

**PROJECT INFORMATION DOCUMENT (PID)  
CONCEPT STAGE**

Report No.: 85209

<b>Project Name</b>	Strengthening the Regulatory and Institutional Framework for Micro, Small, and Medium Enterprise Development
<b>Region</b>	Middle East and North Africa Region
<b>Sector</b>	SME Finance (60%), Microfinance (40%)
<b>Project ID</b>	P147875
<b>Borrower(s)</b>	Government of the Hashemite Kingdom of Jordan
<b>Implementing Agency</b>	Central Bank of Jordan
<b>Environment Category</b>	<input type="checkbox"/> A <input type="checkbox"/> B <input checked="" type="checkbox"/> C <input type="checkbox"/> FI <input type="checkbox"/> TBD (to be determined)
<b>Date PID Prepared</b>	September 16, 2013
<b>Estimated Date of Appraisal Authorization</b>	October 17, 2013
<b>Estimated Date of Board Approval</b>	November 7, 2013

**1. Key development issues and value added of World Bank Group Support**

The proposed operation will foster a more efficient and conducive ecosystem for Micro, Small, and Medium Enterprises (MSMEs) in Jordan, through regulatory and institutional reforms that are transformational in terms of not only enhancing access to MSMEs, but also attaining a fair and more transparent system. This would be achieved by addressing major deficiencies in the financial infrastructure, through improving credit guarantee schemes, protecting the rights of financial consumers and ensuring transparency and access to information, and ameliorating the institutional and regulatory framework of the microfinance sector. The project will also ensure gender mainstreaming throughout its three components.

The operation will be utilized to strengthen credit guarantee schemes that would ultimately encourage banks to lend to MSMEs. The design of new guarantee products tailored to SMEs, which are based on proper risk analysis, will promote Jordan Loan Guarantee Corporate's (JLGC) operations development and sustainability. This will facilitate access to finance for creditworthy firms, when such access is constrained by insufficient credit information and collaterals through reducing the risk and potential losses of creditors, inducing lending to SMEs that are considered more risky by banks. Through focusing on marginalized groups and underserved areas, this component will enhance access to SMEs financing through mitigating the risk.

The project aims at enhancing consumer protection instructions, in order to ensure the protection of the rights of financial consumers and to guarantee a strong, competitive market, as well as to shield consumers from fraud and deception, and to promote transparency and easy access to information. The Central Bank of Jordan (CBJ) has shown strong commitment towards creating a reliable and strong consumer protection system and acknowledges the importance of disclosure, transparency and recourse systems in protecting the rights of financial consumers. The CBJ's newly approved instruction, "Treating Customers Fairly", covers the most critical

bases in a comprehensive and clear approach, to substitute the current fragmented set of rules found in different laws and circulars.

Strengthening the regulatory and institutional framework for microfinance institutions will have a positive impact on the soundness of micro finance institutions (MFIs) and their ability to borrow and on-lend to micro enterprises. This will also increase the numbers of MFIs and micro-borrowers, which will contribute in alleviating poverty and inequality, as their expansion will allow for more outreach in the underserved Governorates, beyond Amman and the main cities. The regulatory framework could ultimately enable MFIs to offer various financial services such as payments and remittances.

The activities expected to be undertaken under this operation would create a more enabling environment for MSMEs and lead to more sustainable private-sector led growth. Improving the regulatory framework will facilitate access to finance and increase the efficiency and competitiveness of the sector. Furthermore, enhancing credit guarantee scheme as well as ensuring consumer protection would ultimately lead to the development of a more transparent, inclusive and fair ecosystem.

The value-added the World Bank Group will bring forward is the cross country experience and regional knowledge, as well as international best practices. There has been extensive work done in the area of MSMEs development, ranging from International Bank for Reconstruction and Development (IBRD) policy lending, to advisory services and technical assistance under the World Bank-IFC Middle East and North Africa (MENA) Regional MSME Facility, as well as the work done to date by the International Financial Cooperation (IFC), and Consultative Group to Assist the Poor (CGAP) technical support across a number of key priority areas to this project. IFC and CGAP, with their extensive experience in supporting reform initiatives and body of global lessons, together with their links to a wide network of international practitioners and other donor agency partners, are further key assets that the CBJ is looking to the World Bank project team to provide, as part of the collaboration on this initiative. The Arab Fund for Economic and Social Development (AFESD) brings in their extensive knowledge of the region, and their priority areas of reform. AFESD has also been providing line of credit to the Arab countries, and has experience in dealing with central banks, banks and apex institutions. AFESD with its competent and experienced leadership has great credibility in Jordan, and is entrusted by the authorities to develop the MSME sector. The World Bank will play a coordinators role, to ensure the most effective use of resources, tapping on the comparative advantage and expertise of the different institutions.

## **2. Proposed Objective**

The main objective of the project is to develop the legal, regulatory and institutional financial infrastructure to enhance financial services and products, as well as to strengthen financial protection mechanism targeting MSMEs.

## **3. Preliminary description**

The proposed project comprises of three main components: (i) strengthening credit guarantees schemes; (ii) enhancing the consumer protection mechanism; and (iii) developing the regulatory

and institutional framework for micro finance institutions. The total cost of the project is US\$ 3.5 million.

***Component I: Strengthening credit guarantees schemes (US\$ 1.5 million).***

This component aims at developing the JLGC SME loan guarantee products, and designing new ones that are tailored to SMEs and are based on proper risk analysis, which address the issues of moral hazard and adverse selection, with the objective of enhancing its operations development and sustainability. Activities under this component will build on the diagnostic work that was undertaken under the Jordan MSME Facility (Pillar I which is led by the World Bank, and IFC contributed with a detailed needs assessment finalized in April 2013), assessing the current system and putting forward phased recommendations. This project will focus on assisting JLGC in expanding its outreach and increasing the impact of its products, especially those targeting SMEs with a focus on marginalized groups, including women and underserved areas. At the same time, it will support JLGC in designing a guarantee product for micro-lending. Strengthening the credit guarantee mechanism will enhance MSMEs access to finance.

