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PROJECT PERFORMANCE ASSESSMENT REPORT

THE REPURLBIC OF MOZAMBIQUE

ENTERPRISE DEVELOPMENT PROJECT

(IDA-33170, IDA-3317A, EECT-28406, NORW-24286, UK-27799)

March 5, 2014

IEG Public Sector Evaluation
Independent Evaluation Group

Currency Equivalents (annual averages)

Currency Unit = Mozambique Metical

2001	US$1.00	MT20.65
2002	US$1.00	MT23.26
2003	US$1.00	MT23.28
2004	US$1.00	MT22.87
2005	US$1.00	MT24.00
2006	US$1.00	MT26.78
2007	US$1.00	MT25.72
2008	US$1.00	MT23.99
2009	US$1.00	MT26.50
2010	US$1.00	MT33.85
2011	US$1.00	MT28.80

Abbreviations and Acronyms

AdM	*Agua de Moçambique* (Mozambique water authority)
AMSME	Africa Micro Small and Medium Enterprise Finance Program
APDF	African Project Development Facility
APL	Adaptable Programs Loans
BAT	British American Tobacco
BCI	Banco Commercial de Investimento
CCAM	Center for Conciliation and Arbitration of Mozambique
CAE	*Confederação das Assoçiaões Economicas de Moçambique* (Confederation of Economic Associations)
CPI	*Centre de Promoçao do Investimento* (Center for Investment Promotion)
CPSDP/PACDE	Competitiveness and Private Sector Development Project / *Projeto de Apoio a Competitivade e do Sector Privado*
DCA	Development Credit Agreement
EDM	*Electricidade de Moçambique* (Mozambique electricity authority)
EDP	Enterprise Development Project (PoDE; *Projecto para o Desenvolvimento Empresarial*)
EFMTA	Economic and Financial Management Technical Assistance Project
FCO	Firm Competitiveness Office
FIAS	Foreign Investment Advisory Service
FSCB	Financial Sector Capacity Building Project
GAPI	*Sociedade de Promoção de Pequenos Investimentos* (ex-Gabinete de *Consultoria e Apoio à Pequena Industria*) sometimes known as *Sociedade de Promoção de Pequenas e Medias Empresas* (Company for the Promotion of Small and Small and Medium Enterprises)
GASP	*Grupo de Apoio ao Sector Privado*(Private Sector Support Group)
IDI	Irish Development Agency
IERP	Industrial Enterprise Restructuring Project
IEG	Independent Evaluation Group
INE	*Instituto Nacional do Estatistico* (National Statistical Office of Mozambique)
IPC	Investment Promotion Center
ISR	Implementation Status and Results Report
LOA	Loan Operations Accounting
LPO	Linkage Program Office
MBN	Mozambique Business Network
MICTUR	Ministry of Industry, Commerce and Tourism

MOZAL	Mozambique Aluminum Company
NBFI	Non-Bank Financial Intermediary
PAD	Project Appraisal Document
PARPA	Poverty Reduction Strategy
PARPA II	Second Poverty Reduction Strategy
PDS	Project Design Summary
PFI	Participating Financial Institutions
PIB	*Parque Industrial de Belualane* (Belualane Industrial Park)
PIU	Project Implementation Unit
PFP	Policy Framework Paper
PoDE	*Projecto para o Desenvolvimento Empresarial* (Enterprise Development Project)
PDO	Project Development Objective
PIU	Project Implementation Unit
PDS	Project Design Summary
PSC	Project Steering Committee
PSD	Private Sector Development
RBSI	Regional Business Support Initiative RPED
SASOL	South African Coal and Oil Company
SMEDP	Small and Medium Enterprise Development Project
SSI	Strategic Sectors Initiative
TAO	Training Advisory Office
TELIM	Technical Learning Component Implementation Manual
TLC/PodECAT	Technical Learning Component
TVET	Technical and Vocational Education Training
UASP	*Unidade de Apoio ao Sector Privado* (Project Implementation Unit)

Fiscal Year

Government: January 1 to December 31

Director-General, Independent Evaluation	:	Ms. Caroline Heider
Director, IEG Public Sector Evaluation	:	Mr. Emmanuel Jimenez
Manager, IEG Public Sector Evaluation	:	Mr. Mark Sundberg
Team Leader	:	Ms. Anjali Kumar

Contents

This report was prepared jointly by Brendan Horton, who visited Mozambique for assessing the project in April, 2012, and by Sushma Narain, who undertook its write up and completion, under the supervision of Anjali Kumar. The report was peer reviewed by Stephen F. Rasmussen, and panel reviewed by Robert M. Lacey. Yezena Z. Yimer provided administrative support.

Tables

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Principal Ratings

REPUBLIC OF MOZAMBIQUE: ENTERPRISE DEVELOPMENT PROJECT (IDA-33170, IDA-3317A, EECT-28406, NORW-24286, UK-27799)

	ICR*	ICR Review*	PPAR
Outcome	Moderately Satisfactory	Moderately Satisfactory	Moderately Satisfactory
Risk to Development Outcome	Moderate	Moderate	Low
Bank Performance	Moderately Satisfactory	Moderately Unsatisfactory	Moderately Unsatisfactory
Borrower Performance	Moderately Unsatisfactory	Moderately Unsatisfactory	Moderately Unsatisfactory

* The Implementation Completion and Results (ICR) report is a self-evaluation by the responsible Bank department. The ICR Review is an intermediate IEG product that seeks to independently verify the findings of the ICR.

Key Staff Responsible

Project	Task Manager/Leader	Division Chief/ Sector Director	Country Director
Appraisal	Marilyn Swann Manalo	Demba Ba	Darius Mans
Completion	Gilberto de Barros	Demba Ba	Michael Baxter

IEG Mission: Improving World Bank Group development results through excellence in independent evaluation.

About this Report

The Independent Evaluation Group assesses the programs and activities of the World Bank for two purposes: first, to ensure the integrity of the Bank's self-evaluation process and to verify that the Bank's work is producing the expected results, and second, to help develop improved directions, policies, and procedures through the dissemination of lessons drawn from experience. As part of this work, IEG annually assesses 20-25 percent of the Bank's lending operations through field work. In selecting operations for assessment, preference is given to those that are innovative, large, or complex; those that are relevant to upcoming studies or country evaluations; those for which Executive Directors or Bank management have requested assessments; and those that are likely to generate important lessons.

To prepare a Project Performance Assessment Report (PPAR), IEG staff examine project files and other documents, visit the borrowing country to discuss the operation with the government, and other in-country stakeholders, and interview Bank staff and other donor agency staff both at headquarters and in local offices as appropriate.

Each PPAR is subject to internal IEG peer review, Panel review, and management approval. Once cleared internally, the PPAR is commented on by the responsible Bank department. The PPAR is also sent to the borrower for review. IEG incorporates both Bank and borrower comments as appropriate, and the borrowers' comments are attached to the document that is sent to the Bank's Board of Executive Directors. After an assessment report has been sent to the Board, it is disclosed to the public.

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IEG's use of multiple evaluation methods offers both rigor and a necessary level of flexibility to adapt to lending instrument, project design, or sectoral approach. IEG evaluators all apply the same basic method to arrive at their project ratings. Following is the definition and rating scale used for each evaluation criterion (additional information is available on the IEG website: http://ieg.worldbankgroup.org).

Outcome: The extent to which the operation's major relevant objectives were achieved, or are expected to be achieved, efficiently. The rating has three dimensions: relevance, efficacy, and efficiency. *Relevance* includes relevance of objectives and relevance of design. Relevance of objectives is the extent to which the project's objectives are consistent with the country's current development priorities and with current Bank country and sectoral assistance strategies and corporate goals (expressed in Poverty Reduction Strategy Papers, Country Assistance Strategies, Sector Strategy Papers, Operational Policies). Relevance of design is the extent to which the project's design is consistent with the stated objectives. *Efficacy* is the extent to which the project's objectives were achieved, or are expected to be achieved, taking into account their relative importance. *Efficiency* is the extent to which the project achieved, or is expected to achieve, a return higher than the opportunity cost of capital and benefits at least cost compared to alternatives. The efficiency dimension generally is not applied to adjustment operations. *Possible ratings for Outcome:* Highly Satisfactory, Satisfactory, Moderately Satisfactory, Moderately Unsatisfactory, Unsatisfactory, Highly Unsatisfactory.

Risk to Development Outcome: The risk, at the time of evaluation, that development outcomes (or expected outcomes) will not be maintained (or realized). *Possible ratings for Risk to Development Outcome:* High, Significant, Moderate, Negligible to Low, Not Evaluable.

Bank Performance: The extent to which services provided by the Bank ensured quality at entry of the operation and supported effective implementation through appropriate supervision (including ensuring adequate transition arrangements for regular operation of supported activities after loan/credit closing, toward the achievement of development outcomes. The rating has two dimensions: quality at entry and quality of supervision. *Possible ratings for Bank Performance:* Highly Satisfactory, Satisfactory, Moderately Satisfactory, Moderately Unsatisfactory, Unsatisfactory, Highly Unsatisfactory.

Borrower Performance: The extent to which the borrower (including the government and implementing agency or agencies) ensured quality of preparation and implementation, and complied with covenants and agreements, toward the achievement of development outcomes. The rating has two dimensions: government performance and implementing agency(ies) performance. *Possible ratings for Borrower Performance:* Highly Satisfactory, Satisfactory, Moderately Satisfactory, Moderately Unsatisfactory, Unsatisfactory, Highly Unsatisfactory.

Preface

This PPAR evaluates the Mozambique Enterprise Development Project (in Portuguese, PoDE: *Projecto para o Desenvolvimento Empresarial*). The project was approved by the Bank's Board on January 27, 2000 in an amount of SDR 19.2 million (US$ 26 million equivalent). It was conceived as one element of a broader donor community supported program for private sector development, with additional support expected from the Norwegian Agency for Development Corporation, the European Union, the UK Department for International Development as well as beneficiaries and the government. Taking account of co-financing, the total projected cost was US$ 47.5 million. Actual expenditures amounted to US$ 39.75 million. The project closed on June 30, 2006.

The Independent Evaluation Group (IEG) prepared the report. It is based on the project completion and appraisal reports, the Development Credit and Loan Agreements, a review of Bank files, review of relevant literature and discussions in the field with the main stakeholders, including the Government of Mozambique and several financial institutions.

The PPAR was undertaken for two reasons: to reevaluate the project in light of the evidence and developments six years following closing; and as part of a larger exercise that assesses the performance of several Bank-financed support for financial inclusion. Elements of the financial system and line of credit are elaborated in Annex C.

Following standard IEG procedures, the report will be shared with the government for comment. No comments received from the Government.

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Summary

This PPAR assesses the performance of the Mozambique Enterprise Development Project, (PoDE: *Projecto para o Desenvolvimento Empresarial*) approved by the Board on January 27th 2000 and closed on June 30th 2006. During the period 2000-2010, which covers the implementation of the project, Mozambique performed well in macro-financial terms. However, despite some achievements at the project level, Mozambique's overall growth remained largely driven by mega-projects concentrated in the extractive industry with few linkages with the broader economy.

The project was conceived to pursue "second generation" reforms aimed at sustainable and inclusive economic growth by broadening the base of private sector participation, building on the gains of early post-conflict reforms. It was one element of a donor community supported program for private sector development. The project's Development Objective was to "help broaden the base of private participation in Mozambican economic growth," through three distinct tracks: boosting the competitiveness of Mozambican private firms; enhancing access to term finance; and building the capacity of selected government and non-government agencies. The project aimed to achieve this first through a learning component that offered external consultancy services and technical training to firms through matching grants and through a program to facilitate supply linkages between Mozambican and foreign owned firms in the country. Second, it aimed to enhance access to term finance through lines of credit, and third, to strengthen the business environment by support to relevant government ministries and business organizations, and through direct support to specific sectors to improve their competitiveness.

Project outcome is rated as moderately satisfactory. The *relevance of project objectives* was high. In principle, its three components - training, access to finance and institutional strengthening - were all relevant to the project's objectives of broad-based growth and they were grounded in diagnostic work that identified these areas as key constraints to growth. However, the *relevance of design* was modest. There were constraints on eligibility that limited potential beneficiaries. The design of the line of credit did not take into account key constraints in the broader environment as well as in the financial sector and M&E design was limited. *Efficacy* is rated, on balance, as substantial, in view of the significant achievement of intermediate targets. The project helped a number of small and medium enterprises to access productivity enhancing technical training, and to establish industrial linkages with megaprojects (boosting linkage sales of project supported firms). The project achieved output targets in training and capacity development as well as important legal reforms. It also helped to establish an economic zone which continues to support linkages of SMEs with the 'mega-projects' and helped some firms to develop export links. Case studies suggest that benefits accrued to project supported enterprises. Yet, it must also be pointed out that the broad set of indicators that IEG used to measure the achievement of the final objective showed that after project implementation, the substantial growth experienced by the Mozambican economy continued to be largely due to its mega projects. *Efficiency* is rated modest, since components were not well linked, reducing potential spill-over benefits.

On balance, and in accordance with IEG and Bank Management's harmonized criteria, Bank performance is rated moderately unsatisfactory. The project quality at entry had some

important weaknesses, which a stronger supervision performance was not able to fully address. The Borrower's performance, overall, was also moderately unsatisfactory. While the government was committed to broad-based private sector development, it delayed signing the modified Development Credit Agreement for changing the restrictive criteria of eligibility beyond domestically owned firms, even after agreeing to do so. This impacted project implementation. Implementing Agency performance was moderately unsatisfactory as there were fiduciary weaknesses in implementation including shortcomings in financial management and delays in procurement.

