



Project Validation Report

Reference Number: CAM 2008-06
Project Number: 30327
Loan Number: 1741
July 2008

Cambodia: Rural Credit and Savings Project

Operations Evaluation Department

Asian Development Bank

ABBREVIATIONS

ADB	–	Asian Development Bank
BME	–	benefit monitoring and evaluation
CAS	–	Cambodian accounting standards
EA	–	executing agency
LFI	–	licensed financial institution
MFI	–	microfinance institution
NBC	–	National Bank of Cambodia
NGO	–	nongovernment organization
OED	–	Operations Evaluation Department
PCR	–	project completion report
RDB	–	Rural Development Bank
SERD	–	Southeast Asia Department
TA	–	technical assistance

Key Words

adb, asian development bank, cambodia, rural credit, poverty reduction, interest rates, lessons, operations evaluation department, ratings

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PROJECT COMPLETION REPORT VALIDATION

A. Basic Project Data		PCR Validation Date:	25 February 2008	
Project Number:	30327		Appraisal	Actual
Project Name:	Loan 1741-CAM: Rural Credit and Savings Project	Total Project Costs (\$ million):	26.56	4.94
Country:	Cambodia	Loan/Credit (\$ million):	20.00	3.74
Sector:	Finance	Cofinancing (\$ million):	3.84	0.02
Financing (\$ million):	ADF: \$20.0 million	Borrower Contribution (\$ million):	2.72	1.18
	OCR: –	Board Approval Date:	27 Apr 2000	
Cofinanciers:	Licensed financial institutions (LFIs)	Closing Date:	29 Mar 2006	25 Oct 2006
Project Officers:	Name: S. Tukuafu	Designation: Southeast Asia Department (SERD) Cambodia Resident Mission	From	To
	V. Hem			
Evaluator: Quality Control Reviewer:	S. Thalakada, Staff Consultant C. Kim, Sr. Evaluation Specialist	Director:	Ramesh B. Adhikari, OED2	

B. Project Description (summarized from the report and recommendation of the President)

- (i) **Rationale and expected impacts.** About 90% of the country's poor lived in rural areas. The poverty incidence was estimated at 36% for the whole country and 40% for rural areas. The limited availability of and access to rural credit and rural savings schemes were major constraints to livelihood development and reduction of rural poverty. No formal financial services existed in rural areas, and rural households relied on informal money lenders and middlemen who charged high interest rates. The unmet demand for rural credit was estimated at between \$50 million and \$100 million. There was an urgent need to strengthen financial services for development of livelihood projects and thereby help reduce poverty, particularly in rural areas.
- (ii) **Objectives or expected outcomes.** The project sought to develop an effective financial services system in rural areas that would increase the supply of and improve access to rural credit and sustainable savings facilities by poor households. These were to be achieved through a private sector initiative by nongovernment organizations (NGOs), which had demonstrated viable credit delivery systems and achieved substantial outreach. The credit to be provided under the loan through these NGOs was expected to facilitate the development of income-generating activities and thereby facilitate poverty reduction.
- (iii) **Outputs.** The project was designed to (a) directly benefit about 260,000 households in rural areas; 70% of beneficiaries were poor, and about 50% were rural women. The subprojects to be financed under the loan were assessed to be viable, with financial internal rates of return from 23% to 91%, and economic internal rates of return from 13% to 62%; (b) expand operations of licensed financial institutions (LFIs); (c) establish a voluntary and sustainable savings mobilization scheme for the rural poor; (d) develop the Rural Development Bank (RDB) as an effective project manager and provider of funds for rural finance, including the development of a benefit monitoring and evaluation (BME) system, and a revolving fund for recycling loan repayments for providing further rural credit; and (e) strengthen the National Bank of Cambodia (NBC) (the central bank) to provide an effective system for regulating and supervising rural financial services.
- (iv) **Principal activities.** Activities included (a) provision of microcredit to finance income-generating subprojects; (b) consulting services to support rural credit and savings schemes of LFIs; (c) technical assistance (TA) related to project management support for RDB, which was to channel the loan to the LFIs; and (d) support to NBC for regulation and supervision of LFIs.

