ADB

Completion Report

Project Number: 34113
Loan Number: 1978
September 2009

Indonesia: Small and Medium Enterprise Export Development Project

Asian Development Bank

CURRENCY EQUIVALENTS

Currency Unit – rupiah (Rp)

		At Appraisal (25 November 2002)	At Project Completion (30 June 2009)
Rp1.00	=	$0.000111	$0.00010
$1.00	=	Rp9,009	Rp10,258

ABBREVIATIONS

ADB	–	Asian Development Bank
ASEAN	–	Association of Southeast Asian Nations
BEI	–	Bank Ekspor Indonesia
BI	–	Bank Indonesia
IRM	–	Indonesia Resident Mission
LIBOR	–	London interbank offered rate
PCR	–	project completion report
RRP	–	report and recommendation of the President
SEIF	–	Small and Medium Exporters' Investment Facility
SMEs	–	small and medium-sized enterprises
TA	–	technical assistance
TAMU	–	technical assistance management unit

NOTES

(i) The fiscal year (FY) of the Government, Implementing Agency, and participating banks ends on 31 December. FY before a calendar year denotes the year in which the fiscal year ends, e.g., FY2000 ends on 31 December 2000.

(ii) In this report, "$" refers to US dollars.

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BASIC DATA

A. Loan Identification

1.	Country	Indonesia
2.	Loan Number	1978-INO
3.	Project Title	Small and Medium Enterprise Export Development Project
4.	Borrower	Republic of Indonesia
5.	Executing Agency	Ministry of Finance Directorate General of Financial Institutions
6.	Amount of Loan	$85.0 million ($72.8 million cancelled on 25 January 2007; $5.7 million cancelled on 24 September 2007)
7.	Project Completion Report Number	PCR: INO 1112

B. Loan Data

1.	Appraisal	
	– Date Started	23 July 2001
	– Date Completed	16 August 2001
2.	Loan Negotiations	
	– Date Started	28 October 2002
	– Date Completed	21 November 2002
3.	Date of Board Approval	17 December 2002
4.	Date of Loan Agreement	20 November 2003
5.	Date of Loan Effectiveness	
	– In Loan Agreement	17 February 2004
	– Actual	18 May 2004
	– Number of Extensions	1
6.	Closing Date	
	– In Loan Agreement	19 May 2009
	– Actual	2 September 2008
	– Number of Extensions	0
7.	Terms of Loan	ADB to the Borrower
	– Interest Rate	LIBOR-based
	– Maturity (number of years)	15
	– Grace Period (number of years)	3
8.	Terms of Relending	Borrower to Bank Ekspor Indonesia
	– Interest Rate	ADB LIBOR + 0.6% + 0.5% for Borrower
	– Maturity (number of years)	15
9.	– Grace Period (number of years)	3
10.	Subloan Terms	Participating banks to subborrower
	– Interest Rate	Bank Ekspor Indonesia rate to participating bank + participating bank spread
	– Maturity (number of years)	8
	– Grace Period (number of years)	3

11. Disbursement

a. Dates

Initial Disbursement	Final Disbursement	Time Interval
18 May 2004	2 September 2008	51 months

Effective Date	Original Closing Date	Time Interval
18 May 2004	19 May 2009	60 months

b. Amount ($'000)

Category or Subloan	Original Allocation	Last Revised Allocation	Amount Canceled	Net Amount Available	Amount Disbursed	Undisbursed Balance
001	850.00	850.00	0	850.00	850.00	0
003	449.00	449.00	0	449.00	449.00	0
004	1,000.00	1,000.00	0	1,000.00	1,000.00	0
005	315.00	110.00	205.00	110.00	110.00	0
006	216.30	216.30	0	216.30	216.30	0
011	200.00	200.00	0	200.00	200.00	0
012	543.48	463.16	80.00	463.16	463.16	0
013	222.22	210.53	11.70	210.53	210.53	0
014	105.43	105.43	0	105.43	105.43	0
015	526.32	526.32	0	526.32	526.32	0
016	388.89	0	388.89	0	0	0
017	241.00	118.20	122.80	118.20	118.20	0
018	955.85	955.85	0	955.85	955.85	0
019	453.31	423.95	29.36	423.95	423.95	0
020	180.00	180.00	0	180.00	180.00	0
022	358.32	358.32	0	358.32	358.32	0
023	273.64	273.64	0	273.64	273.64	0
Total	7,278.76	6,440.70	837.75	6.440.70	6,440.70	0

12. Local Costs (Financed)

– Amount ($)	0
– Percent of Local Costs	0
– Percent of Total Cost	0

C. Implementation Data

1. Number of Subloans by Participating Financial Intermediary

	Number	Amount ($ million)	Percent of Loan Amount
Bank Danamon Indonesia	1	110,000	2.0
Bank Negara Indonesia	22	5,480,685	98.0
Total	23	5,590,685	100.0

2. Sector Distribution of Subloans

	Number	Amount ($)	Percent of Loan Amount
Agribusiness	3	1,000,000	17.9
Food	2	463,158	8.3
Textile and Garments	1	110,000	2.0
Wood Products	13	2,859,245	51.1
Non-Metal	1	273,643	4.9
Transport	2	526,315	9.4
Other	1	358,324	6.4
Total	**23**	**5,590,685**	**100.0**

3. Size of Subloans

	Number	Amount ($)	Percent of Loan Amount
Below Free Limit ($450,000)	21	4,193,400	75.0

Above Free Limit (above $450,000)	2	1,397,285	25.0
Total	**23**	**5,590,685**	**100.0**

4. Geographic Distribution

	Number	Amount ($)	Percent of Loan Amount
Bali	2	383,643	6.9
Semarang	16	3,859,245	69.0
Sidoarjo	2	463,158	8.3
Kalimantan	2	526,315	9.4
Other	1	358,324	6.4
Total	**23**	**5,590,685**	**100.0**

5. Purpose of Subloans

	Number	Amount ($)	Percent of Loan Amount
Investment	13	4,208,885	75.0
Working Capital	10	1,381,800	25.0
Total	**23**	**5,590,685**	**100.0**

6. Type of Subloans

	Number	Amount ($)	Percent of Loan Amount
New	2	200,000	4.0
Expansion	21	5,390,685	96.0
Total	**23**	**5,590,685**	**100.0**

7. Maturity of Subloans

	Number	Amount ($)	Percent of Loan Amount
Up to 3 Years	7	1,071,210	19.2
Over 3–5 Years	9	2,008,995	35.9
Over 5–8 Years	7	2,510,480	44.9
Total	**23**	**5,590,685**	**100.0**

8. Project Performance Report Ratings

	Ratings	
Implementation Period	**Development Objectives**	**Implementation Progress**
From 12 December 2002 to 31 December 2002	Satisfactory	Satisfactory
From 1 January 2003 to 31 December 2003	Satisfactory	Unsatisfactory
From 1 January 2004 to 31 December 2004	Satisfactory	Satisfactory
From 1 January 2005 to 31 December 2005	Satisfactory	Satisfactory
From 1 January 2006 to 31 December 2006	Satisfactory	Satisfactory
From 1 January 2007 to 31 December 2007	Satisfactory	Satisfactory
From 1 January 2008 to 30 September 2008	Satisfactory	Satisfactory

D. Data on Asian Development Bank Missions

Name of Mission	Date	No. of Persons	No. of Person-Days	Specialization of Members
Review Mission[a]	10–20 November 2003	2	22	a, h, g
Review Mission	12–28 October 2004	N/A	N/A	N/A
Review Mission	23–29 October 2005	2	24	g, h
Review Mission	5–9 December 2005	N/A	N/A	N/A
Project Completion Review	27 June–27 July 2009	3	90	f, g, h

IRM = Indonesia Resident Mission, NA = not applicable, SEGF = Southeast Governance, Finance, & Trade Division.
a = director, SEGF; f = staff consultant; g = project analyst, SEGF and project implementation officer, IRM;
h = economist, SEGF and senior financial management specialist, IRM.
a This mission covered four other projects in Indonesia.

E. Related Loans

Loan	Loan Number	Date of Agreement	Amount ($ million)
Development Finance Loan I	981-INO	23 November 1989	200
Development Finance Loan II	1223-INO	2 August 1993	200
Total			400

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I. BACKGROUND

A. History

1. The Small and Medium Enterprise Export Development Project (the Project) for $85 million to the Government of Indonesia was approved by the Asian Development Bank (ADB) in December 2002 using ordinary capital resources. It became effective in May 2004 and was closed in September 2008.

2. The 1997–1998 Asian financial crisis pushed many people below the poverty line in Indonesia. During this crisis, however, small and medium-sized enterprises (SMEs)—especially export-oriented firms—proved to be resilient, as they benefitted from the depreciation of the rupiah. They also provided many job opportunities, thus contributing to poverty reduction. Due to their demonstrated importance in economic recovery and job creation, the Government considered SME development among the country's most important economic initiatives, especially in its strategy for poverty reduction. Thus, the poverty reduction partnership agreement, 2001–2004, noted SME development as a key area for future ADB assistance in Indonesia.[1] The Project also followed up the earlier Industrial Competitiveness and Small and Medium Enterprise Development Program,[2] which focused on developing a regulatory framework and policies, and technical assistance toward the development of SME business development services.[3]

3. The Project aimed to support economic growth, assist in reducing poverty through job creation, and promote labor-intensive exports. As part of ADB's larger assistance strategy, the Project supported the SME export sector directly through investment capital, a market niche within total SME sector lending. Indirectly, the Project was expected to improve the appraisal capacity of banks to undertake investment lending as well as exporter capacity to apply for bank credit. Priority was given to subprojects in provinces with export potential, such as East and Central Java (part of ADB's geographical focus), Sulawesi (part of the East ASEAN Growth area), and Bali. The Project was estimated to cost $113 million equivalent ($85 million or 75% in foreign currency and $28 million or 25% in local currency, with the former involving funding of $85 million from the Small and Medium Exporters' Investment Facility [SEIF]). Of this, ADB provided the full foreign currency cost of $85 million. The balance of $28 million was provided equally by subborrowers' equity and participating banks.

