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Private Sector Development: Recent Lessons from Independent Evaluation

WHAT WORKS

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The private sector is essential to successful development. It is the primary source of employment and the primary pathway out of poverty for those at the bottom of the pyramid.

Private sector activity drives most economic growth, and well-functioning markets can open opportunity and mobility to the poor. Effective financial markets and services can finance enterprises of all sizes, provide a safe harbor for savings, insure against catastrophic risk, and facilitate payments whether across towns or across the globe. Effective product markets can link farmers to global value chains and extend opportunities for entrepreneurship and innovation. The World Bank Group, through its three major bodies – The World Bank (IBRD/IDA), the International Finance Corporate and the Multilaterial Investment Guarantee Agency, views financial and private sector development as central to its developmental and antipoverty mission. A major part of its activities and financial portfolio are oriented toward supporting the creation or expansion of markets, market supporting institutions and policies and private sector participants, to empower the private sector in pursuit of the elimination of poverty and of boosting shared prosperity.

The Independent Evaluation Group (IEG) works at the project, sectoral, country and corporate level to appraise these efforts and capture the lessons that can improve future performance, so that the World Bank Group can more effectively pursue its twin goals. This report highlights some recent evaluations and learning products that provide significant insights and learning from World Bank Group private sector development projects.

This brochure summarizes key findings and recommendations of recent IEG evaluations of financial and private sector development work of the Bank Group from 2014 to 2016.

Growth and Competitiveness

Helping countries achieve the Bank Group's twin goals of eliminating extreme poverty and promoting shared prosperity through rapid and broad-based economic growth, centered on strong contributions from a competitive private sector through country, regional, and global efforts help boost the volume and value of trade, enhance the investment climate, improve competitiveness in sectors, and foster innovation and entrepreneurship.

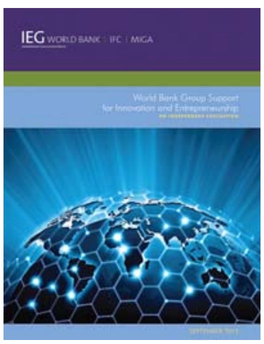
Finance and Markets

Creating the institutions and policies to finance development and enable intermediaries to channel resources to their most valuable use, and facilitating broad access to financial services to encourage inclusive growth.

Public-Private Partnerships

Providing upstream policy advice for regulatory and institutional reforms and downstream transaction support for public-private partnerships (PPPs) to extend the reach and quality of basic service provision, to enhance efficiency, access, sustainability, risk allocation and resource mobilization.

GROWTH AND COMPETITIVENESS



World Bank Group Support for Innovation and Entrepreneurship

IEG's 2013 evaluation of World Bank Group Support to Innovation and Entrepreneurship noted the critical role of innovation in economic growth and the substantial World Bank Group engagement in the area.

Although market and government failures and other bottlenecks impede innovation and entrepreneurship, developing countries need to build the capacity to find, absorb, and use new technologies and processes as well as foster entrepreneurs who can take risks, look for finance, and bring new products and processes to market. The evaluation states that "countries at different stages of development identified five common principles that can be useful in promoting innovation and entrepreneurship:

- Support public investment in research and development (R&D) that focuses on improving efficiency and relevance to end users as well as on strengthening the use of research results in public policy decisions;
- Build domestic science, technology, and innovation capabilities to make effective use of global knowledge;
- Strengthen linkages between public R&D and private sector users of technology and knowledge;
- Build a strong enabling environment, including effective use of information and communications technology; and
- Provide flexible financing arrangements to encourage innovative firms to develop new products, processes, and services."

The World Bank Group's portfolio contains interventions in these areas, and a number of client countries, especially upper middle-income countries like China, Chile, and Brazil have given high priority to innovation in their development plans, which then is reflected in countries strategies of the World Bank Group and its lending portfolio. The evaluation found that interventions may individually be successful, but they do not automatically foster synergies or an integrated system. Instead, it is essential to invest in fostering linkages between actors in the innovation system—and the Bank Group has done so. The examples given in the evaluation suggest that successful projects linked actors from various domains (research, private sector, service providers, government, development partners, and so on) and used a variety of mechanisms, including competitive grants and business incubators to foster the development of innovation and entrepreneurship. Being successful in adopting policies that stimulate private investments in innovation, and making public investment choices that further R&D will require the understanding of the dynamics among agents to make strategic choices about where and how to intervene.

