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**INTERIM EVALUATION OF THE
FINANCIAL SECTOR DEVELOPMENT PROJECT
(No. 940-0014)**

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Presented by:

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TABLE OF CONTENTS

EXECUTIVE SUMMARY	i
Chapter I: INTRODUCTION	1
A. Project Background and Objectives	1
B. Current Status of Project Activities	2
C. Evaluation Purpose and Scope	2
D. Evaluation Methodology	6
Chapter II: EMPIRICAL FINDINGS	7
A. Relevance	7
B. Effectiveness	8
1. Strategic Planning Component	8
2. Technical Assistance Component	10
3. Research and Development Component	13
4. Dissemination of Information Component	14
5. General Project Effectiveness	16
C. Efficiency	19
D. Impact	20
E. Sustainability	22
Chapter III: CONCLUSIONS	23
Chapter IV: RECOMMENDATIONS	26

Table of Contents...../....

APPENDICES

- A. Contractor Scope of Work
- B. Evaluation Scope of Work
- C. List of Individuals Contacted
- D. List of Documents Reviewed
- E. USAID Mission Questionnaires
- F. Summary Descriptions of FSDP Engagements To Date
- G. Diagnostic Framework

EXECUTIVE SUMMARY

INTRODUCTION

This interim evaluation of the worldwide Financial Sector Development Project (No. 940-0014) was prepared for A.I.D.'s Bureau for Private Enterprise by Checchi and Company Consulting, Inc. and Louis Berger International, Inc. under their joint IQC No. PDC-0085-I-00-9060-00 for Development Information and Evaluation Services. The evaluation team was composed of an Institutional Analyst/Team Leader (*Jack Corbett*), an Economic Analyst (*Gilbert Lane*), and a Social Science Research Analyst (*Carol Van Hulzen*). The evaluation was completed in November 1990 and covers project activity through September 30, 1990.

PROJECT DESCRIPTION

The purpose of the Financial Services Development Project (FSDP), a follow on to the Financial Markets Development Project, is to assist developing countries in their efforts to develop and improve domestic capital markets and to augment the flow of financial resources to the private sector. A five-year contract to furnish technical services in support of the FSDP was awarded to Price Waterhouse in September 1988 with the stated objective of "promoting more efficient capital mobilization and allocation through improved strategic planning, policy and institutional reform, introduction of financial instruments and mechanisms, and information sharing." The contract called for four inter-related types of services: (1) strategic planning, (2) technical assistance, (3) research and development, and (4) dissemination of information, to be used in developing a coherent approach to the solution of problems in the financial sectors of A.I.D.-assisted countries.

EVALUATION PURPOSES AND METHODOLOGY

The purposes of this interim evaluation are:

- o To evaluate the relevance, effectiveness, efficiency, impact, and sustainability of project activities and the degree to which the project had achieved its objectives during the period covered by the evaluation; and
- o To provide appropriate recommendations with respect to project design, execution, and administration.

The evaluation methodology involved:

- o Review of project design documents, the amended contract, contractor work products, and related background materials;

- o In-depth interviews with key A.I.D. and contractor staff; and
- o Analysis of responses to questionnaire surveys from USAID Missions that have received FSDP services.

FINDINGS AND CONCLUSIONS

The FSDP was designed to give a cohesion to financial sector assistance that had been lacking in the predecessor project. The four project services components were conceived as being mutually supportive, each in some way giving direction or reinforcement to the other components. The evaluation team devoted special attention to examining the effectiveness of the work performed under these four components.

A.I.D. and the contractor have not found it easy to launch the strategic planning assessments based on the full scope of the diagnostic framework. Consequently in November 1990, the contractor was empowered to use specific sections of the diagnostic framework as appropriate. This contract modification should allow the contractor to accommodate the desires of the USAID Missions which provide the bulk of financing for assessments. There has been an unwillingness on the part of the Missions to devote resources to broad strategic assessments when, in their opinion, more specific financial problems demand attention.

Services under the technical assistance component have been the most widely used of the project's components and have generally been well regarded by USAID Missions and A.I.D./W recipients. Some of these services have been provided at the initiative of A.I.D. and the contractor while others have been in response to Mission needs. While such studies did not flow in most cases from strategic planning assessments, they were related to USAID and host government efforts to free up and develop the financial sector.

Some of the technical assistance services have been aimed at supporting privatization efforts by the Missions and host governments. Although the ability of local financial markets to accommodate the security issues arising from privatization projects can be related to the FSDP's objectives, studies of privatization projects are best aimed at government owned banks and insurance companies. Studies of privatization projects involving industrial and commercial companies should be carried out under other A.I.D. programs, such as the Center for Privatization.

Activity under the research and development component has fallen short of project design expectations. A research agenda involving the publication of four monographs per year of journal quality has not been achieved. A.I.D. has reviewed this contract requirement and has decided that research under the contract has been and will continue to be demand driven. Consequently, the contract was amended in November 1990 to require the production of eight reports a year of high technical quality related to ongoing interventions.

The dissemination of information component shows some opportunities for further improvement. The semi-annual newsletter has been prepared as required but a review

should be made to determine the usefulness of the information it imparts to the Missions regarding studies and projects in the financial sector. Currently the newsletter limits its reporting on such studies to those carried out under the FSDP. Conferences have been organized as planned, as have regional workshops and seminars for Mission and A.I.D./W personnel. Conferences have shown a higher cost per participant than the regional workshops, and it is the conclusion of the team that this higher cost is not clearly justified by a greater contribution to project objectives. Finally, contacts and coordination with international donor agencies have been limited primarily to the field.

RECOMMENDATIONS

Recommendations are provided for modifications in project marketing, execution, and resource allocation to address problems identified by the evaluation team. Substantial resources remain and mid-course corrections should enhance prospects of achieving project objectives.

The recommendations include suggestions for:

- o Better representation of the diagnostic framework tool to USAID Missions;
- o Improved marketing and utilization of financial sector assessments;
- o Tighter definition of the scope of financial sector services;
- o Review within A.I.D. of the project's research objectives and resources, followed by appropriate contract modifications;
- o Improvement of the contents of the semi-annual newsletter;
- o Greater use of regional workshops for information dissemination and Mission familiarization with financial sector developments;
- o More regular contacts between PRE and international donor agencies in Washington for coordination and information sharing purposes.

The recommendations are aimed at focusing the project on the objectives outlined in the project design documents and the contractor's original proposal. The need and demand for rational development of the financial sector in most countries have grown since the initiation of the project. The experience gained by A.I.D. and the contractor in the first years of the project will serve them well in meeting future demands for assistance to the financial sector.

Chapter I

INTRODUCTION

A. PROJECT BACKGROUND AND OBJECTIVES

The Financial Sector Development Project (FSDP) was launched by A.I.D.'s Bureau for Private Enterprise (PRE) in 1988 in support of PRE's goal of increasing capacity in developing countries for market-based economic growth. The purpose of FSDP was to assist developing countries in their efforts to develop and improve domestic capital markets and to augment the flow of financial resources to the private sector. The project was designed as a follow on to the worldwide Financial Markets Development Project (FMDP), which was implemented through a technical assistance contract with Arthur Young and Company from 1985-1988.

A five-year technical support services contract for FSDP was awarded to Price Waterhouse (PW) in September 1988. The contract scope of work called for PW to provide technical assistance through A.I.D. to developing countries to promote more efficient capital mobilization and allocation through improved strategic planning, policy and institutional reform, introduction of financial instruments and mechanisms, and information sharing. The contract provided \$3.6 million in core (PRE) funding for 308 person-months of services and up to \$7.1 million for an additional 880 person-months of services to be funded through USAID Mission buy-ins. This buy-in provision was intended to overcome a perceived weakness of the predecessor (FMDP) project by enlisting full Mission support and commitment for FSDP activities.

Unlike the FMDP contract which focused primarily on the design and implementation of financial markets development projects in response to USAID Mission requests, the FSDP contract called for PW to supply an integrated package of mutually supporting services in four areas:

- 1) **Strategic Planning**, including (a) design of a diagnostic framework to be used by Missions in identifying potential opportunities for financial development and regulatory reform; (b) financial sector assessments; (c) formulation of Mission financial sector development strategies; and (d) preparation of strategy implementation plans. The sector assessments and subsequent three to five year strategic planning tasks were to be conducted for each of ten developing countries that expressed interest in receiving financial sector development assistance.
- 2) **Technical Assistance**, defined as the provision of long-term and short-term expertise in fiscal and monetary policy, financial sector regulations, financial intermediation, education and training, and related areas in accordance with USAID Mission requirements.
- 3) **Research and Development**, defined as original applied research by academic scholars and researchers on topics related to financial sector development, with an

anticipated output of four occasional papers per year over the five-year contract period.

- 4) **Dissemination of Information**, including: (a) publication of a semi-annual newsletter and the occasional papers generated by the research and development team; (b) organization of two conferences per year; and (c) general support to PRE staff in their relationships with other donors and the private sector.

B. CURRENT STATUS OF PROJECT ACTIVITIES

Price Waterhouse (the "contractor") initiated services under the FSDP contract in January 1989. The evaluation provided herein covers the first 21 months of project activity, from January 1989 through September 1990.

Exhibit A was prepared for the evaluation team by the contractor to show the activities that have been undertaken during this period by project component, and the funding source for these activities. Of the 47 activities listed, 31 activities were funded either partially or entirely through USAID Mission buy-ins; one activity (Jordan Equity) was never funded; and 15 activities were funded out of the core contract with no USAID participation.¹ Appendix F provides descriptive information on each activity.

C. EVALUATION PURPOSE AND SCOPE

Checchi and Company Consulting, Inc. and Louis Berger International, Inc. were engaged by A.I.D./PRE to conduct this interim evaluation of the Financial Sector Development Project (No. 940-0014) under their joint venture IQC for Evaluation and Information Services. The evaluation was performed during October and November 1990 by a three-person team consisting of Jack Corbett, Institutional Analyst/Team Leader; Gilbert Lane, Economic Analyst; and Carol Van Hulzen, Research Analyst. A copy of the evaluation Scope of Work is provided in Appendix B.

The team was requested to make an interim assessment of the Financial Sector Development Project that would (1) determine progress to date toward the attainment of project objectives; (2) examine project strengths and weaknesses; and (3) provide appropriate recommendations. Empirical findings were to be presented with respect to project relevance, effectiveness, efficiency, impact, and sustainability. These five lines of inquiry are reflected in the format for the body of the report.

¹Four other activities are expected to be underway by January 1991.

COMPONENT ONE: STRATEGIC PLANNING

COUNTRY/ACTIVITY	FUNDING	SOURCE	TOTAL BUDGET	FSDP COMPONENT
	CORE	BUY-IN		
2. Jordan	\$20,000.00	\$41,000.00	\$61,000.00	
10. Morocco FSA		\$48,965.00	\$54,797.00	1
		\$5,832.00		
24. Thailand FSA		\$19,072.00	\$59,072.00	1
		\$40,000.00		
26. Lesotho FSA		\$25,591.00	\$25,591.00	1
35. Pakistan	\$31,055.71	\$125,050.00	\$156,105.71	1
40. Nicaragua FSA	\$50,989.62		\$53,889.62	1
	\$2,900.00			
43. Bolivia Sector Survey		\$189,920.00	\$189,920.00	1
46. Tunisia FSA	\$98,600.00	\$14,833.49	\$113,433.49	1
SUBTOTAL	\$203,545.33	\$510,263.49	\$713,808.82	

FSDP EVALUATION
FINANCIAL MATRIX

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COMPONENT TWO: TECHNICAL ASSISTANCE

COUNTRY/ACTIVITY	FUNDING	SOURCE	TOTAL BUDGET	FSDP COMPONENT
	CORE	BUY-IN		
1. West Bank/Gaza		\$14,700.00	\$14,700.00	2
3. Belize Credit Survey	\$13,395.90		\$13,395.90	2
6. The Gambia	\$14,493.00	\$18,600.00	\$42,393.00	2
		\$9,300.00		
7. Pakistan Hab River	\$7,076.00	\$75,000.00	\$187,323.00	2
		\$105,247.00		
8. Egypt Equity Finance (Phase I)		\$377,282.00	\$377,282.00	2
9. Guatemala/CABEI	\$12,049.00		\$12,049.00	2
11. Morocco Stock Mrkt.	\$11,929.00	\$36,000.00	\$47,929.00	2
14. Jordan Equity	\$0.00	\$0.00	\$0.00	2
15. Financial RFP	\$9,406.00		\$9,406.00	2
16. Honduras	\$30,000.00	\$98,000.00	\$128,000.00	2
20. Indonesia	\$40,100.00	\$94,700.00	\$552,767.00	2
		\$25,600.00		
		\$107,168.00		
		\$273,455.00		
		\$11,744.00		
21. Fin. Analysis Training		\$177,714.00	\$327,714.00	2
		\$150,000.00		
25. Guatemala		\$54,662.00	\$54,662.00	2
27. 936 Guarantee		\$18,791.49	\$18,791.49	2
30. Bank Analysis		\$19,784.00	\$67,859.00	2
		\$13,860.00		
		\$34,215.00		
33. Bolivia Privatization		\$107,988.89	\$107,988.89	2
34. Tunisia Capital Mrkts.		\$74,616.87	\$74,616.87	2
38. Uganda		\$12,566.07	\$12,566.07	2
39. Eastern Europe		\$6,577.00	\$18,872.43	2
		\$12,295.43		
44. ANE Regional		\$149,898.00	\$149,898.00	2
45. Morocco Sec. Debt	\$2,727.00	\$75,955.00	\$78,682.00	2
47. Ivory Coast		\$28,003.11	\$28,003.11	2
SUBTOTAL	\$141,175.90	\$2,183,700.66	\$2,324,876.56	

**FSDP EVALUATION
FINANCIAL MATRIX**

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COMPONENT THREE: APPLIED RESEARCH

COUNTRY/ACTIVITY	FUNDING	SOURCE	TOTAL BUDGET	FSDP COMPONENT
	CORE	BUY-IN		
13. Modernization	\$29,979.00		\$29,979.00	3
17. Integration	\$35,000.00	\$65,000.00	\$100,000.00	3
18. PRE Housing		\$41,280.00	\$41,280.00	3
19. Private Power	\$35,000.00	\$65,000.00	\$100,000.00	3
28. ANE Concept Paper	\$15,745.00		\$15,990.00	3
	\$245.00			
36. Thailand LDC Bonds		\$51,271.00	\$51,271.00	3
42. Chile LDC Bonds		\$57,462.00	\$57,462.00	3
SUBTOTAL	\$115,969.00	\$280,013.00	\$395,982.00	

COMPONENT FOUR: INFORMATION DISSEMINATION

COUNTRY/ACTIVITY	FUNDING	SOURCE	TOTAL BUDGET	FSDP COMPONENT
	CORE	BUY-IN		
4. Debt Strategy	\$19,456.50		\$19,456.50	4
5. Debt Conference	\$5,510.00		\$5,510.00	4
12. Newsletter I	\$22,912.00		\$22,912.00	4
22. Regulation Seminar	\$13,745.00		\$13,745.00	4
23. FSDP Conference	\$55,958.00		\$55,958.00	4
29. Newsletter II	\$17,115.00		\$17,115.00	4
31. ANE PSO Conf.	\$23,040.22		\$23,040.22	4
32. Algeria	\$13,320.41		\$13,320.41	4
37. Thailand USIS Conf.	\$14,129.00		\$14,129.00	4
41. Bolivia Seminars	\$8,407.00	\$215,881.00	\$224,288.00	4
SUBTOTAL	\$193,593.13	\$215,881.00	\$409,474.13	
TOTAL	\$654,283.36	\$3,189,858.15	\$3,844,141.51	

D. EVALUATION METHODOLOGY

The findings, conclusions, and recommendations of this evaluation are based on in-depth interviews with key A.I.D. and contractor personnel; contacts with USAID Missions that have participated to date in FSDP activities; and review of project documents. Appendices C and D provide, respectively, a list of persons interviewed and a bibliography of source materials. Appendix D contains copies of the questionnaires that were developed by the evaluation team and sent to USAID Private Sector Officers in the following countries:

Belize	Morocco
The Gambia	Nicaragua
Egypt	Pakistan
Honduras	Thailand
Indonesia	Tunisia
Jordan	Uganda
Lesotho	

(The team was unable to get a fax through to Bolivia).

The team greatly appreciates the timely and thorough responses provided by the USAID Private Sector Officers. The team was also able to review the responses of USAID Missions in eight countries (Egypt, The Gambia, Honduras, Morocco, Indonesia, Pakistan, Uganda, and Bolivia) to a questionnaire developed by the contractor for its internal management purposes.

