ADB

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Kazakhstan: Study on Rural Credit and Savings — Part III: Project Proposal

Prepared by

Development Alternatives, Inc.

Asian Development Bank

Study on Rural Credit and Savings in Kazakstan

T.A. No. 2449-KAZ Final Report

Part III: Project Proposal

Prepared for the Asian Development Bank under COCS contract number 96-235

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Currency Equivalents
(As of January 1997)

Currency Unit	-	Kazakstan Tenge (T)
Tenge 1.00	-	$0.01424
USD 1.00	-	70.2

Abbreviations and Special Terms

∴	-	therefore
ADB	-	Asian Development Bank
ASF	-	Agricultural Support Fund
Akta	-	land title
Blue Book	-	ASF Manual of Procedures for Disbursements
DOA	-	Oblast Offices of the Ministry of Agricultural
EBRD	-	European Bank for Reconstruction and Development
GOK	-	Government of Kazakstan
IT	-	Information Technology
JLGs	-	joint-liability lending groups
LIBOR	-	London Inter Bank Offer Rate
MIS	-	management information systems
NBRK	-	National Bank Republic of Kazakstan
NGOs	-	non-governmental organizations
OSC	-	Oblast Steering Committees
PBs	-	participating banks
PMU	-	Project Management Unit
PSC	-	Project Steering Committee
PMU	-	Project Management Unit
Rayon	-	subdivision of an oblast
TA	-	technical assistance
the Trust	-	Rural Development Trust Fund
TACIS	-	European Union Technical Assistance Program
USAID	-	United States Agency for International Development
USD	-	United States Dollar

I. Introduction

A. Background

1. The background to this proposal is contained in Part I and II of the Draft Final Report.

B. Objectives

- to assist the privatization process in selected rural areas through a range of policy measures, market development initiatives and credit operations;
- to improve the effectiveness of the farm restructuring program and reduce the level of subsidy to the agricultural sector;
- to stimulate rural private enterprise in general, and growth in small and micro-enterprise in particular, for income generation and employment creation; and
- to develop experience, policy and practices that can serve as a basis for the design and implementation of other programs.

C. Targeted Beneficiaries

2. The targeted beneficiaries include:

- privatized farms;
- private agribusiness;
- small and micro rural enterprises in all sectors; and
- the unemployed and other disadvantaged groups.

II. Components and Areas of Operation

A. Components

3. The principal aims are to help build an environment favorable to private enterprise in rural areas, to return insolvent farms to viable operation supported by credit delivery systems that reach into small communities, fostering the growth of small and micro- enterprise and offering the disadvantaged an equitable opportunity to prosper.

4. The principal components will be:

- the establishment of a rural development trust fund for donor funds available for support of rural enterprise and the provision of technical services;
- support for the ongoing farm insolvency and debt restructuring program through debt work-out plans for individual farms;
- commercial credit, delivered through a mix of participating banks, NGOs and traders, allied to savings mobilization and the introduction of new security instruments directed at

breaking the overdue receivables circle and releasing assets that could serve as loan security;

- formulation of policy and support for development of wholesale marketing, a marketing information system and revitalizing the inputs supply chain;
- fostering initiatives for services in agricultural extension, veterinary services, farm machinery hire and business advice and training for the private sector; and
- formulation of enabling legislation and the subsequent development of credit unions to build upon the foundation of existing groups and associations as a means of ensuring local resource mobilization in support of local enterprise.

B. Areas of Operation

5. The need to concentrate finite resources for maximum effect and the need to refine policies and procedures to ensure efficacy and practicality before wider replication imposes constraints on the location of project components.

6. Factors influencing the selection of areas in which to initiate operations include:

- the siting of the ADB irrigation project;
- the operating areas of established projects for small and micro-enterprise; and
- the operating areas of established major traders.

7. The areas proposed are:

- Almaty Oblast;
- Taldy-Korgan Oblast; and
- South Kazakstan Oblast.

8. The phasing of entry is shown below in the proposed implementation schedule.

C. Expected Outcomes

9. The expected outcomes are identified in Table 1 overleaf.

Table 1. Expected Outcomes

Objectives	Components	Expected Outcomes
to assist the privatization process in rural Kazakstan	• policy measures • market development initiatives • credit operations	• environment more favorable to private enterprise • modified tax regime • improved marketing channels for rural goods • better access to financial services in rural areas • enhanced professional skills at banks and NGOs • disadvantaged groups' interests better served
to improve effectiveness of farm restructuring program	• farm insolvency and debt restructuring • debt work-out plans for individual farms • gross margin studies	• bankable farm enterprise • reduced subsidies • improved output • higher recovery of loan capital • gross margin manuals
to stimulate rural private enterprise for income generation and employment creation	• commercial credit delivery • policy and support for development of wholesale marketing, marketing information and inputs supply chain revitalization	• functioning wholesale market system • improved savings mobilization • new security instruments • increased solvency of rural enterprise • improved employment opportunity • a viable rural development trust fund
to develop experience, policy and practices as basis for implementation of other programs	• practical application of each of the previous components • agricultural services initiatives • training for private entrepreneurs • formation of credit unions	• replicable models for introduction in other oblasts • functioning agricultural services • appropriate training materials and methods • enabling legislation for credit unions • functioning credit unions

III. Implementation Phasing

10. Implementation will be phased as below:

A. Phase 1: Preparatory Phase

- trust fund establishment;
- publication of credit policy and procedures;
- approval of intermediaries' lending strategies and credit requirements;
- sub-sector and gross margin studies program preparation; and
- training of local personnel.

B. Phase 2: Initial Operations

11. Operations will open in Almaty and Taldy-Korgan Oblasts. An initial operational period (one year, to permit adequate assessment of the efficacy of the lending program) will test and refine policies, procedures and practices and will give local personnel the opportunity to hone new skills in practical application.

12. Personnel from South Kazakstan will be involved in this initial implementation.

C. Phase 3: Expansion into South Kazakstan Oblast

13. Expansion into South Kazakstan Oblast will follow immediately upon completion of the initial year and the amendment, if necessary of policies and procedures.

D. Phase 4: Consolidation and Credit Union Development

1. Consolidation

14. A review of progress at the end of Year 3 will include formulation of consolidation measures required for the reinforcement of gains and the remedy of deficiencies. These measures will come into effect in Year 4 and continue through Year 5. The measures will include the establishment of credit unions.

2. Development of Credit Unions

15. The development of credit unions will be undertaken in a series of stages to ensure:

- legislation regulates practice, yet protects operational autonomy;
- balanced bottom-up/top-down development;
- full comprehension of the demands on and obligations of members;
- candidate associations have built the membership, capital and skills needed;
- business intentions match membership competence; and
- credit discipline is demonstrably high.

16. The stages will be as follows:

Stage 1 (during Phase 1 of project implementation) - the preparation and approval of credit union legislation.

Stage 2 (during Phase 2 of project implementation) - Stage 2 will cover:

- publication of credit union legislation;
- creation of a Credit Union Registry at the National Bank to register and supervise credit unions; the requirement will be:
  - publication of Registry function description and procedures; and
  - assignment and training of personnel.
- the training of personnel in participating NGOs as promoters - the training to cover credit union law and credit union principles and management practice.
- similar training for credit personnel at branches of the participating banks, not as promoters but to ensure that the working relationship between banks and credit unions, when established, is founded on understanding of credit union aims and principles and a higher level of confidence in banks' interest in the development of the small and very small enterprise.

Stage 3 (in Year 3 of the Project) the start of promotion of credit unions in small entrepreneur associations with at least two years of self-managed credit experience, an average repayment rate of 90 per cent or more and a membership of more than 150 members.

Stage 4 (in Year 4 of the Project) - start of credit union formation, registration and operation.

IV. Organization and Management

17. The organizational components of the project are identified below and the structure is shown in Figure 1 overleaf. The components are the following:

A. Rural Development Trust Fund (the Trust)

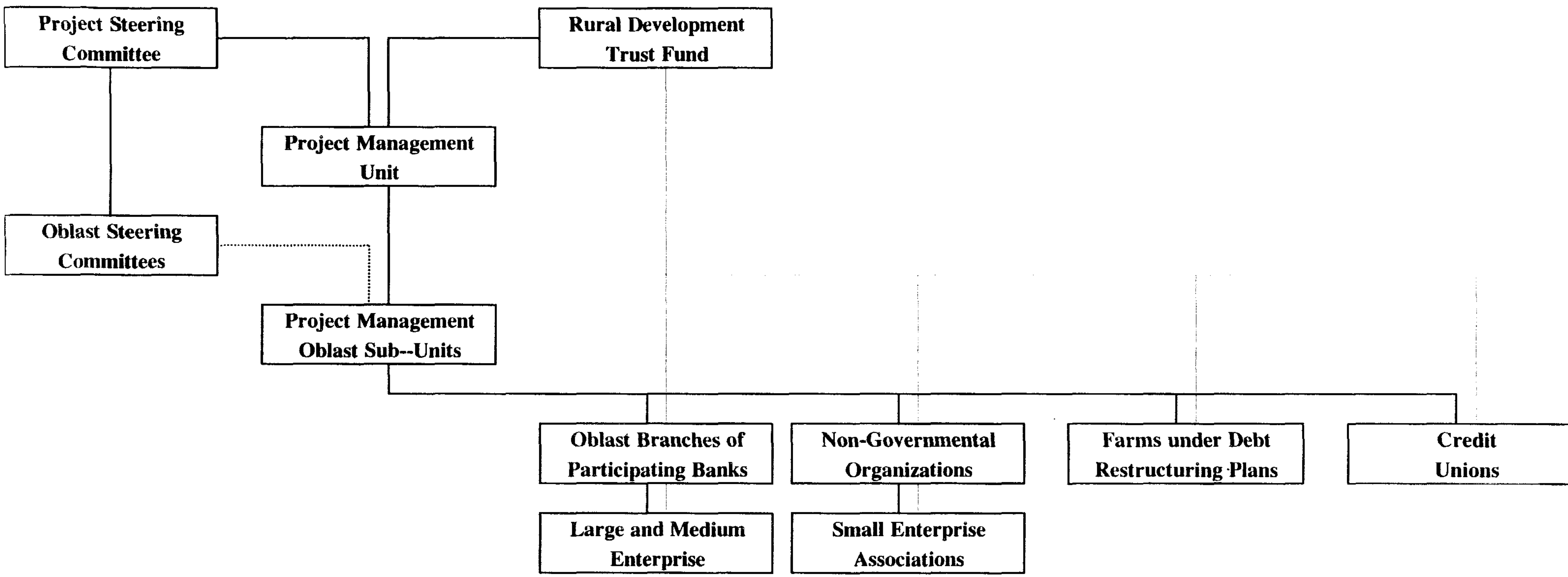
1. Trustees

18. A Rural Development Trust Fund (the Trust) will be established at the National Bank. Trustees will be:

- Asian Development Bank (the Bank); and
- National Bank of the Republic of Kazakstan (NBRK)

19. Other donors providing funds for the Trust may choose to be appointed trustees or may nominate an established trustee to act on their behalf.

Figure 1 Core Structure



2. Trust Managers

20. Trust Managers will be the Head of the Project Management Unit (PMU) and a counterpart appointed by NBRK. The trust managers will be responsible to the Trustees for the management of the Trust's operational activities.

21. Trust managers will report to the Trustees at such frequency and in such form as will be determined by the Trustees and will participate in Project Steering Committee meetings.

B. Project Steering Committee (PSC)

22. The PSC shall comprise the Bank, NBRK, a representative of additional donors (nominated by the donors), a representative of the Ministry of Finance, the Ministry of Economic Affairs and the Ministry of Agriculture, a representative of the participating banks (nominated by the banks) and USAID on behalf of the NGOs.