4. The Project had two components.

(i) **Small and Medium Exporters' Investment Facility.** The SEIF was set up to help small exporters to meet investment requirements for capacity expansion and modernization. The ADB loan augmented the SEIF funds and these were to be channeled to public and private banks through Bank Ekspor Indonesia (BEI). BEI was expected to manage the participating banks' risks, while participating banks managed exporters' risks (with exporters to assume the foreign currency risk of the subloans). These funds were expected to provide long-term foreign currency debt funding to SME exporters and indirectly to their

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1 ADB. 2001. *Poverty Reduction Partnership Agreement between the Government of Indonesia and the Asian Development Bank (2001–2004).* Manila.

2 ADB. 1999. *Report and Recommendation of the President to the Board of Directors on a Proposed Loan to the Republic of Indonesia for the Industrial Competitiveness and Small and Medium Enterprise Development Program.* Manila (Loan 1738-INO).

3 ADB. 2002. *Technical Assistance to the Republic of Indonesia for Strengthening Business Development Services for Small and Medium Enterprises.* Manila (TA 3829-INO).

supporting industries. The purposes were to finance capital investment loans, excluding land purchasing, and to finance preinvestment and permanent working capital, including financing for essential imported inputs (without exceeding 35% of the subloan). The ADB loan was expected to make available long-term funds across Indonesia to SME exporters, who could prudently manage the foreign currency risk. The project appraisal outlined the criteria for bank selection and monitoring by BEI's technical assistance and monitoring unit (TAMU) through quarterly reports (report and recommendation of the President [RRP][4], para. 43). Based on a range of financial criteria (RRP, para. 43), six participating banks were preselected for the Project.[5]

(ii) **Technical assistance grant.** TA[6], in the amount of $500,000 and financed through the Asian Currency Crisis Support Facility, was designed to support project implementation. It sought to strengthen the credit and project appraisal capacity and lending operations of the six participating banks through TAMU. It was also designed to train bankers on SME credit scoring and use of basic trade finance instruments, and to provide financial advisory services for SME exporters to use SEIF funds. TAMU was also expected to assist the Ministry of Finance and ADB in monitoring project implementation and managing the Project. In parallel, the Government of Japan financed an SME promotion program for $5 million to complement this TA.

5. **Loan Terms.** The Government was the Borrower of the $85 million loan, with the loan currency, interest modality, and repayment schedule stated in the Loan Agreement and in accordance with ADB policy on its London interbank offered rate (LIBOR)-based loan product. The Government relent the loan proceeds to BEI, the sole implementing bank. The relending terms and conditions were identical to those of the ADB loan to the Borrower except that the Borrower charged BEI 50 basis points. BEI managed these banks' risk and charged an administration fee. The participating banks managed the commercial risk of exporters and charged onlending interest rates to the final subborrower (i.e., the SMEs) at market rates. TAMU was to support the participating banks' credit assessment of SMEs if necessary. For individual SME exporters, the maximum subloan size financed by ADB was $600,000, with a free limit of $450,000.[7] For exporters with demonstrated business networks of more than 20 SMEs, the maximum subloan size financed by ADB was $1 million, with a free limit of $750,000. Under either type of free limit, the first three subloans made by each participating bank was subject to ADB's approval. Subloans exceeding the free limit continued to require prior ADB approval. The maximum tenor of subloans was 8 years, including a grace period of 3 years.

B. Scope of Operations

6. As stated previously, SMEs demonstrated particular resilience after the Asian financial crisis. Because of their employment-generating capacity, ADB and the Government supported their development as an effective poverty-reduction strategy, as reflected in the poverty reduction partnership agreement. The Government also prepared a midterm action plan for

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[4] ADB. 2002. Report and Recommendation of the President to the Board of Directors on a Proposed Loan and Technical Assistance Grant to the Republic of Indonesia for the Small and Medium Enterprise Export Development Project. Manila, para 43.

[5] These were Bank Bukopin, Bank Danamon Indonesia, Bank Mandiri, Bank Negara Indonesia, Bank Niaga, and Bank Rakyat Indonesia.

[6] ADB. 2002. Technical Assistance to Republic of Indonesia for Small and Medium Enterprise Export Development. Manila (TA 4041-INO for $500,000).

[7] Subloans below $450,000 did not require prior ADB approval and are referred to as "free-limit".

SMEs in April 2002, which highlighted the role of SMEs in broadening Indonesia's economic base and in accelerating necessary structural reforms.

7. After the financial crisis, SMEs grew at a faster pace than the rest of the economy, because many turned to exports to benefit from the favorable exchange rate. SME exports grew by 3.6% in 1998 and 5.8% in 1999. In contrast, larger exporters' exports declined by 0.8% in 1998 and by 0.9% in 1999. Smaller firms (i.e., those with fewer than 100 workers) had higher export growth than larger firms between 1996 and 2000, and their share of exports doubled, although their contribution to exports continued to be modest (2.8% in 1996 and up to 4.1% in 2000). While the recovery was faster among SMEs, it could have been higher if constraints inhibiting their development had been addressed.

8. Direct SME export growth was achieved by finding niche markets and adapting costs and quality to market demand. However, a significant part of SME exports went unrecorded, because they occurred indirectly through subcontracting for larger firms or traders.

9. The industrial structure in Indonesia was dominated by large enterprises in terms of value added, while small firms played a key role in terms of employment creation. The potential of SMEs to generate employment and to add value was highly desirable in a very populated and capital-short country like Indonesia. However, there were many constraints, including (i) a poor policy environment to conduct business; which disproportionately penalized SMEs; (ii) lack of business development services for SMEs; and (iii) lack of financial and physical infrastructure to support SMEs with access to markets, including exports with reliable production. ADB and other agencies had intervened through previous programs (footnotes 2 and 3), which supported the Government in preparing the SME midterm action plan. The Project intended to build on these achievements by providing export-oriented SMEs with a foreign currency funding source for investment in equipment and working capital.

C. Relationship with the Asian Development Bank and Other Lenders

10. ADB and other lenders maintained close coordination in the development of Indonesia's SME sector. Japan, the largest bilateral source of development assistance to Indonesia, provided significant financial and technical support. In 1998, the Japan Bank for International Cooperation provided a $1 billion facility to support Indonesia's export-led economic recovery, which provided for the settlement of transactions based on letters of credit issued by local banks to finance necessary imports for the export sector. In December 2000, the facility was revised to provide working capital ($300 million) in addition to letters of credit confirmation services ($700 million). The Japan International Cooperation Agency also financed a detailed assessment of Indonesia's SME sector, which helped formulate an SME promotion program in Indonesia from 2002 to 2006. Japan was the leader of the SME Donor Committee for the Consultative Group of Indonesia in coordination with ADB; World Bank; and several bilateral sources such as Australia, Canada, Germany, Switzerland, and the United States (RRP, paras. 29–32).

D. Relevance of Design and Formulation

11. The Project was relevant at appraisal, as it addressed a key impediment to SME development in Indonesia—the difficulty in obtaining financing, particularly for investment purposes. A major lesson of the Asian financial crisis was that firms should secure funds to meet their investment needs in the same currency as their revenue streams. Export-oriented SMEs were naturally hedged against foreign currency risks. At the same time, given market conditions prevailing at the time of the appraisal, SMEs had difficulty in obtaining financing, as

Indonesian banks often looked only at collateral and offered only short-term funds. Therefore, introduction of a foreign currency financing mechanism under the Project was expected to help develop SME exporters. As mentioned earlier, the Government (RRP, para. 24) and ADB (RRP, para. 25) gave high priority in their respective plans and strategies for SME development, particularly in light of their potential for job creation and poverty reduction.

12. The Project took into consideration lessons from international experience (RRP, para. 22) and specific lessons from ADB's experience in Indonesia (RRP, para. 23). The Project expected its interest rates to be competitive with alternative funding sources. It also anticipated addressing a constraint in the availability of foreign currency credit for import of equipment by SME exporters, due to the squeeze on foreign currency availability from the financial crisis and reduced availability of credit lines to Indonesian banks (RRP, para. 24).

E. Related Technical Assistance

13. The TA (para. 4 (ii)) was implemented with the establishment of TAMU. The technical assistance completion report[8] rated the TA as *successful.* However, the project completion review (PCR) mission found that BEI had disbanded TAMU during its internal reorganization. BEI did not give a reason for this decision. Thus, TAMU ceased to serve its objectives of project data collection, analysis, and dissemination for ADB and the Ministry of Finance, and training of participating bank staff members in export financing methods and instruments. ADB also did not follow up on TAMU's continuing operation during its project supervision work; therefore, project data for PCR preparation were unavailable.

II. IMPLEMENTATION

A. Lending Policies

14. The Government continued its policy to develop the SME sector. The lending policies of BEI, the Implementing Agency, and those of the participating banks also continued to be supportive of SME development.

B. Characteristics of Subloans

1. Loan Utilization

15. Only $5.59 million (6.6%) of the $85.00 million loan was used by only two[9] of the six participating banks for subloan financing. The balance of $78.56 million[10] (92.4%) was canceled by ADB on the Government's request in January 2007, and the loan was officially closed in September 2008.

16. The poor loan utilization was due to many factors. The main factor was the difference between the participating banks' own resource cost of funds and the ADB loan, with the former being cheaper. The participating banks, therefore, preferred to use their own resources to fund the SME requirements for both investment loans and working capital loans. Appendix 1 gives

[8] ADB. 2006. Technical Assistance Completion Report on Small and Medium Enterprise Export Development. Manila (TA 4041-INO)
[9] These two participating banks were Bank Danamon Indonesia and Bank Negara Indonesia.
[10] The total disbursement amounted to $6.44 million, which included subloan disbursement of $5.59 million and a front-end fee of $850,000, treated as a disbursement.

the cost of funds on bank resources versus ADB funds, as well as the cost of funds differences from 2002 to 2008 on a quarterly basis.

