

A Look at Development Results by Project Size

Larger IFC investments tend to have higher development outcome success rates. This finding holds across IFC sectors, and highlights the challenges small projects face in the market place. Factors driving the development results of IFC's small investments are client management and product quality, but also IFC's own work quality.

Analyzing the development results of IFC's direct investments by investment size shows that IFC's larger investments have consistently yielded superior development outcomes. This analysis highlights results by size and looks at characteristics of successful investments to help understand these findings.

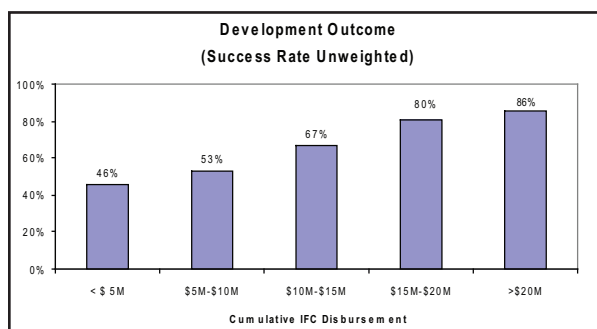
Notes on the analysis

We assessed all active IFC investments that were approved between 1998 and 2003, a total of 469 companies. These investments are generally sufficiently mature to be adequately evaluated. We analyzed information captured in IFC's Development Outcome Tracking System (DOTS), and Expanded Project Supervision Reports (XPSRs) validated by IFC's Independent Evaluation Group (IEG) for 57 larger investments that were evaluated between 2005 and 2006. This includes 49 2006 XPSRs, plus eight 2005 evaluations in cases where 2006 evaluations alone amounted to less than two for a given industry department.

Better Development Results with Larger Investments

Larger IFC investments have higher development outcome success rates. While only 46 percent of the companies with IFC total disbursements of less than US\$5 million achieved high development outcome ratings, 85 percent of the companies with disbursements higher than US\$20 million succeeded to do so (see figure 1). This pattern held true across industries (see figure 2). In-depth evaluations by IFC's Independent Evaluation Group (IEG) show similar results.

Figure 1:
Better development results with larger IFC investments



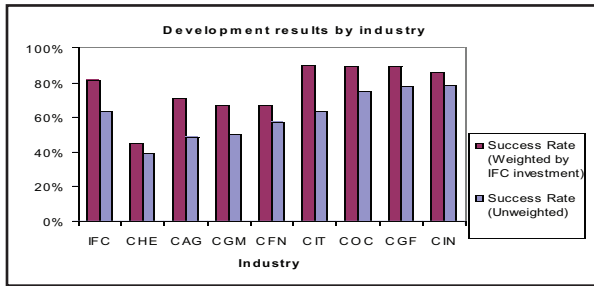
What makes a project a development success?

In order for IFC to consider a project a development success, it must:

- Be profitable (its financial return exceeds the average cost of capital),
- Generate benefits to society above and beyond those to its financiers (usually, the economic rate of return is expected to exceed ten percent), and
- Be socially and environmentally sustainable (meet or exceed our performance standards).

We also assess a project's broader private sector development impact (e.g. a project's demonstration effects.)

Figure 2:
All industries show better development results for larger investments



IFC industry departments

- CHE – Health and Education
- CAG – Agribusiness
- CGM – Global Manufacturing and Services
- CFN – Private Equity and Funds
- CIT – Information and Telecommunication
- COC – Oil, Gas, Mining, and Chemicals
- CGF – Global Financial Markets
- CIN – Infrastructure

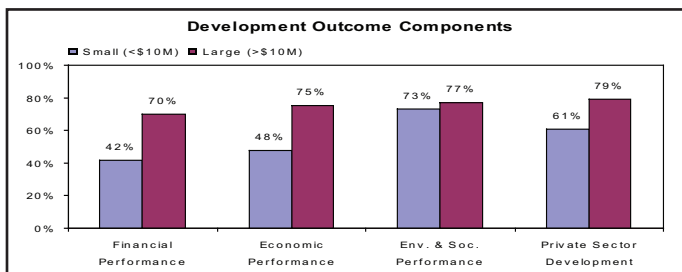
Why do larger projects have superior development results?

If larger IFC investments generate superior development results across the board, what are the drivers of this strong performance? What characterizes successful or unsuccessful operations of different sizes?

Financial and economic performance differentiate small projects most.

