World Bank Iraq Trust Fund
Banking Sector Reform Project (TF094193/P113337)
September 2010

Project Summary Sheet

Title	Banking Sector Reform Project				
Implementing Agency	Central Bank of Iraq (CBI)				
Location	N/A – Institutional Support/Nationwide				
Sector code (OECD DAC)	***24010*** Financial Policy and Administrative Management ***24020*** Monetary Institutions				
Compact Priority	***4.3.3.1*** Undertake specific measures to restructuring State-Owned Banks ***4.3.3.2*** Undertake specific measures to promote private banking				
Project Cost	US$10 million				
Duration	50 months				
Approval Date	April 2009	**Effective Date**	April 2009	**Closing Date**	June 30, 2013
Project Description	The project aims to support the Iraqi authorities in the implementation of Phase I of the "Iraq Banking Reform Strategy" (2008-2012) and its Action Plan, focusing on four main components: (i) institutional and operational restructuring of the two state-owned commercial banks; (ii) financial restructuring of the two state-owned commercial banks; (iii) strengthening the regulatory and supervisory functions of the Central Bank of Iraq; and (iv) project management, monitoring and evaluation.				
Beneficiaries	The project supports the Iraqi government to build a sound banking system, able to provide efficient financial services competitively. The immediate direct beneficiaries would be the two largest state-owned commercial banks—Rafidain Bank and Rasheed Bank—which account for more than 70 percent of the banking system. Ultimately, all Iraqi businesses and citizens will benefit from an improved banking system that can provide the resources needed for Iraq's growth and offer good deposit and payment systems for businesses and households.				
Near Term Employment Creation	N/A				

Strategic Context and Donor Coordination

The donor community has been active in helping Iraq in restructuring the banking sector. The World Bank has been coordinating with all development partners involved in the banking reform, including the IMF, EU, US Treasury, and Financial Services Volunteer Corps (FSVC). The IMF has taken the lead in monetary activities and rebuilding the capacity of CBI. The US has focused mainly on the restructuring and financial audits of the state-owned banks, and helping Iraq draft an operational restructuring plan. FSVC provides technical assistance to CBI to strengthen its internal operations. The World Bank chairs an "Iraq Banking Reform Donors Group", to coordinate efforts, promote complementarity, and avoid overlap.

Project Development Objective

- Support Iraq's implementation of Phase I of the Iraq Banking Sector Reform Strategy
- Strengthen the supervisory framework for financial intermediation

Outputs, Key Activities and Procurement

Outputs	• New organizational structures for the two state-owned banks are adopted • Number of staff trained in each bank would reach at least 100 staff members • Compliance supervisory and regulatory framework (Basle Code Principles)

Activities	•	
Procurement	**Goods:** **Consultants' Services and Training:** **Incremental Operating Expenses:** **Unallocated:**	US$0.35 million US$8.90million US$0.25 million US$0.50 million

Financial Data

Funds Committed	US$1.3 million	**% approved**	13
Funds Disbursed	US$0.4 million	**% approved**	4
Forecast Closing Date	June 2013	**Delay (months)**	

Progress against Indicators

Improvement in functioning of the two state-owned commercial banks, evident in the increase in loan-to-GDP ratios from 4% in June 2006 to 6% in October 2010.	Loan-to-GDP ratios increased to reach 5% in 2009	**% of planned**	
Build-up in provision levels at the two state-owned commercial banks for new loans, reflected in the reserves-to-NPLs ratios, rising from 10% in June 2006 to 20% in October 2010.	The reserves-to-NPL ratios raised from 10% in June 2006 to reach 15% in 2009		
Capital adequacy ratio in line with prudential regulations, reaching up to 4% by October 2010.	Capital adequacy ratio reached 2% in 2009		
Number of staff trained to do bank operation	Number of staff trained to do bank operations reached 4 in 2009		

Qualitative Assessment of Project Performance

Considerable progress has been made over the past months in the implementation of the banking sector reform program. The World Bank has been providing technical support and advisory services to the Iraqi authorities. This has led to the development of a comprehensive, action-specific Banking Reform Strategy-Action plan (2008–2012), which was done in consultations with CBI, BSA, and the senior management of the two state-owned banks, which was led by the World Bank in November 2008. As a result, consensus was reached among all counterparts on a unified strategy, which became the binding document for banking reform in Iraq, and has allowed Iraqi authorities to meet the benchmark set forth by the IMF stand-by Agreement (SBA).

