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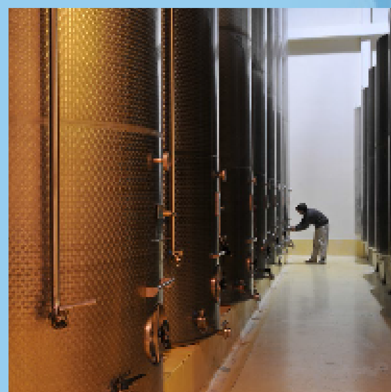

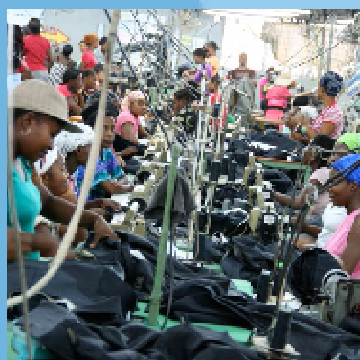

Sector and Thematic Evaluation

How is the IDB Serving Higher-Middle-Income Countries?

Borrowers' Perspective

IDB
Inter-American Development Bank
February 2013

Abstract

Growing income levels, strengthened macroeconomic performance, and increased stability over the past decade have allowed some countries in Latin America and the Caribbean to weather the recent economic crisis and reach investment grade status, thereby expanding their financing opportunities. This changing financial landscape, compounding by substantial variation in institutional effectiveness, and changing development needs associated with rising incomes present new challenges to the IDB as a development finance partner. IDB modes of engagement with an increasingly heterogeneous region will need to be increasingly sensitive and well-tailored to the needs of various country groups.

This evaluation assesses how well IDB's current mode of engagement meets the needs and expectations of countries that have relatively higher income levels and increasing access to diverse funding sources. These countries account for most of IDB's lending portfolio, and IDB must understand their needs and demands if it wants to ensure that its business model, financial instruments, and knowledge products serve them effectively.

For the purpose of this evaluation OVE selected 10 countries as case study countries using three objective indicators: (a) income level, (b) level of access to international financial markets, and (c) the weight of the country in IDB's lending portfolio. The countries, labeled higher middle income countries (HMICs) in this evaluation, are Argentina, Brazil, Chile, Colombia, Mexico, Panama, Peru, Trinidad and Tobago, Uruguay, and Venezuela.

The evaluation finds that IDB remains a valued and trusted development partner in the vast majority of the HMIC case study countries. It is still financially competitive, even in countries with investment-grade sovereign risk ratings, and is particularly so during times of international turbulence. IDB's counterparts particularly value the following aspects of their cooperation with the Bank: the discipline IDB helps impart to project design and execution, along with capacity building related to project management; the opportunity that IDB provides to learn from other experiences in the Region; the seal of approval that IDB's project financing can help provide through its social, environmental, and fiduciary safeguards; and IDB's ability to facilitate medium- to long-term project continuity across political cycles.

However, the evaluation also finds that several aspects require further consideration as IDB moves forward, regarding the usefulness of country strategies; engagement with subnational governments; streamlining of IDB's different private sector windows; fine-tuning of some lending instruments; speed of project preparation and implementation; knowledge creation and sharing; and the introduction of fee-based services. The evaluation provides five recommendations to help IDB strengthen its engagement with High-Middle Income Countries.

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Borrowers' Perspectives

How is IDB Serving Higher-Middle Income Countries?

OFFICE OF EVALUATION AND OVERSIGHT, OVE

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Contents

Acronyms

BRIK	Bank Repository of Institutional Knowledge
CAF	Andean Development Corporation
CCLIP	Conditional Credit Line for Investment Projects
CS	Client support
CT/INTRA	Intraregional Technical Cooperation
FIL	Financial intermediary credit line
GDP	Gross domestic product
HMIC	Higher middle income country
IDB	Inter-American Development Bank
IDB9	Inter-American Development Bank Ninth General Capital Increase
IFC	International Finance Corporation
IIC	Inter-American Investment Corporation
LAC	Latin-America and the Caribbean
MDB	Multilateral development banks
MIF	Multilateral Investment Fund
NSG	Non-sovereign guaranteed
OMJ	Opportunities for the Majority Sector
OS	Operational support
OVE	Office of Evaluation and Oversight
PBP	Programmatic policy-based loan
PDL	Performance-driven loan
RD	Research and dissemination
SCF	Structured and Corporate Finance Department
SG	Sovereign guaranteed
SME	Small and medium-sized enterprises
TC	Nonreimbursable Technical Cooperation
WB	World Bank

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Santiago de Chile skyline during sunset. In 2010, Chile became the second Latin American country (after Mexico) to join the OECD.
(C) Jimmy Baikovicius, 2009

Executive Summary

The Latin American and the Caribbean Region (LAC) has experienced aggregate positive economic growth over the past decade and has weathered the recent economic crisis relatively well. Growing incomes, strengthened macroeconomic performance, and increased stability over the past decade have allowed some countries in LAC to reach investment grade status, thereby expanding their financing opportunities. However, within the regional trends, national experiences have varied widely in terms of growth, financial access, and government effectiveness.

The changing financial landscape, substantial variation in institutional effectiveness, and changing development needs associated with rising incomes present new challenges to the Inter-American Development Bank (IDB) as a development finance partner. The growing heterogeneity in economic conditions, institutional effectiveness, and access to financial markets across the Region increasingly calls for modes of IDB engagement that are sensitive and well-tailored to the needs of various country groups.

This evaluation assesses how well IDB's current mode of engagement meets the needs and expectations of countries that have relatively higher income levels and increasing access to diverse funding sources. These countries account for most of IDB's lending portfolio, and IDB must understand their needs and demands if it wants to ensure that its business model, financial instruments, and knowledge products serve them effectively.

For the purpose of this evaluation OVE selected 10 countries as case study countries using three objective indicators: (a) income level, (b) level of access to international financial markets, and (c) the weight of the country in IDB's lending portfolio. The countries, labeled higher middle income countries (HMICs) in this evaluation, are Argentina, Brazil, Chile, Colombia, Mexico, Panama, Peru, Trinidad and Tobago, Uruguay, and Venezuela.

The evaluation assessed IDB's current engagement in countries with relatively higher income levels and increasing access to diverse funding sources. The main findings include:

- IDB remains a valued, trusted and financially competitive development partner.
- Country Strategies are not considered to be useful in guiding cooperation with the IDB.
- IDB's engagement with the private sector misses the opportunity of potentially valuable synergies with the public sector.
- Knowledge generation activities are significantly concentrated in the current lending portfolio; while Government counterparts demanded higher investments in prospective knowledge generation.

The study draws on various sources of evidence, with significant emphasis on borrower perspectives. Structured interviews were carried out with over 350 stakeholders in the 10 countries, including government counterparts in finance and line ministries, authorities of central banks and subnational governments, private sector representatives, IDB staff, media representatives, academics, and representatives of other multilateral development banks (MDBs). The information collected through interviews was supplemented by a systematic review of OVE Country Program Evaluations for these countries, focused on analyzing the relevance and effectiveness of IDB engagement, the use of IDB's lending instruments, and the value-added of IDB's knowledge products. Comparative portfolio analyses regarding utilization of lending instruments, sovereign-guaranteed (SG) vs. non-sovereign guaranteed (NSG) lending, and core focal areas of support for 2007 to 2011 were conducted, and IDB's portfolio and financial competitiveness was benchmarked against that of other multilateral lenders in the Region. This evaluation complements OVE's Midterm Evaluation of IDB-9 Commitments by documenting borrowers' perspectives.

The evaluation finds that IDB remains a valued and trusted development partner in the vast majority of the HMIC case study countries. It is still financially competitive, even in countries with investment-grade sovereign risk ratings, and is particularly so during times of international turbulence. IDB's counterparts particularly value the following aspects of their cooperation with the Bank: the discipline IDB helps impart to project design and execution, along with capacity building related to project management; the opportunity that IDB provides to learn from other experiences in the Region; the seal of approval that IDB's project financing can help provide through its social, environmental, and fiduciary safeguards; and IDB's ability to facilitate medium- to long-term project continuity across political cycles.

However, the evaluation also finds that several aspects require further consideration as IDB moves forward. Government counterparts reported that **Country Strategies** are not a useful tool to guide cooperation with the IDB. Indeed, most counterparts engaged in formulating the Bank's country program consider that the annual programming exercise is largely conducted irrespective of the Country Strategy; thus the Strategies are reported to require government time and resources without adding much value. Most government counterparts interviewed value the engagement with the Bank on Sector Notes, which are part of the Country Strategy formulation process, though several suggested that the relevance of such notes could be further increased if they focused on particularly challenging development issues of a cross-sectoral nature and/or were used to identify areas for in-depth future technical dialogue on core development challenges.

IDB's direct engagement with **subnational governments** through SG lending has largely been limited to Brazil; in most other case study countries, such engagement must by law be carried out through the central government. Interlocutors in several countries indicated that IDB could provide significant value-added at the subnational level. While IDB possesses instruments for NSG lending to subnational entities, they have barely been used because of shortcomings in IDB's institutional framework for this niche as well as constraining factors on the borrowers' side: heterogeneity in subnational fiscal and technical capacities, moral hazard concerns that motivate central government involvement even in NSG operations, and requirements that IDB loans be channeled through local development banks. To expand its engagement, IDB would need to analyze and map eligible and excluded entities under alternative policy scenarios for SG and NSG operations.

The Bank's engagement with the **private sector** was found to add value through IDB's seal of approval, financial leverage through B-lenders, and the availability of long-term financing during both expansion and recession periods. Borrowers also expressed the view, however, that the Bank's private sector engagement was not clearly focused on niches with high potential additionality. Furthermore, many stakeholders interviewed by OVE considered IDB to be largely a public-sector-oriented MDB with confusing engagement with the private sector through different, uncoordinated, and sometimes competing windows. Therefore, several suggestions were made to consider a merger of these windows and to strengthen coordination between public and private sector operations. This approach was seen as having the potential not only to enhance IDB's competitiveness in the private sector but also to promote the development of such niches as public-private partnerships and innovations in financial intermediaries to expand small and medium-sized enterprises' access to credit.

The vast majority of counterparts interviewed appreciated the broad menu of IDB **lending instruments**, and the recent addition of emergency and contingency lending instruments should help satisfy calls for such instruments. However, several borrowers called for a redesign of the performance-driven loan and expressed demand for loans denominated in local currency and for currency and interest rate swaps.

HMIC counterparts seek still greater agility from the IDB. The study documents that while IDB's average **speed of project preparation** has improved significantly over the last five years, the overall improvement in project preparation periods has been driven largely by reduced preparation times in countries other than the HMIC case study countries. Indeed, the speed of project preparation in HMICs has improved only marginally over time. The **speed of project implementation**, in contrast, has improved in the case study countries, more than in other LAC countries, which raises the question of whether faster preparation times in the latter may have resulted in projects that are less ready for implementation than in the case study countries.

Regarding **knowledge creation and sharing**, Government counterparts in some countries reported that country programming exercises are not sufficiently informed by analytical work and felt that technical cooperation activities (TCs) are too heavily focused on the current portfolio. It was also reported that knowledge about analytical studies, databases, and survey methodologies is highly compartmentalized within IDB, resulting in shortcomings in internal synergies and external accessibility. It was therefore suggested that TC funds be used more strategically, and that some be directed toward joint identification, piloting, and evaluation of relevant and innovative interventions to address evolving country-specific issues. Efforts also need to be made to ensure that the knowledge IDB helps create is known and readily accessible in the Region. Finally, while HMICs value regional knowledge sharing, there is additional demand for learning from countries beyond LAC.

Fee-based services have been suggested as a possible new way of engagement, though government counterparts felt that the potential instrument must be agile and efficient if it is to serve their needs. Such a potential new line of services would need to be carefully assessed with respect to IDB's staffing and incentives. In particular, it would be important to weigh the potential costs and benefits of engaging in this line of activities, including estimating effective demand and studying other MDBs' experiences with fee-based services in LAC.

