Ex post evaluation – Moldova

Sector: 32130 Small and medium-sized enterprises (SME) development
Project: Support of MSMEs through participation in a Moldovan bank - Tranche I (BMZ No. 2010 67 040) and Tranche II (BMZ No. 2013 67 333*)
Implementing agency: A bank in Moldova

Ex post evaluation report: 2016

		Project I (planned)	Project I (actual)	Project II (planned)	Project II (actual)
Investment costs (total)	EUR million	1.00	1.00	1.00	1.00
Counterpart contribution	EUR million	-	-	-	-
Funding	EUR million	1.00	1.00	1.00	1.00
of which budget funds (BMZ)	EUR mill	1.00	1.00	1.00	1.00

*) Projects in the 2016 random sample

Summary: As part of both projects, FC trust funds totalling EUR 2 million were provided in two tranches (EUR 1 million in March 2011 and EUR 1 million in December 2013) to increase equity capital at a Moldovan bank. As part of the previous project (BMZ No. 2006 66 180), FC supported the bank's initial capitalisation in 2009 with roughly EUR 1.7 million. Since the capital increases, the bank has expanded its portfolio in the area of micro, small and medium-sized enterprises (MSMEs), and has also managed to obtain further funding.

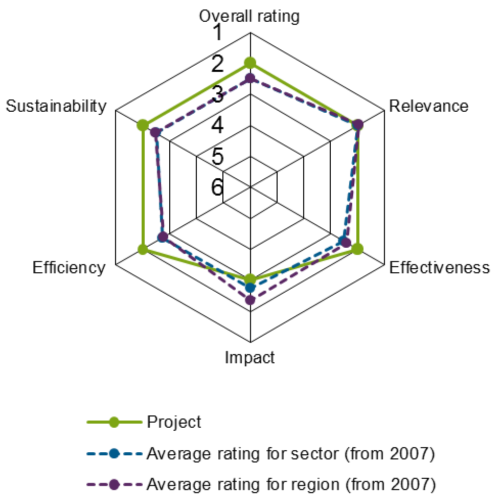
Objectives: Strengthening the bank's capital base was designed to mobilise additional funding through accumulating further deposits from the local population or obtaining long-term loans from private and public investors (leverage), as well as to deepen and strengthen the bank's promotional activities. Indirectly, the bank's stronger capital base was to lead to a sustained improvement of access to loans and other financial services for MSMEs as well as low and medium-income households, particularly in rural Moldova.

Target group: MSMEs and private households in Moldova.

Overall rating: 2

Rationale: In recent years the bank generated good and stable returns on capital and is well-positioned thanks to rigorous streamlining and a modernisation of operations. It succeeded in increasing the volume of both its portfolio and deposits, despite the economic crisis in the country. That said, the crisis did lead to a substantial rise in default rates at the bank in 2015.

Highlights: Since 2015 the bank has served its original target group of the smallest companies only to a marginal extent. The increase in the average loan size is understandable from an efficiency perspective, but makes it more difficult for micro enterprises to access the financial market.



Rating according to DAC criteria

Overall rating: 2

Overall context

The ex post evaluation report comprises the first tranche (of equity participation)(BMZ No.: 2010 67 040, paid in 2011) and also includes the second tranche in 2013 (BMZ No.: 2013 67 333). FC had previously supported the capitalisation of the bank with approximately EUR 1.7 million back in 2009 (BMZ No.: 2006 66 180).

Relevance

A whole series of indicators show that at the time of the project appraisal in 2010, the Moldovan financial sector was still significantly underdeveloped, particularly for micro, small and medium-sized enterprises (MSMEs), and still is today. The share of loans to the private sector relative to the gross domestic product was 39% in 2014, compared to an average of 69% across South-Eastern Europe. While the World Bank's Doing Business report believes access to funding to be a problem of medium importance when considering all types of companies, the Institute of Economy, Finance and Statistics in Chişinău asserted in a 2012 survey[1] that access to funding is by far the problem most frequently cited by small and medium-sized enterprises in Moldova. It also notes that this result has been consistent across all studies carried out over the last 15 years. This particularly applies to the availability of long-term loans. In addition to this quantitative bottleneck, there was and still is a qualitative bottleneck, i.e. an inadequate range of products that are mainly aimed at the traditional bank clientele of established large and medium-sized enterprises and a banking sector that lacks not only an interest in, but also the expertise required for dealing with the needs of smaller business. The project focused explicitly on the core problem, i.e. the need for long-term funding of MSMEs and financial products for poorer private households in the urban and rural areas of Moldova, and essentially integrates well into the country's financial sector strategy.

