KENYA DCA 2006 AND 2010 GUARANTEES EVALUATION

FINAL REPORT – JUNE 2013

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Cover image: The mother in this family has used a loan to buy a dairy cow. Proceeds from the milk sales are helping pay her children's school fees.
Photo: USAID

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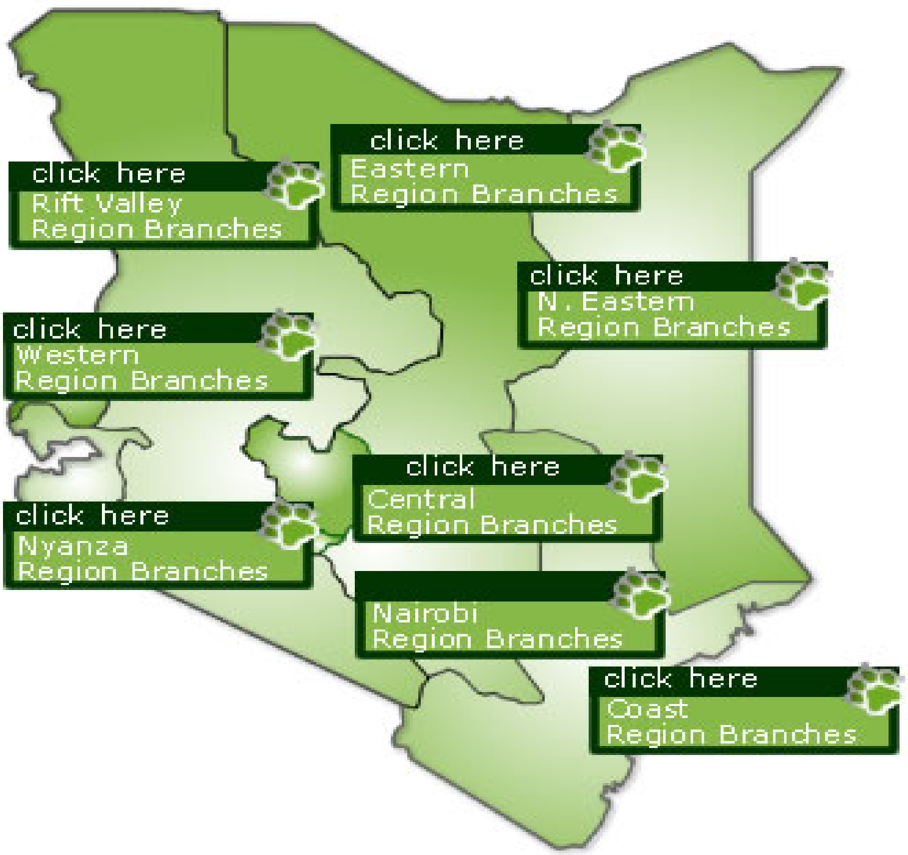
KENYA MAP SHOWING KCB OPERATIONAL REGIONS



Source: *KCB Web site*

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ACRONYMS

ATM	auto-teller machine
AMFI	Association of Microfinance Institutions
CBK	Central Bank of Kenya
CBR	Central Bank Rates
CDF	Constituency Development Fund projects
COMESA	Common Market for Eastern and Southern Africa
DCA	Development Credit Authority
DTMs	deposit taking microfinance institutions
EAC	East African Community
FIRM	Finance Inclusion for Rural Micro-enterprise Project
GDP	gross domestic product
IT	information technology
KARF	Kenya Access to Rural Finance program
KCB	Kenya Commercial Bank
KES	Kenyan shilling
KEMCAP	Kenya Microfinance Capacity Building System
MFI	micro finance institution
MSME	micro, small, and medium enterprise
NPL	non-performing loan
NSE	Nairobi Stock Exchange
PEV	Post-Election Violence
SACCO	savings and credit co-operative
SME	small and medium enterprise
TS	transaction summary (KCB)
USAID	United States Agency for International Development

EXECUTIVE SUMMARY

Under Work Order 12, the Development Credit Authority (DCA) requested that an evaluation be undertaken of the 2006 and 2010 DCA guarantees with Kenya Commercial Bank (KCB). As stated in the DCA Revised Evaluation Framework, "the purpose of USAID evaluation is to ensure accountability to stakeholders and to improve effectiveness in initiatives." The four main objectives of carrying out evaluations encompass both accountability and learning purposes and are stated as: i) Communicate the development contributions to DCA stakeholders (OMB, Congress, USAID Missions) and external partners; ii) Contribute to the dialogue about how to engage financial sector institutions as partners in development efforts; iii) Learn from the intervention's development efforts and to try to examine impact; iv) Strengthen USAID's future application of DCA guarantees as a tool for achieving development results.

- *The Kenyan Economy*

During the period of implementation of the two DCA guarantees (2006-2012), Kenya experienced four waves of crisis, i.e., the Post-Election Violence (PEV), the food and fuels crisis, the global financial crisis, and the 2009 drought that almost caused Kenya's economy to stagnate. While the Kenyan government managed the global crisis well, the domestic crises hit the country hardest. Kenya's economic growth dropped drastically from a high of 7.1 percent in 2007 to a low of 1.6 percent in 2008 due to the effect of the PEV in the first quarter of 2008. The economy recovered to 5.8 percent in 2010 but declined to 4.4 percent in 2011 and 4.3 in 2012. Thanks to the passage of the new constitution in 2010 and its implementation, stronger institutions are emerging that are putting Kenya on sound footing ready to take off. With decisive fiscal and monetary policies, the government has successfully managed to restore confidence in Kenya's medium-term prospects, and the economy is projected to grow at 5.6 percent. The just-concluded peaceful election, continued investments in infrastructure, and a renewed fight against corruption are expected not only to make the economy grow at higher levels but be even better for the creation of jobs.

- *The Financial Sector*

The financial sector in Kenya comprises of 43 licensed commercial banks, one mortgage finance company, 51 microfinance institutions (MFIs) registered with Association of Microfinance Institutions (AMFI) of which eight are deposit-taking microfinance institutions (DTMs) supervised by Central Bank of Kenya (CBK), and 5,544 registered savings and credit co-operatives (SACCOs), with a total membership of 1,857,566 representing 4.8 percent of the population (2010). The objective of Kenya Vision 2030—Kenya's flagship development strategy is to: (i) improve stability, (ii) enhance efficiency in the delivery of credit and other financial services, and (iii) improve access to financial services and products for a much larger number of Kenyan households. KCB is one of Kenya's and East Africa's oldest and largest commercial banks serving more than 2 million customers across the region, with total assets of KES 367.4 billion and capitalization standing at KES 53 billion. The KCB Group is represented in six countries with a total number of 230 branches of which 173 are in Kenya. The bank has experienced steady growth in its net loans and advances, reaching KES 211.7 billion in 2012. Most of the growth has been in its corporate, small and medium enterprises (SMEs), agriculture, micro-credit, and construction sectors.

- *USAID DCA Guarantees*

DCA partial credit guarantees target borrowers and sectors that are constrained by a variety of factors such as the lack of formal collateral that is necessary for most financial institutions, lack of financial literacy, and inadequate property registry systems. Prior to the 2006 DCA guarantee, KCB was widely known as a retail and corporate bank. The SME lending function was embedded in the bank's corporate banking section where borrowing by SMEs was constrained by stringent terms and conditions, and most loan applications were being rejected. By covering 50 percent of the risk exposure with KCB, the DCA 2006 and 2010 guarantees were intended to fix such financial market imperfections and enable the bank to reach borrowers and/or market segments otherwise considered as "High Risk." The guarantee was to target special sectors and products such as agriculture production and processing, manufacturing, tourism, merchandise/trade, 2nd-tier MFIs, clean energy, commerce, constituency Development Fund Projects, construction, and manufacturing.

- *Evaluation Approach and Methodology*

Evaluation Approach: KCB has 173 branches located throughout the country. Time and other resources available did not allow the evaluation to draw up a complete listing of branches. Available resources included 14 days of fieldwork including weekends and a two-person team. The evaluation selected the top four performing regions: Nairobi, Coast, Great Rift Valley, and Central. The borrower sampling was based on predetermined criteria to ensure regional balance, sector representation, gender balance, ethnic mix, loan product mix, and range of loan sizes. In line with the revised DCA Evaluation Framework, the evaluation looked not only at how the lender has implemented the guarantee, but also at how the borrowers were affected. The results were to be analyzed at four levels: inputs, outputs, outcomes, and impact for both lenders and borrowers. The evaluation also looked into exogenous factors to determine how much of the changes at the output, outcome, and impact levels could be attributed to the credit guarantee. Key Questions to be answered as stipulated in the Work Order were as follows:

1. Given the high utilization of both guarantees, did the partner increase credit to the target sectors outside the DCA guarantee? Did it move into any new sectors/industries, types of borrowers, types of loans, or loan terms? If so, how and why? To what extent were the DCA guarantees responsible for improving access by partners' customers to credit outside the guarantees? (Outcome- Lender)

2. Did borrowers seek loans before and after the guaranteed loan from the partner financial institution or other financial institutions? If so, were the requests successful? To what extent were the DCA guarantees responsible for improving the borrowers' willingness to seek credit? (Outcome- Borrower)

3. What additional insights can you provide that access for loans improved for the targeted sectors? What role if any did the DCA guarantee play as a demonstration model? (Impact)
4. What exogenous factors affected the financial sector during the agreement period? How?

Evaluation Methodology: Phase 1: *Desk Review:* of all the documents/reports provided by USAID/DCA prior to commencement of the fieldwork. A Desk Review report was submitted.

Phase 2: *Key Stakeholders Consultations*: consultations that involved visits to KCB/HQ and DAI/Kenya office for meetings with DAI staff and USAID/Kenya representatives.

Phase 3: *Field Phase:* where the evaluation used a traditional survey type questionnaire to capture data and information from the targeted borrower clients in the field. The questionnaire information was analyzed to show outcomes of the guarantees with the borrowers, displayed in tables, charts, and graphs.

