ACGF - Afghan Credit Guarantee Foundation

Unlocking Finance for Growth in Afghanistan
1.2% average historical net loss p.a.

5,100 Cumulative number of guaranteed loans disbursed

219 m Cumulative amount of guaranteed loans disbursed (USD)

10,200 Cumulative number of jobs created

57,000 Cumulative number of jobs retained

45% of outstanding loans to SMEs in financial sector backed by ACGF guarantee (approx.)

24 m outstanding guaranteed loan portfolio (USD)

All data as per the end of January 2019
Credit guarantees and Technical Assistance (TA) to Partner Financial Institutions (PFIs) provided by ACGF demonstrate a positive impact on improving access to finance for small and medium-sized enterprises (SMEs) in Afghanistan. The success achieved during the last 15 years has paved the way for further upscaling of ACGF's activities ultimately leading to a larger, inclusive and more stable SME sector.

Lack of access to finance represents a major impediment in economic welfare and growth particularly for underserved groups and SMEs. The inability to access finance is a common issue due to a range of diverse factors and Afghanistan has been suffering from this market failure acutely.

Since 2004, ACGF - Afghan Credit Guarantee Foundation and its institutional predecessor, the Credit Guarantee Facility for Afghanistan (CGF-A) have sought to bridge the supply-demand gap for SMEs' access to finance by providing credit guarantees and TA for capacity building of Afghan PFIs. CGF-A was founded initially through financing from the German Federal Ministry for Economic Cooperation and Development (BMZ), with further funding from United States Agency for International Development (USAID) and implemented by DEG - Deutsche Investitions- und Entwicklungsgesellschaft. Following a decade of successful performance, ACGF was established by BMZ and DEG in 2014 as a German Charity Foundation. BMZ, DEG and the Ministry of Finance of Afghanistan are represented in ACGF's Board of Trustees. Additionally, since 2017, ACGF has been receiving funding from the Afghan Ministry of Finance under the framework of the Access to Finance Project funded by the World Bank.

On the ground, SME Client Support Afghanistan LLC (SCSA), ACGF's local subsidiary in Kabul and Mazar-i-Sharif, provides ACGF with valuable consulting in guarantee process and supports in ACGF’s TA activities.

ACGF strives to create a wide-reaching and sustainable impact on the Afghan SME-landscape by improving access to finance, creating jobs, developing skills and improving the country's overall financial sector.
Credit Guarantees: Promoting SME Sector Growth

What Is a Credit Guarantee?

Credit guarantees have a significant role in mobilizing finance and serve as a core instrument enabling an increase in the credit lending appetite of financial institutions via mitigating lending risks and absorbing a portion of losses incurred by defaults. Credit guarantees typically strive to stimulate lending to particular sectors and underserved borrowers operating within challenging contexts, such as SMEs.

This instrument is utilized as a means to extend the availability of financing for SMEs which would otherwise be unbankable. Credit guarantees alleviate constraints typically faced by SME borrowers in accessing finance such as:

- Lack of sufficient collateral
- Perceived high risk by the lender of the borrower’s repayment capacity
- Mismatch between loan conditions and repayment capacity of the borrower
- Insufficient loan amount to fully realize borrower’s growth potential
- Lack of proper accounting
- Lack of credit history

Why Are Credit Guarantees Vital for Private Sector Growth?

Lack of access to adequate finance is one of the most significant constraints faced by SMEs worldwide. According to the World Bank, an estimated 50-70% of SMEs in emerging markets¹ (and even higher in Afghanistan) are either not funded or underfunded by the formal financial sector. On the other hand, SMEs are critical drivers of economic growth of a country as they provide jobs, foster exports, production, innovation, diversification, geographic dispersion and most importantly, opportunities for minorities such as women and youth entrepreneurs. Despite the crucial role of SMEs, the credit market for SMEs is characterized by several market failures and imperfections. These market failures are information asymmetries and resulting adverse selection, both of which cause high levels of exclusion by financial institutions. These failures can be effectively remedied through credit guarantees.