These projects are continuations of the first project (BMZ No. 2006 66 180) which, by means of an increase in equity capital in 2007 (EUR 1.7 million) and in personnel support (EUR 0.8 million), supported the bank (project-executing agency) in transitioning from an informal financial institution to a bank. However, in the context of the current increases in capital, the challenges proved to be different due to the economically and politically difficult environment characterised by bankruptcies, raider attacks on banks (hostile takeover attempts) and high political instability. In this difficult environment, the capital increase in two stages was supposed to strengthen above all the bank's reputation as a reliable institution with Western European roots and a double bottom line approach. The project was of great relevance in relation to the problems in the country's financial sector and in relation to the MSME sector. Overall, we therefore assess the relevance of the project as good.

Relevance rating: 2

Effectiveness

The attainment of the project objectives defined at the project appraisal can be summarised as follows:

Indicator	Ex post evaluation
(1) Bank operates sustainably and shows positive year-end results from 2011 onwards.	Achieved. Year-end results from 2011 are positive and on an upward trajectory.

1 Institute of Economy, Finance and Statistics (IEFS): SME's contribution to employment in the Republic of Moldova: Quantitative and qualitative assignment, Chisinau 2013.

(2) The outstanding gross loan portfolio of the project-executing agency is growing by 25% annually (in volume and number) within three years of the capital increase.	Partially achieved. Growth of the loan portfolio compared to previous year by volume (number) in lei: 2011: 36.4% (-0.6%) 2012: 37.1% (25.8%) 2013: 17.6% (8.5%) 2014: 2.7% (-16.6%) 2015: -3.9% (-33.4%)
(3) At least 70% of end loans granted are < EUR 10,000.	Partially achieved. Share of loans < EUR 10,000 in 2015: 71% Share of new loans < EUR 10,000 2012: 82.4% 2013: 79.9% 2014: 64.0% 2015: 38.7%
(4) The share of sub-loans with interest and principal arrears of over 30 days (non-performing loan portfolio) is a maximum of 7% (portfolio-at-risk).	Partially achieved. No longer met in 2015 (8%), under 7% in all previous years.

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the five years since the first capital increase, the implementing agency has made enormous progress in streamlining and modernising operational activities (see also Efficiency). This process includes, in particular, an increase in the average size of loans granted by the bank. The fact that consistent and steadily-growing annual net profit has been achieved from 2011 onwards despite the difficult environment shows, however, that the positive results of the bank are not only attributable to this change in the target group. The bank even set aside reserves for the first time in 2015.

The second indicator, the growth of the portfolio, was exceeded in the three years following the first capital increase, as measured by the volume of the portfolio. However, the target number of loans was not met. Following 2013, after the second capital increase, there was no further growth as measured by volume; the number of loans actually declined significantly while the average volume grew. This is partly attributable to the difficult environment from 2013 onwards, with the decline in the number of loans also being attributable to the above-mentioned realignment of the strategy. From the perspective of the evaluation, an indicator of 25%, which requires the type of rapid and consistently faster growth that typically occurs during the initial phase after a foundation, is no longer suitable for the phase of portfolio consolidation. We consider the growth up to the present time to be appropriate, taking into consideration the economic environment and the fact that the institute was no longer in the dynamic initial phase.

