Report Number: ICRR14904

IEG ICR Review

Independent Evaluation Group

1. Project Data:		Date Posted: 05/31/2016		
Country:	Nicaragua			
Project ID:	P109691		Appraisal	Actual
Project Name:	Micro, Small And Medium Enterprise Development	Project Costs (US$M):	20.00	12.04
L/C Number:		Loan/Credit (US$M):	20.00	12.04
Sector Board:	Financial and Private Sector Development	Cofinancing (US$M):		
Cofinanciers:		Board Approval Date:		06/12/2008
		Closing Date:	12/31/2013	12/31/2014
Sector(s):	General industry and trade sector (44%); Central government administration (30%); Microfinance (13%); SME Finance (13%)			
Theme(s):	Micro; Small and Medium Enterprise support (67%); Regulation and competition policy (33%)			

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2. Project Objectives and Components:

a. Objectives:

The project development objective (PDO), as stated in the Financing Agreement (p.6) was:

"**to improve the competitiveness of Micro , Small and Medium Enterprises (MSMEs) and the business climate that affected those firms**".

b.Were the project objectives/key associated outcome targets revised during implementation?

No

c. Components:

There were four components:

- Improvements to the business and Investment Climate for MSMEs *(appraisal estimate US$4.11 million; actual cost at completion US$3.65 million).* This component was intended to remove administrative and regulatory obstacles for MSMEs, through a) Business process simplification and decentralization; b) Strengthening policy and technology frameworks for MSMEs; and c) Access to Quality Assurance and Certification.

- Matching Grants for MSMEs *(appraisal estimate US$8.36 million; actual cost at completion US$6.44 million)*, The grants were to support *inter alia* innovations, environmental improvements, and forward and backward linkages. This component aimed to increase firm-level productivity and increase value chain efficiency through the provision of matching grants, awarded competitively. The matching grants would not substitute for commercial credit; instead would complement commercial credit with the aim of developing "bankable" MSMEs.

- Increased access to financial services for MSMEs *(appraisal estimate US$4.8 million; actual cost at completion US$0)*. This component was intended to improve MSME access to affordable, reliable financial products, by providing a pilot Partial Credit Risk Guarantee (PCRG) for loans by regulated financial institutions to MSMEs. This component was dropped when the Government decided not to launch the PCRG mechanism on account of institutional and legal changes in 2009 that were incompatible with the component.

- Institutional Strengthening of the Ministry of Economy (MIFIC) *(appraisal estimate: US$1.48 million; actual cost at completion US$1.95 million)*. This component was intended to strengthen MIFIC as project coordinator, Sector-wide Approach Program (SWAP) manager and strategic leader in private sector development. National MSME surveys were expected to be undertaken to better inform public policy discussions. The component was also to cover the costs of procurement and financial management incurred by MIFIC.

d. Comments on Project Cost, Financing, Borrower Contribution, and Dates:

Project Cost: Project costs came in well under budget. To a large extent this reflected the fact that Component 3 was cancelled following the Mid-Term Review in February 2012, resulting in a reduction of US$5.3 million. Apart from this, exchange rate fluctuations in the Special Drawing Right (SDR) /dollar rate that reduced the project budget by US$1.1 million over the life of the project.

Financing: The sources of funding for this project consisted of an IDA credit of US$20.0 million (of which US$12.5 million was disbursed and US$5.3 million was cancelled). The reduction in the credit amount by completion was due to SDR/dollar depreciation.

Borrower contribution. Borrower financing was neither planned nor contributed.

Dates. The project's closing date was extended once for a year in December 2013. This was to mitigate the effects of a year's delay in effectiveness due to a recent (2007) change in Government and the time required to obtain approval by the National Assembly.

3. Relevance of Objectives & Design:

a. Relevance of Objectives:

High.

Nicaragua's private sector is dominated by micro and small businesses, and a large informal sector. Together, at the time of appraisal, these accounted for about 45 percent of the Gross Domestic Product and 74 percent of urban employment. The 2006 Nicaragua Enterprise Survey indicated that access to financing was a major constraint for firms. The combination of guarantee requirements, costs and a conservative banking sector limited access severely by micro, small and medium enterprises. Additionally, the unique lending methodologies that serve the needs of MSMEs were not understood by the commercial banks and finance companies. Bank finance provided less than 15 percent of working capital for small and medium enterprises, and less than 20 percent of their investment finance needs.

