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Sida Evaluation

Carnegie Consult

Evaluation of Sida's use of guarantees for market development and poverty reduction

Case Studies for Evaluation report



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Carnegie Consult

Author: Carnegie Consult.

The views and interpretations expressed in this report are the authors' and do not necessarily reflect those of the Swedish International Development Cooperation Agency, Sida.

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Foreword

In November 2015 Sida commissioned Carnegie Consult to carry out an evaluation of Sida's use of guarantees for market development and poverty reduction with the objective of deepening Sida's knowledge on the guarantee instrument. The evaluation team was led by Hans Slegtenhorst and included Mart Nugteren, Alwin de Haas, Rien Strootman, Marie Heydenreich, Paulo Luswata, Nino Serdarevic, Anders Grettve and Bart Schaap. We wish to express thanks to the evaluation team and gratitude to the time and interest invested by all individuals and officials who have participated in the evaluation. Their collected contribution to this evaluation is an important input to Sida's efforts to further develop its work with guarantees.

Overall the evaluation found that the guarantees of Sida are useful instruments that positively contribute to private sector development. In cases where financial intermediaries are not able to lend to clients because of the risks involved, guarantees have shown to be important instruments to bridge the risks and allow intermediaries to reach out to clients that could otherwise not be served.

The evaluation highlights the importance of Sida selecting suitable banks as well as introducing competition between banks by selecting multiple banks in a guarantee facility to increase utilization and efficiency of the guarantee. Introducing flexibility in terms of guarantee percentages would also help banks to reach out to target groups. While technical assistance for borrowers and banks is seen as a potentially powerful tool, Sida should ensure this is provided in a focused manner and well aligned with the partners in the facility.

Furthermore the evaluations concludes that even if monitoring of results is the responsibility of the financial institutions banks should not be overwhelmed with monitoring of development impact beyond financial indicators. To enhance transparency and ease of monitoring, the evaluators recommend that for portfolio guarantees borrowers should be made aware of the existence of the guarantee, which is not always the case for reasons of moral hazard.

The evaluation also brings attention the importance of regular discussions and training between the Operational Departments of Sida and the Unit for Loans and Guarantees for a better use of the guarantee instrument and successful origination of transactions.

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Abbreviations and Acronyms

BiH	Bosnia Herzegovina
BPS	Basis points
CDFG	Community Development Finance Group
CFO	Corporate Financial Officer
CMA	Capital Market Authority
CMS	Credit Monitoring System
CMS	Credit Management System
CPP	Client Protection Principles
CRB	Credit Review Board
CRDB	Centenary Rural Development Bank
DCA	Development Credit Authority
DEG	The Deutsche Investitions – und. Entwicklungsgesellschaft
DFI	Development Financial Institution
DFID	Department for International Development
EBRD	European Bank for Reconstruction and Development
ECA	Export Credit Agency
EGAT/DC	Office of Development Credit in the Bureau for Economic Growth, Agriculture, and Trade
EIB	European Investment Bank
EKN	Swedish National Export Credits Guarantee Board
FARMA	Fostering Agricultural Market Activity
FIRMA	Fostering Interventions for Rapid Market Advancement
FMO	The Netherlands Development Finance Company
GCMC	Global Commercial Microfinance Consortium
GIZ	German Technical Cooperation
KfW	Kreditanstalt für Wiederaufbau
L&G	Loans and Guarantees
M&E	Monitoring & Evaluation
MFI	Microfinance Institution

MNO	Mobile Network Operators
MoU	Memorandum of Understanding
MTN – (U)	Mobile telecommunication company Uganda
NDF	Non-Deliverable Forward
NGO	Non-Governmental Organisation
NPL	Non-Performing Loan
NSSF	National Social Security Fund
OECD/DAC	OECD Development Assistance Committee
OPIC	Overseas Private Investment Corporation
PFP	Private For Profit
PHS	Private Health Support
PNFP	Private Not For Profit
PPP	Public Private Partnership
SACCO	Savings And Credit Co-Operative
SME	Small and Medium Sized Enterprises
TA	Technical Assistance
TCMP	Traditional and Complimentary Medicine Practitioners
ToR	Terms of Reference
UGX	Uganda Shilling exchange
UHF	Uganda Healthcare Federation
UPTC	UgandaPosts and Telecommunications Corporation's
USAID	United States Agency for International Development
USAID/ DCA	USAID's Development Credit Authority
USE	Uganda Stock Exchange
VSLA	Village Savings and Loans Associations

Glossary of Terms Used

Additionality	Likelihood that the effects observed would not have emerged in the absence of the intervention
Asset base	The underlying assets giving value to a company
Basis points	One hundredth of one percentage point (used chiefly in expressing differences of interest rates)
Collateral	Collateral is a security pledged for the repayment of a loan
Commercial risk	The risk that a borrower will be unable to pay its debts because of business events, such as bankruptcy
Corporate bond, principal, coupon	A security representing the debt of the company issuing it. When a company or government issues a bond, it borrows money from the bondholders; it then uses the money to invest in its operations. In exchange, the bondholder receives the principal amount back on a maturity date. In addition, the bondholder usually has the right to receive coupons or payments on the bond's interest
Disbursements	The actual physical transfer of monetary funds
Effectiveness	The extent to which the direct objectives of the interventions have been fulfilled, or can be expected to be fulfilled
Efficiency	Relationship between inputs and outputs, in this case the extent to which the guarantee intervention – from an organisational point of view – was designed and implemented in a (cost-) efficient way
First loss position	The position in a security that will suffer the first economic loss if the underlying assets lose value or are foreclosed on. The first-loss position carries a higher risk and a higher yield
Impact	The total of all effects of an intervention, positive or negative, expected or unexpected, including effects beyond the direct objectives of the guarantee

Internal rate of return (IRR)	The interest rate which equals, when discounting, positive and negative cashflows resulting from an investment over time. A metric measuring the profitability of potential investments.
Junior/subordinated debt	Debt which ranks after other debts if a company falls into liquidation or bankruptcy
Leverage	The relationship between an initial financial injection and the total value of all monetary inputs which emerge as a result of the initial injection. The ratio of a company's loan capital (debt) to the value of its ordinary shares (equity)
Notes	A note is a debt security obligating repayment of a loan at a set interest rate in a defined time period
Origination fee	A fee charged by the guarantor on entering into a guarantee agreement to cover the cost of processing the guarantee
Relevance	In how far the intervention was a relevant response to address the market development problems in its specific context
Revocable guarantee	A guaranty that the guarantor may terminate without any other party's consent
Revolving bank guarantee	Revolving bank guarantees limit the overall credit to be allowed to a customer with a validity period. The credit gets released once the customer makes the payment and can be used for new sales again
Senior debt	Debt that takes priority over other unsecured or otherwise more junior Debt owed by the issuer
Smart Campaign Client Protection Principles	Minimum standards that clients should expect to receive when doing business with a microfinance institution
Sustainability	How likely is it that positive results especially in terms of financial market strengthening will be sustained over time?
Tier-1 MFIs	Mature, financially sustainable, and large MFIs that are highly transparent
Utilisation fee	A fee based on the actual amount of funds drawn under the guarantee, payable to the guarantor
Yield	The income return on an investment

Preface

Sida commissioned Carnegie Consult to carry out an evaluation of ‘Sida’s use of guarantees for market development and poverty reduction’ on the basis of four specific guarantee interventions in November 2015. The evaluation was carried out between November 2015 – June 2016 including three field visits to Uganda, Bosnia – Herzegovina and New York during March – April 2016. The evaluation report was finalized in June 2016 after feedback from Sida and the reference group.

The following experts were involved in the assignment: Hans Slegtenhorst (team leader), Mart Nugteren, Alwin de Haas, Rien Strootman, Marie Heydenreich, Paulo Luswata, Nino Serdarevic, Anders Grettve and Bart Schaap.

We are grateful for the full support of Sofia Ericsson as the Sida-manager of this evaluation, as well as the support of all resourced staff at the loans and guarantees team at Sida. Anders Berlin and Camilla Rubensson from the Unit for Loans and Guarantees of Sida and Sofia Ericsson from the Unit for Planning, Monitoring and Evaluation joined two field missions as observers. Kalle Hellman, Anders Berlin and Sofia Ericsson also took part in different workshops during the evaluation together with the full evaluation team to discuss and challenge preliminary findings. Their remarks and positive criticism on earlier versions of this report were of great value to the final product.

Staff of USAID, partner of Sida in several interventions, were also very forthcoming in sharing information and facilitating access. Likewise the other partner organisations cooperated well, and this report would not have been possible without their cooperation.

Executive Summary

THE EVALUATION

In November 2015 Sida commissioned Carnegie Consult to carry out an evaluation of 'Sida's use of guarantees to promote market development and poverty reduction'. Since the 4th High Level forum on Aid Effectiveness in Busan in 2011 donors (including the government of Sweden) considered the private sector an important driver for economic growth, job creation and ultimately poverty reduction. For developing the private sector different financial instruments are required which ideally conform to the market circumstances and avoid market distortion. The guarantee instrument of Sida introduced in the late nineties is an example of this new innovative form of development cooperation.

The objective of this evaluation was to deepen Sida's knowledge on the guarantee instrument and to draw lessons of broader relevance from a limited number of interventions, rather than accountability. During the course of the evaluation it was therefore decided to involve Sida as a close observer in the evaluation without compromising the independence of the exercise. Representatives of Sida participated in the field visits and in workshops to discuss the observations and findings. Moreover the findings of the draft report were presented, challenged and discussed in Stockholm both with the steering committee for this evaluation as well as with the staff of the loan and guarantees team.

Sida selected the following four interventions for the evaluation:

- Deutsche Bank, Commercial Microfinance Consortium II, (Global)
- Raiffeisen/USAID (Bosnia-Herzegovina)
- Centenary Bank for Rural Development/USAID Health Guarantee (Uganda)
- MTN Mobile Coverage (Uganda)

Two interventions concerned portfolio guarantees in Uganda and Bosnia-Herzegovina facilitating lending to Small and Medium

Enterprises (SMEs), in Uganda to SMEs and micro-entrepreneurs in the private health sector. The objectives of the other two selected interventions were primarily to develop financial markets and creating leverage through attracting commercial investors. The corporate bond guarantee to MTN was issued to allow a new telecom operator in Uganda to roll out its operations in rural areas in a faster manner, whereas the Deutsche Bank guarantee intended to attract institutional investors for investing in the microfinance sector in developing economies. For the four intervention studies the evaluation team assessed the following evaluation criteria: relevance, efficiency, effectiveness and to a limited extent impact and sustainability. Moreover additionality was addressed, i.e. the likeliness that effects observed would also not have emerged in the absence of the intervention. The resulting synthesis report covered the main questions from the terms of reference for the evaluation.

- When to use, or not to use, the guarantee instrument?
- What to consider when designing and managing guarantees to maximize pro-poor market development impact?
- How to avoid market distortion?
- How to monitor and evaluate guarantee interventions, including assessing additionality?

MAIN FINDINGS

Based on the four interventions the use of the guarantee instrument was found generally relevant and efficient. The interventions were well aligned with the Swedish development policy, country strategies and priorities and were executed in an efficient manner.

In the two portfolio guarantees, Sida co-operated with the US donor agency USAID, who managed the guarantees as agent of Sida. USAID appeared to have good systems in place to monitor the portfolios in a professional and efficient manner. The advantage of this cooperation for Sida is that it reduces the pressure on the own organization while ensuring professional management of the facilities. A disadvantage is that Sida is less involved in the day-to-day follow-up activities and therefore lacks direct control. The selection of partner banks providing the loans to SMEs was found to be critical for the success of portfolio guarantees.

The other two interventions studied were also assessed positively in terms of relevance and efficiency. The intervention of Sida with the telecom operator in Uganda was innovative in that it introduced

a new financial instrument to the Ugandan capital market with the aim of attracting long term funding from local institutional investors. The other intervention targeted at involving institutional investors in microfinance was innovative as well as it allowed to create a fund structure with different layers of risk.

Sida charges a fee for the use of the guarantee instrument to its partners, which is meant to cover its own risk. Presently three players are involved in calculating the fee and assessing the risks: the Swedish Export Credit Board (EKN), the National Debt Office and Sida. Normally Sida subsidizes the premium calculated by EKN which results in a lower fee. USAID, involved in the portfolio guarantees, has its own risk assessment and fee calculation system. The resulting overall pricing system lacks consistency and transparency, which could be improved through clear guidelines and responsibilities.

In none of the interventions so far a claim has been issued as a result of a default. This is beneficial for efficiency and it creates opportunities for re-using the repaid funds for other interventions. At the same time it raises doubts on whether the risks guaranteed warranted a guarantee in all cases, which is a matter of additionality.

Additionality was assessed at two levels: (1) was the intervention additional in developing financial markets?; and (2) was the intervention additional in terms of reaching out to the ultimate target group (SMEs, microfinance institutions)? The interventions in Uganda were largely additional, at both levels. Market distortion was not observed, although the guarantee agreements in the case of the portfolio guarantees had been drawn up with single individual banks. In the Ugandan case the portfolio guarantee was crucial to facilitating larger lending amounts and longer terms for customers. However in the Bosnian case most of the SME lending could also have been provided without a guarantee by the partner bank or by other commercial banks in the country. The latter was the only non-additional intervention in the sample. In case of the microfinance intervention the additionality was greater for the set-up of the financial instrument and the development of the financial market than for the beneficiary level. The liquidity in the market – in particular for well-established microfinance institutes – seemed sufficient at the time.

Technical Assistance appeared to be most useful where it had a clear purpose and target group connected to the guarantee like in

the case of the microfinance intervention. The two portfolio guarantees were loosely aligned with existing Technical Assistance schemes co-financed by Sida. The evaluation could not observe any direct effects of this linkage, in one case the effects of this assistance were insignificant.

The evaluation was not in a position, nor was it meant to be, to go in detail on the impact of the interventions. Here only secondary information was gathered, which generally points to a positive impact on employment and supply of relevant services to the population in the beneficiary countries. This impact was mostly indirect. Expanding a telecom network to rural areas in Uganda supported economic development for micro-entrepreneurs and SMEs and contributed to employment. The same counts for the effects of the two portfolio guarantees on SMEs and SMEs in the health sector. The private health sector intervention in Uganda showed that many borrowers were small local clinics with a large number of customers that can be classified as poor.

Overall the evaluation found that the guarantees of Sida are useful instruments that positively contribute to private sector development. Guarantees in most cases serve viable enterprises or projects, and use resources in an efficient and catalyzing manner.

Interventions aimed at developing local financial markets and attracting and leveraging a different type of investors are important innovative attributions to financial sector development. In cases where financial intermediaries are not able to lend to clients because of the risks involved, guarantees have shown to be important instruments to bridge the risks and allow intermediaries to reach out to clients that could otherwise not be served. The guarantee instrument appears to be however less useful in times of recessions and in circumstances where financial intermediaries face large liquidity problems. It is a necessary but not a sufficient instrument to bring about private sector development.

RECOMMENDATIONS

The evaluation came to the following recommendations to improve the performance of Sida's use of guarantee instruments.

- Suitable financial intermediaries and counterparts should be selected as partners, which have the potential to reach out to the focus groups of Sida. These intermediaries should be able to

cover regions (rural, peripheral) where the target group is predominantly present.

- Selecting multiple banks for implementing portfolio guarantees will introduce competition on the use of the guarantee and will safeguard additionality and better use of the facility. By introducing incentives (guarantee ceilings, varying the cover percentage of the guarantee) banks will be encouraged to improve their performance.
- Incentives could be provided for reaching out to specific borrowers or clients. Introducing a flexible guarantee percentage for specific customers or borrowers could help to reach out to higher risk clients, for example 60-80% for start-ups or innovative entrepreneurs while 50% or less would suffice for established companies.
- The guarantees should serve as an additional security in cases where borrowers lack sufficient collateral or where the financial track record is not fully proven. With respect to the portfolio guarantees it is important to make sure that at the time of contracting the executing banks treat the guarantee as first class collateral and that regulators allow that approach.
- Technical Assistance for borrowers and financial intermediaries is a potentially powerful tool to assist borrowers in becoming bankable which would facilitate the reach out to poorer clients. However this assistance should be made available in a focused manner and be well aligned with the financial intermediaries implementing the facility.
- In principle banks and financial intermediaries prefer unconditional guarantees otherwise the use of the facility may be undermined. It is recommended to minimize conditions where possible.
- For innovative guarantees with the objective to develop (local) financial markets or reach out to new funding sources it is important to make sure that these new funding structures are also additional in terms of their effect on the final target group. The microfinance industry has developed into a mature market with a high liquidity and competitive local and international funding sources. Setting up a new microfinance fund for investors that are unfamiliar with these markets may be additional from the perspective of these investors, but does not contribute to additional funding in the market unless it serves microfinance institutes with

a high risk rating or provides financing instruments with a high risk character (e.g. equity or subordinated debt).

- A market oriented fee should be calculated for the guarantees. This fee may be subsidized, but it should be ensured that the subsidy is in the benefit of the ultimate beneficiaries, not the intermediaries implementing the facility. The subsidy should be made explicit, i.e. as the bridge between the market oriented fee and the fee affordable for the ultimate borrowers.
- For portfolio guarantees it is recommended that borrowers are made aware of the existence of the guarantee and are charged a transparent fee. In some countries this recommendation is not easy to implement as many people and institutions consider interventions of donors free money, which can cause problems of moral hazard. Even more a reason to change this image of donors and treat the private sector in a more market oriented manner.
- When continuing with the guarantee instrument, an adequate monitoring and risk management framework should be developed within Sida that provides timely information on the use and performance of guarantees. In case of the portfolio guarantees, Sida is at present dependent on the systems and management capacity of USAID. These systems are generally appropriate, but ownership by Sida for these interventions could be improved by a better assessment of the circumstances of the intervention at the start and during the course of the evaluation. In the event that Sida implements portfolio guarantees without USAID, the introduction of a monitoring system comparable to the one used by USAID is required. The cooperation between the strategy owner and the Unit for Loans and Guarantees should be strengthened and the local staff of Sida should be more involved in the follow-up.

Intervention paper MTN Corporate Bond Guarantee, Uganda

1 INTRODUCTION

The underlying intervention report presents the findings of the evaluation of the corporate bond guarantee provided by Sida to MTN Uganda. The evaluation is based on a thorough desk-analysis, stakeholder interviews and a field visit to Uganda, which was carried out by three evaluators Hans Slegtenhorst, Marie Heydenreich and Paulo Luswata from the side of Carnegie Consult, assisted by Anders Berlin as an observing team member from Sida.

The report is structured as follows:

- The following paragraph briefly introduces the guarantee facility for MTN Uganda (hereinafter referred to as MTN-U) which is the subject of this evaluation study (a more detailed description can be found in Annex 1 of this report).
- We will then highlight in paragraph 1.3 the approach to the intervention study and the sources of information used, as well as problems and limitations that we faced during the evaluation.
- Chapter 2 is dedicated to a brief context analysis of the financial and the telecom sector in Uganda, which helps to put the evaluation findings in their specific context.
- In chapter 3 we will present the findings grouped under the main OECD/DAC evaluation criteria: relevance, efficiency, additionality, effectiveness, impact, and sustainability.

1.1 Topic of the intervention report

The corporate bond guarantee for MTN-U was the first activity ever of Sida's newly created guarantee department.

Sida had first been approached in October 1998 and in February 1999 by Stanbic Bank Uganda on initiative of one of the main shareholders of MTN-U, Telia Overseas AB. This was at a time when Sida was in the middle of developing its guarantee pilot with no mandate or risk management framework yet in place. The agreement was finally signed as part of a next financing round of MTN-U in June 2001. MBEA brokers in Kampala were brought in to lead the transaction and work out the Prospectus.

The guarantee was supposed to cover the investment of local (institutional) investors into long-term local currency bonds of MTN-U, dedicated to the expansion of the telephone network to 24 identified rural communities.

MTN-U and its Security Agent Stanbic Bank initially aimed at issuing Floating Rate Promissory notes for at least 12.5 bill UGS in tranches via the local Broker MBEA.

MTN-U could draw guarantee letters with a minimum note guarantee amount of SEK 5m equivalent, and a maximum of 32 note guarantees. The maximum total guarantee amount was SEK 80m with the final date for Note Guarantee drawings set at 31 December 2005.

As one of the goals was to increase liquidity in the securities market, the guarantee agreement required listing on the stock exchange as a condition.

In view of the pioneering character and risk in the transaction, Sida extended a full debt guarantee, meaning that the guarantee covered 100% of the commercial risk¹ and investors only carried the risk of the coupon rate. Political risk, force majeure, fraud etc. were excluded. In addition, the obligations of Sida as a guarantor would cease if the UN, EU or Swedish Government effectuated a financial embargo against Uganda.

The floating rate coupon, not to be guaranteed, should be based on the prevailing 182 days T-bill rate, plus a 2% margin. Note holders would get bi-annual payments and have a right to redeem the capital, as per a Pricing Supplement.

Sida charged MTN-U a Note Guarantee Fee of 3% p.a., which was based on the EKN assessment. No arrangement or standby fee was charged. The National Debt Office created a reserve of SEK 40m to cover for potential losses.

In case of default by MTN-U, Stanbic as the security agent would claim payment from Sida and receive an amount in SEK, calculated at the UGS rate at the time of default. Sida had full regress against MTN-U as beneficiary, though without any pari-passu with other lenders, as was normal practice. In an amendment to the guarantee agreement in November 2002, the Sida security was subordinated to another subsequent loan of USD 20m.

¹ The prospectus specifies that "Sida provides a guarantee denominated in SEK. The guarantee amount will be reviewed every 6 months, so that the UGS equivalent of the guarantee amount exceeds the outstanding issued amount by 5%"

Table 1.

Imple- menting partner	Benefi- ciary	Value of guaran- tee	Years	Type of risks guaran- teed	Risk sharing	Pre- mium	Sponsor equity	Security	Agent
MTN Uganda	Stanbic bank on behalf of bond investors	SEK 80m in local currency (12.5 bill UGS)	8	100% Com- mercial	Yes, risk on coupon and political risk excluded	3% p.a.	50% of invest- ment	Regress on MTN (subordi- nated to other lenders)	Stan- bic

1.2 Approach to the intervention study

The intervention study for the MTN guarantee intervention was carried out through a mixed-method approach, including a preparatory desk-analysis of internal documents of Sida that were instrumental to the decision making process, available documents on the bond issuances as well as secondary literature on the telecom sector in Uganda. During a two-weeks field visit to Uganda we collected additional information from the following key informants:

- Sida
- NSSF
- Airtel
- Capital Markets Authority
- Uganda Security Exchange
- Central Bank.

A list of stakeholders interviewed can be found in Annex 2. The field visit was carried out by Hans Slegtenhorst, Marie Heydenreich and Paulo Luswata. Anders Berlin, head of the loans and guarantees department at Sida, joined the field mission to Uganda as an observing team member.

1.3 Problems and limitations

Unfortunately we were not able to get a meeting with the former CFO of MTN, nor could MTN put us in contact with local branches and agents in the areas where MTN was to expand to. We were therefore not able to assess any impact in terms of access to telecom services locally and we were bound to information provided by stakeholders not directly involved in the intervention. Furthermore, monitoring reports that MTN was contractually obliged to provide

to Sida could also not be retrieved. The lack of first-hand information of MTN was a great obstacle to this evaluation.

Apart from that, even though the intervention is a while ago, stakeholders interviewed were very well prepared and forthcoming, and could provide us with valuable insights especially concerning the relevance of the intervention for the development of the local capital market and as well as the impact on the same.

2 CONTEXT ANALYSIS

2.1 Uganda Telecom Sector

The Uganda telecom sector was until the early 90's the sole domain of the government owned Uganda Posts and Telecom Company UPTC, which provided postal services, telephone services in the form of land lines and the post bank. The licensing of the first mobile operator (celtel) opened the market but to a very limited scope as they viewed the service as an elite one and priced that market. However on the lifting of the moratorium to competition in the market a second provider (MTN) was licensed in 1998 and in order to break in the market their strategy was mainly to make the mobile phone available to as many Ugandans as possible. The strategy worked very well and they were able grow enough in less than 5 years to become the dominant player in the field in spite of Celtel's 5 year head start. The government owned UPTC was broken up to create a separate Uganda Postal Services, Post bank and Uganda Telecom Company which specialized in and competed favourable in the provision of telecom services. The industry was further opened out to more providers and a series of mergers saw several names enter and exit the Ugandan Market.

Currently the industry has 24 licensed providers but the Uganda Communication Commission which regulates the industry. However some of these are more active in the data provision rather than voice services which have 5 dominant active players .

