



CREDIT GUARANTEE FUND AFGHANISTAN

**Short-term Technical Assistance
Terms of Reference / Scope of Work**

Date: August 17, 2022

Project	Viability Assessment of ACGF’s Partner Institutions	
Start Date	September 16, 2022	
End Date	December 16, 2022, or the final acceptance of the final deliverable to be provided hereunder, whatever occurs later.	
Reports to	<i>Name - Title:</i>	Detulio Fumo
	<i>Phone:</i>	+258 84 33 00 101
	<i>E-mail:</i>	d.fumo@acgf.de
Contract Type	Lump sum as per the acceptance of the achieved deliverables	

1. Background

1.1. Institutional Background

The ACGF - Afghan Credit Guarantee Foundation ("**ACGF**") was established in September 2014 by the German Federal Ministry for Economic Cooperation and Development ("**BMZ**") and DEG - Deutsche Investitions- und Entwicklungsgesellschaft mbH ("**DEG**") with approval and support from the Government of the Islamic Republic of Afghanistan and from the Central Bank of Afghanistan as well as from the Governments of both the United States of America and the Federal Republic of Germany.

ACGF provides partial guarantees to Afghan partner financial institutions ("**PIs**") which provide credit to local micro, small and medium enterprises ("**MSMEs**"). It also provides technical assistance ("**TA**") to Afghan financial and other institutions. ACGF is supported by its 100 per cent subsidiary SME Client Support Afghanistan LLC ("**SCSA**"), a Kabul-based financial consulting company focused on providing ancillary services to ACGF in the areas of credit guarantee business including TA for Afghan PIs on behalf of ACGF.

ACGF’s mandate is to contribute to strengthening the emerging financial sector and to developing private-sector capacity in Afghanistan, thus, to support the creation of employment and income. ACGF facilitates access to finance for Afghan MSMEs. ACGF’s objectives are achieved mainly by sharing credit risk with the Afghan PIs by providing credit guarantees for MSMEs and by providing comprehensive TA (training, coaching, product development, risk management improvements etc.).

As per the end of March 2022, ACGF (including its legal predecessor CGF-A) has issued. 11,182 guarantees to support a loans of USD 260m to MSME. The market share of ACGF was approx. 44

per cent of all small and medium loans outstanding by banks in Afghanistan at the end of 2020. The average net loss rate since inception is 1.8% p.a. ACGF estimates support of 46,582 jobs in the guaranteed businesses and creation of 12,639 additional jobs.

1.2. Background to Project

The events of August 15, 2021 have pushed Afghanistan into a severe economic crisis heavily affecting the functioning of its financial sector, including:

difficulties with international payments; increasing deposit withdrawals (currently restricted by the DAB) due to eroding levels of trust in financial institutions; subsequent challenges around maintaining sufficient levels of accessible liquidity; deteriorating credit portfolio quality; the complete suspension of new lending; regulatory uncertainty due to missing policy guidance by the DAB with the expectation of a need to fully transition to Islamic finance; increasing income and expenditure pressures; loss of skilled staff; etc..

As the Da Afghanistan Bank (DAB) partly struggles to fulfil its core central bank functions (heavily relying on USD inflows through humanitarian channels to stabilize the domestic currency, and neither being in the position to sufficiently control inflation nor to serve the domestic demand for hard currency), it has established some measures to aid the financial system in this time of crisis, including:

- Auctioning of USD to stabilize domestic currency with the help humanitarian aid inflows.
- Suspending “Asset Classification and Provisioning Regulations” (ACPR). for 6 to 12 months to reduce financial pressures on PI balance sheets in the context of deteriorating assets.
- Issuing of guidelines for the transformation to an Islamic finance regime.
- Deposit withdrawal restrictions for companies and individuals

The above-mentioned issues continue to challenge Afghan financial institutions as a whole. This in turn, also poses significant risks to ACGF as an institution, as e.g. a collapse of the banking system would mean a nearly total loss of prospects to continue operating in Afghanistan.

