civil war. The weak and uneven presence of the Government feeds the control of opportunities by closed elites. The Balanta tend to dominate the military, the Fulani and Mandingo dominate trade, and a variety of coastal groups, such as the Pepel, Manjak and Creoles, with a history of access to formal education, tend to have a strong presence in the administration. This reality has the potential to feed ethnic politics. The newly-elected government is making efforts to strengthen local capacity and moderate the rural-urban divide. Local elections are scheduled for the first time ever in 2017, and the Government has moved to appoint new regional governors.

But there are resilience factors

193. **The relatively peaceful relations between ethnic and religious groups, which has persisted despite decades of cyclical crisis, augurs well for building resilience.** Contrary to experiences elsewhere in the region, and despite an increasing reference to ethnicity and, to a lesser degree, to religion, ethnic relations and religion have remained remarkably peaceful. Guinea-Bissau is a small country with lots of cross-community personal ties, a strong nationalist narrative, and a common language, Portuguese kriol. Even the Balanta, who have been most affected by ethnic narratives have not instrumentalized ethnicity as a main banner for their grievances. Crises have taken place between political and military elites, but beyond the civil war in 1998/99 they have resulted in relatively few casualties beyond political assassinations, and have not trickled down to involve society.

194. **A vibrant if burgeoning civil society exists and is losing patience with the repeated political crises and military interference in political and economic spheres.** Building on the country's tradition of political mobilization, segments of the elite have eagerly seized upon the political liberalization of the 1980s and support of international partners to build a civil society, NGOs, and private media. They have not been immune to politics, bad governance, corruption, and patronage, but have nevertheless created a network with rural roots that can help support reforms, and strengthen accountability, communication, and information sharing, while helping to mediate disagreement. Attempts to build strategic networks, and efforts to build coalitions to gain broad support from different spectrums of society to fight corruption are in their embryonic stages but reflect a growing demand from citizens for better governance. Advances made by Guinea-Bissau in terms of access to information, albeit from a relatively low base, was noted in the 2015 Freedom House report.⁶¹ The very high levels of participation in the 2014 elections and the orderly manner in which these took place are a clear indication of a wish to break with the past and to move forward based on democratic and consensus-building oriented principles.

195. **West Africa has recently experienced some of the most important economic and political progress of the African continent, and Guinea-Bissau's integration in these regional organizations had a significant impact on the country's recent developments.** In particular, membership in ECOWAS has helped generate a certain degree of stability, including more recently through the deployment of the ECOWAS Security Mission in Guinea-Bissau (ECOMIB) to support the transition. ECOMIB is viewed as an important stabilization factor for upholding political balance and avoiding a standoff between the President and the Prime Minister. Similarly, membership in the West African Economic and Monetary Union (WAEMU) has provided some degree of economic stability and has helped the country avoid the inflationary pressures that are normally associated with political crisis and the temporary withdrawal of international financial support.

⁶¹ Guinea-Bissau was among a group of eight countries which recorded an improvement.

6 PRIORITIZATION OF CONSTRAINTS ON PROGRESS TOWARDS THE TWIN GOALS

- *This SCD identifies three main interconnected clusters of areas of binding constraints: 1) lack of inclusiveness and low rural productivity; 2) low and unstable growth; and 3) fragility and weak governance.*
- *The three areas reflect a context where the basic elements of well-being and economic opportunities are inadequate and unequally distributed, forcing people to be trapped in poverty, and where economic growth has been unsatisfactory and volatile. Fragility and weak governance are found to undermine most economic, social, and political structures, further reducing opportunities for shared prosperity.*
- *Top urgent priority areas in which to mitigate these binding constraints include improving basic service delivery, raising productivity in agriculture, diversifying the economy, strengthening market support services, and addressing allocative, technical, and regressive inefficiencies in public spending.*
- *Addressing the impediments to inclusive growth requires confronting the vicious cycle of fragility and elite capture by using flexible strategies to engage directly with the elite and with other actors who legitimately circumvent it to enhance their livelihoods, and also by creating demand for transparency and accountability.*

6.1 Prioritization of development constraints in a challenging politically environment

196. **This chapter brings together the various development challenges confronting Guinea-Bissau under three overarching and interconnected binding constraints, and outlines a number of priority policy actions.**⁶² The evidence in the preceding chapters suggests that the majority of the citizens in Guinea-Bissau are poor, half of which are in a condition of extreme poverty. This is due in large part to limited access to basic services, to low and volatile growth and limited economic opportunities. This has been perpetuated by fragility associated with political events and distortionary policy interventions which have encouraged a large public sector, constrained the growth of the private sector, and diverted much of the public resources toward private gain of the elite. On the basis of this evidence, the SCD outlines three clusters of constraints to poverty reduction and shared growth in Guinea-Bissau: (1) *lack of inclusiveness and low rural productivity*; (2) *low and unstable growth*; and (3) *fragility and weak governance*. In this regard, many of the actions advanced in this section focus on steps to challenge this established framework with the objectives of fostering better delivery of public service, creating an environment to enhance private sector performance, and creating opportunities for shared prosperity.

197. **Results from the prioritization exercise highlight entry points where policy intervention can achieve success, but they also reveal some feasibility risks.** In the first two areas of constraints (low inclusiveness and rural productivity, and low and unstable growth), there is broad consensus in the diagnostics and consultations about the selected policy actions contemplated being able to deliver the desired poverty impact, with some actions even becoming

⁶² The order in which the overarching constraints are presented should not be taken as an indicator of importance.

entrenched. However, success of many of the proposed actions will of necessity require advancements in overcoming some of the barriers associated with fragility and elite capture within the society. In this regard, actions to strengthen the political system to rely on a more participatory and decentralized approach, which is expected to deliver the highest gains in terms of reducing poverty, ranks fairly low in terms of feasibility. In fact, many of the more difficult governance-related reforms score poorly on feasibility and traction, pointing to an unwillingness to break from the established order. This suggests that gains from addressing the other constraints remain at risk. There may, however, be opportunities to use alternative mechanisms, including, as discussed in Chapters 4 and 5, capitalizing on the emergence of a vibrant civil society and on new and more technical political leadership. Moreover, the policy priorities as outlined reflect stakeholder perspectives, as well as best practices drawn from World Bank Group experiences in other fragile states.

198. **There is a recognition that finding solutions that do not tackle the difficult and underlined governance issues in Guinea-Bissau is not realistic.** Identifying which stakeholders will have the incentives to take the lead on specific priorities is beyond the scope of the SCD. Yet, this report argues for a mixture of strategies that combine direct engagement of government with increased participation of other local, regional, and international actors to create a critical demand for transparency and accountability. Explicitly excluding the elite from the reform process may not be realistic and even effective in challenging elite domination. On the contrary, it can exacerbate rather than lessen fragility. Investments that target the poor can build the foundation for inclusive growth, but also empower them by raising the demand for transparency, accountability, and by direct, more effective delivery of basic services. This empowerment can be a major catalyst in the process of strengthening institutions and addressing behavioral norms in public and political spheres. Working directly with beneficiaries, for instance, through community-driven programs implemented by NGOs, can contribute to addressing urgent needs in basic services such as education, health, and water. International actors like WAEMU, ECOWAS, the African Union, and the donor community can also harness forces and align incentives in favor of transparency and stability.

6.2 Prioritization process

199. **The diagnosis and prioritization of developmental constraints occurred in three phases.** The first step drew from the main findings of the analysis. The main challenges in terms of inclusiveness, economic growth, fragility, governance, and sustainability identified in chapters 2 through 5 were mapped to the diagnostics framework. This part of the analysis revealed that most of the foundations for robust, inclusive, and sustainable growth to take off in Guinea-Bissau were not in place. A grouping of the main challenges identified three clusters of interconnected areas of binding constraints: (1) lack of inclusiveness and low rural productivity; (2) low and unstable growth; and (3) fragility and weak governance.

200. **Drawing from the available evidence, the team developed a long list of broad policy areas to partly address each cluster of constraints.** The policy areas were grouped according to pathways to economic development that took into account the binding constraints listed above. To develop the pathway of each policy action, the team analyzed the results chain, from the standpoint of the central objectives of economic growth and poverty reduction. To do this, the team

considered the dimensions of growth, inclusiveness, sustainability, and governance, and then refined the actions within the country context of fragility and political instability. This process helped in the identification and consideration of the most “economically, socially, and politically” relevant priorities. To complement the prioritization process, an extensive benchmarking analysis was conducted, ranking Guinea-Bissau’s performance against the top performer in Sub-Saharan Africa and the top performer worldwide. Anchored by the evidence from these processes, the core team identified a long list of 21 policy areas that reflect the needs and context of Guinea-Bissau. Efforts were made to make each of the policy options as mutually exclusive as possible, but this proved to be difficult given the multiple feedback loops across and within the core areas of constraints.

201. The second step in the prioritization process consisted of consultations with the country team during which the binding constraints were discussed, the policy areas were ranked, and the specific actions within each of the prioritized areas were identified. The core team, in coordination with World Bank experts on Guinea-Bissau, developed a worksheet summarizing the rationale and evidence for the three core areas of binding constraints, as well as the list of policy areas and actions under each of them (Annex 6A). The worksheet included criteria to rank the policy actions encompassing: 1) poverty reduction impacts; 2) feasibility (political and institutional capacity; and 3) traction (ability of the mitigating action to deliver results in the short to medium term). The document described poverty reduction impacts to be the most important filter for the prioritization, in line with the Bank’s twin goals. Feasibility was considered as being independent of what the Bank is or could do in the country. The worksheet was shared with the country team to elicit a vote and ranking of mitigating actions. The results were pooled, averaged, and standardized on a scale of 1 to 10 to ensure comparability and a clear ranking of options.

202. A meeting was held with the country team to discuss the results of the ranking of constraints. The exercise elicited responses from different Global Practices working on Guinea-Bissau. The meeting produced a discussion about the quantitative results where mitigating actions had been prioritized by pooling and averaging of the ranked answers of each respondent. During this meeting, attendees had a chance to raise issues that might not have been raised by the exercise, or to highlight relevant mitigating actions that might not have gained attention from the prioritization exercise alone. Attendees asked for clarification on whether or not mitigating actions had some overlap. It was clarified that where actions had a high level of specificity, some overlap was inevitable. Another clarification included the fact that although some mitigating policy actions may not have been highly ranked, that did not imply the non-importance of that action for the country. Modifications to strengthen and clarify some of the policy actions were also suggested and taken up by the team. Overall, the feedback from the country team consistently identified the top three or four priority policy areas in each of the core clusters of binding constraints.

203. The third and final step in the prioritization process consisted of in-country consultations. The team initially held consultations with different stakeholders from the Government and the civil society in May, 2015. This was useful to further define the hypothesis and areas of analysis for the SCD. A second consultation was undertaken between March 7 and 10, 2016 as a consistency check of the identified areas of binding constraints and the priority mitigating policy actions. The consultations included representatives of the Government, the

private sector, the civil society, and other development partners and donors. There was broad support for the framework, evidence, constraint areas, and mitigating policy actions.

6.3 Binding constraints and prioritized policy actions

204. This SCD has identified three clusters of constraints to poverty reduction and shared growth in Guinea-Bissau. The three core areas of binding constraints are 1) lack of inclusiveness and low rural productivity; 2) low and unstable growth and 3) fragility and weak governance. These areas of constraints follow from the analytical model and existing evidence by reflecting a context where the basic elements of well-being and economic opportunities are inadequate and unequally distributed, and economic growth, a key ingredient for poverty reduction, has been unsatisfactory and volatile. Cutting across most of the economic, social, and political structures of the country, fragility and weak governance, the third set of core constraints, are major obstacles to improving the development outcomes of the country.