Phase 4: *The final phase* was the preparation and finalization of the evaluation report. This includes the option for a PowerPoint presentation of the evaluation findings to USAID/Kenya and/or USAID/DCA office.

Evaluation Constraints: The sampling criteria used by the evaluation could not be applied as the borrowers selected from the KCB transaction summaries (TSs) for the 2006 and 2010 DCA guarantees were either no longer with KCB (especially in the case of the 2006 DCA), some had non-performing loans (NPLs), or the names of other borrowers could not be identified in the KCB database. The prevailing political situation in the country also caused some challenges that forced the evaluation to be postponed several times. Other factors that came into play included new staff at KCB branches who were not familiar with DCA borrowers, failure by KCB to contact and prepare borrowers in a timely manner for the evaluation to administer questionnaires, and lack of clear information and data from the borrowers.

Exogenous Factors: During the implementation of the 2006 and 2010 DCA guarantees, Kenya experienced some internal and external shocks that affected the economy at large. The 2007/2008 PEV and the severe drought that followed in 2009 almost brought the economy to a standstill. In addition, there was the impact of the global financial crisis that peaked in September 2008, followed by the subsequent Euro zone crisis—although the effects on the Kenyan economy were less severe compared to the effects in overseas countries or in other countries in the region. The country experienced another drought in 2011, followed by macroeconomic instabilities in 2012, which exerted their toll. The crises however provided Kenya with an opportunity to implement critical public investment measures and checks that Kenya will need in normal times.

Summary Results at the Input Level: Prior to the 2006 DCA guarantee, KCB was widely known as a retail and corporate bank and had a strictly security-based lending policy.

Consequently, lending to SMEs was constrained as they did not meet the high lending requirements set for corporate borrowers. The perceived potential of the SME market to grow prompted KCB to initiate action to capture the SME space and specifically identify products that were suited to the market. The bank approached USAID/Kenya to partner with them in working with SMEs, which resulted in the 2006 DCA guarantee and its 2010 follow-up. In 2008, KCB also established a special SME unit to manage the DCA guarantees and to promote the bank's venture into the SME sector. Under DCA guarantees, KCB expanded collateral requirements for SMEs to include stocks, motor vehicle logbooks, and personal guarantees. The bank received USAID technical support under both the 2006 and 2010 DCA guarantees, which enabled it to develop new innovative lending approaches for the Kenyan SME marketplace, hence mitigating the stringent underwriting requirements that had resulted in high loan application rejection.

Summary Results at the Output Level: The two DCA guarantees enabled KCB to launch into the SME sector without the fear of incurring heavy losses and to develop a clear strategy for its future involvement in the sector. Although the guarantees did not achieve the financial additionality as only 12 percent of borrowers were first-timers, it nevertheless facilitated KCB's marginal clients to be able to raise their borrowing levels with the bank. In this aspect, it is the view of the evaluation that the DCA guarantees acted as a major marketing tool for KCB's own funds. Unfortunately, the bank did not use the opportunity offered by the guarantee to develop similar products to enable it to sustain its SME lending under the DCA guarantee terms. At the time of the evaluation, KCB had resorted to high collateral requirements for SMEs and it is likely to lose DCA borrowers who are not in a position to meet the high lending collateral requirements. On the economic additionality front, DCA borrowers were able to expand their business and improve profitability with the DCA guaranteed loans. On average, the enterprises surveyed improved their sales and profitability levels.

Summary Results at the Outcome Level: The DCA guarantee enabled KCB to establish an SME unit that had not existed before. Although the bank has been slow to act, it is exploring alternative ways of securing loans such as cash flow-based loans, stocks, logbooks, and chattels that traditionally were unacceptable forms of collateral for the bank. KCB is, however, very slow to change and still thinks in terms of high collateral, whereas the competition has moved to providing collateral-free loans. The bank also focused on providing working capital and channeled very little of the DCA-guaranteed loans into investment capital. Although the DCA guarantee inspired more borrowers to seek loans with KCB, there is a need for the bank to fine-tune its loan processing to meet changing market practices and borrower expectations in Kenya. Failure to do so will see all the gains from the DCA guarantee disappear.

Summary Results at the Impact Level: KCB is yet to venture into the non-security loan market as it is still in the process of developing appropriate instruments. Prior to the DCA guarantee, KCB was not a player in the SME market. The DCA guarantee, however, gave the bank the confidence to attempt to move into such new markets. The guarantees enabled the bank to gain experience in working with SMEs such as through Grace loans that specifically targeted women. KCB has since developed a clear strategy and improved collaboration with other financiers in a bid to expand its SME portfolio and become a major player in the sector. From the borrower perspective, the loans under DCA guarantees were able to facilitate business expansion and enable them to achieve some impressive positive social impact (e.g., employment creation, new business creation, better education for children) as recorded by those interviewed. DCA guarantees had a big demonstration effect on first-time borrowers by giving them confidence to seek additional loans from the bank or elsewhere. KCB's own clients were also able to access bigger loans, which they would not have done without the guarantee. The guarantee ultimately demonstrated the existing potential to KCB and showed that funding SMEs can be profitable business.

RECOMMENDATIONS

Key Recommendations for USAID

1. In future, USAID/Kenya may wish to consider setting up these guarantees as revolving funds to enable the bank to roll out more than one loan cycle. To avoid a situation where the guarantee borrowers are unable to secure follow-up loans, it is recommended that KCB and USAID/DCA agree on a time frame within which the partners/KCB would develop and test new products to kick in after the guarantee. This would also ensure there is no over-dependency by KCB on DCA guarantees.
2. USAID/Kenya should design a cost-sharing mechanism with borrowers, in collaboration with KCB, whereby local financial consulting organizations/business service providers can assist SMEs in improving their operations and preparing the financial statements required to facilitate borrowing.
3. In the future, USAID/DCA should place more emphasis in supporting real sectors of the economy (e.g., agriculture, manufacturing) that are the real movers of the economy, hence the need for long-term capital investments. Currently, there is too much emphasis by KCB on retail trade and commerce.
4. To encourage KCB and any other DCA partners to support long-term capital investment, the evaluation would recommend that USAID consider establishing limits on the proportion of the guarantee that would go to supporting different types of loans (working capital vs. capital investment). Given their choice, financial service partners would offload the entire guarantee to working capital, which is a quick and lucrative line of business for banks.
5. For women business-owners, USAID/DCA may wish to consider working with institutions that are more experienced in developing loan products/services that address the specific needs of women-owned businesses such as the Kenya Women Finance Trust Fund, FAULU Kenya, K-Rep, and Jamii Bora Bank.

Key Recommendations for KCB

1. KCB should improve the financial literacy of its clients so that borrowers are aware of the interest rates and charges levied on them by the bank.
2. KCB should develop good loan products for capital investment and build staff skills and capacity to appraise and manage long-term investment loans for economic development.
3. KCB needs to improve staff skills to analyze the risks associated with SME loans and avoid terming everything as working capital.
4. The bank should improve its capacity to deal with agricultural-related loans that have seasonality regimes that are different from normal loans of the bank.
5. KCB should expedite and roll out loan products that would address the constraints of DCA guarantee borrowers to avoid frustration among its clients who fail to secure follow-up loans, resulting in them shifting to other institutions.
6. KCB may wish to consider decentralizing the loan approval limit as its SME and microloans portfolio grows to avoid delays in securing approval from H/Q.
7. A DCA guarantee loan operational manual should be developed to guide staff on terms and conditions. Clients complained of a lack of clear understanding of loan requirements, resulting in delays in loan approval and back and forth requests for information/data and documentation.
8. KCB has to appraise and finance client requirements appropriately to avoid them borrowing short to fund long-term investment (housing), which is bound to create a mismatch in cash flows and compromise client ability to service obligations.

INTRODUCTION

Kenya is recognized as East Africa's regional hub for trade and finance. Nevertheless, according to the World Bank report, many young Kenyans face considerable hardship, discrimination, and inequality of opportunity in accessing high-quality jobs. Rapid urbanization in the past two decades has also reduced the ratio of Kenyans engaged in family farming from two-thirds to less than half of the workforce. On the other hand, Kenya has a large pool of aspiring and capable entrepreneurs capable of creating economic growth and employment opportunities through establishing and expanding micro, small, and medium enterprises (MSMEs) across the nation. The World Bank has recommended the development of formal and informal enterprises as a way of tackling the high unemployment levels in Kenya.

The SME sector has faced serious challenges in accessing funding to undertake projects that could demonstrate their profitability and positive development impact on Kenya. These challenges are even more difficult in rural areas where the majority of Kenyans (over 70 percent) reside. Most formal banks have pulled out of rural areas due to the perceived high risk associated with rural clients and high cost of doing business. Where finance is available, access is limited by unfavorable terms to the borrower, such as 100-percent collateral requirements and short loan tenors. By covering 50 percent of the risk exposure, the DCA guarantees are designed and intended to fix such financial market imperfections. The guarantees target borrowers and sectors that are constrained by a variety of factors such as lack of formal collateral (which is essential for most formal financial institutions), lack of financial literacy, and inadequate property registry systems. By lowering the risk to lenders, the guarantee mechanism was able to get them to reach borrowers and/or market segments otherwise considered "High Risk." Ultimately, the goal was to make finance and other services available to a large number of people, thus contributing to financial deepening and economic development.

PURPOSE OF THE EVALUATION

Under its Work Order Number 012, the Development Credit Authority (DCA) commissioned an evaluation of the 2006 and 2010 DCA guarantees with Kenya Commercial Bank (KCB). As stated in the DCA Revised Evaluation Framework, "the purpose of USAID evaluations is to ensure accountability to stakeholders and to improve effectiveness in initiatives." The four main objectives of carrying out evaluations that encompass both accountability and learning purposes are stated as:

1. Communicate the development contributions of DCA loan guarantees to DCA stakeholders (e.g., OMB, Congress, USAID Missions) and external partners.
2. Contribute to the dialogue about how to engage financial sector institutions as partners in development efforts.
3. Learn from the intervention's development efforts, and to try to examine impact, assessing the:
    - quality of the effort in its objective of financial deepening,
    - cost-effectiveness of the effort,

- significance of the effort in affecting the financial sector,
- significance of the effort in assisting the partner country achieve its development objectives, and
- impact on borrowers' main goal of increasing investment opportunities and incomes.