The assessment draws four lessons:

- *In post conflict countries with weak institutions and capacity constraints,* achieving major economic reforms requires continuous effort and liaison with many ministries and agencies, over a substantial period of time. Rather than a single project with multiple components, a programmatic approach could also have provided opportunities to learn from each phase as inputs to designing the next.
- *Matching grant programs can potentially be an effective way of providing incentives to firms. To be successful such programs have to be well managed. Outsourcing to a well-established institution with the right expertise helps*. A successful matching grant program for business services requires a combination of international expertise, local knowledge, autonomy in administration, and adaptability to respond to market demand.
- *Too much dispersion in capacity building components could limit deeper institutional reforms.* It is important to avoid focusing simultaneously on too many different issues. The impact would be deeper if institutional reforms and capacity building are addressed in separate projects.
- *Credit line operations that are designed solely to increase the supply of funds do not increase sustainable access to finance if other institutional, legal and regulatory constraints to financial sector development are not addressed.* Lines of Credit require careful preparation, including assessments of not just overall demand but also factors that could dampen demand, such as high interest rates; and on the supply side factors that may limit commercial banks' appetite to lend to small and medium enterprises, even if they have the funds (e.g. limited information on borrowers' creditworthiness, poor laws on collateral, or the availability of other opportunities for investing with potentially lower risk adjusted returns).

Caroline Heider
Director-General
Evaluation

1. Background and Context

1.1 After nearly five centuries of colonial domination, Mozambique became independent in 1975. Besides high levels of poverty, poor infrastructure, large-scale emigration, the newly independent state also faced severe drought, a prolonged civil war and economic mismanagement under the socialist regime.

1.2 In the midst of this turmoil, in 1984, Mozambique's first democratically elected government, aided by the multilateral organizations, launched an ambitious program of "first generation" economic reforms. The reforms resulted in several macro-economic gains including low inflation, a stable exchange rate, and tight fiscal and monetary policies. Additionally, the government undertook significant structural reforms such as the elimination of non-tariff trade barriers and the privatization and liquidation of over 800 public enterprises.

1.3 Since the end of the civil war in 1992 and following the reforms, Mozambique has grown at 8 percent per year, on average, and reduced the poverty headcount index from 69 percent in 1997 to 54 percent in 2003. Further, poverty levels declined more in rural areas than in urban areas, making Mozambique the second country in the world (other than Vietnam) to see such reductions (IMF 2007)

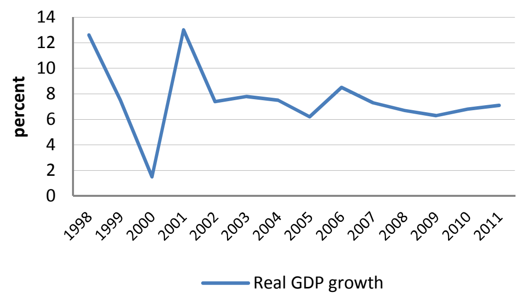
Macroeconomic Context

1.4 During the period 2000-2010, which covers the implementation of the project under review, Mozambique performed well in overall macro-economic terms, albeit with some fluctuations (Figure 1. Mozambique: Macroeconomic, Financial and External Indicators (1997-2011)Figure 1, panels 1.1 to 1.8). The structure of the economy, especially the structure of trade, had changed at the turn of the century, as Mozambique began to increasingly enjoy a resource-led growth spurt, from its extractive industries.

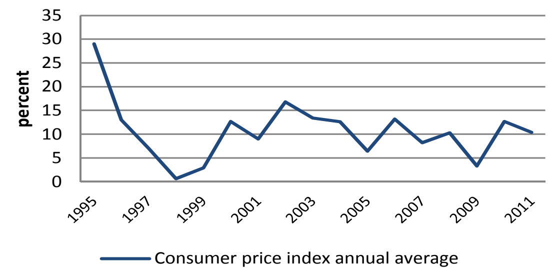
1.5 Despite this spurt, in 2000, real GDP growth collapsed from a rate of 12 percent in 1998 to just about 2 percent, mainly on account of catastrophic floods. But this recession was short lived and growth rebounded the following year. From 2002 onwards, growth fluctuated in the range of 6 to 8 percent per year. The country survived the 2008-2010 financial crises relatively well mainly because direct linkages between domestic and foreign financial institutions are limited. Inflation, which had accelerated from 1999, peaked at 16.8 percent in 2002; since then it has been fluctuating in a range of 5 to 15 percent.

Figure 1. Mozambique: Macroeconomic, Financial and External Indicators (1997-2011)

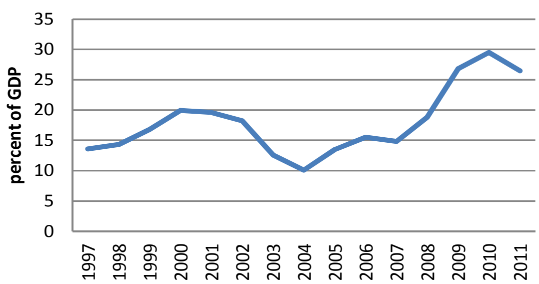
1.1 Real GDP Growth, 1998-2011



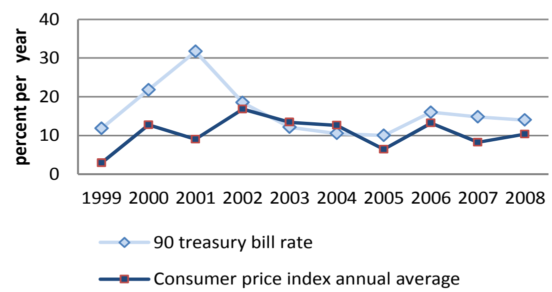
1.2 Annual inflation, 1995-2011



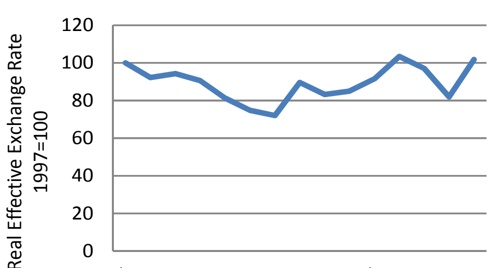
1.3 Credit to the Economy, exc. Government



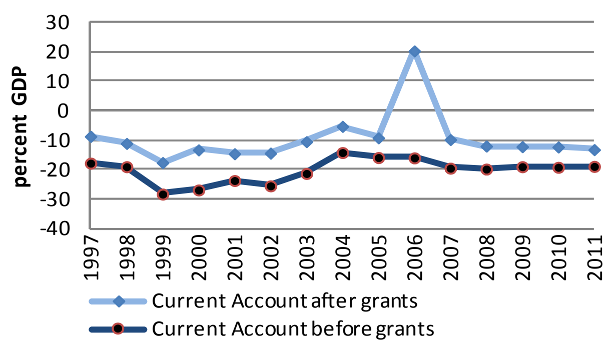
1.4 Inflation and Nominal Interest rates



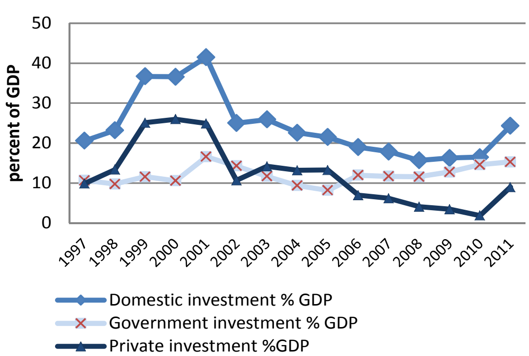
1.5 Real Effective Exchange Rate (1997=100)



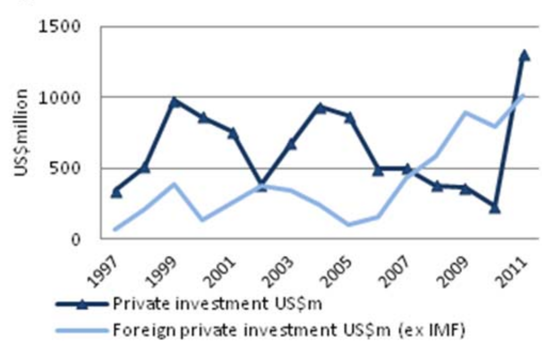
1.6 External Current Account Deficit



1.7 Investment as share of GDP %



1.8 Foreign Investment in US$



Source: IMF

1.6 Despite the steady gains, Mozambique's growth has largely been driven by foreign aid and foreign investment in mega-projects, and has not been inclusive. Mozambique managed to attract investors in several mega-projects concentrated in energy (Cahora gas fields), industry (Mozal Aluminum plant) and mining (Moatize coal mines, Moma Titanium). These foreign owned, export focused, capital intensive projects have not been able to develop linkages with the broader economy. For example, while representing 62 percent of the production value of the manufacturing sector, mega-projects only employ 3 percent of the sector's labor force and 2 percent of urban private sector employment. Also, mega-projects have had limited fiscal benefits — a legacy of the Government's tax incentives to lure foreign investors. The IMF Article IV consultation report (2011) concludes that "Mozambique's growth take-off has not been accompanied by economic diversification nor by commensurate employment creation. Its productive and export base has become increasingly concentrated—a reflection of the emergence of mega-projects and weaknesses in the business environment that have prevented diversification of the economy."

1.7 Mozambique ranks 175th out of 179 on the UN Human Development Index- a measure of health, education and income levels. In 2010, the rising costs of food, fuel and water led to street riots. The unrest underlined the extreme vulnerability of the urban poor to a price shock and the lack of social safety nets. The Third National Household Survey (2008/09) published in 2010 indicated that the incidence of poverty had stagnated at 55 percent since 2003, after a decline from 69 percent in 1997 (IMF 2011).

1.8 The depth of financial intermediation in Mozambique remains low and its financial sector continues to be highly concentrated. The recent Investment Climate Assessment (2009) found that the percentage of firms accessing lines of credit is low, at 13 percent, and had in fact steadily declined from previous surveys in 1997 (35 percent), 2002 (29 percent), and 2006 (26 percent)—especially for small and medium enterprises. Rural populations also remain underserved in terms of financial services: in 2008, branches in rural and peri-urban areas held roughly 20 percent of the number of credit and savings accounts as compared to urban branches, though these areas account for over 60 percent of the country's inhabitants (FSAP 2009).

Project Context

1.9 At the time when the project was conceived, to build on the gains of early post-conflict reforms, the Government of Mozambique had decided to pursue "second generation" reforms aimed at sustainable and inclusive economic growth by broadening the base of private sector participation. Studies conducted by the IFC and the Bank's Foreign Investment Advisory Service office in 1996-97, followed by a survey of 150 firms conducted in 1998 by the Africa Regional Program of Enterprise Development identified key areas that needed to be addressed to improve the business environment. Among them were: modification of labor and land laws; business registration, licensing and reporting requirements; import procedures; and investment promotion. Additionally, access to finance was seen as a binding constraint, especially on the small and medium enterprise sector.

1.10 The government indicated strong commitment on moving rapidly to address the obstacles to private sector expansion. The Enterprise Development Project (*Projecto para o*

Desenvolvimento Empresarial (PoDE), 2006-2007), was conceived as one element of a broader donor community supported program for private sector development and was to build on IDA financed initiatives from1985-1996.[1]

1.11 At the time of preparation of the project, the key problems requiring attention were identified as the lack of skilled labor, weak institutions for private sector development, and a shortage of financing especially for small and medium enterprises and start-ups. The project was to thus work on three distinct though potentially complementary tracks: i) providing support to private firms through promoting their access to training, consultancy, and linkages. ii) promoting access to finance; and iii) building the capacity of selected government and non-government agencies to enable them to provide better professional services to the private sector and to remove business environment constraints.

2. Objectives, Design, and their Relevance

Objectives

2.1 According to both the Project Appraisal Report and the Development Credit Agreement, the project's overall objective was to "help broaden the base of private participation in Mozambican economic growth."

RELEVANCE OF OBJECTIVES: SUBSTANTIAL

2.2 The project's objective to help broaden the base of private participation in Mozambican economic growth were substantially relevant at the time the project was conceived and remained so at the closing of the project for the following reasons:

- The objectives were consistent with several objectives of the 1998 Country Assistance Strategy, which had a central pillar of promoting sustainable and broadly based private sector growth which included developing locally owned enterprises as well as partnerships with foreign capital, and improving the government's institutional capacity in support of private sector development.
- The project's objectives remained equally relevant at the time of closing (2006) with respect to the 2004-2007 IDA Country Assistance Strategy which called for improving private sector competitiveness.
- The project's objectives are also consistent with the most recent Country Partnership Strategy (2012-2015). It's Pillar One: "Competitiveness and Employment" provides the principal support to the overarching goal of broad based, inclusive and pro-poor growth of the Country Partnership Strategy.
- Moreover, the project was also consistent with the government's own development strategy and its initial Poverty Reduction Strategy Paper (*PARPA* in Portuguese) developed during the second half of the 1990s, as well as the Policy Framework Papers that preceded them.

[1] IDA financed two adjustment operations, the Industrial Enterprise Restructuring Project (1989), the Small and Medium Enterprise Development Project (1989); as well as an Economic and Financial Management Technical Assistance Project (1989) and a Financial Sector Capacity Building Project (1994).

