

# Banking on *Municipalities*

## World Bank Support in Europe and Central Asia

**More than 280 million people live in cities in the Europe and Central Asia Region—64 percent of the total population. Through 28 municipal development projects (MDPs) active during the 1998–2008 decade, the World Bank made commitments of \$1.7 billion.**

This portfolio aimed to strengthen the management of 292 municipalities in 16 countries. By number of MDPs, the most active borrowers were the Russian Federation (4 projects), Bosnia and Herzegovina (4), Georgia (3), Turkey (3), Kazakhstan (2), and the Kyrgyz Republic (2). The remaining 10—Armenia, Croatia, Kosovo, Latvia, Lithuania, Poland, Tajikistan, Turkmenistan, Ukraine, and Uzbekistan—hosted 1 MDP each. Thus, half of the Region’s MDPs were in upper-middle-income countries. Countries in the Region with large urban populations but no Bank-financed MDPs are Romania and Belarus.

### PORTFOLIO PERFORMANCE

Sixty-three percent of completed MDPs achieved satisfactory outcomes, and the percentage of satisfactory Bank and borrower performance was a little higher. These figures are somewhat below the Bank-wide averages.

Among successful cases in the Region’s portfolio, **Russia IV** stands out for its outcome rating of highly satisfactory. The project considerably strengthened the financial management of the newly created municipality of Kazan (population 1.2 million) by helping local officials organize and unify municipal accounts, debts, and other obligations. The municipality turned a deficit into a small surplus. Outstanding payables, a major problem at the outset, were substantially reduced. Two-thirds of the project funding was used for urgent repairs to abandoned and derelict schools and health centers, bringing them back into full use. Kazan considerably improved its asset management, divesting some unnecessary inventory. Real estate assets remaining on the municipal books are now leased at 90 percent of their market values, up from 50 percent prior to the project.

Other successful examples included **Bosnia and Herzegovina I**, which helped develop a municipal credit market as intended. In the process, it strengthened financial management both by the municipalities and by five commercial banks that entered this market for the first time, making 28 loans for \$13.3 million.

**Turkey I** helped improve the efficiency of water use in municipalities by substantially improving worker productivity per connection as well as the bill-collection ratio. **Kyrgyz Republic I** was successful in separating road planning, budgeting, and contract administration from

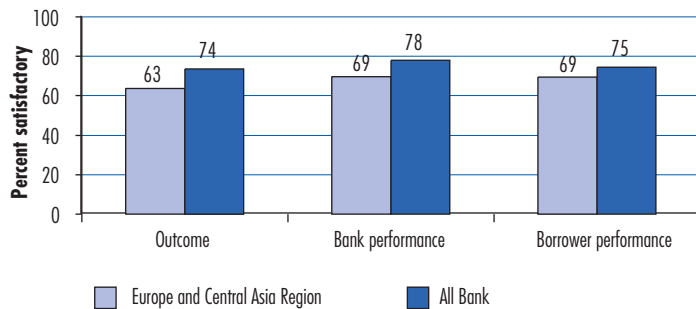
**Table 1: Summary of MDP Portfolio, 1998–2008**

Completed (number)	16
Completed MDPs (% satisfactory)	63
Ongoing MDPs (number)	12
IBRD commitments (US\$ million)	1,496
IDA commitments (US\$ million)	207
Bank commitments per completed MDP (US\$ million)	36
Commitments per ongoing MDP (US\$ million)	94
Wholesale MDPs (number)	6
Retail MDPs (number)	22
Countries served (number)	16
Municipalities served (number)	292

Source: World Bank data.

Note: IBRD = International Bank for Reconstruction and Development; IDA = International Development Association; MDP = municipal development project.

**Figure 1: MDP Portfolio Performance, Fiscal 1998–2008**



Source: IEG special study.