Area of constraints 1: Lack of inclusiveness and low rural productivity

205. Looking ahead, faster economic growth alone will not be enough to bring significant improvements in the living standards of most Guineans. The SCD shows that even the low economic growth recorded in the 2000s would have reduced poverty. Yet, since it happened only at the top decile, poverty increased. More specifically, the proportion of the extreme poor reached a high mark in 2010, accounting for one-third of the population in 2010. The assessment of the equity conditions reveals several reinforcing mechanisms that will likely cause poverty and inequality to persist (i.e. a poverty trap). The low and unequal allocation of human and physical endowments limits the income generation capacity of poor households. Low access to basic services, such as clean water, sanitation, and electricity, coupled with failures in critical markets (for instance, credit), poor infrastructure and natural resource depletion, constrain economic opportunities, undermine asset utilization, and reduce their returns. As depicted in Table 2.1 the extreme poor are at an even greater disadvantage across the vast majority of indicators and hence, along with the moderate poor, have the greatest potential to benefit from the priorities listed below. Other groups, particularly women, are also disadvantaged in the allocation and utilization of resources. Taken together, the low level of assets, and the lack of an enabling context and possibly other behavioral factors, trap most households in the cashew sector, a stable yet low-investment, relatively low-risk, and low-productivity subsistence equilibrium. There is recognition that this area of prioritization is not independent of the others. The context of low rural productivity and lack of inclusiveness is intrinsically linked to low growth and entrenched fragility and weak governance.

206. The top policy priority area identified to address the lack of inclusiveness in Guinea-Bissau is the urgent need to improve service delivery through targeted actions to transform access to basic services. The prioritization exercise highlights interventions in this area as having the largest positive poverty impact, especially among the extreme poor. To target service delivery and human capital, health and education are considered the two main services that need immediate attention. The specific actions prioritized for these two sectors and also for utility services in the short- and medium- term are as follows:

- *Health service.* In health care, better staffing, health financing, and information systems can significantly improve performance. In the short term, support should be given to the development of government workforce policies for hiring and training. The immediate focus should rest on increasing the availability (supply of) and quality of primary-care workers who can provide, in addition to better primary care, reliable maternal and child health services. This is much-needed among the extreme poor, who are more likely to be sick, missing days of work, and facing a greater challenge to poverty reduction. Financing strategies can be improved by including public-private partnerships and by promoting better coordination between donors to avoid redundancies. In the medium and long run additional desirable steps are important, including acquiring more information via health survey data collection (such as the Service Delivery Indicators (SDI) survey promoted by the Bank and other institutions), establishing health quality standards and monitoring, and supporting government performance-based pay policies.

- *Education service.* The establishment of better standards and procedures must be at the core of future improvements. The quality of education requires developing criteria for expansion of education in urban and rural areas, and for the strengthening of hiring, management, and cost control policies. A pressing issue includes developing a strategy to address teacher absenteeism, which needs to be better understood via the SDI survey. Improvements can also be made by introducing timelines for proper planning, recruitment, and hiring of teachers, as well as ensuring that children are present at school on time and able to learn. This has great potential to change the education profile of the country over time, which currently has an astounding 86 percent of extreme poor and 77 percent of moderate poor household heads lacking primary education. In the medium- and long-term the Ministry of Education's capacity and organizational structure should be improved by finalizing organigrams, and by defining narrower roles and responsibilities for staff. More details in the budget planning (that is, a three-year plan) could help improve the efficiency and transparency of education financing.

- *Utility service.* Other important areas include the utility sector where much of service delivery is tightly linked with infrastructure capacity in the country, which is another main focus of the priorities outlined in this section considering that the poor, but above all the extreme poor, are more likely to lack clean drinking water and sanitation. The national utility company, Empresa de Eletricidade e Águas de Guinea-Bissau, or EAGB, faces managerial challenges similar to other institutions in the country; in this particular case, it has lacked a Board Committee for 10 years. Hence, it needs to strengthen performance-based processes within the company and establish a functioning Board. With only 10 percent of households receiving electricity and only one-third accessing basic sanitation, the company needs to reduce technical inefficiencies and waste, which are large even by Bissau-Guinea standards. This implies improving both the technical and financial performance of the utility by updating its technical model of provision of urban service, but also especially its service to rural households.

207. Improved agricultural productivity and market support services are also highlighted as top priorities to address the lack of inclusiveness. Findings from the analysis indicate that improvements in these areas can be achieved by using a three-pronged approach:

- *Extension services to improve crop performance.* Specific focus should be given to developing the skills of producers via extension services and access to more productivity-

enhancing knowledge, and promotion of information and communications technology for farmers (that is, daily pricing data, via mobile phones). This will be greatly beneficial for poor households, who are much more likely to work in agriculture and often lack information due to distance from other farmers or markets.

- *Improved linkages between producers and processors.* Linkages between producers and processors are also important and are dependent on infrastructure. For instance, improving feeder-road infrastructure (often deteriorated in the rainy season) can result in lowering the systemic cost of doing agribusiness. This is central for poor and extreme poor smallholders who can only maximize agricultural profits upon minimizing transaction costs. Increased coordination among producers can strengthen their bargaining power and allow them to gain higher margins on the sales of cash crops. Other areas also need addressing, such as harvesting, storage, and transportation, which can further increase bargaining power by ensuring that producers do not have to sell more than needed at one time.
- *Support for other crops and value chains.* The improvement in capital, input, and skills levels via the abovementioned interventions will also help to develop other value chains, and cash and staple crops, in the medium and long run. Overall, strengthening farmer associations and building partnerships with NGOs can offer opportunities to: (1) exploit economies of scale; (2) facilitate access to inputs, financial services, storage, and marketing; (3) strengthen value chains; and (4) prevent to some extent capture by local elites. Agricultural interventions should be backed by a continuous effort to address the both cumbersome and inefficient land rights matrix in Guinea-Bissau.

208. The SCD finds that another important area for action is to increase the economic and social resilience of households, particularly the extreme poor, to the large variety and high frequency of shocks to which they are exposed. The most common shock in Guinea-Bissau has been related to political instability, sometimes leading to civil unrest, such as during the Civil War of 1998-1999. Households are also exposed to other aggregate shocks, derived from climate variability, such as droughts, late onset of the rainy season, or tidal surges, that affect both smallholder activity near the coast and fishing patterns. Climate change is widely expected to accelerate these changes and make them less predictable. One in three Bissau Guineans are extreme poor and have very little ability to cope with shocks – 90 percent work in agriculture, having low and undiversified incomes, as well as few assets to liquidate in case of crisis. The main priority action identified for this constraint is the need to develop and enhance formal and informal risk management.

- *Social Protection Strategy.* The high level of vulnerability of the poor presents an opportunity to develop a Social Protection Strategy (SPS) for the country – this is particularly pressing for the extreme poor, who lack the most basic assets and mechanisms to exit poverty. This should involve reforming the pension system and increasing the economic infrastructure to communities across the country. A large part of this plan should also involve cash transfer programs to benefit poor households faced with increased risk.⁶³ Priority should be given to proven interventions

⁶³ While it was treated as a separate mitigating action in the prioritization exercise, it is worth recognizing that social safety nets can play an important role in shielding households from negative shocks while increasing their assets, which has been widely documented by rigorous evidence in many developing countries.

that boost credit and provide a safety net in the short and medium run, such as enhancing households' ability to receive and send remittances (that is, mobile money) and that target cash-transfer programs for those most in need (see Table 6.1 below).

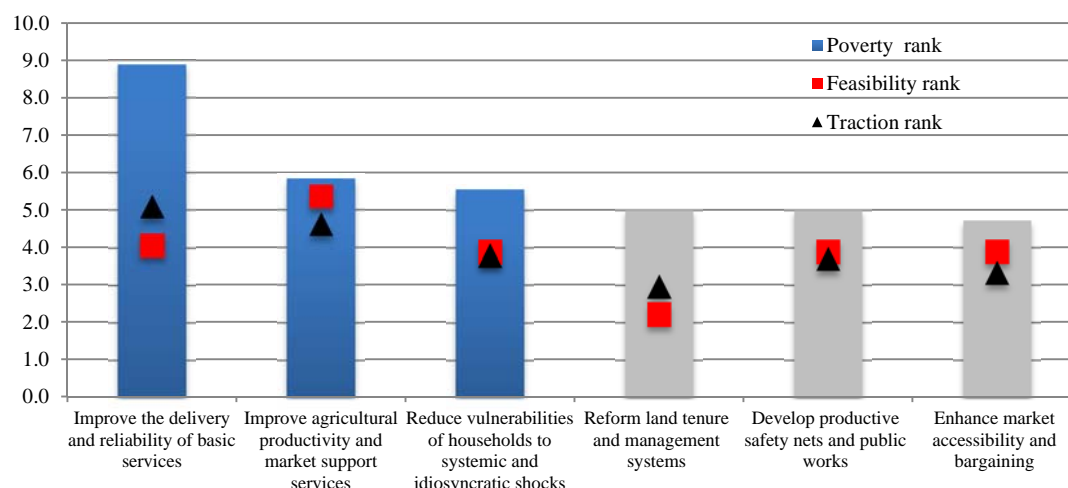
Table 6.1. Ranking of mitigating actions to address constraints to lack of inclusiveness and low rural productivity

Constraints mitigating policy actions	Poverty Rank	Feasibility rank	Traction Rank
Improve the delivery and reliability of basic services (education, health, nutrition, water and sanitation) by: <ul style="list-style-type: none"> • Strengthening staffing, management, training, compensation, and control of hiring and absenteeism mechanisms in the education and health sectors. • Expanding and strengthening performance of basic primary health services, especially maternal and child health. • Adopting centralized criteria and rules for expansion of schools. • Strengthening health information systems, including disease surveillance capacity for early detection and response to disease outbreaks. • Developing a health financing strategy. • Implementing an economic and technical strategy to provide water in rural areas. 	1	3	2
Improve agricultural productivity and market support services by: <ul style="list-style-type: none"> • Improving production practices in the cashew sector through extension services, increasing access to enhance inputs and technologies, providing incentives to replace old orchards, and developing quality standards. • Addressing coordination failures in the cashew market, specifically between producers and processors, to increase the share of the rents accrued by farmers. • Rehabilitating warehouse facilities and developing other logistics services. 	2	2	1
Reduce vulnerabilities of households to systemic and idiosyncratic shocks by <ul style="list-style-type: none"> • Supporting coping and adaptation strategies (for instance, irrigation, enhanced seeds, financial and insurance instruments, credit associations, and so forth). • Developing a social protection strategy. • Piloting and scaling up cash transfer programs to alleviate poverty in the poorest parts of the country, especially in times of crisis. • Reforming the pension system. 	3	1	3
Reform land tenure and management systems to further empower women, and to strengthen the rules that determine how land is used, possessed, leveraged, and sold to boost investments and productivity in the agricultural sector.	4	6	4
Develop productive safety nets and public works to provide work opportunities, and to contribute to building or rehabilitating small-scale infrastructure that yields services to households.	5	4	6
Enhance market accessibility and bargaining by strengthening connectivity (for instance, rural roads), access to information (for instance, telecommunications) and farmers associations.	6	5	5

209. **The remainder of mitigating actions discussed by the team, albeit not ranked as the top priorities, still represent good blueprints for medium- and long-term action in the country.** Having a lower poverty ranking, and sometimes (but not always) lower feasibility and traction ranking, some of the mitigating actions not included as priorities are still important (see Figure 6.1). For example, reforming land tenure and management systems would strengthen the rules that determine how land is used, possessed, leveraged, and sold to boost investments and productivity in the agricultural sector. It is undeniable that Guinea-Bissau has a complex system of property rights, hampering many income-generating opportunities for households. This complexity is perhaps the reason for low traction and feasibility in this mitigating action. The

developing productive safety nets and public works are cross-cutting areas that remain important for Guinea-Bissau, and have the potential to deliver relief to the poorest, increase food security, and encourage investments in human capital and productive assets. Along with an improvement in agricultural output, storage, and margins, enhanced market accessibility and bargaining would greatly benefit smallholders. This mitigating action has strong complementarities with others, and thus part of it will be addressed indirectly, albeit remaining relevant for long-term development in the country.