17. Clearly, the cost of funds gap increased significantly during the loan utilization period. The difference was relatively small (0.88%) when the ADB loan was approved in the last quarter of 2002 (December 2002). However, it increased significantly to 2.83% in the second quarter of 2004, when the loan became effective (May 2004). The difference increased to 4.38% in the second quarter of 2006, when the Government and participating banks finally decided to request cancellation of the unused portion of the loan. When this was canceled by ADB (January 2007), the cost of funds difference was 4.20% in the first quarter of 2007, and it decreased to 2.73% in the third quarter of 2008, when the loan was closed (September 2008). It was further reduced to 1.31% in the fourth quarter of 2008, after the loan was closed.

18. The participating banks' cost of funds decreased due to increased liquidity, which came in the form of both local and foreign currency, as a result of continued economic recovery and restored public confidence in the banking system after the financial crisis. In 2007, the favorable liquidity positions of banks were reflected by loan–deposit ratios of 52.94% for state-owned banks and 51.80% for private banks. On the other hand, the LIBOR rate—on which the ADB loan rate was based—increased from a relatively low rate at the time of the appraisal (July–August 2001) and at Board approval (December 2002). The 3-month LIBOR in the fourth quarter of 2002 was 1.38%, but after the loan became effective and ready for utilization in May 2004, the rate increased from 1.60% in the second quarter of 2004 to 3.51% in the second quarter of 2005. It increased further to 5.51% in the second quarter of 2006 when the Government and participating banks decided to cancel the loan. The rate decreased slightly to 5.36% in the second quarter of 2007. The LIBOR rate further reduced to 1.83% in the fourth quarter of 2008, after the loan was closed.

19. Apart from the LIBOR interest rate issue, the participating banks' cost of funds under the ADB loan was higher compared to their own resources because of the manner in which the ADB loan was structured (i.e., the fees payable to the various intermediaries involved). Those fees were a 0.5% fee to the Ministry of Finance, BEI's provisioning fee of 1.0%, and BEI's overhead cost of 0.3%. When all fees were added to the increasing LIBOR rate, the total cost of funds came to 3.78% in the fourth quarter of 2002. The rate increased to 4.00% in the second quarter of 2004, 5.91% in the second quarter of 2005, and 7.91% in the second quarter of 2006, before it decreased slightly to 7.76% in the second quarter of 2007. The rate decreased again to 4.23% in the fourth quarter of 2008. Meanwhile, the average cost of funds for the participating banks was 2.9% in the fourth quarter of 2002, 1.2% in the second quarter of 2004, 1.9% in the second quarter of 2005, 3.5% in the second quarter of 2006, 3.6% in the second quarter of 2007, and 2.9% in the fourth quarter of 2008.

20. Other factors also made the ADB loan unattractive for the participating banks.

(i) In addition to the higher cost of funds under the ADB loan, the banks were also liable to pay a commitment charge of 0.75% on the undisbursed portions of the ADB loan allocated to them[11] and their portion of the front-end fee[12] (e.g., Bank Rakyat Indonesia's portion of the front-end fee came to $150,000, and it had to

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[11] The ADB loan of $85 million was allocated under subsidiary loan agreements as follows: $50 million for BEI, $20 million to Bank Negara Indonesia, and $15 million to Bank Rakyat Indonesia.

[12] The front-end fee of 1% was payable as follows: BEI, $500,000; Bank Negara Indonesia, $200,000; and Bank Rakyat Indonesia, $150,000, for a total of $850,000.

pay a commitment fee of 0.75% on the undisbursed portion of its loan of $13.5 million, which made its operations under the ADB loan unprofitable).

(ii) Only up to 35% of ADB-financed subloans could be used for financing working capital, which restricted loan utilization as the main SME requirement was for working capital subloans.[13]

(iii) The maximum subloan size allowed was only up to $600,000 for a single enterprise and up to $1 million for a group of SMEs, whereas that limit of a bank was as much as $5 million.

(iv) The free-limit of $450,000 for a single enterprise and up to $750,000 for a group of SMEs was also considered too low, whereas a bank could approve a loan up to a maximum of $5 million for a single enterprise according to their internal financial guidelines. These loan conditions were considered too restrictive. The longer-term tenor of ADB subloans (up to 8 years, including a 3-year grace period) was not attractive for SMEs, as they preferred shorter-term loans particularly for financing working capital loans.

21. Based on discussions with ADB during October–December 2005,[14] the Government requested that ADB

(i) reduce the ADB interest rate from ordinary capital resources to an Asian Development Fund basis;
(ii) allow subloans by participating banks to be made for working capital loans up to 100%;
(iii) increase subloan ceiling amounts;
(iv) allow lending in rupiah, including to indirect exporters;
(v) extend the loan project period; and
(vi) increase imprest account limits to overcome the long delays experienced in disbursing loan proceeds. BEI also requested that in addition to acting as the implementing bank, it would also be allowed to function as a participating bank.

22. ADB staff informed the Government, through an aide-mémoire dated 12 December 2005, that

(i) no change in loan pricing could be considered, and it was not possible to switch from ordinary capital resources to the Asian Development Fund;
(ii) subloans could be financed up to 100% of working capital requirements;
(iii) maximum subloan size could be increased to $2 million;
(iv) local currency lending under the Project was not allowed, as there was no rationale for ADB adding more local currency liquidity to a market, which already had a high degree of liquidity;
(v) extending the loan period was considered a non-issue as project performance had to improve significantly in a short period or the Project would be canceled;
(vi) the size of the imprest account was not considered to be an important factor in poor loan performance, particularly as subloans—if used purely for working capital—would increase the pace of fund flow significantly, and
(vii) for BEI to become a participating bank, it would need to be fully supported by the other banks and the Executing Agency.

[13] At this time, SMEs were still recovering from the effects of the financial crisis; therefore, they had excess unused capacity. Hence, the demand was more for working capital than investment loans for import of equipment.
[14] These discussions were led by staff from ADB Headquarters in Manila. Indonesia Resident Mission staff participated in the discussions.

Only $5.59 million of the loan was used to finance 23 subloans—one at Bank Danamon Indonesia and 22 at Bank Negara Indonesia—for a total of 14 subprojects (Appendix 2). The appraisal estimated the financing of about 150 subloans. As stated, only two banks participated,[15] and the number of subloans was lower than the appraisal estimate.

23. The changes to which the ADB agreed were incorporated in a proposed amendment to the Loan Agreement and sent to the Government in a letter dated 11 May 2006. However, as consensus could not be reached between the Government and ADB, the Government decided to proceed with the cancellation of the unused portion of the loan.

2. Description of Subloans

24. The major portion of the loan proceeds was used by Bank Negara Indonesia (98% by amount) and small portion by Bank Danamon (2%). The major portion of the subloans was used to finance expansion projects (96%), had maturities less than 5 years (55%), was below the free limit (75%), financed mainly the wood products industry (51%), and was located in Semarang (69%). Bank Negara Indonesia used a greater portion of the loan, as its liquidity position was tighter than that of other banks, with loan growth outpacing deposit growth. In 2008, Bank Negara Indonesia loan growth was 26%, while its deposit growth was only 12%.

C. Implementation and Internal Operations of Subprojects

25. The 14 subprojects financed were implemented and are in successful operation.[16] Except for one that had a debt repayment grading of *marginal* in accordance with Bank of Indonesia (BI) guidelines, all others had *good* ratings.

D. Operational Performance of the Implementing Agency and Participating Banks

26. BEI, the Implementing Agency, and the two participating banks, Bank Danamon Indonesia and Bank Negara Indonesia, are operating satisfactorily. A summary of their operational performance for 2004–2008 is in Appendix 3.

27. **Bank Ekspor Indonesia.** BEI's loans to other parties increased from Rp6,050,117 million ($590 million) in 2004 to Rp9,216,530 million ($898 million) in 2008. A 47% increase from 2007 to 2008 was especially significant. The loan–deposit ratio of 578% was exceptionally high in 2004, increasing to 1,017% in 2008. This is because BEI does not take deposits from the public, and it is funded mainly by borrowings, equity from the Government, and reserves.

28. **Bank Danamon Indonesia.** Deposits increased from Rp40,765 billion ($4.0 billion) in 2004 to Rp75,373 billion ($7.3 billion) in 2008, reflecting increasing depositor confidence in the bank. The deposit increase in 2008 was significant, jumping by about 27% from Rp59,528 billion ($5.8 billion) in 2007 to Rp75,373 billion ($7.3 billion) in 2008. Loans increased from Rp30,294 billion ($3.0 billion) in 2004 to Rp66,898 billion ($6.5 billion) in 2008, increasing 25% from Rp53,330 billion ($5.2 billion) in 2007 to Rp66,898 billion ($6.5 billion) in 2008. The

[15] Three banks (Bank Bukopin, Bank Mandiri, and Bank Niaga) did not participate due to excess liquidity and cheaper funds available based on their own resources, while Bank Rakyat Indonesia found its operations under the ADB loan unprofitable.

[16] The PCR mission visited two subprojects as samples in Semarang on 14 July 2009. Both were processing local wood into export products, operating satisfactorily with no debt repayment problems, and meeting environmental guidelines of the Government and compared alternative quotations for procurement under loan proceeds. Both also had incremental increases in employment and exports as a result of using loan funds.

loan–deposit ratio[17] increased from 72.2% in 2004 to 86.4% in 2008, reflecting comfortable liquidity positions. Excess liquidity was invested mainly in government bonds, which declined from Rp17,324 billion ($1.7 billion) in 2004 to Rp13,083 billion ($1.3 billion) in 2008. Bank Danamon Indonesia extended its banking services, with the number of bank branches increasing from 929 in 2004 to 1,871 in 2008, and the number of ATMs increasing slightly from 804 in 2004 to 814 in 2008.

