5. Emerging Messages and Recommendations

Overall, the outcome of the Bank Group assistance to Brazil was moderately satisfactory, although with some important synergies and variability across pillars. For example, the multisectoral SWAp model generated synergies across pillars and made significant contributions to the development of the Program-for-Results lending instrument—one of the Bank’s key corporate-level efforts to improve its operational effectiveness. As for variability across pillars, assistance for equitable Brazil was judged satisfactory, while assistance on competitiveness was judged less than satisfactory. Outcomes also varied within pillars, which provides valuable information from which to draw lessons and recommendations (see Appendix I for the summary assessment by pillars).

One question that emerges regarding the overall strategy was whether the use of a few very large operations (metro and urban rail projects and the sustainable economic management DPL totaling $3 billion) with high opportunity cost relative to the IBRD exposure limit was appropriate. The metro and urban rail projects had clear benefits, but alternative sources of financing might have been available; the SEM DPL was not the proper instrument, given the objectives at hand.

Emerging Messages

The Bank Group had significant impact in Brazil when it served as a trusted partner to think through evolving policy issues that Brazilian counterparts were tackling. In its support for Bolsa Familia, improving learning outcomes in education, pension reforms, and reducing the pace of deforestation, the Bank provided timely analytical inputs and technical assistance to address urgent needs. In Minas Gerais, the Bank worked with the state government to operationalize the results management system. IFC’s advisory support for structuring PPP projects in partnership with BNDES effectively delivered global expertise in project financing. The sharing of specific global experiences relevant to Brazil was particularly valued by the Brazilian authorities as a unique contribution of the Bank Group.

The Bank Group has also made important contributions by creating a platform where diverse stakeholders can examine issues that cut across organizational and sectoral boundaries. This is particularly important when facing trade-offs that involve collective action and resolution. The Bank was instrumental in convening various stakeholders to discuss a standardized approach to water resource management at the federal and regional level. Arguably the largest contribution of
the successful series of multisector SWAps in Ceará was the regular intersectoral meetings to discuss expenditure priorities, monitor progress of activities in various parts of the government, creating synergies, and raising awareness of dependencies among sectoral departments.

Typically these interventions generated long-lasting benefits as their effects evolved and matured beyond the lifetime of the intervention. The benefits can also be replicated across states and municipalities. Assistance to *Bolsa Familia*, pension reforms, and water systems had long-term and countrywide impact, and multisectoral SWAps had important effects at the state level. The pilot work on classroom dynamics, though taking place in a few localities, may over time generate critical knowledge of high relevance at the national level.

**Subnational Focus**

The focus on subnational clients will continue, given the strong demand for Bank financial and knowledge support among states and municipalities, limited needs for financing at the federal level, and the federal authorities’ strong support for subnational lending by the Bank. During the period evaluated, the Bank supported the priorities defined in the dialogue involving the highest level of the subnational authorities—in some cases those priorities emerged through a longstanding relationship that spanned many years, as in Ceará. The Bank coordinated with the federal authorities to ensure that its support was consistent with the framework governing the relationship between the federal and subnational governments, most importantly the Fiscal Responsibility Law. Based on these considerations, as well as the assessments of the commitment for and capacity to implement the agreed activity, the Bank developed its subnational portfolio.

This shift to subnational support has been a success for the Bank. It enabled the Bank to provide customized support to a wide variety of state and municipality challenges. It also helped the Bank remain relevant in Brazil by establishing a mechanism to respond to strong demand for Bank financing and knowledge among subnational governments. The Bank and IFC, with support from the federal authorities, have also been working to direct their operational focus on the north and northeast regions during this period. Progress has been made, although the largest share of Bank lending commitments went to the richer southeast region because of the size of the economies there and sustained dialogue with the Bank over years. The constraint in institutional capacity is particularly relevant in these regions. For IFC, identifying the right investment opportunities was challenging during the period evaluated.
The continuing focus on subnational clients may require identifying specific measures to encourage replication. Eventually, the accumulation of subnational experience may be able to influence countrywide development. The Bank Group has successfully induced such a catalytic process, but the strategy can be further refined. In particular, the Bank Group has yet to identify specific vehicles to facilitate and encourage the replication of positive results achieved in one subnational entity to others.