OVE has five recommendations to help IDB strengthen its engagement with HMICs. They closely mirror recommendations made by OVE in its evaluation of IDB-9 commitments and other related work:

- **Revisit the formal role and content of Country Strategies and Country Programming Documents to balance the need for strategic selectivity with the essentially demand-driven character of the Bank.** The goal of Country Strategies and Programming Documents should be to find the intersection where country demand overlaps with development priorities and Bank capabilities.

- **With regard to lending instruments, review the experience with performance-driven lending in the IDB and peer institutions and consider introducing lending modalities in local currency as well as currency and interest rate swaps.** New approaches to performance-driven lending in other MDBs that link disbursements more closely to results may have lessons for IDB's engagement in HMICs as well.

- **With regard to nonlending work, undertake further reforms to streamline resource allocation processes, allocate funds strategically, and strengthen results monitoring for technical cooperation and capacity-building work.** Ensuring ready accessibility to the Bank's knowledge products both inside and outside the Bank is also important.

- **Restructure the private sector windows of the Bank to integrate them much better with each other and with the public sector side of the Bank.** Better coordination is essential to tap synergies among the Bank's various operational instruments, and this will occur only if the Bank's structure and incentives push strongly in this direction.

- **Continue to explore options for engaging operationally with subnational entities in HMICs, whether through SG or NSG lending or through nonlending instruments.** Helping subnational governments and enterprises improve their effectiveness is potentially an area of strong demand and high development impact for IDB if appropriate instruments for such support can be developed.

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The *Metropolitano* urban transport system in Lima, Perú, operates on the basis of a public-private partnership between the City of Lima and other firms. A clear niche for IDB's additionality is in large infrastructure projects conducted through public-private partnerships.
(C) Santiago Galdos Gago, 2010

1 Introduction

A. Background and evaluation questions

Latin American and the Caribbean has experienced aggregate positive economic growth over the past decade and has weathered the recent economic crisis relatively well. Such factors as sound macroeconomic policies and strengthened financial systems, combined with more progressive social policies, have also resulted in overall poverty reduction, declining inequality, and important expansions in the size of the middle class. Indeed, the aggregate poverty rate for the Region fell from 44.7% in 2001 to 31.3% in 2010. Likewise, income inequality measured by the Gini coefficient declined from 54 to 50 points during the same period, although inequality and vulnerability remain high in the Region (Annex 1).

Within the regional trends, national experiences have varied widely in terms of growth, financial access, and government effectiveness. Between 2000 and 2010, Barbados, Haiti, and Bahamas grew at less than 0.5% yearly, while Peru, Panama, and Trinidad and Tobago grew at yearly rates above 5.5% (Annex 1). Indeed, growing incomes, strengthened macroeconomic performance, and increased stability over the past decade have allowed some countries in LAC to reach investment-grade status, thereby expanding their financing opportunities.[1] Similarly, there is considerable variation in institutional effectiveness across the Region: according to the 2010 Government Effectiveness Index, Haiti and Nicaragua are below the 10th percentile of the global distribution, while Barbados and Chile rank above the 90th percentile (Annex 1).

The changing financial landscape, substantial variation in institutional effectiveness, and changing development needs associated with rising incomes and an expanding middle class present new challenges for the Inter-American Development Bank (IDB,

The evaluation focuses on ten case study countries labeled as Higher Middle Income Countries (HMICs). The main questions ask how well adapted is IDB to the needs of HMICs regarding its:

- Business model.
- Lending instruments.
- Knowledge creation and sharing.

or Bank) as a development finance partner. The growing heterogeneity in economic conditions, institutional effectiveness, and access to financial markets across the Region increasingly calls for modes of IDB engagement that are sensitive and well-tailored to the needs of various country groups.

The main objective of this study is to assess IDB's current mode of engagement with IDB's borrowing members that have relatively higher income levels and increasing access to diverse funding sources. These countries represent a significant share of IDB's lending portfolio (Annex 2), and IDB must understand their needs and demands if it is to continue to adapt its business model, financial instruments, and knowledge products to serve them effectively. For the purpose of this study, these countries are labeled as higher-middle-income countries (HMICs). It should be noted, however, that many of the evaluation questions are relevant to all LAC borrowing countries. This report therefore complements OVE's Midterm Evaluation of IDB-9 Commitments by helping to document borrowers' perspectives.

The study addresses the following evaluation questions:

How well adapted is IDB's business model to the evolving needs of HMICs?

- What is the role of Country Strategies?
- What role do country systems play?
- What has been the role of non-sovereign lending?
- How does IDB's business model compare to that of other multilateral development banks (MDBs)?

How well are IDB's lending instruments suited to the evolving needs of HMICs?

- How well do IDB's lending instruments meet HMIC expectations?
- How do IDB's lending instruments compare to those offered by other MDBs?
- What is the financial competitiveness of IDB's products in different country contexts?
- To what extent do IDB's lending instruments complement those available to countries that have access to international financial markets?

How effectively does IDB share knowledge in HMICs?

- How well are IDB supported knowledge products meeting countries' demands?
- How effectively is IDB applying global knowledge to country programs and projects?

B. Methodology and data sources

This analysis draws on various sources of evidence, with a strong emphasis on borrower perspectives.

- Case studies were completed for 10 HMIC borrowing countries, as described further below. OVE undertook field visits to each country and conducted in-depth structured interviews with a broad range of stakeholders. A total of 353 persons were interviewed, including government counterparts in finance ministries (29 interviewees) and line ministries (109 interviewees), authorities of central banks (13 interviewees) and subnational governments (23 interviewees), private sector representatives (39 interviewees), IDB field staff (88 interviewees), media representatives (18 interviewees), academics (29 interviewees), and representatives of other MDBs (5 interviewees).[2] The templates used for these interviews are provided in Annex 3.
- The analysis also included a systematic review of OVE Country Program Evaluations.[3] We reviewed the relevance and effectiveness of IDB engagement in these 10 countries, examining the lending instruments used and judging the value-added of knowledge products. In addition, we conducted a comparative portfolio analysis with respect to instrument use, sovereign guaranteed (SG) vs. non-sovereign guaranteed (NSG) lending, and core focal areas of support for 2007 to 2011.
- Finally, we contributed to and drew from IDB-9 background papers on the following topics: IDB's lending instruments, knowledge products, progress on the use of country systems, IDB's programming process, and the relevance of NSG lending to the private sector.

Though more than 10 LAC countries potentially fit the HMIC criteria, for practical reasons (resource and time limitations) OVE limited the number of case studies to 10, selecting the countries by balancing three objective indicators: (a) income level, represented by 2010 GDP per capita; (b) level of access to international financial markets, represented by the S&P Sovereign Debt Rating as of March 2012; and (c) the weight of the country in IDB's lending portfolio, represented by the share of 2008-2010 IDB approvals flowing to each country (Annex 2). Weighting the criteria equally in a composite index, OVE selected the top 10 countries: Argentina, Brazil, Chile, Colombia, Mexico, Panama, Peru, Trinidad and Tobago, Uruguay, and Venezuela.[4] As of 2011, these countries accounted for 80% of IDB's outstanding portfolio and 70% of IDB's total available balance for disbursement. For these countries, IDB disbursements accounted for 0.51% of gross fixed capital formation and 0.11% of GDP in 2011.[5] Eight of the 10 countries possess an investment grade sovereign risk rating, allowing them to borrow in international financial markets at competitive terms (see chapter III). As of 2011, multilateral financing accounted for 9.17% of the total external debt of the case study countries, with IDB's participation amounting to 51.4% of this multilateral funding. Both of these ratios have been stable over the last decade (Annex 1). Finally, these countries accounted for 95% of private capital flows to LAC in 2011.

The case study countries have grown faster, achieved stronger poverty reduction, and shown relatively better government effectiveness than the rest of LAC and the world at large during the last decade. Between 2001 and 2011 they had an average real annual GDP growth rate of 4.3%, while the rest of LAC averaged 3% and the world at large 2.53%. Their poverty rates decreased by an average of 13.7 percentage points (from 43.1% to 29.5%), while other LAC countries averaged a reduction of 12 percentage points (from 45.6% to 33.4%) (Annex 1). In addition, the 2010 Government Effectiveness Index averaged 0.12 for case study countries (located at the 57th percentile of the global distribution) compared to -0.28 for other LAC countries (located at the 43rd percentile of the global distribution).

Map of the top 10 members from the Region classified as "High-Middle Income Countries" and included in the case studies.

(C) OVE, 2013

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Both country counterparts and Bank staff underlined the limitations of Country Strategies as effective and flexible planning tools.
(C) Sébastien Duyck, 2011

2 IDB Business Model

A. Country Strategies

There is widespread consensus on the limitations of Country Strategies as strategic tools guiding IDB's engagement. Country counterparts who are involved in elaborating the strategies, as well as concerned Bank staff consistently report that the Country Strategy does not serve to strategically identify an IDB program that marries country development needs with IDB's capabilities and institutional priorities. Case study country officials engaged in the Country Strategy formulation process seek flexibility and pointed out that one of their main concerns was that the Country Strategy be sufficiently broad so that it does not constrain their ability to change priorities between programming periods.

OVE's analysis of the most recent Country Strategies found that, on average, the case study countries' strategies include nine sectors (compared to seven sectors for other LAC countries). Moreover, case study countries' total approvals covered 10 sectors on average, with every country (except for Brazil, Colombia, and Peru, where the strategies have just been approved in 2012) having projects in more sectors than were covered in the strategy (Table 1).

Main findings of the chapter include:

- Country Strategies are very broad, consisting of a collection of sectors weakly linked with programming.
- IDB's discipline in project design, management, and monitoring was appreciated as a key value added accompanying IDB's financing.
- IDB's "seal of approval" was reported to introduce project acceptability across society.
- IDB's participation in private sector projects is seen to help bring credibility, lower risks, and foster financial mobilization.
- However, IDB's engagement with the private sector was reported as uncoordinated between internal private windows and with the public sector of the Bank; thereby missing potentially important synergies.

Table 1. Number of Sectors in Country Strategies

Country	CS period	Number of sectors planned in the Country Strategy	Number of sectors with approved projects since strategy approval (excluding regional integration and other)	
			Loans	All projects (loans and TC)
Argentina	2009-2011	13	15	15
Brazil	2012-2014	13	6	8
Chile	2011-2014	8	4	10
Colombia	2012-2014	11	5	8
Mexico	2010-2012	9	11	15
Panama	2010-2014	6	9	13
Peru	2012-2016	9	3	6
Trinidad and Tobago	2011-2015	8	5	8
Uruguay	2010-2015	10	9	12
Venezuela	2011-2014	4	2	5
Average HMIC		9	7	10
Average other LAC		7	8	12

Source: IDB Country Strategies and Bank systems, approvals of projects up to July 24, 2012.

Indeed, because Country Strategies are so broad, they consist of a collection of sectors weakly linked with programming. As reported in OVE's IDB-9 background paper on Country Strategies and Programming, Country Strategies do not generally articulate a strategic approach for the Bank in key sectors or discuss the implications of the macro-fiscal analysis on the role of IDB or the size of IDB lending allocations.[6] Given their breadth and lack of prioritization, they are weakly linked to programming exercises, leaving ample flexibility for periodic program negotiations between IDB and borrowers. Thus most government counterparts interviewed suggested that the *de facto* situation is equivalent to negotiating the annual program without the existence of a Country Strategy—a situation that they actually appreciate from IDB.[7]

Borrower officials interviewed expressed concern about the absence of an objective and standardized methodology for determining the lending envelope. They pointed out that aside from ensuring that the Country Strategy allows for maximum flexibility, the main point of interest in Country Strategies is the lending envelope.[8] Several counterparts involved in the process expressed concern about the absence of a formal document that describes the mechanism to define the overall lending envelope in the strategy. OVE interviews with Bank staff indicate that the lending envelope is estimated by analyzing the absorptive capacity of the country, historical lending and disbursement levels, the lending capacity of the Bank, and the interest and demand from the authorities for Bank support. HMIC finance officials interviewed would welcome a formalization of this process.

