

PD ARN. 293

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PROJECT ASSISTANCE COMPLETION REPORT

1. Background Data

A.	Project Number and Title:	No. 515-0247 Financial Services Project
B.	Implementing Agencies:	Banco Central, Fedecredito, Ohio State University, Academia de Centroamérica
C.	Original PACD:	June 30, 1995
	Last Revised PACD:	December 31, 1995
D.	Amount Obligated	\$5,317,459
E.	Total Expenditures	\$5,317,459
G.	Host Country Contribution:	
	Total Planned (LOP)	\$2,000,000
	Final Total	\$2,400,000

**PROJECT ASSISTANCE COMPLETION REPORT
PROJECT NO 515-0247
FINANCIAL SERVICES PROJECT**

MAY 31, 1991 - DECEMBER 31, 1995

PROJECT PURPOSE AND GOAL

The Financial Services Project (FSP) was approved in June 1990, and signed on May 31, 1991, "to create an institutional environment that fosters secure, efficient financial intermediaries serving small and medium scale savers and borrowers."

With the FSP, the Mission's goal was to improve financial intermediation in Costa Rica, in order to increase the mobilization of domestic resources, improve their allocation to productive activities, and expand the degree of access to financial services, both loans and deposit facilities, for wider segments of the population. The Mission's basic assumption was that increased financial liberalization would augment savings flows, improve the productivity of investment, and spur growth. The objectives of the FSP were to contribute to the continuation of the financial liberalization efforts of recent years, promote efficiency in financial markets, and increase access to financial services for groups that have been at the margin of formal finance.

The Project's objectives and implementation are divided into three major components:

- *policy analysis and reform*, operating at the macroeconomic level to ensure a policy environment favorable to the expansion of financial services.
- *prudential supervision*, operating at the regulatory level to strengthen supervision of financial institutions, and specifically the security of savings and loan cooperatives
- *financial management and innovation*, operating at the level of individual intermediaries to demonstrate a range of financial innovation to improve services to protect clientele.

PROJECT BACKGROUND

Financial reform is a process requiring public consciousness, political will, and knowledge and technical skill of the experts in the area. It is a long process requiring change in

attitude or mentality on part of the larger public and politicians. USAID began work with the GOOCR to promote financial reform since 1982. However concentrated financial reform efforts began in Costa Rica in 1986, leading to the freeing of interest rates, the elimination of portfolio requirements and other qualitative controls on credit, the expansion of private bank activities, and some initial efforts at strengthening prudential supervision.

The Financial Services Project (FSP) was the result of the Grant Agreement between the Government of Costa Rica (GOOCR) and USAID/Costa Rica, signed on May 31, 1991 (USAID Project No.515-0247) for the sum of \$8.4 million, later reduced to \$5.3 million due to USAID budget constrictions..

The implementation of the FSP required various approaches to finance the project activities. First, Ohio State University Rural Finance Program (OSU) was secured under the USAID/Washington Cooperative Agreement on Financial Resources Management (FIRM), for the sum of \$1.6 million, to provide research, policy analysis, and technical assistance to the different institutions involved. Project implementation began in October, 1991, for an expected duration of four years. The bulk of the efforts were directed at supporting GOOCR efforts at policy development and financial sector management, and supporting GOOCR efforts in the area of legislative reform. OSU sub-contracted with "Academia de Centroamerica" (Academia), in San José, to facilitate implementation in the field. The OSU agreement ended on December 31, 1994.

The Mission then utilized a Grant Agreement with Academia for the period December 1, 1994 to December 31, 1995 obligating the sum of US\$ 840,000. Under this grant, Academia worked more closely with the Central Bank on policy reform, and with the Legislative Branch to draft the financial reform proposals and follow them through the legal system. Academia also provided technical assistance to the Superintendency of Financial Institutions to analyze and improve supervisory systems. In addition Academia worked to further investigate and develop innovations with micro enterprise credit institutions, among other research and dissemination activities.

A Cooperative Agreement between the National Federation of Savings and Loan Cooperatives (Fedecredito) and USAID/Costa Rica was also signed on May 31, 1991 for the sum of \$3.2 million (later reduced in 1994 to \$2.7 million). The purpose of this Cooperative Agreement was to provide support for the regulation and supervision of savings and loan cooperatives, and to develop the required systems. To improve the security and financial solvency of the credit unions, implied working on three levels: the member cooperatives, the National Federation of Cooperatives, and the government regulation organisms. The following objectives were used as directives: 1) improving the safety and soundness of credit unions as financial intermediaries, 2) building public confidence in the credit union movement, 3) strengthening the regulatory infrastructure to protect the savings of credit union members, and 4) creating model strategies for financial intermediaries to use to protect savings.

Under the Cooperative Agreement Fedecredito/USAID, Fedecredito was to contract the World Council of Cooperative Credit Unions (WOCCU) to provide technical assistance in the development of the different components. The Fedecredito/WOCCU contract was signed on October 30, 1992 for the length of the FSP.

