Report Number: ICRR0022659

1. Project Data

Project ID	Project Name	
P131201	Lao PDR SME Access to Finance	
Country	**Practice Area(Lead)**	
Lao People's Democratic Republic	Finance, Competitiveness and Innovation	
L/C/TF Number(s)	**Closing Date (Original)**	**Total Project Cost (USD)**
IDA-54710,IDA-H9580	30-Jun-2019	18,121,519.55
Bank Approval Date	**Closing Date (Actual)**	
09-Jun-2014	31-Dec-2020	

	IBRD/IDA (USD)	Grants (USD)
Original Commitment	20,000,000.00	0.00
Revised Commitment	20,000,000.00	0.00
Actual	18,152,750.68	0.00

Prepared by	Reviewed by	ICR Review Coordinator	Group
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2. Project Objectives and Components

a. Objectives

According to the Financing Agreement (page 5), the project development objective of the of the Lao People's Democratic Republic (PDR) Small and Medium Enterprise Access to Finance Project was "to provide long-term funding sources for banks to provide long-term credit to small and medium enterprises."

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

No

c. Will a split evaluation be undertaken?

No

d. Components

The project had three components.

Line of Credit Facility (US$12 million estimated at appraisal, US$15 million at first restructuring, US$13.6 million disbursed – difference between disbursed and programmed amount due to SDR/US$ exchange rate changes) supported the provision of lines of credit to participating financial institutions for extending long-term local currency loans to SMEs for the implementation of specific investment sub-projects. The implementing agency for this component would be the Department of SME Promotion (DOSMEP) at Ministry of Industry and Commerce (MOIC), acting as apex institution for the line of credit facility.

Risk Sharing Facility (US$3 million estimated at appraisal, US$0 at first restructuring, US$0 disbursed) supported the provision of a risk sharing facility consisting of partial credit guarantees to participating financial institutions to cover potential losses in an eligible portfolio of loans extended to SMEs for the implementation of specific investment sub-projects. The first round of losses would be covered by the Bank resources on a *pari pasu* basis with the participating financial institutions (the risk sharing would allow the lenders to lower their collateral requirements) while any second round of losses would be covered by resources contributed by the International Finance Corporation (IFC). The implementing agency for this component would be the IFC, acting as facility agent of the DOSMEP to manage the trust fund for the facility on behalf of the government.

Technical Assistance (US$5 million estimated at appraisal, US$4.26 million disbursed – difference due to exchange rate changes) supported the provision of technical assistance: to the DOSMEP and other relevant agencies to strengthen their capacity to formulate to implement strategies, policies, and programs related to the promotion of SMEs; to the participating and other financial institutions to improve their SME banking strategies, products, and practices, including their compliance with environmental and social due diligence and safeguard requirements; and to SMEs to build their capacity in business development and administration and financial management. The implementing agency for this component would be the MOIC.

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

Project Cost. The project was estimated to cost SDR 13 million (US$20 million equivalent) at appraisal.

Financing. The project was financed by a credit of SDR 6.5 million (US$10 million equivalent) and a grant of SDR 6.5 million (US$10 million equivalent) from the International Development Association to the Lao PDR for a total financing of SDR 13 million (US$20 million equivalent). The total financing of SDR 13 million (US$18.15 million equivalent) was fully disbursed. The difference between the U.S. dollar equivalent amounts at appraisal (US$20 million) and at closing (US$18.15 million) was due to changes in the SDR/US$ exchange rate over the life of the project.

Borrower Contribution. There was no borrower financial contribution to the project.

Dates. The project was approved on June 4, 2014, became effective on September 15, 2014, and closed on December 31, 2020, a year and a half after the original closing date of June 30, 2019.

