Report Number: ICRR0022245

## 1. Project Data

| Project ID | Project Name |
|---|---|
| P119047 | Financial Sector Rapid Response Project |
| **Country** | **Practice Area(Lead)** |
| Afghanistan | Finance, Competitiveness and Innovation |

| L/C/TF Number(s) | Closing Date (Original) | Total Project Cost (USD) |
|---|---|---|
| IDA-D1400,IDA-H7320,IDA-H8930 | 30-Jun-2014 | 22,067,390.89 |
| **Bank Approval Date** | **Closing Date (Actual)** | |
| 25-Aug-2011 | 31-Oct-2019 | |

| | IBRD/IDA (USD) | Grants (USD) |
|---|---|---|
| Original Commitment | 19,000,000.00 | 0.00 |
| Revised Commitment | 24,666,074.25 | 0.00 |
| Actual | 22,067,390.89 | 0.00 |

| Prepared by | Reviewed by | ICR Review Coordinator | Group |
|---|---|---|---|
| Antonio M. Ollero | J. W. van Holst Pellekaan | Christopher David Nelson | IEGSD (Unit 4) |

## 2. Project Objectives and Components

### a. Objectives

According to the original Emergency Project Paper (page 5) and the original Financing Agreement (page 5), the project development objective (PDO) of the Afghanistan Financial Sector Rapid Response Project was "to assist DAB to develop actions plans for improved banking supervision and implement a modern national payment system for efficient and transparent payment transactions." Da Afghanistan Bank (DAB) is the central bank.

According to the Project Paper (page 10) and the Financing Agreement (page 5) for the first restructuring and first additional financing, dated November 3, 2014, the revised project development objective was "to assist DAB to develop action plans for improved banking supervision and to establish key building blocks of financial sector infrastructure: payment system, movable collateral registry, and public credit registry."

Contrary to the conclusion of the ICR (paragraph 18, page 10), this Review considers that the change in the PDO at the first restructuring reduced the level of ambition of the original PDO and that the change was not marginal. Both the original and revised PDOs aimed at assisting DAB "to develop actions plans for improved banking supervision". Although the scope of the revised PDO was broader than the original PDO, the original PDO was more ambitious because it sought to "implement a modern national payment system for efficient and transparent payment transactions" which also had a defined end point, whereas the revised PDO sought only to "to establish building blocks of an improved banking supervision and financial sector infrastructure, movable collateral registry, and public credit registry" which had an undefined end point. The lack of change in the PDO indicators is not regarded as signaling a marginal change in the project development objective.

For the purpose of the assessment of efficacy in Section 4 the PDO will be parsed as follows:

- Objective 1: "To assist DAB to develop action plans for improved banking supervision."
- Objective 1 - Revision 1: "To assist DAB to develop action plans for improved banking supervision" (no change).
- Objective 2: "To assist DAB to implement a modern national payment system for efficient and transparent payment transactions."
- Objective 2 - Revision 1: "To assist DAB to establish key building blocks of the financial sector infrastructure: payment system, movable collateral registry, and public credit registry."

In Section 6, this Review will undertake a split rating of outcomes because of the formal revision of the project development objective in 2014.

### b. Were the project objectives/key associated outcome targets revised during implementation?
Yes

### Did the Board approve the revised objectives/key associated outcome targets?
Yes

### Date of Board Approval
04-Nov-2014

### c. Will a split evaluation be undertaken?
Yes

### d. Components
The original project had four components:

- **Audits of Commercial Banks** (US$3.5 million estimated) covered the: (a) financial, portfolio, and institutional audits of ten of the country's 17 commercial banks, following international audit standards, to assess their financial condition and suggest action plans to address any identified weaknesses, and (b) assistance in the implementation of the bank actions plans resulting from the audits.

- **Modernization of the Afghanistan Payments System** (US$11 million estimated) supported the development and deployment of the national payment system infrastructure to include: (a) the card and mobile payment switch to support the settlement of card transactions and mobile payments at the Afghanistan Payments System; (b) the Real-Time Gross Settlement System to process large-value, systematically-important, and time-critical payments at the Automated Transfer System; (c) the Automated Clearing House to settle and clear low-value retail payments at the Automated Transfer System; (d) the Centralized Securities Depository to record securities account holdings of market participants in a de-materialized form and to facilitate the automated pledging and lending of securities, also at the Automated Transfer System; and (e) an inter-bank communications network to support the payment systems infrastructure. The first of two pillars of the national payment system, the Afghanistan Payments System was established by U.S. Task Force for Business and Stability Operations and the DAB in 2011 to act as the private-sector national provider and operator of secure financial message switching and interface for participating banks (three banks were members of the Afghanistan Payments System at appraisal). The Automated Transfer System, the second pillar and consisting of the Real-Time Gross Settlement System, Automated Clearing House and Centralized Securities Depository, was envisioned to act as the DAB-operated processor of all electronic payments, replacing the Afghanistan Clearing and Settlement System. This project component also supported: (e) the upgrade of the DAB's existing Core Banking System; (f) the development of the DAB's other internal information technology (IT) systems; and (g) the financing of the initial operating costs and maintenance of the national payment system.
- **Support to the Afghanistan Institute of Banking and Finance** (US$1 million estimated) supported the Afghanistan Institute of Banking and Finance to increase the types and quality of training offered, in coordination with the Financial Access for Investing in the Development of Afghanistan Project, funded by the U.S. Agency for International Development. The Afghanistan Institute of Banking and Finance was created by the DAB and the Afghanistan Banking Association in 2010, under the predecessor Financial Sector Strengthening Project (FSSP), to provide education, training, and research to the banking and financial sector.
- **Technical Assistance, Training, and Project Implementation** (US$3.5 million estimated) provided technical assistance to strengthen the: (a) legal and regulatory framework for the settlement of payments, remittances, and securities, including the development of a comprehensive national payment system law; (b) technical capacity of the DAB to oversee, operate, and regulate the national payment system; and (c) institutional capacity of the DAB to coordinate, monitor, and evaluate this project, including by operating a Project Implementation Cell.

The first restructuring, which broadened the project objective, consolidated the project components into three and added other activities.

- **Strengthening the DAB's Capacity** (US$8 million estimated) merged and expanded the original first and third components to include support for: (a) the development and implementation of action plans following the audits of ten commercial banks; (b) a stock-taking of capacity-building efforts in financial supervision over the last ten years and development and implementation of a capacity-building plan to strengthen the DAB Financial Supervision Department; and (c) review of the bank regulation framework.
- **Development of the Financial Sector Infrastructure** (US$14.7 million estimated) expanded the original second project component to include support for the: (a) establishment of the Public Credit Registry to collect information on loans required by law to be registered with the state, helping the

DAB to better regulate and supervise financial institutions; and (b) establishment of the Movable Collateral Registry to record legal claims to property used as collateral for loans, allowing lenders to check if the collateral had been pledged to another lender, thus helping avoid disputes over property rights. The Movable Collateral Registry would allow borrowers and banks to use movable property rather than immovable property (land and buildings) as collateral, expanding the range of borrowers who could provide security for loans. Both the Public Credit Registry and the Movable Collateral Registry were initiated under the FSSP.