The project was highly relevant to the country's developmental objectives and the Bank's country assistance strategies – both at the time of approval and at closing. The objectives were fully consistent with the Bank's Interim Strategy Note, presented to the Board in 2005, a key objective of which was to bring about an improvement in the investment climate through reforms in the regulatory framework for businesses, so as to *inter alia* reduce bureaucratic costs, improve property rights, broaden financial services and promote environmentally sustainable growth. The project was relevant to the Government's Poverty Reduction Strategy under the National Human Development Plan, which called for a private sector development-led growth strategy, with the MSME sector playing a strong role, aided by a more efficient regulatory framework. It was also consistent with the most recent Country Partnership Strategy (FY13-17), which (para 40) reiterated the importance of improving the investment climate, in order to sustain and diversify local and foreign investment, and supported (Strategic Area 2) the Government's efforts to improve competitiveness, as a means of increasing productivity and raising income levels.

b. Relevance of Design:

Substantial.

The design of project activities was relevant and the results chain could be expected to lead to the desired project outcomes. Component 1 directly addressed the objective of improving the business environment, through steps to simplify business processes and reduce barriers to entry, especially for MSMEs. The provision of matching grants to MSMEs was aimed at improving skills and enhancing productivity, both of which were crucial to the objective of strengthening competitiveness. The design of the matching grants program drew upon the lessons of successful experience, for instance in the need for utilizing an experienced management firm, and implementing a transparent and competitive selection process. The introduction of a pilot Partial Credit Risk Guarantee (PCRG) was a means of addressing a key constraint faced by Nicaraguan MSMEs – that of limited access to finance. The results framework adequately captured the linkage between project activities and desired outcomes, including, for example, the impact of matching grants on product or process quality enhancement projects (including international certifications), introduction of new products/processes, and whether the grants leveraged commercial bank financing. Intermediate outcomes, which constituted the requisite building blocks in the causal chain, were appropriately identified.

Design changes during implementation were also substantially relevant. Both government and Bank team made efforts to ensure that project activities under the components remained relevant to the PDO, adjusting these through three restructurings to maintain consistency with changing priorities.

4. Achievement of Objectives (Efficacy):

"To improve the competitiveness of Micro , Small and Medium Enterprises (MSMEs) and the business climate that affected those firms".

There are two objectives and their achievement is discussed here :

1. Objective: "**To improve the competitiveness of Micro , Small & Medium Enterprises**", Rating: ***High***

Outputs: 628 firms implemented product or process quality enhancement projects – well in excess of the original target of 159 and revised target of 120, and these firms created also 1,196 permanent jobs (1.4 jobs per firm on average) and 351 temporary jobs. Product or process quality enhancement enabled 617 firms to succeed in increasing sales, exceeding the target of 120. The average rise in monthly sales of these firms was 165 percent (in contrast, in 2010, small firms elsewhere in the economy recorded a rise in sales of only 0.8 percent, of medium firms by 0.3 percent and large firms of 12.2 percent).

Outcomes:
The goal of improving competitiveness of MSMEs in Nicaragua appears to have been achieved. Three rounds of matching grants were awarded to 864 participating enterprises (well in excess of the target of 600) to an aggregate of US$5.56 million, just short of the US$5.8 million planned at appraisal. The provision of matching grants was expected to have a direct and positive impact on firm productivity in the medium term through enhancement of skills and production processes. During 2010-14, grants were provided in five (pre-selected) strategic sectors (agribusiness, wood furniture, apparel, leather goods and artisan products) and these resulted in 469 firms introducing new products or processes - well in excess of an initial target of 30 firms and revised target of 80 firms. By providing support to the Intellectual Property Registry, the project saw a tripling of the number of trademarks registered annually, from about 3,000 in 2010 to over 10,000 in 2014, and the number of MSMEs registering their brands jumped from just 26 to 1,196 over the same period. In Nicaragua, the revenue generated from these trademarks also increased significantly from about US$0.4 million to over US$1.2 million over the period.