- It remained consistent with Mozambique's second Poverty Reduction Strategy Paper (*PARPA II* 2006-2010), in particular concerning the need for improved firm level competitiveness through increased factor productivity, better access to medium term finance for small and medium enterprises, an improved business environment, and better institutions to support private sector development.
- Mozambique's third Poverty Reduction Strategy Paper (2011-2014) represented a continuation of the PARPA II. Its principal goal was to reduce the incidence of food poverty (from the current level of 54.7 percent to 42 percent by 2014) through, among other measures, private sector job creation and human development.

Design

COMPONENTS

2.3 The project's objectives were to be achieved by: (i) boosting the competitiveness of Mozambican private firms by strengthening their access to, and use of, support services external to the firm, and providing a more efficient market for training and capacity building services, by establishing forward and backward linkages to existing and new local and foreign buyers and investors; (ii) enhancing access to term finance by both first-time and other borrowers; and (iii) helping to strengthen the capabilities of the Ministry of Industry, Trade, and Tourism (MITT), the Investment Promotion Center, and business organizations with potential to improve the business environment. Accordingly, the project had three components with a total cost of US$39.75 million, of which the Bank financed US$25.1 million (see Section 3.2 for details).

2.4 **Component 1: Technical Learning Component** (expected costs US$13.6 million, actual US$18.74 million) was administered through the following agencies:

- Firm Competitive Office (FCO) to boost the competitiveness of firms by promoting their access to consultancy services on a 50 percent matching grant basis.

- Training and Advisory Office (TAO) to support the development of an active business and technical training market. Matching grants of 50 percent would be made available to qualified trainers to provide training services to local firms.

- Linkage Program Office (LPO) to facilitate supply linkages between Mozambican supplier firms and joint-venture or foreign-owned firms in Mozambique. The three offices would be jointly managed by a single contractor to facilitate information sharing.

2.5 The Technical Learning Component sought primarily to increase competitiveness of beneficiary firms. The main expected outputs and related activities pertained to consultancy services provided in house to beneficiary firms; and/or training provided offsite to employees. The training activities were to be financed through matching grants, to enable the cost of training to be shared by the beneficiaries and the project.

2.6 **Component 2: Line of Credit Component** (estimated costs US$12.7 million, actual US$5.45 million) included the following elements:

- a special facility designed to provide very small, first-time bank borrowers with loans in local currency amounting to a maximum of US$15,000.[2]
- a general facility to finance loans up to US$300,000 for all small and medium-scale borrowers.

2.7 To encourage domestic ownership access was to be restricted to firms that were owned at least 51 percent by Mozambican nationals. Lines of credit would be made available to participating financial institutions in meticais, without foreign exchange risk, and pegged to market-based interest rates, as determined by the participating financial institutions themselves. This component directly sought to address firm's lack of access to credit by addressing the need for longer-term sources of finance for banks. Sub-loans were given for periods of 2-1/2 to 7 years with a maximum grace period of one year.

2.8 **Component 3: Institutional Capacity Building** assistance to the Investment Promotion Center (*Centre de Promoçao do Investimento; CPI*), the Ministry of Industry, Commerce and Tourism (MICTUR), and the Confederation of Economic Associations (*Confederação das Associações Económicas*; CAE) (estimated costs US$17.4 million, actual costs US$12.83 million).

2.9 This component sought to enhance the capacity of key public and private institutions to deliver business support services. These included, prominently, the Investment Promotion Center to promote foreign investment and the development of Export Processing Zones and/or Free Zones), the Ministry of Industry Commerce and Tourism, and regional business associations including their national confederation. The component also included sector specific initiatives to improve their competitiveness and increase exports.

Implementation and Project Management Arrangements

2.10 The overall Executing Agency was the Ministry of Industry, Commerce and Tourism (MICTUR). MICTUR delegated management to an eight person Project Steering Committee (PSC) consisting of four members from the Confederation of Economic Associations, and one member each from the Bank of Mozambique, the Investment Promotion Center, the Ministry of Industry Commerce and Tourism, as well as Ministry of Planning and Commerce. The PSC was supported by a Project Implementation Unit (PIU) – *Unidade de*

[2] The special facility was designed to catalyze commercial bank lending to largely indigenous and small-scale entrepreneurs who often have considerable difficulty in obtaining a first loan as they are viewed as high risk borrowers involving high transaction cost relative to potential revenue generation. Parallel "quasi-equity" funding, equal to 25 percent of total project cost, was to be made available through the PFI at the Government's risk. This funding had no debt servicing requirements during the scheduled life of the PFI sub-loan, and would, therefore, create de facto total equity and quasi-equity of at least 35 percent of project cost which, as it was subordinated to the Bank's loan, significantly reduced lender risk. Under this arrangement, the borrower had a major incentive to repay the bank loan on time as the 25 percent quasi equity would become a grant to the borrower upon full repayment of the loan. Funding under both facilities would be available to finance investment assets including permanent working capital for private sub-borrowers in all sectors (including industry, agro-processing, tourism, transportation, construction and services).

Apoio ao Sector Privado (UASP). The PSC delegated management of each component to agencies and/or private contractors as illustrated in (Table 1).

Table 1. Implementation Agencies by Component

Component	***Implementation Agency***
Technical Learning Component	Competitively selected Management Contractor
Institutional Capacity Building Component	Investment Promotion Center, Ministry of Industry, Confederation of Economic Associations
Line of Credit Component	Bank of Mozambique, Project Implementation Unit.

Source: EDP PAD, World Bank

2.11 Each implementing entity was responsible for the collection of the data relevant to its operations, but the PIU was responsible for its consolidation. No systems for collection, analysis and validation of the data was specified in the PAD

Relevance of Design: Modest

2.12 The proposed causal chain with respect to activities, outputs and intermediate outcomes largely appears convincing as the proposed actions were expected to contribute to achieving the project development objective of broadening the base of private participation.

2.13 The impact of training and capacity building services on enterprise productivity was expected to increase productivity of firms and thus contribute to overall growth. Institutional capacity development was to improve services delivered by participating public and private agencies. Through backward and forward linkages[3] between foreign and domestic firms, the demand for participating firms' products domestically and internationally was expected to increase as reflected by increased production, investments, exports, and new job creation within participating firms.

2.14 In the line of credit participating banks were expected to increase their responsiveness to lending medium-term resources to private enterprises as a result of high levels of initial repayment. The two different designs of the lines of credit - one for first time borrowers and the other for traditional borrowers - as well as the small size of loans under the first time borrower's category, were expected to broaden access to credit and hence increase participation of local firms in economic growth. Taken together these activities were expected to lead up to the achievement of the project's development objective.

2.15 In principle the three components - training, access to finance and institutional strengthening - were relevant to the project's objectives. However, the design suffered from significant limitations, particularly with regard to the lines of credit. Their design did not take into account key constraints in the broader environment, as well as in the concentrated and under-developed financial sector, that together implied that increasing the supply of credit,

[3] These linkages were to facilitate supply linkages between Mozambican supplier firms and joint-venture or foreign owned firms in Mozambique.

on its own, would not be sufficient to ensure its offtake. Limited linkages between components limited potential spillover benefits. Further, to some extent reflecting the Bank's practices at the time when the project was approved, M&E design lacked indicators to measure attainment of the project development objectives.

2.16 High interest rates were identified as a key constraint for small and medium enterprises. Borrowing was costly to enterprises, relative to internally generated funds. High interest rates, which dampened demand, were partly a reflection of lack of competition in the highly concentrated financial markets, but also, low credit bureau coverage, which implied that lenders found it difficult to gauge the potential risks of different borrowers, and maintained high rates as a precaution. Other limitations in the environment that made banks reluctant to lend were poor contract enforcement and a limited framework for secured transactions (i.e., for collateralized lending). Moreover, in a highly liquid economy where banks had the opportunity to hold government securities (a safe asset), there was limited appetite to hold risky assets in the form of loans.

2.17 The PAD acknowledged that high interest rates and a weak credit disciplinary environment were serious problems for increasing intermediation, but concluded, on the basis of interviews with bankers, that there would nevertheless be interested in increasing medium and long term lending if they had an appropriately matched funding base. With hindsight, this assessment proved too optimistic.

2.18 The problems affecting financial intermediation were substantiated by the FSAP in 2003 which concluded that the prohibitively high interest rates (around 30-34 percent in real terms at this time) and the lengthy and unreliable debt recovery mechanisms were the key obstacles to increased lending, and not the availability of term funding.[4] The FSAP also identified reforms that were needed to improve bank's appetite for new credits in the difficult Mozambican lending environment such as the adoption of a new Commercial Code, a law for secured transactions, and increasing coverage of the credit registry.

2.19 These findings were further reiterated by the 2009 FSAP, which pointed out the limited scope of credit registry coverage, lack of infrastructure for moveable collateral, weak financial reporting, limited property registry facilities, high concentration and foreign ownership of banks and overall lack of competition in the banking system. It noted that these were important factors, other than the supply of credit, that constrained access to finance for small firms. The PAD only took only partial note of these risks under the finance component, or their potential impact on the line of credit component

2.20 In practice, the components were not well linked with each other which reduced potential spill-over benefits. The line of credit and technical learning components for example could have been appropriately linked for better results. Several supervision reports

[4] "A number of additional issues such as such inflation, high levels of government borrowings crowding out of the private sector, lack of competition in the financial sector, lack of transparency on high fees and charges, weak truth in lending environment were some of the reasons that contributed to high and for the small bowers untenable interest rates resulting in low demand" (USAID, 2007).

later recommended linking the two component through the PIU but it was not able to successfully incorporate this retroactively.

M&E DESIGN

2.21 Overall project design was complex with several components and sub-components, and an elaborate structure of implementing units, which rendered the project difficult to manage or monitor. The M&E design itself was inadequate, and did not provide an adequate basis for assessing the achievement of the projects' objectives.

2.22 The approach adopted towards M&E partly reflecting Bank practices at the time of appraisal, when a broad log frame approach was considered adequate to link results and outcomes to project activities. As a result, output indicators only partially measured project outputs and intermediate outcome indicators were only identified for some outputs. The project did not track final outcome indicators, at least in terms of its stated overall objective broadening the base of private participation in Mozambican economic growth. The output indicator for the development of linkages of private and small scale firms to foreign and joint venture companies tracked the number of linkages established and the corresponding intermediate outcome indicator was the resulting sales achieved. Other expected performance indicators such as increased production, investments, exports, and new job creation within participating firms that are mentioned in the PAD, were not tracked during implementation.

2.23 The main performance indicator of the training component was the number of trained firms and increase in firm expenditure on training. There was no indicator to assess increase in firm productivity as a result of the training. There was no output or outcome indicator for the line of credit component. The only stated indicator – the percentage of loans that were well performing- was in fact an indicator of quality of the loans, and of bank's loan portfolios, and can at best be used as an intermediate indicator.

2.24 The two proposed project development objective indicators: (i) that at least 20 percent of participating firms were established in 1995 (i.e., were relatively new); and (ii) that at least 30 percent of participating firms were operating outside of Maputo (i.e., that the project achieved broad based geographic outreach) did not provide an adequate basis for assessing the achievement of the project's development objectives.

2.25 Whether the project reached younger or newly formed enterprises was not tracked, as information was not maintained, or reported, on the type and size of enterprises supported. There was no baseline data before 1995 on firm establishment and as such it is not possible to compare the impact of the project's support to younger or new firms. The second indicator tracked the extent of support for firms beyond Maputo, where most mega projects and large private businesses were concentrated, and can thus be considered a proxy for deepening of the private sector. However, this too is an intermediate indicator and does not measure the achievement of the project's development objective. The project did conduct surveys of some beneficiary firms under the technical assistance component in particular, that pointed out both benefits achieved, and their limitations, at mid-term and at closing, although undertaking a quantitative impact evaluation would have been difficult.[5] While efforts were made to improve the monitoring framework towards the end of the implementation period, this was too late to provide the information needed on project performance and outcomes.

3. Implementation

3.1 The loan was approved by the Board on January 27th 2000. The project became effective on August 31, 2000. The Mid-term review took place in April 2003 and the project closed on June 30, 2006.

Project Financing and Costs

3.2 At appraisal the project was expected to cost US$47.60 million, of which US$26 million was to be financed by IDA, and the remainder by other development partners (US$14.20 million), by the government, (US$0.5 million), and by beneficiaries themselves (US$6.90 million) through matching grants and/or equity contribution to subprojects financed by the Line of Credit. The actual cost was US$39.75 million, with IDA disbursing US$25.01 million, and other development partners US$8.69 million (Table 2). The shortfall relative to the originally anticipated amount from development partners' contributions was covered with US$4.90 million from NORAD and US$1.19 million from the European Union, both of which were used to finance additional expenditures in the Technical Learning Component. DfiD's resources were added to finance a self-standing HIV component. Beneficiary financing amounted to US$6.05 million compared to an appraisal estimate of US$6.90 million.

