

ATTACHED TECHNICAL ASSISTANCE

A. Background

1. The capacity development technical assistance (TA) will support the implementation of the Supporting Resilience of Micro, Small, and Medium-Sized Enterprises Finance Project.¹ The Asian Development Bank (ADB) will engage with selected participating financial institutions (PFIs) in customized solutions to increase their outreach to the smaller segment of businesses and to the regions. The PFIs to benefit from this TA have been selected based on their business strategies and top management commitment, including contribution of their own resources to implement the TA. The TA will be implemented over 30 months from the signing of TA agreement letters with the PFIs.

B. Outputs and Key Activities

2. The TA output will be improved capacities of the PFIs to better serve micro, small, and medium-sized enterprises (MSMEs). To improve the sustainability of ADB's credit line, this TA will assist the PFIs in the following areas: (i) institutional development—including market analysis, organizational set up, introduction of new lending techniques, and product development and testing—to support banks in downscaling their lending operations to the smaller segments and development of new products for microfinance organizations; (ii) greater efficiency of the lending process and management of corporate governance and risk issues; and (iii) improvement of internal audit functions. Given the limited TA resources, and to increase the impact of the intervention, the support will be provided individually to a limited number of PFIs. Two PFIs were selected based on the institutional needs assessment carried out during project processing.² Each PFI has confirmed that its top management (i) is committed to conducting business innovations that are scalable and have the potential to demonstrate improvements that will better serve the project's target groups (smaller businesses, rural areas, women entrepreneurs), and (ii) has put in place a project team and agrees to share at least 35% of the individual TA cost. Additional proposals from PFIs may be considered depending on availability of additional resources and provided they meet the above-mentioned requirements. The TA will have the following components:

(i) Nurbank Component

3. Nurbank is ranked 14th of the 35 banks in Kazakhstan, by assets. Its strategy currently centers on three client groups: retail, small and medium-sized enterprises (SMEs), and corporate clients. Nurbank operates through 16 branches and has 15 heads of SME finance. It has prioritized the development of the SME segment—which currently represents around 18% of its portfolio (T45.7 million outstanding at end-2015; 2,635 loans)—and is interested in downscaling its lending to microbusinesses. Nurbank currently defines its SME business as (i) loans up to T640 million (or about \$1.9 million) for small enterprises, and (ii) loans up to T3 billion (\$8.8 million) for medium-sized enterprises. Around 80% of its outstanding SME portfolio in 2015 was made up of small business loans (2,560 loans).

4. Microbusinesses are seen as a new niche opportunity for the bank. Approaching this segment would require market research and a business plan, selection of target locations, drafting of credit technology and products, staffing and on-the-job training, and integration of

¹ The TA first appeared in the business opportunities section of ADB's website on 13 July 2015.

² ADB. 2015. *Technical Assistance to Kazakhstan for Micro, Small, and Medium-Sized Development*. Manila.

information technology systems into the core banking system. It will involve the design and implementation of new lending modes based on cash-flow analysis of the borrowers.

5. The TA will help Nurbank finalize, test, and implement the microbusiness strategy over 24 months.

6. Activities include: (i) market analysis for client segmentation, including identification of regions and branches best suited to pilot-testing of this product; (ii) diagnostic of Nurbank's organizational setup, policies, procedures, and products required to serve micro enterprises; (iii) discussion of recommendations and proposed implementation plans with Nurbank's management and ADB; and (iv) support for and supervision of Nurbank's initial execution of the plans—(a) setup of specialized micro-enterprise lending unit/s, development of middle-line managers, and other staffing provisions; (b) development of credit underwriting policies, (c) creation of training materials for loan officers, and delivery of training of trainers; (d) selection and training of at least 50 loan officers in risk analysis, monitoring, and recovery or workout of loans; (e) design of incentive-based pay schemes for the loan officers; (f) review of internal control and audit practices, identification of changes required related to the new product, and on-the-job training to strengthen such capabilities; and (g) adaptation of the management information system and monitoring system, including possible investment in a revised scoring model with appropriate functionalities for this product. The project is expected to be piloted in two branches and then rolled out to 10 branches during implementation. These deliverables will be accompanied with on-the job training and capacity building.

7. Nurbank will prepare detailed terms of reference for the consulting services in coordination with ADB. By 31 December 2019, it should have achieved the following results:

- (i) Specialized micro-enterprise lending unit set up, and new product(s) defined, responding to existing demand.
- (ii) Product(s) pilot-tested in two branches and subsequently rolled out to at least 10 branches.
- (iii) At least 3,000 micro enterprises served.
- (iv) Ratio of nonperforming loans to total loans in micro-lending business below 5%.
- (v) At least 50 loan officers trained in credit analysis and able to process micro-enterprise loan applications independently within their branch.

b. Asian Credit Fund Component

8. Founded in 1997, Asian Credit Fund (ACF) has four branches and 25 offices across five regions. With a small loan book of T1,919 billion (\$5.6 million) and an average loan size of \$375 (2015), ACF is targeting subsistence-oriented activities in agriculture. It has close to 15,000 borrowers, and 96% of its loans are outside of the two major cities. Individual entrepreneurs represent almost ACF's entire loan book. Close to 90% of the loan book are group loans, i.e. unsecured loans granted to groups of borrowers who sign loan agreements with joint responsibility to repay their loans. One of ACF's priorities to support its future lending growth is to develop a new business line targeting micro and small entrepreneurs (legal entities), with higher average loan sizes. They estimate that there is service gap in the market for entities that want to borrow between \$7,000–\$15,000 on average. In particular, ACF would like to test a "green" product, focusing on investments to improve energy efficiency and use of renewable energy. In addition, ACF will implement a new IT system with more functionalities to use mobile applications in the lending process. This new strategy requires that ACF's designs and tests new products, improves its lending processes, credit monitoring and internal controls.