C. Project Management Unit (PMU)

23. The PMU will be managed by an international consulting company and/or individual consultants selected by the Bank. The PMU will comprise a central unit and oblast sub-units. PMU staffing will be as follows:

Expatriate Personnel:

PMU (Central Unit)
- project manager/credit specialist
- agronomist
- agricultural economist
- microfinance specialist
- credit union specialist
- short term specialist consultants

PMU (Oblast Sub-Units)
- manager/credit specialist
- agricultural economist

Local Personnel:
- lawyer
- accountant
- interpreter
- secretary

- accountant
- interpreter
- secretary

Note: Oblast ASF teams would be attached to PMU Sub-Units; ASF costs to be met as currently but increasingly by interest income.

D. Oblast Steering Committees (OSC)

24. The composition of OSCs will be:

- Oblast Governor,
- NBRK Oblast Director,
- Oblast Directors for Finance, Economy and Agriculture,
- a representative of the participating banks (nominated by the banks),
- a representative of the participating NGOs (nominated by the NGOs),
- PMU (Oblast Sub-Unit) manager.

E. Participating Institutions, Organizations and Agencies

25. Participating institutions, organizations, and agencies, and their main responsibilities are identified in Table 2.

F. Trust Role

26. The Trust will manage funds for credit for rural enterprise development and for the restructuring of rural debt arising from the privatization process.

27. Technical assistance payments, grant funds and training funds will be disbursed by the Bank or relevant donor separately.

G. Coordination with International/Bilateral Donors

28. The principal focus of the project is credit delivery, improved marketing framework and farm insolvency. The development of related aspects - business centers, local NGOs, farm machinery hire and maintenance businesses, for example - and the up-grading of banking skills have on-going international and bilateral programs or would be logical outcomes of current programs. The project will not open such programs where other donor programs can be co-opted to provide technical support and will endeavor to create arrangements that are mutually beneficial and cost-effective for the other donors, the target groups and the achievement of the project's goals.

H. Monitoring and Evaluation

1. Benchmarks

29. Baseline surveys will be conducted in each oblast at the start of operations in the oblast in order to fix the benchmarks against which the progress and impact of the project will be assessed.

Table 2. Participating Institutions, Organizations and Agencies

Institution	Main Responsibilities
The Bank	• funding • oversight and monitoring • trustee
NBRK	• trust domicile • trustee • credit union supervision
The Trust	• funds management • debt restructuring loans approval • monitoring of debt restructuring loans use
PSC	• policy and strategy approval • procedures approval • operational plans and budget approval • liaison with trustees
PMU (Central Unit)	• formulation of policy and procedures • preparation of operational plans • project implementation • PB and NGO selection • coordination of TA input • coordination of other donors' input • approval of PB and NGO credit plans • clearance of farm debt restructuring plans • monitor and supervise loan use and collection • liaison with PSC, OSC's, PBs and oblast authorities • preparation of progress reports
OSCs	• monitoring of implementation • facilitation of operations • facilitation of wholesale marketing operational framework • liaison with PSC
PMU (Oblast Sub-Units)	• operational plans implementation • farm debt restructuring investigation • clearance of loan proposals • supervision of loan use and collection • liaison with PBs and NGOs
Participating Banks (PBs)	• assist applicants with preparation of business plans • process loan proposals for medium and large enterprise • approval and disbursement of these loans • monitoring and supervision of these loans • collection and recovery of loans
NGOs	• develop local associations of private entrepreneurs • assist JLGs and other applicants prepare business plans • approval and disbursement of small and micro loans • monitoring and supervision of loan use • provide/coordinate loan technical support programs • promote and assist development of credit unions
Local Associations	• act on behalf of small and micro entrepreneurs • instill credit discipline, joint liability groups and thrift • ensure sound loan use and repayment • create basis for credit union foundation

2. Progress Review and Analysis

a. Monitoring

30. Monthly management information reports will be required from intermediaries and borrowers. The procedures prepared in Phase 1 will include pro-forma management information reports to be completed. Similar information will be sought from those international and bilateral programs that provide support assistance.

b. Impact Studies

31. PMU will collaborate with local universities and research institutions in the conduct of regular impact studies to determine the effect of the project's operations on the communities in which it is working, to identify areas in which modification is needed and to suggest possible solutions.

c. Project Evaluation

32. Once the project has been completed, an outside agency will be engaged by the Bank, at a time to be determined by the Bank and the Government, to undertake a full evaluation of the project and the benefits delivered.

V. Agricultural Policy and Operational Reform

A. Current Position

33. The position may be summarized by reference to the Bank's report *Strengthening the Implementation of Agriculture Sector Reforms*. The report observes that the reform process has introduced much new legislation and that a substantial policy agenda remains but that the accent should now be upon refinement for clarity and quality.

34. Progress, the report observes, will become increasingly dependent upon capacity to apply market economy principles to develop:

- land registration systems;
- land valuation and land management procedures;
- transformation of farming structures into profitable enterprises;
- restructuring and/or rehabilitation of agri-enterprise;
- rural credit delivery mechanisms;
- commodity marketing infrastructure and exchanges;
- modern information and data processing networks; and
- effective and efficient administrative systems, especially:
  - public accounting
  - taxation
  - judiciaries

B. Action within the Scope of the Proposal

35. Land registration, valuation and management are being addressed by the State Land Committee in a program undertaken with World Bank financial support. IT networks are being developed in relation to the land registration program. These fields are of importance to the objectives that the proposal sets but are not within the scope of the proposal.

36. Transformation of farming structures into profitable enterprises and restructuring and/or rehabilitation of agri-enterprises are given prominence within the proposal. The outcome of in depth diagnostic review of existing restructuring debt and of new applications should give an impulse to the transformation of farming structures as it will require the disposal of non-productive assets and may well include changes in land management and production practice. Restructuring and rehabilitation will focus upon potential viability and the specific needs of each unit examined; again, the need for asset disposal, management change and re-orientation of marketing policy and practice will be central considerations in the design of the remedial plans built for the individual enterprise and borrower.

37. Rural credit delivery mechanisms are a fundamental of the proposal. The aim is to permit diversity and flexibility in order to have several options available to the rural entrepreneur. A further consideration is the development of skills and experience at the level of the client, i.e. staff at oblast and rayon branches of banks, at the NGOs and at the associations and, in time, at the credit unions should have access to training in a form that places emphasis upon practical application.

38. Commodity marketing and exchanges will attract considerable attention because the introduction of warehouse receipt will need the underpinning of a reliable market and marketing system.

39. The purpose of engaging oblast officials in the oblast steering committee is to place strong emphasis upon such issues as taxation and judiciaries in the context of local enterprise development and the prosperity of the community. The PMU will raise these matters but the practical benefits, in terms of economic well-being at the level of the rural town and village, of applying existing legislation in the manner and spirit intended by the legislators may best be demonstrated in practice where the investment needs to be made.

VI. Credit

A. Credit Scope

40. Trust funds will be available to finance seasonal working capital, subject to certain limitations on the goods and/or services to be procured, and to finance medium - and long term (not exceeding 7 years) loans for enterprise recapitalization. No balloon payment lending will be permitted; loan principal repayments will be determined by cash flow projections. The Trust will also consider support for trader credit, machinery leasing, pledge and warehouse receipt financing.

B. Borrower Contribution

41. Borrowers will be required to contribute to the cost of their proposed investments. Their contribution will fund the difference between the total cost of their investment and the amount of the loan the borrower receives. The amount of the loan will be determined by the projected net cast flow from the investment, a minimum debt service coverage ratio, the interest rate, and the maturity of the loan, which would not exceed 7 years. Debt service coverage provided by net cash flow would be at least 2 times for medium and large enterprises and at least 1.5 times for all others and for rehabilitation work-out loans regardless of scale.

42. Compliance will be subject to close scrutiny and inquiry; failure to comply will disqualify the application.

C. Credit Channels

43. Credit will be made available for rural enterprise through three channels:

- the Trust - for farm and agri-business debt restructuring;
- participating local banks for credit to large and medium private enterprise; and
- participating NGOs for credit to small and micro-enterprise

D. Farm and Agri-Business Debt Restructuring

44. The Trust will set aside 40 per cent of available funds from which it will make loans, for recapitalization on the basis of restructuring plans acceptable to the Trust, to farms and agri-businesses that are potentially viable but are currently non-bankable or in financial distress.

E. Credit to Large and Medium Private Enterprise

45. The Trust will set aside 45 per cent of available funds to refinance up to 80 per cent of the value of those loans made by PBs to large and medium rural enterprise as may be judged eligible by the Trust. Use of Trust funds will be subject to regular scrutiny. PBs that contravene the Trust's terms will be disqualified from further eligibility and immediate repayment of the Trust's funds will be required.

F. Credit to Small and Micro Private Enterprise

46. The Trust will set aside 15 per cent of its available funds to finance such small and micro loans managed by participating NGOs, whether to individuals or associations of small entrepreneurs and joint liability groups, as may be judged eligible by the Trust. Participating NGOs will act as agents of the Trust, will be required to submit annual lending projections to the Trust and to finance 20 per cent of each loan from their own resources. Contravention of the Trust's terms will disqualify the NGO from further eligibility and immediate repayment of the Trust's funds will be required.

G. Use of Local Banks and NGOs

1. Use of Local Banks

47. The use of local banks is intended to assist professional skills upgrading, reinforce vigilance over loan portfolio quality and risk management and to strengthen banks' capacity to make longer term loans.

2. Selection of Participating Banks

48. Selection of participating banks will be made by the Trust's trustees. Banks wishing to participate should be in sound financial condition, verified by NBRK's Supervision Department and confirmed by a recent financial audit carried out by international auditors acceptable to the Bank and NBRK. In addition a due diligence audit, to be undertaken by the PMU and NBRK, will examine in detail:

- loan portfolio composition and quality
- quality of lending policy
- quality of lending procedures
- quality of lending practice
- internal controls
- management capacity
- discretion and accountability

49. Loan repayment levels would be expected to show a steady trend of increasing collections, with a current collection rate of not less than 75 percent, a trend of declining arrears age and full compliance with NBRK's instructions on loan account classification and provision.

3. Use of NGOs

50. The use of NGOs is intended to ensure equitable attention to small and micro-enterprise and disadvantaged groups which would otherwise be marginalized in the development process as unbankable. Moreover, the use of NGOs is intended to offset the shortening of commercial bank outreach as these banks withdraw from rural areas they judge unable to sustain formal banking services in the present economic climate.

4. Selection of Participating NGOs

51. Selection of participating NGOs will be made by the Trust's trustees. NGOs wishing to participate will undergo a due diligence audit by the PMU which will require the submission of audited financial statements and an assessment of:

- loan portfolio composition and quality;
- quality of lending policy;
- quality of lending procedures;
- quality of lending practice;
- internal controls;

- management capacity; and
- discretion and accountability.

52. Loan collection rates should show an upward trend and the current collection rate at the due diligence should not be less than 90 percent of payments due. Recovery of arrears, if any, should show an upward trend and not be less than 50 percent of outstanding arrears; arrears should also show a trend of declining age.

5. Additional Requirements

53. Selected personnel from PB branches in the oblasts in which the project will operate must undergo training in the procedures and practices to be applied to Trust funds and PBs will be required to adopt MIS formats and procedures that the Trust will introduce for the monitoring of funds use.

54. Selected staff at the participating NGOs will also be required to attend training in the policies, procedures and practices for lending related to small and micro-enterprise financing and in the associated MIS procedures.