- **Technical Assistance and Training for Project Implementation** (US$3 million estimated) expanded the original fourth component to include: (a) project implementation support for the Public Credit Registry, and (b) project implementation support for the Movable Collateral Registry.

The fourth restructuring added activities to the three project components adopted during the first restructuring.

- **Strengthening the DAB's Capacity** (US$9 million estimated) was expanded to include technical assistance for: (a) development of DAB's internal audit function; (b) adoption by the DAB of the Risk Based Internal Audit; and (c) adoption by the DAB of the International Financial Reporting Standards.
- **Development of the Financial Sector Infrastructure** (US$29.7 million estimated) was expanded to include: (a) the acquisition and installation of a Core Banking System to processes daily banking transactions and post updates to accounts and other financial records; (b) an Enterprise Resource Planning to integrate the management of main business processes in real time and using software and technology; (c) and a Data Warehouse to serve as the central repository of integrated data from one or more disparate sources; (d) the automation of the DAB Internal Audit System; (e) the automation of the DAB Financial Intelligence Unit; (f) the enhancement of the DAB's IT governance and risk management practices; (g) the acquisition and installation of video conference equipment for the DAB; and (h) financial support for the Afghanistan Payments System and Afghanistan Institute of Banking and Finance operating costs.
- **Technical Assistance and Training for Project Implementation** (US$7 million estimated) was expanded to include support for the skills development of the DAB technical staff, including through a combination of intensive skill development courses offered by the Afghanistan Institute of Banking and Finance, on-the-job learning, and financing for degree programs at Afghan universities.

## e. Comments on Project Cost, Financing, Borrower Contribution, and Dates

Project Cost. The original Emergency Project Paper of August 2011 estimated the project cost at US$19 million. The Project Paper of November 2013 estimated an additional project cost of US$6.7 million. The Project Paper of October 2016 estimated an additional project cost of US$20 million.

Project Financing. The project was financed with an SDR 11.9 million (US$19 million equivalent) grant from the International Development Association (IDA) in August 2011, an SDR 4.4 million (US$6.7 million equivalent) additional grant in November 2013, and an SDR 14.4 million (US$20 million equivalent) additional grant in October 2016, for a total financing of SDR 30.7 million (US$45.7 million equivalent) in IDA grants. The sum of SDR 26.4 million (US$22.1 million equivalent) was disbursed, and the undisbursed balance of SDR 14.3 million (US$23.6 million) was canceled shortly before project closing.

Borrower Contribution. There is no record of government counterpart financial contribution to the project.

Dates. The project was approved on August 15, 2011, became effective on September 6, 2011, and closed on October 31, 2019, more than five years after the original closing date of June 30, 2014.

Restructuring. The project was restructured five times: (a) on November 26, 2013, with US$5.61 million disbursed (29.5 percent of the original financing), to revise the project objectives, revise the project components, provide additional financing of SDR 4.4 million (US$6.7 million equivalent), and extend the closing date from June 30, 2014 to June 30, 2016; (b) on January 26, 2015, with US$8.34 million disbursed (32.5 percent of the revised financing), to reallocate funds between disbursement categories; (c) on May 25, 2016, with US$13.32 million disbursed (51.8 percent of the revised financing ), to change the loan closing date; (d) on October 27, 2016, with US$13.43 million disbursed (52.3 percent of the revised financing), to revise the project components, provide additional financing of SDR 14.4 million (US$20 million equivalent), and extend the closing date from June 30, 2016 to June 30, 2018; and (e) on October 28, 2019, with US$22.07 million disbursed (48.3 million of the twice-revised financing), to reallocate funds between disbursement categories and to cancel the undisbursed financing of SDR 14.3 million (US$23.6 million equivalent).

## 3. Relevance of Objectives

### Rationale

The project objectives were relevant to the critical problems faced by the financial sector in Afghanistan at the time of appraisal.

- The failure of Kabul Bank, the country's largest private commercial bank in 2010, and the costly government bailout of the institution in 2011 (costing about five percent of GDP), exposed two serious problems with the country's financial sector: (a) weak banking supervision --- Kabul Bank had US$900 million of bad loans on total assets of US$1.3 billion; and (b) a poor national payment system --- Kabul Bank, which held a third of the banking system's total assets of US$4 billion, held a monopoly processing the payment of salaries to civil servants and security personnel.
- The project objective to assist the central bank "to develop actions plans for improved banking supervision and to implement a modern national payment system for efficient and transparent payment transactions" was relevant to these two critical problems, aiming to prevent a repetition of the Kabul Bank crisis.
- Subsequently, the cancellation of the FSSP (the Bank project to assist the DAB to improve banking supervision and regulation, strengthen access to banking, and promote financial sector reform) and the reallocation of the undisbursed amount from the FSSP to this project broadened the project objectives to cover assistance to the central bank "to develop action plans for improved banking supervision and to establish key building blocks of the financial sector infrastructure, including: payment system, movable collateral registry, and public credit registry" (the creation of the public credit registry and the movable collateral registry had been initiated under the FSSP).

- This revised project objective remained relevant to the problems in the financial sector, which continued to deal with the aftermath of the Kabul Bank crisis, according to the Independent Joint Anti-Corruption Monitoring and Evaluation Committee that conducted the inquiry into Kabul Bank.

The project objectives were aligned with development priorities in Afghanistan at the time of appraisal, restructuring and closing.

- The project objectives were aligned with the *Afghanistan National Development Strategy 2008-2013* (ANDS), specifically with the Economic Governance and Private Sector Development pillar at appraisal and at restructuring. The ANDS envisioned a modern and competitive financial sector as one of the country's main development objectives, and articulated a strategy to expand the availability and range of financial products and services.
- At the time of completion, the project objectives remained relevant to the *Afghanistan National Peace and Development Strategy 2017-2021* (ANPDS). The ANDPS listed eleven national priority programs. The project objectives were relevant to the first priority program which focused on private sector development and highlighted the importance of a private sector-led financial market, where strengthening banking sector oversight was a key priority.

The project objectives were also aligned with the Bank Group strategy in Afghanistan at the time of appraisal, restructuring and closing.

- The project objectives were consistent with the Bank Group *Interim Strategy Note for the Islamic Republic of Afghanistan for the Period FY09-FY11* (ISN), specifically with INS Pillar 3 - Supporting Private Sector Growth. Support under this pillar included lending and advisory services for improving access to finance and strengthening key financial sector foundations, including banking supervision and capacity building training for commercial banks.
- The project development objectives also remained relevant to *Country Partnership Framework for the Islamic Republic of Afghanistan for the Period FY17 to FY20* (CPF), specifically with CPF Pillar 2 - Supporting Inclusive Growth, which emphasized the need for a stable and efficient financial system a priority. Afghanistan's financial system remained underdeveloped and constantly faced stability risks. Continued strengthening of financial sector regulation and supervision remained critical for enhancing financial stability, a key prerequisite for financial sector deepening.
- However, the expected achievement of the objectives such as "to develop action plans" and "to establish building blocks" without many specific outcome indicators reflected a low level of ambition.