Figure 6.1. Human capital base expansion, agricultural technology, and risk-mitigation are top priorities to address low inclusiveness



Source: World Bank staff assessment, 2016

Area of constraints 2: Low and unstable growth

210. **Growth in Guinea-Bissau has been low and needs to be accelerated and sustained in order for the country to make a dent on poverty and foster shared prosperity.** GDP per capita grew by 0.4 percent annually between 2000 and 2014, roughly one-quarter the average recorded for the Sub-Saharan region (1.9 percent). Comparing Guinea-Bissau with its closest 19 African peers in per-capita GDP back in 1990 shows that its rank fell from 10th to 18th as result of having the seventeenth-lowest growth rate in the entire group. The structure of Guinea-Bissau's economy has barely changed over the last two decades and remains largely agrarian. Growth performance is excessively reliant on the production and export of a single commodity, unprocessed cashew nuts, which are concentrated in the first rung of the value ladder. The production of cashews engages more than 75 percent of small farmers, underscoring the tight connection between incomes and movements in farm gate prices or production levels, especially for the poor. This undiversified economic structure has limited the resilience of the economy to mitigate the impact of shocks (terms of trade, political and natural).

211. **Weaknesses in the fiscal system, a precarious business climate, low financial inclusion, and limited and unreliable cross-cutting economic services also put a drag on the economy.** Low and unpredictable public revenues, regressive and distortionary taxation, and poor quality of public expenditure limits the effectiveness and equity of the fiscal policy. The business climate is not conducive to the generation of growth, employment, and productive capital. Guinea-Bissau is

at the bottom for all of the 10 Doing Business indicators. Financial inclusion is among the lowest in Sub-Saharan Africa. Guinea-Bissau's infrastructure that supports production and that provides economic services is in a woeful state, from the port to roads, and from access to electricity and potable water to the Internet. The lack of investments is an important pillar of a vicious circle of low productivity, low growth, limited opportunities, and elite capture, which then feeds back into low investments.

212. A top priority for Guinea-Bissau is to start capitalizing on many of its opportunities for economic growth, which remain largely untapped and could thereby be available to diversify the economy in the medium to long term. This is not only about exploring new industries and sources of growth, but also about involving making traditional sectors and industries (for instance, cashews) more productive and competitive. In this regard, the analysis points to three key areas for intervention over the short to medium term:

- *Fostering moving up the value chain in the cashew sector.* Guinea-Bissau has the potential in the short-run to move to higher value chain segments within the cashew economy through improved processing capabilities. This may require capitalizing on emerging opportunities in ICT, as well as attracting a more dynamic private sector (including FDI-type structures) to usher in a new era of accountability. It is estimated that cashew-processing creates about one full-time job for every three tons of processed raw nuts. Processing 30,000 tons of nuts a year could therefore create around 10,000 jobs, which is essential in Guinea-Bissau, and could increase the returns to cashew production for the vast majority of the rural population (many of them poor) whose livelihoods depend on cashew.
- *Development of value chains in rice, and other agricultural crops.* The country also has potential in the medium to long run to begin a structural transformation of its agrarian economy, capitalizing on green shoots in agriculture, such as rice, sesame seeds, and forestry. Diversification is pivotal in reducing economic vulnerabilities of poor rural households. Central to this process, however, is the need for increased access to inputs, capital, training, and accessibility to markets. Notably, immediate improvements can be promoted by better seed variety and crop management that maximizes yield and land utilization.
- *Development of value chains in fisheries.* With a vast resource base, the fisheries sector of Guinea-Bissau has the potential to make a much greater contribution to the attainment of key development objectives, such as economic growth and poverty alleviation over the near to medium term. This requires investments in landing and processing facilities as well as improved regulation and management of the sector.

213. Given high transaction costs and unreliable infrastructure, it is key that Guinea-Bissau improve its cross-cutting economic and production support services. The prioritization process identified the most pressing actions that have to be taken in electricity, roads, the port, and ICT as follows:

- *Electricity:* This is the main deficiency in Guinea-Bissau, with less than 10 percent of overall households having access to reliable utility. To this end, efficient management of the National Utility Company, (EAGB), is key. The company needs to establish a Board Committee (absent

for over 10 years), institute performance-based systems, sustainably manage its scarce resources (that is by reducing technical losses, currently at 50 percent of cost) and work with regional partners to bring more reliable energy to the country.

- *Road infrastructure*: This is also central to unlocking multiple opportunities in Guinea-Bissau while reducing transaction costs. Feeder roads (that connect main roads to farmers and villages) are in particular disarray. Critical spots are rendered useless during the rainy season, and those spots should be the top priority, with general conditioning as a second priority, and all-road maintenance and management systems as third priority.
- *Port of Bissau*: The port system, another pillar of trade and development in Guinea-Bissau, needs a more rigorous management framework. The focus should rest on physical and administrative bottlenecks; in the short run, the inefficient mesh of administrative stakeholders involved in the port's management needs to be untangled. In the medium-run, storage and docking capacity should be improved, as well as harbor navigability, such as establishment of lighthouses, better water-depth markers, dredging operations, and shipwreck removals (for instance, under the current state, only one ship can enter or leave the harbor at a time).
- *Telecommunications*. The most significant barrier to telecommunications development is prohibitively high costs resulting from the difficulty of doing business and from a general lack of infrastructure (that is oceanic cables and reliable electricity). The top priorities for this sector in the short and medium term are (1) building connections to main broadband providers; (2) developing a regulatory system to create an environment conducive to fair competition between providers; and (3) completing the restructuring process for the incumbent operator's mobile subsidiary Guinetel.

214. Increased financial inclusion is a necessary condition to achieving a more diversified and sophisticated economy. The level of access to financial services and financial literacy is remarkably low in Guinea-Bissau, with both low demand and low supply of such services. With deficient human capital, particularly in education, and with part of the local trading economy (mostly outside of Bissau) based on the bartering of goods, financial services such as savings and credit accounts have a low density. The country only has 1.8 commercial bank branches per 100,000 adults, a little over half of the average for Sub-Saharan Africa (3.4) and significantly less than the world average of 11. The following are three specific priority actions identified to raise financial inclusion (see Table 6.2. and Figure 6.2)

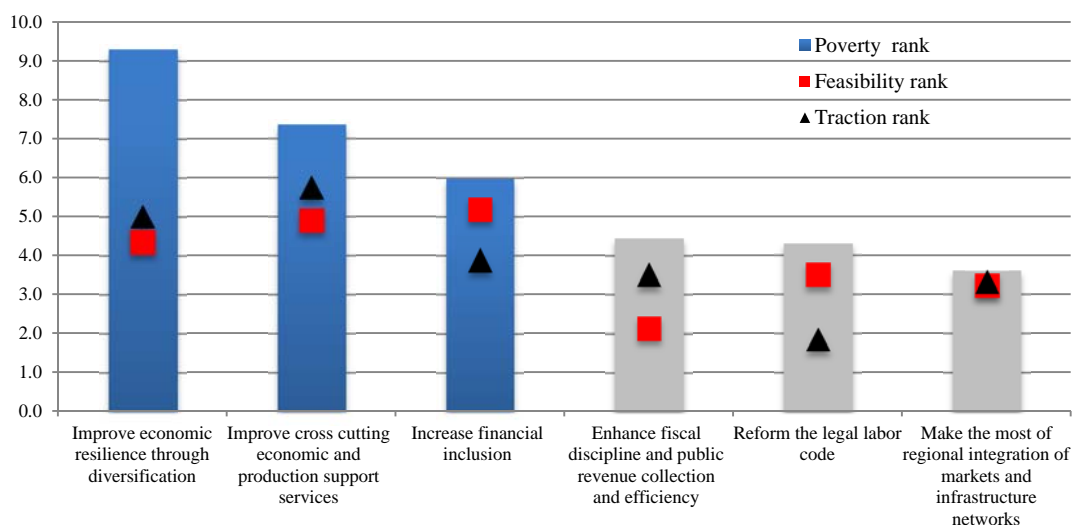
- *Expanding bank account penetration*. This can be accomplished through, for instance, the development of digital, low-fee financial services (for instance, mobile banking, electronic payments, and electronic social transfers).
- *Development of a microfinance policy environment*. This is required for microfinance to take off in Guinea-Bissau. Such a policy environment would allow financially strong institutions from other WAEMU countries (through the regional regulator) to operate branches in the country. This would require overcoming challenges such as allowing companies licensed in other countries to operate in-country, and incentivizing the monetization of the Guinean economy.

- *Enhancing payment systems.* A third option is enhance payment systems through the banking sector, in particular payment of salaries and use of debit and credit cards, which are feasible but nonetheless face similar challenges to the other proposals for better financial inclusion.

Table 6.2. Ranking of mitigating actions to address constraints to low and unstable growth

Constraints mitigating policy actions	Poverty Rank	Feasibility rank	Traction Rank
Improve economic resilience through diversification by: <ul style="list-style-type: none"> • Fostering a higher value chain in the cashew sector through processing. • Supporting the development of value chains in rice, mango, and sesame through increased access to inputs, capital, skills and accessibility to markets. • Developing the value chain in the fisheries by putting in place the conditions for landing and processing the majority of the catches on site. 	1	3	2
Improve cross-cutting economic and production support services (electricity, roads, ports, and telecommunications) by: <ul style="list-style-type: none"> • Improving the technical, operational, commercial, and financial performance of EAGB and the port through a performance-based service and management contract, or concession with a private operator, and a sound institutional framework. • Setting up a road management system covering assessment, funding, and monitoring of maintenance to address the poor condition of the road network. • Improving the secondary and tertiary road network to address the low connectivity of rural populations. • Building connections to main broadband providers. • Developing a regulatory system to create an environment conducive to fair competition between providers in the telecommunications sector. 	2	2	1
Increase financial inclusion by: <ul style="list-style-type: none"> • Expanding bank account penetration through, for instance, the development of digital, low-fee financial services (such as, mobile banking, electronic payments, and electronic social transfers). • Developing a sound microfinance policy environment and allowing financially strong microfinance institutions from other WAEMU countries (through the regional regulator) to operate branches in the country. • Enhancing payment systems through the banking sector, in particular payment of salaries and use of debit and credit cards. 	3	1	3
Enhance fiscal discipline and public revenue collection and efficiency to insulate the country from the volatility associated with grant flows, address the narrow, distortionary and regressive tax base, create much need fiscal space for growth and poverty reduction and safeguard fiscal sustainability	4	6	4
Reform the legal labor code to increase flexibility of the labor market to adjust to economic fluctuations and structural changes while ensuring efficient social protection.	5	4	6
Make the most of regional integration of markets and infrastructure networks to exploit economies of scale, internalize technological spillovers, attract investments and open new markets.	6	5	5

Figure 6.2. Diversification, infrastructure and financial inclusions are top priorities



Source: World Bank staff assessment, 2016

215. **While the prioritization process for improving low and unstable growth has yielded three clear top choices, other mitigating actions will also help to inform the development agenda moving forward.** Other areas remain important to bring about macro-fiscal stability in Guinea-Bissau. Enhancing fiscal discipline and public revenue collection and efficiency would help to insulate the country from the volatility associated with grant flows, to address the narrow, distortionary and regressive tax base, and to create much needed fiscal space for growth and poverty reduction, while safeguarding fiscal sustainability. This mitigating action received a lower poverty ranking and the lowest feasibility ranking, although it remains important and it highlights issues still to be addressed in Guinea-Bissau. Similarly, it is important to reform the legal labor code to increase flexibility of the labor market in adjusting to economic fluctuations, as well as to make potential structural changes, while ensuring social protection. Nevertheless, this mitigating action was agreed to have very low traction due to its complexity and will be on the agenda for long-term change. Finally, the mitigating action with near-equal poverty, feasibility, and traction ranking (all at medium levels) will almost certainly be addressed indirectly through other mitigating actions. Its objective is to make the most of regional integration of markets and infrastructure networks in order to exploit economies of scale, internalize technological spillovers, attract investments, and open new markets.

