IDA14

Strengthening the Private Sector in IDA Countries: Status of World Bank Group Collaboration

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Acronyms

ADB	Asian Development Bank
APL	Adaptable Program Loan
BAPA	Bangladesh Agro-Processor's Association
BDS	Business Development Services
BEI	Bangladesh Enterprise Institute
BMO	Business Membership Organization
BOAD	Banque Ouest Africaine de Développement
CAS	Country Assistance Strategy
CGAP	Consultative Group to Assist the Poorest
CPIA	Country Policy and Institutional Assessment
EBRD	European Bank for Reconstruction and Development
EIB	European Investment Bank
FDI	Foreign Direct Investment
FIAS	Foreign Investment Advisory Service
FMO	Netherlands Development Finance Company
GEF	Global Environment Facility
GOC	Government of Cameroon
ICA	Investment Climate Assessment
IDA	International Development Association
IDB	Inter-American Development Bank
IFC	International Finance Corporation
IFU	Industrialization Fund for Developing Countries
IMS	Investment Marketing Services
IPA	Investment Promotion Agency
IPP	Independent Power Producer/Project
LAC	Latin America and the Caribbean
MFI	Microfinance Institution
MIGA	Multilateral Investment Guarantee Agency
MPDF	Mekong Project Development Facility
MSME	Micro, Small and Medium Enterprise
NGO	Non-Governmental Organization
OBA	Output-Based Aid
OECD	Organization for Economic Cooperation and Development
PDF	Project Development Facility
PEP	Private Enterprise Partnership
PPIAF	Public-Private Infrastructure Advisory Facility
PRG	Partial Risk Guarantee
PSD	Private Sector Development
SEDF	South Asian Enterprise Development Facility
SEED	Southern Europe Enterprises Development
SME	Small and Medium Enterprise
TA	Technical Assistance
WB	World Bank
WBG	World Bank Group

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Status of World Bank Group Collaboration

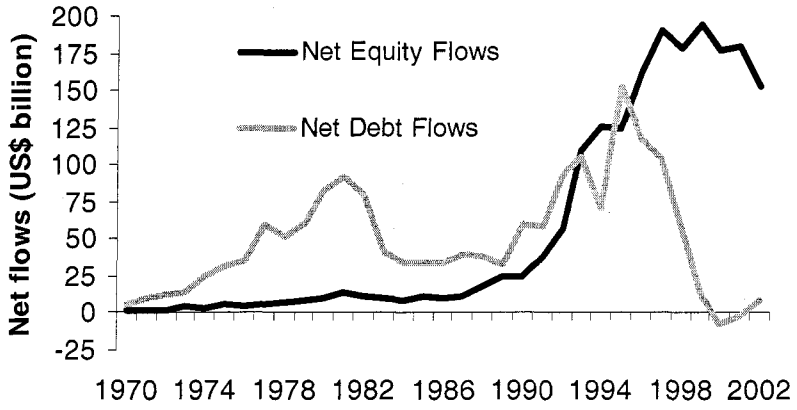
I. Introduction

1. At the IDA14 Replenishment meeting in Washington D.C. in October 2004, Deputies welcomed the increased attention being paid to the private sector development in IDA countries. They requested an update on the World Bank Group's (WBG) efforts to strengthen collaboration among its organizational units.[1] This paper responds to that request.

II. Context

2. A trend towards private sector solutions and new forms of risk sharing is clearly visible in the world and shapes the context in which IDA operates. *First*, following the debt crisis of the 1980s across developing countries, there has been a gradual shift away from debt finance to other types of finance that share risks in more appropriate ways, such as equity instruments. The trend is epitomized by the fact that FDI has become the prominent form of cross-border finance to developing countries (Figure 1).

Figure 1: Financial Flows to Developing Countries by Type



Source: Global Development Finance

3. *Second*, finance to emerging markets has shifted from government borrowing to borrowing by the private sector. Not only is the private sector by far the greatest provider of finance, it is now also the greatest recipient – with roughly double the amount of finance going to private firms compared to public ones (Figure 2).

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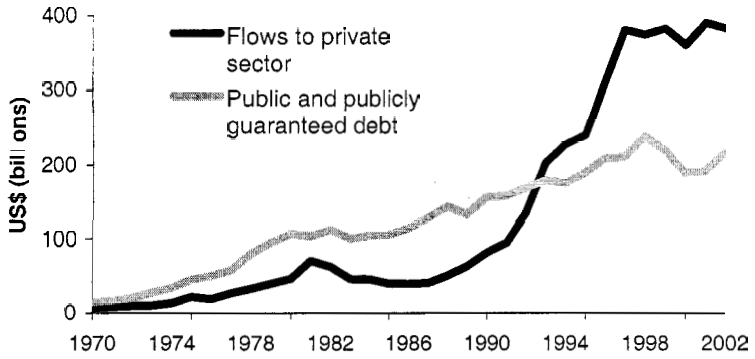
[1] A companion paper *"Strengthening the Private Sector in IDA Countries: World Bank Group's Collaboration with External Partners (November 2004),"* discusses the ongoing efforts to strengthen and improve collaboration with external partners.

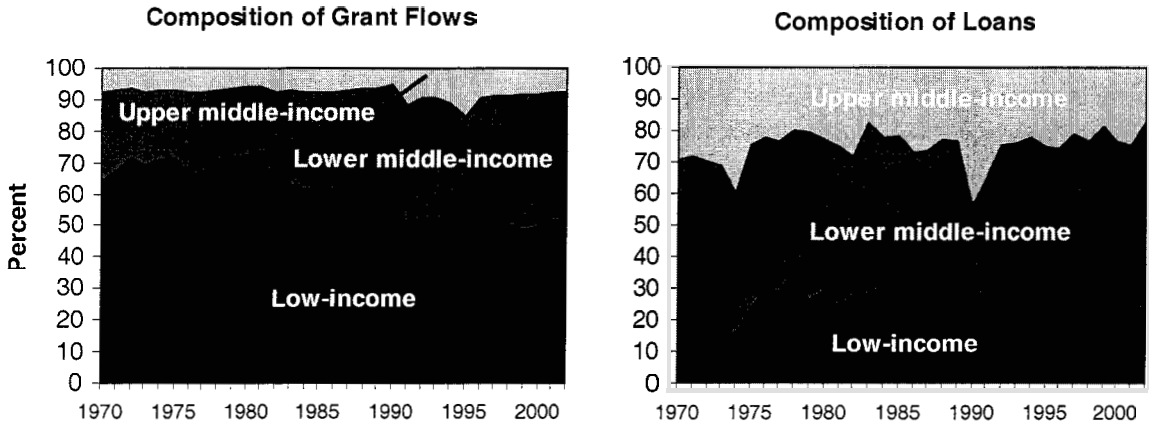
Figure 2: Financial Flows to Developing Countries by Recipient



Note: Private sector flows include nonguaranteed debt, grants by non-governmental organisations, and worker's remittances, plus portfolio equity and direct investment, which are reported net.