In a formal sense, the objectives were well aligned with the government's development priorities and the Bank's development strategies for Afghanistan. However, the project's level of ambition was low, although plausibly realistic for a fragile and conflict-affected state. On this basis, the relevance of the objective is rated substantial

**Rating**

Substantial

## 4. Achievement of Objectives (Efficacy)

## OBJECTIVE 1

### Objective

To assist DAB to develop actions plans for improved banking supervision.

### Rationale

Theory of Change. The conduct of financial, portfolio, and institutional audits of ten commercial banks would help the DAB develop plans to improve banking supervision. The implementation of the action plans based on the findings of the audits, and with the support and oversight of the DAB, would strengthen the commercial banking sector. Moreover, the review of the framework for bank regulation in the country, the development and implementation of a capacity-building plan to strengthen the Financial Supervision Department, the development of the internal audit function, the adoption of the Risk Based Internal Audit, and the adoption of the International Financial Reporting Standards would all strengthen the institutional and technical capacity of the DAB to regulate and supervise the banking system.

Outputs. The project fully met four and partially met one of the nine output targets for the objective to develop actions plans for improved banking supervision. It failed to meet four output targets.

- The audit reports on ten banks were completed as planned, highlighting the strengths and weaknesses of each bank, meeting the target. There were no audit reports on banks in the baseline following the Kabul Bank crisis in 2010-11. Three actions plans were developed to guide supervision and oversight of the weak banks over a five-year period.
- The number of commercial bank staff trained at the Afghanistan Institute of Banking and Finance reached 10,068 by the project closing date, from 1,017 in the baseline, exceeding the target of 6,000. Of these, the number of women commercial bank staff trained reached 1,808, from 243 in the baseline, exceeding the target of 1,200. There was, however, no assessment in the ICR of the impact of this training.
- The DAB approved the regulations to implement the new Banking Law and the regulations for anti-money laundering and combating the financing of terrorism, that were consistent with international regulatory standards, meeting the target. The DAB also developed the following: (a) the Legal Assessment Report against International Standards; (b) the Regulation for the Licensing and Oversight of Payment and Securities Transfer Systems and of Money Service Providers; (c) the General Guidelines on Retail Payment Instruments; and (d) the Regulation on Electronic Fund Transfers. The target was for the DAB to approve regulations for the financial sector that were consistent with international standards, reversing the case in the baseline where the regulations were not fully aligned with international standards.
- The financial statements of the DAB for 2018 were not prepared using the International Financial Reporting Standards, the accounting standards issued by the International Financial Reporting Standards Foundation and the International Accounting Standards Board, but were prepared using local accounting standards, as in the baseline. The target ~~was~~ for the DAB to increase transparency of its finances and financial reporting with the adoption of international central bank accounting and auditing standards by the project closing date was not achieved.
- There was no reduction in the time spent by the DAB to prepare its balance sheet. The target was to reduce the time to prepare the balance sheet by 80 percent, an achievement that would have reflected

the operational efficiency of the DAB. According to the ICR (pages 13-14), the new Core Banking System, Enterprise Resource Planning and Data Warehouse, which would have provided a centralized IT platform for the DAB and help it improve its operational efficiency, was not implemented beyond the preparation of the technical specifications and terms of reference for contracts.

- The target to have an effective Financial Supervision Department, with training processes in place to ensure sustainable capacity development, was only partly achieved. According to the ICR (page 26), the outcome of the technical assistance to help develop the institutional capacity of the department was sub-optimal. The DAB had approved the organization structure of the Financial Supervision Department in the baseline, and the plan was for the continuous implementation of the institutional development action plan over the project implementation period. However, the technical assistance to the department started late in November 2017, after many delays, was only partially delivered.
- The number of on-site and off-site examinations conducted by the Financial Supervision Department increased by 50 percent, exceeding the target for an increase by 10 percent.
- The percentage of the operating costs of the Afghanistan Payments System and the Afghanistan Institute of Banking and Finance covered by their own operating revenues was only 22 percent, well under the target of 50 percent. The achievement of the target would have reflected an improvement in the sustainability of the Afghanistan Payments System and the Afghanistan Institute of Banking and Finance.
- The number of key DAB staff trained was only 331, well under the target of 1,443. The number of DAB staff who were enrolled in, or completed their, Bachelors or Masters programs was 227, slightly under the target of 250. The number of eligible DAB staff in critical functions who completed specialized professional training sessions increased by 76 percent, meeting the target for an increase by 50 percent. The number of key DAB female staff trained under the project was 28, well under the target of 172. However, the ICR provided no assessment of the impact of the training on DAB's efficiency.

<u>Outcomes</u>. The project achieved the sole outcome target defined for the objective to develop actions plans for improved banking supervision.

- Following the audits, the DAB Financial Supervision Department developed *Weak Bank Strategy and Action Plans* to improve the overall condition and performance of the weak banks. Three *Weak Bank Strategy and Action Plans* were developed over five years. Two of these action plans were successfully implemented and the third, which covers the period March 2019 to March 2021, was still under implementation at project closing.
- According to the ICR (page 10), there have been improvements in the capital adequacy, liquidity, governance, and resolution of non-performing loans of the weak banks. This assessment means that the original outcome target in the theory of change that "the commercial banking sector is strengthened following implementation of action plans developed based on the findings of the audits, with support and oversight of DAB" (ICR, Table 1, pages 5-6) was achieved.
- Overall, by the time the project closed, the project was only modestly successful in its objective to “assist DAB to develop actions plans for improved banking supervision” because the action plans were ultimately prepared by DAB with support from the IMF, without specific support from the World Bank (ICR, para 41, page 15). In addition, notwithstanding this achievement in banking supervision, the financial sector itself remained vulnerable, considering the high-risk operating environment and the institutional capacity challenges in the country, according to the ICR, citing the IMF *Staff Report for the*

*2019 Article IV Consultation and the Sixth Review under the Extended Credit Facility Arrangement for the Islamic Republic of Afghanistan.*

**Rating**
Modest

## OBJECTIVE 1 REVISION 1

**Revised Objective**
To assist DAB to develop actions plans for improved banking supervision.

**Revised Rationale**
Theory of Change. Objective 1 - Revision 1 and the theory of change was the same as in Objective 1.

Outputs. The outputs were the same as in Objective 1 for the entire project time period.

Outcomes. The outcomes were the same as in Objective 1 for the entire project time period.

**Revised Rating**
Modest

## OBJECTIVE 2

**Objective**
To assist DAB to implement a modern national payment system for efficient and transparent payment transactions.

**Rationale**
Theory of Change**.** The development and deployment of the card and mobile payment switch at the Afghanistan Payments System to support the settlement of card transactions and mobile payments, the Real-Time Gross Settlement System to process large-value inter-bank payments, the Automated Clearing House to process retail payment transactions; and the Centralized Securities Depository to facilitate the automated pledging and lending of securities, all at the Automated Transfer System, would modernize the country's national payment system.

**Modern National Payment System**

Outputs. The project partially met three of the four output targets for the objective to implement a modern national payment system for efficient and transparent payment transactions.