**COMPETITIVENESS**

There are also several areas with significant potential for catalytic impact but where the Bank Group has not been particularly effective. Most of these areas are in the competitiveness pillar: addressing bottlenecks in infrastructure, particularly in logistics, and the cost of doing business—areas that represent a major constraint to growth and an increasing preoccupation of the authorities. Several Bank documents have also identified a weak environment for competition as a major challenge.

Given the already high tax burden and competing demands for public spending, an improved public investment process and a modern regulatory framework that provides incentives for private sector investment in infrastructure are priorities for Brazil. Although the Bank Group has achieved some success through IFC support for structuring PPP projects in collaboration with BNDES and in selected state DPL and SWAp operations, significant challenges remain. The Bank and IFC have accumulated experience in different aspects of private participation in infrastructure investment; opportunities for synergies through knowledge exchange may exist in this area. Apart from a few successful cases in the water sector, very little else was done to explore this possibility during the period evaluated. Demonstrating the value of Bank Group collaboration in Brazil remains a challenge for the future.

The country strategies and a body of literature on Brazil’s economic growth also recognize the need to address the high cost of doing business. Although some analytical efforts and advisory services have been made, for example, in documenting the variability of this cost across states, the Bank Group has been unable to make a noticeable difference. Similarly, the importance of keeping an open trade regime and its impact on the competitive environment has been raised in the country strategies. So far, little analytical work has been done to document the extent of import protection (and its variance) in Brazil. A common thread in these areas seems to be a limited interest on the side of the counterparts to involve the Bank Group in a collaborative effort.

A challenge for the Brazil country strategy is to maintain flexibility in responding to evolving client demand while ensuring a level of specificity that makes it a
meaningful guide for operations. Achieving flexibility by defining very wide objectives over many areas—a “just-in-case approach,” in which the Bank Group puts on the table all development issues—could serve both the Brazilian authorities and the Bank Group well in a rapidly changing environment. However, an excessively flexible framework could result in pursuing only the outcomes that receive traction from the main counterpart, leaving out other areas even if their importance for overall development is recognized. (Appendix J identifies some instances where CAS outcome indicators were modified midway in the progress report without a clear justification for the changes.) It also risks weakening the Bank Group’s credibility because it could be perceived to have too many institutional objectives and to need better understanding of country challenges. The challenge is to find a balance between flexibility and a strategic vision based on realistic assumptions. For this, a strong and candid consultation with the authorities during the CAS design process is critical.

The country strategies examined in this evaluation included numerous objectives that covered a very wide range of development issues in Brazil. These objectives were often set high in the results chain, far removed from the Bank Group points of intervention. Setting high-level objectives clarifies the strategic direction of the program and helps align individual efforts toward results that can only be achieved through leveraging the linkages between interventions. However, achieving those objectives depends on many factors outside the control of the Bank Group; hence, specifying how Bank Group activities could lead to the intended outcomes requires strong assumptions about catalytic effects and external factors. This is particularly relevant when the size of Bank Group operations is small relative to the size of the economy, as in Brazil. The critical issue with the absence of a clear results chain is that it hampers ex post evaluation and thus learning from experience.

Self-evaluation has the potential to provide useful learning, but significant variability exists in the analyses presented in the CASCRs reviewed for this evaluation. The CASCRs of the FY00-03 and FY04-08 periods are candid in recognizing both successes and shortcomings, providing critical perspectives of program results. In the FY08-11 CASCR, there is less elaboration of problems encountered. Increasing candor in self-evaluation is important for learning from experience.

MIDDLE-INCOME COUNTRIES

Some of the findings of this evaluation may be relevant to the Bank Group work in middle-income countries generally. Many middle-income countries have good access to the international financial markets and well-established fiscal or quasifiscal tools to finance their development activities. They also have advanced institutions
and a high level of human capital. In these countries, Bank Group financial contributions are marginal and its knowledge services add value only when they bring perspectives that are not available in the country. The Bank Group is mostly a catalyst that triggers replication and synergies to generate impacts larger than a single intervention. From the experience in Brazil, the IBRD and IFC have a comparative advantage in sharing lessons from cross-country experiences in areas of interest to the authorities.