Area of constraints 3: Fragility and weak governance

216. **Throughout the SCD, fragility and weak governance emerged as core obstacles to economic development and poverty reduction in Guinea-Bissau.** Fragility constitutes a major challenge to economic development. This is the case for Guinea-Bissau. The country is trapped in a cycle of low growth and high incidences of poverty, anchored by recurrent political instability, and the interlinked competition for rents among the elite have negatively influenced virtually every economic, social and political dimension of the country. Results from the benchmarking analysis show that Guinea-Bissau ranks poorly (at the bottom 10-20 percent) with respect to regional and world averages in virtually all the human capital, physical capital, business climate, transparency,

rule of law, and other quality of institution indicators. Weak governance also translates into mismanagement of the natural wealth, which is being depleted at the current utilization rate (see Table 6.3 for a list and ranking of mitigating actions to address fragility and weak governance.)

217. The top priority in terms of poverty impact under this pillar is to address the allocative, technical, and regressive inefficiencies in public spending. This can be done directly through the budget process where resources are redirected away from selected sectors, such as the military, to areas that contribute to building the human capital of the country, like education and health, as well as physical and institutional capital. Alternative delivery mechanisms, such as working with civil society and or coordinated donor efforts will need to be considered to address this important impediment to growth and poverty reduction in the country. The following are three specific priority actions identified as important areas for action:

- *Strengthening performance, control, and transparency of public revenue.* This requires efforts to protect and progressively improve the capacity of the government to deal with revenue processes *using* procedures and systems to increase revenue collection, as well as the efficiency, effectiveness and transparency of revenue administration.⁶⁴
- *Improve expenditure control, accounting, and reporting capacity.* The public procurement and internal control systems on expenditures are not functional, which lead to an abusive use of exceptional procedures, often bypassing the budget information system. They require efforts to strengthen controls needed for fiscal discipline and to promote transparency and accountability in public expenditures.
- *Introduce equity-based formulas for budget allocation.* Technical inefficiencies could also be reduced by strengthening project appraisal capacity by government bureaucrats, and by introducing equity-based formulas for budget allocation.⁶⁵ This is a longer-term initiative, given the low feasibility, which points to difficulty in breaking established norms, and will include working directly with the authorities as well as with other local and international development partners.

218. Weak governance and fragility can also be mitigated by improving public financial management systems, particularly in budget preparation and execution (see Figure 16.3) The state of public financial management systems is considered poor and underscores the lack of good governance in Guinea-Bissau. Addressing these deficiencies requires improving capacity, efficiency, and operationalization in a wide array of government responsibilities, ranging from budget preparation and execution as first priorities and lowest hanging fruit, to debt management, macroeconomic forecasting, and accounting. Government effectiveness (ranked one out of 10 in Guinea-Bissau) is directly tied to budget preparation and transparent execution (better linkage to policies), helping to improve this pressing outcome. As a third tier of related improvements, interventions should also target systems of internal and external control, such as procurement, auditing, and inspection services, as well as building up a reliable Treasury Committee. In this

⁶⁴ See World Bank Report No: PAD1197.

⁶⁵ Government effectiveness was ranked very low for Guinea-Bissau compared to its neighbors, at 70 percentage points from the top-performer in the sub-Saharan African distribution, further corroborating the priority in reducing government spending inefficiencies. Corruption is also common in Guinea-Bissau, exacerbating this issue; 45 percent of firms reported being expected to give gifts of up to 5 percent of contract value in order to secure a government contract.

context, the WAEMU PFM directives should be ratified as law to help further this process. More specifically, the analysis points to the need for efforts to:

- *Strengthen the link between the budget and policy priorities.* This involves helping the government to prepare a budget that truly reflects key policy choices.
- *Strengthen the government's fiduciary practices.* This involves using well established PFM directives to ensure that the execution of the budget is consistent with accepted norms. This is critical to ensuring that public resources are spent on their intended purposes. Through efforts to empower civil society and creating demand for increased accountability and transparency, this could have the impact of lowering incentives for corrupt activities and mitigating the delicate relationship between private gains and public funds.
- *Publish information on government performance.* This involves strengthening human resources and statistics systems to help the government identify and monitor key policies and carry them out effectively. Transparency would strengthen the link between the budget and implementation of government programs and policies. Rents collected by entrenched elite networks are obtained from a variety of public sources, including tax revenues, license fees, and international aid, and these reforms have the potential of reducing this widespread practice. Increased transparency can also boost government credibility and help legitimize future decisions in light of political disagreements, thereby also reducing political tension and fragility.

219. **Guinea-Bissau also needs to reform public-sector incentives and raise personnel capacity through the establishment of consistent standards for government employees.** Seen as another top priority for Guinea-Bissau, the overall goal is to move the system away from cronyism and toward a meritocracy, reducing incentives for cooperation in corrupt practices, and raising the quality of the public workforce. These reforms can be achieved by looking at best-practices and establishing guidelines for staffing, entry exams, skills development, and performance assessment for civil service linked to quality of service delivery, merit-based job promotion systems, and measures to reduce the fragmentation of government. The appointment of government officials is often based on corruption needs rather than merit. On the "control of corruption" (World Governance Indicator), Guinea-Bissau performed more poorly than many of its neighbors, some of which also suffer from extreme corrupt practices; Guinea-Bissau was 89 percentage points from the top-performer on the distribution of scores for this indicator, which highlights the need to work on this priority.

220. **Another widely agreed-upon mitigating action is the strengthening of the business regulatory environment.** Most of the untapped potential for Guinea-Bissau, in industry, agriculture, fisheries, forestry, tourism, and elsewhere, could be unlocked by businesses if the right regulations were in place. This priority rests on three pillars of actions as follows:

- *Streamlining import/export practices.* One action that needs to be done is strengthening the formal processes of import and export, and reducing the amount of informal interactions between government officials and private sector personnel. This would reduce opportunities for the currently widespread practices of informal dealings. Using the SYDONIA++ customs system that is already in place would be a significant step forward in this regard.

- *Promoting entrepreneurship*: A second priority action is to set up programs that promote entrepreneurship in the country, including the availability of credit and financial education for small businesses.
- *Finalize the land law*: The third most pressing policy recommendation is to finalize the land law, which would strengthen property rights, land management, and administration. Its implementation will require a multi-year process of strengthening of land administration institutions. Because the regulation was never adopted, there is currently a legal vacuum. Needless to say, the regulation of the law in itself will not address the issue of insecure tenure.

221. In the longer run, addressing some of the inefficiencies in the system will require broader reforms, such as addressing the lack of transparency in taxation mechanisms, introducing strong land-titling reform, improving the availability and sustainability of public-private partnerships, and developing strategies to address the informal payments that tread the fine lines of corrupt practices. These frameworks also require strengthening commercial justice, and building capacity for legal professionals in the country. Updating the legal framework to resolve insolvencies and enforce contracts and strengthening the independence and effectiveness of regulators can also contribute positively to the country's business environment.

222. **Reforming the management of natural resources is key to a more prosperous and sustainable future in Guinea-Bissau.** This mitigating action, albeit not ranked highly on the poverty criteria, has a medium-high feasibility ranking, and was agreed upon by the team on the basis of the evidence of the SCD as a cross-cutting area involving risks of irreversibility. In the short term, three issues require urgent attention:

- *Halting the rapid rate of forest loss*. This is caused in large part by cashew expansion and small holders' need for new rice land, but also by illegal felling. Tackling deforestation is essential to maintain a lifeline to the livelihood of many subsistence farmers and will require a range of instruments including land tenure reform, enforcement and surveillance, investments in forest restoration, and tapping into global climate finance opportunities, among others.
- *Optimal management of fisheries resources*. To date, there is no good information about the sustainable catch potential, and the country may soon hit a point of no return in terms of fish stocks. Moreover, it is likely that the country could increase benefits from its fisheries by improving the terms of foreign fishing arrangements and/or increasing domestic landing of the catches.
- *Ensuring sustained finance to the Protected Areas system*. The establishment of the Bio Guinea Foundation is a step in the right direction, but efforts to capitalize the Foundation and contribute to the recurrent cost of the Protected Areas system are greatly needed.

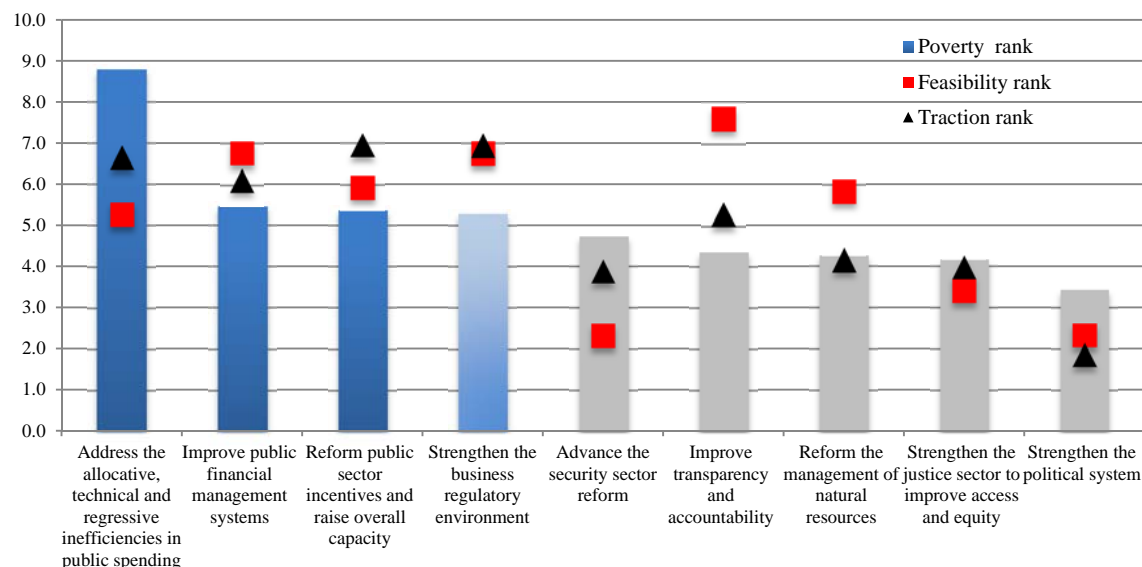
223. In the medium term, policies and investments geared to harness the value of a nature-based economy are key. Eco-tourism in some of the most pristine marine parks in the region and sport fishing, for example, could leverage synergies with commercial fishing in restoring and improving the productivity of the ocean, as well as greatly contributing to GDP and labor creation in years to come. The Bank's role in the near term could be to promote south-south

exchanges to allow Guinea-Bissau to understand how other countries (such as, Costa Rica) turned their economies around based on a peace and environment agenda.