H. Incentives to Participating Banks and Organizations

1. Debt Restructuring

Table 4. Incentives Attached to Debt Restructuring

Organization	Incentives
Government	• reduction in subsidy cost • formal repayment schedules based on cashflow • earlier retirement of debt
ASF	• regularized repayments of loan principal and interest • ∴ regular income to meet costs • staff skills enhanced
Clients	• detailed restructuring plans • assistance in resolving technical and commercial problems • swifter return to bankability

2. Bank Lending

Table 5. Incentives for Participating Banks

Institution	Incentives
Participating Banks	• access to funds for medium and long term lending • potential for diversifying the loan portfolio • attractive interest rates and spread • enhanced professional skills among staff

3. Small and Micro Enterprise Promotion

Table 6. Incentives for Participating Organizations

Organizations	Incentives
NGOs	• access to additional funds • wider scope for activity • larger numbers assisted • additional income potential • enhanced professional skills among staff
Associations	• access to additional funds • wider scope for activity • larger numbers assisted • potential for development of credit unions

VII. The Trust

A. Rationale

55. Most privatized rural enterprise faces financial difficulty, has current assets of little realizable security value for loans, and is under capitalized. Rural outreach of the banks is shortening and banks currently face liquidity problems that oblige them to offer only short-term finance. The dependence of off-farm enterprise on farm prosperity makes such enterprise, with few exceptions, equally unattractive to the banks. The rationale for the Trust is that further impetus to the restructuring work done by ASF is urgently required to return rural enterprise to profitability, that ASF does not possess sufficient capacity or scope and the urgency is such that delay until the banks are once more able to serve rural areas extensively would exacerbate the problem severely.

56. The Trust will supplement the ASF activity in the debt restructuring by providing additional funds and by upgrading the quality of the assessment of farm capacity to return to profitability. In addition, the Trust funds will enable banks to finance viable rural enterprise.

57. The Trust will also provide the means to encourage private initiatives in small and micro-enterprise by adding to the funds made available by NGOs and others. The funds currently available alleviate some of the impact of transition but transformation of the economy has yet to touch many who remain unemployed but who might, with access to some funds, put education and skills to profitable purpose. The banks will not serve these people. The Trust's aim at this level will be to fill the financing gap to some extent and to stimulate viable economic activity and, in so doing, demonstrate to the banks that lending in the rural small enterprise sector can be good business.

B. Functions

58. The Trust's functions are:

- to assist, through funding and technical assistance, the process of rural debt restructuring and to encourage farmers and business owners to adhere to the needed remedies;
- to offer incentives to banks to finance viable rural enterprise and to assist the banks develop the professional skills and capacity required to manage such lending; and
- to provide additional means to ensure incorporation of the small business sector and the disadvantaged into the process for revitalizing the rural economy.

59. The Trust's functions may be summarized as:

Table 7. Trust Functions

Function	Service Provided
Debt Restructuring Agency	• assistance to applicants in planning debt restructuring • finance for viable debt restructuring • finance for viable recapitalization • enhancement of skills of staff and entrepreneurs
Refinance Agency for Banks	• resources for viable rural enterprise financing • development of policies, procedures and practices for longer term lending • enhancement of staff professional skill
Lender (through agents)	• resources for viable rural small and micro-enterprise • development of alternative loan security instruments • refinement of policies, procedures and practices • enhancement of staff and borrower skills

C. Statutes

60. Draft statutes for the Trust are attached in Appendix 1.

61. A principal mandate of the Trust is to reduce the level of subsidy entering the rural economy and to use the funds saved to accelerate the process of reorganization and enterprise efficiency.

D. Resources

62. The resources of the Trust will support only the credit operation. The resources of the Trust will comprise:

- funds made available by the Bank;
- such contributions as other donors may make available;
- Government funds for the restructuring of rural debt; and
- interest income from loans.

63. Oblast administrations will be expected to make funds available to meet costs of associated rural infrastructure improvements.

E. Trust Management

64. Trust activities will be managed by the PMU manager and a counterpart appointed by NBRK. The Trust fund will concentrate its resources and activities in the functions defined above and will not engage in any other commercial eleemosynary activity.

65. The Trust will be managed professionally. Transparency will be a principal concern and the policies, procedures and practices employed will be designed to ensure the quality of appraisal, monitoring, supervision, collection, accounting and audit.

F. Trust Autonomy

66. The Trust will be autonomous in the financing decisions it takes. The sole criterion for advancing finance shall be the commercial viability of the proposal. Customary regard for the demands of zoning, environmental protection and technical feasibility will be observed but these will be pre-qualifying obligations that must be met by the applicant as criteria of eligibility for finance access.

67. Contributions, from whatever source, will be accepted if free from obligation that in any way prejudices the Trust's autonomy in making financing decisions. Funds with specific target group or economic activity focus or with specific purpose exclusions can be accepted, provided that the focus is not so specific as to obviate the Trust's discretion.

VIII. Debt Restructuring

68. The Trust's services for debt restructuring will include:

A. Existing Restructuring Plans

69. No plan remains totally relevant in any environment and should be subject to regular review to allow modification; some business exceed expectation, others fall short. This will be true of the ASF's agreements with those who have been recipients of its financial support.

70. The PMU, acting on behalf of the Trust and in collaboration with ASF personnel in the oblasts, will undertake a review of existing restructuring plans and progress at the clients' worksite. Where necessary, existing plans will be modified to reflect the demands of changes in enterprise circumstance. The Trust will engage specialist assistance, where necessary, to assist resident personnel in designing appropriate responses to technical and commercial problems.

71. The plans thus formulated will include the rationalization of operations, the sale of unproductive assets and changes in management where necessary.

B. New Applicants for Debt Restructuring

72. The service provided to new applicants will be in four parts:

- **review of the enterprise** - resulting in a report that identifies strengths and weaknesses, formulates strategies for reinforcing strengths and eliminating weaknesses and details the main actions required;

- **preparation of a detailed remedial work-out plan** - in which the client will have an active part because he/she will be required to certify in writing that he/she understands the requirements of the plan and will conform to it (a plan that does not involve the implementer in its making is less likely to succeed);

- **approval of the financing of the proposed plan and first withdrawals** - there may be several disbursements at set intervals and conditional upon satisfactory progress; and

- **monitoring and supervision of plan implementation** - the purpose is two-fold: 1) to ensure compliance with the plan and the payments schedules, and 2) to reinforce the business skills development process that began with the preparation of the plan.

C. Non-Agricultural Enterprise Development

73. Improved access to funds, including medium - and long-term financing, will be used not only to foster agriculture related investment but also to encourage new initiatives in enterprise in other sectors. The general improvement in financial well-being of the agricultural and agribusiness sectors should stimulate demand for other goods and services and, while viable agricultural enterprise and agribusiness of all sizes will attract a higher priority, the Trust will ensure that an equitable portion of funds flows into such enterprise. The rationale is that lenders avoid over-exposure in the two dominant sectors and diversify income flows, smoothing the seasonal fluctuations common in agricultural cashflows.

74. In the small and micro-enterprise sector the formation of credit unions will be a prominent feature of activity in the later phases of the project. A flow of savings throughout the year (in the form of share purchase or in deposits made through the credit union to a licensed deposit taker) from small and micro-enterprise in sectors other than agricultural will become a significant factor in the ability of the union to accommodate loan applications. Sectoral diversification of the activities of members helps to provide credit unions with the inflow that allows them to cater to those with seasonally volatile cashflows.

D. Process

75. The process by which the restructuring and implementation would be conducted does not vary. However, the plans developed will vary according to the capacity of the enterprise to operate viably. Enterprises will be classified in one of the following categories:

- not viable;
- potentially viable but unbankable without significant rationalization;
- potentially viable but require further rationalization to become bankable; and
- commercially viable and bankable.

76. The source of financial assistance will differ according to the category in which the enterprise is placed (see overleaf).

Table 8. Sources and Mode of Financing for Different Categories

Enterprise Category	Characteristics	Source of Finance	Mode of Financing and Assistance
not viable	• no exploitable resource that will respond viably to rationalization or new investment	ASF	• debt write off
potentially viable but unbankable without significant rationalization	• exploitable resources available • debt burden stifling initiatives • serious collateral deficiency • owner(s) capable • environment for change good	Trust and ASF	• direct lending from Trust • remedial planning assistance • supervision offers technical and business services and training • integrated links in markets available
potentially viable but need further rationalization to be bankable	• exploitable resources available • results of earlier rationalization encouraging • debt burden less troublesome • collateral deficiency less acute • needs additional rationalization • owner(s) dedication proven • environment for change good	Trust and ASF	• some ASF debt assistance • Trust's partial guarantee against commercial bank loan • supervision offers technical and business services and training • integrated links in markets available
commercially viable and bankable	• profitable • rehabilitation plan targets being achieved • access to security for loans is assured	Commercial Banks	• first come, first served • technical and business service and training available

IX. Eligibility for Financial Assistance

77. The criteria for eligibility are as shown in Table 9 below:

Table 9. Eligibility Criteria

The Individual Borrower

***for all applicants, whatever the circumstances of the enterprise*:**
• a permanent resident of Kazakstan
• of legal age
• of good reputation and no criminal record
• able to demonstrate adequate management, technical, marketing and financial skills
• have a good credit history and good trade reputation
***additional criteria for applicants seeking debt restructuring assistance*:**
• realistic concept of requirement for enterprise rehabilitation
• willingness to adopt rationalization and sale of non-productive assets

The Enterprise

for debt restructuring

• sector	• agriculture and agri-business
• status	• privatized: Akta issued
• size	• all sizes
• feasibility	• technical feasibility assured
• viability	• fundamental viability
• profitability	• operational profit from Year 2
• equity contribution	• net cashflow: debt service cover shortfall
• assets for loan security	• property mortgageable

for small and micro-enterprise

• sector	• all sectors
• exclusions	• existing loan obligations and real estate
• size	• less than 100 employees
• capital	• less than T 5,000,000
• annual turnover	• less than T 27,600,000
• feasibility	• technical feasibility assured
• equity contribution	• net cash flow: debt service cover shortfall
• assets for loan security	• 150% cover of loan amount
• repayment capacity	• operating margin covers debt service 1.5 times

for medium and large enterprise

• sector	• all sectors
• status	• legally registered
• exclusions	• existing loan obligations and real estate
• size	• not less than 100 employees
• capital	• not less than T 5,000,000
• annual turnover	• not less than T 27,600,000
• feasibility	• technical feasibility assured
• equity contribution	• net cash flow: debt service cover shortfall
• assets for loan security	• 150% cover of loan amount
• repayment capacity	• operating margin covers debt service 2 times

X. Terms and Conditions

78. The Trust will offer funds at the following rates of interest to its intermediaries to the enterprises, the commercial banks and the small enterprise associations (through the agency of NGO's)

Table 10. Trust Rates to Intermediaries

To Whom	Rate
To commercial banks (refinancing rate)	Trust's cost of funds + 3 percent
To small enterprise associations	Libor + 2 percent

A. Small and Micro-Enterprise

Table 11. Terms and Conditions (Small and Micro Enterprise)

	Micro-Enterprise	Small Enterprise
maximum maturity of first loan	9 months	12 months
maximum maturity of repeat loans	12 months	24 months
maximum interest grace period	90 days	90 days
payment schedule for interest	monthly payments	monthly payments
principal repayment (first loans)	determined by cash flow projections	
principal repayment (repeat loans)	determined by cash flow projections	
loan denomination	US Dollar	US Dollar
repayment denomination	Tenge[1]	Tenge[1]
maximum loan amount (loans)	USD $500 (T 35,000)	USD $2,500 (T 175,000)
maximum loan amount (repeat loans)	USD $1,000 (T 70,000)	USD $3,500 (T 245,000)
interest rate	Libor + 12 percent[2]	Libor + 12 percent[2]
drawdown period	30 days	30 days
borrower equity contribution	net cash flow: debt service cover shortfall	
security requirement	150 per cent of the value of the loan	

Notes: 1 Tenge equivalent, at the exchange rate of the day of payment, of the Dollar value of the amount due.

