Ninth 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 Ninth Annual Independent Validation Report reviews 27 self-evaluation reports (XASRs) prepared by IIC staff. OVE reviewed each XASR to verify the reliability and impartiality of the analyses, consistency in ratings, and the appropriateness of the lessons learned that were identified. The report covered seventeen financial intermediary projects and ten corporate projects that were approved from 2006 to 2008. The IIC agrees with OVE’s findings, conclusions, and recommendations.

Report Conclusions:

Favorable development outcomes were achieved in 81% (22 projects) of the reviewed projects. If results are considered in terms of overall IIC investment volume (which was US$331 million), then 89% of the funds were directed to projects that achieved favorable development outcome ratings. Development outcomes are measured by the sustainability of results across financial, economic, environmental, and social objectives, as well as general contribution to private sector development. This percentage is slightly lower than in the 2011 OVE report, where 88% of projects achieved favorable development outcomes; however, it is higher than outcomes from the two previous annual reports, where 67% and 74% were deemed to have achieved a favorable outcome. Overall, the ratings of IIC’s mature projects indicate solid progress in achieving a higher number of high development outcome ratings.

IIC’s goal of financing projects with both developmental potential and financial viability has been adequately met in this group. This group had 96% (26 projects) satisfactory Investment Outcome ratings. In terms of investment performance, IIC results have steadily improved over the last three years, from 86% in 2009 to 90% in 2011.

OVE’s report confirms a positive trend in IIC projects achieving favorable development outcomes and it reaches very positive conclusions regarding the quality of the IIC’s work. The projects analyzed in this report and long-term trends suggest that the quality of the IIC’s work is steadily improving. In this year’s report, 89% of projects (24 projects) were rated as having satisfactory outcomes.

Taken together, both trends confirm that the quality of the IIC’s work shows positive correlation with improved development and investment outcomes. OVE’s analysis of all 171 projects reviewed to date indicates that high work quality reduces the likelihood of project failure.

This group of projects also continues the pattern which first emerged in the 2010 OVE report where FI operations outperformed corporate projects in terms of development outcomes. OVE’s first six reports (issued between 2002 and 2009) show corporate projects performing better than

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1 Expanded Annual Supervision Report
2 Favorable (or high) outcome categories refer to “Mostly Successful”, “Successful” and “Highly Successful” in the development outcome 6-point classification range; and to “Excellent” or “Satisfactory” in all the other dimensions’ 4-point classification scale.
financial intermediary projects: 67% of corporate projects received high development outcomes as compared with 47% of financial intermediaries. In the current report, 82% of FI projects had favorable development outcome ratings as compared with 80% of corporate projects.

The report indicates that IIC additionality has continued to improve, with 96% of projects achieving favorable additionality, an increase over the 2010 report where 88% of projects achieved high additionality. However, OVE also noted that the IIC often did not provide specific evidence for justifying additionality. Since the introduction of the Development Impact and Additionality Scoring System (DIAS), the IIC can now provide better evidence showing that the IIC is playing a key role in providing value added to its clients.

OVE concluded that there has been positive (although early) progress in the IIC implementation of the 2011 OVE report recommendations. OVE noted that slow implementation was expected because many of the recommendations required a “cultural change”, slowly developing over time.

According to OVE, the IIC has made progress in standardizing client support in the pre-investment phase, by incorporating technical assistance into project structures, and by strengthening its knowledge management system and use of lessons learned. OVE also noted substantial progress in the “Lessons in Action” online system. This system tracks and categorizes lessons derived from operations, including those of the XASRs. With the system in place, the IIC continues to monitor and update the database, while also, increasing awareness of lessons learned and integrating them into the project cycle.

Overall, OVE concluded that the IIC has fully implemented its project-level performance evaluation system. With the system now in place, OVE suggests that the IIC should not rest on its success but gradually expand the reach of its evaluation system to focus on incorporating lessons learned and obtaining further evidence of replicable successes at the sector level.

OVE has produced nine independent evaluation reports containing almost thirty recommendations. The IIC has implemented or made progress in implementing OVE’s recommendations. The most important recommendations were related to improving the measurement of development outcomes and additionality, establishing a lessons learned database, and providing value added services. As a result, the IIC has put in place, with OVE’s ongoing support, the most compliant evaluation system built upon the Good Practice Standards of the Evaluation Cooperation Group of Multilateral Development Banks (ECG-MDB). The IIC introduced the DIAS in 2008 to enable it to assess development outcomes and additionality throughout project life cycles, from appraisal to evaluation. In 2008, the IIC created the Technical Assistance and Strategic Partnership Division (TAS) to provide value-added services to its clients in addition to its financial support. It launched, in 2010, the intranet portal “Lessons in Action” which facilitates the documentation of lessons learned and feed these into new operations.