The Guarantee Framework Agreements (GFA) provide ACGF with the option to terminate all guarantees under specific circumstances. ACGF’s understanding is that the current situation would allow for the termination of guarantees to protect ACGF from making claim payments to defaulting financial institutions.

To avoid such terminations at that point in time, ACGF and its PIs agreed on an approach that postpones the termination decision by one year and allows for the monitoring of the situation in Afghanistan, and its impact on its PIs. To this end, an alternative termination right was established in respective Memoranda of Understanding (MoU) and subsequent amendment of the GFAs that allow for the termination of all guarantees on the basis of an external viability assessment. By doing

so, ACGF can carefully assess each individual PI's situation throughout the year 2022, with the aim to continue supporting financial institutions in line with its mandate, while safeguarding its capital.

The agreed approach foresees the external viability assessment to be conducted during the last quarter of 2022 by a professional consultancy company (an international professional consultant company in cooperation with a subcontracted reputable local firm or, an professional consultant company with proven experience and knowledge of the Afghan financial context, as well as a local representation (potentially via subcontracting) or with the ability to travel to Afghanistan), performed in line with international standards (including regulatory standards) using a prudent approach considering the Afghan country context. The assessment will focus on the financial institutional strengths and on operational reviews of existing and future business models of PIs.

2. The Assignment

2.1. Objectives

The objective is to conduct a due diligence in order to judge whether ACGF's PIs are considered viable at the end of 2022.

2.2. Scope of Work

During the last quarter of 2022, the Service Provider will undertake viability assessments of four of ACGF's Partner Institutions (PIs) (three commercial banks and one unregulated microfinance institution).

Assessment methodology

Viability defined as "PI's ability to continue its (lending) operations on a sustainable basis" shall be assumed if the assessment comes to the conclusion that there is sufficient reason to believe that the respective PI is or will be in the position to:

- Maintain or regain its financial stability,
- ensure continuity of the institution's critical functions, all those that are necessary to permit smooth business continuity in response to the main target group needs and core activities of the PI
- align with current and future common regulatory/best practice approaches,
- implement the respective institutional strategic plan.

PI viability shall be assessed based on a comprehensive framework, in coherence with common regulatory/best practice approaches for the assessment of financial institutions viability. The

framework shall assess the PI viability based on the assessment of three areas (at reporting date):
 1) the country level risk, 2) PI financials, and 3) PI's operational capacities (including the review of its strategic plan, governance structures, etc).

2.3. Work Plan

No.	Phases, Activities, Deliverables	Suggested Time Frame
0	Preparation	Week 1
0.1	The Service Provider (SP) conducts a kick-off call with ACGF and PI management, risk and operations units to discuss the assignment and align expectations.	Week 1
1	Definition of the Assessment Framework	Week 1 - 2
1.1	<p>The SP reviews the preliminary assessment framework, including the review of the proposed indicators. The contractor suggests adjustments where needed, proposes additional indicators and justifies any in- or exclusions.</p> <p>The SP reviews contractual agreements with PIs and other internal documentation related to the Due Diligence.</p> <p>The SP develops a preliminary list of all documents (FS, manuals, business plans and strategy etc.) that shall be provided by PIs and inform the assessment.</p> <p>The SP interviews ACGF and PIs core staff with the aim of understanding internal positions and needs around the Due Diligence assessment.</p>	Week 1 - 2
	<p><i>Interim Deliverables:</i> Draft assessment framework, including a comprehensive list of PI documents and detailed implementation plan</p>	<i>Within 2 weeks of the assignment</i>
1.2	The Service Provider discusses the draft assessment framework with ACGF staff to validate and further refine the results.	Week 3
	<p><u>Deliverable 1:</u> Final assessment framework including a detailed implementation plan</p>	<i>Within 3 weeks of the assignment</i>
2	Implementation of the Due Diligence	Week 4-9