Although government counterparts interviewed do not value the Country Strategy document, they welcome the process of developing and discussing Sector Notes during the initial stage of the strategy formulation process. Many central and line agency officials interviewed pointed out that the discussion of Sector Notes with IDB specialists provides an opportunity for technical exchange and constructive dialogue on sectoral challenges and at times on international experience also. However, some counterparts expressed concerns about the applicability of international experiences for the specific reality of each country. They wished for Sector Notes that are more than just a compilation of international experience. Such experience should be translated into relevant and actionable interventions for their particular country, and IDB should provide the expertise to match international experience with local needs. Some interviewees also suggested that Sector Notes would be of greater value if they were more focused on the country's specific development challenges and had more technical depth, thus paving the way for medium-term technical dialogue with IDB.

Moreover, counterparts involved in formulating the Country Strategies with Brazil, Mexico, and Uruguay reported that they would favor a thematic approach rather than the current sector approach. They suggested that technical notes should not be fragmented at the sector level because, in their view, such a practice does not recognize the intersectoral synergies toward the solution of broad challenges. Accordingly, they would prefer a thematic vision of development challenges like poverty reduction or productivity improvements, which may encompass multiple sectors.

In sum, the view of country counterparts is that Country Strategies consume significant resources but are not a useful tool. Indeed, in all case study countries, counterparts deemed the elaboration of Country Strategies a time-consuming "bureaucratic process without major implications." Some suggested that the exercise could be substantially improved by focusing it on the preparation of multisectoral thematic or sector-specific in-depth technical notes that could identify areas for further technical dialogue, while using the specific programming exercise to identify the IDB support program, which could conceivably take a somewhat longer (perhaps bi-annual) perspective.

B. Use of Country Systems

The term "country systems" refers broadly to national norms, regulations, procedures, and structures for the management of the public sector. IDB's country systems strategy covers the "fiduciary" systems of procurement and financial management and the "development effectiveness" systems of planning, monitoring and evaluation, and environmental and social safeguards.[9]

The Bank's approach to furthering the use of country systems in its operations combines support for uniform international standards with a demand-driven and country-tailored approach to advance toward those standards. It distinguishes between the "strengthening" of country systems and the "use" of those systems, with strengthening activities done mainly with a view to moving toward "validation" of those systems—that is, establishing their ability to achieve results similar to those that Bank systems would achieve—so that they may be used in Bank-financed projects. As OVE's IDB9 background paper on the use of country systems shows, the Bank's work has focused mainly on moving forward with strengthening and using the fiduciary parts of country systems.

Progress in strengthening and using country financial management and procurement systems has been stronger in the HMIC case study countries than in other LAC countries (Annex 4). IDB has completed assessments of the country financial management systems of all HMIC case study countries, though the actual use of these systems differs by subsystems and countries:

- **Budget subsystem.** Virtually all IDB projects use national systems, except Panama, where 57% of active projects as of June 2012 use national systems.
- **Treasury subsystem.** Argentina and Panama use national systems in less than 10% of projects, Trinidad and Tobago uses them in 86% of projects, and the rest of the HMIC case study countries use them fully.
- **Accounting and reporting subsystem.** Argentina and Peru use national systems fully, while the other HMIC case study countries continue to use IDB's systems.
- **Internal auditing subsystem.** Chile and Mexico use national systems fully, Brazil uses them in less than 20% of projects, and the other HMIC case study countries do not use them at all.
- **External control subsystem.** All case study countries except Panama, Peru, and Venezuela use country systems to at least some extent—from 10% in Colombia to 100% in Mexico, with an average of 49% for the group.

Overall, borrower members value IDB's support in this area, and the various degrees of validation and use of subsystems reflect the countries' varied stages of development.

While IDB counterparts in central and line agencies value IDB's support in developing and strengthening their national procurement systems, counterparts in some case study countries prefer to continue using IDB's procurement systems. IDB has validated Chile's national procurement system for full use in IDB's projects using national competitive bidding, and the systems of Colombia, Brazil and Mexico are due to be validated in the near future. However, except in Panama and Uruguay, counterparts interviewed in the case study countries say they prefer IDB procurement processes over local ones because they enhance competition in the bidding process, yield lower prices, and provide access to better technical assistance and better-quality contractors.[10] In addition, IDB usually provides access to a network of experts to deal with technically difficult procurement processes. Public officials in these countries also report that using IDB systems provides security against future accusations of fraudulent or corrupt bidding processes, as IDB rules provide greater transparency than local systems can.

Some borrowers that prefer IDB's procurement systems conceded that they would prefer to use national systems if those systems had the characteristics they value in IDB's systems. However, they considered that their systems will not be able to develop those characteristics for some time. For example, in Argentina the IDB procurement system allows the use of international bidding processes that would be difficult to undertake under national systems (where foreign bidders would need to comply with local regulations of registration and bid in local currency). And in Peru the use of IDB procurement systems is reported to bring great value-added, making it possible to complete projects within a planned time horizon (something that would be almost impossible to achieve using cumbersome national procurement systems).

Many executing agencies suggested that IDB's fiduciary systems be reengineered and modernized—for example, by going completely paperless. This improvement is seen to have great potential to improve IDB's agility within and beyond the HMIC case study countries.

C. IDB's operational support

Government officials and private sector representatives pointed to several key areas where IDB support adds value beyond financing, including ensuring the technical quality of project design, appraisal, and implementation; enhancing capacity development and corporate governance; and facilitating cross-ministerial and interagency collaboration and communication.

Most government officials and many private sector representatives indicated that IDB's discipline in project design, management, and monitoring is a key added value that comes with IDB project financing. Many interviewees considered that IDB's participation in projects is a key factor contributing to good design quality and rigor in implementation that makes it possible to meet execution targets and milestones. IDB's presence in complex operations involving different sectors, ministries, and government layers has been reported to induce discipline—in attending meetings, reaching consensus, and meeting deadlines—that would not be achieved otherwise. While this observation was made by government counterparts involved in project design and execution across all case study countries, it was particularly highlighted in Brazil, Mexico, and Peru.

Many counterparts in line agencies as well as central ministries that participate in IDB-sponsored projects value the institutional capacity that comes with project design and execution. Counterparts in line ministries and executing agencies—in both central and subnational governments—appreciate the provision of not only discipline in execution but also of operational capacity building in project management. Areas in which IDB participation is reported to strengthen local capacities include project design, organization, management, budgetary, financial, interministerial coordination, monitoring and evaluation, and procurement. This point was highlighted, for example, by representatives of the Health Ministry in Argentina, the Rio de Janeiro Government in Brazil, the Agriculture Ministry in Mexico, and the Social Affairs Ministry in Peru. Box 1 provides an example of the role IDB played in strengthening Panama's Water Authority.

Box 1. Institutional Strengthening of IDAAN in Panama

The institutional strengthening of IDAAN (the Panamanian Water Authority) is a challenge, as it requires changing the culture of this company and transforming it into a modern company. The IDB hired a local company that specializes in business change management and internal and external communications for large organizations and provides services to private sector companies in Panama. With expert advice from this company, the IDB and staff of IDAAN identified key players who would act as advocates or blockers of the reform process. With Bank funding, high-level managers from successful Latin American water companies were invited to Panama to share with IDAAN staff their success stories and in particular to present how they were able to turn their companies around.

The shocking failure to provide water to Panama City in December 2010 and again in 2011 and January 2012 brought this issue to the forefront of the government's agenda, and accelerated the development of a support group formally charged with the reform of IDAAN. The Minister for Canal Affairs, one of the most important public figures in the country, leads the committee that will reform IDAAN. Support by other high-level officials helps ensure that the committee has the leverage needed to succeed. This committee has been instrumental in preparing new water laws for consideration by Congress and financing a business plan for the reform. The business plan includes a road map for the modernization of IDAAN and, importantly, an internal and external communication plan to inform employees and stakeholders about the importance of the reform.

Source: OVE case study

Some line agency counterparts in case study countries expressed their appreciation for the increasing quality-at-entry of IDB projects and the emphasis on securing sound evaluation frameworks and processes to assess projects' impact. At times, even when borrower countries may not need IDB for financial reasons, they have requested IDB support for specific programs to design and verify the impact evaluation—for example, for the Social Protection Network in Colombia, PROCAMPO in Mexico, and the One Laptop per Child program in Peru.

The “seal of approval” implied by IDB’s social, environmental, and fiduciary safeguards is reported to introduce project acceptability across society. In particular, counterparts report that IDB’s participation can be important for a project to be accepted by potential opponents and by the society in general. For example, Brazilian and Mexican authorities report that IDB’s prestige and sound procurement and financial procedures and its environmental safeguards often help subnational governments overcome potentially paralyzing criticism of the pertinence, sustainability, and transparency of investments. Borrower representatives also frequently reported that IDB represents an independent, solid opinion, free of conflict of interest, in decision-making processes. Because IDB is viewed as a credible and impartial third party, analytical work it has supported is reported to often be more easily acceptable to various parties than if it had been undertaken without IDB involvement. It can, thereby, help to reach consensus that could not have been achieved otherwise. Among the many examples provided during case study interviews are the evaluation of alternative science inquiry-based learning for fourth-grade students and teachers in Argentina, the pre-project study for improving the commercial activity and value of historical heritage cities in Chile, and the actuarial analysis undertaken for the comprehensive health insurance program in Peru.

IDB’s participation has also been reported to help secure the continuation of projects beyond the political cycle. Public officials highlighted that IDB financing can increase the likelihood that long-term programs will survive different political administrations, thus making them more sustainable. For example, the conditional cash transfer program Progresa/Oportunidades in Mexico (where the IDB has worked on several fronts) has been sustained through different administrations. Similarly, Venezuelan authorities report that working with IDB funding in large civil works provides the certainty of multiyear financing packages, thus avoiding potential exposure to the country’s annual budgetary process. In Peru, the Bank’s extended support to enhance the phytosanitary standards for agricultural products and eradicate pests such as the fruit fly has helped strengthen the system’s credibility and provide private sector producers with the certainty needed to make investments in long gestation crops.

D. Speed of project preparation and implementation

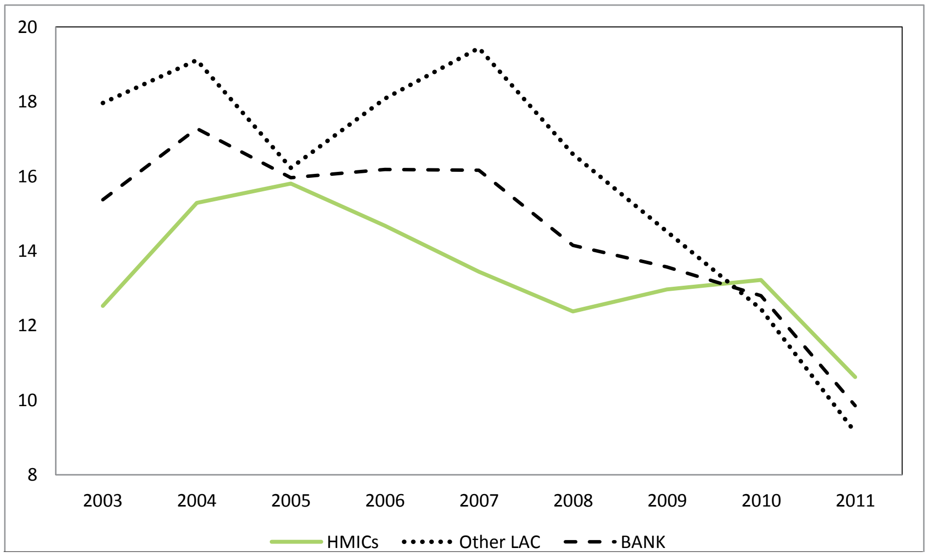
While borrower members recognize and value IDB’s processes and procedures, several counterparts expressed concern about lengthy project preparation periods and indicated that this issue has not improved significantly over time—a somewhat puzzling perception, since IDB project preparation periods have been declining. For investment projects the average time between the beginning of project preparation and approval fell from 24.5 to 19.6 months between 2004-2007 and 2008-2011. This improvement occurred primarily in LAC borrowers other than this HMIC cohort. However, the HMIC case study countries experienced only a marginal decline, from 23 to 21 months, while the rest of LAC borrowers witnessed a reduction from

26.3 to 18 months. A similar pattern emerges for the period between approval and first disbursement using two year moving averages (Figure 1): case study countries showed an improvement of two months between 2003 and 2011 (from 12.5 to 10.6 months), and other LAC borrowers improved by almost nine months (from 18 to 9.1 months).[11] Overall, the evidence confirms that for HMIC case study countries, the speed of IDB project preparation and first disbursement has neither improved nor worsened significantly over time. Furthermore, while IDB's project preparation was faster in HMIC case study countries than other LAC borrowers a decade ago, today that difference has disappeared.