2 The spread does not include the management fees to be negotiated with ASF and the NGOs for acting as the Trust's agents. Associations should restrain administrative costs in order to maximize the association's surplus, from which reserves will be set aside to meet provisions for doubtful and bad debt. Surpluses after reserves for provision will create the endowment for future credit union status, thus relieving members of having to find a significant sum to comply with charter capital requirements.

B. Medium and Large Enterprise

Table 12. Terms and Conditions (Medium and Large Enterprise)

	Medium Enterprise	Large Enterprise
maximum loan term	5 years	5 years
maximum interest grace period	90 days	90 days
payment schedule for interest	monthly payments	monthly payments
principal repayment	determined by cashflow projections	
loan denomination	US Dollar	US Dollar
repayment denomination	Tenge	Tenge
maximum loan amount (loans)	USD $ 250,000	USD $ 500,000
interest rate	market rates	market rates
drawdown period	30 days	30 days
borrower equity contribution	net cash flow: debt service cover shortfall	
security requirement	150 per cent of the value of the loan	

Notes: see Table 10.

C. Clients Under Restructuring Plans

Table 13. Terms and Conditions (Debt Restructuring)

maximum loan term	5 years
maximum interest grace period	180 days
payment schedule for interest (Year 1)	quarterly
payment schedule for interest (from Year 2)	monthly
principal repayment	as determined by the projected cashflow
loan denomination	US Dollar
repayment denomination	Tenge
maximum loan amount (loans)	USD $ 500,000
interest rate	Libor + 10 percent[2]
drawdown period	30 days
borrower equity contribution	net cash flow: debt service shortfall
security requirement	100 per cent of the loan value

Notes: see notes to Table 10.

XI. Policies and Procedures

A. Transparency and Impartiality

79. Uniformity of policy, procedure and practice will be fundamental to transparency and impartiality upon which the Trust will insist. The Trust will prepare and publish manuals of procedure and practice and will install a system of lending audit that will focus upon conformity and lending quality.

B. Small and Micro-Enterprise Lending

80. The policies and procedures for small and micro-enterprise lending are included as an appendix in Part II of the Draft Final Report. The manual includes a section on management information systems for lending and client benefit monitoring. The manual is intended for use not only by the NGOs acting on behalf of the Trust but also for credit unions, once established.

C. Medium and Large Enterprise

81. A similar manual will be published, for use by the participating banks in making loans for which refinancing is sought from the Trust. The manual will follow the loan cycle related structure and the pro-forma document format will be retained but will reflect more detailed data used to mange the risks of medium - and long-term lending. The business plan, for example, will require more specific detail in marketing, production and financial projections and the reports for supervision and variant investigation will reflect the added sophistication of the enterprise and the term of lending. Treatment of legal aspects of lending, in terms of documentation and perfection will be more detailed to reflect the importance of accuracy to loan safety.

82. The manual will, again, not only be a reference work but also a source of training materials. It will contain additional sub-sections, guidelines to technical aspects - for example, analytical methods for appraisal and for asset valuation.

D. Debt Restructuring

83. The manual prepared for medium - and long-term lending will be the basic source of procedure and pro-forma documentation for the processing and management of loans to enterprise for rehabilitation. The **Blue Book** currently in use by ASF will be modified and incorporated into the manual in order to retain the essence of the ASF program.

84. The prospects of an enterprise being successfully turned around will be enhanced by the rigorous application of tests of viability throughout the life of the loan and the content, structure and methodology of procedures and practices will be designed to this effect.

E. Environmental Due Diligence

85. The Trust will publish a manual of procedures for the conduct of environmental due diligence. All enterprises financed through Trust funds will need to meet the criteria of acceptable standards set out in the manual. Due regard will be given to the size of the enterprise, the type of enterprise and the capacity of the enterprise to assume costs for environmental safety. However, all lenders will be required to emphasize the benefits of simple pollution protection practices, not only to the community but to the enterprise itself.

F. Penalties

86. The incentives to borrowers and lenders have been described earlier. Participation also carries obligation and the incentive to observance of obligation is continued participation.

87. The Trust's obligations extend beyond those of the declared aims and objectives and include accountability to the donors, the Government being prominent. The Trust will pursue vigorously for full restitution of all funds outstanding, plus all fees and charges accruing, from any institution or organization failing in its obligations to the borrower or to the Trust.

XII. Flow of Funds

88. Figure 2 overleaf illustrates the flow of funds within the project.

A. Credit Decision Process

89. Figure 3 overleaf presents the flow in the credit decision process.

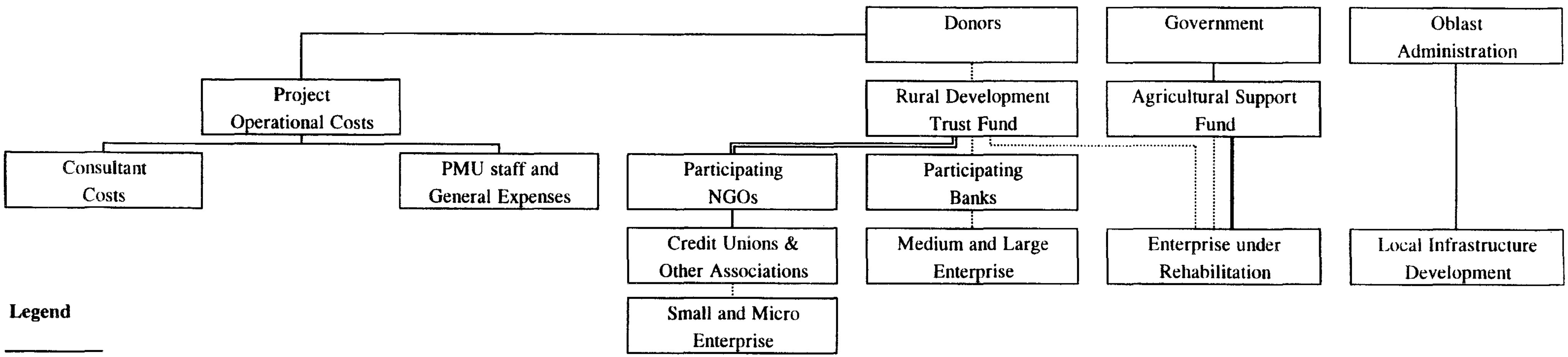
B. Risk Management

90. Risk management is examined in detail in Part II of the Draft Final Report. Risk management is not confined to a few phases in the lending process but is a continuous process throughout loan life. Some facets of risk management are more prominent but failure to apply prudent control in the less evident areas prejudices loan recovery equally. Loan documentation and files in various institutions suggests that most take precautions but that there are deficiencies that could be costly. The following will be the focus of Trust and NBRK attention in judging the quality of participating institutions' risk management:

1. Eligibility and Creditworthiness

91. Before creditworthiness checks are undertaken, compliance with eligibility criteria should be checked. Creditworthiness checks are not confined to checks with other financial institutions but include checks of trade reputation. Confidentiality requires that the applicant authorize access to information and a certificate to this effect should be signed by the applicant; refusal to authorize access should bring the processing of the loan to a halt.

Figure 2 Funds Flow



Legend

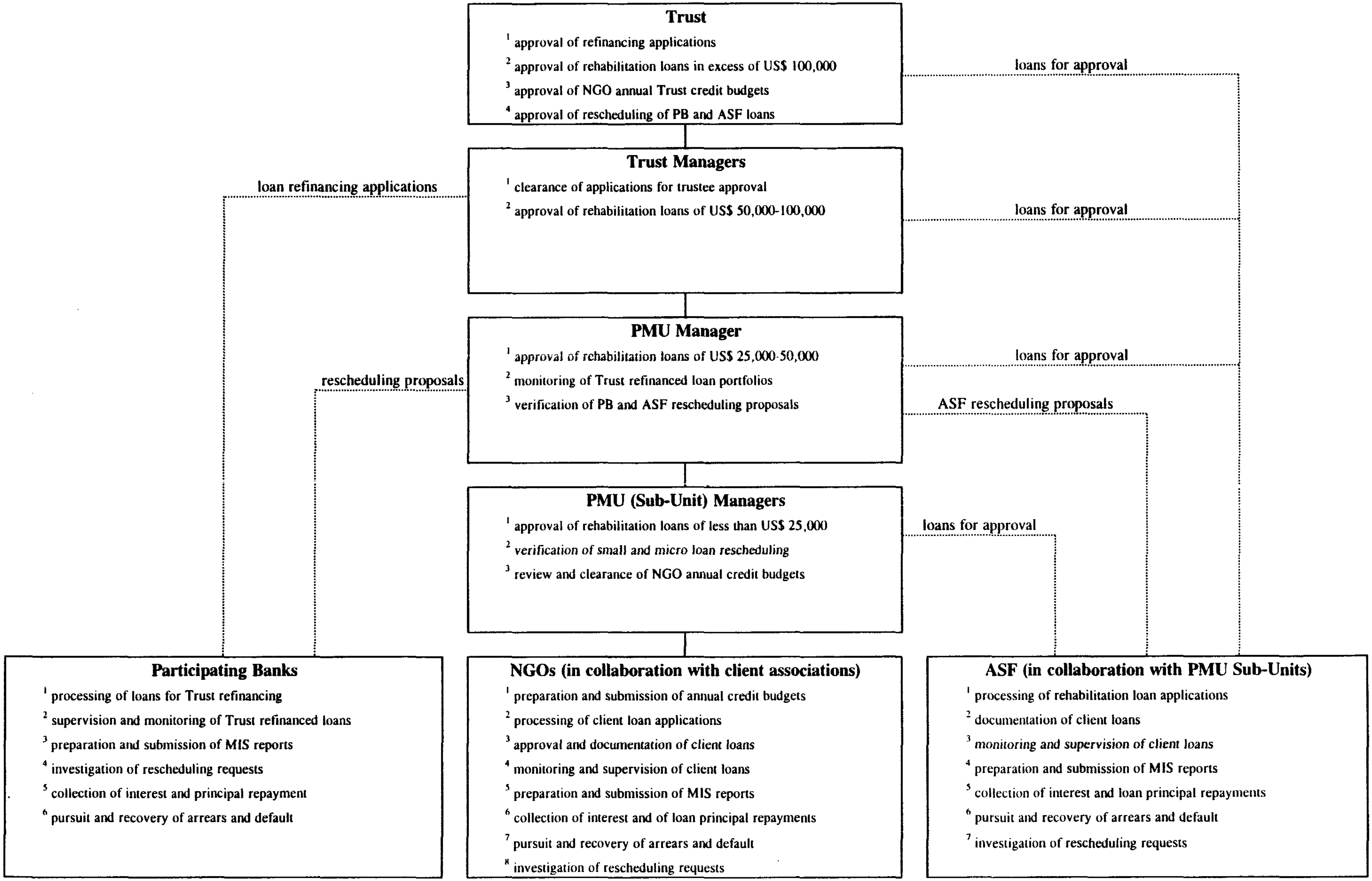
direct payment

loan (issued and recovered)

Loan Funds through Agents: NGOs, CUs

grant or write-off

Figure 3 Loan Decision (and Responsibilities) Flowchart



92. A record of checks made must be kept and the results should be maintained in the loan working file.

2. Business Plans

93. The detail of the business plan will depend on the complexity of the proposal. At a minimum, the business plan will define objectives clearly and should demonstrate knowledge of procurement, processing, marketing, management and costs and returns. A thoroughly prepared plan helps ensure its smooth implementation as many potential difficulties will have been foreseen and plans made to overcome them.

3. Appraisal

94. Appraisal is the process of testing the assumptions and calculations contained in the business plan for accuracy and applying tests to determine capacity to absorb adverse change in the environment without loss of fundamental viability.

95. A feature of many business plans is the inadequacy of the marketing information - detail should include as a minimum access to the markets selected, quantification of demand, market trends, competition, market share targeted, prices and costs. This detail should be subject to vigorous examination since it is the platform on which the proposal rests.