29. **Bank Negara Indonesia.** Deposits increased from Rp105,097 billion ($10.2 billion) in 2004 to Rp163,164 billion ($15.9 billion) in 2008, reflecting increased depositor confidence. In fact, deposits increased by 12% between 2007 and 2008. Loans increased from Rp57,868 billion ($5.6 billion) in 2004 to Rp111,994 billion ($10.9 billion) in 2008, increasing 26% between 2007 and 2008. The loan increase outpaced that of deposits, and the loan–deposit ratio increased from 55.1% in 2004 to 68.6% in 2008, reflecting comfortable liquidity positions. Excess liquidity was invested mainly in government bonds, which decreased from Rp38,943 billion ($3.8 billion) in 2004 to Rp34,655 billion ($3.4 billion) in 2008. Bank branches increased slightly from 943 in 2004 to 998 in 2008, and the number of ATMs increased significantly from 2,272 in 2004 to 2,918 in 2008.

E. Financial Performance of the Implementing Agency and Participating Banks

30. The financial performance of BEI, the Implementing Agency, and the two participating banks, Bank Danamon Indonesia and Bank Negara Indonesia, is *satisfactory*. A summary of their financial performance for 2004–2008 is in Appendix 3.

31. **Bank Ekspor Indonesia.** BEI operated profitably during 2004–2008. Interest income increased from Rp354,927 million ($34.6 million) in 2004 to Rp1,042,985 million ($101.7 million) in 2008. Interest income increased 13% from Rp924,724 million ($90.0 million) in 2007 to Rp1,042,985 million ($101.7 million) in 2008. Net income after tax increased from Rp182,176 million ($17.8 million) in 2004 to Rp241,648 million ($23.6 million) in 2008. It declined from Rp278,398 million ($27.1 million) in 2007 to Rp241,648 million ($23.6 million) in 2008, a drop of about 13% due to increases in interest and other operational expenses. The return on equity increased from 4.9% in 2004 to 5.8% in 2008, while the return on assets declined from 5.1% in 2004 to 2.9% in 2008, but remained within the ADB prescribed limit (i.e., it should be positive).

32. **Bank Danamon Indonesia.** The bank operated profitably during 2004–2008. Interest income increased from Rp6,395 billion ($0.6 billion) in 2004 to Rp14,189 billion ($1.4 billion) in 2008, increasing 18% from Rp12,048 billion ($1.2 billion) in 2007 to Rp14,189 billion ($1.4 billion) in 2008. Net profits after tax decreased from Rp2,408 billion ($0.2 billion) in 2004 to Rp1,530 billion ($0.1 billion) in 2008, partly due to an increase in interest expenses, which increased from Rp2,376 billion ($0.2 billion) in 2004 to Rp5,835 billion ($0.6 billion) in 2008. The nonperforming loan–total loan ratio[18] remained at a fairly satisfactory level and within ADB's limit for a participating bank,[19] dropping from 4.0% in 2004 to 2.3% in 2007, remaining at that level in 2008. Loan loss allowances to nonperforming loans were satisfactory, although dropping from 161.2% in 2007 to 136.7% in 2008. Returns on equity and assets also remained satisfactory, although the return on equity fell from 38.6% in 2004 to 14.6% in 2008. The return on assets dropped from 4.5% in 2004 to 1.5% in 2008, but it was still within the ADB prescribed limit.

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[17] ADB mandated that a participating bank's loan–deposit ratio should not exceed 100%.
[18] ADB mandated that a participating bank's nonperforming loan ratio must not exceed 5%.
[19] ADB mandated that a participating bank's return on assets must be positive.

33. **Bank Negara Indonesia.** The bank was profitable in 2004–2008. Interest income increased from Rp11,788 billion ($1.1 billion) in 2004 to Rp16,628 billion ($1.6 billion) in 2008, increasing 12% from Rp14,878 billion ($1.5 billion) in 2007 to Rp16,628 billion ($1.6 billion) in 2008. Net income after tax dropped from Rp3,090 billion ($0.3 billion) in 2004 to Rp1,226 billion ($0.1 billion) in 2008, due to an increase in interest expenses as well as allowance for possible losses. Interest expenses increased from Rp4,648 billion ($0.4 billion) in 2004 to Rp6,716 billion ($0.6 billion) in 2008. Allowance for possible losses on earning assets jumped from Rp2,128 billion ($0.2 billion) in 2004 to Rp4,359 billion ($0.4 billion) in 2008. The nonperforming loan–total loan ratio increased from 4.6% in 2004 to 8.2% in 2007, but it decreased to 4.9% in 2008, which was still within the ADB maximum limit of 5.0%. Loan loss allowances to nonperforming loans improved from 71.9% in 2007 to 101.0% in 2008. Returns on equity and assets also remained satisfactory, with the return on equity dropping from 29.6% in 2004 to 9.0% in 2008, and the return on assets dropping from 2.5% in 2004 to 1.1% in 2008.

F. Financial Statements and Ratios

34. BEI, the Implementing Agency, and the two participating banks, Bank Danamon Indonesia and Bank Negara Indonesia, have sound financial positions. A summary of their financial statements and ratios for 2004–2008 is given in Appendix 3.

35. **Bank Ekspor Indonesia.** BEI's assets increased from Rp7,437,724 million ($725 million) in 2004 to Rp11,191,257 million ($1,091 million) in 2008, with a 9% increase between 2007 and 2008. Shareholders' equity increased from Rp3,729,931 million ($364 million) in 2004 to Rp4,285,237 million ($418 million) in 2008, increasing slightly by about 3% between 2007 and 2008. BEI was adequately capitalized with a capital adequacy ratio[20] above the required minimum of 8%. The ratio was 39% in 2008 versus 114% in 2004.

36. **Bank Danamon Indonesia.** Its earning assets increased from Rp52,555 billion ($5.0 billion) in 2004 to Rp94,980 billion ($9.3 billion) in 2008, with a significant 20% increase between 2007 and 2008. Shareholders' equity increased from Rp7,804 billion ($0.8 billion) in 2004 to Rp10,579 billion ($1.0 billion) in 2008. However, it dropped slightly by Rp254 billion ($0.02 billion) between 2007 and 2008. The bank was adequately capitalized, with a consolidated capital adequacy ratio of 15.4% in 2008.

37. **Bank Negara Indonesia.** Its total assets increased from Rp136,582 billion ($13 billion) in 2004 to Rp201,741 billion ($19.7 billion) in 2008, increasing 10% between 2007 and 2008. Shareholders' equity increased from Rp12,624 billion ($1.2 billion) in 2004 to Rp15,431 billion ($1.5 billion) in 2008, but it dropped slightly by Rp1,789 billion ($0.2 billion) between 2007 and 2008. The bank was adequately capitalized, with a capital adequacy ratio of 13.5% in 2008, which is above the Bank of Indonesia and ADB minimum limit of 8%.

G. Covenants and Conditions

38. The Government and participating banks generally complied with ADB loan covenants. Monitoring occurred through TAMU. In addition, the participating banks submitted quarterly progress reports and their audited annual reports to BEI on time. They generally met the applicable prudential regulations and guidelines of Bank of Indonesia and ADB. Subproject selection was done by the participating banks on sound due diligence as shown by the

[20] The capital adequacy ratio is that between the paid-in capital and risk-weighted assets. Bank Indonesia and ADB mandated that for the participating banks, the capital adequacy ratio must not be below 8%.

subprojects' operational and financial success and satisfactory debt repayment performance. Two sampled subprojects also showed that they generally met ADB requirements on procurement and the environment. However, the subsequent discontinuation of TAMU caused noncompliance with the related loan covenant by BEI. As a result, subproject data and their compliance status with ADB covenants and conditions were not available. The compliance status with ADB loan covenants and conditions is summarized in Appendix 4.

H. Performance of the Asian Development Bank

39. Project implementation was made difficult due to the change in the economic environment (example, increase in bank liquidity and reduction in the cost of funds of the PBs below the interest rate of the ADB loan) during the project implementation period. There were other early warning signals that the ADB loan was unlikely to succeed, including

(i) delay in signing the Loan Agreement by about 1 year,
(ii) delay in loan effectiveness by about 4 months that included one extension, and
(iii) the cost of funds differential began to shift in favor of the participating banks' own funds as early as the fourth quarter of 2002 (see Appendix 1) or when the loan was approved in December 2002.

40. The Government was reluctant, at a very early stage of project implementation, to request cancellation of the unused portion of the loan for political reasons. However, ADB should have taken the initiative under "spring cleaning" exercises to cancel the unused portion in consultation with the Government and participating banks. Earlier cancellation would have saved the Government and participating banks a considerable amount of commitment fees paid on the unused portion of the loan. In addition, the time, effort, and resources expended by ADB, the Government, and participating banks in pursuing the loan over such a long period of time could have been saved.

41. ADB's discussions with the Government and participating banks took place as late as October–December 2005 in regard to the interest rate issue and other constraints on use of the ADB loan. As mentioned previously, ADB agreed to remove some of these restrictions, but it was too late in the project implementation (December 2005 following those discussions). By then, the Government and participating banks had decided not to proceed any further with the ADB loan, mainly on the issue of the cost of funds difference in favor of the banks' own resources, leading to its ultimate cancellation. Hence, those discussions should have begun much earlier, which would have shown that the loan did not have any prospects for success and that it needed cancellation.

42. Secondly, subloan and subproject data as well as socioeconomic data on subprojects financed were not readily available to the PCR mission, impeding PCR preparation. The PCR—which BEI was required to submit to ADB within 3 months of the loan's closing date—was not submitted. In addition, the appraisal required that project and benefit monitoring and evaluation mechanisms be set up within TAMU. However, these mechanisms did not appear to be functioning properly within BEI. ADB review missions should have ensured that these appraisal requirements were actually met by BEI, and continued to work properly within BEI to make available project data when required. These actions were not done by ADB as expected. The Project was transferred for follow-up by the Indonesia Resident Mission (IRM) on 15 July 2004, that is, about 2 months after the loan became effective.

43. IRM's capability in project management, particularly relating to the financial sector, appears to need strengthening. Weaknesses were shown by the delay and vacillation in taking

action to cancel the unused portion of the loan, as well as shortcomings in general project supervision work. These shortcomings were reflected by the unavailability of required project data, and their continuous analysis and reporting. In the future, before projects are transferred for IRM management, arrangements should be made to train staff members properly. Trainings should cover project management to ensure effective project follow-up and supervision, and staff members should also take full responsibility for overall project management.