Note: MDP = municipal development project.

road construction, as intended, and it helped the municipalities of Jalalabad, Bishkek, and Osh set up their own passenger transport authorities to plan, contract, and monitor the private provision of local services. **Georgia III** helped nine municipalities, housing three-quarters of the country's urban population, to become creditworthy and particularly increased the effectiveness of their delivery of street paving and water supply services.

At the same time, three MDPs turned in a weak performance. The **Poland MDP** had little impact on the development of a commercial credit market for municipal investment. Its performance was undermined by a 1999 Finance Law that prevented municipal borrowing, and the project disbursed very little. **Kazakhstan I** failed to promote efficient municipal management of social assets divested by state-owned enterprises, mainly because the project gave insufficient attention to the financial challenges the municipalities faced. The **Lithuania MDP** did not strengthen municipal management, as intended, because the Association of Local Authorities of Lithuania, slated as the executing agency for the project, lacked the necessary capability and resources to perform this function effectively.

## BETTER CITY PLANNING

### More information

Few MDPs in the Region aimed specifically to strengthen information systems for municipal management and planning. But the need for such information was acute in Georgia in the mid-1990s; three successive MDPs in that country introduced computer equipment and made municipal information more transparent under the law. However, much progress remains to be made, and Georgia can learn from other good experiences, such as Chile's Information System on Municipalities. **Russia I** successfully created a territorial information and analytic system for land, real estate, and infrastructure and a developer's manual, both of which have had a positive impact on the housing market and have become valuable references for potential foreign investors and other parties.

### Monitoring and evaluation

Monitoring and evaluation (M&E) design in MDPs, as for many other projects, was often weak because it focused on the delivery of component outputs rather than achieving project outcomes. Even some output indicators were not always clear or measurable, lacking baseline and endline (target) data. This prevented M&E implementation and use as a feedback mechanism to inform and improve project performance. M&E in the **Latvia** and **Kosovo** projects did not distinguish between output and outcome indicators. These projects especially lacked those indicators that could measure actual institutional improvements against those planned and relied too heavily on users' opinions, expressed through beneficiary assessments. Performance indicators could not be measured for lack of data—for example, on municipal action plans in **Kyrgyz Republic II** or on municipal finances under the first Georgia MDP. During **Georgia II** and **III**, M&E focused more on management information on municipalities, and this information slowly became available in the country. The lack of baseline data undermined the effectiveness of M&E in **Turkey I**, which did not explicitly cite preproject levels of pollution in the Sea of Marmara, for instance.

**Kazakhstan I's** M&E could not capitalize on technical assistance relating to financial management methods and was unable to produce monitoring data on a continuous basis to measure its operating performance. **Russia IV** in Kazan, in contrast, incorporated a strong M&E system, whose design included easy-to-measure indicators such as municipal debt and level of targeted cash-transfer subsidies that were also part of the conditions of tranche release of the structural adjustment design of this loan.

### Urban and spatial planning

Most MDPs in the Region did not include significant urban planning activities. An exception was **Russia I** in St. Petersburg, which drafted several laws to aid the planning process in improving the availability of serviced land. The laws had yet to be ratified at the time of project completion.

### Investment planning and strategies

By training 550 staff in 30 municipalities, **Kosovo's** MDP helped prepare five-year rolling financial plans for the first time and incorporated community inputs through participatory processes. **Kyrgyz Republic I** helped Jalalabad and Bishkek municipalities prepare plans for financing and contracting urban road building, which was separate from the construction itself.

## STRONGER MUNICIPAL FINANCES

### Better financial management

Several MDPs achieved positive results in this area. Among the most notable was **Russia IV** in Kazan, where project technical assistance helped local staff unify the municipal accounts for the first time and make them more transparent. Among other things, computerized accounts allowed Kazan's employees to receive their salaries on time.

