ICR Review
Operations Evaluation Department

Report Number : ICRR11509

1. Project Data:		Date Posted :	06/30/2003	
PROJ ID :	P035628		Appraisal	Actual
Project Name :	Enterprise Development	Project Costs (US$M)	106.00	38.20
Country :	Zimbabwe	Loan/Credit (US$M)	70.00	30.60
Sector(s):	Board: PSD - General industry and trade sector (62%), Micro- and SME finance (37%), Central government administration (1%)	Cofinancing (US$M)	36.00	7.60
L/C Number :	C2851			
		Board Approval (FY)		96
Partners involved :	Government, Enterprises	Closing Date	12/31/2002	12/31/2002

Prepared by :	Reviewed by :	Group Manager :	Group :	
Pierre M. De Raet	Poonam Gupta	Kyle Peters	OEDCR	

2. Project Objectives and Components

a. Objectives

The objective was to support a strong supply response by private sector enterprises to policy reforms undertaken since 1991 under an Economic Structural Adjustment Program (ESAP), through: (i) an increase in the growth of export-based output; and (ii) a broader participation in economic activity, in particular by indigenous firms .

b. Components

There were 3 components and several sub-components:

(a) Business Services Component consisting of : (i) provision of matching grants to existing business associations to help strengthen their services to members; (ii) enhancement of an existing matching grant scheme for individual enterprises entering or expanding into export markets; and (iii) support of the initial costs of creating linkages between established and emerging enterprises through a matchmaking facility (IDA financing US$ 6.4 million);

(b) Finance Component consisting of : (i) a SME Finance Facility for the provision of medium-term funds for the investment and working capital needs of SME firms (IDA financing US$ 25.0 million); and (ii) an Export Finance Facility to support pre- and post shipment export financing for emerging exporters unable to access such financing from commercial sources (IDA financing US$ 35.0 million); these two facilities were set up through an Apex Unit at the central bank and were accompanied, respectively, by a SME Credit Guarantee Fund, and an Export Finance Guarantee Fund; and

(c) Institutional Development Component: provision of support for the strengthening of various institutions which were key to improving enterprise development and export competitiveness (IDA financing US$ 3.6 million).

c. Comments on Project Cost, Financing and Dates

Effectiveness conditions were fulfilled after one year of Board approval . Disbursements totalled SDR 22.6 million (47.51%), with the balance of the Credit cancelled in June 2002.

Implementation encountered two difficulties : (i) lack of demand for funds under the Export Financing and the matching fund facilities; and (ii) weaknesses in the administration of the project . In addition, the increasingly difficult macro-economic environment led the Bank and the Government to recognize that the general economic climate and business environment were not conducive to a sound and sustainable implementation of the project and therefore the need to support and improve the economic reform process . To meet these "emerging priorities", a reallocation of

US$5 million was made in April 1999, by redirecting funds from the lines of credit to the institutional development component to strengthen agencies and ministerial departments in charge of economic policies .

The mid-term review of May/June 1999, confirmed that assessment by recommending a larger and more important reallocation, in the amount of US$18.7 million, in favor of the ID component together with the closure of sub-components that had proved inoperative or had hardly started . This restructuring was agreed with the authorities and submitted to the Board and approved on July 7, 2000. However, as all disbursements to Zimbabwe had been suspended in May 2000, this restructuring was never implemented.

3. Achievement of Relevant Objectives:

The objectives of the project, promoting export-led growth and redressing the dualism in the economy by encouraging the development of indigenous small enterprises, were relevant and in conformity with Bank strategy . However, objectives were not achieved.

Under the first Component, there was little interest in the services offered, mostly as a result of the difficult macro-economic situation and the poor environment for PSD; in addition, the entities responsible for this component encountered administrative and legal problems and were poorly equipped to launch and develop business services . By the mid-term review in May 1999, operations were marginal and no disbursement had taken place under the business associations and matching grant scheme sub-components; the third sub-component, the matchmaking facility, had not yet become operational and it was decided to drop it and reallocate the funds to other uses .

Under the second component, the key objective of creating and supporting a sustainable credit delivery system through the SME line in favor of small indigenous firms was not achieved, mainly because the business environment was negatively affected by the poor macro-economic climate; however the line was almost fully disbursed (see Section 5 below).

Under the institutional development component, progress was achieved in some areas, notably at the central bank where supervision capabilities were strengthened. Support was given to the National Economic Consultative Forum (NECF), where a key policy framework was prepared for the Land Reform Plan, including allowing the private sector to be involved in the reform program. The Customs and Excise Department was completing its automation and improvement plans for the administration of duty-drawback with support from the project. However, little capacity building was achieved by the Administrative Secretariat, responsible for the overall coordination and management of the project, with negative impact on the implementation of all components .

4. Significant Outcomes/Impacts:

A major outcome - under the institutional development component - was the preparation of the Land Reform Plan by the NECF in support of the donor conference on land reform in September 1998.The duty drawback system and the ASYCUDA system for custom administration are working.