Chapter II

EMPIRICAL FINDINGS

A. RELEVANCE

The conditions described by the statement of work for the FSDP contract point to: 1) a critical shortage of private capital flowing to developing nations, primarily because private bank lending has been curtailed and 2) domestic savings which are not large enough to satisfy domestic investment. These conditions continue to prevail and progress towards freer financial intermediation and market driven economies has been, with few exceptions, slow. Still, the recognition by governments and political leaders of the need for greater economic freedom in the market place is encouraging and warrants continued support by the international community in general and by A.I.D. in particular.

Increasingly, the public as well as the experts realize that to state the objectives and goals for change is far easier than to bring about change. Each country has unique characteristics and, while there are common experiences, solutions to market and institutional constraints must be tailored to each country's situation. For example, the interest rate structure in the financial sector of most developing countries frequently has a large measure of artificiality. Institutions have long since learned to live with these rigidities and their operations are based upon the distorted relationships between institutions and markets. Therefore a change in one area of the interest rate complex sets off a chain reaction throughout the financial sector, quickly spilling over into the political and social life of the country.

This example, and there are others, illustrates the wisdom of the original concept of the FSDP in calling for strategic assessments based on a "diagnostic framework" that examine a range of factors presently influencing the financial economy of a given country to guide the selection and execution of specific, timely technical assistance activities. However, in practice, very few countries or USAID Missions had opted for full scale strategic planning assessments in the first two years of the project; in no case has a three to five year strategic plan based on the assessment been adopted. This shortfall was recognized by A.I.D. in a November 1990 modification of the FSDP contract permitting the contractor to use only portions of the full diagnostic framework in conducting strategic planning assessments.

Nonetheless, the project is well positioned to respond to the opportunities offered by recent economic and political changes which have spurred interest in and support for financial sector liberalization. In this sense, the assistance available through the FSDP is relevant and needed.

B. EFFECTIVENESS

1. Strategic Planning Component

Strategic planning was envisioned as a major component of the FSDP. The contractor's successful proposal attached notable importance to strategic planning activities which would "represent the broad framework under which priorities will be developed for all project tasks," and "define the priorities and action plans for technical assistance."

The contractor was to develop a diagnostic framework for conducting a financial sector assessment which could be used by USAID Missions "to identify potential opportunities for financial development and regulatory reform in developing countries." At the same time, the contractor was to use the guidelines established in the diagnostic framework to conduct assessments of approximately ten countries which expressed interest in such assessments. The assessment results were to provide the basis for developing and recommending appropriate financial sector development strategies. These recommendations were to be followed within a period of no more than two months by a strategic plan for implementation covering a three to five year period.

Due to contract start-up delays, the diagnostic framework was submitted by the contractor in April 1989 and approved by A.I.D. in July 1989. The diagnostic framework itself (Appendix G) is a very comprehensive outline of the many institutional, functional and operational areas of a country's financial sector. It was intended to allow a USAID Mission to see the potential reach of the financial sector thus permitting it to decide, in collaboration with A.I.D. PRE and the contractor, just how comprehensive an assessment might be appropriate. A number of uses were outlined for the assessments ranging from assistance to the Missions in the conduct of policy dialogue with host governments and institutions to its use as a tool in providing "a detailed plan of action for policy reform and technical assistance to strengthen individual financial sectors."

There follows a listing of assessment activities carried out to date under the Strategic Planning component of the FSDP:

<i>Completion Date</i>	<i>Strategic Assessment Activities</i>	<i>Client</i>
01/89	Jordan Financial Markets Development Strategy	Mission
• 03/89	Belize Financial Sector Survey	Mission
10/89	Morocco Financial Sector Reform	Mission
02/90	Thailand Financial Sector Strategic Assessment	Mission

* 03/90	Lesotho Financial Intermediaries and Practices	Mission
06/90	Pakistan Capital Markets Assessment	Mission
07/90	Nicaragua Financial Sector Assessment	Mission
10/90	Bolivia Financial Sector Assessment	Mission
11/90	Tunisia Financial Sector Assessment	Mission

- * classified as Technical Assistance in Exhibit A.

The diagnostic framework was not available when the first full-scale financial sector assessment was completed for Jordan in January 1989. Subsequent assessments in other countries have tended to be more restricted in scope and evidence of the impact of the diagnostic framework on these assessments is not clear. However, the use of the diagnostic framework was not heavily marketed and the team has found relatively little awareness of the document and its contents among the USAID Missions queried. Eight of the eleven Missions who responded to our questionnaire had never heard of, or were not aware of having received, the diagnostic framework.

The evaluation team had access to seven assessment reports; two other assessments (Bolivia and Tunisia) were still underway at the time of the evaluation. In the opinion of the team, the assessment of Jordan's financial sector comes closest to a comprehensive financial sector assessment of the type outlined in the diagnostic framework (although this assessment was completed before the framework was approved). The other assessments deal with specific segments of the country's financial sector, such as the banking structure, bank regulation and supervision, capital markets, interest rates, and security pricing. In the case of Thailand, the assessment is more nearly a "reconnaissance" of the sector, producing an assortment of recommendations that might be followed up later by A.I.D.

The assessments for Morocco, Jordan, Nicaragua, and Pakistan were accompanied by recommended strategies and action plans for follow-on technical assistance activities. The reports on Lesotho and Belize, which are more appropriately classified as surveys of a particular aspect of the financial sector, also provided recommended strategies. In the case of Thailand, a number of areas were called to the attention of USAID with the idea that at a later date the recommendations would be narrowed to a group of three or four specific areas which offered the greatest potential for an A.I.D. role.

In its successful proposal the contractor stated that it would strive to "place A.I.D./PRE in a more proactive role to analyze and meet the needs of targeted countries, rather than simply reacting to disparate Mission requests." Clearly, this depended upon the full cooperation of USAID Missions in agreeing to fund fairly broad assessments of the financial sector in their respective countries. However, in practice the USAID Missions often had

other priorities for the use of their resources, and host countries were sometimes not willing to undergo the searching review a full-scale assessment would entail. As a result, A.I.D. and the contractor have had to accommodate the strategic planning component to the perceived needs of the market through a contract modification. This contract modification, approved in November 1990, acknowledges that it is "satisfactory to use sections of the diagnostic framework as appropriate" for strategic assessments.

As indicated, some of the financial sector strategies flowing from the assessments culminated in implementation plans for follow-on technical assistance. Thus far, follow-up has been limited to Morocco, where two detailed studies on stock exchange development and secondary debt market are currently being completed. In the case of Jordan, external events have interfered with plans for further action. Several other USAID Missions have indicated that they intend to act on some strategic recommendations.

2. Technical Assistance Component

Under the technical assistance component of the FSDP, long-term and short-term expertise was to be provided in matters of fiscal and monetary policy, financial sector regulations, financial intermediation, education and training, and related areas in accordance with A.I.D./W and USAID Mission requirements. It was anticipated that a significant demand for technical assistance activities would flow from strategic planning recommendations. While there has been an evident shortfall in the assistance arising from this source, this shortfall has been more than overcome by a widespread demand from the USAID Missions and A.I.D./W bureaus and offices for studies of particular problems and aspects of the financial sector. In this respect, the FSDP is not unlike its predecessor and fully meets one of its objectives.

The following is a list of all technical assistance activities initiated to date, broken down by client source:

<i>Completion Date</i>	<i>Technical Assistance Activities in Countries with an Assessment</i>	<i>Client</i>
04/89	Pakistan Hab River Power Evaluation	Mission
06/89	Jordan Equity Markets (cancelled)	Mission
06/90	Tunisia Venture Capital Feasibility Assessment	PRE/PD
06/90	Bolivia Privatization Strategy	Mission
07/90	• Thailand Local Currency Bonds	Mission

09/90	Morocco Stock Exchange Development	Mission
09/90	Morocco Secondary Debt Market Development	Mission
11/90	Nicaragua Bus System Privatization	PRE/PD

*Technical Assistance Activities in Countries
without an Assessment*

03/89	West Bank/Gaza Credit Guarantee Facility Feasibility	PRE/DP
04/89	Gambia Stock Market Feasibility	Mission
04/89	Egypt Equity Finance Facility	Mission
10/89	Indonesia Stock Market Regulation and Operation	Mission
12/89	Honduras Bank Strengthening Program	Mission
08/90	Uganda Stock Exchange Development Feasibility	Mission
08/90	• Chile LC Municipal and Corporate Bonds	PRE/H
11/90	Guatemala Central Bank Strengthening	Mission
11/90	Sri Lanka Credit Subsidies Appraisal	Mission
01/91	Egyptian Bond Market	Mission

Technical Assistance Activities for A.I.D. Bureaus/Offices

06/89	CABEI Strategic Plan	ROCAP
10/89	Bank Training RFP Analysis	PRE/I
02/90	Financial Analysis Training for Bankers & Borrowers	PRE/I
03/90	Feasibility on Facility for Section 936 CBI Program	PRE/I
04/90	Bank Analysis I-IV	PRE/I

04/90	Programming A.I.D. Financial Activities and Options (Paper prepared for Private Sector Officers Conference 5/90)	ANE
08/90	Eastern Europe Financial Markets Study	PRE/DP
09/90	Eastern Europe Financial Sector Development Study	PRE/DP
10/90	La Financiere (Ivory Coast) Financial Analysis	AFR/MOI
01/91	Financial Sector Technical Assistance and Training	ANE

The studies have all been of short-term duration. The Contractor believes that longer-term assistance might have a more beneficial impact, but except in the case of Indonesia this has not been possible. A clearer commitment on the part of the Missions and host countries to a continuing attack on the constraints facing the financial sector would probably increase individual country demand for longer-term assistance.

Funding for the studies has generally been provided by the clients, which include both USAID Missions and A.I.D./W bureaus and offices. While this has insured a keen client interest in the study output, it has not resulted in the pattern of work envisaged under the contract. The contractor and PRE can attempt to influence the selection and scope of the technical assistance activities, but in the final analysis they must accept and accede to the wishes of the funding source.

The areas of study have included stock and bond markets, bank regulation and supervision, credit guarantees, training for the financial sector, and credit subsidies. Some of the areas covered go beyond those originally contemplated for the project, such as privatization studies. It is argued that the supply of securities limits activity in the financial markets and privatization is a legitimate and desirable means of expanding the supply. The team fully supports the drive towards privatization, but it doubts that this is a wise use of the resources available for studies of the financial sector except in cases of government owned banks and insurance companies which are direct participants in the financial sector. The team sees any increase in the supply of securities arising from privatization as a by-product and incidental to the solution of major problems existing in the financial sector. Likewise studies of private ownership of power generating facilities are only distantly-related to the development of security or financial markets. On the other hand, creating freely and efficiently functioning security markets would certainly encourage privatization as well as private initiatives throughout the economy of an A.I.D.-assisted country.

The evaluation team sent out a questionnaire, included as Appendix D, to determine USAID Mission satisfaction with FSDP services and received responses from 11 of the 13 Missions contacted. All but one of the Missions responding gave very satisfactory ratings to the time lapse between the request for task and the start up, indicating that short-term technical assistance has been provided to Missions in a timely fashion.

In regards to the calibre of personnel provided, five Missions rated the contractor above average and four Missions said that the host country gave above average ratings for the calibre of the personnel. Four Missions indicated some measure of dissatisfaction with the work of the contractor's personnel. In general, the contractor seems to have provided a satisfactory level of performance in technical assistance assignments.

Five of the studies were performed in countries where financial assessments were also carried out. Two of these, both in Morocco, flowed directly from the strategic assessment. Eight technical assistance studies took place in countries where no assessment had been made. This fact does not mean that the objectives of the project are not being served. The studies, in the view of their USAID clients, served the Missions' needs well and fitted into their concepts of developing and freeing up the financial sector.

3. Research and Development Component

The FSDP contract called for the contractor to procure the services of scholars and researchers to conduct original applied research regarding capital formation, private sector financial expansion and overall economic development in Third World countries. This activity was expected to generate four occasional papers over a five-year period, or a total of 20 papers. The contractor and the research and development team were to cooperate in making recommendations for innovative research projects.

A November 1990 contract modification substituted the requirement of four monographs per year of journal quality for a requirement that the project produce eight reports a year of high technical quality related to ongoing interventions.

The following is a list of outputs to date under the research and development component:

<i>Completion Date</i>	<i>Research and Development Activities</i>	<i>Client</i>
02/90	Prefeasibility Study of an A.I.D. Guaranty of Local Currency Bond Issues by Municipal and Housing Authorities	PRE/H
02/90	Modernization of Regulatory and Supervisory Systems of LDC Financial Institutions	PRE/PD
06/90	Private Power and Capital Market Development (Phase I)	ANE
02/91	Policy Framework for Financial Sector Liberalization	PPC

Based upon analysis of the output to date and numerous discussions with A.I.D., contractor, and the research group personnel, the research component has not met the expectations envisioned for it in the project design. The principal problem seems to be the inability of the three parties involved (PRE, PW and the research sub-contractor, FMIRI) to generate and agree upon a research agenda. Establishing an agenda appears to consist of a process in which: (1) FMIRI suggests research topics; (2) PW reviews and modifies the suggestions and prepares a prospective agenda; and (3) PRE acts on the agenda. However, an agenda was submitted to PRE in June 1990 and has not yet been acted upon.

The problem of determining an agenda is perhaps based upon deeper problems which were mentioned to the evaluation team in its discussions with the research group. Several of these are: (1) the uncertainty about A.I.D.'s interest in research, (2) the feeling that there is somewhat of a competitive situation between the contractor and the research subcontractor, and (3) the difficulty in identifying projects which can be marketed, and which must go through A.I.D. administration. There is interest in A.I.D. in a research program more directly related to country problems and interests. To accommodate these problems and interests would involve major changes in the present contract.

Despite these hurdles, three research projects have been completed under the project and another (the Policy Framework Study) is underway. All four activities have been funded either through core or A.I.D./W buy-ins. The only Mission involvement has been through the technical assistance activity (Pakistan Hab River Power Project) which led to ANE's request for a research paper on private power and capital market development that might be applicable to other LDCs.

The Prefeasibility Study of an A.I.D. Guaranty of Local Currency Bond Issues by Municipal and Housing Authorities was requested by PRE/Housing. This FMIRI study served as a building block for two following technical assistance case studies in Chile and Thailand conducted by the prime contractor, using other consultants. The Thailand case study analyzed the feasibility of raising long-term local currency debt to finance public infrastructure and private corporate investment, while the Chilean study focused on A.I.D.-guaranteed local currency bond issues. Both are examples of successful technical assistance projects stemming from the research and development component.

4. Dissemination of Information Component

The principal tasks under this component are: (1) production of an eight-page semi-annual newsletter; (2) publishing of occasional papers generated by the research and development team; and (3) organization (including procurement of speakers) for two annual conferences. Also, PRE staff and the contractor are to cooperate in establishing a strong and cordial relationship with other donor agencies and with the private sector in the U.S. and abroad. The FSDP contract statement of work calls for the contractor was "to actively participate in the development of this project into a center of excellence."

The following is a list of outputs to date under the dissemination of information component:

<i>Completion Date</i>	<i>Dissemination of Information Activities</i>	<i>Client</i>
02/89	Debt Equity Conference (Ivory Coast)	PRE/PD
03/89	A.I.D. and the Debt Crisis (Conference)	PRE/PD
11/89	Newsletter I	PRE/PD
02/90	Role of Business Regulation in an Era of Liberalized Financial Markets (Conference)	ANE
03/90	Financial Sector in Developing Countries (Conference) including Paper on Proceedings	PRE/PD
05/90	Regional Private Sector Officers Conferences (held in Amman and Bangkok)	ANE
05/90	INTRADOS Financial Markets Seminar (Algeria)	PRE/PD
06/90	USIS Conference on Promoting U.S./Thai Investment	Mission
07/90	Bolivia Privatization Seminar/Conference	Mission
08/90	Newsletter II	PRE/PD

As may be seen from the above listing, there has been wide variation in both the content and the substance of the conferences. The level of involvement and participation by both PRE and the contractor has also varied. For example, three of the above listed conference activities (Ivory Coast, Algeria and Thailand) involved the sending by the contractor of one participant to conferences which were organized by offices outside of FSDP, including USAID/OPIC/African Development Bank, INTRADOS, and USIS. Three other conferences (A.I.D. and the Debt Crisis, Role of Business Regulation and the Financial Sector in Developing Countries) were held in Washington, D.C. and involved A.I.D./W personnel only.

