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The World Bank

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Report No: PAD2182

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

PROJECT APPRAISAL DOCUMENT

ON A

PROPOSED LOAN

IN THE AMOUNT OF US$15 MILLION

TO

JAMAICA

FOR A

JM ACCESS TO FINANCE FOR MICRO, SMALL, AND MEDIUM ENTERPRISES PROJECT

December 29, 2017

Finance, Competitiveness, and Innovation Global Practice
Latin America and Caribbean Region

CURRENCY EQUIVALENTS

(Exchange Rate Effective November 16, 2017)

Currency Unit =	Jamaican Dollar (J$)
J$125.73 =	US$1
US$0.01 =	J$1

FISCAL YEAR

April 1 - March 31

ABBREVIATIONS AND ACRONYMS

AFI	Approved Financial Institution
AML/CFT	Anti-Money Laundering/Combating the Financing of Terrorism
BDS	Business Development Services
BOJ	Bank of Jamaica
BRR	Borrower Risk Rating
CBA	Cost-Benefit Analysis
CEF	Credit Enhancement Facility
CPS	Country Partnership Strategy
COSO	Committee of Sponsoring Organizations of the Treadway Commission
DA	Designated Account
DBJ	Development Bank of Jamaica
DTI	Deposit-Taking Institution
E&S	Environmental and Social
EGC	Economic Growth Council
EPIC	Entrepreneurship Program for Innovation in the Caribbean
ERM	Enterprise Risk Management
ESMF	Environmental and Social Management Framework
ERR	Economic Rate of Return
FCGP	Foundations for Competitiveness and Growth Project
FDI	Foreign Direct Investment
FM	Financial Management
FSAP	Financial Sector Assessment Program
FSC	Financial Services Commission
GCT	General Consumption Tax
GDP	Gross Domestic Product
GHG	Greenhouse Gas
GOJ	Government of Jamaica
HR	Human Resources
IDB	Inter-American Development Bank
IFC	International Finance Corporation

IFR	Interim Financial Report
IMF	International Monetary Fund
ISO	International Organization for Standardization
IT	Information Technology
JCCUL	Jamaica Co-operative Credit Union League Limited
JMMB	JMMB Securities Limited
JSE	Jamaica Stock Exchange
LAC	Latin America and Caribbean
LP	Limited Partnership
M&E	Monitoring and Evaluation
MFI	Microfinance Institution
MIS	Management Information System
MOFPS	Ministry of Finance and the Public Service
MSMEs	Micro, Small, and Medium Enterprises
NBFI	Non-bank Financial Institution
NPCB	National People's Cooperative Bank
NPL	Nonperforming Loan
NPV	Net Present Value
OM	Operations Manual
PCG	Partial Credit Guarantee
PEVC	Private Equity and Venture Capital
PIOJ	Planning Institute of Jamaica
PIU	Project Implementation Unit
PPSD	Project Procurement Strategy for Development
PSC	Project Steering Committee
ROA	Return on Assets
ROE	Return over Equity
SBA	Stand-By Arrangement
SMEs	Small and Medium Enterprises
STEP	Systematic Tracking and Exchanges in Procurement
VC	Venture Capital

Regional Vice President:	Jorge Familiar
Country Director:	Tahseen Sayed Khan
Senior Global Practice Director:	Ceyla Pazarbasioglu
Practice Manager:	Zafer Mustafaoglu
Task Team Leader:	Bujana Perolli

BASIC INFORMATION

Is this a regionally tagged project?	Country(ies)	Financing Instrument
No		Investment Project Financing

[ ] Situations of Urgent Need of Assistance or Capacity Constraints

[✔] Financial Intermediaries

[ ] Series of Projects

Approval Date	Closing Date	Environmental Assessment Category
29-Jan-2018	30-Jan-2023	F - Financial Intermediary Assessment

Bank/IFC Collaboration	
No	

Proposed Development Objective(s)

The Project Development Objective (PDO) is to improve access to finance for micro, small, and medium enterprises (MSMEs).

Components

Component Name	Cost (US$, millions)
Enhancement of the Credit Enhancement Facility (CEF)	5.55
Establishment of an SME Fund	7.00
Improvement of enabling environment for access to finance and Business Development Services for MSMEs	1.56
Project management	0.85

Organizations

Borrower :	Ministry of Finance and the Public Service
Implementing Agency :	The Development Bank of Jamaica

PROJECT FINANCING DATA (US$, Millions)

[ ] Counterpart Funding	[✔] IBRD	[ ] IDA Credit	[ ] IDA Grant	[ ] Trust Funds	[ ] Parallel Financing

Total Project Cost:	Total Financing:	Financing Gap:
15.00	15.00	0.00
	Of Which Bank Financing (IBRD/IDA):	
	15.00	

Financing (in US$, millions)

Financing Source	Amount
International Bank for Reconstruction and Development	15.00
Total	**15.00**

Expected Disbursements (in US$, millions)

Fiscal Year	2018	2019	2020	2021	2022	2023
Annual	0.71	2.99	4.82	4.13	1.78	0.57
Cumulative	0.71	3.70	8.52	12.65	14.43	15.00

INSTITUTIONAL DATA

Practice Area (Lead)
Finance & Markets

Contributing Practice Areas

Climate Change and Disaster Screening
This operation has been screened for short and long-term climate change and disaster risks

Gender Tag

Does the project plan to undertake any of the following?

a. Analysis to identify Project-relevant gaps between males and females, especially in light of country gaps identified through SCD and CPF

Yes

b. Specific action(s) to address the gender gaps identified in (a) and/or to improve women or men's empowerment

No

c. Include Indicators in results framework to monitor outcomes from actions identified in (b)

No

SYSTEMATIC OPERATIONS RISK-RATING TOOL (SORT)

Risk Category	Rating
1. Political and Governance	Substantial
2. Macroeconomic	High
3. Sector Strategies and Policies	Moderate
4. Technical Design of Project or Program	Substantial
5. Institutional Capacity for Implementation and Sustainability	Substantial
6. Fiduciary	Substantial
7. Environment and Social	Moderate
8. Stakeholders	Moderate

9. Other	
10. Overall	Substantial

COMPLIANCE

Policy

Does the project depart from the CPF in content or in other significant respects?

[ ] Yes [✔] No

Does the project require any waivers of Bank policies?

[ ] Yes [✔] No

Safeguard Policies Triggered by the Project	Yes	No
Environmental Assessment OP/BP 4.01	✔	
Natural Habitats OP/BP 4.04	✔	
Forests OP/BP 4.36	✔	
Pest Management OP 4.09	✔	
Physical Cultural Resources OP/BP 4.11	✔	
Indigenous Peoples OP/BP 4.10		✔
Involuntary Resettlement OP/BP 4.12		✔
Safety of Dams OP/BP 4.37		✔
Projects on International Waterways OP/BP 7.50		✔
Projects in Disputed Areas OP/BP 7.60		✔

Legal Covenants

Conditions

Type	Description
Effectiveness	The PIU has been established and staffed by the DBJ in a manner acceptable to the Bank. Paragraph 5.01 (a) of Article V in the Loan Agreement.

Type	Description
Effectiveness	The Subsidiary Agreement has been executed on behalf of the Borrower and the

Type	Description
	DBJ in a manner acceptable to the Bank. Paragraph 5.01 (b) of Article V in the Loan Agreement.
Type Disbursement	Description Component 1. The CEF Operational Guidelines have been updated and adopted by the DBJ in a manner acceptable to the Bank. Section III B.1.(b)(i) in the Loan Agreement.
Type Disbursement	Description Component 1. Evidence, acceptable to the Bank, shall have been furnished to the Bank concerning improvements to the CEF corporate governance framework, including ratification by the DBJ's Board of the CEF Board of Trustees' confirmation of the development of an external and internal audit system for the CEF; and adoption of an amended CEF Trust Deed to ensure an adequate representation of banking and SMEs development expertise amongst the CEF Board of Trustees. Section III B.1.(b)(ii) in the Loan Agreement.
Type Disbursement	Description Component 2. The SME Fund Management Firm shall have been procured in accordance with Section I.D.1(a) of Schedule 2 of the Loan Agreement. Section III B.1.(c)(i) in the Loan Agreement.
Type Disbursement	Description Component 2. The SME Fund shall have been legally established, including the issuance of the SME Bylaws, and is fully operational in accordance with Section I.D.1 (b) of Schedule 2 of the Loan Agreement, all in a manner acceptable to the Bank. Section III B.1.(c)(ii) in the Loan Agreement.
Type Disbursement	Description Component 2. The SME Fund Shareholder Agreements shall, have been executed, pursuant to which private shareholders of the SME Fund have committed an aggregate amount of approximately ten (10) million Dollars, all on terms and conditions acceptable to the Bank. Section III B.1.(c)(iii) in the Loan Agreement.
Type Disbursement	Description Component 2. The SME Fund Agreement shall have been executed, in a manner acceptable to the Bank. Section III B.1.(c)(iv) in the Loan Agreement.

PROJECT TEAM

Bank Staff

Name	Role	Specialization	Unit
Bujana Perolli	Team Leader(ADM Responsible)		GFCLC
Luciano Wuerzius	Procurement Specialist(ADM Responsible)	Procurement	GGOPL
Shonell Jodian Robinson	Financial Management Specialist	Financial Management	GGOLF
Andrey Milyutin	Team Member	Senior Financial Sector Specialist	GFCLT
Daniel Ortiz del Salto	Team Member	Operations Officer	GFCLC
Escarlata Baza Nunez	Counsel	Legal	LEGLE
Hana Salah	Social Safeguards Specialist	Social Safeguards	GSU04
Karina Baba	Team Member	Young Professional	GFCLC
Michael J. Darr	Environmental Safeguards Specialist	Environmental Safeguards	GEN04
Monzerrat Garcia	Team Member	Program Assistant	GFCLC
Pasquale Di Benedetta	Team Member	Senior Financial Sector Specialist	GFCFN
Shanthi Divakaran	Team Member	Senior Financial Sector Specialist	GFCLT
Tatiana Cristina O. de Abreu Souza	Team Member	Finance Officer	WFALA

Extended Team

Name	Title	Organization	Location

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I. STRATEGIC CONTEXT

A. Country Context

1. **The Jamaican economy has historically been affected by low growth and high public debt.** Real gross domestic product (GDP) per capita grew by only 0.5 percent per year between 1990 and 2016 (compared to 1.5 percent for Latin America and Caribbean [LAC], excluding high-income countries, and 3.4 percent for middle-income countries worldwide).[1] High levels of crime, constrained access to credit, cumbersome business regulations, and high energy costs have restricted the rate of economic growth.[2] With a debt to GDP ratio of 121.2 as of March 2017, Jamaica's public debt is among the world's highest, crowding out both private and public investment needed to stimulate inclusive growth and poverty reduction. Although Jamaica had made significant progress in reducing poverty, the national poverty rate more than doubled in the wake of the global economic crisis, from 9.9 percent in 2007 to 24.6 percent in 2013.[3] In 2014, the poverty rate was reduced to 20 percent and declined further following increases in per capita income since 2014.

2. **Fiscal and structural reforms launched in 2013 are helping to reverse the trend of low growth rates and rising debt[4].** Fiscal restraint and well-timed liability management operations have reduced the debt to GDP ratio by around 25 percentage points. GDP growth has seen a modest acceleration since the start of reforms rising to 1.4 percent in 2016 from 0.5 percent in 2013. Employment growth rates have been rising steadily during the past two years, and credit quality has improved. Inflation is at historically low levels, averaging 2.3 percent in 2016 (compared to 9.4 percent in 2013). Falling inflation has enabled the Bank of Jamaica (BOJ) to reduce its policy rate by 150 basis points between the beginning of 2013 and the second quarter of 2017. Starting in July 2017, the BOJ changed its policy rate to the overnight deposit rate paid to deposit-taking institutions at the central bank. This move aims at a transition to inflation targeting and more efficient pass-through to market interest rates.

3. **Jamaica is extremely vulnerable to climate change and faces significant environmental threats due to its geographical location**. The country has suffered significant economic losses from the impacts of climate change. Between 2004 and 2008, five major storm events caused damage and losses estimated at US$1.2billion.[5] Evidence suggests that the country will likely observe increases in severe weather events, such as extreme precipitation, flooding, and increases in the intensity and frequency of hurricanes. Those events could affect the coastal ecosystem, fishing infrastructure, tourism, and the financial sector. Damage from future hurricanes could hinder firms' repayment of obligations, which may affect the performance of bank loans. Additionally, Jamaica's vulnerability to sea level rise is more pronounced than in other regions due to the potential impact of storm surges from tropical storms and hurricanes on the coast, partially affecting coastal development and population displacement.[6]

4. **The outlook is for continued modest growth, although risks are substantial.** The World Bank forecasts GDP growth accelerating slightly to 2.3 percent by 2019, assuming faster growth in the United

[1] World Development Indicators. Average of real GDP per capita growth rates (in 2011 US$, purchasing power parity adjusted).
[2] Government of Jamaica - Economic Growth Council. 2016. A Call to Action.
[3] Data from the Statistical Institute of Jamaica. The latest published statistics are from the 2014 survey of living conditions.
[4] Data cited in this paragraph are from the Ministry of Finance and the Public Service and the Statistical Institute of Jamaica.
[5] United Nations Environment Programme (accessed the website in October 2017).
[6] World Bank. 2010. *The Impact of Sea-Level rise on Developing Countries: A Comparative Analysis (Dataset)*.

States, low world interest rates, and continued commitment from the Government of Jamaica (GOJ) to policy reforms.[7] As a small open economy, Jamaica is exposed to external economic shocks—notably shocks to interest and exchange rates—that pose risks to this outlook and that would need to be managed.

5. **The International Monetary Fund (IMF), the World Bank, and the Inter-American Development Bank (IDB) have been supporting the main pillars of the GOJ's agenda for growth.** Two of the eight pillars outlined in the Economic Growth Council's (EGC) agenda focus on maintaining macroeconomic stability, pursuing debt reduction, and improving access to finance. The former pillar has been supported by an IMF programme through an Extended Fund Facility and the subsequent three-year Precautionary Stand-By Arrangement (SBA) approved in 2016. The access to finance pillar has been supported by the World Bank Group through technical assistance since the 2014 Financial Sector Assessment Program (FSAP).

B. Sectoral and Institutional Context

6. **Jamaica's sustained low economic growth and high fiscal deficits over decades had a significant impact on the development of the financial sector.** The ratio of financial assets to GDP, estimated at 77 percent in 2016 for deposit-taking institutions (DTIs)[8] alone, has been inflated by the large proportion of sovereign debt on the financial sector's balance sheet, which crowded out its primary function of lending to the economy. Credit to the private sector provided by commercial banks remains limited, estimated at 27 percent of GDP in 2016, which is well below the regional average of 45 percent. Bank deposits represent about 38 percent of GDP. Credit is concentrated in loans to households and medium/larger corporate entities. In 2016, lending to micro, small, and medium enterprises (MSMEs) represented about 18 percent of the total loan portfolio of DTIs, including credit unions, equivalent to 7 percent of the GDP.[9]

7. **The financial sector appears resilient, although the rising dollarization of deposits presents risks.[10]** As of March 2017, non-performing loans (NPLs) stood at 2.8 percent of total loans (4.0 percent in March 2016). The system appears to have sufficient buffers, with a capital adequacy ratio of about 14 percent, provisions covering 118 percent of NPLs, and a liquidity ratio of 29 percent (liquid assets as a share of liabilities). Moreover, the system is profitable, with return on assets (ROA) at 2 percent. With more than half of the deposits denominated in U.S. dollars, Jamaica's rising deposit dollarization is one of the highest in LAC. While market and liquidity stress tests by the BOJ suggest continued resilience of the financial sector to these shocks, careful monitoring of the dollarization trend is essential.[11]

8. **The GOJ has demonstrated commitment to financial sector reforms to ensure stability, promote diversification, and enhance financial inclusion.** In 2014 and 2015, the Banking Services Act

[7] World Bank. 2017. *Global Economic Prospects: A Fragile Recovery*.
[8] DTIs include banks, building societies, and merchant banks supervised by the BOJ.
[9] World Bank's estimations based on BOJ's Credit Conditions Survey and IMF's World Economic Outlook.
[10] Bank of Jamaica. 2016. *Financial Stability Report*.
[11] High dollarization reduces the effectiveness of monetary policy and central bank capacity to act as a lender of last resort, makes greater exchange rate flexibility costly, and could potentially fuel liquidity and currency mismatch risks in the financial system.

and supporting regulations upgraded the regulatory and supervisory framework for DTIs. Authorities have also reformed the securities dealers' framework and modernized the payments and settlement legal framework and infrastructure, in accordance with international standards. Moreover, following the 2010 Credit Report Act and the licensing of three credit bureaus, the GOJ introduced the Security Interests in Personal Property Act in 2013 to modernize the secured transactions framework. In 2014, an electronic movable collateral registry was established, along with the insolvency law and related regulations.

9. **Access to finance is a significant constraint for firms, particularly for MSMEs, as highlighted by the National Financial Inclusion Strategy for 2016–2020.** MSMEs play a significant role in growth and employment, accounting for 90 percent of jobs.[12] However, they face access to finance constraints that limit their ability to expand and contribute to economic growth. More than 40 percent of firms in Jamaica consider access to finance as a major constraint, especially small enterprises (47 percent, compared to the average of 32 percent in LAC)[13]. According to the 2010 World Bank Enterprise Survey, almost all formal small and medium enterprises (SMEs) have access to checking or saving accounts, but only about 27 percent have a bank loan or line of credit, well below the average of 48 percent in LAC. The top three business environment constraints in 2010 were tax rates, electricity, and access to finance. The lack of and high cost of funding for MSMEs has negative implications, since firms have to rely on their own internal funds. As a result, entrepreneurs delay business expansion and strategic decisions for growth.

10. **According to the 2014 FSAP, factors that have constrained access to finance for MSMEs in Jamaica include, *inter alia:*** (a) a nascent credit reporting system (and associated information asymmetries) and high level of informality, which combined create high credit risk for lenders; (b) lack of adequate traditional collateral, that is, mostly real estate; (c) lack of bank strategies, processes, lending methodologies, and financial instruments that are tailored to the MSME segment (such as factoring and leasing); (d) lack of reliable financial statements from MSMEs, which makes it difficult for banks to assess risks; and (e) the absence of an ecosystem for private equity and venture capital (PEVC).

11. **In order to address key constraining factors of high credit risk and lack of traditional collateral by MSMEs, the Development Bank of Jamaica (DBJ) has been operating a partial Credit Enhancement Facility (CEF).** Established in 2009, the CEF has a capital amount of J$466 million (US$3.6 million) as of March 2017. From inception to March 2017, the CEF has facilitated the issuance of J$2.8 billion (US$21.6 million) in loans, through 329 guarantees totaling J$1.3 billion (US$10.3 million). The guarantee coverage is 50 percent of the loan for general SME loans and 80 percent for smaller loans. The scheme charges a fee of 2 percent on the amount guaranteed for general SME and energy loans and a reduced fee of 1 percent for agricultural loans. To date, there have been 10 claims against the CEF, equivalent to 2 percent of guarantee volumes since inception and 3 percent of the DBJ's current exposure. The portfolio at risk of CEF-backed loans is 9.9 percent excluding public banks and 16.5 percent including public banks.[14]

[12] Ministry of Industry, Commerce, Agriculture, and Fisheries (accessed the website in August 2017).
[13] World Bank Enterprise Surveys, 2010.
[14] The portfolio at risk is calculated by dividing the outstanding balance of all loans with arrears, plus all refinanced (restructured) loans, by the outstanding gross portfolio.