The third indicator – the share of small loans under EUR 10,000 – has been met as measured against the existing overall portfolio. However, the volume of new small loans has fallen significantly short of the target value of 70% since 2014 (64%) and 2015 (39.4%). The average size of new loans rose sharply in 2015 to EUR 33,188 (2013: EUR 10,332). Although smaller loans are not fundamentally excluded in the bank's policy - if they prove promising in a credit assessment based on qualitative criteria - the bank’s future focus will be on loans of more than EUR 30,000. In the wake of the bank’s new strategy, the original main target group of the project will be reached only to a limited extent. It should be noted, however, that as evidenced by on-site spot tests, loans between EUR 30,000 and EUR 100,000 still go to relatively small companies which tended to have well below 30 employees (see also Impact).

The fourth indicator – no more than 7% of loans in delinquency of more than 30 days (PAR 30) – was not achieved in 2015 with a PAR 30 of almost 8%. This was due to the difficult economic environment, which was mainly attributable to an embargo on Russian imports, the economic collapse of Russia and the significant reduction in the numbers of foreign workers, particularly from Russia. However, the maximum share of delinquent loans was significantly lower than in the previous years. The lowest delinquency rates (2015) were lowest among the small loans of between EUR 10,000-50,000 (4.7%), while the rate was highest (12%) for medium-sized loans (EUR 50,000-250,000). In the case of large loans above 250,000, the rate stands at 7.5%, while it has risen from almost zero to 6.2% for very small loans of less than EUR

10,000 in the last few years. The country average, for which we only know the PAR 90 value, is 12%. The financial intermediary's PAR 90 ratio stands at 6% here. When assessing effectiveness and portfolio quality, it must be borne in mind that in recent years, five of the 16 banks in Moldova had to declare bankruptcy, and a further three (the three largest) have been placed under the supervision of the central bank in response to unfair practices. In this extremely difficult environment, the implementing agency continues to serve as a kind of beacon.

Deviating from the project objectives, the financial intermediary has, from the outset, not regarded households as its actual target group for awarding loans, with the notable exception of energy-efficiency projects. This focus has even been reinforced over the course of time, due to the fact that the bank believes that companies operating out of households in Moldova are more likely to belong to the shadow economy and often pursue unlawful or semi-legal transactions that it does not want to support. For these reasons the bank nowadays accepts credit applications only from officially registered companies. Other services, such as current and savings account balances, as well as access to ATMs, are also open to households, although the primary target group here is also MSMEs.

Although the ambitious growth targets have not been met, we assess the overall effectiveness to be only just good, as the bank has served the target group in an extremely difficult environment while achieving an acceptable portfolio quality. This is true despite the fact that the bank's strategy has been focused on larger loans since 2015.

Effectiveness rating: 2

Efficiency

The number of employees fell significantly from 455 in 2010 (and 565 in December 2012) to 194 in December 2015. This reduction was accompanied by a large-scale streamlining of business processes. A total of 23 branches (2010) were converted into 13 service points and just one branch. An automated 24/7 zone is available in all service points, and most also have two or three remaining employees who are seated in such a way that they can directly view the automated area and provide customers with assistance if necessary. In particular by automating services in the service points, the bank has achieved considerable efficiency gains and thus also fulfils a pioneering role in the country. This includes not only traditional ATMs, but also personnel-assisted deposits and the execution of further banking transactions (e.g. interest payments, credit notes, transfers). The Business Client Advisors are located in the bank's headquarters and are assigned to specific sectors (i.e. they operate throughout the country); major retail branches have been closed. According to the management, this did not result in a worsening of the service on offer – the central support of loan customers proved to be even more personalised thanks to the specialisation of the loan managers. This development was made possible by the fact that the number of new small loans granted in particular declined in 2015, resulting in a greater level of consultancy support among the remaining loan customers. This strategy allowed profits to be boosted.

Measured by volume, the bank has moved up the rankings from eleventh place among 16 banks to fifth among 11 banks (note that the three largest banks are in a critical condition under direct central bank supervision), which is also indicative of the relative attractiveness of the bank's range of services. The capital adequacy is above the required 16%, at between 20% and 24%. The number of loans and the amount of credit per employee have increased significantly and the cost-income ratio has improved greatly from 81% (2011) to 54%. The provisions for non-performing loans are also appropriate, at 77% of the PAR 30 portfolio.