Focusing on geographical areas that are less developed would also be relevant. Many middle-income countries have significant regional differences in the level of poverty and strength of institutions. The need for financial and technical assistance is greatest in the areas that are falling behind in various aspects of development. The value of Bank Group support that embodies practical know-how would be high, although the challenges in achieving results would also be greater than in well-off regions.

The “just-in-case” approach noted earlier epitomizes a challenge in working with middle-income countries. Country programs need to combine the flexibility that allows for responding to demands as they emerge and the medium-term strategy that encompasses issues with limited traction from the client in the short-term. This is a difficult balance, but it can be struck through strong, candid dialogue with the relevant authorities as well as candor in self-evaluation.

The nature of engagement also depends on the administrative links between the local and central government. Hence, the lessons in Brazil need to be interpreted in a particular context of countries with a federal system. For Bank Group engagement in federal states, the experience with multisectoral operations—SWAps and DPLs—at the subnational level can be particularly relevant. These operations can contribute to intersectoral dialogue and help resolve trade-offs of a cross-sectoral nature through involving the highest authorities at the regional level and fostering subnational government ownership. Strong institutional capacity for coordination and results monitoring is essential for success in these operations—requirements often fulfilled in advanced middle-income countries. In Brazil, the Fiscal Responsibility Law provided an effective incentive framework for reform.

Finally, middle-income countries have more access to international capital flows, but the flip side is that they can also face unexpected reversal in such flows. It would be prudent for the Bank Group to maintain some lending space to respond to unanticipated shocks, particularly to support the sectors and population groups that are most vulnerable to those shocks.
Recommendations

These issues are particularly relevant as the demand for Bank Group operations remains strong, particularly with regard to subnational entities. A single borrower limit for Bank lending may also become binding in the near future. Cautious management of Brazil’s exposure level would suggest keeping some room to maneuver in case domestic or external shocks call for a rapid countercyclical increase in Bank lending. Thus, leveraging results from lending is more important than ever. The crucial criteria for lending should be interventions that are highly catalytic per dollar loaned. Priorities should be based on their externalities, knowledge sharing, and prospects for demonstration effects and replicability. Synergies among lending, AAA, technical assistance, and Bank Group–wide collaborations need to be explored and maximized. Proliferation of activities should be avoided. The need for leveraging is further pronounced for IFC and MIGA, given the smaller size of their portfolios in Brazil.

The Bank Group program should focus on areas where it has comparative advantage—mainly its ability to examine and discuss issues and trade-offs across sectors and themes. The Bank Group has also been effective in facilitating the dialogue among stakeholders to discuss trade-offs and identify solutions. Hence, areas where there are an important element of public good and calls for collective action are particularly suitable. Given the size of Brazil, these activities are more manageable in the context of assisting subnational governments—a point recognized by both the authorities and the Bank.

There are also activities that fit the above criteria less than others. For the Bank, very large projects relative to total exposure, producing services with an important element of cost recovery, and sponsored by agencies or states that are perceived as creditworthy are less obvious activities to finance. Sometimes the Bank’s financial involvement brings it knowledge sharing and technical assistance activities, which would lead to broad-based institutional strengthening. In such a case, the financing and knowledge component could be unbundled—with the Bank focusing mostly on the latter.

The Bank estimates that Brazil’s GDP grew by 0.9 percent in 2012, and its latest forecast for growth in 2013 is 2.9 percent (World Bank 2013b)—both numbers substantially below the average growth rate of 4.25 percent achieved between 2004 and 2011. As Brazil faces the possibility of lower growth and less favorable global economic conditions, the importance of ensuring the effectiveness of Bank Group operations is growing. Moreover, increased quality of public services and expenditures will remain priorities in coming years. For the Bank Group to remain a
valuable partner in addressing these challenges, this evaluation makes the following recommendations.

1. **Use the potential for wider catalytic effects as one of the main criteria for selecting the sectors and subnational entities with which to engage.** In selecting programs and projects to support in future strategies, the Bank Group should focus on areas where it has comparative advantage and can expect to generate benefits beyond the individual intervention. To identify the combination of Bank Group instruments that can enhance catalytic effects, the results chain must be identified that links individual interventions and objectives, and the intermediate goals need to be specified. This could also help avoid proliferation of objectives and increase selectivity.

