

**PROJECT INFORMATION DOCUMENT (PID)
APPRAISAL STAGE**

Report No.: AB2939

Project Name	Business Environment Strengthening Technical Assistance (BESTAP)
Region	AFRICA
Sector	General industry and trade sector (100%)
Project ID	P103773
Borrower(s)	GOVERNMENT OF MALAWI
Implementing Agency	
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Environment Category	<input type="checkbox"/> A <input type="checkbox"/> B <input checked="" type="checkbox"/> C <input type="checkbox"/> FI <input type="checkbox"/> TBD (to be determined)
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Country and Sector Background

1. The Government of Malawi has finalized a new national development strategy, the Malawi Growth and Development Strategy (MGDS) which was discussed by the World Bank and International Monetary Fund (IMF) in September, 2006. The MGDS merges the previous social sectors focus of the Malawi Poverty Reduction Strategy (MPRS)¹ with the productive sectors focus of the Malawi Economic Growth Strategy (MEGS)². The causality is clearly seen in terms of achieving poverty reduction through economic growth. Fundamentally, the MGDS is a private sector led growth strategy which recognizes the private sector as the “engine of economic growth”. The strategy aims to achieve the Presidential vision of transforming Malawi from being a predominantly consuming and importing country, to one which produces and exports.
2. Malawi’s recent attainment of irrevocable debt relief under the Highly Indebted Poor Countries (HIPC) initiative signifies the return to macro-economic stability that has been championed by the current administration. Despite poor rains and a major food security crisis in 2005/06, Malawi has managed to maintain budgetary and fiscal discipline, and see

¹ Launched in 2001, the MPRS notionally expired in 2005, hence the need for a new national development plan.

² Developed in 2004 in order to strengthen Pillar One (Sustainable Economic Growth) of the MPRS.

improved exchange rate stability and relative reductions in inflation and interest rates. Such macro management has regained the confidence of the international community, demonstrated by resumption of budget support by bilateral donors, a new IMF Poverty Reduction and Growth Facility, and through debt relief. A stable macroeconomic environment is a pre-requisite for sustainable private sector development, and Malawi's strong progress in regaining macro stability means that the Government is increasingly looking to a "second generation" of reforms in the domestic business environment which will seek to stimulate private sector investment and employment creation.

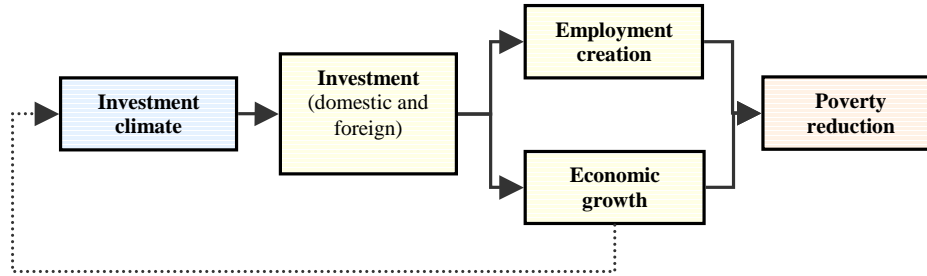
3. The 2006 Malawi Investment Climate Assessment (ICA) provides an up-to-date picture of Malawi's private sector and an effective base line assessment prior to the launch of private sector reforms. Results from the ICA show that Malawi's manufacturing sector is small (accounting for just 11 percent of GDP) and inward oriented (only 14 percent of manufacturing output is exported). Malawi's low cost labor advantages are eroded by poor productivity resulting from poor infrastructure, unreliable utilities and difficulties in accessing affordable finance.
4. The ICA findings confirm the results of previous studies including the 2004 Diagnostic Trade Integration Study (DTIS), which found that many firms are constrained by the small domestic market. The evidence is increasingly showing that the binding constraints to improved trade performance in Malawi lie on the supply-side of the economy. Expansion by Malawi's domestic private sector into regional markets is essential for the country to diversify away from its vulnerable reliance on exports of tobacco, sugar and tea. With the structure of the private sector being a few large firms at the top, many small ones at the bottom and a "missing" middle, a key policy challenge in Malawi is therefore to encourage the large number of small enterprises (many in the informal sector) to grow into the middle space by reducing the costs of formalization and of doing business.
5. In response to the challenges facing the economy outlined above, the Government - through the Ministry of Industry, Trade and Private Sector Development - is leading a PSD reform program that will seek to put private sector development at the heart of Government service delivery. The Government's PSD program draws upon the Bank's ICA and the WB/IFC Doing Business surveys as its analytical foundations and as the basis for monitoring the progress of reforms in key areas affecting Malawi's business environment.

Higher Level Objectives to which the Project Contributes

6. Poverty in Malawi is both widespread and severe with results from the most recent household living standards survey completed in 2005 estimating that 52.4 percent of households are considered poor, and of these 22.4 percent of households are considered ultra poor³. The principal goal of the MGDS is to achieve 6 percent economic growth - the minimum necessary to have a meaningful impact on poverty levels in Malawi. For this growth to be achieved, it is essential that the private sector invests and creates jobs (see Figure 3).

³ Malawi Government (2005) *Integrated Household Survey*, Zomba: National Statistical Office.

