An illustration of a woman with dark skin and hair, wearing a yellow turtleneck sweater and teal pants. She is shown in profile, looking to the left, and is holding several large, colorful puzzle pieces (orange, blue, red) that are scattered around her. The background is white with a pattern of small, light pink dots.

Addressing Country- Level Fiscal and Financial Sector Vulnerabilities

An Evaluation of the World
Bank Group's Contributions



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**WHAT
WORKS**

Addressing Country- Level Fiscal and Financial Sector Vulnerabilities

An Evaluation of the World
Bank Group's Contributions

July 21, 2021

Contents

Abbreviations	v
Acknowledgments	vi
Overview	viii
Management Response	xiv
Chairperson's Summary: Committee on Development Effectiveness	xxiii
1. Background and Context	1
Purpose of the Evaluation	3
2. Identifying Vulnerabilities	8
Country-Level Diagnostics	10
World Bank Support for Identifying Fiscal and Financial Sector Vulnerabilities	11
Client Feedback, World Bank-IMF Collaboration, and Data Issues	17
3. Bank Group Support for Reducing Vulnerabilities	21
Highlights	21
Bank Group Support to Clients in Addressing Vulnerabilities	22
Impact of Bank Group Support in Reducing Country-Level Vulnerabilities	26
4. Making Social Safety Net Systems Adaptable to Economic Downturns	35
Safety Net Crisis Preparedness at the Program, System, and Policy Level	39
5. Conclusions and Lessons	46
Lessons	47
Bibliography	49

Boxes

Box 1.1. Evaluation Scope	3
Box 2.1. Macro-Financial Review and Identification of Vulnerabilities	9
Box 2.2. Integrative Diagnostics Identifying Key Vulnerabilities: Morocco and Ukraine	10
Box 3.1. From Debt Sustainability to Debt Tolerance	28
Box 3.2. International Finance Corporation's Innovative Assistance for Crop Receipts	31
Box 3.3. World Bank Treasury Assistance for Risk Management, Hedging, Reserve Management, and Support for Local Currency Debt Markets	31
Box 4.1. The World Bank's Global Social Safety Network	38

Figures

Figure 1.1. Conceptual Framework Guiding the Evaluation	5
Figure 2.1. Indicators of Fiscal Vulnerability: Ratio of Interest Payments to Tax Revenue (percentage)	13
Figure 2.2. Indicators of Fiscal Vulnerability: Ratio of Gross Government Debt to Gross Domestic Product (percentage)	14
Figure 3.1. Indicators of Financial Sector Vulnerability: Ratio of Nonperforming Loans to Total Loans (percentage)	29

Tables

Table 2.1. Typology of Fiscal and Financial Vulnerabilities Identified in the World Bank's Country-Level Diagnostics for Case Study Countries	12
Table 2.2. Quality of Data on Fiscal and Financial Vulnerabilities	19
Table 3.1. Coherence between Vulnerabilities and World Bank Group Support	24
Table 3.2. Assessment of World Bank Group Effectiveness in Reducing Vulnerabilities and Improving Internal Coordination	27
Table 3.3. Outcomes of Projects and Development Policy Financing Focused on Fiscal and Financial Vulnerabilities	33

Appendixes

Appendix A. Evaluation Design and Methodology	56
Appendix B. Key Fiscal and Financial Sector Indicators for Case Study Countries	72
Appendix C. Identification and Assessment of Fiscal and Financial Sector Vulnerabilities (2010–15 and 2016–18)	86
Appendix D. Comparative Fiscal and Financial Vulnerability Indicators in Case Study Countries	97
Appendix E. Making Social Safety Nets Adaptable to Crises	99

Abbreviations

ASA	advisory services and analytics
CEM	Country Economic Memorandum
COVID-19	coronavirus
DeMPA	Debt Management Performance Assessment
DPL	development policy loan
DSA	Debt Sustainability Analysis
FSA	Financial Stability Assessment
FSAP	Financial Sector Assessment Program
FSSA	Financial Sector Stability Assessment
GDP	gross domestic product
HSNP	Hunger Safety Net Program
IDA	International Development Association
IEG	Independent Evaluation Group
IFC	International Finance Corporation
IMF	International Monetary Fund
NPL	nonperforming loan
SCD	Systematic Country Diagnostic
SOE	state-owned enterprise

All dollar amounts are US dollars unless otherwise indicated.

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Željko Bogetić (lead economist) led the evaluation team and case studies on Jamaica, Morocco, Tajikistan, and Ukraine. Felix Oppong (economist) coauthored the case studies on Benin and Mozambique. Melvin Vaz (senior evaluation officer) coauthored the case studies on Mozambique and Ukraine. Jeff Chelsky (manager) was the lead author of the case study on Bangladesh and coauthored the case study on Ukraine. Shahrokh Fardoust (consultant) coauthored the case studies on Bangladesh and Tajikistan and supported the preparation of the overall Approach Paper. Reza Vaez-Zadeh (consultant) coauthored the case studies on Benin and Morocco and contributed on financial sector issues. Amitava Bhanerjee (consultant) contributed to the case study on Bangladesh and advised on International Finance Corporation-related issues. Ana-Maria Arriagada (consultant) led the work on the social safety nets. Augusto de la Torre (consultant) contributed early advice on financial sector issues. Amshika Amar (consultant) contributed to the Jamaica case study. Johan Manuel Lopez (consultant) provided research analyst support. Dung Thi Kim Chu provided team administrative assistance and logistical support. Cheryl Tokoza was the report's primary editor.

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Overview

Proactively reducing fiscal and financial sector vulnerabilities and strengthening frameworks and institutions for crisis management can make the difference between whether a country bounces back quickly from an unexpected shock or struggles for years to regain its footing.

More than a decade has passed since the global economic and financial crisis rocked the world. A clear lesson that emerged from it was the importance of identifying and addressing country-specific vulnerabilities *ex ante* to build resilience when a shock occurs. The passage of time has given the Independent Evaluation Group (IEG) the opportunity to assess the extent to which the World Bank Group has internalized the importance of addressing country-level vulnerabilities during good times to withstand exogenous shocks when they come.

The 2020 global economic and health crisis caused by the coronavirus (COVID-19) pandemic serves as yet another stark reminder of the importance of proactively managing vulnerabilities to shocks. Immense global public health, demand, and supply shocks hit all countries hard and at nearly the same time, precipitating the deepest peacetime global economic crisis since the Great Depression.

The purpose of this evaluation is to assess Bank Group support to client countries to build resilience to exogenous shocks through the systematic identification of *fiscal and financial sector vulnerabilities* and through efforts to support the reduction of these vulnerabilities. Given the importance of protecting the most vulnerable from shocks, this evaluation also looks at the extent to which the Bank Group has helped client countries adapt their social safety nets so that they can be effectively scaled up in a crisis.

The evaluation looks at the period between 2010 and 2019, after the global recession. It assesses the extent to which the World Bank has been able to assist clients in identifying and reducing fiscal and financial sector vulnerabilities to build resilience to shocks. It aims to inform the design of future Bank Group strategies, operations, diagnostics, and knowledge products that

can help reduce country-level fiscal and financial sector vulnerabilities. Its lessons may also help the effort to “build back better” after the COVID-19 pandemic through contributions to increasing resilience by strengthening fiscal and financial buffers and institutions.

The evaluation covers the three main Bank Group institutions: the World Bank, the International Finance Corporation, and the Multilateral Investment Guarantee Agency. Given the criticality of country context to understanding vulnerabilities, these questions are answered by drawing primarily on case studies of seven countries with which the Bank Group has been continuously engaged over the review period: Bangladesh, Benin, Jamaica, Morocco, Mozambique, Tajikistan, and Ukraine. The case study approach comes with inherent challenges, including ensuring that insights and lessons have sufficient external validity. These challenges have, in part, been mitigated through the careful selection of case studies reflecting diverse degrees of engagement, consistent implementation of the evaluation strategy, and the convergence of findings and patterns.

Main Findings

Identifying Fiscal and Financial Vulnerabilities

A country’s ability to respond to major shocks promptly with appropriate policies depends to a large extent on the adequacy of its preexisting fiscal and financial buffers and the quality of its fiscal and financial sector institutions. This evaluation finds that the Bank Group has generally carried out timely and relevant analyses at the country level to better understand emerging risks and sources of fiscal and financial sector weaknesses. Identification of financial sector vulnerabilities has been, in general, consistent and comprehensive. Identification of fiscal vulnerabilities has been good, although the consistency and completeness of those assessments has varied, especially with respect to quasi-fiscal pressures from state-owned enterprises and contingent liabilities.

Financial sector work is perceived as less politicized by many counterparts, in part reflecting the nature of programs like the Financial Sector Assessment Program (FSAP) and related technical assistance. This can give an

easier entry point for discussions with authorities. Fiscal analysis, however, tended to be more political, and World Bank advice was subject to greater discretion at the country level.

The World Bank's core fiscal and financial sector diagnostics, when available, were of high quality. Its ability to conduct diagnostics was sometimes constrained by a lack of good quality data and insufficient country-level transparency, including with respect to the reliability of debt data in countries with weak disclosure practices. This was a significant constraint on the World Bank's ability to accurately assess fiscal vulnerabilities.

Debt Sustainability Analyses (DSAs) are central to gauging low-income country risk of debt distress. However, underlying assumptions were sometimes overly optimistic, or downside risks were sometimes underestimated, particularly with respect to the contingent liabilities of state-owned enterprises or in assessing the potential impact of a compounding of vulnerabilities. Our case studies cover the period from 2010 to 2019, with the revised International Monetary Fund (IMF)–World Bank Debt Sustainability Framework for Low-Income Countries only introduced in 2018. As a result, many of the case studies make use of the prereform DSA, which has, at times, contributed to the underestimation of fiscal risks.

Identification of fiscal vulnerabilities did not always take a whole-of-government perspective, thereby missing important links among vulnerabilities (for example, state-owned enterprises; state-owned banks; contingent liabilities; and large public investment projects). Among our case studies, we observed that this has led to an understatement of fiscal risks in Bangladesh and Tajikistan.

In most case studies, the World Bank's diagnostic work on the financial sector was comprehensive and credible. This, in part, reflected the rigor of the FSAP and associated technical assistance. However, the need to coordinate with the IMF on FSAP work, and the IMF's prioritization of scarce technical resources on systemically important economies, sometimes constrained the availability to the Bank Group of timely financial stability assessments of smaller or less systemically important economies.

Addressing and Reducing Fiscal and Financial Vulnerabilities

The evaluation finds that countries that received and acted on Bank Group support to address fiscal and financial sector vulnerabilities were generally better prepared to respond to a major shock today than previously. Earlier IEG work found that the Bank Group was generally effective in helping countries *respond to* fiscal and financial sector crises. This evaluation finds that, outside the context of stabilization efforts, it was less effective in working with clients to proactively expand buffers, strengthen institutions, and build capacity for better crisis management.

The reasons for this are several. Earlier IEG evaluations on crisis response have shown that the focus of Bank Group and country efforts postcrisis was often on growth, building buffers and strengthening institutions, and improving the quality of public investment tended to be a lesser priority. In some cases, governments may be less prepared to undertake difficult institutional reforms without the pressures of a crisis.

However, even when conditions were not supportive of comprehensive reform, the Bank Group was generally able, often in coordination with development partners (and the IMF in particular), to build understanding and awareness of challenges and vulnerabilities through analytical work and policy advice.

Building Resilience by Making Social Safety Nets More Adaptable to Economic Downturns

Fiscal and financial crises have distributional consequences and, therefore, require flexibility in safety net systems to cushion the impact quickly and efficiently. Although the World Bank's direct support for social safety nets increased during the evaluation period, especially in low-income countries, it tended to focus more on expanding access to chronically poor people than on building adaptable systems to respond to cyclical or more severe downturns.

But the World Bank is increasingly working with clients to incorporate an “adaptive social protection” approach to reduce the vulnerability of poor and near-poor populations to shocks by building household resilience and

enhancing safety net preparedness through flexible and scalable program designs and dynamic delivery systems.

Despite progress to strengthen social protection delivery systems and social safety net programs, important challenges remain. Coverage of social safety nets is limited, especially in low-income countries, where automatic stabilizers tend to be limited as they do not generally extend to the informal sector. Financing and institutional issues constrain the intake of beneficiaries, registration, and targeting.

Is the Bank Group Equipped to Help Clients Strengthen Fiscal and Financial Sector Resilience?

Building resilience requires knowledge and timely diagnostics, which can be difficult to undertake in the middle of a crisis. To be prepared, clients need to systematically and frequently consider the potential impact of exogenous shocks of various magnitudes. The Bank Group can, as part of its country-level macrofinancial monitoring, make reducing fiscal and financial sector vulnerabilities a more central part of its activities.

The Bank Group has strong staff skills, motivation, and capacity to support clients in identifying and helping reduce fiscal and financial sector vulnerabilities. However, larger countries often absorb the most experienced and skilled staff, at the expense of attention to smaller, lower-income countries. Moreover, the division of labor with the IMF on financial sector issues constrained the Bank Group in its ability to provide timely financial sector support to smaller economies that are not deemed systemically important.

Lessons

This evaluation proposes five lessons on how the Bank Group can improve the identification of and response to fiscal and financial sector vulnerabilities, and support countries in reducing them.

First, up-to-date, accurate, and timely knowledge is the foundation of effective Bank Group support to its clients. It is therefore important for the Bank Group to remain engaged in regular and systematic monitoring and core diagnostics of fiscal and financial vulnerabilities *even when client countries*

are not ready to confront them. This includes attention to the quality of data and to transparency.

Second, the Bank Group is better able to support countries in reducing vulnerabilities when building fiscal and financial resilience is fully and explicitly integrated into Bank Group–supported country strategies, with a clear articulation of priority challenges. Where knowledge is incomplete, analytical and diagnostic needs should be clearly articulated and planned for.

Third, more systematic consideration of the impact of large and compound fiscal and financial sector risks (for example, from state-owned enterprises and contingent liabilities), including in DSAs, is needed to inform policy dialogue with clients.

Fourth, with the IMF increasingly concentrating its financial sector surveillance on systemically important countries, the Bank Group should consider how best to give adequate attention in its financial sector diagnostic work to financial stability issues in less systemically important but potentially vulnerable economies. This may have implications for the division of labor with the IMF on financial sector work as well as resource costs that should be clearly identified and managed.

Fifth, addressing fiscal and financial vulnerabilities is intensely political, with vested interests sometimes opposing appropriate policy reforms and institutional strengthening. To help build domestic demand for better preparedness, Bank Group staff should seek to more regularly undertake outreach and dialogue with parliamentarians, civil society, and local think tanks to foster an understanding of vulnerabilities and their potential costs in an effort to build support for critical reforms.

Management Response

World Bank Management Comments

World Bank management would like to thank the Independent Evaluation Group (IEG) for undertaking this evaluation of the World Bank Group’s engagements addressing country-level fiscal and financial sector vulnerabilities. Lessons learned from the evaluation are directly relevant to recent challenges and policy commitments and will inform World Bank support to client countries facing adverse fiscal and financial shocks exacerbated by the coronavirus (COVID-19) pandemic.

The COVID-19 crisis and its far-reaching impacts have highlighted the importance of integrating monitoring of macrofinancial risks across sectors of the economy. The World Bank has scaled up monitoring of macrofinancial risks, including by focusing macrofinancial reviews on crisis-related risks and their management, stepping up real-time monitoring of revenue developments, increasing surveillance on fiscal risks from state-owned enterprises (SOEs), and enhancing surveys on the accumulation of public expenditure arrears in client countries. Monitoring of fiscal developments in countries participating in the Debt Service Suspension Initiative, undertaken jointly with the International Monetary Fund (IMF), has identified fiscal impacts and responses as well as additional financing needs in low-income countries. To help countries monitor fiscal impacts and design appropriate fiscal strategies, the World Bank has established a COVID-19 fiscal policy window that provided support to 20+ countries by mid-April 2021.

Management notes the IEG evaluation’s conclusion that the Bank Group’s work on addressing fiscal and financial sector vulnerabilities in client countries is both relevant and effective. Management agrees that “the Bank Group has generally carried out timely and relevant analyses at the country level” and that countries that received Bank Group support “were generally better prepared to respond to a major shock today than previously.” Management acknowledges that this has been possible, among other reasons, because “the World Bank Group has strong staff skills, motivation, and capacity to support

clients in identifying and helping to reduce fiscal and financial sector vulnerabilities.” Management believes that the World Bank’s strong country presence contributes greatly to this high level of effectiveness. This evaluation’s findings will enrich management’s continuous efforts to help clients manage fiscal and financial risks and build resilience to external shocks, particularly in the most vulnerable countries.

Management is pleased that the report recognizes the country engagement model’s catalytic role in guiding lending and advisory services and analytics to address fiscal and financial sector vulnerabilities and notes that stakeholder engagement is critical to this model. The report notes that “in all case study countries, a review of diagnostic work and subsequent World Bank–supported country strategies indicates that identified vulnerabilities informed Bank Group lending and subsequent ASA [advisory services and analytics].” This finding highlights the country engagement model’s core strength: that it builds selectively on countries’ own development priorities and articulates results-based engagements based on solid analytical diagnostics and stakeholder consultation. Management agrees with the report that the latter is particularly relevant for efforts to address fiscal and financial vulnerabilities, which are intensely political and subject to vested interests opposing appropriate policy reforms. The report also recommends ensuring dialogue with a broad range of stakeholders (parliaments, local institutions, and the public) to educate and build support for critical reforms. Management emphasizes that such dialogue is already part of the country engagement model and at the core of its operational, policy, and analytical work. This dialogue also includes close engagement with other multilateral development banks (for example, through country platforms on debt issues), which has not been captured in the report.

Management appreciates the rigor with which the case studies were conducted and concurs with the report’s assertion that its “external validity is limited and may apply to countries with similar characteristics to those of the case studies.” Given the context-specific nature of fiscal and financial risks, which vary considerably in origin, impact, management, and government involvement, some of the general conclusions and lessons learned would benefit from further qualification. Notable examples include broad statements about the inability of Debt Sustainability Analysis (DSA) to

capture and estimate risks, a statement that is based on evidence from one country (Benin) collected before the revision of the Low-Income Countries Debt Sustainability Framework (LIC DSF) in 2018. Notwithstanding these limitations, some of the lessons the evaluation provides shed light on areas for further improvement.

Management shares the view that data quality and transparency are essential for continuous monitoring of country-level vulnerabilities. Fostering greater debt transparency is one of the key aspects of the implementation of the Sustainable Development Finance Policy (SDFP) introduced in FY21. The SDFP creates incentives, particularly in the poorest countries, to make progress on performance and policy actions related to addressing debt vulnerabilities. The performance and policy actions help increase transparency (for example, on publication of detailed information on debt, including SOE debt), which informs external and domestic stakeholders and increases scrutiny. The report could better reference (i) how SDFP implementation—outside the period under evaluation—brings the issues of data quality and transparency to the forefront of World Bank dialogue with IDA clients, and (ii) the conclusions of the Non-Concessional Borrowing Policy (NCBP) review after the transition from NCBP to the SDFP in FY21. Several complementary adjustments on the macroeconomic and growth side will be critical to dealing structurally with debt vulnerabilities, and the policy dialogue on debt issues must be anchored in a country program of broader fiscal, macroeconomic, and structural reforms, as the evaluation suggests. Lessons learned from debt relief initiatives, such as the Heavily Indebted Poor Countries and the Multilateral Debt Relief Initiative, highlight the importance of building a strong track record of fiscal, macroeconomic, and structural reforms to address debt vulnerabilities. Debt-related policy dialogue often spills over into broader reform engagements. For example, in some countries, the policy dialogue on debt ceilings in the context of IDA's NCBP significantly deepened reform engagements in other related areas, such as debt management and debt transparency.

Management agrees on the need to integrate risks from contingent liabilities into policy dialogue. In addition, countries are exposed to a wide variety of exogenous shocks that the report does not consider. Addressing fiscal and financial sector vulnerabilities often requires managing certain risks

up front, for example, through early warning systems, food reserves, and so on. Crisis preparedness and risk finance can help vulnerable countries secure prearranged funding to respond to these exogenous shocks, including through market-based financial solutions such as insurance. Quantifying such compound risks and embedding them within financial risk management frameworks is a crucial starting point. The discussion of risk monitoring, which focuses on DSA and the Financial Sector Assessment Program (FSAP), could have acknowledged that managing fiscal and financial sector risks also requires a good understanding of potential risks and their impact, likelihood, and possible mitigation measures.

The claim that the DSA framework is systematically biased to underestimate fiscal risks and does not always capture some extreme scenarios is noted. Realism of growth and financing projections in DSAs is being reviewed more thoroughly. Additionally, the LIC DSF revised in 2018 places greater emphasis on fiscal risks and aims by default at near complete debt coverage of the public sector in the baseline scenario, including risks from SOEs, extrabudgetary funds, and subnational governments, among others. Management is revamping efforts to assess additional risks (for example, natural disaster and climate-related risks) as part of fiscal and debt sustainability assessments. For example, an enhanced approach in the revised LIC DSF expands the stress testing framework to more systematically capture vulnerability to natural disasters and climate shocks.¹ The World Bank along with the IMF has piloted assessments of climate-related financial sector risks and regulatory responses in the context of FSAPs, and further work is under way.

Management concurs that support to smaller economies to address fiscal and financial vulnerabilities should be provided whenever requested and justified and believes that its work through FSAP in these countries is not adequately characterized in the report. Although the report highlights that the “World Bank’s diagnostic work on the financial sector was comprehensive and credible . . . in part [due to] the FSAP and associated technical assistance,” it also claims that the division of labor between the World Bank and the IMF “may have constrained the Bank Group in its ability to provide timely support to smaller economies that are not deemed systemically important.” Notwithstanding the benefits of close collaboration between the World Bank and the IMF in this area, the report could have recognized the modular approach

embedded in the FSAP, including the World Bank's ability to support smaller economies by conducting stand-alone FSAP development modules. The FSAP development modules do not require IMF participation and focus primarily on financial sector development challenges, with the timing and country selection left to the World Bank's discretion and subject to country demand.

Management is pleased that the report highlights the World Bank's critical role in supporting client countries in strengthening social safety nets (SSNs) but notes that SSN adaptability depends on country contexts. The report's recommendation to build adaptive SSNs to respond to cyclical and uncommon downturns cannot be generalized for a broader range of World Bank clients. Focusing on SSN adaptability as the key dimension to evaluate crisis preparedness may be appropriate for countries where such systems already exist, but for the many low-income countries that initially have no such systems (for example, Benin, Mozambique, and Tajikistan in the sample), crisis preparedness may be more reasonably evaluated by whether that system was put in place or not.

International Finance Corporation Management Comments

International Finance Corporation (IFC) management would like to thank IEG for this evaluation report, which provides valuable insights on the effectiveness of the Bank Group interventions in addressing fiscal and financial sector vulnerabilities. Although the scope of the analysis was mostly on the public sector efforts supported by the International Bank for Reconstruction and Development (IBRD) and the International Development Association (IDA), we welcome the lessons learned from the review and appreciate IEG's recognition of IFC's contributions to building resilience in these areas.

