

## **Sixth Independent Evaluation Report to the IIC Board of Executive Directors**

The IIC prepares Expanded Annual Supervision Reports (XASRs) on matured projects (according to good practice standards for multilateral organizations), and the Office of Evaluation and Oversight (OVE) reviews each report to verify the reliability of the analysis, impartiality and consistency in ratings, and completeness of the identified lessons learned. Once this review is completed, OVE then prepares a report for the Board of Executive Directors of the IIC.

Following is a summary of OVE's 2008 Report which reviewed XASRs prepared by IIC staff in 2007. It is the sixth such report on the IIC's evaluation system. The report covered fifteen projects (eight corporate and seven financial intermediary projects) that were approved between 2002 and 2004. As in previous years, the report assessed outcomes and outcome drivers of the IIC's investment operations during the life of projects. It also assessed the implementation status of past recommendations aimed at improving the IIC's evaluation process.

### Report conclusions:

The report reaches very favorable conclusions regarding the IIC's work quality. The group of projects analyzed for this report and long-term trends suggest that the IIC's work quality is steadily increasing.

The report concludes that development outcomes are improving over time. For instance, in the current report 74% of the reviewed projects received high development outcomes compared with 63% and 65% of projects in the Fourth and Fifth Reports respectively. Considering all 113 projects reviewed by the IIC and OVE since 2001, the distribution of development success is continuously migrating towards high outcome categories. OVE concluded that IIC has increased the number of projects with high developmental potential.

There is a difference, however, between the performance of corporate projects and financial intermediary (FI) projects. For the Sixth Report, 88% of corporate projects achieved high development outcomes; while only 57% of FI projects achieved similar outcomes.

As in previous reports, OVE noted that IIC's work quality has been positively correlated with improved development and investment outcomes. Successful projects, those with high development and investment outcomes, accounted for 72% of the reviewed projects. When the IIC exhibited high work quality, the proportion of projects with very high development and investment outcomes increased by 7%. Moreover, the analysis of all 113 projects indicates that high work quality reduces the likelihood of project failure. We should note here, however, that this trend could eventually be affected by the fact that in recent years the IIC made a strategic decision to undertake more risky projects (i.e. greenfields, etc.) in an effort to maximize development outcome and additionality.

As evidenced in previous reports, high development outcomes are directly correlated with high investment outcomes in corporate projects. This confirms the IIC's progress in achieving win-win situations, where good financial returns go along with high development impact. FI projects, however, had a larger share of low development outcomes accompanied by high investment outcomes.

OVE recognizes the need for the IIC to achieve a greater balance in the portfolio between investment and development outcomes. It should be noted that FI operations reviewed in the Sixth Report were those approved between 2002 and 2004. The 2003 Action Plan stated that the IIC would pursue larger deals with stronger financial intermediaries in order to improve investment outcomes and overall portfolio quality. It should be noted that these projects with large financial institutions have been instrumental in enabling Management to stabilize the IIC's returns while reaching a greater number of SMEs. Furthermore, during that time period, the IIC committed to increase its financial intermediary lending to reach the Nuevo León Declaration goals.

Given that the IIC's portfolio is composed solely of non-sovereign guaranteed operations (of which more than half are financial intermediary operations), it must constantly innovate to create a profitable and high-quality asset class. This is necessary if it is to have the ability to venture into other riskier fields (which are currently underserved by the market) without compromising long-term financial sustainability.

The report also notes that implementation of the three new recommendations made in 2007 has been satisfactory. The creation of the new Technical Assistance and Strategic Partnerships division was favorably noted.

The 2008 Report contains three recommendations which are designed to introduce broad measures for improving IIC additionality and development impacts. The general thrust of these recommendations is to encourage the IIC to improve its mechanisms for tracking development impact and additionality.