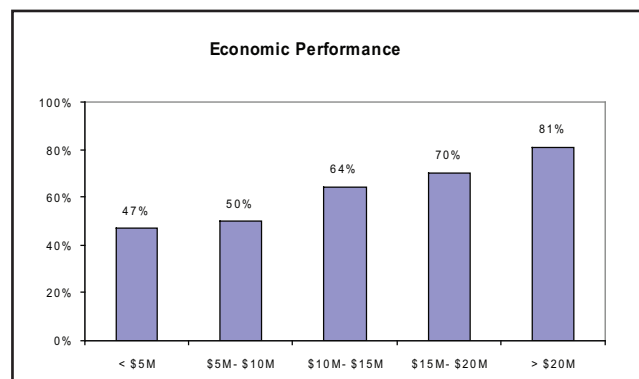
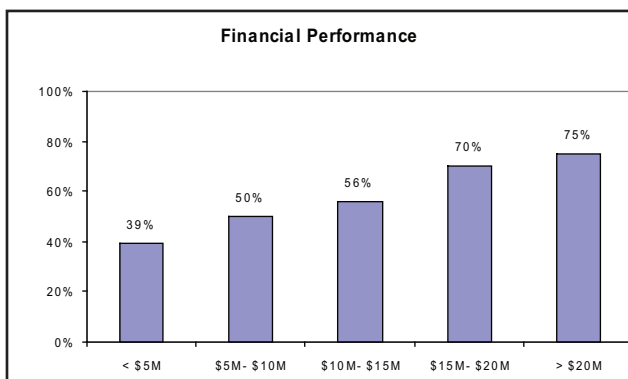
Weaker financial and economic performance appears to explain the relatively poorer development outcome success rates of small investments: investments below \$10 million achieved strong financial performance in only 42 percent of cases, whereas the same was true for 70 percent of investments larger than \$10 million.

Figure 3:
Development outcome by performance dimensions



Less than half of small projects are business successes. This performance pattern is consistent with the experience of the private sector in developed countries: For example, in the United States less than half (44%) of new establishments were still in existence four years later.

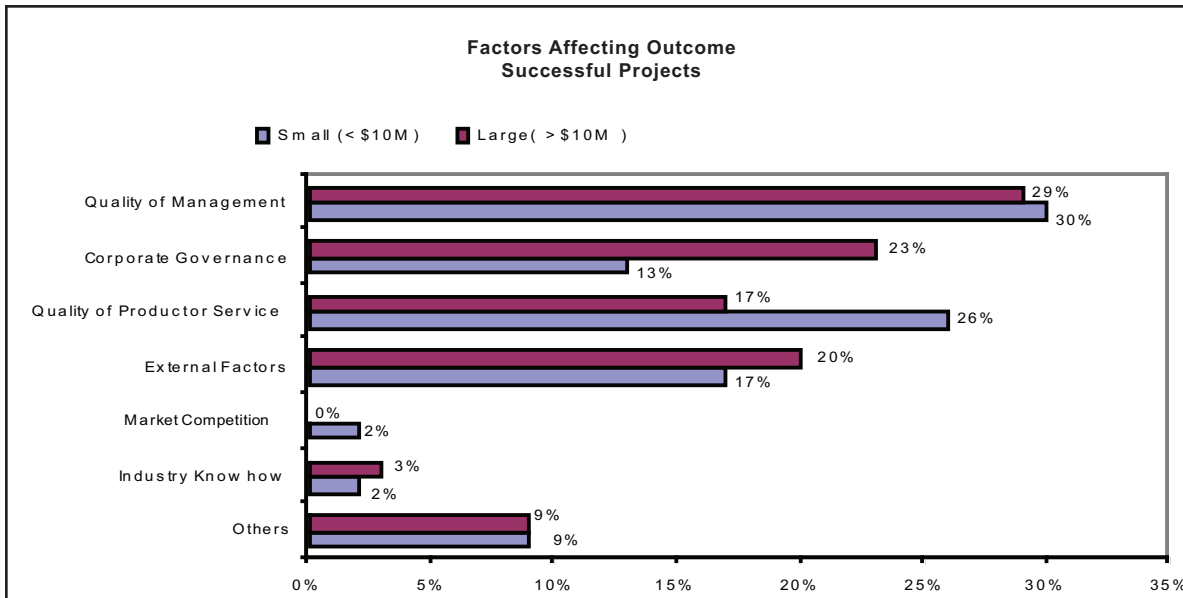
Figures 4 & 5:
Financial and economic performance are highly correlated with investment size



Drivers of success and failure

In-depth evaluations by IFC's Independent Evaluation Group (IEG) show that larger projects tend to have better corporate governance. High quality of management is crucial to success in both large and small projects. Smaller businesses are more vulnerable and seem to require both sound management and high quality products to survive competitive pressures.