Other FSP activities were also directly financed through PIO/Ts applied mostly to invitational travel, information system consultants, project management advisors, and evaluation for the sum of US \$200,000.

MAJOR OUTPUTS AND ACCOMPLISHMENTS

Under the FSP, the Mission expected to achieve the objectives through three closely linked activities: policy analysis and reform, prudential supervision, improved management of financial institutions and innovation in the informal sector. This section of the Close-Out Report will look at each component and the contribution made by the individual contractors and grantees.

POLICY ANALYSIS AND REFORM COMPONENT

The policy analysis and reform component focused on the Central Bank management of factors affecting the financial sector and the legislative reform needed to eliminate distortions to make the sector more competitive.

Accomplishments under the OSU agreement

1. The FSP contributed to the process of financial reform first by evaluating the results of previous financial reform measures which led to the design of new reform initiatives.
2. A main topic for policy debate in late 1991 - early 1992 was the relationships among the rate of devaluation, the rate of domestic inflation, interest rates, and the fiscal deficit. The FSP contributed to this debate through the discussion of models to explain those relationships, involving authorities and representatives of international agencies. This debate led to the abandonment of the crawling-peg foreign exchange regime, the adoption of a freely-floating exchange rate, and the liberalization of the capital account of the balance of payments in April, 1992, which has been one of the most important policy reforms in Costa Rica in recent years.
3. In order to promote new financial reforms, a committee of experts was convened in an effort to arrive at a technical and political consensus. A valuable interaction took place with the Inter-American Development Bank, and policy reform recommendations were

presented for discussion by the Legislative Committee. This committee debated issues related to instruments of monetary control and the independence of the Central Bank, the legal framework for the private and state-owned banks, and the role of prudential supervision during the 1992-1993 period.

4. Substantial success was achieved in improving the policy and regulatory environment for financial sector performance during 1992-1993, primarily through assistance to the GOOCR in developing policy and regulatory changes implemented through Central Bank administrative actions.

5. Specific outputs of the *policy analysis and reform component* include directed research, technical assistance, policy advice, public debate, training, dissemination of reform information and research through the publication of 5 books, 43 technical articles and 45 editorials, as well as through 28 seminars, 31 conferences and 8 study tours for Central Bank officials and legislative representatives.

6. The Central Bank Law amending the previous was drafted and approved by the Special Commission on Financial Reform of the National Assembly, but the law was stymied by the electoral process and the change in administration in May 1994, which stopped its discussion in the General Assembly.

Accomplishments under the Academia Cooperative Agreement:

1. A major accomplishment in 1995 was the passage of the new Central Bank legislation on October 25, which paved the road for further improvements in the Costa Rican financial sector. The FSP financed a legislation project coordinator and several technical consultants for the Special Commission on Financial Reform to draft the bills for discussion. This legislation envisages important changes to increase financial sector efficiency, and includes provisions to strengthen the Central Bank's autonomy and the capability of the supervisory agency to exercise prudential supervision. The former regulatory body AGEF is transformed into the General Superintendency of Financial Entities (SUGEF), ruled by a board of directors (not the Central Bank), with power to intervene any financial intermediary and to set capital base requirements and risk standards.

2. The challenge in 1996 for the Special Commission for Financial Reform is to submit for approval reform legislation for the financial system as a whole, particularly dealing with competition and market integration. The proposed legislation attempts to reduce the current fragmentation of the financial system caused by discriminatory regulations, implies changes to current legislation ruling state-owned banks, foreign banks, credit unions, and other financial entities. FSP consultants drafted this legislation and the bills are being considered by the Central Bank and SUGEF authorities for comments.

3. The FSP also supported the reforms through providing technical assistance, field trips, and seminars to disseminate the state of the art in financial reforms world wide.

4. Several background studies were prepared by experts, including the following outputs:

Financing of Housing- a very useful tool the drafting of new legislation which transforms the mutual into private banks dealing with housing financing.

Financial Openness to Foreign Banking--an analysis of the Mexican experience in foreign banking, useful for legislators in drafting the foreign banking legislation.

Linking fiscal and monetary sectors--a paper based on the Inter American Monetary Fund approach on macroeconomic balances, however it was not considered to have provided new insights.

Management of banking crisis by Central Banks--a collection of Central Bank experiences in managing banking crisis indicating the underlying idea that if reforms develop faster than prudential supervision this may to financial crisis. It is a useful technical tool providing guidelines for designing a strategy to prevent and manage financial crisis, as an alternative to simply bailing out banks in distress.

Agenda for further reform: a summary of achievements and listing of pending issues useful as a guide for future reform.

5. A training program for the Central Bank staff was implemented to improve technical capability in analyzing macroeconomic data and proposing policy recommendations to deal with economic and financial issues.