- The card and mobile payment system at the Afghanistan Payments System "went live" in December 2015, partially meeting the target. The other half of the target --- that the card and mobile payment system process 80 percent of all inter-bank and inter-institutional card and mobile payment transactions on an ongoing basis --- was not met. Only six of 12 domestic commercial banks and one of four mobile network operators joined the platform. According to the ICR (page 12), the low participation rate posed sustainability problems to the payment switch and to the Afghanistan Payments System itself: (a) many of the hold-out banks and mobile network operators had little incentive to join the platform, including that they did not issue cards; (b) a DAB attempt to facilitate utilization of the platform through a circular mandating interoperability between banks and mobile network operators through the Afghanistan Payments System left the decision to join the platform at the discretion of the banks; (c) the Afghanistan Payments System was not able to generate sufficient revenue to maintain the operations, requiring financial support from the project; (d) the DAB took over the Afghanistan Payments System, integrating the latter's operations as a separate department within the central bank, departing from the original vision that the Afghanistan Payments System be a private-sector institution and operation.

- The Real-Time Gross Settlement System, part of the Automated Transfer System, was established at the DAB in 2019 after a lengthy delay (procurement and installation of equipment took seven years, training of the DAB staff was transferred from a location in the United Arab Emirates to Azerbaijan, and the disaster recovery site was relocated from the United Arab Emirates to India). However, the Real-Time Gross Settlement System, while operational at the DAB, was not yet integrated with all operating banks in the country, which implied that the target for the Real-Time Gross Settlement System to be operational with transactions settled in real time could not be considered to have been definitively achieved by the project closing date.
- Interbank payments were settled on the same day across Afghanistan, at least according to tests of settlements at the Afghanistan Payments System and the Automated Transfer System. According to the ICR (page 29), card transactions were settled on the same day at the Afghanistan Payments System using shared automated teller machine networks. All eight interbank transaction types were settled between participant banks on a real time basis in the Real-Time Gross Settlement System. The output target was to improve the timelines for inter-bank payments by project closing to the "same day" in all areas in Afghanistan, from the baseline timelines of "T+1 days" in Kabul and "T+3 days" in other areas.
- The ratings assessed by the *World Bank Global Payments System Survey* for the Afghanistan Payments System did not improve as targeted. Based on the World Bank's report: (a) the rating for *legal and regulatory framework* remained "low", as in the baseline, failing to improve to a target of "medium high"; (b) the rating for *system design and policies for large value payment systems* was not available at closing, as in the baseline, failing to meet the target of "medium high"; (c) the rating for *usage of large-value payment systems* was not available at closing, as in the baseline, failing to meet the target of "medium low"; (d) the rating for *retail payments infrastructure and policies for retail payment systems* remained at "medium low" at closing, as in the baseline, failing to improve to a target of "medium high"; (e) the rating for *efficiency of retail payment instruments and extensiveness of usage of non-cash payment instruments* remained "low" at closing, as in the baseline, failing to improve to a target of "medium low"; and (f) the rating for *oversight functions* remained "low" at closing, as in the baseline, failing to improve to a target of "medium high" (ICR, Table 1, pages 5-6).

<u>Outcomes</u>. The project did not fully meet the sole outcome target defined for the objective to implement a modern national payment system for efficient and transparent payment transactions.

- The national payment system conformed to modern international norms, as established by the Bank for International Settlements and the Payment Systems Development Group of the Bank, contributing to the safety and efficiency of the financial sector. The Afghanistan Payments System was "live", with six banks and one mobile network operator being part of the system at project closing. Since then, there have been ongoing negotiations to increase the number of participants in the card and mobile payment switch. The Automated Transfer System, the replacement for the Afghanistan Clearing and Settlement System, settled transactions between banks on the same day, but the settlement was still done manually rather than automatically. Automatic settlement would only be possible once the full integration of the system with all commercial banks was completed. That this project has created a new national payment infrastructure for that conforms to international norms should play a key role in the development of the digital payment system in the country moving forward. The implementation of a modern national payment system was only modestly achieved when the project closed --- the Afghanistan Payments System remained underutilized and the Automated Transfer System was half-operational, with both systems facing operational sustainability hurdles.

**Rating**
Modest

## OBJECTIVE 2 REVISION 1

**Revised Objective**
To assist DAB to establish key building blocks of the financial sector infrastructure: payment system, movable collateral registry, and public credit registry.

**Revised Rationale**
Theory of Change**.** The development and deployment of the card and mobile payment switch at the Afghanistan Payments System to support the settlement of card transactions and mobile payments, the Real-Time Gross Settlement System to process large-value inter-bank payments, the Automated Clearing House to process retail payment transactions, and the Centralized Securities Depository to facilitate the automated pledging and lending of securities, all at the Automated Transfer System, would modernize the country's national payment system, establishing one of the key building blocks for the country's financial sector infrastructure. In addition, the establishment and operation of a Public Credit Registry to collect data on loans to aid the DAB's supervisory function and of a Movable Collateral Registry to record legal claims on property used as collateral for loans would create registries for debt and collateral, establishing the other key building blocks for the country's financial sector infrastructure.

**Modern National Payment System**

Outputs. The project partially met three of the four output targets for the objective to build the key building blocks for the payment system.

- The card and mobile payment system at the Afghanistan Payments System "went live" in December 2015, partially meeting the target. The other half of the target --- that the card and mobile payment system process 80 percent of all inter-bank and inter-institutional card and mobile payment transactions on an ongoing basis --- was not met. Only six of 12 domestic commercial banks and one of four mobile network operators joined the platform. According to the ICR (page 12), the low participation rate posed sustainability problems to the payment switch and to the Afghanistan Payments System itself: (a) many of the hold-out banks and mobile network operators had little incentive to join the platform, including that they did not issue cards; (b) a DAB attempt to facilitate utilization of the platform through a circular mandating interoperability between banks and mobile network operators through the Afghanistan Payments System left the decision to join the platform at the discretion of the banks; (c) the Afghanistan Payments System was not been able to generate sufficient revenue to maintain the operations, requiring financial support from the project; (d) the DAB took over the Afghanistan Payments System, integrating the latter's operations as a separate department within the central bank, departing from the original vision that the Afghanistan Payments System be a private-sector institution and operation.