4. *Third*, an effort has been made to help the poorest and most indebted countries to position themselves better. Debt relief has been provided and grant programs have been introduced including by IDA. Nevertheless, for now the broad trends towards private finance have largely passed most IDA countries by. They continue to depend on government finance and FDI is often driven by natural resource exploitation rather than more broad-based economic development (Figure 3).

Figure 3: Composition of Flows to Low-Income vs. Middle-Income Countries



Source: OECD Development Assistance Committee

5. Given this context, a number of development institutions have moved or are moving to deal better with the financing approach to private sector development. Various institutions are now offering a broader range of instruments for private clients including guarantees, loans without sovereign counter-guarantee and equity instruments. The European Commission has taken this route with funds often administered by the European Investment Bank (EIB). The new crop of development institutions that emerged in the last two decades tends to focus or at least

have the capability to provide this range of instruments. The European Bank for Reconstruction and Development (EBRD) is a clear-cut case. Others such as the Netherlands Development Finance Company (FMO) and the Industrialization Fund for Developing Countries (IFU) also provide such forms of finance. All the major multilaterals are also pursuing the basic agenda, including Asian Development Bank (ADB) and Inter-American Development Bank (IDB).

III. WBG Collaboration in IDA Countries

III A. The Experience So Far

6. There are three key efforts of collaboration between IDA, IFC, and MIGA. They include: (i) joint work on the investment climate; (ii) joint approaches to new public-private partnerships in infrastructure; and (iii) joint work on Small and Medium Enterprises (SME) support in Africa. These are discussed below.

Investment Climate

7. The goal for the work on the investment climate is to create a reasonably seamless working relationship among all parts of the WBG that deal with reforming the business environment. This involves principally the Bank and IFC regions (including the regional SME facilities) as well as central programs (including Foreign Investment Advisory Services (FIAS) and Multilateral Investment Guarantee Agency's (MIGA) investor marketing service, which are now coordinated under a collaboration protocol).[2]

8. The targeted division of labor is as follows. Central groups like "Doing Business" as well as other staff from the Private Sector Development (PSD) Vice-Presidency work on diagnostic tools, collection of best practice examples, provision of training and relevant analytical pieces that underpin country-specific policy advice/technical assistance. When countries need advice but do not want to borrow, WBG can now deliver freestanding advisory services by combining managers or experts from headquarter teams with staff on the ground, mostly in the SME facilities. Where countries want to borrow either in the form of policy-based lending or technical assistance loans, Bank staff manages those loans drawing on expertise from advisory teams. The precise composition of teams depends country-by-country on availability of relevant staff across the WBG and funding sources that match the particular goals of the assignment.

9. Examples of such collaboration now exist in all regions drawing on all parts of the WBG. The following examples provide a sense of the various collaboration options that are being pursued:

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[2] MIGA's Investment Marketing Services (IMS) department provides tailored advice and capacity-building assistance to developing country investment promotion agencies. FIAS and MIGA work closely to provide a comprehensive package of investment promotion assistance to governments and investment promotion agencies (IPAs). In 2004 FIAS and MIGA, in collaboration with the Commonwealth Secretariat, designed a nine month capacity-building program for IPAs from all 14 member countries of the Pacific Islands Forum Secretariat. In 2002, FIAS and MIGA assisted the Board of Investment in Bangladesh in developing a strategy for investment promotion.

- **Bangladesh**. To carry out the Bangladesh ICA, the World Bank partnered with the Bangladesh Enterprise Institute (BEI) and the South Asian Enterprise Development Facility (SEDF), one of IFC's regional facilities serving SMEs. The ICA reform agenda identified an urgent need for infrastructure reform (especially in electricity), for addressing pervasive corruption and over-regulation, and for improving access to finance, each of which disproportionately burdened SMEs. With the Bank and BEI as partners, SEDF monitored the follow-up to the ICA agenda with a semi-annual panel survey of SMEs. It partnered with an industry association, Bangladesh Agro-Processor's Association (BAPA), to study and work for the reduction of the tax burden on agro-processors. At the request of the Ministry of Commerce, it identified measures to streamline business registration and is providing technical assistance to implement them and to automate the registry of joint stock companies.

- **Kenya**. Following the completion of a FIAS Administrative Barriers study in July 2004, the World Bank incorporated FIAS analysis and recommendations in its economic and sector work and further in its private sector development policy dialogue with the Government. Subsequently, the Bank/IDA and IFC jointly designed the Kenya SME project, which was approved by the IDA Board in July 2004. This project includes reforms in such areas as speeding up the legal and institutional changes to ease business entry and licensing, SME tax simplification; and initiatives to promote increased SME access to finance.

- **Other Examples**. Annex 1 contains other examples from Bolivia, Lesotho, Serbia, and Zambia.

Private-Public Partnerships

10. Collaboration between IDA, IFC and MIGA can help private and public sector players to improve access to better physical and social infrastructure. On the one hand, better management discipline can be brought into these sectors via the introduction of private commercial arrangements. On the other hand, private investors still shy away from some of the risks that surround, for example, infrastructure projects in Africa. Successful schemes tend to involve a blend of public and private funding combined with private management, preferably with adequate exposure to commercial risks so as to provide incentives to perform. Output-based aid (OBA) schemes hold promise, as do schemes that involve small or medium-sized domestic service providers (or combinations thereof).

11. In some cases IDA funds may support the enabling environment or regulatory reform to develop an infrastructure sector and IFC and/or MIGA help finance an infrastructure investment as a private investment. In other cases, IDA supports a private sector infrastructure investment that is also supported by IFC and/or MIGA. Since IDA funds are highly concessional, IDA support is only used in special instances where such subsidized financing is appropriate, for instance: (i) to provide critical technical assistance and advice to help create viable projects, e.g., through supporting regulatory reform; (ii) to extend critical infrastructure access to poor or underserved populations; and (iii) to deal with short term political issues of infrastructure pricing, e.g., phasing in commercial user fees.

12. Examples of WBG collaboration in public-private partnerships include the following:

- **IDA-IFC**

  - **Tajikistan**. IFC's innovative Pamir project will generate and supply electricity under a 25-year concession, taking control of the assets of the state utility and expanding generation capacity through rehabilitation of existing plant, transmission and distribution assets. In addition, the project will provide tariff subsidy mechanisms to ensure basic provision of electricity to the poorest, supported by IDA investment and a grant from the Government of Switzerland. IFC is a lender to and equity investor in the Pamir project.

  - **Côte d'Ivoire**. IDA and IFC and other multilateral and bilateral agencies helped finance the US$223 million Azito Power Project, including a 300MW gas-fired power station and a 225 kV transmission line. An IDA partial risk guarantee covering sovereign and political risks was considered a crucial credit enhancement to secure commercial bank financing. IFC and IDA were able to leverage their respective institutional strengths for the benefit of the client country. Both institutions collaborated closely in terms of project appraisal, sector issues as well as syndication strategy.