12. **The CEF has been underutilized, but the DBJ's adopted improvements have resulted in increased demand by lenders.** The scheme has guaranteed a limited number of loans, as indicated by the low leverage ratio[15] of 1:1.57. The DBJ's guidelines permit a leverage ratio of 1:3, which is relatively conservative in comparison to other international schemes. Although leverage ratios vary widely from 1 to 20 times, several schemes in developing countries observe ratios of 3–5 times, and well-established schemes in developed countries observe leverage ratios of more than 8–10 times.[16] Since mid-2015, the DBJ has taken the following measures to improve the CEF's design, supported by World Bank advisory services: (a) increase of loan coverage from US$41,000 to US$125,000; (b) expansion of MSME eligibility criteria; (c) improved claim process; and (d) extension of guarantees to MSME loans made with lenders' own funds (not just to the DBJ's funded loans through credit lines). In addition, at end-2016, the BOJ allowed for capital relief on the guaranteed portion of the loans, giving more incentives to lenders to use the CEF.

13. **Due to recent enhancements, there has been a significant increase in the take-up for the scheme, and additional improvements are expected to result in higher demand by lenders, thus requiring additional capitalization of the CEF.** For the fiscal year ending in March 2017, the CEF supported J$1.2 billion (US$9.3 million) in MSME loans with 78 guarantees in the amount of J$552 million (US$4.3 million), representing a 95 percent annual increase in volume of guarantees. Further improvements that will be supported by this Project are expected to generate additional demand for the product, including: (a) an efficient mechanism for lenders to submit documentation to the CEF through an electronic management information system (MIS);[17] (b) improvements of operational features, such as the coverage ratio and premiums; and (c) a dedicated marketing effort to differentiate the CEF from other DBJ products.

14. **Beyond the issues affecting credit, the supply of alternative sources of finance for MSMEs is limited.** The absence of other financial products represents a hurdle for MSMEs. Factoring is not developed and is not recognized as a financial service in the banking services legislation. Leasing is also scarcely used partly due to existing ambiguities in the legal and tax treatment of financial leasing.

15. **In addition, there is limited equity financing and risk capital for SMEs.** While Jamaica is known to have a dynamic entrepreneurial environment, many entrepreneurs are in business due to the need for economic survival. A large number of Jamaican entrepreneurs discontinue their business, stating lack of profitability or lack of finance as primary issues.[18] However, high-growth firms make important direct and indirect economic contributions.[19] The development of PEVC presents an opportunity to provide risk capital and capacity building to high-growth firms.

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[15] The CEF's capital to guarantee balances.
[16] A survey of partial credit guarantees (PCGs) (sample of 60 PCGs in 54 countries) showed an average leverage ratio of 3.3 times in 2014, with PCGs in higher-income economies observing higher leverage ratios than in middle- and lower-income economies. Calice, Pietro. 2016. *Assessing Implementation of the Principles for Public Credit Guarantees for SMEs: A Global Survey*.
[17] The MIS is being supported by the Inter-American Development Bank (IDB).
[18] Global Entrepreneurship Monitor. 2016-2017. In 2016, exit rates continued to be high in Jamaica, at 56 percent.
[19] A recent study in LAC estimated that one dollar invested in venture capital (VC) for these firms can generate up to US$6.45 in economic activity. Dalberg and FOMIN. 2012. *Venture Capital: Driving Development in Latin America.*

16. **Current private equity players in the ecosystem do not adequately target Jamaican SMEs.** Despite promising interventions in the angel/start-up segment, the avenues for the expansion of financing for established SMEs in Jamaica remain limited (see annex 4). Although several funds that provide private capital across the Caribbean maintain a presence in Jamaica, there has been a lack of private capital flow to SMEs in the country, similar to the Caribbean region as a whole. Market intelligence has identified a gap in the provision of risk capital for an estimated 150–300 SMEs across a broad set of industries, with financing needs in the range of approximately US$100,000 to US$2 million. The GOJ's intervention to facilitate capital financing to this target segment, through contributing to the capitalization of an SME fund and providing incentives to the private sector, will seek to crowd in the private sector, which is currently not adequately financing this segment of enterprises.

17. **In addition, legal, regulatory, and taxation challenges present some constraints for the development of PEVC.** Key areas that need to be addressed to enable institutional investors to invest further in this asset class include: (a) full enforcement of the Partnership (Limited) Act of 2017 and tax transparency for PEVC funds; (b) thresholds for qualified investors; (c) development of new regulations for fund managers or amendments to existing Collective Investment Scheme Regulations); and (d) domestic investors' ability to invest further in this asset class, onshore and offshore.

C. Higher Level Objectives to which the Project Contributes

18. **The Project supports the GOJ's growth agenda, by supporting 6 of the 15 critical policy actions outlined by the EGC's Growth Framework[20].** Private sector development is a priority in the GOJ's National Development Plan, 'Vision 2030 Jamaica'. In this context, the GOJ aspires to expand the coverage and the range of financial services. In the National Financial Inclusion Strategy for 2016–2020, financing for growth through MSMEs is one of the four priorities of the GOJ's agenda for the sector. In addition, MSME finance is one of the cornerstones of the EGC's Growth Framework.[21]

19. **Building resilience to climate change is vital to Jamaica's growth agenda.** The Project supports Jamaica's Climate Change Policy Framework adopted in 2015. This policy framework aims to support the goals of 'Vision 2030 Jamaica' by reducing the risks posed by climate change to Jamaica's economic and development goals. Despite not being a major emitter of greenhouse gases (GHG), Jamaica has committed to mitigating the equivalent of 1.1 million metric tons of carbon dioxide (CO2) per year by 2030. As for adaption, the country has developed sectoral strategies and actions plans. The Project contributes to the following objectives of the framework: (a) mobilizing climate financing for adaptation and mitigation initiatives and (b) encouraging the private sector to embrace climate change imperatives and promote the development and implementation of technologies and processes that contribute to climate change adaptation and mitigation initiatives.

20. **The Project contributes to the World Bank Group's twin goals of ending poverty and boosting shared prosperity by promoting the expansion of MSMEs and jobs creation.** The Project is strongly

[20] Ministry of Foreign Affairs and Foreign Trade website, http://mfaft.gov.jm/wp/wp-content/uploads/2017/01/EGC-Initiatives.pdf.
[21] Other elements of the EGC's Growth Framework, such as on the anti-money laundering/combating the financing of terrorism (AML/CFT) framework and secured transactions, are being supported by the World Bank through technical assistance.

aligned with the Country Partnership Strategy (CPS) for Jamaica for FY14-17[22] and with the Performance and Learning Review of the CPS for FY 14-19.[23] It is consistent with the CPS strategic thematic area 2 of "enabling environment for private sector growth". Specifically, the Project will contribute to objective 2a "enhanced business environment and entrepreneurship". It is directly linked to the indicator 2.3 "increased number of MSME producers that market products through formal channels" by promoting mechanisms that support the expansion of businesses. In addition, this operation is an important complementary intervention to the current Foundations for Competitiveness and Growth Project (FCGP - P147665).

II. PROJECT DEVELOPMENT OBJECTIVES

A. PDO

21. **The Project Development Objective (PDO) is to improve access to finance for micro, small, and medium enterprises (MSMEs).**

B. Project Beneficiaries

22. **The main Project beneficiaries will be MSMEs in Jamaica.[24]** MSMEs will benefit from financing for investments and business expansion, resulting in capacity and productivity gains. The DBJ, as the implementing agency, and other financial institutions will benefit from capacity building for improving risk management and raising social and environmental safeguards.

C. PDO-Level Results Indicators

23. **The PDO-level results indicators are as follows:**

(a) Number of guarantees issued for MSME loans through the improved CEF
(b) Number of SMEs getting access to risk capital through the SME Fund

III. PROJECT DESCRIPTION

A. Project Components

24. **The Project includes four components:** (1) Enhancing the Credit Enhancement Facility (CEF) for guarantees to MSME Loans; (2) Supporting the establishment of an SME Fund for risk capital financing

[22] World Bank. 2014. *Jamaica - Country* Partnership Strategy for FY 14-17. Report No. 85158 – JM.
[23] World Bank. 2017. *Jamaica - Performance and learning review of the Country Partnership Strategy FY14-19*. Washington, D.C. Report No. 112663-JM. Discussed at the Board on June 23rd, 2017.
[24] The project follows the national definition for MSMEs described in the 'Jamaica Micro, Small & Medium Enterprises (MSMEs) and Entrepreneurship Policy', which was updated in 2017. Based on annual turnover in J$ million, the following thresholds apply: less than J$15 million for microenterprises (less than US$120,000); between J$15 million and J$75 million for small enterprises (US$120,000–600,000); and between J$75 million and J$425 million for medium enterprises (US$600,000–3.4 million).

to SMEs; (3) Improving the enabling environment for access to finance and business development services for MSMEs; and (4) Project Management.

25. **Component 1: Enhancing the Credit Enhancement Facility (CEF) for guarantees to MSME loans (US$5.55 million).** This component aims at improving the operational features of the CEF. It will finance: (a) capitalization of the CEF in the amount of US$5 million; (b) development of a business plan, a financial model, policies and procedures for the operations of the CEF, and training; (c) strengthening of the DBJ's capacity to assess and manage risk of approved financial institutions (AFIs); and (d) marketing and awareness raising to AFIs and MSMEs.

26. **Selection of AFIs will be based on the strengthened DBJ's CAMEL Borrower Risk Rating (BRR) system.**[25] The DBJ will strengthen this system, by: (a) recalibrating the weights for each set of indicators and the metric scales for each variable; (b) improving the assessment of the quality of AFIs' management; (c) enhancing quality control of information; (d) strengthening the early warning system of the model; and (e) automatizing the BRR model through a software. Only AFIs as approved by the DBJ, including commercial banks, credit unions and any other financial institution under the regulation and supervision of a financial supervisor, will be eligible. The Export Import Bank (EXIM Bank) will also be eligible following the DBJ's approval under the strengthened BRR system. Approval of AFIs will be subject to the World Bank's 'no objection'.

27. **The IDB is in parallel capitalizing the CEF in the amount of US$20 million and financing the MIS.** Considering the current capital of the CEF and product features, if the leverage ratio increases to the DBJ's currently maximum allowed ratio of 1:3, the facility would be able to issue only 150 new guarantees, far below the CEF's growth plans. This number would be even lower, if the coverage level increases from 50 percent to 80 percent. In contrast, under a leverage ratio of 3, a joint World Bank and IDB capitalization in the amount of US$25 million will support potentially 1,300 guarantees. If in the future, the leverage ratio increases to more than 3, the CEF has potential to reach a higher number of MSMEs.

28. **The capitalization of the CEF by the World Bank will be completed upon the adoption of the following disbursement conditions:** (a) the CEF Operational Guidelines have been updated and adopted by the DBJ; and (b) evidence, acceptable to the Bank, shall have been furnished concerning improvements to the CEF corporate governance framework, including ratification by the DBJ's Board of the CEF Board of Trustees' confirmation of the development of an external and internal audit system for the CEF; and adoption of an amended CEF Trust Deed to ensure an adequate representation between banking and SME development expertise amongst the CEF Board of Trustees; all in a manner acceptable to the Bank.

29. **Component 2: Supporting the establishment of an SME Fund for risk capital financing to SMEs (US$7 million).** This component will contribute capital to a proposed US$15 million public-private SME Fund of 10 years extendable to 12 or 15 years, which will provide US$100,000 to US$2 million (US$750,000 average amount) in risk capital to established SMEs that have high growth potential and

[25] Currently, AFIs must maintain risk scores of up to 5 in a 10-point scale, which weights CAMEL indicators for capital adequacy, asset quality, management, earnings, and liquidity.

operations in Jamaica, but have not been deemed investment worthy by private equity funds.[26] To ensure commercial orientation, the SME Fund will seek co-investments at the fund level from other private investors and will be run by a private manager. In addition to the risk capital, the SME Fund will also provide capacity building to SMEs to attain a stronger level of growth, preparing them to list on the junior market of the Jamaica Stock Exchange or for sale to a financial or strategic sponsor.[27] The SME Fund Management Firm will be subject to registration and supervision by the relevant supervisory authority in Jamaica.

30. **The Project will support**: (a) capitalization of the SME Fund in the amount of US$5 million; (b) management fees for GOJ share in the SME Fund and potential start-up costs of the fund; (c) feasibility assessments for the fund; (d) legal, regulatory, and taxation reviews to assess gaps in Jamaica's framework for PEVC funds (onshore or offshore) and proposed reforms to ensure an enabling environment for such funds; and (e) technical assistance to the DBJ, the SME Fund Management Firm, and SMEs for the creation and operation of the programme, but primarily to facilitate pre- and post-technical assistance to SMEs to alleviate targeted constraints.

31. **The capitalization of the SME Fund will occur upon compliance with the following conditions:** (a) the SME Fund Management Firm shall have been procured to act as manager of the SME Fund, in accordance with the World Bank's Procurement Regulations and with terms of reference, experience, and qualifications acceptable to the World Bank; (b) the SME Fund shall have been legally established, including the issuance of the necessary bylaws, and is fully operational in accordance with the Loan Agreement, all in a manner acceptable to the Bank; (c) the SME Fund Shareholder Agreements shall been executed, pursuant to which private shareholders of the SME Fund have committed an aggregate amount of approximately US$ 10 million, all on terms and conditions acceptable to the Bank; and (d) the SME Fund Agreement shall have been executed, in a manner acceptable to the Bank.

32. **Component 3: Improving the enabling environment for access to finance and business development services for MSMEs (US$1.56 million).** This component will support improving the enabling environment for access to finance for MSMEs, including the development of financial instruments, such as leasing and factoring, and business development services (BDS) for MSMEs to improve their bankability.

33. **Subcomponent 3.A: Enabling environment for access to finance for MSMEs, including the development of financial instruments (US$0.86 million)**

34. **To encourage the development of factoring, the Project will finance:** (a) a market feasibility study for factoring (ongoing as retroactive financing); (b) potential advisory inputs for legal and regulatory amendments or a factoring law; (c) feasibility assessment of the factoring platform; (d) design, development, and implementation of an online factoring platform; (e) awareness raising and capacity building of AFIs, MSMEs, and other stakeholders on factoring and its benefits.

35. **With regard to leasing, the Project will finance:** (a) market assessment on the leasing sector (ongoing as retroactive financing), (b) potential advisory inputs for legal and regulatory amendments or

[26] Established companies are defined as those with sustained positive cash flow and a growing customer base, which require infusion of growth equity. See Annex 4 for information about the market landscape.
[27] In addition, self-liquidating instruments may be a preferred option to mitigate the challenge of exit.

a leasing law, and (c) awareness raising and capacity building of key stakeholders on leasing and its benefits.

36. **Subcomponent 3.B: Business development services for MSMEs to improve their bankability (US$0.70 million)**

37. **This subcomponent aims at improving the DBJ's capacity to expand and enhance the quality of its MSME support program.** Support will be provided for (a) a performance assessment of the existing Voucher for Technical Assistance Programme; (b) technical assistance to improve the voucher program design; (c) technical assistance to develop a broader strategy to promote BDS for MSMEs; (d) design, development, testing, and implementation of an interactive virtual platform for BDS providers and MSMEs; (e) update of the existing database of BDS providers; (f) an awareness campaign to promote the new and improved programs for MSMEs; and (g) resources to implement the new BDS strategy.

38. **Component 4: Project management (US$0.85 million).** This component will support a Project Implementation Unit (PIU) responsible for the coordination, implementation, and supervision of the project. The Project will finance: (a) the recruitment and training of PIU members; (b) equipment and furniture; (c) monitoring and evaluation (M&E) activities; and (d) the Project's financial audits.

B. Project Cost and Financing

39. **The total Project cost is US$15 million allocated to each component, as summarized below**:

Project Components	Project Cost (US$)	IBRD Financing (%)
Component 1	5,550,000	100
Component 2	7,000,000	100
Component 3	1,560,000	100
Component 4	852,500	100
Total Costs	**14,962,500**	**100**
Front End Fees	37,500	
Total Financing Required	**15,000,000**	**100**

C. Lessons Learned and Reflected in the Project Design

40. **The World Bank Group has been active in the financial sector reform agenda in Jamaica, bringing lessons learned from several years of engagement.** In 2014, the World Bank conducted the FSAP with recommendations that established the analytical foundation for this Project. Subsequently, the World Bank has provided advisory services to the authorities on the National Financial Inclusion Strategy, improving operational features of the CEF, AML/CFT, and other financial sector areas. Lessons learned include the need for significant implementation support and extensive consultations with stakeholders.

41. **For the CEF, the Project has incorporated lessons learned from various World Bank Group lending and technical assistance projects,** including in Madagascar, Ghana, Senegal, Cambodia, Sri Lanka, Haiti, and South Africa. The Project design also considers the Principles for Public Credit Guarantee (PCG) Schemes for SMEs, which establish good practices for public PCGs. Key lessons include a partial coverage ratio to avoid moral hazard; risk-based premiums; transparent, specific, and efficient claims processes; accurate and efficient reporting on loans; and stringent eligibility criteria for MSMEs and lenders.[28]

42. **For the SME Fund, the Project design considers lessons learned from World Bank Group operations and analytical exercises in Croatia, Armenia, Ghana, and Lebanon.** Specific lessons include the following: (a) the financing component should be linked with the broader entrepreneurship ecosystem; (b) fund management is outsourced to a competitively selected professional, without Government participation in the investment committee; (c) commercial discipline is ensured through at least 50 percent co-investment at the fund level by private partners; (d) technical assistance to build SME capacity at pre-investment and post-investment is important to increase investment worthiness and ensure value creation of the portfolio; (e) a feasibility study must be conducted before capital allocation, to identify potential for pipeline, co-investors, a fund manager, and legal, regulatory, and taxation impediments; and (f) the main challenge of Government-sponsored VC funds has been the lack of flexibility to provide liquidity in follow-on funding and to allow for longer-time horizon in funds.

IV. IMPLEMENTATION

A. Institutional and Implementation Arrangements

43. **The DBJ is the implementing agency for this Project.** The PIU will be located within the DBJ and responsible for coordinating, implementing, supervising, finalizing, and documenting all the activities related to the Project**.**

44. **The PIU will be staffed with qualified personnel for the implementation of the Project.** A team will be recruited, trained, and equipped to manage the Project activities. In addition, a technical team from the DBJ and other key stakeholders, such as the BOJ and Financial Services Commission (FSC), will provide technical support to the PIU, including the review and approval of goods and services delivered.

45. **The PIU will report to a Project Steering Committee (PSC), which will be established to guide the high-level strategic direction of the Project.** The PSC will serve as a platform for coordination and decision making at the high levels. The PSC will meet periodically to monitor progress. It will be integrated by representatives of the Planning Institute of Jamaica (PIOJ), Ministry of Finance and the Public Service (MOFPS), BOJ, FSC, and the DBJ, or as otherwise agreed in the Operations Manual (OM).

B. Results Monitoring and Evaluation

46. **The PIU will monitor and evaluate progress toward achieving the PDO.** The PIU will be responsible for monitoring and evaluating the PDO-level and intermediate results indicators for the Project described in the Results Framework (section IV). The PIU will work in close coordination with the

[28] World Bank. 2015. *Principles for Public Credit Guarantee Schemes for SMEs.* Washington, DC: World Bank.

technical team to collect data. Every year, the PIU will prepare an M&E strategy that will be part of the working annual plan. The M&E activities will be financed under Component 4. The PIU will provide the results of its M&E activities on a semiannual basis, through project progress reports.

