Report Number : ICRR13234

IEG ICR Review
Independent Evaluation Group

1. Project Data:		Date Posted :	10/23/2009	
PROJ ID :	P098548		Appraisal	Actual
Project Name :	Second Programmatic Development Policy Loan	Project Costs (US$M):	30.0	34.1
Country:	Macedonia	Loan/Credit (US$M):	30.0	34.1
Sector Board :	EP	Cofinancing (US$M):	10.9	10.8
Sector(s):	General public administration sector (34%) Law and justice (22%) General industry and trade sector (22%) Compulsory health finance (22%)			
Theme(s):	Administrative and civil service reform (29% - P) Legal institutions for a market economy (29% - P) Corporate governance (14% - S) Health system performance (14% - S) Regulation and competition policy (14% - S)			
L/C Number:	L7441			
		Board Approval Date :		03/27/2007
Partners involved :		Closing Date :	12/31/2007	12/31/2007

Evaluator :	Panel Reviewer :	Group Manager :	Group :
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2. Project Objectives and Components:

a. Objectives:

The overall objective of the Programmatic Development Policy Loan program for Macedonia was to assist the government's efforts to promote economic growth and job creation by supporting reforms to (a) improve the investment climate and (b) strengthen governance and efficiency of the public sector . The program consisted of three consecutive loans approved in FY 06, FY07 and FY08, all three with the same objectives and components . This ICR review covers the second loan of the series .

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

No

c. Components (or Key Conditions in the case of DPLs, as appropriate):

The two policy areas of the loan - the investment climate, and governance and efficiency of the public sector - had the following components.

Improving the Investment Climate

1. Judicial reform, to achieve more efficient and effective enforcement of contract, creditor and property rights by courts and enforcement institutions.
2. Labor market reform, to achieve more labor market flexibility.
3. Strengthening financial sector regulation and supervision, through instituting risk - based supervision and accounting reform in banks.
4. Improving the business environment, by eliminating unnecessary regulations and lowering the costs of procedures related to businesses.

Strengthening Governance and Efficiency of the Public Sector

1. Public administration reform, to introduce more effective strategic management and professionalize the civil service.
2. Health sector reform, to improve financial management, transparency and governance of the sector and especially of the Health Insurance Fund (HIF), including procurement of medicines. Despite earlier reforms supported by the Bank, the HIF posed a continuing fiscal risk to the government budget.
3. Decentralization, in support of sustainability of local governments, especially by settling arrears.

d. Comments on Project Cost, Financing, Borrower Contribution, and Dates:

PDPL 2 was approved on March 27, 2007 for US$30 million equivalent (denominated in Euros, IBRD), disbursed upon effectiveness, and closed on schedule on December 31, 2007.

Cofinancing was provided by the Netherlands in the amount of Euro 7 million.

3. Relevance of Objectives & Design:

The program objectives and design were highly relevant. The objectives were well-aligned with the FY04-06 CAS and the FY07-10 CPS. The main pillars of the CPS - foster economic growth and job creation, and improve public service delivery while promoting good governance - paralleled the objectives of the PDPL program, and both ultimately aimed at helping the government achieve its goal of integration with the EU. (Macedonia was granted EU accession candidate status in Nov. 2005).

The PDPL program also closely mirrored the government's reform agenda laid out in several strategic documents. The design of the program was built to follow through on earlier Bank support for improved public sector management (a FY03 Public Sector Management Adjustment Credit and a FY04 Public Sector Management Adjustment Loan), and was expanded to include a focus on obstacles which impeded private sector development, i.e. judicial and labor market reforms, financial sector development and the overall business climate. The strategy embedded in the series of three loans was to first encourage the adoption of new loans to provide a basis for reform and then focus on implementation. Accordingly, the six actions prior to Board presentation for PDPL 1 all dealt with new laws or amendments, of the nine prior actions for PDPL 2 four dealt with laws, and of the eight prior actions for PDPL 3 only two concerned laws. Other prior actions focused on building capacity, implementation or adoption of action plans.

4. Achievement of Objectives (Efficacy):

All prior actions in the program were complied with and there was improvement both in the overall investment climate and in the efficiency and governance of the public sector, as a result of the program's impact in strengthening the necessary legal framework and building implementation capacity.