Private Sector Development in Fragile and Conflict States

The private sector can drive economic growth and employment in fragile and conflict-affected states (FCS), but it faces specific challenges that hamper its development and add to the cost of doing business. Overcoming these challenges requires attention to private sector constraints and largely depends on the government's ability to provide a stable environment and vital services. Based on World Bank enterprise surveys and an analysis of country case studies, the top constraints include political instability, scarce electricity, corruption, and lack of access to finance, land, and transport.

A 2013 IEG evaluation, World Bank Group Assistance to Low-Income Fragile and Conflict-Affected States, concluded that World Bank Group support to FCS did not adequately address the main constraints to private sector-led growth and employment, and it did not sufficiently exploit potential linkages among interventions in different sectors. To enhance its effectiveness, the World Bank Group should develop a realistic framework for inclusive growth and jobs in FCS that ensures synergies and linkages across public and private sector interventions. For instance, investments in infrastructure and human capital development are areas with strong private sector development linkages. Although short term jobs programs can contribute to social cohesion, such gains are not usually sustained in the medium and long term. Interventions in FCS also require tailoring of assistance instruments and tools to the needs and conditions of the local economies and private sectors, characterized by a high prevalence of informal firms and low capacity.

As the private sector continues to exist even during periods of conflict, early engagement and support through all stages of post conflict reconstruction is important to create opportunities and livelihoods. This requires support through both public and private sector instruments. Support programs need to be sequenced to address immediate needs first, then shift to focus on income generating activities and microfinance, and finally on improving the term enabling environment. However, a focus on investment climate reforms was not sufficient to support inclusive growth and jobs in FCS. When fostering inclusive growth and jobs, there is no “one-size fits all” approach. Instead, assistance programs should be designed based on a thorough analysis of the underlying causes of conflict or fragility in each country as well as opportunities for growth and jobs. In this context, agriculture as the largest sector providing employment livelihoods in FCS, should receive special attention, as should certain dominant sectors, such as extractives industries. Given the low capacity environment in many low-income FCS both at the level of the private sector and government entities, delivery of assistance programs should include proactive and ongoing implementation support. Finally, migrant communities and remittances play a large role in many FCS and there is scope for interventions targeting these communities.

Investment Climate Reforms: An Independent Evaluation of World Bank Group Support to Reforms of Business Regulations

The ability of private firms to grow, create jobs, and reduce poverty depends critically on a well-functioning investment climate, defined as the policy, legal, and institutional arrangements underpinning the functioning of markets and the level of transaction costs and risks associated with starting, operating, and closing a business. The World Bank Group has been providing extensive support to investment climate reforms—having financed 819 projects with investment climate interventions in 119 countries for a total estimated value of $3.7 billion over the period FY07–13. This evaluation assessed the relevance, effectiveness, and social value of Bank Group interventions as it pursued inclusion and shared prosperity through support to investment climate reforms.

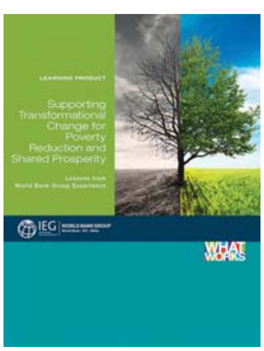
IEG found that the World Bank Group has supported a comprehensive menu of investment climate reforms. These reforms were generally supported in the right countries (those with worse initial conditions) and generally addressed the right areas of the regulatory environment (those most constraining businesses). The Bank Group's diagnostic tools were diverse, but their coverage was incomplete.

Analysis showed that, within the limits of the available measures of investment climate indicators, the Bank Group had been successful in improving the investment climate in client countries, as measured by the number of laws enacted, streamlining of processes and time, or simple cost savings for private firms. However, the impact on investments, jobs, business formation, and growth and the social value of regulatory reforms—that is, their implications for inclusion and shared prosperity as reflected in results—had not been properly included in the design of reforms and assessment of their impact. Instead, Bank Group support focused predominantly on reducing costs to businesses.