Following are highlights of IIC actions to implement the 2013 report recommendations:

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<th>OVE Recommendations</th>
<th>IIC Actions</th>
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<td>1</td>
<td>OVE recommended that the IIC formalize a transitional period at the pre-investment screening stage during which the IIC and its clients could engage in technical assistance activities aimed at improving client readiness,</td>
<td>Currently, the IIC is in the process of overhauling its Direct Technical Assistance (DTA) process. The IIC uses DTA to mainstream support to potential clients and current clients. The main focus is on smaller clients in small countries and on clients in less developed regions of larger economies. Moving forward, the plan is to assign a Technical Assistance (TA)</td>
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paying particular attention to smaller clients, in small and vulnerable countries.

officer to project teams in order to proactively identify technical assistance needs. For example, the IIC already includes environmental engineers on project teams. Ideally, project teams will include a TA officer who will, during screening and appraisal, actively and consistently identify issues that will later need TA.

The IIC uses tools, such as feasibility studies and environmental and labor reviews, as well as activities to enhance competitiveness, monitor IIC projects and strengthen value chains, designed to provide technical assistance for potential clients. Funds can be used to finance specific consulting work in areas such as environmental compliance, financial review, legal advice, and technical evaluation. So far, these programs have been used on a case by case basis, for example when investment officers detect issues at the origination stage that require technical assistance to address perceived weaknesses.

| 2 | OVE recommended that the IIC should enhance its capacity to partner with clients through multi-product, longer term engagements tied to the pursuit of common goals. | The IIC is already undertaking measures to accompany existing clients throughout the project cycle and through the different stages of their institutional life. For example, through TAS programs—including, for example the **FINPyme Technical Assistance**, the IIC is able to provide technical assistance to existing clients that experience problems during supervision. The use of TA is jointly decided by the Portfolio Management Division (PSU), TAS, and Development Effectiveness Division (DEC). The IIC has also had a very positive experience providing follow-up financial services to companies as they grow helping companies to explore new markets for their existing products, and introducing clients to new products and services. The IIC’s experience and its investment in clients improves companies’ likelihood of financial, operational, and developmental success. |