Building resilience has been at the heart of IFC's mission, as has been evident in our work to support our clients during the COVID-19 pandemic. We appreciate that IFC is well-recognized in this report for its complementary role to IBRD's projects in building resilience in the financial sector through its direct project and advisory support as described in the case studies on

Ukraine, Tajikistan, Mozambique and Bangladesh. In fact, IFC's approach to resilience building in our client markets is underpinned by multiple IFC solutions: country-level tools to identify risks, analytical products to gain insights, upstream and mainstream investment and advisory services across global, regional, and country levels. IFC Advisory Services team works collaboratively with IBRD in areas including the support in building and improving financial infrastructure, and policy advisory on public-private partnership frameworks and investment. IFC's collaboration with IBRD via the Joint Capital Markets Initiative supports the development of local capital markets, contributing to building resilience of the financial markets as it promotes the mobilization of stickier, local capital. IFC is well positioned to support the Bank Group Cascade approach, which allows the freeing up of considerable government resources and, therefore, significantly reduces fiscal vulnerabilities.

IFC management appreciates the lessons learned of the report and observes the critical role the private sector can play in addressing vulnerabilities. Given that public-private partnerships can be a sizeable presence and source for contingent liabilities, it would be critical to examine the role IFC can play through both advisory services and investment projects to contribute to the strengthening of resilience in the fiscal space as they identify project-related liabilities and the likelihood of these to materialize. Furthermore, the report mentions the challenges faced by IBRD operations in conducting adequate surveillance, in particular on those countries whose financial systems are not considered to present systemic importance, yet are recognized to be potentially highly vulnerable. In our view, this presents an opportunity for IFC's risk assessment and surveillance procedures to play a supplemental role. Doing so may require an in-depth analysis on how best to integrate existing reporting, analysis, and insights, leveraging country-level tools such as Country Private Sector Diagnostics or country and regional strategies.

IFC management strongly agrees on the challenges surrounding data, especially on contingent liabilities and SOE vulnerability. Data on contingent liabilities and SOEs may not always be systematically collected or may be treated as confidential and accordingly not disclosed beyond a close government circle. Systematic collection of contingent liability and SOE performance data would critically improve crisis preparedness but will require

concerted action with the IMF and others, and a long-term investment in capacity building. Data availability will help in more accurately assessing the problem and in fostering transparency. Although the availability of data will help building fiscal resilience, it is also essential to acknowledge that the risk of contingent liabilities in terms of size and/or unpredictability and controllability shall not be overstated, as terminations or similar payments are generally under the control of the government making this type of risk more manageable as any other subsidy, whereas nontermination type of ongoing costs and contingencies are limited.

IFC management believes that digitization plays a critical role in strengthening SSNs. The section on SSNs in this report makes valuable points on the need to preposition beneficiary registries and cash transfer mechanisms that could be scaled up in crises to provide expanded SSNs. The report also addresses the value clients placed on Bank Group support for credit bureaus and other activities that help bank lending practices. This would argue for the potential for the World Bank and IFC to do more using beneficiary registries and cash transfer mechanisms to advance financial inclusion, digitized payments and the use of transaction-based data to break down information asymmetries that impede access to credit and the reach of banks and nonbanking financial institutions. Progress in integrating the potential for e-commerce, e-government (including tax payments) and outsourced credit scoring could lessen vulnerabilities by improving credit underwriting and indirectly by strengthening incentives for formalizing economic activity.

Strong banking system and financial institutions are a key part of financial sector resilience. Although outside of the scope of this evaluation, bottom-up efforts from the private sector that contribute to addressing financial sector vulnerabilities are essential. IFC works on financial sector resilience as it engages with systemically important banks, where we invest in equity, quasi-equity and subdebt instruments. Through its investments in financial institutions, IFC aims to strengthen capitalization and solvency of our clients and doing so with systemically important banks of our client countries greatly contributes to market-wide stability. These efforts are often also accompanied by technical assistance to improve risk management to build resilience in a bottom-up manner. Moreover, as mentioned in the Jamaica and Ukraine examples, IFC through the Distressed Asset Recovery Program

aims to build financial ecosystems to absorb distressed assets in economic downturns and crisis. The program contributes to the resilience of financial systems as it helps the financial sector offload nonperforming assets of systemic banks, resulting in quicker recovery of lending activities. Finally, understanding the vulnerability in the financial sector is critical for an effective support for countries, and data collection efforts like IFC's recent survey on the impact of the COVID-19 pandemic on financial institutions can be used to help clearly identify challenges faced.

Finally, IFC's response to the COVID-19 pandemic focuses on helping clients weather the negative impact of the pandemic, preserving jobs, rebuilding markets, and enabling long-term development of the private sector in the postcrisis period. The IFC 3.0 strategy aims at placing development at the heart of IFC operations; IFC's role in building the resilience of financial sector via its projects is featured in the Anticipated Impact Measurement and Monitoring system, setting incentives for investment and advisory projects to address vulnerabilities in the financial systems. IFC has had a rapid response to the COVID-19 pandemic, introducing expedited procedures and facilities, resulting in the deployment of \$11 billion investment, directly related to COVID-19 relief in from the fourth quarter of FY20 February 2021 (including mobilization and short-term finance). As part of its framework of Relief, Restructuring and Resilient Recovery, IFC continues to focus in the next years on resilience building in emerging economies, further increasing its contribution and strengthen its complementary role to the Bank Group's work to build resilience in the economies.

¹ This applies to small states vulnerable to natural disasters and low-income countries that meet a frequency criterion (two disasters every three years) and economic loss criterion (above 5 percent of GDP per year), based on the EM-DAT database for the period 1950–2015.

Chairperson's Summary: Committee on Development Effectiveness

The Committee on Development Effectiveness met to consider the Independent Evaluation Group (IEG) evaluation entitled *Addressing Country-Level Fiscal and Financial Sector Vulnerabilities. An Evaluation of the World Bank Group's Contributions* and the draft World Bank Group management comments.

The committee welcomed the evaluation, remarking on the timeliness of the discussion in the context of efforts to build back better after COVID-19-related crises. They noted that this evaluation is one of a cluster of four undertaken on interrelated macroeconomic and macrofinancial issues: the public financial and debt management evaluation discussed by the committee in February, 2021, and the upcoming evaluations on domestic revenue mobilization and the sustainable development finance policy. Members welcomed the quality of the report and the rigor with which the case studies were conducted. Members appreciated management's recognition that lessons learned would inform the Bank Group's initiatives to support client countries' efforts to face adverse fiscal and financial risk and build resilience to external shocks.

Members were pleased to learn that the Bank Group's work on addressing fiscal and financial sector vulnerabilities in client countries is both relevant and effective; that the Bank Group's diagnostic work on the financial sector was comprehensive and credible, reflecting the rigor of the Financial Sector Assessment Program; and that countries that received and acted on Bank Group support to address fiscal and financial sector vulnerabilities were generally better prepared to respond to a major shock. At the same time, members expressed concern about IEG's findings that the Bank Group needs to consider fiscal and financial compound shocks more systematically as part of its macrofiscal monitoring; that the Bank Group's ability to produce timely and comprehensive assessments of the financial sectors of smaller economies is constrained by the division of labor with the International Monetary

Fund on Financial Sector Assessment Program work; and that Debt Sustainability Analysis was sometimes overly optimistic giving a misleading impression of vulnerabilities or underestimating of fiscal risks. Members asked IEG about views on how to overcome these challenges and encouraged management to address challenges to strengthen social protection delivery systems and social safety net programs.

1 | Background and Context

Context

Shocks come in all shapes and sizes, often without warning, and with potentially devastating impacts on economies, livelihoods, and populations. Reducing vulnerabilities to help cushion the impact of shocks and help economies recover more quickly is therefore a priority for policy makers.

Lessons from previous crises make clear that identifying and addressing country-specific vulnerabilities before a shock provides the opportunity to adopt policies that enhance resilience.

This evaluation assesses World Bank Group support to client countries to enhance their preparedness for shocks through the systematic identification of fiscal and financial sector vulnerabilities, as well as support to address these weaknesses. Previous Independent Evaluation Group evaluations have assessed the Bank Group's contribution to building resilience to natural disasters.

The massive 2020 global economic crisis caused by the coronavirus (COVID-19) pandemic highlighted why preparedness is so critical. Immense global public health, demand, and supply shocks hit all countries hard and at nearly the same time. The result was the deepest peacetime global economic crisis since the Great Depression. To a significant extent, the depth of the economic and social impact was a function of each country's preexisting fiscal and financial vulnerabilities; the strength of their fiscal and financial sector policies and institutions; and the size, flexibility, and adaptability of their social safety nets.

Previous crises have underscored this point.¹ A clear lesson in the wake of the 2008 global financial crisis was the importance of identifying and addressing country-specific vulnerabilities ex ante to provide the opportunity for policy makers to enhance resilience to potential shocks. More than a decade has passed since then, giving the Independent Evaluation Group (IEG) the opportunity to assess the extent to which the World Bank Group has helped its client countries internalize the importance of proactive efforts to build resilience to domestic and external shocks.

This evaluation focuses on fiscal and financial sector vulnerabilities. Given their macroeconomic relevance, fiscal and financial sector weaknesses, when combined with major shocks, can also have significant social impact (Claessens et al. 2010; IMF 2011). The channels of impact are numerous. Weak institutional capacity can undermine efforts to understand and manage the fiscal and financial sector impacts of shocks. As economies are increasingly integrated into global trade, capital markets, and supply chains, integration itself can heighten vulnerabilities when external conditions take a turn for the worse. Crises and vulnerabilities can be, and have been, self-inflicted through poor domestic policies. This has led to growing awareness of the need to shift from a reliance on reactive, ad hoc, and ex post responses to shocks to an approach characterized by proactive risk identification and reduction (World Bank 2013).² Failure to adopt policies ex ante to reduce vulnerabilities can turn an exogenous shock into a full-blown crisis. Such policies should support adequate macroeconomic buffers, strengthen financial sector balance sheets, enhance the ability to implement timely countercyclical policy, establish frameworks and institutions to facilitate crisis management, and put in place flexible and adequate social protection sys-

tems. Taking this into account, the focus of this evaluation is on *crisis preparedness* and not crisis response. (See box 1.1, which provides definitions of key concepts used in this evaluation.)

Box 1.1. Evaluation Scope

The focus of this evaluation is on whether the Bank Group has contributed to preparedness for macroeconomic shocks by identifying and helping clients reduce *fiscal and financial sector vulnerabilities*. The focus is on ex ante risk identification and preparedness, not on ex post crisis response and stabilization. Shocks can come from any source, but for the purposes of this evaluation, they are relevant only to the extent that they interact with fiscal and financial vulnerabilities. “Preparedness” can be reflected in institutions, policies, regulations, and balance sheets that help (i) identify fiscal and financial sector vulnerabilities, (ii) reduce key vulnerabilities to minimize their economic impact, (iii) improve the adaptability of social protection systems to shocks, and (iv) expedite recovery.

Source: Independent Evaluation Group.

Purpose of the Evaluation

The purpose of this evaluation is to assess Bank Group support to client countries to enhance their preparedness for shocks through the systematic identification of fiscal and financial sector vulnerabilities as well as Bank Group support in addressing those vulnerabilities. The evaluation also aims to assess the extent to which the Bank Group has proactively supported improvements in client country safety nets so that they can be effectively and efficiently expanded in a crisis. It focuses on the period between 2010 and 2019 and aims to inform the design of future Bank Group strategies, operations, diagnostics, and knowledge products.

The evaluation covers the International Bank for Reconstruction and Development, the International Development Association (IDA), the International Finance Corporation (IFC), and the Multilateral Investment Guarantee Agency and asks five questions. Given the criticality of country context for macro-

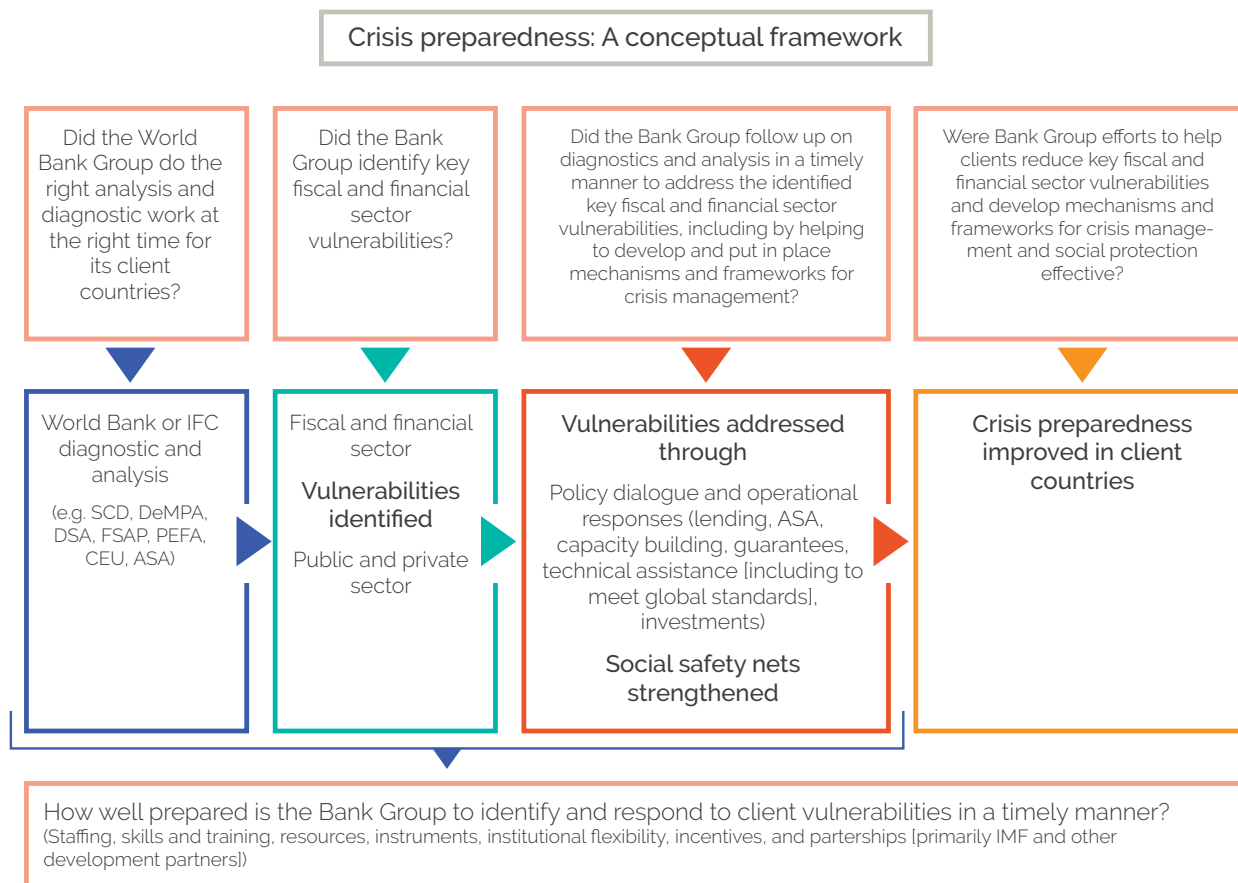
financial country preparedness, these questions will be answered in large part drawing on carefully selected, designed, and implemented case studies within a broader conceptual framework (figure 1.1), a detailed theory of change, reviews of relevant project and knowledge product portfolios, existing project-level and country-level evaluative evidence, and a targeted literature review. The literature review included past IEG and International Monetary Fund (IMF) evaluations related to macroeconomic crises; a review of relevant World Bank diagnostics; and corporate- and country-level semistructured interviews with World Bank, IFC, Multilateral Investment Guarantee Agency, and IMF staff, and other development partners as appropriate (appendix B).

The report is organized as follows: Chapters 2–4 present the main findings on identifying vulnerabilities, reducing vulnerabilities, adapting social safety nets for future crises, and preparing the World Bank for future crises. Chapter 5 provides concluding remarks and resulting lessons.

The following list groups the key questions asked by this evaluation.

- » Identifying vulnerabilities:
 - » Did the Bank Group undertake the right analysis and diagnostic work on client countries at the right time to identify major fiscal and financial sector vulnerabilities?
 - » Did the Bank Group clearly and candidly identify key country-specific fiscal and financial sector vulnerabilities and needed reforms to social safety nets to improve responsiveness in its analytical work and policy dialogue?
- » Responding to vulnerabilities: How did the Bank Group follow up to help client countries address identified fiscal and financial sector vulnerabilities?
- » Reducing vulnerabilities: Were Bank Group efforts to help clients reduce key fiscal and financial sector vulnerabilities and develop mechanisms and frameworks for crisis management and social protection successful? In providing support, did the Bank Group coordinate effectively with key development partners, particularly the IMF?
- » Preparing the Bank Group for crises: How well prepared was the Bank Group (in terms of staffing and incentives) to identify key fiscal and financial sector vulnerabilities and help clients address them promptly?

Figure 1.1. Conceptual Framework Guiding the Evaluation



Note: ASA = advisory services and analytics; DeMPA = Debt Management Performance Assessment; DSA = Debt Sustainability Analysis; FSAP = Financial Sector Assessment Program; IFC = International Finance Corporation; PEFA = Public Expenditure and Financial Accountability; SCD = Systematic Country Diagnostic.

The evaluation employed mixed methods. The main approach was *case study analysis*, including cross-cutting *syntheses of thematic or sector* issues and findings from individual case studies. Seven field-based case studies were conducted of Bank Group client countries, reflecting diverse country circumstances, country vulnerabilities, and experience with exogenous shocks, and diversity by region and income level. The countries selected were Bangladesh, Benin, Jamaica, Morocco, Mozambique, Tajikistan, and Ukraine. The evaluation draws on evidence from multiple sources: extensive document reviews, existing evaluative evidence, semistructured interviews with more than 200 stakeholders, and analysis of quantitative data (for more on methods, see appendix A and IEG 2019).

¹ The global financial crisis reduced the long-run growth path of many countries by between 4 and 8 percent and increased the number of poor people by 64 million (Chen and Ravallion 2009; World Bank 2010b), rolling back earlier gains on growth and poverty reduction. Banking crises alone resulted in an average increase in unemployment of 7 percentage points, an average drop in output of more than 9 percent (Reinhart and Rogoff 2009), and a decline in the incomes of poor people of more than 10 percent, while currency crises have had detrimental impacts on the income of poor people of about 15 percent (Rewilak 2018).

² *World Development Report 2014*, on risk, emphasizes the importance of preparedness, which includes intelligence, protection, and insurance (World Bank 2013).

2 | Identifying Vulnerabilities

Highlights

The World Bank Group carried out timely and relevant analyses to better understand emerging risks and sources of fiscal and financial sector vulnerabilities. The World Bank's diagnostic work on the financial sector was particularly frank, whereas its assessment of fiscal vulnerabilities was sometimes more restrained to accommodate client sensitivities.

The identification of fiscal vulnerabilities did not always take a whole-of-government perspective, thereby missing important links among vulnerabilities (for example, state-owned enterprises, state-owned banks, and contingent liabilities, including from large public investment projects).

At the country level, the Bank Group, on its own and in collaboration with the International Monetary Fund, provided significant, relevant, and timely diagnostic assessments and technical assistance that were appreciated by clients, although limitations on data quality and availability were sometimes problematic.

Monitoring and identification of debt and quasi-fiscal vulnerabilities has been variable. This has been due, in part, to a lack of quality data and data transparency, particularly concerning bilateral debt. Debt Sustainability Analyses have proven useful, but they have not always consistently and adequately captured idiosyncratic, compound, or country-specific shocks. In some cases, this led to underestimation of risks.

The Bank Group made considerable effort to monitor, analyze, and identify fiscal and financial sector vulnerabilities in client countries throughout the evaluation period (2010–19). Some 570 advisory services and analytics (ASA) products were produced with direct relevance to fiscal and financial sector vulnerabilities, with a notable increase over time in financial sector products and technical assistance engagements, as well as debt-focused products such as Debt Management Performance Assessments (DeMPAs), Debt Sustainability Analyses (DSAs), and technical assistance, and the introduction of a global flagship specifically focused on macrofinancial issues (box 2.1). (Also see World Bank [2021], an evaluation of World Bank support for public financial and debt management.)

Box 2.1. Macro-Financial Review and Identification of Vulnerabilities

Since 2017, the Macro-Financial Review (MFR), a semiannual report, has provided integrated analysis of global-, regional-, and country-level risks and vulnerabilities, addressing a key weakness of earlier global reports that were less rooted in the regional- and country-level perspectives. The Independent Evaluation Group reviewed each report published and interviewed the task manager and internal clients. The report also launched a new index of macrofinancial vulnerabilities. Successive semiannual reports have also addressed special topics, such as cross-border banking, blockchain technology, and climate change. There is a confidential version of the MFR that includes country ratings and an internal version without ratings.

The report provides value added to identification of fiscal and financial vulnerabilities in three respects: integration, granularity, and analyses of special topics. First, global-regional-country integration of macrofinancial monitoring and more granular analysis of financial sector vulnerabilities that permits the World Bank to see ahead of the curve is the main value added. The MFR currently covers 44 countries, mostly larger and regionally important economies for which requisite data are available. Second, the report provides a granular analysis with more in-depth analysis than is usually the case in flagship or regional reports. Third, the report provides useful analyses of special topics that shed new light on links among vulnerabilities. However, many smaller, low-income countries are not covered, in large part because of a lack of reliable data.

Source: Independent Evaluation Group.

Country-Level Diagnostics

Major country diagnostics, such as Systematic Country Diagnostics (SCDs), Country Economic Memorandums (CEMs), Public Expenditure Reviews, Public Finance Reviews, Financial Sector Assessment Programs (FSAPs), DeMPAs, and other ASA activities, are the cornerstone of country-level analysis of fiscal and financial vulnerabilities (for examples within the country cases studied, see box 2.2).

Box 2.2. Integrative Diagnostics Identifying Key Vulnerabilities: Morocco and Ukraine

The Ukraine Country Economic Memorandum (2010) was an example of a timely and relevant country diagnostic that identified key fiscal and financial vulnerabilities. On the fiscal side, it highlighted significant threats to fiscal sustainability: pension reform and producer subsidies. On the financial sector, it identified "mounting vulnerabilities in the banking sector due to lax credit analysis in the context of fast credit growth fueled by external borrowing." It also noted that "supervision and regulation [were] not ready to prevent another crisis" (World Bank 2010b). Indeed, this diagnostic, as well as other analyses, such as the 2011 Public Expenditure Review, correctly identified vulnerabilities that contributed to the crisis to come.

In the 2016 Morocco Financial Sector Stability Assessment, the World Bank Group pointed out that although the financial system was broadly resilient, well managed, and free of major vulnerabilities, certain institutional and procedural aspects of the system needed to be strengthened to improve robustness in the face of increasing risks in a volatile international economic environment. In particular, the assessment identified vulnerabilities that required attention: large cross-border exposure to markets in Sub-Saharan Africa, high concentration and limited competition in the banking system, and the nonperforming loans taken out by small and medium-size enterprises.

Source: Independent Evaluation Group.