C. Sustainability

47. **The CEF and the SME Fund are designed to be financially sustainable.** The Project is financing preparatory activities, such as feasibility studies and risk-based financial models, to ensure the financial viability and soundness of the proposed interventions. The Project is also supporting legal, regulatory, and supervisory reforms that will encourage the long-term development of SME finance.

48. **For the CEF, a risk-based model and business plan will determine pricing and adequate coverage ratios**. A balance between providing incentives for lenders to expand lending to SMEs and ensuring enough risk sharing to avoid moral hazard will be pursued.

49. **The SME Fund will be commercially oriented and privately managed, which creates market discipline.** The Project will also support potential regulatory and legal reforms for PEVC in Jamaica, to ensure that an enabling framework is in place for the long-term development of the market for both onshore and offshore PEVC funds.

D. Role of Partners

50. **The World Bank and IDB have collaborated on activities related to the CEF.** In parallel with this Project, the IDB has prepared an investment loan of US$20 million for the capitalization of the CEF. The World Bank, IDB, and the DBJ have worked together to ensure close coordination during project design and will continue to do so during implementation.

51. **The Project is aligned with the IMF's Precautionary SBA[29].** One of the six pillars of this programme is related to structural reforms to increase growth, several of which are supported by the Project, such as developing markets for factoring and leasing and expanding the scale and range of the CEF.

52. **The Project has strong synergies with other projects and builds on the experience of the World Bank Group in Jamaica.** The International Finance Corporation (IFC) has a strong engagement in Jamaica, with advisory services for SME development, credit bureaus, the investment climate, and secured transactions. On the SME Fund, the Project has synergies with the Entrepreneurship Program for Innovation in the Caribbean (EPIC).[30]

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[29] The 36-month SBA with a total access of SDR 1,195.3 million (about US$ 1.68 billion), equivalent of 312 percent of Jamaica's quota in the IMF, was approved by the IMF's Executive Board on November 11, 2016 (see Press Release No.16/503). The Jamaican authorities view the SBA as precautionary, as an insurance policy against unforeseen external economic shocks that could lead to a balance of payments need.

[30] EPIC aims at building a supporting ecosystem for high-growth and sustainable enterprises. It focuses on pre-VC financing and innovation ecosystem, while this Project will support enterprises that are at the immediate next stage of development.

V. KEY RISKS

A. Overall Risk Rating and Explanation of Key Risks

53. **The overall risk is rated Substantial.** The country is entering a demanding transition period, where tough reforms may result in significant adjustment costs before they yield results of growth acceleration, improvements in shared prosperity, and poverty reduction. The key risks that can affect successful implementation of the Project are outlined in the following paragraphs.

54. **Governance and political risk is Substantial.** If growth is not tangible for the population, the political capital of the GOJ to support the heavy reform agenda could weaken further. The Project includes advisory inputs for potential legal and regulatory amendments that would need to be adopted by the Parliament. The World Bank has been engaged in consultations with stakeholders about the potential activities that require such reforms since the 2014 FSAP. The PSC, which will guide the strategic direction of the Project, will also provide a platform for discussing legal and regulatory reforms.

55. **Macroeconomic risk is High.** Economic recovery remains fragile and vulnerable to shocks and imbalances. New exogenous shocks (natural or economic, including lack of FDI for critical projects) or lower than expected economic growth could result in a less favorable business environment. In this scenario, the demand for MSME finance could decline, as firms postpone investment decisions. This would negatively affect lenders' demand for using the CEF and SMEs' demand for risk capital financing from the SME Fund. At the same time, an unstable macroeconomic framework could reduce the risk appetite of financial institutions, as they may face increased credit risks. This risk is mitigated by the macroeconomic reforms supported by the IMF's Precautionary SBA.

56. **Technical design risks are Substantial**, as described by component:

(i) **Component 1 (CEF)**: Risk of insufficient use due to less than expected demand by lenders. This will be mitigated by significant involvement of the private sector during the design and implementation of the improved CEF. In addition, design features will be closely monitored by the World Bank and the IDB teams.

(ii) **Component 2 (SME Fund):** (i) risk of lack of private participation, mitigated by embedded financial incentives to attract private co-investors at the fund level and a private fund manager; (ii) risk of non-commercial influence on SME investments, mitigated by the competitive selection of a private manager and adequate governance arrangements; and (iii) risk of delay in implementation of legal and regulatory reforms, mitigated by conducting legal, regulatory, and tax analysis as retroactive financing, to diagnose the key gaps.

57. **The institutional capacity risk for implementation is Substantial.** The DBJ is a first-time implementing agency for a World Bank-financed project, and the Project requires coordination with different agencies, including the BOJ, FSC, and the SME Fund Management Firm. This risk is mitigated by establishing a well-equipped PIU, which reports to the PSC, and technical assistance for the DBJ.

58. **The fiduciary risk is Substantial.** The financial management (FM) risk is Substantial. Although the DBJ is involved in the implementation of the FCGP, it does not manage the FM aspects of the project and has limited experience. Moreover, the SME Fund Management Firm, once selected, will also need to ensure adequate FM to report to the DBJ. The risk is mitigated by: (a) the hiring of an FM expert in the PIU, who will receive continued training and guidance from the World Bank on FM and disbursement aspects of the Project; (b) the preparation of an OM by the DBJ, which will guide the Project; (c) periodic FM reviews and field visits by the World Bank during project implementation; and (e) an annual external and independent audit of project accounts and technical agencies, under terms of reference acceptable to the World Bank. The risk to implement procurement is rated as Moderate. Risk mitigation measures to be applied by the DBJ include: (a) setting up a system of accountability for procurement decision making with clear functions and authority, and (b) preparing a procurement manual detailing procurement steps and filing procedures.

VI. APPRAISAL SUMMARY

A. Economic and Financial (if applicable) Analysis

59. **The Project will contribute to economic growth and job creation through the increase and diversification of financing mechanisms for MSMEs.** The Project will do so by easing constraints in access to finance and mobilizing private capital. It will leverage Government resources, as guarantees are less capital intensive. Moreover, the Project's financial instruments will be commercially oriented with important demonstration effects for the private sector. The Project will crowd in the private sector for the development of SME finance in the longer term. The expected economic benefits by project component are as follows:

(a) **CEF:** A well-designed CEF will facilitate loans with improved terms to creditworthy MSMEs that lacked sufficient collateral. MSME finance contributes to investments, productivity, employment, and growth. Lenders can expand their client base and diversify their portfolios. Expected positive externalities include, *inter alia*: demonstration effects for other lenders to serve MSMEs, improvements in lending technologies for MSMEs, and better risk management systems.[31] If financially sustainable, the CEF would be revenue generating.

(b) **SME Fund:** The Project will promote gains in productivity and job creation in SMEs, since access to risk capital financing leads to creation and/or expansion of enterprises and products. The Project is expected to have positive spillover effects, including attracting foreign investment, creating a higher volume of exports through upgraded market linkages, creating additional business and growth in the broader supply chain, increasing productivity and competitiveness, and building the risk capital finance ecosystem.

Table 1: Economic Analysis: Summary of Results and Main Assumptions

[31] World Bank. 2012. *Project Appraisal Document: Morocco - Micro, Small, and Medium Enterprise Development Project (APL 2)*.

	NPV (in US$ millions)	ERR (%)	Main Assumptions
Component 1	47.2	124	Sales growth: 10% in one year lag
Component 2	6.6	36	Sales growth: 18% (large), 20% (medium), and 25% (small)
Total - Project	51.8	105	Discount rate: 10%

60. **Under reasonable assumptions, the total project investment is associated with a net present value (NPV) of US$51.8 million (J$6.5 billion) and an economic rate of return (ERR) of 104.7 percent.** The estimated NPV is equivalent to a 0.37 basis points to GDP, based on the 2016 baseline value. Results are robust partly because guarantees do not have the same capital requirements as loans and, therefore, the amount allocated to the CEF can be further leveraged.[32] Key assumptions included (a) a discount rate of 10 percent;[33] (b) annual sales growth of 10 percent, with one year lag, for the CEF's beneficiaries; and (c) sales growth of 18 percent, 20 percent, and 25 percent in sales respectively for large, medium, and small firms of the SME Fund. Economic returns are expected to gradually materialize after the capitalization of the CEF and SME Fund and be sustained after the Project's closing date.[34]

B. Technical

61. **The design of the components is based on a strong policy dialogue on the financial sector in Jamaica and several feasibility assessments that were started through the use of retroactive financing during Project preparation.** Since the 2014 FSAP, the World Bank has provided advisory services to the authorities on a National Financial Inclusion Strategy, improvements to the CEF, AML/CFT, and other areas in the financial sector. Thus, the World Bank brings a combination of technical expertise on financial sector reforms with international experience on the design and impact of such reforms. In addition, early drafts of feasibility assessments have provided valuable inputs to project design.

C. Financial Management

62. **The FM of the Project will be undertaken by the DBJ.** The DBJ is currently one of the implementing agencies of the FCGP, managing the SME line of credit, and is thus familiar with World Bank Financial Intermediary (FI) project policies. The DBJ will liaise with the SME Fund Management Firm, to ensure that all FM requirements are maintained. The DBJ has a well-established control environment and has adequate processes and procedures in place to implement project activities. Internal audits on the DBJ's operations are conducted by the DBJ's Internal Audit Unit. The World Bank performed an FM assessment of this Project in accordance with the World Bank's Policy on Investment Project Financing and the Financial Management Practice Manual.[35] The assessment concluded that the implementing agency has the capacity to establish an adequate FM system for the Project, which can provide accurate and timely information on the status of the funds, as required by the World Bank.

[32] Capital requirements of guarantees are different than loans. The investment in the CEF can be leveraged up to three times.
[33] Following the World Bank's operational guidelines, the 10 percent discount rate is used to represent a hurdle rate for the allocation of World Bank funds across projects. This rate is consistent with other projects in Jamaica.
[34] The rationale behind assumptions and sensitivity analysis is provided in annex 6.
[35] Issued by the Financial Management Sector Board on March 1, 2010.

D. Procurement

63. **A capacity assessment of the DBJ identified that risks are related to the lack of experience with World Bank procurement regulations**. Prior to project effectiveness, the DBJ will have advanced the procurement for several contracts, using the World Bank's procedures and under close supervision, which partly mitigates risks and also helps build their capacity. A procurement expert has been hired as part of the PIU. The assessment proposed for the PIU to: (a) prepare a detailed procurement manual, including filing guidelines, and (b) define a clear accountability system for procurement decision making. The Project Procurement Strategy for Development (PPSD) revealed a limited availability of consultants at the national level, indicating a preference for an international market approach. Larger value consultancies will be procured following the Quality- and Cost-Based Selection method, whereas smaller ones will be procured based on the Consultant's Qualifications. Low-value, low-risk contracts will follow a national market approach.

E. Social (including Safeguards)

64. **The Project is expected to have positive social impacts by promoting the expansion of businesses and supporting job creation and higher incomes.** The Involuntary Resettlement policy (OP 4.12) will not be triggered. The Project will not finance investments, under this Project or in the future, involving: (a) involuntary taking of land resulting in relocation or loss of shelter, loss of assets or access to assets, or loss of income sources or means of livelihood, whether or not the affected persons must move to another location; or (b) involuntary restriction of access to legally designated parks and protected areas resulting in adverse impacts on the livelihoods of the displaced persons. To ensure that OP 4.12 is not triggered, OP 4.12 will be part of the exclusion list in the Environmental and Social Management Framework (ESMF) and OM, and any MSME activity that will trigger this policy will be excluded through a rigorous screening process.

65. **The safeguards specialist to be hired as part of the PIU will receive training by the World Bank, as needed, on OP 4.12, the screening process, and the implementation of a project-level grievance redress mechanism**. The specialist will review the current complaints handling system and modify it as needed to ensure its accessibility to the communities, documentation of complaints, and their timely resolution.

66. **Consultations with project stakeholders and beneficiaries have been held during project preparation and their feedback will also be incorporated during implementation**. Following the mid-term review and every subsequent year, the PIU will organize workshops targeting project stakeholders and beneficiaries to collect their feedback about the program. In addition, the PIU will develop tailored mechanisms to measure the level of satisfaction of the targeted population.

67. **Evidence and qualitative interviews suggest that there is no significant gender gap in access to finance in Jamaica, thus this Project does not propose any gender-based interventions.** Nevertheless, results indicators in the RF will be gender disaggregated for monitoring purposes and to inform future projects. Financial access indicators in the 2014 Jamaica Survey of Living Conditions and in the 2014 Global Findex database did not reveal significant gender imbalances in the access and use of financial services. Moreover, the Project is not expected to contribute to any gender imbalances, since the selection of beneficiaries will be based on financial and commercial merit. The Project's

midterm review will evaluate the disaggregated indicators in the RF in order to assess any possible gender gaps that may arise during implementation, as well as potential actions to address them.

F. Environment (including Safeguards)

68. **The Project has been classified as Category Financial Intermediary (FI).** The Project triggers the safeguards policy on Environmental Assessment (OP/BP 4.01), given the potential for negative environmental and social (E&S) impacts. For Components 1 and 2, specific MSME activities and location are not yet defined, but they are expected to be largely related to machinery financing or small and medium-scale construction works in agriculture, small-scale light manufacturing, construction and real estate development, and tourism. Potential impacts are anticipated to be relatively minor to moderate. With appropriate standard mitigation measures, potential negative impacts will be managed effectively.

69. **Due to the importance of the agriculture and tourism sectors for the economy, the World Bank's Pest Management (OP/BP 4.09), Natural Habitats (OP/BP 4.04), and Physical Cultural Resources (OP/BP 4.11) policies are triggered.** The Project may support activities in agriculture, which might be associated with use and purchase of pesticides. To ensure that harmful pesticides are not used, pesticides financed by the Project must comply with requirements and standards acceptable to the World Bank. The policies on Natural Habitats (OP/BP 4.04) and Physical Cultural Resources (OP/BP 4.11) have been triggered because of the prevalence of ecotourism-related MSMEs, which can negatively affect natural habitat and national heritage sites, if not properly managed. Finally, the policy on Forests (OP/BP 4.36) has been triggered, as some MSMEs expressed interest in bamboo products and teak harvesting on private lands.

70. **An Environmental and Social Management Framework (ESMF) was prepared by the DBJ, approved by the World Bank, and published on November 6, 2017 on both the DBJ's and the World Bank's websites.** The draft ESMF was prepared and delivered for public consultation in a series of workshops in March 2017. The ESMF was revised in August 2017 to include the results of stakeholders' consultations and finalized in November 2017 to reflect the final project design. The environmental procedures defined in the ESMF build on the DBJ's experience in implementing the World Bank's FCGP. The ESMF is consistent with the GOJ's environmental and regulatory requirements and the World Bank's safeguards policies. According to the ESMF, MSMEs will be required to conform to requirements for E&S performance, and AFIs will need to effectively screen the MSMEs (including for the World Bank exclusion list, permit status, and good practice), verify their eligibility for the CEF, and ensure that E&S requirements are clearly included in guarantee agreements. AFIs will need to periodically report on the status of their E&S management efforts, so that the DBJ can conform to relevant E&S requirements. The SME Fund Management Firm will assume a leading role in the management of E&S risk for SMEs obtaining risk capital financing.

71. **The Project includes climate change interventions with adaption and mitigation co-benefits.** The CEF, which will receive a US$5 million capitalization, has a special window with a higher coverage of 80 percent (as opposed to 50 percent for other operations) to support companies seeking financing for energy efficiency activities. The Project is expected to maintain this window to support investments in reduction of emissions and/or absorption of GHG. Similarly, the SME Fund could potentially invest in SMEs with activities that contribute to the reduction of GHG emissions and/or their absorption. Over its

lifetime, the Project is expected to produce climate co-benefits equivalent to 20 percent of the project cost.

G. Other Safeguard Policies (if applicable)

72. **Screening and exclusion criteria are provided in the ESMF to ensure that any MSMEs or activities that will trigger any other World Bank safeguard policies will not be eligible for funding under the Project.** These additional screening and exclusion criteria will exclude any subprojects related to the construction or rehabilitation of dams, which could trigger the policy for Safety of Dams (OP/BP 4.37). Projects on International Waterways (OP/BP 7.50) are also excluded. There are no indigenous peoples or disputed areas in Jamaica, so the policies on Indigenous Peoples (OP/BP 4.10) and Projects in Disputed Areas (OP/BP 7.60) are not applicable. Finally, any projects on the IFC exclusion list are not eligible for funding, nor are any Category A projects.

H. World Bank Grievance Redress

73. **Communities and individuals who believe that they are adversely affected by a World Bank supported project may submit complaints to existing project-level grievance redress mechanisms or the World Bank's Grievance Redress Service (GRS).** At the project-level, the DBJ has already in place an email and a phone number to receive complaints that will be used during project implementation. In addition to those mechanisms, the GRS ensures that complaints received are promptly reviewed in order to address project-related concerns. Project affected communities and individuals may submit their complaint to the independent World Bank Inspection Panel which determines whether harm occurred, or could occur, as a result of World Bank non-compliance with its policies and procedures. Complaints may be submitted at any time after concerns have been brought directly to the World Bank's attention, and Bank Management has been given an opportunity to respond. For information on how to submit complaints to the World Bank's corporate GRS, please visit http://www.worldbank.org/en/projects-operations/products-and-services/grievance-redress-service. For information on how to submit complaints to the World Bank Inspection Panel, please visit *www.inspectionpanel.org*.

VII. RESULTS FRAMEWORK AND MONITORING

Results Framework
COUNTRY : Jamaica
Access to Finance for MSMEs

Project Development Objectives

The Project Development Objective (PDO) is to improve access to finance for micro, small, and medium enterprises (MSMEs).

Project Development Objective Indicators

Indicator Name	Core	Unit of Measure	Baseline	End Target	Frequency	Data Source/Methodology	Responsibility for Data Collection
Name: Number of guarantees issued for MSME loans through the improved CEF		Number	78.00	1178.00	Semi annual	Project Report	Project Implementation Unit - the DBJ
Description: Cumulative number of guarantees issued to MSME loans through the improved CEF. The indicator refers to the number of guarantees issued within the reporting period, as opposed to the number of guarantees outstanding in the portfolio.							
Name: Number of SMEs getting access to risk capital through the SME Fund		Number	0.00	15.00	Semi annual	Project Report	Project Implementation Unit (with data from SME Fund

Indicator Name	Core	Unit of Measure	Baseline	End Target	Frequency	Data Source/Methodology	Responsibility for Data Collection
							Manager).
Description: Cumulative number of SMEs getting access to risk capital through the SME fund.							

