



1. Project Data:		Date Posted : 05/18/2004	
PROJ ID : P008524		Appraisal	Actual
Project Name : Private Enterprise Support	Project Costs (US\$M)	20.3	7.3
Country : Kyrgyz Republic	Loan/Credit (US\$M)	15	4.6
Sector(s) : Board: FSP - Other industry (95%), Banking (5%)	Cofinancing (US\$M)	2.5	2.7
L/C Number : C2717; CP839			
	Board Approval (FY)		95
Partners involved : Japanese Government (PHRD)	Closing Date	12/31/1999	06/30/2003
Prepared by :	Reviewed by :	Group Manager :	Group:
Ilka Funke	Roy Gilbert	Kyle Peters	OEDCR

2. Project Objectives and Components

a. Objectives
To promote the adaptation of private enterprises to a market based system and to assist in the strengthening of key financial institutions of the Borrower.

b. Components
The PESP had two components:

1. Line of credit (planned US\$16.2 million; actual US\$4.1 million) to be channelled directly to private enterprises through a newly created Fund for Enterprise Restructuring and Development (FERD). The project was restructured in 1998, the FERD closed and an apex institution within the Central Bank established to on -lend these funds to eligible commercial banks. Micro-lending was introduced in December 2001.
2. Technical assistance (planned US\$3.9 million; actual US\$3.1 million) to:
 - (i) finance consultant services to enterprises,
 - (ii) provide financial sector support in the form of training to key financial institutions, the financing of an audit for the state-owned Savings Bank (Sberbank), and relevant studies. The financial sector support was revised in 1998 to focus exclusively on strengthening the credit appraisal capacity of participating banks, and
 - (iii) finance the management of the FERD (planned US\$2.5 million) and support project implementation.

c. Comments on Project Cost, Financing and Dates
The project preparation and start-up should have been delayed . It was approved in an unstable economic environment with a weak banking sector and a fragile business environment . The project closed three and one-half years after the initial closing date to allow the credit to disburse . The demand for credit was highly over-estimated. US\$7.1 million (50 percent of the estimated credit component) were cancelled in 2002 to adapt to actual demand .

IDA's actual contribution to the overall project costs fell to 63 percent (compared to 74 percent at appraisal) due to the lack of disbursement under the line of credit component (26 percent of original costs) . Most of the technical assistance (85 percent) was financed under the Japanese Grant . The counterpart funds of estimated US\$2.8 million never materialized, because (i) the local financial twinning institution went bankrupt shortly after loan effectiveness, (ii) the enterprises were not willing to pay for technical assistance, and (iii) the sub-borrowers did not contribute to the investment costs under the Line of Credit . It has to be noted, that the Borrower was unable to confirm the details of the data.

The Bank's administrative costs of the operation amounted to almost one -third of the disbursed amounts . A high percentage for a project with limited outcome .

3. Achievement of Relevant Objectives:

The PESP did achieve its objectives, but only to a limited extent and with significant delay . Only enterprises situated in the Bishek city area were able to profit under the project due to the limited regional operations of the participating banks . All in all, 293 sub-loans (for a total of US\$4.1 million) were approved, of which 266 were credits to small borrowers . Most of the participating enterprises increased their revenues due to the received credit. However, there is no clear evidence presented that the credit and the TA helped the enterprise sector to adopt to a market based system .

A significant amount of the technical assistance was not put to productive use (see 5.5). However, three of the four participating banks were able to improve their sub-project appraisal and risk management skills . Ninety percent of the PESP loan portfolio was classified as performing at loan closing, which - according to the ICR - compares favorably to the remaining banking sector . The banks have continued to use the same lending methodologies for their own lending operations . With the support of a consultant financed under the TA component, credit and risk management procedures for micro-finance lending were developed, and credit officers trained .

4. Significant Outcomes/Impacts:

1. The disbursed PESP-loans made a significant contribution to the availability of foreign currency credit in the Kyrgyz Republic. The loans account for 35 percent and 6 percent of the foreign currency denominate long-term (over one year) and short-term credit portfolio of the whole banking sector at loan closing .
2. The results from a survey involving 50 participating enterprises reveals that most of the sub-borrowers were able to increase their revenues by at least 50 percent due to the received support .
3. Three out of four participating banks improved their financial situation during project implementation . These banks have a market share of currently 19 percent of total banking assets and enjoy increasing depositors' confidence .
4. The PESP was instrumental for building capacity in the participating banks to lend to small borrowers . The developed procedures will also be applied under the follow-up operation financed by a consortium of multinational / bilateral financial organizations .