  - **Ghana**. In Ghana, IDA and IFC have joined efforts to provide a package of advice and financing to help the Government reform the power sector and unblock much needed investments. IFC has received Board approval to optimize the capital structure and finance the conversion of a crude oil fired Independent Power Producer (IPP) (Takoradi II) into a combined-cycle operation, thereby increasing electricity supply without additional fuel consumption. This, together with the IDA-supported reform program, could help to reduce tariffs in Ghana. The joint IDA-IFC team is helping the government to implement a private management contract for the state-owned electricity distribution company and IDA expects to make financing available for much needed capital investments in the distribution network. IDA and MIGA are also contemplating providing support to the West African Gas Pipeline, which would bring natural gas from Nigeria to Ghana and which would enable the Takoradi Power station to switch fuel sources from crude oil to natural gas.

  - **Other Examples**. Annex 2 contains additional examples from Senegal and Cameroon.

- **IDA/IFC- MIGA**. Three other projects of note have involved MIGA and other members of the WBG:

  - **Mozambique**. In 2004, IDA, MIGA and IFC combined WBG Instruments (i.e. an IBRD enclave guarantee, MIGA guarantees and IFC equity investment) to facilitate the mobilization of critical private capital as well as commercial debt financing required for the implementation of a Sasol oil and gas project, consisting of the

development of Mozambique's natural gas industry and export facilities to South Africa. In addition, IFC is helping the Government of Mozambique broaden the participation of local investors and raise financing to cover the shortfall in Mozambican participation in the project. Over the past two fiscal years MIGA has provided a total of US$186 million worth of guarantees for the equity investment and debt financing for the project. Since this is the first large scale privately-financed energy export project in the gas sub-sector, it provides a framework for other future private sector projects and would facilitate further investments in gas exploration and other gas related industries.

- **West Africa Economic and Monetary Union**. In 2004, the joint MIGA and IDA Boards approved a MIGA-IDA guarantee facility in support of small and medium infrastructure projects in the countries of the West Africa Economic and Monetary Union. Banque Ouest Africaine de Développement (BOAD) acts as an intermediary for the new facility. The Agence Française de Développement is a co-guarantor in the project and has provided funding for the secondement of a MIGA staff member to BOAD to assist the institution with the implementation of this program and the development of BOAD capacity.

- **Afghanistan**. In its efforts to enhance its support of conflict-affected countries, MIGA also worked to establish a guarantee facility for Afghanistan, with funding provided by IDA and the Asian Development Bank. The facility is expected to be launched in early FY05.

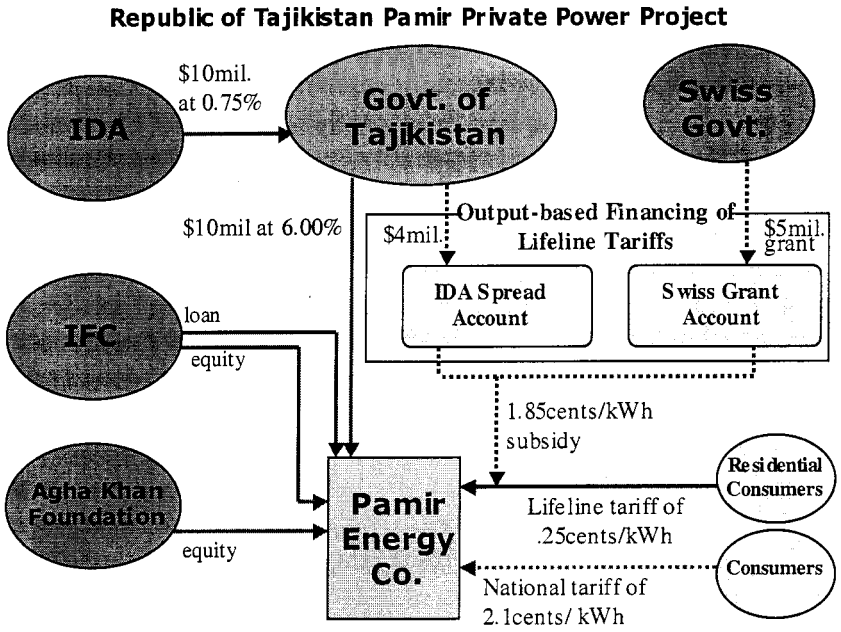
- **Output-based aid (OBA)**. OBA is a core design strategy for supporting private sector projects that aims at ensuring that subsidies reach intended beneficiaries while enabling efficient private sector participation with commercial risk-taking. An example is the delivery of basic services where policy concerns justify public funding to *complement* or *replace* user fees, e.g., to enhance affordability for particular groups of consumers. The heart of the OBA approach is the contracting out of service delivery to a third party – usually private companies but also NGOs – under arrangements that link payments to the results actually delivered. This approach can provide a sharper focus on objectives, improve efficiency and innovation, enhance accountability for the use of public resources and create opportunities for mobilizing private finance and know-how. The World Bank is scaling up the use of OBA and this is a key component of the New Infrastructure Agenda. Currently, over 30 OBA projects, most of which are in IDA countries, are under preparation or implementation. Some of the Public-Private Partnership initiatives involving IFC and IDA have utilized OBA concepts. For example (additional output-based aid examples are in Annex 3):

  - The **Pamir** project in Tajikistan, mentioned earlier, uses OBA concepts in provision of lifeline tariffs for the poor. As shown in Figure 4 below, subsidized IDA finance flows to the government, which on-lends to the power producing company at a higher interest rate. The differential funds an IDA Spread Account, which along with funds from the Swiss Government, is used to finance a lifeline tariff for residential consumers. In this way, part of the subsidy embedded in the IDA credit is unbundled

and used to fund poor users, if and when the private sector performs. In the case of non-performance, subsides are not paid out.

- A small-scale water/sanitation project in **Cambodia,** features IDA credit and grant funds to build partnerships with the private sector and user groups in financing, operating, and maintaining water/sanitation facilities. The projects require designing specific instruments that ensure inclusion of low-income communities. OBA contracts are being awarded to local operators. IFC has supported this operation via the Mekong Project Development Facility (MPDF), one of the SME project development facilities. This example demonstrates that OBA schemes can be deployed to promote small-scale solutions using domestic providers, when this is the appropriate approach. Most of the Bank's OBA pilots work with small-scale providers.

Figure 4: OBA Lifeline Tariff in the Pamir Project



SME Programs in Africa

13. The joint program for SME support in Africa is meant to help create an enabling environment that allows SMEs to flourish and where the IFC can take credit risk without requiring a sovereign counter-guarantee. This should then demonstrate to other investors the possibilities to operate profitably in Africa and lead to greater private investment.