Intermediate Results Indicators

Indicator Name	Core	Unit of Measure	Baseline	End Target	Frequency	Data Source/Methodology	Responsibility for Data Collection
Name: Volume of guarantees provided to MSME loans		Amount(USD)	4412800.00	135954685.00	Semi annual	Project Report	Project Implementation Unit - the DBJ
Description: Cumulative volume of guarantees (in USD) provided to MSME loans through the improved CEF. The indicator refers to the volume of guarantees issued within the reporting period, as opposed to the outstanding balance of guarantees in CEF's portfolio. Projected target values reflect an estimated exchange rate at project's approval (USD 1 = J$ 125). The indicator will be reported in local currency (J$) as well to monitor exchange rate fluctuations.							
Name: Improvements of the DBJ's institutional capacity in credit risk management of AFIs		Text	The DBJ has limited institutional capacity to scale sustainably the CEF's	The DBJ has adequate systems and expertise in place to scale and	Semi annual	Project Report	Project Implementation Unit - the DBJ

Indicator Name	Core	Unit of Measure	Baseline	End Target	Frequency	Data Source/Methodology	Responsibility for Data Collection
			operations.	manage the CEF, in a sustainable manner.			
Description: This indicator refers to recommended enhancements to the DBJ's credit risk management practices for AFIs, including the strengthening of Borrower Risk Rating (BRR) model, the implementation of a software for the qualification of AFIs, and improvements in staff's expertise for credit risk management of AFIs. This text indicator will be achieved when:(i) the DBJ installs and operationalizes a new software to qualify AFIs and monitor their financial performance; (ii) training has been provided to the DBJ staff and the DBJ staff's expertise has been strengthened through training.							
Name: Draft factoring and/or leasing legal and regulatory amendments submitted for approval		Yes/No	N	Y	Semi annual	Project Report	Project Implementation Unit - the DBJ
Description: A "Yes" value will be assigned to this binary indicator when draft legal and regulatory amendments for factoring and/or leasing are submitted to the Parliament for approval.							
Name: Volume of risk capital provided to SMEs		Amount(USD)	0.00	11500000.00	Semi annual	Project Report	Project Implementation Unit - the DBJ (with data from SME Fund Management Firm)
Description: Cumulative volume of risk capital provided to SMEs through the public-private SME Fund. Risk capital refers to investments (equity or quasi-equity) made by the SME Fund in eligible SMEs, according the terms and conditions of the SME Fund. Projected target values reflect an estimated exchange rate at project's approval (USD							

Indicator Name	Core	Unit of Measure	Baseline	End Target	Frequency	Data Source/Methodology	Responsibility for Data Collection
1 = J$ 125). The indicator will be reported in local currency (J$) as well to monitor exchange rate fluctuations.							
Name: New business development service platform operational		Yes/No	N	Y	Semi annual	Project Report	Project Implementation Unit - the DBJ
Description: New Business Development Service Platform designed, developed, tested and functioning online. It will include a virtual market for BDS providers and MSMEs and online tools for business development.							
Name: Percentage of beneficiaries that feel project activities reflected their needs (Citizen Engagement Indicator)		Percentage	0.00	75.00	Semi annual	Project Report	Project Implementation Unit - the DBJ
Description: A survey will measure the satisfaction of the Project's final beneficiaries regarding the activities implemented under the Project. During mid-term review and every year after that, the Project Implementation Unit (PIU) will organize workshops targeting different Project stakeholders/beneficiaries. Workshops will be organized taking into account the type of product/activity, the type of beneficiary, and geographical location. To measure the level of satisfaction amongst the beneficiaries, the PIU will develop a set of questions and other tools with the support of the WB team. Field visits and interviews in situ will also be considered. Moreover, the PIU will collect and evaluate any feedback/complaint received associated with the Project through the DBJ's Grievance Redress Mechanism.							
Name: Private capital mobilized		Amount(USD)	0.00	10000000.00	Semi annual	Project Report	Project Implementation Unit - the DBJ

Indicator Name	Core	Unit of Measure	Baseline	End Target	Frequency	Data Source/Methodology	Responsibility for Data Collection
Description: The core indicator track the amount of direct financing (in the form of equity and/or debt) mobilized by private entities, using private funding, to finance investments within an IBRD/IDA operation or investments (PE, GE, RE, SF, and GU) directly linked to that operation.							

Target Values

Project Development Objective Indicators

Indicator Name	Baseline	YR1	YR2	YR3	YR4	YR5	End Target
Number of guarantees issued for MSME loans through the improved CEF	78.00	200.00	358.00	564.00	831.00	1178.00	1178.00
Number of SMEs getting access to risk capital through the SME Fund	0.00	0.00	2.00	5.00	10.00	15.00	15.00

Intermediate Results Indicators

Indicator Name	Baseline	YR1	YR2	YR3	YR4	YR5	End Target
Volume of guarantees provided to MSME loans	4412800.00	15771544.00	32014469.00	55241852.00	88457010.00	135954685.00	135954685.00
Improvements of the DBJ's institutional capacity in credit risk management of AFIs	The DBJ has limited institutional capacity to scale sustainably the CEF's operations.		Installation and operationalization of the software for AFIs' qualification.	Training has been provided to strengthen DBJ staff's expertise in credit risk management.			The DBJ has adequate systems and expertise in place to scale and manage the CEF, in a sustainable manner.
Draft factoring and/or leasing legal and regulatory amendments submitted for	N	N	Y	Y	Y	Y	Y

Indicator Name	Baseline	YR1	YR2	YR3	YR4	YR5	End Target
approval							
Volume of risk capital provided to SMEs	0.00	0.00	2250000.00	4700000.00	8100000.00	11500000.00	11500000.00
New business development service platform operational	N	N	N	N	Y	Y	Y
Percentage of beneficiaries that feel project activities reflected their needs (Citizen Engagement Indicator)	0.00	0.00	0.00	0.00	0.00	75.00	75.00
Private capital mobilized	0.00		10000000.00				10000000.00

ANNEX 1: DETAILED PROJECT DESCRIPTION

COUNTRY: Jamaica
JM Access to Finance for MSMEs

1. **The Project strongly supports the GOJ's growth agenda, by supporting 6 of the 15 critical policy actions outlined by the EGC's Growth Framework**. These actions are: (a) pursue amendments to BOJ regulations to allow capital relief for the portion of an SME loan with a CEF guarantee; (b) undertake measures to promote factoring and leasing; (c) expand the scale and range of financing and capacity development programs, including the CEF, voucher program, leasing, and factoring; (d) strengthen the ecosystem for VC and angel investment; (e) engage in financial sector regulatory review with a view to assessing regulations that affect access to finance; and (f) pursue required amendments to legislation to allow for inventory and receivables to be recognized as security under BOJ regulations.

2. **The Project has four components:** (a) enhancing the Credit Enhancement Facility (CEF) for guarantees to MSME loans, (b) supporting the establishment of an SME Fund for risk capital financing to SMEs, (c) improving the enabling environment for access to finance and business development services for MSMEs, and (d) project management.

3. **Component 1: Enhancing the Credit Enhancement Facility (CEF) for guarantees to MSME loans (US$5.55 million).** The component will finance: (a) capitalization of the CEF in the amount of US$5 million; (b) development of a business plan, a financial model, policies and procedures for the CEF's operations, and training (US$200,000);[36] (c) strengthening of the DBJ's capacity to assess and manage risk of AFIs (US$150,000), including a software for AFI qualification; and (d) marketing and awareness raising to AFIs and SMEs (US$200,000).

4. **The advisory work will consist of the following:**

(a) Development of a comprehensive business plan and financial model for the CEF

- The business plan and financial model should be driven by principles of financial sustainability and market orientation. Strategic goals should be designed to reflect outreach (number of MSMEs benefitting from the scheme), additionality (capacity to target guarantees to MSMEs that otherwise would not have access to finance), and sustainability (capacity to avoid losses and recapitalizations).

- The business plan should contain the following chapters or equivalent: (i) technical operations (fees, reporting, accounting, auditing, capital management, risk management, and so on); (ii) administration (staff composition, board, MIS, information technology (IT) systems, policies and procedures, and bylaws); (iii) governance structure and responsibilities and regulatory requirements; (iv) matrix of guarantees (by targeted segment, coverage, and fees); (v) financial plan (capital management, revenue generation strategy, funding plan, fee structure, budgeting); (vi)

[36] The development of the MIS will be supported by an IDB project.

performance monitoring; (vii) financial projections (long-term assessment of sustainability and viability); and (viii); five-year road map.

- With regard to governance and institutional structure, the viability, acceptable loss levels, sustainability, and future use of the CEF shall be analyzed as an independent fund in the medium term and propose a transition path to an independent fund if necessary.

(b) Operational policies, procedures and forms, an M&E framework, and a marketing strategy

- **Product lines and targeted market.** A range of products will be developed that both meet specific needs of targeted SME segments and of AFIs. Different guarantee products will consider strategic goals of outreach and sustainability.

- **Product design features,** including on: (i) coverage levels and related covenants and conditions; (ii) coverage tenors; (iii) risk-based guarantee fees; (iv) collateral requirements; and so on. These features shall be determined by the product and risk level. Balanced pricing and coverage ratios will provide sufficient incentives for financial institutions to lend to MSMEs that otherwise would not have access to finance, while simultaneously avoiding excessive risk taking, nonperforming loans, and moral hazard by financial institutions.

- **Risk policy and management.** The CEF's risk policy and management will be updated, reflecting the guidelines established by the business and financial plans.

- **Policies and procedures,** including revisions of policies, procedures, manuals, guidelines, trust deed, and other relevant documents for the issuance of guarantees, including eligibility criteria, payment rules and procedures, risk management, coverage levels, pricing, investment policy, reporting requirements, and others. Documents that will need to be revisited or drafted include: Organization Chart, Roles and Responsibilities, Investment Policy, Capital Management Plan with Emergency Funding Plan, HR Policy, Environmental and Social Policies, Procurement Policy, AML-CFT Policy, Grievance Policy, M&E Policy, IT Policy, Audit and Accounting Policy, Reporting Policy, and others.

- **Operational forms.** Enhanced design of forms used by the CEF, including, among others: (i) eligibility forms, (ii) claims forms, and (iii) guarantee agreements between the CEF and lenders.

- **M&E framework** for monitoring the success of the scheme.

- **Marketing strategy.** A marketing and communications strategy for the revised CEF will be developed awareness raising workshops will be held with lenders on the new benefits and operation of the CEF.

(c) **Training.** An assessment of the training needs of the CEF will be conducted, as well as training workshops on the new products, features, and policies and procedures, and a training plan for three years.

(d) **Strengthening the DBJ's capacity to assess and manage risks.** The BRR was recently updated to ensure that the final risk score weights the following CAMEL indicators: capital adequacy (30 percent), asset quality (20 percent), management (20 percent), earnings (20 percent), and liquidity (15 percent). The BRR has been enhanced with a new process to assess management quality and the model has been recalibrated to increase the sensitivity of the scale, with revised internal benchmarks and the introduction of new variables. To support the DBJ to improve the AFI and microfinance institutions (MFI) qualification process, the Project will support activities on: (i) automatization of the BRR calculation and predictive model through the procurement of a software; (ii) technical assistance for strengthening the model for the qualification process for credit unions and MFIs; (iii) trainings for staff to strengthen capacity for the qualification process of AFIs and nonbanks.

5. **Box 1 presents the eligibility criteria for the enhanced CEF under the Project.**

Box 1.1. CEF - Eligibility Criteria

AFIs. Only AFIs as approved by the DBJ, including commercial banks, credit unions and any other financial institution under the regulation and supervision of a financial supervisor, will be eligible. The Export Import Bank (EXIM Bank) will also be eligible following the DBJ's approval under the strengthened BRR system. Participating AFIs will be subject to the World Bank's 'no objection'. They must comply with the eligibility criteria for the DBJ's operations. They must sign an agreement with the CEF and report annual audited financial statements, quarterly unaudited statements, and monthly monitoring reports of their loan portfolio.

MSMEs. All MSMEs with annual sales of up to J$425 million (about US$ 3.4 million), in line with the MSME definition of the GOJ, will be eligible, if determined creditworthy by AFIs. Eligible MSMEs must have been in operation for at least two years. Start-ups may be eligible, upon DBJ discretion, as described in the CEF's revised operating guidelines.

Sectors. All sectors, excluding mining (except production of mining aggregates, like sand, gravel, marl, lime).

Loan purpose. Investment financing, up to 20 percent of exposure for working capital, and up to 20 percent of exposure for refinancing.

The CEF will be subject to an annual external audit.

6. **Component 2: Supporting the establishment of an SME Fund for risk capital financing to SMEs (US$7 million):** Activities to be financed include the following:

(a) **Capitalization of the SME Fund (US$5 million).** This component will contribute capital to a proposed US$15 million SME Fund. Subject to the feasibility analysis currently being undertaken as retroactive financing, key expected features of the SME Fund are presented in Box 1.2.

(b) **Management fees and start-up costs (about US$825,000**). To incentivize private sector participation, the Project may provide a higher share of management fees and other costs to establish the SME Fund. The exact amount of these fees/costs will be subject to the proposals submitted by fund managers, which will competitively bid on technical as well as financial proposals, highlighting management fees and start-up costs needed to effectively run the fund.

(c) **Legal, regulatory, and taxation reviews and reforms (about US$196,000).** To assess gaps in Jamaica's legal, regulatory, and taxation framework for PEVC Funds (onshore or offshore) and propose reforms for an enabling environment for onshore and offshore funds, including the SME Fund.

(d) **Technical assistance for the creation and operation of the program (about US$979,000).** This activity will provide three layers of support: (i) technical expertise to advise the SME Fund Management Firm on specialized areas, (ii) legal and technical assistance to the DBJ to perform its role as proxy investor (on behalf of the GOJ) in the SME Fund, and (iii) pre- and post- technical assistance to alleviate targeted constraints and needs faced by investees.

Box 1.2. Expected Design of the SME Fund

- Target enterprises are SMEs, as nationally defined, that are 'established', i.e. enterprises with sustained positive cash flow and a growing customer base, which require infusion of growth equity to expand their business. The fund will be sector neutral in its investment strategy.
- Estimated ticket size of US$100,000 to US$2 million, averaging US$750,000.
- Finite life closed-ended fund of 10 years, extendable to 12–15 years, managed by a private fund manager. Given than the Project will close earlier than the life of the fund, the GOJ will be expected to fulfill its residual financial obligations to the fund/fund manager (such as management fees) after the Project end.
- Likely exits through the Junior Market of the Jamaica Stock Exchange (JSE), sale to a financial or strategic sponsor, or self-liquidating instruments.
- Co-investment by other investors at the fund level, with aggregate private investment of approximately US$10 million.
- To incentivize private sector participation, the SME Fund may be structured to deliver asymmetric positive returns to private co-investors at the fund level. Additional features, as described below, that may incentivize private participation include a technical assistance facility to address SME capacity constraints and reimbursement for start-up costs for the SME Fund.
- A SME Fund Management Firm will be selected through an international competitive tender, providing bids on the technical design of the fund, and financial proposals for management fees and envelope for technical assistance for SMEs. The feasibility analyses, which will inform the potential pipeline and provide key inputs into the design of the investment, will be used as reference to evaluate bidding fund managers.
- Key governance features will include an advisory committee with key investors to maintain the strategic direction of the fund and an investment committee, constituted by the fund manager, to undertake investment-related decisions. There will not be any government participation on the investment committee or affiliation to the fund manager. However, the GOJ will retain the right to appoint an advisory committee member.
- The SME fund Management Firm will be subject to registration and supervision by the relevant supervisory authority in Jamaica.
- Investment documents, such as a Limited Partnership Agreement, Subscription Agreement, Management Agreement, Prospectus, or Side Letter, will define the terms and conditions of the GOJ's investment. These Investment agreements, which will include appropriate investor protections for the GOJ and governance arrangements for the fund, must have considered legal advice from the DBJ's legal counsel and must be acceptable to the World Bank, including, without limitation, adherence to World Bank Group policies.
- The SME Fund Management Firm will commit to using the Project funds in a manner that complies with the World Bank's fiduciary as well as E&S safeguards, and the fund will be subject to annual external audits.
- Given the delicate stage of growth and the need to help business owners build leadership and operating

7. **Component 3: Improving the enabling environment for access to finance and business development services for MSMEs (US$1.56 million).** This component includes two subcomponents:

8. **Subcomponent 3.A: Enabling environment for access to finance for MSMEs, including the development of financial instruments (US$0.86 million):**

- **On factoring, the Project will finance:** (a) a market feasibility study for factoring (ongoing as retroactive financing); (b) drafting of legal and regulatory amendments or a factoring law; (c) feasibility assessment of the factoring platform; (d) design, development, and implantation of a factoring online platform; and (e) awareness raising and capacity building of AFIs, SMEs, and other stakeholders on factoring and its benefits.

- **On leasing, the Project will finance:** (a) market assessment on the leasing sector (ongoing as retroactive financing), (b) drafting of necessary legal and regulatory amendments or a leasing law, and (c) awareness raising and capacity building of key stakeholders on leasing and its benefits.

9. **Subcomponent 3.B: Business development services for MSMEs to improve bankability (US$0.70 million).** This subcomponent will support: (a) a performance assessment of the existing Voucher for Technical Assistance Programme; (b) technical assistance to improve this program design; (c) technical assistance to develop a broader strategy to promote BDS for MSMEs; (d) design, development, testing, and implementation of an interactive virtual platform for BDS providers and MSMEs; (e) update the existing database of BDS providers; (f) an awareness campaign to promote the new and improved programs for MSMEs; and (g) resources to implement the new BDS for MSMEs strategy.

10. **Component 4: Project management (US$0.85 million).** This component will support a PIU that will be responsible for the coordination, management, implementation, and supervision of the Project. It will finance: (a) the recruitment and training of the PIU team members, (b) equipment and furniture for the PIU, (c) M&E activities, and (d) the Project's financial audits.

ANNEX 2: IMPLEMENTATION ARRANGEMENTS

COUNTRY: Jamaica
JM Access to Finance for MSMEs

Project Institutional and Implementation Arrangements

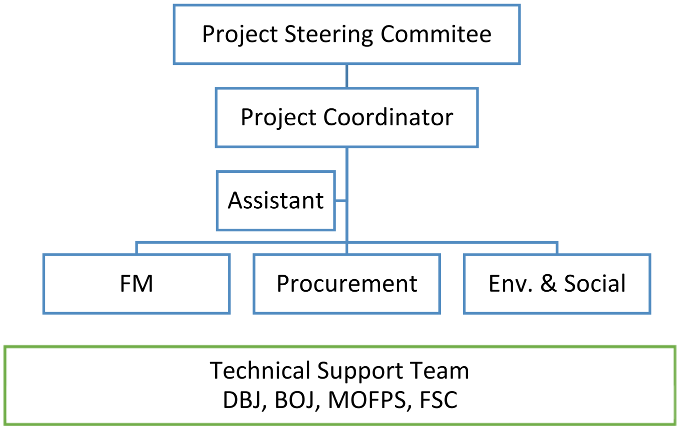
1. **The DBJ is the implementing agency for this Project.** A PIU will be located within the DBJ. The PIU will be responsible for coordinating, implementing, supervising, finalizing, and documenting all the activities related to the Project.

2. **The responsibilities of the PIU will include, among others:** (a) managing the implementation of project activities; (b) managing the procurement, FM, disbursements, and safeguards aspects; (c) coordinating the preparation, adjustments, and use of the project management tools, including the OM, working annual plan, Procurement Plan, and disbursement projections; (d) coordinating with key stakeholders all the technical aspects of the Project; (e) monitoring the progress of the PDO and intermediate results indicators of the Results Framework; (f) preparing project reports; and (g) acting as the main point of contact for the World Bank.

3. **The PIU will be staffed with qualified personnel for the implementation of the project.** A team will be recruited, trained, and equipped to manage the project activities. The PIU will be composed of a core team integrated by: (a) a project coordinator, (b) a procurement officer, (c) an FM officer, (d) an E&S specialist, and (e) an assistant. In addition, a technical team with members from the DBJ and other key stakeholders, such as the BOJ and FSC, will provide technical support to the PIU including the review and approval of goods and services delivered as part of the activities financed by the Project.

4. **The PIU will report to a PSC that will be established to provide strategic direction to the Project.** The PSC will meet periodically to track and monitor the progress of the Project. It will be integrated by representatives of the PIOJ, MOFPS, BOJ, FSC, and the DBJ, or as otherwise agreed in the OM.