III. EVALUATION

A. Loan Appraisal

44. Although the Project design and formulation appeared appropriate at appraisal, its suitability reduced considerably during project implementation, leading to the poor loan utilization status. The appraisal envisaged the financing of about 150 subloans, but only 23 (15%) were ultimately financed. The case for the loan was made on the basis of these points.

(i) SMEs had difficulty in obtaining financing (RRP, para. 17).
(ii) Access to finance for private enterprises and SMEs was drastically reduced during the financial crisis, and the mobilization of financial funds continued to be challenging until the time of appraisal.
(iii) Long-term funds in foreign exchange available for investment had declined (RRP, para. 18).

The ADB loan's interest rate to the subborrowers was also expected to be competitive—a premise that changed considerably during project implementation.

45. The appraisal should have foreseen that change in the economic environment was likely to arise, because there were signs in that direction even at the time of appraisal. The gross domestic product growth rates, foreign exchange reserves, and liquidity in the banking system were all showing upward trends.[21] Had those signs been taken into consideration and a forecast been made at appraisal of the likely economic environment during project implementation, there would have been indications that the ADB loan interest rate might not be competitive.

46. A forecast could have led to alternative foreign currency resources being made available for SME use. Based on such a forecast, it was quite possible that ADB might not have proceeded with the loan or proceeded with a reduced loan size (the subproject pipeline was only $28 million at appraisal). Another option would have been to make the ADB loan structure flexible (in terms of interest rates, fees payable to intermediaries, and subloan conditions) to accommodate any changes necessary arising during project implementation. As stated earlier, with the improving economic performance after the financial crisis, liquidity (local and foreign currencies) of banks increased to the extent that they were able to fund SME working capital and import requirements at cheaper rates with a cost of funds advantage. In these circumstances, the need for the participating banks to utilize the ADB loan diminished

[21] The gross domestic product increased from –13.1% at the height of the financial crisis in 1998, to 4.3% at the time of the appraisal, to 5.0% in 2004 when the loan became effective, and to 6.3% in 2007 when the Government and participating banks requested cancellation of the unused portion of the loan. Foreign exchange reserves increased from $22,401 million in 1998, to $30,754 million in 2002, to $34,724 million in 2004, and to $54,737 million in 2007 (ADB. {2008}. *Key Indicators for Asia and the Pacific {2008}.* Manila). In 2001, the loan–deposit ratio of banks were 6.7%, Bank Bukopin; 26.3%, Bank Danamon Indonesia; 24.7%, Bank Mandiri; 45.0%, Bank Niaga; 35.2%, Bank Negara Indonesia; and 56.1%, Bank Rakyat Indonesia (RRP, Appendix 3, Table A3.4).

considerably during project implementation, leading to a much smaller number of subloans financed against those envisaged at appraisal.

47. The project design and formulation also included too many subloan conditions or restrictions on the use of loan proceeds, including limits on maximum subloan size, low free limits, use of the subloan for working capital only up to 35% of its size, and various criteria that subprojects had to meet to qualify for a subloan. The restrictions were found inappropriate during project implementation, as the participating banks could finance SME requirements better without those limits. These banks also conducted due diligence on prospective borrowers in accordance with their own prudent financial guidelines, and considered the ADB criteria as superfluous. The appraisal should have synchronized the ADB subloan and subproject conditions with those of the participating banks, which would have facilitated greater loan utilization, although the cost of funds difference would still have been present.

B. Implementation

48. Project implementation was not satisfactory. The loan used only $5.59 million (6.6%), and the balance of $78.56 million (92.4%) was canceled.[22] Only 23 subloans were financed against the appraisal's envisaged number of 150 subloans (15%). The Government and ADB discussed ways to increase loan utilization, but the cost of funds differential in favor of the participating bank funds remained as an overwhelming issue that led to loan cancellation.[23]

49. The 14 subprojects, financed with the ADB loan, are operating satisfactorily and repaying the subloans generally within the scheduled dates. Since all are export-oriented, they are generally protected from major changes in the exchange rate. BEI and the two participating banks are also operating satisfactorily, maintaining sound financial positions, and meeting ADB-prescribed financial covenants and those of Bank of Indonesia. An updated project framework is given in Appendix 5.

IV. ASSESSMENT AND RECOMMENDATIONS

A. Relevance

50. Although the Project was relevant at appraisal, its relevance declined during project implementation and completion due to changes in economic circumstances. With economic growth, expansion in foreign exchange reserves, and increased liquidity in the banking system, the participating banks were able to fund SME requirements with their own resources at rates cheaper than those under the ADB loan. The Project's design and structure—with LIBOR-based interest rates and payment of fees to intermediaries—raised the interest rates under the ADB loan above those prevailing in the market, and strict subloan conditions further constrained loan utilization. Thus, the participating banks were not in a position to use the ADB loan, resulting in the Project being rated as *partly relevant.*

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[22] The total disbursement amounted to $6.44 million, which included subloan disbursement of $5.59 million and a front-end fee of $850,000.

[23] Under the TA, a consulting firm (GFA Management) was engaged to support BEI and the Executing Agency in the implementation of the Small and Medium Exporters' Investment Facility. A staff consultant (Frank van Gelder) was also engaged to assist the IRM project officer to provide approval to SME export subprojects. A notice to proceed was issued to GFA Management on 27 November 2003, and the consultant was fielded on 1 December 2003.

B. Effectiveness in Achieving Outcome

51. The Project is rated *less effective* in achieving outcome. The appraisal estimated that the loan would finance about 150 subloans, resulting in additional investment and employment in 150 direct individual exporters and indirectly in up to 3,000 SMEs via subcontracting arrangements (RRP, para. 49). However, the loan financed only 23 subloans for 14 subprojects. Because of the small number of subprojects financed, the envisaged outcome was not achieved, that is, contributing to the development of the SME sector, supporting economic growth, and reducing poverty through job creation and promotion of labor-intensive exports.

C. Efficiency in Achieving Outcome and Outputs

52. The Project is rated *inefficient* in achieving outcome and outputs. The appraisal estimated that the loan of $85 million would be fully used and that the Project would be completed on 31 December 2007. However, when the decision to cancel the unused portion of the loan was made in January 2007 and the loan was canceled in September 2008, only 6.6% of the loan amount had been used. That amount of loan utilization was not commensurate with the time, effort, and resources expended by ADB, the Government, and participating banks in appraising the Project and in its subsequent follow-ups. The few subprojects financed, Implementing Agency, and two participating banks, however, are operating satisfactorily.

D. Preliminary Assessment of Sustainability

53. The Project, as designed and formulated at appraisal, is not workable; therefore, its sustainability is *unlikely* in the prevailing economic environment. As pointed out earlier, because of increased liquidity, the participating banks are able to fund SME requirements with their own resources at cheaper rates than the ADB loan. Since the participating banks and small number of subprojects financed are operating satisfactorily, they appear sustainable.

E. Impact

54. The impact of the Project was minimal compared to that envisaged at appraisal, because the small number of subprojects financed was able to make little impact in developing the SME sector, contributing to economic growth, and reducing poverty through employment creation and promotion of labor-intensive exports. Since the envisaged benefit monitoring and evaluation mechanism was not operating satisfactorily within BEI, information on these aspects could not be extracted. However, the PCR mission was able to gather information in the field, which showed that the few subprojects financed contributed to value addition, employment creation, and export growth. To that extent, they made some impact, but not to the extent envisaged at appraisal. Socioeconomic data on four subprojects financed indicated that they created additional employment for 920 persons and generated additional exports to the value of about $6.9 million per year.

F. Overall Assessment

55. Taking the above individual ratings into account, the Project is rated as *unsuccessful.* The PCR mission discussions with the Ministry of Finance showed that the Government also believed that it was unsuccessful.[24] ADB rated both development objectives and implementation

[24] Discussions were held with the Directorate General of Treasury, Directorate of Investment Management System, Ministry of Finance on 13 July 2009.

progress as *satisfactory* from December 2004 to September 2008 (see "Project Performance Report Ratings" of IRM/ADB as given under item C.8 of Basic Data above), which is unrealistic in view of the overall unsatisfactory performance of the Project during its implementation period.

G. Lessons

56. The following lessons are learned from the Project.

(i) The Project environment changed from the time it was appraised to when it was implemented. Thus, it is important at project appraisal to make the effort to forecast what the project environment will likely be during project implementation. At appraisal, it would have been possible to predict with some degree of accuracy that the liquidity of participating banks would increase, and their cost of funds might be lower than those under the ADB loan, because of the ongoing improvement in the Indonesian economy after the financial crisis. Had that been done, it is possible that the Project might not have occurred or occurred only on a scaled-down basis.

(ii) Delay in the cancellation of the unused portion of the loan made the Government and participating banks pay ADB unnecessary commitment fees. That, as well as other resources expended by the Government, participating banks, and ADB in following up the Project during its implementation period, could have been saved had the unused portion of the loan been canceled earlier. The lesson learned is that early warning signals should be watched carefully. If signs indicate that a loan is going to be unsuccessful, ADB should initiate decisive action to cancel the unused portion of the loan. It can save resources and commitment fees from unnecessarily being incurred on a project that does not have much prospect for success.

(iii) Market fluctuations in interest rates affect lending through private sector banks for private sector entities. The ADB loan, however, did not have flexibility to adjust to the changing interest rates in the market. The long-term tenor of the ADB loan was not a decisive factor, as SMEs mainly required shorter-term working capital loans. The Project was designed on the basis of a traditional public sector development finance institution credit line modality. The structure included LIBOR-based lending and required fees to be paid to the intermediaries involved, which made the loan price out of the market. In addition, the strict conditions and procedures for subloan approval made the use of the ADB loan both inconvenient and time-consuming for the subborrower. The lesson learned is that a public sector-type modality and structure does not have much prospect for success for financing private banks and private sector enterprises, particularly in a more open and fairly successful economy with sizable bank liquidity and foreign exchange reserves, as in the case of Indonesia. In this environment, SMEs seek the cheapest funds available and the most convenient sources from which they could borrow their needed funds. On both counts, this ADB loan was not competitive.