- The Real-Time Gross Settlement System, part of the Automated Transfer System, was established at the DAB in 2019 after a lengthy delay (procurement and installation of equipment took seven years, training of the DAB staff was transferred from a location in the United Arab Emirates to Azerbaijan, and the disaster recovery site was relocated from the United Arab Emirates to India). However, the Real-Time Gross Settlement System, while operational at the DAB, was not yet integrated with all operating banks in the country, which implied that the target for the Real-Time Gross Settlement System to be operational with transactions settled in real time could not be considered to have been definitively achieved by the project closing date.
- Interbank payments were settled on the same day across Afghanistan, at least according to tests of settlements at the Afghanistan Payments System and the Automated Transfer System. According to the ICR (page 29), card transactions were settled on the same day at the Afghanistan Payments System using shared automated teller machine networks. All eight interbank transaction types were settled between participant banks on a real time basis in the Real-Time Gross Settlement System. The output target was to improve the timelines for inter-bank payments by project closing to the "same day" in all areas in Afghanistan, from the baseline timelines of "T+1 days" in Kabul and "T+3 days" in other areas.
- The ratings made by *World Bank Global Payments System Survey* for the Afghanistan Payments System did not improve as targeted. Based on the Bank document: (a) the rating for *legal and regulatory framework* remained "low", as in the baseline, failing to improve to a target of "medium high"; (b) the rating for *system design and policies for large value payment systems* was not available at closing, as in the baseline, failing to meet the target of "medium high"; (c) the rating for *usage of large-value payment systems* was not available at closing, as in the baseline, failing to meet the target of "medium low"; (d) the rating for *retail payments infrastructure and policies for retail payment systems* remained at "medium low" at closing, as in the baseline, failing to improve to a target of "medium high"; (e) the rating for *efficiency of retail payment instruments and extensiveness of usage of non-cash payment instruments* remained "low" at closing, as in the baseline, failing to improve to a target of "medium low"; and (f) the rating for *oversight functions* remained "low" at closing, as in the baseline, failing to improve to a target of "medium high".

Outcomes. The project substantially met the outcome target defined for the revised objective, namely to build the key building blocks for the payment system.

- The national payment system conformed to modern international norms, as established by the Bank for International Settlements and the Payment Systems Development Group of the Bank, meeting the target. The Afghanistan Payments System was "live", with six banks and one mobile network operator being part of the system at project closing. Since then, there have been ongoing negotiations to increase the number of participants in the card and mobile payment switch. The Automated Transfer System, the replacement for the Afghanistan Clearing and Settlement System, settled transactions between banks on the same day, although the settlement was still done manually rather than automatically. Automatic settlement would only be possible once the full integration of the system with all commercial banks was completed. That this project has created a new national payment infrastructure that conformed to international norms should play a key role in the development of the digital payment system in the country moving forward. The Afghanistan Payments System, however, is underutilized and the Automated Transfer System is half-operational, with both systems facing operational sustainability hurdles. Notwithstanding these challenges, the payment system building block was substantially established.

**Movable Collateral Registry**

Outputs. The project did not meet the ~~sole~~ output target for the objective to build the key building blocks for the movable collateral registry.

- The number of items of collateral registered in the Movable Collateral Registry increased from 815 in the baseline (November 2013) to 7,547 at project closing, failing to meet the target for an increase to 10,000 items. The establishment of the Movable Collateral Registry had been initiated in February 2013 under the FSSP, with the assistance of the International Finance Corporation which supported the development of the legal framework, the technical specifications, and the public awareness program for the registry. This project formally launched the Movable Collateral Registry in 2014, providing financing and support for the IT system and for the training of the staff to operate the registry (ICR, para 37, page 14).

Outcomes

- There were no outcome indicators or targets defined for the objective to establish the building blocks for the movable collateral registry According to the ICR, despite the initial gains, the Movable Collateral Registry was not yet fully operational because of: (a) delays with the extension of the support and maintenance contract for the registry, and (b) budgetary constraints at the DAB, which was responsible for maintaining the registry. In the near- to medium-term, the continued operation of the registry would depend on the ability of the DAB to maintain the system. Additional IT work on the registry was planned under a new Bank project. The movable collateral registry building block was established, but it would need more support.

**Public Credit Registry**

Outputs. The project met the ~~sole~~ output target for the objective to build the key building blocks for the public credit registry.

- The number of credit reports sent by the Public Credit Registry to commercial banks rose from zero in the baseline (November 2013) to 440,802 at project closing, exceeding the target for an increase to 250,000 credit reports (ICR, para 37, page 14). The establishment of the Public Credit Registry had been initiated in February 2013 under the FSSP. The DAB issued a circular in November 2014 mandating all commercial banks to make an inquiry with the Public Credit Registry and obtain a credit report before issuing a loan. Managed by the DAB, the Public Credit Registry held around 120,000 records and was linked to 15 commercial banks, four microfinance institutions, as well as the Revenue Department at the Ministry of Finance (ICR, para 37, page 14).

Outcomes

- There were no outcome indicators or targets defined for the objective to establish the building blocks for the public credit registry. According to the ICR, while the gains were substantial relative to the baseline, the coverage of the Public Credit Registry remained limited overall. Only about 1.5 percent of the adult population (294,440 individuals) and 5,818 firms were covered by the registry, based on data from the Bank's *2020 Doing Business* report. Additional IT work on the Public Credit Registry was planned under a new World Bank project. The public credit registry building block was established, but it would need more support.

**Revised Rating**
Substantial

## OVERALL EFFICACY

**Rationale**
The degree of achievement of the original PDO is rated modest on the basis of a modest efficacy rating on Objective 1, namely "to assist DAB to develop actions plans for improved banking supervision" because the financial sector remained vulnerable, and a modest efficacy rating on Objective 2, namely "to assist DAB to implement a modern national payment system for efficient and transparent payment transactions" which was far from being achieved. Hence the overall efficacy with which the project's original objectives were achieved before restructuring was rated modest.

| **Overall Efficacy Rating** | **Primary Reason** |
|---|---|
| Modest | Low achievement |

## OVERALL EFFICACY REVISION 1

**Overall Efficacy Revision 1 Rationale**
The efficacy with which Objective 1 - Revision 1, namely "to assist DAB to develop actions plans for improved banking supervision," was achieved was rated modest. The efficacy with which Objective 2 - Revision 1, namely "to assist DAB to establish key building blocks of the financial sector infrastructure: payment system, movable collateral registry, and public credit registry." was rated substantial. Overall the efficacy of the achievement of the project's objectives after restructuring was rated modest.

| **Overall Efficacy Revision 1 Rating** | **Primary Reason** |
|---|---|
| Modest | Low achievement |

## 5. Efficiency

Economic Efficiency. The original Project Paper did not present an economic analysis of the project. The subsequent Project Papers, prepared for several rounds of restructuring, sketched brief arguments for the project having positive economic benefits: (a) the Project Paper of November 2013 stated that sound financial market infrastructure would improve access to credit --- strong collateral laws and good credit information systems would lead to higher bank lending and were associated with higher bank profitability, lower bank risk, and a higher ratio of bank credit to GDP; (b) the Project Paper of October 2016 stated that the project would contribute to the increased efficiency of central bank operations, more effective regulation and supervision of the financial sector, and improved quality of financial information --- the central bank would be more capable to deliver efficient services to the financial sector and improvements to the financial market infrastructure would restore confidence in the banking sector. No formal economic analyses were presented to support these arguments. The ICR did not present an economic analysis of the project either, although it submitted that: (a) the establishment of critical payment and credit infrastructure would lay the foundation for financial system development which was critical for economic development; and (b) financial stability and access to finance would expand opportunities for the poor and the vulnerable through savings, credit, and payments, leading to better economic opportunities for all.

Operational Efficiency. The project's operation needed to be efficient to be successful, but, according to the ICR (paragraphs 44-46, pages 15-16), the project was marked by operational inefficiencies.