<p>| 3 | OVE recommended that the IIC broaden the scope of its supervision so as to further strengthen client support activities. Furthermore, OVE recommended that PSU, DEC, and TAS jointly establish a client-support identification system to detect opportunities for the IIC to provide additional client support. | The IIC has a well-functioning supervision process, monitored by a Portfolio Supervision Committee (PSC). Alongside TAS and DEC, the committee tracks a client’s ability to meet its financial obligations with the IIC and the company’s development results. This serves two purposes: first, to detect opportunities to provide additional client support (i.e. TA); and, second to flag operations that might require financial restructuring. IIC is now better poised to strengthen client activities. It is important to note that supervision officers are aware of the possibility of providing additional client support through technical assistance to correct operational, managerial, environmental, or legal issues that might arise during supervision. These issues in addition to credit issues are discussed and addressed on a case by case basis in the PSC. |</p>
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<td><strong>4</strong></td>
<td>OVE recommended that the IIC keep standardizing the project appraisal and structuring processes towards greater convergence with IDB-Group standards, including those for evaluability.</td>
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<td>Following OVE’s recommendation, the IIC will work to further improve, formalize, and enhance the structure in place.</td>
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<td>The group of projects evaluated in this report includes projects which were approved between 2006 and 2008. Since then, appraisal and structuring practices have been updated and standardized. For example, the credit process was standardized through new detailed instructions for the Initial Credit Proposal (PIC) and templates for projection modeling. Investment officers attended in house training courses on financial modeling. An instructor was hired to prepare the standardized model. Previously, investment officers relied much more on client projections and assumptions.</td>
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<td>In terms of macroeconomic assumptions, the IIC will benefit a great deal from greater harmonization with the IDB-Group. The IIC is too small to have an economic department and therefore relies on third party information. Information provided by the IDB on inflation rates, commodity prices, interest rates and GDP growth could be an area of coordination among all the private sector windows. In terms of sector assumptions, (i.e. financial institutions, infrastructure, commodities) information and databases could also be shared. Furthermore, periodic comparisons of projections with actual results will enhance the understanding of the reasons for deviation and will help to adjust forecasting models by incorporating findings and lessons learned.</td>
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<td>Given that these challenges are common to all private sector windows this could be a good opportunity to harmonize forecasting assumptions of key macroeconomic and sector variables.</td>
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<td>With respect to evaluability, the IIC is an early adopter of evaluability concepts applied to private sector operations. Given the IIC’s dual mandate of being financially sustainable and developmentally effective, the IIC early on adopted credit practices which created a sound credit driven organization with a strong development focus. Over the last decade, the IIC has worked with OVE to implement an evaluation system, including the adoption of the DIAS system that is compatible with many of the evaluability requirements. As the private sector windows work together to develop a unified evaluability tool, the IIC seems well prepared to converge in the use of these methodologies.</td>
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<td>OVE recommended to expanding and formalizing IIC’s evaluation system, with a focus on enhancing the usefulness of lessons learned, promoting accountability, and generating efficiencies across IDB</td>
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<td>The IIC is planning to conduct case studies to evaluate IIC interventions not only at the project level but on a sector level. Three areas of particular concern have been identified: impact on final beneficiaries in financial intermediary transactions, results from working with large clients, and overall development impact of repeat operations. In addition, program</td>
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<td>Group’s private sector windows.</td>
<td>evaluations such as FINPYME Credit will be carried out. The IIC will benefit from thematic sector and program evaluations by gaining better understandings of the results of its lending which will lead to improved products, services, and methods of intervention. These initiatives go beyond the scope of the OVE - IIC evaluation services agreement and funding issues remain to be addressed. OVE’s services to the IIC are mainly focused on project-level evaluations and related services; however, the IIC would benefit from expanded evaluation services. The IIC is proposing a more systematic approach to evaluation and is looking into other models of MDB’s approaches to evaluating private and public sector activities. For example, the Independent Evaluation Group (IEG) of the World Bank Group in which the IFC is fully integrated into public and private sector evaluations of World Bank programs is an interesting model.</td>
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**Concluding Remarks:**

1. The IIC’s evaluation system is fully compliant with the Good Practice Standards (GPS) for Private Sector Operations issued by the Evaluation Cooperation Group of Multilateral Development Banks (ECG-MDBs). A Third Benchmarking Review commissioned by the ECG concluded that the IIC had the most harmonized evaluation system among all private sector windows of MDBs, including the IFC and EBRD. The review was designed to compare the evaluation practices of multilateral development banks against agreed-upon good practice standards. It concluded that the IIC’s evaluation system met 98% of the ECG-MDB good practice harmonization standards. The review also highlighted the importance of the IIC’s commitment to evaluation.

2. However, Management does not interpret these results as a resting place. On the contrary, IIC is already working on an enhanced DIAS with indicators that go beyond GPS requirements. These indicators will allow more in-depth evaluation of projects and, ultimately, better development results.
Annex A:

**IIC Actions to improve Development Effectiveness**

- In 2012, the IIC underwent some internal restructuring which elevated the Development Effectiveness team from a unit to a division, reporting directly to the General Manager. This change reflects Management’s strong commitment to enhancing development effectiveness, part of the IIC’s dual mandate as a credit-sound organization with a strategic developmental focus.

**Monitoring and Evaluation**

- In 2011, all 60 approvals received a DIAS score. In 2012, 65 projects were approved and in the first four months of 2013, ten projects were approved. Another 22 projects in the pipeline have received a DIAS score. This brings the total to 443 approved projects scored-to-date in the IIC’s development database.

- For the fourth consecutive year, investment officers monitored development indicators during project supervision in the same way they do for financial indicators. The information collected is included in the Annual Supervision Reports. In 2011, 110 operations were updated, and another 130 operations were updated in 2012.

- In 2012, the IIC produced XASRs evaluating 18 projects, including 15 corporate projects and 3 projects with financial intermediaries. Also in 2012, OVE validated 24 IIC project evaluation reports—11 corporate projects and 13 projects with financial intermediaries—88% of which achieved high development outcomes, compared with 81% in 2011.