Restructuring. The project was restructured thrice. The first restructuring in September 2016, with US$5.49 million disbursed, cancelled the second project component after DOSMEP and the IFC were unable to agree on the implementation arrangements for the Risk Sharing Facility (the allocation of US$3 million for this component was reallocated to the first project component), and streamlined the project implementation arrangements within the MOIC (with the Department of Planning and Cooperation at the MOIC assuming overall project fiduciary responsibility and the DOSMEP retaining technical responsibility over the project). The second restructuring in June 2019, with US$17.35 million disbursed, revised the results framework to emphasize development impact rather than transactions and extended the project closing date by a year from June 30, 2019 to June 30, 2020 to complete two technical assistance activities – technical assistance to participating financial institutions and to SMEs – which launch dates had been delayed. The third restructuring in June 2020, with US$18.01 million disbursed, extended the project closing date by six months to December 31, 2020 to complete some project activities which had been delayed by the COVID-19 pandemics (the target dates for the results targets were revised accordingly).

3. Relevance of Objectives

Rationale

Country Challenges. The project development objective was relevant to the development challenges faced by Lao PDR. with SME finance.

- Small enterprises (with 1-19 workers) and medium enterprises (20-99 workers) accounted for 99.8 percent of all business enterprises in Lao PDR, employed 81 percent of the total employed labor force, but contributed to only 16 percent of GDP, reflecting low levels of productivity among SMEs.
- Access to finance ranked as one of three major constraints to business growth for small enterprises, after unfair competition from large enterprises and tax rates, according to the Enterprise Survey of 2012. Similarly, for medium enterprises, access to finance figured as the third major constraint to business growth, after a poorly educated workforce and high tax rates. Only around 25 percent of small enterprises and 47 percent of medium enterprises had a loan or a line of credit from a bank because of complex bank loan application procedures and high loan collateral requirements. Consequently, SMEs relied heavily on informal sources of finance including the *Houay*, the rotating credit and savings associations (ROSCAs) of 12 people who contributed Kip 1 million per month for 12 months to a fund pool which was then loaned to association members.
- The bank-centric financial sector was under-developed, dominated by four state-owned commercial banks which accounted for 64 percent of all deposits and 64 percent of all loans. The banks lacked the capacity and were largely unwilling to lend to SMEs because of information asymmetries (many SMEs were not registered with the government, settled transactions in cash without invoices, and did not keep accounting records) and difficulties in executing collateral (banks took up to five years to take possession of collateral through the judicial system).

Government Priorities. The project development objective was consistent with the government priorities with SME finance.

- Adopted in 2010, the *SME Development Strategy 2006-2010* aimed to create the enabling regulatory environment for SMEs, enhance competitiveness, expand domestic and international markets, improving access to finance, create favorable conditions for establishing business organizations, encourage an entrepreneurial culture. In pursuit of the strategy, the *Investment Promotion Law* was enacted in 2009, the *SME Development Plan 2011-2015* was adopted in 2010, the *SME Promotion Law* was enacted in 2011, an online enterprise registry system and an online credit information system was launched at the Credit Information Bureau in 2011, the *Secured Transaction Law* that would allow SMEs to use movable assets as collateral was approved in 2011, the secured transaction registry was established by the Ministry of Finance in 2013, and microfinance institutions were placed under the regulatory umbrella of the Bank of the Lao PDR.
- Part of the strategy, the government established the SME Promotion and Development Fund with a US$2 million grant in 2012 to provide loans of up to US$30,000 for small enterprises and up to US$60,000 for medium enterprises at nine percent (less than one year) and 10 percent (one-three years) interest. The loans would be granted to SMEs by the Lao Development Bank.
- Additionally, the project development objective was highly consistent with the country's *Trade and Private Sector Development Roadmap*, which, among others, aimed to improve access to finance for SMEs by promoting cash-flow-based SME lending through selected commercial banks and by the establishment of a risk-sharing facility, and with the *Seventh National Socio-Economic Development Plan 2011–2015*, which, among others, aimed to strengthen SMEs as a critical element to achieve economic growth and improve competitiveness.

Bank Strategy. The project development objective was aligned with the Bank Group strategy in Lao PDR.