Country policy notes were often prepared by the World Bank for a new government coming to power. These notes synthesized key findings of policy research and diagnostics, including with respect to fiscal and financial vul-

nerabilities. The 2016 Benin Policy Notes, for example, highlighted challenges to maintaining fiscal discipline and domestic revenue mobilization, and the need to ensure grants and low-cost financing in the budget. Similarly, policy notes for the new government of Ukraine in 2014 laid out a comprehensive view of key fiscal and financial sector issues and an agenda that could serve as a basis for more intensified engagement.

The SCD identifies the key constraints to achieving progress toward the twin goals of ending extreme poverty and promoting shared prosperity (World Bank 2019a). The SCD is prepared once every four to six years and is used to prioritize areas for Bank Group support. The scope of the SCD is not limited to areas where the Bank Group is currently active or where the Bank Group expects immediate country demand. A such, SCDs often include a discussion of fiscal and financial vulnerabilities when these are significant enough to constrain development progress.

The World Bank's assessment of, and outlook for, country-specific macroeconomic risks and vulnerabilities can also be found in the semiannual Macro Poverty Outlook.¹ The Macro Poverty Outlook consists of individual country notes that provide an overview of recent developments and medium-term forecasts of major macroeconomic variables and discuss risks to growth and macroeconomic stability. Case studies reveal varying degrees of consistency and candor in highlighting critical risks, particularly on the fiscal front. This was the case for assessments of fiscal risks in both Bangladesh and Tajikistan, where after 2016, the World Bank downplayed growing weaknesses in the macroeconomic framework related to contingent liabilities, including those related to state-owned enterprises (SOEs).

World Bank Support for Identifying Fiscal and Financial Sector Vulnerabilities

The World Bank's diagnostic work identified various types of fiscal and financial sector vulnerabilities (table 2.1). On the fiscal side, some of the vulnerabilities identified in the case studies included those related to debt sustainability, fiscal space and debt management capacity, contingent liabilities, and the robustness of domestic revenue mobilization. On the financial

sector side, vulnerabilities often manifest in relation to supervision and regulation, nonperforming loans (NPLs), commercial bank resolution frameworks, and the capacity of financial stability agencies such as central banks, financial stability committees, and deposit insurance agencies. In addition, fiscal and financial exposures are often intertwined, especially in commercial bank lending to SOEs or the government, commercial bank holdings of sovereign debt, and state-owned bank capitalization. A review of World Bank identification of fiscal and financial sector vulnerabilities for individual case study countries is summarized in appendix C.

Table 2.1. Typology of Fiscal and Financial Vulnerabilities Identified in the World Bank's Country-Level Diagnostics for Case Study Countries

Fiscal	Fiscal-Financial	Financial
Unsustainable debt (Benin, Mozambique, Ukraine) Fiscal space (Jamaica, Tajikistan) Energy subsidies (Tajikistan, Ukraine) Debt management capacity (Mozambique, Tajikistan) Quality of data and transparency (Mozambique, Tajikistan) Low domestic revenue mobilization (Bangladesh, Benin, Mozambique, Tajikistan)	Bank lending to state-owned enterprises (Tajikistan) Bank holdings of sovereign debt (Jamaica) State-owned banks lending and capitalization needs (Bangladesh, Tajikistan, Ukraine)	Supervision and regulation (Tajikistan, Ukraine) Nonperforming loans (all countries) Commercial bank resolution frameworks (all countries) Connected lending and corruption (Bangladesh, Tajikistan, Ukraine) Capacity of financial stability agencies (all countries) Loan classification (Bangladesh) Commercial bank exposure to foreign markets, cross-border exposure, limited access to banking system and capital market (Morocco)

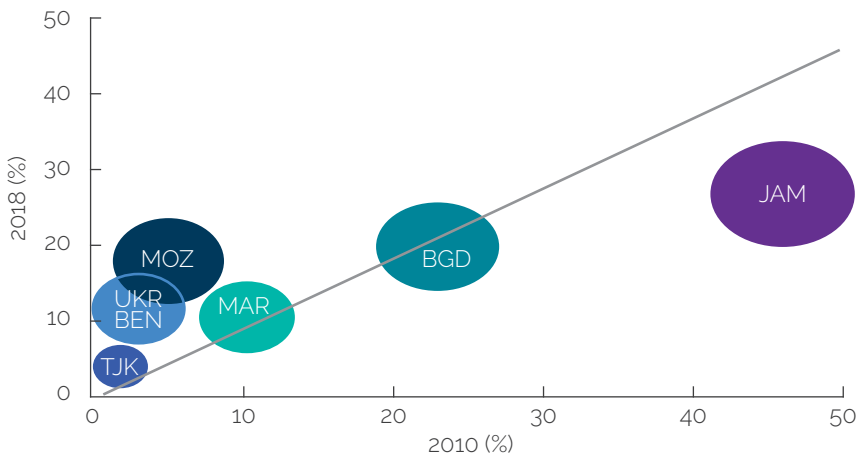
Source: Independent Evaluation Group.

Identifying Fiscal Vulnerabilities

The World Bank's depth, quality, and timeliness of fiscal monitoring, policy dialogue, and analytical work identifying vulnerabilities has been strong in

most countries and situations. Over the evaluation period, fiscal vulnerabilities increased in most case study countries with ratios of public debt to gross domestic product (GDP) rising significantly, as did the burden of budgetary interest payments relative to domestic revenues (figures 2.1 and 2.2). Assessments of Jamaica accurately flagged major weaknesses coming from the high and unsustainable public debt, the associated lack of fiscal space to finance basic services, and the link between fiscal management and constraints to growth.² In Ukraine, the 2010 CEM correctly argued that “the current fiscal model has proven unsustainable and that urgent fiscal reform is necessary” (World Bank 2010b, 63). The World Bank warned that fiscal policies were exacerbating broader macroeconomic risks and that they could have dire macroeconomic consequences, such as the 2014 full-blown currency, banking, and political crisis. Also, the 2011 Public Expenditure and Financial Accountability assessment gave low scores for budget credibility (measured by the difference between budgeted expenditures and outturns), budgetary transparency and comprehensiveness (measured by the extent of unreported government operations and oversight over SOEs), and payroll control and internal and external audit effectiveness (World Bank 2011b, 5–6).

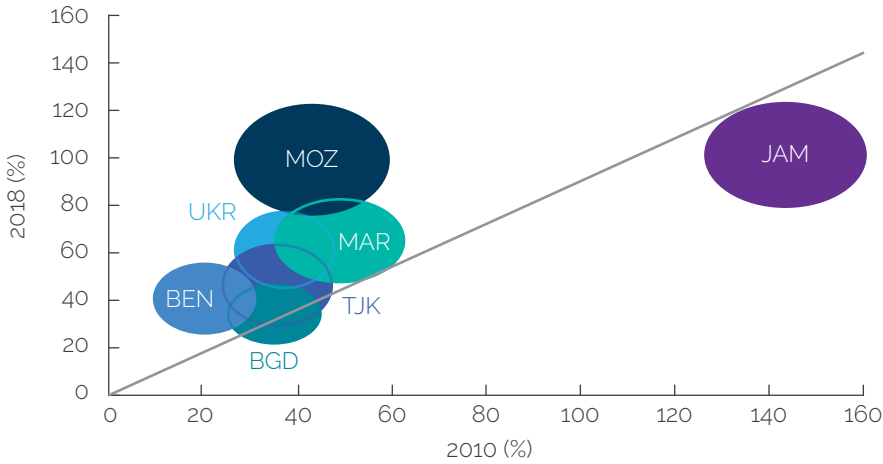
Figure 2.1. Indicators of Fiscal Vulnerability: Ratio of Interest Payments to Tax Revenue (percentage)



Source: International Monetary Fund Article IV consultation.

Note: Area of circles represents the percentage of interest to tax for 2018. BEN = Benin; BGD = Bangladesh; JAM = Jamaica; MAR = Morocco; MOZ = Mozambique; TJK = Tajikistan; UKR = Ukraine.

Figure 2.2. Indicators of Fiscal Vulnerability: Ratio of Gross Government Debt to Gross Domestic Product (percentage)



Source: International Monetary Fund 2019.

Note: Area of circles represents the percentage of debt to gross domestic product for 2018. BEN = Benin; BGD = Bangladesh; JAM = Jamaica; MAR = Morocco; MOZ = Mozambique; TJK = Tajikistan; UKR = Ukraine.

Even when country ownership of economic reform was weak and engagement with the World Bank and the IMF was limited, the World Bank kept abreast of economic developments and flagged emerging vulnerabilities. In Tajikistan, it raised concerns with emerging pressures on liquidity and the government’s budget from a potential drop in remittances. It also consistently warned the authorities of the need to build fiscal buffers and international reserves (World Bank 2012a).

Monitoring and the identification of debt vulnerabilities improved over the evaluation period, resulting in important “red flags” that anticipated debt problems, but key vulnerabilities did not always inform other work. In IDA-eligible countries, the World Bank uses the DeMPA diagnostic to flag risks associated with the quality of debt management. This was the case in Mozambique, where weaknesses in public debt reporting and recording were identified several years before the “hidden debt” crisis erupted in 2016. Elsewhere, the World Bank did not always clearly and consistently raise concerns with rising quasi-fiscal risks. This was the case for Bangladesh, for which the World Bank’s overarching assessment of fiscal stability was dominated by a

DSA that did not take full account of underlying explicit and implicit contingent liabilities and that instead concluded that Bangladesh was at “low risk of debt distress” (World Bank 2018a).

DSAs are central to gauging a low-income country’s risk of debt distress. However, a review of DSAs for the seven case studies for the evaluation period and related field interviews revealed that some of the key assumptions that underpinned the DSA baseline and alternative scenarios were overly optimistic. This was especially true with respect to growth and export revenue projections. Also, explicit and implicit contingent liabilities of SOEs were not fully reflected in any of the case studies during the review period. In Bangladesh and Tajikistan, for example, contingent liabilities arising from SOEs did not feature in the debt sustainability analysis, leading to the underestimation of fiscal risks. The DSA for Bangladesh also did not recognize the implications for debt sustainability of potential overestimation of GDP. In Tajikistan, fiscal vulnerabilities due to the budgetary costs of the Rogun Hydro-Power Project, commercial bank capitalization, and the interconnectedness between commercial bank lending and borrowing from SOEs were identified in World Bank analytical notes. However, inadequate data and transparency, including with respect to bilateral and nonconcessional borrowing, diminished their usefulness to the policy dialogue and policy advice. Debt data transparency is a broader problem, particularly for low-income countries and lower-middle-income countries, that has begun to receive enhanced attention, including as part of the recently adopted Sustainable Development Finance Policy (IDA 2020). Furthermore, the revised IMF–World Bank Debt Sustainability Framework for Low-Income Countries, introduced in 2018, places greater emphasis on contingent liabilities and aims at greater public and publicly guaranteed debt coverage, including with respect to risks from SOEs, extrabudgetary funds, and subnational governments. Where data availability is limited, omissions are flagged and trigger a contingent liability stress test, which is adjusted by the user to fit the country-specific circumstances.

Identifying Financial Sector Vulnerabilities

Financial sector vulnerabilities are monitored through a wide variety of qualitative and quantitative diagnostic assessments, the most comprehen-

sive of which are FSAPs and financial sector assessments or Financial Sector Stability Assessment (FSSAs). Bank staff collaborate with IMF staff on FSAPs, following a modular approach, with the World Bank having the ability to conduct stand-alone FSAP “development” modules without IMF involvement.⁵ However, the World Bank does not conduct stress testing, which is instead conducted by the IMF.

In the financial sector, reflecting lessons from the global economic and financial crisis, diagnostic analyses for case study countries were generally timely and focused on the right issues, especially in Jamaica, Morocco, and Ukraine. In each of these countries, the Bank Group monitored key vulnerability indicators and undertook regular analytical work, even when clients were not committed to significant reform. The 2010 Ukraine CEM noted that “mounting vulnerabilities in the banking sector due to lax credit analysis in the context of fast credit growth fueled by external borrowing were accentuated by the [global financial] crisis” and highlighted currency and maturity risks and underprovisioning for bad loans (World Bank 2010b). It also stated that “supervision and regulation [were] not ready to prevent another crisis.” Even outside of a formal FSAP, the World Bank provided extensive and high-quality monitoring, analytical, and advisory work to Ukraine, which proved critical to a timely response to the financial crises and shocks that started in 2014.

In Morocco, the Bank Group—in a series of diagnostics and policy discussions in the context of financial sector development policy loans (DPLs) and an FSA/FSSA conducted jointly by the World Bank and the IMF in 2016—pointed out that, although relatively resilient and without major vulnerabilities, institutional and procedural aspects of the system could be strengthened to improve the robustness of the system, especially in the face of increasing risks in a volatile international economic environment. The World Bank identified weaknesses in cross-border lending from Morocco to some Sub-Saharan African countries, large single-borrower exposure, and risks from NPLs, although the Moroccan financial system remained deep and broadly well managed. Also, access to the banking system and capital markets remain limited, and with most firms in Morocco being small and medium size, this could contribute to macroeconomic volatility. The FSSA

also noted that the supervision of capital markets and financial market infrastructures needed upgrading.

In Jamaica, in 2010, in the context of a policy dialogue undertaken in close collaboration with the IMF, the World Bank highlighted risks to the financial system from large holdings of sovereign debt, which threatened the liquidity and solvency of the banking system given the high risk of sovereign default. Subsequently, the 2015 FSA/FSSA correctly identified the rise of persistent risks to the financial sector from, among other things, (i) complex financial conglomerates dominating the financial sector and operating in multiple jurisdictions, with the headquarters of some large groups based in jurisdictions with different oversight practices; (ii) the concentrated ownership structure of the financial sector; (iii) related-party and large group exposures; and (iv) large off-balance sheet positions. The 2018 FSAP found the financial system in a stronger position, with a substantial reduction in NPLs, albeit with continued interconnectedness in the repurchase agreement market, a large value payment system, and significant counterparty exposures in the financial sector.

Client Feedback, World Bank–IMF Collaboration, and Data Issues

Interviews with government agencies in case study countries frequently noted appreciation for the quality of the World Bank’s technical analysis and fiscal and financial sector diagnostics and of IMF–World Bank collaboration, including on DSAs (box 2.3). Interviewees provided many examples of how these diagnostics and technical assistance informed subsequent institutional reforms: Ukraine CEM 2011, Morocco FSA 2016, Jamaica CEM 2011, and Mozambique DeMPA 2015/16 and Public Expenditure Review 2014. In some cases, however, when there was disagreement over the conclusions of the diagnostics and what were perceived as overly critical findings, governments were reluctant to publish the findings. This was the case with the Public Expenditure and Financial Accountability analysis in Tajikistan, where the government acknowledged the usefulness of the analysis but decided to delay its publication for internal reasons, and with the financial sector assessments in

Bangladesh. Nevertheless, clients frequently indicated that they valued the World Bank’s analytical work, even when they disagreed with its findings.

World Bank–IMF collaboration in identifying fiscal and financial vulnerabilities has been generally strong, often in the context of joint diagnostics (for example, FSAPs and DSAs), and the quality was generally high. IMF–World Bank DSAs include scenario and shock analyses, with shock scenarios taking into account different assumptions for growth, interest rates, and exchange rates. Country-specific shocks such as to remittances were occasionally included, but shocks associated with quasi-fiscal operations and contingent liabilities were not always well captured by the assessments, often because of a lack of data. Debt transparency on private and bilateral debt has also been an issue.

The World Bank and the IMF conduct joint FSAPs with an agreed division of labor, whereby the IMF focuses on financial stability and the World Bank on financial development issues. Of the seven case studies, FSAPs have been completed in four countries during the evaluation period: Bangladesh, Jamaica, Morocco, and Tajikistan. (There were no FSAPs completed in Benin, Mozambique, or Ukraine during the evaluation period, although the World Bank did undertake considerable financial sector monitoring, analysis, and technical assistance in Ukraine). World Bank and IMF staff report generally good collaboration in their preparation. Itinerant technical visits helped maintain monitoring and policy dialogue. However, in the case of Bangladesh, World Bank staff sought to undertake a full FSAP in the latter part of the evaluation period as financial sector vulnerabilities began to increase. Conversely, IMF staff did not consider Bangladesh to be a priority for scarce FSAP resources, resulting in delays in undertaking a comprehensive analysis of conditions in the financial sector. World Bank staff proceeded with a stand-alone “development” module in 2019.

Shortcomings in data quality and transparency often hindered the World Bank’s ability to analyze, identify, and monitor vulnerabilities, as in the case of bilateral debt in Tajikistan, for example (table 2.2). This evaluation finds that the quality of data needed to adequately monitor and analyze vulnerabilities is low in three out of seven case study countries. Even in countries with significant Bank Group engagement, such as Bangladesh and Ukraine,

the quality of data was deemed moderate, especially with respect to contingent liabilities. Data quality was found to be generally high only in Jamaica and Morocco. The situation is similar with respect to the availability, transparency, and timeliness of data.

Table 2.2. Quality of Data on Fiscal and Financial Vulnerabilities

Country	Quality of Data	Transparency	Timeliness
Bangladesh	Moderate	Moderate	Moderate
Benin	Low	Moderate	Moderate
Jamaica	High	High	High
Morocco	High	Moderate	Moderate
Mozambique	Low	Low	Moderate
Tajikistan	Low	Low	Low
Ukraine	Moderate	High	Moderate

Source: Independent Evaluation Group assessment based on Public Expenditure and Financial Accountability, Public Expenditure Review, Financial Sector Assessment Program, and country reports.

¹ <https://www.worldbank.org/en/publication/macro-poverty-outlook>.

² The subsequent Jamaica Public Expenditure and Financial Accountability Review expounded on institutional vulnerabilities in budget planning, monitoring, and management (Jamaica PEMFAR 2012).

³ The World Bank Group performed a development module for Bangladesh in 2019 and for Jamaica in 2015. Publication of the report on the development module for Bangladesh had not been authorized as of April 2021.

3 | Bank Group Support for Reducing Vulnerabilities

Highlights



World Bank Group support to country clients to help reduce fiscal and financial sector vulnerabilities (as outlined in country strategies and lending and knowledge instruments) was generally well aligned with the findings of diagnostics.



The World Bank's support for reducing financial sector vulnerabilities was significant, with considerable technical assistance to central banks, deposit insurance funds, and financial regulators. Bank Group support for more ambitious reform was more prevalent in countries in the midst of crises.



Outside the context of a full-blown crisis, the World Bank was less effective in persuading countries to undertake the longer-term institutional reforms needed to tighten regulations and strengthen institutional capacity for crisis prevention and management.



Close partnership and coordination with the International Monetary Fund and other partners (usually in the context of a crisis when both institutions were providing significant support) enhanced the effectiveness of Bank Group support.



Although progress has been made to set up and strengthen social protection delivery systems and social safety net programs, important challenges remain, with social safety net adaptability and flexibility across the seven case study countries varying significantly.

Bank Group Support to Clients in Addressing Vulnerabilities

The quality of Bank Group support to client countries to reduce their fiscal and financial sector vulnerabilities and strengthen and adapt social safety nets is evaluated through the lens of (i) *coherence* with identified vulnerabilities, (ii) *complementarity* of the Bank Group's response across its agencies and instruments, and (iii) *collaboration* with the IMF and other partners.

In all case study countries, a review of diagnostic work and subsequent World Bank–supported country strategies indicates that identified vulnerabilities usually informed Bank Group lending and subsequent ASA. The scale and nature of the Bank Group's support differed across and within countries and over time, depending on government commitment and resistance from vested interests.

In countries where commitment to reform was weak or vested interests strong—as was the case in Ukraine throughout much of the early evaluation period, in Bangladesh (particularly in the financial sector), and in Tajikistan—the World Bank emphasized ongoing monitoring and analytical work to stay abreast of developments and conditions in anticipation of a more favorable climate for reform. In Ukraine, the World Bank and IFC supported a strong analytical and advisory program (including through programmatic technical assistance) in close collaboration with other development partners. Collaboration with partners was strong in Ukraine, where the Bank Group, the IMF, the European Bank of Reconstruction and Development, the UK Department for International Development, and the US Agency for International Development maintained particularly close coordination. This created a good basis from which to proceed with reforms to strengthen financial sector resilience when the political climate became more supportive of reform after 2014. However, in subsequent years, despite rigorous identification of vulnerabilities, vested interests in the parliament and the private sector blocked key financial sector legislation and policies, leaving reforms seriously incomplete. In Tajikistan, the 2015 FSAP identified vulnerabilities in the financial sector related to interconnected lending, bank resolution frameworks, and the governance of state banks. The Bank Group engaged with various

shorter-term funding options, such as funding from the FIRST Initiative, to finance needed follow-up technical assistance.

Where ownership of reforms was strong, as in Jamaica, the World Bank responded with intensive dialogue and budget support in close coordination with the IMF. Based on the earlier identified debt vulnerabilities and a policy agenda outlined in a comprehensive CEM, the World Bank provided three successive budget support operations from 2013–17, focusing on fiscal consolidation and investment climate reform in conjunction with a large, three-year IMF-supported arrangement and budget support from the Inter-American Development Bank. These efforts sought to reverse adverse debt dynamics, rebuild fiscal space to finance critical services, and remove constraints to the recovery of investment and growth.

Coherence between identified vulnerabilities and Bank Group support to address them varied across countries, between moderate and high (table 3.1). The degree of coherence fluctuated more on the fiscal side than it did for financial sector support. This may reflect the more political nature of the engagement in the fiscal area, where World Bank support often required significant changes in budget planning, execution, and practices, as well as in transparency and accountability, especially in the relationship between the budget and state-owned banks and enterprises, which often ran counter to vested interests.

In Tajikistan, although the World Bank correctly identified key fiscal vulnerabilities, it struggled to agree with the government on how to support efforts to address those vulnerabilities. In 2016, the World Bank began preparing a series of DPLs to help the government address fiscal issues but, in the end, decided to drop the series before approval, over concerns with the direction of reform, the quality of fiscal management, and transparency. In this environment, the World Bank continued monitoring and keeping abreast of fiscal issues but refrained from significant operational (that is, lending) engagement. By contrast, the World Bank was able to provide considerable support to the central bank through technical assistance and loans, which were viewed by the client as less controversial from the government’s viewpoint, given their more technical nature. In 2019, the World Bank began providing technical assistance to the financial sector to address concerns with financial

stability, NPLs, bank resolution tools, payment system oversight, consumer protection, and corporate governance in the financial sector.

In Benin, support to reduce fiscal and financial sector vulnerabilities was relatively limited, the latter in part because the counterparts for financial sector dialogue were in the regional monetary authority, with which the World Bank had limited contacts and dialogue (and with which the IMF took the lead). In areas where there was confluence of interest and ownership, however, the World Bank responded with significant support.