As indicated, FSDP was also involved in two regional conferences which were held in Amman, Jordan and Bangkok, Thailand. These conferences for Regional Private Sector Officers dealt with promoting trade and investment, improving financial markets and strengthening the enabling business environment. They were organized by the ANE Bureau and regional Missions who also supplied many of the papers. Direct involvement or participation by PRE and the contractor was limited to attendance by one senior PRE

officer and the presentation of one paper by the contractor at the Bangkok conference. Indications are that both of these conferences were successful in stimulating interest in and awareness of various programs and activities in the three subject areas on the part of private sector officers. The value of these workshops was emphasized in a point made by the Director of ANE's Private Sector Development Office who stated that "a central theme through the workshops was to increase substantially the exchange of information and ideas of alternate approaches to design, develop and implement the open markets project and program agenda."

The evaluation team reviewed copies of the two semi-annual newsletters that have been circulated to date and found them to be well prepared. Both newsletters contain brief notes on FSDP engagements along with an occasional paper on a particular aspect of the financial sector, drawn both from A.I.D./PRE and other donor agencies. Early in the life of the FSDP, much emphasis was placed on the proactive nature of FSDP activities in accordance with program objectives, and the newsletter may have been intended to transmit this information. For example, there were plans stated in the contractor's First Quarter Progress Report to develop criteria for selecting countries for financial sector assessments. Likewise the need was recognized for PRE and contractor personnel to pay visits to USAID Missions for the purpose of disseminating information and stimulating interest in financial sector development. In the Fourth Quarter Progress Report, it was stated that a marketing trip has been made to Central America and that "several additional marketing trips to specific regions/countries of focus" were planned. However, as time and circumstances have changed, the drive to carry out marketing activities under the FSDP appears to have diminished.

Both the project design documents and the contract refer to the hope for development of FSDP into "a center of excellence known for its quality of service." This would imply creating an entity that was aware of or involved in the total flow of A.I.D. activity in the financial sector development. This has not been the case. There are many other sources of funding for financial sector assistance and Missions can and have gone to the market on their own with RFP's, free to select an office or contractor other than PRE/PD or Price Waterhouse. In addition, Missions can tap other A.I.D./W sources, such as the IQC for macroeconomic services, for financial sector assistance.

5. General Project Effectiveness

The overall effectiveness of the FSDP may be judged primarily by the degree of success the contractor and PRE have achieved under the four major project components. The contractor's proposal envisioned "a clear integration of project activities at every phase of the project." The conclusion of the team is that while much quality work has been performed under the four components of the project, the FSDP as a whole has not achieved the coherence and effectiveness envisaged for it at the outset.

The team concludes that several factors are responsible for this outcome. Due to the financial arrangements (buy-ins), PRE and the contractor have not always been able to exert a critical influence on the selection and development of project activities. This was

the trade off for attempting to increase the interest and responsibility of the USAID Missions in the development of their country programs. The gap might have been bridged had this structural problem been identified at the initiation of the project and provision been made for a more intense education and marketing effort with the Missions.

The original project objectives of "conducting preliminary assessments and recommending the most suitable form of assistance within the context of specific countries" have been adjusted to accommodate the realities of a demand driven project. Because of the problems which have arisen in carrying out the project in the manner originally envisaged, A.I.D. has revised the project guidelines and modified the contract to eliminate the requirement for comprehensive strategic assessments, stating that "it is satisfactory to use sections of the (diagnostic) framework as appropriate." The evaluation team hopes that this modification will assist PRE and the contractor in fine tuning and targeting specific areas within the financial sectors of developing countries for FSDP activities.

Another factor has been the failure of the research program to develop as anticipated. Despite intense marketing efforts on the part of the contractor, there has been very limited interest within A.I.D./W or at the Mission level in financing research. "Missions are operation arms," we were told by the contractor, and "they (the Missions) don't want to finance research." As a result, the research program has had only a minor impact on other components of the project.

The project has been expanded in scope by its undertaking of studies for the privatization of non financial institutions and the financing of private power generation. The importance of these studies and associated conferences for the development of the financial sector does not appear to be large in spite of the significance of the subject matter.

Throughout this evaluation it was apparent that one of the principal shortcomings in execution of the FSDP was the limited marketing and promotion of project services by A.I.D./W and the contractor. The shortfall stems in part for start-up delays and in part from the project design which left USAID Missions with widely varying interests in control of project development. It was anticipated at project inception that countries would be targeted, that the diagnostic framework would be widely distributed, and that follow-up visits to USAIDs and assessments would be undertaken. At this juncture, with three years in the project remaining, a promotional effort is needed to take advantage of the experience and knowledge gained through the project with financial sector developments in many countries, as well as the increased awareness on the part of USAID Missions and host countries of the importance of the financial sector in mobilizing domestic resources.

The team urges PRE/PD to consider reallocating core funds budgeted for the research component and redirecting funds for the dissemination of information component into a more coherent dissemination, education, and promotion effort. Several specific actions as part of such an effort are suggested, as follows:

- (a) Target 15-20 countries/regions for an intense FSDP effort.

- (b) Produce a booklet that would include the diagnostic framework along with a revised version of the paper entitled Financial Markets Activities: Issues and Options which was prepared by the contractor for ANE and distributed to private sector officers prior to the ANE conferences in Amman and Bangkok.
- (c) Produce a separate booklet containing the first of the semi-annual FSDP Activity/Results reports that have been suggested to replace the Newsletter. The basis for this report already exists in the Summary Description of FSDP Engagements that makes up Appendix A of the FSDP Quarterly Report (October 31, 1990) recently submitted to PRE by the contractor. What needs to be added to these descriptions are brief commentaries on results and future activities. To the extent possible, information on other A.I.D. financial sector activities that are not part of the FSDP should be included in this experience/knowledge base.
- (d) Distribute the above two documents to all USAIDs, and particularly to USAID private sector officers.
- (e) Arrange for visits to the targeted countries by the PRE Project Director and a senior contractor representative with a broad knowledge of the financial sector. These visits by FSDP personnel could be of two to three days duration and would use the diagnostic framework to focus on gaps where FSDP services might effectively be employed. The joint visit would serve both educational and promotional purposes. With all parties present, the Mission would gain a better understanding of how to tap and utilize FSDP resources; A.I.D./W, in turn, would gain insights on country-specific financial sector development constraints and on ongoing USAID Mission assistance to the sector.

The 1991 Annual Work Plan which is currently under review ought to provide funding for such visits.

Another recurring observation by the evaluators is that there are a multiplicity of ongoing A.I.D. activities and programs that address problems of financial sector development that ought to be made part of an Agency-wide base and flow of experience and knowledge. Somewhere and somehow within the "center of excellence" concept, a method needs to be found to document and monitor on an Agency-wide basis all of these programs and activities dealing with the financial sector. Otherwise, cross-fertilization and stimulation potentials will be lost.

The above might best be accomplished internally within PRE, although it is doubtful that increasing direct-hire staff would be feasible at this time. The alternative would be to utilize FSDP core funding (perhaps part of the research component allocation) for the contractor to set up and monitor this suggested data and experience bank on financial sector activities. There is precedent within PRE for a contractor to perform this task in the recently released A.I.D./W Private Sector Project Handbook (the Grimsley Report) developed by Ernst and Young under the PEDS Project. The cooperation of USAID Missions in reporting on ongoing activities would be essential since, in the case of the FSDP, much of the activity takes place at the Mission level.

Establishing a data bank would have other longer-term benefits. The FSDP has shown limited evidence of having built upon the experience and lessons learned from the predecessor (FMDP) project. This shortfall could be overcome through a data bank which would provide a foundation for any Agency effort that might follow the FSDP.

C. EFFICIENCY

The suggestions outlined under the heading of General Project Effectiveness relate to new approaches to financial sector development which PRE might employ. Although a greater effort on the part of PRE and the contractor to promote a more coherent and interrelated use of the project resources would involve additional costs, these costs might be covered by the elimination or reduction in some activities. Elsewhere in this report, it is suggested that some reduction of expenditures in certain areas such as conferences, the newsletter, and research would provide adequate resources to launch a coordinated marketing and educational program. Such a program would have as its objectives the stimulation of interest on the part of the Missions involved in the FSDP and the development of assessment projects of the type envisaged for the strategic planning component.

The team received and noted adverse comments about PIO/T contract processing time within the Agency. While it might seem unnecessary that each task involving buy-ins under the prime FSDP contract requires a complete contract review, this is the case. After discussions and phone calls, the team concluded that the system is not easily correctable. Nonetheless the subject should be pursued by PRE in the hope that some time saving short cuts might be possible while allowing the contract office to carry out its responsibilities.

The team was told that an inordinate amount of the PRE Project Director's time is being spent on handling routine inquiries and paper processing tasks associated with PIO/Ts and buy-ins. As is pointed out elsewhere, one of the major weaknesses in the project has been the lack of adequate marketing/promotion work in the field. To correct this will require some reorganization of effort and associated measures to relieve the paperwork burden and free the Project Director for marketing and promotional activities. Given that other PRE offices managing similar "buy-in" projects are faced with the same problem, consideration should be given to centralizing the processing of PIO/T paperwork within PRE. At this juncture there appears to exist the classic case of an institution trying to accomplish important project objectives while being unable to allocate the needed effort and time to succeed in those areas due to administrative problems and overload.

The efficiency and effectiveness of FSDP could be substantially improved through more coordinated and directed planning efforts by PRE and the contractor. This interim evaluation provides an opportunity for both parties to sit down and chart out a productive and viable work plan for the project over its remaining three years. The team examined the first two Annual Work Plans and found them lacking in depth. Currently the Third Annual Work Plan is under discussion between PRE and the contractor, offering both parties the opportunity to more clearly chart the future development of FSDP priorities and ensuing activities.

D. IMPACT

The team was asked to respond to seven questions related to the impact of FSDP activities. The list which follows addresses all of the questions and several additional impact-related issues which the team believes to be important.

1. There is some evidence of successful utilization of project generated financial sector strategies and implementation plans by USAID Missions and host countries. The reasons for this limited endorsement vary from country to country. In the case of Jordan, external events have halted plans to go forward whereas in the case of Nicaragua, the final report has not been received. In Thailand, action recommendations are very recent and have not been acted upon. Likewise Pakistan is still reviewing the options.

In several countries, specific actions have been taken based upon the strategies recommended. For example, in Morocco two detailed studies (on stock exchange development and secondary debt market development) that were recommended as follow-on activities have been completed. In Honduras, the bankers' association acted on the recommendations and hired its first manager who initiated steps to formulate a strategy. In Lesotho, the findings have been used as the basis for discussion with banks and government which will most likely lead to a policy discussion and workshop later in 1990 or in early 1991. In Belize, the report's recommendation contributed to the Mission's decision not to proceed with a new credit project and, given limited resources, not to be involved in the financial or credit sector as part of its FY 91-95 CDSS strategy, except for phase-out support.

2. Generally, the conclusions and recommendations of the project consultants have been made available to the host country institutions. In most cases they have been well received. There are instances, however, where Missions have not circulated the reports to interested host country agencies and have used them only for internal purposes.

3. It is difficult to say whether there has been any beneficial utilization of the project's research component. The research papers have been circulated; however, such papers at best stimulate thought and comment but rarely achieve direct policy and operational results. Papers relating to guarantees of local currency bond issues for housing and municipalities appear to have been of use to some country Missions.

4. The team does not have evidence of widespread interest in or utilization of the semi-annual newsletter. The newsletter is professionally prepared but is not issued at frequent enough intervals to provide adequate coverage of financial sector development activities. The team is of the opinion that the newsletter or similar publications should include more information on developments in the financial sector which would provide USAID Missions with a ready reference to approaches used and lessons learned in other countries.

5. The conferences and speakers appear to have been successful in terms of the quality of the material presented. However, the value of the conferences as a technique for stimulating interest in financial sector reform in developing countries needs to be approached on a country-by-country basis, with input from both Mission and host country personnel. Although the team was not able to review participants' post-conference written

evaluations, based on discussions with those involved it appears that these conferences, especially the regional ones, have been successful in educating and enabling individuals to share their experiences in the financial sector with others interested in similar activities.

6. The team believes that FSDP activities could be strengthened through more contact between PRE and other donors. Based on discussions with individuals at PRE, the contractor, and donor agencies, the team found limited evidence of a coordinated program of cooperation and consultation with the international agencies located in Washington D.C. This is not to say that contact does not take place, as indeed it has in a number of specific instances; examples cited include coordination with the ADB in Manila, with the World Bank on a project in Guatemala, and with the IDB on a project in Nicaragua, and the meetings of the PRE Project Director with representatives of the InterAmerican Investment Corporation related to the regulation of equity markets in Latin America. Enhanced communications and exchanges of information with other donors, as well as with other offices and bureaus within A.I.D., would not only strengthen coordination of planned and ongoing financial sector development activities, but also help PRE learn from the successes and difficulties of related undertakings. While appreciating that much of the real coordination must take place in the field where the projects are implemented, the team feels it would be useful for PRE to also consult with other donors during the project planning phase to lay the groundwork for field coordination and avoid duplication of effort.

In the planning and selection of FSDP activities, more emphasis needs to be placed on determining A.I.D.'s comparative advantage and in identifying those areas where it can have maximum impact, acting in concert with other donors and policy proponents. For example, the need for interest rate rationalization and related issues are constantly being debated, and reforms are being urged, by the IMF and World Bank with various host governments. These organizations have the resources and program flexibility which together give them the muscle not always available to A.I.D. to influence policy directions. Greater effort ought therefore to be placed on collaboration between the FSDP and other donors and a more conscious effort made to work together. The FSDP may be in a better position to respond quickly to specific requirements for technical assistance services than the international and regional banks which typically provide such services only under major project or sector adjustment loans.

7. The team reserves judgment on the success or failure of the project's "center of excellence" concept. There has been insufficient time for the technical assistance activities completed in the first 21 months of the project to have had significant impact on the financial sector. The seeds planted to date, combined with three more years of opportunity, may yet earn the project its place as a "center of excellence."

It would seem at this juncture that the FSDP ought to be able to identify specific countries where the need, impact, and sustainability of project assistance are or will be greatest and where a concentrated effort is likely to produce significant results. It is a matter of applying a sustained level of technical assistance which over time will bring the desired results.

The above approach should not preclude or even diminish FSDP responsiveness to "free-standing" requests from Missions around the world for technical assistance such as has been provided over the last two years. However, circumstances would seem to dictate that a more intensive marketing and promotional effort ought to be carried out by both PRE and the contractor to ensure maximum impact from the next three years of effort and funding.

Attempts to enhance the potential impact of project resources ought also to recognize that there are varying degrees of sophistication within USAID Mission and host country organizations relative to financial sector matters. The current emphasis being placed by A.I.D. on the private sector as the engine for economic development does not necessarily mean that the Agency has personnel with appropriate background and experience at the Mission level or that Missions have experience at a policy/program level to fully integrate financial sector development with other Mission goals and priorities. Thus, a sustained effort under the FSDP to educate the Missions on issues of financial sector development should be viewed by A.I.D. as a long-term investment in education, strategy development, and country policy direction. With proper organization and targeting, PRE and the contractor both have the resources and talent to assist the USAID Missions to recognize and correct policy and programmatic weaknesses vis-a-vis the financial sector.

E. SUSTAINABILITY

The team believes there will be continuing positive effects arising from the individual studies and recommendations carried out under the FSDP. Virtually all of the measures proposed under FSDP studies would, when carried out, result in institutional changes in the host countries. Better supervision of banks, more efficiently functioning securities markets and new securities designed to attract domestic capital are a few examples of the results of work undertaken in this project. None of these necessarily requires further A.I.D. funding to reap the expected economic benefits. Clearly, related opportunities to advance the liberalization of financial markets will arise and at that time A.I.D. and other donors will have the option of providing further technical assistance. If FSDP activities result in recommendations which are followed up by the USAID Missions and, more importantly, are incorporated into the structure of a host country's financial sector, then the roots of sustainability will begin to grow and the fruit of these projects will ripen.

It is evident that longer-term assistance projects have a greater chance of making an impact upon countries' efforts towards sustained development. Although the FSDP has incorporated no major long-term projects under its umbrella of activities, there are instances where FSDP and/or FMDP activities have influenced the development of long-term financial projects. Examples include two projects, in Indonesia and Pakistan, which operate independent of the FSDP but were developed, at least in part, as a result of FSDP/FMDP studies.

Chapter III

CONCLUSIONS

This section presents the team's conclusions relating specifically to the four components of the FSDP and to the overall project. More detailed conclusions regarding project effectiveness, efficiency, and impact are to be found in sections of the report dealing with these issues.