Table 2. Project Cost by Component (in USD Million equivalent)

	Appraisal Estimate			*Actual as of ICR*	*Difference*
	TOTAL, OW	**IDA**	**OTHER**	**TOTAL**	
Technical Learning in Firms	13.90	6.0	7.90	18.74	4.84
Capacity Building	17.40	7.00	10.40	12.83	-4.57
Finance	12.70	10.00	2.70	5.45	-7.25
Project Implementation	1.20	0.60	0.60	2.73	1.53
Other	2.40	2.40			-2.40
Total	47.60	26.00	21.60	39.75	-7.85

Source: PAD, Annex 1 and ICR Annex 3

3.3 Actual expenditures by component differed from the appraisal estimates with an increase of US$4.84 million for the Technical Learning Component, and reductions of US$4.57 and US$ 7.25 million respectively in the Institutional Capacity Building and Financial Components. Spending on the Institutional Capacity Building Component was less

[5] Mussanhane, Egas. 2006 '*Avaliação do Projecto de Desenvolvimento Empresarial*' *Relatório Final*, PoDE, Maputo, May.

than appraised because the construction of the new Headquarters building for the Investment Promotion Center did not materialize in a timely manner, and was dropped. IDA reduced the Line of Credit by 50 percent, reallocating the funds to other activities[6].

Table 3. Project Costs (Appraisal and Actuals) – by Source of Financing (US$ millions)

	PAD	ICR
IDA	26.00	25.01
DfID		2.60
NORAD		4.90
EU		1.19
Donor cofinancing	14.20	8.69
Government	0.50	
Beneficiary	6.90	6.05
Total	47.60	39.75
Source: PAD Annex 1, and ICR Annex 3		

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Total	47.60	26.00	21.60	39.75	-7.85
Source: PAD, Annex 1 and ICR Annex 3					

Factors that Affected Implementation

CHANGING ECONOMIC CONDITIONS

3.4 The project had been predicated on the continuation of a favorable macro-financial environment and performance. However, several unfavorable factors impacted the project implementation: the floods of 2000 and the ensuing, short-lived recession; the uptake in inflation which led to a rise in interest rates; and financial difficulties at the two largest commercial banks (that accounted for 65 percent of the commercial bank market), which therefore became ineligible to act as Participating Financial Institutions under the project. Overall private investment, including private foreign investment, trended down too, following the two mega projects.

RESTRICTIVE ELIGIBILITY CRITERIA

3.5 Two cross cutting eligibility issues arose which affected implementation:

- First, during preparation, eligibility criteria for the Technical Learning Component and the Line of Credit Component initially excluded firms that were less than 51 percent owned by Mozambican nationals. At negotiations, IDA tried in vain, to get this restriction eliminated on the grounds that it would limit the pool of potential

[6] At the request of the authorities, the Bank reallocated resources to provide funding for infrastructure at the Beluluane Industrial Park.

applicants under both the technical and financial components.[7] Subsequently, during implementation, the authorities acceded to the proposed change but then changed their minds, and delayed signature of the revised credit agreement until early 2005. This significantly compromised implementation.

- Second, agriculture commerce, real estate and financial services were initially excluded from eligibility, but in 2002 Government agreed to include them.[8] Similarly, the eligibility criteria for the Line of Credit for small borrowers were revised to raise the ceiling on individual loans, due to slow disbursements.

COMPONENT SPECIFIC IMPLEMENTATION ISSUES:

3.6 There were no implementation difficulties in the Technical Learning Component thanks to the excellent performance of the contractor (a local consulting company in association with International Development Ireland -- IDI), despite the initial severe shortage of competent local consultants. However, the Institutional Capacity Building component and the Line of Credit component encountered a number of implementation problems.

3.7 The implementation of the Institutional Capacity Building Component was delayed due to difficulties in concluding a satisfactory contract with the management contractor for the Beluluane Industrial Zone; and by slowness of IDA's approval of an environmental assessment needed for the infrastructure investment in the Beluluane Industrial Park. Project implementation was also affected by the government's delay in signing the revised credit agreement which in turn slowed down IDA's approval of the reallocation of US$1.5 million from studies to goods and services needed to finance infrastructure. Additional delays were due to lack of completion of the procurement and investor tracking system. Further, the Sector Specific Initiative sub-component did not materialize as a separate activity.

3.8 Implementation of the Line of Credit component in the first three years of the project's operation was very slow, due to the financial difficulties encountered by the largest banks and their consequent loss of interest in the lines of credit, especially in view of their attendant risks in the context of the lending environment (as discussed above in paras 2.16 to 2.19 and in para3.4). It was only in year four, after adjusting the design of the product to increase the loan size and with an expanded presence of GAPI- a government owned, non-deposit taking development finance institution, rather than a private commercial bank -that the credit line started disbursing at a steadier rate. Ultimately, the credit line was reduced to half (US$ 5.1 million) and at the end of the project, US$ 4.3 million that amount was disbursed. Demand was limited by the high level of real interest rates (over 30 percent) (as discussed in para 2.18 above), by the environmental factors in the financial system, such as the legal and procedural difficulties in collecting on collateral, particularly for loans of less than US$15000, limited credit information, etc., and by factors such as the restrictive eligibility criteria. Moreover with excess liquidity in the banking system and the availability

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[7] There was lack of an agreed interpretation of the term "majority private Mozambican firms" that was used in project documents to define the enterprises eligible for support under PoDE. The Mozambican authorities defined eligibility as those firms who are majority-owned by Mozambicans while the Bank preferred a broader definition of firms registered in Mozambique.

[8] Only private, majority Mozambican-owned firms in manufacturing and services supporting manufacturing and exports (including tourism) were eligible.

of government securities as alternative assets, the attractiveness of holding risky assets – SME loans – was limited. To some extent, the difficulty in disbursement was partially resolved by proactive adjustments during supervision, such as raising the loan size limit from US$ 17,000 to US$ 40,000, and by allowing loans to be made in foreign exchange for the benefit of exporters, and most of all, by increasing the role of GAPI. GAPI was more attuned to lending to small and medium enterprises and startups, but significantly, also had access to funds at a preferential rate, partly conveyed to its borrowers.[9] Nevertheless, the Line of Credit was reduced by 50 percent.

Safeguards Compliance

3.9 The project was classified as category "FI" for the purpose of Environmental Assessment as it involved investment of Bank funds through a financial intermediary. Accordingly, Participating Financial Intermediaries had to screen proposed sub-projects and sub-borrowers carry out environmental assessments for each subproject, so as to ensure with the environmental requirements of the appropriate national and local authorities as well as IDA's environmental policies. There is no evidence that problems were encountered in this regard.

3.10 With respect to Safeguards Compliance the PAD had specified that the Belualane Industrial Zone should comply with IDA's safeguards policies. In line with the advice from the Bank's Environmental Unit, a complete environmental impact assessment was undertaken and its recommendations were taken into consideration for the project-funded infrastructure work. But delays in the completion of this assessment and its approval by IDA slowed down project implementation, a point reiterated to the PPAR mission by the Investment Promotion Center. IDA also recommended a strategic environmental study for the remainder of the 800 hectares covered by the Park, but that study was not completed prior to the project's closure.

Fiduciary Compliance

3.11 During the first three years of the project, financial management appeared satisfactory, though slow. However, in 2004 the Loan Operations Accounting Department (LOA) identified and flagged an increasing number of errors in withdrawal requests. Eventually, IDA decided to suspend the replenishment of special accounts in late 2005 and selected new auditors in 2006 and carried out a special independent audit for the project as a whole. This audit found no evidence of financial fraud, but overpayments of $47,500, that is about 0.12 percent of total disbursements. In this regard, the Project Director explained to the PPAR mission that part of the problem resulted from the complexities of having to manage accounts for four different development partners at the same time.

3.12 Procurement also suffered from increasing weakness as the project progressed on account of weak capacity and the multiplicity of stakeholders, resulting in incomplete documentation, last minute requests, and slow response time. IDA provided substantial

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[9] The access to the credit line in a foreign currency was limited to those enterprises that invoice in a foreign currency in order to remove the foreign exchange risk in making the loans (Aide Memoire, November, 2005).

assistance but it did not result in the removal of all the procurement delays. Overall, there was no evidence of mis-procurement.

4. Achievement of the Objectives

4.1 The achievement of the objective is rated as **Substantial**. The project's development objective was to "help broaden the base of private participation in Mozambican economic growth." The PAD, however, does not specifically define "broadening the base of private participation." According to the PAD the project aimed to support the Country Assistance Strategy objective of "promoting broad-based private sector-led growth" by facilitating the participation of an increasing number of Mozambican firms, especially small and medium sized firms in the growth process.[10] Given the spectrum of interpretations possible as to what "broadening the base of private participation" meant – i.e., whether it meant including more small and medium enterprises in an economy dominated by foreign owned mega projects; or increasing overall private participation in the economy, or both - the PPAR looks at both the outcomes of project specific activities whose target was primarily small and medium sized firms, and at measures of overall private sector growth.

4.2 With regard to the former, the project clearly helped a number of small and medium enterprises[11] and startups to establish industrial linkages with the megaprojects, and helped set up an economic processing zone which has - despite some challenges - continued to further such linkages. It achieved all but one of the project's output targets, as detailed below (paras. 4.7 to 4.8 and paras. 4.13 to 4.16). The project also contributed to key reforms such as the labor law aimed at private sector development.[12] However the project's line of credit component was not successful in expanding access to term finance for SMEs - a key barrier

[10] The primary target population spelled out in the PAD was: (i) approximately 200 small- and medium-sized businesses that are currently exporting or show potential to export (at least 20 percent of firms supported should have been established in 1995 or later and at least 30 percent should operate outside Maputo); (ii) at least 30 local firms that could become suppliers to larger foreign investors that are operating within the country; and (iii) local firms supplying the domestic market, especially the very many small firms likely to benefit from training. The secondary population to benefit from the project will be the employees of these firms, the firms and individuals that benefit from these employees' income, and the firms that provide inputs and services to the exporting firms.

[11] The output targets are not all relevant to the achievement of the project objective (for example the revised targets for the line of credit as the ICR points out). EU (a project partner and co-financier) also commented that "the fact that the targets were exceeded significantly in the Technical Learning Program is a good achievement but that may also reflect on overly conservative targets in the design." With respect to other targets that were supported by the project (such as labor and business environment reform, industrial park) attribution as discussed above is difficult given a number of other players and the contribution of mega projects such as Mozal.

[12]There were a number of other investment climate related reform that the project supported along with other players however overall Mozambique business environment remains challenging and it's Doing Business ranking has gone down by 7 from 139 in 2012 to 146 in 2013 out of 185 countries. An analysis by USAID (2009) shows that that labor conditions remain strict in relation to other countries despite the labor law reform, and may imply that some firms avoid the restrictions either by limiting employees to temporary contracts or by avoiding contracts altogether and adopting informal practices, something frequently raised anecdotally (Bruce Byiers. 'Informality in Mozambique: Characteristics, Performance and Policy Issues' USAID, 2009).

to private sector growth. Recognizing the problems with the line of credit, the project eventually restructured it and the revised numerical output targets for the credit line were largely met.

4.3 The project team conducted a beneficiary survey on the Technical Learning component during the mid-term review as well as at the conclusion of the project, and collected case study evidence on beneficiaries. These surveys found a number of positive results, though also, cases where the design of delivery could have been strengthened.[13] In the absence of systematic sampling, or an impact evaluation of beneficiaries (compared to a control group identified up-front), these results remain ambiguous in terms of project impact. The PPAR team was not able to supplement these efforts six years after project closure, especially in view of the need for baseline information, and difficulties in tracking down beneficiaries after the disbanding of the project implementation unit. Nevertheless the positive findings from the tracking of outputs within the project, as well as the project's own beneficiary surveys, are noted.

4.4 However, as described above (paras.2.21 to 2.25) the project's log frame did not track all outputs, or all intermediate outcomes, let alone final outcome of broad based private sector led participation in economic growth. The PPAR thus constructed its own indicators to track the final outcome of broad based private sector participation in economic growth: the private sector's share in GDP, foreign direct investment (FDI), capital formation, merchandise trade, credit to the private sector and employment. While these broad indicators of private sector growth reflect the final objectives of the project, the PPAR recognizes also that attribution to the project is nonetheless difficult, particularly given its small size relative to the overall economy.

4.5 Based on this broader set of indicators, the PPAR finds that after project implementation, the Mozambican economy experienced strong private sector growth, but this growth was largely confined to foreign owned, capital intensive, export oriented mega projects in the extractive industry. These megaprojects, overall, still have limited linkages to the broader domestic private sector.

4.6 To conclude, different factors are taken into consideration by the PPAR: positive achievements in terms of a broad spectrum of outputs and intermediate outcomes, especially with regard to technical learning, though with clear limitations in other areas – the line of credit. These are combined with limited evidence of achievement of broad overall outcomes based on a broader set of indicators, albeit with reservations about the extent of attribution to the project. Based on these considerations, overall, efficacy is rated as **Substantial.**

[13] Mussanhane, Egas. 2006 '*Avaliação* do Projecto de Desenvolvimento Empresarial' Relatório Final, PoDE, Maputo, May.

Outputs

i) Increasing the competitiveness of Mozambican Private Firms by Strengthening their Access to, and use of Support Services.