Other experiences show that equipment, technical assistance, or training alone is not enough to ensure better financial management. Initially, municipalities made limited use of computing equipment provided through **Georgia I**. **Uzbekistan's MDP** did not lead to improved financial management by the municipal solid waste utility, despite the technical assistance provided. The actual modernization of municipal management did not occur in the **Turkmenistan's MDP** without the widely expected devolution of responsibilities to the local level. Under **Kazakhstan II**, municipal water utilities did not implement modern financial management techniques, for which training was provided, because of discontinuities in leadership. Similar weaknesses in the **Latvia MDP** were partly overcome by twinning the Daugavpils city water utility with the water works of the city of Tampere in Finland.

### Mobilizing own revenues

The Region's MDP portfolio obtained some good results in this area. Technical assistance through Bank supervision of **Russia IV** helped Kazan find alternative sources of revenue, which were urgently needed, as large federal transfers were soon to lapse. Municipalities participating in **Georgia II** increased own-source revenues by 11 percent during 1998–2002, compared with a decrease of 16 percent for other municipalities, thanks in part to the incentives to become creditworthy.

**Kyrgyz Republic I** helped establish urban road funds and raised taxes threefold on private vehicles. The **Uzbekistan MDP** did not succeed in establishing a stable self-financing mechanism for solid waste management through planned tariff adjustments, although a last-minute reprieve prevented the operation's collapse. Specific cost recovery from MDP investments themselves obtained good results in **Turkey I**, where the Bursa municipal water and sanitation utility successfully maintained tariffs at levels sufficient to meet its financial obligations.

### Municipal creditworthiness and debt management

Under **Georgia I** the Municipal Development Fund of Georgia became Georgia's main funding source for municipalities and an instrument for strengthening municipal management. Today the fund has become the government's principal agency for financing major development programs beyond just municipal development. The latest **Georgia III** project saw 9 municipalities, home to 73 percent of the urban population, become creditworthy, also giving some of them access to additional concessional funding. Under the previous **Georgia II**, some municipalities had overborrowed and defaulted on their loan repayments.

Technical assistance to 32 municipalities and, most significantly, to 5 commercial banks under **Bosnia and Herzegovina I** helped municipalities become more creditworthy by increasing revenue collections and helping banks understand their debt portfolio better. The government supported a similar approach under **Kyrgyz Republic II**, partly in the hope of reducing the financial burden of subsidies. The potential foreign exchange risk inherent in external funding of municipal credit does not appear to have constrained municipal creditworthiness in the Region. In Poland, with memories

**Table 2: Municipal Management Focus of Region Portfolio**

Share of all MDPs with a project design focus on:	Completed	Ongoing
<b>City planning</b>		
In objectives (%)	25	33
In components (%)	56	67
<b>Municipal finance</b>		
In objectives (%)	75	25
In components (%)	75	92
<b>Service delivery</b>		
In objectives (%)	88	83
In components (%)	81	92
Number of all MDPs	16	12

Source: IEG special study.

Note: MDP = municipal development project.

of that country's recent high inflation, commercial banks tried unsuccessfully to transfer this risk to equally reluctant municipalities, stalling project implementation. But in most other countries, central governments and their agents have been willing to assume this risk.

### Private finance participation

To date, MDP efforts and results in getting private finance into municipal services have been limited. Poland's project did not succeed in channeling private bank funds into municipalities because of the overall project failure. Private funding of Tashkent's solid waste management under **Uzbekistan's MDP** could not proceed while the operation continued to operate at a loss. Private funding of Kazan's water utility under **Russia IV** was held back because the public operator received support from other donors.

## IMPROVED SERVICE PROVISION

### Investment priorities

As in other Regions and sectors, few MDPs gave much attention to estimating economic rates of return (ERRs), either at appraisal or at completion. To be eligible for project financing, **Bosnia and Herzegovina I** did require participating municipalities to demonstrate that subprojects achieved at least 12 percent ERR, but information on the actual rates achieved was not systematically monitored. After a poor start in neglecting ERR estimates in its earlier projects, **Georgia III** ensured that all subprojects met minimum rates of return. **Kyrgyz Republic I** also reported, thanks to huge savings in operating costs, high ERRs for its urban road investments in Bishkek, Jalalabad, and Osh.