Barriers to Unlocking Finance and SME Competitiveness

Crucial obstacles in the Afghan financial sector need to be overcome in order to promote and stimulate long-term, sustainable economic growth in the Afghan private sector and the national economy.

Afghan SME owners report that existing credit conditions do not sufficiently serve their needs. They state that lack of access to finance is a critical investment constraint which leads them to seek informal lending options. These credit supply-side challenges associated with the country’s fragile formal financial system and market environment are the crucial obstacles that SMEs have been facing.

ACGF is engaged in Afghanistan’s high risk financial market to alleviate these supply-side challenges through following mechanisms:

<table>
<thead>
<tr>
<th>Challenges</th>
<th>ACGF Effects</th>
</tr>
</thead>
<tbody>
<tr>
<td>Objective &amp; subjective risk perception</td>
<td>→ Provide risk mitigation and increase financial institutions’ (FIs) willingness to lend</td>
</tr>
<tr>
<td>Lack of collateral</td>
<td>→ Act as substitute for borrower’s insufficient collateral and render bankable borrowers</td>
</tr>
<tr>
<td>Developing judicial &amp; regulatory system</td>
<td>→ Early and complete claim pay-outs provide liquidity and portfolio cleansing</td>
</tr>
<tr>
<td>Dominant focus on micro and corporate lending</td>
<td>→ Facilitate and promote SME lending, broadening the width of the overall financial sector</td>
</tr>
<tr>
<td>Liquidity surplus of FIs</td>
<td>→ Mobilize otherwise underutilized financial sector capital</td>
</tr>
<tr>
<td>Limited innovation</td>
<td>→ Transfer of knowledge and catalyzing innovation by ACGF through Technical Assistance (TA) projects</td>
</tr>
<tr>
<td>Nascent utilization of innovation among FIs</td>
<td>→ Incentivize new loan product creation, provide competitive advantage and induce competition</td>
</tr>
<tr>
<td>High cost of risk and capital</td>
<td>→ The Afghan Central Bank’s (Da Afghanistan Bank) recognition of guarantees provide incentives for provisioning and capital adequacy</td>
</tr>
</tbody>
</table>
In 2004, the Credit Guarantee Facility for Afghanistan (CGF-A), the predecessor of ACGF, was established. Based on the success of the facility, the donors (see page 14) decided to pursue an incorporation strategy in order to facilitate its own institutional sustainability. With the supervision of DEG the transfer took place in 2014, and ACGF officially started its operations in January 2015. In March 2015, ACGF’s Afghan subsidiary SCSA was established. The know-how, expertise and excellent reputation were ensured by continuing to employ CGF-A staff and management as well as hiring further experts.

ACGF continues to grow by further expanding its activities with existing and new Partner Financial Institutions (PFIs) and undertaking new impactful Technical Assistance (TA) projects. This growth becomes possible based on the support provided by ACGF’s stakeholders, including DEG, BMZ, the Ministry of Finance of Afghanistan, the World Bank, the Da Afghanistan Bank and others.

### Start-up Facility
ACGF is exploring how best to support and promote the next generation of emerging businesses through facilitating access to finance via additional services and specially tailored credit guarantees for new entrepreneurs.

### FinTech
In 2018, ACGF conducted a study to identify how FinTech can enhance SME lending as well as PFIs’ outreach to underserved segments in Afghanistan. ACGF plans to support implementation and operationalization of these findings among underserved borrowers and PFIs.

### Renewable Energy
In order to ease energy shortages and enable access to alternative energy sources, ACGF is in the process of creating tailored credit guarantees to support financing of private loans for solar energy generating panels.