4.7 The output targets were substantially met. The firm competitiveness sub-component supported 714 consultancies for 328 firms in a range of industries, and 40 percent of these consultancies took place outside Maputo. Of the 3,163 workers who received on the-job training, 51 percent were from outside Maputo. A quarter of the firms also received consultancies aimed specifically at preparing them to become suppliers for major investors in the country. The consultancies also allowed nearly 60 supported firms to upgrade their obsolete equipment inherited from privatized state-owned enterprises (SOEs) and to improve production processes.[14]

(i) *Providing a more efficient market for training and capacity building services and establishing forward and backward linkages to existing and new local and foreign buyers and investors*

4.8 The project's linkages program helped to establish the Supplier Development Program to help smaller suppliers meet the standards of international companies. The target of 30 linkages was surpassed with 57 such linkages formed.[15]

(ii) Enhancing access to term finance by both firm time and other borrowers

4.9 Disbursement under this component was hindered by the reluctance of commercial banks to participate. Disbursements picked up only in the fourth year, with the increased presence of a non-commercial Development Finance Institution among the participating financial institutions, a loan size increase from US$15,000 to US$40,000 for first time borrowers, the inclusion of on-lending in forex to exporters, and eventual restructuring to broaden eligibility beyond narrowly defined domestic enterprises.[16] Nonetheless, the credit line was halved to US$ 5.1 million. Only 17 percent of funds disbursed (representing 20 borrowers) took the form of loans of US$40,000 or less, for first time very small borrowers.

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[14] According to the PAD for the Bank project that followed ("The Competitiveness and Private Sector Development Project" (CPSDP) this was an important output that helped lay the foundation for the market for business development training for the target group where none existed. Significantly, the employers partly paid for the training. CPSDP has continued the effort to provide consultancies and training to small and medium enterprises through a matching grants scheme.

[15] Reflecting on the effectiveness of the linkages program, an AfDB private sector profile of Mozambique (2008) concludes that the government strategy of attracting foreign investors and to develop the small and medium enterprises sector through business linkages with the large, foreign-owned projects is not delivering results. Only a handful of local-owned small and medium enterprises have been able to take advantage of opportunities for industrial linkages with large projects. In very rare cases, Mozambican small and medium enterprises have managed to establish and benefit from such linkages, mostly because they either have associated themselves with the foreign partners, or they are affiliates of foreign firms. The lack of information about business development, norms and standards, and difficult access to credit often prevent small companies from taking advantage of business opportunities that could lead to more formal sector employment.

[16] The access to the credit line in a foreign currency was limited to those enterprises that invoice in a foreign currency in order to remove the foreign exchange risk in making the loans (Aide Memoire, November, 2005).

4.10 While nine banks initially signed up as Participating Financial Institutions, more than 85 percent of loan disbursements were undertaken by two financial institutions: GAPI and BCI (Banco Commercial de Investimento). GAPI, a public sector development bank, accounted for more than half of total loan amounts disbursed. Therefore project contributions to the expansion of private credit did not occur. GAPI received funds at relatively favorable terms from the Central Bank, and passed on some of the benefit in its on-lending. This was contrary to the original structure envisaged, and could arguably distort the market.[17]

4.11 While the repayment rate of 85 percent set out as a target in the project documents was surpassed, at 95 percent, this repayment figure only referred to 30 percent of lending. At the time of loan closure, many term loans were far from maturity, and final repayment remained a question mark.[18]

4.12 Notwithstanding, GAPI had some accomplishments, notably, providing advisory services together with credit. And the restructuring also made the positive achievement of broadening eligibility to a wider spectrum of enterprises, beyond narrowly defined domestic enterprises.[19]

iii) *Helping to strengthen the capabilities of the Ministry of Industry and Commerce, Trade and Tourism, the Investment Promotion Center, and business organizations with potential to improve the business environment*

4.13 The main accomplishment under this was the infrastructure support the project provided for setting up the first Industrial Park: Beluluane Industrial Zone. The zone has since attracted 22 firms representing about US$15 million of investment and created 1000 jobs by by the end of 2006. At the end of 2011, these numbers had grown to 34 companies, 2,300 jobs and investments worth about US$245-250 million. The location of the zone facilitated linkages of the firms with the mega project, Mozal[20] (the Mozambique Aluminum Plant) and some of the firms were set up in the Zone with the objective of supplying to that company. The park has thus been a success increasing linkages. The PPAR mission also found however that there have been continuing problems with the supply of infrastructure

[17] The project ICR also rates the line of credit (in its rating of the components) as moderately unsatisfactory. In the follow-up project to PoDE, the Bank dropped the line of credit component altogether, instead supporting training through matching grants. In IFC's project with a commercial bank, it lends at market rates but supports SMEs through training. Likewise GAPI also provided advisory services together with credit.

[18] As noted in previous sections, there were a number of reasons –for the low uptake of the line of credit: on the demand side high interest rates were a disincentive, relative to the cost of internal funding. There were further problems - on the supply side, banks did not want to use the line of credit to lend to SMEs due to issues with collateral, credit information, difficulties in debt recovery, and also, high levels of government borrowing that led to the general reluctance of commercial banks to take on much financial intermediation (ie, taking on more risky assets - loans - when safer assets were available - government securities). As discussed in section 2, the design of the line of credit did not take these factors in the broader environment into account, assuming that making funds available would in itself be enough to ensure offtake. For further discussion on the line of credit component see Annex C.

[19] For a further discussion of the line of credit component see Annex C.

[20] Mozal is an IFC and MIGA supported mega project with the highest Foreign Direct Investment in Mozmabique. Mozal also supports small and medium enterprise development by encouraging linkages.

(water and electricity) to the Zone. There have also been serious and still unresolved conflicts between the Zone Management Company and the Investment Promotion Center (IPC).

4.14 The project supported the Investment Promotion Center (IPC) through staff training and investment promotion missions to Asia and Europe. The IPC satisfactorily implemented its corporate plan and approved at least 150 projects before project closure in 2005. In terms of sustainability, however, the PPAR mission found that the IPC did not eventually acquire its promised new building or the investor tracking software required under the project.

4.15 The project's target output of three round-table conferences between the Confederation of Economic Associations (CAE) and the government was exceeded, with four conferences. The Ministry of Industry met its staff training targets. However, in terms of final outcomes, capacity in these agencies remains a challenge. According to AfDB's country strategy paper (2011-2015) low human capacity in the public administration remains a key constraint to the implementation of the inclusive growth reform agenda.

4.16 The project, along with FIAS/IFC, supported the implementation of a number of legal reforms through advice, staff training studies. A revised Commercial Code was adopted in 2005, some six months before the closure of the project and it was updated again in 2009 after project closure. A new Tourism Law was adopted in 2004, and a new Labor Code in 2007 (Lei Nº 23/2007 de 1 de Augusto). According to donors and private sector lawyers interviewed during the PPAR mission (April 2012), the new Commercial Code constitutes a significant improvement over the earlier one, which dated from the late 19th century, though there is still room for further improvement. The new Labor Code is also more flexible in terms of hiring and firing of workers (reduction in severance pay and termination notice periods); relaxed restrictions for fixed term contracts; and simplified recruitment of foreign workers; and has introduced better dispute resolution mechanisms through arbitrage committees. However, initial evidence from implementation of the new labor law points to concerns over quotas and qualifications vetting and their impact on businesses' ability to hire foreign expertise (ICA, 2009).

Outcome Indicators

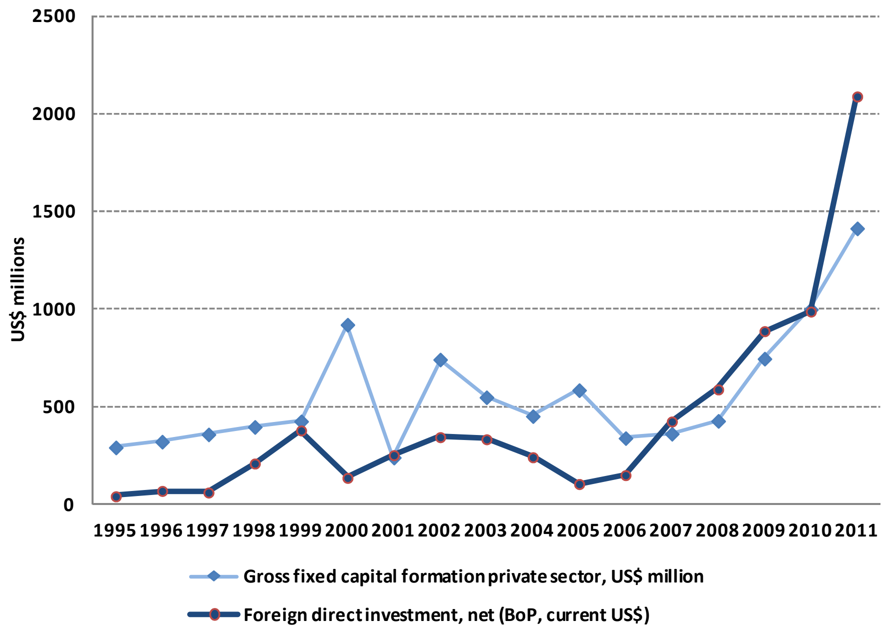
4.17 There were a number of output indicators, but in general, the project did not track outcomes (for example, in terms of job creation, increased productivity among assisted enterprises, etc.) and did not include performance indicators to track the achievement of the project development objective of broadening the base of private participation in Mozambican economic growth. In the absence of such evidence, the PPAR reviewed alternative indicators for private sector participation and contribution in the economy, such as foreign direct investment, capital formation, credit to private sector and employment. While such broad based outcome indicators can be used as a second best, as they are reflective of patterns of private sector growth, attribution to the project is difficult, as mentioned above (para 4.2).

4.18 The project achieved the only intermediate outcome target specified in the PAD of US$5.0 million of linkage sales realized by project supported firms through 57 contracts. By project closing, US$65 million of linkage sales had been realized by project supported firms through 180 contracts. Though the project did not track productivity, the ex-post (beneficiary) survey conducted by the final project evaluation team found that of 42 firms (67 percent of the assisted) indicated that they realized moderate or high benefits from this assistance through improved product quality, more efficient production processes, and better management and financial systems. Several case studies and interviews of beneficiaries conducted by the project team, although falling short of rigorous evaluation, also document benefits to project beneficiaries in different sectors.

4.19 Overall, following the project period, Mozambique experienced rapid economic growth. In 2010 the real growth rate was 6.8 percent and was projected to grow at 7.2 percent in 2011 (IMF, 2011). However, it is unlikely that an expanded domestic private sector contributed in any significant way to this, as growth seems to have been primarily externally driven by the mega projects and other foreign investment and foreign aid. As the IMF Article IV Consultation report of 2011 states: “GDP growth in Mozambique is driven by: (i) large foreign direct investment linked mainly to mining, electricity, tourism, construction and telecommunication sectors; (ii) high levels of overseas development assistance – averaging US$89.2 (one of the highest aid/GDP ratios in Africa); and (iii) strong growth in the agriculture sector. The GDP growth, thus, is not reflective of broad-based private participation in the economy.” Likewise an Economist Intelligence Unit report also noted that “there is still concern that the economy is growing at two speeds. Although the dynamic, capital intensive export sectors – dominated by the Mozal and Sasol megaprojects – are growing strongly, with the help of large inflows of Foreign Direct Investment, economic activity in the rest of the private sector is well below potential” (EIU 2007).

4.20 Capital formation increased, from about US$2.93 billion in the period 2001-2006; to US$3.96 billion between 2007 and end 2011. During this same period, total foreign investment increased from about US$1.45 billion in 2001-06 to almost US$5 billion in 2006-11 (Figure 2). However, most of this private capital formation in Mozambique has been financed by large-scale foreign investors with access to international capital markets and is not attributable to the project that supported local businesses that lacked effective means to finance their investments (USAID, 2007).

Figure 2. Total Private Fixed Capital Formation and Foreign Investment (1995-2011)



Source: World Bank Development Indicators

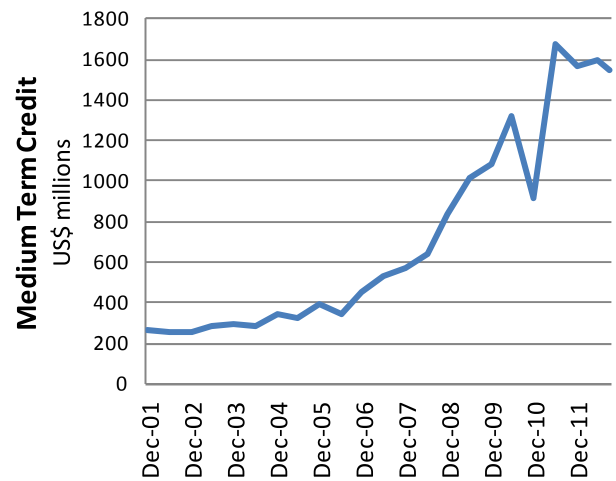
4.21 Merchandise trade as a percentage of GDP also significantly increased, from 32 percent in 1999 to 77 percent in 2011 (WDI 2012). However, Mozambique's foreign trade continues to be dominated by the mega-projects, including aluminum, natural gas pipeline, hydro-electric facility and coal production (OECD 2008). The findings of the Investment Climate Assessment (ICA 2009) also point to the dominance of foreign owned, capital intensive export oriented mega-projects. The contribution of small and medium enterprises-the project's target group-to growth and exports was at best modest which is reflective of the lack of broad based private participation in the economy.[21]

4.22 Private sector credit as a share of GDP also increased in the post project period, albeit modestly. Bank of Mozambique (BOM) data on the total stock of medium term credit outstanding (credit with a term in excess of 2 years) increased from about US$270 million in 2000 to about US$350 million in 2006, at the close of the project. For the principal sectors supported by the project, namely agriculture, industry and transport, the total volume of loans outstanding increased from about US$125 million at the beginning of the project to US$200 million at the end of June 2006. However, big corporations as well as state owned enterprises

[21] "Growth in the past decade has been concentrated at one end of the productive spectrum: foreign-owned, capital-intensive, and export-oriented —mega-projects. These projects are dependent on world commodity prices, have had limited impact on employment creation and productivity spillovers, and until recently, have also brought limited fiscal benefits. At the other end of the productive spectrum are the vast majority of firms, primarily small and medium enterprises (SME), which sell mostly to the local market, face severe resource constraints, and contribute modestly to economic growth and exports. Sustained and broad-based growth in output and employment requires a diversification of exports and production and the creation of a better business environment for greater participation of this part of the Mozambican private sector in the country's economic activity (ICA 2009)."

dominate the credit market. Access to finance (including physical access) for small and medium enterprises, continues to be a challenge, and some of the issues cited in (IMF 2013) remain similar to those that prevailed at the time of the project - lack of adequate credit information due to limited credit registry coverage, high interest rates and the high cost of intermediation. The government is trying to address these issues through legal reform.