It should be noted that 147 participants (or 14 percent of beneficiaries) came from Nicaragua's minority population. Secondly, in terms of gender impact, more than half of the 864 beneficiary firms were led by women entrepreneurs whose firms were relatively more successful in introducing new products than firms led by men. Firms led by women were responsible for 72 percent of all new products introduced and 47 percent of all new permanent jobs created.

2. Objective: "**To improve the business climate affecting Micro , Small and Medium-sized firms**". Rating: High

Outputs:
Intermediate outcomes (outputs) contributing to the achievement of the above outcomes include the fact that streamlined procedures were introduced at the one-stop shop for business registration, including development of a website, plus automation of internal procedures at the Commercial Registry. Secondly, the project supported

major changes introduced in the Commercial Code, including the provision of a new company law, updates to regulations surrounding commercial contracts, and strengthening of the MSME special regime. Thirdly, to address administrative hurdles posing specific constraints to MSMEs, support centers geared to helping MSMEs navigate the business climate were provided with technical assistance and equipment, to enable them to serve their clients better. The result was a doubling of the number of enquiries from MSMEs that the 8 regional offices together attended to. To assist MSMEs enter larger supply chains and take advantage of standards and certification necessary for exporting, the project assisted the National Metrology Lab to upgrade its standardization services, especially for MSMEs, and the Ministry of Health to automate health and food permits, substantially reducing their processing times. Finally, the project assisted the Ministry of Labor, through technical assistance, to upgrade practices in MSMEs in worker health and safety standards. By close of project, the Ministry had trained some 279 MSMEs in good worker health and safety standards, which was expected to lead to an improvement in their productivity.

Among other outputs, institutional strengthening improved the capacity of the coordinating agencies, the Ministries of Economy (MEFCCA) and of Industry & Commerce (MIFIC), to manage the MSME sector and strategize to further improve its competitiveness, whilst also planning further improvements in the business environment. Towards this end, the project provided training to 53 personnel in project management, planning and monitoring (slightly less than the target of 60). As an outcome of the training, the project implementation unit (PIU) delivered clean audits throughout the project period, plus 4 annual operational and procurement plans, which could be considered a satisfactory outcome of the training provided.

Outcomes:
The project contributed significantly to improvement of the environment for doing business in Nicaragua. Key results indicators were met: the time taken for starting a business (as measured by the Bank's Doing Business indicators) declining from 39 days to 13 by the end of the project., as against the target of 27 days equivalent the actual appraisal target was a 30 percent decrease over the baseline, instead of which a 60 percent decrease was achieved), Though the results indicators did not specifically focus on cost-reduction, considerable progress was achieved in this regard during implementation of the project – with costs for starting a business declining from 111 percent of per capita income in 2010 to 74 percent by 2015. The time to obtain a construction permit across 8 municipalities was reduced from 6.4 days to 1.25 days, together with a general strengthening of legal security of companies and their property rights. The project saw an increase in the number of formally registered licenses and construction permits, resulting in an increase in revenue across municipalities of 70 percent between 2012-14 as the reforms became effective.

5. Efficiency:

Economic and Financial Efficiency

Neither an economic nor financial analysis was conducted at appraisal.

Economic analysis was conducted at closure – based on the results of Components 1 & 2 – but it provided no estimates of economic rate of return for the project as a whole, but did estimate a partial NPV for component 2 only. Looking to cost-effectiveness, however, the matching grants program, which was responsible for generating much of the economic activity and job creation benefits of the project, had an operational cost (18 percent) that compared extremely favorably with similar programs in other countries (e.g. Kenya: 57 percent, Argentina: 36 percent, Indonesia: 47 percent), indicating relatively good value for money. For Component 1, which supported reforms to improve the business environment, the ICR makes an attempt to quantify the returns to investment by each beneficiary municipality. Results indicate that the cost per new license or permit issued varied between US$7 to US$13 in five beneficiary municipalities – suggesting reasonably efficient use of project resources (though for two others, located in poorer regions, the cost was significantly higher – reflecting the fact that the business environment was only one of many constraints in attracting investment to the poorer regions). Overall, the project's results were achieved while remaining well within budget.