2.2 Uganda Financial Sector

The Uganda financial sector is dominated by the banking sector which has existed for over a century. It consists of a central bank whose primary role is to maintain price stability and a sound financial system. It is in this latter role that it supervises the industry and manages monetary policy. Under its supervision are 25 commercial

banks or tier I institutions, that provide the full range of banking services, 4 Tier II credit institutions that do not participate in the clearing house, 4 tier III Micro deposit taking institutions that in addition do not deal in foreign exchange transactions and just over 200 forex bureaus and over 100 money remitters. Outside regulation are 3 development banks and a large but unconfirmed number of micro finance institutions that ideally are not allowed to take deposits, Savings And Credit Co-Operative (SACCO's) ideally regulated under the ministry of cooperatives and Village Savings and Loans Associations (VSLA's).

Outside the banking sector is the equity and bond market that only started in 1996 with the setup of the Capital Markets Authority (CMA) to regulate it. The Uganda Securities Exchange was licensed in 1997 and remains the only licensed trading floor. It currently has 16 companies trading on it of which exactly 50% are local and the rest cross listings from Kenya. It has also been used by a few institutions to raise money through bonds with Ugx 300bn having been raised since its inception. However activity has remained below expectation as cost efficiency start at Ugx 15bn, which is above most local company requirements yet due to high interest rates, multinational companies have preferred to raise funds cheaper in their parent markets. The government paper secondary market has also remained primarily over the counter as market players have remained few mainly dominated by the National Social Security Fund, which controls 90% of the pension funds industry.

More recently, mobile money, a funds transfer mechanism through the cell/mobile phone and owned and dominated by the large Mobile Network Operators (MNO) has become a major player in the financial services industry and currently boasts of 15 million accounts and annual transactional turnover in 2014 of Ugx 25 trillion. Though not yet as developed to its full potential (as in neighbouring Kenya) where interest paying deposits and loans can be offered, it has reach and convenience that will enable access to financial services in the rural areas as never before. The recent amendment to the law to allow for agency banking is expected to further deepen access to financial services in rural areas and bring them to the fold of modern banking services in an efficient and cost effective way.

3 FINDINGS OF THE INTERVENTION STUDY

3.1 Relevance

The corporate bond guarantee for MTN-U in 2001 was the first activity ever of Sida's newly created guarantee department. It was developed at a time when Sida did not yet have a clear mandate nor policies in place. Sida was approached by Stanbic on initiative of Telia, a Swedish shareholder of MTN-U.

The goals of the intervention were two-fold: (a) to promote a quicker expansion of the telecom network to 24 specified rural areas and (b) to promote financial sector development by issuing a new type of financial instrument in the local securities market.

The goals are coherent with the Swedish development objectives at the time, and the country strategy for Uganda for 2011-2005 which focusses on poverty reduction, social sectors and contribution to sustained high growth with development of the private sector. According to the government directives to Sida of March 1999, guarantees should only be provided on a risk-sharing basis and for projects with a 'Swedish interest', for example due to development co-operation, and/or Swedish commercial interests in the project. We did not find any evidence that Swedish interest play an important role in the guarantee's assessment and decision making, although two Swedish companies were involved in the project (Telia as a shareholder and Ericsson as a supplier).

In 1998 the telecom sector in Uganda was still in its infancy and risks were considered high. MTN had a very aggressive and innovative expansion approach, and its strategy to introduce a mass market of affordable telephony to both urban and rural areas was considered revolutionary at the time. The specific goal of the financing arrangement with the guarantee was a more rapid integration of 24 rural villages in the telecom system which would lead to high economic and social returns. While these areas eventually would be covered according to MTN-U's licence agreement, these areas 'on the margin of profitability, would be covered faster than otherwise would be the case'.

Other than its competitors MTN's business model was based on local currency earning, which is why it required preferably long-term local currency financing for the intended expansion. Long-term local currency financing was difficult to obtain at the time

however, as banks were little risk taking and providing short tenors, and the local securities and bond market were marginally active. Institutional investors in Uganda were mainly invested in real estate and government securities at the time, and MTN as the first ever corporate bond issue was seen as a welcome possibility to diversify the portfolio. The bond issuance should add liquidity to the securities market and enhance the willingness for local currency financing of institutional investors.

The two consortia leaders Telia and MTN South Africa had the relevant experience as well as the necessary technical and financial resources to support MTN-U in completing and operating the expanded network. Both in terms of access to telecommunication services as well as in terms of capital development, the intervention can be regarded highly relevant and innovative. The intervention was also in alignment with Ugandan national policy which was aimed at a liberalisation of the telecoms market at the time.

No TA was connected to the intervention, but shortly after the Sida guarantee was approved, Sida and GTZ jointly rolled out a technical assistance programme for financial market development in Uganda, the Financial Systems Development Programme, which included support to Uganda's Capital Market Authority, Uganda Security Exchange, bank supervision and a central bank functions for microfinance organisations. Unfortunately we could not retrieve any further information about this programme.

3.2 Efficiency

To understand the processes and timeline of the intervention one has to understand that the MTN guarantee was designed in a (pilot) period when the guarantee instrument had just been introduced to the operations of Sida. Studying the files of Sida we noticed that the first application for a guarantee to attract local financing by MTN was received in 1998, the same year when MTN was awarded the second national operating license. At that stage the Swedish Government had not yet formally approved the introduction of a guarantee instrument (the first Government directive on guarantees is dated November 1999). The lack of a risk policy and formal approval process was probably one of the main reasons why Sida's investment committee discussed the application however was not able to decide at this early stage. Finally in 1999/2000 when MTN Uganda requested Sida to participate in a second round financing due to the very rapid expansion of the network, Sida's investment

committee was able to respond more quickly. The process for assessing and approving the guarantee was very professional and because of the very innovative character of the instrument (first time issuance of corporate bond), Sida worked closely together with MTN and Stanbic Bank in developing the guarantee. Moreover at a number of occasions Sida requested third parties to provide an opinion on structure and risk. In April 1999 Ernst & Young Stockholm informed and advised Sida on the structure of the bond issue and the guarantee. On October 30, 2000 Sida was advised by PM Global Infrastructure, Washington on the financial risks and the soundness of MTN-U's financial position.

From file study and interviews it appears that Sida was pro-actively approached by one of the Swedish shareholders/sponsors of MTN-U, Telia Overseas AB together with Standard Bank (Stanbic). According to an analysis from Sida, MTN-U and Ernst & Young the success of the business model of MTN-U including the expansion to rural areas required additional resources. As the income of MTN-U was based on local currency earnings and to avoid any exchange rate risks MTN-U preferred to borrow in local currency as much as possible. Considering the expansion to new rural areas it was preferred to attract local currency financing with long tenors. Commercial local banks were not very interested because the MTN-U business model was innovative and not proven. Moreover banks were unable to offer tenors exceeding 3 years maximum at the time. Swedish and other foreign banks were not willing to take this sort of risk even when a cover from an Export Credit Agency could be provided. The bond instrument would allow MTN to attract funding from the capital market with a tenor of up to 8 years, while the initial expectation was around 3–5 years.

For the guarantee a risk premium of 3% had to be paid by MTN on an annual basis. The structure of the guarantee and the bond was set up in a reasonable and well balanced way:

- MTN financial position was considered very healthy (only 49% debt of total capitalisation). MTN managed to be profitable already in the second year of operations (2000) and the projections of rolling out the project were realistic and to some extent even conservative);
- The shareholders of MTN Uganda invested US\$ 32,5 m as sub-ordinated shareholders loans and provided a sufficient capital base with the right incentives;

- The guarantee was limited to the commercial risks of the operations
- Early redemption was included in the pricing supplement of each bond issue and in that respect even lowered the risk (in the event that happened);
- The arranging parties were very professional and Sida was well advised by independent professionals.

In hindsight one could conclude that the bond instrument was less efficient for MTN-U than considered beforehand. Although this has not been officially confirmed by MTN (because MTN was not available for an interview), this can be concluded from the fact that not all issuances took place and that the instrument as such has not been used at a later stage. Nevertheless at the time a bond issue was probably the single way to attract local financing at these conditions.

For both Sida, the Uganda financial sector and MTN the creation of the MTN bond originated more from a strategic and pioneering consideration (developing the local financial market) and less as a matter of balancing costs and benefits on short notice. In that respect the investment probably worked out better for Sida than for MTN.

From the file study we learned that the reputation of MTN-U as a genuine Ugandan instead of a foreign-owned company was an important reason for MTN-U to consider this instrument. Among the obstacles for listing the bonds at Uganda's Security Exchange were the cumbersome legal requirements for becoming a public company. MTN-U decided for that reason not apply for a listing of the bonds.

The guarantee has been a success in financial terms. No claims have been raised and Sida collected the agreed guarantee premium. As part of the risk premium EKN charged a fee which also included "admin" as a percentage of the premium (15%), which was transferred to Sida at a later point in time. IWe were not able to verify whether this fee was sufficient to cover all costs involved. Moreover it is difficult to determine whether the guarantee premium of 3% was actually sufficient to cover the risks. In first instance EKN recommended a 3,25% premium and after discussion the premium was finally set a 3%. Compared to EKN's calculation for insurance premiums for Ugandan transaction this is on the low side; however the regular EKB business is very different from the activities of Sida

in developing countries and covers political risk only and no commercial risk.

Table 2.

	Issuance 1	Issuance 2	Issuance 3	Total
Issuance amount	5MMM UGX/ 29,4MM SEK	2,5MMM UGX/ 15,4MM SEK	2MMM UGX/ 12,3MM SEK	9,5MMM UGX/ 57,1MM SEK
Premium	1,596,436 SEK	792,367 SEK	631,468 SEK	3,020,271 SEK

In terms of monitoring the guarantee agreement specified that MTN should provide to Sida:

- quarterly progress reports, covering the physical progress of the Project and the Project costs;
- audited annual reports for the Issuer not later than 90 days after the end of the fiscal year;
- copies of all special reports prepared for the Project; and
- any information reasonably requested by Sida relating to the Project or the Note Issue.

We have only been able to find very few communication on the monitoring of the MTN operations in the archives of Sida.

3.3 Effectiveness

The direct expected output of the guarantee was to crowd-in local institutional investors that were otherwise too risk-adverse to provide longer-tenor loans needed for the expansion to rural villages which in turn should reduce the exchange risk for the MTN Uganda operations. MTN-U and its Security Agent Stanbic Bank initially aimed at issuing Floating Rate Promissory notes for at least UGX 12.5b in tranches via the local Broker MBEA. The project also foresaw a listing of the bonds on the Uganda stock exchange (USE). A pricing supplement would define interest rate and conditions for each issuance of notes. MTN-U could draw guarantee letters with a minimum note guarantee amount of SEK 5m equivalent, and a maximum of 32 note guarantees. The maximum total guarantee amount was SEK 80m over 5 years. Stanbic expected the first tranche to have a tenor of up to 3 years, while the aim was to achieve longer following tenors.

In the end, 3 issues of local currency promissory notes took place in private placements for in total UGX 9.5b and a tenor of 4 years each. The price was the 182 day bill rate + 1.75%. Investors included

pension funds, commercial banks and development banks. All bonds including coupon were repaid on maturity date.

While output level effects were achieved overall, many of the outcome level effects did not materialize however. Although stated as a condition in the guarantee agreement, no listing of the bonds took place. Relatively late in the process (after the first tranche of notes was released) it became apparent that MTN-U was required to become a public company if the notes were to be listed on the stock exchange. Due to the high formal requirements and the prohibitively high costs involved MTN-U did not proceed with the listing, therefore the aim of increasing liquidity of the securities market did not effectuate. Also, to our knowledge MTN did not make use of the bond instrument with or without a guarantee after the intervention to attract financing. On the side of investors, appetite for other types of investments has remained, however there is little offer on the securities and bond market due to various reasons including the small size of companies in relation to the high costs of meeting the transparency requirements as well as a general fear of public scrutiny.

On the project side, MTN successfully expanded mobile telephone network to designated 24 towns and villages. Although the project resulted more costly than planned due to cumbersome procedures to comply with the capital market authority, it was commercially successful and MTN-U's performance improved consistently afterwards. MTN-U expansion happened much faster than in the licence agreement or in MTN's original plan, and it established and maintained a lead position on the mobile phone market in Uganda. This is accompanied with an equally good financial performance of the company. MTN-U's turnover in 2003 was already about USD 15m and net profit stood at USD 30m; in 2015 this was USD 340m and USD 69m respectively.

3.4 Additionality

Additionality can be assessed on two levels for the MTN guarantee intervention, (a) on the level of capital market development and (b) on the level of expansion of the telecom network to rural areas.

For the evaluation team it was difficult to answer the questions whether MTN could have raised alternative funds needed to expand to the designated rural areas without the guarantee.

MTN's need for long-term local currency can be explained by its interest to avoid a large currency mismatch and resulting currency

risk in the face of its dependence on local currency earning on the one hand, and by the long-term nature of the investment (to rural areas) on the other hand.

Stakeholder interviews and file analysis confirm the view that local or foreign banks were not able to provide loans in local currency with long tenors at the time.

The attempt to crowd in local institutional investors through a bond issuance was pioneering and innovative and had not been tried before in Uganda. Sida's credit enhancement was absolutely necessary for the bond issuance to go through in terms of formal requirements and in that respect the evaluation team has no doubt that the introduction of the MTN bond would not have happened without the guarantee of Sida.. To conclude, high additionality can be attributed to the intervention in terms of strengthening the capital market by facilitating the first corporate bond issue in Uganda.

This was acknowledged by investors, banks and supervisors. They all appreciated the initiative and the learning part of it. Although the number of later bond issues is not impressive the experience with the MTN deal was very useful according to several stakeholders and provided practical guidance for similar capital market operations.

On the level of expansion of the telephone network to rural areas the additionality is less obvious. The designated areas were part of the licence requirements and therefore MTN was formally required to cover these areas in any case. The additionality of the guarantee was justified by its capacity to accelerate the process, as in absence of the financing package including guarantee probably the more profitable urban areas would have been given priority.

It can therefore be concluded that without the guarantee the expansion would have happened at a later stage or at less attractive conditions (in forex with shorter tenors).

3.5 Impact

According to the reconstructed theory of change, expected long-term impact included sustained and better access of rural communities to mobile telephone network and higher competition in the telecom market on the one side, and increased liquidity in the long-term local currency (bond) market on the other side.

Since 2000 when the guarantee agreement was signed, the telecom market in Uganda has seen an unexpected and rapid

development. MTN played an instrumental role in this process as it was the first company to venture to rural areas on a large scale and made low-cost telephony the core of its expansion strategy. This development was paired with an introduction of new technologies in the area of mobile telephony, strong competition and a dramatic reduction of costs, which made telecommunication services accessible to many poor people in Uganda. According to research studies of the telecom market² the increase has had large economic effects for Uganda, with high direct and indirect employment created in the telecoms market.

In how far the guarantee contributed to these effects is difficult to determine as it represented only a small part in the total financing of MTN.

In terms of capital market development the anticipated long-term impact has been limited. While the intervention brought certain learning effects for later bond issuances, the securities and bond markets are still not liquid, and there is little interest or capacity for local companies to use to bond instrument to serve long-term local currency financing needs. After the MTN bond, 9 more bond issuances followed, however only two were corporate bonds (UTL and Kakira). This is mainly due to administrative requirements and high costs in relation to the relatively small size of companies in Uganda, but also due to a fear of public scrutiny when own accounts need to be published. MTN is still among the two only corporates to date to go through the cumbersome procedure. The authorities however still remember and appreciate Sida's credit enhancements efforts and use them as an example for other companies.

3.6 Sustainability

Sustainability of the intervention can be defined on the level of MTN's (financial and operational) performance; MTN's and other corporates' possibility to raise local currency debt from the local capital market; as well as rural access to telecommunication services in Uganda in the long-term.

Due to a lack of access to recent annual accounts of MTN Uganda and the lacking input of the management of MTN it is difficult to make a quantitative assessment of the sustainability of the operations of MTN, and its capacity to raise local currency financing (with or without guarantee) in the long term. It is public

² Khymouhendo (2010), *The mobile payphone business: a vehicle for rural women's empowerment in Uganda*. In: Africa and ICT development. IDRC.

knowledge however that MTN managed to expand its business in a very rapid manner and became the leading telecom operator in Uganda (see impact section).

In particular in the early years of the operations the investments of MTN probably exceeded the operational income. At a later stage the local currency income was growing more rapidly which was confirmed by the projections we found in the files of Sida. However for MTN there was no reason to continue with this instrument for the reasons described above.

For the development of the bond and securities market in Uganda the sustainability of the MTN deal has been limited although a certain leaning effect definitely took place. Only a few later bond issues occurred of which only one was issued by a corporate. According to the Capital Market Authorities and the Uganda Securities Exchange this was mainly due to the limited size of companies in Uganda as well as the high administrative and costly requirements.

For poor people living in rural areas the impact of the expansion of MTN was highly sustainable, as coverage and quality of telecommunication increased and costs reduced consistently over the following years.

As mentioned in the paragraph on efficiency the guarantee can be considered cost effective as no claims were raised and the operations of MTN were successful and meeting the projections. The team did not assess any information on the internal expenditure of Sida of assessing and managing the guarantee however.

4 MAIN CONCLUSIONS, LESSONS LEARNED AND RECOMMENDATIONS

4.1 Conclusions

The main conclusions with respect to the MTN-U intervention are:

- The assessment of Sida for providing the guarantee has been executed in a thorough manner. Sida was advised by professionals on the financial capacity of MTN, the feasibility of the project and projections as well as on the status of the financial market;
- The purpose of MTN-U to roll out telecommunication operations all over the country at affordable prices fitted both with the policy of the Ugandan Government (liberalization of the telecom market) as well as the policy of Sida to strengthen the financial market and reaching out to poor rural areas;

- In terms of effectiveness the intervention shows mixed results. It resulted in a somewhat faster expansion of the rural network (in 24 areas) and a contribution to developing the financial market in Uganda by the first corporate bond issue in Uganda. However the intervention did not lead to a public offering as intended nor a follow up of other bond issues by MTN or other local corporates;
- The intervention was additional by allowing MTN to attract local financing and avoid large currency risks. Local banks were not able and willing to provide this sort of finance at similar conditions.
- The risk of market distortion was very limited as competitors used a different business model based on foreign currency income and therefore the intervention with MTN-U can be considered unique at the time of the intervention.
- The efficiency of the intervention can be considered high although the process for approval was a bit lengthy. The guarantee allowed MTN-U to attract local funding at reasonable conditions and the financing package turned out to be successful as no claims were submitted. With regard to the approval process one has to take into account that the bond instrument was quite innovative in the Ugandan context and that at the time Sida was still in a pilot phase with respect to the guarantee instrument.
- The intervention contributed to the successful expansion of the MTN-U business model both in urban as well as in rural areas. Presently MTN-U is the leading telecom provider in Uganda.

4.2 Lessons learned

The intervention had two objectives: 1. Developing the local capital market and 2. Making telecom services available for rural (poor) regions at affordable rates.

The second objective has been accomplished by MTN-U as the guarantee of Sida contributed to a faster roll out in 24 rural areas in Uganda. Although one could argue that the objectives would have accomplished also without the guarantee, it is very likely that the guarantee contributed to the decision of MTN-U to expand their services much faster to rural areas.

With respect to the development of the financial market the intervention was less successful as the public offering of the MTN-U bonds did not materialize, new bond issues of corporate and MTN-U did not happen and the question arises whether the

Ugandan market was ready for this sort of instrument. Although we feel that developing the local capital market is very important from a development perspective, the intervention failed mainly because the local environment was not well studied. In retrospect it appeared that there were no sizable corporates in the Uganda market that were able to make use of this instrument. The number of companies listed at the stock exchange and the absence of larger corporates were indications that developing a bond market in Uganda at the time was very optimistic.

4.3 Recommendations

It is important that when considering developing local capital markets all aspects are well considered not only related to a specific deal, but also in a broader perspective. It is perhaps easy to state ex-post, when evaluating the intervention, that the assessment did not include all aspects that should have been considered. Perhaps a closer cooperation with development banks (DFIs) could help in assessing the market and to make a judgment about whether the introduction of innovative instruments is realistic in its context. On the other hand we know that the success of the introduction of new instruments in developing countries is difficult to predict. As long as the financial risks are well assessed and weighted (as was the case with MTN-U) it is worthwhile to consider this sort of instruments. In general we feel that it is important that developing countries become less dependent on international financing sources in particular when the income of projects is in local currency.

ANNEX 1: DESIGN AND SET-UP OF GUARANTEE & THEORY OF CHANGE

Process of design and Sida's appraisal

1997: In the on-going privatization of the telecom sector in Uganda, an international consortium dominated by the South African telecom company MTN International and Telia Overseas won, through competitive bidding, the second national operating licence in 1997, for the period 1998–2018. MTN Uganda was established as a company by the consortium for building and operating the network.

1998/1999: The same year MTN Uganda initiated an investment programme for rolling out the country's second cellular phone network. Telia Overseas (a Swedish company) contracted Standard Bank Uganda (Stanbic) on behalf of MTN Uganda to arrange the financing, and to raise as much local currency as possible to match the cash-flow characteristics of MTN Uganda. At the time, the local market could not offer adequate long-term financing, therefore Stanbic looked for other options and organised a road show to potential lenders including Sida and Swedfund in Sweden in October 1998.

Stanbic, who was familiar with Sida from other projects, together with Sida and Telia/MTN Uganda developed the idea of issuing debt on the local capital market, which was up to then very poorly developed. A project of this nature was discussed in Sida's Investment Committee in October 1998 and in February 1999, at a time when Sida was in the middle of developing its guarantee pilot with no mandate or risk management framework yet in place. As Sida was unable to make a rapid decision due to the lacking policy framework, MTN Uganda went ahead with the investment without Sida participation. A USD 60m investment programme was financed through a combination of equity (50%), loans, guarantees and quasi-equity loans. The non-equity part was provided by a group of DFIs, including EIB, FMO, DEG, Swedfund and NDF.

1999/ 2000: By 2000, 113,000 of the targeted 193,000 lines were already running. Due to the good performance and good market prospects, MTN Uganda decided in year 2000 on a more ambitious and faster expansion than planned in the licence agreement, requiring an additional investment of USD 50m. For this purpose MTN

Uganda/ Stanbic approached Sida a second time for a local finance guarantee, this time successfully. As Sida's involvement was conditional to creating development impact, the intervention was earmarked to a specific expansion to 24 identified rural communities. MBEA brokers in Kampala were brought in to lead the transaction and work out the Prospectus.

Sida's decision making process

Stanbic Bank Uganda initiated early contacts with Sida and together they developed the idea of the local bond guarantee. In view of the pioneering character and risk in the transaction, Sida was prepared to extend a full debt guarantee within the equivalent of SEK 80m, with investors only carrying the risk of the coupon rate. Political risk was also excluded from the guarantee.

Sida's initial thought on pricing had been a standard 1 % (reflecting that guarantees still did not have full systems or policies in place). They also hoped that some retail investors could take part in a bond issue (introducing new savings forms), but this proved unrealistic at the time.

As policies were in place, EKN came in to assess a risk-based premium. EKN first came up with a rather high fee calculation, until they realized that the envisaged local currency denomination of the issue would significantly lessen the overall risk. In the end, EKN recommended a premium of 325 ± 25 basis points and Sida chose the lower end at 3%.

In December 2000, Sida approved a guarantee of SEK 80m over an eight-year period through Stanbic Bank Uganda for a "floating rate promissory note programme" to raise capital to MTN Uganda on the local market.

Relatively late in the approval process it became apparent that only public companies with three years of operation can issue debt on the local capital market. Under the condition that MTN Uganda would transform into a public company, Sida agreed to offer the first three issuances via private placements. The Uganda Capital Market Authority made an exception to the rule of operation based on the strong support of Sida. Both incidents delayed the approval process.

In June 2001, the guarantee agreement was signed.

Set-up of guarantee intervention

MTN-U and its Security Agent Stanbic Bank initially aimed at issuing Floating Rate Promissory notes for at least 12.5 bill UGS in

tranches via the local Broker MBEA. The guarantee agreement required listing on the stock exchange as a condition.

A pricing supplement would define interest rate and conditions for each emission tranche of notes.

MTN-U could draw guarantee letters with a minimum note guarantee amount of SEK 5m equivalent, and a maximum of 32 note guarantees. The maximum total guarantee amount was SEK 80m over 5 years.

Stanbic expected the first tranche to have a tenor of up to 3 years, while the aim was to achieve longer following tenors.

The guarantee covered 100% of the commercial risk. Political risk, force majeure, fraud etc. were excluded. In addition, the obligations of Sida as a guarantor would cease if the UN, EU or Swedish Government effectuated a financial embargo against Uganda.

The floating rate coupon, not to be guaranteed, was based on the prevailing 182 days T-bill rate, plus a 2% margin. Note holders would get bi annual payments and have a right to redeem the capital, as per a Pricing Supplement. The Security Agent would buy back notes at face value when the Note was due for payment, while optional premature repayment would be discounted (e.g. at 90%).

Sida charged MTN-U a Note Guarantee Fee of 3% p.a., which was based on the EKN assessment. No arrangement or standby fee was charged. The National Debt Office created a reserve of SEK 40m to cover for potential losses.