Strategic Planning:

1. The diagnostic framework developed for the financial sector assessment has not been used to the extent that was anticipated. USAID Missions contacted had limited awareness of this document.
2. The diagnostic framework document contains only a brief one page statement of the purpose of the assessment, of A.I.D. policy, and of the use of the financial sector assessment as a tool for strategic planning. Given the importance attached to this document in the strategic planning component of the FSDP, the presentation of the diagnostic framework to the USAID Missions should be elaborated.
3. While strategy recommendations and action plans for implementation flowing from the financial sector assessments have been submitted by the contractor to USAID Missions and the PRE, these assessments have not been of the scale and scope originally envisioned. This result has been acknowledged by A.I.D. in a recent contract modification.
4. No provision for the marketing of the strategic planning component of the FSDP to the Missions was provided for in the project. At the same time, the power to finance and thus determine the focus and breadth of the assessment studies and related technical assistance was vested in the Missions through the "buy-in" mechanism. While the project design suggested there would be criteria for the selection of the assessment countries, in fact the selection process has been driven by Mission demand which has determined both the nature and scope of project activities.

Technical Assistance:

1. By focusing the FSDP more sharply on the needs and structures of a country's financial sector, it should be possible for the project to have a greater impact than it has had to date.
2. The project has shown its ability to meet the demands of the Missions and A.I.D./W in a competent and professional manner, thus fulfilling one of its objectives.

3. The scope of the project has been broadened by the inclusion of privatization studies without significantly contributing to achievement of the project's central objective of financial sector development.

Research:

1. The research component merits some rethinking. PRE has now had almost four years of experience with financial market activities and has seen FMDP and FSDP, along with other PRE activities and programs, evolve and take direction. Issues of financial sector development are now receiving increased attention and emphasis, worldwide. Given these realities, together with the experience of the past several years, it would seem that A.I.D./W and PRE should take the lead in defining areas to be addressed in a research agenda, while continuing to encourage generation of specific ideas from the field.
2. Given its remove from the main activity of the project and the uncertainty of the client's interest, it may be unrealistic to expect FMIRI to generate an acceptable research agenda and to provide direction to this component, in spite of its evident research capabilities. Missions are too oriented toward action and results to generate research topics or be willing to finance the type of research study envisioned for this component. As we have seen, FSDP is demand driven, especially with respect to the structuring of buy-ins.
3. The prime contractor appears to be most concerned with the strategic assessment and technical assistance components of the project whose services are in far greater demand among the Missions and A.I.D./W bureaus and offices.

Dissemination of Information:

1. Regional conferences or workshops are an effective way of disseminating information on developing and liberalizing the financial sector. They afford good opportunities for sharing of experiences and discussions of mutual problems.
2. The contractor is to be congratulated for putting together two very professional and informative newsletters. The newsletter could be made even more informative if it were to include a comprehensive listing and/or description of activities in financial sector development conducted by A.I.D. so that Mission officers could be kept abreast of studies on security markets, bank regulation and supervision, debt management, and the like. The detailed project descriptions used in the contractor's 4th quarterly report of FY 90 would be especially useful. Such a newsletter would not necessarily be more costly than the present version.
3. Another suggestion would be for the newsletter to include descriptions of related projects being implemented by other donor agencies. For example, the description in

Newsletter II of the role of IFC in financial markets development might have been enhanced by a discussion of several IFC projects. In particular, financial sector projects taking place in countries not participating in the FSDP should be included on a regular basis, since many of these have links with FSDP activities.

4. The project should strive to play a proactive role in financial sector development activities to enhance its chances of leaving a distinctive record of achievement.
5. The marketing of the project should be strengthened even at the cost of other elements. Mission staff change continuously, and the process of education can never end.

General:

1. Contacts and collaboration with other international donors should be strengthened wherever possible.
2. The process of preparing and agreeing on annual work plans offers the opportunity for A.I.D. and the contractor to strengthen the relationship between project execution and project goals while sharpening the project's focus.

Chapter IV

RECOMMENDATIONS

This section presents the team's recommendations relating to the four components of the FSDP and to the overall project. More detailed recommendations on measures to enhance project effectiveness, efficiency, and impact are provided in sections of the report dealing with these issues.

Strategic Planning:

1. The diagnostic framework document should be reviewed and its purposes should be more fully explained, drawing on World Bank, IFC, and other appropriate sources for material on the importance of the financial sector to the process of economic growth. This tool should be widely disseminated at the USAID Mission level, with appropriate follow-up on the part of PRE and contractor staff.
2. The substantial use that is being made of FSDP services by A.I.D./W bureaus and offices as well as by USAID Missions suggests that increased knowledge of the project will bring about increased demand for project services. PRE should review with the contractor how these services can be marketed to effect more concentrated and coordinated attacks on the strictures still existing in many countries' financial markets. Field visits by PRE and contractor staff to selected Missions would be an effective way to encourage greater use of the assessment concept, however modified. Regional workshops can also assist in increasing Mission level awareness and appropriate use of the assessment tool in understanding what is working and what is not working within the financial sector.

Technical Assistance:

1. PRE and the contractor should devote more time and resources to encouraging Missions to use the project's technical assistance services and to ensuring that the availability and objectives of these services are fully appreciated Mission-wide.
2. Care should be taken not to dilute the impact of FSDP resources by undertaking studies that are not directly related to issues of financial sector development. A.I.D. should avoid competition among its programs for a clearly defined project such as one involving privatization or the private ownership of power generating facilities.
3. Missions should be encouraged to stimulate host country interest and involvement in technical assistance projects pertaining to the financial sector, particularly during the design phase. This improves the chances of project recommendations being carried out.

Research:

1. Under the present set of circumstances, it seems clear that the expectations and intent of the project design relative to research are not being met. Several alternate courses are possible:
 - a. Divert some of the resources originally intended for research to other uses, such as a more aggressive marketing of FSDP services in the field. Although the project design and the contract make an allocation for a research component, the demand has not yet been evident nor has a clear agenda been established.
 - b. Centralize the establishment of the A.I.D. research agenda within PRE or some other office which would have responsibility for directing and monitoring its progress.

Dissemination of Information:

1. Increased emphasis should be placed on organizing regional or sub-regional workshops or seminars involving private sector officers as well as other interested Mission personnel. This should be done at the expense of conferences, if necessary.
2. In lieu of publishing a semi-annual newsletter, the contractor should be asked in consultation with PRE to design a less expensive vehicle which could be produced more frequently and be used to disseminate information on studies and other developments in the various segments of the financial sector. The material should encompass work done under both A.I.D. and international auspices.

General:

1. A more coherent marketing and promotional effort should be made, targeted primarily at the Mission level.
3. The Annual Work Plan for 1991 should be revised to sharpen its focus on project objectives and to provide for the recommended marketing effort.
3. A data bank should be established to gather and disseminate information on all A.I.D.-financed financial sector development programs, projects, and activities.
4. PRE should consider creating a support staff position to handle PIO/T and other administrative details in order to free the Project Director for more substantive activities.
5. Subject to existing budgetary limits, FSDP technical assistance services should be aimed towards longer-range assignments and/or toward assisting Missions with the conceptualization and planning of longer-range strategic and technical assistance activities.

6. **FSDP activities should be targeted at a selected group of countries showing absorptive capacity and receptivity for major FSDP interventions.**
7. **Given varying levels of experience and sophistication at the Mission level, greater emphasis should be placed on educating Mission personnel about financial sector development issues.**
8. **Contacts and collaboration with other donors should be expanded and efforts made to determine where A.I.D. has a comparative advantage in joint/overall financial sector activities.**

APPENDICES

APPENDIX A
CONTRACTOR SCOPE OF WORK

THE CONTRACTOR'S SCOPE OF WORK

4.1 Objective

The objective of this contract is to provide technical assistance through A.I.D. to developing countries to promote more efficient capital mobilization and allocation through improved strategic planning, regulatory policies and institutional reform, introduction of financial instruments and mechanisms, and information sharing.

4.2 Task Requirements

The Contractor shall provide professional services for a period of 60 months toward accomplishing the tasks described below. These services shall be funded by PRE at a level up to 308 person/months of effort. An additional level of effort of up to 880 person/months, subject to funding by the Missions, shall be provided by the Contractor as required.

4.3 Task Specific Assistance

4.3.1 Strategic Planning

1. Diagnostic framework and assessment

The Contractor shall design a diagnostic framework to be used by Missions to identify potential opportunities for financial development and regulatory reform in developing countries. This framework shall be submitted within four months from commencement of this contract.

Using that framework, the Contractor shall conduct assessments of approximately 10 countries who have expressed an interest in financial development assistance.

2. Strategy development

Based on the assessments described above, the contractor shall develop and recommend strategies for use by approximately 10 Missions in their financial sector development activities.

3. Strategy implementation

The Contractor shall make strategy recommendations and prepare a plan for implementation. This shall be a plan of action broken down into items that are practical and achievable by a specific USAID and/or host country during a reasonable period of time with the resources available. The plan shall be submitted to PRE and to USAID within two months from completion of the assessment. The purpose shall be to respond as effectively as possible to USAID requests and to plan future technical assistance in a manner consistent with country needs and resources available in the international donor community.

21

4.3.2 Technical Assistance

The Contractor shall provide technical assistance both long and short term in addition to that provided for other tasks in this scope of work. The Contractor shall be prepared to send teams to the field on four to six weeks notice with expertise in the following illustrative areas:

- a. Fiscal and monetary policy
- b. Financial sector regulations
- c. Financial intermediaries
- d. Education and training

(Note that this list is illustrative only and that other areas may be added as required.)

The technical assistance must be responsive to a wide array of concurrently placed demands for expertise in promoting efficient mobilization and allocation of capital through strategic planning, regulatory and institutional policy reform, introduction of financial instruments and mechanisms, and information sharing. The contractor shall be able to provide expertise in the identification, design, implementation and evaluation of A.I.D.-funded activities.

4.3.3 Research and Development

The Contractor shall procure the services of scholars and researchers who shall conduct original applied research regarding capital formation, private sector financial expansion and overall economic development in Third World countries. Suggested areas for research are:

- a. Using the financial system in economic stabilization
- b. Facilitating integration of regional and world financial markets.
- c. Mobilizing domestic savings
- d. Application of technical change to financial systems.
- e. Assessing and allocating risk to the financial system.
- f. Applicability of new financial instruments to developing country financial system.
- g. Lowering costs of financial intermediation.

(Note that this is not an exhaustive list of topics.)

4. This research and development activity shall generate approximately four occasional papers a year during 5 years, based on original research in topics and geographical areas selected in consultation with the contractor, the PRE Project Officer and at least two other professionals with expertise in the subject matter. The completed research, including literature review, methodology, data sources (if applicable), conclusions and suggestions for further research, shall be submitted in accordance to acceptable journal publication standards.

The team selected to perform this research shall be composed by members of academia with both theoretical background and broad experience in applied research in Finance, International Business and Economics, who will enrich this project with a scope and depth of knowledge beyond specific consulting task.

The Contractor and the research and development team shall exercise good judgement and creativity in suggesting innovative research projects. General but insightful suggestions shall be included in the contractor's proposal. Research specifics shall be discussed and agreed upon on an annual basis, or more often if necessary, starting no later than six months after commencement of the project.

The Contractor and appropriate researcher or team of researchers shall make an oral presentation to selected A.I.D. staff upon completion of each research project.

4.3.4. Dissemination of Information

The Contractor shall publish the following materials:

a) A semi-annual newsletter containing items regarding A.I.D. ongoing financial sector projects, as well as related news items about other international donor agencies. This newsletter shall be no longer than 8 pages and of comparable format and quality as a professional association newsletter.

b) Occasional papers generated by the research and development team. These papers shall be similar to a monograph under 100 pages long.

The Contractor shall organize and procure speakers for 2 conferences a year. It is estimated that attendance on average shall be 100 to 150 representative from USAIDs, AID, host countries and the private sector. The contractor shall include in its proposal a creative overall plan to conduct these meetings, the first of which shall be conducted in Washington D.C. during 1989.

The Contractor shall make every effort to cooperate with PRE staff in establishing a strong and cordial working relationship with other donor agencies, and the private sector in the US and in assisted countries.

The Contractor shall make recommendations for and actively participate in the development of this project into a center of excellence known for its quality of service.

Reports/Deliverables

1. Monthly activity reports summarizing the progress, problems and major accomplishments achieved in pursuing the tasks outlines in the Statement of Work included in Section C. Also included in this report should be a report similar to those shown in this Section F.1 B. and II.

2. Annual work plans developed in cooperation with PRE for the purpose of maintaining control over tasks and responsibilities during shorter periods of time than the span of the entire contract, as well as conducting periodic evaluations before the end of the contract. This procedure will allow PRE to continuously improve the project by correcting mistakes and identifying new opportunities of proposed activities, location, skills of the staff, scheduling, and budget (person months and dollars) by labor category and by cost line item.

3. Field Reports prepared within 30 days of the completion of field trips to any country. The Contractor shall propose a format or checklist to be followed uniformly in all reports, which will allow for comparison of developments between periods of time and between countries. A total of five copies of each report shall be submitted to the FSDP Project Officer.

4. Quarterly Reports summarizing the work accomplished to date, suggesting corrective action, and providing a comprehensive statement of the financial status of the project.

5. Delivery Order Report Requirements which will be specified, as required, in each Delivery Order.

6. Final Report summarizing activities undertaken, assessing the progress toward achievement of objectives under this contract, sharing knowledge acquired, and recommending future programs to benefit private sector development in A.I.D. countries. A draft of the final report shall be submitted six months before completion of the contract. This lead time will allow PRE to incorporate the Contractor's assessment of previous activities, along with the evaluation of independent consultants. The final report shall be submitted thirty days before completion of the project.

7. Other documentation relevant to this project such as communication between the Contractor and foreign organizations shall be forwarded to the FSDP Project Officer.

A summary of the specific tasks, as anticipated in the project design is as follows:

Person/Months:

	<u>PRE</u>	<u>Missions</u>
Strategic Planning	50	210
Technical Assistance	135	415
Research and Development	105	185
Dissemination of Information	<u>18</u>	<u>70</u>
Total:	308	880

16

APPENDIX B
EVALUATION SCOPE OF WORK

THE EVALUATION TEAM'S SCOPE OF WORK

The contractor shall conduct interviews and research designed to provide empirical finding to answer the questions listed below.

A. **Relevance.** Do the development constraints the project was designed to address remain major problems that are germane to the current development strategies supported by A.I.D. and pursued by PRE?

B. **Effectiveness.** Provide information to determine whether the project is making satisfactory progress toward achieving its stated goal.

1. **Strategic Planning Task**

a. Has a diagnostic framework for A.I.D Mission use in identifying potential opportunities for LDC financial development and regulatory reform been designed and used in the conduct of country assessments?

b. Have financial sector strategies been recommended to A.I.D Missions as a result of the foregoing country assessments?

c. Have implementation plans for the financial sector strategies recommended in 1.b. above been submitted to PRE and the cognizant A.I.D. Missions?

2. **Technical Assistance Task**

a. Have both long- and short-term technical assistance been provided in a timely fashion to the field in the key project areas of strategic planning, introduction of financial instruments and mechanisms, and information sharing, plus other areas as appropriate?

b. Has the contractor achieved a satisfactory match between assistance requested and consultant skills provided?

3. **Research and Development Task**

a. Has there been conducted original applied research regarding capital formation, private sector financial expansion, overall economic development in developing countries, or other areas as appropriate?

b. Have "occasional papers," based on original research, been produced and oral presentations made to A.I.D.?

4. **Dissemination of Information Task**

a. Does the contractor publish a semi-annual newsletter regarding financial sector activities and related news about other donor activities?

- b. Has the contractor organized conferences and secured speakers for them?
- c. Are strong and cordial working relationships with other donors and the private sectors in the U.S. and A.I.D. - assisted countries being established?
- d. Has there been progress toward the development of the project into a "center of excellence" for financial sector development in developing countries?

5. General Project Effectiveness

- a. Has it been possible to carry out the four main tasks listed above in a coherent and effective manner?
- b. What are the demand requirements for accomplishing each of the four above-cited tasks? Identify any additional resources needed to accomplish these tasks.
- c. Has there been effective collaboration between the PRE Bureau and the prime contractor to provide strategic guidance toward meeting the project goal as well as carrying out each of the project's main objectives?
- d. Are there problems associated with effective implementation of the project as an A.I.D./Washington activity, with its own goals and objectives, while also serving the needs of A.I.D. Missions and host countries?
- e. Has the contractor effectively and efficiently managed its contract responsibilities?
- f. What are the major obstacles to progress toward achieving the project's objectives?

C. Efficiency

- 1. Does the project integrate with other PRE activities and point to possible new areas for Bureau involvement?
- 2. Briefly describe alternate approaches and mechanisms for financial sector development which PRE might employ, and review their costs versus those under the project.