Figure 2.1. PIU



Financial Management

Accounting and Information Systems

5. **The DBJ currently uses the accounting system Great Plains to record and maintain transactions.** The Management Reporter software, which is integrated to Great Plains, is used for reporting purposes. Both the Great Plains and Management Reporter software will be used for recording, maintaining, and reporting on project transactions. The project's transactions will be recorded and reported using the cash basis of accounting. A separate company account will be created in Great Plains specifically for the Project, in which the chart of accounts will be set up by project component, subcomponents, categories, and activities to ensure the provision of accurate and reliable financial information. The OM will be used to guide the day-to-day processes and procedures under the Project.

Budgeting

6. **A budget for the entire life of the Project (master budget) will be prepared by the DBJ, in consultation with the World Bank.** Annual budgets will be derived from this master budget and will be updated as needed to reflect implementation progress. The project's budget will be incorporated into the DBJ's overall annual budget, which will ultimately be reviewed by the MOFPS for approval and inclusion in the GOJ revenues and estimates of expenditures. Once annual budgets are approved by the MOFPS, they will be uploaded to the Great Plains accounting system for monitoring actual against budgeted expenditures. In addition, quarterly budget variance analysis will be conducted, in which variances will be investigated and addressed.

Internal Controls

7. **The daily operations of the Project will be guided by an OM that will incorporate the FM procedures.** The manual will be updated throughout the life of the project as needed to reflect the current procedures. Specific bylaws will also be in place for the governance of the SME Fund and the CEF. The DBJ has a well-established control environment and has adequate processes and procedures in place to implement project activities. Internal audits on the DBJ's operations are conducted by the DBJ's Internal Audit Unit. The findings of the reports will be shared with the World Bank during reviews of the Project.

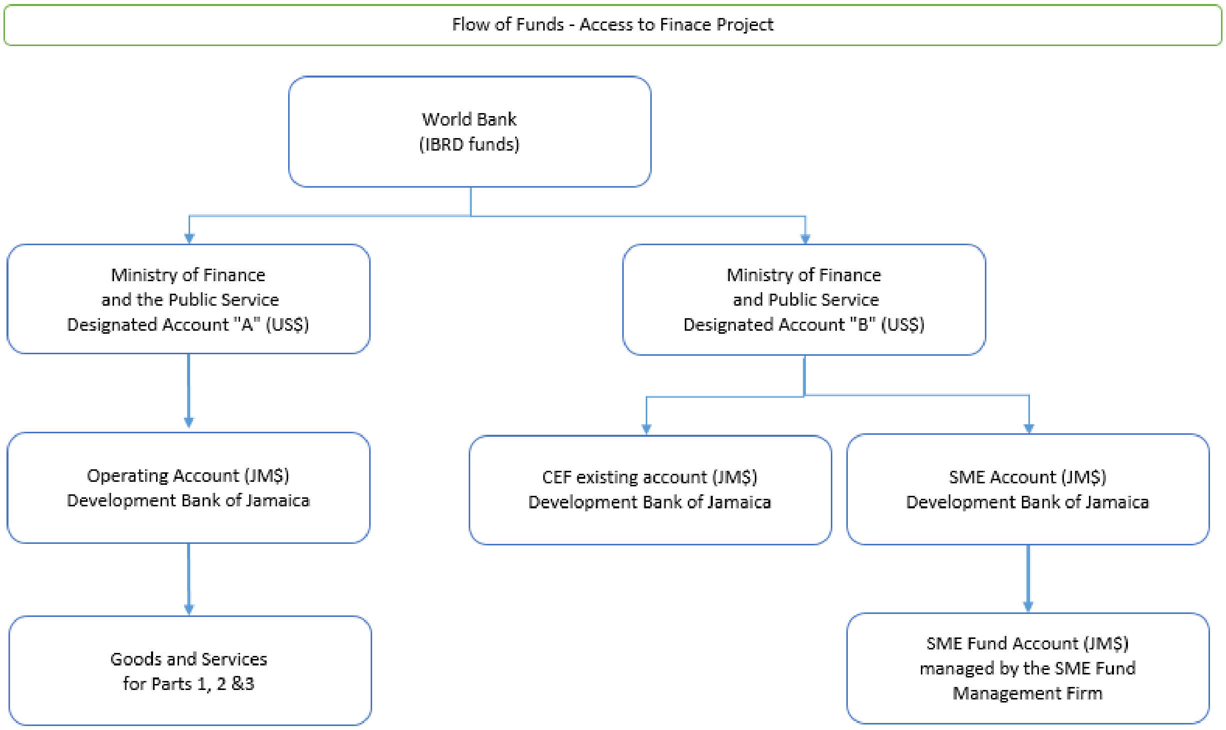
Financial Reporting and Monitoring

8. **Annual audited financial statements and unaudited financial reports will be required during project implementation.** The DBJ will be required to prepare consolidated unaudited interim financial reports (IFRs), which will cover each calendar quarter and will be due within 45 days of each quarter end. The DBJ will be responsible for the timely compilation and preparation of annual project consolidated financial statements, which will be subjected to an external audit by an audit firm deemed acceptable by the World Bank. The audited consolidated financial statements and the Management Letter will be due within six months of March 31 of each year. The implementing entity and the funds under the Project will be subject to annual audits. These audit reports will be shared with the World Bank upon request.

Disbursements and Flow of Funds

9. **The following disbursement methods will be available: Advance, Reimbursement, and Direct Payment.** Disbursements will be primary based on the use of advances. The World Bank will disburse loan proceeds to the MOFPS into two segregated Designated Accounts (DAs) denominated in U.S. dollars, maintained at the BOJ. The first account (DA-A) will finance goods, services, training, and operating costs for regular activities under all components of the Project. The second account (DA-B) will be used for the capitalization of the CEF and the SME Fund.

Figure 2.2. Flow of Funds Arrangements



10. **DA-A.** Funds will be transferred from the DA-A to a correspondent local currency project account in the name of the DBJ established at a commercial bank acceptable to the World Bank. Reporting on the transfers from the DAs and use of funds must be done in the same currency as that of the DA.

11. **DA-B.** For the capitalization of the CEF and SME Fund, advances will be made available up to the amount allocated to each fund upon fulfillment of all disbursement conditions as established in the Loan Agreement, in a manner acceptable to the World Bank. Disbursements for the CEF and SME Fund can be requested in two to three tranches by the borrower. After deposits are made into the DA-B, the MOFPS will transfer within 5 business days after the value date of disbursement request an equivalent amount

to the correspondent local currency accounts owned by the DBJ (CEF account and SME account) in two to three tranches, and maintained at a commercial bank acceptable to the World Bank, all in accordance with the provisions established in the Subsidiary Agreement, SME Fund Agreement, and the OM. The CEF account is the current CEF account operated by the DBJ and maintained at the National Commercial Bank. For the capitalization of the SME Fund, final transfer to the SME Fund account will be made once capital calls are made to the DBJ by the selected SME Fund Management Firm. The DBJ will have 10 business days to validate the capital call request and transfer the amount requested from the SME account to the SME Fund account.

12. **The exchange rate in effect on the date funds were transferred out of the Designated Accounts to the CEF and SME accounts should be used for all reporting purposes.** Any foreign exchange losses arising from such transfers are not eligible to be financed.

13. **The amounts advanced to the DA-B will be considered documented for the World Bank when credited to the CEF account owned by the DBJ and the SME Fund account.** The amounts disbursed for the capitalization of the CEF and SME Fund will be reported in subsequent withdrawal applications through IFRs, including a copy of the deposit receipt evidencing receipt of amounts in the CEF and SME Fund accounts.

14. **Disbursements will be report based.** Advances (except for the capitalizations) will be provided to the DA-A based on six-month forecast and subsequently quarterly IFRs will be used for documentation of expenditures. The minimum application size for direct payments and reimbursements is US$ 650,000 equivalent. Overall disbursement arrangements will follow standard disbursement policies and procedures established in the Disbursement Guidelines for Investment Project Financing, dated February 2017, and in the Disbursement and Financial Information Letter of the Project.

Procurement

15. **Procurement will be carried out in accordance with the 'World Bank Procurement Regulations for Borrowers under Investment Project Financing' (Procurement Regulations).** A PPSD, prepared by the DBJ, describes how procurement in this operation will support the PDO and deliver value for money using a risk-based approach. The PPSD provides adequate supporting market analysis for the selection methods detailed in the Procurement Plan. Mandatory procurement prior review thresholds of the World Bank's procurement procedure are applied (annex 2). All procurement procedures, including roles and responsibilities of different participating entities and units, are defined in the OM.

16. **Procurement Plan.** In accordance with paragraph 5.9 of the Procurement Regulations, the World Bank's Systematic Tracking and Exchanges in Procurement (STEP) system will be used to prepare, clear, and update Procurement Plans and monitor all procurement transactions for the Project. The Procurement Plan for the first 18 months has been prepared by the DBJ in accordance with the results of the PPSD. A summary of the PPSD, including recommended procurement approach for higher-value contracts, is presented in Table 2.1.

17. **Civil works.** Infrastructure and/or civil works are not expected under this Project.

18. **Goods.** Goods to be financed under this Project include software, an electronic factoring platform, and an interactive technological platform.

19. **Non-consulting services.** The Project will finance services related to marketing and awareness campaigns.

20. **Consulting services.** Consulting services to be financed under the Project will include fund management, legal and regulatory reviews, feasibility assessments, capacity building, and technical assistance.

21. **World Bank's Standard Procurement Documents.** Standard Procurement Documents shall be used for all contracts subject to international competitive procurement.

22. **Operating costs.** Operating costs refer to reasonable recurrent expenditures that would not have been incurred by the implementing agency in the absence of the project. The Project will finance operating costs, such as office supplies, communication and advertising costs, computers and equipment maintenance, travel and per diems for local and international staff, and project implementation support personnel. The Project will also finance costs of trainings, travel and per diem of trainers and trainees, and rental of facilities.

23. **Procurement capacity assessment.** The World Bank carried out a procurement capacity assessment of the DBJ. The basic staffing structure, procurement record system, internal controls, evaluation committees' roles and responsibilities, contract signing, and contract administration were reviewed. The DBJ hired a procurement expert as part of the PIU. In addition, current filing practices of procurement records risk their integrity. Lastly, internal approvals may cause undue delays to the process and create undue restrictions to bidder participation because of local registration requirements as the DBJ's staff are not familiar with the World Bank's procurement rules and procedures. The time required by the National Contracts Commission to approve certain procurement processes must also be adequately considered when planning the procurement process.

24. **Supervision arrangements.** The World Bank has started providing intensive hands-on support to the DBJ during project preparation as the DBJ advanced several retroactive financing contracts. Thus, by project implementation, the DBJ should have become familiar with most procurement methods it will use, and the World Bank's support efforts may be reduced. In addition to prior review supervision to be carried by the World Bank, annual supervision missions to visit the field to carry out post review of 1:10 procurement actions are recommended.

25. **Summary of the PPSD.** The Summary of the PPSD is included in table 2.1.

Table 2.1. Summary of the PPSD

Contract Title Description and Category	Estimated Cost (US$)	Risk Rating	Bank Oversight	Procurement Approach Competition	Selection Methods	Evaluation Method
Pre and post investment technical assistance	500,000	3.0	Post	OI	QCBS	n.a.
Fund manager	825,000	2.0	Prior	OI	QCBS	n.a.
Develop business plan for the CEF	200,000	2.0	Post	OI	CQS	n.a.
Legal Advisers to the DBJ (SME Fund)	100,000	2.8	Post	OI	CQS	n.a.
TA to the fund manager	143,000	2.5	Post	OI	CQS	n.a.
Technical advisers to the DBJ	100,000	2.5	Post	OI	DIR	n.a.
Electronic factoring platform	391,500	2.8	Post	OI	RFB	n.a.
Technological platform - BDS	290,000	2.7	Post	OI	RFB	n.a.

Note: OI = open international; ON = open national.

Environmental and Social (including safeguards)

26. **The final ESMF was revised in August 2017 to reflect stakeholders' consultations.** The draft ESMF was disclosed and consultations with key stakeholders were conducted in March 2017. The ESMF was published on the DBJ's website on September 4, 2017, and republished on November 6, 2017 on both the DBJ's and the World Bank's websites, reflecting final project design. Key findings of the consultations include the following: (a) while AFIs may have unique E&S systems, a single standardized summary form is needed to facilitate reporting; (b) some MSMEs are involved in the forestry and agriculture sectors, so triggering the Forest (OP/BP 4.36) and Pest Management (OP 4.09) policies is recommended; and (c) there was also interest in strong support for microenterprises and for at-risk youth and the disabled.

27. **The Involuntary Resettlement policy (OP 4.12) will not be triggered.** The Project will not finance investments, under this Project or in the future, involving: (a) involuntary taking of land resulting in relocation or loss of shelter, loss of assets or access to assets, or loss of income sources or means of livelihood, whether or not the affected persons must move to another location, or (b) involuntary restriction of access to legally designated parks and protected areas resulting in adverse impacts on the livelihoods of the displaced persons. For Components 1 and 2 (CEF and SME Fund), any sub-projects to be financed as part of this Project or at a later stage will be on SME private owned land or land purchased through willing-seller willing-buyer. For land purchases through willing-seller willing-buyer approach, land acquisition must occur by mutual agreement in exchange for a notarized purchase contract based on the market price at the date of acquisition. To ensure that OP 4.12 is not triggered, OP 4.12 will be part of the exclusion list in the ESMF and OM and any MSME activities that will trigger this policy will be excluded through a rigorous screening process.

28. **The Project's environmental management aspects are presented by project component as outlined below.** The protocols adopted by the Project are consistent with Jamaica's regulatory and environmental frameworks (namely the 1991 Natural Resources Conservation Act and the 1997 Environmental Permit and License System) and World Bank Environmental Assessment (OP 4.01) requirements. All the procedural steps are described in detail in the Project's OM and ESMF prepared by the DBJ.

Component 1 (CEF)

29. **MSMEs will be required to conform to requirements for E&S performance, and AFIs will need to effectively screen the MSMEs, verify their eligibility for the CEF, and ensure that E&S requirements are clearly included in Guarantee Agreements.** AFIs will need to periodically report to the DBJ on the status of their E&S management efforts. The DBJ in turn will ensure that the AFIs conform to relevant E&S requirements. The DBJ E&S specialist will oversee these activities.

30. **The MSME screening and processing procedure involves the following steps:** (a) compare with the World Bank's exclusion list; (b) check National Environmental Planning Agency permit status; (c) assign E&S risk category; (d) field visit (optional); (e) prepare documentation; and (f) guarantee administration, evaluation, and reporting.

31. **For AFIs requesting to participate in the CEF, the DBJ shall ensure that the AFI will follow an adequate environmental risk management procedure for MSME financing, consistent with the DBJ procedures**. The DBJ shall require that the AFI: (a) implements the agreed-upon environmental risk management procedure, (b) includes in the financing agreement with each MSME the environmental requirements as established from the implementation of the environmental risk procedure, (c) undertakes appropriate administrative actions commensurate with the level of risk for the MSME investments, (d) promptly informs the DBJ should any significant environmental issues or regulatory noncompliance occur with an MSME financed, and (e) provides the DBJ with an annual report on its implementation of the environmental risk procedure. If the DBJ identifies issues related to the AFI implementation of the environmental requirements, then the DBJ shall work with the AFI to define appropriate corrective actions. With the support of the World Bank, the DBJ shall take reasonable efforts to provide technical support, as needed, to the AFI in its development of implementation of its environmental risk procedure.

Component 2 (SME Fund)

32. **The DBJ will provide safeguards oversight to verify the SME Fund Management Firm's compliance and report to the World Bank, and the SME Fund Management Firm will be responsible for investment screening, assessment, monitoring, and reporting.** The SME Fund will be sector neutral and therefore a broad variety of investments could be included, including agriculture and ecotourism projects. Very high-risk projects (Category A), and those on the World Bank Group exclusion list, will not be eligible.

33. **The SME Fund Management Firm will assume a leading role in the management of E&S risk for SMEs, similar to the role of the AFIs in Component 1 (CEF).** The SME Fund Management Firm will be required to effectively screen the SMEs, verify their eligibility in the fund, ensure that E&S requirements are clearly included in contractual commitments, and periodically report to the DBJ on the status of their E&S management efforts, following and adapting (the process is outlined in the ESMF). The DBJ's environmental policy and management procedure for SME participation will form the basis for the SME Fund's E&S management system. Although it will be modified to address the particularities of the SME Fund, it will maintain an equivalent level of oversight and supervision. The DBJ's role is to ensure that the SME Fund Management Firm applies the system in a manner consistent with its own operations.

Monitoring and Evaluation

34. **The PIU will monitor and evaluate progress toward achieving the PDO.** The PIU will be responsible for monitoring and evaluating the PDO-level and intermediate results indicators for the Project described in the Results Framework (section VII). The PIU will work in close coordination with a technical support team from the DBJ and other key stakeholders to periodically collect relevant information. The entities responsible for managing the main activities of the Project, namely the CEF and the SME Fund, will use the MIS to collect and maintain reliable and updated databases with relevant information including the number of beneficiaries and the volume of funds provided to them, desegregated by type of support, type, and size of MSME or segment of the population, gender, age, geographical region, among others. Every year, the PIU will prepare an M&E strategy that will be part of the working annual plan. The M&E activities will be financed under Component 4. The PIU will provide on a semiannual basis, through project progress reports, the results of its M&E activities.

35. **Key indicators for measuring the PDO are as follows:**

(a) Number of guarantees issued for MSME loans through the improved CEF

(b) Number of SMEs getting access to risk capital through the SME Fund

36. **Key intermediate results indicators include the following:**

(a) Volume of guarantees provided to MSME loans through the improved CEF

(b) Improvements of the DBJ's institutional capacity in credit risk management of AFIs

(c) Volume of risk capital provided to SMEs through the SME Fund

(d) Draft factoring and/or leasing legal and regulatory amendments submitted for approval

(e) New business development services platform operational

(f) Percentage of project final beneficiaries that feel project activities reflected their needs

(g) Private capital mobilized

37. **In addition to these indicators, the Project will monitor additional indicators for analytical purposes** and as useful inputs to define policies and projects aimed at improving access to finance for MSMEs. The Project will monitor increase in sales, employment, and volume of exports. For the SME Fund in particular, additional indicators will monitor the volume of co-investments at the fund level by the private sector, new products introduced, and the number of trainings for SMEs.

38. **The Project will integrate beneficiary feedback as part of its M&E framework.** Key stakeholders and potential beneficiaries have been identified during project preparation and consulted during the development of the project’s ESMF. The Project will periodically engage stakeholders during implementation to obtain feedback with the objective of improving the outcomes of the operation.

39. **Gender imbalances in access to finance indicators do not appear significant in Jamaica.** Thus, this Project does not propose any gender-based interventions. Nevertheless, results indicators in the RF will be gender disaggregated to monitor any potential gender gaps during project implementation and to inform future projects. According to 2014 Jamaica Survey of Living Conditions, 12 percent of households with female heads had a loan repayment or an interest payment, spending on average 12 percent of annual consumption of them (9.3 percent and 13.6 percent respectively, for households with male heads). The 2014 Global Findex database reveals minor imbalances in the use of financial services (use of accounts, debit and credit cards, and saving accounts), although the share of men and women having borrowed from a formal financial institution is similar.[37] With regard to borrowing for business purposes, there is a small gap of 3 percentage points.

Role of Partners (if applicable)

40. **The World Bank and the IDB have collaborated on activities related to the CEF.** In parallel with the Project, the IDB has prepared an investment of US$20 million for the capitalization of the CEF.

[37] The percentage of male adults borrowing from informal lenders and family and friends is significantly higher, but this gap is not observed in borrowing from formal financial institutions.

