ICR Review
Operations Evaluation Department

Report Number : ICRR10847

1. Project Data:		Date Posted :	04/04/2001	
PROJ ID :	P001540		Appraisal	Actual
Project Name :	Fin Sector/apex	Project Costs (US$M)	66.3	61.89
Country :	Madagascar	Loan/Credit (US$M)	45.0	48.13
Sector(s):	Financial Sector Development	Cofinancing (US$M)		17.50
L/C Number :	C2104			
		Board Approval (FY)		90
Partners involved :	IFC	Closing Date	06/30/1997	06/30/2000
Prepared by :	Reviewed by :	Group Manager :	Group :	

2. Project Objectives and Components

a. Objectives

(a) To complement the Government's on-going efforts to restructure the economy through providing funds for investments and reconstituting working capital in industry and other productive sectors, and through supporting small and medium scale enterprises;
(b) Assist in coordinating IMF and Public Sector Adjustment Credit conditionality to improve the efficiency of the financial sector, including expanded term resource mobilization, further interest rate liberalization, deepening of competition in the financial sector through elimination of the Central Bank's prior credit authorization; improvements in the system of credit ceilings and reserve requirements;
(c) Strengthening the appraisal and supervision capabilities of institutions operating in the financial and SME support sector; and
(d) Generation of new employment opportunities.

b. Components

Project objectives were changed because of changing country circumstances and Government priorities. It was restructured three times.

(a) Line of credit to finance investment projects ($47.15 million);

(b) Strengthening the financial sector by holding seminars in project evaluation and credit supervision for higher level staff of participating financial institutions and the central bank of Madagascar and strengthening of regulations and supervision of the financial sector by the Central Bank, including monetary management capabilities. During the first project restructuring in 1996, a sub-component was added to assist in the management and sale of public banks and in 1998 funding was added for a staff retrenchment program resulting from the privatization of two state-owned banks. These amendments to the Credit Agreement were approved by the Board. The changes to the project gave more prominence to the restructuring of the financial sector as a project objective ($8.52 million).

(c) Assistance to the mining sector through preparation of a new mining code, help for small mining operators, and market opportunity studies for specific minerals and preparation of the reorganization of the mining laboratory ($160,000). This component was transferred to other projects, although some preliminary work was financed under the Project Preparation Facility.

(d) Improving the Private sector framework by (i) restructuring of the Chamber of Commerce and Industry and provision of training, and telecommunications and data processing equipment; (ii) establishment of an investment promotion center. During project implementation, support for the restructuring of the Chamber of Commerce and the creation of a one-stop window for private enterprises were transferred to a private sector capacity building project in 1997 ($50,000).

(e) Development of small and medium scale enterprises through: (i) overseas scholarships for in-plant training and in-company visits to SME entrepreneurs and promoters; (ii) feasibility studies for SME promoters; and (iii) technical assistance in management techniques and data processing for SMEs ($1.03 million).

c. Comments on Project Cost, Financing and Dates

Total project cost remained quite close to initial estimates, although funds were reallocated during the project to reflect changing priorities of the Government. The project completion date was extended three times so that from an initial implementation estimate of seven years, the implementation period became 10 years.

3. Achievement of Relevant Objectives:

Major project objectives were met.

(a) Line of credit--this component experienced major disbursement delays in 1990-92 due to severe political instability, in the mid 1990s due to the delay in passage of a banking law, and in the late 1990's due to high inflation and high interest rates. However, by project completion, 64% of the revised line of credit amount had been disbursed. Funds were shifted from the credit line to finance technical assistance for the privatization of two state-owned banks and the staff retrenchment program associated with the privatizations. Since the project was prepared before a detailed monitoring system was required as part of project design, it is difficult to determine how much of an impact the project had. But a PSR dated June of 1998 notes that disbursements from the apex line of credit represented 20% of term loans and 4.5% of credit to the economy from 1990-97. Further, the ICR notes that it helped create about 2,000 new jobs and FMG 69.2 billion of value added. Total enterprise turnover increased by FMG 139 billion. Net income of assisted enterprises increased by FMG 20.1 billion. Enterprise self-financing capacity increased by FMG 49 billion. Export capacity improved from a very low base.
By project end, all banks in Madagascar had participated in the project and 75% of line of credit commitments were provided by private banks which began operation in the early 1990s. Repayment rates were very high; at completion only 3.5% of loans were in arrears. It can be inferred that interest rates were positive in real terms because interest rates were freely determined by participating financial intermediaries, the APEX rate was linked to the Central Bank reference rate which was revised to take into account the price instability of the mid -1990s. Participating bank staff were trained in term lending.