C. Evaluation of Design and Implementation (project completion report assessment and validation assessment)

- (i) **Relevance of design and formulation.** The design and formulation was relevant at appraisal and at entry. The Project was intended to help implement the Government's policy and strategy relate to expansion of rural credit and mobilization of savings for poverty reduction. It was also in line with the key development objective of poverty alleviation of the Asian Development Bank (ADB). The Project was formulated with ADB TA, but there was no lesson from previous projects to be considered as this was ADB's first rural finance activity in Cambodia. The project completion report (PCR) stated that "certain assumptions were rather ambitious—resulting in an overestimation of the total loan amount and an underestimation of the time required for LFIs to be transformed from NGOs to legal corporate entities in order to meet the NBC's licensing requirements". The net result was that it took a long time for LFIs to be set up and become eligible participants. The demand for subloans from the LFIs that became eligible was also low, leading ADB to reduce the loan from \$20 million to \$5 million in December 2002, canceling the balance of \$15 million; the expected outreach was reduced from 260,000 rural households to 65,000. The partial loan cancellation was undertaken in an effort to avoid payment of loan commitment fees after the loan became effective.
- (ii) **Outputs and costs as envisioned during appraisal as compared with actual costs and achievement of outputs; reasons for any deviation.** Actual outputs fell far short of the appraisal estimates, due to cancellation of a significant portion of the loan as noted above. Specifically: (a) only \$3.74 million of the loan was utilized, meaning 81% of the original \$20 million loan and 25% of the revised \$5 million loan were not utilized. The number of household beneficiaries was reduced to 38,068 (including 79% women, compared with the target of 50%), 85% less than the appraisal estimate of 260,000, and 41% less than the revised estimate of 65,000. However, there was a large shortage of rural credit. At the end of June 2006, loans by licensed and registered microfinance institutions (MFIs) (using other funding sources) equaled KR274,686 million (\$67 million), allocated to 398,058 borrowers; (b) LFIs could not further expand their operations due to the ADB loan reduction, and at financial loan closing in October 2006, only five MFIs (out of about 40 eligible microfinance operators) and two banks had become eligible LFIs, and benefited from the ADB facility administered by RDB. As of that date, they had loaned just \$4.94 million (including the ADB loan of \$3.74 million and a revolving fund); (c) support was given for institutional strengthening of RDB, but it did not establish systems for voluntary savings (apparently due to lack of clear instructions and formal approval of NBC), BME (due to problems of recruiting consultants), and a revolving fund; and (d) NBC's regulatory and supervisory framework for MFIs and LFIs was strengthened, which was a positive aspect. In summary, the objectives of the Project relating to poverty reduction, establishment of a savings scheme for rural poor, and institutional strengthening and capacity enhancement were not achieved to the extent expected at appraisal.
- (iii) **Project cost, disbursements, borrower contribution, and conformance to schedule.** The project cost at completion was less than the appraisal estimate due to the reduced size of ADB loan as shown below:

Table 1: Comparison of Project Cost at Appraisal and Completion

(\$ million)		
Component	Appraisal Estimate	Actual at Completion
A. Base Case		
Credit for Subprojects	24.32	4.73
Operational Support for LFIs	1.12	0.03
Project Management Support	0.47	0.07
B. Contingencies		
Physical Contingencies	0.16	0.00
Price Contingencies	0.07	0.00
C. Interest Charge		
	0.42	0.11
Total	26.56	4.94

Source: Project Completion Report

With the cancellation of \$15 million of the ADB loan, the project cost at completion of \$4.94 million was financed by ADB loan disbursements (\$3.74 million) and the revolving funds held by the borrower (NBC) (\$1.18 million) and LFIs (\$0.02 million). The ADB loan disbursement was in respect of credit lines for LFIs (\$3,547,275), vehicles and equipment (\$79,095), and interest paid (\$108,863). The loan became effective in March 2001 and was to be implemented over 5 years, with loan closing in March 2006. However, implementation was delayed for the reasons given earlier; over a period of about 5.5 years, only the amount remaining after loan cancellation could be used, and the loan closed in October 2006.

(iv) Implementation arrangements, conditions and covenants, and related technical assistance.

