

RISK ASSESSMENT AND RISK MANAGEMENT PLAN

Risk Description	Risk Assessment	Mitigation Measures or Risk Management Plan
Macroeconomic		
Economic slowdown further reduces MSME demand for credit and their debt service capacity.	Medium	<p>The government is implementing countercyclical support measures to sustain growth and employment, and improve the environment for MSMEs.</p> <p>Project design allows for longer implementation period to accommodate demand fluctuation.</p> <p>PFI's adjust lending limits and security requirements, and increasingly denominate loans in tenge.</p>
Governance		
Public financial management: cumbersome government procedures for approval of the sovereign guarantee for the project cause delays in loan effectiveness.	Medium	Ongoing dialogue with borrower and guarantor to speed up approval process. Damu now has more experience in handling these internal procedures (based on earlier ADB and other donor projects).
Corruption in the form of loan disbursement fraud	Low	<p>Integrity due diligence and financial management assessments conducted for the project suggest that the PFI's internal controls are sufficient to prevent abuse.</p> <p>ADB's is in dialogue with the government and other key donors involved in MSME development through the Partnership Framework Agreement.</p>
Changes to ownership or controlling parties of a PFI that create governance and reputational risks for ADB	Low	Integrity due diligence was conducted on qualified PFI's. Project review missions will update integrity due diligence files. A change of control and ownership covenant is included in legal agreements.
Project-specific		
Subdued growth and external demand may further depreciate the tenge and thereby hurt banks' solvency, liquidity, asset quality, and profitability.	Medium	<p>NBK is gradually tightening prudential regulations toward Basel III, which will require additional capital injections by banks' shareholders.</p> <p>ADB will closely monitor eligibility of PFI's during disbursement. Loan tenor is limited to a maximum of 36 months and guaranteed by the sovereign.</p>
PFI's asset quality deteriorates.	Medium	<p>ADB will closely monitor eligibility of PFI's during disbursement.</p> <p>The government has introduced measures to facilitate write-offs, and changes to tax and bank secrecy rules to facilitate valuation and execution of collateral, which will help reduce NPLs.</p>

Risk Description	Risk Assessment	Mitigation Measures or Risk Management Plan
		Technical assistance will support customized efforts of PFIs to improve underwriting and risk management.
Loans and other dealings with related parties put PFIs at risk.	Low	Project agreements require PFIs to comply with prudential guidelines set by the regulator, including limits in the ratio of their exposure to all related parties to total capital.

Overall**Medium**

ADB = Asian Development Bank; Damu = Damu Entrepreneurship Development Fund; MSME = micro, small, and medium-sized enterprises; NBK = National Bank of Kazakhstan; NPL = nonperforming loan; PFI = participating financial institution.

Source: Asian Development Bank.