Claim process

In case of default by MTN-U, Stanbic as the security agent would claim payment from Sida and receive an amount in SEK, calculated at the UGS rate at the time of default.

Sida had full regress against MTN-U as beneficiary, though without any pari-passu with other lenders, as was normal practice. Opening negotiations with the senior lenders on pari passu would have required re-opening of the existing Inter creditor Agreement, which MTN-U were unwilling to require, and that would hardly have been acceptable to the senior lenders.

In an amendment to the guarantee agreement in November 2002, the Sida security was subordinated to another subsequent loan of USD 20m.

To our understanding Sida did not have formal processes for handling claims in place at the time, and had discussions with the

Ugandan Central Bank on how to react in the case of a total default (the UGS – USD market was not liquid at the time).

Reporting/ Monitoring

The guarantee agreement determined that MTN should provide Sida with quarterly progress reports, covering the physical progress of the project and the project cost and audited annual reports. Furthermore, as Sida's agent, Stabic was responsible to provide Sida with relevant documentation and reports.

At this point in time, we do not have further information on the quality and frequency of monitoring.

Theory of Change

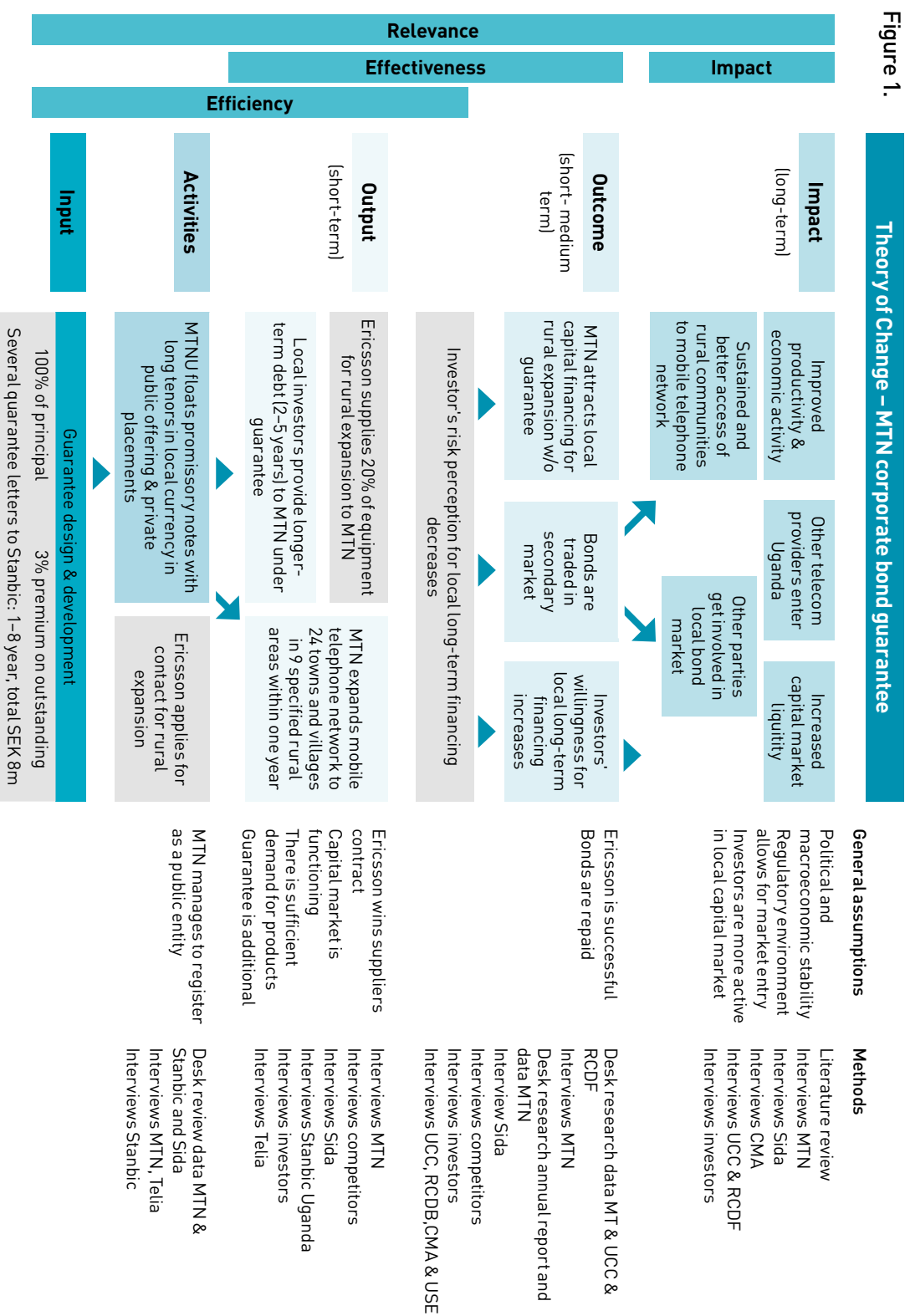
There were some discussions within Sida on which strategy to fit the intervention, as they had both a strategy for the telecom sector as well as on-going programmes for the promotion of the local financial market.

The goals of the Sida intervention were two-fold: (a) to promote a quicker expansion of the telecom network to 24 specified rural areas and (b) to promote financial sector development by issuing a new type of financial instrument in the local secondary market. The direct expected output of the guarantee was to crowd-in local institutional investors that were otherwise too risk-adverse to provide longer-tenor loans needed for the expansion to rural villages and as a result reduce the exchange risk for the MTN Uganda operations.

We did not find any evidence that Swedish interest play an important role in the guarantee's goals and objectives, although two Swedish companies were involved in the project.

The below theory of change is reconstructed on the basis of available policy documents, the 2006 evaluation and discussions with stakeholders at Sida and Stanbic involved at the time.

Figure 1.



Intervention Paper SME Portfolio Guarantee Raiffeisen, Bosnia Herzegovina

1 INTRODUCTION

1.1 Topic of the intervention report

The underlying intervention report contains the findings of the evaluation of the guarantee facility provided jointly by USAID and Sida to the Raiffeisen Bank DD Bosnia-Herzegovina. For the sake of this part of the overall evaluation of Sida's use of guarantees, a team of evaluators consisting of Rien Strootman, Nino Serdarevic and Mart Nugteren visited Bosnia-Herzegovina from 14 till 24 March 2016. The team was accompanied at different periods by Ms Camilla Rubensson and Ms Sofia Ericsson from Sida.

Annex 1 contains a more detailed description of the guarantee facility, so here we will limit ourselves to a brief introduction to the topic. The guarantee facility with Raiffeisen was part of the realisation of interventions foreseen in the Memorandum of Understanding between Sida and USAID of 26 March 2010. The guarantee agreement was signed between the bank, Sida and USAID on 28 September 2010. Sida and USAID would guarantee each 25% of qualifying loans. Maximum cumulative value of disbursements of all qualifying loans was USD 20 million. Maximum value of principals of all outstanding qualifying loans at any one moment is USD 10 million. Maximum maturity of the loans is seven years.

The maximum amount of a qualifying loan is USD 1,500,000. Qualifying borrowers are non-sovereign Bosnia-Herzegovina-registered small and medium-sized enterprises (SMEs), associations, or cooperatives operating in productive or manufacturing sectors. Raiffeisen is supposed to try to target, but is not limited to borrowers active in the agriculture, tourism, wood processing, or metal working sectors (priority sectors). Finally, Raiffeisen is expected to use its best efforts to cooperate with the Technical Assistance (TA) programmes FARMA and FIRMA and to consider proposals recommended for financing by these projects. These proposals are however not binding for Raiffeisen in any way.

The period of the Guarantee Arrangements is from 29 September 2010 till 30 September 2020, whereas the final date for

placing qualifying loans was planned for 30 September 2015. Raiffeisen paid an origination fee (USD 37,500) to Sida as well as an utilisation fee (0.5% per annum on outstanding principal). USAID acted as agent on behalf of Sida under the agreement.

1.2 Approach to the intervention study

Prior to the visit, through telephone interviews and visits in Stockholm, stakeholders from USAID (in Washington and Sarajevo) and Sida were interviewed. Documents obtained from Sida pertaining to the facility had been scrutinised. During the field visit representatives of the Swedish Embassy, USAID, Raiffeisen and borrowers of Raiffeisen were interviewed.

A total of nine Raiffeisen clients throughout the country were visited. Companies visited represented nine out of 23 companies lent to under the guarantee facility, and ten of the 25 loans. All of these clients had obtained a loan covered by the guarantee (one client even two loans) and had not yet repaid this loan fully. These clients were located in different entities (the Federation of Bosnia and Herzegovina and the Srpska Republika, as well as the autonomous district Brcko) and active in different sectors (three of the four priority sectors i.e. agro or food-processing, metal and wood processing, but also textiles, plastics and furniture production).

During the interviews the evaluators used a questionnaire which was directly derived from the evaluation matrix attached here as Annex 3.

For a broader perspective, in the writing of this report the authors benefitted from the USAID Credit Management System (CMS) database, data from the Banking Agency of Bosnia and Herzegovina and the Bosnia-Herzegovina Agency for Statistics. CMS data helped to prepare and structure the interviews, but also to obtain an oversight of the entire guaranteed portfolio. Data obtained from the interviews and from the CMS system were compared with national statistics, e.g. industry averages, to see whether the guaranteed loans resulted in impact or were additional.

In addition, to get a better understanding of the context in which the lending operations occur, interviews were conducted with representatives of the Central Bank, the Banking Agency of the Federation of Bosnia and Herzegovina (the regulatory authority for the Federation) and of the programme FARMA.

The field visit concluded with debriefing and verification meetings with Raiffeisen, Sida and USAID representatives.

1.3 Problems and limitations

In the Inception Report, some possible hurdles were identified. We repeat here those relevant for this intervention study, and the extent to which they actually materialised:

- Lack of willingness of banks to share confidential information on their borrowers – this turned out to be partly valid, the bank e.g. was not willing to introduce us to clients who had repaid the loan. Initial hesitance of Raiffeisen to cooperate and a late reaction of loan officers also resulted in a lower number of companies visited than ideally possible. Only partly was this mitigated by the access to five YouTube films containing interviews with clients, recently shot by USAID.
- Clients or declined clients are not willing to cooperate – this turned out to be not the case for clients, however turned down clients could not be sourced.
- Quantitative approach of assessing additionality might be hard to implement as the financial intermediaries have different reporting and rating standards – partly the case, Raiffeisen uses Basel I and was not willing to provide us with credit rating data on the individual clients.
- Challenges to retrieve baseline data on SME portfolio of Raiffeisen –this was not the case, thanks to our access to CMS.
- Impact assessment limited – this was partly the case, although employment data and some gender data could be retrieved.

In addition to the above, some other hurdles were met:

- No clients prior to 2013 were visited (on request of Raiffeisen – these had repaid the loan) – it is possible that Raiffeisen changed mid-way its approach to using the guarantee but if that is the case than the field visit cannot shed a light on this.
- Likewise, most of the loans in the portfolio had been provided in 2013 or later. This made comparison with national benchmarking data cumbersome or impossible, as national statistics were only available till 2014.
- Evaluators could not mention the guarantee to the clients visited, which resulted in somewhat indirect discussions on the topic of the evaluation, especially since most clients had (had) more Raiffeisen loans.³

³ It was noted that one of the entrepreneurs appearing in the USAID YouTube films was aware of the guarantee.

- Evaluators were accompanied by Raiffeisen loan officers (or in one case the Director of the Branch Office) – in retrospect though we feel that this has not biased the responses.

2 THE CONTEXT ANALYSIS

2.1 General Economic Situation

The war in the nineties left Bosnia-Herzegovina with a devastated economical basis and infrastructure. The effects of this last till present. The first years of this century showed improvement and a relatively high economic growth, at least till 2008. The economy remained highly dependent however on a limited number of activities, such as metal exporting (a heritage of the socialist past as part of Yugoslavia), but also wood and furniture exports. Remittances and foreign aid remain important. After 2008/9, mainly as a result of the economic crisis, growth declined. Unemployment, with rates ranging over 40%, remains a major concern. In 2010 Eurostat data recorded GDP p/cap. as being 29% of the EU average.

The konvertibilna marka (convertible mark or BAM), introduced in 1998, remains pegged to the Euro (BAM = 0.51129 EUR), which has been overall beneficial for confidence in the currency and the banking sector.

Nominal gross domestic product (GDP) in 2014 in Bosnia-Herzegovina amounted to BAM 26.93 billion and grew with 2.48% compared to 2013. With the assumed GDP deflator of 5.2% for 2014, real GDP was estimated to be BAM 25.60 billion (+0.7% compared to the previous year). The industrial output is almost unchanged compared to 2013, a growth of only 0.18% was recorded. In December, the decline of industrial production amounted to 1.36%.

2.2 Finance and the SME sector

The banking sector is dominated by foreign banks, especially from Austria and Italy. About 80% of Bosnian banks are foreign-owned.

Total investment of private enterprises into fixed assets for the period 2010 – 2014 increased at an average annual rate of 3.4%, whereas it is worth noting that private enterprises financed their investments predominantly with equity (53% share in 2014).

Table 3: Private sector investments in '000 EURO by source of financing

Private sector investments in '000 EURO by source of financing	2010	2011	2012	2013	2014	2014 share
Equity	1,270,963	1,251,607	1,263,512	1,384,506	1,355,660	53%
Debt	548,728	581,821	649,265	680,612	849,160	33%
Leasing	66,346	74,981	69,825	59,468	53,017	2%
Other	276,372	273,143	294,989	227,163	276,491	11%
Total	2,164,421	2,183,563	2,279,604	2,353,763	2,536,343	100%

Source: BH Agency for statistics. Investments in 2014

Provision of credits to the private sector for the period 2010 – 2015 were steadily increasing between 2% and 4% on an annual basis, reaching EURO 2.7 billion in 2015.

Table 4: Debt issued to the private sector

	2010	2011	2012	2013	2014	2015
Amount in '000 EUR	2,462,088	2,551,242	2,628,735	2,659,878	2,666,933	2,724,465
% in total placements	48.2	47.6	48.2	47.9	46.7	45.9

Source: Adjusted from Banking agency FBIH reports 2011 – 2015.)

As a percentage of overall usage of funds by banks the relative importance of debt declined however. Investments in government bonds are a safer, yet sufficiently rewarding, alternative than relatively risky private sector lending.

As a result of the economic crisis, after 2008/9 the share of non-performing loans (NPL)⁴ significantly increased. The NPL ratio

⁴ Pursuant to the Decision on minimum standards in managing risks and banks assets classification (FBIH Official gazette, no. 33/12) NPL expresses total disbursements classified in Category C (Sub-standard assets), Category D (Doubtful assets) and Category E (Loss). In accordance with the Article 14 a bank is obliged to classify as NPL those placements that do not generate revenue, in concrete: a) principal amount and/or interest due for payment for 90 days and longer as in initial contract; or b) capitalized interests which the borrower failed to pay for longer then 90 days from initially contracted maturity.

differs among different industries, whereby agriculture and construction industries can be considered most risky for lending. Nevertheless, figures for 2015 show a certain improvement, especially when compared to 2012 or 2013.

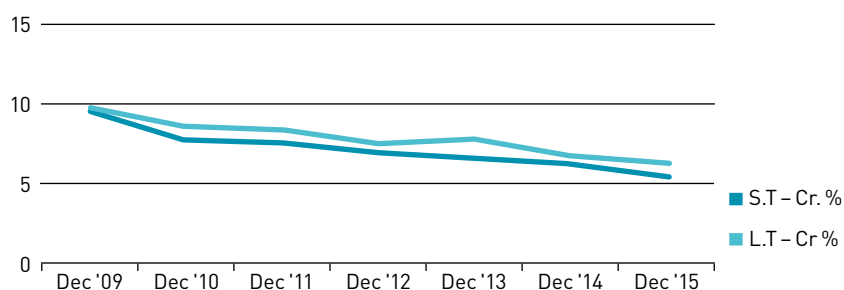
Table 5: NPL by industry in %

	2012	2013	2014	2015
Agriculture	28.6	27.9	19.6	17.0
Industry	15.9	20.0	23.6	21.2
Construction	26.1	29.8	29.1	26.7
Trade	13.3	16.0	15.4	13.2
Tourism	14.1	18.8	15.8	12.7
Other	15.0	15.2	13.2	14.2

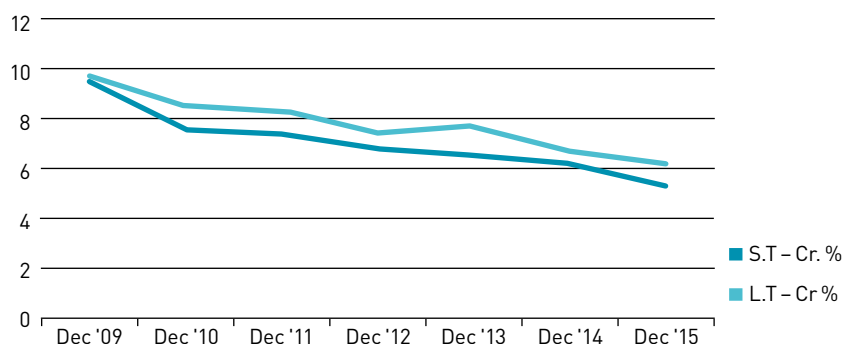
Source: Adjusted from Banking agency FBiH reports 2011–2015

The effective interest rates for credits to private sector declined by almost half over the past six years, as is shown in the next graph. There is competition between banks now in SME lending, and potential clients who are considered a safe risk have a choice in the selection of a bank.

Figure 2: Effective interest rates in period 2009–2015



Source: Adjusted from Banking agency FBiH. Information on banking sector in FBiH in 2015

Figure 3: Effective interest rates in period 2009–2015

Source: Adjusted from Banking agency FBiH. Information on banking sector in FBiH in 2015

3 FINDINGS OF THE INTERVENTION STUDY

In this chapter we will present the findings, grouped along the main OECD/DAC evaluation criteria: efficiency, effectiveness, sustainability, impact, additionality and relevance. An evaluation matrix and a Theory-of-Change for the Raiffeisen guarantee facility are attached to this report. We will revisit the questions in the matrix, when presenting the findings, and in doing so verify the validity of the Theory-of-Change and its assumptions.

3.1 Relevance

The guarantee scheme should contribute both to private sector and financial sector development. The guarantees are expected to result in increased finance to markets (financial additionality) and thereby socio-economic benefits (economic additionality). Leverage of additional funding from private sources is an important objective in that respect.

As described in the context analysis in the previous chapter, in 2010 when the guarantee agreement was signed, Bosnia-Herzegovina was facing declining growth of the private sector, a deteriorating NPL ratio and other risk factors for lending to the private, especially SME sector. Alternatives were available to the banking sector, such as high-interest yielding government bonds.

At the same time, since the banking sector was dominated by foreign banks, access to funding for the financial sector was less of a problem (i.e. not significantly less than elsewhere in the world at that stage).

The choice for a guarantee instrument to facilitate and induce banks to lending to a priority sector seemed logical and relevant.

Alternatives such as a credit line would have been less additional and efficient, and the guarantee instrument would be very instrumental in obtaining leverage. Furthermore, the guarantee instrument ensures that the credits are used to finance SMEs whereas direct funding could be used ('fungibility') to purchase government bonds.

Objectives for USAID and Sida largely coincide here, whereas USAID's motivation was mainly for employment and female involvement in management and entrepreneurship, Sida more generally in poverty abatement and women as owners and/or managers. This makes the selection of USAID as partner in Sida's guarantee activities both logical and relevant.

The selection of the Raiffeisen bank as intermediary was based on the argumentation that this was at the time the largest bank in Bosnia-Herzegovina, had a wide coverage (also encompassing Republika Srpska and Brcko) and a solid reputation. Directing such a bank to SME lending would have had a great impact and from that angle the selection seems relevant. However, although the bank had some SME lending in its portfolio, this was clearly not its preferred activity. The origination fee of USD 37,500 is small for a bank the size of Raiffeisen and cannot be expected to buy commitment. There were some managerial changes in the bank after the signing of the agreement, so it is now with retrospect difficult to say whether USAID and Sida had paid sufficient attention to strategy and governance, i.e. whether the power to change the bank's strategy in the favour of SME lending was indeed with those with whom negotiations took place on the guarantee. It is a fact though that headquarters of the bank in Vienna did not allow for a relaxing of collateral requirements when the guarantee applied. The strong impression is that insufficient attention has been paid to the conservative nature of the bank. USAID which has guarantee agreements signed with more banks in Bosnia-Herzegovina mentioned that Raiffeisen was the only bank not willing to accept the guarantee as first-class collateral.

The guarantee was not restricted to the four priority sectors (agriculture, tourism, wood processing, or metal working) but the bank was invited to pay special attention to these sectors.

In retrospect, this evaluation doubts the relevance of this prioritisation: although these sectors have potential in the country, the objectives of Sida would have been served by lending to every productive sector, and limiting the group of potential borrowers runs the risk of limiting also the outreach. Given the structure of the economy, this focus would do little for diversification of the economy. In addition, wood processing is a very popular activity in the country, and although harvesting is government controlled there is an environmental risk. The same can be said about the wish to involve the Technical Assistance programmes FARMA and FIRMA. The bank was instructed to pay attention to, but was not forced to accept nor was it limited to, suggestions for lending from these two programmes. Such an instruction carries a certain risk since TA-providers are not always best equipped to assess credit worthiness of a client, an assessment which should remain the responsibility of the bank. However: both when it comes to FARMA, FIRMA and the priority sectors the clauses in the agreement were very carefully worded. The bank lent out to different other sectors and the involvement of FARMA and FIRMA was very limited.

Concluding, at the time of the agreement, the selection of a guarantee instrument to boost SME lending in Bosnia-Herzegovina appears to be relevant, the selection of Raiffeisen as intermediary less so.

Over the years, the relevance of a guarantee instrument of this nature may have declined. Especially for SMEs with a good credit history or existing relations with a bank obtaining an investment loan is not over-problematic, in fact (see also the context analysis) banks compete for such clients. Interest rates have steadily declined. Spokesmen of the regulatory authorities told the evaluators that credit lines would be a preferred alternative to guarantees, seen the funding limitations of the banking sector. This however seems to be especially valid for the relatively few indigenous Bosnian banks, which have a more difficult and more expensive access to funding.

3.2 Efficiency

In the Theory-of-Change the steps required to arrive from inputs, through activities, at outputs, can be grouped in ‘design and development of the guarantee instrument’ => ‘identifying and assessing compliant clients’ => ‘increased lending to productive clients at market rates.’ In the design of the guarantee instrument account is supposed to be taken of the regulatory environment.

When looking at the assumptions made to make this happen, it appears that a number of the critical conditions have not been met, such as demand for long-term finance and presence of bankable projects and good business plans.

A given demand for long-term credit was assumed. Given the fact that potential clients did not know about the existence of the guarantee, and that the guarantee did not really influence the terms of the loans, utilisation of the instrument presupposes a certain exogenous demand, driven by clients' expectations on turnover and profit (i.e. the simple existence of a guarantee does not push its use). It is difficult for this evaluation to go back to the situation in 2010/11, since no clients who had borrowed under the scheme prior to 2013 could be interviewed. With reference to the context analysis, it seems fully possible that the macro-economic situation did not favour the emergence of bankable projects and that this limited the use of the instrument. In 2011 and 2012 only four loans were issued, guaranteed under this facility, till September 2013 (three years after the start of the facility) in total nine loans were placed.

The bank mentioned the lack of good and convincing Business Plans as another reason for the low disbursement till end 2013.⁵ Technical Assistance through FARMA did not make a large difference here – this programme reached out to only two clients. The bank was not familiar with FIRMA, nor was any of the companies visited.⁶

After the end of 2013 the utilisation of the instrument by Raiffeisen improved: finally in total 23 SMEs benefitted of 25 loans (two clients received two loans each). The expectation in 2010 was that 50 loans were to be covered by the guarantee. In the meantime the maximum cumulative value of all qualifying loans had been dropped from USD 20 million to USD 10 million. The actual cumulative value of loans reached BAM 10,182,960 (USD 7,441,753), which represents some 74% of the USD 10 million ceiling

⁵ Source: 'DCA Portfolio Management Bosnia TDY' USAID, November 2013

⁶ According to the Firma Evaluation Report of November 2015 in total seven clients of FIRMA received a loan with a DCA guarantee. Apparently this occurred in other banks,

but only 37% of the original expected ceiling.⁷ Obviously, achieving a 100% utilisation would have been practically impossible, a certain reserve will always be respected by a bank, but overall nevertheless utilisation was disappointing.

Utilisation in other banks with whom USAID had signed guarantee agreements was better, despite of the fact that they were operating under similar conditions. A derived efficiency advantage of this was the absence of claims by Raiffeisen on the guarantee so far.

