Kyrgyzstan: Credit Line for the Private Sector IV

Ex post evaluation report

OECD sector	2403000 / Formal sector financial intermediaries	
BMZ project ID	1998 66 294 (Investment) 1999 70 104 (Complementary Measure)	
Programme executing agency	OJSC Commercial Bank Kyrgyzstan (formerly Bank AKB Kyrgyzstan)	
Consultant	ICEE	
Year of ex post evaluation report	**2010 (2009 sample)**	
	Programme appraisal (planned)	**Ex post evaluation report (actual)**
Start of implementation	Q1 2000	Q1 2003
Period of implementation	30 months	60 months
Investment cost	N.A	N.A
Counterpart contribution	N.A	N.A
Financing, of which Financial Cooperation (FC) funds	EUR 5.11 million	EUR 5.11 million
Other involved institutions / donors	-	-
Performance rating	3	
• Relevance	2	
• Effectiveness	3	
• Efficiency	3	
• Overarching developmental impact	3	
• Sustainability	3	

Brief description, overall objective and programme objectives with indicators

The programme comprised a loan in the amount of EUR 4.60 million (BMZ ID 1998 66 294) for the funding of two private Kyrgyz commercial banks (Bank AKB Kyrgyzstan, today OJSC Commercial Bank Kyrgyzstan, and Promstroi Bank), of which only OJSC Kyrgyzstan made use of the credit line in the course of the programme. The programme also included a complementary measure in the form of staff training, with the sum of EUR 0.51 million (BMZ ID 1999 70 104) made available to finance the services of a consultant contracted to support the participating bank in the appraisal, processing and handling of the loan applications.

The borrower was the Republic of Kyrgyzstan, represented by the Ministry of Finance which channelled the loan funds in DEM and EUR to the commercial bank. This bank was in charge of providing medium to long-term loan funds to private enterprises, which were the end-borrowers, for investments in fixed assets and investment-related working capital. Initially, the provision of these loans to the end-borrowers in DEM and EUR required the consent of KfW.

The programme pursued the overall objective of contributing to the further development of the financial system and to the restructuring of the economy of Kyrgyzstan, to the growth of the economy and to the creation of employment through the promotion of competitive private enterprises. The programme objective was to enhance the ability of the implementing banks to supply the target group with medium and long-term investment loans at interest rates that were positive in real terms and in an efficient, needs-oriented and sustainable manner.

The following indicators for the achievement of the overall objective were defined: (a) satisfactory return on equity of the financed enterprises, and (b) increase in the volume of loans granted by all banks to the private sector in relation to GDP. The following indicators were defined for the achievement of the programme objective: (a) positive return on equity in real terms for the banks participating in the programme (measured by profit after tax), (b) portfolio at risk of not more than 10% of the relevant overall loan portfolio.

Programme design / major deviations from the original programme planning and their main causes

The FC funds in the sum of EUR 4.6 million were provided to the Kyrgyz Government, represented by the Ministry of Finance, in the form of a loan at the lending conditions established for Kyrgyzstan (0.75% interest, term of 40 years including 10 grace years). In agreement with the Kyrgyz Government, two banks were selected for the implementation of the programme, AKB Bank and Promstroi Bank. The quadripartite loan, financing and programme agreement dated 2 May 2001 provided for the funds to be channelled by the Ministry of Finance to the banks in DEM. The onlending conditions were set at 4% interest and a term of 15 years including five grace years. The term of 15 years was agreed in order to give the banks the opportunity to re-lend the funds on a medium to long-term basis as a means of contributing to developing structures in the financial system.

Under the terms of the separate agreement, the banks implementing the programme were required to submit to KfW their annual statements, which had to be audited according to IAS. As Promstroi Bank was not able or willing to meet this requirement, it eventually withdrew its participation in the implementation of the credit line. This left AKB as the only bank available to implement the programme, which ultimately was one of the reasons leading to its delayed implementation.