Table 3.1. Coherence between Vulnerabilities and World Bank Group Support

Country	Key Vulnerabilities	Response	Degree of Coherence
Bangladesh	SOEs, contingent liabilities, SOCBs	Limited policy lending to address fiscal vulnerabilities, but extensive technical assistance addressing financial vulnerabilities. Since 2018, a Program-for-Results, Public Financial Management Program to Enhance Service Delivery Project, is supporting the SOEs in increasing debt transparency and profitability, as well as macro forecasting.	Moderate
Benin	Public debt, domestic revenue mobilization, NPLs	Policy-based guarantee focused on fiscal space but limited engagement in financial sector.	Moderate
Jamaica	Public debt, fiscal space, NPLs, banking system concentration, access to finance	Three DPLs targeting reduction of public debt and increase in fiscal space; financial sector DPLs.	High
Morocco	Public sector governance and transparency, commercial bank oversight and regulation, and exposure to foreign markets	DPL series targeting governance and transparency; technical assistance to financial sector resolution framework, overseeing systemic financial market infrastructures, creating a market for NPL management, and greening the financial system.	High

(continued)

Country	Key Vulnerabilities	Response	Degree of Coherence
Mozambique	Unsustainable debt; poor debt recording and monitoring; data transparency; central bank supervision, regulation, and resolution framework	Three PRSCs targeting fiscal, debt management, and transparency; extensive technical assistance to financial sector.	High
Tajikistan	Dependence of liquidity on remittances, debt management, SOBs, bank supervision and regulation, resolution frameworks, energy subsidies	Policy-based lending targeting fiscal issues dropped. Technical assistance to financial sector including bank supervision, NPL resolution, deposit insurance strengthening, bank corporate governance, and remittances.	Low to moderate
Ukraine	Debt management capacity, energy subsidies; supervision and regulation of commercial banks, bank resolution frameworks, NPLs, corruption and connected lending	DPL series targeting fiscal vulnerabilities, separate financial sector DPF, extensive technical assistance on financial sector.	High

Source: Independent Evaluation Group.

Note: DPF = development policy financing; DPL = development policy loan; NPL = nonperforming loan; PRSC = Poverty Reduction Support Credit; SOB = state-owned bank; SOCB = state-owned commercial bank; SOE = state-owned enterprise.

The Bank Group drew on complementarity among its agencies, particularly where IFC had a substantial presence. IFC responded to identified vulnerabilities in the financial sector and by providing direct project and advisory support that was broadly complementary to that of the World Bank. This was common in the agriculture sector, which often had significant links to budgets and financial sectors, implying vulnerabilities through commodity price and credit risk and bank exposure to the sector. IFC support included developing innovative farmer crop receipt mechanisms to reduce the impact on farmer income of volatile commodity prices (Ukraine), consumer protection, and financial literacy (Tajikistan). IFC also provided direct investment and advisory support to banks focused on raising corporate standards and improving governance and risk management (Bangladesh).

These interventions complemented the World Bank's engagement in the financial sector. The IFC benefited from the World Bank's analytical work.

World Bank and IFC staff worked well together in Mozambique through the IDA Private Sector Window. However, evidence from field visits indicates that IFC's capacity to respond in some cases was constrained by a limited staff presence in the field (for example, in Benin).

The degree of coordination and complementarity of World Bank and IMF support to help reduce fiscal and financial sector vulnerabilities varied across countries and sectors and depending on whether there was a crisis under way. In response to major crises in Jamaica, starting in 2013, and in Ukraine, starting in 2014, the World Bank and IMF contributed to highly coordinated, large-scale, and well-integrated stabilization programs accompanied by technical assistance. In the wake of the Arab spring, Morocco benefited from World Bank budget support in areas of governance and accountability that indirectly addressed some underlying fiscal vulnerabilities, whereas the IMF took the lead on macroeconomic policy dialogue and the provision of contingency financing to limit external contagion. At the other end of the spectrum, in Tajikistan the World Bank and IMF did not have strong coordination or integration to address fiscal and financial sector vulnerabilities, although the teams met periodically to discuss financial sector issues. In Bangladesh, Benin, and Mozambique, coordination with the IMF was more limited in scope and intensity.

Impact of Bank Group Support in Reducing Country-Level Vulnerabilities

The effectiveness of the Bank Group's support in reducing vulnerabilities is assessed taking into account observed changes in vulnerability indicators over the evaluation period, given the nature of the Bank Group contribution. In-depth country case study assessments indicate that the Bank Group contributed significantly to reducing vulnerabilities in Jamaica and Ukraine starting from (and perhaps in part because of) the presence of a major crisis, alongside strong government ownership and large-scale World Bank support, complementary to and well coordinated with the IMF, and internally across Bank Group agencies. Still, despite substantial contributions, outcomes in Jamaica stood out, as government ownership has been sustained, including through the broad stakeholder consensus engendered by its economic and

policy monitoring committee. By contrast, ownership in Ukraine waned and progress in reducing vulnerabilities slowed. At the other end of the effectiveness spectrum were countries with limited institutional capacity or substantial internal opposition to reforms and debt transparency (Bangladesh, Mozambique, and Tajikistan), which limited the effectiveness of the Bank Group’s contribution (table 3.2).

Table 3.2. Assessment of World Bank Group Effectiveness in Reducing Vulnerabilities and Improving Internal Coordination

Country	Change in Vulnerabilities from 2010 to 2019	Bank Group Contribution	Bank Group Internal Coordination
Bangladesh	Moderate to high	Moderate	Moderate
Benin	High to very high	Low or moderate	Moderate
Jamaica	Very high to moderate	High	High
Morocco	Moderate to low or moderate	Moderate	High
Mozambique	Moderate to very high	Low	Moderate
Tajikistan	High to high	Low	Low
Ukraine	High to moderate	High	High

Source: Independent Evaluation Group evaluation team assessment.

In Ukraine, World Bank–supported reform resulted in a large cleanup of the banking system with about half the country’s 180 banks being declared insolvent and sent for resolution. Most large banks returned to minimum capital adequacy requirements, and the institutional capacity of the National Bank of Ukraine and Deposit Guarantee Fund were strengthened significantly. However, a number of key banking reform laws and regulations were blocked in parliament, drawing into question the implementability of reforms. Results have been particularly modest in dealing with the challenges in state-owned banks. Despite periods in which progress was difficult, the World Bank and IFC worked well together in Ukraine, with the World Bank focusing on policy, regulatory, and resolution frameworks and reform initiatives, and IFC on transactions (for example, bank privatization). IFC also achieved results in improving NPL management, bad asset resolution, operational risk, financial risk, and building the market for distressed assets.¹

In contrast, in Mozambique, despite concerns from the earlier DeMPA about weaknesses in debt reporting and recording, the issue received little atten-

tion from the World Bank or the government before the eruption of the hidden debt crisis. In Tajikistan, the restructuring and resolution of state-owned banks was postponed indefinitely, despite clear risks to fiscal and financial sector stability. Because of low uptake, however, advice did not translate into a reduction of vulnerabilities. Debt buildup continued unabated.

Box 3.1. From Debt Sustainability to Debt Tolerance

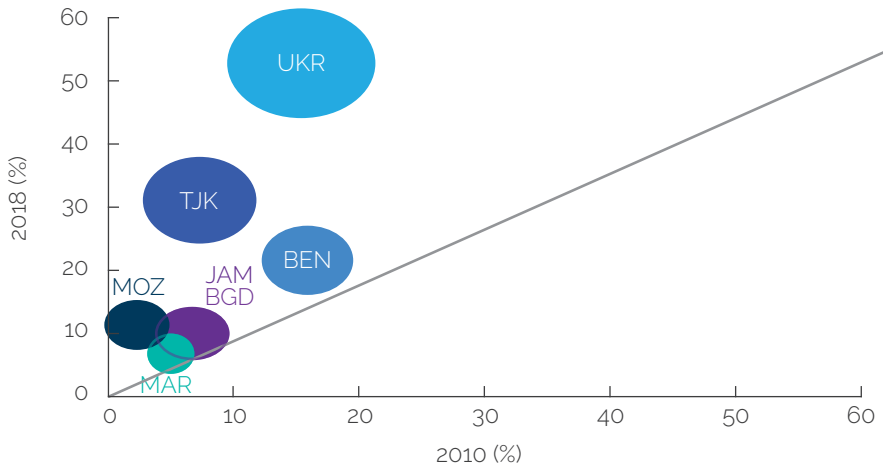
The traditional approach to debt sustainability incorporated a relatively narrow menu of shocks (typically, growth and interest rate shocks).

The more recent International Monetary Fund–World Bank Debt Sustainability Framework (DSF) guidance and tool kit, however, emphasizes the concept of debt tolerance. It recognizes that stabilizing the debt ratio may not be enough to avoid a debt crisis, depending on the level at which debt is stabilized and the kinds of shocks to which it is exposed. The new DSF, therefore, aims to identify different tolerance levels for debt so that an “early warning signal” can be provided to fiscal and debt policy. The DSF tool kit now contains a wider menu of shocks that are taken into account, including contingent liabilities such as public sector guarantees or state-owned enterprises. However, in practice, at the country level, fully accounting for these shocks outside of central government budget operations is proving difficult because of data constraints. The revised International Monetary Fund–World Bank Debt Sustainability Framework for Low-Income Countries, therefore, offers greater potential for standardized contingent liability shocks.

Source: Independent Evaluation Group team assessment.

In the financial sector, the Bank Group had a mixed record of success during the evaluation period. Figure 3.1 illustrates the change in NPL ratios in case study countries during the evaluation period, reflecting unrecognized NPLs from the previous period in some countries.

Figure 3.1. Indicators of Financial Sector Vulnerability: Ratio of Nonperforming Loans to Total Loans (percentage)



Source: International Monetary Fund Article IV consultation.

Note: Area of circles represents the percentage of nonperforming loans to total loans for 2018. BEN = Benin; BGD = Bangladesh; JAM = Jamaica; MAR = Morocco; MOZ = Mozambique; TJK = Tajikistan; UKR = Ukraine.

Effectiveness was particularly low in Bangladesh, with the authorities canceling a major World Bank operation aimed at improving the governance of the banking sector after it had been approved by the World Bank Board. In Morocco, despite the fact that financial sector vulnerabilities were low, the Bank Group provided effective assistance to enhance financial system soundness and efficiency, including risk management procedures for banks; the supervisory framework; bank resolution procedures; access to credit; and development of the capital market. The two DPLs in support of micro, small, and medium enterprise (MSME) and capital market development helped strengthen the institutional and regulatory framework of the financial sector, extending the program of credit guarantees to MSMEs to facilitate higher access of MSMEs to finance and supporting capital market development through strengthening the organization, instruments, and supervision of the capital market. With the advice of the World Bank and the IMF, the new banking law extended the central bank’s regulatory and supervisory power to financial conglomerates, microfinance institutions, and offshore banks. The law also aims at improving cross-border supervision and tightening rules for consolidated risk manage-

ment. IFC supported both the strengthening of the public credit bureau and the setting up of private credit bureaus. In Mozambique, after sustained engagement through two financial sector DPLs, the central bank raised banks' minimum capital requirement and the minimum capital adequacy ratio from 8 percent to 12 percent, and crisis management arrangements were tested through a simulation exercise. The government has also passed a law aligning the national crisis management framework with the Financial Stability Board's key attributes of effective resolution regimes for financial institutions.

In Ukraine, the Bank Group, working with the IMF, provided assistance for the massive restructuring of the banking sector after the 2014 crisis. Quantitative and qualitative indicators of banking system soundness show corresponding improvements (appendix C) over this period. However, efforts to support longer-term institutional reform to improve sector governance and prevent a reemergence of crisis conditions were less successful, as critical legislation became stuck in various parts of the legislative process. At the same time, the Bank Group was able to support capacity building in the central bank and the successful establishment of a deposit guarantee fund. IFC introduced a previously nonexistent crop receipts mechanism to farmers, which improved risk management, thereby helping limit government and financial sector contingent liabilities (box 3.2). The World Bank Treasury also provided technical assistance and advisory support to the Central Bank of Ukraine on risk management, hedging, and reserve management, as well as for the development of the local currency debt market (box 3.3, which includes examples of World Bank Treasury assistance to other countries).

Client feedback suggests that technical assistance and advisory support to the central bank and related bank reform (for example, bank resolution frameworks) has been especially valued. Clients valued Bank Group support for the establishment and development of credit bureaus and other activities that help strengthen bank lending practices. Evidence from IEG validations of World Bank staff self-evaluations indicate that, in countries with strong ownership and intensive Bank Group engagement closely coordinated with the IMF and other development partners, project outcomes were generally rated higher with a smaller variance than in countries with weak ownership and less intensive engagements, for example Benin and Mozambique (table 3.3).

Box 3.2. International Finance Corporation's Innovative Assistance for Crop Receipts

The International Finance Corporation (IFC) crop receipt program is an innovative financial instrument to expand access to finance for small farmers. By reducing financing risks for farmers, the instrument contributes to reducing fiscal and financial sector vulnerabilities that may arise from crop failure and large swings in crop prices. Crop receipts are a preharvest financial instrument that allows farmers to use future harvests as collateral, enabling them to purchase high-quality seeds and other essentials. This instrument can help ease collateral constraints in the rural economy by providing financiers with additional security. IFC, through its Ukraine Crop Receipts Project implemented in partnership with the State Secretariat for Economic Affairs of Switzerland, introduced crop receipts in 2015. As of April 2020, small farmers have issued 4,000 crop receipts to receive \$1 billion in financing (for details, see Emerging Europe [2018]). The crop receipts program is addressing the market failure of commercial banks not lending to small farmers because agricultural land used by small farmers is rented and therefore cannot be used as collateral. There is minimal foreign exchange risk because 95 percent of the loans to small farmers in this program are in local currency. One of IFC's major clients in the crop receipts program is OTP bank, a Hungarian bank and currently one of the top three banks in Ukraine. OTP has a crop receipt portfolio of 260 clients (about \$60 million in financing). The interest rate offered by OTP to small farmers is 22 percent, above the average market rate of 17 percent.

Source: Independent Evaluation Group.

Box 3.3. World Bank Treasury Assistance for Risk Management, Hedging, Reserve Management, and Support for Local Currency Debt Markets

The World Bank Treasury has supported risk reduction in a number of countries through integrated risk management projects, hedging operations, and advice on reserve management. These activities have helped countries strengthen overall macroeconomic management and improve buffers against risks. The Treasury has been active in all seven case study countries, but most effectively in Jamaica and Morocco. The Treasury assisted Morocco in 2019 to secure reinsurance of catastrophic risk until 2023. It also sold call options to Morocco to hedge butane price risk in 2019.

(continued)

Box 3.3. World Bank Treasury Assistance for Risk Management, Hedging, Reserve Management, and Support for Local Currency Debt Markets (cont.)

The Treasury assisted Caribbean Catastrophe Risk Insurance Facility member countries, including Jamaica, to issue catastrophe bonds (catbonds) to insure against major disasters without creating new public sector debt. The bonds transferred natural disaster risks to capital markets and eased the need to build up large budget reserves. The countries benefited from Treasury support throughout the preparation and market execution of the bonds. The Treasury is currently working with the IMF on incorporating a "hurricane clause" into Paris Club regulations, allowing the debt to be restructured in case of a hurricane.

The Treasury has served as an intermediary in swap transactions to assist countries in hedging against exchange rate risk and commodity price fluctuations, aligning the currency composition of borrowed resources with their international trade and improving the currency profile of their debt. The intermediary role of the Treasury in these operations reduces service costs compared with a direct commercial swap and obviates the need for collateral. Morocco is a notable beneficiary of these operations. In 2012, its dollar-denominated bonds were swapped with euro-denominated loans, facilitating Morocco's international payments, which are mainly in euros. The Treasury also assisted the government to buy a call option to protect against increases in prices of butane, the main commodity benefiting from a price subsidy.

Through its Reserve Assets Management Program, the Treasury has also improved the management of country foreign exchange reserves to conform to international best practices. The program has been especially effective in Jamaica, assisting the central bank in establishing separate management strategies for working capital, which is used to smooth out exchange rate fluctuations; a liquidity tranche used for debt payment; and an investment tranche of longer-dated assets.

Finally, the Treasury assisted the Moroccan Treasury in revising the strategy for managing the central government debt. This included technical assistance support to Moroccan authorities for borrowing in local currency and on other issues related to the currency composition and the role of the domestic debt market within the context of the Medium-Term Debt Management Strategy.

Source: Independent Evaluation Group.

Note: ICRR rating scale runs from 1 (highly unsatisfactory) to 6 (highly satisfactory).

Table 3.3. Outcomes of Projects and Development Policy Financing Focused on Fiscal and Financial Vulnerabilities

Country	Average ICRR Rating	Average ICRR Outcome	Variance	Projects and DPL Programmatic Series (no.)
Bangladesh	3.8	Moderately satisfactory	2.0	6
Benin	3.2	Moderately unsatisfactory	0.1	6
Jamaica	4.0	Moderately satisfactory	0.0	6
Morocco	4.1	Moderately satisfactory	0.1	7
Mozambique	3.9	Moderately satisfactory	0.8	7
Tajikistan	4.0	Moderately satisfactory	0.0	3
Ukraine	5.0	Satisfactory	0.2	6

Source: Independent Evaluation Group ICRR database.

Note: DPL = development policy loan; ICRR = Implementation Completion and Results Report Review.

¹ The International Finance Corporation Crisis Management Services Project was evaluated by the Independent Evaluation Group in 2013 and found positive results, albeit in small banks accounting for about 2.5 percent of total financial sector assets.

4 | Making Social Safety Net Systems Adaptable to Economic Downturns

Highlights

As a complement to building fiscal and financial sector resilience, countries need to establish and adapt social safety nets to ensure they are flexible enough to respond to the increased and temporary need associated with economic downturns.

With World Bank support, progress has been made to establish and strengthen social protection delivery systems and social safety net programs that can serve as the foundation for a social safety net that can become more flexible in response to a shock. However, important challenges remain in terms of enhancing the coverage, the dynamism of systems, and the flexibility and scalability of such programs.

The World Bank has expanded its support for an “adaptive social protection” approach to build household resilience and enhance the shock responsiveness of safety nets and social protection delivery systems.

Social protection mechanisms are necessary to mitigate social impacts during severe economic downturns. Without social safety nets, economic crises can drive vulnerable households into poverty, make those who are already poor even worse off, cause irreversible losses to human capital and household assets, and stir social unrest. A major lesson from the food, fuel, and financial crises between 2007 and 2009 is that social protection arrangements—including intake and registration—must be put in place during normal times and that safety nets should be more adaptable and flexible in the face of major economic downturns.

This lesson has not been fully absorbed. To be sure, the World Bank has contributed to a better understanding of which safety net programs can be used to prepare and react to economic downturns. This requires building the basis for rudimentary systems in low-income countries and promoting safety net system harmonization in middle-income countries. Although World Bank support for social safety nets has concentrated on helping countries move from fragmented programs to systems, the primary focus has been on expanding access to chronically poor people, rather than on the ability of systems to respond in an economic downturn. In the case study countries, neither the governments nor the World Bank were specifically focused on the flexibility dimension of social safety net system performance, except in Jamaica.

In advanced economies, social insurance provides effective crisis response mechanisms (automatic stabilizers) and active labor market programs that can be rapidly deployed to address increased unemployment. However, such interventions are linked to formal sector employment, which is limited in developing countries. Social safety net programs provide consumption smoothing and protection against poverty and vulnerability and are an effective instrument to address the impact of a large crisis on poor and vulnerable people (Banerjee et al. 2017; World Bank 2010, 2011, 2012). As a result, social safety nets have become a de facto social protection crisis management instrument in the developing world, even though most programs have been designed to address chronic poverty.

During the evaluation period, the World Bank stepped up financial, technical assistance, and knowledge support for safety nets in all case study countries,

some of them for the first time (Mozambique, Tajikistan). Assisting clients in building delivery systems for normal and crisis times became part of the World Bank's longer-term agenda of support, especially in low-income countries. To this end, the World Bank made substantive knowledge investments, promoted strong global partnerships, and mobilized trust funds (box 4.1) for social safety net capacity building (Bangladesh, Benin, Jamaica, Mozambique, and Tajikistan).

The World Bank conducted diagnostic work to identify gaps and strengthen social safety net systems in client countries. Strengthening these systems was thought to increase the capacity of the safety net to respond in a crisis. But the focus of this work was from the point of view of supporting chronically poor people rather than preparedness to respond to a severe economic downturn that could exacerbate poverty and generate new poor people. For example, in Morocco and Ukraine, the World Bank's policy advice was to reduce large energy subsidies as part of a fiscal consolidation at the same time as making subsidies more targeted to poor people. Ukraine's 2018 Public Finance Review recommended rebalancing the social assistance system to gradually make the well-targeted but smaller guaranteed minimum income scheme the primary safety net for poor people, with the housing utility subsidy becoming a secondary safety net to protect against excessive utility costs. Similar, though less extensive, reforms were carried out in Tajikistan.

In Benin and Mozambique, where initial safety nets were extremely weak or nonexistent, the World Bank focused on foundational work to identify entry points to help build targeted safety systems for chronically poor people, even though the specific programs supported (cash transfers and public works) could be expanded to provide temporary support during a cyclical downturn. This work also revealed that in low-income countries, low domestic revenue mobilization remains a major constraint to effective safety net systems and their capacity to react in a crisis (as documented in the case studies for Benin, Mozambique, and Tajikistan).

Box 4.1. The World Bank's Global Social Safety Network

The World Bank promoted strong partnerships with donor and United Nations agencies, nongovernmental organizations, and others to build country social safety net systems with technical and financial assistance; to leverage knowledge exchange; and to improve interagency coordination. Key initiatives include the following:

- » The Rapid Social Response (RSR) Program to provide catalytic resources to assist low-income countries in their response to the economic turbulence of the past decade and boost capacity for future response. By March 2013, the RSR's \$34 million fund had leveraged \$3.1 billion from International Development Association for 45 projects in 34 countries, mainly in Africa (World Bank 2013). Following the global financial and economic crisis, the RSR shifted to supporting scalable social protection systems. As of December 2018, the RSR had leveraged more than \$9.6 billion for social protection projects in more than 100 International Development Association–eligible countries (World Bank 2019c).
- » The Social Protection Inter-Agency Cooperation Board, co-chaired by the World Bank and the International Labor Organization, and created in 2012 by the Group of Twenty countries to support countries in improving social protection systems and to promote the exchange of knowledge, policy experience, good practices, and data and information. A major achievement was the development of Inter-agency Social Protection Assessment tools, including a core social protection system diagnostic (16 countries completed; 6 in progress), identification (12 countries completed, including Morocco; 5 in progress), and social protection payments (13 countries completed, including Jamaica; 5 in progress).
- » Collaboration with the International Labor Organization and the World Food Programme on the production of the Atlas of Social Protection Indicators of Resilience and Equity (ASPIRE) to benchmark the scope and performance of social safety nets, social insurance, and active labor market programs. As of May 2020, ASPIRE had data for more than 120 countries based on national administrative and household survey data (including data for all evaluation case study countries).
- » The World Bank–wide Identification for Development Initiative to help countries build robust and inclusive digital identification systems through analytics, assessments, and financing. These systems are foundational to the development

(continued)

Box 4.1. The World Bank's Global Social Safety Network (cont.)

of social safety net registries and targeting systems. (Initiative work is ongoing in Bangladesh, Benin, Morocco, and Mozambique.)

- » Promoting South-South knowledge exchange on social safety nets and systems, including cash transfer communities of practice in Africa, Asia, and Latin America and the Caribbean, and arranging knowledge forums on key topics, such as designing and delivering social protection systems for urban areas (2015) and adaptive social protection (2018).

Source: ILO n.d.; World Bank 2019c, n.d.b; World Bank ASPIRE database (<http://datatopics.worldbank.org/aspire>).

