

ICR Review  
Operations Evaluation Department

1. Project Data: Date Posted : 09/22/2004

PROJ ID : P081845	Appraisal	Actual
Project Name : Development Support Credit	Project Costs 300.00	300.00
	US\$M )	
	(US\$M)	
Country : Bangladesh	Loan/	
	US\$M ) 300.00	
	/Credit (US\$M)	300.00
Sector (s): Board: PS - Banking (25%), General energy sector	Cofinancing US\$M )	
	(US\$M)	
(25%), Central government administration (20%), General industry and trade sector (20%), Law and justice (10%)		
L/C Number :	Board Approval FY )	03
	(FY)	
Partners involved :	Closing Date 12/31/2003	12/31/2003

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## 2. Project Objectives and Components

## a. Objectives

The overall objective of the project was to support the implementation of the I -PRSP in two areas: governance and fiscal sustainability. The specific objectives were :

- 1) to stabilize the macro-economic environment (with the IMF in the leading position);
- 2) to improve the governance of the financial system;
- 3) to reduce the financial hemorrhage caused by State -Owned Enterprises (SOEs);
- 4) to improve the availability and enhance the efficiency of the energy sector; and
- 5) to enhance overall accountability and transparency and reduce corruption .

## b. Components

The Credit supported actions in five areas corresponding to the five objectives :

- 1) macro-economic environment: a satisfactory implementation of the PRGF program;
- 2) financial system: strengthen the regulatory and oversight framework and institutions;
- 3) SOEs: reduce the budgetary drain, adopt a new privatization policy, and make progress in closure and /or restructuring of loss-making SOEs;
- 4) energy sector: establish a new pricing framework and an energy regulator; and
- 5) governance: improve procurement and enhance public financial accountability .

## c. Comments on Project Cost, Financing and Dates

The one-tranche Credit was approved on the basis of actions taken prior to negotiations and disbursed upon effectiveness in June 2003. It was closed on December 31, 2003, the original date. The project was the first

development policy operation since about 10 years and the first in an anticipated series of three in support of the implementation of the I-PRSP. It was grounded in extensive AAA, some carried out jointly with ADB . It provided for triggers for further lending, discussed and agreed with the authorities at the highest level at preparation /appraisal.

With some triggers delayed and some revised, the second operation has been postponed from FY 04 to FY05.

### 3. Achievement of Relevant Objectives:

1) The objective of maintaining a satisfactory macro framework was substantially achieved through 2002 and 2003, notably with fiscal indicators improving .

2) Achievement of financial sector objectives is considered moderately satisfactory . The role of the central bank was strengthened both in the conduct of exchange rate and monetary policy and in bank supervision . The Nationalized

Commercial Banks (NCB) were brought under the supervision of the central bank; their market share fell to 40

percent of total financial assets from 67 percent four years earlier. But measures aimed at privatizing the state

owned bank were slower than expected and some triggers for the next operation were delayed .

3) Achievement of SOE objectives is considered satisfactory. The fiscal drain from the SOE sector disappeared in FY03 as the

SOE sector showed a net profit, but it deteriorated again in FY04, to show a net loss, although the loss was smaller than it had been

□ prior to FY03 (Table below). Overall, the SOE sector has shown improved performance with respect to its net drain on the fiscal

situation, and the manufacturing sector in particular has improved due to Government's applying a hard budget constraint and to the

divestiture of a larger than expected number of enterprises.

### Trends in SOE profits and losses (in billion takas )

	FY01	FY02	FY03	FY04
Net profit/loss	-25.4	-14.2	1.0	-8.0

4) The objective of improving the efficiency of the energy sector has had mixed success and overall is considered moderately unsatisfactory. On the positive side, power system losses have continued to decrease and collection rates have increased over the

FY02-04 period, and a new petroleum, gas, and power pricing framework was adopted; an Energy Regulatory Commission Act was

passed that establishes a regulatory agency. Electricity prices were adjusted in September 2003 but not in March 2004, as

expected, and petroleum prices were not increased at all in September 2003 or March 2004, as expected, but prices of kerosene

and other petroleum products (jet fuel and furnace oil) were increased in May - June 2004 by varying amounts.