(iv) A more viable instrument for SME promotion would have been to consider the use of ADB credit guarantees scheme under the Partial Credit Guarantee Facility, that is, the ADB private sector window. This facility could have been extended to a selected number of viable private banks operating at the regional level to guarantee up to a certain percentage of well-defined SME loan portfolios without a counterguarantee from the Government. Credit guarantee operations had greater success prospects than loans in situations where there was high liquidity and foreign currency reserves in the market. ADB used such a facility through a

selected number of private banks for SME promotion with success in the Philippines.

H. Recommendations

57. The following project-related recommendations are made.

(i) An ADB inception mission should clearly establish project monitoring and benefit monitoring and evaluation mechanisms as recommended in the RRP within the project implementing agency and ADB. Thereafter, the subsequent ADB review missions should rigorously follow up, check, and report in their back-to-office reports whether the Implementing Agency is, in fact, receiving the reports expected, analyzing them, and taking appropriate action on them.

(ii) To facilitate PCR preparation, ADB should send a reminder to the Implementing Agency on PCR preparation and submission to ADB. In addition, ADB should send a questionnaire to obtain information and data as required for PCR preparation to the implementing agency 2 months before commencement of PCR fieldwork. Thereafter, ADB should make regular contact with the Implementing Agency to ensure that that information is being prepared and will be available to the ADB at least 2 weeks prior to commencement of PCR fieldwork.

(iii) Before a project is transferred for IRM custody, arrangements should be made to train IRM staff members in the skills and expertise needed to ensure proper management of that project and its success during implementation and completion. Thereafter, IRM's portfolio management unit should fix staff responsibilities and ensure that project management is being rigorously carried out with proper data collection, analysis, and regular reporting to management.

(iv) The project performance evaluation report on the Project should be prepared in 2 years, in 2011.

58. The following general recommendations are made for ADB consideration.

(i) ADB should conduct, in the design and formulation of a project, appraisals to take into account the economic conditions at the time of the appraisal, as well as those likely to prevail during project implementation and to ensure project success during project implementation and at completion.

(ii) ADB should take immediate and decisive action to cancel the unused portion of a loan, if early warning signals show that a project is unlikely to succeed. This saves resources and commitment fees unnecessarily being incurred on a project that had no prospects for success.

(iii) ADB should extend partial credit guarantees under the Partial Credit Guarantee Facility to a selected number of regional-based private banks to guarantee up to a certain percentage of well-defined SME loan portfolios without a counter guarantee from the Government.

Statement on Cost of Funds of Participating Banks

and those under the ADB Loan
2002—2008
(Quarterly Basis)

Description	2002	2003				2004				2005				2006				2007				2008			
	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
LIBOR 3 million	1.383	1.288	1.116	1.16	1.157	1.111	1.604	2.005	2.558	3.1	3.505	4.055	4.53	4.99	5.509	5.373	5.36	5.348	5.359	5.494	4.979	2.783	2.765	3.122	1.829
OCR Rate																									
(LIBOR + 0.6%)	1.983	1.888	1.716	1.76	1.757	1.711	2.204	2.605	3.158	3.7	4.105	4.655	5.13	5.59	6.109	5.973	5.96	5.948	5.959	6.094	5.579	3.383	3.365	3.722	2.429
MOF fee (0.5%)	2.483	2.388	2.216	2.26	2.257	2.211	2.704	3.105	3.658	4.2	4.605	5.155	5.63	6.09	6.609	6.473	6.46	6.448	6.459	6.594	6.079	3.883	3.865	4.222	2.929
BEI Provisioning (1%)	3.483	3.388	3.216	3.26	3.257	3.211	3.704	4.105	4.658	5.2	5.605	6.155	6.63	7.09	7.609	7.473	7.46	7.448	7.459	7.594	7.079	4.883	4.865	5.222	3.929
BEI Overhead Cost (0.3%)	3.783	3.688	3.516	3.56	3.557	3.511	4.004	4.405	4.958	5.5	5.905	6.455	6.93	7.39	7.909	7.773	7.76	7.748	7.759	7.894	7.379	5.183	5.165	5.522	4.229
Risk Premium																									
(assuming lowest risk premium of 0%)	3.783	3.688	3.516	3.56	3.557	3.511	4.004	4.405	4.958	5.5	5.905	6.455	6.93	7.39	7.909	7.773	7.76	7.748	7.759	7.894	7.379	5.183	5.165	5.522	4.229
Total COF to Participants	3.783	3.688	3.516	3.56	3.557	3.511	4.004	4.405	4.958	5.5	5.905	6.455	6.93	7.39	7.909	7.773	7.76	7.748	7.759	7.894	7.379	5.183	5.165	5.522	4.229

Average Bank Cost	2.9	2.24	2.29	2.2	1.91	1.16	1.17	1.01	1.3	1.5	1.9	2.59	3.03	3.37	3.53	3.45	3.43	3.55	3.63	3.9	3.55	3.28	2.91	2.79	2.92
Range of Bank COF	8—4.63	5—3.34	05—50	0—2.34	6—4.69	4—1.79	2—1.82	5—1.52	9—2.11	9—2.41	7—2.94	3—4.35	2—4.04	7—4.27	9—4.57	3—4.68	0—4.57	4—4.97	3—5.04	5—5.86	1—4.58	7—4.09	7—3.75	0—3.67	9—3.94
COF Gap (SMEEDP COF-	0.883	1.448	1.226	1.36	1.647	2.351	2.834	3.395	3.658	4	4.005	3.865	3.9	4.02	4.379	4.323	4.33	4.198	4.129	3.994	3.829	1.903	2.255	2.732	1.309

BEI = Bank Ekspor Indonesia; COF = Cost of Fund; Libor = London Interbank Offered Rate; MoF = Ministry of Finance; OCR = Ordinary Capital Resources; SMEEDP = Small and Medium Enterprise Export Development Project.
Sources: Bank Ekspor Indonesia

Analysis of the interest rate movement

The LIBOR rate, on which the ADB loan rate was based, increased from a relatively low rate at the time of the appraisal (July-August 2001) and at Board Approval (December 2002). Three month LIBOR in the fourth quarter of 2002 was 1.38%, but after the loan became effective and ready for utilization in May 2004, the rate increased from 1.60% in the second quarter of 2004 to 3.51% in the second quarter of 2005. It kept on increasing to 5.51% in the second quarter of 2006 when the Government and the PBs decided to cancel the loan. The rate decreased slightly to 5.36% in the second quarter of 2007. The LIBOR rate further reduced to 1.83% in the fourth quarter of 2008, after the loan was closed.

Apart from the LIBOR interest rate issue, the COF of the PBs under the ADB loan was higher compared to their own resources, because of the manner in which the ADB loan was structured, i.e., the fees payble to the various intermediaries involved. For example, those fees were: 0.5% fee to MOF, BEI provisioning of 1%, and BEI overhead cost of 0.3%. When all these fees were added to the increasing LIBOR rate, the total COF to a PB under the ADB loan came to 3.78% in the fourth quarter 2002. The rate kept on increasing to 4.00% in the second quarter of 2004, 5.91% in the second quarter of 2005, 7.91% in the second quarter of 2006, before it decreased slightly to 7.76% in the second quarter of 2007. The rate decreased again to 4.23% in the fourth quarter of 2008. Meanwhile, the average cost of funds for the PBs was: 2.9% in the fourth quarter of 2002, 1.2% in the second quarter of 2004, 1.9% in the second quarter of 2005, 3.5% in the second quarter of 2006, 3.6% in the second quarter of 2007, and 2.9% in the fourth quarter of 2008.

Table A2.1: List of Sub Loans / Sub projects and Their Characteristics

Sub-project		No. of Sub Loans	Amount	Purpose
I. BNI				
Name				
1	CV Mekar Abadi	1	449,000	Investment
		2	118,200	Working capital
			567,200	
2	CV Sumber Alam Sakti	3	110,558	Working capital
		4	115,534	Working capital
		5	773,908	Investment
			1,000,000	
3	CV Rajawali P. Furniture	6	162,877	Investment
		7	53,423	Working capital
			216,300	
4	CV Sylva Kriya Gemilang	8	70,000	Investment
		9	130,000	Working capital
			200,000	
5	CV Kalika Intergraha	10	36,900	Working capital
		11	68,530	Investment
			105,430	
6	PT 689	12	161,075	Working capital
		13	302,083	Investment
			463,158	
7	CV Surya Mandiri	14	210,526	Investment
8	PT Pelayaran B. Samudra	15	303,030	Investment
		16	223,285	Investment
			526,315	
9	CV Putra Tama Jaya	17	332,467	Working capital
		18	623,377	Investment
			955,844	
10	PT Eastwind Mandiri	19	180,000	Investment
11	Artanis Pratama Jaya	20	423,945	Investment
12	CV Lead Studio	21	273,643	Working Capital
13	CV Sutra Utama	22	358,324	Investment
II. BDI				
14	CV Gloria	23	110,000	Working capital
	TOTAL		**5,590,685**	

BDI = Bank Danamon Indonesia; BNI = Bank Negara Indonesia; CV = Commanditaire Vennootschap ; PT = Perseroan Terbatas.

Source: Bank Ekspor Indonesia.