Implementation arrangements were satisfactory. However, as the Executing Agency (EA), RDB was expected to act as a wholesale banking institution to provide funds to LFIs, but began to retail funds directly to borrowers as well in contravention of the agreement with ADB (later withdrawn by ADB), and was thus competing with other LFIs. NBC was the EA for developing the regulatory framework for licensing MFIs and the prudential supervision of LFIs, including licensed and registered MFIs. The PCR stated that NBC performed the designated tasks adequately.

The loan conditions, covenants, and the status of compliance with them were given in Appendix 2 of the PCR. They were designed to cover environmental, social and financial aspects. However, an important financial covenant not included by ADB required participating LFIs to prepare and present their financial statements in accordance with internationally accepted accounting standards. The financial positions of five beneficiary MFIs (Thaneakea Phum, Seilanithih, Cambodia Entrepreneur Building, Amret, and Hattha Kaksekar) and two banks (Acleda and Canadia) for the financial year ending 31 December 2005 were audited by independent and reputable auditors (local subsidiaries of internationally reputable accounting firms operating in Cambodia), but they were prepared and presented in accordance with Cambodian accounting standards (CAS) and guidelines issued by the NBC, with qualifications as follows: "The accounting principles applied may differ from generally accepted accounting principles adopted in other countries and jurisdictions. The accompanying financial statements are therefore not intended to present the financial position and results of operations and cash flows in accordance with accounting principles and practices generally accepted in other countries and jurisdictions other than Cambodia". The PCR stated that the covenant that required RDB to maintain a revolving fund was "complied" with, but ADB Operations Evaluation Department (OED) is of the view that it was "partly complied" with, because although the fund was established, part of it was returned. Also, the PCR stated that the covenant regarding recruitment of consultants for accounting systems, information and BME was "partly complied" with, but OED is of the view that it was "not complied" with (see below).

The consulting services provided under the Project to support the project management unit in project implementation were only partially used due to the reduced size of ADB loan and recruitment delays. Similarly, the TA associated with the Project did not fully serve the intended purposes. Some institutional strengthening of the NBC took place, through establishment of a regulatory and supervision framework for MFIs. The consultants assisted RDB and the LFIs in developing rural credit and savings products, and environmental screening procedures, but these were not implemented. Also, there were changes in activities, with less emphasis given to strengthening the capacity of MFIs in financial management and banking than planned initially, and more given to strengthening RDB's capacity for assessment of wholesale credit. Other important components of the Project were also not implemented, as indicated earlier, with the result that opportunities for institutional strengthening and capacity enhancement were lost. The procurement of vehicles, equipment, and some small civil works for RDB followed ADB's *Guidelines for Procurement* and was done in a timely manner.

(v) Performance of the borrower and Executing Agency. The Government was able to onlend the ADB loan (via the RDB) only through NGOs registered as LFIs and MFIs. The registration and licensing processes began with the Project, and the borrower and EA lacked prior experience with them. They explored ways to streamline the registration and licensing process in order to bring these MFIs into the formal sector, but the results of their efforts in the sector generally followed cancellation of a majority of the ADB loan. To minimize delays in loan utilization, the borrower and EA could have been more proactive in expediting procedures (through the Registrar of Companies and Ministry of Commerce) that enabled NGOs to be converted into corporate entities, and thus become eligible LFIs. They could also have helped recruit and field consultants to provide the planned consulting and TA services for institutional strengthening, capacity enhancement, and project implementation. They also failed to implement other vital TA components (e.g., recruitment of

consultants for accounting and BME systems). Hence, OED rates the performance of the Borrow and EA in the Project “partly satisfactory”. Paragraph 31 of the PCR noted that NBC’s subsequent efforts to license and supervise the MFIs were successful, and about 40 MFIs were in operation at project closing. However, the Project’s direct contribution in this regard cannot be measured and is considered limited, as only five MFIs became participants under the ADB loan, due to the loan’s partial cancellation in December 2002.

- (vi) **Performance of ADB.** OED rates ADB’s performance “partly satisfactory”. The formulation of the Project by ADB was inadequate in two vital respects. First, ADB should have anticipated that it would be time consuming and difficult for NGOs to convert to corporate entities (and thus become eligible loan conduits), due to the costs involved, the need to form legal entities (with shareholders, boards of directors, and capital structures), and the cumbersome and time-consuming procedures (preparation of memoranda and articles of association, and the registration process). In such circumstances, it would have been prudent to have deferred loan effectiveness or to have provided assistance to initiate the conversion process earlier, which would have enabled the Project to avoid long implementation delays and the need to dramatically reduce the size of the loan. Second, ADB should have performed a better market and demand analysis, and been aware of the various constraints to creation of new demand for an ADB loan. This failure resulted in a lost opportunity, in terms of not being able to finance other livelihood development projects, and reduce the incidence of poverty in the country.