4. Strengthen USAID's future application of DCA guarantees as a tool for achieving development results.

Unlike past evaluations, which focused on financial deepening from the lender perspective only, the updated framework expands the examination to how borrowers are affected in line with the ultimate objective of stimulating economic growth. The evaluation is designed to capture what is happening to borrowers' incomes and revenue flows, as compared to those of non-borrowers.

OVERVIEW OF THE KENYAN ECONOMY

Central Bank of Kenya (CBK) reports show that Kenya's economic growth dropped drastically from a high of 7.1 percent in 2007 to a low of 1.6 percent in 2008[1], before reaching 2.6 percent in 2009. In 2012, the Kenyan economy grew by 4.3 percent (less than the 4.4-percent growth it achieved in 2011 and 5.8-percent growth in 2010). According to the World Bank[2], Kenya's growth has averaged only 4 percent since 2008. This is lower than the average for Sub-Saharan Africa (excluding South Africa), which grew close to 5 percent, and substantially lower than its East African neighbors Uganda, Tanzania, and Rwanda, which together grew at an average of 6.8 percent. Although Kenya's economy has slowed historically during election years, the World Bank estimates that the Kenyan economy will grow at 5.6 percent in 2013 in a high-case scenario or remain at 4.1 percent at a low-case scenario. With the passage of the new constitution in 2010 and its implementation, stronger institutions are emerging, which puts Kenya on a sound footing ready to take off. Kenya's domestic revenue mobilization remains among the highest in Africa. The country's just-concluded peaceful election, continued investments in infrastructure, and a renewed fight against corruption are expected not only to make the economy grow at higher levels but be even better for the creation of jobs.

During the period of the implementation of the two DCA guarantees (2006-2012), the country experienced four waves of crisis, including the Post-Election Violence (PEV), the food and fuels crisis, the global financial crisis, and the 2009 drought that almost caused the Kenya's economy to stagnate. While the Kenyan government managed the global crisis well, the domestic crises hit the country hardest. Kenya withstood another difficult year in 2012 as policy tightening and weaker global demand slowed economic activity. With decisive fiscal and monetary policies, the government has successfully managed to restore confidence in Kenya's medium-term prospects. Performance of Kenya's primary exports of coffee and tea remains weak, and the current account deficit is growing ever larger, ending 2012 with a projected record deficit of $4 billion (11.5 percent of GDP). Strategically, Kenya has benefitted from Africa's growth momentum through trade, and its natural position as a hub for East Africa and beyond. Nearly 50 percent of its export trade is directed towards the East African Region, supported by Kenya's membership in the East African Community (EAC) and Common Market for Eastern and Southern Africa

1 Central Bank of Kenya Economic Review (2010)
2 World Bank Economic Survey (2012)

(COMESA). Many international companies are choosing Kenya as their regional headquarters. *Annex B* gives the Gross Domestic Product status of Kenya's sectors by value and growth rate over the period of 2005 to 2011.

OVERVIEW OF THE FINANCIAL SECTOR IN KENYA

Currently, there are 43 licensed commercial banks and one mortgage finance company in Kenya. Out of the 44 institutions, 31 are locally owned and 13 are foreign owned. The locally owned financial institutions comprise three banks with significant shareholding by the government and state corporations, 27 commercial banks, and one mortgage finance institution. As at December 31, 2010, the Association of Microfinance Institutions (AMFI) had 51 registered member institutions comprising commercial banks, deposit-taking microfinance institutions (DTMs), wholesale and retail microfinance institutions, development institutions, and insurance companies. There are eight DTMs supervised by CBK. Innovative forms of microfinance and progressive government policies have helped to make Kenya's microfinance sector one of the most developed in Sub-Saharan Africa. It is expected that the microfinance industry will play a pivotal role in deepening financial markets and enhancing access to financial services and products by the majority of the Kenyans. Leading contributors to this dynamic is the success of the M-Pesa mobile banking system. According to the FinAccess Study[3], access to formal financial services in Kenya increased from 17 percent in 2006 to 24 percent in 2009. By 2010, the proportion of Kenya's adult population that used the services of formal financial institutions had risen to 29 percent.

Kenya also has one of the largest and the most vibrant savings and credit co-operative (SACCO) sector in Africa, commanding 62 percent of the total deposits/savings. SACCOs are a very important part of the financial sector in Kenya, providing savings, credit, and insurance services to a large portion of the population. There were 5,544 registered SACCOs in Kenya as at December 31, 2010. Out of the 3,983 active SACCOs in Kenya, 218 or 6 percent were deposit taking. The total membership of SACCOs at December 2010 was 1,857,566 representing some 4.8 percent of the total population. The critical role of SACCOs has been recognized under the Kenya Vision 2030 of mobilization of savings for investments. The Kenya Vision 2030, launched in 2007, is a national long-term development blueprint whose aim is to transform Kenya into a newly industrializing, middle-income country providing a high quality of life to all its citizens by 2030[4].

The main objectives for the financial sector as articulated in Kenya Vision 2030 are to: i) improve stability, ii) enhance efficiency in the delivery of credit and other financial services, and iii) improve access to financial services and products for a much larger number of Kenyan households. The financial sector in Kenya recorded its highest expansion in 2010, growing at 8.8 percent. During 2010, the Kenyan banking sector also witnessed continued growth on various key fronts, including an increase in the number of service providers, advancements in technology that facilitated service delivery channels, geographical expansion by service providers

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[3] FinAcess National Survey 2010 is prepared by the Financial Sector Deepening and the Central Bank of Kenya

[4] Kenya Vision 2030 Web site: http://www.vision2030.go.ke/

both within Kenya and regionally, and greater product differentiation resulting in niche market growth.

KENYA COMMERCIAL BANK OVERVIEW

The Kenya Commercial Bank is one of Kenya and East Africa's oldest and largest commercial banks with total assets of Kenyan shillings (KES) 367.4 billion and capitalization standing at KES 53 billion. The KCB group subsidiaries operate a total number of 230 branches located in Kenya (173), South Sudan (20), Tanzania (11), Uganda (14), Rwanda (11), and Burundi (1). The expansive branch network is complemented by 940 ATMs across the region that offers 24-hour access to its quick serve services and 4,627 KCB Group agents[5]. The bank also offers mobile banking, Internet banking, and Diaspora banking service platforms that can be accessed on a 24/7 basis. KCB serves more than 2 million customers across the region. Shareholder equity rose by 20 percent from KES 44.4 billion in December 2011 to stand at KES 53.3 billion in 2012. KCB is a publicly quoted company with more than two billion authorized shares, trading at the Nairobi Stock Exchange (NSE), Uganda Securities Exchange, Dar-Es-Salaam Stock Exchange, and Rwanda Over-the-Counter Market.

The KCB Group consolidated financial statements show that the bank's balance sheet grew by 11 percent from KES 330.7 billion in December 2011 to KES 367.4 billion in 2012. Customer deposits rose by 11 percent from KES 259.3 billion in 2011 to KES 288 billion in 2012, stepping up an increase in customer footprint, agency, and mobile banking platforms. The growth in net loans and advances was however modest, rising from KES 198.7 billion over the same period in 2011 to KES 211.7 billion in 2012.

The assets of the Kenyan subsidiaries of KCB grew from KSH282.5 billion in 2010 to Ksh304.1 billion in 2012. Loans and advances increased from KSH179.84billion in 2011 to KSH187 billion in 2012. This is seen as a substantial growth from 2009 and 2010 positions of KSH98.7billion and Ksh137.3 billion respectively. Net Interest Income grew by 27% from KSH21.9 billion in 2011 to KSH27.8 in 2012 while the bank has seen its profitability rise from KSH2.7billion in 2007 to KSH11billion. Financial statement of the banks show that in the last five years 2007 – 2012, the highest growth has been in its corporate, small and medium enterprises (SMEs), agriculture, micro-credit, and construction sectors. Concentration of risk in the Microcredit sector has grown from Ksh24 billion in 2007 to Ksh56 billion in 2012, Ksh3.5billion to Ksh20 billion under the SME sector; Ksh31billion to Ksh77.8billion under corporate.

THE SME SECTOR IN KENYA

No one common definition of an SME exists in Kenya. KCB currently defines an SME as a business with between six and 50 employees or an annual turnover of less than KES 50 million. The Financial Sector Deepening GrowthFin study[6] definition extends this to include a profit-

[5] KCB Website and 2008-2012 Financial Statements Information

[6] FSD / Grofin Study on SME Trade Finance Review of Facilities Available in Kenya. http://www.fsdkenya.org/pdf_documents/09-07-21_SME_Trade_Finance.pdf

driven entity whose financial needs are either too large or too complex for microfinance, which has been excluded from mainstream financial institutions that consider the financial needs of SMEs too small. While SMEs face many constraints, the lack of appropriate financial products and services invariably appears as one the leading hurdles to realizing growth. Where finance is available, access is limited by unfavorable terms like collateral requirements of 100 percent to 150 percent, high interest rates and bank charges, and short loan tenors. On the other hand, the Grofin study found that many SMEs are reluctant to seek credit citing reasons such as: i) the cost of getting a loan is too high, ii) interest rates are very high, iii) it is difficult to meet the requirements for getting a loan, or iv) there is a common perception that borrowing from a formal lender will imply losing assets. There are also strong indications that women entrepreneurs face greater obstacles in obtaining finance than men. Regarded as the "missing middle" and often excluded from the formal financial sector, SMEs are increasingly being recognized as a viable and profitable niche by lenders. Most commercial banks in Kenya have recently taken to aggressively targeting the SME banking businesses to diversify their balance sheet and reduce risks arising from a rise in interest rates that was heavily affecting its traditional retail segment.