- Procurement and contract management were problematic: (a) the project staff lacked the capacity to develop technical specifications and manage complex procurement processes, despite implementation support from the Bank task team; (b) every procurement package required layers of high-level institutional approval --- each stage of the procurement process required review and approval by the DAB Governor's Office, leaving the project directors without any authority to approve or sign project documents; (c) the creation and organization of the procurement evaluation teams took considerable time and effort --- the evaluation team for each procurement contract required the approval by DAB department directors and the DAB Governor; (d) there was a lack of interest from qualified bidders due to security challenges and complex logistical arrangements that hindered travel; and (e) procurement and contract management disputes resulted in numerous rounds of advertisement or rebidding, leading to substantial delays.
- There was a high turn-over of project staff: (a) there were four Project Implementation Cell directors over 2017-2019; (b) all project directors were civil servants with other responsibilities apart from those with the project, resulting in capacity constraints; (c) in early 2017, the project director was promoted and assigned to the DAB human resources department; (d) a new project director was appointed but resigned before the expiration of the12-month appointment; (e) another project director was hired in November 2018 but was moved to a different DAB department in June 2019.
- The project did not complete any of the activities planned under the fourth restructuring and second additional financing of October 2016. The procurement activities could not be completed before project closing and the project was unable to utilize US$23.6 million of the project funds. This amount was subsequently cancelled through a restructuring ahead of the project closing date.

## Efficiency Rating

Modest

a. If available, enter the Economic Rate of Return (ERR) and/or Financial Rate of Return (FRR) at appraisal and the re-estimated value at evaluation:

| | Rate Available? | Point value (%) | *Coverage/Scope (%) |
|---|---|---|---|
| Appraisal | | 0 | 0<br>☐ Not Applicable |
| ICR Estimate | | 0 | 0<br>☐ Not Applicable |

* Refers to percent of total project cost for which ERR/FRR was calculated.

## 6. Outcome

The overall outcome rating for the project is moderately unsatisfactory  The rationale for this rating is that the relevance of objectives was substantial, with the project objectives being: responsive to deficiencies in banking supervision by the DAB and to problems with the outdated national payment system; consistent with the government's *Afghanistan National Development Strategy 2008-2013* and the *Afghanistan National Peace and Development Strategy 2017-2021;* and aligned with the Bank Group *Interim Strategy Note for the Islamic Republic of Afghanistan for the Period FY09-FY11* and *Country Partnership Framework for the Islamic Republic of Afghanistan for the Period FY17 to FY20*.  The overall efficacy of the project's achievements towards the original objective and the revised objective were both modest.  The project's efficiency was assessed as modest because of the lack of evidence available to assess economic efficiency as well as a poor record on operational efficiency, marked by major procurement and contract management problems, a high-turnover rate in project management leadership, an inability to complete many project activities, and a failure to disburse 47 percent of the project financing.  These elements in the project's performance are presented in the table below.  It shows that the project's overall outcome is moderately unsatisfactory indicating significant shortcomings in the achievement of its efficacy, efficiency and relevance.

**Overall Outcome Ratings**

| Rating Dimension | Original Objectives | Objectives After First Revision |
|---|---|---|
| Relevance of Objectives | Substantial | |
| Efficacy | | |
| Objective 1: To assist DAB to develop actions plans for improved banking supervision. | Modest | |
| Objective 1 - Revision 1: To assist DAB to develop actions plans for improved banking supervision. | | Modest |
| Objective 2: To assist DAB to implement a modern national payment system for efficient and transparent payment transactions. | Modest | |
| Objective 2 - Revision 1: To assist DAB to establish key building blocks of the financial sector | | Substantial |

| | | |
|---|---|---|
| infrastructure: payment system, movable collateral registry, and public credit registry. | | |
| Overall Efficacy | Modest | Modest |
| Efficiency | Modest | |
| Outcome Rating | Moderately Unsatisfactory | Moderately Unsatisfactory |
| Outcome Rating Value | 3 | 3 |
| Amount Disbursed, US$ million | 5.61 | 16.46 |
| Disbursement, percent | 25.4 | 74.6 |
| Weight Value | 0.76 | 2.38 |
| Total Weights | 3.14 | |
| Overall Outcome Rating | Moderately Unsatisfactory | |

### a. Outcome Rating

Moderately Unsatisfactory

## 7. Risk to Development Outcome

Afghanistan faces multiple risks in sustaining the development outcome of this project. Several measures, supported by international donors, are helping the government address some of these risks.

Operational and Financial Risk. Although the key elements of the national payment system have been installed and are deployed, there are serious risks to their operational sustainability. The Afghanistan Payments System is underutilized with only six of 12 commercial banks and one of four mobile network operators participating in the card and mobile payment switch. The Automated Transfer System is not fully automated as the integration of the system with commercial banks has not been completed. The operational underperformance implies that the financial sustainability of these system is also at risk, earning less than the expected revenues that would support operations. Similarly, the DAB faces financial constraints maintaining the Movable Collateral Registry.

Political Risk. Afghanistan remains in a "high-intensity conflict" situation, according to the Bank, which reports annually on fragile and conflict-affected situations globally. The level of violence in the country remains elevated, notwithstanding the signing of the "Agreement for Bringing Peace to Afghanistan" between the U.S. and the Taliban in February 2020. After a promising start, negotiations between the government and the Taliban have stalled in an impasse over sensitive procedural questions including Islamic law. Meanwhile, plans for the withdrawal of the last remaining U.S. troops and NATO forces are stirring fears of renewed large-scale conflict.

Macroeconomic Risk. Afghanistan is still a fragile and aid-dependent country, where insecurity combined with episodes of political uncertainty and adverse weather events have kept real GDP growth low in recent years. As in the past, continued financial assistance from international partners is critical to helping the government pursue its economic objectives, including inclusive growth, poverty reduction, and selfreliance. The IMF and the government reached a staff-level agreement in August 2020 on an economic reform program to be supported by a new three-and-half year SDR 259 million (US$364 million) arrangement under the Extended Credit Facility. Building on the 2016-19 Extended Credit Facility program that was successfully completed in December 2019, the new arrangement will focus on addressing structural fragilities that hamper growth, economic resilience, and equitable social outcomes.

Covid-19 Risk. The Covid-19 pandemic has inflicted heavy damage on the Afghan economy, which is expected to contract by about 5 percent in 2020, leading to a rise in unemployment and poverty. The authorities have taken emergency measures to respond to the pandemic, boosting critical health spending and rolling out social assistance to households hit hard by the crisis. The IMF approved Afghanistan's request for emergency assistance in May 2020 with the disbursement of SDR 161.9 million (US$220 million equivalent) under the Rapid Credit Facility to help meet the urgent fiscal and balance of payments needs stemming from the crisis. The Bank also approved the Afghanistan Covid-19 Response Development Policy Grant in July 2020, with US$100 million from the IDA and US$100 million from the Afghanistan Reconstruction Trust Fund, to help the government strengthen policies that promote faster recovery and keep basic infrastructure such as water, electricity, and telecommunications afloat and running.

## 8. Assessment of Bank Performance

### a. Quality-at-Entry

Prompted by the Kabul Bank crisis of 2010-11, the project was prepared promptly, in three months. It was also prepared in accordance with the Bank's *Rapid Response to Crises and Emergencies Policy* (Operational Policies and Bank Procedures (OP/BP) 8.00).