Within the FY12–15 CPS, several areas seem to fit these criteria. For example, the continued emphasis on northeast Brazil provides operational focus. Of particular importance is assisting the efforts to develop the capacity to screen, select, and appraise public sector projects, reduce *Custo Brasil*, and strengthen the institutional and regulatory framework for PPP, particularly in infrastructure. Many of these interventions could have a subnational focus that could be followed up with efforts to encourage replication.

The Bank has developed a comparative advantage in several areas that are also of interest to the Brazilian authorities. Assistance in the design and implementation of *Brasil sem Miseria* and further strengthening *Bolsa Familia*—particularly in monitoring and impact evaluation—is a case in point. Potential for catalytic effects could be high in supporting pilot projects in ECD and disseminating the knowledge developed about how classroom dynamics influence students’ learning outcomes.

One of the most important contributions of the Bank program was the development of a multisectoral model, as most successfully demonstrated in Ceará and Minas Gerais. Even when operations are not multisectoral by design, the Bank’s convening role has proved effective where aspects of multiple sectors intersect, for example, in water resource management. Given the promising results, the Bank should continue pursuing opportunities for such an engagement, incorporating lessons from experience. Some of these lessons are that coordination across sector departments within the government is crucial for success and that the capacity of the counterpart authorities to promote collaboration across sectoral boundaries is key. In addition, the success in multisectoral operations depends much on the degree of ownership of the program by these authorities. More important, the activities that cut across sectors sometimes involve difficult trade-offs and political decisions; thus, involvement of the leadership at the highest level is important.
Given the strong demand for Bank Group support in states and municipalities, the Brazil country program will continue to focus on supporting subnational clients. To further enhance the leverage and catalytic effect of subnational operations, the Bank Group should identify ways to encourage the replication and demonstration effects of positive results achieved in one subnational entity or regions in others.

2. Enhance lending and nonlending support for improvement in the quality of public investment and the enabling environment for private sector investment. This could be done through a combination of financial support as well as knowledge and advisory services. Because the room for expansion in public spending is limited, it is important to continue undertaking various analytical work to identify the constraints to private participation in infrastructure investments and reduce the cost of doing business. Equally important would be new avenues through which the Bank could work with the federal and subnational governments to strengthen their capacity for public investment planning and project selection.

Given that both the IBRD and IFC have accumulated knowledge on private participation in infrastructure, this is an area where synergies from Bank Group collaboration can be usefully explored. For example, IBRD could help improve regulatory frameworks at the state and federal level, with IFC inputs based on its experience in structuring specific projects, which could then be followed up by an expansion of PPP transactions with IFC support. If necessary, this could be done by focusing on states that are particularly interested in attracting private investment—ideally to be replicated later in other states. The ongoing and future analytical work on private participation in infrastructure investments could provide impetus to this work. Similarly, IFC’s diagnostic work and advisory services on business environment could provide inputs into the Bank’s work on ways to address the cost of doing business. MIGA could also offer guarantees that would facilitate private sector participation in infrastructure investments. For that, MIGA needs to strengthen its business development capacity.

3. Continue to promote sustainable rural development, taking advantage of the opportunities presented by the new Forest Code. Brazil’s recently adopted Forest Code provides a new framework for strengthening the harmonization of conservation, development, and poverty reduction. Brazil will face economic and institutional challenges in implementing the Code’s provisions. These include completing a universal rural environmental cadaster in the near term and finding productive, cost-effective, and environmentally beneficial ways for private landholders to comply with forest reserve obligations under the Code. Building on past and ongoing work, the Bank and IFC should be prepared to offer technical and financial assistance, as required, to help meet the challenges of implementing the
new Forest Code in a way that is cost-effective, poverty-reducing, and environmentally sound.

4. Enhance dialogue with authorities and think tanks to identify policy issues where the Bank Group could provide timely knowledge and advisory support. Knowledge activities are areas where the Bank Group can have important positive externalities and catalytic effects per dollar loaned and per dollar of Bank budget resources. The Bank’s managerial focus, staff incentives, and internal resource allocation need to ensure sufficient budgetary resource allocation to enable high-quality knowledge activities with potential for catalytic impact.