- The *Country Partnership Strategy for the Lao People's Democratic Republic for the Period FY12-FY16* (CPS) supported three objectives: improving competitiveness and connectivity, sustainable natural resource management, and inclusive development. The project objective was fully aligned with the first of these three CPS objectives, specifically by "creating the environment for SMEs in manufacturing, agribusiness, services to formalize and grow," "responding to government requests for SME support," and "developing a risk sharing facility to facilitate an expansion of credit to SMEs in Lao by the commercial banking sector by covering a portion of the potential losses."

Rating
High

4. Achievement of Objectives (Efficacy)

OBJECTIVE 1
Objective

To provide long-term funding sources for banks to provide long-term credit to small and medium enterprises.

Rationale

Theory of Change. The provision of a line of credit to financial institutions serving the SME market would enable the financial institutions to expand their lending to SMEs including by providing longer-term credit which would not be feasible using the contemporary financial institutions' limited capital resources. Moreover, the provision of technical assistance to financial institutions, SMEs, and the DOSMEP, as the government agency responsible for SME development, on topics including credit risk analysis and management, portfolio management, SME sector assessment, SME loan management and monitoring, and SME strategy development would strengthen the institutional and technical capacity of financial institutions to service the SME market, the SMEs to better access bank credit, and the DOSMEP to act as the country's SME development authority. Overall, financial and technical assistance would help expand SME finance and develop the SME sector.

Outputs. The project achieved six and failed to achieve one of seven output targets defined for the project objective to provide long-term funding sources for banks to provide long-term credit to small and medium enterprises.

- The number of direct project beneficiaries reached 191 SMEs by the project closing date, exceeding the target of 150. These included the SMEs which received sub-loans from funds recycled by participating financial institutions (repayments received from the first round of lending were used by the financial institutions for a second round of lending). The 191 beneficiary SMEs received 202 sub-loans.
- The percentage of women beneficiaries (SMEs owned by women) was 58 percent, exceeding the target of 20 percent.
- The percentage of non-performing loans (NPLs) among the SME loans made was 0.17 percent, exceeding the target of 5 percent. One sub-loan was classified as an NPL (grade C, D, or E in the loan classification system), while 16 sub-loans were placed on the watchlist (grade B) by the project closing date. Altogether, 52 sub-loans were affected by the economic downturn triggered by the COVID-19 pandemic. In response to the economic crisis, the central bank issued BOL Policy No. 238 as a regulatory forbearance measure offering deferred payments on loans and allowing banks to freeze their loan classification to those prevailing before the onset of the crisis and for a duration of one year. According to the ICR (pages 31-32), the NPLs might increase when the central bank eventually lifts the freeze on changes to loan classification by banks.
- The number of SME banking strategies developed by participating financial institutions was two, meeting the target of two.
- The number of staff at the DOSMEP receiving training was 95, exceeding the target of 30. Of the staff trained, the number of women was 50. The training in the English language was provided by the Vientiane Institute.
- The number of SMEs benefitting from technical assistance was 803, exceeding the target of 600. The SMEs participated in the training provided by the International Labor Organization.
- No cross-ministerial and action-oriented SME Development Action Plan for 2021-2025 was developed, failing to meet the target. According to the ICR (page 33), the activity was cancelled due to the poor quality of the plan submitted by the consultant.

Outcomes. The project achieved two and partly achieved the third of three outcome targets defined for the project objective to provide long-term funding sources for banks to provide long-term credit to small and medium enterprises.

