ICRR 10849
Report Number : ICRR10849

ICR Review
Operations Evaluation Department

1. Project Data: Date Posted : 05/08/2001

PROJ ID : P064853		Appraisal	Actual
Project Name : Private Sector Adjustment Loan	Project Costs US$M) (US$M)	303.7	303.7
Country : Romania	Loan/ US$M) Loan /Credit (US$M)	300	300
Sector (s): Financial Adjustment	Cofinancing US$M) (US$M)	3.7	3.7
L/C Number : L4489			
	Board Approval FY) (FY)		99
Partners involved : Trust Fund for Social Cost Mitigation	Closing Date	03/31/2000	06/30/2000

Prepared by : Reviewed by : Group Manager : Group :

2. Project Objectives and Components

a. Objectives

The two tranche loan provided immediate balance of payments finance and supported reforms, begun under the earlier unsuccessful FESAL, in the enterprise, financial, and social sectors . In the enterprise sector , the reforms were to (a) accelerate privatization of state owned enterprises (SOE), (b) enforce hard budget constraints on remaining SOEs and close big loss makers (e.g. mines), and (c) implement an action plan to stimulate private sector development and streamline the business environment . In the financial sector , the objective was to (d) strengthen the banking system, (e) restructure state banks as a prerequisite for their privatization, (f) improve central bank regulations, and (g) further develop the government securities market . In the social sector, the aim was to (h) create income support programs for displaced workers, (i) ensure adequate budget support is available for this purpose, (j) improve employment services for displaced workers, (k) strengthen social assistance programs for long - term unemployed and poor, and (l) inform the general public and affected workers about the rationale for the reform and about the government's mitigating support .

b. Components

The reform measures that were conditions for tranche release are listed below .

In the enterprise sector , the specific conditions were to (1) complete contracts with acceptable international investment banks for the privatization of at least 3 of the 4 identified firms (Sidex, Alrom, Alprom, Tarom);

(2) select 5 additional large firms for privatization and appoint investment banks to handle their sale; (3) select 5 large SOEs for workout or liquidation and appoint liquidators; (4) conclude contracts with agents to sell at least 30 large SOEs in pools; (5) privatize at least 15 large SOEs and 600 small and medium sized SOEs which together amount to 5% of the State Ownership Fund's total assets; (6) sell the State Ownership Fund's residual shares in at least 160 firms; (7) liquidate or stop the operations of firms that account for at least 12% of the losses in State Ownership Fund; and (8) reduce the operating losses by 25% in the 6 mining companies; and have contracts for closing and environmental mitigation work for at least 10 mines.

Improvements in the business environment were to: (1) complete a study on the regulation of electricity, telecom, railways and oil & gas and appoint advisors to prepare a privatization strategy for electric generation and distribution; (2) enact laws to improve security interests in personal property; and (3) submit amendments to the corporate and personal income tax laws.

In the financial sector , state owned banks were to be restructured, a necessary step to their later privatization, prudential oversight was to be improved and the government securities market developed . Specific conditions were to (1) have a plan, appoint a privatization advisor, and complete a due diligence report on the loan portfolio of Banca Comercialia Romania; (2) have a plan and appoint a privatization advisor for Banca Agricola (BA) and have the Asset Resolution Agency take over at least half BA's non -performing assets; (3) take irreversible measures to liquidate Bancorex; and (4) list specific measures to improve banking supervision and bad loan provisioning and of the Asset Resolution Agency's staff and advisors .

Social sector conditions were to: (1) enact the Framework Law on Collective Dismissals; (2) finance Unemployment Fund shortfalls; (3) report to the Bank on unemployment levels, benefits & cash flow forecasts for the Unemployment Fund; (4) enact laws to accredit NGOs to administer micro -credits; and (5) analyze the number and level of social assistance benefits and a plan to improve delivery .

c. Comments on Project Cost, Financing and Dates

3. Achievement of Relevant Objectives:

The conditions were fulfilled, and the second tranche was released less than a year after the first . Many of the objectives have been achieved (e.g. privatization and the reduction of the fiscal drain through loss - making SOEs), others (e.g. protecting creditor interests in property) require sustained implementation and more time is needed to assess their attainment.

Enterprise privatization was difficult, but the numerous conditions were met . The privatization of the steel company, Sidex, was dropped because of misprocurement of the investment bank arranging its sale; but is planned to be sold under the planned PSAL2. Experience from other transition countries shows that enterprise workouts are

difficult,
but losses appear to have declined and many unprofitable mines closed . Fourteen contracts for the technical closure
and environmental work of mining companies have been concluded .
The improvements in the business climate focused on passing laws and planing the future privatization of utilities .
The ICR refers to the plans but does not elaborate on what is in them or them how they are being implemented .
Bank privatization and liquidation are similarly difficult . The tranche release conditions stop short of closure or sale;
so although the necessary steps are being taken, the outcomes are still unclear . The improvements in the
supervisory capacity of the central bank is as yet untested . The problem loans have been lodged in the asset
recovery unit and the ICR mentions delays in appointing staff and managers which suggests that difficult tasks still lie
ahead.
The mitigation of social costs was largely to make worker entitlements more needs -based and affordable to the
government. The Unemployment Fund "borrowed" from the Finance Ministry to meet the tranche conditions, but this
is not sustainable. The ICR mentions that a planned Social Sector Development Loan will incorporate the findings of
the GOR report that was a loan condition . The ICR does not comment on the effectiveness of the microcredit
scheme for displaced workers or the content of the "communications strategy that was implemented ."

4. Significant Outcomes/Impacts:

The loan's significant achievement was to reduce the large losses of SOEs . Plugging this fiscal drain appears was
important both for structural reform and macro -economic stabilization. The outcomes are, however, vulnerable to
reversals because the conduit to the banking system remains (and the region warns that "there is evidence of direct
overdraft assistance").

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

6. Ratings :

	ICR	OED Review	Reason for Disagreement /Comments
Outcome :	Satisfactory	Satisfactory	
Institutional Dev .:	High	Substantial	The central bank's supervision dept ., the main permanent government entity supported by the loan, is yet untested .
Sustainability :	Likely	Likely	
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:

8. Assessment Recommended? Yes No

Why? The earlier FESAL that attempted many of the same reforms was rated unsatisfactory . An audit of
both the FESAL and PSAL would show what the government and the Bank may have learnt from the experience .

The decline in enterprise losses is welcome; but the indicators are vulnerable to poor accounting and a closer look at
these issues may be warranted .

9. Comments on Quality of ICR:

Satisfactory. It would have been helpful if the ICR provided data on the reduction of SOE losses . It could have also
specified the details of the social safety net and whether training displaced workers was effective, especially since
the loan document expected some 200,000 workers (10% of the labor force) to be adversely effected .