D. Impact

- 1. Is there evidence of successful utilization or adoption by A.I.D., its Missions and host countries of project-generated financial sector strategies and implementation plans?
- 2. Is there evidence of awareness and/or acceptance by host country institutions and A.I.D. Missions of conclusions reached and recommendations furnished by project consultants?

3. Is there evidence of interest in and beneficial utilization of outputs from the project's research and development component, including "occasional papers?"

4. Is there evidence of beneficial utilization of the contractor's semi-annual newsletter by A.I.D., its Missions, other entities?

5. Is there evidence that the conferences organized and speakers selected by the contractor have been successful in terms of impact on participants and host country institutions?

6. Is there evidence that PRE's working relationships with other donors and the U.S. and host country private sectors are successful or improving?

7. Is there evidence that the project "center of excellence" concept is being successfully advanced and well received?

E. Sustainability Is there evidence to suggest that the positive effects of the project are likely to be sustained after A.I.D. funding has ended?

APPENDIX C
LIST OF INDIVIDUALS CONTACTED

LIST OF INDIVIDUALS CONTACTED

A.I.D./PRE/PD Personnel:

Russ Anderson
David Cowles
Sandra Frydman
Ted Lee
Michael Newman
Michael Unger

Other A.I.D./W Personnel:

Bob Archer, ANE
Fred Kirchstein, PPC
Lance Marston, ANE
Dan Roberts, PRE/I
Gary Vaughn, ANE
Sean Walsh, PRE/H

USAID Mission Personnel:

Guillermo Bolanos, USAID Honduras
Lawrence Brown, USAID Egypt
Joseph Carroll, USAID Bolivia
James Dempsey, USAID Jordan
Dick Goldman, USAID Pakistan
Jim Grossman, USAID Thailand
David Jessee, USAID Nicaragua
Mark Kraczkiewicz, USAID Morocco
Barry MacDonald, USAID Jordan
Catherine McIntyre, USAID Lesotho
Peter Riley, USAID The Gambia
Art Villanueva, USAID Belize

Contractor (Price Waterhouse) Personnel:

Richard Breen
Barbara Friday
Leonard Horwitz
August Rimpel

Subcontractor Personnel:

Ted Barnhill, FMIRI
Steven Sharpe, Shearson Lehman Hutton
Roger Manivaring, Nathan Associates
Leveo Sanchez, Development Associates

APPENDIX D
LIST OF DOCUMENTS REVIEWED

**REVIEWED THE FOLLOWING
REPORTS PRODUCED FROM ASSESSMENTS, TECHNICAL ASSISTANCE,
CONFERENCES AND RESEARCH ACTIVITIES**

- Belize**
Financial Sector Survey, March 1989.
- Bolivia**
Privatization Strategy, June 1990.
- Egypt**
Equity Finance Facility, April 1989.
- The Gambia**
Stock Market Feasibility, April 1989.
- Honduras**
Bank Strengthening Program, December 1989.
- Jordan**
Financial Markets Development Strategy, January 1989.
- Lesotho**
Financial Intermediaries and Practices, March 1990.
- Morocco**
Financial Sector Reform, October 1989.
- Nicaragua**
Nicaragua Financial Sector Assessment, July 1990.
- Pakistan**
Capital Markets Assessment, June 1990.

Hab River Power Group Proposal Evaluation, April 1989.
- Thailand**
Financial Sector Strategic Assessment (Reconnaissance), February, 1990.

U.S.I.S. Conference Promoting US-Thai Investment, June 1990.
- Tunisia**
Venture Capital Feasibility Assessment, June 1990.
- Uganda**
Stock Exchange Development Feasibility, August 1990.
- West Bank/Gaza**
Credit Guarantee Facility Feasibility, March 1989.

Asia/Near East Bureau

Programming A.I.D. Financial Activities: Issues and Options, April 1990.

The Role of Business Regulation in an Era of Liberalized Financial Markets, February 1990.

PRE/Housing

Prefeasibility Study of an A.I.D. Guaranty of Local Currency Bond Issues by Municipal and Housing Authorities, October 1989.

Local Currency Bonds in Thailand, July 1990.

Municipal and Corporate Bonds in Chile, August, 1990.

PRE/Investments

Eastern Europe Financial Markets Study, August 1990.

Financial Analysis Training for Bankers and Borrowers, (Draft training manual prepared by Development Associates.), February 1990.

Feasibility for a Facility for Section 936 of the CBI Program, March 1990.

PRE/PD

Modernization of Regulatory and Supervisory Systems of LDC Financial Institutions, Research, November 1989.

A.I.D. and the Debt Crisis, March 1989.

Newsletter I, November 1989.

Newsletter II, August 1990.

The Financial Sector in Developing Countries, March 1990.

ROCAP

CABEI Strategic Plan, June 1989.

APPENDIX E
USAID MISSION QUESTIONNAIRES

45'

FSDP EVALUATION QUESTIONNAIRE

(Sent to Countries in which there was an assessment)

Checchi and Company Consulting/Louis Berger International have been contracted by A.I.D. to conduct an interim evaluation of the PRE/PD Financial Sector Development Project (FSDP), (940-0014). The FSDP contractor, Price Waterhouse (PW) may have already communicated with you in early October requesting your evaluation of their work. The Checchi/Berger Evaluation Team has had access to some Mission responses; however, we need an independent evaluation response from you. We urgently request your cooperation in completing the following brief questionnaire and returning it to us no later than November 2. Thank you very much in advance for this cooperation.

- 1) Price Waterhouse performed a Financial Sector Assessment in your country. This study was a major component under this project and the Evaluation Team is very eager to have your views on the assessment and other PW work in your country. In addition to returning the questionnaire, please anticipate a phone call the week of October 29th with more specific questions on the assessment.
 - a) Was the assessment initiated primarily by the Mission for its own needs or was there a strong host country interest in having the study and its recommendations?
 - b) Have actions been taken to carry out the recommendations and if not what were the barriers?
 - c) Do you believe studies of this breadth and scope are useful or are they duplicative or overlapping with studies done by others?

- 2) We have adopted a numerical rating system to facilitate your replies and to establish a degree of uniformity among USAID Missions. On a scale of 1 (least favorable) to 10 (most favorable) how would you rank the following aspects of the task performed for your Mission? Please feel free to append narrative comments to any numerical rating.
 - a) How would you rate PRE/PW in terms of making you aware of the services they can provide with respect to FSDP:
 - 1) financial sector assessments
 - 2) short- and long-term technical assistance
 - 3) research on specific topics
 - b) Did the Contractor adhere to the Scope of Work?
 - c) Did the Contractor provide a clear and practical implementation plan for Mission

- d) How would you rate the calibre and level of analysis upon which implementation plans were based?
 - e) What was the calibre of personnel provided as viewed by USAID;
as viewed by the host country?
 - f) How was the final report received by USAID;
by the host country?
 - g) How would you rate the time lapse between request for task and start up?
 - h) How would you rate the time lapse between start up and receipt of final report?
- 3) Has the Diagnostic Framework (developed by Price Waterhouse for financial sector assessment and distributed by PRE) been of use to the Mission?
- 4) What changes could be made within PRE/PW administration and/or funding of FSDP so that it would be more responsive to your needs?
-
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FSDP EVALUATION QUESTIONNAIRE

(Sent to Countries in which there has been no assessment)

Checchi and Company Consulting/Louis Berger International have been contracted by A.I.D. to conduct an interim evaluation of the PRE/PD Financial Sector Development Project (FSDP), (940-0014). The FSDP contractor, Price Waterhouse (PW) may have already communicated with you in early October requesting your evaluation of their work. The Checchi/Berger Evaluation Team has had access to some Mission responses; however, we need an independent evaluation response from you. We urgently request your cooperation in completing the following brief questionnaire and returning it to us no later than November 2. Thank you very much in advance for this cooperation.

- 1) (Country and project specific questions were asked which are unique to each Mission.)
- 2) We have adopted a numerical rating system to facilitate your replies and to establish a degree of uniformity among USAID Missions. On a scale of 1 (least favorable) to 10 (most favorable) how would you rank the following aspects of the task performed for your Mission? Please feel free to append narrative comments to any numerical rating.
 - a) How would you rate PRE/PW in terms of making you aware of the services they can provide with respect to FSDP:
 - 1) financial sector assessments
 - 2) short- and long-term technical assistance
 - 3) research on specific topics
 - b) Did the Contractor adhere to the Scope of Work?
 - c) Did the Contractor provide a clear and practical implementation plan for Mission
 - d) How would you rate the calibre and level of analysis upon which implementation plans were based?
 - e) What was the calibre of personnel provided as viewed by USAID;
as viewed by the host country?
 - f) How was the final report received by USAID;
by the host country?
 - g) How would you rate the time lapse between request for task and start up?
 - h) How would you rate the time lapse between start up and receipt of final report?

- 3) Has the Diagnostic Framework (developed by Price Waterhouse for financial sector assessment and distributed by PRE) been of use to the Mission?
- 4) What changes could be made within PRE/PW administration and/or funding of FSDP so that it would be more responsive to your needs?

APPENDIX F

SUMMARY DESCRIPTIONS OF FSDP ENGAGEMENTS TO DATE

SUMMARY DESCRIPTIONS OF ALL FSDP ENGAGEMENTS

- | <u>NO.</u> | <u>LOCATION</u> | <u>TITLE</u> |
|-------------------|-----------------------------------|--|
| 1. | <u>West Bank/
Gaza</u> | <u>Credit Guaranty Facility Feasibility Study</u> |

Given limited credit facilities available for Palestinian small and medium-sized enterprises, the Asia/Near East Bureau sponsored an FSDP consultant to assess the potential for a credit guarantee program in the West Bank/Gaza. The consultant interviewed twenty-five persons in banking, government, industry and private voluntary organizations and prepared a report which discussed economic and financial situations. The consultant found that the West Bank/Gaza's economy is constrained more by political and security realities than by economic ones. In particular, the report highlighted the continuing demand for short-term credit by small industries and merchants and concluded that the proposed USAID/Jordan loan guarantee program would have a high probability of success. This activity is complete and the final report was submitted in June, 1989.

- | | | |
|----|----------------------|--|
| 2. | <u>Jordan</u> | <u>Financial Markets Development Strategy</u> |
|----|----------------------|--|

An FSDP Team was contracted by USAID/Jordan to develop a comprehensive financial markets strategy that would identify constraints and recommend ways to overcome them.

The FSDP team offered approximately twenty recommendations aimed at assisting the Mission in the development of a full-scale financial sector development strategy. The strategy would aim to foster greater competition among banks and to help the Jordanian financial sector develop a wider variety of financial instruments. FSDP consultants emphasized the need for market forces to play a greater role in the Jordanian banking sector and the need for a shift in the role of the central bank. The team recommended that in order to facilitate greater competition among banks, USAID should encourage the modification of the role of the Central Bank from that of a prior approver of individual credits to that of a prudential regulator and supervisor. This activity is complete and the final report was submitted in May, 1989.

- | | | |
|----|----------------------|---------------------------------------|
| 3. | <u>Belize</u> | <u>Financial Sector Survey</u> |
|----|----------------------|---------------------------------------|

FSDP conducted a survey of the Belizian financial sector, at the request of USAID/Belize. The FSDP team found that commercial bank domination of the financial sector reduces

competition. The team also found the commercial banks to be deficient in their project analysis capabilities. The FSDP team identified possible areas for A.I.D. intervention, including policy dialogue, technical assistance and training programs to address these constraints. The team found USAID/Belize to be well positioned to play an active role in policy dialogue between donor organizations, Belizian financial institutions, and the government, and able to provide targeted assistance to selected financial institutions. This activity is complete and the final report was submitted in May, 1989.

4. Washington A.I.D. and the Debt Crisis Seminar

This seminar brought together a group of distinguished bankers and economists to exchange ideas with the A.I.D. Administrator and selected senior staff about the appropriate role for A.I.D. in contributing to the planning and execution of U.S. Government strategies to deal with the LDC debt crisis. Participants discussed the status of the crisis, alternative strategies and innovative approaches for alleviating the debt crisis. Among the specific program initiatives identified for A.I.D. were debt for development programs and technical assistance and training in financial sector development. This activity is complete and conference proceedings were compiled following the event.

5. Ivory Coast Debt/Equity Conference

A.I.D., in conjunction with OPIC and the African Development Bank, sponsored a workshop on debt conversion techniques in Abidjan. An FSDP consultant was contracted to present an overview of worldwide debt conversion trends and to provide an update on worldwide country debt conversion programs. The consultant focused on such factors as the current status of legislation and regulations, the types of debt conversion transactions executed, the volume of debt conversion transactions, and trading discounts. This activity has been completed.

6. The Gambia Stock Market Feasibility Study

FSDP was contracted by USAID/The Gambia to analyze the feasibility of establishing a stock market in the Gambia since the absence of an equities market was viewed as an obstacle to privatization. The FSDP consultants concluded that a stock market is presently not feasible for a number of reasons, including the small size of the country's economy, a lack of

investor demand for securities, and the limited number of enterprises that would be likely candidates for a public offering of securities.

The FSDP team recommended alternatives to the establishment of an organized trading exchange, and offered strategies aimed at creating the necessary pre-conditions for equities trading at a future date. For example, the Central Bank is targeted to work with commercial banks to "open a window" for information and trading of publicly owned shares. This engagement has been completed and the final report was submitted in May, 1989.

7. Pakistan Hab River Power Group Proposal Evaluation

At the request of the Government of Pakistan, USAID/Pakistan contracted FSDP to serve as an advisor to the government in analyzing a proposal by the Hab River Power Group to construct a private power plant. The FSDP team conducted contractual, financial and financial risk analyses of the proposal, and assisted the government throughout a series of negotiations which culminated in the signing of an Implementation Agreement and a Power Purchase Agreement.

Among the conclusions found in the extensive FSDP evaluation were: (1) the principle sources of financial risk are operational factors, such as working capital requirements; (2) the necessary capital can be raised, since offshore investors and Pakistani nationals view the project as an attractive investment; (3) the Pakistani financial system is sufficiently liquid to support the local debt financing requirements of the Hab River Power project and; (4) existing regulatory constraints inhibit efficient local capital markets operations and must be waived if capital is to be raised. Examples of such regulatory constraints include the method of setting the stock price of an initial offering, limitations placed on converting debt into equity, and underwriting restrictions placed in local financial institutions. This engagement has been completed and a draft final, considered as final by the Mission, was submitted in June, 1989.

8. Egypt Equity Finance Facility Feasibility Study

The first phase of this multi-phase activity was completed and a draft final report was prepared in June, 1989. For the first phase, an FSDP team assisted USAID/Cairo in designing a program to encourage domestic equity investment. The team conducted a survey of Government officials, business leaders

and other public and private sector figures to solicit their views and recommendations on the need for and feasibility of establishing an equity financing facility in Egypt.

The FSDP team found that (1) the Government's regulation and subsidization of industry have had an adverse effect on economic activity and competition, (2) the absence of private equity financing in the Egyptian private sector has resulted in the neglect of many investment opportunities in tourism, agricultural processing and small-scale industry and, (3) there is ample liquidity in the Egyptian financial sector to support private equity investment. The team concluded that USAID/Cairo could provide essential support to the equity financing process, assisting with the creation of a private intermediary institution to link equity financing proposals with Egyptian investors and with the creation of an investment pool to place and mobilize funds. This engagement remains active pending receipt from USAID/Cairo of requests for further assistance.

9. Central America CABEI Strategic Planning

FSDP was asked to assist CABEI with strategic planning and to advise ROCAP on a policy to guide its relations with the Bank. The consultant recommended that CABEI be used as a channel for loans to the private sector. The consultant also noted the important role CABEI could play to support Central America's development, particularly efforts at economic integration. Finally, the consultant recommended that CABEI undergo a significant strategic planning process, identify areas which account for low profitability and reform some elements of the Bank's management. This effort is complete and a final report was submitted in May, 1990.

10. Morocco Financial Sector Assessment

USAID/Morocco contracted FSDP to review the characteristics of the Moroccan financial system, evaluate recent changes and proposed reforms and recommend a program of technical assistance for financial sector reform. The team found that, in responding to the 1984 World Bank study of the financial sector, Moroccan authorities have achieved a return to real interest rates, a substantial reduction in the subsidy involved in Treasury borrowing and increased competition between commercial banks and public sector investment banks. Despite these advances, the team found the principal constraints to financial sector development to be insufficient use of market incentives and a high reliance on controls. The financial sector's most notable deficiency was identified as

the absence of a secondary debt market for short-term debt instruments. Another constraint was the ineffective functioning of the Stock Exchange.