Given the relatively limited experience of AKB in lending longer-term investment loans, the programme conception initially required all loan applications to be submitted to KfW for approval. This procedure proved to be excessively complicated. In local discussions, the representatives of the bank expressed their view that significant progress in implementing the programme only became apparent when the credit processing was reset after completion of the complementary measure. The funds made available under the complementary measure were used in particular for support measures in the analysis and appraisal of the end-borrower applications in the medium and long-term lending business, as well as for the ongoing monitoring of the loan portfolio.

Key results of the impact analysis and performance rating

In regard to the intended impacts, the results of the ex post evaluation demonstrate that the assumptions pertaining to the impact chains remain valid. The provision of loans to support the private sector contributes to increasing investment, creates jobs and income and thus induces further investment. The programme objective corresponded with both the developmental objectives and guidelines of the BMZ and the strategies of the Kyrgyz Government. On the basis of plausibility considerations, it can also be assumed that by providing financing for the private sector the programme has also contributed to Millennium Development Goal 1 (to cut income poverty in half). The programme harbours no direct potential for the reduction of gender disparity, nor is it expected to have any specific impacts on the environment or governance.

Based on a combined assessment of all impacts and risks described above, we have arrived at the following rating of the programme's developmental efficacy (information on success ratings can be found in the technical information:

Relevance: The credit line and the complementary measure were designed to enhance the capacities of the onlending banks. The banks for their part were expected to provide private enterprises with opportunities to competitively expand their activities by supplying them with investment loans. The increase in entrepreneurial activity was expected to contribute to the growth of the economy and the creation of new employment. The conception of the programme and the assumed impact chain were plausible and continued to be relevant at the time of the ex post evaluation as well. The difficulties private enterprises have in accessing investment loans at market conditions continue to pose a central obstacle to the growth of the private sector. The programme was aligned with the developmental priorities of the BMZ and the Kyrgyz Government. Donor coordination was appropriate. We rate the relevance of the programme as good (sub-rating 2).

Effectiveness: The programme objective was to enhance the ability of the implementing banks to supply private enterprises with up to 500 employees with medium and long-term investment loans at interest rates that were positive in real terms and in an efficient, needs-oriented and sustainable manner. The indicators established for measuring the achievement of the programme objectives were a positive return on equity in real terms for the banks participating in the programme and the portfolio at risk in the respective overall loan portfolio (not more than 10%). For 2008, AKB achieved a return on equity of 28% which translated into a positive return on equity of 8% in real terms after adjusting for the 20% inflation rate. The PaR of AKB (more than 30 days overdue) on 30 June 2009 was 8.1% and improved to 7.3% on 30 September 2010, remaining below the established maximum value. However, the maximum value had clearly been set too high. If currently generally accepted indicators had been applied (portfolio at risk > 30 days less than 5%), the value would be slightly higher. Both programme success indicators have thus been formally fulfilled, although the threshold of the second indicator was set much too high. We rate the effectiveness of the programme as satisfactory (sub-rating: 3).

Efficiency: The loans were granted at market conditions. The impression we obtained from visits to a sample selection of end-borrower enterprises was that the end-loans were used for meaningful investments (good allocation efficiency). The impacts achieved with the programme appear to be in an adequate proportion to the funds invested under the programme. The bank's production efficiency appears to be reasonable. The representatives of AKB explained that significant successes in regard to the lending volume and repayment rate were only observed after the lending process had been reset following the completion of the complementary measure and after the lending was aligned with EBRD processes. The loan approval process initially agreed with KfW was described by all sides as too complicated. The programme conception was not adapted fast enough to accommodate the structural implementation problems. The resulting delay in the disbursement of the programme funds therefore contributed to the downgrade of this sub-rating. The fact that the bank's positive development was only partly brought about by the FC programme adversely impacted the sub-rating as well. The financing requirements existed and the programme contributed to meeting them, but it was negatively affected by the complicated loan processing. This is evidenced by, among other things, the withdrawal of a second bank that was to participate in the initial programme conception. We rate the efficiency of the programme overall as satisfactory (sub-rating: 3).