Simplicity of design and good risk assessment play a special role in achieving satisfactory outcomes. Political instability and lack of political commitment remain major problems, limiting the effectiveness of investment climate reforms.

In supporting investment climate reforms, the World Bank and IFC use two distinct but complementary business models. Although coordination and business unit integration within the World Bank Group on investment climate reforms was higher than other areas of work; coordination was mostly informal, relying mainly on personal contacts. IEG offered three main recommendations:

- Expand the coverage of current diagnostic tools and integrate them to produce comparable indicators.
- Develop a differentiated approach to identify the social effects of regulatory reforms.
- Ensure that the Bank Group takes advantage of the complementarity and strengths of the World Bank and IFC business models when designing the new Trade and Competitiveness Global Practice.



World Bank Group Support to Transformational Engagements: An IEG Learning Product

Transformational engagements are a critical pillar of the World Bank Group's strategy for achieving its twin goals of eliminating extreme poverty and boosting shared prosperity, as a means to scale up its development impact by helping its clients catalyze more fundamental or transformational changes. IEG reviewed evaluative evidence for a diverse group of Bank Group interventions to understand the mechanisms and conditions for transformational engagements and to distill lessons and implications. To apply this concept to Bank Group interventions, IEG defined transformational engagements as interventions or series of interventions that support deep, systemic, and sustainable change with the potential for large-scale impact in an area of a major development challenge. Such engagements help clients remove critical constraints to development, support fundamental change in a system, have large-scale impact at the national or global level, and are economically, financially and environmentally sustainable.

IEG found that these engagements were difficult to do, required sustained efforts over long periods, and were a small share of the Bank Group's portfolio. Among country level engagements selected for this review, transformational countries on average grew much faster than their comparator countries for the entire review period with faster and more sustained poverty reduction and social progress. IEG found that, while there is no single prescription for catalyzing transformational change, there are some mechanisms that increase its likelihood:

- Identifying and addressing the binding constraints to progress toward a development objective
- Adopting systemic tactics that address multiple constraints in interrelated parts, including through cross-sectoral approaches
- Scaling up and replicating effective approaches and innovations and of novel financing instruments
- Changing behaviors by modifying incentives of beneficiaries, introducing market forces, or increasing the flow of information.

IEG also identified distinguishing factors related to the enabling environment and to the design and implementation of interventions:

- Rigorous diagnosis and analytical work to underpin the design of interventions.

- Adapting interventions to local context, capabilities, and social norms.
- Early and broad engagement with stakeholders to forge consensus.
- A focus on building and strengthening local institutions.
- Striking a balance between a strategic understanding of key, systemic constraints and pursuing reforms through a set of sequenced and focused interventions, while limiting project complexity.
- Ongoing support to clients through continuing, sustained engagements and a series of interventions designed to facilitate deep reforms. This implies undertaking more selective, programmatic engagements.
- Using Bank Group staff with strong technical skills and, in some cases, an entrepreneurial attitude -- both critical to designing and implementing transformational engagements. However, the Bank Group's institutional incentives need to align with addressing the most binding constraints.
- Robust monitoring and reporting systems to ensure proper targeting of beneficiaries and to facilitate learning, as well as to inform adjustments to the project or program during implementation.

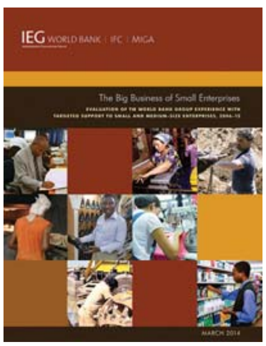
Interventions to foster transformational change carry a higher risk, but IEG's analysis shows that these are well compensated by the results that can be achieved.