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2.1	<p>Based on the final assessment framework, the SP undertakes the due diligence assessment.</p> <p>To this end, the SP reviews PI documentation, conducts interviews with PI representatives and undertakes on-sight inspections.</p> <p>In particular, the SP shall examine three main assessment categories: 1) the country level risk, 2) PI financials, and 3) PI's operational capacities (including the review of its strategic plan, governance structures, etc).</p> <p>1. Country Risk Assessment</p> <p>While it is known to both parties that Afghanistan has and will remain in a high-risk environment, the SP shall assess the overall country risk and its possible effects on the future viability of PIs' operations. The main aim of this assessment is to understand the readiness of the PI in addressing the challenges imposed by the country risk levels of Afghanistan.</p> <p>To this end, the SP specifically assess:</p> <ol style="list-style-type: none">1. Political and macroeconomic context: Current economic crisis with critical effects on international trade, employment, etc.2. Industry Risk - Financial System and MF Sector: Crisis effects on FS ability to transact, access international funds, rely on deposits, etc.3. Regulatory Risk - Tax and Supervision Compliance: anticipated conversion to a fully Islamic Finance regime <p>A special consideration of the following country-level conditions (and any others stipulated in the final assessment framework) shall be made against the responses implemented by the PI:</p> <ul style="list-style-type: none">- Access to international funds: Afghanistan's ability to access external financial resources to sustain functioning of the Government and the economy; sufficiency of internal resources to enable a full functioning of the Government; sufficiency of humanitarian aid inflows to ensure the provision of basic goods and services to the majority of Afghans. Relatedly, DAB's ability to properly execute monetary policy and financial sector supervision, and thus to support Afghan financial institutions.- Country-level sanctions regimes.- Overall security conditions. <p>2. Financial Assessment</p>	Week 4-8
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	<p>Based on the final assessment framework and considering the results from the country level risk assessment, the SP shall evaluate the last available financial statements (ideally as of August 2022) provided and maintained by PIs (Balance Sheet, Income Statement) verifying the stated figures, their correctness and ensure that a prudent approach is implemented related to estimates and the valuations used.</p> <p>The SP shall further develop a most likely scenario in terms of PIs' overall framework conditions and project the future evolution of selected variables as well as stress-testing selected indicators, to properly assess PIs' potential future viability.</p> <p>In line with international best practices and regular practices in Afghanistan, some adjustments to the existing standards shall be considered:</p> <ul style="list-style-type: none"> - Non-consideration temporary time-bound relief measures (e.g. relief in credit classification/ provisioning policy).¹ - Careful assessment of collateral valuation at current market condition (e.g. mortgage assisted by immovable property guarantee, loan assisted by central government guarantee); - Consideration of outstanding guarantee claim payments by ACGF <p>The assessment shall include:</p> <ol style="list-style-type: none"> 1. Financial Performance <ul style="list-style-type: none"> - Profitability and Sustainability: Historic and projected profits & losses, including the breakdown of income streams, the breakdown of costs, impairment provisions and key ratios (e.g. net interest margin, cost/income, loan impairment); concentration to customer/ segment, with exception of one-off items, carefully considering the impacts of extraordinary revenues/costs of 2022 and their future sustainability. - Efficiency and productivity 2. Solvency and AML <ul style="list-style-type: none"> - Capital adequacy and solvency - Liquidity management and risk - For both, particularly compliance with national regulations (Financial Capital amount, Total Capital ratio, Tier 1 ratio) and liquidity ratios (Broad liquidity ratio, Quick liquidity ratio) 	
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¹ The classification of the exposures should be assessed in line with ACPR, for instance, days past-due criteria on the correct PAR class without considering any relief for the loan portfolio; at the same time, provisioning level should be updated accordingly (so to account for potential losses on P&L) and capital determined consequently.

In line with international best practices and regular practices in Afghanistan, some adjustments to the existing standards shall be considered:

- Additional buffers for thresholds to account for additional needs under stressed market conditions,
- Adjustment of Asset Risk weights for various exposures (e.g. to central governments/ DAB, foreign and local banks to institutions)
- Consideration of hard commitments (letter of comfort) by shareholders or other stakeholders (with positive effects on capital adequacy ratios) by means of capital increases or comparable measures
- Revision of classifications of high-liquid assets and liquid assets to assess the real liquidity profile of financial instruments for each relevant currency, in line with Basel definitions for high-quality liquid assets.
- Indebtedness, funding stability and concentration risk, particularly considering future financial needs and plans (e.g. current negotiations with funders, expectations on the stability of deposits under consideration of eroding levels of trust among depositors, etc.).
- Overall market risks exposure and management (interest rate risk, FX risk).