- In 2012, the IIC made significant progress in developing the DIAS Plus Matrix, or an expanded DIAS with a more sharpened focus on key development results. The matrix is organized along the IIC’s nine industries, with a separate template for each industry. Each template consists of cross-cutting indicators as well as sector specific indicators that will facilitate the aggregation of project results. The DIAS Plus Matrix will be filled out with baseline and target indicators. Additionally, each year during the life of the project, indicators will be input with recent data so as to track the progression of a project from start to finish. The DIAS Plus Matrix is expected to be implemented in the second half of 2013. A pilot phase, lasting between 6 months to a full year, will test the soundness of the instrument, the data, and the process.

- The IIC has been continuing its efforts to update its Lessons in Action database. This knowledge management tool facilitates the documentation of lessons learned and project experiences both at the IIC and within the IDB Group. Currently, the Lessons in Action website contains more than seventy IIC lessons learned, with plans to expand the database in 2013 though new lessons drawn primarily from 2010 XASRs and OVE’s
recommendations in its 9th Independent Evaluation Report. The updated database will help identify, document, disseminate, and further apply lessons learned from collective operational and corporate practices. The tool represents an important step toward building an institutional knowledge base on issues relating to SME development. Once the database is brought up to date, a second phase will begin which aims to fully integrate lessons into the project cycle through widespread training in future lesson documentation and increased awareness of the importance of capturing and using lessons from past experiences to shape and inform future operations in the region. Emphasis will be on dissemination through brown bag lunches and seminars with investment officers.

**Harmonization Efforts**

- In recent months, the IIC has been in close and frequent contact with its peers in SCF in an attempt to harmonize efforts, especially with regards to sector indicators included in both windows’ new results framework matrices. The coordination will continue as the results measurement instruments evolve. SCF is currently implementing some changes to its Development Effectiveness framework; it is implementing a) a revised Development Effectiveness Matrix (DEM), b) a new Results Matrix and c) a revised Evaluability checklist. The revised DEM is very similar to the DIAS and maintains basic alignment with good practice standards; the most significant difference is a difference in methodology in how both units approach scoring non-financial additionality.

- Early 2013 also marked the beginning of a joint IDB-IIC effort to develop a renewed vision for the IDB Group’s work within the private sector. A working group has been set up with members of all four private sector windows of the IDB Group, including four IIC employees from the Operations, Legal, and the Development Effectiveness Divisions. The Working Group aims to develop a Results Framework according to five designated Priority Business Areas: increasing MSME access to finance, developing infrastructure for competitiveness and global and regional integration, promoting competitiveness through innovation, promoting the social inclusion and economic empowerment of vulnerable populations, and fostering green growth through environmental sustainability.

- The IIC, along with SCF, continues to participate in the Development Results Indicators Harmonization Working Group to further harmonize development indicators—including cross-cutting and sector specific indicators—for private-sector oriented development finance institutions (DFIs). In 2012, the Working Group hired a consultant to coordinate harmonization efforts among the various DFIs. The IIC has been an active participant in this harmonization exercise and participated in a March 2013 London meeting with other DFIs where consensus was reached on some first indicators. Discussions on remaining indicators, methodology, and outstanding harmonization issues continue to be addressed by the Working Group. Most recently, the IIC reviewed and commented on a third draft of proposed harmonized indicators, and has carefully considered the Working Group’s harmonization efforts when defining its own set of indicators to be used in the DIAS Plus tool.

- In early 2013, FinnFund approached the IIC asking to use the DIAS as a benchmark for the evaluation of its ex-ante appraisal tool called the Development Impact Assessment Tool (DIAT). This demonstrates the DIAS’ strong reputation among its DFI peers.

**Strengthened Focus on Additionality: Technical Assistance**
In 2012, the IIC, with the support of a consulting firm, developed a measurement framework for its technical assistance operations, called the DIAS for TAS. The DIAS for TAS enables the IIC to measure development results of technical assistance products. Currently, this measurement framework is being assessed and discussed by TAS officers along with members of various divisions of the IIC; it will be implemented as soon as consensus is reached.

In 2012, IIC donors approved US$9.3 million in funding under the IIC’s six technical assistance programs. Contributions from Austria, France, Italy, Norway, the Republic of Korea, Spain, Switzerland, and the United States, as well as Belgium’s Walloon Region, the Clean Technology Fund, and the Nordic Development Fund, helped ensure the continued delivery of training and technical assistance services to thousands of Latin American and Caribbean SMEs looking to enhance their management and planning capabilities.