Table 6.3. Ranking of mitigating actions to address constraints to fragility and weak governance

Constraints mitigating policy actions	Poverty Rank	Feasibility rank	Traction Rank
Address the allocative, technical and regressive inefficiencies in public spending by: <ul style="list-style-type: none"> • Strengthening performance, control, and transparency of public revenue. • Improving expenditure control, accounting and reporting capacity. • Introducing equity-based formulas for budget allocation. 	1	5	2
Improve public financial management systems by: <ul style="list-style-type: none"> • Strengthening the link between the budget and policy priorities. • Strengthening fiduciary practices (procurement, auditing and reporting, and inspection). • Making public timely and comprehensive reports on government performance. 	2	2	3
Reform public sector incentives and raise overall capacity by: <ul style="list-style-type: none"> • Establishing minimum entry requirements and where appropriate training existing staff to carry out core functions. • Implementing a meritocracy system for career advancement to reduce fragmentation. • Establishing, staffing and maintaining reform coordination units to ensure capacity building and national ownership of reforms. 	3	3	1
Strengthen the business regulatory environment by: <ul style="list-style-type: none"> • Streamlining import and export procedures (for instance, customs declaration, arrival and inspection of goods) to reduce opportunities for fraud • Streamlining the procedures to start new businesses and register property • Updating the legal framework to resolve insolvencies and enforce contracts • Strengthening the independence and effectiveness of regulators Adopting land regulation policy to fill the existing legal vacuum on issues related to land titling, registry, concession, management, and administration.	4	2	1
Advance the security sector reform to reduce military interference in political and economic spheres while mitigating risks in the process that could trigger new instability.	5	7	7
Improve transparency and accountability by making more information publicly available (e-government), and investing in statistics, and strengthening the roles of oversight and accountability institutions (national, subnational, civil society).	6	1	4
Reform the management of natural resources to preserve the country's natural wealth by: <ul style="list-style-type: none"> • Halting the rapid rate of forest loss through land tenure reform, enforcement, surveillance, and investments in forest restoration, and tapping into global climate finance. • Enhancing the management of the country's fisheries resources through the implementation of the already developed legal and regulatory framework, generating information about the sustainable catch potential and improvement in the terms of foreign fishing arrangements. • Ensuring sustained finance to the Protected Areas system 	7	4	5
Strengthen the justice sector to improve access and equity and develop effective conflict resolution systems that address the weakness, favoritism, and corruption of the justice sector, and the resulting impunity that contributes to fragility.	8	6	6
Strengthen the political system to rely on a more participatory and decentralized approach that enhances political participation, stabilizes democratic institutions, breaks the rural-urban divide, and addresses the disconnect between the State and the society.	9	7	8

Figure 6.3. Inefficiencies in public spending, financial management systems, public sector capacity and the business regulation were considered top priorities to address fragility and weak governance



Source: World Bank staff assessment, 2016

224. **Other mitigating actions not ranked as the highest priority are still relevant and will be addressed, even if indirectly, through the list of prioritized actions.** For example, advancing the security sector reform to reduce military interference in political and economic spheres, while mitigating risks in the process that could trigger new instability, remains a pressing need, as does improving transparency and accountability by making more information publicly available (e-government), investing in statistics, and strengthening the roles of oversight and accountability institutions (national, subnational, and civil society). The issues of stability, accountability, and transparency have been discussed through other mitigating actions and reinforced here, ensuring that they are tackled through other pathways. The justice sector also needs strengthening in order to improve access and equity and to develop effective conflict resolution systems that address the weakness, favoritism, and corruption of the justice sector and the resulting impunity that contributes to fragility.

BIBLIOGRAPHY

- Acemoglu, D., and J. Robinson. 2012. "Why Nations Fail: The Origins of Power, Prosperity, and Poverty". New York: Crown Publishing,
- Acemoglu, D., S. Johnson, and J. Robinson. 2001. "The Colonial Origins of Comparative Development: An Empirical Investigation." *The American Economic Review*: 91(5):1369-1401.
- O'Regan, D., and P. Thompson. 2013. "Advancing Stability and Reconciliation in Guinea-Bissau: Lessons from Africa's First Narco-State." Special Report. Africa Center for Strategic Studies, Washington, DC.
- AEO (African Economic Outlook) 2014. "Guinea-Bissau."
http://www.africaneconomicoutlook.org/fileadmin/uploads/aeo/2014/PDF/CN_Long_EN/Guinee_Bissau_EN.pdf.
- Aghion, Philippe, Diego Comin, Peter Howitt, and Isabel Tecu. 2009. "When Does Domestic Saving Matter for Economic Growth." Harvard Business School Working Papers 09-080, Harvard University, Cambridge, MA.
- Aisen, Ari and Francisco José Viegas. 2010. "How Does Political Instability Affect Economic Growth?" 5/2010, (Núcleo de Investigação de Políticas Económicas) NIPE, Universidade do Minho, Portugal.
- Alesina, Alberto and Roberto Perotti. 1996. "Budget Deficits and Budget Institutions," NBER Working Papers 5556, National Bureau of Economic Research, Inc., Cambridge, MA.
- Attanasio, Orazio P. Attanasio, and Miguel Székely, 1999. "An Asset-Based Approach to the Analysis of Poverty in Latin America". Research Department Publication 3075, Research Department, Inter-American Development Bank, Washington, DC.
- Barro, Robert J. 1991. "World Interest Rates and Investment," NBER Working Paper 3849, National Bureau of Economic Research, Inc., Cambridge, MA.
- Beck, T, O.de Jonghe, and G, Schepens (2011). "Bank Competition and Stability: Cross-Country Heterogeneity", London: Center Discussion Paper, Centre for Economic Policy Research,
- Boubacar-Sid, Barry [editor], Edward G.E. Creppy, Estanislao Gacitua-Mario, and Quentin Wodon. 2007. "Conflict, livelihoods, and poverty in Guinea-Bissau." Working paper 88, World Bank, Washington, DC.
- Bussolo, Maurizio and Luis F. Lopez-Calva. 2014. "*Shared Prosperity : Paving the Way in Europe and Central Asia*," World Bank Publications, Number 17696," Calculations Based on Figures Reported in Optimizing Guinea-Bissau's Natural Wealth, World Bank, Washington DC.
- Carter, Michael and Christopher Barrett. 2006. "The economics of poverty traps and persistent poverty: An asset-based approach." *Journal of Development Studies*, Taylor & Francis Journals vol. 42(2): 178-199.
- CEM, World Bank. 2015. "*Guinea-Bissau Country Economic Memorandum: Terra Ranca! A Fresh Start*." Report No. 58296-GW, "Global Practice: Macroeconomics and Fiscal Management." World Bank, Washington, DC. .

- Center for Systemic Peace. *Database of Coups d'Etat, 1946-2014*.
<http://www.systemicpeace.org/inscrdata.html>.
- Cont, Walter, and Guido Porto. 2014. "Measuring the Impact of a Change in the Price of Cashew Received by Exporters on Farmgate Prices and Poverty in Guinea-Bissau." World Bank Policy Research Working Paper 7036, World Bank, Washington DC .
- Deléchat, Corinne, Ejona Fuli, Dafina Mulaj, Gustavo Ramirez, and Rui Xu. 2015. "Exiting from fragility in Sub-Saharan Africa: The role of fiscal policies and fiscal institutions." *IMF Working Paper* 15/268, IMF, Washington, DC.
- Essama-Nssah, B. and Peter J. Lambert. 2011. "Influence Functions for Distributional Statistics." Working Paper Series. Verona, Italy: Society of the Study of Economic Inequality.
- Firpo, Sergio, Nicole M. Fortin, and Thomas Lemieux. 2007. "Unconditional Quantile Regressions," NBER Technical Working Paper 0339, National Bureau of Economic Research, Inc., Cambridge, MA.
- Firpo, Sergio. 2007. "Efficient Semiparametric Estimation of Quantile Treatment Effects," *Econometrica*, *Econometric Society*, vol. 75(1): 259-276, 01.
- Goldstein, Markus, and Christopher Udry. 2008. "The Profits of Power: Land Rights and Agricultural Investment in Ghana." *Journal of Political Economy*, University of Chicago Press, (December) vol. 116(6): 981-1022.
- International Labor Organization. 2015. "Key Indicators of the Labor Market: 9th Edition." ILO, Geneva, Switzerland.
- International Monetary Fund. 2015. "Guinea-Bissau Selected Issues". IMF Country Report 15/195. IMF, Washington, DC. International Monetary Fund. 2015. "Article IV Consultation and Request for a Three-Year Arrangement Under the Extended Credit Facility." Press Release, Staff Report, and Statement by the Executive Director for Guinea-Bissau. IMF Country Report 15/194, IMF, Washington, DC.
- Jong-A-Pin, Richard, 2009. "On the measurement of political instability and its impact on economic growth," *European Journal of Political Economy*, Elsevier, vol. 25(1), (March): 15-29.
- Karras, G., 2006, "Is Africa an Optimum Currency Area? A Comparison of Macroeconomic Costs and Benefits," *Journal of African Economies*, Vol. 16 (2): 234–58.
- Kauffman, Daniel, Aart Kraay and Massimo Mastruzzi. 2009. "Governance Matters VIII: Aggregate and Individual Governance Indicators 1996-2008." Policy Research Working Paper 4978. World Bank, Washington, DC.
- Marshall, Monty, and Benjamin R. Cole. 2014. "Global Report 2014: Conflict, Governance and State Fragility." Center for Systemic Peace, Vienna, VA.
- MICS, UNICEF. 2015. *Multiple Indicators Cluster Survey*.
http://www.unicef.org/statistics/index_24302.html.
- Mincer, Jacob A. 1974. "Schooling and Earnings," in "Schooling, Experience, and Earnings": 41-63. National Bureau of Economic Research. Cambridge, MA.

- Patrinos, Harry Anthony, Cris Ridao-Cano, and Chris Sakellariou. 2006. "Estimating the Returns to Education: Accounting for Heterogeneity in Ability." Policy Research Working Paper 4040, World Bank, Washington, DC.
- Rodrik, D., A. Subramanian, and F. Trebbi. 2004. "Institutions Rule: The Primary of Institutions, Geography and Integration in Economic Development," *Journal of Economic Growth*: 9:131-165.
- Temudo, Marina Padrão, and Manuel Bivar Abrantes. 2014. "Changing Policies, Shifting Livelihoods: The Fate of Agriculture in Guinea-Bissau.. *Journal of Agrarian Change*: 13(4): 571-589.
- UNICEF. 2011. "Female Genital Mutilation/Cutting: A Global Concern".
[http://www.unicef.org/media/files/FGMC_2016_brochure_final
UNICEF_SPREAD.pdf](http://www.unicef.org/media/files/FGMC_2016_brochure_final_UNICEF_SPREAD.pdf).
- World Bank. 2015. "World Bank 'Risk Management Concept Note for Latin American and the Caribbean." World Bank, Washington, DC.
- World Bank. 2014. "Colombia Systematic Country Diagnostic". World Bank, Washington, DC. World Development Report. 2011. "Conflict, Security, and Development." World Bank, Washington, DC. World Development Report. 2016. "Digital Dividends." World Bank, Washington, DC.
- Zhao, Xiaodan , and Yoonbai Kim. (2009). 'Is the CFA Franc Zone an Optimum Currency Area?' *World Development* 37(12):1877-1886.