6. The abolition of the state-owned bank's monopoly on checking accounts is a fundamental change within the Costa Rican financial sector, however, the inefficient clearing system in the country proposed a major problem to keep banks competitive. The FSP financed a pre-feasibility study indicating the terms of reference to establish the general framework, services, and cost of computer equipment required to develop an Integrated System of Financial Services for an national payment system. The implementation of the new system is expected to begin in October 1996.

PRUDENTIAL SUPERVISION COMPONENT

A key ingredient in a successful financial reform is the strengthening of the prudential supervision tools. An important task for the FSP has been the amplification of the

supervisory role played by AGEF, and the institutional building to meet the new obligations of a Superintendency. Non-bank financial intermediaries pose special challenges for the supervisory authorities. Likewise it was important to help informal financial institutions obtain financial solvency and recover the public's confidence after the liquidity crisis that the credit union system had faced in 1989.

Accomplishments of the OSU Agreement

1. The FSP was involved in the debate about a new organizational structure for this office, and the need to extend its responsibilities to all financial institutions to provide a more secure financial market for the savers. This was a period of consciousness raising among financial institution representatives, legislators and the general public.

Accomplishments of the Academia Agreement

1. As indicated previously, the FSP consultants drafted a reform proposal and worked with the Special Commission on Financial Reform to create a new regulatory body, transforming the General Auditor of Financial Entities (AGEF) to that of a General Superintendent of Financial Institutions (SUGEF), extending its responsibilities and jurisdiction to all financial intermediaries. This legislation passed in October 1995 implied major organizational restructuring and training for the AGEF personnel.

2. Technical assistance to SUGEF had important implications for the Costa Rican financial sector and the economy in general. This helped meet the IDB's conditionality under SAL III, which required the GOOCR to set up an action plan to enforce prudential supervision. According to SUGEF officials, without the technical assistance provided under the FSP, it would have been very difficult to comply with IDB's conditions.

3. Providing technical support to the SUGEF was one of Academia's most ambitious activities which would set the basis for developing technical and administrative changes to strengthen SUGEF's supervisory capability. Technical assistance included a diagnosis of needs performed by expert international consultants, and the consequential design of a strategic plan. This was followed by the design of a human resource training plan including techniques to evaluate a banks' patrimony sufficiency, preparation of supervision and inspection handbooks, and the design of instruments to monitor financial intermediaries performance. Due to PACD time restrictions, the FSP financed only the initial three month period of the training plan. However, given that the institution has been criticized as inefficient to prevent financial crisis, the SUGEF is committed to continue the training process at all costs.

Accomplishments of the Fedecredito Agreement

1. A major accomplishment of Fedecredito has been the culmination of its efforts in drafting the Supervision of Savings and Loan Cooperatives reform law for new credit union legislation. Fedecredito brought together legislators and cooperative managers to discuss and analyze issues. In April 1994 the law was passed and the General Auditor of Financial Institutions' (AGEF) authority was expanded to include credit unions. Due to Fedecredito's efforts under the FSP, the passage of this Financial Supervision of Savings and Loan Cooperatives Law provided the cooperatives with more than a two year head start over other financial institutions, since the Financial Institution Supervision Bill was not passed until October 1996.
2. By law AGEF initiated supervision in November of 1994, but had not provided guidelines for supervision and reporting. Fedecredito and WOCCU provided technical assistance to AGEF to help train the AGEF personnel in the organization and function of Cooperatives.
3. Fedecredito also assumed the responsibility of providing technical assistance and training to prepare the member Savings and Loan Cooperatives to comply with the new information and accounting procedures required established in the April 1994 law, by working to strengthen the cooperatives financial solvency, and to complete the implementation of standard policies, norms, and operating systems in order to improve management effectiveness and to control adherence to prudential regulation.
4. AUDICOOP, an organizational unit providing auditing and prudential supervision services to member cooperatives as a semi-decentralized organizational unit within Fedecredito, was organized and staffed in July 1993. AUDICOOP was approved by the SUGEF as an auxiliary auditor in May 1996.
5. AUDICOOP has been effective in developing manuals and procedures for standardizing the members' financial systems and reporting. Currently all financial reports abide by the SUGEF regulations, and reports are being sent by the cooperatives to AUDICOOP bimonthly as a preventive measure of supervision. AUDICOOP has performed financial or operational audits on all of the 50 member cooperatives. The final evaluation report on Fedecredito's technical assistance indicates that the general managers of the cooperatives rated very highly the AUDICOOP assistance, and 65% are contracting AUDICOOP's audit services because they find them to be excellent quality and within the market range of costs.