Moreover, under the FINPYME Diagnostic program the IIC received resources from the US Government to implement FINPYME Mujer Empresaria, a gender focused version of the diagnostic methodology in El Salvador and Peru. For the FINPYME ExportPlus program, the IIC received approval from Korea to deepen its activities in Guyana and Suriname and to launch the program in Jamaica. And the Italian government provided resources to launch the program in Bolivia. Under the FINPYME Family Business program, resources were approved by Korea to provide IIC clients with knowledge and tools on how to improve their corporate governance. Jointly with the FINPYME Technical Assistance program five current IIC clients received advisory services in issues related to governance of family-owned SMEs. Furthermore, under the FINPYME Technical Assistance program, starting in May 2012 DEC and TAS jointly developed a procedure to streamline technical assistance (TA) into the IIC’s operations. As a result, eleven companies received advisory services to enhance their competitiveness, develop feasibility studies and environmental and social reviews and to monitor the construction of projects. Under the same program the IIC received resources to retain consultants to work at headquarters and in the region in the execution of technical assistance programs and in the identification of potential IIC clients. Under the GREENPYME Program, the IIC received resources from Korea to complement the scholarship program by providing training in Korea to 11 participants and also received resources from the Clean Technology Fund to continue GREENPYME activities in Colombia. Finally, the IIC received resources from Korea to start the implementation of a knowledge network for SMEs in the Latin American and the Caribbean region.

Strengthened Focus on Additionality: Environmental and Social Sustainability

A large part of the IIC’s additionality efforts in recent years has focused on promoting environmental and social sustainability. In October 2012, the IIC launched its third Sustainability Week with two training workshops in Panama City. The workshops were designed to provide financial institutions with useful tools for making sustainability a crosscutting focus of their practices, and to raise awareness among SMEs about the importance of energy efficiency. These activities formed part of the IIC Sustainability Week, an IIC capacity-building initiative consisting of workshops geared to financial intermediaries and their clients. In 2012, the Environmental Risk Management for the Financial Sector workshop was organized by the IIC in collaboration with the IDB’s Environmental Safeguards Unit (ESG), and the energy efficiency workshop was organized by IIC in collaboration with Banco General. Previous partner local banks for
the Sustainability week workshops in 2011 and 2010 include Banco Itaú-Unibanco and BAC San José. Over the past three years a total of 103 participants from 63 financial institutions have attended the workshops. In addition, training was provided to the SME clients of BAC San José, Itaú-Unibanco, Banco General, as well as NGOs and other companies as part of an additional workshop held on risks and opportunities in energy efficiency and climate change. Approximately 185 participants attended these energy efficiency workshops.

- In 2012 the IIC began working on developing a new Environmental and Social Sustainability Policy, which will be submitted to the IIC Board for approval in the second quarter of 2013. The purpose of the new policy is to convey the IIC’s commitment to sustainable development, an integral part of its approach to risk management, as well as its development mandate.

Strengthened Focus on Additionality: Corporate Governance

- In September 2011, the IIC joined 29 development finance institutions in signing the Corporate Governance Development Framework, a set of guidelines for promoting good corporate governance in lending and investment activities. As part of the working group, the IIC has made significant advancement in developing a corporate governance screening questionnaire to be used for the evaluation of potential IIC clients. In January 2013, the IIC held an Investment Officer training workshop regarding the questionnaire and identifying corporate governance risk. As part of the working group, IIC’s Senior Corporate Governance Officer participated in the Corporate Governance Development Framework meeting that took place in February 2013 in the Philippines. Regarding client support on Corporate Governance, the IIC held a client training workshop in November 2012 to promote good corporate governance practices by family-owned businesses in Cancun. 43 representatives of 17 SMEs attended the workshop. The participants received training in areas such as the role of women in family businesses, the role and duties of the board of directors, succession planning, and the intergenerational transfer of ownership. In September 2013, the IIC will organize its second client training workshop in Lima, Peru with approximately 60 representatives from family businesses in the region. In addition, over the course of 2012, five one-on-one technical assistance projects were implemented for family-owned SMEs in Mexico, Costa Rica, and Paraguay. The IIC also provides group workshops for non-clients to promote good governance practices through its FINPYME Family Business program. In September 2012, two workshops were organized in Medellin and Cali, Colombia with a total of 133 representatives from 59 SMEs participating.