D. Evaluation of Performance (validation assessment)

- (i) **Relevance.** The design and formulation were relevant at appraisal and at entry. The project was designed to support the Government’s promotion of rural development, as outlined in Cambodia’s National Development Plan 1996–2000, and was in line with ADB’s operational strategy for rural development. However, certain assumptions were ambitious, resulting in an overestimation of the total loan amount and an underestimation of the time required for LFIs to be transformed from NGOs to legal corporate entities, as required to meet NBC’s licensing requirements. The Project’s relevance decreased due to implementation delays, which reduced demand for the ADB loan facility compared with the appraisal estimate. Combined with the growing burden of the loan commitment fees, the reduced demand led ADB and the Government to cancel 75% of the original \$20 million loan, reducing the expected outreach to only 65,000 households (25% of the original estimate). At loan closing in October 2006, the loan facility ultimately used only \$3.84 million (19.2% of the original amount). The consulting services were cancelled and the TA component not fully used. Thus, the selected design of the Project—in terms of poverty reduction, increased savings mobilization among the rural poor, and institutional strengthening and capacity enhancement—was not as relevant as it could have been in addressing development needs. Therefore, with the above shortfalls combined, the Project is rated “partly relevant” by OED.
- (ii) **Effectiveness in achieving outcome.** The OED rates the Project “less effective” in achieving the envisaged outcome. Only 38,068 households were assisted with livelihood development subprojects against the appraisal estimate of 260,000. Thus, the impact on poverty reduction was low compared with that envisaged at appraisal. Also, components such as a voluntary savings scheme for the rural people, a fund for recycling of loan repayments for further rural development, and a subproject BME system were not established. Hence, poverty reduction and institutional strengthening and capacity enhancement were not achieved to the extent envisaged at appraisal.
- (iii) **Efficiency in achieving outcome and outputs.** The OED rates the Project “less efficient” in achieving outcome and outputs. The PCR did not rate the Project as a whole under this efficiency criterion. It only rated the performance of individual institutions such as the NBC and RDB. There was considerable delay in the implementation of the Project at its early stage. It took the same amount of time (about 5 years) as envisaged at appraisal to help only 38,068 households against the appraisal estimate of 260,000 households, and utilize only \$3.74 million of the original loan of \$20 million for that purpose. Over that same period, a majority of the consulting portion of the project was canceled, and only a portion of the TA utilized.
- (iv) **Preliminary assessment of sustainability:** OED assesses the sustainability of the Project “less likely”. The viability of the assisted subprojects after implementation was not known. The PCR does not appear to have carried out a baseline field survey of even a sample of assisted subprojects in an independent

manner to assess their financial and economic viability to ensure sustainability, but it did undertake a financial analysis of LFIs. It stated that “the reported repayment rates were above 95%”, although the sources of cash flow for such repayments were not stated, including whether they were made through funds generated by the assisted subprojects, or using funds from other sources. Such information is vital to judge the viability of the subprojects and their sustainability. Only five MFIs out of about 40 eligible microfinance operators became eligible LFIs over the 5-year implementation period, in addition to the two banks. Thus, the Project’s objective to expand LFI operations was not achieved. With such a drastic reduction in the project scope, the sustainability of the Project as originally designed became doubtful. The financial statements of the five MFIs and the two banks were prepared and presented in accordance with CAS, and were qualified as mentioned earlier. It is not known whether the assisted subprojects survived following establishment; their present status, viability and sustainability are also unknown. Therefore, while the LFIs appear financially viable, it was not possible for OED to judge their viability and sustainability based on the information provided by the PCR. The institutional strengthening and capacity enhancement of NBC and RDB that was achieved through the Project should help to some extent in developing a sustainable rural credit system for the country to facilitate poverty alleviation.