96. Frequently output capacity is over-estimated, staffing levels are inappropriate to the investment and prices have no clear relationship to costs.

97. Any doubt in any aspect should be referred to the applicant and, if the explanation is inadequate, the loan should be declined.

4. Security

98. Assets taken as security for the loan are collateral insurance against the loan going bad; they are not a substitute for viability. Moreover, taking security is intended to ensure credit discipline, the possible loss of assets being a restraint to misuse of the loan; however, security is an effective restraint only if clients are convinced that the seizure and disposal of assets given in security of a loan will be pursued vigorously.

99. There is a need for lenders to be more innovative in adopting other instruments of security than the current reliance upon machinery and equipment and the season's harvest. Other forms of security can be obtained through hypothecation of future assets and the acceptance of warehouse receipts.

5. Documentation

100. The quality of documentation - contracts, security documents, demand and seizure documents, etc. - and their safekeeping is vital to the lending institution's assurance of repayment. The requirement for each form of security document is that they be correct in all detail since any error or omission can render

the instrument invalid. The perfection of contracts and security documents must be subject to the closest scrutiny before any loans are approved for disbursement.

101. Originals of such documents are held in a separate security packet and should be placed in a fireproof safe. Custodial responsibility must be assigned to a single person and access to these documents should be closely controlled.

102. Failure to advise the guarantor of any and all change in the terms and conditions of the loan guarantee and to obtain the signed agreement of the guarantor to maintain the guarantee in the changed circumstances may void the guarantee.

6. Records

103. The maintenance of complete records is essential to good loan management. The principal deficiencies are:

- originals of contracts and security documents are held in working files;
- absence of manual records - loan cards, etc. - in case of computer failure;
- absence of control sheets on which to record movements of loan funds;
- absence of disbursement authorizations and receipts for goods delivered;
- absence of supervision visit reports in the working file; and
- absence of loan term extension/rescheduling investigation reports.

7. Disbursement

104. No disbursement should be made without the client's authorization in writing. Such authorization should be made on a pro-forma document to ensure uniformity and clarity - such documents can be vital in the event of dispute over loan use and release.

105. No disbursement should be made without a check of receipt of the goods or services for which the funds have been released. A pro-forma document detailing the goods and services, the shortfalls (whether in quantity or quality) and the price paid should be completed during the delivery check, made by the client and supervising officer, and should be signed by the client and countersigned by the supervising officer.

106. Where the disbursement includes the purchase and installation of equipment and machinery, the checks of receipt will include an additional visit at the time of the trial run to ensure that the equipment meets the operating specifications - these are vital to the business achieving the output assumptions in the business plan.

8. Monitoring

107. Imperfect information continues to impede the lender once the loan has been made. Lenders seek to minimize this imperfection through monitoring loan account activity and results and through physical supervision.

108. Monitoring, even of micro loans, is a basic component of portfolio management. There are two aspects to monitoring:

- **individual enterprise monitoring** - as a minimum, clients should be required to maintain simple records that will permit submission of management accounts that cover six elements:

  - income
  - expenditure
  - stocks
  - creditors
  - debtors
  - cash

  This information becomes the platform for developing stock, creditors, debtors and cash management policy - which is in the interest of the client. The management account submissions can be used by the supervising officer not only to judge the viability of the enterprise but also to guide the client in developing professional skills.

  Monitoring of individual account performance and the classification of that performance is a NBRK stipulation for second tier banks; whether non-financial institutions are required to report this performance or not, prudence suggests that application of the classification categories is in the interests of the lender.

- **portfolio management** - balanced risk within the overall loan portfolio must be a predominant concern: over-exposure in any sector or sub-sector or to any single borrower or enterprise must be identified rapidly and redressed.

  Portfolio management is concerned with the quality of the loans outstanding, the potential for loss and the areas most susceptible to adverse change. It also measures the lender's performance in relation to performance targets.

  The tool for monitoring portfolio performance is a management information system (MIS). The sum of the manual and computerized systems constitute the MIS. MIS reports in general should be drawn from a (computerized, if possible) database on applicants and borrowers and the loan ledgers. The reports should be designed to be:

  - loan specific, giving detailed loan parameters on a loan-by-loan basis for better tracking of loan performance and comprehensive loan management;
  - position-specific, so that individual credit officers and their Managers receive detailed reports only for the loans under their supervision, making reports more useful for monitoring performance, establishing priorities and determining specific necessary action;
  - sector-specific, so that sectoral performance can be more easily monitored and strategic decisions on portfolio priorities taken by senior management; and
  - comparative, so that each management level can compare the performance of the loans or area under their or their subordinates' control with other loans or areas, in order to

enhance appreciation of sectoral or regional differences in the portfolio, assist with strategic portfolio management and monitor performance at all levels.

The reporting requirements should generally be monthly and should be:

- a loan report for management and work planning purposes; and
- a summary report for senior management and others authorized to receive the information.

The loan MIS report provides a complete listing of loans, classified and subtotaled by loan class. The percentage recovery (and the movements from month to month) provide a guide to the long term performance of the portfolio; these percentages provide some guide to the provisions for bad debt which will be required. The aging of the overdue balances provides an indication of the collectibility of the overdues. Generally, the older the overdues, the less the chance of collecting the debt. The information concerning the collection rate provides a continuous measure of performance in meeting the annual collection target.

This information can also be subtotaled by credit officer and loan status category. This provides a guide to the performance of the portfolios of each credit officer and should be used by the individual credit officer to schedule supervision visits. It also allows the credit officer to see readily where effort is required to improve recovery, both by status category overall and by individual loan. It also allows the credit officer to identify whether a small number of loans are responsible for depressing the recovery performance or whether the problems in the portfolio are widespread.

The MIS summary provides an overview of portfolio performance in sufficient detail for senior management and other recipients to inquire into different aspects of each lender's loan portfolio. Summary subtotaling by loan class, credit officer, subsector, loan size and region are examples of how the presentation can be used to provide management with different perspectives on the portfolio.

9. Supervision

109. Supervision is the physical review of progress. It is a comparative exercise that uses the business plan, whether the original or any amended/updated version, as the basis for the assessment of progress. It is not a policing action and, indeed, should be the vehicle for enhancing the business and technical skills of the clients.

110. Frequency, and content, of supervision visits should be related to loan classification - satisfactory accounts need less frequent visits than those that have arrears. Visits should have two outcomes:

- a plan for work between the current visit and the next visit; for problem loan accounts all remedial action must have the borrower's written affirmation in order to avoid later recrimination that the business failed because remedies were imposed by the lender against the judgment of the borrower; and
- a report, to be placed on the working file, that details succinctly progress, shortfalls related to the projected targets, the causes and the remedies and work schedule agreed.

10. Variation and Rescheduling

111. Variation and rescheduling should be exceptional. All variation and rescheduling requests should be investigated at the same depth as the original appraisal. The investigation ought to be less time-consuming because the need should have been identified during normal supervision and fully reported. Variation and rescheduling should be investigated by an officer other than the supervising officer in order to minimize subjective assessment. Where there is the slightest doubt about the safety of the lender's funds, variation or rescheduling must be denied.

112. Rescheduling of Trust funded loans will be permitted, when circumstances warrant, but not encouraged. Where natural disaster causes a borrower(s) to be unable to meet repayment schedule, each rescheduling case will be subject to careful verification of damage incurred and the Trust shall be advised, in writing, of all variations with details of the new repayment schedules.

113. All rescheduling of Trust funded loans to medium and large enterprise and for debt restructuring will require written clearance from the trustees before the variation contracts may be signed and become effective. All rescheduling of small and micro loans, other than in circumstances of *force majeure*, will require written confirmation from the PMU Sub-Unit.

11. Arrears and Default

114. The pursuit of arrears and default should be vigorous and immediate. Policy and procedures should be precise about the timing and form of the lender's reaction to arrears and default and no latitude should be permitted. Leniency, for whatever reason, without investigation sends signals to other clients and weakens credit discipline. Investigation of arrears, once arrears persist, should be impartially applied and, where the fault merits, variation or rescheduling can be considered.

115. Default is the lender's loss - not all defaulters default for lack of funds.

12. Technical and Financial Risk

116. Observance of the fundamentals will reduce risk but no lender should be unwilling to consult with specialists when technical or financial aspects prove exceptional in their complexity.

13. Delivery Systems

117. There is risk associated with the delivery system. Viability and integrity of institutions acting as channels for funds need to be investigated as carefully as the borrower. Eligibility to act as an intermediary should be based on clearly defined criteria and should be subject to regular review. In part, the review is maintained by the MIS reports of loan portfolio status but regular reviews of the institutions' solvency ought to be carried out. Compliance with policy, cost of delivery, and the quality and impartiality of service should also be a focus of regular review - weak cost control may be offset by a diminution of quality of service.

XIII. Issues In Focus

118. The project will bring into sharper focus, through practical experience, the following issues:

A. Credit

119. EBRD experience suggests applicant articulation of the proposal is often as much a constraint to financing as the need for credit. A good business opportunity is prejudiced as a bankable proposal, if the plan is inconsistent and not fully coherent.

B. Skills of Financial Institution Staff and of Entrepreneurs

120. The problem lies not in the ability to comprehend and apply the basic concepts but in the lack of skills and knowledge. There may be a further constraint in the case of bank officers - the lack of incentive: personnel management in most banks is meticulous in many facets but performance assessment, assessment-based incentives and promotion is an area that warrants attention; for the branch field officer, the incentive to visit clients is negligible and is further reduced by the lack of mobility.

121. Training for bank personnel in the branches, for members of local NGOs that are involved in lending, for borrowers and for entrepreneurs in general will be a practical concern of the project and is treated in more detail below.

122. The issue of incentives and performance assessment is one that cannot be addressed in detail by the project but will arise frequently in lending audit assessment of portfolio quality.

C. Efficacy of Debt Restructuring on Farm Viability and Rural Prosperity

123. Throughout the project's life the monitoring of debt restructuring impact on the individual units and on rural communities will be of considerable interest and impact and benefit studies will be conducted in collaboration with local authorities. The results of these studies will be compared with the progress reports from supervising officers, borrower management information and lender portfolio status; where necessary, the results will be translated into policy and procedure changes.

124. A further interest will be to determine what production mixes and patterns appear to give the best return to the investor and to examine the possible effects in terms of logistical support, market potential and price response since these will be of importance to sub-sector exposure limits and to market policies and frameworks for the development of marketing channels and wholesaling.

D. Land Mortgage

125. Although the necessary legislation[1] exists for the mortgage of land use rights and a value is set upon land at transfer into private ownership, the mortgage of land to financial institutions faces

[1] Decree (Law of Real Estate Mortgage) of 10 December 1993; Decree (Rates of Payment for land sold or granted into Private Ownership) N576 of 8 May 1996; and Resolution (Mortgaging Land Use Rights) of 6 June 1996.

difficulties in that a market for rural land hardly exists. There is a rental market but the term of the rental is single season. Rental rate does not appear to reflect a value of production foregone by the lessor, although the amount paid may be perceived by the lessor as better compensation than working the land - to understand rental values better it would be necessary to examine specific cases in detail.

126. Rental rates might prove a more satisfactory means of setting a safe realizable value upon land as security for a loan but there will be a need to examine the rental market in some depth in order to gauge demand for rental and the effect of introducing rent-based mortgage values upon rental price levels.

E. Lien and Hypothecation of Current and Future Assets

127. The contracts for seasonal lending, apart from those under the promissory note scheme, do contain, in effect, lien over future production. Security in the form of lien over assets created by the loan, customarily vehicles and equipment procured by the loan, is accepted. Stocks of raw materials from manufacturing enterprise are also acceptable but finished goods in many cases are not attractive to the lender.

128. Examination of the use of hypothecation as a means of widening the asset base for loan security will be an area of regular review with the participating financial institutions.