Although the project itself was barely implemented, the **Poland MDP** did lead commercial banks to require that municipalities' proposals for subprojects meet minimum ERR requirements.

Unconvincing reasons for the lack of ERR estimates in this Region are similar to those given in other Regions, such as Bank guidelines not requiring them for emergency projects and lines of credit.

### Procurement

Several MDPs gave municipalities a first opportunity to become involved in the competitive procurement of works and services, with some positive results. Under **Russia IV**, Kazan municipality voluntarily adopted local competitive bidding—not required with a structural adjustment loan—which resulted in lower-price contracts. Sole-source purchasing was reduced from 55 percent of total to 25 percent, which was better than the target of 35 percent.

The **Uzbekistan** project introduced international competitive bidding to Tashkent municipality that resulted in significant cost savings in the acquisition of a new fleet of 270 solid waste collection vehicles. **Georgia III** enabled municipalities to play a greater role in procurement than had been possible under the earlier operations, although local management there still needs to be strengthened more. More centralized political arrangements in some of the Region's countries leave procurement as a government responsibility.

### Operations and maintenance

There was little evidence of MDP attention to ongoing operations and maintenance. In **Kyrgyz Republic II**, however, each participating municipality had to adopt a prioritized five-year road maintenance program for its urban roads and streets. The **Uzbekistan MDP** established a repair and maintenance depot, generously equipped with spare parts at the outset, to keep the fleet of new solid waste collection vehicles on the road. Under the **Latvia MDP**, the lack of such a facility put the vehicles of one major Riga bus company at risk.

### Services—Most affected sectors

Among all activities undertaken, the projects performed best in improving services and related infrastructure, especially for urban street paving and drainage, neighborhood upgrading, and basic sanitation and other environmental improvements. **Georgia II** successfully completed 89 subprojects in 11 municipalities, with two-thirds of project investment in Tbilisi and three-fourths of investments in road rehabilitation and water supply. The greatest improvements were in urban road paving and clearing blocked drainage that caused periodic flooding.

Under **Georgia I**, during the country's post-independence phase, infrastructure and services were preserved and improved for power, heating, and water. The Tbilisi Metro, which is used by 90 percent of the city's population, was “rescued” through the emergency funding of signaling systems and spare parts. Dysfunctional sewerage systems in the municipalities of Batumi and Poti were restored to working order, though service levels were still short of desired goals. Restoring heating to hospitals and school buildings in five municipalities allowed continued operation throughout the winter.

**Kazakhstan II** allowed the water utility to supply good quality drinking water to 37,000 people in two municipalities. The project's

cleanup of sewage spills had an immediate health impact: between 1999 and 2002, the number of dysentery cases fell from 83 to 8, and typhoid cases fell from 83 to 0. According to the beneficiary assessment of the **Kosovo MDP**, 90 percent of respondents felt that the 115 (mostly school and water supply) subprojects implemented in 30 municipalities did respond to their needs; 84 percent were satisfied with results that they felt helped reduce water-borne diseases.

**Kyrgyz Republic I** exceeded its target by substantially improving 105 kilometers of roads, making the municipalities of Jalalabad, Bishkek, and Osh more accessible. **Latvia's MDP** helped improve drinking water quality, and untreated water was no longer being discharged into the Daugava River. The **Lithuania MDP** contributed only modestly to improvement in conditions of municipal service infrastructure, but it did help reduce street lighting energy costs in Vilnius. The **Turkmenistan** project helped increase bus and trolley services in Ashgabat, fully meeting targets, as well as contributing to enhanced reliability and frequency of services.