This would be delivered through technical assistance to JLGC, targeting six key areas of competencies to achieve scale, sustainability and efficiency, mainly in the areas of: segmentation, risk management, delivery model, payment rules, analytics and systems, organization and human resources. This component follows a phased approach:

***Phase I*** (8–10 months duration), aims at achieving transformational quick wins that would facilitate achieving key objectives within a limited time frame. This phase focuses on: (i) market demand research; (ii) product management; (iii) risk management; and (iv) marketing strategy and outreach plan. It is estimated that US\$ 600 thousand would be required to provide JLGC with all the resources and support needed to successfully complete the first phase.

***Phase II*** (4–6 months duration), will be scoped after Phase I delivery and finalization, whilst providing adequate assurance that key objectives are materialized and impact is being adequately assessed throughout the organization and with relevant stakeholders. This phase would cover: (i) payment rules; (ii) analytics and systems; and (iii) organization and human resources. The cost amounts to approximately US\$ 400 thousand.

In addition, there is a need for institutional reforms and capacity building of JLGC, in order to fully achieve a successful re-alignment of the organization with market demands, in terms of products, services and outreach, and to also get it on the path to long term sustainability. This would require additional funding amounting to US\$ 500 thousand. This would include, study tours for cross-regional support and knowledge-sharing from successful international loan-guarantee schemes. Hence, the total cost of the second component is US\$ 1.5 million.

***Component II: Enhancing the consumer protection mechanism (US\$ 1.2 million).***

This component aims at creating a reliable and strong consumer protection system in Jordan, which highlights the importance of disclosure, transparency and recourse system in protecting the rights of financial consumers. The objective is to operationalize the Treating Customers Fairly, CBJ Instructions No. 56 of 2012, which aims at promoting financial inclusion and consumer protection. The project will support the establishment of the Consumer Protection Unit at CBJ, as well as, build its capacity to perform its mandate in terms of ensuring financial

intermediaries compliance of these instructions, and empowering the unit to enforce such instructions. This component aims to guarantee that MSME clients are receiving timely and appropriate information, adequate service, that they are not subjected to improper behavior or corruption practices, and that financial intermediaries do not create unnecessary hurdles or discrimination. Furthermore, it will improve transparency, accountability and governance. It will also prevent abuse of the illiterate segment of the population, especially in the marginalized areas.

This will be delivered through: (i) conducting study tours on responsible finance and financial consumer protection; (ii) establishing a Consumer Protection Unit at CBJ to handle complaints; and (iii) providing capacity building to CBJ to use consumer research on a regular basis, to see if it is working and to identify barriers created by some financial institutions, such as minimum balance amount for opening a bank account. This will include techniques such as surveys, qualitative research (focus groups), mystery shopping, and analysis of complaints data. Furthermore, this component will also finance financial literacy programs through CBJ, informing the clients of their legal rights, giving them better understanding of the different financial products offered in the market.

Strengthening the capacity of the Consumer Protection Unit will enable it to enforce the following disclosure and accountability issues: (i) mandatory plain-language disclosures of all key prices/terms/conditions; (ii) requirement that all key information be stated in the contract; (iii) the required disclosure of total cost of credit (which analytical work has shown to be more comprehensible for many consumers including those with lower levels of education and financial sophistication); (iv) the specific requirements that no additional fees can be charged beyond those that are disclosed; and (v) the requirement that any variable pricing is explained clearly to the customer up-front and is based on observable benchmarks in the market.

***Component III: Developing the regulatory and institutional framework for micro finance institutions (US\$ 800 thousand).***

This component aims at supporting policy, legal and regulatory reforms to develop the micro finance sector. Recognizing the importance of its role as a financial regulator and supervisor, for not only banks but also for non-bank financial institutions (NBFIs), the CBJ took the decision to regulate and supervise the microfinance sector. This would entail setting a legal and regulatory framework that is conducive to micro finance, as well as institutional reforms that would allow CBJ to undertake such mandate.

The project will provide support to CBJ in drafting and finalizing the By-law, and the Executive Regulations, which will codify and regulate the MFI's ability to borrow—a key step that would foster the expansion of the micro sector, and ensure its compliance with the prudential regulations. The regulations would move all MFIs under the regulatory and supervisory umbrella of the CBJ, and at a later stage, all NBFIs. It will comprise of prudential rules with a focus on fit and proper requirements, strong governance rules, and internal and external controls. The regulation would also adopt general definitions for microfinance and for the permitted financial services to allow MFIs, pending the approval of the CBJ to engage in other financial services besides microcredit, such as micro savings and micro insurance. The project will also support CBJ in establishing a Microfinance Unit, which would be responsible for enforcing rules, ensuring compliance with the regulations, and supervising MFIs. This component will also finance capacity building of the Unit, and training of its staff.

#### **4. Safeguard policies that might apply**

The proposed project is classified as a Category C, as it is likely to have minimal or no adverse environmental impacts. No environmental safeguards instruments other than the Integrated Safeguards Data Sheet (ISDS) need to be prepared for this project. It is highly suggested that capacity building of financial intermediaries include training on the application of Jordan's Ministry of Environment's EIA regulation 37/2005 to sub-project screening and standard mitigation procedures.

#### **5. Tentative financing**

Source:	(\$m.)
Borrower	0
International Bank for Reconstruction and Development	3.50
<b>Total</b>	<b>3.50</b>

#### **6. Contact point**

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