DCA INTERVENTION IN KENYA

Through its DCA program, USAID partners with financial institutions to encourage lending in underserved areas due to the perception of high risks. The DCA partial credit guarantees target borrowers and sectors that are constrained by a variety of factors such as the lack of formal collateral that is necessary for most formal financial institutions, lack of financial literacy, and inadequate property registry systems. By covering 50 percent of the risk exposure with KCB, the DCA 2006 and 2010 guarantees were intended to fix such financial market imperfections and enable the bank to reach borrowers and/or market segments otherwise considered as "High Risk." The guarantees were intended to help KCB lend more confidently, reduce strict collateral requirements, and extend loan tenors for targeted borrowers, ultimately increasing the flow of credit to areas and activities that need it the most, making finance and other services available to a large number of people, and contributing to financial deepening and economic development. Additionally, the two DCA guarantees were to:

- Improve SME financial product offerings by helping KCB to better address the working capital and long-term financing needs of SMEs.
- Expand bankable SME segments by changing KCB's perception of bankable SMEs and permanently increasing its exposure to SMEs.
- Increase KCB's capacity to appraise SMEs by providing technical assistance and strategies to further develop SME engagement.

MAIN CHARACTERISTICS OF THE 2006 AND 2010 DCA GUARANTEES

Table 1: Summary Characteristics of the 2006 DCA Guarantee

Authority	DCA
Type	Loan portfolio Guarantee
Guarantee Party	Kenya Commercial Bank
Maximum Portfolio Amount	$7,900,000
USAID Guarantee Percentage	50%
Guarantee ceiling	$3,950,000
Terms of the Guarantee	September 2006 - September 2011
Origination Fees	1% of Guarantee Ceiling
Utilization Fees	1% of Outstanding principal
Maximum Loan Amount	$50,000 for SMEs $300,000 for MFIs
Tenor	Not specified in the agreement
Qualifying Borrowers	Non-sovereign micro, small, and medium enterprises, private small and medium enterprises, and 2nd-tier MFIs with 5- 10 employees
Qualifying Projects	Agriculture production and processing, manufacturing, tourism, merchandise/ trade. and Second-Tier MFIs

***Source**: 2006 DCA Guarantee Agreement*

Table 2: Summary Characteristics of the 2010 DCA Guarantee

Authority	DCA
Type	Loan portfolio Guarantee
Guarantee Party	Kenya Commercial Bank
Maximum Portfolio Amount	$5,750,000
USAID Guarantee Percentage	50%
Guarantee ceiling	$2,875,000
Terms of the Guarantee	September 2010 - September 2017
Origination Fees	1% of guarantee ceiling
Utilization Fees	1% of outstanding principal
Maximum Loan Amount	$250,000
Tenor	Not specified in the agreement
Qualifying Borrowers	Non-sovereign micro, small and medium enterprises (MSMEs) defined as having 100 or fewer employees, MFIs, and SACCOs. Encourage MSMEs that are majority-owned and/ or operated by women and/or require cash flow-based lending.
Qualifying Projects	Agriculture production/values addition, clean energy, commerce, constituency Development Fund Projects, construction, and manufacturing. At least 20% to clean energy sector areas of solar, wind, biogas, and small hydroelectric power generation.

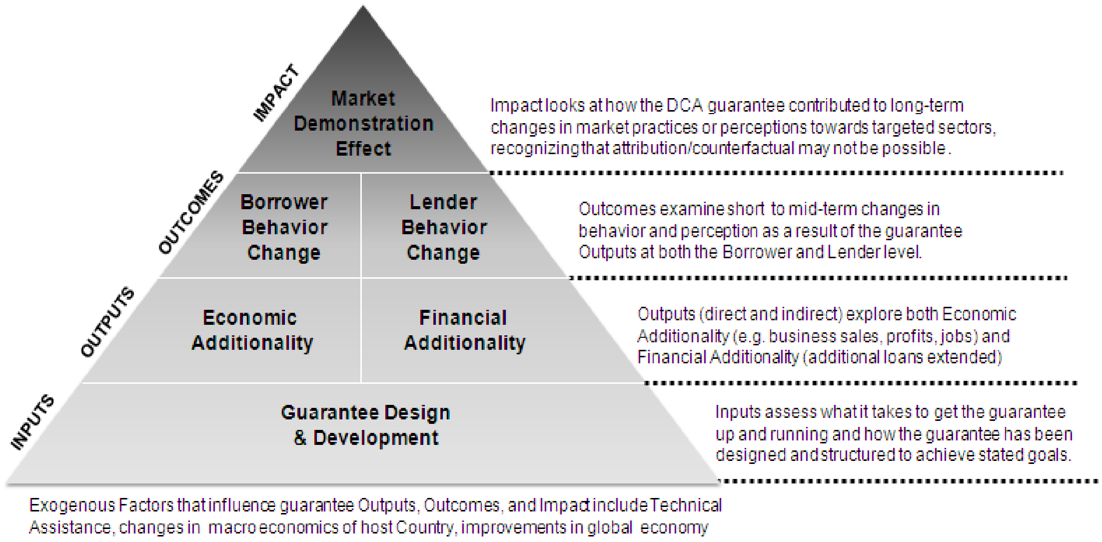
***Source**: 2010 DCA Guarantee Agreement*

METHODOLOGY AND INDICATORS

EVALUATION APPROACH

In line with the revised DCA Evaluation Framework, the evaluations looked not only at how the lender has implemented the guarantee, but also at how borrowers were affected. The results were to be analyzed at four levels: inputs, outputs, outcomes, and impact for both lenders and borrowers. The evaluation also looked into exogenous factors to determine the degree to which changes at the output, outcome, and impact levels could be attributed to the credit guarantee (see *Figure 1* below).

Figure 1: DCA Guarantee Theory of Change



Key Questions to be answered as stipulated in the Work Order were:

1. Given the high utilization of both guarantees, did the partner increase credit to the target sectors outside the DCA guarantee? Did it move into any new sectors/industries, types of borrowers, types of loans, or loan terms? If so, how and why? To what extent were the DCA guarantees responsible for improving access by partners' customers to credit outside the guarantees? (Outcome- Lender)

2. Did borrowers seek loans before and after the guaranteed loan from the partner financial institution or other financial institutions? If so, were the requests successful? To what extent were the DCA guarantees responsible for improving the borrowers' willingness to seek credit? (Outcome- Borrower)

3. What additional insights can you provide that access for loans improved for the targeted sectors? What role if any did the DCA guarantee play as a demonstration model? (Impact)

4. What exogenous factors affected the financial sector during the agreement period? How?

- *Sample Selection Criteria*

KCB has 173 branches spread across the country. Time and other resources available did not allow for a complete enumeration. Available resources consisted of 14 days of fieldwork including weekends and a two-person team. The 2006 DCA guarantee had 1,068 loans, whereas the 2010 DCA had 847 loan accounts, for a total of 1,915 loan accounts. To reduce the regions and branches to be visited, the evaluation selected the top four performing regions based on the total loans approved. In each of the KCB regions, the evaluation selected 20 borrower names from the bank's transaction summary (TS) data, based on the predetermined criteria designed to ensure regional balance, sector representation, gender balance, ethnic mix, loan product mix, and range of loan sizes. As the TS did not show the originating branch, the sampled list was forwarded to KCB headquarters (H/Q) for verification and transmission to the respective KCB branches. In the initial meeting with KCB H/Q - SME unit, it was agreed that the regional SME managers and the business managers at the respective KCB branches to be visited would act as the contact persons for the evaluation team in the field. *Table 3* gives a list of all the KCB branches visited by the evaluation in each of the four regions. A map showing the spread of KCB regions is provided in the front section of this report.

Table 3: Regions and KCB branches visited by the evaluation

Nairobi Region	Great Rift Valley Region	Coast Region	Central Region
Biashara stree Branch	Eldoret Main branch	Treasury Square Branch	Machakos Branch
Moi Avenue Branch	Eldoret west Branch	Town center Branch Mombasa	Thika Branch
River Road Branch	Njoro Branch	Kiasauni Branch	Githunguri Branch
Limuru Branch	Iten Branch	Mvita Branch	
Kikuyu Branch	Nandi hill Branch	Kilindini Branch	
Kiambu Branch	Nakuri Main branch		
	Flamingo Branch		

Source: *Evaluation Field Report*

EVALUATION METHODOLOGY

Initially, the evaluation was to be carried out by a team of two senior-level professionals hired by DCA/Washington office. Unfortunately, Mr. Joseph Auma who had been identified to support the preparation and review of the interview tools and data analysis opted out of the evaluation task as he found USAID's terms difficult. DAI/Kenya office assisted the evaluation team in identifying a local statistician, and Mr. Gerald Mbuthia Kinuthia was later hired to support the team in analyzing the tools after the fieldwork. Ms. Karuri designed the lender and borrower evaluation tools and administered the same in the field, assisted by a research assistant hired locally. DAI/Kenya assigned the evaluation with a vehicle and a driver throughout the fieldwork period. The office also assisted the evaluation in securing meetings with KCB H/Q. Unfortunately, the proposed meetings with non-DCA lenders and the CBK did not materialize as anticipated, even with intervention by DAI.

The evaluation process began in February 2013, and the desk review report was submitted on February 18. Initially, the fieldwork scheduled between February 19 and March 1 had to be postponed due to the prevailing political situation in the country. It was not until April 26 that the evaluation was able to resume in earnest. The evaluation has been guided by the revised

DCA Evaluation Framework, which specifies the evaluation questions, indicators, sources of data, and analyses. *Annex A* of the report contains the Revised Evaluation Framework and Indicators used to guide the evaluation process. *Annex C1* and *Annex C2* contain the borrower interview tool used and the list of questions that guided discussions with KCB, respectively. The evaluation was divided into the following four main phases.