Figure 1

IDB Approval to First Disbursement (SG Investment Loans)

Note: Two-year moving average.
Source: OVE, using IDB's Datawarehouse.



The average time from project approval to disbursement is longer for IDB than for either CAF or the World Bank (WB) in the case study countries. As Figure 2 shows (using two year moving averages), for 2011 the average period between approval and first disbursement for SG investment lending was 6.8 months for the WB, while IDB averaged 10.6 months. However, this difference was larger in 2007 and has narrowed over the last two years. Although there is no official database from CAF, country case studies and interviews with CAF staff agree that the average period between approval and disbursement is about 3 months—significantly shorter than both the IDB and WB. This difference was attributed to CAF's approach of using local regulations for safeguards compliance, while IDB and WB have parallel and more demanding requirements.

When considering preparation time, IDB must consider the potential trade-off between speed and technical quality of project design, including readiness for implementation, which affects the speed with which an approved project can be implemented and funds disbursed. So far the speed of execution has increased over time for IDB in the aggregate (Figure 3). Interestingly, this improvement is heavily driven by HMICs, while speed of project execution in other LAC borrowers has been mostly stable, raising the question of whether faster preparation times in the latter may have resulted in projects that are less ready to execute than in the case study countries.

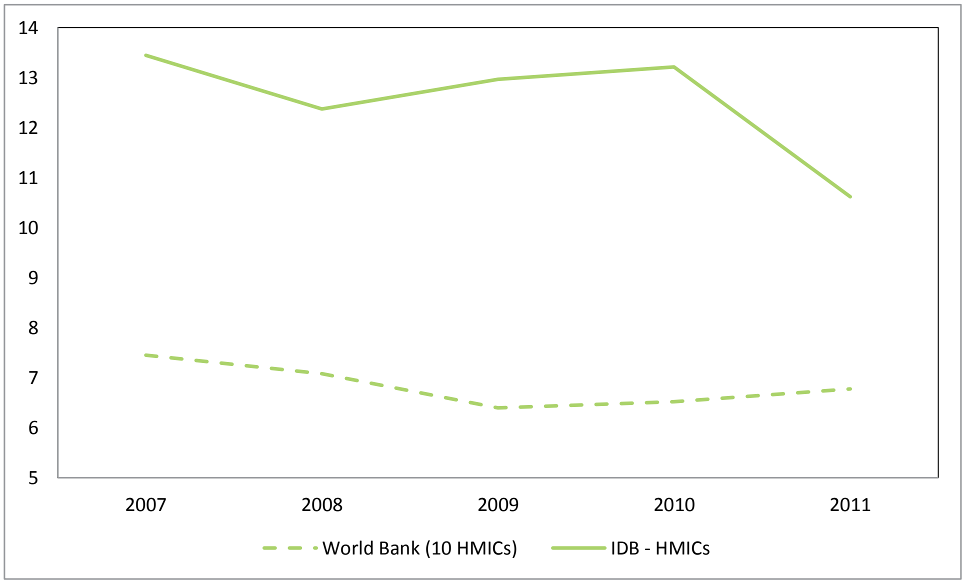


Figure 2

Approval to First Disbursement (SG Investment Loans), in months

Source: OVE, using IDB's Datawarehouse and data provided by WB

All MDBs have improved their overall disbursement speed in the HMIC case study countries and are now at about the same level (Figure 4). However, when only SG investment loans are considered, IDB has shown consistent improvements through time, while the WB's investment portfolio recently recovered to the levels of the mid-2000s, after a temporary dip (Figure 5). Indeed, in 2006 the WB's investment portfolio disbursed a significantly larger share of available loan balances than the IDB in the case study countries, while from 2007 onward the IDB has experienced continuous improvements.

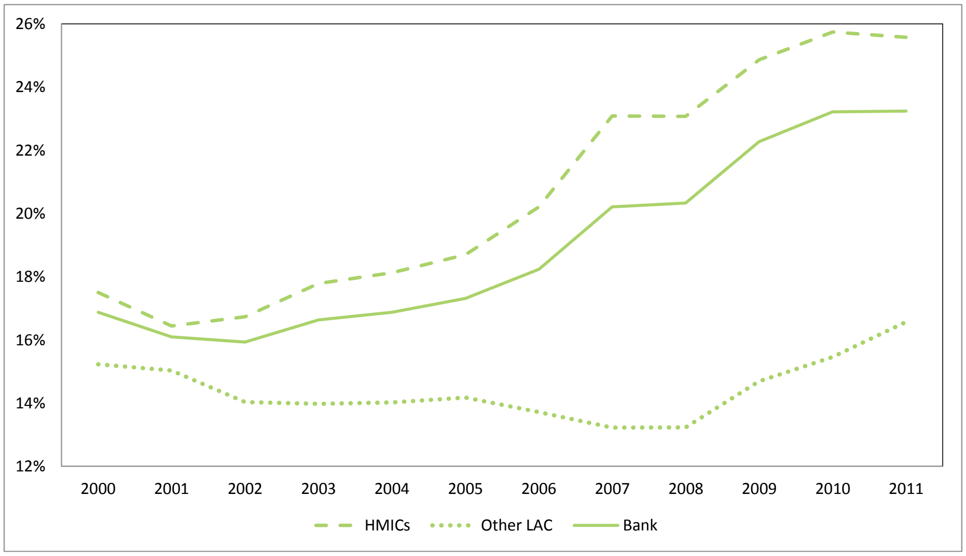


Figure 3

IDB Portfolio Disbursement as a Percentage of Available Funds (SG Investment Loans)

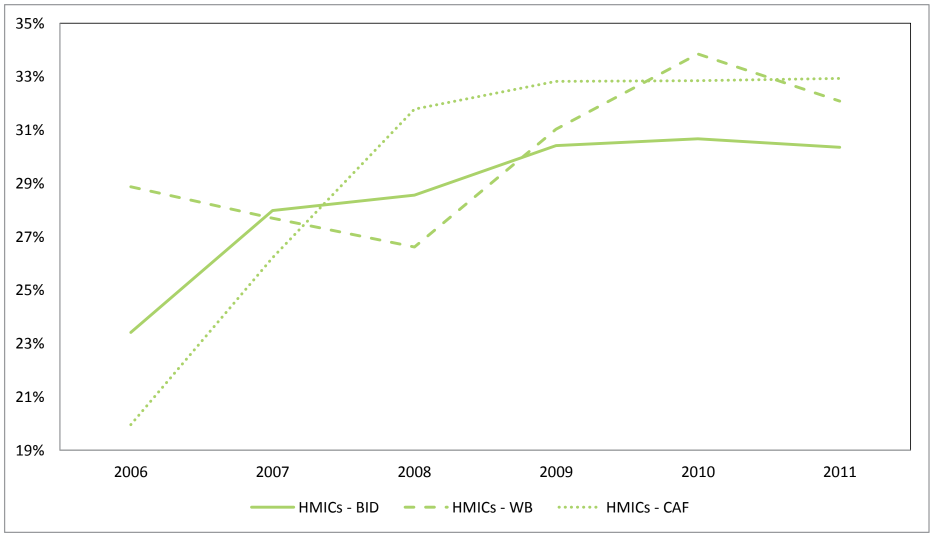
Note: Portfolio disbursement as a percentage of available funds (year t) = disbursed (t) / [undisbursed balance (t-1) + approval (t)]; three-year moving average.

Source: OVE, using IDB's Datawarehouse.

FIGURE 4

MDB's Overall Portfolio Disbursements as a Percentage of Available Funds

Note: Portfolio disbursement as a percentage of available funds (year t) = disbursed (t) / [undisbursed balance (t-1) + approval (t)]; three-year moving average. IDB and WB include SG investment and policy loans. CAF includes SG and NSG operations.
Source: OVE, using IDB's Datawarehouse, CAF annual reports, and data provided by WB.



Executing agency representatives in several countries pointed out that in their experience, the technical capacity, country knowledge, and operational proficiency of a particular IDB project team leader can have a significant bearing on the speed with which projects are prepared, processed, and implemented. In this respect, central and line agency staff in most case study countries expressed appreciation for IDB's technical and operational decentralization. They highlighted the technical capacity and responsiveness of field-based IDB specialists. The dual administrative and technical roles of locally-based team leaders were seen as helping to find mutually acceptable and feasible solutions when problems arose. In the view of many government specialists interviewed, this gives IDB an advantage over some of the other development partners and allows it to come up with technically sound interventions that are well adapted to local conditions. While government counterparts value IDB's technical and operational decentralization, some also suggested that IDB's responsiveness might be further improved if more decision-making authority could be delegated to the Country Representative.

FIGURE 5

IDB and WB Portfolio Disbursements as a Percentage of Available Funds (SG Investment Loans)

Note: Portfolio disbursement as a percentage of available funds (year t) = disbursed (t) / [undisbursed balance (t-1) + approval (t)]; three-year moving average.

Source: OVE, using IDB's Data warehouse and data provided by WB.

E. IDB's engagement with Subnational Governments

There were contrasting views about IDB's direct involvement with subnational governments. Advocates argue that in a country with a relatively developed central government that has financing options, IDB, as a development institution, should channel financial and technical resources to weak subnational governments to strengthen relatively poor local capacities, institutions, and services. However, others argue that precisely because local capacity and financial resources are limited, IDB should channel its efforts to increase local governments' fiscal and technical capacities through the central government. In practice, IDB's direct involvement with subnational governments is concentrated in Brazil (through SG operations), where the experience has been positive and instrumental in strengthening local capacities. Mexican authorities report seeing IDB as a potential ideal partner at the subnational level, but the country's institutional and legal framework has limited IDB's engagement (see Box 2). Similarly, except in Brazil, legal frameworks in the other case study countries are designed in such a way that subnational SG involvement needs to be channeled through the central government.

Box 2. Mexico: Potential for Further IDB Subnational Involvement

The Government of Mexico recognizes that it has yet to develop an adequate mechanism to strengthen subnational governments' institutions and management capacity. Given IDB's track record, the government sees the Bank as a potential ideal partner to help the development of subnational governments. Even though the country's institutional and legal framework does not allow IDB to lend directly to subnational governments—a factor that has prevented IDB from growing in the subnational sector—the limited support the Bank has provided to subnational governments has been very well received and appreciated. Subnational governments seek IDB assistance for reasons other than financial additionality, because it helps them to identify, design, and execute sound investment projects and enhances their institutional capacity and knowledge. PRODEV has been an effective tool to help several Mexican states strengthen their public finances, but its reach and sustainability are limited.

Source: OVE case study

Although IDB has instruments for NSG operations with subnational entities, they have barely been used. Indeed, a recent OVE evaluation of NSG subnational lending shows that IDB's institutional framework is not relevant for this niche;[12] it reinforces the need to understand the potential market for subnational lending, and to analyze and map eligible and excluded entities under alternative policy scenarios for both SG and NSG operations. Clearly, the choice and manner of IDB involvement in this market is not expected to be binary and absolute. Indeed, several factors need to be taken into consideration, such as the within-country heterogeneity in sub-national fiscal and technical capacities, moral hazard concerns that might make central governments' involvement desirable even for NSG operations, country requirements that IDB loans need to be channeled through local development banks (which affects funding costs), and the IDB's own financial limitations compared to subnational needs. However, with appropriate analysis, it should be possible for IDB to proceed cautiously and gradually in the direction of greater subnational involvement.