Figure 1: Investment Climate Reforms and Poverty Reduction



7. With a few large firms at the top, many small and micro enterprises at the bottom and very few firms in the middle space, one major policy challenge in Malawi is to encourage small and micro scale businesses to grow and migrate into that “missing middle” where they can create more jobs and export more.
8. The World Bank program under the current CAS, presented to the Board in February 2007, is fully aligned with the country’s MGDS and focuses its support in four key strategic areas: (i) Improving smallholder agricultural productivity and integration into agro-processing; (ii) Putting in place a foundation for longer term economic growth through improved infrastructure and investment climate; (iii) Reducing vulnerability at the household level, especially from HIV/AIDS and malnutrition; and (iv) Sustaining improvements in fiscal discipline, budget execution, and accountability of the civil service. Each of the CAS outcomes is explicitly linked to MGDS goals. - employment and income generation; fighting HIV/AIDS; improving human development; decentralization and strengthened public service delivery, and improved M&E. Improvements in these areas are to be pursued against a backdrop of continued macroeconomic stability and the promotion of good governance. In the area of employment and income generation the Bank’s assistance is comprised of mutually-supportive actions intended to create a minimum infrastructure platform for private sector-led growth: (i) creation of an enabling environment for PSD; (ii) alleviation of infrastructure bottlenecks for growth; (iii) exploitation of growth potential in the rural economy; (iv) provision of appropriate education and training for economic growth; and (v) ensuring the improvement and sustainable use of natural resources.
9. The BESTAP project is an integral part of the CAS and contributes to achieving Malawi’s development strategy by addressing the constraints to PSD related to the business environment, weak market linkages, inadequate enterprise skills and institutional support to PSD. As already mentioned above, the project complements the ongoing efforts led by the Bank and other donors (see Annex 2). The IFC has had minimal activity in Malawi in recent years due to the uncertain macroeconomic environment. However, following recent improvements in the investment climate, the IFC is now actively looking for new opportunities in Malawi, and is working closely with the Bank on technical assistance opportunities that are complementary to their investment operations.
10. Other donors welcome the World Bank’s involvement and assistance in addressing important gaps in PSD. Because of the Bank expertise in areas such as improving business environment and increasing access to finance they view the World Bank’s participation as crucial for the

program's success. Bank support will focus on areas where: a) the Bank has a comparative advantage; b) it leverages private sector as well as other donors' participation; c) it supports the emergence of a broad-based entrepreneurship culture, and d) public sector institutions can be transformed to enhance private sector and MSME growth.

11. World Bank participation in the project will enable the government to draw from best practices developed in other regions in a wide variety of fields. For instance, the project will support the introduction of innovative approaches to enhance enterprise creation and competitiveness through regional cooperation, support to the private-public partnership and dialogue. An added advantage of the World Bank's involvement is the cross sector and agency experience the World Bank can draw upon, both within Southern Africa and from other regions.

Project Components

12. The project supports the achievement of the Government's strategy of facilitating private sector led economic growth through four mutually reinforcing components (A detailed project description is given in Annex 4):

- a) *Component One*: Strengthening property rights institutions and business facilitation;
- b) *Component Two*: Strengthening private sector development support institutions and services;
- c) *Component Three*: Promoting access to finance and productivity.
- d) *Component Four*: Capacity Building and Implementation Support

Component One: Strengthening property rights institutions and business facilitation (Total: US\$4.3 million, of which IDA 80%; EC 20%).

13. This component will support activities aimed to improve the regulatory environment in which the private sector operates, to strengthen the institutions that protect private property rights and allow speedy and low cost business facilitation. It has the following three sub-components:

14. *Sub-component A: Streamlining the regulatory environment for business (Total: US\$. million, of which IDA US\$. million; EC US\$. million).* The sub-component will address the large legislative backlog of economic laws, many of which require wholesale revision, that inhibit private sector development in Malawi and support introduction of key legislation. Activities will include: (i) technical assistance to prioritize the economic laws in need of revision based on a cost-benefit analysis of the impact of revising any given Act; (ii) hiring two legal draftspersons in the Ministry of Justice (MoJ) who will be dedicated to working on the drafting of legislation that has a demonstrable impact on the costs of doing business; (iii) training and systems development to strengthen the legislative drafting capacity of MoJ; and (iv) outreach activities to engage key stakeholders in the legislative reform program including parliamentary committees, civil society and the private sector. A Corporate Governance Report on the Observance of Standards and Codes will be prepared under this component.

15. *Sub-component B: Improving access to commercial justice (Total: US\$.., IDA .. EC\$.. million).* This sub-component will provide support for the establishment of a Commercial Division of the High Court to relieve the current large backlog of commercial cases in Malawi's court system and to strengthen contract enforcement. Delays of up to 24 months in the resolution of commercial disputes have been highlighted as a major impediment to doing business in Malawi. This sub-component will fund: (i) procurement of information systems for efficient court management and alternative dispute resolution services (ADR; (ii) institutional capacity building through a linkages program under which Malawian commercial court judges, registrars and ADR administrators will serve short term attachments in other countries with similar legal systems; and (iii) foreign commercial court judges/ ADR administrators to serve short term assignments in Malawi and allow for on-the-job learning by Malawian counterparts. World Bank Institute (WBI) who undertook the initial institutional assessment, is already involved in this activity, and will continue to be involved through project implementation.

16. *Sub-component C: Improving business and land registration services (Total: US\$... million, of which IDA US\$... million; EC US\$... million).* This sub-component will enable the business and land registries to improve their effectiveness in establishing businesses and facilitating the registration and securitization of land-based assets. Institutional assessments for these agencies were undertaken as part of the Doing Business Survey. The following activities will be supported by the project: (i) systems diagnosis and specification; and (ii) information technology investment in the Registrar General's department (for registering a company and business name) and in the Lands Registry (for registering and transferring immovable property titles) (iii) Computerization of procedures and data processing and archiving, and streamlining of documentation and procedures; (iv) restructuring of the registries' operations and procedures and (v) staff training and workshops. Computerization of the current manual business registry systems will significantly reduce the time taken to start a business and will encourage the migration of informal firms to the formal private sector. Similarly, computerization of the Lands Registry will reduce time taken to register and transfer land titles, and simplifying procedures for using land as collateral. The project will also support installation of a facility for remote on-line access, registration of companies and property titles, using streamlined procedures.

Component Two: Strengthening private sector development support institutions and services (Total: US\$4.2. million, of which IDA 80%; EC 20%).

17. This component will build capacity in institutions that provide essential services to the private sector in order to improve the quality and volume of services delivered, and to strengthen institutions that provide policy direction on private sector development issues.