Figure 3. Medium Term Credit, All Sectors 2001-2011



Source Bank of Mozambique

4.23 According to the FSAP Update (2009), the private sector credit-to-GDP ratio at 12.8 percent in 2009 is particularly low, up only marginally since the 2003 FSAP. The outreach of the banking sector has expanded but access to financial services overall remains low and fragmented. While large corporations have relatively good access to credit, small and medium enterprises do not. The Investment Climate Assessment of 2009 further adds that the percentage of firms accessing formal finance (13 percent in 2009) is not only low but has declined from previous surveys (29 percent in 2002 and 26 percent in 2005). State owned enterprises, that currently dominate the enterprise sector, account for 80 percent of total non-government credit (ICA, 2009).

4.24 The Investment Climate Assessment (ICA 2009) notes that access to finance was the second most often cited obstacle to business operations by Mozambican firms, confirmed as a key obstacle through empirical analysis linking access to finance indicators to firm-level productivity in Mozambique. The empirical analysis of this ICA, taking into consideration demand factors, found a highly credit constrained environment: more than two-thirds of the sample was credit constrained.[22] Survey results also showed that collateral requirements for lending are high and that financing for investment is largely based on retained earnings.

[22] The percentage of credit constrained firms increased to 82 percent when the sample was limited to credit-demanding firms that (i) had applied for and been denied credit or (ii) had not applied for credit due to reasons such as : ‘application procedures too complex’, ‘collateral requirements unattainable’, or ‘possible loan size and maturity insufficient’.

4.25 Overall, data show a limited role played by small and medium enterprises in formal-sector employment generation - an indicator of the low level of broad based private participation in economic growth. While data from the 2008 Enterprise Survey indicates that the average growth rate of full-time employment between 2003 and 2006 was 44 percent, the ICA of 2009 points out that this figure should be interpreted in the context of a very small base. Employment growth rates of large firms dominated those of small and medium enterprises over the period 2003–06, despite increasing informality.[23] Sixty eight percent of the urban workforce and 87.5 percent of the rural workforce operates informally and overall 75 percent of the economically active population is employed informally in Mozambique (INE, 2006 cited in USAID, 2009). In fact the increasing informality is cited by the surveyed firms in the latest Investment Climate Assessment (2009) as a top constraint (even above access to finance which topped the list in ICA 2003) to private sector development in Mozambique. The balance of the evidence therefore suggests that while during the project period Mozambique's economy grew; the growth was dominated by mega-projects and cannot be attributed to an expanded private sector. *A fortiori*, attribution to the project, particularly given its small size, is tenuous.

4.26 Nevertheless, the project did assist small and medium enterprises and startups to establish industrial linkages with the megaprojects and achieved all but one of the project output targets. The project achieved the only intermediate outcome target specified in the PAD of US$5.0 million of linkage sales realized by project supported firms through 57 contracts. By project closing, US$65 million of linkage sales had been realized by project supported firms through 180 contracts. The project also supported key legal reforms aimed at private sector development and helped set up the economic zone which, despite some issues, continues to further linkage of small and medium firms with the mega projects. However, the project was not successful in increasing SME's access to private credit through the line of credit as the design did not take into account the existing barriers in the broader environment and in the financial sector. But recognizing early the problems with the uptake of the line of credit, the project restructured (halving the line of credit) and largely achieved the revised target. While a rigorous impact evaluation was not carried out and six years after project closure the PPAR mission was not able to collect such data, the available ex post evaluations as well as anecdotal evidence from case studies suggest that several benefits accrued to the project supported enterprises.

4.27 In view of the significant outputs as well as achievement of the intermediate targets **efficacy** is rated as **Substantial**

5. Efficiency

5.1 Efficiency is rated as **Modest**

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[23] According to the World Bank Country Partnership Strategy (2012-2015) about 90 percent of all private businesses in Mozambique are small to medium-size enterprises. Over-regulation, administrative procedures, and rigid labor laws discourage most of these firms from formal registration. However, informal enterprises were not the target of this private sector development project which focused on formal registered enterprises.

5.2 An assessment of whether the costs involved in achieving the project objective were reasonable in comparison with the benefits and with recognized norms cannot be based on traditional measures of efficiency for several reasons. First, since there is no objective measure of achievement of the project objective of broadening the base of private participation in Mozambican economic growth, it is not possible to conclude if the costs of achieving the project results were reasonable. Second, even if the efficiency analysis would focus on the cost-benefit analysis of achieving individual project components, the assumptions on which the PAD bases the cost-benefit analysis are largely theoretical. For example, the assumption that the Technical Learning component would lead to an increase in output of about 10 times the matching grants amount were based on other countries' experience with similar technical learning program. No other explanation was offered by the project team.

5.3 The Economic Rate of Return under the first component alone was 47 percent, assuming that a dollar of the matching grant resulted in an output increase of 10 times the grant amount. This assumption was not supported by any data on what really happened. The PPAR mission was unable to update this information, due to the non-collection of relevant data. This reinforces the message made earlier that much more attention should have been paid to monitoring and evaluation, with particular attention to estimation of outcomes and impact. The assessment of the project's efficiency has thus to be based on aspects of design or implementation that either contributed to or reduced efficiency:

- Lack of an agreed interpretation of the term "majority private Mozambican firms" that was used in project documents to define the enterprises eligible for support under PoDE. The Mozambican authorities defined eligibility as those firms who are majority-owned by Mozambicans while the Bank preferred a broader definition of firms registered in Mozambique. This issue was finally resolved early in 2005, but only after it had limited the pool of potential applicants under both the technical and finance components.
- The finance component faced a number of issues that delayed its start and ultimately led to a reduction in the allocation of the credit line by half. Many of those issues were outside the project's direct control. The excess liquidity in the banking system, the availability of less risky government securities, and the legal and procedural difficulties in collecting on collateral all conspired to make banks hesitant to use the credit line. For small and medium enterprises, high interest rates acted as a disincentive to borrow and a preference for relying on internal sources of financing. PoDE responded through modifying the loan features, and, significantly, allowing a development financial institution, GAPI, to play a large role in disbursing the credit line.
- Weak internal controls at the PIU, especially of financial management, audits and accounts resulted in large numbers of errors in withdrawal applications. These problems intensified in the final eighteen months of the project as activities increased, and with the need to pay the project's many stakeholders under four different donor accounts (the IDA credit and three Trust Funds). The accumulation of inaccuracies and errors in the withdrawal applications resulted in a slowing down of transfers and delays in payments which impacted implementation during that project period and affected the project's transition arrangements. This also served to illustrate overall

project complexity, and weak linkages across the numerous components, that rendered project management difficult, in addition to limiting beneficial spillovers.

5.4 Overall the project was likely not the most efficient or least-cost alternative. The components were not well linked with each other, thus reducing potential spill-over benefits: For example, the technical support to private sector firms could have been used to help develop financially viable projects to be presented to financial institutions for financing. Furthermore, the institutional capacity building component was too broad and dispersed the support among too many beneficiaries. Further, disbanding of the Technical Learning unit resulted in a loss of accumulated experiences.

6. Ratings

Outcome

6.1 Overall project outcome is rated as **Moderately Satisfactory**. The *Relevance of Project Objectives* was High. In principle, the three project components: training, access to finance and institutional strengthening, were all relevant to the project's objectives of broad-based growth. However, the *Relevance of Design* was Modest. The design of the line of credit in particular did not take into account the key constraints in the broader financial environment that would limit offtake, and limit private bank participation. The various components were not meaningfully linked. To some extent reflecting the Bank's practices at the time when the project was approved, M&E design suffered from a shortage of indicators to measure attainment of the project development objectives. *Efficacy* is rated as Substantial. The project did help a number of beneficiary small and medium enterprises to establish industrial linkages with the megaprojects and achieved important outputs including legal reforms. It largely achieved its intermediate outcome targets. The broad set of indicators that IEG used to measure outcomes and the achievement of overall project objectives – in the absence of impact evaluation and indicators that tracked project outcome- showed that after project implementation, the Mozambican economy experienced strong private sector growth, but this growth was largely confined to mega projects. Yet, IEG acknowledges difficulties of attribution of these overall outcomes to the project. *Efficiency* is rated as Modest since overall the project was overly complex, yet its myriad components were not well linked with each other, thus reducing potential spill-over benefits. Moreover its excessive complexity contributed to project management difficulties, especially towards the end of the implementation period.

Risk to Development Outcome

6.2 The PPAR rates the risk to development outcome as **Low.**

6.3 The ICR rated the risk to development outcome as Modest based on the following: the PIU was disbanded, a new contract with the contractor who had managed the TLC component was not envisaged hence availability of business development services and training especially outside of Maputo was impacted and the Line of Credit had not worked.

6.4 Actual developments suggest that the risk to development outcome has since declined. Promotion of private sector development continues to have a high priority for the government and its G-19 development partners. IDA has continued to provide support to training and learning within firms through a subsequent private sector development project (CPSDP). The policy reforms that PoDE helped realize are likely to remain in place. The government is likely to remain committed to the process of improving the business environment investment climate. The Investment Promotion Center (IPC) was asked by IFC to take over management of the MOZAL linkage program, and the Investment Promotion Center reported to the PPAR mission that Government funding has been secure since PoDE's closure. On the institutional front, the IPC continues to function, the Industrial Zone in Belualane continues to grow though there is scope for improvement with respect to both.

6.5 Although the revolving fund has not been set up, the landscape with respect to credit for small and medium enterprises has changed. IFC has extended two specific loans to a commercial bank, (BCI) with the objective of expanding access to medium term credit for small and medium enterprises, and is proposing to extend this to other banks as well. These projects have assisted the Bank in extending financing to the small and medium enterprises, including women entrepreneurs (Gender Finance) as well as growing its retail business in line with IFC's strategy. IFC will replicate this approach with other banks, including supporting the establishment of new greenfield banks to spur competition in the sector, and potentially local currency lending.[24]

6.6 To build on the advances supported by the project, IDA undertook a new project, (CPSDP), approved in 2009 built around the following pillars: (i) improving enterprise competitiveness, including through matching grants for business development services; and (ii) improving the business enabling environment through support to Mozambique's Business Environment Strategy (focus on trade facilitation, licensing reform and public private dialogue). This later project effectively incorporated key lessons from the present project (PoDE). Its PIU is located within the Ministry of Industry and Commerce with the goal of mainstreaming project management functions. At the same time, the World Bank is providing further technical support to technical and vocational education training through the PIREP project.

6.7 Finally, the macro-economy continues to be satisfactory under the IMF's Policy Support Instrument Program (IMF Country Report No. 12/140). The country managed the recent economic and financial crises well, including the resulting social problems. The country continues to enjoy considerable external support. According to the most recent Financial Sector Stability Assessment, the financial sector appears to be in much better health than ten years ago. Inflation decreased from about 16 percent at end 2010 to about 2.5 percent in February 2012 (source IMF Press Release No. 12/91) and if maintained should over time lead to lower interest rates.