Overall, production efficiency can be rated as very good.

The target group of MSMEs (and private households with regard to deposits and other services, but excluding loans) was reached over the course of the project by means of target-group-appropriate products, which were increasingly offered; despite this fact, significantly fewer small loans have been issued since 2015. Above all, it was possible to increase the volume of customer deposits more than three-fold from 2010 to the end of 2015, which has significantly improved the funding base. Following marked fluctuations, the number of customers with cash, savings and term deposits increased from 38,000 to 56,000 during this period: the figure initially rose to over 77,707 (2013), before falling to 45,049 (2014) and finally settling at the current value of 56,000 in 2015. The average deposit level increased by almost 30% in local currency during this period, but fell from EUR 1,930 to EUR 1,744 when calculated in euros.

According to its own reports, the bank is the only one to offer MSME loans with terms of up to ten – and in exceptional cases up to twelve – years. Responsible finance is an important aspect of employee training. The intensive credit check, especially in relation to the company's concept aside the raw numbers, is designed to prevent borrowers from over borrowing. However, the increase in the share of non-performing loans (PAR 30) to just under 8% in 2015 (PAR 90: 6%) shows that despite intensive credit checks, the implementing agency also suffers under the difficult general conditions – even when the country average at PAR 90 is 12%. The problem was recognised by the management and the bank has introduced further early warning indicators, such as drastic declines in sales volume at the MSME borrowers or arrears after just seven days (PAR 7).

An alternative to equity investment by the FC would have been the granting of a loan. The participation not only had the advantage of being able to exert greater influence on business policy but also had a positive impact on the bank's reputation in a very fragile environment. The bank's level of indebtedness (leverage ratio) remained stable throughout the capital injection between 2010 and 2015. The advantage for the bank is that, as opposed to a conventional loan in euros, it is the FC and not the bank that bears the exchange rate risk.

We consider the allocation efficiency as satisfactory overall, so that we can assess the overall efficiency as good.

Efficiency rating: 2

Impact

The overall developmental objective of the project was to contribute to the creation of employment and income in the target group MSME and to the improvement of living conditions of the population. It was also expected that other financial institutions would follow suit and take up or expand the business area of the MSME sector.[2] The bank does not have any comprehensive statistics on the number of employees of its customers or their revenues. It is thus difficult to measure the project's impact due to the lack of baseline data which is why an impact assessment is carried out based on semi-structured interviews with customers and customer advisors on the ground. These interviews show a classical pattern of effects: lending generally led to the realisation of a project which, for example, comprised more modern and more efficient machinery, a site extension, purchase of a transport vehicle and (or) the purchase of current assets (merchandise, primary inputs, intermediate products, etc.). Initially, with regard to the companies visited, small loan amounts of less than EUR 10,000 were borrowed. These amounts increased up to EUR 100,000 for projects later on. As a result of the increase in the average loan amounts, fewer small initial investments are now being supported by the bank. However, productive potential can also be found amongst the larger companies of the current target group.

In individual cases, people were laid off after the modernisation of the business. Yet, there was almost always a subsequent increase in revenue, with the result that new employees were again recruited in the medium term, even in the wake of investments geared towards efficiency improvements and modernisation. It is plausible to assume that jobs and income at the supported businesses have developed parallel to the increase in the loan portfolio. The previously acceptable losses in the portfolio generally indicatee worthwhile investments.

Alternative financing options (supplier credit, credit card, credit limits) for smaller loans under EUR 10,000 – i.e. for loan sizes that the bank only wants to offer to a limited extent – are often available to MSMEs in the market, but may be less target-group-oriented. This problem applies in particular to loans of between EUR 10,000 and EUR 30,000, which will no longer be the focus of the bank's activities in the future either.

The share of rural loans has remained constant at about 26%, with the bank granting an above-average share of agricultural loans; this segment has risen from 15% to 21% over the years.