14. IDA funds are used primarily to provide technical assistance on the enabling environment, capacity building for SME support services, and training of financial institutions that may lend to SMEs or provide micro-finance services. IDA can also provide credit lines to banks for on-lending to SMEs. The IFC is to provide investments or guarantees without a sovereign counter guarantee. IDA and IFC are currently developing new combined products that

would strengthen the ability of IFC to provide incremental investments. By bringing commercial approaches to financing schemes involving IDA, commercial discipline is to be strengthened. In future new approaches, the concessional element of IDA financing could also be deployed so as to reward institutions that show sound performance e.g., by maintaining a high-quality portfolio. Examples have been developed under the auspices of the Consultative Group to Assist the Poorest (CGAP, Box 1). These are the financial sector incarnation of output-based aid (also found in EBRD).

Box 1: CGAP Approach to Awarding Subsidies Based on Performance

CGAP is a consortium of 29 bilateral and multilateral donors who support microfinance. With a team of microfinance specialists housed in the World Bank, CGAP serves the microfinance industry, donors and microfinance institutions (MFIs) through the three categories of services provided: technical tools and services, training and capacity building, and technical advice and exchange. CGAP also has a small grant facility that provides funding for these activities and for strategic investments in MFIs. A large part of CGAP's mission is to promote "best practice," especially in the way donors support MFIs. Using its grant fund, CGAP has developed an investment-style approach to grant making that ties tranched funding to institutional performance. The key focus is on the achievement of financial performance measures that will enable the MFI to reach sustainability and thus a significant number of poor clients.

The performance contract that accompanies CGAP's equity-like funding leaves the use of funds entirely at the discretion of management; reporting, monitoring, and continuation of disbursements are tied to the MFI's fulfillment of performance thresholds at the institutional level. These thresholds are designed to lead the microfinance institution to "full financial sustainability," the ability to cover all costs including the commercial cost of funds. They generally step up over time and include indicators such as profitability, efficiency (cost per dollar lent), portfolio quality, and growth (numbers of clients reached). Because most of a microfinance institution's funding is usually soft, achievement of full financial sustainability implies that it will generate substantial surpluses that will be retained to fund yet more services to poor clients.

15. Some examples of the current IDA-SME projects in Africa include:

- **Nigeria**. Approved in December 2003, IDA funds will be used to: (i) provide technical assistance to financial institutions in order to create new specialized institutions and to help existing ones develop new products tailored to Micro, Small and Medium Enterprises (MSMEs) and increase their internal capacity; (ii) bring the expertise required to reduce the cost of business registration, improve the legislative framework for leasing and secured transactions, and establish a credit bureau and a movable collateral registry; (iii) increase the competitiveness of firms in specific industries and provide technical assistance to training/consulting service providers to develop new products and expand; and (iv) build the capacity of key public institutions in charge of SMEs. IFC will target investments in MSME financing institutions, leveraging IDA technical assistance funding (ACCION, approved in Sept. 2004, is the first of such investments).

- **Ghana**. The project, earmarked for roughly US$47 million, will: (i) increase MSME access to medium-term finance and to sustainable microfinance services through SME

loan portfolio partial guarantees, an SME risk capital fund, and strengthening and extending the outreach of MFIs; (ii) promote the competitiveness of selected industries, including enhancing linkages and know-how transfer between large businesses and SMEs and working within high potential value chains and focused training in competitive subsectors; (iii) promote a conducive business environment through reducing the time and cost of business registration and licensing, policy work on leasing and credit bureaus, developing the capacity of Business Membership Organizations (BMOs), and reforming the national system of technical regulations for certification and standardization; and (iv) strengthen the institutional capacity of Government through working with the policy unit of the Ministry of Private Sector Development and the SME Directorate of the Ministry of Trade, and supporting the localization of an SME information platform.

- **Mali**. The Mali Sources of Growth project is scheduled for Board discussion in December 2004. The approximately US$12 million SME component of this US$55 million project which also includes telecommunications and postal reform and mining sector reform, will: (i) provide support to improve the investment climate by (a) streamlining the registration process in terms of cost and time involved in business start-up operations, (b) developing procedures to streamline the corporate taxation process, and (c) improving commercial dispute resolution and arbitration mechanisms; (ii) improve Business Development Services by (a) developing a mechanism to strengthen the capacity of service providers to serve MSME clients and address market needs more appropriately, using various BDS tools including an establishment of a Consultant Accreditation Program of local consultants, business associations, and financial institutions, and (b) setting up an electronic information system (SME Toolkit) that will provide information on BDS services, access to finance, the investment climate, fiscal issues pertaining to MSMEs, tools on best practices in business, as well as other issues that concern small businesses. The access to the finance component will provide technical assistance to support institutional developments intended to increase the availability of term finance and other specialized products suitable for SMEs. This will include the development of a stand-by liquidity facility, an IFC Trade Enhancement facility and a Partial Guarantee product.

- **Additional examples**. Additional examples for Kenya, Madagascar, and Uganda are in Annex 4.

III B. Problems Being Solved Under Current Collaboration Mechanisms

16. The examples presented above of various WBG interactions indicate that a great deal is underway to leverage the resources and tools to address development needs of the private sector in IDA countries. Much has been learned from these undertakings regarding how to effectively leverage the various resources of the WBG. From this base of experience, a number of issues have been identified that have, to various extents, hindered the coordination of the institutions. In some cases, this led to missed opportunities, delays in project development, and difficulties bringing projects to implementation. These are discussed below.

Culture

17. Because PSD is a crosscutting theme, implementing WBG programs in IDA countries requires unusual levels of collaboration and coordination within the Group, including the IFC, MIGA, Bank regional vice-presidencies, multiple disciplines and networks within the Bank, as well as several specialized facilities, including FIAS and the SME Project Development Facilities (PDFs). Challenges remain in better tapping all the resources in the WBG. However, collaboration is improving, and a number of channels have been developed to further enhance it. Good and regular communication has proven the key to effective collaboration and tends to overcome the "culture" differences between different parts of the group in almost all cases. A description of some of the enhanced communication channels developed was provided in the earlier IDA paper "Strengthening the Private Sector in IDA Countries."[3]

Procedures

18. In many cases of WBG collaboration in Public Private Partnerships and MSME development, projects involve government entities (e.g., regulatory bodies, ministries) and private sector entities (e.g., for service delivery). The government may initiate various types of procurement to select the private service provider and WBG members may at some point in the process be involved with both parties. Thus, two issues become important: (i) the procurement process must meet high standards of transparency and fairness; and (ii) the selection process must avoid any potential or appearance of conflict of interest. At the same time, because these projects involve private sector business, the procedures developed must allow for quick decisions to be made. The WBG has developed processes to manage these issues:

- For *procurement*, where IDA funds are used, IDA procurement rules are followed. At times, the government procurement processes were traditionally too slow for effective private sector participation, particularly in the case of private financial institutions bidding to become part of IDA-IFC MSME on-lending and TA programs. However, progress is being made in overcoming this problem through better use of flexible IDA procurement features (e.g., sole sourcing, fast track, and pre-qualification options) that are already allowed for but have not been practiced in ways conducive to private sector participation.