5) The objective of improving governance was partially achieved. The law creating the Anti-Corruption Commission was expected

to be enacted by June 30, 2004, and its members appointed thereafter. An anti-corruption strategy, including the strengthening of

the Auditor General 's Office, is being developed. Following approval of a template for procurement reform prior to negotiations, the

Government issued draft guidelines, expected to clarify public procurement. The process of implementing the Supreme Court

directive of 1999 on separation of the judiciary and the executive was pursued and a Judicial Service

Commission established. The Commission is operational, but the Judicial Pay Commission is still to be established. The process of separating accounting and auditing was also pursued. Here also, some triggers had to be postponed and/or revised.

#### 4. Significant Outcomes/Impacts:

- 1) The role of the central bank in banking supervision was strengthened .
- 2) The NCBs fall now under the supervision of the central bank and their importance in the banking sector was reduced.
- 3) The size of the public sector in manufacturing was reduced .

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

- 1) In the financial sector, there was stronger than expected political opposition to bank privatization and divestiture, and triggers originally set for the follow up operation in this area have been delayed. In addition, the Government does not currently plan to divest any shares of Sonali Bank as had been originally agreed.

- 2) On SOE reforms, the Privatization Act recently passed has not been followed up by the necessary regulation to implement it.

Some privatization triggers for the next operation are behind schedule and the privatization process has not been entirely satisfactory (privatization bidding handled by the Privatization Commission was not satisfactory, according to the Region, but it is not clear whether line ministries are better equipped to handle the process).

- 3) Reforms in the energy sector are key to reducing the fiscal drain of the SOE sector because the technical and financial losses in this sector are so large. The new pricing formula in energy called for a tariff increase in March 2004 which did not occur; petroleum prices are currently between 20 and 35 percent below prices indicated by the formula. The required price adjustments have become triggers for the next Development Support Credit operation. Although the Energy Regulatory Commission act was passed, the agency is far behind schedule in becoming operational.

6. Ratings :	ICR	OED Review	Reason for Disagreement /Comments
Outcome :	Satisfactory	Moderately Satisfactory	See sections 3 and 5.
Institutional Dev .:	Modest	Modest	
Sustainability :	Likely	Non-evaluable	Although initial reform steps were taken, it is not clear that the Government's commitment is strong enough to resist political and labor union pressure; policy reversal could result.
Bank Performance :	Satisfactory	Satisfactory	
Borrower Perf .:	Satisfactory	Satisfactory	
Quality of ICR :		Satisfactory	

#### NOTE:

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) One-tranche operations provide the flexibility to adapt to changing circumstances and avoid the pressure and - sometimes embarrassment - accompanying the release of tranches .
- 2) In development policy operations, conditionality should stress effective implementation of laws and /or measures rather than their adoption by the Government or submission to parliament .

3) In view of the long-standing and protracted dialogue between the Bank and the Government on reforming the energy sector, the most appropriate strategy for the Bank is probably to concentrate on developing an environment in

which the private segment of the industry can flourish and erode the position of the public segment .

4) Timeframes for the privatization/restructuring of SOEs are measured in decades rather than years and adjustment

operations should be accompanied by enterprise -specific TA to assist in the restructuring /divestiture.

8. Assessment Recommended? Yes No

☐ Why? As part of the series of operations covering the reform program under the I - PRSP and PRSP.

9. Comments on Quality of ICR:

The ICR is satisfactory, although the Region subsequently provided considerable additional information to OED that served to

highlight both significant gaps in the information provided by the ICR and inconsistencies in information and point of view between

the Region and its ICR. For example, the ICR assessed achievement of objectives in the energy sector as moderately

unsatisfactory, while the Region presented only positive developments in the energy sector and disagreed with OED's assessment

that progress in this sector had been unsatisfactory. It was not clear whether the Region was disagreeing with its own ICR. In

addition, the Region noted that there had been an agreement to adjust power prices in the sector once a year, while the Program

Document and the ICR both stated that the agreement called for price adjustments twice a year, or more frequently if called for. The

Region stated that further price adjustments were not required in March 2004, while the ICR states that "petroleum prices were (at

the time of the ICR, June 2004) 20-35 percent below prices indicated by the DSC formula".

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