Kazakhstan: Credit Line for SMEs

Ex-post evaluation

OECD sector	24030 – Financial intermediaries of the formal sector	
BMZ project ID	1998 65 114	
Project-executing agency	Three private Kazakh commercial banks: - ATF Bank - Kazkommertsbank (KKB) - Bank Turan Alem (BTA)	
Consultant	LFS Financial Systems GmbH	
Year of ex-post evaluation	**2005**	
	Project appraisal (planned)	**Ex-post evaluation (actual)**
Start of implementation (disbursement)	1999	2000
Period of implementation (disbursement)	4 years	5 years
Investment costs	no information available	no information available
Counterpart contribution	no information available	no information available
Financing, of which Financial Cooperation (FC) funds	EUR 13.8 million	EUR 13.8 million
Other institutions/donors involved	none	none
Performance rating	2	
• Significance / relevance	2	
• Effectiveness	2	
• Efficiency	2	

Brief Description, Overall Objective and Project Objectives with Indicators

The FC funds served to refinance loans extended by three private Kazakh banks to small and medium-sized enterprises (SMEs), namely ATF-Bank (formerly Almaty Merchant Bank), Bank Turan Alem (BTA) and Kazkommertsbank (KKB).

The programme objective was to enable the three commercial banks refinanced under the programme to extend medium and long-term investment loans to the target enterprises in an efficient and sustainable manner and in line with demand. The programme objective was to be considered achieved if the following indicators are achieved:

- The portfolio at risk does not exceed 5% of the loan portfolio (in arrears for more than thirty days);
- Loan losses do not exceed 5% of the loan portfolio (uncollectible for more than 180 days);
- The return on equity of the banks (measured by after-tax profit) is positive in real terms.

The overall objective of the project was to promote competitive private SMEs and thus to contribute to restructuring the Kazakh economy. A satisfactory return on equity of private SMEs was defined as the indicator for the achievement of the overall objective. The return on equity was to be determined through random samples at the time of the final evaluation.

Programme Design / Major Deviations from the original Programme Planning and their main Causes

Under the project the Republic of Kazakhstan, represented by the Ministry of Finance, was given a loan of EUR 13.0 million and a grant of EUR 0.1 million for personnel support measures. The banks had the possibility to take up sub-loans both in local currency and in foreign currency. At the time of project appraisal sub-loans were planned to amount between EUR 5,000 and EUR 510.000. The maximum amount was raised in several steps to EUR 1 million. Due to uncertainties in the demand forecast no separate micro loan component was included in the project. The exchange rate risk was born by the sub-borrowers. Deliberately, no specifications were set with regard to terms and conditions for sub-loans in order to give banks an incentive to fix such terms on a case-by case basis and in line with market requirements.

Originally, the target group was SMEs with up to 50 employees in the manufacturing industries, the crafts and the service industry. But larger SMEs with 50 to 200 employees also have a substantial demand for loans and are at the same time facing considerable difficulties in obtaining loans from the formal banking sector. In consequence, due to the high demand for loans by “larger“ SMEs and the sluggish start of lending the number of employees of eligible enterprises was raised to 200 – in analogy with lending practice of the ADB and the World Bank. Roughly two thirds of the loan volume was committed to enterprises with fewer than 130 employees. Against the background that lending to SMEs in Kazakhstan is little developed we consider the change in the definition of the target group to comprise larger companies as justified in terms of development policy objectives.

The maturity of most of the sub-loans was three to four years, depending on the economic lifetime of the investment goods financed. The FC funds were disbursed by KfW directly to the banks according to the disposition fund procedure. As soon as available funds have been used for sub-loans KfW disbursed further funds upon the request of the respective banks (on a “first come – first serve” basis). The total funds were disbursed as follows:

	Total	Number of loans	Average loan amount
ATF-Bank	EUR 6,055,808	23	EUR 262,726
KKB	EUR 4,953,646	10	EUR 495,346
BTA	EUR 2,795,426	10	EUR 279,543
Total	**EUR 13,804,880** [a)]	**43**	**EUR 320,695**

a) Including remaining funds in the amount of EUR 14,308 together with loans used on a revolving basis.

Altogether 43 sub-loans were extended in the first round of disbursement. The average loan amount was EUR 321,000, which is clearly lower than the maximum amount of EUR 1 million. A major share of the loans (42%) was extended to enterprises in the area of food processing, 26% went to the manufacturing industry and 23% to the service sector (other sectors: 9%). As had been agreed, the bulk of loans were extended to enterprises in the Almaty region (65%) The capital mobilisation effect during the first use of funds was negligible at the ATF-Bank and at BTA. In only few cases did banks extend additional small-volume working capital loans refinanced from their own funds. KKB, on the other hand, extended EUR 5.5 million from its own funds to the promoted enterprises in addition to the FC funds of EUR 4.9 million. When extending the originally available funds for the second time altogether 33 loans were handed out for a total of EUR 8.4 million. The average loan volume in this second use of funds was EUR 255,000. The three banks provided complementary loans for altogether EUR 10.1 million. As a result the overall picture in terms of capital mobilisation during the second use of funds is much more positive.