Safety Net Crisis Preparedness at the Program, System, and Policy Level

In the case study countries, World Bank support for safety nets has focused on interventions *with the potential to play* a significant role in mitigating the impact of a crisis. Program-level preparedness requires a mix of programs suitable for combating chronic poverty that can be “adapted” and quickly scaled up in response to an economic downturn. To this end, it is essential to have at least one well-established program with expansive coverage that is appropriate to address the social impacts of an economic crisis (Grosh et al. 2011). Flexible program designs allow quick adaptation to increased demand by adjusting targeting criteria; increasing beneficiaries or benefit levels; relaxing conditionalities; streamlining grievance and redress processes to manage targeting errors (which may be critical to manage social tensions during a crisis); increasing public communications so that program changes are explained; and setting “sunset clauses” to scale back programs once a crisis recedes. In Jamaica, the World Bank supported the development of a graduation, or exit, strategy for beneficiaries of its flagship cash transfer program. In Benin, Mozambique, and Tajikistan, World Bank support has been in the form of establishing cash transfers and public works programs. In Morocco, a social protection investment project was approved in 2017 to expand

coverage of a unique identifying number for the Moroccan population and foreign residents and to improve targeting of social safety nets.

Support to build social protection systems has been a major World Bank priority in all case study countries. Having these systems in place provides a preparedness infrastructure on which specific programs could be adjusted or expanded. These “building blocks” enable programs to function in either normal or crisis times so that “the right people receive the right transfer amounts at the right time” at the lowest possible cost. These include outreach; intake and registration; assessment of needs and conditions; eligibility and enrollment; payment of benefits or provision of services (if any); and monitoring and management of beneficiaries, including program exit (George and Lindert 2017).

To be prepared for an economic downturn, it is essential that operational systems have the ability to quickly identify and target the newly vulnerable; that payments can be delivered quickly, predictably, and with low transaction costs to a greater number of beneficiaries; and that management information systems for beneficiary monitoring and management can ensure basic fiduciary standards, as well as interaction between individuals and program agencies along the delivery chain. Technological innovation in the use of big data, biometrics, and digital payments has greatly enabled the development of social protection systems in the past decade.

With World Bank support, Benin, Mozambique, and Tajikistan have started to put in place basic social protection systems as part of setting up cash transfer or public works programs with the longer-term goal of providing national platforms for other safety net programs. In case study countries with existing programs and institutional capacity, the World Bank is supporting the overhaul of specific system components such as intake and registration, payments, and beneficiary management (Bangladesh), and harmonization of programs and systems to exploit potential synergies and improve coverage, targeting and efficiency (Bangladesh, Morocco). In Jamaica and Ukraine, countries with better-established systems and expansive program coverage, World Bank support is leveraging the integration of core business processes for program delivery to serve as integrated platforms for multiple social pro-

tection programs and beyond, such as health insurance, scholarships, utility subsidies, and disaster risk management.

Adaptive Social Protection

Although this work is incipient in case study countries, the World Bank is supporting an increasing number of countries to incorporate an “adaptive social protection” approach. This is forming around two areas related to crisis preparedness, drawing from synergies among social protection, climate adaptation, and disaster risk management: (i) building household resilience *ex ante* so that poor and near-poor households are better able to withstand large shocks and (ii) enhancing the capability of social safety nets to respond to large shocks by introducing more flexible and scalable program designs and more dynamic delivery systems, including the use of early warning systems and defined triggers for activating the response and release of resources from program contingencies or additional funds (World Bank 2018b).¹

Effectiveness

Overall, this evaluation finds that significant progress has been made to set up and strengthen social protection delivery systems and social safety net programs. However, social safety net preparedness across the seven case study countries varies significantly at program, system, and policy levels. Jamaica, which has received longer-term World Bank social protection support, shows the strongest adaptability at all levels, thanks in part to strong and sustained government leadership since the early 2000s. In Bangladesh, Morocco, and Ukraine, policy, systems, and programs are of moderate strength with differing weaknesses, including in terms of institutional coordination and political economy constraints, hindering implementation progress. These dimensions of flexibility are the weakest in Benin, Mozambique, and Tajikistan, where social protection systems are only nascent (table E.1).

Remaining Challenges

The World Bank’s experience in the case study countries reveals several difficult *challenges*, especially in low institutional capacity and resource-constrained settings. Although by 2015 all countries had at least one safety

net program (World Bank 2015), social safety net coverage remains limited for poor and vulnerable people, especially in low-income countries. For example, in Benin, public works and cash transfer programs cover about 3.5 percent and less than 4 percent of extremely poor households, respectively (World Bank 2017). Safety net coverage of the poorest quintile stands at close to 10 percent in Tajikistan and less than 2 percent in Mozambique (ASPIRE database, last year available). In contrast, safety net coverage of the poorest quintile in Jamaica and Ukraine stands at 72 and 47 percent, respectively (ASPIRE database, last year available).

The development of social safety net registries or databases with household- and individual-level socioeconomic information, operational data, and information to capture vulnerability is a major challenge in most case study countries. In Morocco, for example, the development of a national identification system so that people can assess their identity is necessary to build a robust social registry. The usefulness of a registry, as a basis to determine eligibility for one or more programs in a large shock situation, depends on (i) coverage of current and potential beneficiaries, (ii) relevance of the information that is collected and stored in the registry to detect newly vulnerable people, (iii) inclusion of operationally relevant information on potential beneficiaries to quickly deliver benefits in a shock situation, and (iv) having up-to-date information to represent current household circumstances.

More than 30 developing countries are integrating beneficiary registries of safety net programs, and a similar number are in the process of doing so (Barca 2017). By 2018, more than 26 African countries were using social registries and another 16 were developing them, many with World Bank support. However, most of these registries require significant expansion, strengthening, and adoption by programs to become a meaningful instrument for responding to economic downturns. Benin and Mozambique's registries cover close to 12 and 0.3 percent of the population, respectively (Beegle et al. 2018).

A related challenge has been that traditional poverty targeting methods for social safety net programs, including proxy means tests, lack the ability to detect sudden changes in household welfare levels. In many countries, registries on which targeting mechanisms are built tend to use a mass registra-

tion approach conducted in geographic areas with high poverty once every three to five years. For crisis purposes, an approach that is on demand and on a rolling basis, where people can register at any time close to where they live, would be more appropriate. Of the case study countries, only Jamaica and Ukraine have more open registration. Although more developing countries are moving toward such a dynamic approach (such as Brazil, Chile, Georgia, and Turkey), most countries tend to have static registries due to (i) limited fiscal space, (ii) difficulty removing those who no longer qualify, (iii) rigid eligibility criteria, and (iv) limited administrative capacity, including lack of access points across the country for people to apply. Even when registries cover a large share of the population and serve many programs (Dominican Republic, Indonesia, Pakistan, Philippines), data quickly become outdated, which reduces usefulness for cyclical purposes (Leite et al. 2017).²

In some countries, the lack of formal identification (foundational ID systems) inhibits the ability of people to access a range of services and social safety net transfers because they are unable to prove they are who they say they are. In Benin, the national ID registration rate stands at about 68 percent (World Bank 2017), and in Mozambique, fewer than half of births are registered (Jeronimo 2019; see box 4.1). This is a pervasive problem compounding the issue of low coverage in low-income countries.

Although an area of rapid innovation, payment systems can represent another bottleneck area since social safety net programs in many countries use a variety of delivery methods depending on the accessibility and availability of private providers (cash-in-envelope, banking system, smart cards, debit cards, prepaid cards, cell phones). For example, in Mozambique, payments are manual, and in Morocco, the post office is the authorized agency for social protection payments (Leite et al. 2017). Nevertheless, digital government-to-person payments are being increasingly adopted and have the potential for more efficient, transparent, and reliable delivery, even in low-capacity environments. In 2013, the World Bank's Universal Financial Access 2020 initiative included Bangladesh, Morocco, and Mozambique among the 25 target countries for heightened financial inclusion engagement (ISPA 2015). In Bangladesh, a government-to-person payment system pilot is enabling the beneficiaries of three safety net programs to select among seven payment providers (Baur-Yazbeck et al. 2019).

Lack of safety net financing is another major issue, especially in the low-income case study countries. In Bangladesh, Benin, Mozambique, and Tajikistan, lack of fiscal space and/or low domestic revenue mobilization prevent safety net programs and systems from reaching sufficient scale and coverage to become a meaningful tool for crisis response. In Morocco, resource reallocation may be an option to boost financing for targeted safety net programs (World Bank 2017). Some countries are experimenting with (Jamaica) or exploring (Bangladesh, Benin, Mozambique) different strategies and instruments to ensure financing for social safety net interventions (albeit to respond to climate shocks), such as contingency funds, contingent credit lines, disaster insurance, and index-based triggers.

¹ For example, the Ethiopia Productive Safety Net Program has been adapted to scale up. During the Horn of Africa drought of 2011, the program supported 3.1 million additional households for three months and extended the duration of transfers to more than 85 percent of its 7.6 million beneficiaries. The Kenya Hunger Safety Net Program (HSNP) preregistered all households (374,000) in the poorest northern counties of the country, opening bank accounts and issuing debit cards for them. Only 27 percent of these households are regular HSNP beneficiaries; the others receive a one-time transfer only if they are deemed to be “at risk,” as determined by a vegetation condition index derived from satellite data. Thus, the program may temporarily scale up to 50–75 percent of the area’s population (Watson 2016, cited by Beegle 2018). As a result of the preregistration and automatic trigger, the HSNP took only two weeks between the shock and the first payment in the 2015 and 2016 droughts (Bowen et al. 2020).

² The World Bank has started to experiment with the use of remote sensing, GIS and cell phone data, machine learning, and high-resolution satellite imagery to predict poverty, which could help address some of these constraints (Bowen et al. 2020).

5 | Conclusions and Lessons

This evaluation finds generally high-quality diagnostics and dedicated and motivated staff across different countries contributing to helping countries identify and reduce fiscal and financial sector vulnerabilities. This broad picture is confirmed uniformly by extensive interviews with client governments, development partners, the financial sector, and other agencies and institutions. However, large programs and resources tend to attract more seasoned staff, and small programs in smaller countries often rely on periodic support from more senior staff who also devote considerable time to larger countries.

By and large, World Bank staff undertake necessary, timely, and relevant analysis to identify vulnerabilities, although this is, at times, made more difficult by the need for greater transparency in fiscal data—especially on SOEs and debt. Difficult issues are raised in diagnostic reports and during policy dialogue with client governments. Only in one case study (Bangladesh) was frankness of assessments constrained (largely by a desire to maintain good relations with country authorities).

This evaluation found differences in the rigor with which fiscal versus financial sector vulnerabilities were identified and acted on. To some extent, this reflected differences in the main diagnostic tools used and data availability. Financial sector work is perceived as less politicized by counterparts, in part reflecting the nature of programs like the FSAP and related technical assistance, giving an easier entry point for discussions with authorities. Fiscal analysis, however, tended to be more political, and World Bank advice was subject to greater discretion at the country level.

As a general point, the Bank Group needs to consider compound shocks more systematically and regularly as part of its macrofiscal monitoring. Existing tools like DSAs raise awareness of sustainability issues with clients but can give a misleading impression of vulnerabilities when the assumptions on which they are built are overly optimistic, exclude contingent liabilities (both explicit and implicit), or fail to contemplate a compounding of shocks. This evaluation notes cases such as that of Benin, where the DSA insuffi-

ciently captured a scenario with a significant drop in economic activity, as happened in 2019 after the closure of the border with Nigeria. Similarly, the 2013 Tajikistan DSA did not consider downside risks to remittances, which fell from 40 percent to 20 percent of GDP the next year. In Bangladesh, the DSA did consider the implications of implicit and explicit contingent liabilities and widespread concerns with the quality of GDP data (which World Bank staff believed to have been systematically overestimated for political reasons).

IEG asked clients to indicate areas where the Bank Group could do better. Clients indicated that the Bank Group brings substantial value in providing quality analysis to identify vulnerabilities, which is an important public good in country-level work, but more needs to be done to support clients to strengthen data systems and capacity for generating better, timelier, and more frequent data on both fiscal (especially debt) and financial vulnerabilities, and to disseminate information and analysis more broadly within countries. Finally, clients report that the Bank Group could sometimes do better in terms of timeliness and responsiveness to their requests for technical assistance and advice, especially in smaller countries with smaller Bank Group programs.

Lessons

This evaluation identifies five lessons related to how the Bank Group can improve identification of, response to, and support for the reduction of fiscal and financial sector vulnerabilities:

First, up-to-date, accurate, and timely knowledge is the foundation of effective Bank Group support to its clients. It is therefore important for the Bank Group to remain engaged in regular and systematic monitoring and core diagnostics of fiscal and financial vulnerabilities, *even when client countries are not ready to confront them*. This includes attention to the quality of data and transparency.

Second, the Bank Group is better able to support countries to reduce vulnerabilities when building fiscal and financial resilience is fully and explicitly integrated into Bank Group-supported country strategies, with a clear ar-

tication of priority challenges. Where knowledge is incomplete, analytical and diagnostic needs should be clearly articulated and planned for.

Third, more systematic consideration of the impact of large and compound fiscal and financial sector risks (for example, from SOEs and contingent liabilities), including in DSAs, is needed to inform policy dialogue with clients.

Fourth, with the IMF increasingly concentrating its financial sector surveillance on systemically important countries, the Bank Group should consider how best to give adequate attention in its financial sector diagnostic work to financial stability issues in less systemically important but potentially vulnerable economies. This may have implications for the division of labor with the IMF on financial sector work as well as resource costs that should be clearly identified and managed.

Fifth, addressing fiscal and financial vulnerabilities is intensely political, with vested interests sometimes opposing appropriate policy reforms and institutional strengthening. To help build domestic demand for better preparedness, Bank Group staff should seek to more regularly undertake outreach and dialogue with parliamentarians, civil society, and local think tanks to foster an understanding of vulnerabilities and their potential costs in an effort to build support for critical reforms.

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APPENDIXES

Independent Evaluation Group

*Addressing Country-Level Fiscal and
Financial Sector Vulnerabilities*

Appendix A. Evaluation Design and Methodology

In line with the Approach Paper (World Bank 2019), the evaluation focused on the following questions:

- » Identifying vulnerabilities:
 - » Did the World Bank Group undertake the right analysis and diagnostic work on client countries at the right time to identify major fiscal and financial sector vulnerabilities?
 - » Did the Bank Group clearly and candidly identify key country-specific fiscal and financial sector vulnerabilities and needed reforms to social safety nets to improve responsiveness?
- » Responding to vulnerabilities: Did the Bank Group follow up help client countries address identified fiscal and financial sector vulnerabilities, including by helping to design and put in place appropriate mechanisms and frameworks?
- » Reducing vulnerabilities: Were Bank Group efforts to help clients reduce key fiscal and financial sector vulnerabilities and develop mechanisms and frameworks for crisis management and social protection successful? In providing support, did the Bank Group coordinate effectively with key development partners, particularly the International Monetary Fund (IMF)?
- » Preparing the Bank Group for crises: How well prepared is the Bank Group (in terms of staffing and incentives) to identify key fiscal and financial sector vulnerabilities and help its clients address them in a timely manner?

The evaluation employed a multilevel, mixed methods approach informed by a conceptual framework and theory, and data collection covered corporate and country-level analysis (with a focus on the fiscal, financial, and social safety net dimensions of crisis preparedness). The main component of the evaluation approach was *case study analysis*, including a cross-cutting *synthesis of thematic and sector issues*. Findings arose from individual case studies. Seven field-based case

studies were selected as a purposive sample from Bank Group client countries to reflect diverse country circumstances, country vulnerabilities and experience with exogenous shocks, and regional diversity and income levels.

Design

The evaluation design matrix (table A.1) shows how different methods apply to different questions and different levels of analysis: country, thematic, and partnerships and synergies. The evaluation covers the following Bank Group institutions: the International Development Association and the International Bank for Reconstruction and Development, which together are known as the World Bank; the International Finance Corporation (IFC); and the Multilateral Investment Guarantee Agency.

Table A.1. Evaluation Design Matrix

Level of Analysis	Questions 1 & 2: Diagnostic Work	Question 3: Operational Response	Question 4: Effectiveness of Operational Response	Question 5: Corporate Readiness
Cross-cutting	Literature review PRA for identification and case selection Theory of change development Review of relevant data on crisis preparedness indicators			
Corporate				Semistructured interviews Review of relevant documentation and corporate data
Selected countries	Review of key diagnostic instruments and knowledge products Semistructured interviews	Review of country strategies PRA (for example, PADs) Semistructured interviews	PRA (for example, ICRRs) Semistructured interviews	Semistructured interviews
Cross-case perspective	Pattern analysis Narrative synthesis across countries on fiscal, financial, and social safety net dimensions of crisis preparedness			

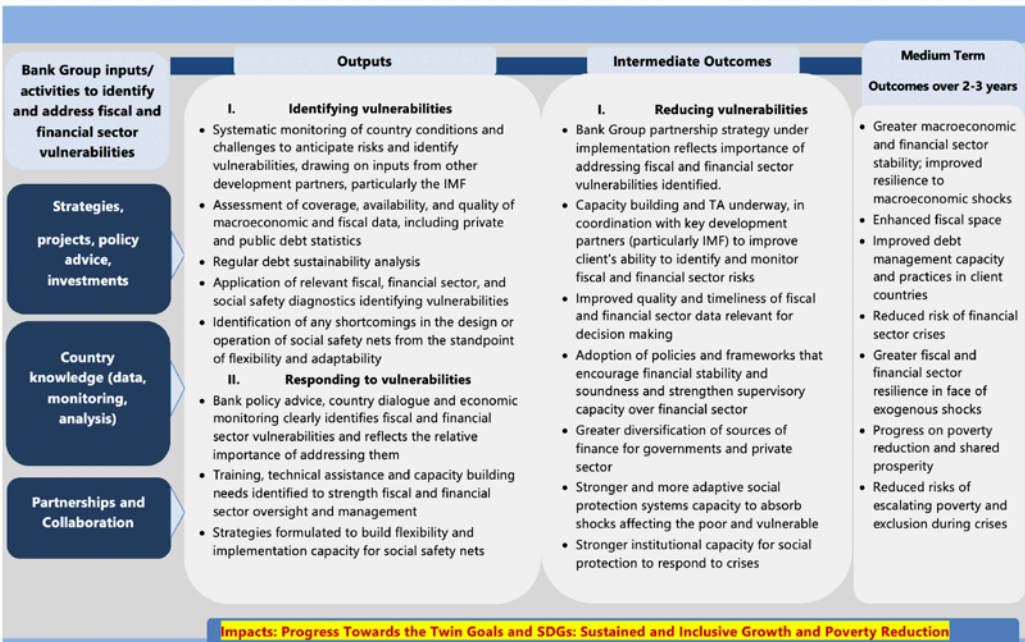
Source: Independent Evaluation Group.

Note: ICRR = Implementation Completion and Results Report Review; PAD = Project Appraisal Document; PRA = portfolio review and analysis.

Theory of Change

The theory of change posits that the Bank Group’s country strategies; lending, project, investment, and knowledge services; and convening power are key elements of support to client countries to help reduce vulnerabilities to shocks. It is based on an examination of past Independent Evaluation Group evaluations on related subjects, related literature on crisis preparedness, and extensive corporate interviews to understand the Bank Group’s approach to identifying, addressing, and reducing fiscal and financial vulnerabilities. Bank Group support for reducing fiscal and financial sector vulnerabilities contributes to outputs and intermediate outcomes that improve institutional capacity and policy readiness to reduce vulnerabilities and strengthen social safety nets (figure A.1).

Figure A.1. Theory of Change for Reducing Key Vulnerabilities in Client Countries



Source: Independent Evaluation Group staff, based on the World Bank 2013, 2017, Financial Sector Strategy, and Social Protection Strategy.

Note: IMF = International Monetary Fund; SDG = Sustainable Development Goal; TA = technical assistance.

Portfolio Review

General Portfolio

The portfolio review followed a two-stage approach. First, the evaluation team analyzed the general portfolio related to reducing fiscal and financial sector vulnerabilities, which was identified based on theme codes and additional screening of project objectives, pillars, and summaries using text analytics and manual screening to eliminate inclusion and exclusion errors. In the next stage, the team developed a more targeted portfolio for countries that had Systematic Country Diagnostics (SCDs) and Country Partnership Frameworks in the evaluation period and a minimum engagement of the Bank Group in terms of core macroeconomic and financial sector diagnostics. It then classified countries into three groups: those that were in crises, those that were near crises, and those that were not in crises. This narrower “target portfolio” was subject to a more in-depth review, which included a review of existing project validation evaluation evidence from Implementation Completion and Results Report Reviews and Project Performance Assessment Reports. This target portfolio also served to select a purposive sample of seven countries, which were studied in detail using Bank Group country strategies and lending, project, and analytic and advisory interventions. The portfolio review aimed to include relevant projects in the broad areas of macrofiscal and debt management, the financial sector, and social safety nets. IFC and the Multilateral Investment Guarantee Agency, which played a considerably smaller role than the World Bank in the Bank Group’s activities geared toward addressing and reducing fiscal and financial sector vulnerabilities, were assessed at the country level.

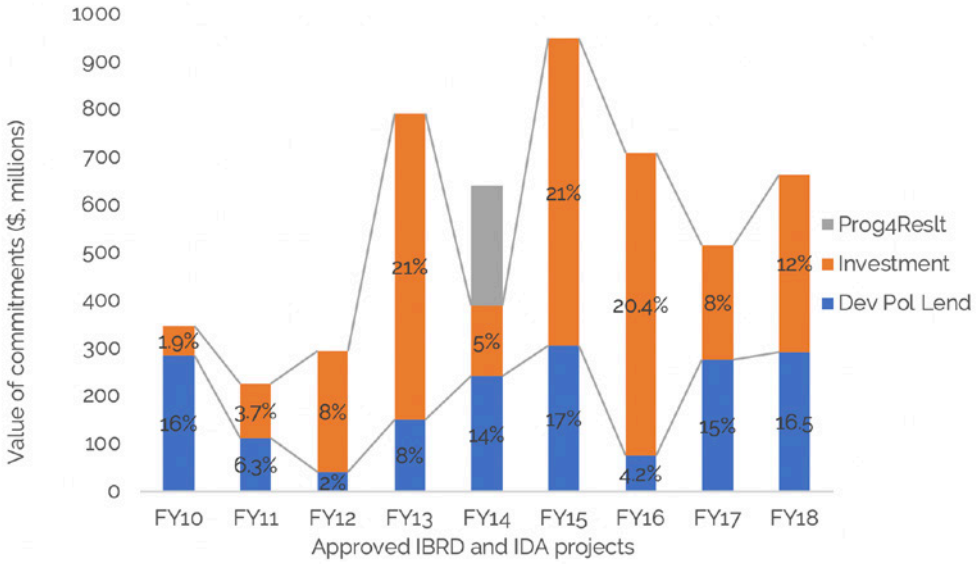
For the evaluation, the team identified projects that had at least one relevant thematic contribution greater than or equal to 20 percent of the value of the project. A total of 204 World Bank projects were identified as relevant to the evaluation.