ANNEXES

Annex 1A. The Guinea-Bissau performance in development indicators compared to regional and global benchmarks

1. The analysis below provides another lens of comparison between Guinea-Bissau and its peers, as well as with the rest of the world. In the benchmarking previously done throughout this document, Guinea-Bissau is identified as a country with significant challenges to development. The results in Annex Figure 1A.1 below represent a consolidation of many concepts highlighted before. It uses a methodology that compares Guinea-Bissau across a host of indicators as well as across several countries, adding to the prioritization process in the country, and reiterating areas where Guinea-Bissau has wide gaps and could therefore most benefit from investments. The goal of this exercise is to highlight deficient areas where, if addressed, opportunities for higher and consistent growth can be unlocked, moving towards ending extreme poverty and boosting shared prosperity throughout the country.

2. To apply the benchmarking methodology, indicators that represent the areas explored in this SCD were selected across different topics (also relying on the limited availability and frequency of those indicators for Guinea-Bissau). The benchmarking methodology creates an algorithm to compare Guinea-Bissau against two groups of peers; its neighbors in Sub-Saharan Africa and the world. Within these two groups, Guinea-Bissau is then benchmarked against the group's best performer, considering a normalized range within the sample of data for each indicator. The countries selected for the 'peer' group encompass the African social, political, and economic context, which is shared by Guinea-Bissau due to its geographical location. The other group, comprised of all countries in the world for which data is available on a particular indicator, provides a broader perspective of comparison outside the African context.

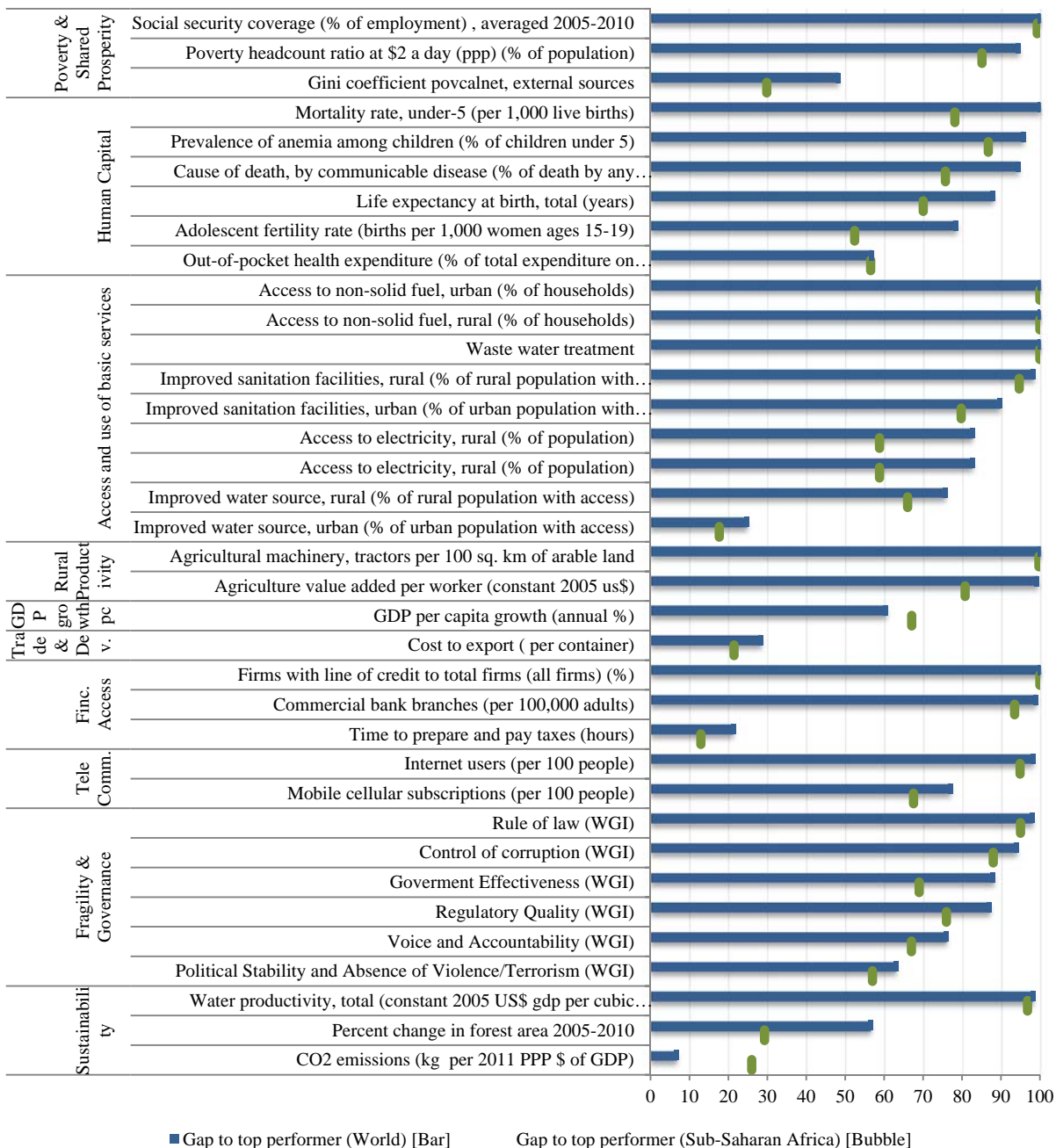
3. Across each indicator, the average of the last five years of available data (2009-2013) was used to avoid outlier values that might deviate from the norm. To ensure better comparability in terms of level of development, countries above the 95th percentile of GDP per capita distribution were removed from the sample. Using the selected variables, the distance between Guinea-Bissau and its peers was defined on each indicator. Considering the high dispersion of some countries across certain indicators, the distance in terms of percentiles within the sample (that is, Sub-Saharan Africa and the world) was used instead of the absolute or proportional distance. The analysis was carried out to allow for a comparison both with its peers, defined as the set of countries p , and the world, defined as the set w , where w includes all the countries of p . While p is a conditional comparison that controls for the country's geographical location (that is Sub-Saharan Africa), w is an unconditional comparison.

4. The measure used to benchmark Guinea-Bissau was its gap with respect to the best performer on a particular indicator⁶⁶. The following representation is used to explain how the gap was calculated. To evaluate the gap in any given indicator i between Guinea-Bissau (gnb) and the best performer (bp) in the set $s = \{p, w\}$ $g_i^s(\text{bp}, \text{gnb})$. It is defined as:

⁶⁶ The calculation of this gap draws heavily from the Colombia Systematic Country Diagnostic (2015) and the methodology developed by Samuel Freije-Rodriguez and Daniel Valderrama Gonzalez.

$$gi(bp, gnb)s = 100 \frac{|v_{i,bp}^s - v_{i,gnb}|}{|v_{i,bp}^s - v_{i,wp}|}$$

Annex Figure 1A.1. Guinea-Bissau exhibits significant gaps in development when compared to other Sub-Saharan African countries and the world



Source: World Bank staff calculations using the World Development Indicators (2016)

5. Where v_i^s, bp is the value of the best performer of the set s , including either the World (w) or the peer group (p), in indicator i ; v_i, gnb is the value of Guinea-Bissau in indicator i ; and v_i, wp is the value of the worst performer in indicator i . Given the small number of countries that constitute p , the best performer is defined as the country with the lowest value in the 10th decile. On the other hand, in the case of set w , considering that there is a sufficient number of countries to define percentiles, the best performer is the country at the 95th percentile. Once each indicator's best performer has been defined, the gap is normalized using the range of the distribution. To isolate the effect of the outliers in the value of the range, the range is defined as the distance between the 5th and 95th percentile for both sets. This normalization allows for the control of the specific variance of each indicator, assigning a higher value for narrow distributions, such as the Gini index. Moreover, this range allow for the limitation of the gap from 0 to 100 for indicators in which the best performers are countries with the lowest indicator value; for example, the case with mortality rate.

Annex 2A. Dissecting the drivers of negative growth in Guinea-Bissau with Recentered Influence Function (RIF) and Oaxaca-Blinder decompositions

1. Using the framework proposed by Firpo et al. (2007), we can better understand the drivers of negative growth in Guinea-Bissau from 2002 to 2010. While an ordinary least squares (OLS) can be used to estimate the average effects of each household characteristic, Firpo et al. (2007) demonstrated that it is possible to go beyond the mean estimation, using a recentered influence function (RIF) regression to estimate quantile effects, providing a level of detail that is more useful for policy application. The outcome variable of each quantile regression can be further decomposed, using the logic of the Oaxaca-Blinder decomposition, to estimate endowment and structural effects in each quantile, effectively linking each percentile of growth to household characteristics, as well as to a decomposition of effects. This annex, by using the method outlined above, models the mean differences in distribution of consumption expenditure between 2002 and 2010. Consumption is assumed to be a function of demographic characteristics, such as household size, sex, and age of head of household; endowment characteristics, such as education and experience; household assets, such as roof, wall, access to sanitation, electricity, among others; location characteristics, such as living in Bissau, proximity to markets; and employment in agriculture (the largest sector of employment in the country). Whereas the Oaxaca-Blinder decomposition is commonly used to understand differentials in outcomes by gender or race, we follow Essama-Nssah et al. (2013) using this logic to understand the differences in consumption expenditure between two years. We model a simple OLS regression to estimate the average returns to a series of household characteristics in Guinea-Bissau, using the log of per adult-equivalent consumption as our left-hand side variable and a vector of covariates on the right-hand side.

Findings

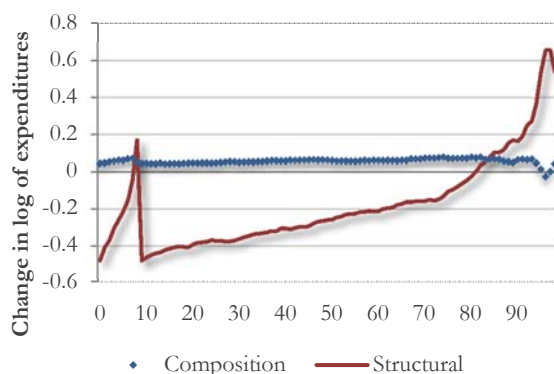
2. The initial results from an overall Oaxaca-Blinder decomposition (Annex Figure 2A.1) show the growth incidence curve driven most strongly by structural effects, meaning the distribution of returns (which are a function of asset ownership and intensity of usage, moderated by price levels) for the aggregate consumption expenditure model benefits the non-poor much more than the poor and is a larger driver behind the overall shape of the growth incidence curve. The endowment effect is smaller in magnitude across the distribution, but nonetheless positive sloping up to the 80th percentile and negative sloping thereafter, meaning it has a similar effect on the growth incidence curve.