Bank Performance

6.8 Bank performance is rated **Moderately Unsatisfactory.**

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[24] World Bank, Country Assistance Strategy 2012-2015

QUALITY AT ENTRY

6.9 Quality at entry is rated **Moderately Unsatisfactory**. The project's objectives were aligned with the country's priorities and bank's assistance strategy. However, the project quality at entry had some important deficiencies:

- The analysis with respect to the SME credit did not take into account the lessons learned from previous projects where the Line of Credit was not successful. In 1998, for example, the ICR of the predecessor loan, the IDA financed Small and Medium Enterprise Development Project (Cr. 2082), highlighted the devastating outcome of its Line of Credit, under which 73 percent of the sub-loans defaulted. A similar experience was reported in the PAD for the Industrial Enterprise Project, which also closed in FY99.The PAD acknowledged that the "now closed IDA-financed SMEDP line of credit was viewed as a failure, both in terms of "disbursement and repayment effectiveness," the decision to go ahead was based on the perception that the "environmental conditions for a second line of credit for essentially the same purpose have improved dramatically."
- The PAD had acknowledged that high short and long-term interest rates and a weak credit disciplinary environment were serious problems for increasing intermediation, but concluded on the basis of interviews with bankers that the latter would be interested in increasing term lending if they had an appropriate term funding base. The project did not identify any risk of potential participating financial institutions limited appetite for the targeted segment. The evidence of poor design was reflected in initially slow disbursements, even though nine banks had signed up. Sub-project eligibility criteria in terms of firm ownership and collateral requirements were considered too severe and the cost of resources too high. The line of credit had to be halved. It finally accelerated thanks to the expanded role of a public development finance institution among participating financial institutions, the raising of the loan limit for the first time borrowers from US$15,000 to US$ 40,00 and the expansion of eligible borrowers to include foreign owned enterprises in addition to Mozambican enterprises.[25]

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[25] The restrictive eligibility criterion for beneficiary firms which were confined to 'domestic enterprise' or 51 percent local ownership restricted the pool of eligible enterprises. The evidence of the design flaw is that this restrictive criterion had to be dropped and the Development Credit agreement was modified. The aid memoire dated December 3, 2001, sums up many of the issues with the credit line: "*Prospective clients feel that it was… inaccessible and expensive (interest is almost 40 percent), commercial banks find the project risky and would like a mechanism to share the risk (guarantee fund). In addition, commercial banks had to reject several viable projects due to the restrictive eligibility requirements for sector-specific and ownership criteria. On the first time Borrower credit line, banks and clients reconfirmed that the maximum credit should be raised to US$40,000, which has been agreed with IDA"* Likewise, the above restrictive eligibility criterion also applied to technical learning.. The Aid memoire dated 2004 thus states*: " Firms whose capital is not held in majority by Mozambican citizens have been precluded from accessing the assistance of PoDE/CAT under the Firm Competitive Office (FCO). Based on discussion with several matching grant experts as well as firms in Mozambique, it is the mission's view that this practice is resulting in delaying or denying training to what could be thousands of Mozambicans*"

- The institutional arrangements for the technical assistance were complex, and the capacity-building component included too many partners: the Investment Promotion Center, the Belualane Industrial Zone, several Ministries – Industry, Commerce and Tourism, and a variety of Private Sector Institutions. Too much dispersion in capacity building components limited deeper institutional reforms and put a strain on the already weak capacity in the newly created coordination unit.
- Finally, although perhaps reflecting prevailing practice at the time of project preparation, the project suffered from significant shortfalls in terms of an appropriate monitoring and evaluation framework This impacted the tracking and assessment of the achievement of the project development objective.

QUALITY OF SUPERVISION

6.10 Quality of Supervision is rated **Moderately Satisfactory.** The project had two supervision missions per year and carried out an in-depth preparatory mission prior to the mid-term evaluation as suggested in the Project Appraisal Document There was a high degree of continuity as the project had two TTLs throughout the project life and both were based in Maputo. This also facilitated continuity in project management, and liaison with authorities. Responding to needs as they arose, the project reallocated funds as needed for example for building infrastructure at the Beluluane Industrial Park. The Bank team was also instrumental in stressing to the authorities the need to adequately fund the Investment Promotion Center after the closure of the project, with positive results. The Bank was quick to modify the matching grant program to allow full travel subsidy outside Maputo; this allowed for much greater outreach and contributed to expanding the project's impact. The Bank drove the process of building the capacity and transferring additional responsibility to the local staff working in the Technical Learning Program, thus ensuring that the gained expertise would remain in country. The Bank recognized early on the problems in the implementation of the line of credit and recommended reallocation and even cancellation of the credit line. The Bank approved GAPI- a development finance institution - to access the credit line. Though it did not address the problem of access to private credit, it finally resulted in the disbursements of the loans.

6.11 However there were several shortcomings in supervision too. The Bank Loan Administration Department identified and flagged an increasing number of errors in withdrawal requests, but the Bank's Financial Management Unit was slow to respond to the risk of significant underlying financial mismanagement issues. A subsequent independent audit confirmed the weaknesses in financial management but found no evidence of financial fraud, though there was an overpayment of $47,500, about 0.12 percent of total disbursements which was reimbursed to IDA. In retrospect, the Bank's Financial Management Unit should have been more proactive in following up, conducting on-site inspections and providing written assessment of the PIU's financial management weaknesses, and reporting to Bank management.

6.12 Candor and Quality of Performance Reporting is also wanting in that despite implementation difficulties in several areas, as well as the perception of weaknesses in financial management, the Implementation Progress (IP) rating was systematically satisfactory until the final ISR. This did not reflect the many difficulties faced by the project, and the ratings should have been lowered much earlier. Indeed the ICR itself says, with respect to financial management, that "a downgrading of the IP rating as withdrawal request errors accumulated eighteen months before project closing could have alerted management of the severity of the financial management difficulties faced."

6.13 The project lacked a well-structured monitoring and evaluation system, to some extent reflecting the Bank's practice at the time of project approval. A strengthened framework that was added one year before the closing of the project still did not include indicators to fully assess the achievements of overall project objectives.

6.14 Based on Moderately Unsatisfactory Quality at entry and Moderately Satisfactory Quality of Supervision, Overall Bank performance is rated **Moderately Unsatisfactory**, in accordance with the IEG/OPCS harmonization criteria.

Borrower's Performance

6.15 Borrower's performance is rated **Moderately Unsatisfactory.**

GOVERNMENT PERFORMANCE

6.16 Government Performance is rated **Moderately Satisfactory**. The government was fully engaged in the design of the project and committed to its success. The private sector development unit in the Ministry of Commerce was committed to reforming the policy environment throughout the project and took a lead role in advocating for a more enabling environment for the private sector. But there were two areas of weakness. First, the Government initially restricted eligibility to firms that were owned at least 51 percent by Mozambican nationals, agreeing to change this position only at the midterm review. But having agreed to the change, the authorities then vacillated and delayed the signature of the modified Credit Agreement for ten months which meant that the decision did not become active until the last year of the project, with an adverse impact on project implementation. Second, the government was slow and erratic in disbursing counterpart funds, most of which were supposed to finance salaries at the Investment Promotion Center which also compromised the efficiency of this key component of the project.

IMPLEMENTING AGENCY

6.17 Implementing agency performance is rated **Moderately Unsatisfactory.** During the first three years of the project, financial management appeared satisfactory, though slow. Irregularities, if any, went unnoticed in four unqualified audit reports but were eventually discovered by the Bank team. In 2004 the Loan Operations Accounting Department (LOA) identified and flagged an increasing number of errors in withdrawal requests. Eventually, IDA decided to suspend the replenishment of special accounts in late 2005. New auditors were selected in 2006 and a special independent audit for the project as a whole was conducted. The audit did not find any evidence of financial fraud. There were, however, overpayments of $47,500; about 0.12 percent of total disbursements.

6.18 Procurement also suffered from increasing weakness as the project progressed on account of weak capacity and the multiplicity of stakeholders, resulting in incomplete documentation, last minute requests, and slow response time. IDA provided substantial assistance but it did not result in the removal of all the procurement delays. Overall, there was no evidence of mis-procurement.

6.19 In interviews with the PPAR mission the Project Director emphasized the complexity of the project and its financial management arrangements, stating that the undisputed claims of slowness in the latter half of the project with respect to disbursements and procurement resulted from a desire to avoid even the appearance of financial improprieties. The Director, and a number of other persons interviewed, also pointed to sometimes strained relations with Bank staff which also impeded project management. Given the shortcomings in financial management as well as procurement and the lack of adequate arrangements for monitoring and evaluation, the performance of implementing agencies is rated as moderately unsatisfactory.

6.20 Based on Moderately Unsatisfactory implementing agency performance and Moderately Satisfactory government performance, Overall Borrower performance is rated **Moderately Unsatisfactory**, in accordance with the IEG/OPCS harmonization criteria.

Monitoring and Evaluation

6.21 This PPAR rates the Monitoring and Evaluation as **Modest**

6.22 Design: The M&E design had significant weaknesses. The project did not have a formal monitoring and evaluation framework (Bank projects before 2000 were not required to do so) and the project's log frame did not track final outcomes or all intermediate outcomes. Efforts to retrofit a framework were noted in the project's ISR as of June 2005, where it was first used, one year before project closing. The key performance indicators were refined to better reflect expected outputs, regional outreach and to establish some benchmarks, but did not include outcome / impact indicators to measure achievements of project development objectives. Most indictors were output indicators and measurable outcome data were mostly not tracked. Responsibility for the collection of performance data was dispersed among the various sub-agencies without a clear system for data collection or collation.

6.23 Implementation: The limited availability of measureable indicators to track intermediate and final outcome impacted good project management, particularly for results. Data collection arrangements, albeit with diverse agencies, were made but there seems to have been little consolidation either at the PIU or by the IDA team.

6.24 Use of M&E. Little use was made of the M&E system, largely reflecting its inherent design and implementation weaknesses. There is no evidence that the information collected through the M&E system was analyzed and used to modify project management and/or resource allocation. Rather, such information originated from day to day contacts between the PIU and the IDA TTLs who were based in Maputo as well as from the mission Aide-Memoires.

7. Lessons

The assessment draws four lessons:

7.1 *In post conflict countries with weak institutions and capacity constraints, achieving major economic reforms requires continuous effort and liaison with many ministries and agencies, over a substantial period of time.* Rather than a single project with multiple components, a programmatic approach could also have provided opportunities to learn from each phase as inputs to designing the next. The value of a phased approach was demonstrated by the follow on private sector development project, which incorporated lessons from the present project. This is another reason why multi-donor multi-year operations, with significant policy and institutional development content, have a very important role to play, and could be complementary to stand-alone operations.

7.2 *Matching grant programs can potentially be an effective way of providing incentives to firms. To be successful such programs have to be well managed.* Outsourcing to a well-established and well run institution with the right expertise helps. A successful matching grant program for business services requires a combination of international expertise, local knowledge, autonomy in administration, and adaptability to respond to market demand. Project's outsourcing of the management of the matching-grant to a firm with solid expertise in the field contributed to its relative success.

7.3 *Too much dispersion in capacity building components could limit deeper institutional reforms.* The main lesson from the Institutional Capacity Building component is that it is important to avoid focusing simultaneously on too many issues at the same time– in this case promoting investment, developing an industrial zone, building ministerial capacity, supporting private sector institutions, and improving the business environment. The impact would have been deeper if institutional reforms had been addressed in separate projects.

7.4 *Credit line operations that are designed solely to increase the supply of funds do not increase sustainable access to finance if other institutional, legal and regulatory constraints to financial sector development are not addressed.* Lines of Credit require careful preparation, including assessments of: (i) overall demand; (ii) factors that dampen demand (such as high interest rates); and on the supply side (iii) factors that may limit commercial banks' appetite to lend to small and medium enterprises, even if they have the resources (e.g. limited information on borrowers' creditworthiness legal, regulatory environment, and firm-level constraints).

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Annex A. Basic Data Sheet

REPUBLIC OF MOZAMBIQUE: ENTERPRISE DEVELOPMENT PROJECT (P049874) (IDA-33170, IDA-3317A, EECT-28406, NORW-24286, UK-27799)

Key Project Data (amounts in US$ million)

	Appraisal estimate	Actual or current estimate	Actual as % of appraisal estimate
Total project costs	26.00	24.96	95.99
Loan amount	26.00	26.00	100.00

Cumulative Estimated and Actual Disbursements

	FY00	*FY01*	*FY02*	*FY03*	*FY04*	*FY05*	*FY06*	*FY07*	*FY08*	*FY09*
Appraisal estimate (US$M)	2.84	8.13	15.57	25.05	26.00	26.00	26.00	26.00	26.00	26.00
Actual (US$M)	0.00	3.89	6.69	9.78	13.27	19.06	23.58	24.98	24.98	24.96
Actual as % of appraisal	0.00	47.82	42.93	39.03	51.05	73.31	90.71	96.08	96.08	85.99
Date of final disbursement:	October 2008									

Project Dates

	Original	Actual
Initiating memorandum	05/21/1998	05/21/1998
Negotiations	02/11/1999	02/11/1999
Board approval	09/14/1999	01/27/2000
Effectiveness	08/31/2000	08/31/2000
Closing date	06/30/2005	06/30/2006

Task Team Members

Names	Title	Unit	Responsibility/Specialty
Lending			
Tyler S. Biggs	Consultant	PRMTR	private sector development Specialist
Neil Simon M. Gray	Chief Admin. Officer	LCRRM	Joint TTL at preparation
Anthony Martin Hegarty	Chief Financial Management Off	LCRRM	Financial Management
V. S. Krishnakumar	Manager	AFTPC	Procurement
Brian David Levy	Adviser	PRMPS	Joint TTL at preparation
Marilyn Swann Manalo	Sr Operations Off.	AFTPS	Joint TTL at preparation
Francesco Sarno	Consultant	AFTS3	Procurement
Andrew L. Singer	Consultant	AFTP4	Matching Grant Schemes
Jose M. Sugar	Consultant	LCSAR	Disbursement
Kishor Uprety	Sr Counsel	LEGMS	Counsel
Supervision/ICR			
Maxwell I. Aitken	Senior Manager	CSMST	Advice SME TA & Financing
Sherri Ellen Archondo	Sr Operations Off.	AFTFS	TTL (1999-2002)
Slaheddine Ben-Halima	Sr Procurement Spec.	AFTPC	Procurement
Mazen Bouri	Young Professional	YPP	ICR
David Bridgman	Lead Investment Promotion Offi	MIGOP	Investment Promotion
Paul A. Burnett	Finance Analyst	LOAG2	Disbursement
Gerard A. Byam	Director	AFTQK	Advice on Credit Line
Antonio L. Chamuco	Procurement Spec.	AFTPC	Procurement
Muhamet Bamba Fall	Underwriter	MIGOP	Investment Promotion
Joao Francisco Ferreira	Finance Officer	LOAG2	Disbursement
Teresa De Jesus S. McCue	Finance Analyst	LOAG2	Disbursement
Suzanne F. Morris	Senior Finance Officer	LOAG2	Disbursement
Maria Isabel Nhassengo-Massingue	Procurement Asst.	AFCS2	Disbursement
Michael Ochieng	Lead Finance Officer	LOAG2	Disbursement
Miguel-Santiago da Silva Oliveira	Finance Analyst	LOAG2	Disbursement
Bradford L. Roberts	Operations Officer	CSMLK	Business Development
Cecilia Sager	Lead Investment Promotion Offi	MIGOP	Economic Zones
Ahmet I. Soylemezoglu	Lead Financial Sector Speciali	AFTFS	Advice on Credit Line
Adelia N. Chebeia Suurna	Program Assistant	AFCS2	Program Support
Joao Tinga	Financial Management Analyst	AFTFM	Financial Management
Ronaldo Toledo	Investment Officer	CGMDR	Investment Promotion
Gilberto de Barros	Sr Private Sector Development	AFTPS	TTL (2003- end of project