ANNEX 3: IMPLEMENTATION SUPPORT PLAN

COUNTRY: Jamaica
JM Access to Finance for MSMEs

Strategy and Approach for Implementation Support

1. **The implementation support strategy was developed considering the risks and mitigation measures related to the operation and targets the provision of flexible and efficient implementation support.**

(a) **Technical support.** A team of financial sector specialists will provide technical support and guidance to the DBJ and key stakeholders. The technical team will review and comment terms of reference and other technical documents. Technical advice will also be provided during implementation support missions.

(b) **Procurement.** A senior procurement specialist will provide ongoing guidance to the DBJ with regard to procurement processes and will participate in project implementation support missions, post-review assessments, and site visits. In addition, the World Bank will review selection processes defined as prior review in STEP.

(c) **Financial management.** An FM specialist will provide implementation support to the DBJ. The World Bank will supervise the Project's FM arrangements by reviewing the semiannual project reports as well as the annual audited financial statements. In addition, during implementation support missions, the World Bank will review the FM and disbursement arrangements.

(d) **Operations.** During project implementation, the World Bank will provide implementation support to the team members of the PIU to prepare, update, and use the project management tools, including the OM, work annual plan, procurement plan, and disbursement projections.

(e) **Safeguards.** The environmental and social specialist will provide support and ongoing guidance to the DBJ with regard to environmental safeguards aspects including the application of the ESMF. In addition, the specialist will participate in project implementation support missions and site visits.

2. **The Implementation Support Plan will be reviewed periodically to ensure that it continues meeting the implementation support needs of the Project.**

Implementation Support Plan and Resource Requirements

Time	Focus	Skills Needed	Resource Estimate	Partner Role
First year	Task management	TTL/financial sector specialist	12	
	Procurement	Procurement specialist	6	
	FM	FM specialist	6	
	Safeguards	Environmental specialist	6	
	Operations support	Operations officer	6	
	Technical support	2 financial sector specialist (CEF, PEVC)	12	
12–60 months	Task management	TTL/financial sector specialist	40	
	Procurement	Procurement specialist	24	
	FM	FM specialist	24	
	Safeguards	Environmental specialist	24	
	Operations support	Operations officer	24	
	Technical support	2 financial sector specialist (CEF, PEVC)	48	

Note: TTL = task team leader.

Skills Mix Required

Skills Needed	Number of Staff Weeks	Number of Trips	Comments
TTL/ financial sector specialist	52	15	
Procurement specialist	30	10	
FM specialist	30	10	
Environmental specialist	30	10	
Operations officer	30	10	
Financial sector specialists	20	10	2 financial sector specialists (CEF, PEVC)

Partners

Name	Institution/Country	Role
IDB	Jamaica	Partner

ANNEX 4: FINANCIAL SECTOR BACKGROUND

A. Overview of the Financial Sector

1. **The financial system in Jamaica is fragmented, with a reasonable number of participants, which are interconnected through conglomerates.** In 2016, financial assets were estimated at 176 percent of GDP, distributed among DTIs and non-bank financial institutions (NBFIs). DTIs consist of 6 commercial banks (34 percent of assets), 3 building societies (9 percent), and 2 merchant banks (1 percent). They are supervised by the BOJ and account for 44 percent of total assets. Concentration is high, with the two largest banks accounting for 73 percent of bank assets. NBFIs include securities firms (19 percent of assets), pension funds (14 percent), life insurance companies (10 percent), unit trust funds (6 percent), credit unions (3 percent), and nonlife insurance companies (2 percent). With exception of credit unions, which are expected to be supervised by the BOJ, NBFIs are under the scope of the FSC.

Figure 4.1. Estimated Market Share in Financial System Assets (percent), in December 2016

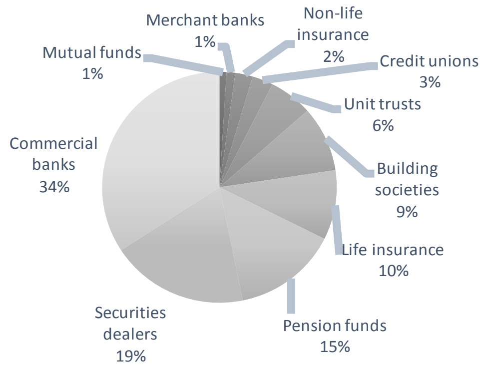
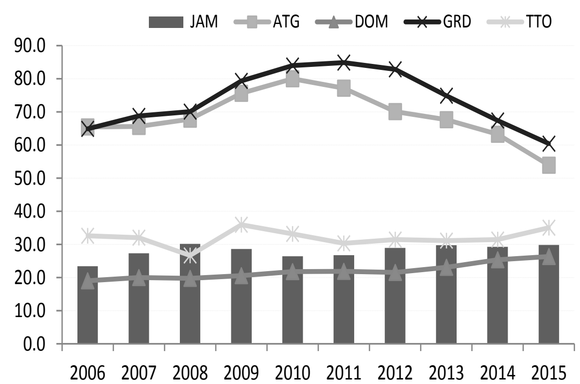


Figure 4.2. Credit to Private Sector to GDP (percent) - Regional Comparison[a]



Source: BOJ's Financial Stability Report (2016) and Finstats.
Note: a. Latest comparison data for 2015.

Figure 4.3. Commercial Banks - Credit and Deposits to GDP

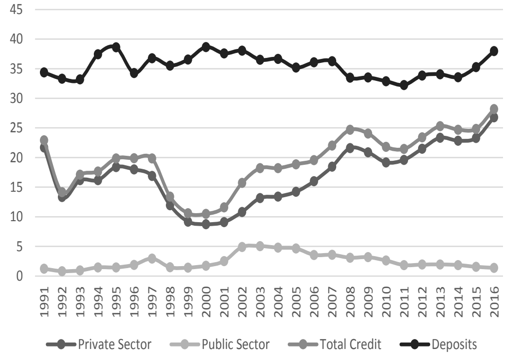
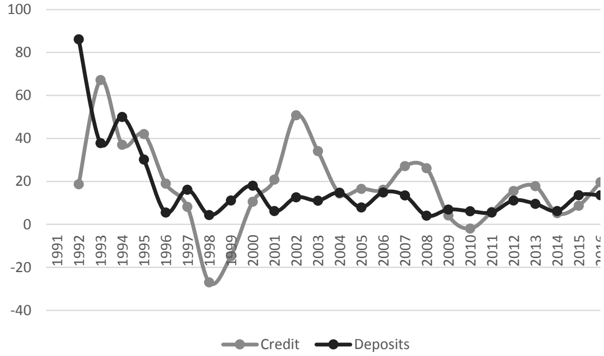


Figure 4.4 Commercial Banks - Credit and Deposits Nominal Growth (percent)



Source: BOJ and IMF's World Economic Outlook.
Note: Numbers for commercial banks only.

Table 4.1. Banking System in Jamaica

Name	Type	J$, millions	Share (%)
National Commercial Bank	Commercial bank	459,128	32.7
Scotiabank Jamaica	Commercial bank	329,224	23.4
JN Bank	Commercial bank	161,866	11.5
Sagicor	Commercial bank	115,358	8.2
Victoria Mutual	Building society	98,410	7.0
First Caribbean	Commercial bank	90,902	6.5
First Global	Commercial bank	57,198	4.1
JMMB Bank	Commercial bank	35,769	2.5
Scotia Jamaica	Building society	28,451	2.0
Citibank	Commercial bank	18,850	1.3
EXIM Bank	Public bank	8,778	0.6
MF&G Trust & Finance	Merchant bank	1,868	0.1

Source: BOJ and institutions' websites.

2. **The contribution of the banking sector to the Jamaican economy has been historically modest.** Financial intermediation has been sluggish, with credit to the private sector never surpassing its peak of 36 percent of GDP. In 2015, bank credit to the private sector was equivalent to 29.9 percent of GDP, substantially lagging behind the LAC region and Caribbean small states (46 percent and 43 percent, respectively). The country's cycle of low growth and high debt, exacerbated by financial shocks and natural disasters, has brought volatility to the sector. As of March 2017, bank credit to the private sector has increased by 39 percent (10 percent and 21 percent in 2015 and 2016, respectively).

3. **Further strengthening the resilience of the financial system is one of the pillars of the new IMF SBA.** In the next 12 months, authorities are planning to introduce new legislation to improve the resolution framework for distressed financial sector entities. They are also planning to introduce a Micro-Credit Act and Credit Unions legislation by end-2017. Finally, legislation to define the regulatory rules and consolidated supervision for financial holding companies is also being planned.

Table 4.2. DTIs - Core Prudential Indicators (percent)

in percent, unless otherwise stated	**2012**	**2013**	**2014**	**2015**	**2016**	**Mar-17**
Capital to risk-weighted assets	14.1	15.1	15.9	14.9	14.9	14.6
NPLs to gross loans	7.0	5.4	5.0	4.1	2.9	2.8
Provisions to NPLs	90.3	95.7	101.6	106.7	116.6	118.5
Liquid assets to assets	22.6	23.6	28.2	26.3	n.a.	n.a.
Liquid assets to liabilities	26.7	26.3	31.5	26.5	27.4	29.5
ROA (annual)	2.4	2.0	2.1	2.1	2.9	2.0
ROE (annual)	14.9	13.8	14.6	14.1	18.6[a]	n.a.
Net interest margin to income	54.8	54.6	50.7	52.0	n.a.	n.a.
Non-interest expense to income	22.2	28.9	24.8	27.4	n.a.	n.a.

Source: BOJ and IMF.
Note: ROE = Return over equity; a. Estimated.

4. **Prudential indicators are sound.** The banking sector is adequately provisioned, with provisions fully covering non-performing loans (NPLs), and capitalization of 14.6 percent. NPLs have gradually decreased over the years, mainly driven by continuous write-offs, reaching 2.8 percent of total loans in

March 2017. Robust profitability ratios have ensured capital replenishment, with banks reporting an ROA of 2 percent, in the same period.

5. **However, some vulnerabilities exist due to the rising dollarization of investments and deposits.** As of March 2017, 46 percent of deposits were in foreign currency, constituting one of the highest dollarization rates in the region. The authorities are planning measures to reduce the risk of dollarization, including the equalization of reserve requirements for foreign currency and domestic currency deposits, as well as a cost-benefit analysis (CBA) on stricter requirements for foreign currency deposits.[38]

Table 4.3. Commercial Banks - Aggregated Balance Sheet (in J$, millions, Unless Otherwise Stated)

	2012	**2013**	**2014**	**2015**	**2016**	**Feb-17**
Assets						
Credit to private sector	282	334	352	388	471	544
Foreign assets	126	154	202	235	265	312
Government bonds and reserves	157	148	154	159	189	233
Other assets	56	60	70	87	85	102
Credit to public sector	25	28	29	26	24	26
Cash and investments	10	11	11	11	12	11
Total assets	**656**	**735**	**819**	**906**	**1,047**	**1,228**
Liabilities						
Core deposits	317	331	369	428	485	577
Time deposits	98	126	119	129	140	180
Foreign liabilities	40	48	53	80	110	114
Public sector deposits	30	30	29	30	42	39
Other liabilities	79	89	129	110	129	317
Total liabilities	**564**	**625**	**700**	**777**	**906**	**1,058**
Net capital	**92**	**110**	**118**	**128**	**141**	**170**
Memorandum items						
Foreign currency deposits	176	207	233	266	308	360
Foreign currency deposits as percent of total deposits	*39.6*	*42.5*	*44.9*	*45.3*	*46.1*	*46.4*
Foreign currency loans	106	137	122	121	159	165
Foreign currency loans as percent of total loans	*34.5*	*37.7*	*32.0*	*29.3*	*32.0*	*28.9*
Foreign currency investments	126	154	202	235	265	312
Foreign currency investments as percent of total investments	*36.1*	*41.2*	*46.1*	*47.9*	*48.1*	*56.3*

Source: BOJ.

6. **Credit unions can play a significant role to enhance financial inclusion, but they have capacity constraints.** Following the consolidation of the sector, there are currently 29 credit unions, which form part of the national association, Jamaica Co-operative Credit Union League Limited (JCCUL). Credit

[38] IMF. 2016. "Jamaica : Request for Stand By Arrangement and Cancellation of the Current Extended Arrangement Under the Extended Fund Facility-Press Release and Staff Report". Country Report No. 16/350.

unions are currently self-regulated through the JCCUL, and the BOJ maintains some oversight. The Credit Union legislation expected to pass by 2018 will bring credit unions under official BOJ supervision. With J$92 billion in assets (US$738 million) in February 2017, credit unions' assets are equivalent to about 3 percent of GDP. Through 120 branches in 14 parishes, credit unions had roughly 900,000 members (~30 percent of the population), 2 million deposit accounts, and 150,000 loan accounts. They are mainly focused on consumer loans (85 percent of credit portfolio) and are also offering mortgage (12 percent) and other loans (3 percent).

7. **Credit unions' growth has been constrained by limited funding sources and maturity mismatches.** In 2016, their assets increased by 7.4 percent (8.1 percent in 2015). Credit unions primarily depend on members' contributions and short-term commercial loans to fund their operations. NPLs appear to be manageable: while using a more stringent definition (net loans), credit unions reported an NPL to loans ratio of 3.8 percent in December 2016. In February 2017, credit unions reported a capital to assets ratio of 18.3 percent, and over the last three years, they have reported positive net profits.

Table 4.4. Credit Unions - Balance Sheet Data and Key Indicators

	Unit	2014	2015	2016	Feb-17
Total assets	J$, billions	82.3	89.0	95.6	92.2
Total loans (net of provisions)	J$, billions	55.7	59.6	63.7	60.9
Total investments	J$, billions	11.2	12.2	15.3	15.4
Cash and placements	J$, billions	9.4	10.7	9.8	9.4
NPLs (90 days)	J$, billions	1.9	2.4	2.4	n.a.
Capital base	J$, billions	9.7	10.2	11.2	16.9
Total savings fund	J$, billions	62.3	67.7	73.4	71.3
Member savings	J$, billions	44.6	49.1	54.1	51.8
Term deposits	J$, billions	17.7	19.7	19.3	19.5
Net income	J$, billions	1.4	1.7	1.3	n.a.
Capital to assets	%	11.8	11.5	11.7	18.3[a]
NPL / loans (net of provisions)	%	3.4	4.0	3.8	n.a.
Net income / total income	%	12.7	8.7	10.7	n.a.
ROA	%	1.7	1.1	1.4	n.a.
Number of credit unions	#	37	34	32	29
Membership	# (millions)	1.02	1.00	0.95	0.89
Deposit accounts	# (millions)	2.04	2.16	2.20	2.20

Source: BOJ's Annual Report (2016).
Note: a. Capital ratios were revised in 2017. Original numbers for 2014–2016 were maintained.

B. Access to Finance for MSMEs

8. **Access to credit for SMEs in Jamaica is particularly low.** Almost all formal SMEs have access to checking or saving accounts, but only about 27 percent have a bank loan or line of credit, well below the average of 48 percent in LAC.[39] Investments are mostly financed with own funds, and the financing gap

[39] World Bank. 2010. *Enterprise Surveys: Jamaica Country Profile*.

might be as high as 40 percent of GDP.[40] About 70 percent of investments by SMEs are financed internally (the LAC average is 62 percent). The limited supply of debt and equity financing mechanisms for this segment, or its prohibitive cost and requirements, has a negative impact on entrepreneurship, business profitability and stability through the business life cycle, and employment.

Figure 4.5. Proportion of Firms with Access to a Bank Loan or Line of Credit, 2010 (percent)

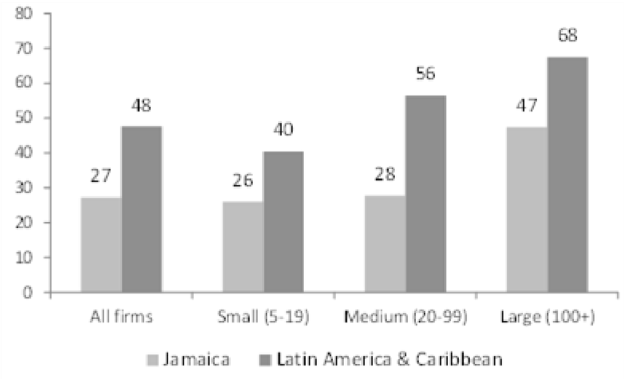
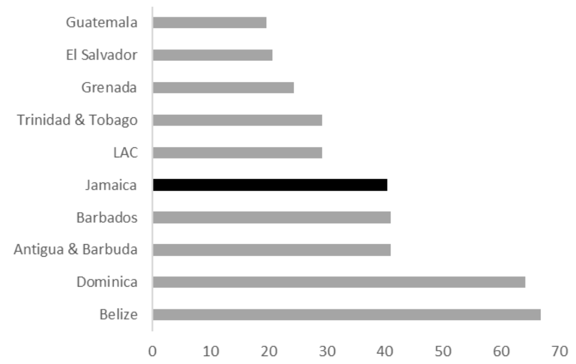
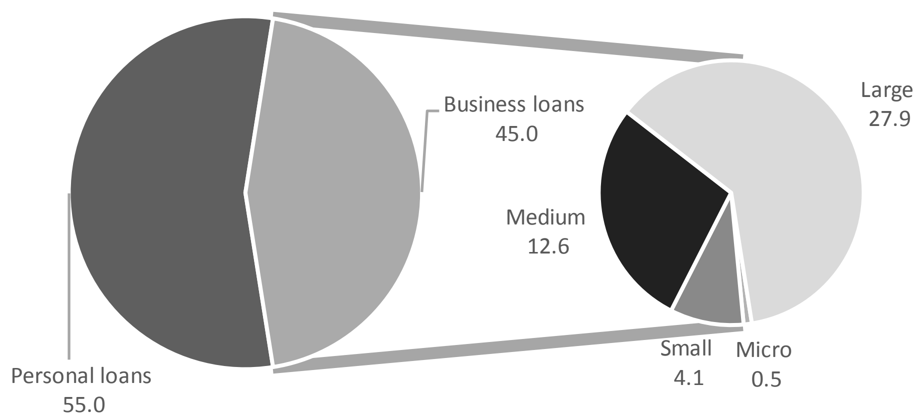


Figure 4.6. Share of Firms Identifying Access to Finance as a Major Constraint, 2010



Source: Enterprise Surveys.

Figure 4.7. DTIs - Credit to the Private Sector, December 2016



Source: BOJ.

9. **Lending by commercial banks is tailored to large corporates and selected sectors, while other alternatives for financing are limited.** Financial institutions lack instruments, lending practices, and credit risk assessment tools that are specifically designed for SMEs. Non-bank financing is narrow, with credit unions focusing on consumer finance and the microfinance sector being underdeveloped. Factoring and leasing are scarcely used. In terms of equity financing, VC is not developed, because the ecosystem for risk capital is still at nascent stages. As explained in the sector context, a combination of factors is behind the limited access to finance for MSMEs.

[40] According to the IFC Enterprise Finance Gap Database (2010), the financing gap for MSMEs was estimated at US$5.3 billion.

10. **A nascent financial infrastructure and limited competition in the banking sector have contributed to increased credit risk in the past and, consequently, to a higher cost of financing.** Financial institutions have balanced the higher credit risk by limiting the supply of credit, increasing the cost of financing, and/or requiring significant collateral from MSMEs. The cost of financing is particularly burdensome for MSMEs. As of March 2017, banks' lending rate in local currency for large corporates was less than 9 percent, compared to about 21 percent for micro enterprises, 11 percent for small enterprises, and 10 percent for medium enterprises.[41] Credit unions and MFIs charge microenterprises rates of above 50 percent. Banking spreads have historically been driven by insufficient competition in the financial sector. Spreads have increased substantially at the onset of the 2008 financial crisis, jumping to 14 percent in 2010. Since then, however, lending spreads have come down to 12 percent, which is still well above the 6–7 percent range observed in the region. In addition to the cost of financing, high collateral requirements, ranging from 190 percent to 240 percent of the loan, also present a significant challenge.