Phase 1: ***Desk Review:*** The first phase was the desk review of all the documents/reports provided by USAID/DCA prior to commencement of the fieldwork. These included the KCB TS reports, which were a major source of insight into the performance of the two guarantees. The desk review report was submitted for transmission to DCA/Washington on March 18, 2013. The desk review report submission was delayed slightly due to the withdrawal of the second team member, which necessitated adjustment in the deliverable timetable to allow the remaining evaluator sufficient time to complete the report.

Phase 2: ***Key Stakeholders Consultations*:** These consultations involved visits to KCB/HQ, DAI/Kenya office for meetings with USAID/Kenya representatives and DAI staff. With KCB H/Q staff, the evaluation opted to use a series of broad questions to guide the discussions instead of the questionnaire approach. The questions were guided by the key evaluation questions in the Work Order and the DCA Evaluation Framework. Because of their busy schedule, it was agreed with KCB H/Q staff that they would provide the evaluation with a written response. It took KCB H/Q one month (March 26-April 25) to provide the response, which unfortunately was not very helpful to the evaluation. The list of evaluation questions given to KCB H/Q staff is provided in *Annex C2* of the report. Brief consultations were held with Mr. Mark Rostal, DAI, who was part of the two USAID/Kenya projects that were involved in the implementation of the DCA guarantees—The *Kenya Microfinance Capacity Building Program (KEMCAP)* and the *Kenya Access to Rural Finance program (KARF)*—as well as, the *Financial Inclusion for Rural Microenterprise project (FIRM).* Unfortunately, efforts to obtain some form of end-of-project reports to provide data for a more comprehensive review of the two prior projects had not materialized by the finalization of the evaluation. The evaluation was therefore not able to make a determination of the success or otherwise of the technical support given to KCB.

Phase 3: ***Field Phase:*** The evaluation used a traditional survey type questionnaire to capture data and information from the targeted borrower clients in the field. This was to enable the evaluation to gauge how the DCA-guaranteed loans had performed with borrowers and to answer some of the key evaluation questions. Of the 71 interviews conducted, 69 respondents were viable. This exceeded the target of 50 set by the evaluation in the initial work plan.

Phase 4: ***Final Report and Presentation of Findings***: The final phase was the preparation and finalization of the evaluation report. This included the option for a PowerPoint presentation of the evaluation findings to USAID/Kenya office support.

The evaluation fieldwork plan and deliverable and revised time frames are attached in *Annex D* and *Annex E* of this report, respectively. A brief summary of the experts' schedules is given in *Table 4* below.

Table 4: Experts' Time Schedules

Task	Period	Output
Desk review phase	Submitted on March 18, 2013	Desk review report
Stakeholder consultations/field consultations	March 26 – April 16, 2013	Fieldwork plan and consultations finalized
Draft report preparation	April 17 - May 7, 2013	Draft final report
Report review and presentation	May 7 - May 31, 2013	Final report

Source*: Evaluation Report*

DATA ANALYSIS METHODOLOGY AND PROCEDURE

After the data was collected using the semi-structured questionnaire, the researcher verified the completed questionnaires to check for the pattern of the responses. A master template was then created that corresponded to the questionnaire for data entry. The responses were coded numerically for the ease of data entry. The questionnaires were serialized to create a unique code as an identifier. Two research assistants were hired to help in data entry using the MS Excel template. Data validation was done by taking a random questionnaire and rechecking for the data entry errors. The data was then exported for analysis to Predictive Analytics SoftWare, PASW version 17.0.1. The researcher invoked the PASW syntax method to label the data using the predetermined codes, clean the data, perform logical checks, tabulate with respect to the demographic profile of the respondent, and perform extra analysis as per the requirement of the data.

From the survey tool, the demographics were cross-tabulated by region, DCA agreement year, and gender of the respondent. For comparative analysis, the researcher segregated the data by ownership of loans with respect to the subject loan where 67 percent (n=46) of the respondents had loans prior to subject loan, 72 percent (n=50) had loans after subject loan. This ownership of the prior and after the subject loan was interlocking. However, 12 percent (n=8) were still paying the subject loan. Therefore, the comparative analysis comprised 69 respondents in total.

EVALUATION CONSTRAINTS

***KCB headquarter (HQ) staff*:** During the initial meeting, KCB H/Q staff expressed concern with the timing of the evaluation and the short notice given by DCA/Washington. Branch staff were either very busy, away on leave, or on training. The sample borrower list was eventually reviewed and forwarded to the regional SME managers and KCB branches, but in some cases, the borrowers were not contacted until the evaluation team was on the ground. At some of the branches, the evaluation team had to contact and prepare the clients for the interviews, which slowed down the evaluation process.

***Prevailing political climate*:** The evaluation had to be postponed several times as it coincided with the general election in the country. The evaluation process was put on hold, and the work plan was revised accordingly. First, there was the March 4, 2013 general election with heightened campaigns, resulting in DAI suspending all fieldwork two weeks before the election. Then, there was the contested election, supreme court proceedings, and awaited decision. Due to the 2007/2008 Post Election Violence, there were fears and concerns of a repeat of the same, which left the country paralyzed. Although the evaluation started on March 26, it was disrupted by the long Easter weekend. Fieldwork eventually kicked off well on April 1, 2013.

Changes in the sample list: Initially, the evaluation had intended to interview only borrowers from targeted sectors of the 2006 and 2010 DCA Guarantee Agreements. Using the KCB TS spreadsheets, four top performing regions were selected: i.e., Great Rift Valley, Central, Coast, and Nairobi. A review of the sampled list by KCB H/Q revealed that many of those selected were either no longer KCB clients (especially in the case of the 2006 DCA), or were NPLs that would be unwilling to be interviewed, or others for which the KCB database no longer contained name identifiers. (The evaluation was informed that the client names had been erroneously switched and others lost in the process of migrating data from the legacy IT system (TC3) used by KCB to the new (T24) system.) Consequently, only about a third of the names on the initial list were viable. Equipped with these few names, the evaluation decided to venture into the field to find additional borrowers with the help of the branches. To facilitate the exercise, the evaluation forwarded electronic copies of the TS to the four regional SME managers for transmission to the all branch managers and business managers in their respective regions. Due to these challenges, the evaluation team opted to interview whoever was available to meet with them.

***Challenges in contacting DCA borrowers*:** At the branch level, the evaluation noted that a good number of KCB staff and business and branch managers were newly posted. They did not know the whereabouts of the DCA guarantee customers very well, especially those borrowers who were no longer KCB clients. This made contacting the customers and getting them to agree to be interviewed by the evaluation a challenge. To save time, the evaluation decided to invite the clients to the branches instead of visiting them at their places of work. This worked out very well, expedited the process, and enabled the evaluation to administer more interviews than initially targeted.

***Lack of information and data from borrowers*:** Most of the borrowers interviewed by the evaluation had difficulties recalling the information and data that was required to complete the questionnaire. This was especially the case for those clients from the 2006 guarantee, many of whom had fully repaid their loans. This problem was compounded by the fact that most businesses do not have good recordkeeping systems, especially where the borrower is elderly, illiterate, or semi illiterate. Apart from lacking records, some of those interviewed seemed very suspicious and unwilling to share their information with the interviewer. Sales and profit data was given very reluctantly and seemed to be very conservative.

***Rainy season*:** The evaluation coincided with the start of the "long-rains" season in Kenya. The heavy downpour experienced in most parts of the country visited, disrupted the evaluation process, particularly in the Rift Valley and Central regions. In some cases, seeing borrowers in the afternoon—especially those out of the main town centers—was challenging. To save time, the evaluation decided to focus on borrowers within town, who were easier to reach.

EXOGENOUS FACTORS THAT MAY HAVE INFLUENCED THE GUARANTEES PERFORMANCE

Macroeconomic instabilities: The World Bank Economic Survey[7] indicates that since the 2007 elections, the only year when Kenya grew above 5 percent was 2010—this being the only year in which Kenya did not experience internal or external shocks. In 2008 and 2009, the PEV and a severe drought brought the economy to a standstill. In 2011 and 2012, another drought and macroeconomic instability exerted its toll on the economy. Tightened monetary policy, together with an easing in global food and fuel prices, enabled CBK to bring inflation under control, and stabilize the economy by end of 2012. With the decline in inflation and interest rates in 2013, the successful election and transfer of power is expected to boost the economy to return to its natural growth potential of at least 5 percent in 2013.

Post-Election Violence: The PEV that took place in Kenya in the 2007-2008 period mainly affected the 2006 DCA implementation, although it had serious negative implications across all the sectors and adversely affected Kenya's economic performance. Not only was growth negative but also inflation rose sharply largely due to the increase in food prices arising from the shortages caused by the inability to transport food effectively in the first quarter of the year. Lending rates rose soon after the PEV, with banks arguing that they needed to maintain their profit margin in order to retain a positive interest earning in real terms, in the face of uncertainty in loan repayment due to economic performance uncertainty and rising inflation. Because all of the loans made by KCB are secured, borrowers interviewed reported they had been obliged to repay loans to avoid loss of their assets. Like all the financial institutions in the country, the bank had borrowers that were affected by the PEV. Some were displaced from the PEV hotspots, some lost their businesses altogether, and others incurred heavy losses and damage to business that will take years to recover.

Fast forward to March 2013 and the fears of a repeat of the 2007-2008 chaos and political violence gripped the country in the run-up to the March 2013 election. Most business people interviewed during the evaluation were very cautious, especially those that had experienced heavy losses in the Rift Valley and Coast regions in the 2007-2008 PEV. Most of them had run down their stocks, and at the same time, importers had stocked up on dollars in the run-up to the election, anxious over possible unrest and disruption to trade. This put pressure on the shilling, which in January 2013 hit a seven-month low against the dollar. Fortunately, Kenyans held a peaceful election, and there has been an upswing in the economy as evidenced in the strengthening of the shilling against the dollar from a high of KES 87:$1 in February/March 2013 to the current KES 81:$1.