Figure 6:
Large investments -quality of management and sound corporate governance are critical to success



Project example 1:

Management quality and sound corporate governance drive successful banking in Africa

After careful screening, IFC selected a local African bank among 89 potential candidates for investment, recognizing its management’s strong local knowledge, exemplary banking standards and sound corporate governance. IFC committed US\$ 20 million to the bank in the form of a credit line to lend on to private companies in various productive sectors,

a resource previously non-existent in the country. The bank’s recognized strengths contributed to establishing best practice standards and strengthening the country’s entire banking sector. IFC’s line of credit to the bank supported industries such as manufacturing and construction, and the bank has grown from 14 branches in 2000 to 78 branches in 2005.

Project example 2:

Management skill and sound corporate governance drive performance of flour mill in the Middle East

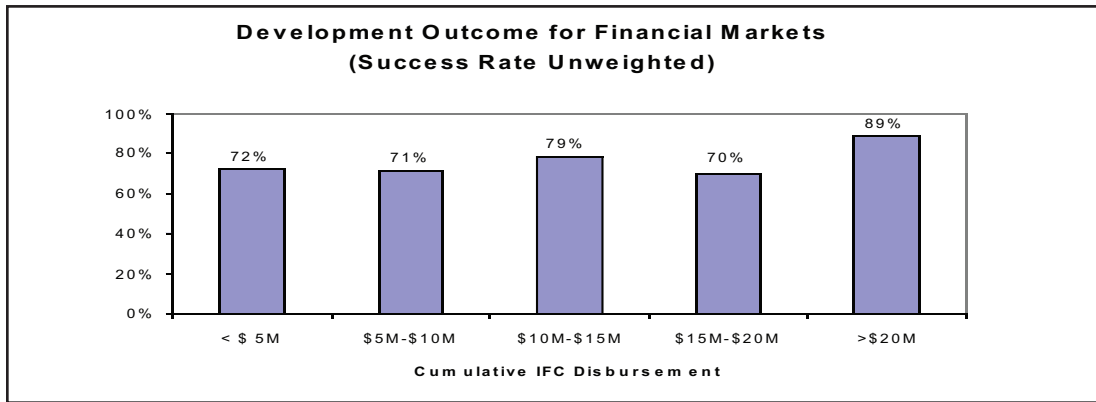
IFC disbursed US\$ 8 million for a project to set up a flour mill and grain silos in the Middle East in 2000. Although the project entailed enhancements to the operational capabilities of the company’s management, unsatisfactory results were attrib-

uted to inadequate management and poor disclosure of information that exacerbated problems faced by the company.

Quality of Product or Service is Vital to Success of Small Projects

Innovative products or services are particularly important to the success of small projects. While all industries achieve higher success rates for larger investments, this pattern is less pronounced for financial markets and infrastructure projects (figure 2). In IFC’s financial market portfolio, smaller companies - often new entrants - have been able to build high quality loan portfolios and enjoy relatively high success rates – comparable to larger projects at or above 70 percent (figure 7).

Figure 7:
Financial markets enjoyed high success rates for all investment sizes



Project example 3:

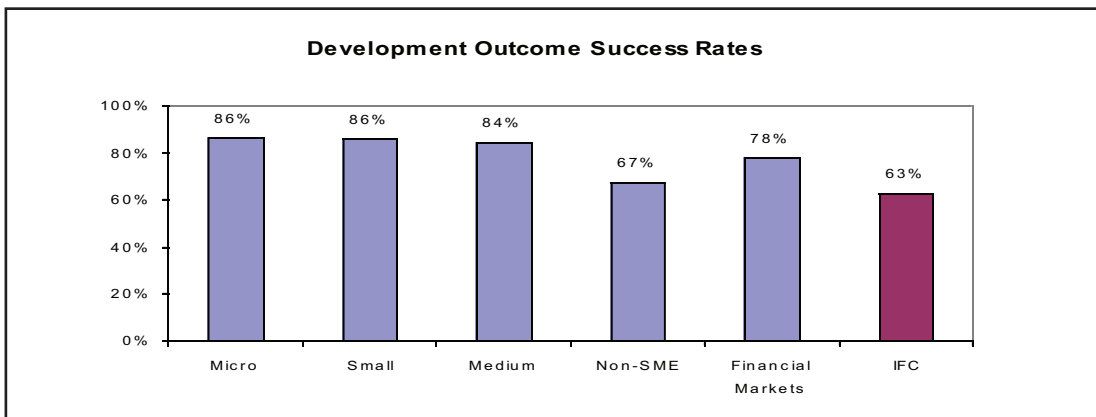
Success through innovation in the insurance market in Latin America

An IFC-supported life insurance company in Latin America – at US\$ 4 million a small investment for IFC - emerged as a leader in the annuity insurance market, challenging existing players. The company offered new products and services to the middle segment of the population, and effectively helped to promote long-term domestic savings and provided retirees with options for private pension plans. This small project's success - its impressive operational performance, enterprise value build-up and market leadership - was driven by the quality of client management and innovative products and services.