- The volume of bank support, measured as the U.S. dollar value of lines of credit to SMEs, reached US$16.14 million by the project closing date, exceeding the target of US$15 million. The final volume of sub-loans to SMEs of US$16.14 million exceeded the target due to the recycling of funds by participating financial institutions and despite exchange rate losses which reduced the actual amount disbursed to participating financial institutions to US$13.6 million. The long-term project funds allowed the participating financial institutions to lengthen the maturity of SME sub-loans to an average 4.8 years.
- The increase in employment at beneficiary SMEs was 4.3 percent by the project closing date, only partly meeting the target of 10 percent. According to the project impact assessment, the number of full-time staff at project-supported SMEs actually increased by 13 percent, but declines in family labor and part-time staff moderated the increase in the overall number of staff to 4.3 percent only. The growth in employment at project-supported SMEs, albeit lower than target, occurred while the overall economy recorded rising unemployment rates of 4.1 percent in 2012 and 15.7 percent in 2018. Moreover, the aggregate unemployment rate worsened significantly during the COVID-19 pandemic.
- The percentage of trained staff at the DOSMEP, SMEs, and participating financial institutions who reported the medium or intensive use of lessons learned from capacity building measures reached 75 percent, exceeding the target of 70 percent. The impact assessment showed that: (a) 73 percent of SMEs used the Business Plans and improved their accounting system; (b) 64 percent of staff at the MOIC used English "a lot" and 36 percent "a little"; (c) 25 percent of government staff who were trained on environmental and social safeguards shared their knowledge with others; (d) all four participating financial institutions (100 percent) which were trained on environmental and social safeguards used the E&S Toolkit for SME access-to-finance loans; and (e) three of four participating financial institutions (75 percent) which received access-to-finance training used the lessons learned from the training in their operations.

Rating
Substantial

OVERALL EFFICACY

Rationale
With the project meeting six of seven output targets and two of three outcome targets, the degree of achievement of the project development objective to provide long-term funding sources for banks to provide long-term credit to small and medium enterprises is assessed as substantial.

Overall Efficacy Rating

Substantial

5. Efficiency

Economic Efficiency. A formal economic cost-benefit analysis was not conducted for the project at appraisal because the sub-loans could not be identified *ex-ante*. A formal analysis was not prepared at closing either. Rather, the ICR (pages 18-19) argued that the project was cost effective because the project achieved the quantitative targets on: (a) a lower US dollar financing (due to the depreciation of the US dollar against the SDR over the project life), and (b) higher economic costs due to interest rate caps by the Bank of the Lao PDR – the central bank imposed interest rate caps (the spreads between deposit and lending rates) on domestic currency loans in 2015, foreign currency loans in 2017, and interbank foreign currency loans in 2018 (the caps would be lifted in 2019). The interest rates caps did not directly affect lending under the project, but exacted costs on bank lending operations and finances in general, including of those participating under the project.

Operational Efficiency. The project funds were fully disbursed. The financing for the second project component, which was cancelled for good reasons, was reallocated to the first project component and fully disbursed. The project was completed one and a half years after the original closing date because of delays with two technical assistance activities (which were eventually completed) and because of operational difficulties associated with the COVID-19 pandemic. Moreover, because of the last two restructuring episodes, the project incurred US$360,000 in incremental costs for project management consulting work and for technical assistance to the participating financial institutions over the 18-month project extension period.

Efficiency Rating

Modest

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

	Rate Available?	Point value (%)	*Coverage/Scope (%)
Appraisal		0	0 ☐ Not Applicable
ICR Estimate		0	0 ☐ Not Applicable

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

6. Outcome

The project objective was highly relevant to the development challenges faced by Lao PDR in SME finance, consistent with the priorities of the government, and aligned with the country strategy of the Bank Group in Lao PDR. The project achieved six of seven output targets and two of three outcome targets defined for the project development objective. The efficacy of the project is rated as substantial. There was no basis to assess the economic efficiency of the project. The project funds were fully disbursed but the project took one and a half year longer to complete. The efficiency of the project is therefore rated as modest. Since there were moderate shortcomings in the project's efficiency, its overall outcome is rated moderately satisfactory.

a. Outcome Rating

Moderately Satisfactory

7. Risk to Development Outcome

Credit Risk. Credit risk – the risk of default on a debt arising from a borrower's inability to make required payments of principal or interest – remains prevalent in finance, including in SME finance. In this operation, technical assistance was extended to participating financial institutions to improve their SME strategies, banking products, and credit underwriting practices. The financial institutions would have gained expertise from the experience with this project and from the technical assistance activities to better appraise SME sub-project loan applications, conduct due diligence on SME borrowers, and manage credit and portfolio risks.