F. IDB's engagement with the Private Sector

NSG approvals flowing to HMIC case study countries accounted for 70% of overall Bank NSG approvals during 2007-2011.[13] In addition, NSG approvals represented 12.9% of overall (SG and NSG) approvals within HMICs during the same period, while NSG lending accounted for 9.9% of overall approvals for the rest of the Bank's borrowers. Interviews with private sector representatives in the case study countries brought to light a number of issues, both where the Bank's support clearly adds value as a development finance institution and where it falls short.

Private sector representatives, ranging from financial institutions to enterprises engaged in natural resource extraction, pointed out that in many instances IDB's environmental and social safeguards help make complex and often controversial projects acceptable to both civil society and other financiers. IDB's participation is often seen as a seal of approval, given the rigor of its technical appraisal and environmental and social safeguards requirements. It was repeatedly stressed that the chances that a nongovernmental organization or community will oppose a project are reduced when IDB is behind it to ensure adherence to environmental and social safeguards.

Entrepreneurs in some countries pointed out that adherence to IDB's standards provides them with a sense of stability, as national standards may be in flux. In addition, some pointed out that collaboration with IDB on the safeguards front has helped them gain a better command of such issues and taught their staff how to adequately address them. Both entrepreneurs and managers of financial institutions also reported that if a project passes IDB's technical and environmental standards, there is a clear positive signaling effect that induces other financiers to lower financing barriers. In addition, when IDB acts as the primary lender in a syndicated loan, it brings its AAA credit risk rating, which is transferred to the B-lenders that would not have participated otherwise. Therefore, IDB's participation in private projects is seen to help bring credibility, lower risks, and foster financial mobilization (see Box 3).

Box 3. Peru Liquid Natural Gas Project

At the time of approval (first half of 2008), the Peru Liquid Natural Gas (LNG) Project—the largest single private sector project in Peru's history—needed to raise US$2.25 billion. Peru LNG clients said that there was no way they could have raised the needed funds without the participation of IDB and IFC. IDB provided US$800 million (the largest loan of this nature in IDB's history), and IFC approved US$300 million. Fifteen private banks also participated in funding the project, and the borrower indicated that none of them would have been likely to get involved without the IDB and IFC signaling effect and seal of approval.

In addition, clients reported that IDB brought technical expertise and regional knowledge. Particularly on environmental and social issues, IDB specialists helped them foresee what complications might arise and be proactive, drawing on experience in other countries. This was of high value for Peru LNG and helped avoid several potential problems with local communities.

Finally, clients reported that Peruvian environmental regulation was still being modified at the time of project approval. Even if the project could have been financed with private banks only, it would have been required to comply with local environmental standards at approval. Although local environmental requirements were in general less stringent than IDB standards, there would have been a risk that they might change in mid-course according to the political cycle. With IDB participation, certainty about the requirements from the outset of the project provided security in the long term.

Source: OVE case study

IDB provides long-term financing, which is typically unavailable from private financial institutions. Both corporate and financial clients in Colombia, Mexico, Peru, and Uruguay reported that IDB fills a gap in providing long-term funds. Financial sector clients in Colombia, Mexico, and Peru also reported that use of IDB funds is a funding diversification strategy in terms of maturity duration. Furthermore, financial clients emphasized that IDB funding provides a cushion that offsets declines in private flows during periods of crisis. However, given higher IDB "hassle costs" in terms of safeguards and monitoring requirements, some financial entities in Chile and Peru suggested that IDB financing is only attractive for loan amounts above US$100 million.

Private and public sector representatives in several countries reported that, because of IDB's capabilities in leveraging B-lenders and the importance of its seal of approval for project acceptability, a clear niche for IDB's additionality is in large infrastructure projects conducted through public-private partnerships. To be fully effective, such engagement would require close coordination between IDB's private (NSG) and public sector (SG) operations. As OVE's IDB9 background paper on Private Sector Development points out, such coordination can enhance the business environment through improved policies and regulations, while supporting supply response by firms.

Another relevant role was reported to be in fostering innovation through financial intermediary lines (FILs). Private sector representatives in industrial groups and chambers of commerce in Chile, Colombia, Peru, and Uruguay pointed out that such innovations should be focused on attacking market failures and information asymmetries that prevent small and medium-sized enterprises (SMEs) from gaining efficient access to finance. For example, a project in Peru, as part of the screening process for financial institutions, implemented psychometric tests that measure potential borrowers' willingness to pay.[14] However, this type of engagement has not been widespread, and FIL projects have been mostly concentrated in the provision of funds for onlending to qualifying SMEs.[15] Financial intermediaries in Mexico, Peru, and Uruguay reported using this approach as a funding diversification strategy to expand their portfolio, which in any case would have been financed during financially stable periods with alternative sources in IDB's absence. This would suggest that, besides the provision of stable funding, such FILs may not have provided much developmental value-added.

Private sector representatives report that while IDB's engagement with the private sector should have a developmental perspective, IDB should also be competitive as a financial institution. Country case studies identified several shortcomings regarding IDB Group involvement in the private sector. First, private sector counterparts acknowledged the lack of a brand name for IDB in the private sector. IDB is perceived as a public sector bank with a confusing engagement in the private sector through different, uncoordinated, and sometimes competing windows (Structured and Corporate Finance, or SCF; Opportunities for the Majority, or OMJ; Multilateral Investment Fund, or MIF; and Inter-American Investment Corporation, or IIC). Therefore, several suggestions were made to consider a merger of these windows and to strengthen coordination between public and private sector operations. Second, the SCF/OMJ product mix includes loans and guarantees, while only the IIC can engage in equity transactions. Third, counterparts also point out the absence of local currency instruments in IDB's product mix. Fourth, several SCF clients expressed concern about the high costs of engaging with IDB caused by having to apply New York law to the operations. This substantially increases attorney and consultant fees, an expense they believe could be reduced if they were to use local counsel.[16]

G. Comparisons with other MDBs' lending portfolios in HMICs

With the objective of benchmarking IDB's portfolio concentration vis-à-vis other MDBs operating in HMIC case study countries, OVE gathered information about CAF and WB approvals during 2007-2011. The analysis shows that the WB is relatively more engaged in policy lending, while the CAF has primarily concentrated on NSG lending but has a sectoral engagement similar to IDB's.

While IDB has a high portfolio concentration in HMIC case study countries, the WB's concentration is even higher. SG approvals during 2007-2011 show that while the IDB provided more financing than the WB in LAC, the WB has led the IDB in approvals for the HMIC case study countries (Table 2). Moreover, as Table 2 also shows, the IDB and the WB appear to be following different engagement patterns in the HMIC case study countries, with the IDB focusing on investment lending in the productive sectors and the WB having a relatively higher incidence of policy-based lending and a more even distribution across sectors.

Table 2. IDB and WB SG Approvals by Sector and Instrument, 2007-2011

	HMIC		Other LAC	
	IDB	World Bank	IDB	World Bank
Approvals 2007-2011 (US$ million)	38,125	40,948	13,675	5,809
Panel 1: Distribution by Sector				
Social Sector	17%	29%	19%	28%
Productive Sector	74%	51%	58%	39%
Reform and Modernization of the State Sector	9%	20%	23%	34%
Panel 2: Distribution by Instrument				
Investment Lending	81%	58%	59%	46%
Policy Based Lending	19%	42%	41%	54%

Source: OVEDA, using IDB's Datawarehouse and WB data.
Note: Social sector includes projects in education, health and social investment. *Productive sector* includes projects in transportation, energy, urban development, water and sanitation, agriculture and rural development, environment and natural disasters, financial markets, industry, private firms and SME development, science and technology, sustainable tourism, and trade. *Reform and modernization of the state sector* includes projects classified as such in IDB's Datawarehouse and projects classified as public administration, law, and justice in WB's project database.

CAF engagement has been relatively more concentrated in NSG lending. Total CAF approvals for HMIC case study countries during 2007-2011 were US$35,774 million, with 53.3% ($19,061 million) directed through NSG lending. By contrast, IDB NSG approvals for HMICs in the same period were at US$5,662 million, which represented 12.9% of total IDB approvals.[17] The distribution of CAF approvals by sector is similar to IDB's: 79.5% of approvals went to the productive and infrastructure sector (compared to 74% in IDB), 12.1% to the social sectors (compared to 17% in IDB), and 8.4% to structural reforms (compared to 9% in IDB).

3

The menu of lending instruments offered by the IDB was perceived as positive by borrower officials, with specific preferences by country.
(C) Ken Teegardin, 2011

3 Lending Instruments and Financial Competitiveness

A. IDB's Lending Instruments and borrowers' needs

In general, counterparts at finance ministries consider that IDB's menu of SG lending instruments is appropriate, though their use among individual countries varies. As discussed in the IDB-9 Background Paper on Lending Instruments, IDB currently offers nine investment lending instruments in addition to policy lending and emergency lending instruments, and this array compares favorably with that offered by other MDBs.

Borrower officials interviewed uniformly perceive this array of instruments as positive, as their preference is to have a substantial menu from which to choose according to their needs. And indeed, instrument use among the 10 HMICs is far from being homogeneous, as seen in Table 3. For example, Chile mostly concentrated on performance-driven loans (PDLs), Argentina and Mexico on conditional credit line investment projects (CCLIPs), Brazil and Venezuela on specific investment operations, and other HMICs on programmatic policy-based loans (PBPs). In general, counterparts reported that if they have a positive experience with a specific lending modality that meets their needs, they tend to use it as the primary form of interaction with IDB.

Countries showing a preference for the CCLIP report that it facilitates agility through a long-term partnership with IDB. Overall, 87% of all IDB CCLIP approvals between 2007 and 2011 have been to Argentina, Brazil, and Mexico. Both government counterparts and IDB staff have identified the usefulness of the CCLIP in organizing sector work in a long-term strategic perspective (see Box 4). In addition, borrowers report feeling assured of continuous IDB support. Furthermore, although each project under the CCLIP needs individual approval, executing agencies report that project preparation is easier.[18] However, they also perceive that recent changes—such as the requirement that new projects may be approved only when 75% of previously approved resources have been committed or 50% of them invested, and when

The analysis in this section finds that:

- The diverse menu of IDB lending instruments is appreciated by Government counterparts and their utilization is heterogeneous across countries.
- A potential gap in IDB's lending instruments is the absence of a performance-based instrument that disburses against observable and verifiable project outputs.
- IDB and World Bank financial terms are comparable, while CAF's are less advantageous.
- IDB is either at par or more competitive than borrowing in international financial markets.

Table 3. 2007-2011 SG Approvals by Instrument

Instrument	Argentina	Brazil	Chile	Colombia	Mexico	Peru	Panama	Trinidad and Tobago	Uruguay	Venezuela	HMIC	Other LAC
Investment Lending Instruments GN-2564-3												
Specific Investment Operation	17.4%	40.4%	19.6%	21.1%	11.2%	11.2%	15.3%	22.8%	39.2%	57.4%	25.3%	35.2%
Global of Multiple Works Operation	20.5%	19.3%	0.0%	8.3%	2.9%	9.3%	2.0%	0.0%	0.0%	4.6%	11.7%	2.9%
Multi-Phase Lending Project	12.6%	3.5%	0.0%	13.6%	5.7%	0.9%	17.7%	9.7%	0.0%	0.0%	7.1%	5.7%
Global Credit Operation	0.0%	2.3%	0.0%	0.0%	1.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.9%	1.2%
Technical Cooperation Loan	0.0%	0.1%	0.4%	0.2%	0.0%	0.4%	0.0%	0.0%	0.4%	0.0%	0.1%	0.0%
Project Preparation & Execution Facility	0.0%	0.0%	0.6%	0.0%	0.0%	0.1%	0.0%	0.0%	0.1%	0.0%	0.0%	0.2%
Sector Facility	0.0%	0.0%	0.0%	0.0%	0.0%	0.7%	0.0%	0.0%	1.5%	0.0%	0.1%	0.1%
Innovation Operation	0.0%	0.3%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.1%	0.1%
Immediate Response Facility for Emergencies	0.3%	0.0%	0.0%	0.0%	0.0%	0.0%	1.3%	0.0%	0.0%	0.9%	0.2%	0.3%
Performance Driven Loan	0.0%	0.5%	65.4%	0.0%	0.0%	3.1%	0.0%	0.0%	13.2%	0.0%	1.3%	1.4%
Project Using a CCLIP (Conditional Credit Line Investment Projects)	45.2%	29.1%	11.7%	10.1%	56.1%	1.5%	0.0%	0.0%	3.9%	0.0%	31.1%	8.3%
Other Investment Loans												
Hybrid Operation(*)	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	9.9%	0.0%	0.0%	0.1%	1.6%
Supplementary Financing (**)	4.0%	0.7%	0.0%	0.0%	0.0%	0.0%	3.2%	0.0%	6.2%	37.0%	3.4%	2.1%
PBLS/PBP/EMEs												
Policy Based Loan (PBL)	0.0%	3.9%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	1.1%	11.1%
Programatic Policy Base Loan (PBP)	0.0%	0.0%	2.3%	46.8%	23.1%	72.8%	26.9%	57.6%	35.4%	0.0%	16.3%	15.1%
Financial Emergency Operation (EME)	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	33.6%	0.0%	0.0%	0.0%	1.3%	14.6%
TOTAL millions of US$	7,551	10,479	428	4,212	8,666	1,620	1,489	503	1,016	2,160	38,125	13,675