Overarching developmental impact: The overall objective of the programme was to contribute to the further development of the financial system and to the restructuring of the economy of Kyrgyzstan, to the growth of the economy and to the creation of employment through the promotion of competitive private enterprises. The indicators defined to measure the achievement of the overall objective were a satisfactory return on equity of the financed enterprises and an increase in the volume of loans granted by all banks to the private sector in relation to GDP. As no data on the return on equity generated by the sub-borrowers are available, the portfolio at risk of all loans in the bank's portfolio that are past due more than 30 days was used as a proxy indicator since the repayment rate of the funded credit line is not very expressive. Considering that the portfolio at risk was still relatively low, it can be said that the return on equity generated by the financed enterprises was satisfactory on average. The second indicator for the overall programme objective, however, shows a different outcome. Since no comparative figures were available at the time of conclusion of the loan agreement, the data captured at the reference data of 31 December 2004 (first publication of these figures by the National Bank) were used as proxy. On this reference date, the share of loans in the private sector in relation to GDP still amounted to 15.8%, but this ratio deteriorated to 7.8% as at the reference date of 31 December 2008. This would mean that the indicator for the overall objective was not fulfilled. It can be presumed, however, that this share was lower at the time of programme appraisal and conclusion of the loan agreement, so that this indicator for the overall objective can still be assumed to have been partly fulfilled. In summary, the indicators for the overall objective have been only partly fulfilled.

Leaving the system of indicators for the measurement of the overall objective of the programme aside, it can be ascertained from a development-policy perspective that the granting of the loans achieved positive employment impacts for the financed enterprises. According to information provided by several of the eight enterprises visited on the occasion of the ex post evaluation, the investments financed through the programme were decisive for the establishment or expansion of the respective enterprise. In addition, capacity utilisation appeared to be high in the majority of the visited enterprises, and some of them are planning further capital expenditure, which suggests a positive contribution to the growth of the economy of Kyrgyzstan even if two of the enterprises reported that they were feeling the impacts of global economic crisis. A negative outcome is the fact that the onlending conditions provided for the exchange rate risk to be passed on to the sub-borrowers who generated no foreign currency income of their own, greatly increasing their repayment obligations as a result of the devaluation of the KGS during the course of the programme. We therefore rate the overarching developmental impacts of the programme as satisfactory overall (sub-rating 3).

Sustainability: The bank appears to have a well-established lending business that can be assumed to continue growing in the future. Thus, for example, lending to the private sector has grown strongly in the past years. With a view to the supported enterprises, the fact that the vast majority of them were still operating at the time of the ex post evaluation and were able, by and large, to meet their contractual obligations in spite of the currency devaluation, appears to demonstrate that the financed assets are operating and recovering the costs. Most of the visited enterprises expressed a continued interest in expanding their business activities and in additional financings. Of the roughly 70 employees who were trained under the complementary measure, only a few are still working for the bank. According to the bank, however, most of those who have left continue working in the financial sector, so the skills they have acquired under the complementary measure have the potential to continue to have a sustainable impact. The organisational and institutional capacities established by the complementary measure (even if, regrettably, somewhat late), on the other hand, appear to have been largely maintained within the bank and developed further. We rate the sustainability of the programme as satisfactory (sub-rating: 3).

After weighing the individual evaluation criteria described above, we rate the overall developmental efficacy of the programme as satisfactory (performance rating 3).

General conclusions and recommendations

In order to ensure that SMEs are reached as a target group, care should be taken that a common understanding of the definition and the meaning of the classification of enterprises as SMEs exists between the programme executing agency, the financiers and the shareholders. This recommendation applies particularly to countries in which the SME definition is unclear.

In countries with volatile currencies, care should be taken that the currency risks in financial sector programmes do not have to be borne by the end-borrowers. This applies in particular to programmes designed to support small and medium-sized private enterprises that usually cannot generate foreign currency revenues.

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 overall developmental efficacy. The scale is as follows:

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

Ratings 1-3 denote a positive or successful assessment while ratings 4-6 denote a not positive or unsuccessful assessment

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

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

Sustainability level 2 (good sustainability): The developmental efficacy 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 developmental efficacy 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 developmental efficacy.

Sustainability level 4 (inadequate sustainability): The developmental efficacy 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. Ratings 1-3 of the overall rating denote a "successful" project while ratings 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 objective ("overarching developmental impact") and the sustainability are rated at least "satisfactory" (rating 3).