### Timeline and Outlook

<table>
<thead>
<tr>
<th>Year</th>
<th>Event</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>The Credit Guarantee Facility for Afghanistan (CGF-A) establishment</td>
</tr>
<tr>
<td>2005</td>
<td>Start of cooperation with FMFB</td>
</tr>
<tr>
<td>2006</td>
<td>Start of cooperation with AIB</td>
</tr>
<tr>
<td>2004 - Ongoing</td>
<td>SME lending - establishing SME units with 6 Financial Institutions</td>
</tr>
<tr>
<td>2012</td>
<td>Start of cooperation with Ghazanfar</td>
</tr>
<tr>
<td>2013</td>
<td>USD 100m loans guaranteed (cumulative)</td>
</tr>
<tr>
<td>2014</td>
<td>ACGF establishment</td>
</tr>
<tr>
<td>2015</td>
<td>SCSA establishment</td>
</tr>
<tr>
<td>2017</td>
<td>Scaling up projects with MISFA</td>
</tr>
<tr>
<td>2017 - 2019</td>
<td>Funding under the World Bank’s Access to Finance Project through Ministry of Finance of Afghanistan</td>
</tr>
<tr>
<td>2018</td>
<td>Start of cooperation with OXUS</td>
</tr>
<tr>
<td>2018</td>
<td>USD 200m loans guaranteed (cumulative)</td>
</tr>
<tr>
<td>2019/2020</td>
<td>Start-up facility</td>
</tr>
<tr>
<td>2019</td>
<td>Ongoing/future Partnership with 2 further PFIs to be established by 2020</td>
</tr>
<tr>
<td>2020</td>
<td>Future Renewable energy projects</td>
</tr>
<tr>
<td>2017 - present</td>
<td>45% of outstanding loans to SMEs in financial sector backed by ACGF guarantee</td>
</tr>
</tbody>
</table>
ACGF & SCSA: Success of International Cooperation

International Know-How: ACGF

ACGF’s head office is based in Cologne, Germany. ACGF has lean staffing with headcount of 8 experts, who are responsible for supervising guarantee operations, issuance of guarantees, coordinating TA and deciding on the overall strategy of ACGF. International know-how ensures adherence to best practices and enables ACGF to be a catalyst for innovation in Afghanistan.

Afghan Expertise: SCSA

SME Client Support Afghanistan LLC (SCSA) is the Afghan-based subsidiary of ACGF. SCSA is a financial consulting company working across all regions of Afghanistan, with headquarter in Kabul and an office in Mazar-i-Sharif.

SCSA consists of an experienced team of over 15 professional finance and technical specialists who contribute ongoing ancillary services to ACGF. SCSA’s professionalism and experience became one of the key factors for ACGF’s success and its positive recognition in the market.
Credit Guarantee Operations

How Credit Guarantees Work?

ACGF’s credit guarantees are provided to PFIs under the terms of mutually agreed framework agreements. ACGF strongly relies on the operations of its PFIs and seeks to minimize duplication of processes, while in general still carrying out independent appraisals at guarantee origination, claim issuance and refunds stages. ACGF’s guarantees are partial guarantees with a standard coverage of 72%, which is adjusted depending on the loan amount or type of borrower (for example, higher coverage for start-ups). Currently ACGF issues individual credit guarantees, however, blanket and portfolio guarantees are being considered.

After issuance of credit guarantees, ACGF supported by SCSA closely monitors the guarantee portfolio based on the monthly PFI reports. Based on these reports, when it is necessary, inquiries and joint reviews of delinquent cases are carried out. After 180 days of delinquency, eligible claims submitted to ACGF are paid out without the requirement of exhausting all legal means by the respective PFI. Subsequently, in case of partial or full repayment by the borrower of already claimed guarantees, the PFIs and ACGF share the refunds in alignment with a predefined quota.

Transparent rules, clear communication and efficiency across all stages of the credit guarantee cycle enable ACGF to achieve a good working cooperation with its PFIs.
Technical Assistance to the Afghan Financial Sector

Strengthening Capacity

Developing capacity of institutions and providing Technical Assistance (TA) to stakeholders within the Afghan financial sector such as financial institutions (FIs), regulatory and government institutions create positive impact and promote overall economic stability in Afghanistan.