18. *Sub-component A: Establishing a one-stop shop at the Malawi Investment and Trade Centre (MITC) (Total: US\$.. million, of which IDA US\$... million; EC US\$... million).* Activities to be supported under this sub-component are: (i) development of a legal and regulatory framework for setting up a one-stop-shop for investment, exporting and business licensing in the new Malawi Investment and Trade Centre through effective devolution of licensing authority; (ii) streamlining of MITC operations and procedures (iii) provide a systems investment and capacity building package to improve service delivery once the one-stop-shop legal framework is in place; and (iv) staff training and workshops. This sub-component will

involve PEP Africa and FIAS, who will undertake the necessary institutional assessment and continue to be involved during project implementation.

19. *Sub-component B: Establishing an institutional framework for Public Private Partnerships (PPPs) (Total: US\$. million, of which IDA US\$. million; EC US\$. million).* Activities to be supported are: (i) establishing the legal and institutional framework for facilitating private investment in public infrastructure, through PPPs; and (ii) establishing and providing technical assistance to a small PPP Unit. Inadequate infrastructure is a major constraint to private sector investment in Malawi. Given that only limited resources are available in the public sector and from donors, this activity will seek to maximize the flow of private investment into the infrastructure sectors. A PPIAF funded consultancy, which included an institutional assessment, has conducted extensive stakeholder consultations on the design of an appropriate legal and institutional framework for PPPs in Malawi. This sub-component will support implementation of the agreed recommendations.

20. *Sub-component C: Improving private sector development policy analysis and delivery (Total: US\$... million, of which IDA US\$... million; EC US\$... million).* This sub-component will provide: (i) support for establishment of a small *Doing Business* Unit in the Department of Private Sector Development (ii) systems investment and (iii) capacity building - to ensure that the analysis and implementation of policy, institutional and legal reforms to reduce the costs of doing business is a continuous and sustained process. Bank's ICA and *Doing Business* surveys have been the analytical foundations for the Government's medium-to-long term PSD reform program and at the same time confirmed the Government's serious capacity inadequacies to anchor and oversee the program. This sub-component responds to the Government's request for support in building its capacity to maintain these reforms over the medium-to-long term.

21. *Sub-component D: Supporting a sustainable framework for public-private dialogue (Total: US\$... million, of which IDA US\$... million; EC US\$. million).* This sub-component will support the following activities: (i) establishment of a public-private dialogue (PPD) secretariat in the Malawi Confederated Chambers of Commerce and Industry (MCCCI); (ii) technical assistance and capacity building within MCCCI; (iii) restructuring MCCCI's operations and procedures and (v) staff training and workshops. Effective PPD is essential in Malawi to ensure shared ownership and understanding on the respective roles and responsibilities of the public and private sectors. It is accepted that implementation of the previous MPRSP and MEGS was not as strong as it could have been. Deeper government engagement with the private sector on policy formulation and implementation, with mutual accountability on agreed actions would lead to more effective implementation and better results. This component will be implemented with support from the IFC and drawing from the Bank's experience with Presidential Investor Councils.

Component Three: Promoting access to finance and productivity enhancement (Total: US\$5.3 million, of which IDA 80%; EC 20%).

22. Malawi's private sector is characterized by a "missing middle", with comparatively few enterprises located in between the many micro and informal sector businesses, and the larger

multinationals and conglomerates. The objective of this component is to support the growth and development of micro and small enterprises, into this middle market.

23. *Sub-component A: Establishment of a sustainable SME finance institution / investment fund (Total: US\$.. million, of which IDA US\$... million; EC US\$... million).* This sub-component will support the following activities: (i) technical and advisory services in support of an existing Ministry of Finance initiative to establish either an SME investment fund or loan guarantee fund, in support of better access to finance for small-scale businesses. To ensure effective governance, the fund will be managed by the private sector and Government's contribution will be capped with the majority of funding coming from the private sector (both domestic and foreign).

24. *Sub-component B: Business Growth Scheme (Total: US\$... million, of which IDA US\$... million; EC US\$... million).* This sub-component will strengthen capacity of private firms, mostly indigenous owned SMEs, as well as their representative organizations through provision of financial and technical assistance to build the capacity and international competitiveness of private business and professional/ business associations. The Business Growth Scheme (BUGS) will be independently managed in order to ensure effective provision: (i) direct assistance to individual private firms, covering 50 percent of the cost of service fees and of invoiced travel costs on a reimbursement basis. The firm itself will cover the remaining 50 percent of the cost. (ii) Cost-sharing grant assistance to representative business and professional associations to build their capacity to better serve their members. BUGS will cover 50 percent of the costs of service fees and associated travel costs for the use of external services on reimbursement basis. (iii) BUGS HIV/AIDS grants will support expenditures by firms of contracting outside specialist to conduct on-site HIV testing at the firm's premises. These grants are intended to complement existing support being provided to firm-level HIV/AIDS activities under other existing schemes.

25. Purchases of any specialized service, considered by the BUGS Unit likely to make a significant contribution to addressing the key weaknesses or gaps identified in the firm diagnostic, will be eligible for grant support. Examples of services likely to be used include market research, product design, product quality improvement, selection of production machinery, factory layout, training of production and other staff, design of advertising materials, selection of advertising media, selection of local and foreign distributors or agents.

26. *Sub-component C: Restructuring of Malawi Rural Finance Company and the Malawi Savings Bank (Total: US\$.. million, of which IDA US\$.. million; EC US\$.. million).* Access to credit is one of the top constraints to private sector development in Malawi, especially in rural areas. Currently the two state-owned banks - the Malawi Rural Finance Company (MRFC) and the Malawi Savings Bank (MSB) - are not meeting performance targets, particularly financial sustainability and service standards targets. Working with the Reserve Bank of Malawi, the project will: (i) undertake/ update a feasibility/ option study of how the strategic goals of improving service provision and financial sustainability (ii) provide technical assistance and advisory services to implement agreed restructuring measures in MRFC and MSB to achieve necessary efficiency gains and improved access to finance by SMEs in Malawi.

Component Four: Project Implementation and Capacity Building (Total: US\$.. million, of which IDA 80%; EC 20%).