3. Loan portfolio quality management

- Loan Portfolio Concentration
- Portfolio quality
- Credit operations and risk management
 - Capacities and the impact (if any) of staff turnover
 - Assess the adjustments made on the lending policies to properly address the challenges on managing the lending cycle (loan origination, assessment, decision, monitoring, delinquency management, collection) under the current market situation
 - Ability to properly implement lending processes (post-disbursement loan monitoring, manage delinquencies, undertake recoveries, loan reporting)
 - Ability to structure (and availability of) appropriate lending products
- Credit risk coverage

3.Assessment of Governance and Operational Capacity

	<p>Based on the final assessment framework and considering the results from the country level risk and financial assessment, the SP shall undertake the assessment of the PIs' governance and operational capacity. Based on an agreed prioritization² the following areas shall be considered:</p> <ol style="list-style-type: none"> 1. Ownership and support by shareholders, in particular their commitment to provide additional capital 2. Supervisory Board (composition, skills, supervisory and strategic functions) 3. Executive management and top level management capacities (skills, experience, quality of decision making, risk appetite, market position, particularly considering current levels of staff turnover in management positions) 4. Overall HR and Staffing capacities, especially considering the increased turnover 5. Risk Management 6. Internal Control and Internal Audit functions 7. Compliance Management System (KYC), especially considering the elevated risks related to international sanctions 8. MIS, Reporting capacity and information quality 9. Access to (inter)national transfer system, with a special focus of its ability to send/ receive international and national payments and its impact on critical institutional functions 10. Ability and willingness to transform to an Islamic Finance Regime, considering the overall level of development and acceptance of Islamic structures at the PI (e.g. approvals obtained by the DAB) 11. Appropriateness of the PI's business model and its strategic plan to function sustainably and remain viable, by assessing in how far the plan: <ul style="list-style-type: none"> - addresses the current situation and its market position; provides reliable estimates/ assumptions, particularly on delinquency, income generation and disbursement volume - provides adequate and realistic expected return on equity/asset, funding availability and diversification, risk level of the strategy (the complexity and ambition of the strategy compared to the current business model, etc.) assesses the main exogenous/ internal factors that influence the success of the business model (IT, resource & operational capacity, etc); - considers PI's ability to adjust and implement the strategic plan 	
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² Under guidance of ACGF the SP shall define the extent of assessment for each of the mentioned areas. A special focus shall particularly be given to points 10) and 11).

	<i>Interim Deliverable:</i> Draft operational and financial framework assessment notes/reports for four PIs	<i>Within 9 weeks of the assignment</i>
3	Discussion of Findings and Finalization of Report	Week10-13
3.1	The SP discusses the draft deliverables with ACGF and based on the feedback given, undertakes additional evaluation measures to enhance preliminary findings.	Week 10
3.2	The SP shares the findings with PIs to confirm the stated information, and adjust (where necessary) based on feedback provided by PIs.	Week 11
3.3	The SP prepares final reports for each PI, including business plan evaluation, country-level risk assessment, consolidated portfolio, financial and performance information, governance and operational capacity assessment, as well as a final judgement of each PIs viability.	Week 10-13
	<u>Final Deliverable:</u> Final due diligence reports for four PIs, including business plan evaluation, country-level risk assessment, consolidated portfolio, financial and performance information, governance and operational capacity assessment, as well as a final judgement of each PIs viability.	<i>Within 13 weeks of the assignment</i>
Total LoE		13 weeks

The Service Provider will give notice to ACGF in writing or via e-mail of the completion of deliverables and request acceptance. An approval and/or acceptance of deliverables by ACGF may require several feedback and revision rounds until deliverables are considered final. Review and acceptance of a deliverable must take place no later than 10 days after the Service Provider has given notice in writing or via email of a deliverable being ready for acceptance. The Service Provider should be available to hold discussions and present deliverables over conference call with ACGF/SCSA and the project beneficiary, when necessary.

