Kazakhstan: MFF- Small and Medium Enterprise Investment Program

**Project Rationale and Linkage to Country/Regional Strategy**
ADB is committed to support SME development in Kazakhstan. However, because of the poor health of the banking sector, it is difficult for ADB to provide traditional nonsovereign credit lines and guarantee operations. For example, ADB's 2009 Countercyclical Support Program helped the government to fund post-crisis SME credit support operations. At the request of the government, ADB looked at a number of options to provide continued support over the medium term through its sovereign operations. The government requested flexibility in lending products as the health of the finance sector improves, and asked that these products help to mitigate currency, interest, and tenor mismatch issues. Damu also requested assistance in improving its efficiency and effectiveness to enable it to raise external financing over the longer term. In response, ADB developed the investment program, which is consistent with ADB's overall strategy for Kazakhstan and reflects lessons learned. The investment program is designed as an MFF, under which a series of local currency loans and other financing products will be provided over the medium term. The MFF enables flexibility as it will allow ADB to provide different forms of support (direct loans or guarantees) to Damu to help fund its lending to Participating Financial Institutions (PFIs). The MFF also enables ADB to enter into a multiyear partnership with Damu (and possible cofinancing partners) while creating stability and credibility at the level of the financing plan. To reflect lessons learned, the investment program envisions a series of medium-term, fixed-rate, local currency loans to Damu that will be used to fund back-to-back subloans to PFIs for onlending to SMEs. By providing such loans, ADB will directly address currency, interest rate, and tenor mismatch risks. Experience has shown that these financial risks have been a significant cause of stress for SMEs and their banks. For the tranche 1 loan, ADB raised local currency through cross-currency swaps with international bank counterparties. ADB has been able to leverage its relationships with international banks and utilize its AAA rating to extend the tenor and lower the pricing of cross-currency swaps. For subsequent tranches, ADB will work with MOE and Damu on the issuance of local currency bonds (LCBs) by ADB or, with an ADB guarantee, to provide continued support over the medium term.

**Impact**
The project's impact will be sustained job creation and economic growth through SME development.

**Implementation Progress**

- **Description of Project Outputs**
  - Medium-term financing to SMEs
  - Improved effectiveness and efficiency of Damu
  - Improved financial sector outreach, with a focus on women entrepreneurs

- **Status of Implementation Progress (Outputs, Activities, and Issues)**
  - By the closing date of Tranche 1, September 2013, a total of 2,337 loans were disbursed by PFIs to 734 SME borrowers, using ADB proceeds. For inconsistencies with Data indicators interpretation, refer to changes made to MFF DMF. The average amount lent to each SME borrower was $244 million ($290,000) and the average loan was $234 million ($90,000). Women were 30.5% of total SME borrowers.
  - Between 2012 and 2013 Damu approved 8 changes to its internal risk management processes and 6 changes to improve its corporate governance.

**Geographical Location**

**Summary of Environmental and Social Aspects**
Environmental Aspects

The facility has been categorized as FI in accordance with ADB's Safeguard Policy Statement (SPS, 2009). Safeguards due diligence has been conducted to assess potential environmental and social risks and impacts associated with qualified PFI's likely future portfolios, along with their commitment and capacity for environmental management. Tranche 1 was treated as category C for environmental safeguard components based on ADB's SPS. Tranche 2 under the MFF will be treated as Category B for environment safeguard components based on ADB's SPS. Damu and each of the PFIs will have in place or establish an ESMS to be maintained as part of its overall management system to meet Kazakhstan national laws and norms and ADB's safeguards requirements. Each PFI that receives proceeds of a loan under the Facility is required to submit to ADB: (i) a copy of its ESMS to be used in implementing this loan for ADB approval prior to submitting its first withdrawal application; and (ii) semi-annual report on its compliance with its ESMS. The PFIs will prepare and submit semi-annual environmental monitoring reports on the implementation status of their ESMS to ADB.

To ensure compliance with ADB's safeguard policy on environment, the selection criteria for PFIs include an assessment of their internal environment and safeguard systems. Eligibility criteria for onlending will be limited to low risk SMEs whose environmental impacts are expected to be negligible and for which no environmental evaluation will be required. For the first tranche the Mission Team's assessment concluded that the financial intermediary's business activities had minimal or no adverse environmental impacts. Therefore the Project is treated as a category C project. Lessons learned on environmental management from ADB's experience with credit line through the private sector operations will be built into the Project design.

Indigenous Peoples

The loan covenants covering all tranches for this MFF loan will ensure that projects that will be financed will have no adverse impact on indigenous peoples. Therefore, this FI loan is treated as category C.

Stakeholder Communication, Participation, and Consultation

During Project Design

The European Bank for Reconstruction and Development (EBRD) actively supports SMEs in Kazakhstan. EBRD programs fund international advisers who provide capacity building and training for SMEs and support to rural SMEs to improve their operations, enter new markets, and gain access to financing. The United States Agency for International Development has supported programs that have provided extensive training on business and consulting essentials to mostly start-up entrepreneurs and nongovernment organization business service providers. EBRD has extended several credit lines to commercial banks to fund lending to SMEs. Their projects are sometimes supported by technical assistance (TA) to help banks introduce a credit scoring methodology and improve their SME lending policies. The World Bank has provided Kazakhstan with the Second Agricultural Post-Privatization Project ($96.1 million), which has a component for promoting sustainable rural microfinance. The International Finance Corporation promotes SME development through its debt and equity investments in banks that provide loans to SMEs. ADB coordinated closely with other development partners in preparing the investment program and MFF.

During Project Implementation

Consultation with business associations and development partners (EBRD, WB, IFC) takes place as part of the review missions.

Business Opportunities

Consulting Services

Under TA 7634-KAZ: Improving Capacity to Support SME Development, ADB engaged a qualified team of consultants in accordance with its Guidelines on Use of Consultants by ADB and its Borrowers (2013, as amended from time to time). Seven individual experts and 1 consulting firm were recruited to implement the TA. A firm was hired to conduct a survey to clarify ongoing constraints to SME development and help define measures that Damu can implement to more effectively address such constraints. The TA commenced on 17 November 2011 and was completed on 31 December 2013.

Procurement

As this is a financial intermediation loan, there is no procurement involved in this project, other than consulting services.

Responsibility ADB Officer

Song, Dai Chang

Responsible ADB Department

Central and West Asia Department

Responsible ADB Division

Public Management, Financial Sector and Trade Division, CWRD

Timetable

<table>
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<tr>
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<tr>
<td>Concept Clearance</td>
<td>02 Jul 2010</td>
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<tr>
<td>Fact Finding</td>
<td>19 Jul 2010 to 30 Jul 2010</td>
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<td>MRM</td>
<td>17 Aug 2010</td>
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<td>Approval</td>
<td>29 Sep 2010</td>
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MFF Facility Concept 0048-KAZ

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<td>Counterpart</td>
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Project Page

https://www.adb.org/projects/44060-013/main

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