27. This component will fund the following activities: (i) provision of procurement, financial management, M&E and coordination services, (ii) provision of project management and business advisory services for BUGS and (iii) operational costs and goods necessary for project implementation support and the functioning of BUGS business advisory services. The Privatization Commission (PC), which has been managing the Privatization and Utility Reform Project, will assume the above functions - while MITPSD builds its capacity. There will be a review of MITPSD's capacity after two years of implementation to determine whether such project management functions can be mainstreamed in MITPSD.

1. Financing

Source:	(\$m.)
BORROWER/RECIPIENT	0
International Development Association (IDA)	15
EUROPARTNERS BANK	3.7
Total	18.7

Lessons Learned and Reflected in the Project Design

28. This project has been designed drawing upon the World Bank Group's experience in Sub-Saharan Africa and other regions and has benefited from the inputs of various World Bank Group specialized teams, and from the utilization of a strong in-country design team. Specifically the project draws upon the large amount of analytical work carried out by the World Bank Group and the Government of Malawi in recent years, including the 2004 DTIS, the 2006 ICA, the annual Doing Business surveys, the 2006 Malawi Country Assistance Evaluation (CAE), the 2006 Governance and Anticorruption Report (GAC), and the Portfolio Improvement Plan (PIP) prepared by the Country Management Unit jointly with the Quality Assurance Group (QAG). Lessons have also been learned from the experiences of other donor projects supporting the sector and from the experiences of MCCCCI and National Action Group (NAG) in facilitating public-private dialogue in Malawi.

29. The project design reflects the following key lessons learned:

(i) ***Building strong public-private partnership.*** The importance of building an effective private-public dialogue is a key area in the Africa Region's private sector strategy as experience has demonstrated the difficulties in implementing change without ownership by the public and private sector. The project design draws on this lesson and makes the private-public interface a central feature of the project. To ensure that there is ownership and a buy-in of the project and its measures by the Government and the private sector, the project team has carried out extensive consultations during project preparation, including establishment of six Working Groups comprised of public and private sector members, as well as workshops and seminars on capacity building, commercial courts, and licensing reforms. To continue this partnership the project provides support to institutionalize the public-private sector dialogue. Also, the team coordinated with the donor community during project preparation to minimize overlapping and duplication, and to benefit from synergies where possible. The team will continue these close relationships during project implementation. An important element to successful private public dialogue is the ability of the private sector to debate, research and present issues to the public sector. The private

sector's ability to articulate clear positions supports the Government in developing a focused growth strategy. The project has included capacity building for the private sector representative organizations to enable them to develop clear policy positions and solutions.

(ii) ***Simplicity of design.*** Given the limited implementation capacity in Malawi, ensuring that the design of the project is simple and with clear actions, objectives and expected results is essential. A significant recent trend in the Malawi portfolio has been the need to restructure a number of projects in order to simplify their design and to retrofit stronger M & E frameworks. The need to simplify projects is prompted by the pervasive weak capacity to implement projects in the country. In relation to this project, the project team has attempted to incorporate simple designs, implementation arrangements and adequate M & E systems and not design the project above the country's capacity to implement. The project team has selected priority interventions (from a large number of potential interventions) based on a careful assessment of the likelihood of successful implementation and achieving demonstrable improvement in Malawi's business enabling environment.

(iii) ***Ownership.*** The objectives of the project will include implementation of a series of policy, legal and administrative reforms. Such reforms can only be achieved if there is significant commitment to the objectives of the project, and most importantly a belief in, and appreciation of the importance of this project that is both broad and deep across Malawi's public sector. The fact that this project was conceived as a technical and financial support measure to an existing Government of Malawi reform program on private sector development helps to ensure that national ownership remains strong. While appetite for reform across government is not even, the project has strong champions at the political and technical levels in key government agencies. Experience shows that institutional reforms can succeed when there is committed leadership and the Bank programs work closely with champions of reform in government and in collaboration with a broad range of stakeholders.

(iv) ***Implementation Arrangements.*** A major challenge with regard to this project has been choosing an implementation structure which balances the need to get results, with the need to build capacity in the public sector. The well known low capacity in the Ministry of Industry, Trade and Private Sector Development has led to the Government ruling out the Ministry itself leading implementation of project activities. Instead, such implementation has been devolved to beneficiary agencies themselves in the majority of cases and to the private sector in some instances. The PIU's role will be limited to core functions such as (financial management, procurement and M & E) which will be undertaken in consultation with counterparts in the beneficiary agencies. The Privatization Commission, which has been managing the Privatization and Utility Reform Project, will assume the core functions - while MITPSD builds its capacity. There will be a review of MITPSD's capacity after two years of implementation to determine whether such functions can be transferred to MITPSD.

A related question was the implementation period for the project. Four projects in the Malawi portfolio have requested and have been granted extensions of closing date. This suggests some underestimation of implementation challenges at the project design stage. The BESTAP project team has opted to go for a 5 year (rather than 4 year) project to recognize that the

significant reforms expected under the project together with the low implementing capacity in Malawi – means more rather than less time will be required to complete the program.

(v) ***Cost sharing/matching grant.*** Experience suggests that MGS are most effective when they are demand driven, with cost sharing to ensure adequate ownership and willingness to pay; based on a realistic business development plan; reimbursement basis; gradually declining subsidy element; no productive activity is excluded; first-come, first-serve. Grants will be provided in tandem with pro-active promotion, and with free hand-holding “technical assistance” to firms. It is important to note that while these matching grants will go to private firms, the products developed and the demonstration effects of success will represent private goods that are expected to facilitate sustainability (i.e., private firms willing to fully pay for Business Development Services (BDS)).

(vi) ***Private management of matching grant scheme.*** Experience indicates that what works best is a combination of local professionals together with international specialists. The local professionals bring to the task knowledge and appreciation of local culture, market realities, and business practices. The international specialist(s) bring to the task international best practice in operating the programs, plus appreciation of the market realities facing exporters when selling to distant industrialized countries. The project will adopt the mixture of private management in sector pilot programs and the MGS scheme.