(*) Hybrid loans provide financial support for sector or subsector policy changes, as well as funds for capital investment. They contain a policy reform (fast-disbursing) component to finance a variety of expenditures linked to policy changes and institutional reform, and an investment component targeted to specific investments in the sector, which helps consolidate these new sector policies. The mix of policy-related funds and investments included in the loan varies, depending on the particular needs of the sector or subsector. Disbursements of the investment component are not necessarily linked to the conditionality of the sector component.
(**) Supplementary financing covers a funding gap in a previous operation.
Source: OVE, using IDB's Datawarehouse

80% of expenditures under the previous loan have been justified—are jeopardizing its advantages. For example, representatives of the PROSAP agency in Argentina reported that such requirements have made them seek alternative funding from CAF to continue with their pipeline of projects. PROSAP works with projects at the subnational level, and expenditure justifications for fiduciary purposes are made at different rates in different provinces: some justify expenditures in 5 days, others in 50 days. Therefore, justifying 80% of expenditures before a new disbursement could be approved would slow the execution of current projects for unnecessarily longer periods. In their view, such rules depart from the project reality, inserting unnecessary bureaucracy that harms IDB's agility and making it lose a niche that was exclusive to IDB.

Box 4. CCLIP Use in Argentina

Argentina has used the CCLIP intensively. For 2007-2011, approvals equivalent to US$3,413 million (representing 45.2% of the country's total approvals) were channeled through this instrument. Argentinian counterparts in executing agencies and IDB staff reported that CCLIPs bring the country several advantages. First, they organize sector work with IDB under medium- to long-term goals. In the context of a country that has lacked a Country Strategy since 2007, this strategic orientation provides great value from the Government's standpoint. Second, given the IDB's limited financial envelope relative to the numerous sectors and average project size demanded by the country, the CCLIP facilitates internal resource allocation between different sectors at the national level. Third, the instrument divides operations into different phases with a high degree of coherence between them. Therefore, in a country where projects are of considerable size and operated in a diverse array of sectors, the CCLIP is a very useful instrument.

Source: OVE case study

Experience with the PDL has yielded lessons for its potential redesign. The PDL was introduced in 2003 as a pilot for six years, with the last PDL approval taking place in November 2009 (BR-L1236).[19] Government counterparts at ministries of finance and executing agencies familiar with this instrument, as well as local IDB staff, noted that the design of the PDL suffered from two main shortcomings. First, the PDL required that disbursements be made against achievement of outcomes. Outcomes can take a substantially longer time to achieve than outputs, and it is often difficult to attribute outcomes directly to IDB financing, as they are achieved through financing from various sources. Second, countries needed to present documentation for expenditures made to achieve the outcomes, as well as verification that relevant contracts complied with IDB procurement requirements. In short, PDL added the outcome requirements on top of the requirements for traditional investment lending. This "double bureaucracy" increased transaction costs, offsetting the initial rationale for a performance-based instrument.

The Provincial Agricultural Services Program (PROSAP) in Argentina provides services and business plans to farmers in Argentina's provinces. Representatives of the PROSAP agency reported that the requirements of the Conditional Credit Line for Investment Projects (CCLIP) have made them seek alternative funding from CAF to continue with their pipeline projects.

(C) IDB, 2009

Accordingly, a potential gap in IDB's lending instruments appears to be the absence of a performance-based instrument that disburses against project results. Counterparts in finance ministries and executing agencies in Chile, Colombia, Peru, and Uruguay emphasized that the PDL characteristics made it unreliable, but that they would greatly welcome a reformulated PDL linking disbursement to the achievement of tangible and verifiable results and not requiring expenditures verification. The WB has developed such an approach, and some borrowers report that it constitutes a significant advantage over IDB.[20] IDB staff interviewed also agreed that such an improved instrument could be useful for projects where results can be reported objectively through reliable information systems and verified.

Among finance ministries visited, there was frequent demand for lending modalities in local currency as well as currency and interest rate swaps. Many interviewees noted the absence of SG local currency instruments. HMICs usually hedge currency risks with financial market swaps, which are relatively costly, so they would like to see the expansion of IDB lending in local currency in countries where local financial markets allow for it. In addition, there was demand for IDB-designed swaps for both currency and interest rate risks.[21]

B. IDB's financial competitiveness

The financial terms offered by the IDB and the WB are comparable, while CAF's are less advantageous. For example, as of December 2012, the financial charges for IDB's standard investment SG loans were 87 basis points over 3-month LIBOR, 85 basis points over 6-month LIBOR for comparable WB investment loans and 355 basis points over 6-month LIBOR for CAF (Table 4). Although the WB offers more loan options (including both variable and fixed spreads), the overall effective financial cost of the current IDB and WB portfolios in the 10 HMIC case study countries is similar. Indeed, as of August 2012, the effective annual loan charge on IDB's SG HMIC portfolio was 2.87%, and on the WB's 2.85%.[22] CAF's annual effective financial cost as of August 2012 was 4.75%, almost two percentage points above the IDB and WB terms.[23] This gap reflects the differential funding costs between institutions, as the IDB and WB enjoy a AAA credit risk rating, while CAF has an A+ rating.

IDB's financial competitive advantage over CAF may well weaken over time. As explained in the IDB-9 background paper on Financial and Risk Management, while CAF's lower risk rating means its cost of borrowing is higher, the spread has narrowed considerably. Furthermore, under the new rating methodology proposed by S&P, CAF's reliance on balance-sheet (as opposed to callable) capital favors its approach and places it on a course to plausibly reach a AAA rating within the next five years.

As Figure 6 shows, IDB's ordinary capital SG financial charges as of December 2012 compare either at par or favorably for HMICs with respect to sovereign borrowing in international financial markets even after considering hedging costs for interest rate risk.[24] In particular, IDB offers significantly better financial terms for countries

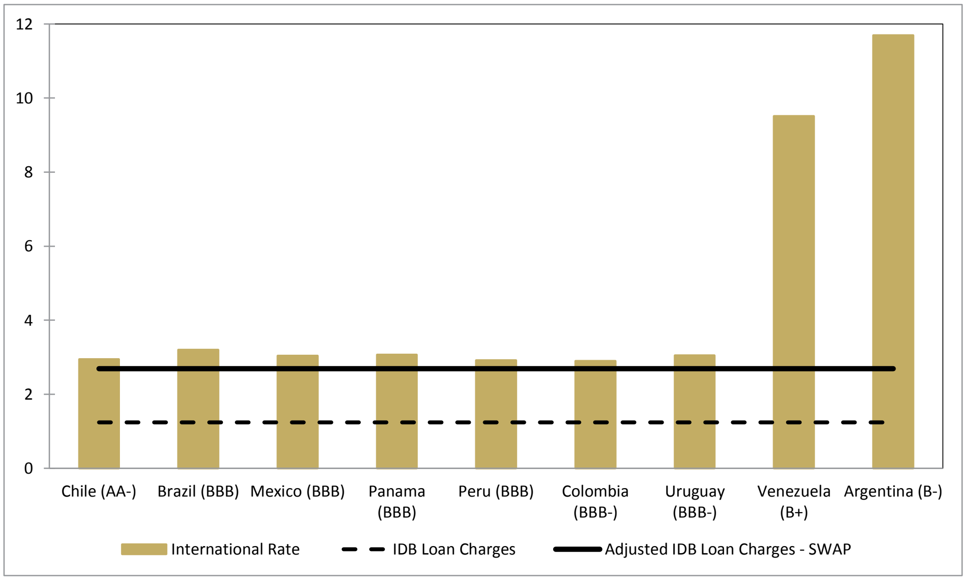


Figure 6

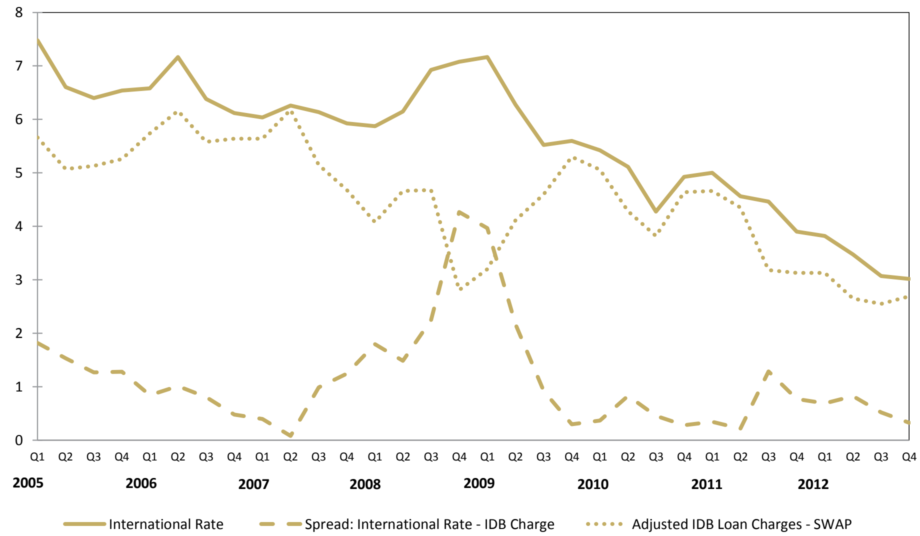
IDB's Financial Costs versus International Financial Markets

Note: As of December 31, 2012. International rate (10Y TBill + EMBI+). For Chile: 10Y TBill + EMBI. No data are available for Trinidad and Tobago. IDB loan charge for ordinary capital loans includes 3-month LIBOR as of December 31, 2012 (0.34%), IDB lending spread (0.62%), funding margin (0.03%) and credit fee (0.25%) for the third quarter of 2012. Adjusted IDB loan charge includes the 10Y LIBOR swap as of December 31, 2012 (1.79%), IDB lending spread (0.62%), funding margin (0.03%) and credit fee (0.25%) for the third quarter of 2012. A similar exercise, considering 30 years maturity financing, yielded similar results.

FIGURE 7

IDB's Financial Costs Trends for Investment Grade HMICs

Note: International rate (10Y TBill + EMBI+). For Chile: 10Y TBill + EMBI. International rate obtained from all HMICs except Argentina, Venezuela, and Trinidad and Tobago. IDB loan charge for ordinary capital loans includes 10Y LIBOR swap, IDB lending spread, funding margin and credit fee. A similar exercise, considering 30 years maturity financing, yielded similar results.



with relatively higher levels of sovereign risk ratings; in Argentina and Venezuela IDB costs are more than 7 percentage points better. In addition, subnational government representatives in Brazil noted that IDB provides them with favorable financial terms, as it is likely to be a long time before financial markets are sufficiently deep to finance Brazil's subnational government needs at sustainable interest rates.