Institutional Risk. The DOSMEP benefitted from technical assistance provided under the project to strengthen its institutional capacity to manage credit lines, according to the ICR (page 17). Institutional capacity building at the DOSMEP is vital since it serves as the government's principal SME promotion and development authority. The DOSMEP also acts as the apex institution that manages lines of credit to the SME sector, including from the SME Fund which mobilizes financing from various sources for SME development. The sustainability of the development outcomes of the project relies in part on the capacity of the DOSMEP to advance the development of the SME sector and to manage new lines of credit to SMEs including from the SME Fund.

Macroeconomic Risk. Although the economy contracted 0.4 percent in 2020, amid the COVID-19 pandemic, GDP growth is forecast to rebound to 4.0 percent in 2021 and firm up to an average 4.7 percent in 2022-23, in the baseline, according to the Banks's *East Asia and Pacific Economic Update* of April 2021. A return to growth (GDP grew 4.7 percent before the pandemic in 2019) should provide the supportive macroeconomic environment to sustain the outcomes achieved by the project in SME activity and SME finance. The government, however, has to continue with policy and structural reforms, set before the pandemic, to advance the country's long-term economic prospects, including by improving revenue administration, optimizing spending, reducing civil service recruitment, refocusing on capital spending, strengthening economic governance, and modernizing legal frameworks according to the *IMF Staff Report on the 2019 Article IV Consultation*, which remains relevant.

COVID-19 Risk. COVID-19 had an uneven impact across firms in the East Asian economies, according to Banks's *East Asia and Pacific Economic Update* of April 2021. In particular, "Smaller firms, SMEs, and especially microenterprises suffered a proportionally larger drop in sales than large firms. These differences persist after controlling for initial labor productivity, firms' age and location (whether in the capital region or elsewhere in the country), and firms' linkages to international markets (either via imports or exports)." An effective containment of the health crisis should help support a recovery of economic activity moving forward. The government obtained a US$33 million loan from the Bank in April 2020 for the Lao PDR COVID-19 Response Project which aimed to support preparedness and emergency response activities, strengthen the capacity of the health system to respond to public health emergencies, and finance activities related to project management and monitoring.

8. Assessment of Bank Performance

a. Quality-at-Entry

Analytical Foundations. The project design was informed by the Bank's *Lao PDR Enterprise Survey 2012* and the government's *SME Development Strategy 2006-2010,* prepared in cooperation with Germany's Gesellschaft für Internationale Zusammenarbeit, and *SME Development Plan 2011-2015,* prepared by the DOSMEP.

Lessons Learned. According to the Project Appraisal Document (pages 10-11), the project design reflected lessons learned from other Bank SME finance operations. For the line of credit facility: the financial institutions must have a pipeline of bankable SME sub-projects; SMEs need to exhibit robust managerial skills and have strong borrower accountability; and, the project requires clearly defined and transparent performance indicators. For the risk sharing facility: participating financial institutions must fully understand the product; the Bank would need to closely coordinate with the IFC; and the participating financial institutions must firmly commit to the target market and have a clear vision of their prospective market position.

Technical, Operational, and Safeguards and Fiduciary Plans. Plans for the implementation of the project were adequate, except for the implementation arrangements for the risk sharing facility.

- A Project Implementation Manual, acceptable to the Bank, set the: eligibility criteria for financial institutions to participate in the line of credit facility; eligibility criteria for SMEs to receive sub-loans from participating financial institutions; and the terms and conditions under which participating financial institutions would make sub-loans to SMEs.
- The project would be carried out in accordance with an Environmental and Social Management Framework, an Environmental and Social Management System, and Safeguards Assessments and Plans. Participating financial institutions would be required to adopt and comply with the policies and procedures of the Environmental and Social Management System.
- The project would be carried out in accordance with the Bank's Anti-Corruption Guidelines, Procurement Guidelines, and Disbursement Guidelines.
- The lack of an agreement during project implementation between the DOSMEP and the IFC on administrative arrangements forced the cancellation of the second component of the project. The ICR (pages 10-11) explains that the DOSMEP was reluctant to adopt the IFC risk sharing facility model under which the facility would be administered by the IFC with only a limited role for the DOSMEP. This crucial aspect of the proposed facility should have been resolved at project preparation.