FINANCIAL MANAGEMENT AND INNOVATION

The financial management and innovation component implied institutional strengthening and innovations to assure credit to small and micro enterprise clientele. During the first three years, OSU extended assistance to three large NGO's (Acorde, Avance, FINCA). However, throughout the four and a half years of the FSP, assistance was provided basically to two "federations" to help meet the project objectives of sound management and financial solvency for organisms that deal directly with the savings of the less advantaged; these were FINCA and Fedecredito,

The 1987-1989 financial crisis provoked in the savings and loan cooperatives a weakness in the financial and social structure, deteriorating their images and causing serious liquidity problems. Two factors openly influenced the liquidity and profit of the cooperatives: the loss or reduction in members' savings and term deposits, and the recuperation of credits with the consequential effect in payment default. The FSP provided training and technical assistance to Fedecredito personnel, who in turn worked directly with the cooperatives.

Under this section, the accomplishments include efforts of OSU/ Academia and Fedecredito to improve administrative procedures, increase market penetration, and develop innovative financial products.

Accomplishments of the OSU Agreement

1. In the area of micro enterprise finance, OSU completed diagnostic studies of the Asociación Costarricense de Desarrollo (ACORDE), a second-level organization for NGO's, the Fundación Integral Campesina (FINCA)), with its network of 180 community banks, one of the most important organizations that supply financial services to rural micro enterprises, and Avance Microempresarial, an urban NGO with a large credit portfolio.
2. The FSP also assisted the Government of Costa Rica to design and implement with the American Development Bank an institutional mechanism for the disbursement of a large IDB loan for microenterprise credit activities.
3. Academia, sub-contracted by OSU, provided technical assistance to ACORDE. In the mid-term evaluation ACORDE highly rated Academia assistance, and indicated that it has reached a self-sufficiency level. It has increased interest rates and lowered administrative costs.
4. FINCA also has rated well the assistance provided by Academia. Technical assistance included preparation of an organizational manual emphasizing decentralization and financial assistance in the form of strategic financial projections for alternative means of attaining self-sufficiency.

5. An innovation of OSU was the design of "Certificados de Aportación Patrimonial" (CAPs) which was implemented in 20 FINCA community banks. The CAPs are "stock" in the bank as patrimony to better define the owners.

6. In general outputs of the financial management and innovations component consisted of direct research and dissemination on Costa Rican microenterprise financing, management training, and institutional strengthening; two books, 40 technical papers and operational manuals; five seminars for 359 participants; and two observational trips for different policy makers and managers.

Accomplishments of the Academia Agreement

1. The efforts of Academia were directed at continuing efforts of the previous experience: the development of manuals, training and technical assistance to community banks in development of accounting systems, savings/credit policies, and capital strengthening through the "CAPs". Beneficiaries of the training were over 500 promoters and rural bank board members of FINCA.

2. The efforts of Academia also included an evaluation of the status of the "Juntas Rurales" (small farmer directive boards of the National Bank rural branches), in order to analyze an innovative service in credit. The evaluation proposes an institutional transformation of the "Juntas" and a new concept of development banking.

Accomplishments of the Fedecredito Agreement

1. Fedecredito re-organized its technical assistance model, and with WOCCU assistance in the first months of 1995, designed a Directed Integrated Technical Assistance Model, which addressed the needs of the cooperatives, and improved the efficiency in the use of human resources. WOCCU elaborated a new methodology for diagnosis of the cooperatives' status, which allows for the measurement and monitoring of the gap between the financial and administrative structure of the cooperatives and the respective parameters of a solvent and secure structure. This new TA methodology is an improvement over the prior strategy of dealing with all the different needs of the cooperatives in a general manner, i.e. the same service for all cooperatives regardless of their size and needs.

2. As a major accomplishment under the goal of financial stability the Program for Total Restructuring (RETO), was implemented, thereby providing assistance to a group of currently 22 cooperatives that chose to be involved after having analyzed the results of the diagnosis which indicated the gap between the ideal model and status of their cooperative. This program allows for technical assistance in the area of planning,

marketing, finances, organization, and human resources. The RETO program supports and challenges the cooperative until it can reach a competitive status, which will permit the cooperative to then form part of the "Zurqui Initiative".

3. The Zurqui Initiative increases the cooperatives competitive capacity with 1) integrated financial products such as the credit card (FEDECARD), debit card and others, 2) an intensive advanced technology to interconnect the cooperatives on a national level to provide a better service, 3) an aggressive effort of shared marketing on a national and local level to be positioned as "everybody is Federed" , and 4) a public image of sound solid integrated financial institutions. The outputs are literally translated into an inter-cooperative credit card of local and international service, a debit card that can be applied at any of the participating cooperatives and commercial businesses, long-term savings plans, insurance policies, the Master Savings Account, connectivity between cooperatives to check cliental status, withdrawals, automatic cashiers, and information communications center. In addition, the marketing campaign to achieve the unified image in the cooperatives of Fedecrédito, positioned as the national network, FEDERED, included outputs such as standard building sign, two TV commercials, and publicity publications.