- To prevent any possibility of *conflict of interest*, rules are employed that have become well established for a number of different Bank-IFC operations, such as the joint Bank/IFC investment departments in telecommunications and oil, gas and mining.

Scaling up output-based aid

19. The first wave of output-based aid projects are now under implementation and initial results are encouraging. A sample of 14 IDA projects in different sectors (from the universe of over 30 OBA projects currently under implementation) estimated that they improve service delivery of infrastructure services to a total of 18.6 million people. If successful, scaling up of OBA operations in the Bank could lead to a significant increase in the allocation of IDA

[3] "Strengthening the Private Sector in IDA Countries," IDA/SecM2004-0653, September 27, 2004, Box 8, p. 18.

resources to the provision of infrastructure services to the poor. There is also likely to be a continued growth in use of joint Bank Group support for OBA projects, as was pioneered in the Pamir project. The Bank is also managing a trust fund, the Global Partnership for Output-Based Aid (GPOBA), which is helping in the design and evaluation of OBA schemes and disseminating knowledge on OBA. The WBG will undertake a review of OBA to draw lessons learned from these pilot experiences early during the IDA14 period. This will allow learning from experience and a scaling up of the successful practices identified at the pilot stage.

Supporting the private sector with IDA Guarantees

20. IDA partial risk guarantees are important for supporting the private sector in client countries.[4] Introduced in 1997, the guarantees enable member countries to attract private investment and international commercial financing particularly for infrastructure projects. The IDA guarantee program is currently limited to Partial Risk Guarantees (PRGs). Through this instrument, IDA provides a guarantee for lenders to private investment projects against debt service defaults that result from nonperformance of government obligations. These guarantees are intended as an instrument of last resort to help fill financing gaps in cases where IBRD exposure could not be increased and neither MIGA nor IFC could provide sufficient support and lenders would only be prepared to participate with an IDA guarantee of sovereign risks.

21. However, the policy of treating IDA guarantees as equivalent to credits in terms of their draw on commitment authority and country allocations has been identified as one of the factors leading to relatively limited demand for the guarantee product. To lower these disincentives, on March 30, 2004, the Executive Directors approved an amendment to the IDA Guarantee Pilot Program that reduces the "cost" of the guarantee by lowering the backing of new guarantees from 100 percent to 25 percent.[5] Under the new policy, the assistance envelope for a given country as established in the CAS would be increased by 75 percent of the face value of IDA guarantees included in that country's lending program.

IV. Summing Up and Possible New Directions

22. As discussed in Section III, during IDA13, several efforts were made to improve collaboration among WBG institutions with a view to creating a more integrated approach to deploy the various instruments of the Group. As discussed above, key collaborative efforts revolve around the following: (i) improving diagnostic underpinnings through Investment Climate Assessments, Doing Business reports, as well as other analytical pieces and policy advice; (ii) forging public-private partnerships to improve access to better physical and social infrastructure, and partnering with the private sector through innovative OBA approaches; and (iii) creating joint programs for SME support in Africa.

23. While much has been learned to date from the WBG undertakings regarding how to effectively leverage the various resources, a number of challenges have been identified. Some are being resolved under current collaboration mechanisms. For instance, good and regular communication has proven key to effective collaboration and helps overcome the "culture"

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4 Also see the background note to IDA Deputies entitled, *"IDA Guarantees Pilot Program, (November 2004)."*

5 "IDA Guarantees Amendments to Pilot Program," March 17, 2004. IDA/R2004-0057.

difference between different parts of the Group. Progress has been made in efficient implementation of appropriate procurement and conflict of interest procedures. Initial assessments indicate that OBA projects show promise and efforts are underway to scale up these activities. Finally, a new method for counting IDA guarantees against country allocations has been implemented and should encourage their use.

24. Going forward, as experience grows, the WBG will take stock of its collaborative efforts to promote private sector development. Of special interest in IDA countries are the projects based on the innovative OBA approach that help extend infrastructure and social services to the poor in an affordable manner. The Group will conduct a comprehensive review of OBA-based projects, and as lessons are distilled, ways of scaling up the projects will be explored. The findings of the review of OBA-based projects will be shared with the Deputies at the mid-term review.

25. Moreover, extension of the concept of regional IDA operations[6] to include private sector implementing entities might be another important way to improve the efficacy of WBG support to the private sector. Cross regional programs could be important for infrastructure projects. Additionally, the IDA-IFC MSME programs often have features that would enhance their viability if done on a regional basis, particularly because financing intermediaries and related support institutions often operate in several countries, where scale economies make operation in only one country uneconomic. In the context of the review of the regional pilot program (expected to be shared with Deputies at the mid-term review), IDA will explore ways to increase private sector involvement in regional projects.

26. Also looking ahead, comprehensive reviews of OBA projects and the IDA-IFC Africa MSME pilot program in Africa could focus on (among other things) whether lack of Government capacity in client countries to participate in OBA and other private sector schemes have led to missed opportunities to harness private enterprise. If this is the case, then an important issue to be explored is whether IDA should lend directly to the private sector without sovereign counter-guarantee when promising operations are constrained by lack of capacity in the public sector to respond in a timely manner.

27. However, with respect to lending without sovereign guarantees, IDA would be faced with a number of critical financial and risk management challenges. Taking on private sector credit exposures would change the very nature of IDA in a substantial manner. The advantages and disadvantages of lending directly to the private sector would have to be weighed carefully. The WBG intends to look into this and a detailed analysis will be provided to the Board of Executive Directors and the Deputies around the time of the mid-term review.

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[6] A pilot program for regional projects was started during IDA13 period.

Annex 1: Additional Examples of Collaboration Among WBG Members on Investment Climate Reform in IDA Countries

Latin America

Bolivia. Following the findings of a World Bank investment climate assessment in Bolivia, the IFC LAC facility teamed with FUNDES, an NGO, to streamline the procedures for registering a business in the city of La Paz. The project achieved a dramatic streamlining of business licensing and registration procedures:

- Increased number of registered businesses by 20 percent
- Reduced average required visits to complete registration from 6 to 2
- Increased transparency in municipal administration
- Designed support software for business registration and authorization procedures (www.ci-lapaz.gov.bo)
- Created new infrastructure for customer service

Africa

Lesotho. FIAS did an administrative barriers study in 1997, which was not acted upon because of political instability and elections. In 2003, the new reformist government informed the Bank that it was willing to move on reform in general and a private sector strategy in particular. The administrative barriers study findings were adopted as part of the reform mix, and the government indicated a willingness to act on licensing and business registration issues. The Bank (and government) asked FIAS to provide technical assistance for the design of a licensing and business registration reform, with the intention of having a subsequent Bank private sector development project finance the implementation. FIAS has provided the technical assistance, and the Bank is now preparing the project.