This, however, should not mean undermining the role of lending. Experience shows that value often comes from a combination of lending and knowledge support: several counterpart officials have pointed to the significance of learning that takes place during project implementation. The Bank Group was effective when it sustained close interactions during implementation, as in the case of its support for Bolsa Familia and multisectoral programs in Ceará and Minas Gerais. IFC’s advisory support for PPP project structuring is also associated with providing “how-to” advice on during implementation. The effort is rather in search of an optimal mix of lending and knowledge support, acknowledging that the emphasis on knowledge may have to intensify, given the constraints in lending.

The findings of this evaluation show that the Bank Group can provide unique perspectives on issues that the authorities need to tackle in the short run, particularly if provided in a timely basis. The ability to engage and have a candid dialogue at both the federal and subnational levels will be important for identifying the issues of immediate interest for the relevant authorities. Strengthening of regular dialogue with various think tanks, such as the Institute of Applied Economic Research, would likely bring in further insights in this respect.

5. Continue analytical work on selected topics with important long-term implications, even though traction with the authorities may be limited in the short term. The focus on issues that have short-term value should be balanced with continued work on issues of significance to Brazil over the medium term. This would help avoid the risk of adopting an excessively flexible strategy that could result in pursuing only the outcomes that receive strong traction from the main counterparts, leaving out areas recognized as important for overall long-term development. The authorities may consider the longer-term matters less urgent either because they are not needed for inputs to policymaking or because they involve difficult political trade-offs. Even so, the Bank Group would be advised to continuously undertake some minimum analytical work in these areas to balance...
the flexibility in operational response with the stability in the strategic directions of
the program.

In this evaluation, several such issues have been identified, particularly in
competitiveness, where sustained analytical efforts are especially relevant. For
example, a review of Brazil’s experiences with concessions in different sectors to
extract lessons would benefit the Bank and IFC support to PPPs. An assessment of
institutional and regulatory constraints affecting public agencies in the planning,
selection, and execution of public sector investment projects could help improve the
quality of public investments. Analyses of the experience with direct credit and the
implications of the open trade regime could shed light on medium-term efforts to
enhance competitive environment.

In this context, continued strengthening of networks with Brazilian think tanks and
institutions would be beneficial. It would also be useful to broaden knowledge
exchange among development partners in Brazil, given that the need to seek
catalytic effects is common across these organizations. It would also allow the Bank
Group to keep updated on critical long-term development issues, balancing the
operational focus on practical policy applications in the short term.

6a. Expand IFC’s work on PPPs. IFC has added significant value in its support for
PPP project structuring, and demand remains high for innovative projects that can
be replicated and scaled up elsewhere in Brazil. Thus, the PPP collaboration with
BNDES could be expanded further. The expansion of PPP projects in Brazil depends
critically on the enabling regulatory environment and its predictability. This link
provides an area for close collaboration between the IFC and the Bank as noted
earlier.

IFC should also pursue further expansion of direct investment in infrastructure
projects and project sponsors. IFC’s direct investments in infrastructure and public
service delivery have the potential to transfer nonrecourse and limited-recourse
project financing as well as its environment and social standards—the skill that is
highly needed in Brazil to broaden private participation in infrastructure
investment. As its work in the water sector has shown, involving Bank sector experts
for technical advice, particularly in areas where IFC is entering with limited past
experience, would be useful.

6b. Enhance the design and targeting of IFC’s activities to expand SMEs’ access to
long-term financing. IFC has pursued its strategic objective of supporting SMEs
through financial intermediation via second-tier banks. To make this program more
effective, IEG suggests several courses of action. First, the high levels of short-term
trade finance guarantees triggered by the global financial crisis in 2008–09 should now be rebalanced by shifting the emphasis toward the expansion of long-term loan and equity financing, where the SMEs face a strong constraint. Second, the present definition of sub-borrowers includes enterprises that are far larger than those typically considered as SMEs. This needs to be modified to increase precision in targeting SMEs.