Wastewater collection systems and networks with 80 percent treatment were put in place in Bursa city under **Turkey I**, which led to increased service coverage between 1993 and 2000—from 93 percent to 97 percent of the population for water supply and from 73 percent to 82 percent for sewerage. Over the same period, unaccounted-for water fell from 65 percent to 45 percent. **Uzbekistan** obtained positive environmental results by helping restore Tashkent's solid waste management system. For the most part, the environmental impacts of roads, water, and solid waste subprojects of **Georgia I–III** were positive, especially through improving air and water quality in the poorer neighborhoods of the beneficiary municipalities.

### Services—Private provision

Private provision of services was relatively low among this Region's MDPs. **Kyrgyz Republic I** helped three municipalities—Jalalabad, Bishkek, and Osh—establish passenger transport authorities and plan, contract, and monitor the private provision of services. Construction is now awarded to private contractors, and major equipment has been sold to the private sector.

Under **Turkey I**, the Bursa Metropolitan Municipality contracted waste collection and landfill operations to private contractors. It also promoted private participation for meter reading, billing, and invoicing. The **Turkmenistan MDP** helped increase private participation of the suburban and intercity transport to 70 percent, but greater effort could have been made at deregulation, to allow greater competition. Under the **Uzbekistan** project, an international tender in 2003 for the private operation of Makhsustrans's Chilanzar and Shaihantaur districts of Tashkent failed to yield any bids because of doubts about the profitability of the operations without subsidies.

### Income level of beneficiaries—Poverty reduction

Only four MDPs have explicit poverty-reduction objectives. The **Kosovo MDP** broadly met its Regional poverty goals. The project directed the majority of its social services toward the disabled,

### Box 1: Key to MDPs Referred to in Text

**Armenia:** Third Social Investment Fund Project. **Bosnia and Herzegovina:** I—Local Development Project; II—Community Development Project; III—Solid Waste Management Project; IV—Urban Infrastructure & Services Project. **Croatia:** Coastal Cities Pollution Control Project. **Georgia:** I—Municipal Infrastructure Rehabilitation Project; II—Municipal Development Project; III—Second Municipal Development & Decentralization Project. **Kazakhstan:** I—Social Protection Project; II—Atyrau Pilot Water. **Kosovo:** Second Community Development Fund. **Kyrgyz Republic:** I—Urban Transport Project; II—Small Towns Infrastructure & Capacity Building Project. **Latvia:** Municipal Services Development

Source: IEG.

Project. **Lithuania:** Municipal Development Project. **Poland:** Municipal Finance Project. **Russia:** I—St. Petersburg Center City Rehabilitation Project; II—Northern Restructuring Project; III—St. Petersburg Economic Development Project; IV—Kazan Municipal Development Project. **Tajikistan:** Municipal Infrastructure Project. **Turkey:** I—Bursa Water & Sanitation Project; II—Municipal Services Project; III—Istanbul Municipal Infrastructure Project. **Turkmenistan:** Urban Transport Project. **Ukraine:** Urban Infrastructure Project. **Uzbekistan:** Tashkent Solid Waste Management Project.

women, and youth and generated 26,188 days of temporary employment. But there is less evidence on outreach to other vulnerable groups such as widows, victims of conflict, inhabitants of remote villages, and so forth.

Under **Russia IV** in Kazan, the newly created Municipal Department of Social Protection identified eligible poor recipients through the municipality's new computerized database of 23,900 assisted families to replace earlier untargeted subsidies with direct cash payments, which also produced an overall savings to the municipality. Several "one-stop shops" were created to provide these services to the beneficiaries.

### CONCLUSIONS

- By continuing to do more wholesale MDPs that emulate the successful cases in this Region, positive MDP impact can be broadened to benefit more municipalities.
- New MDPs could make better and more intensive use of simple ERR estimates to determine investment priorities and measure efficiency of results.
- M&E of new MDPs needs to be stronger than in the past, especially in measuring the achievement of objectives through quantified baselines and targets.