The clients interviewed overall were positive about the services received from Raiffeisen, although the price of the loans was in several cases (see also the case descriptions in the Annex) considered high. Assessment and decision procedures were fast (one month), whereby valuation of the collateral was mentioned by some clients to be the most expensive and cumbersome. From the side of the bank, the co-operation with USAID, the acting agent of the Sida/USAID guarantee facility, was appreciated – the only problem mentioned was the understanding that loans guaranteed under this facility could not be restructured without losing the guarantee.⁸

3.3 Additionality

Additionality is clearly an issue. The evaluation matrix mentions two main questions:

- Would the additional lending have happened without the guarantee?
- Was there a commercial alternative to the USAID/Sida guarantee?

As to the first question, on the basis of the interviews and observations during the nine company visits, the evaluation team is of the opinion that most likely Raiffeisen would not have granted *all* of the

⁷ It should be noted here that the rationale to lower the ceiling was not the desire to show a better utilization rate, but the fact that since loans were given out at a longer maturity, revolving of outstanding loans would not be possible and the non-utilised guarantee allowance could not have been used for other purposes..

⁸ Somewhat confusingly, several clients mentioned a restructuring of their loan, one as recent as only two months ago. Different loans were grouped together, repayment terms changed etc. Given the fact that the clients were not informed about the guarantee they may well have been talking of other loans, which was also suggested by representatives from the bank. In addition, this understanding is not fully correct: restructuring is possible after having received approval of the agent.

loans discussed under the same conditions (e.g. maturity), but some borrowers could have obtained the loans also without the guarantee. The following substantiates this view.

All of the clients visited are existing Raiffeisen clients, several had received loans before, including long-term development loans. They had overall built up a good reputation. Some clients may have presented a higher risk profile, one entrepreneur for example who had been partner in a company banking with Raiffeisen earlier but now had set up an own business. Although first-time borrowers were not specifically targeted, their presence is an indication of additionality. In the entire portfolio covered by the guarantee there are only three first-time borrowers.

Raiffeisen did not treat the guarantee as first-class collateral, despite a written statement of March 2010 by the Banking Agency of Bosnia and Herzegovina that the USAID/SIDA guarantee was to be treated as such. Instead, it treated the guarantee merely as a comfort factor, enabling a loan where otherwise it would have been declined after some discussion, however insisting still on high collateral.

Collateral demands were stringent: over the period 2010-2013 the ratio of the value of collateral to the size of the loan ranged from almost 0.75 to seven (with one case of zero, for a very small loan backed up by a personal guarantee), averaged at over two with only one case (0.75) where the ratio was below one. In the period after September 2013 (including the companies visited under this evaluation) collateral requirements were somewhat less stringent, averaging at 1.3 but with only three companies where the relation between the value of the collateral and the loan size was below one. All of these three were corporate clients. Over the entire portfolio, this ratio is 1.5.

Some of the loans are very small, i.e. less than USD 100,000, in one case the loan represented only some 5% of the annual turnover of the company.⁹ It is likely that such an investment could have been financed alternatively, e.g. from equity or even excess cash.

Unfortunately, despite our request, Raiffeisen did not provide us with risk rating of guaranteed clients, neither with those of non-guaranteed clients, so we cannot make a comparison between

⁹ Such loans are backed up by a personal guarantee and the resulting zero collateral biases the average for the collateral value / loan size ratio even downwards.

guaranteed and non-guaranteed clients, nor for guaranteed clients over time.

When referring to the second question, the presence of commercial alternatives, it is likely that many clients could have financed the investment through regular financing from other banks. All clients visited banked with other banks and mentioned that they had been approached and received offers for loans from other banks. We recognise that this evidence is somewhat anecdotal, and for triangulation purpose we present therefore a table in which we compare liquidity and solvency figures for the Raiffeisen guaranteed portfolio with the average of SMEs which had benefitted from external finance in the entire Bosnian economy over the period.

The official database of financial statements of 26,440 enterprises is being used to stratify business operations of those SMEs that are granted a long-term loan in 2013, ranging between BAM 200,000 and BAM 1,500,000. In total 536 SMEs have been used to benchmark on the ratio total assets / total debt. We then allocated the Raiffeisen clients in the guaranteed portfolio to the specific solvency categories.. In addition, we have also shown the relation between the collateral provided to Raiffeisen and the size of the guaranteed loan (which may be smaller than total debt) derived from the CMS. Unfortunately on clients in Republika Srpska and Brcko no figures on debts and assets were available, and they do not figure in the table (n = 15).

Table 6: Comparison between Raiffeisen guarantees and SME database

Total assets/ Total debt	Distribution in ranking 536 enterprises	Nmbr of guaranteed Raiffeisen clients in category	Distribution of ranking guaranteed Raiffeisen clients	Average collateral coverage USAID/ Sida guaranteed loan in Raiffeisen portfolio
>3	10%	0	0%	
2-3	14%	7	47%	1.35
1.5-2	18%	3	20%	2.8
1-1.5	48%	5	33%	1.79
<1	10%	0	0%	
	100%	15	100%	

Two conclusions can be drawn. First, of 536 SMEs which received a term loan from any bank in 2013, the largest group (48%) falls in rank 4 in terms of assets coverage. This is obviously not because this is the group most attractive to the banks for long term lending, but merely because it is the largest group in the entire population. Second of all, the table shows that the group of beneficiaries of the Sida/USAID guaranteed loans have a better risk rating than the overall group, this despite of the fact that the loans are 50% guaranteed. The average actual collateral is for all groups above 100%. This clearly shows the conservative approach of Raiffeisen and the limited additionality of the guarantee.

We have repeated the above exercise for profitability (Earnings before Interest, Taxes and Depreciation / Long-Term Debt) and for liquidity (Current Assets / Current Liabilities). Also from this comparison it appears that the risk profile for guaranteed Raiffeisen clients is better than the national average of long-term borrowers.

Table 7: Key finance ratio's companies in database and Raiffeisen portfolio

Rank on profit-ability EBITDA/ L.T. Debt	Distribution in ranking 312 enter- prises	Distribution of ranking guaranteed Raiffeisen clients ¹⁰	Rank on liquidity Curr. Ass/ Curr. Liab.	Distribution of ranking 450 enter- prises	Distribution of ranking guaranteed Raiffeisen clients
>1	10%	31%			
0.8–1	4%	0%	>3	9%	0%
0.5–0.8	11%	0%	1–3	53%	73%
0.3–0.5	19%	23%	0,5–1	33%	27%
0–0.3	57%	46%	>0.5	5%	0%
	100%	100%		100%	100%

In two cases the guarantees were combined with the EBRD 'energy-efficiency' credit line, under which the borrowers upon successful completion of an investment beneficial for energy efficiency obtained a five percent rebate of the loan amount. This also lessened the additionality of the guarantee for these two cases.

None of the above indicators in itself provides a sufficient answer, but all seem to point at a limited additionality: the guarantee may have induced Raiffeisen to lend out to SMEs it might not have

¹⁰ For two enterprises this information was not available, n = 13.

provided a loan to at the same maturity, but a large share of companies served could, especially over the period 2013 till present, have financed their investments alternatively, mainly through other banks.

3.4 Effectiveness and sustainability

In the Theory-of-Change the effectiveness is pictured as the extent to which, through the increased lending to productive sectors and SMEs by Raiffeisen:

- turnover and income in the serviced SMEs improves;
- share of SME lending in the business of Raiffeisen increases; and
- potential of SMEs as a market is demonstrated (to other banks).

The nine visited companies without exception used the loan for investments in premises or equipment, one also partly for Working Capital. The following table shows the use of the 25 loans, according to the CMS.

Table 8: Purpose of the loans issued by Raiffeisen

Purpose	Nmbr Loans
Premises (building or buying)	7
Equipment	9
Working Capital	4
Equipment and WC combined	4
All (Prem., Eq, & WC)	1

Source: CMS

Respondents also mentioned an increased or at least sustained turnover and income where without the loan it would have been declining. The following table demonstrates percentage growths of turnover and profitability for a part of the portfolio in the Federation of Bosnia and Herzegovina.¹¹

¹¹ Unfortunately, again figures were not available for the companies located in the Republika Srpska nor the district Brcko. We also had to take out from the table some clients who received a loan only in 2015 or 2016, as well as a client on which no data could be retrieved. Unfortunately, because of these data limitations on only one client who received a loan prior to 2013 data were available. For confidentiality reasons, names of companies are hidden.

Table 9: Turnover and profit growth (decline) for a part of the Raiffeisen portfolio

No.	Loan	Date	% growth turnover			% growth P/L		
			2013	2014	2015	2013	2014	2015
1	534,369	Jan 14		-62%	-68%		-95%	-35%
2	690,000	Oct 13		11%			-9%	
3	232,744	Mar 13	25%	16%		-79%	1096%	
4	180,000	Nov 13		-2%	-48%		-35%	-49%
5	766,685	Nov 13		-1%	-48%		8%	-58%
6	127,000	Jul 13	-59%	-27%		-242%	-14%	
7	181,892	Apr 13	0%	10%		-85%	69%	
8	210,000	May 13	-13%	-13%		23%	-198%	
9	300,000	Feb 14		-11%			-8%	
10	149,767	Sep 13		9%			-65%	
11	1,100,000	Aug 11	-57%	-32%		321%	-47%	
12	400,000	Mar 14		9%			260%	

Source: FBiH Agency for financial intermediation official database of financial statements.

The picture is mixed but it is clear that the majority of clients did not record a growth in profit nor turnover after having received the loan. On the other hand, a few clients recorded a significant growth. The impression created by these data is not confirmed however by the visits to the clients.¹² Most of them, as can be read in the descriptions in the Annex, mention growth and increase in employment. The Bosnian statistics may not always be accurate and the time span is very limited to give a reliable picture. For example, losses may be due to start-up costs of the investment not yet covered by increased income.

The effect of Technical Assistance could not be tested, since the two companies which had co-operated with FARMA were located in the Republika Srpska, and had repaid their loans.

At the end of 2014, the importance of the USAID/Sida guaranteed loans for Raiffeisen was as follows:

¹² Four of the twelve clients in the table above were also visited by this evaluation.

Table 10: Magnitude of guarantee portfolio vs. total Raiffeisen portfolio

	%
USAID/Sida guar. Share of Total Raiffeisen Investment Finance provided to SMEs	12
USAID/Sida guar. Share of Total Raiffeisen Inv. Fin. provided to SMEs incl Micro	10
USAID/Sida guar. Share of Total Raiffeisen Lending to SMEs	7
USAID/Sida guar. Share of Total Raiffeisen Lending to SMEs incl Micro	5

Source: CMS, Raiffeisen Annual Report 2014

The previous section already mentioned the less than expected number of loans issued under the guarantee facility. It is therefore unlikely that the guarantee facility has had a large and sustainable effect on the share of lending to SMEs in the overall loan portfolio of Raiffeisen.

Likewise, a total of 23 cases cannot have had a large demonstration effect on other banks. The visits to the nine clients revealed though that, be it small, a certain demonstration effect was there: since the Raiffeisen bank is known as a conservative but solid bank, the fact that a client had obtained a loan from Raiffeisen attracted other banks to these clients.

3.5 Impact

In the Theory-of-Change the following effects constituting impact are mentioned:

- increased employment and earnings in the directly financed enterprises and, through the value chain, in Bosnian suppliers;
- increased lending to SMEs through other banks as a result of the demonstration effect;
- related income for small entrepreneurs and their workers.

The limited outreach obviously restricts the impact. The previous section mentioned the lack of a demonstration effect, if at all this effect is limited to existing Raiffeisen clients who have now more banking alternatives. This limits the discussion to the employment and supply chain effect.

Clients visited normally mentioned maintained or increased employment, from one or two to 26. Some of this was seasonal. One

more client was planning to employ 30 workers more in the near future.

For USAID employment is the most important motivation for applying its guarantee instrument in Bosnia-Herzegovina.

In the following table development of employment since the obtaining of the loan is shown for the same group of twelve clients for whom above turnover and profitability development was shown:

Table 11: Employment effects of part of the guaranteed portfolio

No.	Loan	Date	Employment (abs.)			% growth		
			2013	2014	2015	2013	2014	2015
1	534,369	Jan 14	76	45	43	-41%		-4%
2	690,000	Oct 13	12	19		58%		
3	232,744	Mar 13	29	41		32%	41%	
4	180,000	Nov 13	27	28	25	4%		-11%
5	766,685	Nov 13	28	32	33	14%		3%
6	127,000	Jul 13	3	2		-25%	-33%	
7	181,892	Apr 13	43	43		-4%	0%	
8	210,000	May 13	13	15		-13%	15%	
9	300,000	Feb 14	64	60		-6%		
10	149,767	Sep 13	8	9		13%		
11	1,100,000	Aug 11	16	12		-20%	-25%	
12	400,000	Mar 14	6	8		33%		

Source: CMS, BH Agency for statistics.

It appears here that the majority of clients indeed record positive employment effects.¹³ There were employment declined, with one exception, the absolute numbers were small. Attribution to the loan is of course not always self-evident: among the clients visited in one case the loan enabled the purchase of premises which previously were rented, so this had no net effect on employment.

Total employment in Bosnia-Herzegovina, being declining or virtually stagnant till 2013, showed again a growth of 5.4% in 2014 and 2.3% in 2015. Comparing this to the above figures it appears that six companies have reported growth in employment in 2014

¹³ Referring to table 9 above, increased employments costs may for a short period put profit under pressure.

above the industry average. Official employment data are unreliable however, there is a lot of seasonal labour and informal labour, as was also apparent in the companies visited.

The visited entrepreneurs employed both male and female employees. Among the visited enterprises three were women-owned, in the whole portfolio according to the CMS this number amounts to four.

CMS does not provide data on the supply chain. In the companies visited in four cases inputs were sourced from Bosnian sources. In one case this was wood: wood processing is a popular business in Bosnia and the cutting of timber is a government-controlled process. This may therefore have had a small effect on national income and government revenue, but hardly on the private sector. In the remaining cases agricultural inputs were sourced, one of these enabling a significant income increase for a number of cooperative herb growers. The two remaining cases showed positive effects on turnover for cattle growers and grain farming. The majority of clients visited processed imported material (mainly from the EU and Turkey).

The evaluation also looked at the possibility of false competition and market distortion through the use of the guarantee instrument, as a negative effect. If at all, this effect is negligible. Loans were normally provided at market conditions, providing no unwarranted advantages to clients. As described above, Raiffeisen used the guarantee conservatively. The scale of its use makes market distortion at the level of the financial sector unlikely. The conservative use, which hampered effectiveness and efficiency of the instrument, has here admittedly a positive effect: irresponsible lending, i.e. lending to clients who could not have afforded the terms of the loan, was avoided ('no harm was done').

4 CONCLUSIONS, LESSONS LEARNED AND PRELIMINARY RECOMMENDATIONS

4.1 Conclusions

The main conclusions drawn from this intervention study are:

- Both the selection of a guarantee instrument and the selection of USAID as partner were relevant at the start of the intervention. The selection of Raiffeisen as partner however was less relevant, given the lack of importance paid by the bank to the SME sector as clients.

- General efficiency of procedures of Raiffeisen, Sida and USAID is good, but overall efficiency is undermined by the limited deployment of the guarantee instrument by Raiffeisen.
- This low deployment (50% of expectations in terms of number of borrowers, 37% in terms of credit volume) has also negatively affected effectiveness and impact.
- The main reason for the above is the conservative approach by Raiffeisen to the instrument and to the SME sector, although they may have had a point in not considering the guarantee facility to be first class collateral.
- At the effectiveness level, strengthening of SMEs in terms of turnover and profitability shows a mixed picture. A large group of clients seem to show a declining performance. Loans are used, as intended, for productive purposes and clients visited also mentioned a grateful use of the loan for investments.
- Effectiveness in terms of increased SME lending by Raiffeisen and through a demonstration effect by other banks is small.
- There is a modest impact in terms of increased employment and spill-over effects to suppliers in the value chain. Negative effects are virtually absent.
- Additionality is doubtful. The guarantee may have induced Raiffeisen to provide finance to some clients at a larger maturity, but virtually all clients were existing clients with a loan history. In addition, a major part of these clients could have financed their needs through other banks or other sources of finance. Effectiveness and impact are therefore only to a limited extent attributable to the guarantee instrument.
- The effect of Technical Assistance through FIRMA and FARMA was not visible for this evaluation. FIRMA and FARMA were virtually unknown to the bank.

4.2 Lessons learned

Lessons learned and recommendations are obviously influenced by the limited use of the instrument.

The main lesson learned, in the opinion of this evaluation, is that, when selecting a partner bank for the channelling of a guarantee, attention should be given to the real motivation and willingness of this bank to enter the SME market. This attention should then cover also the recent operations of the bank, the alternative earning opportunities for the bank, governance and decision making

competences of the parties with which the discussions are held and the willingness of the bank to value the guarantee as sufficient collateral.

More lucrative investment options in government bonds posed a competition to lending to the private sector and real decision making on e.g. collateral requirements was held at headquarters of the bank in Vienna. An origination fee of USD 37,500 is an insignificant expenditure for a bank and does not buy commitment.

4.3 Preliminary recommendations

The present agreement limits the overall guaranteed percentage of the loan to the 50% guarantee provided by Sida and USAID. This should be, in order to safeguard additionality, extended to other instruments provided by donor or International Financing Institutes such credit lines. The guarantee should not be used where loans already contain other concessional elements.

It might have been beneficial for additionality of the agreement had also included a minimum size of the loan, e.g. USD 100,000 or USD 150,000.

The bank did not mention the guarantee to the client, afraid that this would have a bad effect on repayment discipline. To the evaluation it seems unlikely that loans would have defaulted if clients had known about the guarantee. This secrecy appears at least cumbersome for external monitoring and evaluation. In general, the agreement could have been more transparent in the conditions to opening books and giving access to (ex-) clients for evaluation purposes.

At this very instance in Bosnia-Herzegovina the relevance of a guarantee scheme through existing banks for general SME lending seems restricted, additionality might be limited. An increasing number of banks and other financial institutes, some of them devoted to SMEs and/or micro-enterprises, has embarked on this market and there now seems to be a tough combination between banks to source good clients. There appears to be now a need for more focused instruments, better directed at underprivileged and underserved clients, such as starting enterprises with little collateral, returning diaspora (reportedly, Sida and USAID are now in the process of setting up such a facility), or others.

ANNEX 1: DESCRIPTION OF THE SIDA GUARANTEE FACILITY WITH RAIFFEISEN BANK & THEORY OF CHANGE

Process of design and Sida's appraisal

In 2008–2010 as a result of the financial crisis, in Bosnia Herzegovina (BiH) a lack of access to finance for SMEs was observed. The decision for cooperation between USAID and Sida on guarantees in BiH was made both bottom-up (originating from existing good cooperation between USAID and Sida in BiH) and top-down (as a result of the Washington-Stockholm agreement to cooperate on Private Sector Development). The guarantee arrangement is made under the Memorandum of Understanding between Sida and USAID dated 26 March 2010. Under this MoU, USAID shall act as agent on behalf of Sida.

The selection process in 2009/2010 of Raiffeisen was done jointly, although USAID was 'in the drivers' seat'. Over 20 banks were visited during the design phase. The idea was to find a bank which was large, leading and interested (Raiffeisen fit that profile) and one more medium-sized (Volksbank was selected as midsized bank and showed indeed a good utilisation, but since that bank was later acquired by the Russian Sberbank cooperation was halted after the Ukraine crisis started).

Raiffeisen is the number one bank in the country, had a good coverage and lending base, and credit policies and credit review were solid. Raiffeisen was reportedly, prior to the guarantee already involved in lending to productive and manufacturing sectors, this was however not the core activity of the bank. It was however a new partner for USAID, and the hope was that, if this bank would develop SME finance as a core element of its strategy, a large impact could be achieved in terms of financial market strengthening, SME development and related employment creation.

The cooperation between USAID and regulators is good (BiH is the only country where USAID has such a cooperation) and the Banking Agency of the Federation of BiH had earlier on issued a statement that the USAID-Sida guarantee can be seen as 1st class collateral. Therefore it came as a surprise to USAID and Sida that Raiffeisen did not treat the guarantee as such. Only on

a case-by-case basis the guarantee is seen as collateral for Raiffeisen. The relatively small size of the guaranteed amount (USD 10m) versus a situation in BiH where the number of Non Performing Loans was drastically growing and lending dropped, is a possible explanation for this.

Set-up of guarantee intervention

Table 12.

Imple- menting partner	Benefi- ciary	Value of guaran- tee	Years	Type of risks guaran- teed	Risk sharing	Origi- nation fee	Utilisa- tion fee	Secu- rity	Agent
USAID	Raif- feisen	USD 10m	10	50% (Sida 25% and USAID 25%)	Sida 25%, USAID 25%, Raif- feisen 50%	0.75%	0.5% p.a. to Sida and USAID	Pari- passu	USAID

Conditions for the guarantee

The guarantee percentage Sida provided amounts to 25%, with a maximum of USD 2,500,000 or (whichever lowest) SEK 24,500,000. Likewise, the guarantee percentage of USAID amounts to 25%, with a maximum of USD 2,500,000. The total percentage guaranteed by donor and/or development agencies incl. Sida and USAID may not exceed 50% (i.e. other guarantors are therefore practically excluded). Further conditions include:

- Period of the Guarantee Arrangements from 29 September 2010 – 30 September 2020 (signed on 28/9/2010).
- Final date for placing qualifying loans is five years prior to expiration date, i.e. 30 September 2015. This date was extended to 31 March 2016 in the 2nd amendment to the Agreement dated July 2015.
- The maximum cumulative value of disbursements of all outstanding qualifying loans is USD 20m. This ceiling was lowered to USD 10m in the 1st amendment to the Agreement dated May 2014.
- Maximum value of principals of all outstanding qualifying loans at any one moment is USD 10m.

The Fee structure is as follows:

- Origination Fee: 0.75% of guaranteed ceilings (i.e. USD 37,500) payable to Sida;
- Utilisation fee: 0.5% per annum, of average of outstanding principal guaranteed in a (half year);guarantee period, payable semi-annually to Sida;
- Fees are paid in USD.

Qualifying loans and borrowers

Qualifying borrowers are non-sovereign Bosnia and Herzegovina-registered small and medium-sized enterprises (SMEs), associations, or cooperatives operating in productive or manufacturing sectors. The Guaranteed Party, Raiffeisen in this case, shall use its best efforts to target, but is not limited to borrowers active in agriculture, tourism, wood processing, or metal working sectors. Certain sectors (e.g. military, material for abortion, etc) are excluded, for others (pharmaceuticals a/o) prior permission from USAID is required.¹⁴

Maximum amount of a qualifying loan is the (local currency equivalent of) USD 1,500,000. Currency of the loan is Euro or Bosnian Mark.

Maturity of Qualifying Loans depends on the date of issue:

- Placed before 30/09/2012: six months to nine years
- Placed after 30/09/2012: three to seven years

Assessing clients

Raiffeisen as the guaranteed party is responsible for the decision on whether or not a client qualifies, in case the client qualifies, Raiffeisen registers the loan in the USAID on-line Credit Management System (CMS). USAID and Raiffeisen have each at all time the authority to remove a loan from the guaranteed portfolio. We were told that often, actual verification of compliance of a loan with the guarantee scheme is done by USAID only once a claim is made.

Claim handling

Raiffeisen can only submit a claim if

- Raiffeisen has made a written demand to the defaulting party for repayment;
- Raiffeisen has done everything legally possible to regain the funds due including realisation of the collateral, only the net

amount due after valuation of the realised collateral is covered by the guarantee; or

- Raiffeisen has provided USAID with convincing evidence that what is stated in the bullet point above is not possible.

USAID will verify whether indeed the loan claimed did qualify; and above action by Raiffeisen has been taken.

Payment of a claim will not be released within 90 days of the issue of such claim by Raiffeisen. Any value still recovered within these 90 days or later by Raiffeisen will be used to reimburse USAID.