The outputs under the Zurqui Initiative were not totally financed by the Project. The Initiative emphasizes the active participation of Fedecrédito with the associated credit unions in the implementation of strategic products to better position FEDERED in the Costa Rican financial market. This shared implementation of responsibilities should lead to a higher probability of successful implementation.

4. Fedecrédito with WOCCU's assistance, developed a plan and procedures to operate a Structural Strengthening Fund as a complement of the RETO Program, whereby the cooperatives who meet their annual goals of reorganization and improved management of the financial portfolio are eligible for funds that help resolve their institutional and bad debt reserves deficiencies. Participation in the Structural Strengthening Fund will allow the cooperatives to become more financially solid entities, and therefore protect the savings of the associate members.

5. The systems and controls of the "Liquidity Facility" were created for a better financial administration of the liquidity of the cooperatives, which permitted the operation of an inter-cooperative Compensation Chamber to check credits and debits of the services rendered in the inter-cooperative interchange of products on a nationwide level.

6. Project funding of US \$270,000 was used to procure the following components to support the information technology initiatives: 60 microcomputers, 60 modems, a RISC server to host financial databases from selected credit unions, four laptops, one desktop, one laser printer, and presentation equipment. Although a modest contribution to the overall information technology system being developed by Fedecrédito and the associated credit unions, this equipment helped initiate the process.

Thirty-six Project funded microcomputers and modems support the credit card program at 36 cooperatives; the other 14 support an information training center established in Fedecredito to provide training to the cooperatives' personnel. In addition, the technical assistance provided through an IRM contract played an important role in defining and initiating the clear path that Fedecredito has defined to position itself more competitively in today's financial market.

For two years, Fedecredito worked on developing in DOS a system for the financial management exclusively for the cooperatives. However, this work was discarded when Banca 2000, a modern prepared package of banking software in Fourth Generation developed in Costa Rica, was presented to Fedecredito, with the option of adapting it to the cooperative needs. Currently the operational standardization of the financial supervision software for credit unions is in advancing stages. With this new development of information systems using Banca 2000 several stages of control will be met: standardization of services among the cooperatives, control of accounting information, data base for managerial decision making, and a monitoring system to constantly evaluate the status of the cooperative within the system. The Project did not finance the purchase of the Banca 2000 software, but did finance the information technicians working on the adaptation and implementation process.

7. All of these outputs were part of a process requiring work plans, standardization of procedures and equipment, and more that anything an extraordinary effort of training in the fields of legislation, financial and economic analysis, strategic planning, marketing techniques, managerial leadership, computation, internal control and supervision, and financial products.

8. Other specific outputs include 16 study tours of 75 participants, 42 management courses, and several inter-cooperative exchanges. Of thirteen credit unions facing extremely serious financial problems, twelve are now considered financially viable entities.

EVALUATION

This section reviews the principal recommendations of the three evaluations performed on the FSP, and the major outcomes by the end of the Project. A major *Midterm Evaluation of the FSP*, considering all elements of the Project was performed in 1993. In March of 1996 a *Final Evaluation of the Academia Agreement Grant* analyzed Project implementation and outputs in the policy financial reform component. Also in 1996, an *Analysis of the Impact of the Technical Assistance provided by Fedecredito to the Cooperatives* provided insight as to the Fedecredito's effectiveness in meeting Project objectives.

Mid-Term Evaluation, and follow-up of the recommendations

The *Mid-term Evaluation* prepared in 1993 on all components of the FSP, analyzed the first three years of project implementation. The evaluators indicated one major criticism in the financial policy and reform component, which was that "insufficient provision was being made for public dissemination and for the contributions that the FSP is uniquely positioned to make toward ensuring the continuity and the quality of public debate on financial sector policy issues in Costa Rica". The *Final Evaluation on the Academia Agreement Grant* indicates that during 1995 Academia made a successful effort for wider dissemination of the Project's outputs through seminars and workshops. All background studies were presented and discussed in seminars.

The *Mid-Term Evaluation* indicates that much progress had been made during the first part of the Project in the institutional development of Fedecrédito. The organizational framework was in place and basic policies and procedures had been designed. The enactment of the law regulating the financial intermediation activities of credit unions was an important breakthrough for the future of the credit union movement. The Mid-term Evaluation recommended that Fedecrédito develop a technical support work plan to help cooperatives increase their own capability to implement standardized accounting norms, become more financially solvent, increase their market, and implement credit innovations.

This recommendation was satisfied during the last year of the Project, with the "Iniciativa Zurqui" and the RETO Program that provided leadership and guidance to the cooperatives to become more financially solvent and competitive.

The Mid-Term evaluation also recommended that Academia continue supporting FINCA with technical assistance and training, activities which were continued in depth during 1995. However, the Final Evaluation on the Academia Agreement Grant indicates that more assistance is still required to reach a point of financial consolidation in the community banks.