The project's design was informed not only by insights drawn from the Kabul Bank crisis (see Section 3), but also by lessons learned from the FSSP and from a separate analytic work on the country's payment system.

- The project succeeded the FSSP, approved in 2009 and scheduled to close in 2014, which aimed "to help the DAB improve its core function of banking supervision and regulation and to help improve access to formal banking services by establishing the key building blocks for further financial sector reform." According to the ICR (page 8), the design of the FSSP had been overly ambitious. In contrast, the scope of this project was more focused, aiming to help the DAB "to develop actions plans for improved banking supervision and implement a modern national payment system."
- The project would eventually carry over two activities initiated but not completed by the FSSP --- the creation and operationalization of the Public Credit Registry and the Movable Collateral Registry. The Bank and the DAB considered it necessary to expand the project development objective. The objective of this project "to assist DAB to establish key building blocks of financial sector infrastructure: payment system, movable collateral registry, and public credit registry" was more specific and focused than the objective of the FSSP "to help improve access to formal banking services by establishing the key building blocks for further financial sector reform."
- The project also benefitted from the FSSP having previously created the institutions to help improve bank supervision, namely the Afghanistan Institute of Banking and Finance, and to

strengthen the national payment system, namely the Afghanistan Payments System (see Section 2.D).

- The design for the national payment system was informed by the assessment done by the Bank's Payment System Development Group in 2010 on the Afghanistan National Payment System, part of the South Asia Strengthening Payments, Remittances and Securities Settlement Systems Project, funded by the multi-donor trust fund Financial Sector Reform and Strengthening Initiative. The study recommended the creation of the Automated Transfer System, including the Real-Time Gross Settlement System and the Automated Clearing House, to replace the Afghanistan Clearing and Settlement System for processing all electronic payments in the country. The other key findings and recommendations of the assessment were summarized in an appendix to the original Project Paper (pages 19-20).

The Bank conducted a comprehensive analysis of the operational risks faced by the project and offered measures to mitigate the risks. The Project Paper (pages 25-31) rated country risk, economic management risk, security risk, "systemic corruption" risk, and "delivery quality" risk as "high".

- To mitigate "delivery quality" risk, the Project Paper recommended that government and the Bank: (a) ensure high quality terms of references, (b) ensure the high quality of short lists, and if a short list were not satisfactory, to re-advertise the assignment, (c) provide a provision for security costs in the request for proposal for critical assignments, (d) rely on firms rather than individuals for critical assignments, for which security would be easier to provide; (e) closely monitor the work of the consultants and firms and take remedial actions early on.
- To mitigate "systemic corruption" risk, the Project Paper recommended that the Bank: (a) support strengthening the public accounting and auditing systems; (b) support tax administration reforms; (c) provide strong upstream project preparation assistance, including for procurement; (d) provide strong support to sectors more susceptible to corruption, with a strong focus on transparency; (e) broaden and strengthen the policy dialogue with government on achieving greater transparency and public accountability in government transactions.

### Quality-at-Entry Rating
Satisfactory

## b. Quality of supervision

The Bank relied on two institutional arrangements for the implementation of the project, drawn from the FSSP. The Project Steering Committee, chaired by the DAB Governor and including the heads of all DAB departments involved in the project, would provide strategic guidance and managerial direction for the project and oversee its implementation. The Project Implementation Cell, led by the Project Director, would be responsible for the preparation of the annual work program, the coordination of the work by the DAB departments, and the provision of technical and supervision support for project implementation.

On one hand, there were particular strengths with Bank supervision.

- The Bank provided implementation support through regular official supervision missions and frequent virtual engagement with the Project Steering Committee and the Project Implementation

Cell. The conduct of the missions was facilitated by the low turnover of project task team leaders (two task team leaders over nine years) and their frequent travel from duty stations in Kabul, Delhi, Dubai and Washington DC. The Bank prepared 12 Implementation Status and Results Reports over the eight-year life of the project.

- In addition, the Bank provided programmatic advisory services and analytics, under which task teams delivered technical assistance and capability development services to the DAB. The Afghanistan Financial Sector Development Project delivered several technical assistance activities to help build the digital payment system, improve the institutional capacity of the DAB, and promote the broader financial sector stability objective. The key outputs included: a Banking Sector Review, covering the legal and regulatory framework for banking; advice on corporate governance and risk-management at the DAB; and an assessment and action plan for digital finance, as listed in the ICR (paragraph 63, page 19).
- The Bank also engaged the government in policy dialogue. The staff proactively identified emerging issues which were subsequently addressed through five restructurings, including two additional financing initiatives, each expanding the scope of the project with activities aligned with the project objectives.

On the other hand, there were also significant deficiencies.

- Formal supervision documents, notably Aide Memoires, which were important for relaying the progress with the project implementation to the government, were not prepared bi-annually as normally expected Only one Aide Memoire was filed in each of the last two years, 2018 and 2019, when project implementation experienced substantial delays.
- The Bank task team downgraded the rating for project implementation only in the last Implementation Status and Results Report, rather than when the project started to face implementation challenges.
- According to the ICR (paragraph 26, page 12; paragraph 54, page 18; and paragraph 61, page 19), the institutional capacity of the DAB for procurement was not well vetted, particularly for procurement related to the fourth restructuring and second additional financing. At that time, the project management functions of the Project Implementation Cell, which was dissolved in 2016, were transferred to various departments at the DAB. These departments had limited experience with procurement, hindering progress with the implementation of the Core Banking System, Enterprise Resource Planning, and Data Warehouse.

### Quality of Supervision Rating
Moderately Satisfactory

### Overall Bank Performance Rating
Moderately Satisfactory

## 9. M&E Design, Implementation, & Utilization

## a. M&E Design

The Financing Agreement called for the DAB, as project implementing entity, to monitor and evaluate the progress of the project and to prepare: (a) quarterly project reports containing the project M&E data, and (b) monthly reports containing the detailed balance sheet data of the commercial banks covered by the project.

The original Project Paper listed one outcome and two output indicators for the objective to develop action plans for improved banking supervision, and one outcome and four output indicators for the objective to implement a modern national payment system for efficient and transparent payment transactions.

- The outcome indicator for the first objective --- that the "commercial banking sector was strengthened following implementation of action plans developed based on the findings of the audits, with support and oversight of DAB" --- was not well defined and gave no indication on how it would be measured.
- The outcome indicator for the second objective --- that the "payment system conformed to international norms, as established by the Bank for International Settlements and the Payment Systems Development Group of the Bank, by the end of project, contributing to safety and efficiency of the financial sector" --- was better defined, specifying the use of Bank for International Settlements and Bank data to determine "conformity with international norms."

The revision of the project objectives and expansion of the project components following five restructuring episodes revised the set of results indicators for the project. The final set consisted of one outcome and nine output indicators for the objective "to develop action plans for improved banking supervision" and one outcome and six output indicators for the objective "to establish key building blocks of financial sector infrastructure: payment system, movable collateral registry, and public credit registry."