Risk Assessment and Mitigation Measures. The Bank carefully assessed the operational risks to the project and recommended adequate mitigation measures.

- The country's financial system faced substantial systemic risk arising from past aggressive credit growth, weak banking supervision framework, and limited enforcement of rules and regulations by the central bank. To mitigate the associated stakeholder risk to the project, the Bank would assist the Bank of the Lao PDR strengthen its institutional and technical capacity to monitor the financial sector.
- Some state-owned banks did not publish their financial statements and annual reports, making it difficult to assess the performance of any one commercial bank. To mitigate the project design risk, the project would set strict eligibility criteria for participating financial institutions and limit the participation in the project to no more than six of 31 commercial banks.
- The capacity of the DOSMEP to meet the Bank's environmental and social safeguards and procurement and financial management fiduciary standards was unknown. To mitigate the governance risk: the project would provide technical assistance to DOSMEP on environmental and social safeguards and on fiduciary standards; the National Implementation Unit at the MOIC would support the DOSMEP on the implementation of environmental and social safeguards, procurement, and financial management; and, the proposed risk sharing facility trust fund was to be administered by the International Finance Corporation on behalf of the government.

Quality-at-Entry Rating

Moderately Satisfactory

b. Quality of supervision

The Bank supervised the implementation of the project regularly. There were 11 implementation support missions and one mid-term review mission over the six and a half year life of the project. According to the ICR (page 26), each mission closely reviewed the project's performance and progress and identified problems and courses of action to take project implementation back on track. In addition to the formal supervision missions, the Bank supported the implementation of the project with bi-weekly consultations with the government during the early years of the project. The consultations were detailed and covered issues including the selection of participating financial institutions, the transfer of funds from the Ministry of Finance to the MOIC, the disbursement of sub-loan funds from participating final institutions to SMEs, and the progress of technical assistance activities.

As part of the implementation support, the Bank reviewed due diligence reports prepared by the DOSMEP on participating financial institutions and confirmed the eligibility of the financial institutions prior to their selection for the project. The Bank conducted workshops for the DOSMEP, the participating financial institutions, and SMEs on the Bank's environmental and social safeguards and procurement and financial management standards.

The Bank prepared 13 Implementation Status and Results Reports (ISRs) over the six and a half year duration of the project, or two ISRs a year, the average for Bank investment project financing operations. The ISRs were detailed and analytic, covering issues including the effect of the interest rate caps imposed by the central bank, the impact of the COVID-19 pandemic, and the implications of the country's macroeconomic performance and outlook on project implementation.

The Bank acted expeditiously to address problems identified during implementation supervision.

- The second project component was dropped at the first restructuring in 2016 after the IFC and the DOSMEP failed to agree on administrative arrangements for the risk sharing facility, and the financing for the facility was reallocated to the first project component.
- The National Implementation Unit at the MOIC was designated as the project executing agency and the DOSMEP as the project technical implementation agency at the first restructuring in 2016 to address early issues related to project coordination.
- The Project Implementation Manual was revised in 2018 to allow for a 50:50 ratio of investment to working capital in SME loans instead of the original 70:30 ratio in response to the early experience under the project and changed economic and financial conditions.

Although the Bank project team leader (TTL) changed thrice, the managerial turnover did not adversely affect the supervision of the project, according to the ICR (page 26), as the TTL was backed by an able country-based co-TTL. The Bank also had a strong in-country staff.

Quality of Supervision Rating
Satisfactory

Overall Bank Performance Rating
Moderately Satisfactory

9. M&E Design, Implementation, & Utilization

a. M&E Design
The Project Appraisal Document (pages 10-20) originally defined 9 output indicators and 4 outcome indicators for the objective to provide long-term funding sources for banks to provide long-term credit to small and medium enterprises. The indicators would be revised and reduced to 7 output and 3 outcome indicators after the cancellation of the second project component and other changes made during restructuring (see Section 9.b). The results indicators were well-defined, had credible baseline data and results targets, and had available sources of data.