Administrative and Organizational Efficiency

The project experienced delays in implementation that necessitated a one-year extension in time frame, and corresponding delays in disbursement of funds. A one-year delay in implementing amendments to the Commercial Code resulted from procurement and government-approval issues. A 20-month delay in start-up of the matching grants component, took place on account of disagreements with the Government on whether to place the component within MIFIC or *Banco Produzcamos*. These delays were largely avoidable and not indicative of a high degree of organizational efficiency. On the positive side, the diligence of the implementation team (supported by the Bank team) resulted in the achievement of most of the targets within the extension

period.

On the basis of these factors, efficiency is rated as **substantial**.

a. If available, enter the Economic Rate of Return (ERR)/Financial Rate of Return (FRR) at appraisal and the re-estimated value at evaluation:

	Rate Available?	Point Value	Coverage/Scope*
Appraisal	No		
ICR estimate	No		

* Refers to percent of total project cost for which ERR/FRR was calculated.

6. Outcome:

The project's objectives are rated as being highly relevant, and design is rated substantially relevant. Efficacy is rated high for each of the project's objectives, and efficiency is rated substantial. On this basis, overall outcome is considered to be satisfactory.

a. Outcome Rating: Satisfactory

7. Rationale for Risk to Development Outcome Rating:

The risk to development outcome is judged to be relatively low.

Technical: The skills enhancement training and capacity-building made available to beneficiaries under the matching grants program could be expected to have a long-term impact in terms of productivity and competitiveness gains, and opportunities to access finance. Similarly, the risk that reforms of the business environment, which have had a generally positive impact on investment and job creation, would be reversed seems low, except possibly in remote areas, where beneficiaries may lack the funds to maintain and operate equipment.

Political/Institutional: The policies introduced by the Government to support streamlined investment procedures and improve the general climate for investment retain the support of the current administration. The Commercial Registry set up an in-house IT team to maintain the equipment provided under the project, and conduct software updates on a regular basis. The One-Stop Shop for Investment is currently operating and is facing an increased demand in terms of number of applications. The Intellectual Property Registry (RPI) has seen an increase in number of applications, and an express desk has been created to process (usually MSME) trademark and patent registration applications. The Government has introduced an RPI training plan to raise further awareness among MSMEs to protect their intellectual property rights.

a. Risk to Development Outcome Rating: Negligible to Low

8. Assessment of Bank Performance:

a. Quality at entry:

Project design built on previous Bank operations in Nicaragua - such as the Competitiveness Learning and Innovation project (2006), analysis, including enterprise surveys of firms, the Municipal Scorecard Study of 2008, and annual Doing Business reports on business environment constraints. The lessons of these activities (and of similar Bank activities in other countries) were incorporated into the design. The project was designed after extensive consultations with the private sector and other stakeholders. To determine which groups had been marginalized in the development of the country's private sector, a social assessment was conducted to highlight the importance of women, African descendants and indigenous groups. The pilot Partial Credit Risk Guarantee scheme (though later cancelled) was designed after consultation with the financial sector to determine the likelihood of commercial banks participating in the program. Incentives built

into the design to promote bank participation were based on lessons of past PCRG schemes in Nicaragua, emerging market experiences with PCRG in Chile and elsewhere, and the Bank's experience with PCRG schemes for MSMEs in India, Madagascar and Ghana. Guiding principles for the PCRG were based on international best practice, including steps to minimize moral hazard and financial risk, establishing ex-ante eligibility criteria for financial institutions' participation, and establishing a "stop-loss" mechanism to prematurely terminate a poorly-performing program. Monitoring and evaluation arrangements put in place were fairly detailed in their tracking of project activities and intended results.

Quality-at-Entry Rating: Satisfactory

b. Quality of supervision:

The Bank team appears to have been reasonably diligent in supervision of the project. The Borrower's report emphasizes that the project was properly monitored, with three supervision missions per year on average being conducted. The Bank team maintained a regular and proactive dialogue with government counterparts. The Bank team contributed significantly to the success to the matching grants program by ensuring the preparation of an Operational Manual for implementing the program and providing the methodology of for monitoring the Business Improvement Plans approved. Bank staff were also very responsive to changing circumstances during implementation of the project, for instance in the cancellation of the PCRG component and its funding. As mentioned in Section 10(c), the team was similarly responsive to adjusting project activities to include support to the Intellectual Property Registry so as to improve access for MSMEs.