Lending Portfolio in Low-Income Countries

In low-income countries (LICs), World Bank support to reduce fiscal and financial sector vulnerabilities came in the form of investment projects, development policy loans, and Program-for-Results, with notably increased

overall lending since 2013. The main instrument of support was investment lending, although development policy financing dominated in some years (for example, 2010; see figure A.2 and table A.2).

Figure A.2. Value of Lending Commitments to Reduce Fiscal and Financial Sector Vulnerabilities by Instrument in Low-Income Countries



Source: Independent Evaluation Group.

Note: Dev = development; FY = fiscal year; IBRD = International Bank for Reconstruction and Development; IDA = International Development Association; Pol = policy; Prog4Reslt = Program-for-Results.

Table A.2. Size of the Total Lending Portfolio to Reduce Fiscal and Financial Sector Vulnerabilities by Instrument in Low-Income Countries (FY10–18)

Lending Instrument	Total World Bank Commitments (\$, billions)
DPL	1.8
Investment	3.1
P4R	0.2
Total	5.1

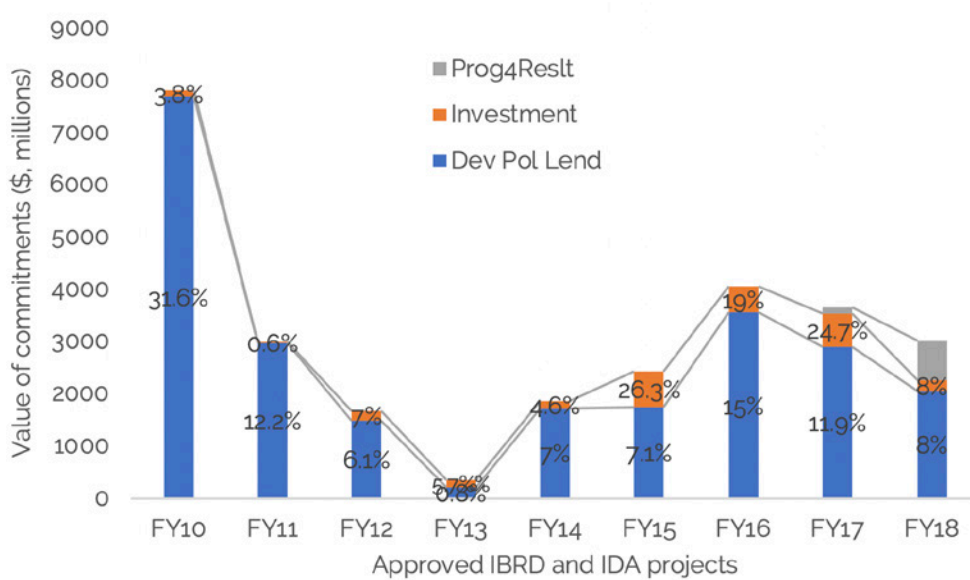
Source: Independent Evaluation Group.

Note: DPL = development policy loan; FY = fiscal year; P4R = Program-for-Results.

Lending Portfolio in Middle-Income Countries

In middle-income countries (MICs), the World Bank supported reduction in fiscal and financial sector vulnerabilities largely through development policy loans over the evaluation period (figure A.3 and table A.3).

Figure A.3. Value of Lending Commitments to Reduce Fiscal and Financial Sector Vulnerabilities by Instrument in Middle-Income Countries



Source: Independent Evaluation Group.

Note: Dev = development; FY = fiscal year; IBRD = International Bank for Reconstruction and Development; IDA = International Development Association; Pol = policy; Prog4Reslt = Program-for-Results.

Table A.3. Size of the Total Lending Portfolio to Reduce Fiscal and Financial Sector Vulnerabilities by Instrument in Middle-Income Countries (FY10–18)

Lending Instrument	Total World Bank Commitments (\$, billions)
Development policy lending	24.3
Investment lending	2.6
P4R	0.8
Total	27.7

Source: Independent Evaluation Group.

Note: FY = fiscal year; P4R = Program-for-Results.

World Bank Nonlending: Analytic and Advisory Activities

The Bank Group engaged in significant monitoring, analysis, and identification of fiscal and financial sector vulnerabilities throughout the evaluation period, 2010–18. At the country level, this was reflected in Country Economic Memorandums (CEMs), Public Expenditure Reviews (PERs), Public Finance Reviews, Financial Sector Assessment Programs (FSAPs), Debt Management Performance Assessments (DeMPAs), Macro Poverty Outlooks, and other advisory services and analytics. World Bank and IFC knowledge in this area was also reflected in the advisory and capacity-building efforts of key fiscal and financial sector institutions (for example, ministries of finance, central banks, banking supervisors, deposit guarantee agencies, and commercial banks).

The first selection criterion for identifying the relevant analytic and advisory activities product portfolio was to select products that have at least one thematic contribution of greater than or equal to 70 percent the sum of all contributions. Lower thresholds of thematic contribution resulted in unreasonably large numbers of knowledge products that were largely not relevant

for the evaluation. This analysis led to the selection of 720 advisory services and analytics products, which were categorized under three main themes (finance, fiscal, and social protection) and yielded 570 products.

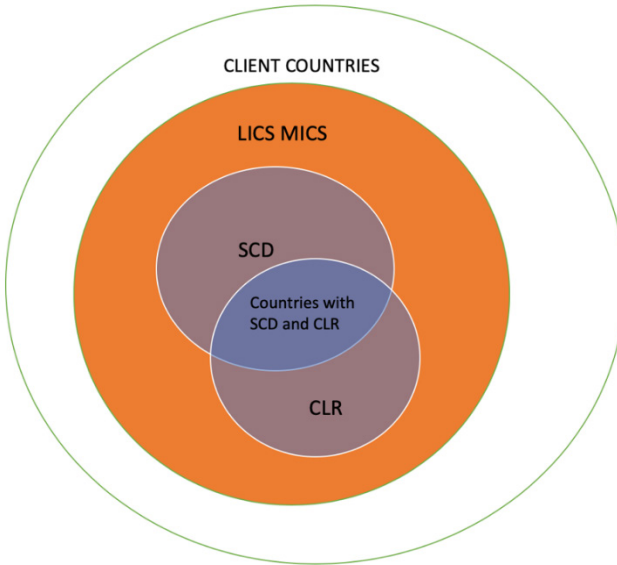
Comparative Case Studies

Selection

A reference group of countries had a minimum portfolio of Bank Group strategic country engagement, including knowledge and lending interventions, and diagnostics. Countries were selected that had direct World Bank engagement in the fiscal and financial sectors (for example, from FSAPs, CEMs, Public Expenditure and Financial Accountability [PEFA] assessments, PERs, and Public Finance Reviews). Specific case study countries were selected to ensure a range of fiscal and financial vulnerabilities, which was measured using a set of indicators of fiscal health (for example, ratios of debt to gross domestic product, primary and overall fiscal balances, and DeMPA and PEFA scores) and of financial sector health (for example, financial sector balance sheet, credit, and liquidity indicators), supplemented by qualitative judgment about vulnerabilities based on a review of the World Bank’s strategic, fiscal, and financial diagnostics (SCDs, CEMs, PERs, FSAPs) and IMF assessments (for example, Article IV consultation reports).

Figure A.4 illustrates how filters were used in the selection of countries. The outermost white circle represents the total number of client countries. The orange circle is a mix of LICs and MICs. The shaded blue region consists of countries that have completed both an SCD and Completion and Learning Reviews during the review period.

Figure A.4. Case Study Country Selection



Source: Independent Evaluation Group.

Note: CLR = Completion and Learning Review; LIC = low-income country; MIC = middle-income country; SCD = Systematic Country Diagnostic.

Analysis was conducted to narrow the choice of countries: Inclusion of both LICs and MICs that have SCDs and Completion and Learning Reviews. LICs and MICs for the period of evaluation were selected using the World Bank income classification as of June 2018.

The next step was to identify and select case study countries from these 89. The selection criteria to select LICs were that the country must have had a PEFA assessment, FSAP (or at least a similarly deep financial sector diagnostic or technical assistance engagement), and a DeMPA during the evaluation period. The criteria identified seven LICs: Benin, Madagascar, Malawi, Mozambique, Rwanda, Tajikistan, and Uganda.

Of these countries, Benin, Mozambique, and Tajikistan were selected based on a diversity of current fiscal and financial vulnerabilities using a combination of indicators supplemented and informed by any recent FSAP assessments, IMF Article IV consultation reports, and World Bank macroeconomic assessments.

The selection criteria for MICs were as follows: The country must have had a PEFA assessment and FSAP during the evaluation period. The selection criteria generated 29 countries: Albania, Argentina, Armenia, Azerbaijan, Bangladesh, Belarus, Belize, Bosnia and Herzegovina, Cambodia, Colombia, Georgia, Ghana, India, Indonesia, Kyrgyz Republic, Mauritania, Mauritius, Moldova, Mongolia, Montenegro, Morocco, Panama, Papua New Guinea, Paraguay, Peru, Serbia, Tunisia, Vietnam, and Zambia.

Of these, Bangladesh, Jamaica, Morocco, and Ukraine were selected, taking account of geographic and regional diversity. The selection was based on a diversity of current fiscal and financial vulnerabilities using a combination of indicators supplemented and informed by recent FSAP assessments, IMF Article IV consultation reports, and World Bank macroeconomic assessments. Jamaica was selected even though it did not have a recent PEFA assessment because significant fiscal and financial sector engagement had been done in the context of a large World Bank program.

Execution

A case study template and interview protocols were used to ensure a common question and interview framework and comparative lens across case studies. Within case studies, the team compared and contrasted evidence from interviews with client governments, the Bank Group, and other institutions involved in supporting the reduction in fiscal and financial sector vulnerabilities. The team executed two initial pilot country case studies (Tajikistan and Ukraine), which tested the protocols and guided subsequent case studies. All the case studies were executed between April and November 2019.

Design

The following questions were asked of stakeholders across case studies.

Q.1 To what extent do you think the WBG was helpful in identifying vulnerabilities in your area of work? [Yes, to a large extent, to a moderate extent, to a modest extent or no]. Explain briefly. Provide examples and periods.

Q.1.a. In your view, what are the major contributions of the World Bank Group in ex-ante identification of key macro-fiscal and macro-financial vulnerabilities in your country since 2010? {identify types of vulnerabilities and reference diagnostics used}

Q.1.b. Did the WBG fail to identify any macro-financial vulnerabilities that emerged later? What were they?

Q.2 What was the nature and structure of support provided by the World Bank Group to your country to address identified macro-fiscal and macro-financial vulnerabilities?

Q.2.a. Did the Bank-supported Strategy fail to follow up on some of the key identified vulnerabilities? Why?

Q. 2.b. After identifying vulnerabilities, was support provided by the World Bank Group timely?

Q.2.c. Did the World Bank Group support your country in developing appropriate frameworks and risk mitigation measures to address the key macro-fiscal, macro-financial vulnerabilities? Which ones?

Q.3 How effective was Bank Group support?

Q.3.a. How well does the World Bank Group collaborate with partners in achieving results?

Q.4 Did the World Bank Group have the adequate staffing, skill sets and diagnostic tools to help your country to identify and reduce fiscal and financial sector vulnerabilities and strengthen social safety nets?

Q.5. What are some of the key lessons for the World Bank Group to enable it to improve its support to your country in identifying and addressing fiscal and financial sector vulnerabilities and strengthening social safety nets? What could have been done better?

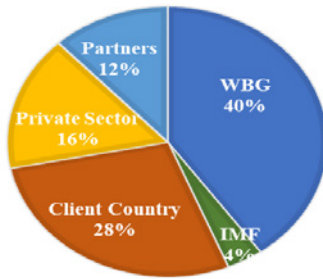
NVIVO-Aided Qualitative Analysis of Interviews

Qualitative data analysis through natural language processing using NVIVO was used to systemically organize and analyze nonnumerical, unstructured data from interviews. Over 200 interviews were undertaken with approx-

imately 300 individual stakeholders. Text queries enabled evaluators to gather relevant information pertaining to each diagnostic question. After subsequent tabulations of data, common themes emerged across case studies. Select findings from the NVIVO-aided analysis of qualitative information from the interviews is provided below (figures A.5–A.9).

Figure A.5. Number and Structure of Mission Interviews by Stakeholder Group

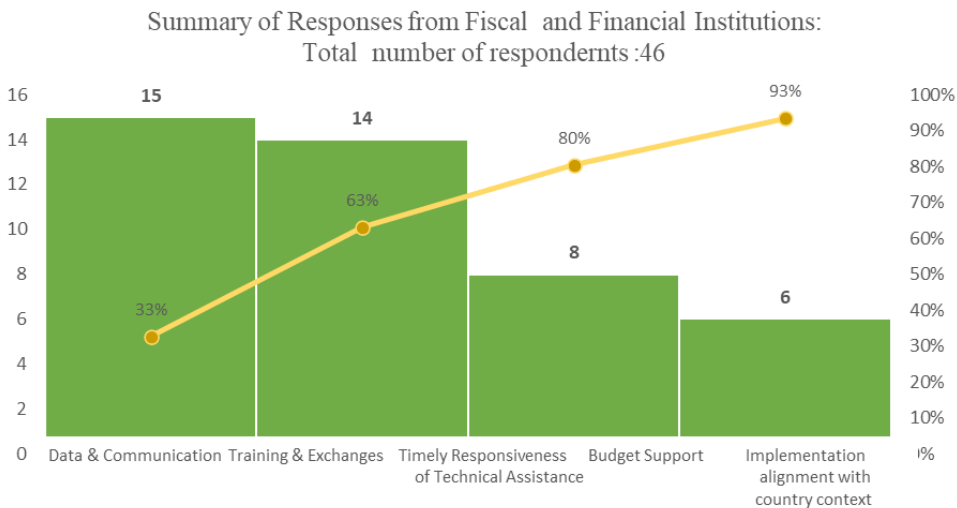
COMPOSITION OF MISSION INTERVIEWS
EVALUATION: FY10-FY19
TOTAL: 147 [220 INFORMANTS]



Source: Independent Evaluation Group NVIVO analysis of mission interviews.

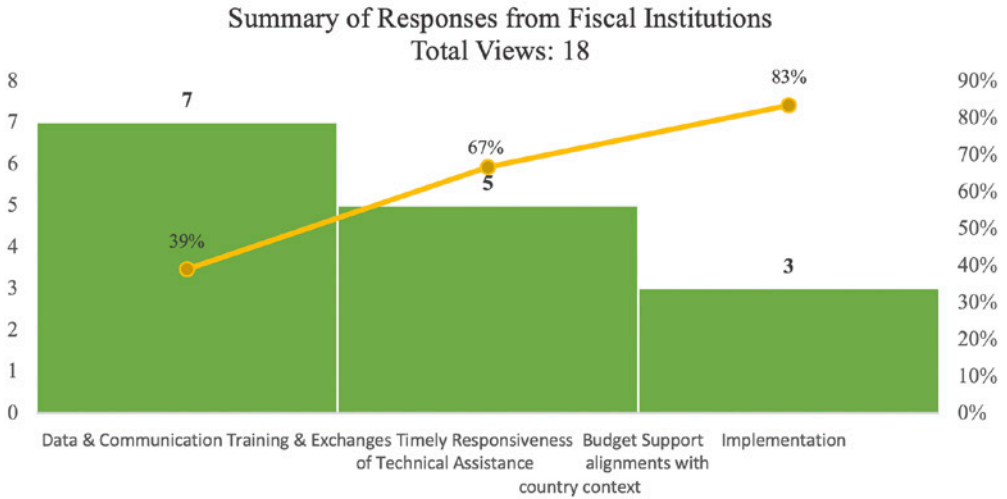
Note: FY = fiscal year; IMF = International Monetary Fund; WBG = World Bank Group.

Figure A.6. Overall Client Feedback: What Could the World Bank Group Do Better?



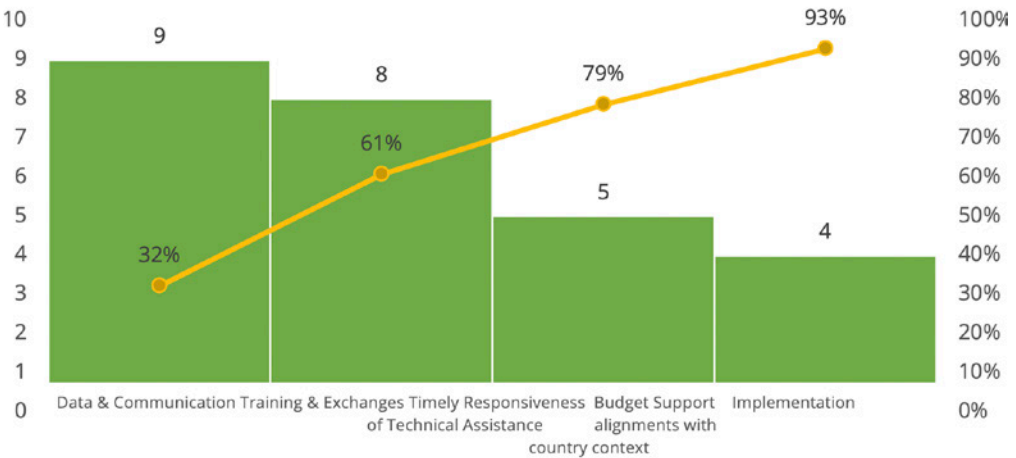
Source: Independent Evaluation Group NVIVO analysis of mission interviews.

Figure A.7. Fiscal Client Feedback: What Could the World Bank Group Do Better?



Source: Independent Evaluation Group NVIVO analysis of mission interviews.

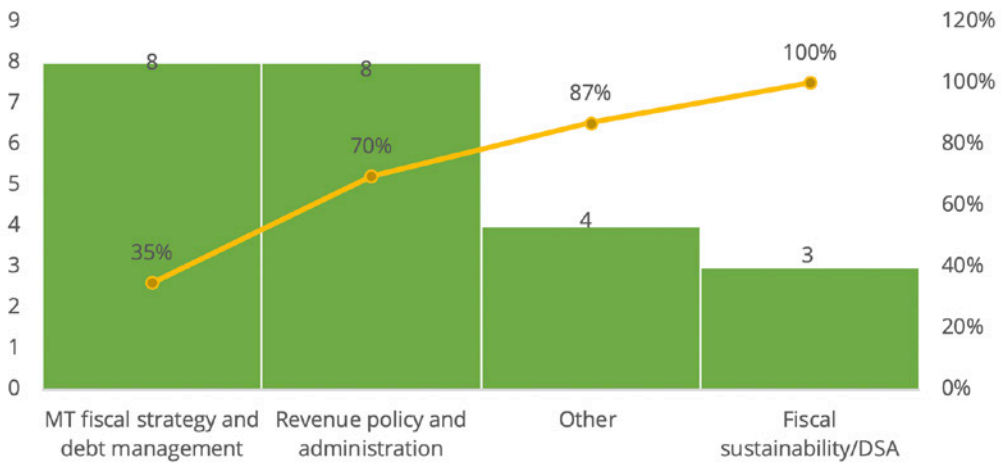
Figure A.8. Financial Institutions Client Feedback: What Could the World Bank Group Do Better?



Source: Independent Evaluation Group NVIVO analysis of mission interviews.

Note: Figure is a summary of responses from 28 views.

Figure A.9. Client Feedback: Areas of World Bank Effectiveness on Fiscal Vulnerabilities



Source: Independent Evaluation Group NVIVO analysis of mission interviews.

Note: Responses from 23 views. "Other" refers to World Bank assistance in other fiscal areas such as pensions. DSA = Debt Sustainability Analysis.

Validity of Findings

The evaluation uses corporate, case study, and cross-case study analysis, triangulating findings from different sources, which include literature review (World Bank and external), document reviews and data analysis, current and past government officials, and corporate level and country-level interviews with World Bank and IMF staff, development partners, the private sector and other stakeholders.

Internal validity of case study findings reflects the in-depth assessment of cases using multiple data sources and methods. External validity is limited and may apply to countries with similar characteristics to those of the case studies: countries with a minimum of Bank Group engagement in terms of SCDc and Country Partnership Frameworks highlighting fiscal and financial vulnerabilities.

Limitations

Limitations of the dominantly case study approach include that the sample may be biased and that underlying information may exclude countries with

rising fiscal and financial vulnerabilities and in which the Bank Group had attempted engagement but for various reasons was not able to develop a tangible program. Poor quality or availability of data in some countries may limit the granularity and precision of the analysis; but it might also point out vulnerabilities that need to be addressed in the future. In addition, when assessing the effectiveness of Bank Group interventions related to social safety nets, the evaluation did not find unambiguous benchmarks, making it difficult to separate the assessment of the quality of social safety nets overall and their flexibility to absorb major shocks.

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¹ A Public Expenditure and Financial Accountability assessment can be undertaken for a country or a province in a country. For this analysis, the Independent Evaluation Group considered only country Public Expenditure and Financial Accountability assessments.

² The three countries that are high income according to the World Bank classification of June 2018 were Argentina, Croatia, and Panama. These countries have been included as they were categorized as middle income during the evaluation period, 2010–18.

Appendix B. Key Fiscal and Financial Sector Indicators for Case Study Countries

Table B.1. Key Fiscal and Financial Sector Indicators for Bangladesh (percentage of gross domestic product, unless otherwise indicated)

Indicator	2010	2011	2012	2013	2014	2015	2016	2017	2018
Fiscal									
Gross government debt	35.5	36.6	36.2	35.8	35.3	33.7	33.3	32.5	34.8
External debt stocks, short term (DOD, current; \$, billions)	2.9	2.1	2.0	3.7	4.2	6.6	7.8	10.8	9.0
Fiscal balance	-2.7	-3.6	-3.0	-3.4	-3.1	-4.0	-3.4	-3.3	-4.1
Primary balance	-0.8	-1.9	-1.1	-1.4	-1.0	-1.9	-1.5	-1.6	-1.7
Government revenue-to-gross debt	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Financial									
Gross government debt	35.5	36.6	36.2	35.8	35.3	33.7	33.3	32.5	34.8
Nonperforming loans to total loans	7.3	6.1	10.0	8.9	10.0	8.8	9.2	9.3	10.3
Capital to risk-weighted assets	9.3	11.4	10.5	11.5	11.3	10.8	10.8	10.8	10.5
Tier I capital to risk-weighted assets	...	8.3	7.1	8.3	8.6	8.0	8.1	7.5	6.8
Returns on assets	1.8	1.5	0.6	0.9	0.6	0.8	0.7	0.7	0.7
Liquid asset to total assets	23.0	25.4	27.1	32.5	32.7	26.5	24.9	19.9	20.3
Liquid assets to short-term liabilities	...	...	43.8	57.9	47.8	47.8	46.0	34.0	44.5
Short-term debt (% of total reserves)	26.4	22.9	15.4	20.6	18.6	24.1	24.3	32.2	28.2

Source: IMF 2018a, 2019b; World Bank Open Data (<https://data.worldbank.org>).