Table A2.2: Characteristics of Sub Loans

	Description	No.	Amount ($)	Percentage of Loan Amount
1	**Number of Subloans by Participating Bank**			
	Bank Danamon Indonesia	1	110,000	2.0
	Bank Negara Indonesia	22	5,480,685	98.0
	Total	**23**	**5,590,685**	**100.0**
2	**Sector Distribution of Subloans**			
	Agri-business	3	1,000,000	17.9
	Food	2	463,158	8.3
	Textile and Garments	1	110,000	2.0
	Wood Products	13	2,859,245	51.1
	Non-Metal	1	273,643	4.9
	Transport	2	526,315	9.4
	Other	1	358,324	6.4
	Total	**23**	**5,590,685**	**100.0**
3	**Size of Subloans**			
	Below free-limit ($450,000)	21	4,193,400	75.0
	Above free-limit (above $450,000)	2	1,397,285	25.0
		23	5,590,685	100.0
4	**Geographic Distribution of Subloans**			
	Bali	2	383,643	6.9
	Semarang	16	3,859,245	69.0
	Sidoardjo	2	463,158	8.3
	Kalimantan	2	526,315	9.4
	Other	1	358,324	6.4
	Total	**23**	**5,590,685**	**100.0**
5	**Purpose of Subloans**			
	Investment	13	4,208,885	75.0
	Working Capital	10	1,381,800	25.0
	Total	23	5,590,685	**100.0**
6	**Type of Subloans**			
	New	2	200,000	4.0
	Expansion	21	5,390,685	96.0
	Total	**23**	**5,590,685**	**100.0**
7	**Maturity of Subloans**			
	Up to 3 years	7	1,071,210	19.2
	Over 3 to 5 years	9	2,008,995	35.9
	over 5 to 8 years	7	2,510,480	44.9
	Total	**23**	**5,590,685**	**100.0**

Source: Bank Ekspor Indonesia.

BANK EKSPOR INDONESIA
Table A3.1:Summary of Financial Statements
(Income and Balance Sheets and Ratios)
(2004—2008)

(in Rp billion unless stated otherwise)

Financial Year Ending 31 December	**2004**	**2005**	**2006**	**2007**	**2008**
I. INCOME STATEMENTS					
Interest Income	354,927	561,378	839,392	924,724	1,042,985
Interest Expense	(127,539)	(218,292)	(337,094)	(437,775)	(461,316)
Net Income	227,388	343,086	502,299	486,949	581,669
Operational Income	98,703	38,672	18,364	27,938	28,078
Operational Expense	(59,612)	(88,076)	(160,769)	(109,985)	(259,913)
Operational Profit	266,480	293,682	359,895	404,901	349,834
Other Operational Expense	(45)	(152)	730	705	1,308
Income before tax	266,435	293,530	360,624	405,606	351,142
Tax	(84,259)	(93,019)	(114,402)	(127,208)	(109,494)
Net Income	182,176	200,511	246,222	278,398	241,648
ROA (%)	5.09	4.37	4.5	0.041	0.0293
ROE (%)	4.99	5.37	6.39	0.0695	0.058
II. BALANCE SHEETS					
Assets					
Cash on hand	47	121	357	230	464
Placement with Bank Indonesia	9,990	47,963	-	6,999	-
Placement with other banks	764,206	1,357,607	1,108,186	1,127,794	634,142
Loans Receivable - net	6,050,117	4,600,393	5,797,750	6,258,052	9,216,530
Other assets	613,364	1,529,038	1,898,285	2,898,962	1,340,121
Total Assets	7,437,724	7,535,122	8,804,579	10,292,037	11,191,257
Liabilities					
Due to other banks	1,128,675	914,490	60,000	778,930	697,450
Other Liabilities	1,232,589	1,407,102	2,553,683	1,949,395	2,256,090
Fund Borrowing	1,346,529	1,376,362	2,197,334	3,397,629	3,952,480
Total Liabilities	3,707,793	3,697,953	4,811,017	6,125,953	6,906,020
Shareholders' Funds					
Equity	3,000,000	3,000,000	3,000,000	3,000,000	3,000,000
Reserves	729,931	837,168	993,562	1,166,084	1,285,237
Total Stockholder's Funds	3,729,931	3,837,168	3,993,562	4,166,084	4,285,237
Total Liabilities and Shareholders' Funds	7,437,724	7,535,122	8,804,579	10,292,037	11,191,257
Capital Adequacy Ratio (CAR %)	1.142	1.1239	0.7372	0.5772	0.3909
Loan-deposit ratio (BI Regulation) (%)	5.78	28.0294	5.875	14.0506	10.1669

Source: BEI, Annual Report 2007.

BANK DANAMON INDONESIA (BDI)
Table A3.2: Summary of Financial Statements (Income and Balance Sheets and Ratios) (2004—2008)

(in Rp billion rupiah unless stated otherwise)

Financial Year Ending 31 December **BALANCE SHEET**	**2004**	**2005**	**2006**	**2007**	**2008**
CONSOLIDATED BALANCE SHEETS					
Assets	58,821	67,803	82,073	89,410	107,268
Erning Assets	52,555	59,968	73,236	78,907	94,980
Government Bonds	17,324	14,102	18,702	15,808	13,083
Loans [a b]	30,294	36,757	42,986	53,330	66,898
Deposits [c d]	40,765	47,089	56,930	59,528	75,373
Total Funding [e]	45,044	53,342	66,281	70,976	88,029
Shareholder's Equity	7,804	8,589	9,442	10,833	10,579
CONSOLIDATED STATEMENTS OF INCOME					
Interest income	6,395	8,129	10,896	12,048	14,189
Interest Expenses	(2,376)	(3,526)	(5,251)	(4,912)	(5,835)
Net Interest Income	4,019	4,603	5,645	7,136	8,354
Normalized Fee Income	690	1,080	1,358	1,741	1,997
Normalized Operating Income	4,709	5,683	7,003	8,877	10,351
Normalized Operating Expense	(1,963)	(2,909)	(3,428)	(4,255)	(5,604)
Pre-Provision Operation Profit	2,746	2,774	3,575	4,622	4,747
Normalized Cost of Credit	(833)	(814)	(1,332)	(1,240)	(1,076)
Normalized Net Profit Before Tax	1,913	1,960	2,243	3,382	3,671
Goodwill & Minority Interest	(163)	(206)	(202)	(222)	(261)
Normalized Income Tax	(637)	(559)	(652)	(1,043)	1,076
Normalized Net Profit After Tax	1,113	1,195	1,389	2,117	2,334
Non Recurring Items (After Tax)	1,295	808	(64)	-	(804)
Reported Net Profit After Tax	2,408	2,003	1,325	2,117	1,530
Earnings Per Share (in rupiah)	490.75	407.71	268.91	423.27	303.70
KEY FINANCIAL RATIOS (%)					
Net Interest Margin	8.6	8.9	9.6	10.4	11.1
Cost to Income	41.5	48.8	48.9	47.9	54.1
Normalized Cost of Credit	2.1	3.2	2.9	2.3	1.6
Normalized Return on Average Assets	2.1	1.8	1.8	2.4	2.4
Normalized Return on Average Equity	17.9	15.2	16.5	22.9	22.3
Reported Return on Average Assets	4.5	3.1	1.8	2.4	1.5
Reported Return on Average Equity	38.6	24.2	15.6	22.9	14.6
Loan to Deposits[f]	72.2	80.8	75.5	88.1	86.4
Non Performing Loans to Total Loans	4.0	2.6	3.3	2.3	2.3
Loan Loss Allowances to Non Performing Loans[g]	136.5	145.0	141.7	161.2	136.7
Capital Adequacy Ratio (Consolidated)[h]	25.6	22.7	20.8	20.3	15.4
OTHERS					
Number of Employees[i]	26,185	28,829	31,227	35,342	41,617
Number of Branches[j]	929	1,327	1,392	1,426	1,871
Number of ATMs	824	779	754	690	814

a Loan include consumer financing receivables.
b Loans purchased at IBRA are stated at purchase price.
c Reclassification Prima Dollar from current account into saving in 2007.
d Reclassification FRCD from Time Deposit to Borrowings in 2007.
e Includes deposits and long-term funding.
f Includes deposits from other banks.
g Includes collateral value.
h Consolidated CAR after market risk charge and amortization of subordinated debts for 2006, 2007 and 2008.
i Include 14,079, 1536 and 643 employees of Adira Finance, Adira Quantum and Adira Insurance, respectively.
j Includes 300, 46, and 42 branches of Adira Finance, Adira Quantum and Adira Insurance, respectively.
Source: BDI, Annual Report 2007.

BANK NEGARA INDONESIA (BNI)
Table A3.3: Summary of Financial Statements
(Income and Balance Sheets and Ratios)
(2004—2008)

(in Rp billion rupiah unless stated otherwise)

Financial Year Ending 31 December **BALANCE SHEETS**	**2004**	**2005**	**2006**	**2007**	**2008**
Total Assets	136,582	147,812	169,416	183,342	201,741
Marketable Securities (Gross)	6,479	3,773	4,956	16,201	9,874
Loan (Gross)	57,868	62,659	66,460	88,651	111,994
Government Bonds	38,943	37,444	41,227	36,701	34,655
Customer Deposits	105,097	115,372	135,797	146,189	163,164
Borrowing and Marketing Securities Issued	6,497	6,913	5,544	7,578	9,886
Subordinated Debt	2,285	2,433	2,239	934	-
Total Liabilities	123,930	135,891	154,597	166,094	186,279
Equity	12,624	11,885	14,794	17,220	15,431
INCOME STATEMENTS					
Interest income	11,788	12,707	15,044	14,878	16,628
Interest Expenses	(4,648)	(5,536)	(7,667)	(7,410)	(6,716)
Net Interest Income	7,141	7,172	7,377	7,467	9,912
Other Operating Income	2,763	2,101	2,861	4,130	3,549
Operating Income	9,904	9,273	10,238	11,597	13,461
Other Operating Expenses	(4,686)	(5,752)	(6,258)	(7,626)	(7,228)
Pre-Provision Income	5,218	3,521	3,980	3,971	6,233
Allowance for Possible Losses on Earning Assets	(2,128)	(1,256)	(1,319)	(2,704)	(4,359)
Net Operating Income	3,090	2,266	2,661	1,268	1,875
Net Non Operating Income	(16)	(10)	179	213	58
Income Before Tax	3,074	2,256	2,840	1,481	1,932
Income Tax	19	(839)	(911)	(579)	(706)
Net Income After Tax	3,093	1,417	1,929	902	1,226
Minority Interest	(3)	(2)	(3)	(4)	(3)
Net Income	3,090	1,415	1,926	898	1,222
Earning Per Share (in rupiah)	233	106	145	64	80
FINANCIAL RATIOS (%)					
ROA	2.5	1.6	1.9	0.9	1.1
ROE	29.6	12.6	22.6	8.0	9.0
NIM	5.6	5.4	5.2	5.0	6.3
Loans to Deposit Ratio	55.1	54.2	49.2	60.6	68.6
Capital Adequacy Ratio (CAR)	17.1	16.0	15.3	15.7	13.5
NPL Gross	4.6	13.7	10.5	8.2	4.9
NPL Net	1.4	8.4	6.6	4.0	1.7
LLR / NPL Gross	117.5	50.4	55.1	71.9	101.0
Cost to Income Ratio	47.3	61.9	61.1	65.8	53.7
Operating Expense to Operating Income	78.6	84.9	84.9	93.0	90.2
Net Open Position (NOP)	4.7	8.2	6.8	6.1	7.6
OTHERS					
Number of Branches	943	950	972	983	998
Number of ATMs	2,272	2,272	2,325	2,476	2,918
Number of Employees	18,874	19,894	19,116	18,320	18,032

ROA = Return of Average Assets ; ROE = Return of Average Equity ; NIM = Net Interest Margin;
NPL= Non Performing Loans; LLR = Loan-Loss Reserve.
Source:BNI, Annual Report 2007.