Alternatives Considered and Reasons for Rejection

30. Several alternatives were considered during project design. First, consideration was given to focusing the project on specific sectors such as agri-business, tourism or manufacturing, but this approach was rejected because of the limited success of narrowly-defined projects in Malawi and other countries and because a broader focus gives greater flexibility in responding to market opportunities. Focusing on one specific area of intervention, and making interventions more sequential was also considered. However, it was decided that a combined set of interventions would generate greater impact. The distinct and complementary nature of the interventions included in the project generates important benefits that are mutually-reinforcing. Consideration was also given to providing technical assistance through the budget support program. The DPL will leverage and complement the highly specialized nature of assistance being provided by the project. There is a need in Malawi to build private sector capacity and enhance learning experiences, which demands a flexible program focused on opportunities, independent of the budget cycle and of public sector management. In addition, the limited success of programs which are funded and managed by the public sector led the team to adopt an approach where the private sector manages the program as such as possible, ensuring greater private sector participation and ownership.

31. The project team also considered leaving support of the PSD program to other donors. This was rejected because there are only a limited number of other donors operating in Malawi, and none has a significant PSD program or a dedicated PSD advisor/department. While all donor country programs should now be aligned with the MGDS, it is not yet clear whether any other donors have the willingness or capacity to implement anything more than *ad hoc* support to private sector development activities.

32. The World Bank's has significant comparative advantage in private sector development interventions is widely accepted and recognized by the Government and by other donors. With an in-country PSD team, and with a strong technical and diagnostic background based on successful implementation of the ICA and *Doing Business* surveys, the most appropriate intervention was the design of a new project in support of the Government's own PSD program. The European Commission has agreed to enter a co-financing arrangement with the World Bank in support of this project.

IMPLEMENTATION

Partnership Arrangements

33. Private sector development activities are under-funded in Malawi and have historically suffered from changing priorities and "focal areas" among donors. However, recent improvements in macro-economic management, together with Government-led efforts to prioritize growth as the best means of achieving sustainable poverty reduction, means that supporting private sector development is being seen as increasingly important within the donor community. The first Malawi Joint Country Program Review (DFID, EC, GTZ, Norway, World Bank) carried out in February 2006 found that donor support to private sector development has tended to be erratic and unfocused, with significant overlaps and gaps. Poor Government leadership in the past and a limited focus on the role of the private sector in driving growth has compounded this problem. Therefore the MGDS - a private sector-led growth strategy - provides a new opportunity to rationalize donor support around a clear nationally-owned development plan.

34. Key donors participated in the design process of this project including the EC, DFID and USAID. The EC has agreed to co-finance the project. The EC has asked the Bank to manage their financial contribution to the project on their behalf under a trust fund arrangement. As a preparatory step during the diagnosis of a private sector reform agenda, MITPSD coordinated the work of public-private technical working groups on reducing the costs of doing business in five areas⁴. Strong private sector representation in these groups, which were each chaired by the private sector, ensured that a business facilitation reform agenda, which this project will build upon, was agreed upon with strong public-private partnership. The process of preparing this project also benefited from the active participation of the National Action Group Secretariat, MCCI and from members of the Integrated Framework Steering Committee.

Institutional and Implementation arrangements

35. The project will be overseen by a Private Sector Development Steering Committee (PSC) which is already in existence and has guided the conceptualization and development of the project from the beginning. This committee is chaired by the Minister of Industry, Trade and Private Sector Development and has significant private sector representation as well as representation from other government departments who will be implementing some of the project activities. Membership of the PSC will be restructured to include all the project beneficiaries and will be as follows; MITPSD, MoJ, Commercial Division of the High Court,

⁴ Getting credit, trading across borders, paying taxes, dealing with licences, and closing a business.

Registrar General's Office, Ministry of Lands, Malawi Investment and Trade Centre, MoF, MCCCCI, Reserve Bank of Malawi and Ministry of Economic Planning and Development. The PSC will be meeting on a quarterly basis.

36. In addition, the Project Review Committee (PRC) will (i) provide technical and operational guidance for the project; (ii) review and approve quarterly progress reports prepared by the Project Manager; and (iii) proactively address any technical and implementation problems affecting project progress. PRC will comprise PIU, BUGS Program Manager, and Director of Private Sector Development.

37. The overall operational direction will be provided by the Principal Secretary for Private Sector Development. The PC, through its PURP PIU, will provide core functions – financial management, procurement and monitoring and evaluation for the project. In order to maximize capacity building opportunities, all other project implementation activities will be undertaken by the beneficiary agencies themselves or by the private sector. While the PC will be responsible for the core project management functions for the project, actual implementation responsibility of the various components will be with designated persons within the beneficiary agencies and these designated persons will then be working closely with the PC on and be submitting regular reports to the PC who will consolidate these reports for reporting to the Project Steering Committee. Details of the various institutions involved in the implementation are contained in Annex 6.

38. The implementation arrangements were selected based on the need to ensure effective execution of the core project management functions balanced with ensuring ownership by and capacity building for the beneficiaries of the various project components. The option of using the PC was chosen after consultations with Operations Advisers and the Government. By having implementation responsibility in the hands of designated persons in the beneficiary agencies, it is expected that this will result in more ownership of the project at the local level and sustainable results at the end of the project.

39. The major capacity constraints that need to be addressed are project management skills, particularly knowledge of World Bank financial, procurement and monitoring and evaluation procedures. These are necessary to ensure effective project implementation. This constraint will be addressed by use of the PC where such skills already exist and by building the capacity of staff in MITPSD at the same time.

40. The PC PURP PIU staff has experience in managing Bank-funded projects. Systems have been established and a dedicated Project Accountant in the PIU will support the implementation and maintenance of centralized financial management, internal controls, disbursements and financial reporting procedures for the project as a whole. This arrangement is further strengthened by separating and devolving implementation authority and budgets to the component executing agencies.

Component Executing Agencies.