9. ACF's has limited capabilities to carry out its internal audit functions. Internal audit is carried out by one person and supervised by the head of audit of Mercy Corps' subsidiary in Kyrgyzstan. ACF plans to strengthen this function by enlarging the unit, improving operational procedures for internal control and enhancing the capacities of staff.

10. Activities and deliverables include: (i) market analysis for client segmentation, to identify growth potential, profitable product lines, and products' features; (ii) develop credit risk assessment policies and procedures; (iii) develop risk-based pricing methodology; (iv) train ACF's trainers on new credit assessment and policies and support later training of all relevant staff; (v) review of internal control and audit practices, identify gaps and provide assistance to improve practices, staff capabilities and risk-analysis automation. The project is expected to be piloted in one branch and then rolled out to other branches during the implementation period.

11. ACF will prepare detailed terms of reference for the consulting services in coordination with ADB. By 31 December 2019, it should have achieved the following results:

- (i) Lending policy and procedures for new products for micro and small enterprises are in place and have been successfully tested.
- (ii) New products are rolled out in at least 10 branches.
- (iii) Lending to micro and small enterprises increased to 3% of total portfolio.
- (iv) At least 15 loan officers have been trained.
- (v) Internal audit department staffed and audit processes revised and implemented.

C. Cost and Financing

12. The total cost of the TA is estimated to be \$1 million, of which \$500,000 will be financed on a grant basis by the Government of Luxembourg through the Financial Sector Development Partnership Fund. The PFIs will provide at least \$500,000 in the form of staff, logistical support, translation services, funding of training and workshop expenses (including resource persons), local travel, marketing expenses and additional national consultants as required. The selected PFIs will fund significant parts of the TA, amounting to no less than 35% of each individual TA cost. The PFIs will also cover any investment costs related to these projects.³ The detailed cost estimate is presented below:

Cost Estimates and Financing Plan (\$'000)

Item	Total cost
A. Asian Development Bank^a	
1. Consultants	
a. Remuneration and per diem	
i. International consultants	300.0
ii. National consultants	100.0
b. International and local travel	50.0
2. Contingencies	50.0
Total	500.0

^a Financed by the Financial Sector Development Partnership Fund and administered by ADB. The PFIs will provide at least \$500,000 in the form of staff, logistical support, translation, training and workshop expenses (including resource persons), marketing expenses, local travel and national consultants.

Source: Asian Development Bank estimates.

³ For example, a revised scoring model with appropriate functionalities for microloans or tablets for data collection for loan officers in the case of Nurbank, or software for automation of the internal audit function in the case of ACF.

D. Implementation Arrangements

13. The TA will be implemented over 30 months, from loan effectiveness and after signing of TA agreement letters with the PFIs. ADB will be the executing agency for the TA, with the Central and West Asia Department acting as the focal point. ADB will monitor TA implementation through regular project visits to Kazakhstan, and telephone and e-mail contact. Periodical reporting by each PFI to ADB will include the following: (i) brief quarterly progress reports on the TA areas; and (ii) a final report on the status of the project, lessons, description of the tasks undertaken, and results achieved. Ad hoc communication on specific topics will take place as required.

14. Consultants will be engaged by ADB in accordance with the Guidelines on the Use of Consultants (2013, as amended from time to time). An estimated 12 person-months of international consultants and 20 person-months of national consultants will be required. The consultants will be engaged through a firm using the consultant qualification selection (CQS) method. Disbursements under the TA will be made in accordance with ADB's *Technical Assistance Disbursement Handbook* (2010, as amended from time to time). Simplified outline terms of reference for consultants are below.

E. Outline Terms of Reference for Consultants

15. All experts will have the ability to effectively communicate with clients and their staff when analyzing, identifying solutions, and delivering related training. Fluency in English is required and Russian is desirable. Expertise required includes:

16. **Small business banking experts** (two international experts, for a total of 10.5 person-months; and one national, for 14 person-months). The consultants will have at least 15 years of MSME banking experience, including experience as a microfinance organization, bank, head of department, or branch manager. Experience in MSME lending in Kazakhstan is desired, and is definitely required in similar transition economies. The consultants will hold at least a bachelor's degree in finance, economics, or a related field. The consultants will (i) conduct market analysis for client segmentation and help design downscaling strategies for Nurbank and new product opportunities for small legal entities for ACF (including "green" products); (ii) conduct a diagnostic of Nurbank's organizational setup, policies, procedures, and products required to serve micro enterprises; (iii) provide recommendations and agree on an implementation plan; (iv) support and supervise Nurbank's execution of the plans—(a) setup of specialized micro-enterprise lending unit(s); (b) development of credit underwriting policies; (c) design of incentive-based pay schemes for the loan officers; and (d) adaptation of management information and monitoring systems. The consultants will also support ACF to (i) develop credit risk assessment policies and procedures; (ii) develop risk-based pricing methodology; and (iii) train ACF's staff.

17. **Internal Audit Specialist** (one international for 1.5 person-months; and one national, for 6 person-months). The consultants will have at least 15 years of experience in internal controls, risk management and internal audit in a bank or a large microfinance organization. For international expert, experience in Kazakhstan is desired. For the national expert, experience in working with international organizations will be valued. The consultants will support ACF (i) in reviewing internal control and audit practices and identify gaps against best practices; and (ii) in improving practices, staff capabilities and risk-analysis automation, including identification of suitable technical solutions.