Reporting

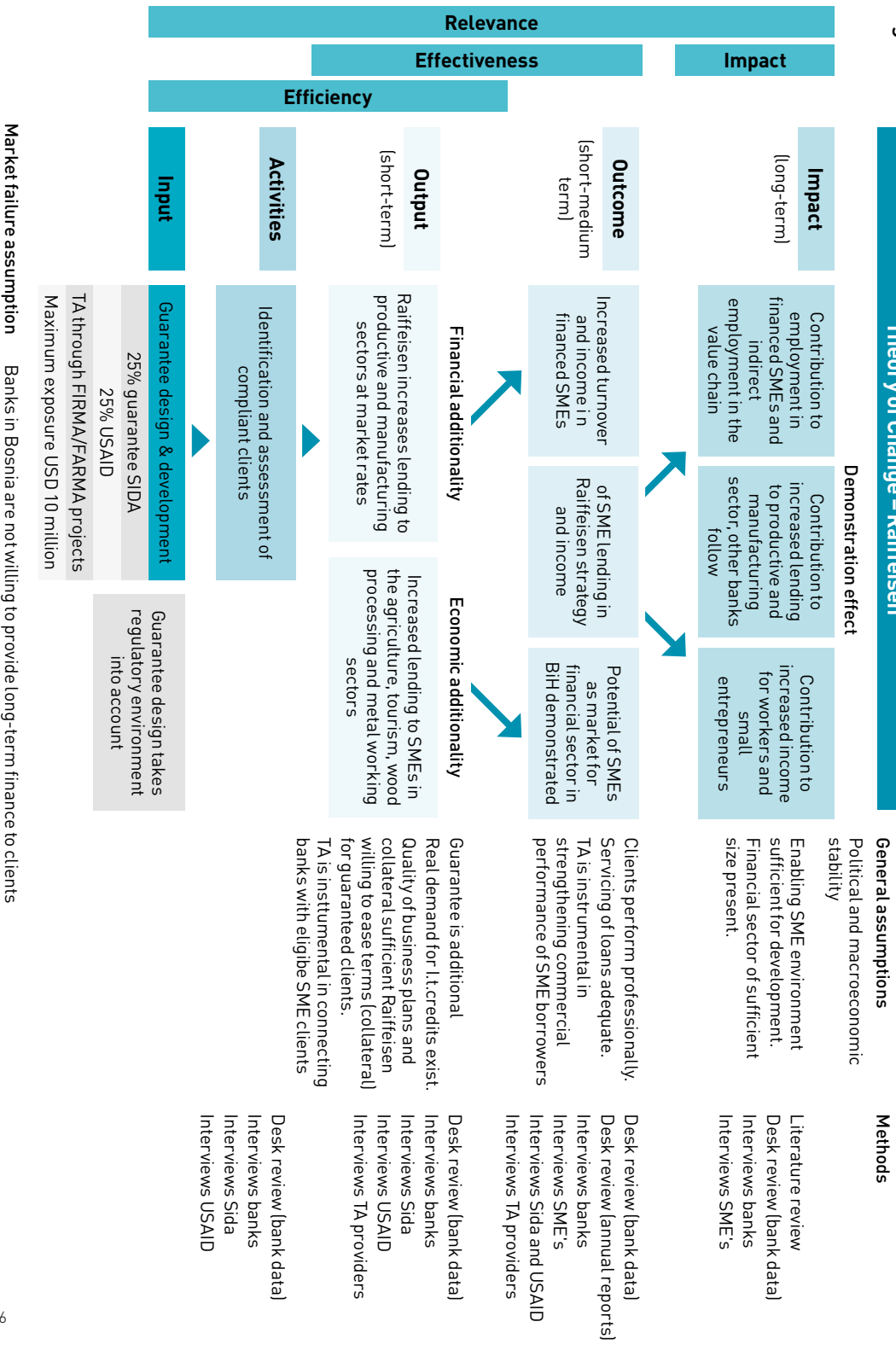
- Semi-annual (April-Sept; Oct-March) portfolio reporting, in the prescribed format in CMS. Of new loans placed in the previous period financial indicators are provided of the borrower plus information on existing employment and number of new labour places expected as a result of the loan;
- Annual audited statements on performance of the portfolio;
- Annual Environment Compliance Certification.

Other conditions:

Raiffeisen is expected to use its best efforts to cooperate with USAID and Sida-funded SME and agriculture development programmes (note: FARMA and FIRMA) and to consider proposals recommended for financing by these projects. These proposals will however be considered according to the applicable lending policies and procedures of Raiffeisen, and are not binding for Raiffeisen in any way.

Figure 4.

Theory of Change – Raiffeisen



Intervention paper Centenary Health guarantee

1 INTRODUCTION

The underlying intervention report presents the findings of the evaluation of the health portfolio guarantee provided jointly by USAID and Sida to Centenary Rural Development Bank Uganda (CRDB). The evaluation is based on a thorough desk-analysis, interviews and a field visit to Uganda, which was carried out by three evaluators Hans Slegtenhorst, Marie Heydenreich and Paulo Luswata from the side of Carnegie Consult, assisted by Anders Berlin as an observing team member from Sida.

The report is structured as follows:

- The following paragraph briefly introduces the guarantee facility and related TA instruments which are the subject of this evaluation study (a more detailed description can be found in Annex 1 of this report).
- We will then highlight the approach to the intervention study and the sources of information used, as well as problems and limitations that we faced during the evaluation.
- Chapter 2 is dedicated to a brief context analysis of the financial and the health sector in Uganda, which helps to put the evaluation findings in their specific context.
- In chapter 3 we will present the findings grouped under the main OECD/DAC evaluation criteria: relevance, efficiency, additionality, effectiveness, impact, and sustainability.

1.1 Subject of the evaluation

The agreement for the portfolio guarantee was signed between USAID, Sida, and CRDB in December 2012. It is part of a series of interventions under the Memorandum of Understanding between Sida and USAID dated March 2010 for the provision of joint guarantees.

Table 13: Set-up of the guarantee

Imple- menting partner	Benefi- ciary	Guarantee Ceiling	Years	Type of risks guaran- teed	Risk sharing	Origi- nation fee	Utili- sation fee	Secu- rity	Agent
USAID	Cente- nary Rural Develop- ment Bank	USD 900k/ SEK 8.55m in UGX (Sida portion)	7	30% principal (Sida portion)	USAID 30% Sida 30% CRDB 40%	1% (to Sida)	0.75% p.a. (to USAID)	Pari- passu	USAID

The guarantee was set-up as a loan portfolio guarantee covering term-loans to privately-owned and operated micro, small, and medium enterprises as well as healthcare workers in the health value chain. The total cover is 60% of the principal amount of which Sida and USAID each guarantee 30%.

The maximum authorised portfolio was set at the UGX equivalent of USD 3m and the guarantee has a total duration of seven years, from September 2012 up to September 2019. The guarantee was set up with the following restrictions:

- 30% of the guaranteed portfolio is restricted to lending outside of the Central region
- The maximum cumulative principal amount made to one borrower is the UGX equivalent of USD 300,000
- The loan cannot be used for refinancing purposes, repayment or repurchase of an existing loan without specific request to and permission from USAID

CRDB had to pay an origination fee of 1% of the sum of the Sida Guarantee Ceiling in USD directly to Sida, i.e. USD 9,000. The utilization fee was set at 0.75 % per annum of the combined average outstanding principal amount that is guaranteed by the guarantors, payable semi-annually in Ugandan Shilling to USAID.

USAID was assigned the role of agent for Sida, responsible for handling all communication with CRDB including obtaining reports as well as monitoring utilization and managing the claims process.

TA was not included in the agreement, it was noted however that the success of the guarantee would hinge on the activities of existing TA programmes of USAID to borrowers in the field of business plan development and financial literacy (through the PHS programme).

This 5-year programme is carried out by an American company (Cardno) and covers trainings for bank staff and workshops for companies in addition to different activities beyond the purpose of the guarantee.

1.2 Approach to the intervention study

This evaluation is based on a mixed methods approach which includes document review, analysis of loan data and interviews with borrowers and other key informants.

During the inception phase we researched the set-up of the CRDB guarantee facility and the process leading up to the decision through document review and interviews with USAID, Sida and CRDB. We designed a customized evaluation framework in line with the reconstructed theory of change, including project specific evaluation questions, indicators and sources of information.

Elaborating on the results of the document analysis, the desk phase review analysed relevant documents from USAID and Sida on the use of the guarantee, guaranteed lending volumes, fee income and claims; characteristics of the portfolio of guaranteed loans as well as the cost-structure of the guarantee. Most of this information was obtained from the credit monitoring system (CMS – a web based reporting database) of USAID which was made available to the evaluation team. The CMS system was also used to select a sample of borrowers for in-depth study.

The 10 days field visit to Uganda took place from 3 to 15 April 2016. The first week was dedicated to meetings with the following stakeholders in Kampala to understand the context in which the lending operations occur:

- Embassy of Sweden/ Sida
- USAID
- CRDB
- PHS, the TA provider related to the guarantee
- Ecobank, another bank implementing a guarantee in the health sector for USAID and Sida
- aBi Trust and Finance, the largest provider of guarantees in Uganda
- Ministry of Health, private-public-partnership department
- Uganda Healthcare Federation (UHF)
- Central Bank.

During the second week the team travelled to the Western and South Western part of Uganda for interviews with (rural) branches of CRDB and collected primary data from a sample of borrowers. In total we visited 9 branches in rural, urban and peri-urban areas and collected relevant historical loan documentation and additional information of 12 borrowers from the responsible relationship manager of the respective branches. All of these borrowers had received between one and four loans covered by the guarantee. We visited 7 of the 12 borrowers in the sample for semi-structured interviews. The reason we did not visit all was that some of the borrowers were sometimes located very remote and travelling took longer than expected, or that they were not available at the time of the visit. Chapter 3 and the annex contain more information on the borrowers and branches visited.

The field visit commenced and concluded with a briefing and debriefing at the Embassy of Sweden. A list of stakeholders visited can be found in Annex 2. For confidentiality reasons we have not included the names of borrowers.

1.3 Problems and limitations

Generally we were very satisfied with all stakeholders' willingness to cooperate and share requested data, including CRDB and the borrowers themselves. We were asked by CRDB not to mention to borrowers that they were covered by a guarantee for the sake of payment discipline, which made it slightly more difficult to conduct the interviews and ask questions related to the guarantee. Below we show other risks and limitations that were identified in the inception report as well as new limitations we were faced with in the field.

Table 14.

Risk/ limitation	Practical relevance
Willingness of banks to share confidential information of their borrowers	Not applicable
Clients are not willing to cooperate	Not applicable
Quantitative approach of assessing additionality might be hard to implement as FIs have different reporting and rating standards	Applicable, CRDB does not have an internal risk rating system. Therefore, a mixed-method approach based on loan data and interviews with relationship managers and borrowers has been implemented to assess additionality.

Risk/ limitation	Practical relevance
Challenges to retrieve baseline data on Health portfolio of Centenary Bank	Applicable, CRDB does not stratify loans to the health sector. A quantitative assessment of the growth of the health portfolio at portfolio level could therefore not be implemented.
Impact assessment limited	Applicable, the scope and time of the field visit did not allow for an in-depth impact assessment on household level. The variety of client visited as well as interviews with other key informants provided us with an indication for the probable impact of the lending activities of CRDB including for potential negative/ crowding-out effects.
Small sample of borrowers	Semi-applicable, the remote location of some borrowers made it nearly impossible to visit more than two borrowers per day.
Balance sheet and P&L data of borrowers not available	Applicable, (audited) or any accounts are rarely available for especially the smaller enterprises, which makes a quantitative analysis of borrower's performance impossible
Administration of guarantees not fully up to date	Applicable, therefore more time than expected was spent for interviews at branches and CRDB HQ

2 CONTEXT ANALYSIS

2.1 Uganda Health Sector

As at its last census in August 2014, Uganda has a population of 35 million and a nominal GDP per capita of USD 771 (2015). While Uganda is performing better than its peers on major health indicators it is still lagging behind its Millennium Goals in health. Through a tiered network of 300 health facilities the Government of Uganda can only cater for approximately 50% of the required health services of the country. In full recognition of this short fall and in view of its overall policy, government therefore strives to provide an enabling economic and policy environment for the private sector to flourish and therefore provide the shortfall. This is directed through the National policy on public private partnership in health.

Private sector health provision is through the private for profit (PFP) health facilities that vary greatly in size and in the facilities they provide and these cater for up to 40% of the health services in

the country. The rest is provided by Private not for profit (PNFP) facilities, which are mainly church based and Traditional and Complimentary Medicine Practitioners (TCMP). The limited public health sector facilities though free, have almost always been found wanting in availability of personnel, medicines and/or equipment, due to poor funding. It is common for the very personnel working in the public health units to be the same ones running the private clinics as a means of augmenting their meagre remuneration. Drugs are also in short supply and patients are often provided with prescriptions to procure the drugs from the private pharmacies.

While the PNFP are usually well funded and consequently well stocked in personnel, equipment and medicine, they are much fewer and far in between and therefore not accessible to a large portion of the population, and therefore only cater for up to 10% of the need. This therefore leaves remaining 40% to be catered for by the PFP's. These are numerous but vary greatly in size with the majority being at the equivalent health Centre III status and below, with only 12% at health centre IV (mini hospital) level. The larger facilities when outside the central regions are mainly confined to in the town and large trading centres leaving patients with serious ailments to travel up to 20km or more to access them.

2.2 Uganda Financial Sector

The Uganda financial sector is dominated by the commercial banking sector which has existed for over a century. It consists of a central bank whose primary role is to maintain price stability and a sound financial system. It is in this latter role that it supervises the commercial banking industry and manages monetary policy. Under its supervision are 25 commercial banks or tier I institutions, that provide the full range of banking services, 4 Tier II credit institutions that do not participate in the clearing house, 4 tier III Micro deposit taking institutions that in addition do not deal in foreign exchange transactions, and just over 200 forex bureaus and over 100 money remitters. Outside regulation are 3 development banks and a large but unconfirmed number of micro finance institutions that ideally are not allowed to take deposits, Savings And Credit Co-Operative (SACCO's) ideally regulated under the ministry of cooperatives and Village Savings and Loans Associations (VSLA's).

The Uganda banking industry experienced major improvements since its dearth during the mid to late 1990's when several banks had to either be closed or taken over by the central bank due to poor

management. The size of the banking Industry consolidated balance sheet has since 2001, grown ten-fold in Uganda shilling terms, from UGX2 trillion (\$1.2Bn) to UGX22 trillion (\$6.5Bn) as at end of 2015. The branch network has also grown from 100 in 15 banks to about 600 over the same period. The July 2007 lifting of a moratorium on licensing new banks by the Bank of Uganda positively impacted on this growth. Until 2007/8 much of the industry was concentrated around the major urban centres and the branches were used mainly to grow the deposits which were then generally on lent to government, the corporate clients, and the retail, sectors. Competition has however compelled them to venture more aggressively into the SME space which they had traditionally found difficult to work effectively with. However of the 25 tier 1 banks, only 2, genuinely operate in the rural area and one of these only became a bank in the last 2 years. This leaves the rural areas to the mercies of the lower tier regulated (only 8) and the unregulated financial service providers. This limits both the products that are available to them and due to the limited economies of scale of the providers, a generally more expensive banking experience, which has discouraged many rural dwellers from the formal financial services industry.

Outside the banking sector is the equity and bond market that is only started in 1996 with the setup of the Capital Markets Authority (CMA) to regulate it. The Uganda Securities Exchange was licensed in 1997 and remains the only licensed trading floor. It currently has 16 companies trading on it of which exactly 50% are local and the rest cross listings from Kenya. It has also been used by a few institutions to raise money through bonds with Ugx 300bn having been raised since its inception. However activity has remained below expectation as cost efficiency start at Ugx 15bn, which is above most local company requirements yet due to high interest rates, multinational companies have preferred to raise funds cheaper in their parent markets. The government paper secondary market has also remained primarily over the counter as market players have remained few mainly dominated by the National Social Security Fund, which controls 90% of the pension funds industry.

More recently, mobile money, a funds transfer mechanism through the cell/mobile phone and owned and dominated by the large Mobile Network Operators (MNO) has become a major player in the financial services industry and currently boasts of 15 million accounts and annual transactional turnover in 2014 of UGX 25 trillion!. Though not yet as developed to its full potential (as in

neighbouring Kenya) where interest paying deposits and loans can be offered, it has reach and convenience that will enable access to financial services in the rural areas as never before. The recent amendment to the law to allow for agency banking is expected to further deepen access to financial services in rural areas and bring them to the fold of modern banking services in an efficient and cost effective way.

3 FINDINGS OF THE INTERVENTION STUDY

In this chapter we will present the findings, grouped under the main OECD/DAC evaluation criteria: relevance, efficiency, effectiveness, additionality, impact, and sustainability. The evaluation matrix and a theory-of-change for the CRDB health guarantee intervention can be found in the annex of this report. We will revisit the questions in the matrix when presenting the findings, and thereby verify the validity of the theory-of-change and its assumptions.

3.1 Relevance

The main goal of the intervention for Sida was to promote access to private healthcare in Uganda, with special attention to rural areas, by catalysing private capital for investments in the health sector. USAID initiated the project and carried out a detailed assessment for selecting the implementing financial institution.

As outlined in the context analysis, the public healthcare system in Uganda is dysfunctional and highly underfunded and especially poor people in rural areas do not have sufficient access to health care facilities. Government expenditure on health remains inadequate only meeting between 40% and 50% of the national health requirements with the rest being met by donors and out of pocket expenses.

The government of Uganda recognizes the shortcomings of the public sector and supports the privatization of the health sector. Along these lines it has set up a PPP-unit to accommodate the role of the private sector. Although laws and regulations are generally in place, supervision of private healthcare enterprises remains an issue. Regulations to prevent an oversupply of drugs and guarantee fair and consistent pricing of services are barely enforced by the public authorities, which can make the sector prone to unethical behaviour. There are initiatives for self-regulation which try to compensate for this lack of oversight.

Among the many constraints for-profit health enterprises face in the provision of quality health services is the lack of adequate financing for equipment, working capital and construction needs. On one hand the banks have perhaps little understanding of the health sector and have treated and assessed its players as just another set of SME businesses. The private health facilities owners have been medical professionals with no or very limited business management training and/or financial record keeping skills, which has made assessment of their businesses by the banks very difficult. Many of the health facilities need medium to long term financing to allow for their expansion and also lack collateral in the favoured form of traditional brick and mortar registered property. On the other hand the health providers lack knowledge to understand the requirements of the banking industry and its services. They have therefore tended to rely more heavily on retained earnings than external bank finance which can allow for more rapid expansion and growth.

The guarantee was supposed to work by increasing the value of the collateral for those enterprises that lack sufficient securities, thus increase the number of clients that would be able to access finance and also to increase access to higher credit amounts. USAID and Sida also decided to increase the usual guarantee cover by 10% to 60% due to the high perceived risk of the health sector. The expectation was that after some time, through building a financial track record with the bank and demonstrating the viability of the business through successfully repayment of the loans under the guarantee, the bank would favorably adjust its risk perception and enterprises in the health sector would be able to access finance without the guarantee. TA for improving loan officers' understanding of the health sector, and for increasing business management and financial literacy skills of (potential) borrowers, should support the effects of the guarantee.

The intervention is found relevant in terms of the overall goal of access to health and in line with the national policy on health as well as the country strategy for Uganda 2009-2013. This strategy has four priority sectors including health and within each sector, support may be provided through public channels, multilateral organizations, civil society and the private sector.

The support was also in line with the thematic priorities human rights and gender with a bearing on the rights of women to accessible sexual and reproductive health services. The guarantee intervention is focused on smaller SMEs along the broad private healthcare

value chain with a focus on rural areas (30% target) as well as women owned businesses. Many women are generally employed in the health care sector and core activities of many clinics are HIV treatment and family planning.

From Sida's former strategy owner for health in Uganda we understood that there are some concerns about providing support to the private healthcare sector, mainly due to the lack of supervision and potential crowding out of public healthcare services. While we have found no evidence to support the crowding out hypothesis and we still believe the intervention is very relevant, it seems that the strategy owner and the loan and guarantees department could have communicated better to address these issues when the guarantee was designed and approved. This would have increased ownership of the intervention within the organization.

The intervention is also considered very relevant in terms of targeting the market failure that causes low lending volumes to health sector enterprises. The set-up of the guarantee, 60% cover and a focus on rural areas, is also considered adequate to achieve higher lending to the target group from an ex-ante perspective. The selection of CRDB as the implementing financial institution was a very relevant choice, it has a history as a MFI with a high representation in rural areas and a focus on the lower segments of the SME sector. CRDB is also one of only two commercial banks in Uganda that serves clients with unregistered collateral. Although not subject of this evaluation and also not part of the same guarantee agreement, the selection of Ecobank which is implementing another health guarantee for USAID and Sida seems to have been less relevant as their focus is on the higher segments of the SME sector and mainly on the Central region. One weak point in the assessment was that internal policies of CRDB concerning collateral were not fully taken into account. It was expected that the guarantee would lower the collateral requirements by 60%, which is not realistic since CRDB does not value the guarantee as first class collateral and it only covers loss on principal only and not loan amount issued.

From the outset the idea to make TA available in particular for borrowers in the health sector can be considered as an important and relevant addition to the financial instrument.

The cooperation with USAID was a good choice given their experience with guarantees and their capacity to monitor and follow up the intervention from a financial perspective. In Uganda, USAID and Sida's policy on health are aligned overall, but Sida could have

put more effort to monitor do-no-harm and market distortion indicators, as these are of less importance to USAID and do not make part of the regular monitoring.

3.2 Efficiency

The initiative for the guarantee came from USAID who also acted as an agent for Sida, thereby taking responsibility for all communication with CRDB including monitoring and follow-up as well as handling of claims. In the light of Sida's limited local capacity and the vast experience of USAID with guarantees, this has been an efficient choice, even though it means Sida has less control over the design and the progress of the intervention this way. We understood that decision taking at the level of DCA can be lengthy in some instances.

Inside Sida there seems to be segregation of responsibilities which leads to inefficiencies and a lack of good oversight of the guarantee. Monitoring responsibilities and ownership have not always been clearly divided between the loans and guarantee department in Stockholm and the Sida office in Kampala. We have heard different experiences about the communication between USAID and Sida, very positive from the side of USAID, but locally Sida has not always felt similarly involved. This can be partly explained by the character of the silent partnership but also by a lack of initiative and internal coordination issues on the side of Sida.

The guarantee is smoothly integrated into the credit approval process of CRDB overall. Centenary branches are able to approve loans within 2-5 days and borrowers don't even notice that they are covered by a guarantee to avoid moral hazard. CRDB passes on the guarantee fees to borrowers by charging them a higher administration fee (3% instead of 2%), which it explains to borrowers through the higher credit value. This way, CRDB does not bear any extra costs for using the guarantee, but also has a high incentive to place more than necessary loans under guarantee. One shortcoming is that CRDB does not state the reason for using the guarantee in their loan approval documents, thereby it is difficult to verify in retrospect whether the guarantee was used as intended.

It is difficult to make any firm statements with respect to the correctness of the fee calculation at the time of creation. The premium calculation of USAID was very much based on the country risk, the financial strength of CRDB, the performance of its loan portfolio and the performance of Ugandan banks in general.

Also in terms of reporting, processes are generally efficiently handled through the credit monitoring system (CMS) of USAID, which CRDB uses to register and remove guaranteed loans. During our research we found that the database was not always up to date and some data was inconsistent with the information we received from branches and paper files. CRDB reports on development indicators on a voluntary basis, which seemingly does not cause a high administrative burden for the bank either. In-depth monitoring on development indicators is mainly done by Cardno, the technical assistance provider. From a financial perspective the efficiency of the guarantee is high, to date there have been no claims.

The USAID and Sida contract with CRDB currently allows applying the guarantee instrument in only one manner. The contract stipulates that the cover amounts to 60% of value of the loan amount and 40% is for the risk of CRDB. When studying a number of cases and visiting the clients and the branch offices of CRDB we noticed that in some cases the full amount of the guarantee was not actually needed, which gives rise to the question whether the guarantee can be applied in a more flexible and tailored manner. The advantage of the present system is that it is transparent and easy to understand for all parties involved (in particular for the CRDB loan officers). The disadvantage is that the full 60% guarantee is used in all cases; even in the case where a guarantee for e.g. 40% could have achieved the same result. The present set-up is not able to introduce incentives for specific clients or groups of clients for that reason. One could imagine that the bank would be able to get 80% cover for new borrowers, start-ups and/ or clients with unregistered collateral while the more established companies in the sector would get a lower guarantee percentage.

The present threshold of the facility is sufficient to meet the demand from borrowers. The understanding of and limited focus on the health sector by banks together with the prudent credit policy of CRDB and the unclear indicators for the use of the guarantee are probably important explanations for that limited use. However the lack of competition among banks in using the guarantee and the set up of the facility may have stimulated and encouraged this somewhat conservative way of making use of the facility. CRDB is the single bank using the guarantee facility as Ecobank focusses on another segment. Another issue is the efficiency of the present non revolving set up of the guarantee facility in line with USAID's regulations. In the present system the maximum cumulative amount

of all loan disbursements under the guarantee must not exceed the Ugandan Shilling equivalent of USD3,000.000. This means that every loan, independent of the tenor, will reduce the available guarantee volume by its respective amount. A guaranteed loan with a tenor of 4 months 'eats up' as much guarantee volume as a guaranteed loan with a tenor of 3 years. Overdraft facilities, for example, are currently not covered as they would quickly fill up the available guarantee volume. In the absence of proper working capital facilities, overdraft facilities can be very beneficial for companies with a seasonal business. Revolving bank guarantees on the other hand allow credits to get released once the borrower makes the repayment and subsequently can be used for new loans again. The introduction of a revolving facility may of course have implications for Sida and USAID in terms of budget allocation and perhaps premium calculation. On the other hand it may simplify the (more flexible) use of the guarantee. By introducing a ceiling over the full guarantee period, the maximum permitted exposure can be lower than in the case of a non-revolving facility which allows CRDB to make efficient use of the guarantee. For the purpose of this intervention report it is not possible to discuss this subject in all details and aspects however we feel that it represents an important consideration for future operations.