Coming Soon

World Bank Group Support to Industrial Competitiveness and Its Implications for Jobs

Productivity, competitiveness, and more and better jobs are key to economic development and are at the top of government development agendas. Supporting industry competitiveness has been an important part of World Bank Group activities. IEG assessed the contribution of the World Bank Group's industry-specific support to helping improve productivity and competitiveness in developing countries, and the implications of that support for jobs. Industry competitiveness can be enhanced through several different approaches including those that are geared to the economy as a whole, those that are industry specific, or those that are a mix of both. The evaluation focuses on industry-specific support in four industries—agriculture, manufacturing, tourism, and information and communication technology. Employment is a central aspect of the productivity and competitiveness agenda. The evaluation illustrates the complex effects of productivity improvements on jobs and job quality.

Finance and Markets

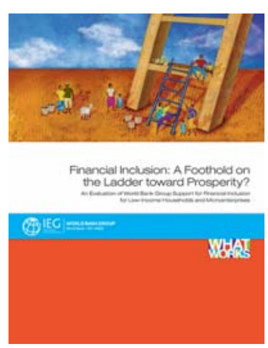


The Big Business of Small Enterprises: Evaluation of the World Bank Group Experience with Targeted Support to Small and Medium-Size Enterprises, 2006–12

IEG's evaluation The Big Business of Small Enterprises observed that the World Bank Group promotes the growth of small- and medium-sized enterprises (SMEs) through both systemic and targeted interventions. A critical challenge is to root the many activities now undertaken in this broad space in a clear understanding of the characteristics and dynamics of SMEs, their role in the broader economy, and their actual and potential contribution to jobs, growth, and shared prosperity. A closely related challenge is to formulate clear strategies that connect interventions to intended outcomes and that are accompanied by solid measurement systems that provide evidence of results and allow learning.

Targeting means focusing benefits on one size class of firms to the exclusion of others. Targeted support for SMEs is a big business for the World Bank Group, averaging around $3 billion a year in commitments, expenditures, and gross exposure over the 2006–12 period. In the context of broader reforms, targeted SME support can be a powerful tool and, given the size of the recent program, it is vital for the World Bank Group to use it effectively. Targeting SMEs is not an end in itself, but a means to create economies that can employ more people and create more opportunity for citizens to achieve prosperity. A thriving and growing SME sector is associated with rapidly growing economies.

As the World Bank Group continues to support SMEs, to help them realize their potential contribution to developing economies, the IEG evaluation concludes that, to make targeted SME support more effective, the Bank Group needs to do several things. Targeted support for SMEs needs to be firmly rooted in a clear, evidence-based understanding of how the proposed support will sustainably remove the problems that constrain SMEs' ability to contribute to employment, growth, and economic opportunity. This requires a tailored research agenda to support and assist these clarifications and refinements of its SME support approach, using the best qualified researchers. Likewise, interventions that make it their objective to assist SMEs should be designed in ways that they define and justify the specification of the beneficiary group, provide specific targeting mechanisms, and include impact indicators in their results and monitoring and evaluation frameworks. Finally, the Multilateral Investment Guaranty Agency's (MIGA) Small Investment Program should undergo a radical change in approach to providing guarantees for investments in SMEs, considering either a merger with its regular program or a fundamental redesign to improve performance.



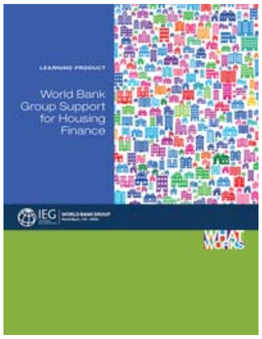
Financial Inclusion - A Foothold on the Ladder toward Prosperity?

Access to financial services has long been believed to lift people out of poverty by allowing them to seize economic opportunities. Strong progress has been made in the last three years: the number of people reached by formal financial services increased by 700 million. Yet, a substantial credit gap remains, and 2 billion adults do not have access to formal financial services. IEG's evaluation, Financial Inclusion: A Foothold on the Ladder toward Prosperity?, seeks to inform both the short-term drive and longer-term activities concerned with connecting the poor to financial services that improve their well-being.