While it is difficult to establish causality, there is at least a plausible association between the program's achievements and macroeconomic outcomes which included increased growth and investment as well as reduced unemployment, until the 2009 downturn associated with the global economic crisis, when growth turned negative and investment dropped. Real GDP growth rose from 3 percent in 2003/2004 to 4 percent in 2006 and 5.9 percent in 2007. The investment to GDP ratio grew from less than 21 percent in 2003/2004 to 21.9 percent in 2006 and 24.2 percent in 2007. Unemployment which was estimated at 36.3 percent in 2006, dropped slightly to 35.2 percent in 2007.

The Investment Climate

1. Judicial Reform

The expected outcome was more efficient and effective enforcement of contract, creditor and property rights by courts and enforcement institutions. New laws adopted under PDPL 1 included laws on Civil Procedure, on Enforcement, on Bankruptcy and on Cental Administrative Procedure. Under PDPL 2, new laws on Courts and on Administrative Disputes were adopted and a Chamber of Enforcement Agents was created. By the end of the program judicial efficiency had increased: 22 of the 27 basic courts recorded a reduction in backlogs of court proceedings, enforcement of court cases increased from 18 percent in 2005 to 39 percent in 2009, and the average duration of bankruptcy procedures had fallen from 3 years and 7 months to two years and 2 months. Efficacy is rated *substantial.*

2. Labor Market Reform

The expected outcome was increased labor market flexibility. Under PDPL 1 a new Labor Relations Law was enacted to facilitate market flexibility. Under PDPL 2 a legislative framework establishing alternative labor dispute resolution mechanisms was drafted. By the end of the program there was some small reduction in unemployment rates, and there was an increase in the share of the labor force with part -time and fixed term contracts: fixed term contracts increased from 43.3 percent of the labor force in 2004 to 57.6 percent in 2008. Efficacy is rated *substantial.*

3. Financial Sector Regulation and Supervision

The expected outcome was strengthened banking regulation and supervision, as well as improved transparency and governance. Under PDPL 1 a diagnostic of the bank supervisory process and an assessment of banks' governance resulted in the adoption of a Supervisory Development Plan (SDP) to help supervisors move towards a more risk-based supervisory approach and strengthen governance. Under PDPL 2 implementation of the SDP proceeded with assistance from an IMF sponsored resident advisor, and a new Banking Law and amended Central Bank Law were adopted. Also, stronger anti-money laundering policies and procedures were adopted. While the results of these reforms are not immediately visible, financial intermediation as measured by the credit to GDP ratio increased over the period. Efficacy for this components is rated *substantial.*

4. Business Environment

The expected outcome was an improved business environment. A report on the Observance of Standards and Codes (ROSC) was finalized in 2005 and a new corporate Audit Law was adopted under PDPL 1. Under PDPL 2 key ROSC recommendations were implemented, a "guillotine" process was launched to quickly eliminate unnecessary, illegal or business-unfriendly regulations, a Business Registration Law became effective and implementation of the Audit Law got underway. By the end of the program, Macedonia's ranking in the Doing Business survey had improved from 81 (out of 155) in 2006 to 71 (out of 181) in 2009. Other indicators such as the time and cost of registering a business also improved, and the number of registered businesses increased substantially. Efficacy for this component is rated *substantial.*

Public Sector Governance and Efficiency

1. Public Sector Administration

The expected outcomes were more effective strategic management and professionalization of the civil service. Under PDPL 1 all (but one) ministries completed strategic plans, civil service recruitment was embedded in a new organic budget law, and a policy of decompression of salaries was continued. Under PDPL 2 the ministries' strategic plans were implemented, a strategic plan for the civil service was prepared and a draft Law on Public Wages was further amended. In terms of outcomes, however, the ministries' strategic plans were poorly linked to budget proposals and salary reform proved to be politically more difficult than expected. Efficacy for this component is rated *negligible.*

2. Health Reform

The main expected outcome was improved financial management, transparency and governance of the Health Insurance Fund (HIF), especially in the area of procurement of medicines. Under PDPL 1 a new Health Insurance Law was submitted to Parliament and financial reporting to improve transparency was initiated. Under PDPL 2 the Health Insurance Law was adopted as was a National Health Strategy, and implementation of a plan to sanitize health sector finances was initiated. By the end of the program, improvement in the procurement of medicines was a major achievement, which led to considerable savings. There was also much progress in resolving the arrears of the HIF and of health care institutions. Efficacy for this component is rated *substantial.*

3. Decentralization

The expected outcome was achievement of financially viable local governments. A formula for revenue sharing was adopted under PDPL 1 as was a strategy reducing municipal arrears. PDPL 2 continued to support these initiatives. Sixty municipalities were able to settle arrears by end-2007, leaving 26 municipalities which had not yet cleared their arrears. The revenue-sharing formula is now well-established and there has been a substantial reduction in municipal arrears. Efficacy for this component is rated *substantial.*

5. Efficiency (not applicable to DPLs):

N.A.