3. In a more detailed dissection of endowment and structural effects, looking at the contribution by category of variables, such as demographics, assets, location, and employment, endowment effect is driven upwards by the distribution of a household's asset-base, and downwards by its distribution of demographics, while the distribution of living in Bissau, working in agriculture, or having better market access are more or less neutral up to the 90th percentile (Annex Figure 2A.2). Households at the top of the consumption distribution have more assets, including education, work experience, land, and other household assets, and such endowments are driving the positive slope of the curve and significantly higher incidences of consumption growth at the top percentiles of the distribution.

4. On the other hand, the distribution of the returns to market access (price effects) is negative with a negative slope, implying that the poor may see slightly higher (or “less negative”) returns from better market access than the non-poor (Annex Figure 2A.3). This makes sense since the poor largely depend on agriculture (smallholder and subsistence) and may benefit from having stronger linkages to markets where they can sell or trade goods. The distribution of returns to agriculture is upward sloping and higher for the 90th percentile, likely a reflection of the non-poor’s ability to use economies of scale, better access to market, a larger productive asset-base, and strategies to maximize returns which are unavailable to the poor. The distribution of returns to demographics, assets, and living in Bissau are fairly neutral and therefore deemed less influential here.

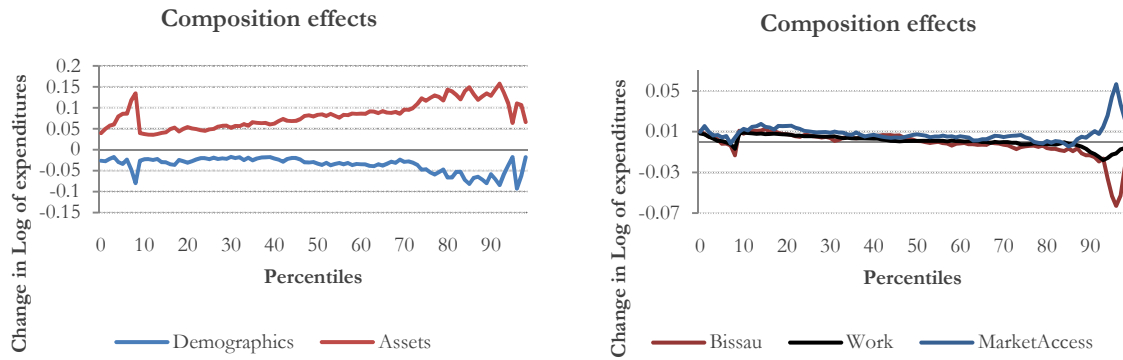
5. A detailed decomposition (Annex Figure 2A.4) further dissects composition and structural effects into each of the variables (that is, education, geography, employment) contributing to their magnitude, where the overall effects are the sum of those variables’ coefficients. The distribution of returns to participation in agriculture by percentile is positively sloped, indicating that in both years, returns were higher for the top part of the consumption distribution. In 2010, however, the returns were reduced for the poor and enhanced for the non-poor. Returns to land ownership were also both more pro-poor and higher in 2002 compared to 2010. Proximity to markets yielded similar benefits across time, while living in Bissau used to have higher returns for the poor, shifting down to a positive but nearly neutral distribution in 2010. The positive sign of the coefficient for living in Bissau is illustrative of an urban bias; growth tends to be more pronounced in urban areas, with households benefiting from proximity to markets, better schooling, and employment, with higher returns, relative to their rural counterparts, who may have less access to markets and basic services, and may practice subsistence or smallholder agriculture.

Annex Figure 2A.1. Composition and endowment effects for the Guinea-Bissau growth incidence curve (2002-2010)



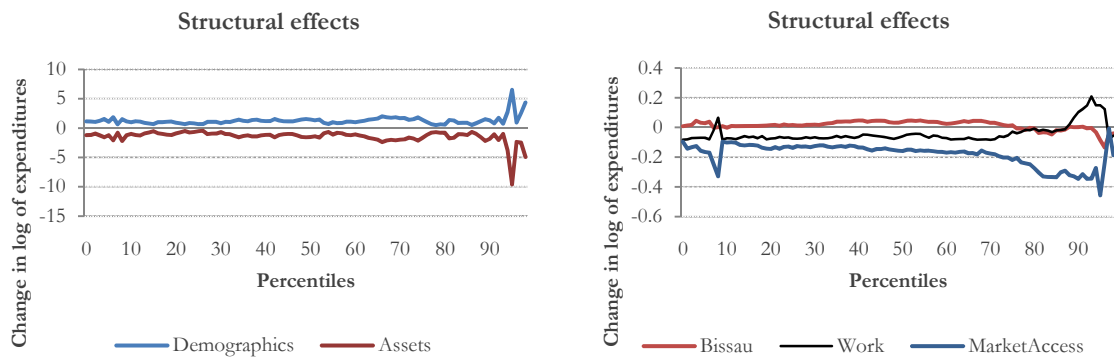
Source: World Bank staff calculations using ILAP 2002 and 2010 data.

Annex Figure 2A.2. Panel A: Composition effects



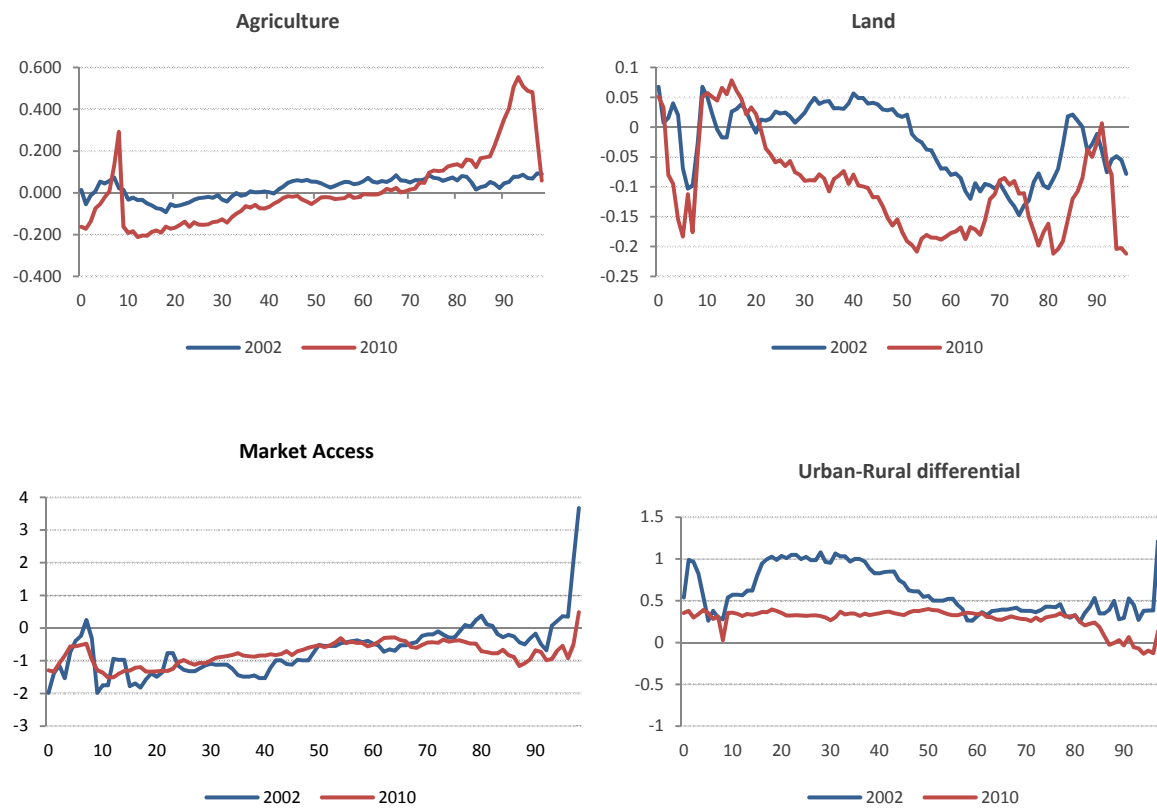
Source: World Bank staff calculations using ILAP 2002 and 2010 data.

Annex Figure 2A.3. Panel B: Structural effects



Source: World Bank staff calculations using ILAP 2002 and 2010 data.

Annex Figure 2A.4. Returns to select variables (inputs)



Source: World Bank staff calculations using ILAP 2002 and 2010 data.

Annex 2B. Mincerian Regressions

Annex Table 2B.1. Mincerian regressions for log of monthly earnings in poor and non-poor households (2010)

VARIABLES	HH Head		Synthetic	
	Non-Poor	Poor	Non-Poor	Poor
	lwage	lwage	lwage	lwage
Years of Education	0.0151 (0.0611)	-0.00438 (0.0455)	-0.0109 (0.0542)	-0.0116 (0.0467)
Years of Education squared	0.00593 (0.00594)	-0.000176 (0.00452)	0.00517 (0.00554)	-0.000471 (0.00527)
Primary premium	-0.00654 (0.0360)	0.0304 (0.0280)	0.0178 (0.0501)	-0.000241 (0.0352)
Secondary premium	0.0224 (0.0236)	0.0364 (0.0229)	0.0340* (0.0202)	0.0529** (0.0237)
Tertiary premium	0.0559* (0.0288)	0.0519* (0.0288)	0.0624*** (0.0233)	0.0845*** (0.0277)
Observations	931	1,232	984	1,391
R-squared	0.303	0.213	0.292	0.192

Robust standard errors in parentheses. Regressions include controls for experience (linear and squared), individual and household demographics and sector of employment. *** p<0.01, ** p<0.05, * p<0.1.

Source: World Bank staff calculations using ILAP 2010.

Annex 2C. Climate Change Impacts

Annex Table 2C.1. Guinea-Bissau's climate is changing in a number of ways

<u>Event</u>	<u>Historical Trend</u>	<u>Future Projections</u>
Temperature	Average yearly temperature has increased about 1°C, and observations suggest a shortening of the cool season to only two months	Mean annual temperature is projected to increase between 0.96-0.98°C for 2010-2039 and 1.77-1.95°C for 2040-2069.
Precipitation	Increased irregularity; overall trend of decreased mean annual precipitation and seasonal precipitation during the rainy season. A late start to the rainy season has been observed.	Most models project an average rise in precipitation by 3.71-3.8 percent for 2010-2039 and an increase of 3.40-3.84 percent for 2040-2069. By the end of the 21st century many models project mean precipitation over West Africa to increase during the rainy season with a small delay in the start of the rainy season. Projections for 'days without rain' show an increase during the dry season.
Sea Level	Rising trend; High tides have been increasing.	Rise projections throughout the 21st century and increase by 0.4 m (low emissions scenario, RCP2.6) to 0.7 m (high emissions scenario, RCP8.5) by 2100.
Floods		'Days with extreme rain' expected to slightly increase. Regional models indicate an increase in the number of days with extreme rainfall in May and July over West Africa.

Annex 3. Prioritization Worksheet
GUINEA-BISSAU - SYSTEMATIC COUNTRY DIAGNOSTIC
CONSULTATION WITH COUNTRY TEAM ON PRIORITIES

IMPORTANT INFORMATION

This SCD identifies three core interconnected areas of binding constraints: 1) *lack of inclusiveness and low rural productivity*; 2) *low and unstable economic growth*; and 3) *fragility and weak governance*. These constraints follow from the analytical model adopted in the SCD in that they reflect the evidence that poor governance and the limited provision of public goods are major obstacles to stimulating growth and reducing poverty in Guinea-Bissau.