The evaluation found that:

- The World Bank Group contributed significantly to progress in financial inclusion. It has reached a significant share of the microfinance industry and helped make it more sustainable. Yet it is unclear how much of this support reaches actual microenterprises and the poor—as opposed to substantially larger businesses, including SMEs
- World Bank Group support to create policy frameworks that allow financial intermediaries to better serve the needs of the poor was effective. Yet its approach to identifying and tackling constraints to financial inclusion is neither systematic nor comprehensive—of particular concern are areas that affect the poor, like mobile banking or rural savings and credit cooperatives.
- Through its global partnerships, the Bank Group has been able to substantially increase its impact in advancing financial inclusion; however, partnerships also carry some risks and costs.

Most importantly, the World Bank Group's strategy on financial inclusion can be strengthened. The Bank Group's public commitment to universal financial access (UFA) by 2020 is likely to yield a push for transaction accounts. However, high dormancy rates of newly opened accounts raise doubts about whether providing access through such accounts results in universal inclusion. Instead of focusing on "headline numbers," the relevant goal may be to provide service to everyone with a productive and beneficial use. Finally, IEG's findings point to a need for a more sequenced and evidenced approach as evidence has been growing showing that financial inclusion has been less effective in fighting poverty than was previously hoped.



World Bank Group Support to Housing Finance Hundreds of millions of people live in inadequate conditions with little or no access to decent housing. Housing finance is critical to the functioning of the housing market. Creating sustainable and effective housing finance requires the mobilization of longer-term sources of funding for both rental and owner-occupied housing, which is often missing in emerging markets. In response, the Bank Group's approach has evolved over time from the use of traditional stand-alone operations, to the development of more strategic and comprehensive solutions including both supply side (such as reducing legal and regulatory constraints) and demand side (such as provision of guarantees and financing) interventions.

This learning product aimed to provide lessons from experience about successful practices related to World Bank Group housing finance projects, primarily from evaluated World Bank loans or IFC investments and advisory services, including a total of 55 projects. Analysis shows that the Bank Group allocates resources primarily to countries with low mortgage penetration rates that are in the most need. Despite its important role, the Bank Group has only limited resources requiring a strategic allocation and the gap in coverage of countries with low access to housing finance continues to be wide Additionally, the dedicated staff and resources it deploys have both fallen below the pre-2008 financial crisis levels, creating challenges to achieve more with less.

Summary of Findings

- If commercial banks are willing to provide mortgage loans they are logical partners in housing finance projects but they need to be fully committed to mortgage lending.
- Non-Bank Financial Institutions have strategic weaknesses that endanger their long-term viability. They might need to diversify funding sources, expand, or convert themselves into a bank.

- Sustainability can be enhanced when there is a strong link with advisory services, but it has to be adequately timed.
- There are certain preconditions for the development of capital markets and primary market interventions. When these are not in place, adequate sequencing, timely interventions, and committed sponsors can have compensating effects.

A needs assessment is fundamental to design interventions tailored to specific country requirements. If expanding affordable housing is a key objective of an intervention, it needs to be targeted and the results adequately measured.

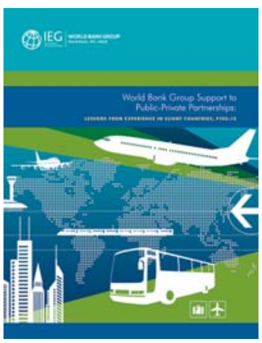
If there is no mortgage financing, the low-income segment should not come first, but rather be introduced gradually.

Coming Soon

Evaluation of the World Bank Group's Support for Capital Market Development

Well-functioning capital markets help channel capital towards areas that are essential for development and poverty reduction. Capital markets, for the buying and selling of long-term security instruments, enable issuers of securities (e.g. governments and businesses) and investors (such as insurance and pension funds) to trade such instruments within a particular market infrastructure of regulations, institutions and norms. Bank Group support encompassed interventions that spanned virtually all these areas of capital market development, that is, issuers, investors and market infrastructure. The forthcoming evaluation covers World Bank and IFC support for all capital market segments, and the Bank Group's role supporting development of the issuance and investor sides as well as of market infrastructure.