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

1. The original design of the project was overly complex and the implementation arrangements left ample room for political interference in the day-to day management decisions of the main vehicle, the FERD . Even though the restructured project improved the institutional arrangements, the lending procedures were still too complex and collateral requirements were high .
2. The size of the loan was too big compared to the prevailing economic situation and the fragile business environment. It was based on an inaccurate assessment of bankable projects . After restructuring, the limited number of participating banks and their reluctance to operate in the regions limited the outreach of the LOC component and the institutional development impact .
3. The foreign exchange risk was not taken into consideration at appraisal and only insufficiently during restructuring . The sub-loans were dollar-denominated, thus leaving the borrowers vulnerable to exchange rate risks that they could not sufficiently hedge against . This could easily have reversed the results of the line of credit component .
4. Enterprises were not willing to borrow for technical assistance, even on a shared cost basis, due to the availability of grant funding and misconceptions about the utility of TA . This jeopardized the initial idea to combine much needed training with credit to foster the adaptation of private enterprises to a market based system .
5. Almost US\$3.3 million of associated Japanese grant funds were spent without a clear developmental impact . The FERD was closed after having received intensive training and considerable financial support (almost 40 percent of the PHRD grant). Neither the Entrepreneurial Referral and Information Services (set up under a complementary PHRD grant to assist entrepreneurs in developing small and medium-scale businesses) nor the Kyrgyz Project Promotion Agency (which received support to help build a pipeline of bankable projects) had a significant impact, as enterprises made little use of their services . Another PHRD grant (US\$604,000 in 1994) to help enterprises to develop business plans and to initiate a first pipeline of projects financed under the line of credit did not bear fruit .
6. There was a lack both of monitoring and of procurement arrangements . The FERD lacked a procurement and MIS system, and the new apex institution in the Central Bank did only start applying the procurement guidelines after two years. The key performance indicators were only sporadically monitored . These shortcomings were further aggravated by the frequent turn-over of Bank task managers - seven during the eight years of effectiveness . This resulted in a lack of institutional memory .

6. Ratings:	ICR	OED Review	Reason for Disagreement /Comments
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Outcome :	Unsatisfactory	Moderately Unsatisfactory	The ratings are equivalent - OED only uses a different terminology than does the ICR.
Institutional Dev .:	Modest	Modest	
Sustainability :	Likely	Likely	
Bank Performance :	Unsatisfactory	Unsatisfactory	
Borrower Perf .:	Satisfactory	Satisfactory	
Quality of ICR :		Satisfactory	

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

7. Lessons of Broad Applicability:

1. A line of credit is not an appropriate tool in an unstable economic environment with a weak financial sector . In retrospect, it would have been advisable to delay the PESP and wait for an improvement in the overall macro-economic performance and the impact of a financial sector adjustment operation, that was successfully launched in FY96. The results of the PESP in later years clearly support these findings .
2. There needs to be a careful assessment of the demand for loans and technical assistance . In an economy in transition, alternative forms of financing (such as leasing, capital financing, mortgages) should also be taken into consideration.
3. Enterprises will not pay for TA if it is perceived as a waste or if grants are available from other donors .
4. The foreign exchange risk needs to be taken into consideration . Exposing enterprises to risks that they are unaccustomed to and cannot hedge against can jeopardize earlier results of an operation or contribute to an unsatisfactory outcome.

8. Assessment Recommended? ☐ Yes ☒ No

9. Comments on Quality of ICR:

The ICR gives a fair picture of the developments under the PESP . It provides useful numeric background information on the output of the project as well as a summary of results and lessons learned based on a survey and workshop with 75 stakeholders. However, the ICR does not sufficiently elaborate on the outcome of the stated objectives . It would have been useful to have more information on this in the main part of the report . The overall assessment of the operation might have profited from this.