[7] World Bank - Kenya Economic Update -: Running on one Engine / Kenya's Uneven Economic Performance June 2010, Edition No.2

***Financial crisis shocks/impacts*:** According to CBK annual reports for 2010 and 2011, the impact on the Kenyan economy of the global financial crises that peaked in September 2008, followed by the subsequent Euro zone crisis, was less severe as compared to the impact on overseas countries as well as on other countries in the region. Kenya's strong macroeconomic policies and its relatively limited integration in the global economy shielded it from some of the worst aspects of the 2008/9 global downturn. Determining the impact of the global financial crisis, however, was made somewhat more difficult as it was mixed with the residual effects of the PEV that had hit the country in the first three months of 2008. Kenya has sought to mitigate the effects of such external shocks by seeking more diversified markets for its products (agriculture) and tourism. The government also responded to the global downturn by formulating a KES 22-billion ($300 million, 0.9 percent of GDP) fiscal stimulus program. The fiscal stimulus focused mainly on social sectors, including social protection and infrastructure investments. The global crisis provided an opportunity to implement critical public investment measures and checks that Kenya would need in normal times. The fiscal stimulus was complemented by other measures that responded to the domestic food crisis, such as duty exception on maize.

***Drought and natural disasters*:** While Kenya has responded to the global shocks very well, the 2009 drought created a heavy toll on its economic activity. The domestic food crisis that developed as a result of the severe drought was compounded by weak governance and irregularities in the operations of the government-run maize board. In addition, the drought caused enduring electricity shortfalls that hit the manufacturing sector. The agriculture sector, hit hard by the drought, contracted by 2.4 percent. The situation was most severe for maize—Kenya's main food staple. Due to shortages and imprudent policies that led to the "maize scandal," prices increased to double the world market level, which hit Kenya's poor especially hard. Tea, traditionally Kenya's strongest export earner, suffered reduced output from the drought but benefited from global price increases. Horticulture exports experienced a double dip of declining output and prices, reflecting a downturn in global demand. On a more positive note, the livestock sub-sector expanded by 3 percent despite the severe drought as a result of policy incentives and micro credit to dairy farmers, which demonstrates the potential of agriculture once appropriate incentives are in place.

***Markets and competition*:** Kenya's financial sector is the largest in the East and Central African region. It is vibrant, modern, and highly competitive. MFIs are a popular source of finance for SMEs in Kenya as MFIs are more flexible with their lending requirements. Other sources of finance for SMEs include cooperatives, government instruments, international institutions, and donors, as well as personal finance opportunities. The capacity of the SME risk profile—combined with the lenders' lack of sophisticated risk-assessment techniques—makes many of them appear undesirable as credit customers for business banking. As SMEs outgrow the capacity of MFIs, which tend to offer small, short loans via group-lending methodologies, the large SMEs will have to seek loans from banks.

Corruption: Corruption is pervasive in Kenya, affecting all the levels of the economy, especially in the private sector. Most transactions involving government, from obtaining contracts to paying taxes, seem to have a corrupt element. According to the World Bank Kenya Economic Update 2012 report, 71 percent of firms interviewed say they need to give gifts to obtain government contracts worth an average of 12 percent of the value of the contract. To demonstrate the serious effects of corruption, the report indicates that if the private sector could redirect the money it now spends on corruption to job creation, it could add 300,000 jobs, which would be sufficient to hire every unemployed urban Kenyan between the age of 15 and 34.

RESULTS OF THE GUARANTEE INPUT LEVEL

Q.1 What was the motivation for the 2006 and 2010 DCA guarantees with KCB? Who originated the effort?

As noted earlier, the Kenyan banking sector had emerged from the 1980s and 1990s weighed down with a momentous nonperforming assets portfolio, and KCB was no exception. To mitigate the risks of default and loss, the KCB had a strict security-based lending policy. This helped the bank to clean out the bad loans that were undermining the banks' earnings through bad debt write offs from KES 25.1 billion in 2002 to KES 2.2 billion in 2007[8]. Prior to the 2006 DCA guarantee, KCB was widely known as a retail and corporate bank. The SME function was embedded in the bank's corporate banking section, which was not specialized in articulating the uniqueness and special needs of SMEs. For SMEs, borrowing was a challenge due to KCB's stringent lending terms/requirements, especially on the issue of raising security. Consequently, most loan applications were being turned down because they did not meet the requirements set for corporate borrowers, which KCB staff were more familiar with. KCB at the time was also not lending to some of the sectors such as agriculture. Any agribusiness loans handled by the bank were managed at corporate level. The bank was also not very active in the trade and commerce sectors. The perceived potential of the SME market prompted KCB to initiate action to capture the SME space, and specifically to identify products that were suited to the market. The bank approached USAID/Kenya to partner with them in working with SMEs, which resulted in the 2006 DCA guarantee and its 2010 follow-up. In 2008, KCB established a special SME unit to manage the DCA guarantees and to promote the bank's venture into the SME sector. Under the SME scheme, securities were expanded to include stocks, motor vehicle logbooks, and personal guarantees. With the DCA guarantee, the lending margins on different types of collateral were raised.

Q.2 Was any technical support provided to KCB by USAID and/or borrowers to accompany the guarantee?

USAID technical support to KCB: Both the 2006 and 2010 DCA guarantees had a technical support component that was implemented alongside the guarantee programs. Under the 2006 DCA, technical assistance support was provided through USAID/Kenya's *Kenya Microfinance Capacity Building Program (KEMCAP)*. Under this guarantee, KCB was to receive support from USAID/Kenya to develop new lending approaches innovative to the Kenyan marketplace and influence the stringent underwriting requirements that resulted in the existing high loan

[8] CFCStanbic Financial Services research@cfcgroup.co.ke

application rejection. Unlike the 2006 DCA guarantee, the 2010 DCA with KCB was supported through the *Kenya Access to Rural Finance program (KARF)*. This reflects a change in tactic following the 2006 DCA guarantee. Additional TA to KCB under the 2010 guarantee took place through the *Financial Inclusion for Rural Microenterprise project (FIRM),* a USAID and Government of Kenya partnership designed to expand and deliver innovative financial services to small businesses and entrepreneurs, including lending for projects in agriculture, renewable and clean energy, information and communication technology, gender and youth, and policy reform. Feedback from KCB H/Q confirms that the TA was able to help KCB to widen its scope on lending to SMEs and to grow its portfolio by creating more flexible terms on lending, thus attracting more customers. The collaboration has improved the overall credit appetite of KCB lending, whereby security such as stocks are now considered. The upsurge in the use of the 2010 DCA is in part due to in-house training and heightened awareness of the KCB teams in the field of the existence of the guarantee.

- *USAID Technical Support to Borrowers*

In terms of accessing USAID technical assistance by borrowers, KCB had a non-disclosure policy for its association with USAID under the DCA guarantee. This was to avoid any misconception by borrowers regarding the loans that would impact negatively on their willingness to repay. Asked if they had accessed any USAID technical assistance in any way at all, borrowers responded positively only in the Central Region, Githuguri area. This was in relation to the Ngombe Loans that were being promoted by the USAID/FIRM project. A few of those interviewed had also heard of other USAID-supported programs, especially the USAID APHIA Plus program in the health sector.

During discussions with guarantee borrowers, the evaluation noted that many of them face serious constraints in preparing financial reports and documentation required by the bank to support their borrowing requirements. Most complained of the high cost involved in preparing such reports. Unlike consumer lending—where applicants have a job with a regular income (pay slip)—SMEs lack a stable, verifiable paycheck. Their income is mostly cash-based and can change significantly from month to month. Many SMEs also do not have proper financial recordkeeping, which constrains the ability of lending institutions such as KCB to lend to SMEs against business cash flow statements. To mitigate this constraint, the evaluation is of the opinion that the USAID/DCA guarantee in collaboration with KCB should work out a cost-sharing mechanism with the borrowers, whereby local financial consulting organizations/ business service providers can support SMEs in improving their operations and preparing the required statements. This would limit the SMEs' risk significantly and improve the quality of their proposals to the bank. Support for the costs of such consulting services should be designed in a way that: 1) remains transparent, 2) partially covers the costs to SMEs, and 3) allows a reasonable remuneration for the local consultant. In the same way that the DCA guarantee was used to help KCB's entry into the SME sector, USAID should support a similar program to help build SME capacity through improved financial system development.

Q. 3: Did the structure of the guarantee help KCB to achieve the intended goals?

KCB was able to achieve the intended goals. The two DCA guarantees were fully committed, except for the small amount under the 2006 DCA, and claims against the loans amounted to only $558,538. The 2006 guarantee achieved its objective of strengthening KCB's ability to finance loans to targeted SMEs by covering 50 percent of the risk exposure on the principal loans. The bank was also to expand financial services to underserved clientele especially women, which it did under the Grace loan scheme. In addition, the follow-up 2010 guarantee that was intended to last four years was utilized within a year of the obligation date. This reflects the high demand for the DCA guarantee by the bank to support its SME lending. The DCA guarantees also enabled KCB to establish an SME unit to manage the guarantee.

Since then, KCB has moved on to develop new SME products. Under the DCA guarantee, KCB redefined its engagement with the SME sector by putting in place different categories of loans to SMEs (see KCB's circular of June 2007): i) ***Upper-tier SMEs***: Minimum loans of KES 1.0 million and maximum loan of KES 5.0 million; ii) ***Lower-tier SMEs***: Minimum loans of KES 100,000 and maximum loans of KES 1.0 million; and iii) ***Wholesaling to second-tier MFIs and SACCOs***: Maximum loans of KES 20 million. The segmentation of SMEs into "small SMEs" and others is a positive development as the needs of the smaller segment of SMEs are different from those of other segments. The DCA guarantees also enabled KCB to modify its collateral requirements under the different SME loan categories, such as the use of chattels mortgage, floating debenture over machinery and equipment, and loans against stocks/debtors/and personal guarantees. Under the 2010 DCA, KCB was able to initiate in-house training and awareness creation for its officers, which accelerated the use of the guarantee. By allowing the bank to experiment with SMEs, the DCA guarantees opened the bank up to a market niche, which otherwise would have taken KCB a long time to enter given its very conservative nature.