In general, the findings of the Mid-Term Evaluation were very positive and the major recommendation was to extend the FSP another year in order to continue the efforts started in all areas and provide time to reach more concrete results. The Mission followed through by extending the FSP through December 31, 1995. A review of the outputs indicate that the most impacting results in legislation and supervision were accomplished during this final year.

Final Evaluation on the Academia Grant Agreement

The Final Evaluation of the Academia Grant Agreement indicated that the fundamental change observed in 1995 was the practical focus on the issues, as compared to the academic bias observed in previous years by the lead contractor. Significant progress

on the legislative front was achieved. Most of this success was due to the permanent participation of an FSP advisor and short term consultants who worked with the Special Legislative Committee on Banking Reform in preparing a new draft Central Bank Law, a monetary law, and a law extending the AGEF supervision responsibilities to all financial institutions.

Authorities interviewed in the final evaluation indicate that without the Project, it would have been very difficult for legislators to have the technical background and expertise to justify and propose policy changes. The background papers provided under the FSP were considered useful inputs in supporting financial reforms, because they were prepared by experts, and this allowed an optimal use of limited time.

Authorities believe that the next round of discussions in the General Assembly on the Law of the Financial Intermediaries, drafted under the FSP, will not be as difficult as the Central Bank Law and Supervisory Law since most of the ideological constraints have been overcome. The policy debate is at this point in time more technical and less political.

Recent Latin American experience shows that reforms toward financial liberalization without adequate supervision regulation and skills leads to financial chaos. The FSP made a valuable contribution by introducing the idea of prudential supervision in conjunction with the other financial reforms.

The SUGEF auditors agreed that without the FSP, it would have been very difficult to set up a new regulatory body for financial institutions. The FSP contributed to a new thinking about financial supervision. Under previous regulation, AGEF intervened after an institution was declared insolvent; now SUGEF is better prepared to anticipate financial crisis.

*Final Evaluation on the Technical Assistance Provided
under the Fedecredito Cooperative Agreement*

The passage of the Law on Supervision of Savings and Loan Cooperatives was a major breakthrough for Fedecredito in their efforts to make cooperatives conscious of the need to work toward financial solvency and security. Cooperatives now had no choice but to improve their administrative capacity and financial portfolio. The Mid-Term Evaluation indicated that for the remaining portion of the Project during 1995, that Fedecredito's highest support priorities for the credit unions should include reaching concrete results in the following:

- 1) Developing innovative saving mobilization products and marketing strategies.
- 2) Improving financial and credit policies.
- 3) Implementing standard prudential norms and operational and internal control

- systems to strengthen managerial efficacy and improve accountability.
- 4) Developing coordination arrangements between AUDICOOP and AGEF to ensure that AUDICOOP is able to provide useful support for AGEF.
 - 5) A study to determine and establish a strategy to increase the credit union's permanent capital.

Although Fedecredito spent the first few years directed at developing the adequate support structure and the drafting and passage of the Supervision Law, it did indeed redirect its priorities to reaching the Project objectives with concrete results over the final year of Project implementation. The above five priorities were all achieved as described in the section *Major Outputs and Accomplishments*.

In the *Assessment of the Technical Assistance provided by Fedecredito to the Cooperatives*, a qualitative evaluation summarizing the responses of 17 General Managers, (35% of the member savings and loan cooperatives), analyzed the direct technical assistance (TA) provided by Fedecredito to small, medium and large cooperatives over the 54 months of the Project.

In general, all the managers indicated that Fedecredito had done an excellent job in obtaining input from the cooperatives to help draft the Law of Supervision of Savings and Loan Cooperatives, and the consequential analysis of the impact or implications of the law in relationship to the cooperative administrative procedures at that time.

Ninety percent of the managers felt that Fedecredito provided excellent support to the cooperatives in updating manuals and reporting procedures through technical assistance provided by AUDICOOP in the adjustment of the cooperatives to the new Supervision Law over a two year period. The managers felt that their audits were very professional, and that the results always were presented in a proactive preventive manner for discussion, rather than the usual investigative accusation approach used by most auditors. The majority of the cooperatives continue to contract AUDICOOP for annual audits.

The cooperatives indicated mixed feelings about the improvement of the Office of Technical Assistance. The majority (60%) felt that technical assistance had improved substantially over the last four years, but many felt that things were about the same. All of the cooperatives of the sample did have contact and technical assistance from TA or AUDICOOP (generally both) in the past two years. In general, the medium and large cooperatives were satisfied with the new direction of technical assistance, and the Zurqui Initiative. The small cooperatives generally expressed that Fedecredito TA was generally efficient and effective, but that current corporative plans were not economically feasible for them. In the case of five small cooperatives in the central area of Cartago, the TA advisors have been working with them to consider a merger. The general managers and boards members of these cooperatives are currently considering this option and initiating the required feasibility studies with Fedecredito.