41. Management and implementation of individual project subcomponents will be mainstreamed to the following agencies with the following focal points which have been agreed with the Government of Malawi:

- a. MITPSD and MoJ for reducing the regulatory burden on private business
- b. MITC for streamlining business licensing reforms;
- c. Registrar General's Office for streamlining registration reforms
- d. Lands Commissioner for improving land title transfer and registration
- e. Registrar of the High Court for the Commercial Courts
- f. MCCI for Public-Private Dialogue
- g. Ministry of Finance for Public Private Partnerships
- h. Reserve Bank of Malawi and MoF for restructuring MRFC and MSB and improving access to finance;
- i. BUGS Program – a competitively recruited person from the private sector

42. These focal points from the executing agencies will be formally designated by responsible Principal Secretaries, Registrar General and CEO of MCCI and be responsible to the Project Manager for effective implementation of project activities in their agency/ Ministry. Focal points will be responsible for day-to-day implementation of the activities under respective subcomponents; programming of annual plans and budgets; monitoring, public relations and reporting. They will manage all the technical aspects (with assistance from long term advisors where applicable); they will prepare all terms of reference and manage the supervision of consultants. They will be responsible for preparing all reports required under the credit for the respective project components.

43. The BUGS is in direct support of the project objective of promoting private-sector led economic growth. The specific objective of BUGS is to facilitate growth in private sector economic activity. The scheme will run for the five years of the project and will be operated by a small unit, established for the purpose, consisting of two experienced professionals recruited from the private sector. The intention is that BUGS-supported firms will, as a direct result of this support, increase their annual turnover at a rate at least 20 percent higher than the rate that non-supported firms manage, over the same period. BUGS will achieve this objective by the use of a mix of two specific forms of assistance to individual private firms:

- (a) Direct technical assistance will be provided to firms by the BUGS Unit. This will start with a detailed standard diagnostic. The unit will then provide direct mentoring & consulting help on how to implement an agreed business growth plan within each supported firm (i.e. general business consulting);
- (b) Where more specialized help is required, to support a plan for growth by a particular firm, then the unit will provide matching grants, to part-fund the use of outside expert specialist help (e.g. choosing the right machines; quality control; product design; advertising planning; market research; book-keeping & accounting systems; management information systems; etc.).

44. The scheme will be open to any private business entity, providing work to Malawi nationals within Malawi. The scheme will recognize that the vast majority of such firms are not

yet officially registered. These are the taxpayers of the future. They, too, will be helped to grow by BUGS, but will be encouraged to register, once they reach the level where income tax (individual or corporate) becomes payable.

45. BUGS matching grants will cover 50 percent of the direct costs of such help, in the form of fees and directly-attributable expenses. Grants will not cover the costs of hardware, nor of salaries. Only the direct incremental costs of buying specialized services will be covered. No individual firm, or group of firms under common control, may receive a cumulative total of grants from BUGS in excess of \$50,000. Grants will be paid strictly on a reimbursement basis only. Each firm being offered grant assistance will be required to sign a letter of agreement with the BUGS Unit, specifying the activities being supported, the supplier(s), and the costs. Once proof is provided that the activities have been satisfactorily completed, only then will the grant be paid.

46. Within the BUGS grant fund, there will be a small allocation of \$200,000 to support expenditures by BUGS-eligible firms on the use of outside service providers, to provide on-site HIV/AIDS testing at these firms' premises.

47. Sample surveys of firms, covering both those assisted and a control group of those not assisted by BUGS, will be carried out, firstly at the time of the Mid-term Review, and then at the time of the Completion Report. These surveys will form the basis for determining whether or not the BUGS scheme achieves its stated objective.

48. Further, for the BUGS program, a dedicated approvals committee will be established under the PRC. Any grant that takes a cumulative total over \$x or individual total over \$x received by any one firm, or group of firms under common control, will require a "no objection" from the BUGS Approvals Committee. Members of the BUGS Approvals Committee will be selected by the PRC and will consist of two government members and one private-sector member. Meetings of this sub-committee will be called by the BUGS Program Manager, as needed. The BUGS Manager will report to the Project Manager.

49. POM including the Project Implementation Plan, Financial Management Procedures Manual and Procurement Plan will be finalized by project effectiveness. A mid-term review will take place in November 2009 with the objective of assessing progress to date and if necessary to re-direct the project by integrating additional lessons learned and realities on the ground.

Institutional arrangements and capacity building

50. The capacity of implementing agencies will be enhanced through provision of information management systems and online services delivery. The design of the systems will be based on a participatory approach using up-to-date and user-friendly application technology allowing each technical implementing agency as well the PC to participate interactively in the production, analysis and exchange of data and information both generated within the project cycle and the day-to-day operation of the executing agencies. This will foster a greater ownership and accountability for the project implementation results and outcomes.

51. The system will improve data harmonization and minimize duplication as well as strengthen particularly the capacity of the company registry, business licensing and MITC to respond to the Government's need for information and data to improve management of these agencies, compare its business environment with international standards and attract potential investors. The capacity of the implementing agencies will be strengthened with technology equipment, training on data collection, content management, information updates and basic system troubleshooting and maintenance. The M&E specialist within the PC will provide technical support to implementing agencies designated focal points as well as coaching and mentoring on data collection, management and reporting.

Supervision Missions

52. The Bank's supervision mission will include representatives of the EU (co-financiers) and will be as regular as possible considering the nature of the project. The supervision mission's objectives will include ensuring that strong financial management systems are maintained for the project throughout its life. A review will be carried out regularly to ensure that expenditures incurred by the project remain eligible for IDA funding. A mid-term review will be conducted with the objective of assessing progress to date and if necessary to re-direct the project by integrating additional lessons learned and realities on the ground. Frequency of supervision missions proposed is one every 6 months (includes special procurement supervision for post-review/audits). See Annex 11.

Monitoring and Evaluation Outcomes/Results

53. The M & E system will be based on the agreed Results Framework and monitoring arrangements (see Annex 3). The PC will be responsible for conducting M&E activities. Baseline data collection for all the agreed indicators will be initiated by the PC in partnership and collaboration with the designated focal point in each implementing agencies during the project start up phase where applicable for each agreed performance indicators. The designated focal points of the implementing agencies will be responsible for the data collection and reporting of their respective component and subcomponent.