The Bank team appears to have provided adequate support to the Government to comply with fiduciary and safeguards requirements – e.g. through provision of training on procurement forms. Financial management support was also satisfactory, with support and guidance being provided to the government, as needed.

Quality of Supervision Rating: Satisfactory

Overall Bank Performance Rating: Satisfactory

9. Assessment of Borrower Performance:

a. Government Performance:

Implementation suffered from governmental processes and decision-making that could (and should) have been smoother. These include for instance (a) a one-year delay in project effectiveness that arose from governmental policy requiring National Assembly approval, (b) a decision mid-stream to move responsibility for half the project (Component 2 and part of Component 4) from MIFIC to MEFCCA, which was somewhat disruptive, (c) a decision by the Government to change – midstream - the structure of the committees in charge of amendments to the Commercial Code, which proved to be quite disruptive, and (d) a series of legal and institutional changes that gave rise to a conflict of interest between *Financiera Nicaraguense de Inversiones* (FNI), the lead institution responsible for implementing the Partial Credit Risk Guarantee (PCRG), and other commercial banks. This, together with the introduction in 2009 of Law 663 of the System of Societies of Reciprocal Guarantees for MSMEs, creating a legal environment that was incompatible with the proposed operation of the PCRG, led eventually to the cancellation of that project component.

Government Performance Rating Moderately Satisfactory

b. Implementing Agency Performance:

Coordination with the two key ministries responsible for implementing the project, MIFIC and MEFCCA, and the different agencies, institutions and municipalities involved was generally satisfactory. The Ministry of Finance too was supportive of the project's objectives. The Project Implementation Unit (PIU) and implementing agencies were committed to the project and generally performed well, particularly given their lack of experience with World Bank projects. They were able to conduct extensive stakeholder consultations as well as to coordinate parallel donor efforts in complementary areas. They also coordinated well between

the 14 different governmental agencies and municipalities involved in implementation of Component 1, and to resolve implementation issues in a timely manner. Monitoring of project activities and results indicators was conducted satisfactorily. Financial management was generally sound, although the PIU failed to monitor the US$/SDR exchange rate, and the loss of US$1.1 million of project resources that occurred over the project's life with the result that planned activities and procurement were misaligned with the resources available (though the subsequent cancellation of one component provided some flexibility to mitigate the situation). Procurement performance was satisfactory, notwithstanding some delay on account of the learning curve in dealing with Bank procedures. Due diligence on safeguards was satisfactory, the PIU making efforts to extend the project benefits to indigenous minorities and women through the formulation and implementation of an Indigenous Peoples Plan.

Implementing Agency Performance Rating : Satisfactory

Overall Borrower Performance Rating : Moderately Satisfactory

10. M&E Design, Implementation, & Utilization:

a. M&E Design:

Monitoring indicators and targets were for the most part adequate to measure the achievement of the project's developmental objectives. The objectives were clearly specified (notwithstanding the lack of a sufficiently high-level indicator for the matching grants component), and the indicators adequately reflected desired outcomes. Indicators were quantitative and relatively easily measurable. Data sources for monitoring the indicators were clearly identified (these included surveys of beneficiary firms and "exit polls" of registrants with the property registry), and an evaluation timetable was included for assessing the matching grants component.

b. M&E Implementation:

The PIU and project team closely monitored regular data reports, conducting surveys and on-site visits of beneficiaries (to collect data), where appropriate. Some real-time adjustment of activities in Component 1 was made on the basis of such feedback received. Although two indicators were included in the M&E framework in order to track the times required to obtain a trademark and a patent, the project team went beyond these to track additional data, so as to obtain a more comprehensive picture of the access of MSMEs to intellectual property rights.

c. M&E Utilization:

Feedback from monitoring and evaluation played a role in helping corrective action on activities be taken on a timely basis. For instance, when a majority of recipients reported that the lack of trademarks and patents, and the cumbersome process of obtaining them, was constraining the potential growth of their businesses, the project team was able to adjust activities to include support to the Intellectual Property Registry specifically targeted to improving access for MSMEs.