C. Venture Capital

11. **The DBJ has worked with the IDB, through its Multilateral Investment Fund (MIF), to support an entrepreneurial and early stage ecosystem in Jamaica.** This program has included several activities, ranging from training and capacity building for PEVC stakeholders to a Fund of Funds program. The DBJ has earmarked J$ 1 billion over the next five years to be invested in PEVC funds supporting Jamaican businesses.[42] Since the first request for proposal for eligible PEVC funds was held in 2015, the first two recipients of a capital infusion are Portland Private Equity Fund II and Caribbean Mezzanine Fund. However, these initiatives are not primarily focused on risk capital for SMEs. Several other promising initiatives have also spurred the risk capital ecosystem. Two angel networks—First Angels in Kingston and Alpha Angels in Montego Bay—set up through InfoDev-EPIC programs, currently operate in Jamaica. Their investment sizes are small, ranging from US$45,000 to US$180,000. InfoDev is launching a Caribbean Investment Facilitation Project that includes a co-investment grant facility to crowd in investments by angel investors and angel investor groups in start-ups and an investment readiness grant facility to prepare start-ups for investments by angel and VC investors.[43]

12. **Given these foundational steps in the early stage ecosystem, there is a need to address the continued risk capital gap for established SMEs in Jamaica through a proposed SME Fund.** Despite promising interventions in the angel/start-up segment, the avenues for expansion financing for established SMEs in Jamaica remain limited. Other players in the market do not target Jamaica SMEs or only serve SMEs risk capital needs to a limited degree.

13. **According to market intelligence, there are approximately 150–300 Jamaican SMEs that fall within this category, ranging in sectors from tourism to manufacturing, construction, and creative entertainment.** The World Bank conducted an analysis of the pipeline for a proposed SME Fund in Jamaica based on focus groups and one-on-one interviews with 48 SMEs. Of the 48 SMEs in need of risk

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[41] Based on annual turnover, the BOJ's Credit Conditions Survey adopts the following definition for MSMEs: less than US$100,000 (micro), US$100,000 to –5 million (small), and US$5–25 million (medium). Based on loan size, the thresholds used are less than US$10,000 (micro), US$10,000–100,000 (small), and US$100,000 to US$1 million (medium).

[42] DBJ's Annual Report - 2014/2015.

[43] Divakaran, Shanthi, Michel Noel, Patrick J. Mcginnis, Sam Schneider, Sam Raymond, Erik Huitfeldt. 2016. "Investing Back Home: The Potential Economic Role of the Caribbean Diaspora." World Bank Group, Washington, DC.

capital, 20 were deemed worthy of further due diligence, indicating that a pipeline for a US$15 million SME Fund, investing an average of US$750,000 per deal, likely exists. The analysis indicated that there is investor interest in new investment vehicles to deploy Jamaican dollar capital. Through the GOJ participation, financial and other incentives will be provided to private investors to contribute to the SME Fund, with demonstration effects for the development of PEVC for SMEs in the longer term. [44]

14. **While the Junior Market of the Jamaica Stock Exchange provides an avenue for equity financing for SMEs (in the range of US$500,000 to US$5 million), there are limited listings on the market, which is still relatively illiquid.** As of June 2016, there are 33 securities listed on the JSE Junior Market, from which a total of J$5.2 billion (US$40 million) had been raised. Securities dealers may take equity positons in SMEs before listing them on the junior market, but these brokers find that many of their SME clients seeking equity financing lack the operational history to list and need an alternative source for risk capital. Market intelligence therefore identifies a proposed vehicle that would provide risk capital to Jamaican SMEs in the range of approximately US$100,000 to US$2 million.[45] In addition, a feasibility study found a critical need for risk capital for SMEs with revenues in the range of J$50 million (~US$390,000) to J$200 million (~US$1.5 million), which are not being serviced adequately, to fund expansion, working capital, governance, and accounting services. The study also found that growth sectors in the economy, such as tourism, business processing outsourcing services, emerging ICTs, alternate energy, agri-business, and manufacturing, represent the most attractive prospects for investment. Market analysis also suggests that quasi equity may often be more palatable for Jamaican SMEs reluctant to cede ownership. Finally, as studies on global SME Funds show, technical assistance for SMEs pre and post investment can help deploy capital.[46]

15. **While second to deal flow, legal/regulatory/taxation constraints can also hinder the flow of domestic and foreign capital to PEVC in Jamaica.** Legal and regulatory analysis indicates four main areas of potential reform:

(a) **Legal structure.** Ensure Partnership (Limited) Act of 2017 is fully in force and fiscal laws clearly provide tax transparency for the LP structure.

(b) **Definition of qualified investors.** Ensure definition for investors qualified to invest in PEVC has thresholds that are aligned to global standards.

(c) **SME Fund Management Firm-oriented regulation.** Develop new regulation (or amend existing Collective Investment Scheme regulations) to register and supervise SME Fund managers, for above- and below-threshold assets under management, in alignment with international practice and develop the capacity of the FSC to supervise the SME Fund managers.

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[44] Based on interviews conducted during project preparation with commercial banks, development agencies, market brokers, the Jamaica Stock Exchange, fund managers, and a total of 48 SMEs to triangulate on a meaningful estimate.

[45] The World Economic Forum has identified a persistent gap in financing for businesses that require between US$50,000 and US$2 million in external capital. See Divakaran, Shanthi, Patrick J. McGinnis, Masood Shariff. 2014. *Private Equity and Venture Capital in SMEs in Developing Countries: The Role for Technical Assistance.* Policy Research Working Paper No. 6827. World Bank, Washington, DC. © World Bank. https://openknowledge.worldbank.org/handle/10986/17714 License: CC BY 3.0 IGO."

[46] Divakaran, Shanthi, Patrick J. McGinnis, Masood Shariff. 2014. *Private Equity and Venture Capital in SMEs in Developing Countries: The Role for Technical Assistance.* Policy Research Working Paper No. 6827. World Bank, Washington, DC.

(d) **Institutional investment.** Ensure domestic institutional investors' ability to invest in the PEVC asset class both onshore and offshore is in alignment with global norms.

16. **Currently, domestic institutional investors do not invest significantly in the asset class.** The FSC regulates Collective Investment Schemes, such as mutual funds and unit trusts, as defined by regulation under the Securities Act. These regulations will need to be reviewed to ensure appropriate exemptions for closed-ended funds, offering more light-touch regulation for PEVC funds.

17. **There is also lack of clarity about the ability of PEVC funds to mobilize capital from domestic institutional investors.** There are currently 411 active pension funds in Jamaica that cannot invest in the asset class unless a PEVC vehicle is listed. However, the FSC notes that upcoming regulation will allow pension funds to invest in the asset class, whether registered offshore or onshore.[47] This regulation is expected to come into force in 2018. In addition, there is lack of clarity on how much pension fund assets under management can be invested in foreign currency denominated assets. Pension fund investment guidelines allow the funds to invest up to 20 percent in foreign currency denominated assets versus the BOJ Act, which caps this at 5 percent (for all investors). There are currently 16 insurance companies in Jamaica[48] that could potentially invest in the asset class, even though the Insurance Act of 2001 does not specify PEVC in categories of investment, because Insurance Regulations of 2001 leave open the possibility to invest in the asset class subject to certain limitations.[49] An initial review indicates that insurance companies are not active in this asset class. The MOFPS and Tax Administration Jamaica have issued Approved Venture Capital Company Guidelines, which outline modes of tax relief for VC companies incorporated under the Companies Act in Jamaica and engaging in VC deals in the country. The tax framework needs to provide incentives for PEVC funds in a nondiscretionary manner.

D. Development Bank of Jamaica

Overview

18. **Established in 2000, the DBJ is a development bank offering second-tier lending, guarantees, and direct lending for strategic projects for the country.** The DBJ is a wholly owned government institution[50] through shares owned by the Accountant-General. In 2010, the bank was constituted from the merger of the Agricultural Credit Bank Limited and the National Development Bank, followed by the incorporation of the National Investment Bank of Jamaica Limited in 2006. Under the purview of the MOFPS, the DBJ was constituted as a limited liability company incorporated under the Companies Act.

Products and Services

19. **The DBJ is committed to supporting entrepreneurs and the productive sectors.** The DBJ provides funding and technical assistance to large projects while supporting MSMEs through different channels. The bank's main activities include:

(a) Second-tier lending to AFIs, MFIs, and the National People's Cooperative Bank (NPCB);

[47] This is one priority action of the EGC's Growth Framework in the IMF's SBA.
[48] Six life insurance companies and 10 property & casualty insurance companies.
[49] 10 percent of assets, based on their minimum capital requirement, and only up to 1 percent in any one entity.
[50] The majority of shares are owned by the Accountant-General of Jamaica, a Corporation Sole, with the exception of two shares, which are held by the Chairman of the Board of Directors.

(b) Guarantees through the CEF;

(c) Direct lending to selected projects in strategic areas for the country;

(d) Capacity development and technical assistance to MSMEs, through the Voucher for Technical Assistance Programme;

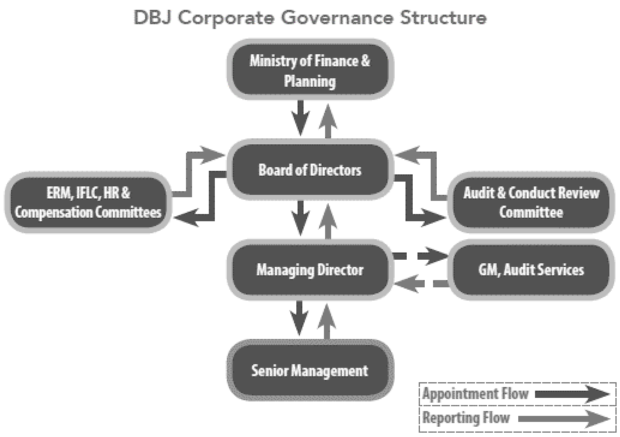
(e) Investments in PEVC funds through the Jamaica Venture Capital Programme; and

(f) Structuring and management of public-private partnerships and privatization transactions.

Corporate Governance

20. **The DBJ's legal framework falls under different laws, including the Companies Act, the Public Bodies Management and Accountability Act, the Financial Administration and Audit Act, and the Pension Act (Superannuation and Retirement Schemes).** Each year, management presents an annual report to the Accountant-General and the Board of Directors, who jointly review the results and activities planned for the coming year. The General Meeting also approves dividends and external advisors, which are renewed every five years.

Figure 4.8. Corporate Governance Structure of the DBJ



Source: DBJ (2016).

21. **The DBJ's advances in corporate governance over recent years demonstrate a high level of commitment to strive for the best corporate governance practices in place.** Spurred in part by the MOFPS issuance in 2012 of the guidelines for the Corporate Governance Framework of Public Bodies, the DBJ has issued a number of internal policies, from risk to IT and human resources (HR) policies, to enhance further operational efficiency. A policy on corporate governance has also been issued, which is also routinely reviewed by the internal audit function. This corporate governance framework is implemented by the Board of Directors, with support of four subcommittees and an independent internal audit.

22. **The DBJ's Board has a significant representation of private sector representatives.** The management of its own retirement scheme puts the DBJ under the regulatory requirements for pension funds by the FSC (Pension, Insurance, and Capital Market Regulator); hence, directors are first identified on the basis of the FSC's fit and proper standards and then presented for final clearance to the FSC, at the end of the appointment process. Candidates are all recommended by the MOFPS and ratified by the Accountant-General, who acts as the holder of the DBJ shares on behalf of the GOJ. Among the selection requirements are contribution to the country and its economy, integrity, sound and independent judgment, financial literacy, knowledge of the business, and commitment of time.[51] The board is

[51] DBJ's Annual Report - 2014/2015.

composed of 13 members, 11 of whom are selected from the private sector, and the remaining 2 are civil. The board chair is separate from top management, although the Managing Director remains part of the board composition. The board is formed by experienced Jamaican professionals, with technical qualifications and working experience in finance, business, and/or law.

23. **The subcommittees support the board with the following functions:**

(a) Audit and Conduct Review Committee, responsible for oversight of governance, risk management, internal controls, financial statements, and compliance with legal and regulatory requirements

(b) Investment, Finance, and Loans Committee, responsible for investment and lending policies, monitoring risks in the investment portfolio, recommendations of investments, and approval of loans to AFIs, according to levels established by the board

(c) HR and Compensation Committee, in charge of monitoring employment practices and their compliance with labor laws, as well as recommendations of a remuneration policy

(d) Enterprise Risk Management Committee, responsible for the assessment of risks and recommendations of risk tolerance levels and senior management

24. **The board is also supported by Internal Audit, Risk Management, and Compliance function, which act as an independent review and consultancy body.**

25. **The board should increase efforts to strengthen risk and audit matters.** The board of directors meets monthly, while the subcommittees meet on a quarterly basis. While the presence of subcommittees is a good practice and it facilitates the workings of the board, audit and risk management issues are mainly discussed in committee meetings and filtered through to the main board only if the committee deems it appropriate. Risk and audit matters should be discussed monthly and further analyzed through the committees.

Risk Management

26. **The DBJ uses an integrated Enterprise Risk Management Framework.** While customized to the DBJ's operations, this framework was designed heavily influenced by COSO and the ISO 31000:2009 ERM framework.[52] The DBJ has defined appetite levels as well as tolerance limits for each business activity, which have been established and reviewed quarterly by the ERM Board Committee and approved by the board of directors. Compliance, audit, and risk controls are well set and evolve following the evolution of the business of the DBJ. The DBJ is transitioning to a new loan management software, and this has direct implications on audit processes and procedures (a new auditor with IT expertise is being hired) and risk data generation and aggregation.

[52] Committee of Sponsoring Organizations of the Treadway Commission (COSO), International Organization for Standardization (ISO), and Enterprise Risk Management (ERM).

Business Model

First-tier Lending

27. **Direct lending represents roughly 32 percent of the DBJ's loan portfolio, which is equivalent to US$47 million.** Since 2006, this modality of credit has not been a priority to the DBJ, being restricted to strategic and transformative projects. In the fiscal year of 2016, 7 direct loans were approved (6 in foreign currency). In total, there were 15 projects, fully collateralized as required, mostly serving the agriculture and services sectors. Candidate projects have first to demonstrate economic impact and receive endorsement from line ministries, before they are appraised by the DBJ's credit department. Maximum and minimum lending limits are US$5 million and J$50,000 (or equivalent) per project, and the DBJ can only lend up to 70 percent of total project costs, if it is the sole lender. The DBJ's preferred modality for direct lending is through syndication of co-financing with AFIs. In this case, the DBJ can only lend up to 65 percent of project costs not financed by others. The project debt to equity ratio must be at least 70:30. The DBJ's development mandate is achieved through the provision of lower rates (ranging from 4.5 percent to 12 percent), longer repayment periods (up to 12 and 15 years for private and public projects, respectively), and more flexible equity-like repayment terms (such as granting of extended moratoria of up to 3 and 5 years) to lower the overall costs of financing.

Table 4.5 DBJ - Loan and Guarantee Portfolio, Outstanding Balance, in J$, millions

	2013	2014	2015	2016	2017	% in 2017
First-tier lending	**5,234.4**	**5,681.6**	**5,567.2**	**5,416.3**	**5,842.9**	**32**
Second-tier lending	**6,732.2**	**9,581.9**	**11,161.8**	**11,901.5**	**12,386.5**	**68**
Loans to AFIs	*4,954.2*	*7,780.3*	*9,314.9*	*9,880.1*	*10,221.6*	*83*
Loans to NPCB	*1,192.7*	*1,264.5*	*1,078.9*	*958.2*	*803.6*	*6*
Loans to MFIs	*585.3*	*537.1*	*768.0*	*1,063.2*	*1,361.3*	*11*
Total loans	**11,966.6**	**15,263.5**	**16,729.0**	**17,317.8**	**18,229.4**	
CEF - Origination	**166.8**	**83.9**	**218.7**	**282.3**	**551.6**	
CEF - Balance				**477.7**	**730.6**	

Source: DBJ.
Note: Fiscal year ended in March.

Second-tier Lending

28. **The DBJ's financing to MSMEs is facilitated through credit lines to AFIs (which are banks and credit unions) and MFIs.** At the end of fiscal year 2017, there were 23 and 14 accredited AFIs and MFIs, respectively. Through these wholesale lending windows, AFIs and MFIs are responsible for credit assessment and fully bear the credit risk of loans. As of March 2017, the DBJ's second-tier portfolio accounted for 68 percent of total loans, which is approximately equivalent to US$99 million.

Financial Soundness

Portfolio Quality

29. **With total assets of US$231 million at the end of fiscal year 2017, the DBJ's main exposure relies on its credit portfolio.** Loans accounted for about 62 percent of assets in that period. Over the last

decade, the DBJ has increasingly shifted toward supporting MSMEs, as opposed to focusing on direct lending and infrastructural loans. In 2017, loans and receivables (first- and second-tiered) have increased by 1.9 percent, versus 3.6 percent and 8.2 percent observed in 2016 and 2015, respectively.

30. **The DBJ's prudential indicators have demonstrated prudent risk management.** Despite poor economic conditions, the bank has managed to keep low NPLs given its focus on the wholesale lending portfolio. As of March 2017, overall NPLs accounted for 4.6 percent of gross loans (3.6 percent, reported in March 2016). The top 20 credit exposures (including both AFIs and projects) account for about 87 percent of loans. For direct lending, NPLs accounted for 2.9 percent of the portfolio, and for second-tier lending, NPLs were about 1.8 percent.

Figure 4.9. DBJ - Assets Composition (percent)

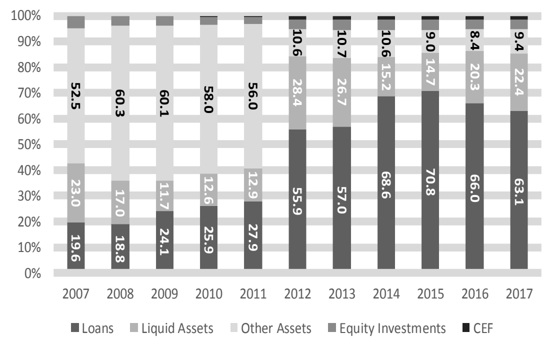
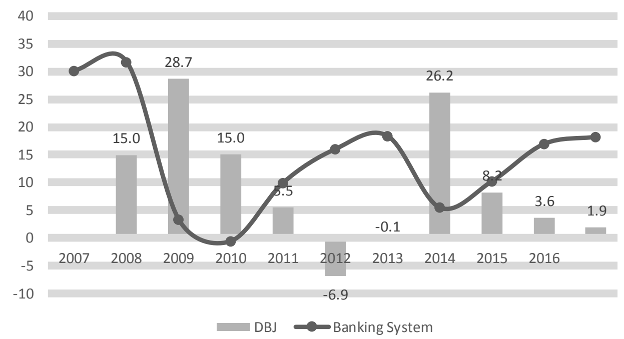


Figure 4.10. DBJ - Loans, Receivables, and Guarantees Growth (percent)



Source: DBJ.