Table B.2. Key Fiscal and Financial Sector Indicators for Benin (percentage of gross domestic product, unless otherwise indicated)

Indicator	2010	2011	2012	2013	2014	2015	2016	2017	2018
Fiscal									
Gross government debt	28.7	29.9	26.7	25.3	30.5	42.4	49.7	54.4	54.6
External debt stocks, short term (DOD, current; \$, billions)	0.2	0.3	0.5	0.2	0.2	0.1	0.1	0.1	0.1
Fiscal balance	-0.4	-1.3	-0.3	-1.9	-2.3	-7.6	-5.9	-5.8	-4.7
Primary balance	0.1	-0.9	0.3	-1.4	-1.9	-6.9	-4.7	-3.8	-2.5
Government revenue-to-gross debt	0.7	0.6	0.7	0.7	0.6	0.4	0.3	0.3	0.3
Financial									
Nonperforming loans to total loans	15.8	15.6	18.6	21.2	21.5	22.1	21.8	19.4	21.6
Capital to risk-weighted assets	10.0	12.5	9.2	9.5	9.0	7.9	9.3	11.9	8.2
Tier I capital to risk-weighted assets	...	...	...	...	...	...	...	...	...
Returns on assets	1.1	1.5	1.3	1.1	1.0	0.2	0.3	0.2	...
Liquid asset to total assets	30.8	28.0	22.9	21.9	23.0	18.9	16.2	14.5	14.4
Liquid assets to short-term liabilities	...	...	...	...	...	...	...	...	...
Short-term debt (% of total reserves)	...	...	...	...	...	...	...	...	...

Source: IMF 2019a, 2019b; World Bank Open Data (<https://data.worldbank.org>).

Table B.3. Key Fiscal and Financial Sector Indicators for Jamaica (percentage of gross domestic product, unless otherwise indicated)

Indicator	2010	2011	2012	2013	2014	2015	2016	2017	2018
Fiscal									
Gross government debt	143.2	141.7	145.0	140.5	139.7	121.3	121.7	109.4	101.1
External debt stocks, short term (DOD, current; \$, billions)	1.1	1.0	1.8	1.4	1.5	1.5	1.6	1.7	2.0
Fiscal balance	-6.3	-6.4	-4.1	0.1	-0.5	-0.3	-0.2	0.5	1.2
Primary balance	4.6	3.2	5.4	7.6	7.5	7.2	7.6	7.5	7.5
Government revenue-to-gross debt	0.19	0.18	0.18	0.19	0.19	0.22	0.25	0.29	0.32
Financial									
Nonperforming loans to total loans	6.5	8.9	7.0	5.4	5.0	4.1	3.5	3.5	...
Capital to risk-weighted assets	18.2	16.1	14.1	15.1	15.9	14.9	14.5	14.5	...
Tier I capital to risk-weighted assets	...	...	...	...	...	...	...	...	...
Returns on assets	2.8	4.1	1.2	0.4	1.9	2.7	1.9	1.9	...
Liquid asset to total assets	...	...	...	...	...	...	...	...	...
Liquid assets to short-term liabilities	...	...	...	...	...	...	...	...	...
Short-term debt (% of total reserves)	43.6	43.3	88.4	79.2	59.4	51.2	49.6	44.9	56.4

Source: IMF 2018b, 2019b; World Bank Open Data (<https://data.worldbank.org>).

Table B.4. Key Fiscal and Financial Sector Indicators for Mozambique
(percentage of gross domestic product, unless otherwise indicated)

Indicator	2010	2011	2012	2013	2014	2015	2016	2017	2018
Fiscal									
Gross government debt	43.3	38.0	40.1	53.1	62.4	88.1	121.6	103.2	100.4
External debt stocks, short term (DOD, current; \$, billions)	0.6	0.3	0.3	0.7	0.4	0.8	0.6	1.1	1.2
Fiscal balance	-3.8	-4.8	-3.9	-2.7	-10.7	-7.2	-6.3	-3.4	-5.3
Primary balance	-3.1	-3.9	-2.9	-1.9	-9.6	-5.9	-3.3	0.0	-1.5
Government revenue-to-gross debt	0.6	0.7	0.7	0.6	0.5	0.3	0.2	0.3	0.3
Financial									
Nonperforming loans to total loans	1.9	2.6	3.2	2.3	3.2	4.3	5.7	12.6	11.1
Capital to risk-weighted assets	14.4	17.1	17.9	16.9	15.1	17.0	8.8	21.5	23.8
Tier I capital to risk-weighted assets	13.7	16.1	16.9	16.0	13.6	15.5	14.2	20.8	22.6
Returns on assets	3.0	2.6	2.5	1.9	2.1	2.0	1.3	0.7	2.5
Liquid asset to total assets	22.4	27.8	33.4	17.3	13.5	18.6	20.7	12.8	13.9
Liquid assets to short-term liabilities	...	...	...	23.1	17.6	24.9	28.9	17.8	19.9
Short-term debt (% of total reserves)	26.7	10.2	11.7	21.5	13.6	31.0	26.4	32.4	37.8

Source: IMF 2019b, 2019c.; World Bank Open Data (<https://data.worldbank.org>).

Table B.5. Key Fiscal and Financial Sector Indicators for Morocco (percentage of gross domestic product, unless otherwise indicated)

Indicator	2010	2011	2012	2013	2014	2015	2016	2017	2018
Fiscal									
Gross government debt	49.0	52.5	56.5	61.7	63.3	63.7	64.9	65.1	65.2
External debt stocks, short-term (DOD, current; \$, billions)	2.7	3.8	4.2	5.4	7.6	6.9	8.9	7.5	7.4
Fiscal balance	-4.3	-6.6	-7.2	-5.1	-4.8	-4.2	-4.5	-3.5	-3.7
Primary balance	-2.0	-4.4	-4.7	-2.5	-2.1	-1.4	-1.8	-0.9	-1.3
Government revenue-to-gross debt	0.5	0.5	0.5	0.5	0.4	0.4	0.4	0.4	0.4
Financial									
Nonperforming loans to total loans	4.8	4.8	5.0	5.9	6.9	6.8	7.1	7.0	6.8
Capital to risk-weighted assets	12.3	11.7	12.3	13.3	13.8	13.7	14.2	13.8	14.0
Tier I capital to risk-weighted assets	9.7	9.6	10.2	11.1	11.6	11.4	11.5	10.9	10.5
Returns on assets	1.2	1.1	1.0	1.0	0.9	0.8	1.1	0.9	0.9
Liquid asset to total assets	12.0	11.4	10.5	12.5	13.3	16.1	14.3	13.6	12.0
Liquid assets to short-term liabilities	16.0	16.1	14.7	17.4	17.7	21.2	18.3	16.7	14.9
Short-term debt (% of total reserves)	11.6	19.0	24.3	28.5	37.5	30.2	35.6	28.7	30.4

Source: IMF 2019b, 2019d; World Bank Open Data (<https://data.worldbank.org>).

Table B.6. Key Fiscal and Financial Sector Indicators for Tajikistan (percentage of gross domestic product, unless otherwise indicated)

Indicator	2010	2011	2012	2013	2014	2015	2016	2017	2018
Fiscal									
Gross government debt	36.6	35.3	32.3	29.1	27.7	34.7	42.0	50.4	47.9
External debt stocks, short-term (DOD, current; \$, billions)	0.6	0.7	1.0	1.1	1.2	1.0	0.8	0.7	0.9
Fiscal balance	-3.0	-2.1	0.6	-0.9	-0.1	-2.0	-9.0	-6.0	-4.8
Primary balance	-2.5	-1.6	1.1	0.1	0.4	-1.5	-8.3	-5.5	-3.5
Government revenue-to-gross debt	0.63	0.71	0.78	0.93	1.03	0.86	0.71	0.59	0.56
Financial									
Nonperforming loans to total loans	7.4	7.2	9.5	15.9	25.0	29.9	54.0	...	...
Capital to risk-weighted assets	27.1	24.4	25.9	22.1	14.7	11.1	15.1	19.5	...
Tier I capital to risk-weighted assets	23.7	21.2	23.3	20.2	12.0	8.3	26.4	28.5	...
Returns on assets	1.2	0.2	0.8	1.5	-3.7	0.4	-3.2	-0.4	...
Liquid asset to total assets	26.0	24.5	30.0	30.0	21.5	25.0	32.4	29.6	...
Liquid assets to short-term liabilities	62.5	65.1	83.7	79.7	71.4	65.7	80.5	75.8	...
Short-term debt (% of total reserves)	149.1	140.9	157.6	170.8	227.2	194.7	126.2	57.7	68.0

Source: IMF 2019b; IMF Financial Soundness Indicators (database); World Bank Open Data (<https://data.worldbank.org>).

Table B.7. Key Fiscal and Financial Sector Indicators for Ukraine (percentage of gross domestic product, unless otherwise indicated)

Indicator	2010	2011	2012	2013	2014	2015	2016	2017	2018
Fiscal									
Gross government debt	40.6	36.9	37.5	40.5	70.3	79.5	81.2	71.9	63.9
External debt stocks, short-term (DOD, current; \$, billions)	27.3	32.7	34.8	34.8	22.7	20.0	20.2	22.3	20.7
Fiscal balance	-5.8	-2.8	-4.3	-4.8	-4.5	-1.2	-2.2	-2.2	-2.3
Primary balance	-4.1	-0.8	-2.4	-2.3	-1.2	3.0	1.9	1.6	1.2
Government revenue-to-gross debt	1.1	1.2	1.2	1.1	0.6	0.5	0.5	0.5	0.7
Financial									
Nonperforming loans to total loans	15.3	14.7	16.5	12.9	19.0	38.0	30.5	54.5	52.9
Capital to risk-weighted assets	20.8	18.9	18.1	18.3	15.6	12.3	12.7	16.1	16.2
Tier I capital to risk-weighted assets	15.1	14.0	13.8	13.9	11.2	8.3	9.0	12.1	10.5
Returns on assets	-1.5	-0.7	0.5	0.3	-4.2	-5.5	-12.5	-1.8	1.6
Liquid asset to total assets	18.8	18.7	22.2	20.6	26.4	33.0	48.5	53.9	51.1
Liquid assets to short-term liabilities	91.2	94.7	90.3	89.1	86.1	92.9	92.1	98.4	93.5
Short-term debt (% of total reserves)	78.9	103	141.5	170.6	301.0	150.5	130.2	118.3	99.4

Source: IMF 2017, 2019b; IMF Financial Soundness Indicators (database); World Bank Open Data (<https://data.worldbank.org>).

Table B.8. Coherence between World Bank Group Responses to Identified Vulnerabilities

Country	Key Vulnerability	Intervening Contextual Factors	Response Instruments, Products, and Processes	Degree of Coherence
Bangladesh	<p>Fiscal risks from SOEs and contingent liabilities from the energy sector</p> <p>Financial vulnerabilities from SOBs and undeveloped and uncompetitive capital markets</p>	<p>Moderate ownership</p> <p>Limited impact of the global financial crisis undermined client government sense of urgency for crisis preparedness</p>	<p>Fiscal: Policy lending was halted by the World Bank during much of the review period (2013–18), and project lending focused more on institutional and capacity-building aspects of the country's fiscal vulnerabilities and less on fundamental fiscal reforms. Programmatic policy-based lending resumed in 2018–19 but focused less on financial vulnerabilities.</p> <p>Financial: Technical assistance on financial sector reforms (P130030) (2012) focused on SOBs; 2013 Anti-money laundering and combating terrorism financing technical assistance; 2015 Financial Sector Support Project (P150938) to improve financial market infrastructure, regulatory, and oversight capacity and long-term finance; a project for the Modernization of State-Owned Financial Institutions (P155363); IFC engagement was more limited: investments in seven banks and advisory services to three banks focused on raising corporate standards and improving governance and risk management.</p> <p>Social safety net: to be added.</p>	Moderate

(continued)

Country	Key Vulnerability	Intervening Contextual Factors	Response Instruments, Products, and Processes	Degree of Coherence
Benin	<p>High public debt</p> <p>Low domestic revenue mobilization</p> <p>High NPL and concentration in the banking system</p> <p>Almost nonexistent SSN at the beginning of the period</p>	<p>Moderate ownership</p> <p>Extreme dependence of the economy on informal trade with Nigeria</p>	<p>Fiscal: Policy-based guarantee used to retire expensive debt and reduce interest payments and increase fiscal space.</p> <p>Financial: Limited engagement with regional monetary authority.</p> <p>Social safety net: Very large World Bank response with series of projects to establish SSN where there was none. This began under project PNDCC, which closed a few years ago. A project that followed it—PSDCC—which consisted of a pilot SSN program and capacity building for SSN systems. This program had featured cash transfers in two parts. The first was unconditional. The second was a transfer related to the public works program. The World Bank helped the government in building the first social registry, with 200,000 households. Households were also mapped across space and linked to potential threats (for example, river flooding). Project ACCESS to scale up cash transfer project and further build the social registry so that by the end of the project there would be a national and complete social registry. Finally, CAT DDO is under preparation and has an SSN pillar.</p>	Moderate

(continued)

Country	Key Vulnerability	Intervening Contextual Factors	Response Instruments, Products, and Processes	Degree of Coherence
Jamaica	<p>Very high and unsustainable debt</p> <p>Lack of fiscal space</p> <p>Banking system concentration and ownership of sovereign debt</p> <p>Low access to finance at the beginning of the evaluation period, but significant improvement at the end</p>	<p>High ownership</p> <p>High social/stakeholder consensus of fiscal and financial reforms</p> <p>Debt crisis in 2012/early 2013 threatening sovereign default</p> <p>Large and frequent natural disaster shocks</p>	<p>Fiscal: Three DPLs (2013, 2015, 2017) focusing on strengthening fiscal management, PFM, and investment climate reforms; complementary technical assistance.</p> <p>Financial: Access to finance DPL focused on the reduced incentive for banks to diversify lending to the private sector, inadequate credit reporting system, information asymmetries in the market, and the high level of informality that raises risks for banks.</p>	High
Morocco	<p>Weaknesses in public sector governance and transparency</p> <p>Commercial bank oversight and regulation</p> <p>Exposure to foreign markets</p>	<p>High ownership</p> <p>Political and macro-economic stability</p>	<p>Fiscal: Two-operation DPL series (Hakama) focusing on governance and transparency that underpin fiscal and financial sector vulnerabilities.</p> <p>Social safety net: The World Bank had a large program focusing on supporting government in developing a system of ID cards and the targeting of subsidies. It was coordinated with a reduction of fuel subsidies to which the World Bank contributed.</p>	High

(continued)

Country	Key Vulnerability	Intervening Contextual Factors	Response Instruments, Products, and Processes	Degree of Coherence
Mozambique	<p>Unsustainable debt</p> <p>Hidden debt</p> <p>Data transparency</p> <p>Capacity for debt management</p> <p>Data transparency</p> <p>Domestic revenue mobilization</p> <p>Supervision and regulation</p> <p>Bank resolution framework</p> <p>Fragmented safety net with small and poorly targeted programs; it had low coverage and low levels of benefits</p>	<p>Low institutional capacity and ownership</p>	<p>Fiscal: Poverty Reduction Support Credits 9-10-11 series targeted debt management, PFM vulnerabilities, and social protection, and a Public Sector Reform project focused on capacity building for PFM. National Statistics and Data for Development project responded to DeMPA (2017).</p> <p>Financial: Technical assistance to the central bank on bank resolution frameworks. Financial Sector Technical Assistance Project (2011/12). Financial sector DPLs 1-2 supported the establishment and capitalization of a deposit guarantee fund and selectively expanded its bank resolution mandate. IFC advised on an assessment of bank assets and standards.</p> <p>SSN: Based on a prior diagnostic, a Rapid Social Response Trust Fund was mobilized to pilot a public works program and an operational platform for SSN programs, which informed the design and implementation of the Social Protection Project.</p>	<p>High</p>

(continued)

Country	Key Vulnerability	Intervening		Degree of Coherence
		Contextual Factors	Response Instruments, Products, and Processes	
Tajikistan	<p>High dependence of liquidity to remittances from the Russian Federation</p> <p>SOBs</p> <p>Energy subsidies</p> <p>Domestic revenue mobilization</p> <p>Supervision and regulation</p> <p>NPLs</p>	Low ownership	<p>Fiscal: Response limited to analytics. DPL series that was being prepared in 2016 was dropped due to governance issues.</p> <p>Financial: FIRST Initiative has been used to finance needed follow-up technical assistance. Support NBT efforts to strengthen financial stability monitoring and response mechanisms, so that it can respond promptly and appropriately to early indications that risk is building up. The technical assistance will provide support to the NBT in deploying stress test models and macroprudential instruments. IFC has been supporting the NBT on on-cash, mobile, and new financial instruments. The World Bank and IFC provide support on consumer protection and financial literacy.</p> <p>SSN: An SSN project is focused on enhancing access to electricity where the government is not doing enough.</p>	Low/Moderate

(continued)

Country	Key Vulnerability	Intervening		Degree of Coherence
		Contextual Factors	Response Instruments, Products, and Processes	
Ukraine	Debt management capacity Energy subsidies Supervision and regulation of commercial banks Bank resolution frameworks NPLs Corruption and connected lending	High ownership after 2014 currency and banking crisis	Fiscal: Two DPL series supporting fiscal consolidation through the reform of energy subsidies. Technical assistance on capital budgeting. Three loans were in the energy sector and included attention to tariff and subsidy reforms. Financial: Menu of World Bank DPLs, IP, extensive technical assistance to the central banks, and a deposit guarantee fund. Policy-based guarantee focused on financial sector vulnerabilities. IFC advisory and projects in the financial sector including investment climate for agribusiness project targeting improvements in regulations. SSN: Two SSN loans.	High

Note: CAT DDO = catastrophe deferred draw down option; DeMPA = Debt Management Performance Assessment; DPL = development policy loan; IFC = International Finance Corporation; IP = Investment Project; NBT = National Bank of Tajikistan; NPL = nonperforming loan; PFM = public financial management; SOB = state-owned bank; SOE = state-owned enterprise; SSN = social safety net.

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Appendix C. Identification and Assessment of Fiscal and Financial Sector Vulnerabilities (2010–15 and 2016–18)

Table C.1. Identification and Assessment of Fiscal Vulnerabilities in World Bank Diagnostics in Case Study Countries, 2010–15

Country	Main Fiscal Vulnerabilities Identified	Assessment
Bangladesh	<p>Low tax revenues to GDP ratio</p> <p>Moderate fiscal deficits</p> <p>Moderate but rising contingent liabilities at SOEs</p> <p>Moderate but rising subsidies to SOEs with losses</p> <p>Capital injections into weak publicly owned commercial banks with rising NPLs</p>	<p>World Bank Group staff were aware of the fiscal vulnerabilities and flagged most of the main fiscal vulnerabilities in a timely manner through PERs (2010, 2015); a CEM (2012); and Development Updates. The 2010 assessment was particularly forthright. Fiscal risks associated with implicit contingent liabilities of SOEs did not receive the same level of attention. The 2015 PER update acknowledged that risks could be particularly large if several are realized together and the government is not able to issue sufficient debt to cover payments. The PER recommended that the government evaluate fiscal risks posed by contingent liabilities—including from pensions and SOEs—and take steps to mitigate them.</p>

(continued)

Country	Main Fiscal Vulnerabilities Identified	Assessment
Benin	<p>Rising public debt (largely from regional financial institutions) and high debt service</p> <p>Low domestic revenue mobilization</p> <p>Disproportionate dependence on Nigerian economy and the impact of Nigeria's restrictive trade policies on government expenditures</p> <p>Excessive reliance on donor financing of the budget</p> <p>Economic concentration arising from elite capture and an oligarchic structure to narrow the tax base, leaving many informal activities outside the tax net</p>	<p>The World Bank consistently identified the right fiscal vulnerability diagnostics, such as the 2009 CEM and 2012 PER, a DeMPA (2011), and policy notes on expenditures (2014) and financial management (2014). The DSA appropriately indicated moderate risk of external debt distress. However, it insufficiently captured an extreme risk scenario that would result in a significant drop in economic activity, as happened in 2019 after the closure of the border with Nigeria.</p>
Jamaica	<p>Very large and unsustainable public debt</p> <p>Limited fiscal space</p> <p>Public pension liabilities</p> <p>Weaknesses in PFM</p>	<p>The World Bank identified the right fiscal vulnerabilities in a timely manner in a CEM (2011) and a subsequent PER, which devoted substantial attention to the analysis of fiscal and debt issues and to outlining the necessary fiscal consolidation agenda. This diagnostic work and associated policy dialogue were carried out in close collaboration with the IMF and the IDB, which took the lead on tax policy issues, while the World Bank focused on pensions and PFM issues.</p>
Morocco	<p>Limited fiscal space due to large gasoline subsidies</p> <p>Fiscal transparency</p> <p>Overly centralized and outdated budget management</p>	<p>The World Bank correctly identified these vulnerabilities in the context of sectoral development policy lending dialogue, but its focus on macro vulnerabilities was not comprehensive and was often left to the IMF. As a result, some areas were missed. More could have been done to develop a stronger pipeline of analytical work focusing on vulnerabilities arising from low expenditure efficiency, especially social expenditures, and domestic revenue mobilization, where there were issues with tax incentives.</p>

(continued)

Country	Main Fiscal Vulnerabilities	
	Identified	Assessment
Mozambique	<p>High fiscal deficits with arrears accumulation</p> <p>Unsustainable and high external debt stock</p> <p>Potential "hidden debt"</p> <p>Budget rigidities</p> <p>Inadequate data transparency</p>	<p>The World Bank identified each of these key vulnerabilities correctly and in a timely manner (CEM 2012 and 2014 PER), including the hidden debt in a DeMPA (2008), many years before it became a problem in 2016. However, governance issues and difficult policy dialogue limited follow-up, World Bank response, and effectiveness. Vulnerabilities related to budget rigidities due to the high cost of debt service and the public sector wage bill persist.</p>
Tajikistan	<p>High dependence of the economy and the budget on revenues from remittances, which reached 48% of GDP in 2013</p> <p>Potential fiscal costs of bank lending to SOEs</p> <p>Management of public investment projects</p> <p>Weaknesses in debt management</p>	<p>The World Bank correctly identified these major sources of vulnerabilities in the 2011 CEM, the 2015 DeMPA, and economic updates. However, engagement in diagnostics was not systematic. Several fiscal vulnerabilities could have been highlighted more, including the quality and transparency of fiscal and quasi-fiscal data. Also, the 2013 DSA assumed a very optimistic growth path for remittances (9% per year) and did not explore the possibility of an extreme drop in remittances, which occurred the next year when remittances fell from more than 40% to 20% of GDP.</p>
Ukraine	<p>Large and unsustainable energy subsidies</p> <p>Lack of expenditure controls</p> <p>Escalating fiscal costs of the banking crisis and large contingent liabilities among SOEs</p> <p>External financing conditions</p> <p>Budget transparency</p>	<p>The World Bank identified the right vulnerabilities in its 2010 CEM, warning of the looming fiscal and debt crisis, which materialized in 2014. The Public Expenditure and Financial Accountability Review (2011) also correctly identified several weaknesses in the budget process, transparency, audits, and the public investment decision-making process. However, fiscal policy dialogue was stymied by vested interests, which significantly influenced policy.</p>

Source: Independent Evaluation Group.

Note: CEM = Country Economic Memorandum; DeMPA = Debt Management Performance Assessment; DSA = Debt Sustainability Analysis; GDP = gross domestic product; IDB = Inter-American Development Bank; IMF = International Monetary Fund; NPL = nonperforming loan; PER = Public Expenditure Review; PFM = public financial management; SOE = state-owned enterprise.