Zambia. FIAS carried out an administrative barriers study in 2003. A joint ARCS/Investment Climate Assessment survey was designed by FIAS and the Africa World Bank private sector department, and was carried out by the World Bank and local consultants. The recommendations of the administrative barriers study were incorporated by government into a private sector development reform plan, whose implementation is being supported by the Bank initially through a component of an existing Bank project, then a new enterprise development project (approved by the Board in mid-2004).

Eastern Europe and Central Asia

Serbia. FIAS supported an administrative barriers study in 2003/2004 that was carried out primarily by a local institute, using a self-assessment methodology. Work on inspections was carried out jointly by the institute and SEED (Southern Europe Enterprises Development), a facility of IFC. SEED published its own report of this work, and the findings and

recommendations were incorporated in the final administrative barriers report prepared by the Institute. The Institute also made use of the findings of a business survey that it conducted on behalf of the Bank as a component of the Bank's Investment Climate Assessment study. FIAS and the Bank's private sector department have maintained close contacts as the administrative barriers and Investment Climate Assessment were carried out at the same time, and because the Bank has financed the preparation of a regulatory impact assessment tool that FIAS proposed to be used within the implementation of the administrative barriers study recommendations.

Annex 2: Additional Examples of Collaboration Among WBG Members on Public-Private Partnerships in IDA Countries

Senegal. In Senegal, the IFC organized trust funds and commissioned a study to assess the investment requirements of the electricity sector. Based on the results of this study and preliminary market soundings, IFC and IDA advised the government to invite the private sector to develop an Independent Power Project (IPP). IFC contacted a number of potential international bidders for the IPP, while IDA arranged trust funds for advisors to help the government with the bidding process, and supported the government in assessing and monitoring private sector participation in the project. Two international companies submitted bids for the project and contract negotiations with the preferred bidder are at an advanced stage. It is expected that a combination of IFC, IDA, and other development institutions (potentially including MIGA) will provide financing support to the project.

Cameroon. In 2001 IFC advised the Government of Cameroon (GOC) on the privatization of Sonel, the integrated national electric utility, which also benefited from strong support from IDA. Over the last two years IFC and IDA have been working in close cooperation in Cameroon to help address the critical needs of the electricity sector. IFC is leading a syndicate of Development Financial Institutions made up of the European Investment Bank, Proparco, African Development Bank, Deutsche Investitions-und Entwicklungsgesellschaft mbH (DEG) and IFC that is considering a financing to the private concessionaire, AES Sonel, for its post-privatization capital expenditure program. IDA is helping the Government of Cameroon to: (i) strengthen power sector institutions; (ii) develop a generation expansion plan in the country; and (iii) develop and finance a 150-200MW gas-fired plant.

ANNEX 3: Additional Examples of Output-Based Aid

(IDA Countries)

AFRICA REGION (AFR)					
Country	**Sector**	**Bank Project Name**	**Project Description**	**OBA Component**	**Project Status**
CAPE VERDE	Transport	Road Sector Support Project (P087004)	Project's objectives are to improve access roads linking villages and rural areas to main roads and improving island networks.	Performance maintenance and rehabilitation component, building on Chad experience.	Bank Pipeline: Approval 01/2005 GPOBA funding 03/2004 for feasibility .
CHAD	Transport	National Transport Program Support Project (P035672)	Main objective of US$67 million credit is to improve year-round access to markets and services through a more efficient transport system and better transport services. These development objectives are also those of the National Transport Program, which is financed only in part by the project (roughly 25 percent), and in part by other donors and the Government. Possible follow-on project being developed.	An OBA-type US$11.5 million contract started in July 2001 covering the management, maintenance and rehabilitation during 4 years of 440 km of the main east-west highway. True risk to private sector of OBA payments is limited, but pilots seen as good starting point for further risk balance in future regional projects. The pilot project is generally considered to be successful. The Bank funds 80 percent of the total contract amount of this pilot contract. Possible follow-on project being developed.	Bank Active: Effectiveness 03/2001 GPOBA funding 03/2004 for possible additional roads .
DRC	Health	Emergency Multisector Rehabilitation and Reconstruction Project (P057296)	The project consists of a US$44 million grant covering health sector and US$410 million credit covering other areas. Specific project objectives are (a) rebuilding agricultural production, (b) rehabilitate and reconstruct critical infrastructure, (c) restore essential social services, and (d) strengthen capacity of government regarding development programs.	8 contracts are signed in April 2003.with NGO to support 67 Health Zones (8 million people). Contracts include performance-based payments that would award those performing particularly well in delivering health services to the poor.	Bank Active: Effectiveness 11/2002. GPOBA Pipeline GPOBA for funding to support designing, implementing and supervising such a system.

ANNEX 3: Additional Examples of Output-Based Aid

(IDA Countries)

MADAGASCAR	Transport	Transport Infrastructure Investment Project (P082806)	The major development objectives of the US$150 million project are to rehabilitate the country's major transport infrastructure and facilitate trade. The APL is divided into three phases, with the first focusing on essential reforms and highest priority investments.	Performance maintenance and rehabilitation component, building on Chad experience.	Bank Pipeline: Approval 07/2005 GPOBA funding 03/2004 for feasibility.
MALAWI	Multisector	Rural Infrastructure Services (P057761)	The project is aimed at expanding access to and improving the quality of infrastructure services (telecommunications, electricity and water) in selected districts in Malawi.	OBA components are still being designed, but it is expected that they will be based around connection expansion subsidies, particularly for telecommunications and electricity.	Bank Pipeline: Approval 07/2005 GPOBA Pipeline.
MOZAMBIQUE	Electricity	Energy Reform and Access Project (P069183)	Objectives of IDA Credit US$40 million are to increase access to modern electricity services in urban and peri-urban areas. The objectives are to be accomplished through a combination of reforms for improved industry performance and investments in electricity supply infrastructure.	Connection subsidies for small-scale providers; the first phase of this APL, includes about five rural concessions, for the first of which, in Northern Inhambane. The project aims to provide connections to 5,000 households within five years; up to 15,000 additional connections are to financed under the other concessions. Concession for Northern Inhambane awarded, to start operations by May 2004.	Bank Active: Effectiveness 03/2004 GPOBA funding 06/2003 for design of subsidy fund flows.
MOZAMBIQUE	Telecom	Mozambique Communication Sector Reform Project (P073479)	The objective of the US$14.9 million credit is to improve access to and quality of efficient and affordable communications services by creating an enabling environment for competition and private participation in sectors deemed critical to facilitate national and regional market integration, i.e., telecommunications, postal and air transport infrastructure and services.	The OBA component is estimated at US$3 million. The approach to be used is the negative concession for provision of payphone and possibly Internet services in rural areas, under selected pilots.	Bank Active: Effectiveness 06/2002 Design of bidding documents under preparation. Tender expected in 2005.