The team recommended a four phase approach involving analyses of specific issues, an assessment of training needs, and the design and implementation of a training program. This engagement has been completed and the final report was submitted in March 1990. Two follow-on engagements have resulted from the consultants' recommendations including studies of the secondary debt market and of the stock exchange.

11. Morocco Stock Market Development

At the request of USAID/Rabat, an FSDP team was engaged to assist Morocco in developing the legal, regulatory, fiscal, and institutional environment needed for an effectively functioning equity market. The Government of Morocco is interested in strengthening the role of the Stock Exchange and has developed new accounting standards and has proposed amendments to current legislation regarding financial disclosure, taxation of capital gains and dividends, and the regulation of the Stock Exchange.

The team found that the Casablanca Stock Exchange is not operating at full capacity and privatization was identified as key to the growth and development of the Exchange. The team recommended that government control over operations be transferred to the private sector and that government limit its role to a regulatory capacity. The team further suggested that the proposed draft laws and regulations be strengthened to more effectively support information disclosure and discourage fraudulent behavior. The consultancy took place during September and October, 1990 and the team is currently preparing a draft final reports in English and French.

12. Washington Newsletter I. FSDP Update

The first issue of the semi-annual newsletter, FSDP Update, was completed and published in November 1989. The newsletter included background information on FSDP goals and activities, reports on A.I.D. projects in Senegal and Indonesia, and information about the activities of other donor agencies.

13. Washington Modernization of Regulation and Supervision of LDC Financial Institutions

FSDP prepared a major research study on the modernization of developing country systems of prudential regulation and supervision of financial institutions. This is a crucial area for financial sector development, because in the absence of adequate regulatory and supervisory systems, financial sector liberalization can lead to instability. The FSDP study defined the basic principles and essential requirements that should govern modernization of developing country systems of prudential regulation and supervision, and highlighted some of the areas best suited for technical assistance.

Areas identified by FSDP for A.I.D. technical assistance include: creation of effective legislative and regulatory frameworks for financial supervision; development of specific legislation that deals with problem and/or insolvent institutions; development of accounting standards and forms for prudential reporting; design of an off-site examination program; strengthening of the role of external auditors; training of supervisory staff; and establishment of credit risk bureaus. This activity is complete and the final report was submitted in February 1990.

15. Washington PRE/I Training, RFP Analysis

In order to conduct a series of training workshops on financial analysis techniques, the Financial Sector Development Project was requested to conduct a proposal solicitation, evaluate the responses, negotiate with the top-ranking firm and prepare a subcontract. This activity is complete.

16. Honduras Bank Strengthening Program

USAID/Honduras has engaged FSDP in a multi-phased effort to strengthen the Honduran banking sector. To this end, FSDP teams have worked closely with the Mission and with the Honduran Bankers' Association, AHIBA. To date, the following assistance has been provided:

o A former commercial banker with Latin American extensive experience was fielded in November 1989 to meet with the commercial banking community and the management of AHIBA in order to assess AHIBA's needs and recommend a program of assistance. A report outlining AHIBA's basic training requirements was prepared and submitted in final form in March 1990.

o In December 1989, an FSDP consultant with expertise in Library Science assessed the library holdings of the Central Bank and AHIBA, and the needs of the banking community. He recommended a program to expand the Central Bank Library System beyond Tegucigalpa and San Pedro Sula, proposed a Banking Documentation Center, and recommended that the Central Bank and AHIBA plan to issue and disseminate banking publications. This study was submitted in March 1990.

o Building on previous technical assistance, USAID/Honduras requested a consultant to assist AHIBA in developing strategic, management, and operating plans. The consultant met with AHIBA and USAID officers during August 1990. He reviewed AHIBA's by-laws, and assisted the organization develop a business plan, a management plan and an operating budget. A draft final report was submitted in September 1990 (both Spanish and English versions) and Price Waterhouse is awaiting comments from the Mission prior to preparing the final report.

o USAID/Honduras has asked Price Waterhouse Washington to assist AHIBA in the development of its bank training program. A curriculum design specialist, librarian, financial analyst and financial sector specialist are being recruited for this engagement, which will take place the end of 1990 and the beginning of 1991.

o In an effort to establish a Credit Reference Bureau, USAID/Honduras has requested a credit collection specialist to assist in the development of a Credit Bureau for use by AHIBA member banks. Price Waterhouse is currently recruiting consultants for this engagement.

17.

US, Pakistan, Chile Forging Greater Integration and Internationalization of Financial Markets

FSDP has undertaken a major study of ways to forging stronger linkages between financial markets in developing and developed countries. This three-phased research project is designed to develop a policy analysis framework which will be useful to A.I.D. and host country governments in achieving greater integration and internationalization of their financial sectors. The three phases include 1) a literature review, 2) case studies to evaluate developing countries' experiences in gaining access to international capital markets and in attracting foreign investment, and 3) a comprehensive analysis of findings. To date, the first two phases have been completed. A literature review was submitted in March 1990 and draft final case studies for Chile and Pakistan were submitted in October 1990

The gradual but sure emergence of the stock market was cited as a positive sign of Chile's economic well-being. Both the privatization process as well as the presence of foreign institutions among financial intermediaries in Santiago also reinforce the impression that the Chilean Stock Market is poised for impressive growth. The Chilean experience has shown that in order for financial liberalization to be effective, it must be followed through completely. Even considering the set-backs that Chile has encountered, the researchers found that a decade and a half of financial liberalization has been beneficial for the Chilean economy and that many of the omissions of the first round of liberalization (in the late 1970s and early 1980s) have been rectified, creating an environment conducive to economic growth, political stability and social welfare.

In the case of Pakistan, the researchers found the process of financial integration and internationalization to be uneven at best. The country's emerging equity market is weak, and there is no viable long-term bond market. Financial integration with the international market is limited, and is primarily dependent on official bilateral and multilateral sources of foreign funds. Foreign private banks, on the other hand, have been reasonably successful in penetrating the local Pakistani market. The researchers noted that there have been various movements in recent years to strengthen the process of integration and internationalization, including the issuing of licenses for foreign investment and joint ventures.

A final report synthesizing the project's overall findings will be submitted in November 1990.

18. Washington Prefeasibility Study of an A.I.D. Guaranty of Local Currency Bond Issues by Municipal and Housing Authorities

FSDP was sponsored by PRE's Office of Housing to study the feasibility of offering A.I.D. guarantees for local currency municipal bond issues. Due to a decline in multilateral and bilateral aid, municipalities in many developing countries are seeking alternative means of financing, including local currency bond issues. FSDP research concluded that A.I.D. guarantees could help stimulate local bond markets, and would accomplish several A.I.D. policy objectives, including: stimulating capital markets development, reversing capital flight by offering alternatives for investment, encouraging decentralization through the strengthening of local governments, and stimulating administrative and fiscal reform by local governments.

The FSDP report suggested, for example, that bonds could be issued for housing, infrastructure and industrial development. In addition, it was suggested that initial projects be kept straightforward and that local investors assume some of the risk. The report also advised that A.I.D. technical assistance focus on specific areas, including administrative and fiscal reform of municipal governments. The final report was submitted in February 1989. As a result of this study, case studies have been undertaken in Thailand (Activity 36) and Chile (Activity 42).

19. US, Thailand, Private Power and Capital Market
Philippines Development

Building on knowledge gained through experience with the Hab River Power Project, FSDP has conducted research on the potential for private financing of major power projects. Case studies have been undertaken in the Philippines and in Thailand.

In the case of the Philippines, researchers found that energy demand is estimated to grow by 4.5 percent for the next five years, however the power supply shortage represents a real constraint to economic growth. Private enterprise can participate effectively in the formulation, construction, operation, and maintenance of infrastructure facilities under private ownership and financing. Despite the limitations of Philippine financial institutions and markets, the researchers cited the potential for raising local currency funds although they also noted the complexity and time consuming nature of the process.

Researchers found that in Thailand local markets have the capacity to finance individual large projects costing hundreds of millions of dollars. However, they do not have the capacity to finance all needed investments throughout the economy. Development of the debt market would provide a needed source of long-term financing and the researchers noted that both local and international banks seem eager to help develop a secondary market for debt securities.

Draft finals for both case studies were submitted in October 1990 and the final report, synthesizing all project elements, will be submitted in November 1990.

20. Indonesia Stock Market Regulation and Operation

FSDP is working with the Government of Indonesia to strengthen stock market supervision, regulation and operations in order to accommodate significantly increased activity on the capital markets. FSDP advisors recommended a new regulatory regime for the stock market, the brokerage industry, underwriters, and other supporting professions. The recommendations touched upon a broad range of key issues, including fair play and disclosure requirements in registration statements, codes of practice and conduct, and new accounting rules to ensure accuracy in reporting. FSDP has been working closely with the Mission and the GOI to assist in drafting a capital markets regulatory decree, in making the stock exchange a private body, and in reviewing the training needs of the capital market executive agency (Indonesia's SEC).

21. Washington Financial Analysis Training

FSDP contracted Development Associates (DA) to prepare and deliver training workshops to credit officers and small businessmen in USAID host countries. DA was to deliver up to ten five-day workshops over a nine month period in selected countries. A draft training manual was prepared and submitted to AID and a preview workshop was held. There was no further activity requested and the activity ended upon the termination date of the subcontract.

22. Washington The Role of Business Regulation in an Era of Liberalized Financial Markets Seminar

At the request of the Bureau for Asia and the Near East, FSDP sponsored a one-day seminar entitled "The Role of Business Regulation in an Era of Liberalized Financial Markets." Held in Washington, D.C. on February 23, 1990, the seminar briefed representatives of ANE and other A.I.D. Bureaus on the role of properly conceived regulation, particularly with regard to the private provision of public services. The workshop also focused on A.I.D.'s role in providing assistance in regulatory affairs. Financial markets specialists from Price Waterhouse, led four sessions on the globalization of financial markets, banking regulation, capital market regulation, and utility regulation. The ANE Bureau was very pleased with the seminar, and felt that it had been effective in increasing awareness of the importance of financial sector regulation. A conference report was submitted to AID in February 1990.

23. Washington The Financial Sector in Developing Countries - Issues for the 1990s, Conference

On behalf of the Bureau for Private Enterprise, FSDP organized a two-day conference on key financial sector issues. Participants included A.I.D. representatives, academics, private and public sector figures, and financial sector practitioners from A.I.D. countries. Held in Washington, D.C. in March 1990, the conference aimed to exchange information on financial sector development and to explore A.I.D.'s role in this process.

The conference focused around three major themes: the policy framework for financial sector liberalization, the strengthening of financial institutions, and the development of capital markets. Dr. Malcolm Gillis, conference chairman emphasized the internationalization and globalization of finance, the importance of a well-trained work force, and the instrumental role that accounting standards and financial regulation must play in financial sector development. Dr. Gillis saw a potential role for A.I.D. in training and education, in the provision of financial expertise, and in donor coordination. The final version of the Conference Report was submitted to A.I.D. in June 1990.

24. Thailand Financial Sector Strategic Assessment

USAID/Thailand requested an FSDP team to conduct a reconnaissance of the Thai Financial System, with the aim of assisting USAID/Thailand to develop a long-term financial markets strategy. The FSDP team developed a set of preliminary recommendations on areas suited for A.I.D. interventions. These measures include: expanding the equity market by increasing the number of companies listed on the Thai Securities Exchange, improving the quality of financial information by establishing a Thai Chartered Financial Analysts program, and mobilizing national savings through the organization of a national savings program. The team advised that its recommendations be supported by detailed research before an actual portfolio of projects is launched. FSDP also recommended that a financial markets conference be organized to explore ways in which Thailand could improve the efficiency of its financial markets and establish itself as a regional financial center. This activity is complete and a final report was submitted in April 1990.

25. Guatemala Central Bank Strengthening

USAID/Guatemala requested assistance from FSDP to assist the Central Bank in modifying instruments and regulations needed for a liberalized financial system. The activity was canceled following changes in Central Bank priorities.

26. Lesotho Financial Intermediaries in Lesotho: Implications for the Agricultural Sector

An FSDP consultant was sponsored by USAID/Lesotho to analyze the structure of the country's economy and financial markets, as part of a multidisciplinary project that studied agricultural sector development. The consultant focused on constraints caused by the dependence of Lesotho's economy on that of the Republic of South Africa, since this dependence affects the formulation and execution of fiscal and monetary policies.

The consultant recommended a number of measures which Lesotho's monetary authorities could undertake to facilitate the provision of credit for agricultural activities. The recommendations included: introducing graduated payment obligations or tailoring loan repayments to borrowers' capabilities, instituting re-financing arrangements, and establishing tax incentives to encourage lenders to obligate longer-term funds to certain types of agricultural activities. This activity is complete and the final report was submitted in June 1990.

27. Caribbean Feasibility Study for a Guaranty Facility for Section 936 of the CBI Program

The passage of Section 936 of the IRS Code made approximately \$14 billion in earnings of U.S. companies in Puerto Rico available for medium and long-term financing of private sector projects in the Caribbean Basin. However, only seven projects have been funded under this program since its inception--a number far below anticipated levels.

FSDP was contracted by PRE's Investment Office (PRE/I) to identify constraints on the use of 936 funds, to assess the viability of a 50% A.I.D. guarantee program for increasing the flow of funds, and to recommend a workable guarantee structure. The team found that the 50% guarantee proposed by PRE/I's Private Sector Revolving Fund is not attractive to U.S. commercial and investment banks in Puerto Rico since they require a full (100%) guarantee for risks associated with Section 936 loans. The report recommended several approaches that PRE/I should follow if it wishes to pursue the

development of a guarantee facility on this basis. These recommendations include full guarantees for projects between \$1 million and \$3 million in size and limited guarantee coverage to projects generating foreign exchange or having access to export earnings in off-shore accounts. This activity is complete and the final report was submitted in June 1990.

28. Washington Programming A.I.D. Financial Markets
Activities: Issues and Options for ANE

This FSDP assignment outlined specific activities or programs that A.I.D.'s Asia/Near East/Europe (ANE) Bureau could support to promote financial markets development. The report was designed to stimulate discussion at ANE private sector conferences held in Jordan and Thailand in May 1990; it provided practical interventions that A.I.D. could undertake in the area of financial sector development. Some of the options presented include: the drafting or revision of securities laws and regulations, the development of audit and accounting standards, support for improved bank regulation and supervision, and the development of mutual funds and contractual savings institutions (insurance companies and pension plans). This activity is complete and the report submitted in April 1990, was used as the basis for discussion at the May meetings.

29. Washington Newsletter II, FSDP Update

The second issue of FSDP Update was prepared and distributed to A.I.D. Mission and Bureau personnel in July 1990. The newsletter contains articles covering the ANE Seminar, the FSDP Conference, modernization of regulation and supervision of LDC financial institutions, the status of FSDP Research, the IFC Capital Markets Division, as well as updated information about recent FSDP projects.

30. Worldwide Bank Analysis for PRE/I

FSDP has assisted the PRE/Investment Office in evaluating Loan Portfolio Guarantee (LPG) applications. An FSDP consultant has provided qualitative and quantitative analyses of applications by private banks in Africa and Latin America for the LPG program. The consultant evaluated the asset quality, capital adequacy, profitability, and liquidity of applicant financial institutions in order to assess the credit risk to A.I.D. for including these institutions in the LPG program.

The existing evaluation model was also reviewed by the FSDP consultant, and changes necessary to use the model for evaluation of leasing companies, instead of banking institutions, were recommended. Project deliverables for this engagement have been submitted directly to PRE/I.

31. Thailand and Jordan ANE Private Sector Officer Conferences

The FSDP Deputy Director attended Private Sector Officer Conferences held in Thailand and Jordan. The consultant discussed and explained the many ways in which FSDP could provide assistance to USAIDs in the ANE region to foster stronger private and financial sectors in those developing countries. This activity is complete.

32. Washington INTRADOS Financial Markets Seminar (Algeria)

Under FSDP sponsorship, two Algerian central bankers attended an Intradoss Seminar entitled "Building Effective Financial Markets." Attendance at this seminar was important for the Algerian government's current program of reforming the Algerian economy. This activity is complete.

33. Bolivia Privatization Strategy

At the request of USAID/Bolivia, FSDP assisted the Government of Bolivia in defining a privatization strategy including an analysis of potential financing options for privatization. FSDP performance on this task has received the highest praise from the USAID/Bolivia Mission Director and Private Sector Officer. The team held numerous discussions with key Ministers (Finance, Planning, Industry, and Commerce), the Economic Advisor to the President, Congressional leaders, private sector executives, and members of the opposition. These meetings served as input for the strategy design, and were an important opportunity to initiate the consensus building process. This project attracted a great deal of media attention in Bolivia, with the team's activities being widely and favorably covered by both the print and electronic media.