Key Results of the Impact Analysis and Performance Rating

The FC project helped – in coordination with similar programmes implemented by other donors - to sustainably increase the offer of medium to long-term loans to the SME sector. This is reflected in a broader offer of financial services (SME loans) and a deepening of the financial sector (opening up SMEs as a new customer group). We consider it to be a positive sign that the banks use the FC funds on a revolving basis in the SME sector and further expand this area of business by using their own funds. The fast turnover of revolving funds clearly indicates that market conforming and profitable financial structures have been established. The project has a positive signalling effect on the Kazakh banking sector: it is profitable for the banks to grant loans to SMEs.

Every third programme bank targets a very specific sub-segment of the SME target groups: KKB addresses mainly larger SMEs (of up to 200 employees). The other two banks regard especially the middle range (80 to 130 employees) as their target group. Most recently KKB has also increasingly focussed on smaller SMES (fewer than 80 employees).

The performance of the sub-loans is good. At the time of the ex-post evaluation none of the loans was in default. At the target group levels substantial employment effects have been achieved. Roughly 750 jobs were created or safeguarded under the first use of funds and about 200 more jobs under the second use of funds.

BTA works together with its loan customers on the basis of the “house-bank principle”. Especially for smaller enterprises it may be easier and faster to obtain a loan if they have a stable long-term relationship with their bank. In the event of such a “house-bank“ relationship it might also generally be possible to obtain a loan with less collateral. Due to the house-bank principle BTA is also able to solve the classical dilemma between the need to obtain as much security as possible for the loans and the desire to reach as many small enterprises as possible. It is vital for Kazakh banks to survive that they are careful in their assessment of smaller enterprises and the collateral they demand from such enterprises, especially against the background of persisting economic uncertainties in the region and sometimes high non-performing loans in the Kazakh banking system.

In the loan appraisal procedure it was taken into account that no loans were granted for investments that may harm the environment. Due to the use of modern production and disposal technologies most of the projects had generally positive environmental impacts.

The project makes an important contribution to improving the economic situation of the target group (SMEs). Due to the creation and/or safeguarding of jobs the project made a certain contribution to the economic development and, thus, to reducing poverty. The employment effects prevented many people from slipping below the poverty line.

In a summarized assessment of all impacts and risks described above we have arrived at the following rating of the project’s developmental effectiveness:

Effectiveness

The programme objective was to enable the three commercial banks refinanced under the programme to extend medium and long-term investment loans to the target enterprises in an efficient and sustainable manner and in line with demand. Measured by the target indicators the programme objectives were fully achieved. The project had sustainable impacts on the financial sector. The quality of the portfolio of loans financed under the FC project was good. None of the 76 loans handed out in the context of the first and second use of funds was jeopardized by default or even loss. All three programme banks work fully cost covering in their lending activities in the SME field and even make a profit. We deem it positive that the three banks want to continue the extension of SME loans on a revolving basis and even want to expand it by providing refinancing funds of their own. A negative aspect is that it took a long time until the programme actually took effect. Despite the economic stagnation at the time when the programme was started this long period might have been avoided if a consultant had been assigned to assist the programme in the early stages. Already at the time of the project appraisal it had been noted that the lacking access to loans about which SMEs were complaining was not only due to the deficient supply of loans offered by the banks but also to the facts that there were deficits in the identification of profitable investment projects and that the SMEs themselves could not present meaningful and informative loan applications and documents. Overall, we rate the achievement of the programme objectives as satisfactory (sub-rating: 2).

Significance / Relevance

The overall objective of the project was to promote competitive private SMEs and thus to contribute to restructuring the Kazakh economy. A satisfactory return on equity of private SMEs was defined as the indicator for the achievement of the overall objective. Random samples of all SMEs that had received a loan under the SME project were surveyed in the context of the ex-post evaluation. All of them worked profitably. As private-sector enterprises they make a contribution to the modernisation and restructuring of the Kazakh economy. Approximately 750 new jobs were created or secured in the private sector. Still, it has to be noted that in the majority of cases only SMEs with an excellent credit standing are given access to loans. With its house-bank concept the BTA has shown ways to establish and maintain long-term relations also with small enterprises. Today the three banks have become successfully established in the international capital markets and use this market for refinancing purposes. Thus, we become less dependent on donor financing. The efficiency of the project is somewhat reduced due to the fact that the FC funds were made available to the three banks only for a period of 10 years. If the period of availability of the funds had been longer, this would have had a positive impact on the significance. Overall, we classify the project's developmental relevance and significance as satisfactory (sub-rating 2).