Supporting small players indirectly through financial intermediaries achieves superior success rates

Lending to small financial intermediaries shows strong development results. Further, lending to large financial institutions with specific targeted lending to micro, small and medium sized enterprises (MSMEs) also achieves comparatively strong development results. Separating out this group of clients constitutes only a rough measure, because many of IFC's financial markets clients that do not specifically target MSME lending still lend to smaller clients.

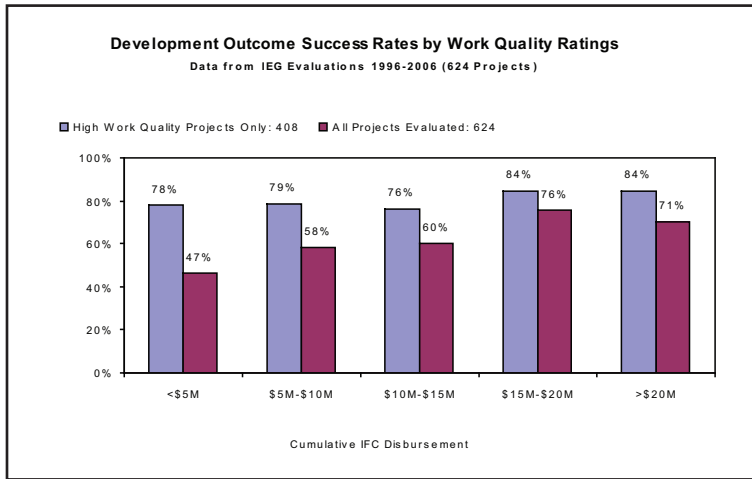
Figure 8:
Strong development results: reaching MSMEs through financial intermediaries



High work quality can mitigate otherwise lower development results for smaller projects

IEG's in-depth evaluations also assess the quality of IFC's work, which comprises of (1) screening, appraisal and structuring of the project, (2) supervision and administration, and (3) IFC's role & contribution. IFC's work quality was in general better for larger investments. However, the finding also shows that when IFC's work quality is high, it significantly increases the likelihood of development success for investments under \$10 million (figure 9).

Figure 9:
Consistently high work quality can mitigate the lower success rate of smaller projects.



Project Example 4:
IFC's high work quality contributes to successful development outcomes of small project.

IFC invested in an Eastern European bank to help them develop and expand. During appraisal in 2001, an IFC team identified that the bank had excellent management reporting capabilities and accounting systems, however, it was not utilizing the capability adequately in the decision making and risk-management functions. The bank has indicated that the IFC-sponsored technical assistance directed management's attention to these areas and the subsequent assistance received was instrumental in formalizing their focus on attention to the importance of the internal audit function and use of information. The project generated positive effect on local economy, serving the needs of 4,500 SME clients, about 20% market share in the SME sector. The project also had a demonstration impact for other investors that followed IFC's example and provided funding to the bank.

Implications for IFC

Consistent with private sector experience, IFC's larger investments achieve superior development outcome success rates. Small projects face particular challenges in the market place. For example, they are vulnerable to market shocks such as price fluctuations, and bureaucracy and red tape hinder them disproportionately. Not surprisingly, small companies have higher failure rates, including in OECD countries.

The relatively poorer performance of small investments can largely be explained by their poorer financial and economic performance. It does not in itself mean, however, that IFC should disengage from making small investments: by challenging established players, often with new and innovative products, small businesses perform a very important role in the functioning of competitive markets. The question is how IFC can be most effective in reaching these smaller players that may have difficulty in attracting funding from elsewhere.

IFC projects that reach small players indirectly through financial intermediaries generate strong development results. This finding supports IFC's strategy to reach larger numbers of small companies more efficiently and successfully through wholesale solutions such as credit lines or capacity building through local institutions; activities that – where successful – promise to be sustainable beyond IFC's involvement.

Management quality, sound corporate governance and quality of product or service are key drivers of project performance. Given these findings are based on evaluations of projects approved before 2001, there is reason to believe that more recent projects will achieve better development results: since then, IFC has substantially strengthened its assessment of management quality and corporate governance.

IEG analysis shows that IFC's own work quality helps to improve development outcome success rates for small investments. This finding suggests that IFC can enhance the performance of its small investments through targeted improvements in its own work quality, for instance through staff training and incentive setting.