2.4. Technical Details of the Assignment

3.2.1. Methodology

The activities and deliverables of the assignment are anticipated to be conducted in one continuous intervention of the Service Provider. The Service Provider may propose additional activities, adapt the structure of the assignment or the level of effort if deemed necessary for a successful implementation of the assignment.

3.2.2. Logistics

The Service Provider will be responsible for the timely delivery of activities and deliverables. The Service Provider will report to Detulio Fumo. All communication, as well as written documentation/deliverables, will be in English.

3. Application of Service Providers

The deadline for submission of proposals is September 9, 2022. Please submit the proposal and related documents via email to Detulio Fumo (d.fumo@acgf.de) and Jana Steverding (j.steverding@acgf.de) including a written confirmation of the proposal validity period not less than two weeks beyond the submission deadline. Any proposals received beyond the mentioned deadline will be rejected and not included in the proposal evaluation process. ACGF reserve the right to decide to not implement the assignment or to terminate the procurement process if it is deemed appropriate.

The Service Provider may request a clarification of any part of the Terms of References (“ToR”) until September 2, 2022, any request for clarification must be sent by email to Detulio Fumo (d.fumo@acgf.de) or Jana Steverding (j.steverding@acgf.de). Any request for clarification received beyond the mentioned deadline will not be addressed.

ACGF’s evaluation process is fair, transparent, free of discrimination, and adheres to the provisions in this document. ACGF exercises the authority to evaluate and select the best proposal. The proposal will be the basis for negotiation and ultimately signing the contract with the selected Service Provider.

The Service Provider is explicitly encouraged to present a detailed critical analysis and an interpretation of the assignment objectives and the ToR. This might encompass critical comments and doubts about suitability, consistency, and feasibility of individual aspects and the entire concept, if any. The methodology suggested must take a constructive account of these.

3.2. Qualification of Service Provider

The qualification for necessary project skills:

1. Regional familiarity: The Service Provider will have either 1) familiarity with the Afghanistan banking environment, regulation, and accounting practices, or 2) a subcontractor, that has such familiarity.
2. Regional presence: The Service Provider or its subcontractor have a local presence or can travel to Afghanistan.
3. Language requirements: The Service Provider and the subcontractor will have staff who speak English and preferably a local language.
4. Relevant experience: The Service Provider has significant advisory/commercial banking expertise in regard to financial and risk assessment of financial institutions and have performed similar assessments in the past.
5. The team:
 - a. The leaders of the Service Provider's project team shall consist of industry experts with a minimum of 10 years of experience in commercial banking, financial sector supervision/ regulation, and/ or financial sector audit.
 - b. The leaders of the Service Provider's project team shall consist of securitization industry experts with a minimum of 5 years of relevant work experience in undertaking Due Diligence assessment of financial institutions.

The qualification of the Service Provider should be supported with references to relevant past assignments including (a) assignment synopsis, (b) duration and period, (c) client name and contact details, (d) relevance for underlying project (e) CV's of project team personnel and their respective roles, responsibilities, and LoE.

If a sub-contractor is foreseen by the plan, then proof of sub-contractor's qualification should be provided as well.

3.3. Required Items for Application

In response to the posting of the ToR, the service provider must include the following items as part of its proposal:

1. **Critical analysis** of ToR and suggested LoE (1-2 pages).
2. **Methodology** for completing the activities and deliverables detailed in the ToR (2-4 pages).
3. **Work Schedule** including all intended activities, LoE and timeline.
4. **Financial offer** in USD including:
 - (1) Breakdown of total costs
 - a) Service fee: Fee per day or lump sum with breakdown of costs;
 - b) Project support costs: lump sum with breakdown of costs or to be reimbursed against invoices;



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- c) Expenses: international travel, national travel, transport, accommodation, per diem allowances, etc. to be reimbursed against invoices;
 - d) Taxes: if applicable
- (2) Tentative payment schedule
5. **Written confirmation of proposal validity period** not less than two weeks beyond the submission deadline September 9, 2022
 6. **Signed Declaration of Undertaking** (please see Attachment 1)