A final report was submitted in English and Spanish in September of 1990. The report includes an outline of the key components of a successful privatization strategy and guidelines for the drafting of a privatization law. The team included FSDP Project Director, J. Richard Breen; Auguste Rimpel, Price Waterhouse's Director for International Consulting Services; Richard Downer, a Price Waterhouse

partner who has served as privatization advisor to former Prime Minister Seaga in Jamaica; Steven Sharpe, a Vice President at Lehman Brothers (formerly Shearson, Lehman, Hutton); and Jeanne Balcom of Price Waterhouse/Washington.

34. Tunisia Venture Capital Feasibility

An FSDP team assessed the feasibility of venture capital and other non-asset based lending mechanisms in Tunisia. The purpose of such mechanisms would be to encourage the start up or expansion of viable private enterprises in Tunisia. The team met with private and public sector leaders to determine whether USAID resources could be used effectively to support the venture capital process in Tunisia. In addition, the team examined ways to promote more Tunisian-American commercial joint ventures. The team concluded that USAID/Tunis should not use its resources to establish a new venture capital facility at this time, but that well-placed assistance to indigenous venture capital efforts could be very effective. A draft final report was submitted in July 1990 and will be finalized upon receipt of comments from A.I.D.

35. Pakistan Capital Markets Assessment

FSDP fielded a consulting team to Pakistan to conduct a Capital Markets Study. The FSDP team was to identify those areas for USAID technical assistance over the next several years. The FSDP team recommended, inter alia, the liberalization of the interest rate structure, technical assistance to support the development of a private life insurance industry, and promotion of increased competition among financial institutions. Additionally, the FSDP team highlighted a number of activities in which USAID assistance would produce the greatest rewards and benefits in strengthening the capital markets in the near future. A draft final was submitted in August 1990 and the final report, incorporating mission comments, is underway as of this writing.

36. Thailand Local Currency Bonds Case Study

As a follow-on to FSDP research on the feasibility of A.I.D. guarantees of local currency bond issues by municipal and housing authorities, completed in February 1990, an FSDP team recently conducted a case study in Thailand. The objective of this study was to analyze the feasibility of raising long-term local currency debt in Thailand to finance public infrastructure and private corporate investment. The team, comprised of Steven Sharpe, a Vice President from

Lehman Brothers, and a Housing Finance Specialist, studied local currency bonds and other financial instruments issued in the Thai capital market for the purpose of infrastructure, housing, and corporate investment. The draft final report was prepared and submitted in August 1990. It concluded that with the appropriate policy, legal, and regulatory changes, a medium- to long-term debt market could be developed in Thailand over the next three to five years and that the opportunity exists to utilize A.I.D. local currency guarantees as an instrument to support the mobilization and use of local currency borrowing for development.

37. Thailand Promoting US-Thai Investment USIS Conference

As part of an effort to forge greater linkages between the U.S. and Thai business communities, an FSDP consultant participated in the USIS conference "Financial Globalization and Thai-U.S. Investment Relations." In addition, the consultant met with business leaders in Bangkok and assisted USAID in developing a strategy to strengthen ties with the private sector.

One of the most relevant issues raised at the USIS conference was access to the Thai financial market by foreign firms. The consultant noted that the absence of a Thai-U.S. tax treaty is a serious handicap for improved private sector ties. Although there were many reservations expressed about opening Thai markets to foreign firms, there was enthusiasm over a USAID effort in the area of legal and regulatory reform. A draft final report was submitted in August 1990.

38. Uganda Stock Exchange Development Feasibility

The Financial Sector Development Project was contracted to assist the Kampala Stock Exchange. The private Kampala Stock Exchange has recently been established by a local group which includes the Governor of the Central Bank, and this initiative has been approved by the President of Uganda. The FSDP consultant identified areas of possible assistance which USAID/Kampala could provide to promote the stock exchange. The consultant recommended that primary emphasis should be on securities industry education adapted to local needs and conditions. A draft final was submitted in September 1990.

39. Washington Eastern Europe Financial Markets Studies

FSDP consultants have prepared two research studies regarding financial markets and institutions in Eastern Europe. In both cases, the research was conducted in Washington and the methodology included extensive telephone interviews within the U.S., to the U.K. and to Western and Eastern Europe.

The first study, entitled Eastern Europe Financial Markets aimed to broadly define the state of financial sectors in Poland, Hungary and Czechoslovakia. The study was designed to assist PRE/I in determining the utility of the Loan Portfolio Guarantee (LPG) Program in mobilizing medium- and long-term financing for small and medium size enterprises in Eastern Europe. A draft final was submitted in August 1990.

A second study, Eastern Europe Financial Sector Development Study, provided a descriptive list of bilateral, regional and multilateral donor agency activities in Eastern Europe. Financial Sector support programs of the World Bank, IFC, IMF, European Economic Commission, the British Know How Fund, and several German Financial institutions were reviewed. A draft final was submitted in October 1990.

40. Nicaragua Financial Sector Reform

A four-member consulting team was fielded to Managua to devise a strategic plan for Nicaraguan financial sector reform. The team met with Nicaraguan ministerial and Central Bank officials, international financial institution advisors, high level officials from the four remaining commercial banks in Nicaragua and private sector representatives. In addition, the team met with members of the Nicaraguan banking community residing in Miami to assess the community's willingness to return to Nicaragua. The team found that among the problems that need to be addressed, the most pressing are: macroeconomic stabilization, assistance to the Central Bank in building its accounting and auditing capabilities, restructuring of the financial regulatory framework, and allowance for the formation of non-bank intermediaries. The team acknowledged that additional technical assistance would be needed to resolve the aforementioned problems. Upon its return to Washington, the team met with officials at AID/Washington to discuss the possibility of financial sector reform. PRE, LAC and State Department officials attended the Washington debriefing which concluded with a question/answer session.

A draft final was submitted in August 1990 and a final report is under preparation, incorporating Mission comments.

41. Bolivia Privatization Seminars and Conference

FSDP is assisting USAID/Bolivia and the Bolivian private sector in planning, organizing, and managing a seminar and a conference on the privatization process. Both events are key components of Bolivia's privatization strategy and aim to increase public support for the initiative.

The seminar took place in October 1990. FSDP organized a closed-door meeting to work at the technical level with senior government officials on the implementation of privatization program. The seminar was chaired by the Minister of Planning, and included the participation of the Mayor of La Paz, the President of the Chamber of Deputies in the Senate, the President of the Economic Commission in the Senate, and a team of Price Waterhouse privatization advisors. Presentations were made by Maria Julia Alsogaray, an Argentine senator responsible for telephone system privatization in Argentina, and Ellis Juan, Vice Minister of the Investment Fund responsible for implementing privatization in Venezuela. The discussion at this seminar resulted in consensus among the Bolivian leadership on how to proceed with privatization and culminated with a briefing to the President of Bolivia.

A privatization conference, aimed for a much wider audience, is currently in the planning stages. The theme of the conference "Privatization and Economic Reactivation" and it is scheduled for November 19, 1990. This conference is designed to increase public awareness of the benefits of privatization to economic growth and to build public support for the process. Approximately 350 participants are expected to attend; presentations will be made by an international group of experts, many from Latin America, with first-hand experience in the privatization process.

42. Chile Local Currency Bonds Case Study

An FSDP team recently concluded a pre-feasibility study of A.I.D.-guaranteed local currency Chilean bond issues. The team was very encouraged by the prospects for A.I.D. to participate in the development of a Chilean bond market. The consultants noted a large and rapidly growing pool of long-term domestic savings in the Chilean financial markets. The potential for success is even further enhanced by the balanced legal and regulatory framework. The team noted that a "culture" of responsible financial and economic management has been successfully implanted in Chile, including low and stable inflation rates, high levels of growth, and growing levels of both domestic and foreign investment. The team concluded that the experience in Chile could provide the model for other

countries where A.I.D. is assisting in developing financial markets. A draft final report was submitted to A.I.D. in October 1990.

43. Bolivia Financial Sector Assessment

At the request of USAID/Bolivia, FSDP performed a financial sector assessment. A senior level, multidisciplinary and international team examined the Bolivian financial system and the financing needs of the private productive sectors. The assessment identified and analyzed constraints and proposed interventions to rectify them. The team's principal findings were that after four years of sound economic policy the financial system is still fragile but is gaining strength. The banking system remains weak and as yet is unable to play a strong role in development finance. Key recommendations in this area are to: "modernize" the banking law; strengthen bank regulation and supervision; strengthen the Central Bank's capacity to manage the financial system properly; establish a restructuring fund to aid regulators to deal with crucial issues of bank restructuring; and establish a small saver guaranty fund. As of this writing, the draft final report is being prepared.

44. ANE Regional Financial Markets

FSDP has been requested by ANE, now ENE, to provide ongoing assistance in training and studies on financial markets. Among the types of activities scheduled are: financial sector assessments, modernization of regulatory and supervisory systems, capital markets development, and financial institutions development/restructuring.

45. Morocco Secondary Debt Market

At the request of USAID/Rabat, an FSDP team was engaged to assist Morocco in assessing the feasibility of developing a secondary debt market. The team was to analyze the conditions under which a secondary debt market could successfully function and develop an action plan for its creation.

The team found the financial system to be overly reliant on the Central Bank and insufficiently driven by market forces. For example, they found that when the commercial banks need liquidity, they tend to borrow primarily from the Central Bank and, to a lesser extent, in the interbank market. The development of a secondary market in short-term debt instruments would allow banks to adjust their liquidity positions without borrowing from the Central Bank. In

addition, it would provide a vehicle for the monetary authorities to influence both the banks' willingness to extend credit and the general structure of interest rates through the use of open market operations. The creation of a secondary market would further assist in establishing a market-based reference rate against which all other rates could be measured.

As an initial step, the team recommended that a secondary, market for short-term Treasury bills of 3, 6, and 12 months maturity be created in Morocco in 1991. Trading in other products such as commercial paper of bankers acceptances, might be considered in a later phase of market development. Preliminary draft reports were prepared in English and French and submitted to USAID/Rabat for comment.

46. Tunisia Financial Sector Assessment

At the request of USAID/Tunis, a four person team has been fielded to assess the Tunisian financial sector. The team is to examine the structure and characteristics of financial institutions, instruments, and the regulatory environment. The team will examine both money and capital markets. Based on their constraints analysis, the team will develop a strategy for USAID assistance targetted to overcome barriers to financial sector development.

As of this writing the team is in the field. Reports will be prepared in both English and French.

47. Ivory Coast La Financiere Portfolio Analysis

AFR/MDI contracted FSDP to conduct a portfolio analysis of a holding company, La Financiere, in the Ivory Coast. FSDP evaluated the current worth of the companies in which La Financiere holds equity in order to facilitate pricing of future share certificates. The FSDP team, composed of two chartered accountants from Price Waterhouse Abidjan and a financial markets analyst from Price Waterhouse Washington, reviewed the financial statements of the companies. They also examined aspects of the Ivorian economy and local industrial sectors in which companies operate in order to conduct a true valuation of La Financiere's portfolio. As of this writing, draft final report on this engagement is under preparation at Price Waterhouse.



APPENDIX G
DIAGNOSTIC FRAMEWORK

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FINANCIAL SECTOR ASSESSMENT

**A DIAGNOSTIC TOOL FOR USAID_s TO DEFINE
FINANCIAL SECTOR DEVELOPMENT STRATEGIES**

**AID/PRE
FINANCIAL SECTOR DEVELOPMENT PROJECT
(FSDP)**

Price Waterhouse



Purpose of the Financial Sector Assessment

The primary purposes of a Financial Sector Assessment are to enable missions to evaluate what is and is not working within the financial sector as it exists today, and to identify obstacles that constrain the financial sector in meeting the needs of all productive sectors. As a diagnostic tool, it is designed to provide missions with the knowledge necessary to formulate plans, action steps, and conduct policy dialogue.

A.I.D. Policy

A.I.D. policy, as spelled out in the "Policy Paper on Financial Market Development" calls for:

"A system of financial markets that is integrated and relatively undistorted, one that relies heavily on competitive financial institutions, and on policies to facilitate competition. This system should be capable of effectively mobilizing private savings, allocating those savings to investments yielding maximum returns, and maximizing the participation of the general populace."

Underlying this policy expression of the ideal system is the recognition that developing countries' financial sectors suffer from a mix of policy constraints, distortions, and other obstacles to efficient capital mobilization. The FSA is meant to provide a comprehensive means for identifying the major obstacles to financial sector growth in order to determine how best to increase the private sector's access to capital.

The FSA as a Tool for Strategic Planning

The FSA, as a tool for systematically evaluating a country's financial system, can be used as the basis for developing a strategy for the development of that sector. This diagnostic can also be used on a selective basis, as some missions will not wish or need to apply equally rigorous efforts to every aspect of the diagnostic. In many cases, missions have already identified the elements of the financial sector on which they wish to focus. It is expected that missions will apply the sector assessment selectively, working with PRE and Price Waterhouse in defining specific assessment needs.

Other Potential Uses of the FSA

While the FSA can be used as a means for developing the information needed for a comprehensive financial sector strategy, it can also be used in a more focused fashion to help develop PPs and PIDs. In addition, the assessment can provide a more knowledgeable basis for A.I.D. missions as they approach their dialogue responsibilities with host governments. A comprehensive assessment would include:

- o An evaluation of the effect of macro-economic policies on the financial sector, including an assessment of trends in financial deepening and the significance thereof;
- o An assessment of policies that inhibit savings, and identification of policy changes necessary to mobilize increased savings;
- o Consideration of the effects of directed credit policies by the government and recommendation of strategies to introduce market oriented policies in a manner which limits shocks to the system;
- o Evaluation of the legal and regulatory frameworks to determine their effects on the financial sector;
- o A strategy for financial sector progress, including recommendations which lead to a more competitive financial system, and increase the diversity of the products and services it offers to clients. Specific recommendations should be made concerning requisite changes in institutions, forms of capital mobilization, and degree of completion.

Contents of the FSA

A complete sector assessment is divided into eight areas:

- I. **Macro-Economic Conditions**
- II. **Analysis of Institutional Structure, Forms of Financing Terms and Conditions in Formal Sector and Comparison with Existing Informal Sector**
- III. **Financial Sector Analysis - Flows Within the Financial System**
- IV. **Legal and Regulatory Issues**
- V. **Socio-Political Environment and Linkages to the Financial System**
- VI. **Linkages - Actual and Potential - to International Capital Markets**
- VII. **Existing AID and Other Donor Programs**
- VIII. **Strategic and Program Recommendations**

Exhibits 1 to 3 present samples of both the content and process of an FSA.

Sources of information: interviews; Government reports and documents; past studies and plans; A.I.D. in-house documents; in-country institutions (financial reports, plans, etc.) surveys of lenders, corporations, etc.

Framework Elements in More Detail

I. Economic Policy Analysis

A. Overall assessment of macro-economic conditions, primary driving forces, likely future trends, key sectors, GNP, relative sizes of GNP constituents as they are likely to impact progress of the financial system.