Many country stakeholders in finance ministries recognized the favorable IDB financial terms and stressed the fact that those terms are available during both stable and turbulent international scenarios. Finance ministry officials in all HMIC case study countries, regardless of the country's sovereign risk rating, perceived this as an important value-added. Countries that have favorable sovereign borrowing conditions in stable times are affected by international lending constraints during turbulent times, when IDB financing becomes more relevant to them. Figure 7 plots average international lending rates vis-à-vis IDB financial costs (adjusted for interest rate risk hedging) for HMICs with investment-grade sovereign risk ratings. While IDB's financial cost is consistently below international rates, the spread was particularly evident during the 2008 financial crisis: in the last quarter of that year the difference between IDB costs and international financial markets was 427 basis points.

Counterparts in finance ministries expressed satisfaction with IDB's development of new fast-disbursing instruments geared toward responding during episodes of systematic and idiosyncratic shocks: the Development Sustainability Credit Line, designed to protect poverty-related programs; the Contingent Credit Line for Natural Disasters that complements the Contingent Credit Facility for Natural Disasters, providing additional resources in the event of natural disasters; and the Deferred Drawback Option for PBL/PBP that would allow countries to prepare reform operations ahead of time, with the option of expedited disbursement when needed. For Uruguay, in particular, IDB's main value added was perceived to be as a reliable lender during periods of international turbulence (see Box 5).

Box 5. IDB's Perceived Role in Uruguay

IDB's financial conditions are currently similar to what Uruguay could get in international financial markets. Indeed, as of December 2012, the spread between the country's international rate and IDB's hedging adjusted charges was 36 basis points for a 10-year loan and 58 basis points for a 30-year loan. However, Uruguay could experience unfavorable conditions during international crises. For example, in December 2008 the spread between international rates and IDB hedging adjusted charges was 606 basis points for a 10-year loan and 630 basis points for a 30-year loan. Thus, Uruguayan authorities in the Finance Ministry report that the main advantage of working with the IDB is the possibility of accessing financial resources at reasonable costs during international financial turbulence.

This contingent role has been met through the use of PBL/PBP instruments, which accounted for 45% of the country's approved portfolio in 2005-2009. Therefore, Uruguay welcomes the IDB's new contingent instruments, which they believe will be relevant and useful as they take advantage of IDB's role as a reliable lender during periods of international financial turbulence.

Source: OVE case study

4

IDB Capacity-building event on Citizen Security projects, in 2011.
(C) IDB, 2011

4 Knowledge Creation and Capacity Building

A. Nonreimbursable Technical Cooperation

Technical cooperation (TC) grants are the IDB's largest source of funding for knowledge generation. TCs are classified as operational support (OS), client support (CS), or research and dissemination (RD), and they can be financed with income from the Bank's ordinary capital or donor trust funds. Between 2008 and 2011, a yearly average of US$152 million has been approved for TCs—approximately 80% for OS and CS, and 20% for RD.[25] IDB's investments in knowledge generation are heavily concentrated around current operations (through OS and CS) rather than in anticipatory knowledge generation for future operations (RD). Although economic and sector work generated by the Vice Presidency for Sectors and funded with administrative budget is also focused on prospective knowledge generation, yearly investments under this modality are comparatively lower (in the range of US$24 million).[26]

Several counterparts in economics and line ministries in Colombia, Mexico, Panama and Uruguay reported that programming exercises are not sufficiently informed by analytical work. They perceived that this situation emerged because TC-funded analytic work is generally undertaken after deciding on projects. Therefore, analytic work plays a role in the design of projects, but not in identifying a prospective and innovative agenda for future engagement.

Related to the previous point, some counterparts called for increased operations-related prospective research. They suggested that TC funds be used more strategically, and that some be directed toward joint identification of relevant, innovative, and

The evidence within this chapter shows that:

- Investments in non-reimbursable technical cooperation are largely concentrated in the current lending portfolio and less so in prospective knowledge generation.
- Government counterparts demanded a more strategic use of technical cooperation funds towards joint identification, piloting and evaluation of potentially scalable innovative interventions.
- Demand for agile fee-based services exploiting IDB's positioning as an independent international entity was identified.

Counterparts in finance and line ministries in Chile, Colombia, Mexico, and Peru reported that, although they may not need substantial IDB financing for investment projects, it would be valuable to be able to obtain its assistance for the design, supervision, and evaluation of budget-funded projects through a fee-for-service arrangement.

(C) Willie Heinz, 2002

prospective interventions that might evolve into a medium- to long-term operational agenda. One option suggested by counterparts in line ministries and academics in Argentina, Peru, Chile, Colombia, and Mexico was the introduction of pilot projects with rigorous impact evaluation designs directed toward potential scale-up in future lending operations. For example, a pilot in Argentina that tested and demonstrated the effectiveness of teaching methods for science and mathematics in fourth grade was then scaled up at the national level after its effectiveness was demonstrated through a rigorous impact evaluation. However, this type of engagement now occurs on an ad-hoc basis, and IDB has not handled it with a systematic, integrated, and coordinated approach.

Counterparts in executing agencies report appreciating IDB's responsiveness in providing opportunities to learn from relevant regional experiences. In particular, borrowers value IDB's ability to bring practical experiences from other member countries to help them think about how to solve specific problems. This is achieved not only through the regional knowledge of IDB specialists, but also through the exchange of experiences provided via the Intraregional Technical Cooperation (CT/INTRA).[27] For example, a neighborhood upgrading project in Uruguay benefited from the experience in a project in Argentina with procuring secondhand houses for relocating squatters. In a few cases, however, line agency counterparts expressed concerns about IDB trying to introduce practices from other countries that were not amendable to local conditions. In Trinidad and Tobago, for example, some interviewees felt that the Bank was at times too quick to recommend solutions from other Latin American countries that were not suitable to local conditions.

Borrowers are also interested in global learning from countries beyond LAC. On this front, they typically found the WB to have an advantage over IDB. This issue was also identified in recent Country Program Evaluations for Brazil, Chile, and Colombia. In some cases, IDB has partnered with other agencies to provide global knowledge to HMIC counterparts. For example, as noted in the IDB-9 background paper on Knowledge Products, IDB worked with the UK's Department for International Development to enable relevant officials from the Colombian health ministry to partner with UK government organizations and draw on experience from the UK and New Zealand. The program of combined fiduciary studies with the WB is another example of this type of engagement. Therefore, IDB may wish to explore to what extent these kinds of partnerships could be integrated as a systematic part of IDB's knowledge services. This could help satisfy the growing demand from HMICs for global knowledge from more advanced countries with experiences relevant for their individual development paths and challenges.

B. Reimbursable knowledge services

Counterparts in some HMICs suggested it would be helpful if advisory services could be unbundled from financing. Borrowers reported valuing IDB's technical assistance in project design and execution, but such assistance is tied to IDB's financing. Counterparts in finance and line ministries in Chile, Colombia, Mexico, and Peru reported that, although they may not need substantial IDB financing for investment projects, it would be valuable to be able to obtain its assistance for the design, supervision, and evaluation of budget-funded projects through a fee-for-service arrangement (see Box 6). The new Country Strategy for Peru raises the possibility of fee-based services. Except for the Special Program of Reimbursable Advisory Services signed with Chile in 2001, IDB does not have a framework for fee-based services.

Box 6. Potential Demand for Fee-Based Services in Colombia

Government officials were generally positive about the possibility of introducing fee-based services, although a couple of interviewees considered that such an arrangement would run counter to IDB's not-for-profit development objectives. The interviewees who saw fee-based services as a potentially useful instrument mentioned several advantages.

- It could help improve the quality of IDB's TC. When TC is free, recipient countries have little incentive to complain about low-quality work.
- It could make it possible to hire highly qualified local consultants at competitive rates without generating incompatibilities with the government salary structure. When TC projects are executed by government agencies, the consultants hired for the TC must receive wages that are consistent with those prevalent in the rest of the government. This makes it very difficult to hire highly qualified consultants whose wage rates greatly exceed local salaries.
- It could help dissociate technical assistance from financial cooperation. In most cases, technical assistance is linked to loan operations. Some interviewees mentioned instances in which IDB was not able to provide technical assistance unless the country took on a loan on a related topic.

Source: OVE case study

IDB's positioning as an independent international entity is a comparative advantage that could be exploited in the provision of advisory services. Some government counterparts who saw a value in a fee-based service product line suggested a potential IDB niche in developing independent studies on controversial topics. While governments could rely on private consulting firms for such services, they report that such studies would not have the level of public acceptability that IDB, with its "honest broker" positioning, could provide. This observation was reported at the Ministry of Energy in Chile and the Ministries of Finance in Colombia and Peru. However, counterparts in Chile reported that if IDB were to offer such services, the response time from client requirement to product delivery should not exceed three months, to be competitive.

Under the current IDB internal structure, the advantages of operating as a consulting firm are limited. Given constraints on overall staffing, there are likely to be trade-offs in using staff time to manage fee-for-service contracts, even if there is cost recovery for institutional overheads. Furthermore, countries' demands may well be in areas not covered by the lending program, under which borrowers would expect to receive services as part of IDB's regular support. Therefore, IDB needs to assess the desirability of establishing such a business line, including internal incentives, resources needed, the potential market, and other MDBs' experience (see Box 7).

Box 7. Examples of WB Fee-Based Services Experiences in LAC

Procurement Strengthening in Trinidad and Tobago
The WB provides fee-for-service technical assistance in Trinidad and Tobago; for example, it prepared a review of procurement practices and recommendations for improvements. According to high-level staff in the Ministry of Finance, the WB's support is more focused and complete than the support provided by IDB. The IDB tends to provide support with "one-consultant" teams, and the quality of their reports in some cases is not good. By contrast, the WB sends teams of consultants and there is a general perception that their outputs are of better quality than the IDB's.

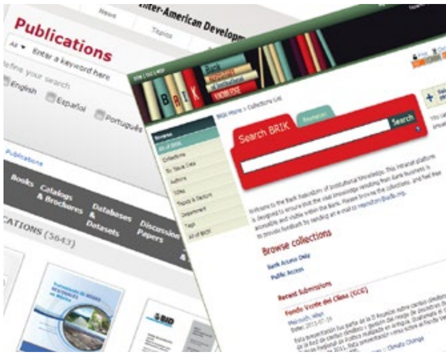
Advisory Services in Chile
Chile has limited needs as a borrower; however the country has identified the WB as a relevant partner in the design and implementation of its development agenda. Chile turns to the WB for knowledge and advisory services, delivered on a programmatic basis through a cost-sharing program. The program consists of five to six studies per year; the US$800,000 program is financed 50% by Chile and 50% by the WB. The program has been successful in providing support to key reforms in education, public sector management, insurance, and infrastructure concessions. In education, the WB is analyzing policy options to improve the student finance system for tertiary education.

Source: OVE case study

C. Accessibility of IDB's knowledge

Although IDB has accumulated a considerable body of knowledge, its institutional memory related to analytical work is weak. Until recently, IDB had no inventory of analytical work accompanied by a central repository of databases related to this work. In 2012 the Bank Repository of Institutional Knowledge (BRIK) was created to fill this gap. However, the TCs used to produce analytical studies, data collections, and survey methodologies are still highly compartmentalized and therefore not readily available. As a result, IDB as an institution is still unable to share knowledge internally, create synergies, identify information gaps, and prioritize investments in knowledge efficiently. Line agency counterparts in several countries report that local staff members have the capacity to fill country-specific knowledge gaps, but their knowledge is compartmentalized and vulnerable. When staff rotate, they keep their information and do not pass it to their replacement.

Thus the BRIK is a necessary but not sufficient condition for effective knowledge sharing. It provides the tool to organize knowledge produced by the Bank, but it does not solve the internal compartmentalization culture in the production of knowledge, which often misses opportunities to exploit synergies. The main challenge now is BRIK's implementation and the extent to which IDB staff will effectively use and manage this tool, which will require a change in institutional culture.



BRIK, the new Bank Repository of Institutional Knowledge, is a necessary but not sufficient condition for effective knowledge sharing within and outside the Bank.
(C) OVE, 2013

Most government counterparts, academics, and media professionals perceived IDB's knowledge dissemination efforts as low, and said they did not know about or have access to IDB's knowledge products. They perceived the Bank's track record of publications addressing issues of relevance for individual countries as poor. The majority of actors interviewed in academia, consulting, media, research, and government agencies reported not knowing what IDB's contribution to knowledge was and where to find it. They indicated that when they needed research about specific issues in a country they referred to the WB's work. To address perceptions like these, the Office of External Relations is working with the Knowledge and Learning Sector to integrate the BRIK with the external website's publication module and is also working on an initiative to improve the IDB website's search tool. Again, however, it will be important to ensure that IDB staff use such tools to their full potential.