While routine data collection was handled by the PIU, an external consultant was utilized to conduct an in-depth evaluation of all three rounds of the matching grants component. Arrangements to collect additional data through surveys and on-site visits were also put in place by the PIU. These were helpful in allowing modifications to be made in the design and eligibility conditions of the matching grants program, for instance, to improve MSME targeting and maintain the relevance of the scheme.

M&E Quality Rating: High

11. Other Issues

a. Safeguards:

The project, which was classified Category 'B' under OP/BP4.01 Environmental Assessment, and OP/BP 4.10

Indigenous Peoples safeguard policy was triggered. An Indigenous People's Plan was formulated and implemented. Government counterparts were committed also to establishing local safeguard criteria to prevent any adverse environmental effects of the project. Towards this end a Negative List of activities was developed for the matching grants facility, as well as the Partial Credit Risk Guarantee, to ensure that activities under these components had a neutral or positive environmental impact. An effort was made, for instance, to include women, minorities and indigenous peoples among project beneficiaries in Components 1 and 2. Outreach communications were translated into indigenous languages. An Environmental and Social Management Framework was formulated and implemented for Component 2. Worker health and safety were also addressed under the project at both firm level and policy level (the former through various improvement plans for beneficiary firms in Component 2; the latter through the drafting of manuals and guidelines for good practices, specifically targeted to MSMEs).

b. Fiduciary Compliance:

Financial Management
The PIU's financial management and procurement arrangements were adequate and improved over time, as familiarity with the Bank's procedures increased. Supervision consistently rated FM issues in the Satisfactory/Moderately Satisfactory range. Some financial management (FM) issues were reported, including lack of internal control mechanisms and late submission of the external audit for 2011-12. Audit recommendations were however all addressed by project close. The ICR does not report on the extent to which financial covenants were complied with.

Procurement
Very few contracts were to be procured under the project, which did not experience procurement problems; although contract management was affected by institutional capacity constraints. According to the Task Team Leader, some implementation delays did arise on account of procurement-related issues, mostly due to lack of experience in defining specifications and estimating costs. However, the Bank worked with the project team on these issues, which resulted in a marked improvement in implementation during last two years of the project.

c. Unintended Impacts (positive or negative):

d. Other:

12. Ratings:	ICR	IEG Review	Reason for Disagreement/Comments
Outcome:	Satisfactory	Satisfactory	
Risk to Development Outcome:	Negligible to Low	Negligible to Low	
Bank Performance:	Satisfactory	Satisfactory	
Borrower Performance:	Satisfactory	Moderately Satisfactory	Government performance was moderately satisfactory because of delays in implementation of the project arising from slow procedures and/or decision-making.
Quality of ICR:		Satisfactory	

NOTES:
- When insufficient information is provided by the Bank for IEG to arrive at a clear rating, IEG will downgrade the relevant ratings as warranted beginning July 1, 2006.
- The "Reason for Disagreement/Comments" column could cross-reference other sections of the ICR

Review, as appropriate.

13. Lessons:

The ICR drew seven lessons, the most important of which (with editing) is:

Success in implementation of matching grants programs , especially for Micro, Small and Medium Enterprises, calls for significant hand-holding at the application stage. Grant applicants need assistance to identify relevant and practicable training appropriate to their business needs. After grants are awarded, close monitoring of the implementation of such programs, including on-site visits to beneficiary firms, is essential to enable early detection of problems and their mitigation.

14. Assessment Recommended? ○ Yes ● No

15. Comments on Quality of ICR:

The ICR is well-written, concise and generally consistent with guidelines. The quality of the analysis and evidence is results-driven and satisfactory overall. The ICR could however have contained some more information on fiduciary compliance. Secondly, the planned date for effectiveness has been incorrectly stated in the ICR Project Data Sheet (see Key Dates), which suggests that planned and actual effectiveness dates were identical, notwithstanding the one-year delay that took place. Finally, the lessons drawn could have been somewhat wider in their application.

a.Quality of ICR Rating: Satisfactory