Public-Private Partnerships



World Bank Group Support to Public Private Partnerships—Lessons from Experience in Client Countries FY02-12

Public-private partnerships (PPPs) are now used in more than 134 developing countries, contributing about 15 to 20 percent of total infrastructure investment. Nonetheless, most developing countries and the World Bank Group itself—continue to see significant potential and need for expanded use of PPPs to help build infrastructure for growth. Designing, structuring, and implementing PPPs remains a challenging and complex endeavor. Their success depends on the enabling environment in which they are embedded. The World Bank Group has supported countries to create an enabling environment for PPPs along with structuring advice and finance. This evaluation finds that:

- The World Bank's upstream policy reform and institution building reaches the right countries. Most of this work aims at sector reform, which, however, failed in almost half of the cases because of the complexity and political implications of the reform processes. Advice on how to manage fiscal implications from PPPs is rarely given.
- The World Bank Group has made a significant contribution to capacity building for PPPs, but a lack of local skills and resources for the preparation of a PPP pipeline and bankable PPP projects poses a serious limitation across most World Bank-supported countries.
- IFC Advisory Services have achieved important impacts in advising on PPP structuring, despite the fact that only about half of the projects result in the award of a contract, mostly because of volatile government commitment.
- IFC also added value when investing in PPPs during due diligence and implementation, but a higher share of its portfolio could be located in markets with less developed PPP frameworks.
- The Multilateral Investment Guarantee Agency (MIGA) increased investors' confidence and effectively implemented PPPs in those countries that are about to develop PPP frameworks.
- PPPs supported by the Bank Group are largely successful in achieving their development outcomes, but data are scarce on the effects on the poor.
- The three Bank Group institutions deploy their respective comparative advantages well, but their approach should be more strategic and better tailored to countries.

Recommendations

- Translate the World Bank Group's strategic PPP intentions into an operational framework.
- Better assist governments in (i) making strategic decisions with regard to the level and nature of private sector participation and (ii) assessing fiscal implications.
- Identify avenues to increase IFC investments in PPPs located in countries and markets that do not yet have a well-developed enabling environment.
- Ensure broad stakeholder consultation and government commitment in IFC's advisory work.
- Provide authoritative guidance to staff on how to handle unsolicited PPP proposals.

- Define principles for the monitoring of PPPs over the long run to capture all vital performance aspects of PPPs, including—where relevant—user aspects.

Coming Soon

Public-Private Partnerships in Health: World Bank Group Engagement in Health PPPs: An IEG Synthesis Report

Governments from both developed and developing countries are increasingly looking at PPPs as a way to expand access to higher quality health services by leveraging capital, managerial capacity, and know-how from the private sector. From FY04 to FY15, the Bank Group approved 78 projects that provided support for health-related PPP operations, of which 53 were IFC projects (49 of these are advisory projects and four are IFC investments) and 25 World Bank lending projects. However, PPPs involve complex contracting which is likely to generate a distinctive set of challenges in developing country settings. This review provides insights into the Bank Group's work of applying PPP arrangements in the health sector, to distill knowledge with regard to what works (and what does not), review the quality of work in structuring PPP arrangements, and identify lessons to be learned from successful and failed efforts to structure health PPPs approved during FY04-16. The approach is based on a desk-based portfolio review of Bank Group projects.

Key Insights

Although the Bank Group supported countries that need its support the most, IEG found weaknesses in sequencing, completeness of advice, monitoring and evaluation, and aftercare.

IEG offered five lessons:

- When advising governments on the various models for providing health services, both IFC and the World Bank should act as one Bank Group and discuss the whole span of options ranging from the public and mixed options to the various types of potential health PPPs, taking account of the sector reform context of a country and its overall maturity and track record in using PPPs.
- To be better positioned to deliver such strategic advice, the Bank Group should better integrate its sector reform and policy work on the structuring and financing of PPPs.
- Pro-poor access and affordability need not only be systematically considered at the design stage; they should also be tracked to ensure that the poor actually benefit from PPPs.
- The PPP Fiscal Risk Assessment Model (PFRAM) tool, jointly developed by the Bank Group and the IMF to assess fiscal implications, should be systematically applied to the structuring of PPPs with substantial fiscal implications.
- Given the long contractual life of PPPs, the new practice of preparing post-completion reports after the PPPs have gone into operation should be mainstreamed so that these reports can be prepared at an appropriate time.

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