- There was no outcome indicator for the activities related to strengthening the DAB's institutional and technical capacity for banking regulation and supervision.
- The single outcome indicator for the second objective --- that the "payment system conformed to international norms" --- pertained only to the first of three financial sector infrastructure components supported by the project. The other two, covering the Public Credit Registry and the Movable Collateral Registry, had output indicators and had no outcome indicators, although outcome indicators could have been readily defined for these project interventions.

## b. M&E Implementation

According to the ICR (page 18), there were no shortcomings in the quality of the data reported but the reporting was irregular. Many indicators in the results framework were qualitative in nature, monitoring whether a specific event occurred, and there was no need to design a sophisticated management information system to collect and analyze the project data.

## c. M&E Utilization

According to the ICR (page 18), while the data collected under the M&E plan were utilized to inform management decisions on issues related to the restructuring such as revising the project components and extending the project duration, challenges were observed with preparation of quarterly and annual progress reports. These reflected challenges with the capacity of both the DAB and the Project Implementation Cell to perform their M&E functions. In particular, progress reports submitted by the Project Implementation Cell were often late or irregular.

### M&E Quality Rating

Modest

## 10. Other Issues

### a. Safeguards

Environmental Safeguards. The project was classified as an Environmental Assessment Category "C" project at appraisal, for which no environmental review was required. The category classification was not revised during restructuring. According to the ICR (page 18), no environmental compliance issues were recorded during project implementation.

Social Safeguards. No social safeguards issues were raised or discussed at appraisal and during project implementation.

### b. Fiduciary Compliance

Procurement. The Financing Agreements for this operation required: (a) compliance with the *Guidelines: Procurement of Goods, Works and Non-Consulting Services under IBRD Loans and IDA Credits and Grants by World Bank Borrowers* and the *Guidelines: Selection and Employment of Consultants under IBRD Loans and IDA Credits and Grants by World Bank Borrowers;* and (b) the use of international competitive bidding for the procurement of goods and non-consulting services and quality- and cost-based selection for the procurement of consultant services. Other methods of procurement would have to be specified in a Procurement Plan. Moreover, the Procurement Plan would have to specify contracts requiring prior review by the IDA; all other contracts would be subject to post review by the IDA. The ICR (page 19) reports that during implementation, several issues and complaints related to procurement and to the management of several contracts were referred to Bank's Integrity Vice Presidency (see Section 5). The last Implementation Status and Results Report rated procurement as unsatisfactory.

Financial Management. The Financing Agreements required: (a) compliance with the *International Development Association General Conditions for Credits and Grants* and the *World Bank Disbursement Guidelines for Projects* for the withdrawal of the proceeds of the financing and for the financing of eligible expenditures; (b) the conclusion of the Afghanistan Payments System Sub-Grant Agreement between the DAB and the Afghanistan Payments System and the submission to, and approval by, the IDA of the Afghanistan Payments System Sustainability Plan; (c) the submission by the DAB to the IDA of quarterly interim unaudited financial reports for the project; and (d) the submission by the government to the IDA of annual audited financial statements. The ICR did not discuss any issues related to financial management during project implementation. This was surprising sine the last Implementation Status and Results Report rated financial management as moderately unsatisfactory.

### c. Unintended impacts (Positive or Negative)

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### d. Other

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## 11. Ratings

| Ratings | ICR | IEG | Reason for Disagreements/Comment |
|---|---|---|---|
| Outcome | Moderately Unsatisfactory | Moderately Unsatisfactory | |
| Bank Performance | Moderately Satisfactory | Moderately Satisfactory | |
| Quality of M&E | Modest | Modest | |
| Quality of ICR | --- | Substantial | |

## 12. Lessons

Three lessons are drawn from the ICR (pages 20-21), with some adaptation.

**The development outcomes of project interventions are likely at risk without proactive steps to ensure their post-project operational sustainability.** In this project, the card and mobile payment switch at the Afghanistan Payments System remains underutilized. The Automated Transfer System is half-operational. And the Collateral Registry has not been adequately maintained. The lesson is that measures for strengthening operational sustainability include: (a) cost recovery schemes; (b) options to shift responsibility over operational costs to government budgets; and (c) legal covenants mandating national rather than donor responsibility over operations. Incentives for banks to participate in an Automated Payment System include: (a) a fee structure that incentivizes the timely submission of payment transactions; (b) collateralized liquidity support to mitigate liquidity risk; and (c) settlement guarantee mechanisms.

**The complexity of projects needs careful consideration in fragile and conflict-affected settings.** In this project, the creation of a new modern national payment system tested not only the political commitment of the government and the institutional and technical capacity of the central bank but also the business judgment of banks and financial services providers and the operational ability of technology suppliers and technical consultants to bid for projects and deliver on contracts. More extensive planning and stakeholder consultation at the design stage, including for contingencies in a wide range of adverse conditions, would have helped the government and the Bank prepare for a rough project implementation. However, scaling down the scope and scale of the project to what could be reasonably achieved in a fragile and conflict-affected setting would have been a better alternative. In this project, the central bank was loaded with too many mandates compared with its staff and financial capacity. The lesson is that reducing the scope and scale of a project to what can be reasonably achieved in an fragile and conflict-affected setting is the best strategy.

**The inability to contract for, and to obtain the delivery of, quality consulting services can derail the implementation of technical assistance-intensive project activities.** In this project, the contracting for consultant services proved to be difficult, delaying the delivery of technical assistance to key institutions and derailing the initiation and completion of several project activities. According to the ICR (page 20), problems with the procurement and delivery of consulting services were not unique to this project but are prevalent across Afghanistan owing to the difficult security situation in the country. The lesson is that at project design, consideration needs to be given to permitting consultants to use technology (audio and video conferences, remote communications, rather than in-person appearances) to deliver technical services, encouraging consultants, who would otherwise be deterred by difficult travel and living arrangements, to bid for projects. Another lesson, during implementation, was that more extensive use of the hands-on extended implementation support mechanism, in which the Bank deploys a dedicated procurement specialist to provide close support to implementing agencies throughout the procurement process, can be a successful option.

## 13. Assessment Recommended?

No

## 14. Comments on Quality of ICR

The ICR presents a succinct and results-focused record of the project, in line with OPCS guidelines for the preparation of ICRs. Changes to the project objectives and components are well summarized in pages 6-9, the final set of results indicators is concisely presented, and the outputs and outcomes of the project are concisely recorded.

The assessment of efficacy is candid. The conclusion was that the facilities for improved banking supervision, the National Payment System, the Movable Collateral Registry, and the Public Credit Registry were all established by the Afghanistan Payments System and DAB, but the operational sustainability of these innovations remain questionable. Many activities aiming to strengthen the institutional capacity of the DAB, such as the implementation of the International Financial Reporting Standards, was not achieved.

The assessment of efficacy is more comprehensive than that required by the simple monitoring of the results indicators, given the weak M&E design for the project. The discussion of operational efficiency is well grounded, covering problems with procurement and contract management and the staffing of the project management function. However, there is no discussion of financial management, which at the end of the project's implementation was rated moderately unsatisfactory by supervision missions..

The lessons offered by the ICR are useful.

**a. Quality of ICR Rating**
Substantial