ANNEX 3: Additional Examples of Output-Based Aid

(IDA Countries)

NIGERIA	Telecom	Privatization Support Project (P070293)	US$114.29 million credit attempts to support transparent and effective implementation of the Federal Government of Nigeria's privatization program through expanded private investment and improved efficiency in the productive sectors, and in infrastructure. Also aims to create an enabling environment for PSP and competition in infrastructure services, notably in telecommunications and electric power.	Negative concessions for rural areas have been agreed by government as part of a rural telecommunication access strategy; consulting assignment for the design of pilot projects under way; WB funding (up to US$ 4 million) is provided for pilot projects; Design of pilot projects finalized, identification of additional funding sources under way.	Bank Active: Effectiveness 11/2001
RWANDA	Health	Poverty Reduction Support Credit 1 (P085192)	The US$80 million PRSC I, II and III will support the Government of Rwanda's policies for reducing poverty as outlined in the PRSP published in 2002. The key objective of the PRSP is to reduce poverty by supporting policies that lead to rural development and investment in infrastructure, enhanced human development, and support to transparent governance and public sector management.	PRSC will be supporting the expansion of pilot performance based contracting schemes. The specifics have not yet been agreed upon.	Bank Pipeline: 01/2005 GPOBA Pipeline
SENEGAL	Electricity	Electricity Project (P073477)	The proposed US$100 million IDA APL program will support the delivery of quality electricity services in SENELEC areas and will promote private sector participation the country's electricity sector.	Details being developed. OBA rural connection scheme, possibly under a minimum subsidy concession approach for up to 18 concession areas.	Bank Pipeline: Approval 07/2004
TANZANIA	Transport	Transport Sector Project APL (P055120)	Objectives are to remove constraints to transport services on road network and to strengthen the management and implementation capacity of TANROADS.	Performance maintenance and rehabilitation component, building on Chad experience.	Bank Pipeline: Approval 07/2005 GPOBA funding 03/2004 for feasibility.

ANNEX 3: Additional Examples of Output-Based Aid

(IDA Countries)

UGANDA	Telecom	Energy for Rural Transformation Project (P069996)	US$49.15 million credit and US$12.12 million GEF grant. Phase 1 will put in place a functioning conducive environment and commercially oriented, sustainable service delivery of rural/renewable energy and Information & Communication Technologies (ICTs). GEF objective is build in-country capacity for renewable energy.	Telecom component of US$5.5 million is aimed at implementing OBA schemes, as the telecom sector reform agenda was successfully implemented under a previous project. OBA scheme involves negative concessions for rural areas, including public telephone services, Internet Points of Presence and telecenters in each of 154 rural sub counties. Estimated subsidy requirement US$ 6 million, WB funding estimated of US$ 5 million. Drafting of tender documents to be finalized by early 2004. Pre-qualification announced in March 2004	Bank Active: Effectiveness 07/2002
UGANDA	Electricity	UG Fourth Power Project (P002984)	Project is being restructured to accommodate IDA financing to support declining subsidy associated with privatization of UEDC, a power distribution company.	Declining subsidy scheme to reduce tariff increases that would be required to bring tariffs up to cost covering levels. Private operators have been selected and negotiations have largely been completed: awaiting approval from boards of private operators.	Bank Active: Effectiveness 04/2002
EAST ASIA & PACIFIC REGION (EAP)					
Country	**Sector**	**Bank Project Name**	**Project Description**	**OBA Component**	**Project Status**
CAMBODIA	Water	Provincial and Peri-Urban Water and Sanitation Project (P073311)	The US$16.9 million credit and US$3.1 million grant aims to assist the country in moving forward to fulfill the MDGs in water supply and sanitation by 2015. The project design aims at building partnerships with the private sector and user groups in financing, operating, and maintaining constructed facilities, after designing specific instruments that ensure inclusion of low-income communities residing in the service areas.	Connection subsidies to small-scale providers under least subsidy concessions to establish small networks in 4-5 selected communities, subsidies being provided for about 40 percent of envisaged connections; OBA contracts already awarded to local operators in four provincial towns.	Bank Active: Effectiveness 11/2003 GPOBA funding 06/2003 for reviewing options for scaling up project.

ANNEX 3: Additional Examples of Output-Based Aid

(IDA Countries)

EUROPE & CENTRAL ASIA REGION (ECA)					
Country	**Sector**	**Bank Project Name**	**Project Description**	**OBA Component**	**Project Status**
GEORGIA	Telecom	Georgia Telecommunications Reform Project (P087143)	A small lending operation is being prepared which will include a US$3 million OBA component.	Project being developed based on the South Caucasus PPIAF grant. The OBA component will expand on the experiences gained through the pilot to most of the remaining provinces of Georgia.	Bank Pipeline: 01/2005
TAJIKISTAN	Electricity	Pamir Private Power Project (P075256)	The objective of the US$10 million IDA credit and US$8 million IFC loan is to improve reliability, and enhance the quality of electricity supply in the Gorno Badakshan Autonomous Oblast region, through private sector involvement, in a financially, environmentally, and socially sustainable manner. The project components shall include: 1) completion of the existing Pamir hydro plant 2) rehabilitation of several power plants 3) rehabilitation of transmission lines 4) technical assistance, and consulting services, to be financed by Pamir Energy and the IFC.	OBA subsidy to cover difference between lifeline tariff for domestic consumers and the costs of supply, totaling US$9-10 million annually.	Bank Active: Effectiveness 03/2003
LATIN AMERICA & CARRIBEAN REGION (LAC)					
Country	**Sector**	**Bank Project Name**	**Project Description**	**OBA Component**	**Project Status**
BOLIVIA	Electricity, Telecom	Decentralized Infrastructure for Rural Transformation (P073367)	The objectives of the US$20 million IDA credit are to expand and improve rural infrastructure access, specifically for solar home systems and mobile telecom services, with specific connection targets being developed.	The OBA components would focus on subsidies linked to the provision of approximately 20,000 new solar home systems in remote areas, which will be divided into lots to be offered to the private sector through competitive bidding. Similar projects on a smaller scale will take place in the telecom sector.	Bank Active: Effectiveness 12/2003 GPOBA funding 06/2003 for design of tendering process for solar home lot allocation.