5

Downtown Sao Paulo, at dusk. Brazil was one of LAC emerging high-middle income countries being consulted for the evaluation. IDB's direct engagement with subnational governments is largely limited to Brazil.
(C) Diego Torres Silvestre, 2012

5 Conclusions and Recommendations

This study has documented the perspectives of a broad range of representatives in 10 HMICs regarding IDB's business model, lending instruments, financial competitiveness, knowledge generation, and overall value-added, and supplemented that feedback with additional analysis to see how well the Bank is serving this client group. The evaluation concludes that IDB overall remains a valued and trusted development partner in the vast majority of the HMIC case study countries. It is still financially competitive, even in countries with investment-grade sovereign risk ratings, particularly during times of international turbulence.

IDB's counterparts particularly value the following aspects of their cooperation with the Bank: the discipline IDB helps impart on project design and execution, along with capacity building related to project management; the opportunity IDB provides to learn from other experiences in the Region; the seal of approval IDB's project financing can help provide through its social, environmental, and fiduciary safeguards; and IDB's ability to facilitate medium- to long-term project continuity across political cycles.

The evaluation, however, also finds that several aspects of IDB's business model need further consideration as the institution moves forward. Among the most important issues to address are the following:

Country Strategies. Most government counterparts reported that Country Strategies require government time and resources without resulting in a tool that is useful to guide areas of cooperation with the IDB. Most government counterparts interviewed value the engagement with the Bank on the Sector Notes that are part of the Country Strategy formulation process, though several suggested that the relevance and technical depth of such notes could be increased.

Non-Sovereign Guaranteed approvals flowing to HMIC case study countries accounted for 70% of overall Bank NSG approvals during 2007-2011.
(C) FOMIN, 2011

Subnational governments. IDB's direct engagement with subnational governments is largely limited to Brazil; in most other case study countries such engagement must by law be carried out through the central government. Yet interlocutors in several countries indicated that IDB could provide significant value-added at the subnational level. While IDB possesses instruments for NSG lending to subnational entities, they have barely been used because of shortcomings in IDB's institutional framework for this niche and constraining factors on the borrowers' side.

Private sector. While IDB's engagement with the private sector has been reported to add value regarding IDB's seal of approval, financial leverage through B-lenders, and the availability of long-term financing during both expansion and recession periods, there was also a view that such characteristics are not clearly focused on niches with high potential additionality. Several suggestions were made to consider a merger of the IDB Group's various private sector windows and to strengthen coordination between public and private sector operations. This approach was seen to have the potential not only to enhance IDB's competitiveness in the private sector, but also to promote the development of such niches as public-private partnerships and innovations in FILs directed toward addressing market failures that prevent SMEs' access to credit.

Lending instruments. IDB's broad palette of lending instruments was appreciated by most borrowers interviewed, and the recent addition of emergency and contingency lending instruments should help satisfy calls for such instruments. However, several borrowers called for a redesign of the PDL. There was also demand for loans denominated in local currency and for currency and interest rate swaps.

Speed of project preparation and implementation. While the average time required for project preparation has fallen over time in IDB, this improvement has largely been driven by reduced preparation periods in countries other than the HMIC case study countries. Disbursement speed, in contrast, has improved in the case study countries, more than in other LAC countries. HMIC counterparts seek still greater agility from the IDB.

Knowledge creation and sharing. Government counterparts in some countries reported that country programming exercises are not sufficiently informed by analytical work and felt that TCs are too heavily focused on the current portfolio. It was also reported that knowledge about analytical studies, databases, and survey methodologies is highly compartmentalized within IDB, resulting in shortcomings in internal synergies and external accessibility. It was therefore suggested that TC funds be used more strategically. While HMICs value regional knowledge sharing, there is additional demand for learning from countries beyond LAC. Efforts also need to be made to ensure that the knowledge IDB helps create is readily accessible in the Region.

While IDB possesses instruments for NSG lending to subnational entities, they have barely been used because of shortcomings in IDB's institutional framework for this niche and constraining factors on the borrowers' side.

(C) Willie Heinz, 2003

Fee-based services have been suggested as a possible new way of engagement, though government counterparts felt that the potential instrument must be agile and efficient if it is to serve their needs. Such a potential new line of services would need to be carefully assessed with respect to IDB's staffing requirements and incentives.

OVE has five recommendations to help IDB strengthen its engagement with HMICs. They closely mirror recommendations made by OVE in its evaluation of IDB-9 commitments and other related work.

- **Revisit the formal role and content of Country Strategies and Country Programming Documents to balance the need for strategic selectivity with the essentially demand-driven character of the Bank.** The goal of Country Strategies and Programming Documents should be to find the intersection where country demand overlaps with development priorities and Bank capabilities.

- **With regard to lending instruments, review the experience with performance-driven lending in the IDB and peer institutions and consider introducing lending modalities in local currency as well as currency and interest rate swaps.** New approaches to performance-driven lending in other MDBs that link disbursements more closely to results may have lessons for IDB's engagement in HMICs as well.

- **With regard to nonlending work, undertake further reforms to streamline resource allocation processes, allocate funds strategically, and strengthen results monitoring for technical cooperation and capacity-building work.** Ensuring ready accessibility to the Bank's knowledge products both inside and outside the Bank is also important.

- **Restructure the private sector windows of the Bank to integrate them better with each other and with the public sector side of the Bank.** Better coordination is essential to tap synergies among the Bank's various operational instruments, and this will occur only if the Bank's structure and incentives push strongly in this direction.

- **Continue to explore options for engaging operationally with subnational entities in HMICs, whether through SG or NSG lending or through nonlending instruments.** Helping subnational governments and enterprises improve their effectiveness is potentially an area of strong demand and high development impact for IDB if appropriate instruments for such support can be developed.

Endnotes

Endnotes

[1] In 2001 Bahamas, Barbados, Chile, Trinidad and Tobago, and Uruguay were classified as investment-grade countries. In addition to those countries, Brazil, Colombia, Mexico, Panama, and Peru are now classified as investment-grade countries.

[2] See Annex 2 for distribution of interviewees by country.

[3] The strategic periods covered by these CPEs are as follows: Argentina (2003-2008); Brazil (2007-2010); Chile (2006-2010); Colombia (2007-2010); Mexico (2007-2011); Panama (2005-2009); Peru (2007-2011); Trinidad and Tobago (2000-2008); Uruguay (2005-2009); and Venezuela (1999-2007)

[4] For methodological details on the selection of the case study countries, see Annex 2.

[5] Sources: IDB's Datawarehouse and World Development Indicators.

[6] Country Strategies include lists of analytic work used in their preparation. Most such lists include Independent Macroeconomic Assessments, Debt Sustainability Analysis, Growth Diagnostics, or other documents that indicate that the Bank invests in analyzing the economies of countries in the Region. From the information provided in the Country Strategy, it is not usually clear how the analysis is used in defining priorities for the Bank.

[7] In Trinidad and Tobago concerns were expressed that the 2011-2015 Country Strategy proved too confining because the government's priorities had changed, when IDB stated that annual programming needed to be consistent with the directions outlined in the strategy.

[8] Some government counterparts contrasted the IDB's approach to Country Strategy and program formulation with that of the CAF, which was seen as an even more demand-driven institution. CAF consults with borrowers on their desired financing from CAF over a 10-year horizon and uses those desires to help determine its capital needs. It then infers the required contributions of paid-in capital over that 10-year horizon. Thus CAF's strategic plans are focused on securing financial resources to satisfy borrowers' demands. However, there is no systematic formal development of country strategies that set out areas of engagement over the medium term.

[9] Strategy for Strengthening and Use of Country Systems, 2009 (GN-2538).

[10] For Mexico, counterparts report that for routine procurement processes involving purchases of standardized goods, the national system would be preferable. However, for complex processes or for hiring specialized consultants, implementing agencies prefer IDB systems with their higher transparency and technical assistance.

[11] Note that the period between approval and first disbursement includes two subperiods: the period between approval and eligibility, and the period between eligibility and first disbursement. The first subperiod shows the same pattern with HMIC agility stable and non-HMIC agility improving. The second subperiod shows improvement for both groups, going from an average of 2.5 months in 2004-2007, to an average of 1.6 months in 2008-2011.

[12] An Evaluation of the Bank's Non-Sovereign Operations with Sub-National Entities: 2007-2010 (RE-402).

[13] IDB NSG approvals totaled US$ 8,048 million between 2007 and 2011, of which US$5,662 million was directed to HMIC case study countries. During 2003-2006, 82% of NSG approvals went to case study countries, while this figure decreased to 70% for 2007-2011.

[14] Note that the Multilateral Investment Fund (MIF) has introduced several psychometric-based lending pilots in LAC. However, besides isolated interventions like the example mentioned here, IDB Group FIL projects have not focused on scaling up such pilots or included these innovations in a structured and general approach.

[15] See Fourth Independent Evaluation of SCF's Expanded Project Supervision Report Exercise, RE-332-6.

[16] Local law is used extensively by the IIC and MIF. However, SCF uses New York law when there are co-lenders, who typically demand New York law as they are more familiar with it.

[17] CAF NSG aggregate lending to LAC during the 2009-2011 period has been mostly concentrated in short-term loans (credit lines) accounting for US$9,925 million (or 81% of its lending for the period). IDB Group NSG lending was concentrated in medium- to long-term loans, accounting for US$4,227 million (or 88% of its lending for the period).

[18] Indeed, the CCLIP provides substantial time savings in the preparation of subsequent loans for both the IDB and the client. First, subsequent operations are submitted to the Board on a no-objection basis. Second, the executing agency and the project's activities and outputs remain the same as under the initial loan, thus requiring fewer missions and preparation time for the responsible unit than a non-CCLIP operation. Third, a Project Profile (PP) is not required, saving time in the preparation of the PP and the ERM review

[19] See GN-2278-2 (2003), Proposal for a Pilot Program for Performance-Driven Loans (PDL). Revised version.

[20] See Program for Results instrument at www.worldbank.org/ProgramforResults.

[21] The World Bank offers such instruments; see http://treasury.worldbank.org/bdm/htm/hedging_products.html.

[22] Effective annual loan charge is a proxy obtained through the ratio of annual debt servicing to outstanding disbursed balance.

[23] In terms of repayment periods, CAF loans can be short-term (1 year), medium-term (1-5 years), and long-term (over 5 years). Therefore, the comparison is not direct. However, when computing the annual effective financial costs, all debt servicing and outstanding disbursed balance is pulled together.

[24] We proxy the financial cost of sovereign borrowing in financial markets using the J.P. Morgan Emerging Markets Bond Index Plus (EMBI+) spread over the 10-year US Treasury Bill. For Chile, we use the J.P. Morgan EMBI because EMBI+ is not available. These benchmarks measure total return (annual effective yield to maturity) performance of international government bonds issued in foreign currency. The EMBI+ measures both Brady bonds and other sovereign debt, while the EMBI measures only Brady bonds. To qualify for index membership, the debt must be more than one year from maturity, have more than US$500 million outstanding, and meet stringent trading guidelines to ensure that pricing inefficiencies do not affect the index.

[25] Note that the MIF has approved a yearly average of US$52.3 million in TCs in HMICs during the same period. However, the focus of our analysis is IDB-approved TCs.

[26] For year 2012, investments in economic and sector work included Personnel Cost (US$12.1 million) and Non-Personnel Cost (US$12.2 million); see 2012 Approved Program and Budget. Final Version, GA-248-7.

[27] Intraregional technical cooperation (CT/INTRA) operations are those in which one or more institutions in the Bank's borrowing countries provide technical assistance to one or more institutions in another IDB borrowing country. The general purpose is to contribute to the transfer of know-how and technology that could help the economic and social development efforts of the Bank's member countries, as well as to promote cooperation among borrowing members. The program serves to support and stimulate bilateral cooperation.