3.3 Effectiveness

In this paragraph we will discuss in which manner the guarantee was applied and the direct and indirect effects that resulted on the output and outcome level.

Lending strategy

After CRDB, USAID and Sida entered into the guarantee legal agreement, the head office of the bank sent out a communication to all branches on how to implement the guarantee. The format of that instruction only mentions the general conditions of the agreement with USAID and Sida (maximum amount, fee, use, insufficient securities etc) and does not explain to the branches how to apply the guarantee and in particular how to define "*insufficient*" securities.¹⁵ Some branch officers we interviewed in the field mentioned that there have been meetings/trainings to explain the use of the guarantee while others are not aware of such meetings at all and complained about the lack of instruction.

¹⁵ See annex for the memo dated October 22, 2012

In the short term, the guarantee influences the lending strategy of CRDB in the following way: Centenary has the general policy that the cash flow of the borrowers should be able to serve the payment obligations including the interest and principal instalments of the loan. In case cash flow is insufficient no (new) borrowing will be allowed (with or without the guarantee). Although it is not always very clear which criteria were used for placing a loan under guarantee, the field visit revealed that the guarantee enhanced in particular the ability to provide longer tenors and higher amounts that are not sufficiently covered by registered collateral. This is by less than 60% however, which was the expectation of Sida and USAID when designing the guarantee. The average collateral/loan ratio for loans under guarantee is still very high at 174%. The following chapter on ‘additionality’ provides more details on the influence of the guarantee on the collateral requirements of CRDB.

Output level

According to the theory of change expected outputs of the intervention were:

- CRDB increases lending to health sector borrowers (in rural areas)
- Health sector borrowers show an increase in revenue and job creation

The guarantee agreement was signed in September 2012 for a total cumulative volume of the UGX equivalent of USD 3,000,000 over 7 years (until December 2019). By May 2016, 3.5 years after the start of the intervention, 63.6% (USD 1,908,697) of the available guarantee volume had been used. A total of 109 loans to 79 unique borrowers have been extended under the guarantee (some borrowers have been covered in consecutive loan transactions). The current balance of loans outstanding is USD 683,390. The outstanding loans ratio (NPL 90) is 1.83%, however no claims have been made.

The average loan amount on portfolio level has been UGX 50,562,373, equivalent to USD 15,183 calculated with the current exchange rate (3 May 2016). 14% of the guaranteed loans have been extended to first time borrowers, 30% to borrowers outside the Central region, and 8% to women owned businesses. All figures are taken from the CMS database from May 2nd 2016.

The guarantee is well used, if also primarily for existing borrowers. In the course of 2013 USAID decided to put the guarantee on

hold for six months for this very reason, which delayed the progress of the guarantee utilization. Furthermore, we witnessed some cases of refinancing (the guaranteed loan was used to pay off an outstanding loan balance) which is not allowed under the contract between Sida, USAID and CRDB without prior USAID notification and authorization.

A balance of USD1,091,400 remains for covering loans until September 2018, as the final date for placing qualifying loans under coverage is at last one year prior to the expiration date of the guarantee. CRDB will have to speed up if it wants to utilise the whole guarantee amount in the time remaining, also as the maximum tenor of loans under guarantee decreases as the guarantee period proceeds. The tables below show some key figures around the utilisation of the guarantee on portfolio level.

Table 15: Utilisation of guarantee on portfolio basis (May 2016) (part 1)

Total Number of Loans	Number of Borrowers	Cumulative Utilization Percent	Outstanding Balance	Outstanding Loan 90+ Days	Total Number of Claims
109	79	63,62%	\$683.390	1,83%	0

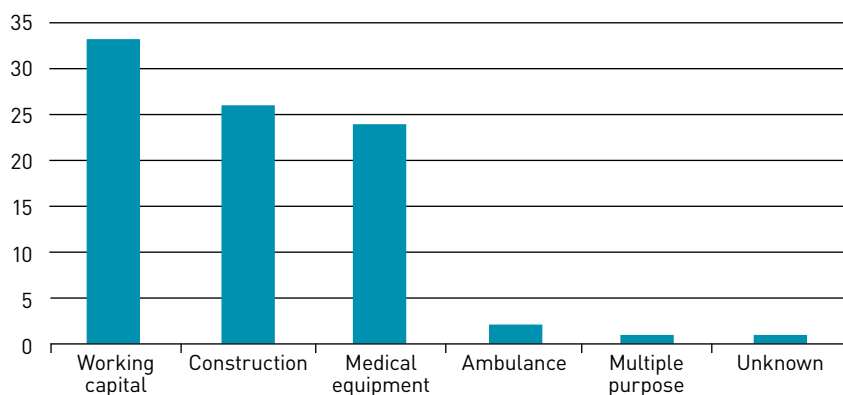
Table 15: (part 2)

Average loan amount	Average % collateral	% First Time Borrowers	% Woman Owned	% Rural
UGX 50.562.373	174%	14%	8%	30%

Table 15: (part 3)

0 Employees	1–5 Employees	6–10 Employees	11–50 Employees
2	64	26	17

The figure below shows that the guarantee is primarily used for working capital, construction, and purchase of medical equipment. The majority of the clients are small clinics and the average business has 1–5 employees.

Figure 5: Purpose of the loans (March 2016)

From the field visits we learned that the guarantee was not very pro-actively marketed to potential clients. In one branch only one health sector client could be identified. In most cases borrowers were not aware of the guarantee as according to CRDB the very knowledge of donor intervention could be an incentive for not repaying the loan. Therefore marketing the guarantee as such was not possible. Another reason that the health guarantee was not on top of the priority list of the branches is that CRDB has its business in rural areas primarily in the agricultural sector. The health sector was often not recognised as an important part of their portfolio and growth potential.

Moreover, the technical assistance seems to be provided to a limited number of branch staff and is not generally viewed as an instrument for improving the understanding of the health sector. Loan officers don't treat health sector borrowers differently from general SMEs in the loan approval process.

On the side of TA to borrowers, 40% of the loans on the program are trained clinics according to the technical assistance provider. We were not able to confirm this number during our field visit as the region we visited was not well represented in the TA portfolio.

Centenary Bank does not register and report the health sector as a separate sector, therefore, no information is available to assess the development of the health sector portfolio of CRDB. As mentioned earlier, only few first time borrowers were recruited. At the same time, for the sample of borrowers visited the size of the loans increased on average with 171% and the tenor increased by 127% (see table 16).

Although there is no objective data to prove that the health portfolio of CRDB has increased, our desk analysis and interviews with borrowers and branch managers therefore indicate that the health sector portfolio has grown over the years, primarily because the guarantee allowed CRDB to increase the size and the tenor of the loans for the existing clients. Reporting on the health sector is supposed to start with the implementation of a more robust IT system scheduled for the last quarter of 2016.

Outcome level

In the medium-term, the theory of change predicts that

- Centenary will continue lending to private sector health enterprises without the guarantee
- Centenary launches health specific loan products
- Borrowers' willingness to seek credit increases

Due to the early timing of the evaluation we are only able observe some of the above mentioned effects.

An important indirect effect of the guarantee is that borrowers are able to improve and expand their collateral position by the construction of new premises or expansion of the present ones, and in a few cases register/formalize their ownership of the new/expanded collateral. The increase of collateral improves the credit-worthiness of the borrower and thereby its ability to apply for new loans at CRDB or other banks. This should also allow CRDB to provide consecutive loans without a guarantee. Unfortunately, we have not observed such a case in our sample. For borrowers without registered collateral this expectation is less evident anyhow.

The absence of claims in the portfolio is an indication of a prudent and conservative lending policy for CRDB. At the same time, this is an indication that risks in the health sector are actually lower than CRDB expected beforehand. From the theory we would expect that CRDB will therefore adjust its risk-perception for this sector in the longer-term which would have an effect on, for example, its collateral requirements towards health sector borrowers in the absence of a guarantee. At this point in time however, there is no indication that the risk perception of CRDB towards health sector borrowers has actually decreased nor that the overall credit assessment of Centenary has been changed as a result. Neither is there a separate lending department for health, or health specific loan products.

Loan officers adhere to strict lending guidelines, which are the same across sectors (even those they are more familiar with) and mainly depend on the loan history of a borrower, the cash flow characteristics and the available collateral. Only with the guarantee being in place, the effect of higher lending can be sustained by temporarily increasing the value of the collateral. Internal guidelines pose strict limitations to the maximum amount and tenure of the loans in relation to available collateral which would come into effect again when the guarantee gets withdrawn. None of the borrowers we visited had received a non-guaranteed loan after the guaranteed loan, and loan officers confirmed that the higher standard collateral requirements will return when the guarantee is removed which result in borrowers being able to borrow less again.

3.4 Additionality

Additionality is an important criterion when evaluating the guarantee intervention. It asks the question whether the additional lending would have happened without the guarantee, through CRDB or any other (commercial) bank in Uganda.

For the evaluation team it was not possible to make an assessment on portfolio level by comparing the risk weighting of guaranteed loans in the health sector with loans without the guarantee. This data is not available in the bank and is not reported to the Central Bank.

To assess additionality we therefore need to understand the overall policy of Centenary Bank with respect to their lending operations. In principle Centenary considers the following criteria when approving loans to borrowers:

- Character of the borrower
- The cash flow of the operations of the borrowers should be sufficient to cover both the costs of the operations as well as the repayment of interest and principal of the loans.
- The collateral should be acceptable and sufficient to cover the borrowing.

In the Ugandan country context the most common form of collateral acceptable to banks is land and this can be distinguished in two forms: unregistered and registered land. The lack of an efficient registry makes verifying ownership and interests in land, difficult, costly and time consuming. Chattels can also be used as collateral however the majority has not been registered. To banks and

financial intermediaries collateral is an important consideration for lending as in event of default the bank has a fall back position. It is therefore critical that the creditor ascertain ownership of the collateral ex-ante.

CRDB can generally provide loans of up to 12 months in tenor against unregistered land. However the maximum loan amount varies from branch to branch with the highest limit of UGX 30m being in the cities, municipalities and town. Otherwise, loan regardless of estimated value on unregistered land are subject to the cash-flow calculation and the above branch and product limits, in that order of priority..

The guarantee can increase the maximum tenor up to 24 months and the maximum loan limit to 83.3% of collateral (security is 120% of loan amount).

For registered land, the tenor limit depends on both branch and product. Mortgages go up to 10 years and are the maximum. The maximum loan amount is generally equal to 80% forced sale value of registered collateral or less (125% collateral/loan ratio), depending on the cash flow of the borrower.

For registered collateral, the guarantee helps increase the loan amounts beyond the 80% of the forced sale value (as determined by the valuer) and increases the period. Unlike unregistered properties, there is no hard and fast rule on how it is applied but in all cases the cash flows must be able to pay the loan.

In table 16 we present a number of indicators for the borrowers in the sample such as the percentage increase in the loan amount and in the loan tenor for borrowers as well as the collateral/loan ratio.

As expected, the guarantee allows Centenary bank to provide larger loans and for longer tenors. For registered collateral, the average loan amounts was UGX32m and had a tenor of 30 months. For unregistered land, this is lower at UGX18m and 19 months respectively. The average increase in loan amount and tenor does not differ much between registered and unregistered land and is 171% and 127% respectively. In a number of cases we even note an increase in the loan amount by 200%.

In line with the above we conclude that the guarantee was additional.

Interestingly the average collateral requirements for registered securities are higher than for unregistered securities and in most cases above the 125% collateral/loan ratio which is used for loans without guarantees. Due to a lack of portfolio data we cannot

compare this with unguaranteed loans, but from the fact sheets of the loans and the interviews with bank staff it was not always fully clear why the guarantee was needed. In some cases we found that for well known borrowers (with earlier loans) collateral was more than 2 times the value of the assets and therefore the guarantee was not necessary in our opinion. In one case we noticed that the guarantee was used for a credit facility (of 4 months) for opening a letter of credit for the import of medical equipment (contract value USD 588K and a guarantee for USD 300K (maximum amount for guarantees). The L/C was paid by a donor agency from a grant. It is unclear why the guarantee was used. In practice this means that almost 10% of the guarantee threshold was used for a facility with a tenor of only four months and equipment that was donated.

With respect to the question on the presence of commercial alternatives, we found, – on the basis of the interviews and the fact sheets of the loan sample, that it is not very likely that other commercial banks were able to provide loans in the case of borrowers with unregistered collateral. In Uganda there are very few banks who have a similar branch network and that are active in the health sector. Ecobank's guarantee with USAID and Sida in the health sector has not yet succeeded in building a portfolio in health, partly because of the absence of a rural branches network. In some cases we noticed that borrowers in the sample had a relationship with other bank(s). However CRDB was the single bank that was able to serve borrowers with unregistered collateral with that type of loans. MFIs are able to provide loans to borrowers without strong collateral requirements as well; however the loans are much smaller and the interest rates are much higher than those of banks. Therefore the conclusion can be drawn that the loans provided by CRDB with the guarantee are indeed additional to these that are available in the local market.

Table 16: Utilisation of guarantee for sample of borrowers (part 1)

No.	Purpose	Amount	% in- crease	Tenor	% in- crease	Interest rate	Collat- eral	% Col- lateral	Reg. col- lateral	Earlier loans
1	Medical equipment	30	200%	24	200%	prime + 4	58	193%	R	6
2	Working capital business	35	175%	24	200%	prime + 6	30	86%	U	11
3.1	Drugs & medicine	40	114%	24	100%	prime + 6	273	683%	R	14
3.2	Completion staff quarters	50	125%	36	150%	prime + 4	273	546%	R	15
4.1	Equipment + pay-off loan	80	123%	60	167%	prime + 6	155	194%	R	8
4.2	Ambulance	35	350%	36	150%	prime + 6	155	443%	R	1
4.3	Hospital equipment	65	186%	24	67%	prime + 3	155	238%	R	3
5.1	Stock drug store	13	108%	24	100%	micro-auto: 29	20	154%	U	6
5.2	additional capital	15	115%	24	100%	micro-auto: 29	23	153%	U	7
6	Dental equipment	30	300%	24	100%	prime + 6	36	120%	R	4
7.1	Ultra-sound machine	12	n/a	12	n/a	micro-auto: 29	12	100%	U	2
7.2	building new clinic	15	125%	12	100%	micro-auto: 29	26	173%	U	3
8.1	WC drug shop	30	200%	24	200%	prime + 5	30	100%	R	2
8.2	WC drug shop	50	167%	24	100%	prime + 2	52	104%	R	3
9	Ultra-sound machine	15	n/a	18	n/a	micro-auto: 29	40	267%	U	0
10.1	Expansion clinic	8	160%	18	150%	micro-auto: 29	25	313%	U	8
10.2	Medical equipment	12	150%	18	100%	micro-auto: 29	25	208%	U	9
10.3	Furnish clinic	20	167%	18	100%	micro-auto: 29	25	125%	U	10
11.1	Construction clinic rooms	15	100%	12	67%	micro-auto: 29	80	533%	U	5
11.2	completion comm. Building	40	267%	24	200%	prime + 4	80	200%	U	6
11.3	Construction	50	125%	24	100%	prime + 4	40+80	240%	R + U	7
12	Completion medical centre	40	160%	24	80%	prime + 5	40	100%	R	7

Table 16: (part 2)

Average totals	Loan amount	% increase	Loan tenor	% increase	% Collateral
Average sample	32	171%	24	127%	240%
Average unregistered	18	152%	19	124%	210%
Average registered	45	166%	30	120%	259%

3.5 Impact

The theory of change lists three main impact effects:

1. Coverage of private sector health care enterprises increases (in rural areas)
2. Other banks increase lending to health sector enterprises
3. Financing terms for private health sector enterprises improve

As mentioned in the chapter risk and limitations as well as in the inception report, the scope of this evaluation does not allow us to make an in-depth assessment of the impact created by the guarantee intervention. This is both due to the limited time spent in the field as well as due to the timing of the evaluation. Three and a half years after the start of intervention we can at most recognise short-term effects on the output level and some medium term effects on outcome level and it will take more time for impact level effects to realise. This evaluation can therefore only indicate the direction of the impact. Our findings are based on a limited number of borrowers visited, mostly small clinics and pharmacies, as well as discussions with different stakeholders from the health sector value chain in Uganda.

From the sample of borrowers visited we found evidence that the guaranteed loans resulted in productive investments as intended. Loans were used for an expansion of private clinics, for example via the construction of additional rooms for in-patients, and made it possible for clinic owners to purchase a new type of medical equipment (for example an X-Ray, patient monitors), which was not available in the area until then. The conditions of the clinics varied greatly, businesses in the rural areas often had a very limited range of equipment and testing available. Services ranged from malaria and STI testing and treatment to family planning and child health counselling, basic laboratory services and minor surgery, and were

made available at very affordable rates, sometimes cheaper than at public hospitals. Private facilities are considered more efficient and higher quality than public health centres overall (even by the government) due to better services provision, for example the time doctors spend with patients explaining them the use of specific drugs. At public facilities, patients often wait for hours (even a whole day) until receiving treatment, and drugs are often not available.

Although private clinics are not free, and therefore by definition do not serve the poorest people in the value chain, we have found a strong poverty relevance. Some clinics we visited were located very remotely, far away from any public facility. Patients in need are treated even if they cannot repay immediately, sometimes flexible repayment options are found or payment is waived. Clinic owners named figures around 5–10% of defaulting patients, which confirms the poverty relevance.

From an impact perspective we can therefore conclude that the loans resulted in an improved quality and accessibility of healthcare in rural areas for most cases in the sample. We have also one case where the poverty relevance is less evident, however this was an exception to the general impression we got in the field.

We have found no case of irresponsible lending (in fact the bank is rather conservative in providing loans), and also no evidence for crowding out of public healthcare in rural areas or other harm done. We do recognise the need for supervision of private healthcare in the field of pricing, quality standards and supply of medicine. As this is not expected to be provided by the government currently, initiatives for self-regulation of the private sector should be supported.

In terms of market development we have not found evidence that other banks have ventured into the health sector due to the intervention, neither for improved credit terms for private healthcare enterprises due to increased competition. It is too early to make any conclusions in this regard.

3.6 Sustainability

Sustainability can be measured in a number of ways. An important aspect is the sustainability of the instrument from the point of view of Sida and USAID. Considering the very limited number of defaults up to now (2) and the fact that none of these defaults resulted into a claim under the guarantee, it can be concluded that the fee income will be sufficient to cover the costs arising from defaults, although it may be that defaults will increase in the coming years. This does not

consider the operational costs of Sida, nor USAID. It is difficult to say that because there were no claims under the guarantee for CRDB's health portfolio yet, the health sector in general performs better than other sectors. The data for that are presently too limited to make the sort of statements.

The guarantee has had a sustainable effect on the borrowers that benefitted from the guarantee in the following way. From the loan fact sheets of the sample of borrowers with registered collateral it was observed that turnover, value of the collateral as well as the assets increased considerably from one guaranteed loan application to another. With this improved creditworthiness borrowers will be able to borrow higher amounts in future applications, even without the guarantee being in place. In the case where borrowers are not able to present registered collateral to the bank, CRDB will be restricted in increasing the loan amounts as internal policy sets limits for that kind of lending and an increase of the value of unregistered collateral is more difficult to assess. In these cases it can be said that sustainability hinges on the presence of the guarantee. Without the guarantee the volume of lending will be limited again, and has to come to a large extent from the cash flow of the operations.

With respect to the knowledge and risk perception of CRDB we have only witnessed minor changes to date. Major changes in policy cannot be expected on the short term. The policy of CRDB as well as other banks with respect to SME-finance (including the health sector) is very much based on cash flow analysis and the value of registered collateral. One could expect that on a longer term with much more experience in this and other sectors the policy will be more relaxed and in particular collateral will be rated higher. However this is an expectation and so far there are no signs that this will actually result in a different policy of CRDB towards the health sector.

In the chapter on efficiency we already mentioned the lack of competition among banks in using the guarantee and the conservative (somewhat risk adverse) approach of CRDB. In principle we feel that the credit assessment of CRDB is professional and takes into account all relevant risk aspects. In some cases (e.g. with unregistered collateral) the guarantee has potentially helped CRDB to make a more realistic risk assessment of clients. The absence of competition and specific incentives as discussed in the chapter efficiency however prevent or at least delay a more risk taking approach which disadvantages sustainability.

4 CONCLUSIONS AND PRELIMINARY RECOMMENDATIONS

4.1 Conclusions

- The guarantee intervention very much fitted in the overall policy of Sida and the national government of Uganda with respect to the health sector. However it is important that do-no-harm principles such as crowding out of public health care are well taken into account, both during the assessment of the intervention as well as during the monitoring of the facility;
- Appointing USAID as the agent of the facility is a very good approach from an efficiency point of view and to reduces pressure on the execution capacity of Sida. USAID is well equipped to manage this sort of facilities and step in when unforeseen circumstances occur. It also allows Sida to leverage its resources to achieve larger coverage as the committed funds without the collaboration with USAID would have essentially only covered half the loans they will be able to cover within the collaboration. A disadvantage of this approach is that Sida is less involved in the operations and does not participate in discussing problems that may arise.
- CRDB is an excellent partner for executing the facility because of its rural outreach and focus on SMEs and micro-businesses. The health sector however is not a priority sector for CRDB and therefore the roll out of the instrument is limited;
- CRDB has been successful in implementing the guarantee for the health sector. In particular existing borrowers benefitted from the guarantee by enabling them to obtain bigger and longer term loans, and to expand their business and asset base.
- Refinancing is not very well defined in the contract of USAID/ Sida and CRDB. CRDB insists in almost all cases that earlier loans are repaid or will be repaid through the new facility. In principle there are arguments that favor this approach; however the agreement does not allow refinancing as a matter of principle.
- The additional 1% processing/acceptance fee paid by borrowers covers the utilization fee that CRDB has to pay to USAID and Sida. Moreover the fee is an additional assurance that the instrument is not competing with fully commercial facilities as these

costs are paid for by the borrower (without their knowledge however);

- The combination of providing a guarantee and technical assistance (for both CRDB as well as borrowers) is a very relevant and good approach. From the interviews we learned that this TA has been provided in a limited number of cases and did not lead to a different risk perception of the health sector as such;
- It is not possible to observe whether the health portfolio of CRDB has actually increased over the years (since the guarantee was available); however the field visit showed that in almost all cases the borrowers were able to obtain larger loans
- The lending strategy of CRDB towards health sector borrowers has so far only changed in the short term, with the guarantee being in place. The presumed advantage of the guarantee (60% extra collateral) however did not fully materialize;
- Although it is still early in the process, there is no indication that the guarantee has had an effect on the longer-term risk perception and lending policy of CRDB towards health sector borrowers. The policy of CRDB with respect to risk assessment continues for all sectors in the same way and in that respect health is not an exception. From a risk point of view, in terms of managing portfolios and avoiding defaults, this approach is healthy.
- An extensive impact measurement was not possible in the scope of this evaluation. The field visits revealed that borrowers were able to expand their operations by financing the expansion of construction of clinics and facilities and buying better equipment that improved the efficiency of their operations. A large number of borrowers that were visited mentioned that a substantial number of their clients were not able to pay the cost of their consultation or treatment sometimes up to 30%, resulting in writing off these fees. This is an indication that a large number of very poor rural people are served by these clinics and doctors;
- The guarantee is provided in only one format (being a 60% cover) and is therefore not able to introduce incentives for the bank (a higher coverage) to target specific target groups and clients. Moreover the present non-revolving nature of the guarantee is less efficient.

4.2 Recommendations

- In the approval phase when assessing the relevance of the intervention, make sure that a thorough analysis is made of the results of the guarantee in terms of do-no-harm principles. This increases ownership and prevents later discussions;
- At the contracting stage it should be clear and agreed upon how and when to use the guarantee. It is important that the guarantee provides comfort to banks to lend to borrowers for loans they cannot serve at their own risk. It should be clear for all loan officers by introducing guidelines how the guarantee can assist them in the lending operations and risk assessment;
- Find a clear division of tasks between the L&G department and the strategy owner for monitoring the guarantee. Consider outsourcing the monitoring to a local expert with knowledge of the financial and the health sector if capacity is restricted;
- Regularly control the use of the guarantee by loan officers at different branches, and check how the guarantee affects the credit approval process. Ask to include a motivation for using the guarantee in the credit approval documents;
- Consider introducing another health guarantee facility with another bank or microfinance institution to introduce competition in using the guarantee. Moreover introduce more incentives for the use of the guarantee. One could consider the introduction of a flexible (higher) guarantee percentage for specific groups (for instance start ups, innovations etc) or awarding banks that make good use of the facility by increasing the guarantee ceiling. In that respect a revolving threshold is recommended;
- Consider supporting the supervisory capacity of the public sector, or self-regulation initiatives of the private sector in health with TA to compensate for the lack of oversight. The umbrella organisation of private healthcare providers, the Uganda Health Federation (UHF), is very active in this area.