The ability of KCB to roll out more loans under the 2010 guarantee was, however, constrained by the way it was structured. The guarantee was not set up as a revolving fund. Hence, KCB was not able to lend against it once it was fully committed in the first round. The design of the 2010 guarantee was influenced by the implementation experience of the 2006 guarantee which had taken five years to commit (September 2006 - September 2011), with 99.03 percent utilization, and $558,538 in claims paid for 280 defaulted borrowers. The 2006 guarantee was implemented at a time when KCB did not have adequate structures and experience in working with SMEs. Unlike the 2006 guarantee, the 2010 guarantee reached 100 percent utilization after only one year from the obligation date, and as at the time of the evaluation, no claims have been paid. Had the 2010 DCA been structured as a revolving fund, KCB would have been able to roll out more loans as the repayments are received, and a financing gap created. In the future, USAID/Kenya may wish to consider setting up these guarantees as revolving funds to help the bank to generate more than one cycle of loans. To avoid a situation where guarantee borrowers are unable to secure follow-up loans, it is recommended that KCB and USAID/DCA agree on a time frame for developing and testing new products. This will help the bank to avoid a situation where it is overly dependent on DCA guarantees.

Q4. Did the structure of the guarantee encourage KCB to lend more for working capital purposes rather than investments?

All the DCA Guarantee Action Package specifies is that borrowers have access to two loan types: investment capital (i.e., improved equipment, updated technology) in addition to working capital. The guarantee agreement did not specify the proportion of the guarantee to be used for each type of loan. *Table 5* shows that 97 percent of the 2006 guarantee and 91 percent of the 2010 guarantee secured loans for working capital purposes and that 28 (3 percent) loans under the 2006 guarantee and 77 (9 percent) loans under the 2010 guarantee were for capital investment.

Table 5: Types of Loans Under 2006 and 2010 DCA Guarantees

Type of Loan	2006 DCA Guarantee			2010 DCA Guarantee		
	Number of Loans	%	Total Value	Number of Loans	%	Total Value
Working Capital	1040	**97**	7,437,514.00	770	**91**	5,149,219.00
Capital Investment	28	**3**	383,616.00	77	**9**	567,011.00
Total	1068	**100**	7,821,130.00	847	**100**	5,716,230.00

Source: *KCB Transaction Summary*

The evaluation sought to know why there was such a huge difference. The explanation given by KCB H/Q was that the staff in the branches were unable to distinguish between investment and working capital when entering data in the bank's IT system. Apparently, the first option on the KCB loan management system dropdown was working capital, and this became a default function and the easiest option for the branches to populate. The issue here is that loans for working capital and those for investment purposes would normally follow different appraisal processes and their terms and conditions should vary. One distinguishing factor is the loan repayment period, which should be longer for investment capital. KCB staff guidelines issued in June 2007 stipulate term loans with a maximum of three years and working capital with a maximum of 12 months. Grace loans had a maximum grace period of six months. Information derived from the TSs shows that working capital under both the 2006 and 2010 guarantees had a repayment period of up to 48 months, whereas investment capital had 45 months under the 2006 DCA and up to 36 under the 2010 guarantee. See *Table 6*. To avoid overemphasis on working capital lending and to encourage KCB and any other DCA partners to support long-term capital investment, the evaluation would recommend that USAID consider specifying the proportion of the guarantee that would support different types of loans.

Table 6: DCA 2006 and 2010 by Loan Type and Tenor

Type of Loan	2006 DCA Guarantee		2010 DCA Guarantee	
	Tenor by Months			
	Minimum	Maximum	Minimum	Maximum
Working Capital	3	48	6.5	48
Investment Loans	12	45	12	36

Source: *Transaction Summary*

Without longer repayment periods, it is difficult to finance investment in new business, buy equipment, or invest in new technology because such investments may not yield sufficient revenues in the short-term to repay a loan. What the evaluation discovered from among the few borrowers that were interviewed was that most of those borrowing for working capital were diverting the funds to the purchase of fixed assets, including real estate development. The arguments put across by borrowers was that it was easier to secure working capital loans from KCB than investment capital loans. The borrowers claimed that the KCB investment loan requirements were too tedious and expensive for them to fulfill. They singled out the cost of obtaining financial reports and legal fees as some of the costs that make such loans expensive. Borrowing short to fund long-terms investment (housing seems most popular) is bound to create a mismatch in cash flows and would compromise client ability to service obligations. This may eventually result in bad loans unless the borrower has other sources of income from which to repay the working capital loan.

The evaluation met clients who complained that they had applied for an overdraft facility, but the bank opted to give them a term loan instead. Explanation put across by KCB staff was that new borrowers did not have the skill to manage overdraft accounts. The evaluation also learned that the DCA guarantee does not support overdraft facilities. It should be noted, however, that for working capital purposes the loan option is much more expensive for SMEs—especially those in trade and commerce—as compared to the overdraft. The overdraft allows the borrower to pay interest on the amount overdrawn. The use of term loans for working capital could be the reason why some of the borrowers diverted the funds to purchase fixed assets. They never really intended to borrow for working capital but it was the easier option. Processing working capital loans is also easier for bank staff, which could explain the large size of the trade and commerce loan book. There is a need for the bank to develop good loan products for capital investment and build staff skills and capacity to appraise and manage long-term investment loans for economic development.

RESULTS OF THE GUARANTEE OUTPUT LEVEL

FINANCIAL ADDITIONALITY (ADDITIONAL LOANS EXTENDED)

Simply making guaranteed loans is insufficient evidence of KCB's success. The key objective is additionality[9]. The success of the DCA guarantee program is best told by the partner financial institution's additional lending through its ability to expand outreach and financial services to previously unserved entrepreneurs (i.e., the extra lending that occurs to the target group), but would not have been possible without the guarantee. The additionality argument is harder to make for large institutions such as KCB, however, as they are not as resource-constrained as their smaller counterparts. In this situation, loans that are supposedly made because of a guarantee may simply substitute for some loans the institution would have made anyway. The evaluation was therefore keen to determine during discussions with KCB staff and interviews

[9] Additionality is the extra lending that occurs to the target group that would not have been possible without the guarantee. If the guarantee accomplishes its objectives, lenders will increase lending to the target client and/or the terms will be softer (e.g., reduced collateral requirements, lower interest rates, longer terms).

with the borrowers if the loans to SMEs met the additionality criteria. As the guarantee was to address KCB's high and prohibitive lending terms (collateral, tenor, and high interest rates), additionality could only be achieved by changing these terms to attract borrowers who would not qualify under KCB standard terms. Of the 69 borrowers interviewed, only eight (12 percent) were first-time borrowers. These are the borrowers who accessed the subject loan because of the attractive terms that it offered. The rest were existing KCB clients who were now able to scale up their borrowing under guarantee terms. The evaluation learned that the bank staff would refer loan applications only to the guarantee after they failed to meet the KCB standard terms and conditions. The guarantee was therefore able to facilitate loans that KCB would otherwise have turned down, hence fulfilling the additionality criteria.

Q. 1 Did KCB re-orientate its SME lending strategy in line with the DCA guarantee targets?

KCB plans to grow its income from the SME market segment through an enhanced product portfolio and cross-selling opportunities. According to information on its Web site, in 2012 KCB had an SME deposit book valued at KES 30 billion and an SME customer base of about 100,000 accounts. The bank's ultimate goal is to offer specialized value addition and deposit-taking services in a holistic approach to meet the finance and business advisory needs of the local SMEs that have a vision to grow and become large, profitable companies. The segment of SMEs targeted comprises sole traders, small limited-liability companies, farmers, MFIs, SACCOs, and NGOs with a turnover of up to KES 50 million that have the capacity to enjoy loan facilities of up to KES 5 million. Products targeted include a specialized agricultural financing package geared toward SMEs seeking to grow their potential through value addition in the dairy, maize, and tea sub-sectors. Although information on the KCB Web site does not mention the role of the DCA guarantee, it is expected that part of the lending to these and other targeted sectors would be supported by the guarantee.

Q.2 How did KCB find borrowers? Did it market the DCA guarantee loan?

KCB did not market the DCA guarantee loans to avoid compromising a borrower's willingness to repay. DCA loans were created in the normal course of business with the decision to assign a particular loan to the guarantee being left to the loan officers. Clients would apply for facilities under regular KCB terms. Where the application qualifies except for weaknesses in the security, the officer would use the DCA guarantee to bridge the collateral gap to meet required levels. Borrowers under the DCA guarantee were not privy to the role of guarantee in facilitating their loans. This was noted and upheld even during the evaluation. In 2008, KCB created a special Grace Loan window for women borrowers under special conditions. The loan product had a six-month grace period, which became its undoing. KCB also created a special window for MFI and SACCOs with loans of up to KES 20 million repayable over 48 months. These special facilities were a silent way of the bank to market the DCA guarantee.

ECONOMIC ADDITIONALITY (BUSINESS SALES, PROFITS, JOBS)

Q.1 How did DCA guarantees influence the borrowers' economic additionality (e.g., sales, profit, job creations/salaries)

Sales and profits: Economic additionality here refers to the positive net effect on sales, profits, and job creation arising from additional loans generated through a DCA guarantee. All 69 borrowers sampled by evaluation had experienced growth in sales and profitability when compared with their position prior to the DCA-guaranteed loans from KCB. *Table 7* compares the level of gross sales and net profits prior and after the DCA-guaranteed loans among borrowers in the four regions sampled, and by gender.