54. Data collection and reporting on the regulatory environment for business subcomponent will be the responsibility of the MITPSD focal point. This will enable the MITPSD to develop sound policy analysis. For the Commercial Courts subcomponent, the designated focal point will be responsible for collecting data and reporting on improving access to commercial justice, the enforcement of contracts and insolvency with respect to time and procedures for settling commercial disputes. The project will support the provision of an information technology platform, computer equipment and network installation for an efficient and effective court and case management.

55. For the business and land registration subcomponent, the Registrar General and Lands Commissioners' Offices will be responsible for collecting data and reporting that focuses on time, procedures and costs of registering a company, business name and the time, procedures and costs of registering and transferring immovable property titles. The project will support the provision of information systems platform to computerize both the business registration and

licensing, and land registration processes through online registration. The project will also support computer equipment and network installation for the Registrar General's department and the Lands Registry.

56. The MITC will be responsible for data collection under the one-stop shop subcomponent for investment, exporting and business licensing. Data collection, management and reporting will initially focus on permits and licenses issuance to assess quality of services delivery. The MITC will work in collaboration with the business licensing and registration department, and Lands Registry for data harmonization and consistency. The project will support establishment of an online business licensing platform and capacity building to improve service delivery to the private sector. The MITC also will work closely with the Doing Business Unit responsible for collecting, managing and reporting data and information on Doing Business indicators.

57. For promoting access to finance and enhancing productivity of SMEs, The Manager of SME finance subcomponent will be responsible for data collection and reporting on small-scale business start-ups and services to beneficiary SMEs on financial products such as loans, equity, quasi equity and guarantees. The BUGS Program Manager will be responsible for data collection, management and reporting on the number of SMEs accessing the scheme and the impact on their productivity level. Overall, the PC will be responsible for consolidating and preparing all periodic fiduciary and M & E reporting including impact and output indicators to IDA as well as the annual project audit. In addition the PC will submit to the Bank an Implementation Progress Status Report quarterly.

Sustainability

58. The project is supporting the Government's vision of that Malawi should become a "producing rather than consuming country, one which exports rather than imports". This vision is enshrined in the MGDS, around which all development assistance is now being aligned. Trade and private sector development issues have not generally been accorded a high priority in previous Government policy under the MPRS, and recent donor support to Malawi has tended to focus more on social sector development and the improvement of social outcomes, rather than tackling the underlying causes of poverty in Malawi - namely economic under-performance.

59. The MGDS places clear responsibility for achievement of social outcomes and poverty reduction on raising the rate of economic growth. The PSD Reform Program was launched as a Government initiative, with full national ownership. The program was initially conceived without donor assistance, and the Bank was invited to provide technical and financial support to implement the strategy and reform program. As PSD is cross-cutting and reaches across all areas of national policy, a prerequisite to achieving the MGDS goals of economic growth and private sector development has to be the effective mainstreaming of PSD issues across the public sector in Malawi and this is also a key issue for ensuring the sustained impact of this project.

60. Many of the constraints to PSD do not require large expenditures, merely the diagnosis of policy, legal and administrative reforms, and technical support in implementing such changes. Therefore the cost of such actions is quite low, while the impact can be high. The Government of Malawi is committed itself to improving Malawi's performance as assessed by the annual Doing

Business surveys. Similarly, while many aspects of reducing the cost of doing business can be tackled with low-cost actions, others require resources well beyond the scope of this project. As a landlocked country Malawi's private sector suffers from very high transport costs for both exports and imports. Critical to the sustainability of the project is further investment in infrastructure, not just in transportation but also in power, telecommunications and the water supply. The ongoing privatization program, and the facilitation of public-private partnerships as envisaged under this project will play an important role in addressing these infrastructure constraints, but additional public and private investment will be required to achieve real change.

61. Another critical factor to sustainability is achieving a change in attitude of key public service agencies and their staff, which are now being increasingly viewed as service providers rather than civil service gatekeepers. While the project can support government in the diagnosis and implementation of economic and policy reforms, in the end it is on-the-ground implementation of such policies that has the greatest impact on the private sector. Equally, while the project can channel supplemental resources to key institutions that serve the private sector, attitudes will remain a critical factor in determining how effectively such additional resources are deployed. In light of the above, a major cross-cutting emphasis of the project will be on changing the mindset and attitudes of the public sector.

Critical Risks and Possible Controversial Aspects

62. The overall risk rating of this project has been assessed as medium. Improvements in macroeconomic management and public sector governance are the foundation of an improved private sector enabling environment, but a number of institutional risks remain.

Risk	Risk mitigation measures	Risk rating with mitigation
<i>Change in Government.</i> A change in Government would be a risk if it resulted in a departure from current thinking on the role of the private sector in driving economic growth.	This risk is mitigated by ensuring that ownership and understanding of the program is both broad and deep throughout the civil service, and therefore able to withstand changes in political leadership.	L
<i>Macro-economic crisis / loss of fiscal discipline.</i> Macro stability is a pre-requisite for sustainable private sector development. Hence ensuring that Malawi's achievements in this regard are maintained is essential to the success of the program.	Credibility of the current Government is closely linked to the maintenance of macro stability and an important element of the program will be mainstreaming PSD issues across Government and society, especially the importance of low and stable interest rates and inflation for private sector investment.	L
<i>Staff turn-over in Government.</i> Staff attrition in Government, not least as a result of Malawi's HIV/AIDS epidemic, is a constant challenge for building and maintaining capacity.	In order to address this challenge, staff at all levels, across departments within MITPSD and other key institutions were involved early during project design, appraisal and implementation.	M
<i>Poor project financial management.</i> Funds may not be used efficiently, or for	The use of financial management and procurement staff from the terminating	M

the exclusive purposes intended. Internal audit functions and procurement procedures may be weak, thus jeopardizing project expected outcomes.	Privatization and Utility Reform Project will ensure efficient financial management from the outset.	
Overall risk rating		M

Credit/Grant Conditions and Covenants

88. **Conditions of Negotiations:** The recipient has to prepare and submit prior to negotiations the following documents in a form and content that is acceptable to IDA:

- a. an 18 month procurement plan that is acceptable to IDA
- b. a template Interim Financial Report format that is acceptable to IDA
- c. draft Letter of Sector Policy
- d. draft Project Implementation Manual
- e. terms of reference/ job descriptions for all personnel to be recruited under the project

89. **Conditions for Board:** The recipient has to prepare and submit prior to Board presentation the following documents in a form and content that is acceptable to IDA:

- a. a final Project Implementation Manual
- b. Letter of Sector Policy signed by the Government

90. **Effectiveness Conditions:** The only condition required for effectiveness is that the recipient should have completed the recruitment of all project personnel and have them on board.