ANNEX 1: DESIGN AND SET-UP OF GUARANTEE & THEORY OF CHANGE

Process of design and Sida's appraisal

USAID initiated the Centenary Health guarantee intervention. In 2010 Sida and USAID had closed a Memorandum of Understanding for cooperation in the field of guarantees. In 2011, as a follow-up to an earlier cooperation in Bosnia (also part of this evaluation), the investment manager of USAID approached Sida in Kampala to participate in a guarantee intervention in the private health sector. For Sida, the concept of for-profit private healthcare was looked at critically as it had not undertaken any activities in this market earlier. After good discussions and a thorough market assessment of the gap in the public healthcare market, and a recommendation for a guarantee structure by USAID, Sida decided to get on board.

There was a conscious effort to find ways to work together and meet both parties' goals. USAID was the leading partner in the development of the guarantee, with core-responsibility for all the ground work including due diligence, selection of banks, drafting the term sheet and drafting the agreement. However all this was to be done in constructive dialogue with the L&G department of Sida. In April 2012, the USAID Credit Review Board (CRB) made a recommendation for approval which included a thorough risk assessment of the guarantee based on several risk factors including (a) country (b) lender (c) borrower and (c) transaction risk. USAID has a standardised model for these assessments.

Shortly after, in May 2012, Sida assessed the appraisal and approved participation in September 2012.

Two departments were involved in this process from the side of Sida. The strategy owner at the Embassy in Kampala was leading in the relevance assessment and approval of the guarantee, while the L&G department supported the Embassy from a technical/ financial perspective in consultation with EKN. On the basis of the market and risk assessment done by USAID and some general features of the guarantee, EKN gave a recommendation on the risk premium to Sida which was in line with the premium proposed by USAID.

There were discussions around an anti-abortion clause in the agreement which almost prevented the agreement from being signed, however in the end this conflict was resolved.

The guarantee agreement between Sida, USAID and Centenary Rural Development Bank was signed in September 2012.

Set-up of guarantee intervention

The guarantee was set-up in 2012 as a loan portfolio guarantee covering the health portfolio of CRDB, with 60% total guarantee jointly underwritten by USAID/Uganda and Sida.

The maximum authorised portfolio was set at the UGS equivalent of USD 3m and the guarantee had a total duration of seven years. Sida and USAID both guaranteed 30% of the principal amount.

TA was not included in the agreement, it was noted however that the success of the guarantee would hinge on the activities of existing TA programmes of USAID to borrowers in the field of business plan development and financial literacy.

Qualifying Borrowers/ projects

- Eligible borrowers are Ugandan privately-owned and operated micro, small, and medium enterprises in the health value chain; and Ugandan healthcare workers. Qualifying projects included loans that fall within the broad Ugandan private healthcare value-chain (including pharmaceutical wholesalers, retail dispensaries, service delivery franchisers, community health insurance providers, personal loans for housing and education for health care workers, and transportation investments by and for the use of healthcare providers as a business investment).
- To encourage portfolio diversification, as well as to ensure equitable geographic distribution of the guarantee's benefits, 30% of the guaranteed portfolio was restricted to lending outside of the Central region.
- The maximum cumulative principal amount made to one borrower was set at the UGS equivalent of USD 300,000.
- In order to ensure that there will be true risk sharing between the Guarantors and the Guaranteed Party, no qualifying loan should be eligible for coverage if more than 60% of total payments of principal on such Loan were guaranteed by a government or international donor organization, including USAID and Sida.
- The loan cannot be used for refinancing purposes, repayment or repurchase of an existing loans

Fees

The guarantee agreement set an origination fee of 1% of the sum of the Sida Guarantee Ceiling (USD 9,000) to be paid in USD directly to Sida. No subsidy was given by Sida on the fees in this case.

The utilization fee was set at 0.75 % per annum of the combined average outstanding principal amount that is guaranteed by the guarantors, payable semi-annually in Ugandan Shilling to USAID.

Claim procedures

USAID was assigned the role of agent for Sida, responsible for handling all communication with CRDB, monitoring as well as claim procedures.

CRDB has to register any loan to be placed under coverage in USAID's internet-based credit management system (CMS) or send in excel, a "certification of qualifying loan schedule" together with the relevant qualifying loan schedule to USAID. This loan schedule is to be regularly updated by CRDB and includes data on the borrower, type and terms of the loan, as well as disbursements, repayments and other potential changes in the conditions of the loan.

USAID is also the party to handle any claim procedures in case a borrower under coverage defaults on the loan.

After reasonable collection efforts against the defaulting party and no earlier than 90 days after request for full repayment, CRDB may make a claim. USAID endeavors to decide on the claim within 30 days, and in case of a positive decision pays the claim within 60 days of approval. The currency of guarantee payments is the Ugandan Shillings.

CRDB shall continue collection efforts against the defaulting borrower for so long as commercially reasonable and reimburse USAID and Sida on a pro-rata basis after deducting expenses for the collection effort.

In all cases, payment obligations to USAID and Sida rank at least pari-passu with other unsecured or subordinated debt of the defaulting borrower.

Reporting and communication

CRDB has to report monthly to USAID with an overview of the qualifying loan schedule for all loans under coverage. Additionally, CRDB is to submit annual audited financial statements to USAID. USAID and Sida reserve the right to conduct additional audits and reviews including on qualifying borrowers.

Reporting on development indicators by CRDB is voluntary and includes the following data on the guaranteed portfolio:

- Woman Owned
- First Time Borrower
- Number of employees
- Sector
- Average Revenue
- Average Assets

Monitoring

The Memorandum of Understanding (MoU) between Sida and USAID defines that USAID as the agent is responsible for managing the claim process, obtaining reports and record and terminating and suspending the co-guarantee agreement. To our knowledge there is no specific agreement for reporting under the Centenary Health guarantee.

At USAID, monitoring of the guarantee is a coordinated effort between the mission of USAID in Kampala and the Office of Development Credit (EGAT/DC) at USAID Headquarters in Washington. Financial monitoring of the guarantee is the task of the portfolio manager in Washington, while monitoring of development indicators rests with the mission. The monitoring of development indicators is not exhaustive and partly lies with the TA providers giving support to borrowers. A monitoring plan defines the roles and responsibilities of all stakeholders. The following monitoring plan exists for the CRDB health guarantee:

Table 17.

Action	Role	Timeline
Meet with Centenary Bank to discuss pipeline of clients	Mission Kampala	Quarterly
Semi-Annual Qualifying Loan Schedule Review (Credit Management System)	Mission Kampala	Every 6 months
Fact Sheet distributed to partners on utilization and areas for collaboration	Mission Kampala	Semi-Annual
Centenary Bank Training on product development	T.A. Providers (HIPS)	2012
Business Development Training for potential clients (including developing business plans, value chain linkages)	T.A. Providers (PHS)	Ongoing
Refer clients to Centenary Bank	T.A. Providers (PHS)	Ongoing

At Sida, the L&G department is responsible for financial monitoring and Sida has access to the CMS system of USAID. The Embassy is responsible for following up on development effects, however only receives (annual) reports from USAID on request. There is no formal agreement on how development monitoring takes place. Indicators on the impact level (provision of financial services in rural areas) are not collected to our knowledge [the monitoring plan of USAID defines that baseline data will be determined and collected by the mission in Kampala however Sida does not apparently benefit from this data].

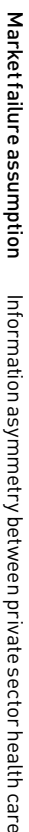
We understand that earlier there had been intensive contacts with the missions and quarterly reporting was provided, but communication is currently less frequent. There are no official meetings with USAID unless specifically required. From the data we collected and the interviews during the inception period it was not clear how issues such “*as crowding out public healthcare*” and “*do no harm*” were treated and incorporated in the monitoring system. These issues will be further addressed in the evaluation.

Theory of Change

Sida’s main goal of the intervention is to promote access to private healthcare in Uganda with special attention to rural areas, in alignment with the country and thematic strategy. The subordinated goals are to catalyse private capital for investments in the health sector. As TA was not part of the agreement and therefore out of the influence sphere of Sida, we included it as an assumption.

The following Theory of Change is reconstructed from policy and strategy documents of Sida and USAID, as well as interviews with both parties.

Demonstration effect



Political and macroeconomic stability

Loans are successful and meet demands borrowers
Borrowers manage to pay back loans on time
Health portfolio centenary is increasing

Centenary offers products suitable to the health sector and additional to the market and fulfill demand	Desk review (bank data)
Centenary has sufficient liquidity	Interviews Centenary and some others banks
OR Central Bank regulation allows for different risk weighting	Interviews Sida
There are profitable projects with good business plans and	Interviews USAID
	Interview Central Bank (provided their willingness to cooperate)

Literature review
Interviews banks
Interviews Sida
Interviews USAID
Interviews WHO Uganda
Interviews borrowers
Interviews ministries (counterpart Sida) & Min Health

- Desk research (bank data)
- Desk review (annual reports and CB data) (if available)
- Interviews banks
- Interviews borrowers & rejected borrowers (if possible)
- Interviews Sida
- Interviews USAID

Intervention paper Deutsche Bank / GCMC II Fund, Global

1 INTRODUCTION

1.1 Topic of the intervention report

The underlying intervention report contains the findings of the evaluation of the guarantee facility provided by Sida to the GCMC II microfinance fund, managed by Deutsche Bank. For this intervention, a team of evaluators consisting of Alwin de Haas and Rien Strootman visited New York, Washington DC and Boston from 13 till 15 April 2016.

Annex 1 contains a more detailed description of the guarantee facility, so here we will limit ourselves to a brief introduction to the topic. After the success of GCMC I, Deutsche Bank created a new fund with a layered structure with 80% senior notes and four more subordinated tranches. Sida provided a 50% guarantee on the subordinated (most risky) tranche of GCMC II. This tranche amounts to USD 3 million, and therefore the guaranteed amount is USD 1.5 million. The guarantee facility between GCMC II and Sida was signed in 2012.

The premise of GCMC II Fund is that “Microfinance is an important tool in the effort to improve the circumstances of the working poor in the developing world when it is practiced with a focus on the consumer [of the MFI]”. The term of the Fund is seven years, and GCMC II’s purpose is to target micro finance institutions (MFIs) that are implementing practices that reflect high standards of customer protection and customer service. GCMC II searches for MFIs that display the abovementioned characteristics, but also balance their social motivations with reasonably strong financial performance and sustainability. Finally, it searches for MFIs that have already, or will endorse the Smart Campaign’s Client Protection Principles¹⁶ and search for certification in the (near) future. GCMC II searches to also provide loans to Social

¹⁶ Smart Microfinance is being fully transparent in the pricing, terms and conditions of all financial products. Smart Microfinance is working with clients so they do not borrow more money than they can repay or use products that they do not need.

Enterprises¹⁷. The latter category can at maximum be 15% of the total fund size at a certain point in time.

GCMC II can use Local Currency loans, however in case loans are provided in local currency, GCMC II uses hedging mechanisms to reduce foreign currency and interest rate risks.

1.2 Approach to the intervention study

Prior to the visit to New York, stakeholders from Sida and other fund managers were interviewed through telephone interviews and visits in Stockholm. Documents obtained from Sida and Deutsche Bank related to this facility had been scrutinised. During the field visit, representatives of Deutsche Bank and two investors were interviewed.

During the interviews the evaluators used a questionnaire which was directly derived from the evaluation matrix attached here as annex 3.

1.3 Problems and limitations

In the inception report, some possible hurdles were identified. We repeat here those relevant for this intervention study, and the extent to which they actually materialised. Furthermore, we added some limitations that came to light during the evaluation phase:

Visiting the MFIs that received funding from GCMC II was not part of the evaluation. It was therefore difficult to draw conclusions on the outreach of GCMC II (development effects, impact, poverty reduction, etc).

The time between the visit to New York and writing this report was limited. As a result, only a few telephonic interviews with MFs have taken place at this point.

GCMC II is only halfway its lifespan. Therefore, it is not yet possible to draw conclusions about the cost-effectiveness of GCMC II, as claims (if any) will only be submitted at the end of the lifetime of the fund.

2 FINDINGS OF THE INTERVENTION STUDY

In this chapter, we will present the findings, grouped along the main OECD/DAC evaluation criteria: relevance, efficiency, additionality, effectiveness, sustainability and impact. The evaluation matrix and

¹⁷ Social enterprises are defined as social businesses in the fields of healthcare, education, energy or other areas that improve the quality of life.

the Theory-of-Change for the GCMC II guarantee facility are attached to this report. We will revisit the questions in the matrix, when presenting the findings, and in doing so verify the validity of the Theory-of-Change and its assumptions.

2.1 Relevance

The guarantee scheme should contribute both to private sector and financial sector development. Leverage of additional funding from private sources (catalyzing private funds) is an important objective in that respect.

According to the Sida appraisal document, and interviews with Deutsche Bank, the Microfinance Industry was experiencing headwinds during the period of the inception of GCMC II (2010/2011). This was mainly related to a number of cases of over-indebtedness in India, but also negative press in for example Nicaragua and Bosnia. At the same time Sida (and Deutsche Bank) continued to believe that the case for supporting the Microfinance Industry was a strong one, also given the poverty reduction focus of Sida. Although the headwinds were local, the fear of a spillover effect of the global financial crisis was also cause for concerns. Access to financial services (such as savings products, insurance and loans) gives people an ability to handle economic risk and the opportunity to invest in for example schooling, housing, and/or businesses to create opportunities to escape from poverty. In years prior to the intervention of Sida, Deutsche Bank had gained experience with the GCMC I Fund (whereby USAID provided a guarantee to the funders of the Fund).

With GCMC II, Deutsche Bank aimed to introduce both a new fund structure and also to explicitly support MFIs that balance social goals and financial responsibility, and also demonstrate customer care and product innovation. Therefore the aims of the GCMC II Fund fitted well with the focus of Sida (as described in the Swedish paper “Strategy for Global Thematic Development Corporation 2011 – 2014”). Furthermore, Deutsche Bank also proposed a Technical Assistance program as part of GCMC II and requested Sida to provide funding for this program. Although the decision by Sida to also support the TA program was taken at a later stage, the existence of a TA program, and the goal (promoting CPP) was definitely a positive element of the GCMC II proposition for SIDA.

Box: The Smart Campaign's Client Protection Principles

Smart Microfinance is fully transparent in the pricing, terms and conditions of the financial products. The goal is that clients of MFIs do not borrow more money than they can repay. Furthermore, Smart Microfinance introduces complaint systems and respectful collection practices. The following core principles are part of the core principles:

- Appropriate product design and delivery
- Prevention of over-indebtedness
- Transparency
- Responsible Pricing
- Fair and respectful treatment of clients
- Privacy of client data
- Mechanisms for complain resolution

In the appraisal documents, another goal mentioned was to attract private institutional investors to invest in (MFIs through intermediation of) the GCMC II fund. In order to provide comfort to these private investors, GCMC II would have a layered structure with several risk classes. A total of 20% subordinated tranches provide a safety cushion to the senior debt. Whereas these higher risk subordinated tranches would in principle also be open to private investors, limited uptake was expected due to the higher risk nature of these investments. Deutsche Bank itself would take the most junior (most risky) position in GCMC II the so-called “Subordinated Notes” (see figure in annex 1). The support provided by Sida effectively reduced the first loss position for Deutsche Bank in GCMC II by providing a 50% guarantee cover on Deutsche bank's position of USD 3m in total.

Deutsche Bank approached Sida with the idea to participate in the GCMC II structure. USAID had provided a guarantee for the GCMC I fund, but had indicated to Deutsche Bank that it would not be able to support the new GCMC II structure as well due to internal regulations¹⁸. As described above, the goals of GCMC II coincided with the goals of Sida, and therefore the decision was made by Sida to support the GCMC II Fund.

The process of designing the fund structure was an iterative process between, Deutsche Bank and possible investors. Some investors were unable to participate in a fund that would take equity

¹⁸ [check with Deutsche Bank/Sida] New internal regulations at USAID limiting the ability to support fund-like structures as opposed to individual beneficiaries.

participations, and therefore it was decided to create a 100% debt fund. During the start-up phase of GCMC II, the structure was modified several times, in response to investors' wishes. The structure with Sida guaranteeing the most risky tranche of GCMC II was however decided upon in an early stage and helped in setting up the remainder of GCMC II, allowing other investors to join. Without this guarantee, the GCMC II would not have been launched at all.

Compared to other funds already active in the MFI market, three elements are particularly of interest in GCMC II. First, the layered structure with different risk classes enabled investors to participate at their own comfort level, whereas most other funds have a "flat" structure (equal risks for all investors). Furthermore, the structure of a (subordinated) loan fund differed from most other funds active during 2012, whereby loans and equity were often combined. Finally, GCMC II distinguishes itself from other funds by providing loans to social enterprises, in addition to the MFI focus. This last element of GCMC II was introduced upon instigation of certain "bankers" within the Deutsche Bank organisation, as they came in contact with enterprises through other programs, and wanted to gain experience in financing enterprises directly themselves¹⁹. Deutsche Bank found that for SE's third party funding was practically only available through equity but not in the form of debt. The investors and Sida did not object as comfort was derived from the fact that the total amount of the (riskier) loans to social enterprises would be limited to 15% of GCMC II.

2.2 Efficiency

In the Theory of Change, the steps required to arrive from inputs, through activities, to outputs, can be grouped in 'design and development of the guarantee instrument', to 'providing debt to MFIs with high standards of CPP in line with fund investment criteria', 'investors subscribing for several tranches of GCMC II', and 'MFIs providing loans to their clients'. Outputs of this process are 'MFIs developing new products and serving more clients, with better Customer Protection Principles, other investors getting comfort from the risk positions Deutsche takes in the GCMC II Fund and more clients getting served by MFIs.

¹⁹ "Bankers" as opposed to GCMC II management professionals who are involved on a daily basis and reside within the Community Development Finance Group of Deutsche Bank.

One of the key assumptions was that there would be sufficient demand from MFIs for the debt instruments GCMC II can provide. In practice, GCMC II was able to find sufficient MFIs, and a reasonable geographical spread was achieved. It was noted by Deutsche Bank however, that although they made several attempts to lend to MFIs in Africa, the competition from mainly DFIs and NGOs was impossible to beat, as these parties were offering local currency loans at below-market rates.

MFIs were targeted by GCMC II in many different ways. In some cases, the MFI approached GCMC II for a loan directly, whereas other MFIs came to GCMC II from the (existing) network of Deutsche Bank. Also links between MFIs and GCMC II were established during sector conferences.

Another key assumption was that given the GCMC II structure and its subordination levels, commercial investors would be willing to invest substantially in GCMC II. In practice it still remained challenging to get commercial investors to subscribe for large tickets in GCMC II. The involvement of DFI's such as KfW and OPIC turned out to be crucial for a successful launch of GCMC II. While there were 21 investors in GCMC II at the outset, the cumulative share of the uptake of Deutsche Bank (Fund sponsor), OPIC and KfW across the different tranches amounted to just under 50% at launch of GCMC II. An overview of all investors is attached in annex 4.

Sida's appraisal process started in April 2012, and a month later EKN provided the calculation for the appropriate fee for the guarantee. In July 2012, the guarantee agreement was signed between Deutsche Bank and Sida. The essence of the guarantee is that Sida and Deutsche Bank share any potential losses on the USD 3 million Subordinated Notes (as mentioned: this is the most subordinated tranche) on an equal basis²⁰. From the side of Sida, the global department was involved, as well as the Loans & Guarantee department. In relation to the high (first loss) risk of guaranteeing the most subordinated tranche of the GCMC II, the guarantee premium as calculated by EKN (3%, see box below) can be considered low. This is especially true when taking into account that Sida subsidized the guarantee premium²¹.

²⁰ The maximum exposure of Sida therefore amounting to USD 1,5 million.

²¹ The premium was set at 3% of the guaranteed amount and later subsidized by 50%, reducing the effective cost to GCMC II to 1,5%.

EKN provided a premium/price related to the guarantee. The premium was determined on the basis of a risk assessment of fifty MFIs as well as the countries where these MFIs are located. The (expected) diversification of GCMC II resulted in a premium of 300 bps per annum.

In the (internal) decision making documents of Sida, it is further indicated that a subsidy can be used to minimise the costs of a guarantee in order to benefit the poor. In this case the premium was 50% subsidised by Sida with 150 bps reducing the “effective premium” down to 150 bps per annum.

In general, we see the logic behind using a subsidy. However, in this case the subsidy directly benefited Deutsche Bank, and did (in the best case) only indirectly influence the rates GCMC II charged to its clients (MFIs and Social Enterprises). In the opinion of the evaluators, the subsidy was not necessary and even the 300 bps as charged by EKN could be considered low, especially in light of the 8.5% IRR expectation of Deutsche Bank on the subordinated notes. Even accounting for the fact that the guarantee is an “unfunded” instrument requiring no upfront outlay this is a big difference. Assuming a funding rate of 1.55% (7 year USD swap in April 2012) Deutsche Bank could effectively expect a return of (850 bps – 150 bps – 155bps=) 545 bps on USD 1,500,000 subordinated loans, without bearing any risk.

The GCMC II fund was set-up as a closed-end fund, with a term of 7 years. GCMC II is currently half-way since inception. At this point in time, returns are falling behind plan in order to achieve the originally envisioned returns for the different tranches. In order to achieve planned returns, GCMC II needs to re-invest GCMC IIs that have been repaid by the MFIs²². This will however become more and more difficult since the remaining lifetime of GCMC II is limited, and it will therefore become harder to find suitable lending opportunities. In the last couple of years re-investing will become nearly impossible as this would imply providing loans with a maturity of less than 2 years.

Deutsche Bank runs its microfinance business through its Community Development Finance Group (CDFG), which is based in New York. Sida was offered a seat at the advisory committee of GCMC II, however Sida decided not to take such a position. The primary reason being that Sida felt that there should be a clear distinction between Sida’s role as “Program Manager” and the role of the Deutsche Bank team and the advisory committee who were managing and overseeing GCMC II on a day-to-day basis.

²² The cost of holding funds on deposit, the so called “negative carry” is relatively high due to low interest rates and the absolute return target of GCMC II.

Furthermore Sida assessed that the investment criteria of GCMC II and the capabilities of DEUTSCHE BANK were sufficient to ensure GCMC II was properly managed.

Every quarter²³, Deutsche Bank prepares a report to all its investors where an update is provided regarding funding side of GCMC II, the portfolio is reviewed, (financial) performance of the investees is discussed and the technical assistance updates are discussed. Furthermore, annually an investor meeting is held in Amsterdam²⁴ as GCMC II is formally based there. In practice all relevant decisions are taken by the professionals from CDFG in NY. Usually none of the investors are physically present at the investor meetings, however a number of investors participate through a telephone conference. Deutsche Bank indicated that the reporting requirements of Sida were no different compared to other investors in GCMC II. The reports as provided by Sida contain sufficient information regarding outreach, (financial) performance and general portfolio information.

2.3 Additionality

Two major ways of addressing additionality can be derived from the Theory of Change and the evaluation matrix:

- Would GCMC II have been set-up and operational without the guarantee?
- Would there be additional lending from MFIs to end-clients without GCMC II?

The guarantees are expected to result in increased finance to markets (financial additionality) and thereby socio-economic benefits (economic additionality). Based on the document review and the field visit, the evaluation team is able to provide an answer to the first question. In order to be able to answer the second question, a number of (telephone) interviews were conducted with beneficiaries (MFIs and SEs), other fund managers, Deutsche Bank and other investors in GCMC II. Furthermore, an analysis was made whereby the magnitude of the GCMC II loan was compared to the total funding attracted by the MFIs in the portfolio.

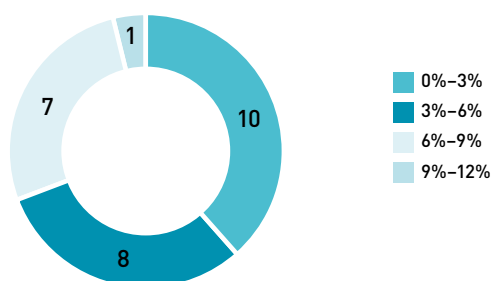
The question whether GCMC II would have been operational without the guarantee was answered based on interviews with Sida,

²³ Monthly update reports with less information are prepared as well.

²⁴ The reason why Amsterdam is chosen will be further analysed by the consultants.

Deutsche Bank, other fund managers and investors in GCMC II. Deutsche Bank indicated convincingly that in 2012, GCMC II would not have been launched if no guarantee had been provided, as the full USD 3 million position was considered to be too risky for Deutsche Bank²⁵. USAID already indicated not to be interested to participate in the follow-up GCMC fund (see section 1.2), and therefore the commitment of Sida has been instrumental in launching GCMC II. This was further underlined since Deutsche Bank was, based on Article 122a of the Capital Requirements Directive, obliged to participate in every tranche of GCMC II.