Consistent with the approach taken in other SCDs, the evidence was reviewed and a list of mitigating policy actions to partly address each constraint identified. The pathways of each priority was then mapped to the central objectives: economic growth and poverty reduction. This helped in the identification of the most “economically, socially and politically” relevant actions and led to a subset of policies that, to the extent possible, are mutually exclusive given the multiple feedback loops. For the exercise to be relevant, you are encouraged to accept the realities of modern day Guinea-Bissau which will help to determine what is feasible. There are actions that may have significant poverty reduction impacts but, given your perspective of the current context in the country, implementation may not receive much traction. For example, the redistribution of income to the poor may face significant institutional and political challenges, and as such, actions in this specific area may fail to deliver expected outcomes. Feasibility relates to the likelihood of a particular action taking root, while traction goes one step further to focusing on the ability to deliver results in the short to medium term




ACTION REQUIRED

We are seeking your guidance and input to improve this document, for which priorities may need to be added, dropped, or revamped. Your comments and suggestions will feed into a revised and narrowed list that we hope to discuss with the country team on February 12. In this regard, we are requesting your assistance with **two** things:

- **Rank the mitigating policy actions identified within each of the core areas of constraints** along three criteria: *poverty reduction impacts*, *feasibility*, and *traction* to achieve the biggest impact in the shorter term. Since there are 9 mitigating policy actions identified for Area of Constraint 1, numbers 1 and 9 correspond to the highest and lowest rankings. This system is to be maintained for the other two priority areas. Each mitigating policy action should be ranked within (not across) each of the criteria; and

- As this is a preliminary list, please feel free to **provide comments (in the section provided) to further improve this list**, including but not limited to, additional actions to be considered for inclusion.

Other Instructions

-  You are encouraged to read the paragraph at the top of each area of constraint which describes the thought process and the analytics underlying the identification of the core areas of constraints before proceeding to the ranking exercise.
-  Insert any additional comments you may have in the space provided at the end.
-  Please submit your rankings and other comments directly to Rohan Longmore and Javier Baez **no later than Thursday, February 11 (noon, DC time)**.

NOTE: Confidentiality – rankings submitted will remain confidential and results will be presented in an aggregated manner.

Area of constraints 1: *Lack of inclusiveness and low rural productivity*

Rationale: Faster economic growth alone will not be enough to bring significant improvements in the living standards of most Guineans. The SCD shows that even the low economic growth recorded in the 2000s (assuming it distributionally neutral) would have reduced poverty by over 8 percentage points. Yet, in reality, since growth happened at the top, and the rest of the income distribution saw their consumption fall, poverty increased by 3.7 percentage points. Underlying the lack of inclusiveness is a low and unequal allocation and utilization of the endowments (human, physical, and natural capital) that are critical to raise the income generation capacity of households. Adults in the bottom two quintiles had completed just two years of schooling on average. At 54 years, life expectancy is three years below the regional average and maternal mortality is one of the highest in all of Africa. At 78 per 1,000 live births, infant mortality is 30 percent higher than the Sub-Saharan average and more than double the world average. Well over a third of the population (36.4 percent) still lacks access to safe water, and close to two-thirds has no access to modern sanitation. Only 6 percent of households have electricity, mostly self-generated. Key endowments are not only low but also used at suboptimal levels. Certain groups, particularly women, are disadvantaged in the labor market, and virtually all of the economically active population express a desire to have an extra job or work more hours. The exploitation of natural resources is inefficient and hinders their sustainability. Further compounding this context, rural productivity is low, indicating a low equilibrium in most markets and returns on productive factors that are inadequate, undiversified, and eroded by high transaction costs and significant exposure to uninsured shocks.

The analytical work carried out for the SCD identified the following six actions to mitigate the constraints underlying the lack of inclusiveness and low rural productivity in Guinea-Bissau:

Constraints mitigating policy actions	Poverty rank	Feasibility rank	Traction rank
2.1 Improve service delivery and the human capital base of the population (basic education, health, nutrition, water and sanitation, skills development).			
2.2 Enhance market accessibility and bargaining by strengthening connectivity (for instance, rural roads), access to information (for instance, telecommunications) and farmers associations.			
2.3 Reform land tenure and management systems to strengthen the rules that determine how land is used, possessed, leverage, and sold to boost investments and productivity in the agricultural sector.			
2.4 Improve agricultural technology and market support services (access to inputs and technologies, agricultural extension, logistics, storage, electricity, and so forth) that are likely to have a positive impact in the cashew sector and other untapped agricultural opportunities.			
2.5 Reduce vulnerabilities of households to shocks by developing and enhancing formal and informal risk management, coping and adaptation strategies (for instance, irrigation, enhanced seeds, financial inclusion such as mobile banking, index-based insurance, credit associations, and so forth).			
2.6 Develop productive safety nets and public works to deliver relief to the poorest, increase food security, encourage investments in human capital and productive assets, and contribute to building or rehabilitating small-scale infrastructure that yields services to households.			

Area of constraints 2: *Low and unstable growth*

Rationale: Growth in Guinea-Bissau has been low. GDP per capita grew by 0.7 percent annually between 2003 and 2014, less than half the average recorded for the Sub-Saharan region (1.5 percent) during the same period. Comparing Guinea-Bissau with its closest 19 African peers in per capita GDP back in 1990 shows that its rank fell from 10th to 18th as a result of having the seventeenth-lowest growth rate in the entire group. The structure of Guinea-Bissau's economy has barely changed over the last two decades and remains largely agrarian. Growth performance has been low and volatile with the production and export of a single commodity (unprocessed cashew nuts) – concentrated in the first rung of the value ladder - as the engine of growth. The production of cashews engages more than 75 percent of small farmers, underscoring the tight connection between incomes and movements in farm gate prices or production levels, especially for the poor. This economic structure has two broad implications: i) it has limited the resilience of the economy to mitigate the impact of shocks (terms of trade, political, and natural); and ii) it has limited the income and opportunities of the population, creating incentives for intense competition for rents which is one of the reasons for the low public investments (across all sectors) and the underdevelopment of other industries with economic potential within and outside of the cashew sector (cashew processing, rice, fisheries, mining, and tourism). Low and unpredictable public revenues, regressive and distortionary taxation, and poor quality of public expenditure limits the effectiveness and equity of the fiscal policy. The business climate is not conducive to the generation of growth,

employment and productive capital. Guinea-Bissau is at the bottom of all of the 10 Doing Business indicators. Financial inclusion is among the lowest in Sub-Saharan Africa. Guinea-Bissau's infrastructure that support production and provide economic services is in a woeful state, from the port to roads, and to access to electricity, potable water, or the internet. The lack of investments is an important pillar of a vicious circle of low productivity, low growth, lack of opportunities, elite capture which then feeds back into low investments.

The analytical work carried out for the SCD identified the following six actions to mitigate the constraints underlying the low and unstable economic growth that has characterized Guinea-Bissau:

Constraints mitigating policy actions	Poverty rank	Feasibility rank	Traction rank
3.1 Improve economic resilience through diversification by capitalizing on green shoots in agriculture (rice, sesame seeds and fishery) and other sectors (mining and tourism), and moving to higher-value chain segments (cashew processing).			
3.2 Improve cross-cutting economic and production support services to reduce the cost and improve the reliability of productive services and to generate additional investments, employment, and growth (electricity, ports, telecommunications, roads, and so forth).			
3.3 Increase financial inclusion through higher financial literacy and access to finance to raise savings and generate additional investments for growth.			
3.4 Reform the legal labor code to increase flexibility of the labor market to adjust to economic fluctuations and potential structural changes while ensuring an efficient degree of social protection.			
3.5 Enhance fiscal discipline and public revenue collection and efficiency to insulate the country from the volatility associated with grant flows, to address the narrow, distortionary, and regressive tax base, to create much needed fiscal space for growth and poverty reduction, and to safeguard fiscal sustainability.			
3.6 Make the most of regional integration of markets and infrastructure networks to exploit economies of scale, internalize technological spillovers, attract investments, and open new markets.			

Area of constraints 3: *Fragility and weak governance*

Rationale: Throughout the SCD, fragility and weak governance emerge as core obstacles to economic development and poverty reduction in Guinea-Bissau. Fragility constitutes a major challenge to economic development. Fragile or conflict-affected states (FCS) have historically underperformed in a wide array of indicators (WDR, 2011). This is the situation in Guinea-Bissau, where recurrent fragility and the interlinked competition for rents among the elite have negatively influenced virtually every economic, social, and

political dimension of the country, and are largely responsible for the country's "stop-and-go" development path. Recent estimates show that GDP per capita in Guinea-Bissau could have been 65-90 percent higher had it not been for its endemic fragility. Poverty is high (69.7 percent) and it has been increasing between 2002 and 2010. Weak institutions and governance are at the center of the rentier nature of the economy, which means that public institutions are geared toward providing private goods to elites –political and military ones– rather than public goods to citizens. This broken social contract is reflected in the poor provision of basic public goods and services, economic opportunities, and justice. Benchmarking analysis undertaken for this SCD shows that Guinea-Bissau ranks poorly (at the bottom 10-20 percent) with respect to regional and world averages in virtually all the human capital, physical capital, business climate, transparency, rule of law, and other quality of institution indicators. Another major negative implication of weak governance is the mismanagement of the country's natural wealth, which at the current utilization rate is depleting the main capital that would eventually allow its citizens to escape poverty and embark on a path toward greater and shared prosperity.

The analytical work carried out for the SCD identified the following nine actions to mitigate the constraints underlying fragility and weak governance in Guinea-Bissau:

Constraints mitigating policy actions	Poverty rank	Feasibility rank	Traction rank
1.1 Improve public financial management systems (budget preparation, execution, debt management, macro forecasts, accounting), including systems of internal and external control (procurement, auditing, and inspection services, Treasury Committee).			
1.2 Address the allocative, technical, and regressive inefficiencies in public spending by redirecting resources away from some sectors (military) to areas that contribute to building the human, physical, and institutional capital of the country (education, health, electricity), strengthening project appraisal capacity, and introducing equity-based formulas for budget allocation.			
1.3 Improve transparency and accountability by making more information publicly available (e-government), investing in statistics, and strengthening the roles of oversight and accountability institutions (national, subnational, civil society)			
1.4 Reform public sector incentives and raise capacity through establishing guidelines for staffing, entry exams, skills development, and performance assessment for civil service linked to quality of service delivery, merit-based job promotion systems, and measures to reduce the fragmentation of government.			
1.5 Strengthen the business regulatory environment by streamlining the procedures to start new businesses and register property, updating the legal framework to resolve insolvencies and enforce contracts, and strengthening the independence and effectiveness of regulators.			

1.6 Reform the management of natural resources to address unsustainable practices and preserve the country's natural wealth (the main foundation for current and future growth), jobs, poverty reduction, and shared prosperity in Guinea-Bissau.			
1.7 Strengthen the political system to rely on a more participatory and decentralized approach that enhances political participation, stabilizes democratic institutions, breaks the rural-urban divide, and addresses the disconnect between the State and the society			
1.8 Advance the security sector reform to reduce military interference in political and economic spheres while mitigating risks in the process that could trigger new instability.			
1.9 Strengthen the justice sector to improve access and equity and develop effective conflict resolution systems that address the weakness, favoritism, and corruption of the justice sector, and the resulting impunity, that contribute to fragility.			