In 90% of the sample, the advisors of the TA Office were considered to be good technicians with a desire to help the cooperatives resolve their problems, but 100% of the general managers complained of the high rotation rate of the TA advisors, which led to inconsistency and lack of follow-up. The larger cooperatives felt that although the advisors were good technicians, what they require are senior consultants. The large and medium large cooperative managers had a good recall of the direct technical assistance provided by the different WOCCU consultants over the years. The smaller cooperatives with general managers of less technical preparation in the financial area felt that the TA was always very helpful.

Currently, Fedecredito is reorganizing the TA Office to maintain a team of 5 top consultants that could be contracted by the cooperatives according to their specific needs. This plan responds to the interest of the larger and medium-sized cooperatives.

The Zurqui Initiative was well known by all the managers, although only 60% of the sample cooperatives is participating in this plan. The medium and large cooperatives are quite enthusiastic about the Zurqui Initiative. Some small cooperatives indicate that although they cannot participate in the plan, believe the Initiative to be a positive goal to strive toward, and that this Initiative has further stimulated the integration of the Federation. On the other hand, a small percentage of cooperatives felt left out of the interests of Fedecredito with the new Zurqui Initiative, which is directed at marketing and financial products which are above their financial capacity.

In general, there was a positive response from all managers when asked what Fedecredito had done in the past few years to benefit the federated system. Technical assistance was high on the list, in particular in relationship to the Zurqui Initiative and the RETO Program. The outstanding sense is that Fedecredito has taken a turn and is starting to work "as a system", with the cooperatives benefit in mind, rather than an entity of its own feeding off the cooperatives. This attitude has fomented a higher degree of integration and teamwork among the members.

During the FSP implementation period the cooperatives were disappointed in the results of the information system, indicating that Fedecredito had promised them a comprehensive software designed for the savings and loan cooperatives, but after two years of development, there were no results. The cooperatives moved ahead and found their own systems and developed the software that they needed, many consulting with one another.

Meanwhile, after two years of financing the development of a specific information program system, Fedecredito decided to purchase a pre-developed banking service software program (Banca 2000), and contract the adaptations required for implementation with the cooperatives. The software will be sold by Fedecredito to the cooperatives. However, only three of the 17 sample cooperatives indicated interest in implementing in the near

future the Banca 2000 software once adapted; and one of these cooperatives is the pilot project which does not have to purchase the software.

Nevertheless, a great deal of satisfaction is manifested by the managers in reference to the interconnection plan to get cooperatives linked on the same system. They consider it a good competitive strategy. The FSP did make a modest contribution toward this goal with the purchase of 36 PCS, modems, and a RISC server to support the implementation of the interconnection plan.

Fedecredito accredits WOCCU with helping them achieve objectives on a quicker pace, applying the adage "No man is prophet in his own territory." In essence the Fedecredito General Manager and Project Managers felt that they would have achieved the same objectives without WOCCU assistance, but that the stimulation and TA to the coops was very beneficial to bring about the change in mentality required to support the cooperatives to become competitive financial entities in today's market.

WOCCU assistance passed through different stages, not always consistent with Fedecredito's thoughts and needs. The first two years were directed mostly to providing technical assistance and training for the cooperatives. Although the cooperatives recognized this training as valuable, there was a lack of integration with Fedecredito. The third year was directed at developing accounting manuals that would be consistent with the new law and training Fedecredito personnel. The last year was directed at training Fedecredito TA advisors in new models and planning procedures, to promote further that last step in change of attitude of the cooperatives toward becoming competitive viable financial institutions with new products to offer.

In summary, Fedecredito did meet the Project objectives. Solid bases were established to continue the process of improving image, products and services, and the financial solvency and security of the savings and loan cooperatives providing a wide range of services all over the country to groups that are not serviced by the larger state and private banking entities.

STATUS OF COMPLETION

PROCUREMENT

Although originally programmed, there were no procurement procedures for the General Auditor of Financial Entities under the FSP. The funds were transferred to other elements of the project.

Fedecredito did directly purchase \$270,000 in computer equipment under the Cooperative Agreement. IRM consultants provided assistance to Fedecredito to develop the terms of reference and approve budgets. At the PACD, IRM performed an evaluation of the new system and indicated that the system was well implemented and of great utility to help meet Project objectives.

Fedecredito also contracted the World Council of Credit Unions under the Cooperative Agreement to provide technical assistance in the different Project objectives. WOCCU completed their contract satisfactorily and all financial charges have been reimbursed.

FINANCIAL STATUS

Academia de Centroamerica

All expenditures were reimbursed. The final 1995 had not questioned costs. The remaining funds of US \$10, 000 were decommitted and de-obligated.

Ohio State University

The contract completion date was December 31, 1994. As of 5/30/96 the sum of \$315,425 remained in the project to cover Advance of Charges (AOCs) that were being processed by USAID/Washington. The USAID/CR CONT office and the Project Officer did everything possible to have Washington forward the AOCs during the year 1995 up to June 1996, in order to decommit the remaining funds. Since the AID/CR Mission was to close out programs by July 1996, these funds were decommitted from the project and assigned to the Policy and Training Support Project so that the El Salvador Mission would be able to forward the AOC payments.

