



# Conclusions and Recommendations

**T**hroughout the developing world, the private sector has been a key contributor to growth and poverty reduction in recent years. The current global financial and economic crisis places some of these hard-won gains under threat because of much tighter credit conditions, weaker capital inflows, and reduced developed-country import demand. It has also revealed certain market and nonmarket failures and imperfections.

In response to the crisis, development institutions can play important financial and nonfinancial roles. These include providing finance to viable enterprises where it is now lacking (sending positive signals to other investors), acting as an honest broker in financial restructurings, and offering advice that helps address institutional weaknesses, for instance, with regard to effective regulation and good governance. This report examined IFC's experiences in financing development (Part I) and providing knowledge for development (Part II), with a view to informing IFC's future strategic and operational directions, including its response to the current global crisis.

## Conclusions

### *Financing Development*

Concerning IFC's efforts to finance development, the review found that project development results (along with IFC financial returns) improved overall between 2006 and 2008. However, performance in Africa, Asia, and Middle East and North Africa, and in nontelecommunications IT, continued to lag. FI environmental and social ef-

fects ratings remained weak, reflecting continued client and IFC weaknesses. Bank Group impact in these regions will be vital in the coming years. Environmental and social impact will be critical in view of the mounting difficulties in these areas.

Stronger overall results reflected several factors: i) the exit of a particularly weak performing cohort of projects that matured in 2005 (51 percent of projects maturing in 2005 realized high development outcomes, compared with 75 percent maturing in 2008); ii) more favorable economic conditions in much of the developing world (until late 2008, by which time most evaluated projects had been substantially implemented); iii) improving IFC project appraisal and structuring quality; iv) the conscious move by IFC toward larger projects, which have been more likely to achieve higher ratings than smaller projects, due in part to greater internal scrutiny; and v) especially strong performance in Europe and Central Asia and in Latin America and the Caribbean, where the majority of mature operations are located. In these regions, business conditions were

most supportive and IFC work quality strongest. South Asia exhibited improving performance, with higher IFC work quality than in the past.

Performance lagged considerably in East Asia and the Pacific, Middle East and North Africa, and Sub-Saharan Africa—with barely half of projects in these regions meeting or exceeding specified benchmarks and standards. External conditions played some role—projects in Sub-Saharan Africa and Middle East and North Africa generally featured high levels of country, sponsor, and product competitiveness risks—but the quality of IFC's work and contribution to the project tended to have a larger impact. This was especially the case in EAP, where nearly 40 percent of projects exhibited low IFC additionality.

Among IFC's strategic sectors, project performance showed continued improvement in health and education, better performance in agribusiness, continued strong performance in infrastructure and financial markets, and lagged performance in nontelecommunications IT (software and Internet).<sup>1</sup> In other sectors, such as oil, gas, mining, and chemicals, projects achieved relatively poor ratings. Risk exposure was a clear factor in weak nontelecommunications IT projects, most of which were small operations involving inexperienced sponsors and unclear product competitiveness. However, work quality was also well below par—rated high in just 40 percent of cases. Strong IFC work quality was in evidence in the health sector, where the Corporation showed that it had learned lessons from past experience, although the portfolio had less diversity than envisaged. In oil, gas, mining, and chemicals, projects did not meet benchmarks for a number of reasons: technical weaknesses of the sponsor; higher than expected asset acquisition cost, and in one case, poor environmental compliance. Environmental and social effects ratings were stable for real-sector projects, but remained weak in FI operations, reflecting a need to focus on strengthening client capacity and securing commitment, while addressing shortfalls in IFC additionality.

Given the current global financial crisis (an extreme exogenous risk), projects in early implementation are expected to be hardest hit, in

development terms. Such projects represent about 40 percent of IFC's outstanding portfolio (62 percent by volume), thus downside risk to IFC's development "return" is substantial. Going forward, strong IFC work quality and additionality will be required (e.g., in making well-timed, catalytic, new investments; providing corporate finance; acting as an honest broker in restructurings; and helping to improve governance and regulation).

### **Knowledge for Development**

IFC AS have been growing rapidly—so much so that AS teams now dominate IFC's presence on the ground. This rapid growth has happened in largely uncontrolled manner, and raises some important strategic questions. These include whether, in grafting a consulting business onto a bank, IFC has the right balance between AS and investment operations; possible quality trade-offs, given substantial organizational change and a high reliance on short-term consultants; and an increased possibility of COI and market distortion (where AS is offered together with financing, and is provided at less than market value). IFC has taken steps to improve the organizational alignment and delivery of its AS, but more needs to be done to improve internal focus and accountability, and to complement better the efforts of others.