91. **Legal covenants:** Standard financial covenant included in the financing agreement are the following: (i) Submission of audited financial statements within six months after the year end (ii) Submission of un-audited interim financial statements within 45 days after each calendar quarter, to cover such calendar quarter (iii) Submission of any other information as required by IDA.

Economic and Financial Analyses

92. The project cost-benefit analysis of the BESTAP indicates that the project will generate a net present value estimated at about US\$20.33 million corresponding to an economic rate of return of 49.44 percent. The project is expected to have a positive impact on employment as a result of acceleration of output growth in the supported sectors where a minimum of 2,500 jobs are expected to be created by supported SMEs.

63. The project will also have a positive impact on the Government's fiscal position. It is estimated that the activities associated with the project will generate more than US\$3.5 million during the project cycle from incremental taxes paid by employees and corporate income taxes. The informal sector will also benefit from the project to an extent which cannot be quantified.

Technical

64. The project draws heavily on the results of the ICA that demonstrated the need to integrate policy reforms initiatives and improve the business environment with technical and financial support to nurture the private sector and assist in its repositioning to a market-led economy. The project aims to improve business environment through reducing the costs of doing business, improving the legal framework for firms' entry, exit and operations. The project aims to bring new technology and management know-how to private firms. The matching grant component is expected to provide an important impetus for skills and technological upgrading within private firms. Finally, modernization of the legal framework for private business and TA to develop a Credit Guarantee Scheme aims at increasing the availability and access of to finance for SMEs.

Fiduciary

65. The PURP PIU will implement and coordinate the BESTAP. The PURP is currently under the PC in Blantyre. The PIU is a dedicated PIU that has been coordinating the multi component PURP and supports activities in various entities of the Government across various ministries. The PIU has been in charge of preparing the consolidated procurement plan, providing advise on implementation and coordinating the reporting on procurement implementation and carrying out internal quality assurance systems for procurement in all the project component implementing agencies. The project component implementing agencies for the proposed BESTAP include the following: (i) The Ministry of Justice, (ii) The Commercial division of the High Court (iii) Registrar General's Department (v) Lands Registry (vi) MITC (vii) MoF/ PC (viii) MITPSD (ix) MCCI (x) Secretary to the Treasury (xi) Director of Private Sector Investment (xii) Reserve Bank of Malawi.

66. The PIU comprises 5 professional and 5 support staff. It has acquired sufficient experience in implementing the Bank funded PURP and would have a comparative advantage to implement the proposed BESTAP. It has also supported the preparation of the BESTAP as funds from the PURP have been used to carry out the BESTAP preparation activities. The staff of the PIU includes a Procurement Specialist who will support the implementation and maintenance of the overall procurement plan for the project. The Procurement Specialist of the PIU will provide support and oversight including quality assurance reviews and monitor implementation progress of all the components. This function will be further supported and strengthened by the existence and carrying of procurement by each implementing agency. Each Implementing Agency has a dedicated Procurement Specialist who works with technical specialists. The Procurement Specialists in the implementing agencies will provide periodic progress reports and will as appropriate make requests to the Bank for review and clearances through the Procurement Specialist of the PIU. The procurement Specialist of the PIU will work with and be supported by other qualified and experienced staff of the PIU and the support systems that are in place for implementing the project which will be articulated in the Project Implementation Manuals which the Government needs to prepare and review preferably before contract effectiveness. The manuals will be an additional safeguard to ensure that procurement under the BESTAP conforms to the minimum requirements for Projects funded by the Bank.

67. The PIU financial management staff has experience in managing Bank-funded projects. Systems have been established and a dedicated Project Accountant in the PIU will support the implementation and maintenance of centralized financial management, internal controls, disbursements and financial reporting procedures for the project as a whole. This arrangement is further strengthened by separating and devolving implementation authority and budgets to the component executing agencies.

Social

68. There are no social issues triggered by this project. A number of project components are expected to lead to favorable social outcomes, including employment generation and poverty reduction. Key stakeholders from both the public and private sector have been consulted throughout project design and involved in the project design through participation in several workshops and other consultative mechanisms such as technical working groups. Project implementation arrangements builds on a public private partnership which has begun to be developed.

Environment

95. The project is a category C and no environmental assessment is required. However, since the project intends to strengthen the private sector, including SMEs, the capacity building support will include environmental training at appropriate institutional levels, with a focus on environmental and social screening of projects which will be implemented at some point in the future. The aim would be to build this capacity now. BESTAP will draw on the Infrastructure Services Project in Malawi, in this regard.

6. Safeguard policies

Safeguard Policies Triggered by the Project	Yes	No
Environmental Assessment (OP/BP 4.01)	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Natural Habitats (OP/BP 4.04)	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Pest Management (OP 4.09)	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Physical Cultural Resources (OP/BP 4.11)	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Involuntary Resettlement (OP/BP 4.12)	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Indigenous Peoples (OP/BP 4.10)	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Forests (OP/BP 4.36)	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Safety of Dams (OP/BP 4.37)	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Projects in Disputed Areas (OP/BP 7.60)*	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Projects on International Waterways (OP/BP 7.50)	<input type="checkbox"/>	<input checked="" type="checkbox"/>

* By supporting the proposed project, the Bank does not intend to prejudice the final determination of the parties' claims on the disputed areas

Policy Exceptions and Readiness

69. The project does not require any exception from Bank policies. Assessments and preparation of fiduciary arrangements, staff and consultant selection, monitoring and evaluation systems and implementation and procurement plans meet the regional criteria for readiness of implementation.

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