- (v) **Impact (both intended and unintended).** The Project had a limited impact compared with the appraisal expectation. The impact on poverty reduction was not that significant, as only 38,068 households were assisted in developing livelihood projects. A positive aspect was that about 79% of the recipients were women compared with the appraisal target of 50%. A baseline survey was not conducted, making it impossible to accurately estimate the number of assisted enterprises that have survived (the casualty rate of micro enterprises is normally high), their viability status, and the actual contribution being made by them towards poverty reduction through continuous income generation. Such a survey would have also shown the impact made by the assisted projects on the environment during their actual operations. BME-based results were also not available, as the system was not established. There was some impact on institutional strengthening and capacity enhancement in NBC and RDB.

E. Overall Assessment, Lessons, and Recommendations (validation assessment)

- (i) **Overall assessment.** The Project was rated “partly successful”, compared with the PCR rating of “successful”:

Table 2: Overall Performance Assessment

Criterion	Weight (%)	Rating Value	Rating
1. Relevance	20	1	0.2
2. Effectiveness	30	1	0.3
3. Efficiency	30	1	0.3
4. Sustainability	20	1	0.2
Total Rating			1.0

Rating value: Relevance: highly relevant 3.0, relevant 2.0, partly relevant 1.0, and irrelevant 0. Effectiveness: highly effective 3.0, effective 2.0, less effective 1.0, and ineffective 0. Efficiency: highly efficient 3.0, efficient 2.0, less efficient 1.0, and inefficient 0. Sustainability: most likely 3.0, likely 2.0, less likely 1.0, and unlikely 0. Highly successful: overall weighted average is greater than 2.7; successful: overall weighted average is between 1.6 and less than 2.7; partly successful: overall weighted average is between 0.8 and less than 1.6; and unsuccessful: overall weighted average is less than 0.8.

Source: ADB. 2006. *Guidelines for Preparing Performance Evaluation Reports for Public Sector Operations*. Manila.

(ii) Lessons

(a) There were long delays in starting the Project and dispensing ADB loans to subborrowers, because eligible on-lenders could not be easily identified, and adequate regulations, controls, and supervision were not in place. Future projects should avoid these problems.

(b) The majority of the ADB loan was canceled and the project scope was reduced from \$20 million to \$5 million. This was due in part to lower-than-expected demand for the Project's funding (grants and other donor funds were available at more competitive terms, and demand from financial intermediaries for ADB funds was low), and in part because of the Government's growing commitment fee burden, which began with loan effectiveness. Demand increased after most of the ADB loan was canceled. Future microfinance projects, especially in the field of rural credit for the poor, should consider these factors in their demand analysis.

(iii) Recommendations

(a) In light of lessons (a) and (b) above, on-the-ground realities and market conditions should be taken into account in the design and formulation of projects.

(b) In light of lesson (b) above, ADB in similar situations should consider assisting policy reform, institutional strengthening and capacity enhancement, and financial infrastructure development in the rural credit field rather than lending funds directly for the rural credit.

(c) The loan covenants package should be more carefully packaged to strengthen safeguards and ensure project sustainability.

F. Monitoring and Evaluation Design, Implementation, and Utilization (validation assessment)

Subloans and subprojects were monitored by LFIs, and LFIs monitored by NBC and RDB. RDB submitted quarterly performance reports to ADB, and ADB carried out regular supervision missions. However, the PCR should have carried out an independent survey of a cross-section of subloans and subprojects to assess their viability and sustainability. For similar purposes, the financial statements of the LFIs should have been prepared and presented in accordance with internationally accepted accounting standards. In their absence, it was not possible for OED to judge the effectiveness of the monitoring and evaluation system.

G. Other (safeguards, including governance and anticorruption; fiduciary aspects)

The project management unit maintained a separate account for expenditures and all other financial transactions under the Project. It was to be in accordance with generally accepted accounting procedures in Cambodia and to be audited annually by external auditors satisfactory to ADB. The PCR did not mention whether these audits had been done or what the results were. Hence, OED was not in a position to comment on the fiduciary aspects of the Project. The survey referred to earlier could have also verified whether the subprojects carried out the required environmental safeguards. In the absence of such evidence, OED was unable to comment on this issue.

