



1. Project Data :			
OEDID:	C2250		
Project ID:	P010374		
Project Name :	Fourth Small and Medium Industries Project		
Country:	Sri Lanka		
Sector:	Other Finance		
L/C Number:	C2250		
Partners involved :	Asian Development Bank and Japanese JGF		
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Date Posted :	04/03/1998		

2. Project Objectives, Financing, Costs and Components :

This financial intermediation credit, for US\$45 million, was approved in FY91 and closed in FY98 with 1.6 percent of the original credit canceled. Objectives: deepen policy dialogue with GOSL on financial sector issues; support the GOSL to improve: Customs and Excise Duties, environmental protection, and SMI policies and institutions; and to provide credit, through the banking sector, for long -term capital investment by eligible enterprises. The ICR was prepared by the South Asia Region and includes a Borrower's assessment of the credit as an appendix.

3. Achievement of Relevant Objectives :

The project objectives were fully accomplished in important areas : the institutional development of the participating credit institutions, particularly in terms of their debt recovery practices, was improved; the credit supported SMI entrepreneurs in their subproject implementation; and the credit advanced in policy development in both the financial and trade sectors. The delay in disbursement of the credit occurred because the Credit's terms made two large state banks (SCBs) ineligible to participate in the program for a portion of the credit period . However, both institutions ultimately improved sufficiently to become eligible again . Nevertheless, even though they have improved, problems remain with both institutions. The project played a catalytic role in strengthening environmental regulatory policy, but the performance of the technical assistance programs was mixed : the modernization of the Customs and Excise Department was implemented satisfactorily, but little was done on the issues of the non -bank financial sector.

4. Significant Achievements :

The second tier lending institution that served as the credit's implementing agency was privatized during the project, and the strength and performance of the banking sector were significantly improved . Accessibility of credit is now not a problem in Sri Lanka, although high real interest rates are .

5. Significant Shortcomings :

Both the Bank and the GOSL underestimated the complexity and political difficulty of fundamental restructuring of the two large state-owned banks. Even though improvements have occurred, their performance still distorts and impedes the functioning of the financial sector . Bank research indicates that this slower than anticipated financial reform process is a frequent occurrence . Evidence indicates that financial reform is rarely accomplished over the course of one project . Hence, the follow up work proposed on broader financial sector issues, and proposed work on financial reform seems appropriate and well targeted. As the ICR shows, an additional shortcoming of the intermediation process used in the credit is the continued reliance on a government-run guarantee scheme that penalizes good performance by lenders .

6. Ratings :	ICR	OED Review	Reason for Disagreement /Comments
Outcome:	Satisfactory	Satisfactory	

Institutional Dev .:	Substantial	Substantial	
Sustainability :	Likely	Likely	
Bank Performance :	Satisfactory	Satisfactory	
Borrower Perf .:	Satisfactory	Satisfactory	
Quality of ICR :		Satisfactory	

7. Lessons of Broad Applicability :

The importance of seeking financial viability and strengthening the internal efficiency of participating credit institutions is difficult to exaggerate, and should be a component of credit lines such as this one .
Well-functioning financial institutions can effectively and productively distribute Bank credits in productive ways. However, it is important that such loans focus on the sources of imperfection which prevent lenders from carrying out effective intermediation in the first place . In addition, Bank research on the need for a long-term commitment for fundamental financial reform is supported by the experience of this credit .

8. Audit Recommended? ☐ Yes ☒ No

9. Comments on Quality of ICR :

The ICR is of satisfactory quality . It effectively summarizes an extensive amount of information on a complex, multi-faceted project in a lucid, coherent way .