Table A4.1: Status of Compliance with Loan Covenants

Covenant	Reference in Loan Agreement	Status of Compliance
A. Execution of the Project		
i) A TAMU shall continue to be maintained by BEI	L.A. Sch. 3 para.2 (a)	Not complied with
ii) TAMU carry out various assigned responsibilities as outlined	L.A. Sch. 3 para.2 (b)	Not complied with
iii) Allocation of Loan Proceeds (i) up to $50,000,000 million to BEI, (ii) up to $20,000,000 million to BNI, and (iii) up to $15,000,000 to BRI	L.A. Sch. 3 para.5(a)	Complied with
B. Eligibility Criteria		
1. Qualified Enterprise (QF) and Project (QP) are:		
i) Exporter who shall earn sufficient foreign exchange revenue to sub-loan repayment schedules	L.A. Sch. 3 para.10 (a) (i)	Complied with
ii) Sponsor's equity contribution should be at least 25%	L.A. Sch. 3 para.10 (a) (ii)	No data to verify
iii) The financial internal rate of return (FIRR) shall not be less than 12%	L.A. Sch. 3 para.10 (a) (iii)	No data to verify
iv) A minimum debt service coverage ratio of 1.20 times no later than 3 years after disbursement of a sub-loan or at the QP's attainment of full production	L.A. Sch. 3 para.10 (a) (iv)	No data to verify
v) Maintain positive cash flow after repayment of sub-loan's principal and interest throughout the sub-loan repayment period	L.A. Sch. 3 para.10 (a) (v)	No data to verify
vi) Have and maintain adequate collateral in accordance with the concerned PB's internal credit assessment and Bank Indonesia regulations	L.A. Sch. 3 para.10 (a) (vi)	No data to verify
vii) Have no adverse environmental impact and conformed with other regulations and standards of the Borrower and ADB	L.A. Sch. 3 para.10 (a) (vii)	Two sampled sub-projects show environmental impact looked into in their due diligence and had no adverse environmental impact
viii) Preference given to QEs located outside Jakarta	L.A. Sch. 3 para.10 (a) (viii)	Complied with
C. Sub-loan Terms		
i) Sub-loans not exceeding $600,000 each to SME exporters which are direct sub-loan debtors	L.A. Sch. 3 para.12 (a)	Complied with
ii) Sub-loans not exceeding $1,000,000 to a group of not less than 20 microenterprises or SMEs	L.A. Sch. 3 para.12 (b)	Complied with

Covenant	Reference in Loan Agreement	Status of Compliance
iii) Sub-loans for (i) fixed investment, including but not limited to capital goods; (ii) technology for new investment projects or modernization of existing enterprises, and (iii) foreign currency cost of initial and incremental working capital necessary for operationalization of fixed investment, not exceeding 35 percent of the total sub-loan	L.A. Sch. 3 para.12 (c)	Working capital loans given for maximum of 35% of sub-loan but no data to verify whether sub-loan financed foreign currency costs of working capital
iv) Sub-loans which do not finance land use rights, taxes, duties and wages	L.A. Sch. 3 para.12 (d)	No data to verify
v) Sub-loans which do not finance project involving production of firearm, narcotics, tobacco or spirits	L.A. Sch. 3 para.12 (e)	Complied with
vi) Sub-loans which do not exceed 75% of the total cost of a QF	L.A. Sch. 3 para.12 (f)	No data to verify
vii) The foreign exchange risk with respect to repayment of the sub-loan shall be borne by QF	Implementation Agreement (I.A) Sch. Para.7(a)	Complied with
viii) Sub-loan repayment periods shall be based on cash flow forecasts for QFs, but shall in no event exceed 8 years, including a grace period o f no more than 3 years	I.A.Sch. para.7 (b)	Complied with
ix) The interest rate shall be LIBOR plus 125 basis points, where applicable, a PB risk premium agreed under Relending Agreements, and such spread as may be based on the risk of the QE.	I.A.Sch. para.7 (b)	Complied with
D. Eligibility of BEI and PBs		
(a) PB concerned meets, exceeds or is otherwise in compliance with all prudential regulations and guidelines of Bank Indonesia, as amended from time to time, including but not limited to (i) a net open position (NOP) not in excess of 20%; (ii) a loan to deposit ratio provisions sufficient to cover non-performing assets; (iv) compliance with legal lending limits (LLL) under Bank Indonesia's regulations, and (v) a CAR of not less than 8%	I.A.Sch. para.1 (a)	Complied with
(b) BEI and PB concerned meets, exceeds or is otherwise in compliance with (i) a ratio of net nonperforming loans (NPLs) to total loan portfolio not in excess of 5%, and (ii) a positive Return on Assets ratio	I.A.Sch. para.1 (b)	Complied with
(c) BEI meets, exceeds or is otherwise in compliance with all applicable prudential regulations and guidelines of Bank Indonesia, as amended from time to time; and	I.A.Sch. para.1 (c)	Complied with

Covenant	Reference in Loan Agreement	Status of Compliance
(d) Each PB shall submit through the TAMU an annual Letter of Representation to ADB of the PB concerned to, inter alia, (i) past and projected financial conditions in terms of solvency, liquidity, profitability, portfolio quality and efficiency in financial intermediation; (ii) past and projected lending to SMEs; (III) credit appraisal capabilities for lending to SMEs, and (iv) application of corporate governance standards and practices acceptable to Bank Indonesia	I.A.Sch. para.2	TAMU disbanded by BEI. Data not available to verify

Table A5.1: Project Framework

Design Summary	Performance Indicators/Targets	Monitoring Mechanisms	Assumptions and Risks
Goal Poverty reduction in Indonesia Balanced and sustainable economic growth Commercial, financially viable and sustainable private sector SMEs	Absolute poverty reduced by 50% from 20% in 2002 to 10% in 2015 Total non-oil and gas exports increased from $50 billion (2002 baseline) to at least $75 billion by 2015 Share of SME exports increased from 10% (2002 baseline) to at least 15% by 2015	Government macroeconomic and social statistics ADB project performance audit report	Due to increased liquidity in the market, both in foreign and local currency, interest rates of participating banks became cheaper than those offered under the ADB loan.
Purpose Increased exports by SMEs Increased SME employment opportunities	Value of direct exports by SMEs increases from $4 billion (2002 baseline) to at least $6 billion by 2005 Employment increases attributable to SMEs of 1.5 million job-years by 2015	Government macroeconomic labor, trade, and social statistics regarding SME performance ADB project completion report	Macroeconomic and political stability Overall government comprehensive economic and regulatory reforms SMEs will improve product design and quality to capture export markets.
Outputs Institutional capacity building of participating banks in credit appraisal of SME projects under market conditions Enhanced capacity of participating banks to undertake sound credit approval and risk analysis of subprojects and to provide financial advisory services for SMEs	Small and Medium Exporters' Investment Facility providing business advisory services by the end of the Project Financing of 100–150 subborrowers via participating banks by 2005, consistent with objectives and regional priorities of the Project Enhanced credit appraisal and risk analysis systems operational in last 3 years of the participating banks by 2005	Project progress reports by TAMU at BEI Quarterly reports by TAMU at BEI showing participating banks; financial indicators for continuing participation ADB loan review missions Visits to participating banks by TAMU Visits to TAMU by ADB review missions	Continued improvements in corporate governance by participating banks Ability of subborrower to meet lending criteria Effective aid coordination on SME matters will continue.
Activities Establish competent TAMU by BEI in 2002 Develop SEIF Conduct capacity building, training, and	SME exporters with access to business development services through business centers in selected cities across Indonesia	Reviewing and monitoring by ADB missions	Adequate absorptive capacity of participating banks for TA input Existence of financially and commercially viable subprojects that meet the

Design Summary	Performance Indicators/Targets	Monitoring Mechanisms	Assumptions and Risks
presentations for participating bank counterpart staff members on project financing (together with other aid agencies) On an as needed basis, provide financial services for SME subborrowers Provide long-term foreign currency debt funding for SME exporters	Start: 2003 Complete: 2005 Responsible: TA consultants Start: 2003 Complete: 2005 Responsible: participating banks Start: 2003 and continuing Responsible: participating banks		Project's development goals
Inputs Loan TA consultants	 $85 million loan $0.5 million International, 18 person-months Domestic, 22 person-months	 ADB disbursement records ADB project records	

ADB = Asian Development Bank, BEI = Bank Ekspor Indonesia, SEIF = Small and Medium Exporters' Investment Facility, SMEs = small and medium-sized enterprises, TA = technical assistance, TAMU = technical assistance management unit.