The M&E plan called for the government to perform the M&E function for the first and third project components and the IFC for the second project component. For the government, the responsible body would be the Project Management Unit at the DOSMEP. The government and the IFC would prepare bi-annual Project Reports and submit them to the Bank within 45 days after the end of each reporting period. In addition, the government and would prepare and submit the project Mid-Term Report to the Bank within 24 months from the effectiveness date of the project.

b. M&E Implementation

Following the restructuring of the project, the Bank revised some results indicators to reflect the decisions made for the project components, the changed level of ambition of one technical assistance activity, and for more relevant measures of the results of technical assistance and training activities.

- The output and outcome indicators for the cancelled second project component – number of direct project beneficiaries and percentage of female beneficiaries for the risk sharing facility and outstanding SME loan portfolio for the risk sharing facility – were dropped.
- The target for the number of SMEs benefitting from technical assistance was raised from 80 (by end 2018) to 600 (by end 2020).
- The output indicator "formulation of SME census plan and methodology" was dropped. The output indicator "cross-ministerial and action-oriented SME Development Action Plan for 2021-2025 is developed" was added to measure the result of technical assistance activities directed at the DOSMEP.
- The outcome indicator "increase in sales by beneficiary SMEs" was dropped. The outcome indicator "increase in employment by beneficiary SMEs" was added.
- The outcome indicator "SME Development Master Plan, 2016-2020" was dropped. The outcome indicator "Percent of trained staff at the DOSMEP, participating financial institutions, and SMEs reporting medium- of intensive-use of lessons learned from capacity building measures."

The Project Management Unit at DOSMEP remained responsible for M&E before and after the restructuring which assigned overall project fiduciary responsibility to the Department of Planning and Cooperation at the MOIC and project technical responsibility to the DOSMEP.

The M&E plan was implemented as revised. The M&E quality was rated substantial in the last ISR (of December 2020).

c. M&E Utilization

According to the ICR (page 24), the M&E data were effectively used throughout project implementation. The M&E data were used by the Bank in the ISRs filed for the project, by the DOSMEP for its quarterly reports, and by the Bank and the government for the three project restructuring episodes.

Information from the Impact Assessment complemented the M&E data after the project closed.

M&E Quality Rating

Substantial

10. Other Issues

a. Safeguards

Environmental Safeguards. The project was classified as an environmental assessment category FI (Financial Intermediary) at appraisal and triggered environmental safeguard policies *OP 4.01 - Environmental Assessment*, *OP 4.04 - Natural Habitats*, and *OP 4.36 - Forests*. To address potential environmental risks, an Environmental and Social Management Framework (ESMF) would be developed to govern the environment and social screening, assessment, and mitigation of potential negative environmental impact of SME sub-projects and an Environmental and Social Management System (ESMS) would be established for financial institutions participating in the risk sharing facility. According to the ICR (page 25), the ESMF was included in the Project Implementation Manual and disclosed at the Bank's Infoshop. The DOSMEP, participating financial institutions, and SMEs were also trained on the Bank's environmental safeguards. The ICR (page 25) noted that "Weak enforcement and non-compliance of E&S standards and procedures were also evidenced at the local level. However, with training and support of the DOSMEP's and WB's E&S specialist to mitigate the short comings observed, both the PFIs and SMEs had a better understanding of the impacts of the M&E interventions in the approval of and implementation of sub-loans by the end of the project." Hence, overall, safeguards were ultimately rated satisfactory in the final ISR. The Environmental Assessment (OP 4.01), Natural Habitats (OP 4.04), and Forests (OP 4.36) safeguards were each rated satisfactory in the finale ISR. Compliance with overall environmental safeguard policies was satisfactory, according to the Bank project team's advice to IEG when asked for confirmation.