Following are highlights of IIC actions to implement the 2008 Report recommendations:

#	OVE Recommendations	IIC Actions
1	IIC should develop a better understanding of the processes, products, and systems required to maximize additionality. OVE recognizes the IIC's significant progress towards better measuring project additionality via the DIAS system. However, OVE believes that there is still a gap in regards to what specific products and/or modes of intervention the IIC would need to deploy in order to maximize overall additionality.	<ul style="list-style-type: none"> <li>The IIC is committed to improving its performance in maximizing additionality. This ongoing process encompasses many actions which have been taken over the past 18 months. So as to best describe what the IIC has accomplished in this respect, see Annex A, which describes what the IIC has done to introduce and implement actions for improving additionality and development impact. This Annex deals with both Recommendations 1 and 3.</li> </ul>
2	IIC should develop better mechanisms to track and maximize development effectiveness, not only at the client level, but also among final beneficiaries. OVE believes that the IIC has emphasized a mode of intervention that focuses on individual transactions. It recommends that the IIC adopt a longer-term perspective focused not only on individual transactions with its	<ul style="list-style-type: none"> <li>OVE and the IIC are working together to prepare a study to assess the development impact of the IIC's FI lending in an effort to gain a more precise understanding of what it would take to assess development impacts at the final beneficiary level. This study should lead to improved products, services, and methods of operation and should maximize the IIC's overall additionality. The planned FI study would also be applicable to the IIC's lending in other sectors.</li> </ul>

	<p>direct clients, but also on the effects on final beneficiaries, to whom it may direct a variety of treatment via different IIC operations and/or clients.</p>	<ul style="list-style-type: none"> <li>• The IIC and OVE are developing a plan to conduct case studies to evaluate IIC interventions not only on individual transactions, but on a sector level. By developing mechanisms that do not overwhelm staff and borrowers, the IIC will benefit by having a better understanding of the results of its lending, and this should eventually lead to improved products, services, and methods of operation.</li> <li>• In order to continuously refine and develop its products and services, the IIC, with the assistance of OVE, is preparing a protocol which would systematically address the concerns express the IIC's additionality and development effectiveness.</li> </ul>
3	<p>IIC should implement a continuous feedback mechanism to track additionality and developmental results, in order to utilize the lessons learned to refine and/or develop IIC products and services.</p>	<p>See Annex A</p>

Annex A:

**IIC Actions to improve Development Impacts and Additionality**

- In 2007, the IIC introduced a “portfolio approach” to help maximize its development impact and additionality while keeping within the bounds of managerial prudence and long-term sustainability.
- The Development Effectiveness and Corporate Strategy unit was created to improve the IIC’s work on developmental impact and additionality. The decision to link development effectiveness and corporate strategy was an effort to strengthen the IIC’s commitment to development effectiveness. The unit includes two positions fully dedicated to development impact assessment, working in close coordination with the engineering and environment team, whose work is a consistent source of added value in the IIC’s interventions. The unit’s role as strategic and policy advisor to Senior Management also serves to enhance the IIC’s impact through short- and medium-term planning. As part of the new integral planning approach, the unit has developed a Development Impact and Additionality Scoring system (DIAS).
- During 2008, the DIAS was deployed, implemented, and fully integrated into the project preparation and approval workflow of the IIC. All 63 approvals for 2008 were scored. Fourteen projects currently in the IIC’s pipeline for 2009 have received at least an initial development appraisal.
- A retrofit exercise, which covered 140 projects approved between 2005 and 2007, has validated the assumptions and results of the approach to the DIAS system. It appears that the system is working well and it is a good tool to evaluate both the financial and development impact of IIC projects. This brings the total to 217 projects scored to date in the IIC’s developmental database.
- DIAS requires that during appraisal investment officers identify indicators which will be used to assess performance at the end of the project. Appraisal documentation must include information regarding how projected development outcomes and expected additionality were estimated so that the same process can be followed later in determining actual results. A full-time development officer was hired in 2007 to provide support to investment officers in this process. This officer receives the information and completes the DIAS matrices. This individual also assists with determining baselines, calculating economic impact, and determining monitoring indicators.
- Each project receives a rating at entry. During supervision, projects will be assigned a rating annually based on monitoring data regarding developmental performance.
- Training of investment officers to use the DIAS system was provided in February and July 2008 at the investment officers retreat.
- A workshop on to use the DIAS system was provided to Board members in October 2008.
- During 2009, investment officers will monitor development indicators during project supervision in the same way as financial indicators. Information collected will be included in Annual Supervision Reports.
- DIAS facilitates strategic portfolio management and portfolio ranking. This system will greatly facilitate appraisals of portfolio performance and will link the financial and development aspects of each project. This will enable the IIC to provide a broader view of the development performance of its portfolio.

- The developmental quality of operations is an integral part of investment officers' performance evaluation and bonus pay decisions.
- The Lessons Learned Database (which is posted on the IIC's intranet) was updated in 2008.