ANNEX 3: Additional Examples of Output-Based Aid

(IDA Countries)

NICARAGUA	Electricity	Offgrid Rural Electrification (PERZA) (P073246)	The US$12 million IDA credit and US$4 million GEF grant aim to support the sustainable provision of electricity services and associated social and economic benefits in selected rural sites. This would be accomplished by (i) supporting the Government in the design and implementation of its national rural electrification strategy; (ii) implementing innovative public/private off-grid electricity delivery mechanisms in several pilot sites for later replication on a national scales; and (iii) demonstrating in the pilot areas the potential of targeted rural microfinance and business development services (BDS) to significantly enhance the development impact of rural electrification.	OBA solar home system connection scheme, and isolated systems for about 18,000 new connections in area outside of existing concessionaire's area (Union Fenosa). The national electrification fund (FODIEN) must be re-developed and made sustainable to manage OBA funds. Payments made for a combination of connections, continued maintenance, and training.	Bank Active: Effectiveness 11/2003 GPOBA funding 11/2003 for assisting with the development of electrification fund.
NICARAGUA	Telecom	Nicaragua - Telecommunication Reform (P055853)	US$15 million project, aimed at supporting the reform of the telecommunications sector, including new legal and regulatory framework, capacity building to the regulator, privatization of the incumbent, and an OBA component. The design, and operations of a rural telecommunications development fund will be supported, to provide incentives for private investments, thus improving the sector's services in those areas.	The OBA component is estimated at US$1 million. The approach to be used is the negative concession for provision of payphone and possibly Internet services in rural areas, under one selected pilot project. Based on this experience a US$10 million follow-up operation is being proposed to scale-up the experience gained through the pilot throughout Nicaragua. Regulatory instruments and tender documents ready. Exact location of the pilot under discussion. Tender to be launched in mid 2004.	Bank Active: Effectiveness 04/2000
MIDDLE EAST & NORTH AFRICA REGION (MNA)					
Country	**Sector**	**Bank Project Name**	**Project Description**	**OBA Component**	**Project Status**

SOUTH ASIA REGION (SAR)					
Country	**Sector**	**Bank Project Name**	**Project Description**	**OBA Component**	**Project Status**
BANGLADESH	Water, social services	Social Investment Program Project (P053578)	IDA credit to support the provision of basic services to selected districts in Bangladesh and to promote innovative approaches to meeting infrastructure needs through the local private (for-profit and not-for-profit) private sector.	OBA schemes for small scale water supply and social services; social assistance component of the project will develop an OBA scheme in two districts, where NGOs will be responsible for providing maternal and child health care and increasing immunization coverage. Partial-OBA small-scale water schemes being developed to feasibility stage.	Bank Active Effectiveness 04/2003
INDIA	Health	Rajasthan Health Systems Development Project (P050655)	US$89 loan with main objectives being to (a) increase access to health care services by the poor and (b) improve the quality of health care services through institutional development.	OBA scheme targeted with an existing network of NGOs working on family planning, reproductive health and communicable disease control and treatment.	Bank Approval 03/2004. OBA components being developed.
INDIA	Electricity	Rural Electricity Access Project (P083789)	US$50 million loan to demonstrate scalable sustainable institutional models for increasing access to electricity services in rural areas and to contribute to growth of rural incomes and improved delivery of social services through supply of electricity services to targeted rural areas.	Subsidy mechanisms still being designed but OBA approaches for piloting private sector provision are being considered.	Bank Pipeline: Approval 09/2005
NEPAL	Telecom	Telecommunications Sector Reform Project (P050671)	The objectives of the US$22.56 million IDA credit is to support telecommunications sector reforms to increase access by developing a competitive and liberalized market structure and enable the private provision of telecommunication infrastructure and services in rural areas.	Negative concession for rural service; license to provide telecommunications services in the Eastern Development Region. The operator has to provide at least two public access lines in each of 534 village development committees (VDC) and operate services in these VDCs for at least 10 years. License awarded to STM Telecom Sanchar Private Limited on November 21, 2003. The hub installation and commissioning will be completed in April 2004. Service roll out in all 534 VDCs will be completed by June 2005.	Bank Active Effectiveness 05/2002

Annex 4: Additional Examples of IDA-IFC MSME Programs in Africa

Kenya. The Kenya SME project was approved by the IDA Board in July 2004. The project supports the Government program to increase the competitiveness of MSMEs through mutually reinforcing components: (i) access to finance; (ii) strengthening enterprise skills and market linkages; and (iii) improving the business environment. The project aims to increase productivity and employment in participating MSMEs. This objective will be achieved by strengthening financial and non-financial markets to meet the demand of MSMEs, strengthening institutional support for employable skills and business management, and reducing critical investment climate constraints on MSMEs (reforms in such areas as speeding up the legal and institutional changes to ease business entry and licensing, SME tax simplification). The project will focus on key value chains and on both formal small and medium enterprises and informal microenterprises that have high potential for dynamic growth, including "graduation" from informal to formal status.

Madagascar. The Integrated Growth Poles Project is expected to be discussed at the Board in March/April 2005. This IDA program intends to act as a strong catalyst for very broad economic growth with three very focused geographical areas of Madagascar: Antananarivo/Antsirabe, Nosy Be and Fort Dauphin. The overall project includes the following components: transportation, roads, and port development; export processing zones; tourism/parks; telecommunications; investment climate; and MSME development.

The MSME component will consist of the three following sub-components, which may include the following activities (yet to be finalized, as pre-appraisals have not yet taken place):

- Access to Finance: development of a quasi-equity investment fund; Analyze and possibly establish new leasing company(ies); establish a greenfield MSME bank and/or strengthen the SME banking activities of existing financial institution(s); analyze the possibility of establishing risk mitigation facilities to promote lending/investments in Nosy Be and Fort Dauphin, and/or to MFIs.
- MSME Capacity Building: training - largely funded through matching grants, to develop new courses, increase market for existing courses, establish apprenticeship programs, and consider establishing training institutions; firm level consultancies - in key sectors within the poles, offer matching grants for essential consultancy services; developing value chains - hire a specialist in each pole to encourage business-to-business exchanges, to improve access to TA and to financing, in some cases perhaps establishing service companies (mass purchasing inputs, offering transport/storage facilities, etc.).
- Business Enabling Environment: computerize and improve access to existing pledge registry/moveable collateral systems; analyze the need to establish specialized repossession regulations, and perhaps a repossession agency, for leasing - and implement if needed; support GUIDE (SME registry & promotion) expansion; possibly support some expansion costs of SME support centre to Nosy Be and Fort Dauphin.

Uganda: Uganda Private Sector Competitiveness Project II, approved on September 2, 2004, aims to increase MSME creation and growth. The proposed Credit will help finance three mutually reinforcing components: (i) development of serviced industrial land and improvements in the provision of financial services; (ii) the improvement of enterprise capacity, particularly in MSMEs; and (iii) improvement to the business environment and land registry. In particular two components of the project will focus on MSME growth and creation. These will aim to improve enterprise capacity by increasing enterprise investment in skills (including investment in skills for women), and by raising productivity and improving the quality, standards, and reliability of MSME producers and export value chains. This objective will be achieved by scaling up the ongoing matching grant scheme implemented successfully under the first Private Sector Competitiveness Project. The scale up will focus on: (i) increasing the regional outreach of the scheme; (ii) improving technology; (iii) improving skills; (iv) improving financial management of MSMEs to enable access to finance; and (v) rolling out new financial products by financial institutions.