Table 4.6. DBJ - Prudential Indicators (percent, Unless Otherwise Stated)

	2012	2013	2014	2015	2016	2017
Capital to risk-weighted assets	n.a.	47.8	43.8	50.8	47.5	50.5
Tier 1 capital ratio	n.a.	11.8	9.6	9.8	8.9	9.3
Tier 2 capital ratio	n.a.	36.0	34.2	41.0	38.5	41.2
NPLs to gross loans	4.2	12.7	6.2	7.4	3.6	4.6
Provisions to NPLs	187.2	85.8	75.4	61.7	66.6	67.8
Cash reserves to assets	28.4	26.7	15.2	14.7	20.3	22.4
Cash reserves to liabilities	53.6	40.8	23.9	24.3	31.8	34.3
ROA (annual)	10.2	-11.1	3.2	4.5	1.3	1.4
ROE (annual)	21.6	-32.1	8.8	11.5	3.6	4.1
Net interest margin	5.3	6.2	6.2	5.8	4.9	3.2
Operational expense to income	35.9	38.0	30.8	31.1	46.6	47.9

Source: DBJ. Fiscal year ended in March 2016

Capital Adequacy and Provisioning

31. **Capital buffers against losses are adequate, though they have been decreasing recently.** Credit provisioning has been low, with a coverage of 68 percent of NPLs (67 percent in March 2016). Capital

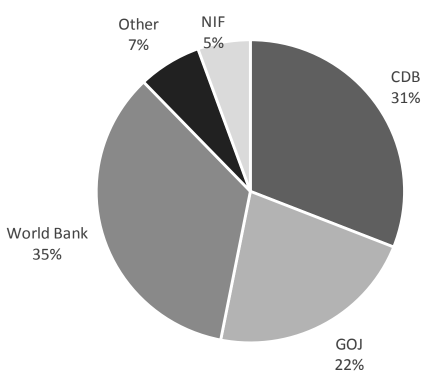
adequacy ratios have been historically very high, reaching 50.5 percent in March 2017 (47.5 in March 2016).

Profitability

32. **Declining capital ratios are explained by lower capital replenishment from profits.** This is a result of declining net interest margins and lower profitability ratios, which mirror the more attractive interest rates for borrowers. In 2017, ROA and ROE improved to 1.4 percent and 4.1 percent, respectively (1.3 percent and 3.6 percent in 2016, respectively), but are still below previous years' levels. Over the last decade, the DBJ reported losses only in 2013, when it decided to aggressively provision against potential losses in an investment in the tourism sector. Recovery efforts have led to a reversal in provisioning in the following year.

33. **Local ratings have been affirmed with a stable outlook.** In 2016, the Caribbean Information and Credit Services reaffirmed the DBJ's regional corporate ratings at CariBBB+ (foreign currency) and CariA- (local currency), and on the national scale rating at jmAA. The outlook of the ratings is stable. The DBJ has submitted financial statements according to International Financial Reporting Standards, which were audited independently by PricewaterhouseCoopers.

Figure 4.11. DBJ - Funding Structure, in 2017



Source: DBJ's 2017 Annual Report.

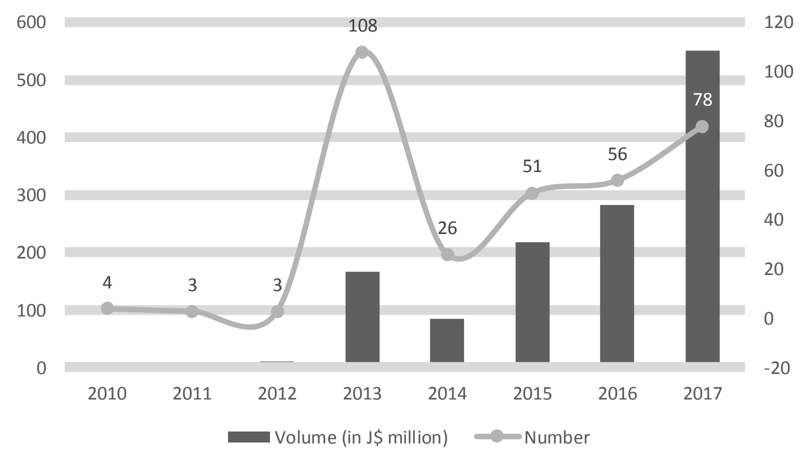
Funding and Liquidity

34. **The DBJ is not a DTI.** The DBJ's funding is composed of its own capital and long-term credit lines from international organizations, such as the Caribbean Development Bank and the World Bank. While direct loans are funded mainly by credit lines from the PetroCaribe Development Fund and capital, wholesale lending is supported by funding coming from international organizations, the National Insurance Fund, and PetroCaribe, as well.

35. **The bank's long-term and stable funding base allows it to avoid maturity mismatches and enjoy a comfortable liquidity position.** In terms of foreign currency, the DBJ's balance sheet has a mismatch, with foreign assets accounting for 47 percent of the total, in comparison with foreign currency liabilities, which account for 66 percent of the total. This net long position has generated substantial financial gains, boosting the DBJ's operating income.

Figure 4.12. Volume (left) and Number of Guarantees (right) since Inception

Credit Enhancement Facility



Source: DBJ.
Note: Fiscal year ends in March 2016.

36. **Over the recent years, the CEF has observed a consistent positive trend in usage.** In the fiscal year 2017, the facility issued 78 guarantees in the amount of J$552 million (US$4.4 million approximately), in contrast with the 56 guarantees issued in 2016, in the amount of J$282 million.[53] The average guarantee size has consistently increased over recent years, from J$2.0 million (~US$16,400) during the CEF's first year of inception ended in March 2010. Overall, average coverage levels have also increased, reaching 46 percent in 2017 from 28 percent as of March 2010. Of note, the guarantee coverage on small loans increased to 80 percent from 50 percent in November 2014.

Figure 4.13. Sector Distribution - by Volume

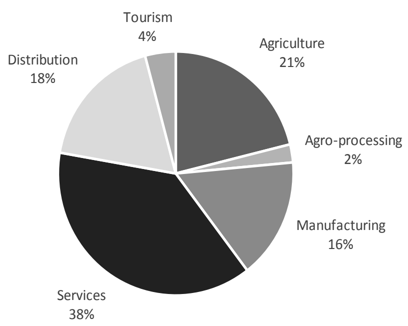
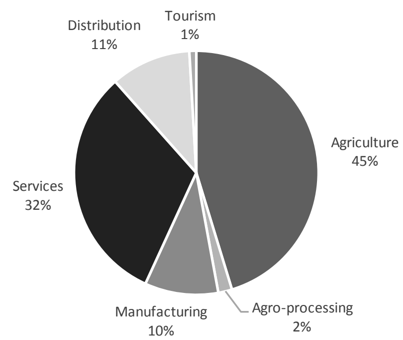


Figure 4.14. Sector Distribution - by Number of Guarantees



Source: DBJ.

37. **Historically, the main sectors supported by CEF guarantees have been agriculture and services.** Since its inception, roughly 45 percent and 32 percent of the 329 guarantees issued have been in agriculture and services, respectively. In terms of volume, 21 percent and 38 percent of the volume originated went to agriculture and services, respectively. Manufacturing (16 percent of volume) and distribution (18 percent) are also relevant.

[53] In the fiscal year ended in March 2013, the CEF's activity spiked to over 100 transactions due to the extensive use of the CEF by one lender.

Box 4.1. CEF - Existing Product Features[54]

The CEF provides the following coverage to AFIs:

- General SME loans: 50 percent of loan up to maximum of J$15 million (~US$118,000), whichever is lower
- SME energy loans: 80 percent of loan up to a maximum of J$15 million, whichever is lower
- Small loans (J$6.25 million or less; ~US$49,200): 80 percent of loan up to a maximum of J$5 million (~US$39,370), whichever is lower

The following fees are applied on the principal outstanding of guarantees at the time the fee is due:

- SME loans and SME energy loans: 2 percent per year plus the general consumption tax (GCT) applicable to guarantee fees. The following formula applies for annual payments:
  - Annual Fee = 2 percent × [percentage of loan guaranteed × amortized principal]
- Agricultural loans: 1 percent plus GCT. The following formula applies for annual payments:
  - Annual Fee = 1 percent × [percentage of loan guaranteed × amortized principal]
- **Submission of claims.** AFIs must undertake the necessary diligence in collection and exercising their rights under their loan agreements with the SME borrower. The CEF will not process a claim until the procedures have been complied with and no earlier than 30 days after the written demand by the AFIs.

[54] Several product features will change depending on the financial model and business plan that will be developed.

ANNEX 5: FINANCIAL INTERMEDIARY ASSESSMENT

1. **An assessment of the DBJ took place based on eligibility criteria in accordance with OP 10.00:**

(a) The bank must be duly licensed and at least two years in operation.

(b) The bank's owners and managers must be considered 'fit and proper'. The bank must have qualified and experienced management and adequate organization and institutional capacity for its specific risk profile.

(c) The bank must maintain capital adequacy.

(d) The bank must have adequate liquidity.

(e) The bank must have positive profitability and an acceptable risk profile. It must maintain the value of its capital.

(f) The bank must have well-defined policies and written procedures for management of all types of financial risks (liquidity, credit, currency, interest rate, and market risk, as well as risks associated with balance sheet and income statement structures) and operational risk.

(g) The bank must classify its assets and off-balance-sheet credit risk exposures (at least four times per year) and make adequate provisions. It must have adequate portfolio quality. The bank should not have more than 10 percent of criticized assets (that is, classified as doubtful and at a loss).

(h) The bank must have adequate internal audits and controls for its specific risk profile.

(i) The bank must have adequate MIS.

Table 5.1. Summary of the DBJ Appraisal

Criterion	Comments
1. License	Adequate. Under the purview of the MOFPS, the development bank was constituted in 2010, as a limited liability company incorporated under the Companies Act of Jamaica. It is not under the supervision of the BOJ.
2. Owners/managers 'fit and proper', governance quality	Overall adequate, although FSC's fit and proper criteria are the benchmark, not the BOJ's criteria.
3. Capital adequacy	Adequate.
5. Liquidity	Adequate, reflects long-term and stable credit lines.
6. Profitability	Profitability has been on a declining trend.
7. Policies and risk management functions	Adequate in principle; several changes have occurred in policies and processes, but have not been tested yet.
8. Asset quality and provisions	Adequate; NPL ratio is slightly above the banking system's average.
9. Internal audit and controls	Adequate; IT skillset is also being contracted for audit purposes.
10. Adequate MIS	Several changes have occurred in risk policies and new MIS platform; testing has not been completed yet.

ANNEX 6: ECONOMIC AND FINANCIAL ANALYSIS

1. **Basis for economic analysis.** An economic analysis of the Project was conducted to help address three key questions:

(a) Do the expected benefits from the project activities outweigh their costs?

(b) Is public sector financing the appropriate vehicle?

(c) Is there sufficient value added to justify World Bank contribution?

2. **The CBA approach was adopted to calculate the NPV and ERR for the main components of the Project: Components 1 and 2 (CEF and SME Fund).** To be economically acceptable, a World Bank-financed project must produce a positive NPV. An economic analysis was not conducted for other components, given the challenge of attributing specific outcomes to them. Nevertheless, their costs were included in the analysis.

3. **Time horizon.** The analysis considered impacts on beneficiaries supported between the funds' capitalization and the Project's closing date (five years). Benefits for MSMEs (increase in sales) are materialized with a one-year lag. Moreover, a residual value was included for the SME Fund at project closure to reflect the 10-year fund life. Economic returns are likely estimated with a downward bias, because they do not reflect benefits sustained beyond the project cycle.

4. **Summary.** Under conservative assumptions, the total project investment is associated with an NPV of US$51.8 million (J$11 billion) and an ERR of 104.7 percent. The results are robust partially because guarantees do not follow the same capital requirements as loans and, therefore, the amount allocated to the CEF has more leverage. A sensitivity analysis with three conservative scenarios was performed for each component and consolidated for the Project. While the probability of these scenarios materializing simultaneously for both components is low, the project-level NPV is robust for two out of three scenarios, ranging from −US$11.7 million to US$24.5 million. The assumptions for each component are described in the following paragraphs, and a 10 percent discount rate was used.

Component 1: CEF

5. **Evidence on the impact of public PCGs on firms' performance is scarce.** A panel-data study in Colombia found that firms that have gained access to credit backed by a PCG were able to grow in terms of output (6 percent in one year) and employment (3.7 percent). However, the study could not find evidence on productivity, wages, or investments. The study suggests that firms might use credit for working capital purposes, as opposed to capital investment.[55] In the Republic of Korea, public PCGs were associated with increased sales and employment growth, as well as higher wages and firm survival rates. In the United States, districts with a higher number of guaranteed loans were associated with higher employment.[56]

[55] Arraiz, Melendez, and Stucchi. 2012. *Partial Credit Guarantees and Firm Performance: Evidence from Colombia*.
[56] Gozzi and Schmukler. 2016. *Public Credit Guarantees and Access to Finance*.

6. **Economic costs are represented by project disbursements equivalent to US$25.5 million.** These include the US$5 million and US$20 million loans from the World Bank and IDB, respectively. The analysis assumed that the capitalizations would start within the first year of project implementation (2018). The analysis adopted project disbursements as a conservative approach, given that the guarantees are paid back by the private sector. The analysis included additional economic costs: (a) J$35 million in implementation costs, growing at 10 percent per year, and (b) non-recoverable losses on claims, based on a 3 percent NPL ratio and 35 percent credit recovery.

7. **Expected economic benefits are increase in sales at the firm level, as a result of increased access to finance.** The analysis assumed that firms would observe a 10 percent increase in sales with a one-year lag. To be conservative, the analysis did not take into account growth in sales beyond that. An estimated 1,100 guarantees will be issued during the project cycle. Using average annual sales for MSMEs of US$1 million, these estimates yield an increase in sales of US$107 million. Under these assumptions, the component would produce an NPV of US$47 million and an ERR of 124 percent.

8. **These assumptions are considered conservative.** Actual economic costs are far lower than project disbursements. On the other hand, economic benefits are likely higher, because growth in sales are expected to sustain over time and multiplier effects were not included in the analysis. This approach to economic benefits is consistent with the one adopted for the SME line of credit of the Jamaica Competitiveness and Growth project. More importantly, the analysis does not include a residual value to reflect the long-term nature of a capitalization (that is, financial outflows are limited to claims), which will have impacts beyond the Project.

9. **A sensitivity analysis showed that returns of the component are sensitive to the number of guarantees issued, the size of targeted firms, and expected growth in sales.** The following scenarios were taken into account:

(a) Economic benefits would be lower if the CEF decides to target smaller firms. If sales are 25 percent smaller, the NPV would remain positive at US$30 million, with an ERR of 86 percent.

(b) Returns would be also lower in the event of lower issuance of guarantees. Assuming 50 percent of guarantees projected in the base case scenario (550 guarantees), the NPV would be US$13 million and the ERR 47 percent.

(c) Finally, the analysis also simulated scenarios with different growth in sales and default rates. Under the most restrictive scenario (scenario 3), the NPV would be equivalent of negative US$6 million and the ERR would be −8 percent.

Table 6.1. CEF - Assumptions for Sensitivity Analysis

	Scenario 1	Scenario 2	Scenario 3
Growth in sales (%)	7	5	3
Default rate (%)	6	7	8
NPV (in US$, millions)	23	8	−6
ERR (%)	68	33	−8

10. **Following conservative assumptions, a preliminary financial analysis was also conducted.** The analysis projected revenues and expenses, with the CEF as an independent entity. During the project cycle, the projected profits for the expanded CEF would sum up to US$5.2 million, and the ROE is projected at 5.2 percent by Year 5 (currently at 4.7 percent). Financial sustainability is also supported by a steady stream of investment income coming from the capital injection, which would more than cover operational expenses. To be conservative, the analysis did not incorporate operational improvements, which are expected from the project.

Component 2: SME Fund

11. **Evidence on the real effects of private equity investments is positive, although varying across countries and industries.** Research shows that PEVC is often associated with higher revenues, employment, and operating efficiency.[57] A recent World Bank-funded project in Morocco indicated positive economic and social returns supported by higher sales and employment growth over the investment horizon, increased levels of training, improvements in corporate social responsibility functions, and existence of community support programs. Studies in the United States found significant increases in productivity and improvements in operating performance.[58] A panel-data study in Europe shows that private equity investments had beneficial effects on entry, especially in countries with stronger judicial systems and lower informality. The same study also suggests that private equity generates value through fostering entrepreneurial activity in the economy.[59] Finally, public support for risk capital can contribute to the mobilization of private resources. In Latin America, a Dalberg study commissioned by the IDB found that VC-backed companies in their sample observed revenue growth rates of 23 percent, surpassing the national economy's growth rate. Moreover, these companies doubled their size in a period of 4–5 years. The same study estimated that US$1 invested in VC can generate up to US$6.45 in economic activity through wages, payments to providers, and taxes.[60]

12. **A similar approach was adopted for this component.** The analysis was restricted to project disbursements of US$7 million. The first capitalization tranche was projected to occur by Year 2 of project implementation. The economic model assumed 18–25 percent increase in sales as benefits, based on firm size. To be conservative, the analysis did not incorporate sales growth beyond that point. The analysis assumed that the fund would make 20 investments during the project cycle. A residual value was included to reflect the benefits beyond the project's closure (the SME Fund is expected to be a 10-year fund, including a divestment period). The model also incorporated probabilities of success (that is, the probability of a firm realizing expected sales). Under these assumptions, returns for the SME Fund would be an NPV of US$6.6 million and an ERR of 36 percent.

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[57] Paglia and Harjoto. 2014. *The Effects of Private Equity and Venture Capital on Sales and Employment Growth in Small and Medium Sized Businesses*.
[58] Davis et al. 2014. *Private Equity, Jobs, and Productivity*; Cohn and Towery. 2013. *The determinants and consequences of private equity buyouts of private firms: Evidence from U.S. corporate tax returns*.
[59] Popov and Roosenboom. 2009. *On the Real Effects of Private Equity Investment: Evidence from New Business Creation*.
[60] Dalberg and FOMIN. 2012. *Venture Capital: Driving Development in Latin America.*

Table 6.2. SME Fund - Main Assumptions for Base Case Scenario

	Average Revenues (J$, millions)	Average Investment (US$, millions)	Revenues Growth (%)	Probability of Success (%)	Number of Investees
Small	175	0.20	25	50	7
Medium	300	0.75	20	70	8
Large	425	1.50	18	85	5
Overall	*Up to 425*	*Average 0.750*			*20*

13. **The assumptions adopted are considered reasonable and downward biased.** The analysis took into account only one year of project impact on sales, while growth will likely be sustained over time. More importantly, the analysis did not incorporate other indirect effects. Direct impact of the SME Fund through sales and jobs by itself is not expected to be sizeable. However, as research shows, the component is expected to have: (a) indirect positive impact on output and employment within related supply chains and (b) a demonstration effect. Both are difficult to capture and are materialized beyond the project cycle. The analysis did not incorporate these indirect benefits (employment, innovation, exports, value chain growth, and entry of new firms). Finally, the analysis did not reflect the incremental supply of equity financing beyond the Project's life.

14. **The CBA for this component has significant limitations, but it highlights the importance of the design of the fund and the profile of targeted firms.** Real returns will be driven by the mobilization of private resources and the development of a sufficient pipeline of investments. As such, the adequate design of the fund and incentives for the private sector are critical. The profile of firms is another crucial aspect. As the sensitivity analysis below shows, the NPV could become negative, depending on the fund's features. However, these assumptions are very conservative.

Table 6.3. SME Fund - Assumptions for Sensitivity Analysis

	Scenario 1	Scenario 2	Scenario 3
Growth in sales (%)	100% of base case	75% of base case	50% of base case
Fund size	US$11 million (75%)	US$7.5 million (50%)	US$5 million (30%)
NPV (in US$, millions)	3.6	−1	−3.7
ERR (%)	25	−5	−17