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

The project team showed creativity in designing project components (e.g., matching grant scheme, match making facility and export finance facility discussed in section 2b). The design of the credit line was consistent with current best-practice. In April 1999 and again at mid-term review in May/June 1999, the Bank team showed flexibility in redirecting funds from the lines of credit to meet the "emerging priorities" of sound macro-economic management. The project also followed a participatory approach to ensure stakeholder ownership and used grant financing available from DFID to support implementation. However, there were two major shortcomings.

(i) While the team working on the EDP was poorly placed to second guess the judgement on the macroeconomic situation, management should have been able to see the risks to macroeconomic stability posed by flaws in sequencing of reforms in the macro program and the potentially negative impact of the large fiscal deficit on enterprise development and on the line of credit for SMEs. At the time of appraisal and Board approval, the Central Government fiscal deficit (excluding grants) was above 10 percent, while the consolidated deficit was about 13 percent and financing of fiscal deficits was absorbing substantial private savings and keeping real interest rates high .

(ii) The line of credit under the second component was suspended in November 1998 after most of it was disbursed at interest rates that were substantially below the risk free T-bill rate and inflation rate. OP 8.30 governing financial intermediary lending (or lines of credit) states in para 15 that Bank funds are priced to be competitive with what the participating financial institutions and their borrowers would pay in the market for similar money, taking into account, as relevant, maturities, risks and scarcity of capital ....FIL funds are lent to participating FIs at rates agreed with the Bank that (a) are not negative in real terms; (b) provide adequate margin to FIs to cover costs ...

Two months after effectiveness, in June 1997, the retail interest rate (from participating financial institutions to sub-borrowers) was 10 percentage points below the T-bill rate (from 2 percent below at effectiveness) and 15 points below by December 1997. The retail rate was increased from 14 to 20 percent in May 1998, but it was still 10 points below the T-bill rate and by October 1998 it was almost 17 points below the T-bill rate. The same divergence is noted when comparing the retail rate with the inflation rate, as there was parallel movement between the T -bill rate and the inflation rate. Credits under the SME line were extended for a maturity of five years (with a grace period of 18 months), increasing the likelihood of increasing negative rates in a climate of high inflation . OED was unable to get the actual disbursement profile of the SME line of credit or how much was undisbursed when the line was suspended in November 1998. However, the various PSRs indicate that disbursements were fast : the PSR of 10/14/97 notes a dramatic increase in the use of the line; the one of 3/18/98 notes continued strong demand, the one of 6/9/98 also indicates that disbursements were faster than expected and the PSR of 11/10/00 states that the line was almost fully disbursed; about US$24.9 million were disbursed out of US$ 25 million. The region notes that a large segment of SMEs were reached by this program but information gathered for OED's Zimbabwe Country Evaluation indicates that subsidized funds were directed primarily to privileged political party members .

6. Ratings:	ICR	OED Review	Reason for Disagreement /Comments
Outcome:	Unsatisfactory	Unsatisfactory	
Institutional Dev .:	Modest	Modest	
Sustainability :	Unlikely	Unlikely	
Bank Performance :	Satisfactory	Unsatisfactory	At the time of preparation and appraisal of this project, central government deficits averaged 10 percent of GDP and parastatal losses another 2-3 percent. The sequencing problems in the macroeconomic program (where a reduction in tax rates and interest rates were sequenced to come before expenditure reductions from parastatal reform and public employment reductions) made it unlikely that Zimbabwe would achieve macroeconomic stability as was evident in 1993-94. The second tranche of SAC II could not be released in mid-1997 (at the time the EDP became effective) because the central government deficit had risen to 12.5 percent of GDP. The view of the team working on EDP is that they had reasonable expectation that the macroeconomic situation would stabilize. The wholesale interest rate at project effectiveness in April 1997 was 9.84 percent until April 1998 when it was raised to 13.9 percent. Retail interest rates were at 14 percent until April 1998 when the rate was increased to 20 percent. However, *both* rates, in particular the retail rate were below the T-bill and inflation rates in contradiction of the OP governing financial intermediary lending. The region is of the view that there were no interest rate ceilings on the wholesale rates and that "expost the retail rates tended to be negative in real terms."
Borrower Perf .:	Unsatisfactory	Unsatisfactory	

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:

In a country where political and economic governance has deteriorated to the point of distorting lending schemes in favor of privileged political party members, the Bank should discontinue operations which may become a vehicle for such activities.

8. Assessment Recommended? ○ Yes ● No

9. Comments on Quality of ICR:

While the ICR is of satisfactory quality it could have provided more analysis of the subsidization of the wholesale and retail interest rates and of its magnitude compared with the T-bill, commercial bank lending rates and inflation rates. It should have included a clear discussion of the background and reasons leading to the April 99 reallocation and the June 1999 mid-term proposed reallocation.