(b) Financial sector reform--the implementation of this component resulted in the substitution of direct for indirect methods of management of monetary aggregates, the system of central bank credit authorization was eliminated, bank-by-bank credit ceilings were abolished, auctions were introduced to permit the central bank to manage liquidity. Availability of information was also improved. A new banking law was enacted in 1996, which clarified the relationship between the central bank and the banking commission and established the powers of the banking commission with respect to prudential regulation. That law also established a system of risk ratios for bank lending portfolios. Equally significantly, two public banks which accounted for 60% of banking sector deposits in the early 1990s were privatized in 1998 and 1999. Redundancy payments were made, which eased the transition of 1,160 staff removed from the privatized state banks.

(c) Private sector component--the condition to restructure the Chamber of Commerce was replaced by a condition to amend the banking law. Further assistance to the Chamber was provided under a separate loan. The creation of the one-stop window for private enterprises was also transferred to that project, as was the creation of the investment Promotion Center. The communication and motivation campaign was carried out. However, no information was given to factually assess its impact, and the Government noted that the campaign was not as successful as had been envisaged because of the prevailing unstable economic conditions.

(d) Development of small and medium scale enterprises--Three entrepreneurs received scholarships to study abroad; 175 entrepreneurs received training in Madagascar to improve their knowledge of accounting and management information systems. During the midterm review, the in-country training component was revised to have private providers of training as the Ministry of Economy and Plan proved unable to implement this sub-component.

4. Significant Outcomes/Impacts:

Important fundamental changes were made to the framework and functioning of the financial sector, particularly the conduct of monetary policy, through the reforms adopted by the central bank.

Two large state-owned banks were successfully privatized, reducing the drain on the Government budget and improving the allocation of resources in the economy.

The amount of term finance available was increased. More private banks were encouraged to provide term loans. Staff of participating banks were trained in project evaluation methods. New jobs were created. Enterprise turnover, value added and net income improved, as did self-financing capacity. Export capacity improved, although from a very low base.

5. Significant Shortcomings (including non-compliance with safeguard policies):

There were no significant shortcomings.

6. Ratings:	ICR	OED Review	Reason for Disagreement /Comments
Outcome:	Satisfactory	Highly Satisfactory	The ICR team underestimated the impact of the major changes made.
Institutional Dev .:	Substantial	High	Fundamental changes were made in the legal and regulatory structure and the management of the financial sector by the Central Bank. It appears that these changes would be difficult to reverse.
Sustainability:	Likely	Likely	
Bank Performance:	Satisfactory	Highly Satisfactory	The Bank was very flexible in responding to changed country circumstances and to Government requests to modify project goals. The Department stayed the course for ten years, using the flexibility afforded by the Credit Agreement and the supervision process to facilitate project implementation.
Borrower Perf .:	Satisfactory	Highly Satisfactory	For the most important reforms, the ICR team underestimated the role of the Government and associated institutions.
Quality of ICR:		Exemplary	

NOTE: ICR rating values flagged with ' * ' don't comply with OP/BP 13.55, but are listed for completeness.

7. Lessons of Broad Applicability:

(a) Flexibility in project design and in responding to changed country circumstances contributed significantly to the positive outcomes of the most important components of the project, financial sector reform and the line of credit. This appears to be a case where building policy reform conditions into an investment loan was a reasonable proposition.

(b) Long term commitment by the Government and key actors like the central bank and the Ministry of Finance are key to responding to changed circumstances, as is flexibility on the part of the Bank.

(d) Increasing the technical competence of the key implementing agencies is crucial.

(c) Continued dialogue and cooperation between the Bank and the IMF, leading to complementary interventions, is critical for financial sector reform. The positive role and consistent messages of other donors funding related projects/programs is also important.

(d) Continuity in the teams discussing structural and sectoral reforms was key.

(e) It was important to provide adequate funds for staff retrenchment under the bank privatization program.

8. Assessment Recommended? ● Yes ○ No

Why? Because this project set the scene and was a catalyst for major changes in the financial and private sectors operating environment. Components of this project were transferred to other projects having the same overall objectives. This project is to be followed by a series of projects which aim to deepen the reforms already undertaken.

9. Comments on Quality of ICR:

The ICR is very well written and comprehensive. It would have been useful if the ICR could have distinguished somewhat more between the role of this project in financial sector reform and the role of the policy framework, as delineated in the IMF program, since the two were designed in close collaboration. However, this is not a major defect of the report.

Despite the fact that the SAR did not include a clear monitoring and evaluation system, having been produced before that was a standard Bank requirement, the ICR included a clear statement of component by component goals and quantitative indicators of achievement of project objectives, when available.

The table of original costs in the ICR is inconsistent with the appraisal costs as indicated in Annex 2 of the ICR.