Staff Time and Cost

Stage of Project Cycle	Staff Time and Cost (Bank Budget Only)	
	No. of staff weeks	USD Thousands (including travel and consultant costs)
Lending		
FY98		111.84
FY99		173.97
FY00	16	61.46
Total:	**16**	**347.27**
Supervision/ICR		
FY00	4	7.33
FY01	16	60.70
FY02	14	51.63
FY03	29	114.43
FY04	25	91.14
FY05	16	68.05
FY06	23	94.47
FY07	14	79.13
Total:	**141**	**572.14**

Annex B. List of Persons Met

Organization	Name	Function
Banco Comercial e do Investimento	Manuel Soares	Director
	Ibraimo Bhai	Director Central
	Daniela Santos	Coordenadora
Banco Nacional de Investimento	Adriano Maleiane	CEO
Banco Terra	David Gerbrands	Director
Beluzone	Neima Jossub	Legal Manager
	Nelson Ventura	Chief Executive Officer
Cimpogest	Gerry Marketos	Managing Partner
	Kenneth Gunn	Director
Organization	**Name**	**Function**
Centro de Promoção de Investimentos	Lourenço Sambo	Director General
	Gil Bires	Director Projects Department
	Lúcia Mendes	Project Officer
CTA (Confederação das Associões Economicas)	Eduardo Macuácua	Economic Assessor
DANIDA	Theo Larsen	Adviser
Enterprise Development Project/PoDE	Mariamo Carimo	Project Director
European Union	Myriam Sekkat	Attachée
GAPI	Antonio Souto	PCA
	Anabela Mucavele	Director
International Finance Corporation	Vivian Owuor	
	Florença Rashid	
Millenium Bank	Omar Mithá	Director
Ministry of Planning and Development	M.Usman	Advisor
Organization	**Name**	**Function**
Ministry of Trade	José Egidio Paulo	Coordenador
	Florêncio Chavango	Economist
Norwegian Embassy	Carlos Mate	Assessor
PACDE	Carlos Sergio Macamo	Coordenador
	Artur Gobe	Gestor do MESE
	Victor Tivane	Business Growth Scheme Advisor
Sal & Caldeira	José Manuel Caldeira	Managing Partner
Speed Mozambique	António S. Franco	Economist
TechnoServe	Jane Grob	Director, Invesment Advisory
USAID	Elsa Malipele	Agribusiness and Rural Finance Advisor
World Bank	Patrick Verissimo	Sr. Agricultural Economist
	Mazen Bouri	Sr. PSD Specialist

Annex C. Mozambique's Financial Sector and Lines of Credit

THE BANKING SECTOR.

1. Mozambique was sparsely banked in 1987 with only 3 commercial banks, one other credit institution, one insurance company, and no microfinance institutions. The situation barely improved over the next two years, the most notable development being the establishment of 22 foreign exchange bureaux. But there was substantially more growth in the period 1997-2010, so that by the end of 2010, the number of commercial banks had increased to 16. There were also 11 credit cooperatives, 3 leasing companies, 24 foreign exchange bureaux and 117 microfinance institutions.

2. At the same time, however, most banks were concentrated in urban areas, especially Maputo, Beira and Nampula. Even in 2010, there were only 385 branches in 52 districts, so that 76 districts, corresponding to 60 percent of the country, were without any banking services at all.

Annex C, Table 1: Financial Institutions, 1987-2010

Type of Institution	1987	1997	2007	2010
Commercial Banks	3	5	12	16
Credit Cooperatives	0	1	11	11
Financial Leasing Companies	0	1	3	3
Other credit institutions	1	0	1	1
Investment Companies	0	0	1	1
Foreign Exchange Bureaux	0	22	24	24
Insurance Companies	1	2	4	4
Correctoras de Segura	0	0	7	7
MicroCredit Institutions	0	0	59	117

Source: *Ministerio da Administracao Estatal, Estrategia de Financas Rurais em Mocambique*

CREDIT GROWTH.

3. The period prior to the Enterprise Development Project was characterized by macroeconomic instability and serious problems in the financial sector. Instability soon after Board approval of the project was on account of disastrous floods which led to a recession as well as a banking crisis in which two of the largest banks, that had had special privileges in terms of purchase and holdings of Treasury Bills, had to be recapitalized. There was a significant increase in interest rates and a concomitant rise in inflation soon after the project was approved, which contributed to reduced demand for loanable funds.

LINES OF CREDIT: INTEREST RATES AND ONLENDING ARRANGEMENTS

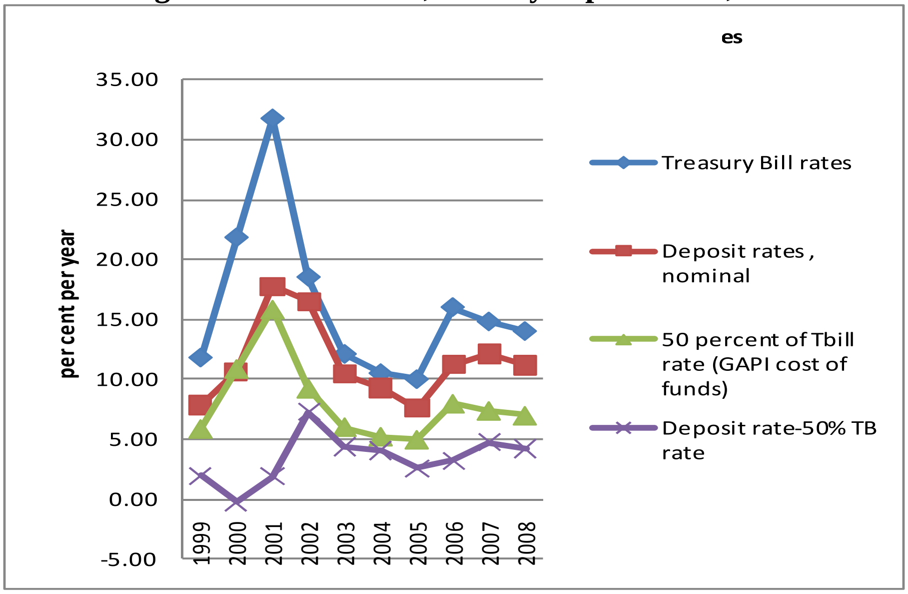
The Bank's Enterprise Development Project (PoDE).

4. The line of credit under the EDP, for US$10 million, was to be disbursed through the Bank of Mozambique (BdM) to eligible Participating Financial Intermediaries. These would pay the BdM the 6 month variable deposit rate and on lend at market rates of their determination in local currency (metacais). There were two facilities: (i) a special line for first time borrowers initially limited to US$15,000 per loan and subsequently increased to US$40,000 and (ii) a traditional line (i.e., for any borrowers, not only startups) of up to US$300,000. Initially, 9 banks signed up, but disbursements initially proceeded very slowly because sub-project eligibility criteria were considered too severe and the cost of resources too high. As a result, the line of credit was reduced by 50 percent to US$5 million, and a Development Finance Institution- GAPI *Sociedade de Promoção de Pequenas e Medias Empresas* (Company for the Promotion of Small and Small and Medium Enterprises)– was encouraged to assume a significant role as a Participating Financial Intermediary.[26] Following this, disbursements did pick up and by the time the operation closed in 2006 a total of US$4.34 million had been disbursed of which 75 percent by GAPI and most of the remainder by one commercial bank, BCI. It was agreed that PFIs could make loans directly in foreign exchange, for the benefit of participating exporters. However most loans were made in local currency (metacais), with margins of 6-8 percent over the cost of funds, and 3-6 percent in the case of GAPI. Early evidence suggested that repayment rates were high, in excess of 95 percent, however this applied to only a part of the loans and final repayment could not be assessed at the time of loan closure as most of the term loans were still outstanding. It was suggested that the Central Bank (BdM) would create a revolving fund using the proceeds of the repayments. However, the fund has not been set up in the six years since the closer of the project. There is no agreement with the BdM in this regard.

5. Participating financial institutions were supposed to pay the BdM the 6 month deposit rate, and they charged market interest rates for their loans. The Bank of Mozambique, acting as trustee for the Government, earned the difference between the cost of IDA funds and the six month deposit rate, and participating financial institutions made market determined spreads. By contrast, GAPI reported to the PPAR mission that it negotiated a preferential rate equal to 50 percent of the Treasury Bill rate, and this was confirmed by the director of the EDP project. The result was an implicit interest rate subsidy to GAPI of between 2.5 and 4.75 percent depending on the year, which GAPI said it passed forward to its sub-borrowers.

[26] GAPI was originally set up by the Friedrich Ebert Foundation (FEF) – a German NGO – in order to promote local development through small firms. The institution was originally named "Gabinete de Consultaria et Apoio á Pequenia Industria." (Bureau for Consultancy and Assistance to Small Firms. In 1990, this was transformed into a financial institution, jointly owned by FEF and the BPD (the People's Development Bank, and subsequently into a joint stock company in 1999, with capital owned by the Friedrich Ebert Foundation and the Ministry of Planning and Finance (MPD) who acquired BPD shares when this Bank was privatized. MPD shares were subsequently to be sold to private investors but this has not yet occurred. GAPI is a non-deposit taking institution, and draws its funds from its own capital as well as a number of donors (KfW, USAID, the Nordic Development Fund, the African Development Fund, and exceptionally the World Bank (through IDA's PoDE project). Traditionally, GAPI has borne no risk on funds accessed through Lines of Credit (except for PoDE). PoDE has specialized on lending to Agricultural and Industrial Enterprises in the provinces. (Simonetti et al, 2007).

Annex C Figure 1: T-Bill Rates, 180 day deposit rates, and GAPI's Cost of PoDE Funds



Source: IMF, Bank of Mozambique and Mission estimates

OTHER INTEREST AND ON-LENDING RATES: EIB, IFC AND USAID

6. The **European Investment Bank (EIB)** also established a line of credit in favor of a number of commercial banks in 1999, also for US$10 million at a rate of one percent in foreign exchange. It was understood that commercial banks would on-lend at the LIBOR (six month interbank) rate plus an unrestricted commercial margin. Fifteen loans were made for a total of €5.6 million, with loan values ranging from €200,000 to just under €500,000 and an average loan size of €375,000. Like the IDA Line of Credit, this did not disburse quickly and EIB cancelled 50 percent of it in 2003, mainly because the local banks overestimated the demand for small and medium enterprise borrowing at the time of appraisal. Moreover, after signature (1999) interest rates started to rise sharply, quickly attaining about 35 percent. Thus IDA was not alone in experiencing difficulties with disbursements of its loans.

7. On the other hand **IFC's subordinated loan** to the Banco Comerciale de Investimento (BCI) of US$8.5 million for small and medium enterprises, by increasing its Tier 2 capital, was successful in fully disbursing. The loan was also accompanied by a technical assistance loan from IFC's medium and small enterprise facility to enable BCI to strengthen the institution's capabilities with respect to credit approval processes and marketing for the medium and small enterprise market segment; risk management and internal controls, especially branch compliance and controls; branch management, especially, enabling branches to cross sell and better serve the medium and small enterprise segment. IFC offered training to about 100 women entrepreneurs some of whom were also BCI customers. This loan was fully disbursed and followed by a second one of US$30 million, extended in 2010. As of 2012, disbursements by BCI of the latest loan had attained US$19 million.

8. It is interesting to note that IFC, in its 2008 loan to the Banco Comercial e de Investimento (BCI), included the provision of technical assistance to BCI to help it improve its capacity to provide technical assistance to sub-borrowers in the preparation of projects. And IDA's next private sector development project following PoDE – the Competitiveness and Private Sector Development Project (CPSDP) – set up an arrangement with IFC so that sub-borrowers from BCI, under the IFC loan to BCI are able to get technical assistance from the matching grants facility of the CPSDP project. The 2008 IFC project in fact made a subordinated loan to IFC, which enabled it to increase its tier II capital, so enabling it to increase the amount of loans it could make to clients. Funds were on-lent in domestic currency to commercial sub-borrowers with margins of 6-8 percent. BCI told the PPAR mission that these margins were the same as those applied to PoDE funds. The 2010 follow up loan was a senior loan, priced at LIBOR plus 350 basis points.

9. There was no evidence of any subsidized credits being extended by Government to SMEs/targeted sub-borrowers. The ICR reported that the IDA line of credit was compromised by subsidized lines of credit from USAID pertaining to flood relief (in 2001) and the European Investment Bank (EIB). No evidence could be found pertaining to USAID. EIB gave two lines of credit, the first in 1999 and the second in 2003. As explained above, EIB lent to PFIs at 1 percent in foreign exchange and they had to on-lend in domestic currency at the MAIBOR rate plus a risk margin of their choice.