Good progress has been made to date towards the objectives laid out by the GOI in its comprehensive five-year Banking Reform Strategy. Despite delays in the speed of implementation and slower than anticipated disbursement due to the complex situation on the ground, the PMU has made progress in the implementation of the four components of the project. Some achievements have been made in the organizational structure and the IT infrastructure of the two state-owned banks. On organizational structure and capacity building, proposals had been received and evaluated and negotiation started in April 2010. On internal audit and compliance, technical and financial proposals were received, however all proposals were damaged because of the recent attack on CBI and PMU. On risk management, timing to publish EOI will be decided upon based on the recommendations of the organizational restructuring. On IT Training, EOI was advertised and RFP were sent to the short listed firms but due to the attack the closing dates were extended. On training of the Branch Mangers and training of Human Resources contracts, technical proposals were evaluated and World Bank's No Objection was granted but the proposals were damaged because of the attack.

On financial restructuring, the Ministry of Finance, in coordination with CBI has been working on addressing the problem of non-performing loans (NPLs). NPLs for the two state-owned banks had declined to reach ID110 billion in December 2009 (a reduction by 23 percent as of June 2007). The financial restructuring of Rasheed Bank and Rafidain Bank would be accelerated through the establishment of a Financial Restructuring Reconciliation Committee, which would be chaired by a representative from the Ministry of Finance (as the owner of state-owned banks), and comprising management of the two state-owned banks. CBI and BSA agreed to be observers, while Ernst and Young (E&Y) would be active members to guide on audit issues. This Committee would work under Restructuring Oversight Committee (ROC), and would focus on addressing the problem of external debt rather than NPLs of SOEs, which is quite negligible as opposed to the former.

CBI is currently working on its regulatory and supervisory authority. The contract with the selected consultant was signed on April 2010 and the consultant commenced his task at CBI, Baghdad on May 30, 2010. On Banking Supervision training, three institutions were short-listed but only the Central Bank of Egypt submitted their proposals before the closing date.

The project is in the midst of procuring training for branch managers of the two targeted state-owned banks (estimated cost US$630,000); training services for Human Resources; training services for the development of computer skills for staff of the two state-owned banks (estimated cost US$1.0 million); and training for risk management and internal and audit compliance (estimated cost US$1.6 million). Recently, no-objection was provided for the contract signing of the advisory and training services to the supervision department of the CBI (cost US$685,000) and hiring of an external auditor. It is expected that disbursement will increase significantly in the coming months.

Major Implementation Obstacles

Although significant progress has been made to date by the PMU in the implementation of the four components of the project, the unsettled political environment in Iraq has contributed to delays in the speed of project implementation. Disbursement has been very slow due to implementation capacity bottlenecks in Iraq, which impose long procedures in preparing and analyzing contracts, the assignment of needed consultants and training institutes, negotiation periods, and receipt of approvals from the stakeholders.

Good progress has been made in signing consultancy contracts, issuing RFPs, and receiving proposals, however the June attack caused serious delays that affect the progress in implementation. The PMU had reallocated themselves to a temporary location but cannot function efficiently because of the tight security around that alternative location. The PMU will need to reallocate again to a new location within the Rafidain Bank—HQ close to the CBI location. The June 13, 2010 attacks led to the destruction of all records, including procurement and financial management records, as well as PMU equipment. The World Bank explored areas in which further support can be provided to CBI in procurement of office equipment and furniture for the PMU, to resume working in an efficient business environment, replacing the destroyed assets.

Furthermore, capacity-building activities such as technical training are behind schedule and the lack of interest by international consulting firms and individuals to work in Iraq remains a challenge. However, we are anticipating the signing of a number of contracts during the coming period but most of these contracts have six month duration which will not be fulfilled by the original closing date of October 31, 2010. Hence, the World Bank cannot provide its no objection to these contracts as they go beyond the closing date. Moreover, the unstable security conditions have also impacted the project, including the attacks on the CBI on June 13, 2010 which led to damage of the PMU office (furniture, documents and equipments), hence the need for a project extension to June 30, 2013 to ensure full implementation of the project's key components.