F. Savings Mobilization

129. Access to small and micro credit will require a pre-application period of a savings and the maintenance of a minimum savings level throughout loan life. At each step up in loan size the qualifying and minimum savings level rises. The purpose of the savings requirement is to create, in the first instance, additional assets with which to secure the loan and, in the second, a reserve upon which the entrepreneur can fall back in emergency. In Part II of the Draft Final Report it is proposed that savings be deposited with the Narodny Bank in a single account opened by the depositor's association or the NGO managing lending to the association and the records of individual deposits and withdrawals be maintained by the association or the NGO. The principal concern will be the safety of savings.

130. NBRK's regulation and supervision of banks and its status as a trustee will enable the Trust to maintain a close watch on the solvency of the deposit-taker but the Trust will not be able to guarantee the deposits. However, the Trust will work with NBRK and other institutions in seeking means of giving depositors greater security and in designing other forms of savings that will spread the risk of loss; life assurance, used as loan security under a deed of defeasance, might be a means of giving the potential borrower at all sizes of enterprise a useful instrument of savings and collateral.

131. The Trust, through its regular surveys for benefit monitoring, will maintain a constant review of savings capacity but will not fix loan limits as a multiple of savings, at least not until there is better empirical evidence of enterprise ability to generate savings at a level commensurate with a multiple of three or four to one and to maintain that level throughout loan life.

G. Warehouse Receipts

132. Warehouse receipts may be a means of breaking the receivables cycle and of releasing working capital to farms and agribusiness. It would be of considerable value to those working under rehabilitation plans.

133. Warehouse receipts in mature market economies are common currency in trade. Commercial law establishes the obligations and rights of the parties involved in the storage and deposit of commercial goods in warehouses. The essence of warehouse receipt is confidence and access to restitution. Reliable warehousing trade allows ownership of goods deposited to be transferred without the movement of the goods; ownership is transferred through the transfer of title to the warehouse receipt by endorsement of the receipt.

134. The value of a warehouse receipt lies in its acceptability in the market. For acceptability to be general and value to be sustained, the warehouse receipt must offer the holder the assurance of a national, impartial and competent certification. This may not be possible at present in Kazakstan outside the grain trade and some other commodities such as wool, cotton, sugar and tobacco.

135. A depositor, of grain for example, will receive a receipt stating the amount and the grade of the grain deposited and the grain may not be removed without presentation of the receipt of deposit. The grain is stored in bulk by grade but ownership may be several or many. A depositor may place his/her grain in bulk but request receipts for partial amounts, to the aggregate of the deposit made, since smaller lots may be more readily negotiable.

136. At the time of sale of the grain, the depositor/vendor records the name of the buyer on the receipt, signs below the name of the new owner and passes the receipt to the new owner who may now go to the warehouse and withdraw the grain (or whatever goods the receipt covers) or who may on-sell the receipt to another buyer. The number of times the receipt is transferred does not affect the location of the goods bought/sold unless the buyer wishes to remove the goods from the warehouse, at which time the receipt is presented and possession is taken of the goods.

137. The additional value of warehouse receipts is that they can be placed as security for a loan: the warehouse receipt is assigned to, and deposited with, the lender. The lender, if the warehouse receipt system is soundly based, tightly regulated and legally enforceable, is reasonably assured of clearing the debt in the event of default by the borrower. When repayment of the loan is made, receipt is returned to the borrower; in the event of non-payment, the lender presents the receipt for the goods to the warehousing enterprise and removes them for sale or, more simply, sells the receipt on the commodities exchange or to clients in commodity dealing. Distance is no constraint to sale and transfer. Banks and other agencies act as intermediaries for a fee.

138. At regular intervals throughout the period in which the goods remain in the warehouse, the owner of the goods is required to meet storage and other charges. At the time of a transfer of ownership, through the purchase of the receipt, liability for those charges is also transferred but charges accruing up to the date of transfer remain the liability of the receipt-holder (owner) before the transfer. The charges outstanding are usually discounted from the sale price.

139. The project will aim to develop the warehouse receipt as a recognized instrument of trade and as an acceptable asset for the securing of credit.

H. Borrower Contribution

140. Borrower discipline is enhanced by his/her having a significant stake in the project financed. Borrower contribution towards the cost of the investment proposed for financing has been set in recognition of the straits of rural economic life. Lenders will be required to insist upon the contribution requirement being adhered to and lending audit will examine the composition and value of contribution to ensure that there is compliance. Where compliance is found to be artificial, the loan will be recalled and losses will be borne by the lender.

I. Loan Denomination, Interest Rates and Foreign Exchange Risk

141. Loans will be denominated in US Dollars and interest rates will reflect market rates for the US Dollar. However, the foreign exchange risk will be transferred to the borrower by requiring payment of interest and loan principal repayment in US Dollars or in Tenge; Tenge repayment will be at the USD : Tenge rate of exchange prevailing at the date of payment.

142. Trust funds will be extended to PBs, for the refinance of loans to medium and large enterprise at Libor + 5 per cent; the rate for on-lending by PBs will be the market rate. The spread for PBs allows for capital accumulation and the risk but this may not be passed to shareholders as dividends. Audit will be required to examine costs and margins associated with financing with Trust funds to ensure margin use is commensurate with the intention.

143. Finance for debt restructuring will be extended by the Trust through the ASF, working in collaboration with the PMU and PMU Sub-Units. ASF will act as the Trust's agent and will receive a fee, the level of which will be established by the trustees, to meet its operating costs.

144. Finance of small and micro-enterprise will be extended by the Trust through selected NGOs, working in collaboration with the PMU Sub-Units. The selected NGOs will act as agents for the Trust and will receive a fee, the level of which will be established by the trustees, to meet their operating costs and to build a reserve from which to endow credit unions when formed.

145. The Trust will examine the extension of credit for the pre-financing, through traders, of agricultural production.

146. The Trust will scrutinize the use of its funds with care to ensure that lenders do not mis-categorize enterprise in order that the borrower may benefit from unentitled access to funds for which the enterprise is not eligible. Where such is found to be the case, the loans will be recalled immediately and the lender will bear any loss ensuing.

J. Markets and Marketing

147. The project will examine, with the local authorities and technical institutions, the marketing (including marketing information, transport and storage) constraints faced by rural enterprise and will explore avenues for the relief of these constraints. It is anticipated that the role of the local authorities in the development of a favorable market environment will be the most significant.

K. Technical and Training Support

148. The project cannot provide the full range of support that might accelerate the speed of economic up-turn and nor can it deploy the expertise that others have gained, either for reasons of cost or from absence of previous input in Kazakstan.

149. TACIS and USAID has been approached to consider how it might align some of its assistance with the activities of the project in those fields where the expertise gained by TACIS and USAID through current or past project implementation in Kazakstan might be profitably allied to the credit program. The areas of interest are:

1. Training of Banking Personnel

150. Training should be taken to the oblasts, with credit staff as the priority, and offering courses for in-service training related to the processing and management of credit for short, medium and long term. The aim would be to build on TACIS and USAID experience in this field from the banking training schools they have established in Almaty. Each of their bank training programs has been in existence since early 1994 and has developed course materials in Russian for over 25 specific banking courses. Each training courses has a one to two week duration and the cost is borne by the participant. In addition, the banking schools have successfully trained local trainers to teach all of the offered courses.

151. Were such training available, TACIS and USAID might consider including short courses for the training of NGO personnel and the management's of associations and credit unions. This would blend well with the TACIS program for private farmers organization support.

152. Financial Institutions which qualify as participants in the Project Proposal will be required to have all personnel involved in the implementation, operation and supervision of the project certified through a training program. The certification process will be as follows:

- Senior Management. Required to attend six, two-week bank training courses that include an in-depth examination of the basic fields indicated in paragraph 153. Participation in a study tour to visit a ongoing project in Eastern Europe or the Former Soviet Union and a minimum of two, two-week continuing education courses will be required after each year;
- Loan Officers. Same as Senior Management; and
- Staff. Required to attend three, two-week bank training courses that will include a comprehensive review of the basic fields indicated in paragraph 153. One month continuing education courses after each year.

153. A detailed training needs assessment for senior bank management and those engaged in credit operations is given in Table 14. The basic fields to be covered would be:

- the business plan;
- financial analysis;
- appraisal;
- monitoring and supervision;
- variation and recovery; and
- portfolio management.

2. Private Farmers Organization Support

154. The value of this program is not only in the organizational aspects but in the technical features that enable the members to improve production practices and productivity. The expansion of this program to provide backing to credit for small and micro enterprise associations in preparation for, and during use of, the Trust's funds would give additional assurance of sound risk management practice and would offer borrowers the prospect of better returns on their investment.

3. Business Advice

155. TACIS is involved in the development of business skills. The development of business skills at all levels would be a major contribution to the profitable use of credit. The Small Business Center network needs an outside stimulus in order to move beyond the current somewhat passive role. Their contribution, through advice, training and commercial venture involvement (as some already demonstrate), would be of real value were TACIS to extend its present support for business planning to the oblasts, using the Small Business Centers as the focal point for business skills development. Business planning assistance is already offered through the Peace Corps Volunteer support to Small Business Centers but TACIS might complement this service by upgrading the business training that the centers offer.

4. Technical Services

156. Banks do not have the technical expertise required for long term lending to agribusiness and farms; the technical services in the oblasts lack the market orientation that would make their technical advice more germane to the lending decision. TACIS could provide the means whereby both gain the necessary skills and experience needed.

157. There is a need for detailed examination of gross margins for agriculture and the preparation of a manual of gross margins related to regional production potential and tying this to the development of the working relationship between the banks and the local technical services would be invaluable. TACIS has undertaken similar work in the Kyrgyz Republic and some work has been done on gross margins in Kazakstan.

Table 14. Training Needs related to Credit Delivery

The Business of Banking	Law related to Banking	Credit Operations		The Business Plan	Enterprise Accounting	Information Systems	Management in Banking	Sub-Unit Supervision
Services that Banks offer	Banking Law	The Principles of Lending	Collection and Recovery	Structure of a Business Plan	Accounts for Business	Computer Literacy	Human Behavior	Lending Audit
Bank/Client Relationship	Law related to Loan Security	Project Identification	Lending for Agro-Industry	The Marketing Plan	Management Accounts	Information Security	Personnel Policies	
	NBRK Regulations	Inquiry Counseling	Lending for Small Business	Defining the Assumptions	Budgeting and Planning	MIS Development	HR Planning	
	Securities and Documentation	Appraising Proposals	Portfolio Management	Preparing the Cashflow	Performance Assessment	MIS for Portfolio Management	Performance Appraisal	
	Law related to Land Mortgage	Financial Analysis	Security Valuation	Defining Management Capability	Interpreting Financial Statements	Management Accounts	Remuneration and Incentives	
	Law related to Pledge and Lien	Marketing	Financing Requirements	Debt Service Coverage	Cost Analysis	MIS for HR Management	Manpower Development	
		Monitoring and Supervision	Provision and Write Off		Budget Control		Managing Training	
		Variation and Rescheduling	Technical Orientation		Stock/Inventory Management			
		Problem Account Management	Records Management		Debtor/Creditor Management			

XIV. Longer Term Perspectives

158. The purpose of the proposed intervention by the Bank is not only to bring practical assistance to rural enterprise and communities but also to refine the processes by which the assistance is delivered into a replicable model for wider use throughout the country.

159. The period for which debt restructuring assistance will be required is not less than five years and may be longer. Active participation with ASF will clarify this.

160. Support for small and micro private enterprise will remain principally in the domain of non-governmental organizations although commercial banks may develop some interest, confined essentially to rural towns, once the reliability and discipline of such enterprise has been demonstrated by other credit channels. This will present donors with a dilemma since continued support for small and micro rural enterprise outside the urban areas will need to be sustained by other means than through formal bank channels. The credit union, developing at a pace commensurate with member skills and financial resources, is likely to be the most suitable vehicle.