Social Safeguards. The project also triggered social safeguard policy *OP 4.10 - Indigenous Peoples.* To address potential social risks, an Ethnic Groups Planning Framework would be developed for the project. The DOSMEP, participating financial institutions, and SMEs were also trained on the Bank's social safeguards. The Indigenous Peoples (OP 4.10) safeguard was rated satisfactory in the last ISR. Compliance with overall social safeguard policies was satisfactory, according to the Bank project team's advice to IEG.

b. Fiduciary Compliance

Procurement. There were initial delays with procurement, owing largely to coordination problems between the DOSMEP and the National Implementation Unit at the MOIC. However, once the roles of the DOSMEP and the MOIC in the project were more clearly delineated (see Section 8.B), procurement activities progressed steadily. Procurement for two technical assistance activities remained the exception, nonetheless (see Section 2.E and Section 5). The National Implementation Unit at the MOIC exercised fiduciary responsibility over procurement, supported by a local procurement consultant and an international procurement advisor. Procurement was rated satisfactory in the final ISR.

Financial Management. There were no problems with financial management. The National Implementation Unit at the MOIC assumed responsibility over financial management. All required interim financial reports were submitted and on time. All audit reports were clean and did not have any qualifications. Financial Management was rated satisfactory in the last ISR.

c. Unintended impacts (Positive or Negative)

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d. Other

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11. Ratings

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

12. Lessons

Three lessons are drawn from the ICR (page 27-28), with some adaptation.

Lines of credit are not a panacea for all problems with SME finance and must be matched by interventions that address structural impediments to SME lending. In this operation, a fourth of the project funds was devoted to technical assistance to help address issues associated with information asymmetries and collateral requirements in SME lending. Technical assistance was delivered to participating financial institutions to improve their SME strategies, banking products, and credit underwriting practices. Technical assistance was also delivered to SMEs to develop their business development and financial management capacities and skills. Moreover, technical assistance was obtained from the IFC to help develop the country's credit information system and secured transactions business (where the lender acquires a security interest in collateral owned by the borrower). Altogether, these efforts should help increase the preparedness of financial institutions to lend to SMEs and improve their access to credit.

Drawdowns from a line of credit by financial institutions should be staged and linked to performance. Although subsidiary financing agreements between the DOSMEP and participating financial institutions allowed advances of up to US$2 million upon signing of the agreement, good practice showed that funds transferred in tranches and linked to results boosted performance by the participating financial institutions. In this project, participating financial institutions requested the DOSMEP for fund transfers, submitting a list of loans made with supporting documents including the original loan applications filed by the SME borrowers. Participating financial institutions that actually extended loans to SMEs for eligible sub-projects gained priority over the project funds.

Continuing policy dialogue with the monetary authorities and banking supervisors helps strengthen the enabling environment for SME lending. In this project, policy decisions by the Bank of the Lao PDR posed challenges to project implementation. In December 2015, the central bank capped local currency deposit rates and the spread between the local currency deposit and lending rates at an average 4 percent. In December 2017, the central bank capped the spread between foreign currency deposit and lending rates at 3 percent and limited loan fees to 3 percent of the approved loan amount. In February 2018, the central bank capped the interest rates in the interbank market on the Laotian kip, the Thai baht, and the US dollar for maturities of one-week to one-year. According to studies in 2019, the series of interest rate caps exerted pressure on the banks' return on assets and return on equity, distorted prices in the funding market, boosted re-dollarization, and motivated a shift to unregulated providers. Continuing policy dialogue by the Bank with the authorities and the private sector helped convince the central bank to remove the interest rate caps in 2019.

13. Assessment Recommended?

No

14. Comments on Quality of ICR

The ICR was prepared following OPCS guidelines.

The assessment of the efficacy of the project was evidence-based and candid. The ICR assessed the achievement of the output and outcome targets clearly. It also described well the cancellation of the second project component, namely the risk-sharing facility, which would have been vital to lowering collateral requirements on SME lending. The ICR also noted in adequate detail two technical assistance activities which started late and delayed the closing date for the project by 18 months. The central bank imposed caps on deposit-loan spreads which slowed down bank lending in general; the way this impacted the project was also clearly analyzed.

The quality of the analysis of various aspects of project performance was substantial, especially those factors affecting project implementation. The lessons drawn were evidence-based and would be generally useful to both the design and implementation of future SME finance operations.

a. Quality of ICR Rating
Substantial