Figure 7: Magnitude of GCMC II loan compared to total debt by MFI



Based on the interviews mentioned on the previous page, it became abundantly clear that the subordinated debt provided to MFIs was additional. The tenors of the loans were relatively long (up to seven years) and MFI had no/limited alternatives to attract other types of subordinated debt.

The senior debt provided to the MFIs shows a more diffuse picture. During the time of the set-up of GCMC II (starting in the second half of 2010), liquidity in the market decreased somewhat, and there was a fear of a spillover effect from the global financial crisis to the MFI market. However, this spillover effect never materialized (especially not so when looking at Tier-1 MFIs), and liquidity in the market increased soon to higher than pre-crisis levels. Furthermore, given the limited magnitude of the GCMC II financing compared to total financing of these MFIs, the additionality for these loans is questionable.

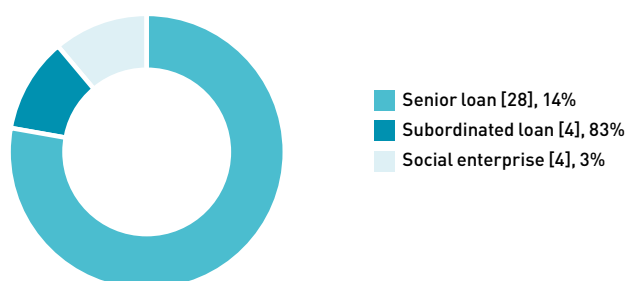
Based on a document review, the funding provided by Deutsche Bank to the social enterprises appeared to be additional. A lot of

²⁵ Although formally a debt position in GCMC II, the subordinated position could be based on the risk profile considered to be an equity position.

funds active in the SME market in Africa offer equity, and a fund offering debt is a rare phenomenon.

We note however, that these conclusions are merely based on literature, a study of the annual reports of the MFIs that received finance, MIX²⁶ and market knowledge, and only to a limited extent based on interviews with the beneficiaries of the financing.

Figure 8: Exposure of GCMC II by product (year end 2014)



2.4 Effectiveness and sustainability

In the Theory-of-change the effectiveness is pictured as the extent to which, through the increased lending by MFIs:

- Client protection principles become common practice at MFIs
- GCMC II provides senior, junior and subordinated loans to MFIs globally
- MFI clients have improved access to finance

During the time of writing this report, the annual report over 2015 was not yet available. Therefore, numbers in this section relate to year-end 2014 figures. At year-end 2014, 83% of the portfolio of GCMC II consisted of senior loans to MFIs, 14% of subordinated loans to MFIs and 3% of loans to social enterprises.

At year-end 2014, USD 91 million was disbursed (compared to a fund size of USD 100 million) to 35 borrowers. Indirectly, 1.2 million projects have been supported by GCMC II.

²⁶ <http://www.mixmarket.org/>

Figure 9: Number of loans provided in USD and Local Currency at year-end 2014

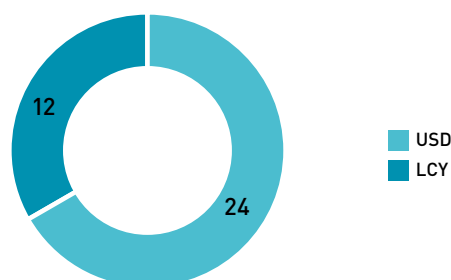
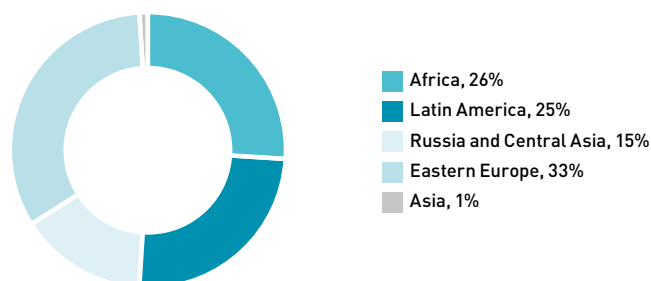


Figure 10: Geographical spread of the GCMC II at year-end 2014



The chosen structure of GCMC II with different risk classes enabled investors with different risk appetites to participate in the structure. On the levels of the subordinated debt, the mezzanine and the junior tranches, DFIs such as KfW and OPIC participated, whereas on the level of the senior notes more commercial investors participated. During one of the interviews with investors, it was indicated that without the chosen structure, and the creation of a low-risk “senior” tranche this investor would not have been able to participate in GCMC II, as the risk would have been assessed to be too high.

Technical assistance related to GCMC II

Sida provided SEK 5.5 million of Technical Assistance. In principle, the maximum amount per borrower is USD 50,000, and clients need to contribute 50% of the project costs. Technical Assistance could be used for:

- Certification for smart campaign
- Customer service related to social enterprises
- Knowledge-sharing initiatives between the borrowers of GCMC II.

In March 2015, 14 consortium II borrowers received TA funding, and most of the TA related to Smart Campaign certification.

It is at this moment premature to make an assessment of the cost-effectiveness of the guarantee and GCMC II until the end of the lifetime of GCMC II, as only by then the cost-effectiveness can be assessed. So far, performance has been good, with all loans being repaid.

2.5 Impact

In the Theory of Change, the following effect constituting impact are mentioned:

- CPP common practice within MFIs and
- Funds and commercial banks will take all risks on their own books in future funds
- Contribution to poverty reduction by improved access to finance

Within Deutsche Bank, the demonstration effect of GCMC II (and GCMC I) was clearly visible by the follow-up fund(s) that Deutsche initiated. One follow-up fund continued to focus on MFIs and Social enterprises, however used a completely different structure with only two investor classes (senior notes and a subordinated tranche, partly guaranteed by Sida) . Deutsche Bank is in the process of setting up a Fund that does not use a guarantee at all. A number of commercial investors that were part of GCMC II also invested in the follow-up funds and/or showed interest in such funds. Access to finance and poverty reduction is the most important motivation for applying the guarantee instrument for GCMC II. In the table below the number of clients reached at year-end 2014 are shown.

At year-end 2014, 7,264,380 borrowers were reached by the MFI's that received a loan from GCMC II. Of these borrowers, 3,320,772 borrowers (46%) were female borrowers.

The impact on poverty reduction is more difficult to assess. Compared to the full worldwide MFI market, the outreach of GCMC II is very limited. The MFI market is estimated to be around USD 8 billion by year-end 2015²⁷, and the GCMC II fund size of approximately USD 100 million is small in comparison to the full market. Furthermore, most of the MFIs in the portfolio of GCMC II can be classified as tier-1 MFIs. Tier-1 MFIs already have the widest range of funding possibilities, as these MFI have licenses and are considerably larger than Tier-2 and Tier-3 MFIs.

The evaluation also looked at the possibility of false competition and market distortion through the use of the guarantee instrument, as a negative effect. This effect appeared to be negligible. Loans

²⁷ <http://www.responsability.com/funding/data/docs/es/10427/Microfinance-Market-Outlook-2015-DE.pdf>

were provided at market conditions, providing no unwarranted advantages to MFIs. Furthermore, it became clear from the interviews with Deutsche Bank that competition in the sector is fierce, and since the expected returns are clear from the several investors, GCMC II could not offer loans below market rates.

3 CONCLUSIONS, LESSONS LEARNED AND PRELIMINARY RECOMMENDATIONS

3.1 Conclusions

The main conclusions drawn from this intervention study are:

- Back in 2012, GCMC II would not have been launched by Deutsche Bank in case no guarantee would have been provided by Sida.
- The pricing of the guarantee is not in line with the risk profile and expected return on the subordinated notes.
- The particular structure of the GCMC II, providing loans to MFIs and Social enterprises was relevant when GCMC II was set-up. The layered structure of GCMC II differed from other funds, that used a more “flat structure”.
- The magnitude of the loans compared to the total debt of the MFIs was fairly limited (mostly between 0% and 6%). The subordinated loans as provided by GCMC II can clearly be considered additional. The additionality of the senior loans is questionable.
- The chosen layered structure enabled commercial investors to participate in GCMC II that otherwise would not have been able to invest in GCMC II.
- Within Deutsche Bank, a demonstration effect was present, as new funds have been set-up, and currently a Fund is set up that does not use a guarantee at all.

3.2 Lessons learned

The main lesson learned in relation to the guarantee to GCMC II relates to the pricing element. When considering such guarantee in the future, compare the price of the guarantee with the expected return of the notes that are guaranteed. Although Sida might decide that a fully commercial return is not necessary, the price should not significantly deviate from market rates.

The use of a guarantee to enable the set-up of a fund is a good way to have a large outreach. Furthermore, the expected demonstration effect seems to take place, although this should be re-assessed in

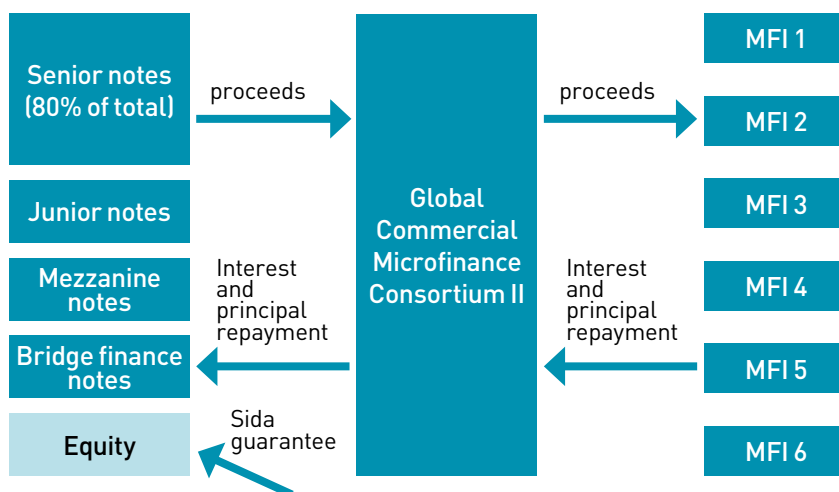
the future. Furthermore, Sida should make a clear assessment of the additionality of the used instrument (fund) including the target beneficiaries.

ANNEX 1: DESCRIPTION OF THE SIDA GUARANTEE FACILITY WITH DEUTSCHE BANK

Process of design and Sida's appraisal

The initiative for the Global Commercial Microfinance Consortium II (GCMC II) guarantee intervention came from Deutsche Bank in 2012. The Microfinance Industry was experiencing headwind, especially concerning a number of cases of over-indebtedness in India. However, at the same time Sida (and Deutsche Bank) continued to believe that the case for supporting the Microfinance Industry was a strong one, also given the poverty reduction focus of Sida. Access to financial services (such as savings products, insurance and loans) gives people an ability to handle economic risk and the opportunity to invest in for example schooling, housing, and/or businesses to create opportunities to escape from poverty. In years prior to the intervention of Sida, Deutsche Bank had gained experience with the GCMC I Fund. With GCMC II Deutsche Bank aimed to introduce both a new fund structure and also to explicitly support MFIs that balance social goals and financial responsibility, and also demonstrate customer care and product innovation. Therefore the aims of the GCMC II Fund fitted well with the focus of Sida (as described in the Swedish paper "Strategy for Global Thematic Development Corporation 2011 – 2014"). Furthermore Deutsche Bank also proposed a Technical Assistance program as part of GCMC II and requested Sida to provide funding for this program. Although the decision by Sida to also support the TA program was taken at a later stage, the existence of a TA program, and the goal (promoting CPP) was definitely a positive element of the GCMC II proposition for SIDA.

In the appraisal documents, another goal mentioned was to attract private investors to invest in the GCMC II fund. In order to provide comfort to these private investors, Deutsche itself would take the most junior (most risky) position in GCMC II (see figure below). The support provided by Sida effectively reduced the first loss position in GCMC II by providing a 50% guarantee on Deutsche Bank's position of USD 3 million in total.

Figure 11: Structure of the GCMC II Fund:

Related to the design as described above, the following tranche sizes and returns were targeted for GCMC II:

Table 18.

Investor class	Tranche size	Expected return	Term
Senior notes	USD 80m	IRR 4.3%	7 years
Junior notes	USD 10m	IRR 5.5%	7 years
Mezzanine notes	USD 3m	IRR 6.9%	7 years

The technical structuring novelty of the GCMC II was the fact that, at the outset, the equity investment²⁸ required in GCMC II would be a relatively low at 3%. The equity investment is the most junior position in a fund, and should something go wrong during the lifetime of GCMC II (for example MFIs not repaying their loans), the equity will be used first, before the capital of other investors is used. As lower capital requirements generally translate into more and/or cheaper financing to MFI's this was an important potential benefit of the structure. The low equity content was made possible by structuring the payments to investors in such a way that additional equity would be built up during the first two years of GCMC II. Deutsche Bank calls this a “self-generating equity cushion”. As GCMC II would pay senior and junior noteholders a lower

²⁸ The term “equity” is used by DEUTSCHE BANK as well as subordinated notes. In this inception report, we used equity.

coupon (interest) during these years the equity buffer (the amount not paid as coupons) would increase rapidly to the level required to protect equity holders. Excluding extremely negative scenario's (with big losses in first two years) this approach was expected to work well as the potential write-offs of the equity would only take place much later, at the time GCMC II would be closed down²⁹.

Compared to the GCMC II fund described above, the GCMC I had a different structure. In GCMC I the senior noteholders benefited from a guarantee by USAID and the first loss position of GCMC II was covered by a grant from DFID. In GCMC II the senior investors had to derive all their comfort from the subordinated / equity positions coming after them in the so-called "waterfall" (i.e. first the senior noteholders are fully paid, then the Junior noteholders, then the Mezzanine noteholders, then the bridge financing providers – replaced by the self-generated equity cushion after two years – and finally the USD 3m funded by Deutsche Bank). The SIDA guarantee effectively halved Deutsche Bank exposure on the equity to USD 1.5m which played an important role in getting Deutsche Bank's investment in GCMC II approved. Deutsche Bank also invested in the Mezzanine notes (USD 150k), the Junior notes (USD 500k) and in the Senior notes (USD 8.5m).

Sida considered that a guarantee was the most efficient instrument at the time. Sida felt that providing a grant was not an alternative since Deutsche Bank is a private commercially oriented company and providing a grant might lead to market distortion.

Deutsche Bank runs its microfinance business through its Community Development Finance Group (CDFG), which is based in New York. Sida was offered a seat at the advisory committee of GCMC II, however Sida decided not to take such a position. The primary reason being that Sida felt that there should be a clear distinction between Sida's role as "Program Manager" and the role of the Deutsche Bank team and the advisory committee who were managing and overseeing GCMC II on a day-to-day basis. Furthermore Sida assessed that the investment criteria of GCMC II and the capabilities of Deutsche Bank were sufficient to ensure GCMC II was properly run.

²⁹ During this two year period three investors temporarily bridge-financed this equity in order to ensure appropriate subordination levels for the other investors in GCMC II. After two years the build-up of the equity cushion was sufficient to repay the equity bridge financing

The appraisal process started in April 2012, and a month later EKN provided the calculation for the appropriate fee for the guarantee. In July 2012, the guarantee agreement was signed between Deutsche Bank and Sida. From the side of Sida, the global department was involved, as well as the L&G department.

Set-up of guarantee intervention

Table 19.

Implementing partner	Beneficiary	Value of guarantee	Years	Type of risks guaranteed	Risk sharing	Origination fee	Utilisation fee	Security	Agent
Sida	Deutsche Bank	USD 3m	7	50% equity part of fund	Yes, shared first loss position with Deutsche Bank	n.a.	3% p.a. (of which 1.5% subsidized)	Pari-passu	Deutsche Bank

As described in the figure above, the equity, which was 50% guaranteed by Sida formed the most junior position in the waterfall. Deutsche Bank subscribed for USD 3 million in equity, hence the exposure of Sida equalled USD 1.5 million.

Payment under the guarantee is made if GCMC II fails to make a full principal repayment to Deutsche Bank after GCMC II has closed. The Sida guarantee ensures a 50% risk share in any realised principal losses on the equity.

TA was initially not included in the agreement, however a year later a TA program was also signed relating to the CPP (“smart campaign”) of beneficiaries of GCMC II.

Qualifying Borrowers/ projects of GCMC II

The GCMC II Fund targets loans to MFIs as well as loans to social enterprises. Below, the main characteristics of both categories are summarized:

Type 1: MFI Investments

GCMC II seeks to provide flexible financing to assist MFIs in meeting their long-term funding needs, with the additional goal of offering funding that can support product innovation, particularly in the area of housing microfinance.

The details of the products that GCMC II intends to offer to MFIs are as follows:

- Type of Funding: Senior or Subordinated debt
- Term: Up to seven years

- Amount: Subject to Article VI(A), up to US USD5m or 5% of the total portfolio (following the second anniversary of GCMC II's closing) and prior to the second anniversary, 5% of total investors' commitments at final closing.
- Currency: USD, local currency via swaps
- Rate: Market-based, varying by product and tenor
- Product Use: On-lending for general portfolio or directed to housing portfolio
- Technical Assistance: Where MFIs receive loans to direct toward housing microfinance products, they may also receive technical assistance from a housing microfinance expert consultant. The investment Committee of the GCMC II fund will need to approve the use of TA related to housing microfinance.

Subordinate loans to MFIs are limited to less than 15% of the loan portfolio, in aggregate, following the second anniversary of the Initial Closing Date.

Type 2: Social Enterprises

GCMC II will offer short term, secured loans directly to Social Enterprises that seek to improve the quality of life at the Bottom of the Pyramid. The details of the products that GCMC II intends to offer to Social Enterprises are as follows:

- Type of Funding: Senior debt
- Term: 2-3 years, renewable [originally envisioned to be max 1 year ?]
- Maximum amount per commitment: Subject to Article VI(A), up to US USD 5m or 5% of the total portfolio (following the second anniversary of the Initial Closing Date) and prior to the second anniversary, 5% of total investors' commitments at final closing.
- Currency: USD, local currency via swaps
- Rate: Market-based, varying by product and tenor

Aggregate loans to social enterprises are not to exceed 15% of the entire investment portfolio, following the second anniversary of the closing date of GCMC II.

Type 3: Eligible Investments

The Eligible Investments represent the portion of the Investments of GCMC II that are temporarily placed or deposited with international investment grade banks. The list of these financial institutions ("Eligible Financial Institutions") with which GCMC II can place or deposit its excess cash liquidities shall be approved by the Advisory Committee of the GCMC II fund.

Fees

EKN determined that the guarantee fee should amount to 3% of the amount guaranteed to Deutsche Bank. Following negotiations, Sida decided to subsidize the fee by 50%. Therefore, the guarantee fee effectively amounts to 1.5% of USD 1,500,000 annually.

Furthermore, Sida was paid for negotiating and preparing the term sheet (SEK 300k).

Claim procedures

In case GCMC II fails to fully repay the principal amount of the equity (USD 3m) when they become due upon closure of GCMC II after seven years, Deutsche Bank (as fund manager) can make a claim with Sida under the guarantee. As mentioned the guarantee is effectively a loss sharing mechanism, covering 50% of a loss suffered by Deutsche Bank on the equity. Sida will make an assessment of the claim, and if it is found genuine, reimburse DEUTSCHE BANK (pro-rata) for 50% of the total losses suffered.

Reporting and communication

Deutsche Bank provides Sida annually with an audited annual report. In addition, Sida is also entitled to receive a quarterly unaudited financial report in addition to the quarterly activity report of GCMC II. However, time-wise, there is very limited capacity within Sida's Loans & Guarantees team to closely monitor GCMC's financial performance on a quarterly basis.

Furthermore, EKN makes a semi-annual risk assessment based on the information Sida provides. Finally, an evaluation report of development impacts and the activities needs to be submitted in 2020.

Monitoring

At Sida, the L&G department is responsible for financial monitoring. The global department is responsible for following up on development effects.

Theory of Change

Sida's main goals of the intervention is to improve access to appropriate financial services to the poor by promote commercial investors to participate in a fund that invests in MFIs and social enterprises. A Technical Assistance programme was set-up later to facilitate a proper implementation of CPPs. Therefore, this is included in the ToC below.

The following Theory of Change is reconstructed from policy and strategy documents of Sida and USAID, as well as interviews.

Figure 12.

Theory of Change – Deutsche Bank Global Commercial Microfinance Consortium II

Demonstration effect

Impact
(long-term)

Contribution to the solution regarding overindebtedness

Funds of commercial banks will take all risks on their own books in future funds

Contribution to poverty reduction by improved access to finance

Outcome
(short-medium term)

CPP become common practice at MFIs

GCMC II provides junior and subordinated loans to MFIs globally

Improved access to finance for MFI clients

Financial additionality

Economic additionality

Output
(short-term)

MFIs develop new products and serve more clients, as well as better CPP

GCMC II takes junior position and this gives comfort to other (institutional) investors

MFIs provide loans and therefore access to financial services increase

Activities

Debit is provided to MFIs with high standards of CPPs in line with fund investment criteria

Deutsche Bank subscribes for subordinated notes in Microfinance Fund

MFIs provide loans to their clients

Input

Guarantee design & development

50% guarantee SIDA

Subsidy 50% of guarantee fee (1.5%)

Subsidy CPP for MFIs

7 year SEK 14 million max.

General assumptions

Political and macroeconomic stability

Methods

(see also evaluation matrix)

Microfinance is an important tool to improve living circumstances

Private investors remain interested in sector

Private investors have sufficient resources

Access to finance leads to poverty reduction

Projects are successful

Investors earn the returns they expect

Interviews MFIs
Interviews DB
Interviews investors
Interviews SidaDeutsche Bank offers (subordinated) debt to MFIs
Investors are interested in the returns offered by the Fund
Sufficient MFIs with need for debt are available
Interest rates paid by MFIs are sufficiently high
MFIs are interestedInterviews MFIs
Interviews DB
Interviews investors
Interviews Sida
Desk research

Relevance

Effectiveness

Impact

Efficiency

Market failure assumption

Deutsche Bank would not assume the full risk of the most junior position in the Fund

ANNEX 2: INVESTORS IN GCMC II

Table 20.

CONSORTIUM II NOTEISSUANCE	Senior	Junior	Mezz	Bridge (Repaid)	Sub	Total
AXA France VIE	4,000,000	–	1,000,000	–	–	5,000,000
AXA Lebensversicherung AG	4,750,000	–	–	–	–	4,750,000
AXA Versicherung AG	4,750,000	–	–	–	–	4,750,000
AXA Krankenversi- cherung AG	4,750,000	–	–	–	–	4,750,000
Calvert Social Investment Foundation, Inc.	–	–	–	–	–	–
CNP Assurances	8,000,000	–	–	–	–	8,000,000
Co-operative Bank PLC	5,000,000	–	–	–	–	5,000,000
Deutsche Bank AG (Cayman Islands Branch)	8,500,000	500,000	150,000	–	3,000,000	12,150,000
AJK Trust	175,000	–	–	–	–	175,000
NAK Trust	175,000	–	–	–	–	175,000
Développement International Desjardins	–	–	1,000,000	–	–	1,000,000
Everence Community Investment Inc.	–	–	–	–	–	–
Money In Motion, LLC	250,000	–	–	–	–	250,000
Kreditanstalt für Wiederaufbau	9,250,000	5,000,000	750,000	–	–	15,000,000
Left Hand Foundation	400,000	–	100,000	–	–	500,000
Monarch Community Fund, LLC	–	–	–	–	–	–
OPIC	15,500,000	4,500,000	–	–	–	20,000,000
State Street Foundation, Inc.	3,000,000	–	–	–	–	3,000,000
Storebrand Livsfor- sikring AS	4,750,000	–	–	–	–	4,750,000
SPP Livförsäkring AB	4,750,000	–	–	–	–	4,750,000
Colorado Seminary	250,000	–	–	–	–	250,000
	78,250,000	10,000,000	3,000,000	4,000,000	3,000,000	98,250,000

Case Studies for Evaluation report

The overall objective of this report is to deepen Sida's knowledge about the guarantee instrument as a tool for market development and poverty reduction. The focus of the evaluation is on lessons learned from four specific interventions, as to the extent to which the guarantee instrument actually manages to bring about the expected and desired changes, possible hurdles met, either unforeseen problems or possible misconceptions in the design, and ultimately on ways to improve the working of the instrument in the future.

The evaluation was carried out by Carnegie Consult with the support of associates and local consultants. Consultants involved in the assignment include Hans Slegtenhorst, Mart Nugteren, Alwin de Haas, Rien Strootman, Marie Heydenreich, Paulo Luswata, Nino Serdarevic, Anders Grettve and Bart Schaap. Anders Berlin and Camilla Rubensson from the Unit for Loans and Guarantees of Sida and Sofia Ericsson from the Unit for Planning, Monitoring and Evaluation joined two field missions as observers.



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