XV. Risks

161. The design of the pilot project should be aimed at achieving not only the objectives but also at limiting risks that may include:

- demand for rehabilitation credit being artificially stimulated to the detriment of commercial loans through banks;
- demand for rehabilitation credit being slow in developing because the terms may be more demanding than applicants would wish - since the aim is to return these enterprises to profitable operation and to recover the Trust's and the Government's money, no relaxation should be considered because the outcome will be enterprises that survive only on subsidy;
- diversion of credit from rural enterprise to urban trade - refinancing review will need to scrutinize applications carefully and audit should be instructed to examine this possibility: the penalty must be loss of eligibility to participate as a lender;
- high levels of default - the quality of selection and appraisal must be subject to regular review, pursuit of default must be vigorous, immediate and undeviating and access to Trust funds must be refused to those who are unable to manage their loan portfolio adequately; and
- legal and administrative reforms do not progress at the pace commensurate with some of the project's objectives and goals.

XVI. Technical Assistance Requirement

162. Proposed technical assistance (TA) is as follows:

A. Project Management Unit

- project manager (credit specialist) and Trust manager
- agronomist
- agricultural economist
- microfinance promotion specialist
- credit union specialist
- short term specialists
  - — agricultural economist (gross margins manual)
  - — agricultural management information systems
  - — agricultural marketing
  - — wholesaling and warehouse receipt
  - — dairy and milk products
  - — small ruminants
  - — tanning and leather
  - — wool and cotton

B. Project Management Oblast Sub-Units (3)

- manager/credit specialist x 3
- agricultural economist x 3

163. Terms of reference for the long term TA specialists are attached in Appendix 2.

Logical Framework

	Verifiable Indicators	Verification Sources	Principal Assumptions
Goal			
to develop a competitive enabling environment for rural enterprise	• new legislation covering private enterprise • more amenable tax and local authority practice	• published law • project monitoring • client business results • project surveys	• economic viability of rural areas • continued government support for market economy reform and price liberalization
Purpose			
to foster rural private enterprise of all sizes and all economic sectors in the selected oblasts	• viable private enterprise growth • increase in employment • higher per capita income • subsidy levels falling	• project benefit monitoring • client management accounts • DOA and local statistics reports • agricultural expenditure review	• viable business potential exists • rural entrepreneurship equal to the opportunities • business skills rapidly acquired
Activities and Output			
Enterprise Financing	• portfolio growth • portfolio sectoral range • portfolio quality	• MIS leading indicators • MIS reports • lending audit	• longer term lending capability will provide incentive for commercial bank support of rural enterprise
Debt Restructuring	• improved farm viability • portfolio growth and quality • dues collection	• MIS leading indicators • ASF reports to government • benefit monitoring reports	• fundamental viability of agriculture and associated processing sector
Skills Development	• numbers trained • quality of lending • quality of businesses financed	• course reports • MIS leading indicators • project surveys	• training is a central element in the improvement of financial services to agriculture and rural enterprise

	Verifiable Indicators	Verification Sources	Principal Assumptions
Activities and Output			
Credit Delivery Outreach - rural community access improvement	• bank branches strengthened • local NGO growth and quality • small business center quality	• NBRK supervision reports • project reports • benefit monitoring surveys	• environment for creation of viable rural institutions for credit delivery from community resources exists
Loan Security Instruments	• acceptability of land as security • use of warehouse receipt • life assurance acceptable	• loan contracts • legislation and loan contracts • loan contracts	• there is a need for instruments to unlock the overdue receivables cycle
Savings Mobilization	• increase in savings levels and frequency	• MIS reports • benefit monitoring surveys	• constraints will be the solvency of deposit-takers and low confidence in safety of banks as repositories
Entrepreneur Associations	• increased numbers established • membership growth • growing management quality	• project progress reports • benefit monitoring reports • loan portfolio performance	• associations will test community cohesion and discipline needed for credit union operation
Credit Unions	• credit union legislation • credit unions formed • credit unions operating credit	• law published • Registrar of Credit Unions • loan portfolio reports	• credit unions offer best community based means for sustainable local mobilization of local resources
Replicable Models	• model refined and available for replication nationwide • workable mechanisms created for principal activities	• project reports • legislation • published manuals • evaluation reports	

Appendices to the Proposal

Appendix 1 - Trust Statutes

Trust Statutes

Part I. Preliminary

1.1 The name of the organization is the **Rural Development Trust Fund**, hereinafter referred to as the Trust.

1.2 The Trust is domiciled at the National Bank of the Republic of Kazakstan, hereinafter referred to as NBRK, of 21 Koktem-3, Almaty 480070.

1.3 The Trust is a non-profit organization.

1.4 The objectives[1] for which the Trust is established are:

- to provide credit for the fostering and development of rural private enterprise of all sizes and in all economic sectors;
- to provide credit in support of the restructuring of private farm and agri-business debt; and
- to foster rural private enterprise, and the growth of small and micro enterprise in particular;

1.5 Although domiciled at NBRK, the Trust is an autonomous entity; the State is not liable for the obligations of the Trust nor is the Trust liable for any obligation of the State.

1.6 Charter capital for the Trust is US Dollars

Part II

Alteration of Capital

2.1 The benefactors of the Trust may from to time increase the capital of the Trust by such amounts as the activities of the Trust warrant.

Reserve and Capitalization of Profits

2.2 The trustees shall from to time set aside such sums as proper as a reserve from which to make provision, in accordance with the regulations issued by NBRK, against doubtful and bad debt. The trustees shall capitalize all amounts, after setting aside the above reserve or reserves, to the credit of the profit and loss account or otherwise available as a means of extending the capacity of the Trust to make credit available to the private enterprise sector in the rural areas.

1 The Regulations governing the conduct of business activity for the achievement of these objectives will be formulated and published by the Trustees and shall be included in any document or manual defining the procedures by which the Trust's business activities shall be conducted.

Trustees

2.3 The number of trustees shall be a minimum of two but may be increased to include representatives of such institutions and organizations as may place funds at the disposal of the Trust. The initial trustees shall be:

- the Asian Development Bank, hereinafter referred to as the Bank, and
- the National Bank of the Republic of Kazakstan, hereinafter referred to as NBRK.

Borrowing Powers

2.4 The trustees may not exercise any powers to borrow money or to charge Trust undertakings or any part thereof or to issue debentures or other securities whether outright or as a security for any debt or liability or obligation of the Trust unless such powers have been authorized by the Government of the Republic of Kazakstan and the Board of Directors of the Bank and of such other institutions as may be appointed as trustees by virtue of their placing funds at the disposal of the Trust and such authorization has been set out in writing.

Powers and Duties of the Trustees

2.5 The business of the Trust shall be directed by representatives of the trustees, appointed in writing by the individual trustees, who may pay all expenses incurred in promoting and operating the Trust and may exercise all such powers of the Trust as are not by these Statutes required to be exercised by the Government of the Republic of Kazakstan, the Board of Directors of the Bank and the Boards of such other institutions as may have been appointed trustees or by the agents of these same, subject nevertheless to the provisions of these Statutes, regulations issued by NBRK for the management of credit operations and regulations prescribed by the Trust for the undertaking of its business. No regulation made by the Trust shall invalidate any prior act of the trustees that would have been valid if that regulation had not been made.

2.6 The trustees may from time to time and at any time by power of attorney appoint any company, firm or persons, whether nominated directly or indirectly by the trustees, to be attorney or attorney of the Trust for such purposes and with such powers, authorities and discretion's (not exceeding those vested in or exercisable by the trustees under these Statutes) for such period and subject to such conditions as they (the trustees) may deem fit. Any such powers of attorney may contain provision for the protection and convenience of persons dealing with such attorney as the trustees may consider fit. The trustees may also authorize any such attorney to delegate all or any of the powers, authorities and discretion's vested in him/her.

2.7 All receipts for moneys paid to the Trust and all promissory notes, bills of exchange, drafts or other negotiable instruments shall be signed, drawn, accepted, endorsed and otherwise executed, as the case may be, in such manner as the trustees shall from time to time by resolution determine.

2.8 The trustees shall cause minutes to be made in books provided for the purpose:

- of all appointments of officers made by the trustees;
- of all the names of all the persons present at each meeting of the trustees and of any committee of the said trustees;
- all resolutions and proceedings at all meetings of the Trust, of the trustees and of committees of the trustees; and
- every trustee present at any meeting of the trustees or committees of the trustees shall sign his/her name in a book kept for that purpose.

Proceedings of the Trustees

2.9 The trustees may meet together for the dispatch of business, adjourn and otherwise regulate their meetings as they may deem fit but shall meet at least once in every three months.

2.10 Questions arising at any meeting shall be decided by unanimity reached by consensus except where the interests, rights and obligations of a donor as stated at the time of placing funds with the Trust may be infringed, in which case the question shall referred to the Board of Directors of the donor institution.

2.11 All acts done by any meeting of the trustees or of a committee of trustees shall, notwithstanding that it be afterwards discovered that there was some defect in the appointment of any trustee of any such trustee, be as valid as if every such person had been duly appointed and was qualified to be a trustee.

Secretary

2.12 A Trust Secretary shall be appointed from the senior management of NBRK for such term and upon such conditions as the trustees deem fit. Any secretary so appointed may be removed by the trustees.

2.13 The secretary shall be responsible for the maintenance of the records of the acts and meetings of the trustees and of such committees as the trustees shall create.

The Seal

2.14 The trustees shall provide for safe custody of the Trust seal which shall be used only by authority of the trustees or of a committee of the trustees authorized by the trustees in that behalf. Every instrument to which the seal shall be attached shall be signed by a trustee and countersigned by the secretary or a second trustee or by a person appointed by the trustees for that purpose.

Responsibilities of the Trustees

2.15 The responsibilities of the trustees shall include but not be restricted to:

- direction of the activities of the Trust;
- formulation of policy relating to the loans and guarantees extended with the Trust's resources;
- selection of the banks and other institutions through which the Trust will extend financial support;
- authorization of contracts agreed, and the terms and conditions therein, between the participating institutions and the Trust;
- the preparation of an annual report of the activities of the Trust and of the use of the Trust's budget and the submission of this report to the Government and to the benefactors of the Trust;
- appointment, and dismissal, of the Trust's managers;
- supervision of the activities of the Trust's managers;
- approval of the remuneration of such employees as the Trust shall require for the effective conduct of its activities;
- authorization of the Trust's operational expenditures; and
- promotion of the Trust and the raising of additional financial resources for the pursuit of the Trust's activities.

Trust Managers

2.16 The Trust shall appoint two managers, one by choice of Trust benefactors and the other from the senior management of NBRK. The responsibilities of the managers include but are not restricted to the following:

- implementation of the trustees' decisions;
- reporting to the trustees on the activities of the Trust;
- reporting to the trustees on the status of the Trust's loan and guarantee portfolio and applications for loans and guarantees as may require the trustees' approval;
- release of funds for loans and guarantees in accordance with the trustees' instructions;
- preparation of the Trust's annual report and the budget;
- management of the Trust's day-to-day business activity;
- appointment and dismissal of Trust employees as may be necessary to the good conduct of the Trust's activities;
- arrangement of the meetings of the trustees; and
- representing the Trust in such manner and degree as shall be authorized by the trustees.

Accounts

2.17 The financial year of the Trust shall be 1 January - 31 December.

2.18 The trustees shall cause proper books of account to be kept with respect to:

- all sums of money received and expended by the Trust and the matters in respect of which such receipt and expenditure takes place;
- all sales and purchases of goods and services of the Trust; and
- the assets and liabilities of the Trust.

2.19 Proper books shall not be deemed to be kept if such books of account fail to give a true and fair view of the state of the Trust's affairs and to explain its transactions.