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

	Rate Available?	Point Value	Coverage/Scope*
Appraisal		%	%
ICR estimate		%	%

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

6. Outcome:

The PDPL program for Macedonia was highly relevant because the issues which it addressed - the investment climate and public sector efficiency and governance - were important constraints to Macedonia's development and its prospects for eventual EU accession. While the components of the program were fairly modest, i.e. primarily adoption of new laws and their implementation, they were important preconditions for development and, on average, they were achieved with substantial efficacy.

a. Outcome Rating : Satisfactory

7. Rationale for Risk to Development Outcome Rating:

The PDPL program's achievements are being reinforced by continuing Bank and other donor assistance to further strengthen the investment climate and public sector efficiency and governance. Government commitment to these objectives remains strong largely because of the prospects of eventual EU accession, which will necessitate continued progress in the various component areas of the PDPL program. At this juncture, the global economic crisis is having a substantial negative impact on the macroeconomy but, on the positive side, Macedonia's financial sector appears to be relatively sound, and the government has continued to pursue its reform efforts after completion of the PDPL program.

a. Risk to Development Outcome Rating : Moderate

8. Assessment of Bank Performance:

The program was a continuation of earlier Bank assistance, was designed on the basis of good ESW, and implemented in coordination with other donors. Close cooperation with government counterparts and other donors, together with continuity in the Bank's team, assured effective supervision . In some areas, such as procurement of medicines, or settlement of municipal arrears, it was primarily because of the Bank team's firm adherence to objectives and power of persuasion with counterparts that effective solutions could be found.

a. Ensuring Quality -at-Entry:Satisfactory

b. Quality of Supervision :Satisfactory

c. Overall Bank Performance :Satisfactory

9. Assessment of Borrower Performance:

All prior actions were fulfilled and followed through upon without major controversy . Government commitment to the reforms was strong as exemplified by its rapid implementation of the regulatory "guillotine" and its insistence on procurement discipline in the health sector . Capacity development in implementing agencies was substantial and was a major benefit of the program in several agencies, notably the HIF, the ministry of labor and the Central Bank .

a. Government Performance :Satisfactory

b. Implementing Agency Performance :Satisfactory

c. Overall Borrower Performance :Satisfactory

10. M&E Design, Implementation, & Utilization:

Monitoring and evaluation indicators were identified but were not designed to be systematically measured in the framework of a results matrix, expect for the civil service component . As a result here was no effective implementation of an M & E framework, At the same time, data on progress in the various components were available from a variety of sources (USAID reports, EU progress reports) and were used in the ICR to measure progress towards objectives.

a. M&E Quality Rating : Modest

11. Other Issues (Safeguards, Fiduciary, Unintended Positive and Negative Impacts):

12. Ratings:	ICR	IEG Review	Reason for Disagreement /Comments
Outcome:	Satisfactory	Satisfactory	
Risk to Development Outcome:	Moderate	Moderate	
Bank Performance :	Satisfactory	Satisfactory	
Borrower Performance :	Satisfactory	Satisfactory	
Quality of ICR :		Satisfactory	

NOTES:
- When insufficient information is provided by the Bank for IEG to

arrive at a clear rating, IEG will downgrade the relevant ratings as warranted beginning July 1, 2006.
- The "Reason for Disagreement/Comments" column could cross-reference other sections of the ICR Review, as appropriate .

13. Lessons:

A prime lesson from this program is that exogenous forces, in this case the prospect of eventual EU accession, can play a dominant role in assuring government commitment to reforms .

A second lesson is that continuity of champions for reform on the government side and continuity in Bank teams are essential for successful reform outcomes .

14. Assessment Recommended? ○ Yes ● No

15. Comments on Quality of ICR:

This is a clear, concise, and well-written ICR. The quality of evidence and the quality of analysis are both sufficient for an evaluation of the outcome of the program . The ICR conforms to Bank guidelines and is internally consistent. It does not provide details on the achievements at the three different stages of the program; some of this can be found in the program document for PDPL 3, but quantitative information on implementation outcomes is largely available only at the conclusion of the program, not at the conclusion of PDPL 1 and PDPL2.

a.Quality of ICR Rating : Satisfactory