B. Macro-Economic Policy

1. Debt policy, sources of debt, potential for debt/equity conversions

2. Types of domestic debt instruments, total amount of domestic debt, annual domestic debt placement, domestic debt terms, channels of distribution

3. Credit allocation policies - use of subsidies, which sectors, terms and conditions

C. Foreign Exchange Policy and Reserves

1. Impact of exchange policy on domestic savings mobilization by deposit institution

2. Impact on domestic savings mobilization in capital markets

D. Monetary Policy

1. Interest rate policy

2. Installments of liquidity management

3. Treasury financing needs

4. Money supply growth rate, relationship to inflation

II. Analysis of Institutional Structure, Forms of Financing, Terms and Conditions

A. Formal Credit (Non-Debenture) Markets

1. Central Bank

(Role, authority, discount practices, directed credit, fund allocation policies, reserve requirements, deposit insurance reporting requirements, quality of information, regulatory authority, quality of supervision)

2. Commercial Banks

3. Finance Companies

4. Insurance Companies

5. Savings Institutions

6. Credit Unions

7. Investment Banks

8. Mortgage Banks

9. Other specialized credit institutions

(Pension Funds, Social Security, Other)

10. Development Banks

11. External Debt Sources

12. Foreign Exchange Brokers

For each of the above (2-12) determine:

- o **Types of instruments, terms and conditions, sectors served, future plans, barriers to growth (includes consumer credit, retail commercial, interbank)**
- o **Availability of foreign exchange hedging mechanisms, letters of credit, other trade instruments**
- o **Access to domestic capital, sources and terms**
- o **Management and staff capability, types of information, back office and cost control systems**
- o **Access to professional training programs**
- o **Monitoring and portfolio workout capacity (ability to identify, clarify, and treat non-performing assets)**
- o **Financial ratios, relative profitability, including overhead and transaction costs**
- o **Recent history, number of new entrants, mergers, failures**
- o **Within and across segments, determine degree of competition**
- o **The effectiveness of the existing system of prudential regulation and supervision of financial entities**

B. Capital Markets (actual and potential sources of risk capital)

1. Supply of Capital

(System size, liquidity)

2. Securities Market(s)

a. Type of market, level of activity, types and numbers of issues traded:

- o Commercial Paper
- o Bonds (Debentures)
- o Convertible Securities
- o Stocks
- o Options/Warrants

b. Supply of securities, potential vs. actual, comparison of rates of return and risk of various debt and stock securities vs. alternative forms of investment

c. Demand for securities, market volatility

d. Degree of public/institutional ownership

e. Market regulations, who can trade, conditions of trading

f. Disclosure laws/regulations, degree of sophistication and credibility of audit firms

g. International Public Offers (IPOs), activity

3. Informal Markets

a. Savings mobilization capability

b. Terms, conditions and end uses of lending

c. Private placement

d. Supplier credits

e. Remittances

4. Securities Regulatory Organization

- a. Regulatory authority, securities listing requirements**
- b. Brokerage licensing requirements, trading rules**
- c. Credibility, audit authority, disclosure requirements, staff capability**
- d. Prospectus requirements, sufficiency of information disclosed**

C. Privatization

- 1. Number, type of various privatization activities**
- 2. Plans for public stock issuance**

D. Accounting Institutions and Standards

- 1. Type, number, and competency of accounting firms**
- 2. Accounting standards, sophistication of accounting industry, presence of accounting standards**

III. Financial Analysis and Indicators

A. Domestic Savings Rate

B. Financial Efficiency

1. Degree to which system mobilizes funds at low opportunity costs, distributes to areas of highest return, adjusted for risk (Interest rate spreads)
2. Cost of capital mobilization

C. Financial Depth

1. Ratio of money (currency plus demand deposits) to GDP (Relative to other countries similar in economic size and type)
2. Annual volume in capital markets, stock exchange

D. Capital Flows

1. Net internal/external capital flows (e.g. degree of capital flight)
2. Assessment of factors behind flows

E. Demand for Capital (Small, Medium, Large)

1. Assess needs by sector, identify how needs currently are met, or unmet
 - a. Equity
 - b. Debt - long term investment vs. short term (working capital, receivables financing)
2. Government capital and state enterprise capital consumption, how much and on what terms
3. Start-ups - how capitalized, difficulty in obtaining capital, barriers to growth

IV. Legal and Regulatory Policies

A. Tax Policy

1. Taxation on interest, dividends, capital gains
2. Tax incentives/disincentives that affect investment attractiveness

B. Partnership/Incorporation Requirements

C. Securities Law

D. Bank and Non-Bank Regulatory Institutions and Policies

1. Control of Risk
 - a. Deposit Insurance
 - b. Bank Examination
2. Minimum Capital Requirements
3. Restrictions on Entry and Expansion

V. Socio-Political Environment

A. Cultural Values

B. Political Conditions

VI. Linkages to International Capital Markets

A. Credit Flows

B. Capital Flows - through quantity of bond issues in foreign markets; and foreign purchases on local stock markets

C. Donor Activities in the Financial Sector

1. Loans, swaps, equity
2. Technical assistance
3. Plans to enhance financial sector

VII. Existing A.L.D. Programs

A. Financial Sector Programs

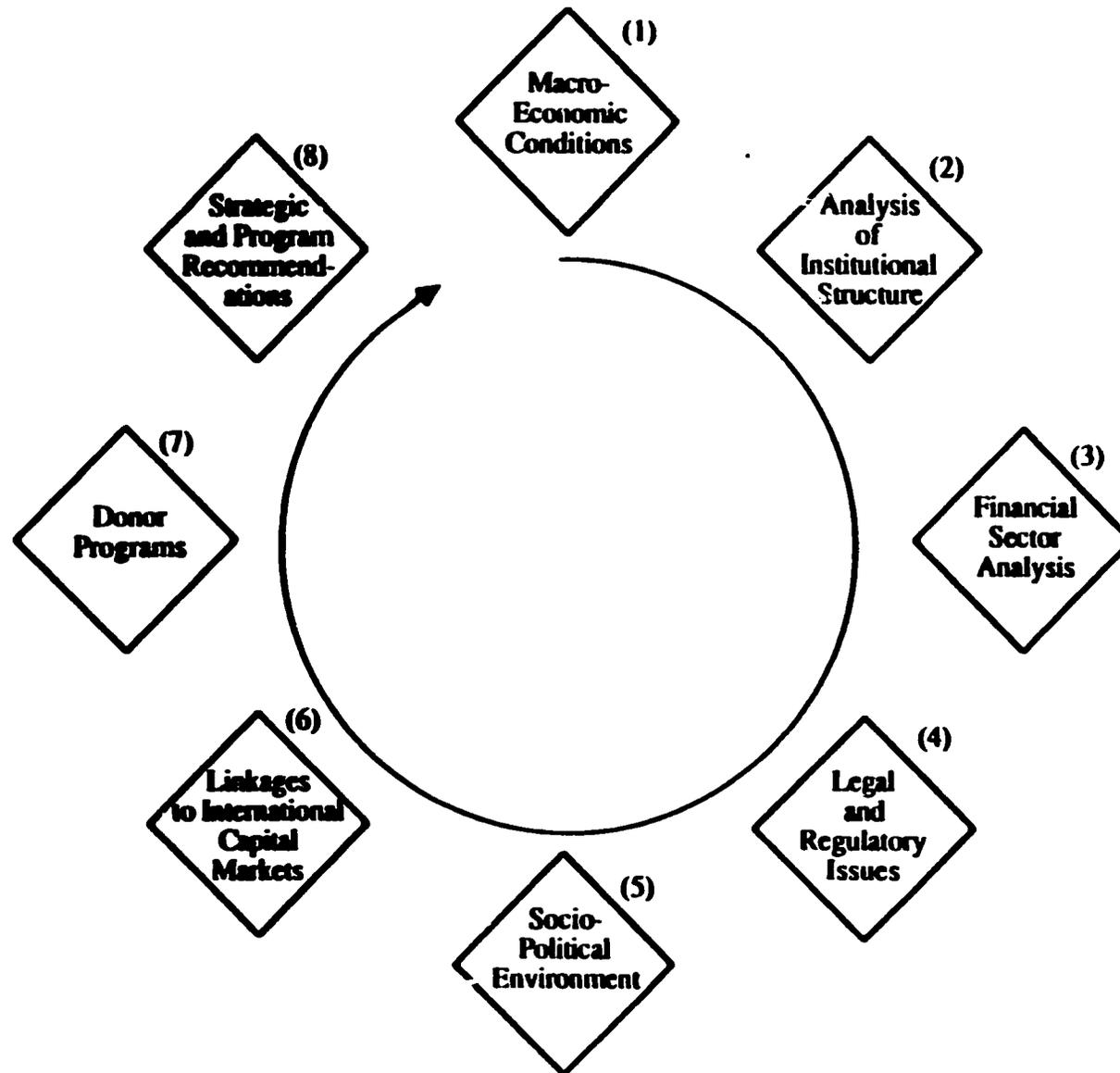
B. Other Programs with Financial Components

VIII. Recommended Strategy and Programs

A. Broad Strategy Recommendations for Financial Sector Development

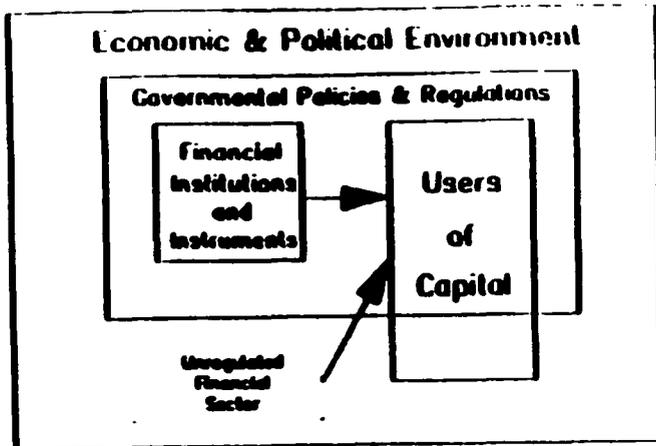
B. Specific Program Recommendations

The Financial Sector Assessment Process

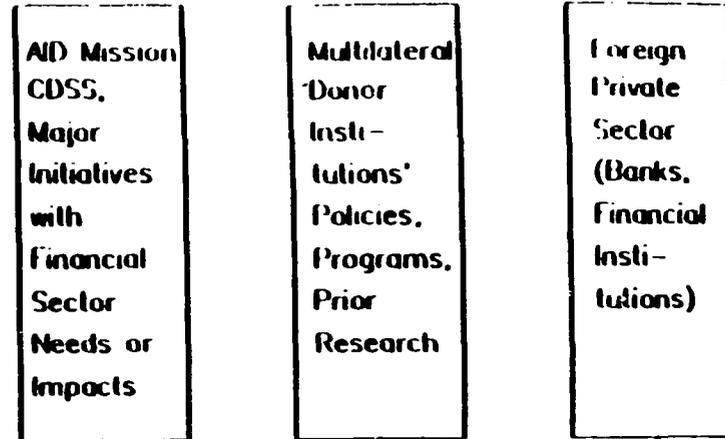


STRATEGIC PLANNING PROCESS

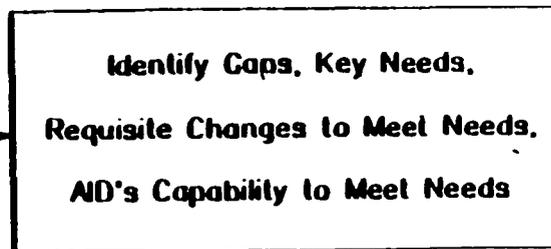
1. Assess the Financial Market Environment



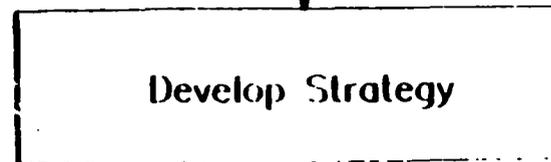
2. Assess Existing Efforts and Programs



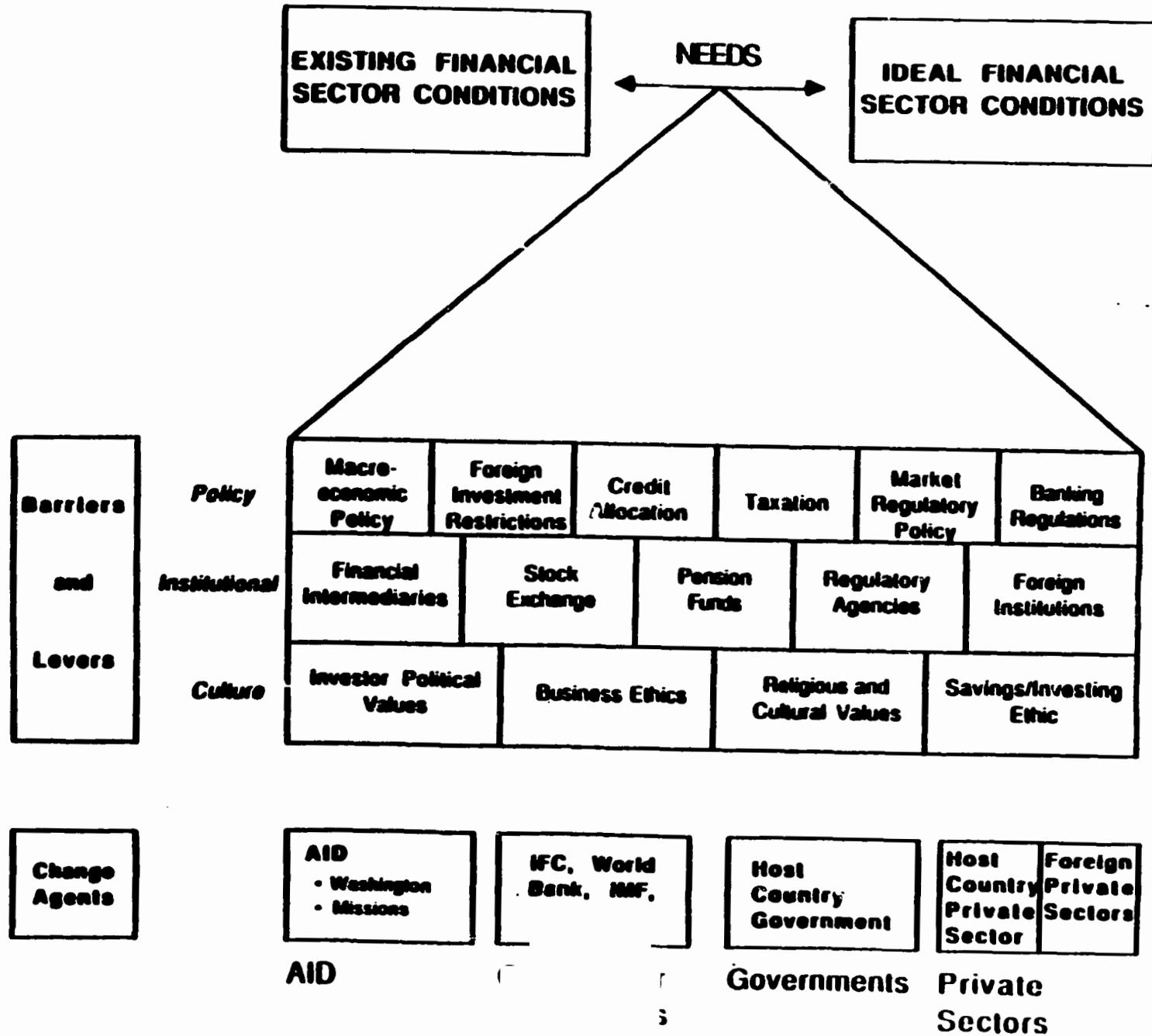
3.



4.



GAP ANALYSIS



FINANCIAL SECTOR ANALYSIS: AN EXAMPLE

FINANCIAL SECTOR COMPONENTS AND FACTORS

	SUPPLY OF SECURITIES	DEMAND FOR SECURITIES	FINANCIAL INTERMEDIARIES	DISCLOSURE	REGULATORY NEEDS LEGISLATION	OTHER	
CONSTRAINTS AND MECHANISMS	POLICY	<ul style="list-style-type: none"> • TAX INCENTIVES • INTEREST RATE POLICY • SUBSIDIES 	<ul style="list-style-type: none"> • ETHNIC BARRIERS • TAX INCENTIVES • FOREIGN INVESTMENT NOT ALLOWED 	<ul style="list-style-type: none"> • BIAS AGAINST PRIVATE SECTOR • POLICY PREVENTS COMPETITION 	<ul style="list-style-type: none"> • INADEQUATE FINANCIAL DISCLOSURE POLICIES 	<ul style="list-style-type: none"> • LACK OF INVESTOR PROTECTION • PRICE LIMITS 	<ul style="list-style-type: none"> • ACCESS TO FOREIGN EXCHANGE
	INSTITUTIONAL	<ul style="list-style-type: none"> • BIAS TOWARD PRIVATELY HELD COMPANIES 	<ul style="list-style-type: none"> • PENSION FUNDS DO NOT INVEST IN SECURITIES 	<ul style="list-style-type: none"> • LACK OF SKILLS • DOMINANCE BY STATE-OWNED INSTITUTIONS • INEFFICIENT ENTITIES 	<ul style="list-style-type: none"> • LACK OF ACCOUNTING STANDARDS BOARD 	<ul style="list-style-type: none"> • INADEQUATE REGULATORY AGENCY 	<ul style="list-style-type: none"> • INFORMAL MARKET PREVAILS
	CULTURAL AND OTHER	<ul style="list-style-type: none"> • STATE-OWNED ENTERPRISES PREVAIL 	<ul style="list-style-type: none"> • POLITICAL UNREST 	<ul style="list-style-type: none"> • LACK OF BUSINESS ETHICS 	<ul style="list-style-type: none"> • TRADING RULES NOT RESPECTED 	<ul style="list-style-type: none"> • TRADE SETTLEMENT PERIODS ARE TOO LONG 	<ul style="list-style-type: none"> • ETHNIC/ RELIGIOUS CONFLICTS WITH FREE MARKET APPROACH

Note: Table is not complete. Boxes in the diagram have been filled in for description purposes only.