Table C.2. Identification and Assessment of Fiscal Vulnerabilities in World Bank Diagnostics in Case Study Countries, 2016–19

Country	Main Fiscal Vulnerabilities Identified	Assessment
Bangladesh	<p>Major weaknesses in debt management</p> <p>Rising energy costs and other subsidies</p> <p>A number of mega infrastructure projects, some with PPP arrangements and nonconcessional financing</p>	<p>Reflecting a difficult relationship with the government, the World Bank was muted in its concerns about the cumulative impact of subsidies, pensions, and rapidly mounting implicit and explicit contingent liabilities. The overall assessment of the macroeconomic framework and the soundness of the fiscal policy in published documents left the impression that the fundamentals were sounder than was actually the case. Although SOCBs are consistently cited as a fiscal vulnerability that could affect fiscal sustainability, the MPO made only one mention of possible fiscal implications of SOEs (spring 2017 MPO, which notes that "reforming SOEs could lessen strains on the budget") and made no mention of potential implicit contingent liabilities from private banks (despite weaknesses in banking supervision) as central bank independence was "substantially eroded" (fall 2018 MPO). Fiscal risks associated with implicit contingent liabilities of SOEs increased substantially due to mega projects, which failed to receive much attention. The 2019 DSA indicates that "favorable debt dynamics" will keep PPG external debt on a declining path. But DSA simulations did not include risks arising from implicit liabilities or concerns with overstated GDP and are based on optimistic growth projections. The 2019 MPO describes macroeconomic fundamentals as "strong," despite downside risks, which include "financial sector vulnerability, reform reversals, fiscal pressures, and a loss of competitiveness."</p>
Benin	<p>Continued high public debt and debt service</p> <p>Low domestic revenue mobilization</p> <p>Excessive dependence on the Nigerian economy, which escalated into a temporary closure of the border</p>	<p>The World Bank continued to monitor and identify the right vulnerabilities, all of which carried over from the previous period and some of which intensified (for example, disruption to the large informal trade with Nigeria). Policy notes (2016) and SCDs (2017) provided a comprehensive synthesis of main development issues, including fiscal vulnerabilities.</p>

(continued)

Country	Main Fiscal Vulnerabilities	
	Identified	Assessment
Jamaica	<p>Large albeit substantially reduced public debt</p> <p>Improving fiscal space</p> <p>Remaining weaknesses in PFM</p>	<p>The World Bank remained abreast and continued to identify and monitor fiscal vulnerabilities during an intensive policy dialogue and monitoring in the context of three DOF operations in close coordination with the IMF and IDB.</p>
Morocco	<p>Continued issues in fiscal transparency and citizen participation in the budget process</p> <p>Contingent liabilities from public sector entities</p> <p>Rising, albeit moderate, public debt and vulnerability of debt to shocks</p>	<p>The World Bank continued to identify and monitor fiscal vulnerabilities, mainly in the context of a series of two development policy financing operations focused on public sector governance and PFM. An IMF/World Bank DSA indicated that debt is sustainable under assumptions of various interest rate, growth, and other external shocks. However, investment and natural shocks were not taken into account, although these risks were recognized as important. These latter risks are considered latent risks, which is part of a different analysis and not part of the DSA. The World Bank Treasury Department also helped the Ministry of Finance identify various debt scenarios in response to interest rates and exchange rate shocks. Finally, a CEM, Morocco 2040 (2017), appropriately put Morocco's vulnerabilities in a broader context of economic and social fabric, suggesting the need to change the development model.</p>
Mozambique	<p>High fiscal deficits with arrears accumulation</p> <p>Unsustainable and high external debt and SOE debt</p> <p>Reduced official external financing due to hidden debt, strong budget rigidities, and inadequate data transparency</p>	<p>The World Bank identified the right vulnerabilities, including in the 2016 SCD and DeMPA, as well as in annual economic updates and in policy dialogue in concert with the IMF.</p>
Tajikistan	<p>Significant annual budgetary costs of the Rogun dam</p> <p>Significant increase in external debt</p> <p>Limited fiscal space</p> <p>Fiscal cost of bank recapitalization</p> <p>Fiscal risks of frequent natural disasters</p> <p>Risk of fiscal implications of rising corporate debt</p>	<p>The World Bank has correctly identified these risks, including in the 2018 SCD. The 2018 DSA has correctly classified the risk of external debt distress as high. However, greater emphasis could have been placed on the low quality of data and fiscal and quasi-fiscal transparency. This undermines confidence in the assessments of debt and fiscal risks generally.</p>

(continued)

Country	Main Fiscal Vulnerabilities	
	Identified	Assessment
Ukraine	High energy subsidies Lack of fiscal space Rigid social expenditures Inefficient tax system and tax administration	Starting in 2014, the World Bank stepped up its analytical engagement. The World Bank identified the right vulnerabilities in its Programmatic Public Finance Reviews in 2017 and 2018; in the intensive technical assistance policy dialogue on the Gas and Heating Tariff Reform (2015); and in the Social Safety Net and Energy Reform (2017).

Source: Independent Evaluation Group.

Note: DeMPA = Debt Management Performance Assessment; DSA = Debt Sustainability Analysis; IDB = Inter-American Development Bank; IMF = International Monetary Fund; MPO = Macro Poverty Outlook; PFM = public financial management; PPG = public and publicly guaranteed; PPP = public-private partnership; SCD = Systematic Country Diagnostic; SOCB = state-owned commercial bank; SOE = state-owned enterprise.

Table C.3. Identification and Assessment of Financial Vulnerabilities in World Bank Diagnostics in Case Study Countries, 2010–15

Country	Main Financial Vulnerabilities	
	Identified	Assessment
Bangladesh	SOCBs were undercapitalized and unprofitable with significant connected lending SOCB risks were systemically significant The performance of private commercial banks began to deteriorate in the face of weak supervision Integrity of the financial sector in Bangladesh has been compromised by banking sector loan scams and embezzlements, and weaknesses in regulatory and supervisory frameworks	The World Bank Group had clear and detailed knowledge of the financial sector vulnerabilities in Bangladesh and a well-prioritized view of how the issues needed to be addressed. Staff conveyed a clear and consistent message with respect to significant and increasing financial sector vulnerabilities. Staff recommended bringing all banks, including SOCBs, under Bangladesh Central Bank's supervision and installing professional management in the banks.

(continued)

Country	Main Financial Vulnerabilities	
	Identified	Assessment
Benin	<p>High concentration of bank loans in a small number of systemic private and public sector enterprises that were closely related to trade with Nigeria</p> <p>High regional bank exposure to several state levels</p> <p>Persistently high number of NPLs</p> <p>Inadequate implementation of regulations to formalize and ensure adherence to rules governing microfinance institutions</p>	<p>The World Bank rightly identified financial sector vulnerabilities in financial sector reviews that preceded the review period (2007) The 2011 microfinance Ponzi scheme, however, moved the spotlight of World Bank diagnostics and dialogues to microfinance and inclusion. However, there was no FSAP or systematic monitoring or follow-up in the policy dialogue. Instead, Bank Group efforts focused on the risk posed by the weak private sector in Benin and on microfinance issues. More comprehensive diagnostics, such as FSAP, with associated monitoring and dialogue, were missing.</p>
Jamaica	<p>Heavy exposure to sovereign risk</p> <p>Vulnerability to rollover and interest rate risks on public debt</p> <p>Large numbers of NPLs</p> <p>Low competition and heavy concentration in lending to households and larger corporations and evidence of market segmentation</p>	<p>The World Bank identified sovereign risks early in the 2011 CEM and subsequent PER. These were aimed at lowering credit risks and NPLs and improved capital adequacy. The Bank Group also identified other risks and assisted with the Banking Services Act, amendments to the Bank of Jamaica Act, and upgrades to the regulatory and supervisory framework and risk management by banks.</p>
Morocco	<p>Weak supervisory framework</p> <p>Concentration and competition in banking</p> <p>Inadequate crisis preparation procedures at banks</p>	<p>The Bank Group identified these vulnerabilities correctly, and it advised the central bank for credit institutions to develop annual crisis preparation plans. Bank Group support was instrumental in identifying vulnerabilities in the financial sector and in helping alleviate resistance to reforms by the stakeholders. However, the World Bank did not sufficiently emphasize in its dialogue the issues of concentration and competition among banks or the ease of entry into the market.</p>

(continued)

Country	Main Financial Vulnerabilities	
	Identified	Assessment
Mozambique	<p>High numbers of NPLs and banks' exposure to the government and SOEs</p> <p>Limited financial safety nets: weak resolution framework and deposit insurance scheme</p> <p>Small and highly concentrated insurance sector</p>	<p>The World Bank and the IMF prepared joint FSAP in 2009, which has helped Mozambique in identifying macrofinancial vulnerabilities that were relevant and timely to the needs of the country.</p>
Tajikistan	<p>Inefficient intermediation and financial infrastructure</p> <p>High bank concentration</p> <p>Two-thirds of deposits being short term and denominated in foreign currency</p> <p>A rapid rise in NPLs</p> <p>High dependence on remittances from the Russian Federation to maintain bank liquidity</p>	<p>The Bank Group correctly identified key vulnerabilities and had a good and timely understanding of financial sector vulnerabilities. The Bank Group conveyed its understanding of vulnerabilities to the authorities through advisory and analytics work and technical assistance and supported the country with project lending to the financial sector.</p>
Ukraine	<p>Weak regulation and supervision</p> <p>Low capital adequacy and high numbers of NPLs</p> <p>Inadequate bank resolution and restructuring framework for state-owned banks</p> <p>Low bank data transparency and quality of bank governance</p> <p>Currency and maturity risks in a highly dollarized economy</p> <p>Severe underprovisioning for potential problem loans</p> <p>Weak financial stability architecture</p>	<p>These were the right vulnerabilities, which were clearly identified in the 2010 CEM, along with a recommended reform agenda. The World Bank had a good understanding of banking sector challenges and the role that corruption played in the low quality of banks' governance and performance. One area that deserved attention was a nascent insurance sector, which entirely escaped regulatory attention.</p>

Source: Independent Evaluation Group.

Note: CEM = Country Economic Memorandum; FSAP = Financial Sector Assessment Program; IMF = International Monetary Fund; NPL = nonperforming loan; PER = Public Expenditure Review; SOCB = state-owned commercial bank; SOCE = state-owned enterprise.

Table C.4. Identification and Assessment of Financial Vulnerabilities in World Bank Diagnostics in Case Study Countries, 2016–18

Country	Main Financial Vulnerabilities Identified	Assessment
Bangladesh	<p>NPLs in the banking system were described in 2016 as a “major concern” Heightened risk from policy changes that eroded bank supervisory independence and allowed defaulters to reschedule loans on easy terms while leaving loan classification standards</p>	<p>The World Bank Group correctly identified these vulnerabilities, and MPOs between spring 2016 and December 2019 raised increasing concern about financial sector vulnerabilities, regularly noting that financial sector weaknesses have the potential to derail investment and growth as weak governance in the banking sector limits lending capacity, diverts credit away from productive investment, and imposes large recapitalization costs.</p>
Benin	<p>Continued high concentration of bank loans in a handful of enterprises, which are also exposed to trade with Nigeria Large numbers of NPLs Inadequate regulation and enforcement of microfinance institution</p>	<p>The World Bank had a broad understanding of the financial sector vulnerabilities, and the 2018 financial sector review highlighted these issues, in particular those related to regulation of microfinance institutions. However, microfinance institutions account for only 10 percent of assets. A broader and deeper diagnostic such as an FSAP, with deeper treatment of banking sector issues that account for 90 percent of financial sector, was missing.</p>

(continued)

Country	Main Financial Vulnerabilities	
	Identified	Assessment
Jamaica	<p>Continued exposure to sovereign risk and rising credit to the private sector</p> <p>Significant counterparty exposures in the financial sector owing to the complex financial conglomerates that operate in multiple jurisdictions with different oversight practices</p> <p>The concentrated ownership structure of the financial sector, related-party and large group exposures, and large off-balance sheet positions</p> <p>A weak bank resolution framework that could hinder effective crisis resolution because of the lack of a resolution authority and the absence of an appropriate insolvency law</p>	<p>The Bank Group stressed that as banks reduce their sovereign exposure and seek new opportunities for lending and investment, it had become urgent for the central bank to improve its supervisory vigilance and enhance its ability to detect and control excessive risk taking. The Bank Group assisted with the preparation of proposed legislation to make the central bank the resolution authority with the appropriate level of independence and to introduce a modified insolvency framework to cover the entire financial sector under a single law.</p>
Morocco	<p>Cross-border exposure</p> <p>Three major banks amount to 20–30% of total assets and a third of profits</p> <p>Large credit concentration and competition in banking</p> <p>The ownership structure in banking industry is not conducive to a level playing field in the banking market and can lead to supervisory capture and collusion</p> <p>Inadequate bank resolution procedures</p>	<p>Overall, the World Bank identified key risks but did not always consider extreme risk scenarios. The FSAP stress tested exposure and found this risk limited, but it did not consider the extreme shock of a drop of GDP by 6% (as had happened in the 1990s), which the client considered unrealistic. Also, FSSA stress tests showed that default by the three largest corporate clients of any of the largest eight banks could lead to the commercial banks' undercapitalization. Under a World Bank technical assistance project that began in 2016, the country's bank resolution framework was upgraded, but more work is needed.</p>

(continued)

Country	Main Financial Vulnerabilities	
	Identified	Assessment
Mozambique	Continued high NPLs and banks' exposure to the government and SOEs Weak resolution framework and deposit insurance scheme Small and highly concentrated insurance sector	The World Bank diagnostic has not changed fundamentally from the previous period, still focusing on the right vulnerabilities, which were exacerbated by the broader economic and debt crisis in this period. Monitoring and dialogue continued in relation to programmatic financial sector DPOs. The 2016 SCD, however, did not look at financial sector stability and vulnerability issues, instead focusing on access to credit only.
Tajikistan	Low public confidence in the banking system reflected in a decline in total bank deposits to only 15% of GDP Seventy percent of deposits in short term and denominated in foreign currency with attendant currency and interest risks Directed lending and NPLs Contingent liabilities from the banking sector arising from governance of the banks	The Bank Group continued to have a good understanding of financial sector vulnerabilities through its advisory services and analytics work (FSAP 2015/16; SCD 2018; CEM 2018/19). The World Bank and IFC teams (together with the IMF in the FSAP) correctly identified major weaknesses in the financial and banking sector in a timely manner. Through its extensive technical assistance and analytical work for the banking and financial sector, the Bank Group succeeded in increasing awareness of the major vulnerabilities and their channels of transmission, and in increasing the technical and operational capacity of the central bank. Governance issues and the lack of political will led to a further increase in Tajikistan's financial vulnerabilities.
Ukraine	Corruption and vested interests that were behind related-party lending Weaknesses in supervision Poor corporate governance in state-owned banks	The Bank Group identified the right vulnerabilities in the SCD and in the intensive financial sector policy dialogue, just-in-time notes, and technical assistance and financial assessments. There was a clear prioritization of risks. Vested interests in the parliament, however, stymied progress in addressing vulnerabilities. There was also a lack of public understanding of the overarching strategy and motivation for financial sector actions supported by the World Bank. Greater attention could have been paid to the insurance sector, which remained poorly monitored and regulated.

Source: Independent Evaluation Group.

Note: CEM = Country Economic Memorandum; DPO = development policy operation; FSAP = Financial Sector Assessment Program; FSSA = Financial Sector Stability Assessment; GDP = gross domestic product; IFC = International Finance Corporation; IMF = International Monetary Fund; MPO = Macro Poverty Outlook; NPL = nonperforming loan; SCD = Systematic Country Diagnostic; SOE = state-owned enterprise.

Appendix D. Comparative Fiscal and Financial Vulnerability Indicators in Case Study Countries

Table D.1. Comparative Fiscal and Financial Vulnerability Indicators in Case Study Countries, 2010–18 (percentage of gross domestic product, unless otherwise indicated)

Fiscal Indicators	2010	2011	2012	2013	2014	2015	2016	2017	2018
Gross government debt	35.5	36.6	36.2	35.8	35.3	33.7	33.3	32.5	34.8
Bangladesh									
Benin	28.7	29.9	26.7	25.3	30.5	42.4	49.7	54.4	54.6
Jamaica	143.2	141.7	145.0	140.5	139.7	121.3	121.7	109.4	101.1
Mozambique	43.3	38.0	40.1	53.1	62.4	88.1	121.6	103.2	100.4
Morocco	49.0	52.5	56.5	61.7	63.3	63.7	64.9	65.1	65.2
Tajikistan	36.6	35.3	32.3	29.1	27.7	34.7	42.0	50.4	47.9
Ukraine	40.6	36.9	37.5	40.5	70.3	79.5	81.2	71.9	63.9
Primary fiscal balance									
Bangladesh	-0.8	-1.9	-1.1	-1.4	-1.0	-1.9	-1.5	-1.6	-1.7
Benin	0.1	-0.9	0.3	-1.4	-1.9	-6.9	-4.7	-3.8	-2.5
Jamaica	4.6	3.2	5.4	7.6	7.5	7.2	7.6	7.5	7.5
Mozambique	-3.1	-3.9	-2.9	-1.9	-9.6	-5.9	-3.3	0.0	-1.5
Morocco	-2.0	-4.4	-4.7	-2.5	-2.1	-1.4	-1.8	-0.9	-1.3
Tajikistan	-2.5	-1.6	1.1	0.1	0.4	-1.5	-8.3	-5.5	-3.5
Ukraine	-4.1	-0.8	-2.4	-2.3	-1.2	3.0	1.9	1.6	1.2
Government revenue-to-gross debt									
Bangladesh	28.0	28.0	31.0	31.0	31.0	29.0	30.0	31.0	29.0
Benin	66.0	63.0	72.0	73.0	56.0	41.0	31.0	34.0	34.0
Jamaica	19.0	18.0	18.0	19.0	19.0	22.0	25.0	29.0	32.0
Mozambique	60.0	72.0	67.0	59.0	51.0	32.0	22.0	27.0	26.0
Morocco	55.0	52.0	50.0	45.0	44.0	42.0	40.0	41.0	40.0
Tajikistan	63.0	71.0	78.0	93.0	102.0	86.0	71.0	59.0	56.0
Ukraine	107.0	116.0	119.0	107.0	57.0	53.0	47.0	55.0	65.0

Fiscal Indicators	2010	2011	2012	2013	2014	2015	2016	2017	2018
Nonperforming loans to total loans									
Bangladesh	7.3	6.1	10.0	8.9	10.0	8.8	9.2	9.3	10.3
Benin	15.8	15.6	18.6	21.2	21.5	22.1	21.8	19.4	21.6
Jamaica	6.5	8.9	7.0	5.4	5.0	4.1	3.5	3.5	...
Mozambique	1.9	2.6	3.2	2.3	3.2	4.3	5.7	12.6	11.1
Morocco	4.8	4.8	5.0	5.9	6.9	6.8	7.1	7.0	6.8
Tajikistan	7.4	7.2	9.5	15.9	25.0	29.9	54.0	...	...
Ukraine	15.3	14.7	16.5	12.9	19.0	38.0	30.5	54.5	52.9
Capital to risk-weighted assets									
Bangladesh	9.3	11.4	10.5	11.5	11.3	10.8	10.8	10.8	10.5
Benin	10.0	12.5	9.2	9.5	9.0	7.9	9.3	11.9	8.2
Jamaica	18.2	16.1	14.1	15.1	15.9	14.9	14.5	14.5	...
Mozambique	14.4	17.1	17.9	16.9	15.1	17.0	8.8	21.5	23.8
Morocco	12.3	11.7	12.3	13.3	13.8	13.7	14.2	13.8	14.0
Tajikistan	27.1	24.4	25.9	22.1	14.7	11.1	15.1	19.5	...
Ukraine	20.8	18.9	18.1	18.3	15.6	12.3	12.7	16.1	16.2

Source: IMF 2019a, 2019b.

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Appendix E. Making Social Safety Nets Adaptable to Crises

Table E.1. Assessment of Social Safety Net Adaptability—Country Typology

Crisis Preparedness	Delivery Systems		
	Policy Level	Level	Programs Level
Strong (Jamaica)	<p>Strong government leadership</p> <p>Overall SP strategy and clear institutional setup x policy formulation, oversight, delivery systems management, and program implementation</p> <p>Appropriate program mix of key country risks and vulnerabilities</p> <p>Good capacity and current data x social impacts and SP readiness assessments</p> <p>Contingency plans x crisis response with coordinated programs and institutions</p> <p>Financing plans and options x fast countercyclical response</p>	<p>Wide coverage of integrated platforms to support key functions across programs such as social registry, grievance and redress, and payment systems</p> <p>On-demand registration</p> <p>Well-developed IT systems enabling good information flows and process automation; further systems' integration and interoperability efforts in progress</p>	<p>Well-established, appropriate programs with large coverage, and progressive targeting</p> <p>Adequate level of benefits and duration of support</p> <p>Sound program administration systems^a</p> <p>Design and implementation flexibility x temporary program expansion and scaling down after crisis</p>

(continued)

Crisis Preparedness	Delivery Systems		
	Policy Level	Level	Programs Level
Moderate (Bangladesh, Morocco, Ukraine)	<p>Variable government leadership</p> <p>Overall SP strategy and clear institutional setup for key functions, but limited capacity or systematic coordination and implementation</p> <p>Fair program mix of key country risks and vulnerabilities</p> <p>Capacity x social impacts and SP readiness assessments limited by outdated information</p> <p>Limited or partial contingency planning and financing options x fast crisis response</p>	<p>Limited coverage but expanding integrated platforms x key functions such as social registry and payments systems across more than one program</p> <p>Limitations for dynamic targeting, mainly a mass registration approach</p> <p>IT architecture and systems under development and moving to integrate; parallel systems remain in some programs</p>	<p>Have one or more progressively targeted programs to build on, but without expansive coverage</p> <p>Low level of benefits or duration of support</p> <p>Most program administration systems need improvement</p> <p>Moderate to low program flexibility and capacity x temporary expansion and scale down</p>
Nascent (Benin, Mozambique, Tajikistan)	<p>Limited government leadership, strong donor influence, weak coordination</p> <p>Country may have an SP strategy, but institutional capacity and financing constraints hinder implementation</p> <p>Inadequate program mix of key country risks and vulnerabilities</p> <p>Low capacity and lack of data x social impacts and SP readiness assessments</p> <p>No contingency planning and financing options x crisis response</p>	<p>Building one or more flagship programs including key building blocks of SP system: beneficiary or social registry and payments system</p> <p>Mass registration approach</p> <p>Static targeting, very limited capacity to quickly expand registration</p>	<p>Large-scale response calls x fundamental changes to range, size, and targeting of programs</p> <p>Negligible level and duration of benefits</p> <p>Need large-scale capacity building to develop necessary administration systems</p>

Source: Independent Evaluation Group. Developed from Bastagli 2014; Grosh et al. 2011; Marzo and Mori 2012; McCord 2013; Oxford Policy Management (2015–2018); and this evaluation's case studies.

Note: a. These include outreach; eligibility criteria; payment systems; MIS for program operations and fiduciary compliance; grievance and redress; monitoring and evaluation; and a communications strategy (Grosh et al. 2011).

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The World Bank
1818 H Street NW
Washington, DC 20433