AS delivery quality reflects client commitment, effective project design, and implementation (including getting the right global/local and in-house/consultant staffing mix), M&E, and collaboration with others. While IFC's approach to delivery compares well to that of other MDBs, there are also substantial gaps that need to be addressed—particularly in matching corporate intent with consistent implementation in the field. This also applies with respect to the execution of the pricing policy and provision of reliable M&E data, as well as ensuring good quality project design and implementation, and effective collaboration with other actors, including the Bank. Getting the right staffing mix has been a particular challenge, with a heavy reliance on relatively new staff and external, short-term consultants. Such dependence has considerable implications for the quality and continuity of IFC AS, and preservation of global knowledge leadership.

Available results data suggest better performance in Southern Europe and Central Asia, weaker performance in Latin America and the Caribbean (prior to a recent reorganization) and for global projects; and a strong association between country conditions (including the pursuit of AS activities in high-risk countries), delivery quality, and results. Additionality is fundamental for better performance, and may be enhanced by some—though not all—combinations with IFC investments (e.g., better ratings when combined with loans, and for second generation linkage projects in agribusiness and manufacturing). More benchmarking may be helpful. At all stages of delivery, M&E data provided by staff and consultants (in particular) has remained unreliable. Relatedly, IFC-commissioned reviews of AS facilities, products, and projects, while offering insights on the organization and delivery of AS, have exhibited shortcomings in independence and design.

Charging effectively for IFC's advisory services is perhaps the most important step going forward. Effectively charging clients for service will introduce a market test for AS, and is likely to have a positive impact on all aspects of the AS business: in creating incentives for greater client buy-in, stronger project design and implementation, stronger M&E, development of products that best meet demand, and ensuring IFC additionality. In the immediate term, IFC would need to strictly implement the current pricing policy, which is largely cost-based (i.e., the price the client is expected to pay is a proportion of the cost of the project, rather than its value per se). Over time, efforts should be made to move to a market value-based approach for pricing, to make sure that IFC does not run the risk of crowding out other knowledge providers. IFC investments are priced according to this principle for the same reason. The current economic crisis, and its likely effects on donor and IFC funding, is an opportunity for the Corporation to push harder in the direction of value-based pricing, and to encourage other development institutions to do likewise.

## Recommendations

This review comes at a time of deep distress in financial markets and of severe downsizing in private economic activities. This reminds us of the

critical importance of sustained development of the private sector, for which regulatory frameworks are important and excessive deregulation costly. In these circumstances, this review provides further findings on what IFC might do to enhance development effectiveness and additionality:

### *Operations during the Crisis:*

**Effectively manage the tension between protecting the portfolio and responding to opportunities during crisis.** In the past, this tension has not always been managed adequately and IFC has missed opportunities to have a deeper impact. Experience suggests the importance of arrangements to isolate portfolio problems from new business development, mitigating conflicts of interest that may impede effective collaboration with the Bank and the IMF, and of clear rules of engagement for crisis response, particularly for staff in the field. Experience also indicates the important role IFC and the Bank Group must play in promoting sound frameworks for prudent financial risk management and safeguards for sustainable private sector development. This is especially relevant today, as the world reexamines the roles of governments and markets in the wake of the financial crisis.

### *Role in Advisory Services:*

**Set out an overall strategy for IFC advisory services, addressing the need for a clear vision and business framework that is more closely linked with IFC's global corporate strategy.** Following years of unchecked growth and recent organizational changes, the role of AS in IFC's business model needs to be addressed. The strategy would need to better articulate IFC comparative advantages, objectives, and goals for AS in different contexts (a source of confusion among staff), and to consider the best staffing combinations (with respect to internal or external, as well as global or local staff), delivery unit organization, incentives, and performance measures to help realize these objectives and goals.

**Pursue more programmatic AS interventions.** Evaluation shows that IFC achieved better results in AS projects that were carried out in conjunction with other AS interventions. One-

off activities have been less effective. However, programmatic efforts of this kind have been in the minority (about a fifth of all AS projects), and IFC should accordingly seek to expand this type of intervention.

**Improve execution of the AS pricing policy through greater client contributions.** Over the longer term, it would be important to seek client contributions that reflect value and impact (i.e., not just cost, to create a true test of client demand, incentives for better AS delivery, and to ensure IFC is being additional).

**Strengthen AS performance measurement and internal knowledge management.** In the short term, it would be important to have more hands-on M&E support in the field, after-

project-completion follow-up, better lessons-capture (including from dropped or terminated projects), and more arms-length facility, product, and project reviews. In the medium term, it would pay to introduce an Expanded Project Completion Report system (akin to the Expanded Project Supervision Report system for investment operations, and carried out later than the PCR to better capture impacts), more programmatic impact evaluation and impact research, setting results-based targets for AS in its corporate scorecard, and regular benchmarking of IFC AS activities and systems with other providers of knowledge services, including other MDBs and commercial providers. In the longer term, the aim could be to establish a specialized research unit focusing on generating and bringing together private sector development knowledge work.