2 Indicators were not defined for the overall development goals.

The bank’s support has contributed to stabilising the financial system. According to the bank, however, lending to MSMEs in its present form has been replicated by only one other institution in Moldova, in which a French bank is a shareholder. The bank continues to play a pioneering role in other activities, such as the provision of banking facilities with automated deposit and withdrawal machines. This automation is gradually being introduced by some of the bank’s competitors. Yet, even in the country’s capital, the counter rooms of many banks are still not up to modern standards (high staff numbers, time-consuming processes, etc.).

Altogether we rate the impact of the project as satisfactory.

Impact rating: 3

Sustainability

The increase in equity capital was supposed to substantiate the results achieved since the bank was founded and the initial capitalisation by FC (among others) had been paid in. This has been achieved to a large extent, as the bank is now profitable and significantly more resistant to the current crisis in the country's financial sector as a result of streamlining and modernising its operations. Whether the country’s economic situation improves or a continuing crisis further deteriorates the quality of the bank’s portfolio depends on a large number of factors and cannot be assessed by the evaluation.

Following a decision by the management, the bank will gradually withdraw from offering very small loans below EUR 30,000. On the one hand, the decision to raise the average loan size appears to strengthen sustainability because it is accompanied by the positive development of the bank’s profit. On the other hand, the impact of the project is reduced for the group of micro-entrepreneurs, and in particular for those entrepreneurs who want to take out a small loan for the first time (and who have the potential to borrow larger amounts in the future). It is to be assumed that the group of companies that require small loans of less than EUR 30,000 cannot be provided with loans of the same quality in the future.

Maintaining the current policy of limited services for micro-entrepreneurs, the bank will continue to be more active in the area of small enterprises compared to other institutions in Moldova, and will make an important contribution here. The current degree of professionalism in lending is testament to the fact that the bank will also be able to maintain its position in this segment.

As a result of the bank’s solid financial position and despite the move away from the smallest loan volumes, we continue to assess the overall sustainability as good.

Sustainability rating: 2

Notes on the methods used to evaluate project success (project rating)

Projects (and programmes) are evaluated on a six-point scale, the criteria being **relevance**, **effectiveness**, **efficiency** and **overarching developmental impact**. The ratings are also used to arrive at a **final assessment** of a project's development effectiveness**.** The scale is as follows:

Level 1	Very good result that clearly exceeds expectations
Level 2	Good result, fully in line with expectations and without any significant shortcomings
Level 3	Satisfactory result – project falls short of expectations but the positive results dominate
Level 4	Unsatisfactory result – significantly below expectations, with negative results dominating despite discernible positive results
Level 5	Clearly inadequate result – despite some positive partial results, the negative results clearly dominate
Level 6	The project has no impact or the situation has actually deteriorated

Rating levels 1-3 denote a positive assessment or successful project while rating levels 4-6 denote a negative assessment.

Sustainability is evaluated according to the following four-point scale:

Sustainability level 1 (very good sustainability): The development effectiveness of the project (positive to date) is very likely to continue undiminished or even increase.

Sustainability level 2 (good sustainability): The development effectiveness of the project (positive to date) is very likely to decline only minimally but remain positive overall (this is what can normally be expected).

Sustainability level 3 (satisfactory sustainability): The development effectiveness of the project (positive to date) is very likely to decline significantly but remain positive overall. This rating is also assigned if the sustainability of a project is considered inadequate up to the time of the ex post evaluation but is very likely to evolve positively so that the project will ultimately achieve positive development effectiveness.

Sustainability level 4 (inadequate sustainability): The development effectiveness of the project is inadequate up to the time of the ex post evaluation and is very unlikely to improve. This rating is also assigned if the sustainability that has been positively evaluated to date is very likely to deteriorate severely and no longer meet the level 3 criteria.

The **overall rating** on the six-point scale is compiled from a weighting of all five individual criteria as appropriate to the project in question. Rating levels 1-3 of the overall rating denote a "successful" project while rating levels 4-6 denote an "unsuccessful" project. It should be noted that a project can generally be considered developmentally "successful" only if the achievement of the project objective ("effectiveness"), the impact on the overall development goal ("impact") **and** the sustainability are rated at least "satisfactory" (level 3).