Efficiency

We rate the production efficiency of the project as sufficient. All three banks have interest margins that are positive in real terms and allow them to work profitably. Though there are certain difference between the three programme banks, the key figures on operative efficiency are at a normal level, non-performing loans are clearly lower than the sector average and the provisions for loan losses are sufficient. Only with regard to the risk-weighted equity ratio do the three banks have difficulties to keep up with the fast growth in their lending business and range rather at the lower end of the minimum requirements (this goes in particular for ATF-Bank and BTA). We rate the allocation efficiency as very good. The loans are being granted at market conditions to the target group. Overall, we rate the efficiency of the programme objectives as satisfactory (sub-rating: 2).

Taking the sub-categories effectiveness, efficiency and significance/relevance into consideration, we judge the project's developmental effectiveness to be satisfactory (rating 2).

General Conclusions

If several financial institutions qualify for the refinancing of the SME lending business, an APEX structure is usually recommendable. Under such an apex structure, all qualified institutions will then basically have equal access to refinancing funds and will have to compete for the funds.

A phenomenon frequently noticed when examining SME credit lines is that the overall maturity of the loan granted to the recipient country is usually considerably longer than the terms of the individual loans handed on to the banks involved. In order to increase the significance of this type of projects it would be worthwhile to adjust the on-lending maturities to the overall maturity of the loan, especially with the aim in mind to ensure the revolving use of the funds on a long-term basis.

Banks that have already built up a diversified refinancing base with funds granted under German FC or have even established a sustainable access to funding in the international capital market should in the future be given FC funds especially for the purpose of building up business areas or to extend loans to customer groups which the banks would usually not service due the high risks and/or low margins involved but which still deserve support for development-policy reasons (e.g. environmental credit lines).

Considerable synergy potentials exist with a view to donor harmonisation, part of which could have been realized at a relatively low cost. Indeed, in the area of financial sector promotion some institutions receive support from different donors for the same business area (SME lending). In most cases the planning and implementation of the projects with regard to target groups, terms and conditions, reporting, staff support measures etc. was done separately for the individual institutions. This caused a substantial burden for the banks supported and resulted in considerable efficiency losses.

It is necessary to strengthen the offer of financial services (e.g. through a refinancing credit line and staff support measures to train the personnel at the involved financial institutions). Often, however, a credit relationship and an efficient lending process cannot be established because the demand for loans is too weak. Enterprises that do not have access to the formal financial sector often find it difficult to establish the documents required for a loan application (e.g. preparation of a business plan and key financial figures, structuring of securities, etc.). These bottlenecks can be tackled through staff support and training measures, which should formally not be implemented at the banks.

Agreements covering the developmentally sound utilisation of counterpart funds (e.g. for training measures, consulting services etc.) should already be concluded at the time of project appraisal. This might be a reasonable way to increase the efficiency of the funds.

Legend

Developmentally successful: Ratings 1 to 3	
Rating 1	**Very high or high degree of developmental effectiveness**
Rating 2	**Satisfactory developmental effectiveness**
Rating 3	**Overall sufficient degree of developmental effectiveness**
Developmental failures: Ratings 4 to 6	
Rating 4	**Overall slightly insufficient degree of developmental effectiveness**
Rating 5	**Clearly insufficient degree of developmental effectiveness**
Rating 6	**The project is a total failure**

Criteria for the Evaluation of Project Success

The evaluation of the "developmental effectiveness" of a project and its classification during the ex-post evaluation into one of the various levels of success described in more detail below concentrate on the following fundamental questions:

- Are the **project objectives** reached to a sufficient degree (aspect of project **effectiveness**)?
- Does the project generate sufficient **significant developmental effects** (project **relevance** and **significance** measured by the achievement of the overall development-policy objective defined beforehand and its effects in political, institutional, socio-economic and socio-cultural as well as ecological terms)?
- Are the **funds/expenses** that were and are being employed/incurred to reach the objectives **appropriate** and how can the project's microeconomic and macroeconomic impact be measured (aspect of **efficiency** of the project conception)?
- To the extent that undesired **(side) effects** occur, are these tolerable?

We do not treat **sustainability**, a key aspect to consider for project evaluation, as a separate category of evaluation but instead as a cross-cutting element of all four fundamental questions on project success. A project is sustainable if the project-executing agency and/or the target group are able to continue to use the project facilities that have been built for a period of time that is, overall, adequate in economic terms, or to carry on with the project activities on their own and generate positive results after the financial, organisational and/or technical support has come to an end.