ICR Review

Operations Evaluation Department

Report Number: ICRR11433

1. Project Data:		Date Posted: 03/27/2003		
PROJ ID:	P008561		Appraisal	Actual
Project Name:	First Private Sector Development Project	Project Costs (US$M)	49	38.4
Country:	Moldova	Loan/Credit (US$M)	35	32
Sector(s):	Board: PSD - Other industry (85%), Banking (6%), Central government administration (6%), Payment systems securities clearance and settleme (3%)	Cofinancing (US$M)	7	5.6
L/C Number:	L3977			
		Board Approval (FY)		96
Partners involved:	Government of the Netherlands	Closing Date	07/31/2001	06/30/2002

Prepared by:	Reviewed by:	Group Manager:	Group:
Elliott Hurwitz	Laurie Effron	Kyle Peters	OEDCR

2. Project Objectives and Components

a. Objectives

The principal objective of the project was to support and accelerate the Government reform program in the enterprise and financial sectors, focusing especially on strengthening the banking system and on delivering finance to support development of private and privatized enterprises. Specifically, the project was designed to: (a) accelerate emergence and growth of small- and medium-scale enterprises (SMEs); (b) streamline larger enterprises and release underutilized assets into the market; and (c) increase efficiency of resource mobilization and credit allocation by providing assistance to restructure the banking system, strengthen banking infrastructure, and provide institutional development support for solvent banks. The genesis of the project originated in a survey of enterprise demand for credit and establishment of a State Creditor's Committee to oversee the creditor-led adjustment program.

b. Components

1. **Enterprise sector strengthening component**: Support enterprise adjustment by providing post-privatization assistance through a new enterprise assistance agency, ARIA, to selected large enterprises; the incentive for loss-making enterprises to seek assistance was the potential, under a restructuring law, that they would be liquidated if they did not attempt to upgrade their operations. The loan also financed automation of the Tax Administration in the Ministry of Finance (MOF). 2. **Financial sector strengthening component**: Provided resources, through qualified participating banks, for medium-term loans to private and privatized enterprises. This component also assisted in development of banking skills in the PFIs, the automation of the National Bank of Moldova, and the further development of the payments system. A grant from the government of the Netherlands in the amount of US$ 5.6 million also provided training for participating banks in lending practices, developing SMEs as customers, and upgrading management information systems.

c. Comments on Project Cost, Financing and Dates

Overall project cost was US$38.4 million, compared to the appraisal estimate of US$49 million. During the course of the project, US$6.3 million was reallocated from other project components to the enterprise restructuring component. The project was financed by 2 loans for an original amount of US$35 million, of which $32 million was disbursed (with the difference mainly accounted for by exchange rate fluctuations). The difference between the anticipated overall project cost and the actual was due to (a) exchange rate fluctuations, and (b) smaller contributions from the Borrower and the private sector than envisioned. The project closed on June, 2002, one year later than envisioned.

3. Achievement of Relevant Objectives:

1. **Enterprise sector strengthening**: ARIA provided restructuring services to 93 firms; 63 were actually restructured, 19 entered but did not complete the program; and 11 went through bankruptcy (3 were reorganized and 8 liquidated). A survey of 430 companies showed that the 91 firms which received assistance from ARIA from 1995 to 2000 experienced a 16% increase in sales per employee, compared with a 13.4% decrease among the 339 firms surveyed

which did not receive assistance. The survey also showed that the share of the country's total exports by firms receiving assistance rose from 4% to 18.2% during the period.

In addition, ARIA provided advisory assistance to 480 SMEs, of which 80 were spin-offs from restructured larger firms, and 370 were start-ups located in 7 enterprise incubators in industrial parks (30 were in other categories). The services provided to the SMEs included management training, business planning, and market research. Also, the automated tax collection and fiscal management program financed by the project --which utilized application software financed by other sources--was fully operational by project close.

2. **Financial sector strengthening component** : The project financed 107 sub-projects directly and an additional 57 projects from the revolving fund, with loans averaging US$ 336,000. On a national basis, lending to the enterprise sector went from an average term of 3-6 months, with interest rates of 18-30% per year, to an average term of 32 months with an interest rate of 15.4%.
Subproject viability was very good, with a repayment rate at project close of 98%.

Eight banks met project eligibility requirements and benefited by (1) improving their operations to become eligible to participate; (2) gaining experience in credit and risk appraisal. As noted above, they also received training (under the Dutch grant) in SME lending practices, implementation of loan analysis, and also upgraded their management information systems.

Finally, the project also provided systems to upgrade the internal processes of the NBM.

4. Significant Outcomes/Impacts:

- The project demonstrated that there was substantial demand for enterprise advisory services and willingness on the part of firms to pay for them
- ARIA trained more than 400 local consultants in enterprise diagnostics and restructuring techniques (compared to an original project goal of 200), and disseminated its knowledge through seminars, workshops, and mass media
- Approximately 40 consulting firms have developed that employ consultants trained by ARIA
- Participating banks strengthened their capacity to appraise loans and do business with SMEs
- Based on the success of this project, a second PSD project was undertaken (PSD II), and the Borrower has indicated interested in a potential PSD III project

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

- ARIA's institutional and legal status was not firmly established by project close, which made its future vulnerable to changes in government policy
- The Government transferred the technical unit established with the NBM to the MoF, contrary to the recommendation of the Bank
- Procurement problems led to the cancellation of the effort to upgrade the banking sector payments clearing system

6. Ratings:	ICR	OED Review	Reason for Disagreement /Comments
Outcome:	Satisfactory	Satisfactory	
Institutional Dev.:	High	High	
Sustainability:	Likely	Likely	
Bank Performance:	Satisfactory	Satisfactory	
Borrower Perf.:	Satisfactory	Satisfactory	
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:

- The model of the Bank as a "knowledge broker" proved effective. This involved the horizontal dissemination of learning, rather than the contrasting role of the Bank as a "knowledge storehouse"
- The process of creditor-led restructuring, with a special agency available to provide expert assistance, can provide significant gains in the efficiency of the firms involved
- There is substantial demand for enterprise restructuring services, and beneficiary firms are willing to pay for these services (during the project, ARIA's fees covered around 30-50% of its costs)

8. Assessment Recommended? ● Yes ○ No

Why? The project presented a potentially innovative and successful approach to enterprise restructuring which could well have applicability elsewhere. An audit for this project is scheduled for completion in FY 05.

9. Comments on Quality of ICR:

The ICR is exemplary. The evidence and data presented to substantiate arguments and ratings are substantial and

compelling;
a significant effort was made during the project to monitor its impact . The Lessons Learned are insightful . The ICR might have provided a better explanation of how 7 banks were eligible to participate, given that the country's banking system was severely undercapitalized .