H. Ratings:	PCR	OED Validation	Reason for Disagreement/Comments
Relevance:	Relevant	Less relevant	The Project's relevance at entry decreased as only 19% of the original loan was utilized; consulting services were not used to set up an MIS, accounting systems, and a BME system; and use of TA was limited. NBC and RDB were partially strengthened.
Effectiveness in Achieving Outcome:	Effective	Less effective	The Project's effectiveness was limited, as 81% of the approved loan was not utilized and only 15% of the originally envisaged beneficiary households were actually assisted; consulting services not used; and use of TA was limited.
Efficiency in Achieving Outcome and Outputs:	Did not assess the efficiency of the Project as a whole	Less efficient	The Project was less effective because of the considerable delay, especially at the early stage of project implementation. Actual implementation took the 5 years, as envisaged at appraisal, but used only 19% of the loan and financed only 15% of the households envisaged at appraisal.
Preliminary Assessment of Sustainability:	Likely	Less likely	Given the drastic reduction in the project scope, the potential for project sustainability as originally designed became very limited. It was not possible to judge sustainability of the assisted subprojects as a field survey to assess their actual viability was not carried out.
Borrower and EA:	Satisfactory	Partly satisfactory	The Borrower and EA should have played more proactive roles to reduce implementation delays and ensure greater utilization of the loan, and consulting and TA services, as originally planned. The MFIs were ultimately implemented and supervised, but most did not participate in the ADB loan, as the majority of the loan had already been canceled.
Performance of ADB:	Satisfactory	Partly satisfactory	The Project's design and formulation was flawed, resulting in initial implementation delays and severe underutilization of the loan and consulting and TA services. ADB subsequently intervened to address problems based on the substantially reduced scope. Overall, ADB's performance was partly satisfactory.
Impact:	Stated that 79% of women benefited against 50% target; repayments reported to be 95%; LFIs carried out due diligence on environmental safeguards to be adopted	Unable to rate	The impact on poverty reduction and institutional strengthening and capacity enhancement was limited, as compared to that envisaged at appraisal. The expected impacts of the voluntary savings scheme and revolving fund were not realized as these were not established. Some strengthening of NBC and RDB took place, which should help future rural credit schemes. Most households assisted (79%) were women beneficiaries, compared to the 50% appraisal target.
Overall Assessment:	Successful	Partly successful	The overall Project was partly successful. It suffered from long implementation delays, significant underutilization of the loan, and largely unused consultancy and TA services. Accordingly, relevance decreased and poverty reduction was achieved only to a limited extent.
Quality of PCR:		Partly satisfactory	See the comments on the PCR quality below.

I. Comments on PCR Quality:

- (i) The PCR guidelines (PAI 6.07)^a require that project performance be assessed against the original project design and scope at appraisal. However, the PCR seems to have assessed project performance, at least in part, against the significantly reduced project scope at the later stage of its implementation.
- (ii) The PCR should have carried out a survey of subprojects to assess their sustainability, made a thorough evaluation whether the subprojects made their loan repayments using internally generated cash or with other sources of funds, and should have been supported by evidence from field survey and analysis (see lesson no. (iv) and para. 51 of the PCR).
- (iii) In view of above, the analysis in the PCR could have been strengthened.
- (iv) The rating on efficiency in achieving outcome and outputs evaluated only the individual institutions involved, instead of the Project as a whole, as required.

^a ADB. 2006. *Project Administration Instructions*. PAI 6.07: Project Completion Report. Section 6: Internal Procedures and Reports. Manila.

J. Need for Project Performance Evaluation Report

Considering the small size of the utilized loan amount (\$3.74 million against the \$20 million planned) and the substantially limited outcomes of the Project, a project performance evaluation report is not recommended.

REGIONAL DEPARTMENT'S RESPONSE TO THE PROJECT COMPLETION REPORT VALIDATION REPORT

On 18 February 2008, Director, OED2, Operations Evaluation Department (OED), received the following comments from the Governance, Finance, and Trade Division, Southeast Asia Department (SERD).

SERD appreciates OED's efforts to produce an independent validation report on the completed Loan 1741-CAM. Since the validation exercise, undertaken by an independent consultant commenced only after the PCR had been finalized, in hindsight, an independent consultation with the beneficiaries of the project could have better explained the differences in rating. The validation report is based purely on the PCR and additional information provided by SERD.