ACGF uses TA complementary to credit guarantees with the aim of nurturing new partnerships and improving the existing ones. The TA services provided by ACGF and SCSA are dedicated to strengthen the capacity of its Partner Financial Institutions (PFIs) for SME lending with the long-term mission of stabilizing the Afghan financial sector, strengthening the growth of SMEs, improving environmental and social business standards and ultimately driving job creation in Afghanistan.

Technical Assistance to Afghan Financial Institutions

Together with SCSA and external consultants, ACGF works directly with managers and credit officers of PFIs. ACGF and SCSA professionals actively participate in strategic consulting on all aspects of how PFIs engage in SME lending and credit risk management in line with international best practices. Emphasis is put on consulting and developing tailored approaches associated with mitigating SME credit risk, effective loan portfolio management and credit structuring to ensure that the viability of SME loan applicants is efficiently assessed. Consequently, loans are appropriately structured to properly match the needs of SME borrowers.

Expertise in the Afghan Context

In light of ACGF’s more than 15 years of experience in operating within Afghanistan, implementing tailored TA approaches within its operations has been found to be a key component in paving the way for assessing and minimizing SME credit risk and enhancement of SME lending. In this framework, TA plays a critical role in enabling innovation in SME lending products and processes of PFIs and stimulating outreach to new groups of borrowers such as women owned-businesses and businesses seeking finance for sustainable energy sources.
In 2017, ACGF covered 45% of SME loans in Afghanistan. ACGF’s loans have reached different regions of the country, helping the development of the regional economy, as well as the national.
External Evaluation of ACGF

Evaluation of ACGF’s Performance and Effects on Afghanistan

In 2018, an independent evaluation with the focus on measurement and assessment of ACGF’s impact was conducted by Steward Redqueen, one of the leading international evaluation experts. The report was based on intensive research and consultations with 26 relevant stakeholders.

The findings of the evaluation revealed that ACGF, as an intervention, can be considered a systematic actor in Afghanistan’s SME finance market due to its long-running track record, stable performance and high impact in the country’s challenging financial landscape.

The Overall Assessment Compiled the Following Key Results:

- **Contribution to major development impact as a highly relevant market intervention which effectively supports in addressing the major issue of a lack of financing for SMEs.**
  - The evaluation concluded that by combining guarantees with ongoing capacity building and specific Technical Assistance (TA), ACGF has been able to alleviate these lending risk related concerns for PFIs and to effectively facilitate SME lending.

- **Achievement of stable operations and portfolio quality throughout the history of its operations despite a highly fragile and risky lending environment.**
  - ACGF’s involvement in SME sector has produced a marked improvement in job security growth, revenue of SMEs and incomes of the individuals which consequently left an impact on a more stable banking system, while maintaining a good portfolio quality.

- **ACGF’s unique approach to enable access to finance is considered as a major component contributing to its operational stability.**
  - 4 characteristics are identified:
    - A case-by-case individual guarantee approach
    - Guarantee capital’s secure location
    - Organizational set-up: local front office and lean head office in Germany
    - Provision of TA

- **Acknowledgement as a respected reliable partner among Afghan financial institutions.**
  - With 15 years of operations, ACGF has gained a reputation for being a dependable and successful credit guarantee fund and is considered a trusted partner by local Afghan PFIs. ACGF has received positive feedback on all aspects of its operations.
Average SME Guarantee Recipient Breakdown and Macro Economic Impact

8 → 10
Average number of employees at time of the loan and at present

38%
Total job growth

19%
of jobs are held by women

Companies experienced decline in employment
24%

Companies experienced retain or increase in employment
76%

How did the loan affect your personal life?