2.20 The books shall be kept at the Trust domicile or, subject to the stipulations of the laws of the Republic of Kazakstan, at such other place as the trustees deem fit and shall be open to inspection of the trustees and such other officers as the Government and the benefactors may authorize.

2.21 The trustees shall cause to be prepared and laid before the Government and the Trust benefactors such audited profit and loss accounts, balance sheets and other financial reports as the Government and Trust benefactors shall require and at such frequency as they shall stipulate.

Financial Resources

2.22 The financial resources of the Trust comprise:

- contributions from the State budget;
- loans received from domestic and foreign sources;
- borrowing guaranteed by the State;
- recovered loan and guarantee funds;
- profit on operations; and
- other sources permitted by the State and the Trust benefactors.

2.23 The Trust shall place those funds not extended as loans and guarantees in foreign currency interest-earning deposits with NBRK.

2.24 The Trust's funds shall be made available for loans and guarantees in the proportions stated below:

- debt restructuring for private farms and agri-business: 40 per cent
- large and medium private rural enterprise: 45 per cent
- small and micro private rural enterprise: 15 per cent

2.25 The proportions given in clause 2.24 above may, from time to time, be altered by lending seasonality, *force majeure* and other operational factors. The trustees shall also review the proportions at each half year and may amend them where the circumstances warrant. The allocation of Trust funds for small and micro loans, however, shall not be set at less than 15 per cent of available funds.

Supervision and Audit

2.26 The activities of the Trust will be supervised by the Supervision Department of NBRK.

2.27 The Supervision Department shall be responsible for:

- ensuring the Trust's compliance with the statutes;
- review of the annual audit of the Trust's use of its financial resources and the reports submitted by the Trust; and
- compiling, for submission to Government and the Trust benefactors, a supervision report at the end of each half year.

2.28 The Trust shall engage an internationally recognized auditor acceptable to the Government and the Trust benefactors to undertake an annual audit of the records and financial reports of the Trust and to submit a report to the Government and to the Trust benefactors.

Winding Up of the Trust

2.29 The Trust may be wound up solely at the discretion of the Government and the Trust benefactors. In the event of the winding up of the Trust, the Government and Trust benefactors shall issue instructions for the manner of the winding up and will appoint the person or persons who shall be responsible for the closure.

Appendix 2 - Terms of Reference for Technical Assistance Personnel

Terms of Reference for Technical Assistance Personnel

A. Background

1. Rural finance in Kazakstan faces difficult times. Agricultural production and income have declined during the 1990s as a result of structural changes required for the establishment of a market economy. These changes have resulted in drastically different agricultural price relationships, in land tenure arrangements, in marketing and, consequently, in income and expenditure flows. These changes only add to the riskiness of agricultural income, which has always been affected in Kazakstan by significant variations in arable crop yields from year to year.

2. The Government of Kazakstan (GOK) has requested Asian Development Bank to assist its efforts to develop rural finance and supporting systems. Purely financial tasks include participation in rationalizing the financial structure of privatized farms, capitalizing agribusiness, development of rural credit unions to stimulate small and micro enterprise and the generation of a sound loan portfolio. Activity combining credit and support systems include promotion of private agribusiness participating in viable marketing chains and the development of agricultural extension, veterinary services, machinery hire and business advice and training for entrepreneurs. Activity that does not require credit support consists of policy, legislation and regulations. These tasks, designed to promote sustainable employment, are to be implemented through financial market institutions, support systems and by refinement in GOK policies and practices affecting rural productivity.

3. The Bank's assistance will include .... (list), supported by technical assistance over a period of five years, with possibilities for extension. The time is consistent with global experience regarding the minimum time required for a new financial institution or system to reach sustainability. Progress may be even slower in agricultural finance because of seasonality. Five agricultural years offer only five chances to refine procedures, perfect systems, gain the confidence of clients and to identify and master risk which is substantial. Industrial and commercial finance has shorter cycles, enabling lenders to develop mature portfolios in less time than required for agriculture. The Bank's purpose, therefore, is to provide support until durable systems are developed in collaboration with GOK and others participating in the project.

B. Technical Assistance Requirement

4. Technical assistance will consist of the following level of effort.

5. Long Term Internationally-recruited Specialists:

Project Management Unit

- project manager/credit specialist (1) - five years
- agricultural economist (1) - five years
- agronomist (1) - five years
- microfinance promotion specialist (1) - five years
- credit union specialist (1) - five years

Project Management (Oblast) Sub-Units

- manager/credit specialists (3) - five years
- agricultural economists (3) - five years

6. Short Term Internationally-recruited Specialists:

The terms of reference for short term specialists will be drawn up by the project manager, and approved by the trustees, when specialist assistance is judged to be required. The short term specialist requirement includes, but is not confined to, the following specialist fields:

- agricultural management information systems
- agricultural marketing
- wholesaling and warehouse receipt
- dairy and milk products
- small ruminants
- tanning and leather
- wool and cotton

7. Terms of Reference for Long Term Specialists:

Project Manager/Credit Specialist

8. The project manager is one of the two Trust Managers and is jointly responsible to the Trustees for the management of the Trust's affairs in accordance with the duties set out in the Trust's statutes.

9. As project manager, he/she is the chief operating officer in the project and will be responsible for the management of the project's activities and the coordination of international and local specialist and administrative personnel.

10. As credit specialist, he/she will be responsible for the quality of the overall loan portfolio, reviewing all refinancing and debt restructuring proposals, including all rescheduling, presented for trustee approval and will have authority for the approval of debt restructuring loans of US$ 25,000-50,000.

11. The project manager shall be fully conversant with commercial lending operations, risk management, rural finance and work-out of loans in default and shall be capable of training project staff in lending procedures and the evaluation of risk-adjusted debt capacity. he/she shall have at least ten years' experience in these fields, including five years as a senior manager, and shall have an advanced qualification in finance, banking or a related subject. He/she should be fluent in English. A knowledge of Russian or a Turkic language would be an advantage.

Agricultural Economist (at the Project Management Unit)

12. Reporting to the project manager, the PMU agricultural economist will be responsible for determining the relative viability of farm enterprises, i.e. different crops and livestock, and efficient cropping patterns. This information is essential for sound agricultural lending. The agricultural economist will lead efforts to construct actual and representative gross margin tables and farm plans for use in evaluating farm debt capacity, maintaining a close working relationship with the PMU agronomist.

13. The PMU agricultural economist should provide technical leadership to agricultural economists in the PMU Sub-Units in the oblasts. He/she should be capable of training project staff, bank personnel, extension officers and others with an interest in agricultural value added.

14. The PMU agricultural economist should have an advanced degree in agricultural economics and ten years' practical experience. He/she should be fluent in English. A knowledge of Russian or a Turkic language would be an advantage.

Agronomist

15. The agronomist, reporting to the project manager, is responsible for advising project staff and participating institutions at all levels about viable yields and risks of different farm enterprises (e.g. different crops and livestock) and good husbandry practices under different local conditions. He/she will work in close collaboration with the PMU agricultural economist and with the credit specialists at the PMU and the sub-units. He/she will also advise local bankers, the NGOs and ASF who seek information on agricultural science.

16. The agronomist should be familiar with farming systems in Kazakstan or in areas with similar agricultural conditions and with scientific research conducted on major crops. He/she should have at least ten years' practical experience and an advanced degree in agricultural science. He/she should be fluent in English and in a language spoken in Kazakstan.

Micro-finance Promotion Specialist

17. The Micro-finance promotion specialist, reporting to the project manager, will be responsible for guiding PMU Sub-Units and participating NGOs in the development of the micro-enterprise loan portfolio and related services for micro-entrepreneurs. He/she will maintain close working relations with the agricultural economist and agronomist on matters relating to micro-enterprise and agriculture.

18. The micro-finance promotion specialist should have good practical experience of finical analysis, international micro-finance 'best practice' and the requirements for creating sustainable micro-finance portfolios. He/she should have at least eight years' experience in small and micro lending and be capable of training project credit specialists, bankers, NGO staff and managers at the entrepreneur associations in lending procedures and practices. He/she should be fluent in English; a working knowledge of Russian or a Turkic language would be an advantage.

Credit Union Specialist

19. The credit union specialist, reporting to the project manager, is responsible for the promotion of credit unions in project areas and assisting the development of the credit union supervisory body at the National Bank of the Republic of Kazakstan. He/she should be familiar with credit union law and regulations in countries where credit unions are successful and dynamic, with credit union operations and with the governance problems inherent in co-operative structures and how to manage these problems: successful promotion requires attention to each of these concerns.

20. The credit union specialist should have at least ten years' relevant experience in credit unions, their apex institutions or similar co-operative finance institutions. He/ she should have an academic degree in business, finance, economics or a related relevant subject. Fluency in English is required. Knowledge of Russian or a Turkic language would be an advantage.

Managers/Credit Specialists at Oblast PMUs

21. Oblast PMU managers will be responsible to the project manager for the conduct of project operations in their respective oblasts. They will coordinate the activities of the other specialists assigned to the oblast PMUs.

22. Their principal concern will be the quality of the loan portfolio for debt restructuring by ASF and of portfolios of Trust funded loans at the participating bank branches and NGOs. They will have authority to approve debt restructuring loans of US$ 25,000 or less and the rescheduling of small and micro loans at the participating NGOs. They will verify and clear NGOs' annual credit budget submissions before these are presented to the trustees for approval. They will supervise the delivery and quality of other services provided through the project.

23. Oblast PMU managers will be responsible for the maintenance of good working relations with local authorities and will be members of the oblast steering committee. They will be responsible for the training their staff, ASF personnel and the staff at the participating NGOs and entrepreneur associations. They, and their staff, will work closely with the credit union specialist.

24. Oblast PMU managers should be experienced in commercial lending operations, risk management, rural finance and work-our of loans in default. Each manager will have at least eight years' experience in these fields, including three as a manager, and an advanced qualification in finance, banking or a related subject. They should be fluent in English and a knowledge of Russian or a Turkic language would be an advantage.

Agricultural Economists at Oblast PMUs

25. Agricultural economists at Oblast PMUs, reporting to the Oblast PMU managers, are responsible for determining the relative viability of farm enterprises, i.e. different crops and livestock, and efficient crop patterns for use in lending decisions.

26. Agricultural production or investment loans will require a farm budget or plan that indicates yields, consumption on the farm, prices and costs, senior claims on cash flow such as high priority household or farm expenditures that will be undertaken before debt service could be reasonably be expected and net benefits before debt service. Budgets and plans should be drawn up from harvest to harvest and plans for investment should use 'Year 0' to indicate the period of investment and 'Year 1 and subsequent Years' for the following period of operation, so that loan receipts and debt service are not netted out in the initial period. Budgets and plans should use normal year assumptions and each should also include an alternative budget to reflect the risk and adversity that could reasonably be expected.

27. Oblast agricultural economists should have an advanced degree in agricultural economics, farm management, business administration or a related subject and at least five years' relevant practical experience. Each should be fluent in English and a knowledge of Russian or a Turkic language would be an advantage.

28. Terms of Reference for Locally-recruited Specialists:

Legal Specialist/Lawyer at the Project Management Unit

29. The legal specialist/lawyer shall advise the project manager on all legal questions relating to the project and its operations. He/she will be responsible for the design of loan agreements and other contracts, for participating in negotiations with those borrowers who default for material sums and for the coordination of such legal action as the project may take against defaulters. He/she shall monitor, and advise project staff of, financial sector regulatory measures having a direct or indirect impact on the project. He/she will also work with the credit union specialist to secure the approval and publication of legislation for credit unions and the establishment of the credit union registry at NBRK.

30. The legal specialist/lawyer will a have a law degree and accreditation to practice law in Kazakstan. He/she will have at least five years' experience as a practicing lawyer and a good working knowledge of technical and conversational English. He/she will be fluent in Russian and/or a language spoken in Kazakstan.