Fedecredito

All expenditures were reimbursed, and the remaining funds of US\$90 were decommitted from the Cooperative Agreement. The 1994 audit report has been submitted in draft. There are no major findings nor questioned costs. Conversations with the auditors and Fedecredito indicate that the final report for 1994 and 1995 should be presented by June 1996. The auditors indicate that at this point the 1995 does not indicate questioned costs.

Overall FSP Project.

The Project goals have been successfully completed. All Project funds have been decommitted and de-obligated. The two points of remaining unfinished business are 1) the pending reimbursement for the AOCs for the OSU contract, and 2) the 1994-95 audit findings, if any, on the Fedecredito Cooperative Agreement which will have to be followed up USAID/CR Controllers Office until time permits or by El Salvador. The FSP can be closed out.

LESSONS LEARNED

1. The Central Bank Law was drafted for approval by the Commission of the Legislation, in the later part of 1993, but the law was stymied by the electoral process and the May 1994 change in administration. This led to a change in commission members and additional hashing over the law during a two and a half year period before its approval in November 1996. A lesson learned for project planning is projects that have strong political components or can be affected by the current political issues should be programmed to begin and end within the same administration whenever possible to avoid rehashing issues and loss of time.

2. The lead contractor for the first three and a half years of the Project was Ohio State University. Although evaluations indicate that the products were of high quality as far as legislative reform, the products tended to stay on a theoretical level. Direct results were achieved on a practical level during the last year of the project administered by a local NGO. The first few years were used to create consciousness about the need for reform, and to guide the legislators in drafting that reform. However, the procedure was more directed when the local grantee, Academia, actually hired consultants to draft the reform laws for discussion by the Special Commission members. This method allowed the members to discuss with more direction any of their misgivings or areas that required more research. Having a written draft legislation to analyze made a big difference in producing a product within a restricted time period.

3. The overhead committee of the FSP as conceived was never functional. Although the commitment of a highly placed government official, such as the Central Bank President, undoubtedly serves to highlight the host country's government support of a project and provides access and visibility for project implementors, in practice it is unrealistic to expect that a person with such time pressures and responsibilities will be able to devote the necessary time and attention to providing project leadership and continuity. This is even more difficult to achieve, in a case such as the FSP where the project had components that dealt with specific institutions on a micro-level. A more practical approach may be to assign counterpart leadership and management responsibilities to a senior, but nonpolitical government official from the relevant agency, enlisting the support of top political leadership only as needed to accomplish specific project objectives.

4. A broad lesson sited in the Mid-Term Evaluation, that can be gleaned from FSP experiences during the first phase is that the pace of change that can be achieved in a democracy--absent a major crisis--is inversely proportional to the extent to which democratic processes have taken root. Costa Rica is an example of a developing country with highly developed democratic institutions and traditions. The legislature has considerable say over the policy proposals of the executive branch, and the legislature is

highly partisan. In such settings the pace of change can be excruciatingly slow to create the conditions where a genuine consensus can be achieved. Projects with such goals should be aware of the time restraints for project implementation.

5. In the case of the FSP, the Prudential Regulation and Financial Innovation components, originally conceived of as highly conceptual and sector wide in scope, became rather narrowly redefined during the project development process towards technical assistance activities aimed at particular financial sector institutions. Although sector wide efforts to improve prudential regulation and work in developing broadly accessible financial innovations can be compatible with macro-level policy development, this is not necessarily the case when assisting credit unions in improving self-regulatory capabilities or when providing direct technical assistance to PVO umbrella organizations. In the FSP, the narrowing of scope for these two components that took place between the Project Paper and Grant Agreement stages, led to increased difficulties in project coordination during implementation, as implementors were faced with the problem of having to coordinate between two dissimilar project segments.

6. Efforts in the micro enterprise component were not very extensive possibly due to Academia being side-tracked by the magnitude of the Financial reform and Supervision assistance components. From the onset, a direct grant with another PVO would have been more effective to extend the micro enterprise component beyond assistance to one or two institutions, and to produce more impacting research of financial innovations for the informal sector.

7. In general the objectives of the FSP were very global, making it difficult to monitor project implementation and measure achievement. Although concrete actions were taken, and successful concrete results were achieved, (such as the Central Bank Law, Law of Supervision of the Cooperatives, the Zurqui Initiative and RETO, training and manuals), many expectations of the project results were qualitative, which led to piecemeal modification during implementation and difficulty in measuring accomplishment.

8. Delay in the submission of audit reports is a common problem, especially if project agreements coincide with the end of the country's fiscal year. It would be a good practice to require semiannual audits in the Agreement to avoid this general problem in project supervision and close-out.