<table>
<thead>
<tr>
<th>negative</th>
<th>no effect</th>
<th>positive</th>
</tr>
</thead>
<tbody>
<tr>
<td>3%</td>
<td>0%</td>
<td>0%</td>
</tr>
</tbody>
</table>

For 84% of SMEs the guarantee-backed loan led to business growth as well as an improvement of their livelihoods

Additionality

All Partner Financial Institutions (PFIs) confirmed that their lending would be significantly lower without ACGF guarantees
ACGF's business model strongly relies on a close cooperation of carefully selected partners. Currently, ACGF engages in formal partnerships and TA projects with Afghan financial institutions and additional engagements will begin in the near future. ACGF continuously considers new partners focused on lending to the SME sector.

**Afghanistan International Bank**
Afghanistan International Bank (AIB) was founded in 2004, and since then it has established itself as a pioneering leader in Afghanistan’s banking sector and Islamic finance lender. Over the past years AIB has built an enduring institution that combines international expertise with local knowledge, giving a deep-rooted understanding of customer needs that is grounded in the highest international standards and best practice.

**The First MicroFinance Bank**
The First MicroFinanceBank (FMFB) has a commercial banking license and started operations in 2004. FMFB is part of the Aga Khan Agency for Microfinance (AKAM), which has programs in over 15 countries throughout the developing world. Its prime objective in Afghanistan is to contribute to poverty alleviation and economic development through the provision of sustainable financial services to the poor and underserved.

**OXUS**
OXUS Afghanistan was founded in 2007 by OXUS, a Paris-based network of microfinance institutions. OXUS Afghanistan is registered as a corporation, providing four different product types: collateral-free group loans, small personal loans, individual loans and small and medium enterprise loans. Since 2018, upon completing preparatory TA projects, ACGF has started credit guarantee cooperation with OXUS.

**Ghazanfar Bank**
Ghazanfar Bank (GB) is a licensed commercial Afghan bank belonging to leading business groups of Afghanistan. GB offers financial services and products under conventional and Islamic Banking across various regions of Afghanistan. GB emphasizes the fact that its highly experienced and qualified team has the expertise, enabling GB to offer to its client specialized skills in a traditional way.

ACGF had intermittent cooperation with GB since 2012. After strategic discussions in 2018 - 2019 ACGF and GB have embarked on a new growth path of increasing and diversifying cooperation.

**FINCA Afghanistan**
FINCA is a Kabul-based Micro Finance Institution, which offers financial products to its target markets (including micro- and SME sectors with specific focus on agriculture), primarily financing working capital and short-term assets. FINCA's approach is market-oriented and it relies on mobilizing the Afghan resources to foster the development in a sustainable way.

The cooperation between ACGF and FINCA in the past was focused on TA to strengthen FINCA’s institutional capacity for SME lending, improve processes and promote innovation. Based on its established SME lending capacity, FINCA and ACGF are planning to start their credit guarantee cooperation in 2020.
Guaranteed Loan Portfolio & Disbursement in USD, Annually

Proportion of Guaranteed Loans Disbursed in AFA, Remaining Percentage in USD

ACGF (and CGF-A) Claims Disbursed vs Refunds

Number of PFI Staff Trained

As of March, 2019

Claims
USD 2,931,561

Refunds
USD 1,057,287

450+
ACGF's Donors

Success in Development Cooperation

ACGF’s donors have contributed starting capital, Technical Assistance (TA) funds and provided impetus to the establishment and growth of ACGF. BMZ, DEG, the Ministry of Finance of Afghanistan together with the World Bank have been pivotal in supplying the respective funds and in some cases, providing strategic guidance towards ACGF’s current institutional success.

Representatives from BMZ, DEG and Ministry of Finance of Afghanistan are members of ACGF’s Board of Trustees. They define and guide the foundation’s strategic decision-making.

BMZ
Since 2004, BMZ has contributed financial resources and laid the grounds for the establishment of CGF-A, the predecessor of ACGF. BMZ intensively facilitated the process of transition from CGF-A to ACGF and ensured the Afghan governmental support for the transformation of the organization’s status from facility to foundation.

DEG
From 2004 until the end of 2014, DEG was the trustee of CGF-A. Being responsible for the head office function of CGF-A, DEG played a crucial role in supporting development of the foundation’s operational framework and local partnerships. In 2014, DEG intensively supported the transition process from CGF-A to ACGF and provided a repayable grant to ACGF enabling its further upscaling.

World Bank
The World Bank is a vital source of financial and technical assistance to Afghanistan. The World Bank’s Access to Finance Project has become the specific framework in which ACGF is involved via the Ministry of Finance of Afghanistan. In March 2017, following the approval by the Ministry of Finance, ACGF received up to USD 8.1 million in funding to expand credit guarantee activities and broaden TA activities to introduce better SME lending practices for Partner Financial Institutions (PFIs) and facilitate lending opportunities. The funding is used towards expansion of ACGF’s credit guarantee portfolio and carrying out more than 35 TA projects for ACGF’s PFIs, including training over 200 staff members of PFIs. Considering ACGF’s ongoing success in stimulating SME lending in Afghanistan, in 2019, the Government of Afghanistan with the support of the World Bank is exploring opportunities for providing further support.

Ministry of Finance of Islamic Republic of Afghanistan
The Ministry of Finance provides funding to ACGF within the framework of the World Bank’s Access to Finance Project. The expansion of ACGF’s guarantee operations and TA activities implemented within the framework of this project serves the ultimate goal of improving access to finance among SMEs across Afghanistan, unlocking the potential of the SME sector to stimulate economic growth and improve livelihood of the Afghan people.
ACGF and the UN’s Sustainable Development Goals

ACGF contributes to the advancement of the United Nations Sustainable Development Goals in Afghanistan. ACGF strives to achieve transformational change through strengthening of the financial sector, which provides credit to SME sector, in turn creating new and securing existing jobs.

**Goal 5: Gender equality**
Approximately 19% of employees in the supported SMEs are women. Also, TA projects are designed for financial inclusion of women entrepreneurs.

**Goal 10: Reduced inequalities**
Targeting SMEs across underserved minorities in all regions of Afghanistan and improving access to finance.

**Goal 8: Decent work and economic growth**
More than 10,200 jobs created and secured, over 57,000 retained since inception.

**Goal 13: Climate action**
Training staff of financial institutions within the framework of Environmental and Social Risks, hence promoting support to environment-friendly businesses.

**Goal 9: Industry, innovation and infrastructure**
Over USD 219 million total guaranteed loans issued by financial institutions to Afghan SMEs.

**Goal 17: Partnerships for the goals**
Working with national, regional and international actors.
Shaping the Future of Afghanistan

The ultimate goal of ACGF’s work is to create positive impact on SMEs, owners and employees and their families in Afghanistan.

Impacting Academics

While studying education management at a university in Iran, Mohammad dreamed of returning to his home in Afghanistan and founding his own school. Many schools in Afghanistan face critical challenges, including over-crowding, insufficient number of teachers and a lack of supplies for the students. Mohammad saw potential to make an impact on the educational experience of Afghan children. He returned to Kabul after completing his studies and in 2009, he took a chance to make his dream a reality and opened a private school in his home district.

In less than a decade, with four SME loans guaranteed by ACGF, Mohammad was able to grow his private school from 400 students to over 3,000 students and hire 100 experienced, dedicated teachers and staff.

Significance of Agriculture and Society

Afghanistan is known for its fine quality fruits and nuts. Production and further export of these became possible for a Herat-based borrower of one of ACGF’s PFI’s. The company was initially concentrated on trading and wanted to introduce their products to international markets. With a guaranteed loan of USD 39,000, it became possible to install new machineries, to comply with the international standards of dried fruit packaging and production.

By gaining tremendous success, the company has extended the number of its female workers to increase their income level with independent access to education and health service. Now, 33 skilled female workers enjoy better life quality. The company’s commitment to introduce Afghan dried fruits to new markets, meanwhile upholding the social standards for their employees leave impacts on society and the national economy.