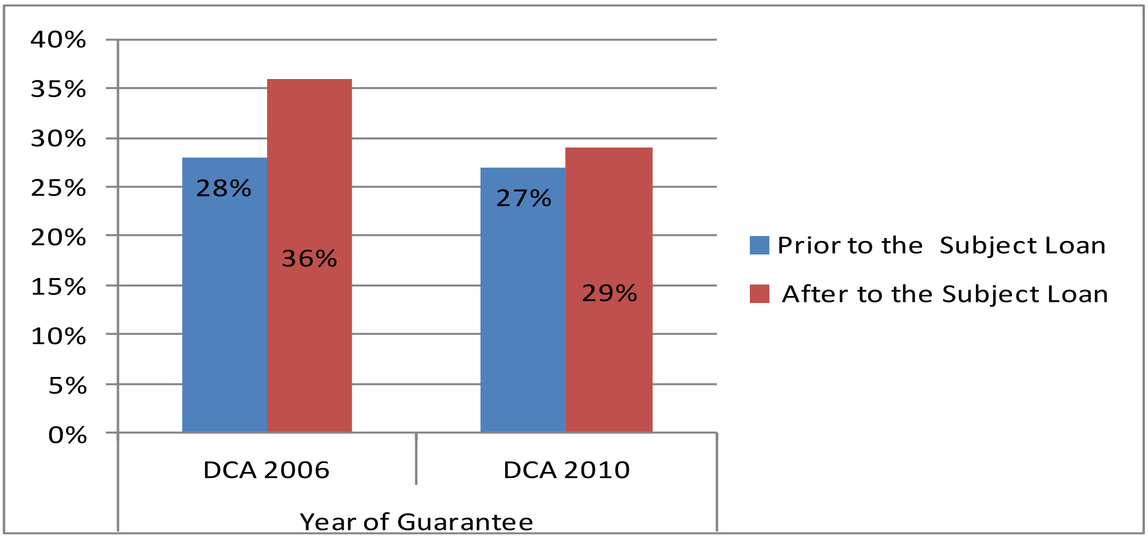
Table 7: Average Gross Sales and Net Profit Margins in Percentage by Region and DCA, 2006 and 2010

		Total	Rift Valley	Nairobi	Coast	Central	Male	Female	DCA 2006	DCA 2010
Prior Gross sales	Mean	2,793,505	4,520,485	1,606,667	402,727	1,233,333	60,000,000	13,000,000	60,000,000	13,000,000
Prior Net Profit %	Mean	27	28	35	26	21	22	35	28	27
After Gross Sales	Mean	30,033,731	47,354,604	1,033,333	685,778	5,231,250	46,610,846	3,095,919	70,726,441	2,362,688

Source: *Evaluation Field Reports*

As the table shows, there was an increase in the mean average in gross sales across all the regions visited, with a rise in enterprises and net profit margins. An interesting aspect of this is that enterprises in Central Region experienced growth in profit margins from 21 percent to 34 percent after the DCA-guaranteed loan. Of interest also is that women-owned enterprises had higher profit margins than those operated by men. Their net profits grew from 35 percent to 42 percent after the DCA-guaranteed loan, whereas that of men-operated enterprises increased from 22 percent to 25 percent. This is in part because women are attracted to retail, trade, and personal services where the cost of entry is low—and therefore have greater growth potential. Because of their limited resources, women also tend to maximize on profits, whereas men can afford high turnovers even with small profit margins. *Figure 2* below, which is based on the sample used, shows that for the 2006 DCA-guaranteed loan after profitability margins were higher than those for the 2010 DCA.

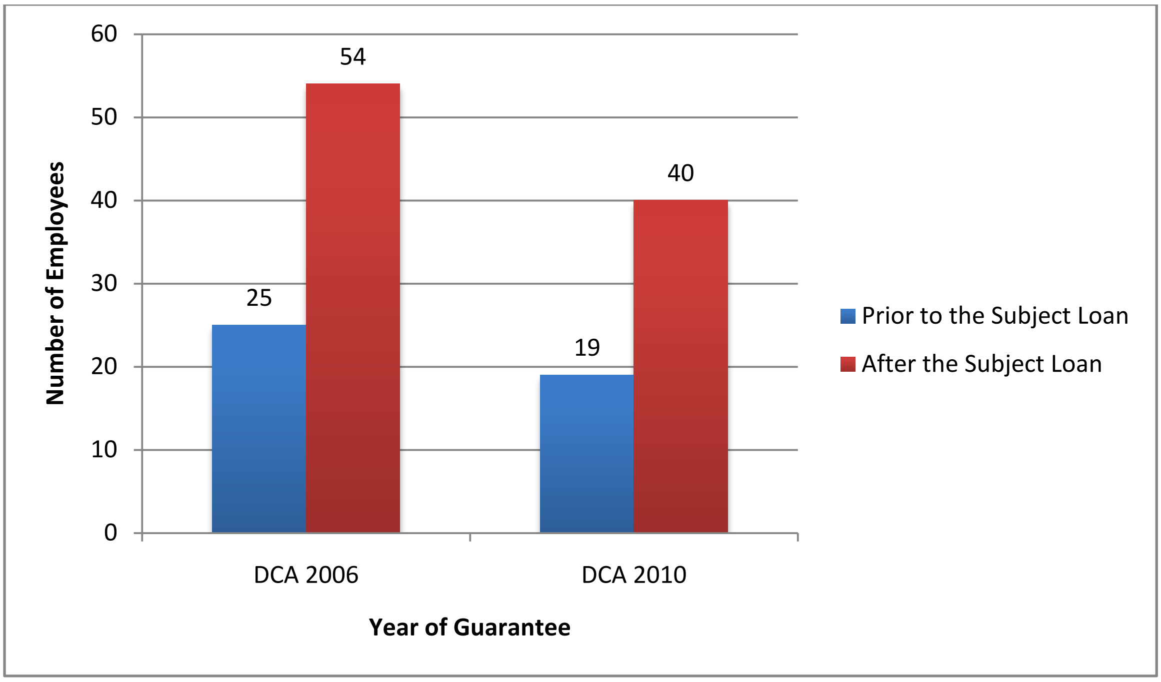
Figure 2: Prior and After Net profits in Percentage for 2006 and 2010 DCA Guarantees



Source: *DCA Evaluation Field Reports*

Job Creation and salaries: The Kenya National Bureau of Statistics put the unemployment rate in Kenya at an all time high of 40 percent in December 2011, and a record low of 12.7 percent in December 2006. According to the 2009 population and housing census, 34 percent of the Kenyan population are aged between 15 and 34. Unemployment among the youth constitutes 70 percent of total unemployment in Kenya. The World Bank recommends development of formal and informal enterprises and of manufacturing and industrial sectors geared toward exports as the best way for Kenya to increase higher-level wage jobs and absorb its growing workforce. The 20 enterprises surveyed under the 2006 guarantee employed 25 persons prior to the DCA loans. The number went up after the DCA loan to 54 employees—a 53-percent increase. Employment for the 49 2010 DCA guarantee enterprises rose from 19 to 40 persons—52-percent increase. The sample is indicative of an employment creation trend among the enterprises funded under both the guarantees. The results of the survey are shown in *Figure 3* below.

Figure 3: DCA 2006 and 2010 Employment Generation

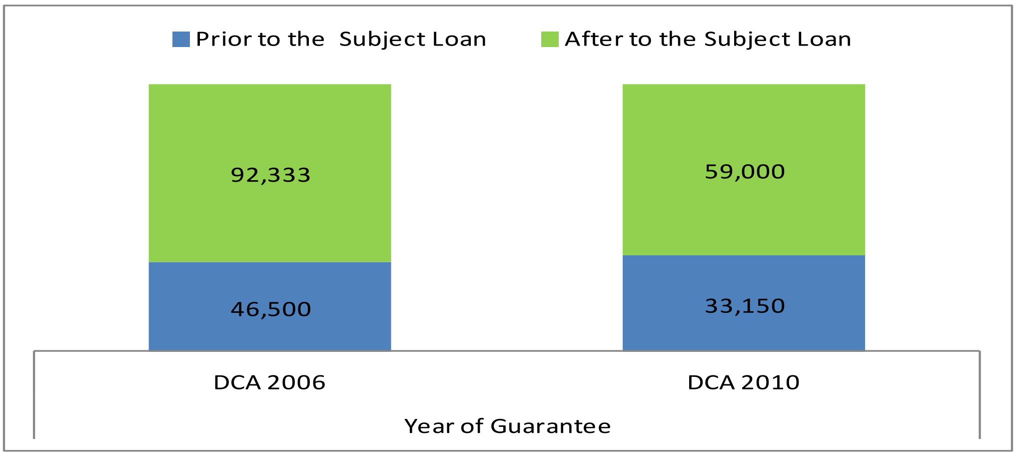


Source: *DCA Evaluation Field Reports*

As observed in other parts of this report, Trade and Commerce received 65 percent and 89 percent of the DCA 2006 and 2010 guaranteed loans, respectively. For the most part, these loans were for working capital mostly to support buying and selling, which has become the dominant occupation driving employment in Kenya. Although manufacturing was a target/ strategic sector under both the 2006 and 2010 guarantees, according to the data received from KCB, no loans were made to this sector under the guarantees. The farming sector, which traditionally has been the main job creator for the family and the economy at large, received only 3 percent of the total loans. Like most other profit-driven institutions, KCB tends to lend more to retail trade and commerce, which offers quick and higher returns.

Overall, the evaluation also noted that there was improvement in average monthly salaries paid to the workers by the 69 enterprises reviewed, in the after subject loan period, as compared to the prior period as shown in *Figure 4* below. Enterprises funded under the 2006 guarantee recorded a 199-percent increase in salaries, whereas those funded under the 2010 guarantee showed a 178-percent increase.

Figure 4: Salary Changes (in KES) for the 2006 and 2010 DCA Guarantees.



Source: *DCA Evaluation Field Reports*

RESULTS OF THE GUARANTEE - OUTCOME LEVEL:

LENDER BEHAVIOR CHANGES DURING AND AFTER THE GUARANTEE

The two DCA guarantees were intended to help KCB lend more confidently, reduce strict collateral requirements, and extend loan tenors for targeted borrowers. The bank was to extend credit facilities to bankable SMEs that often failed to qualify for financing for reasons of lack of or inadequate collateral. The guarantee was also to encourage lending to MSMEs that were majority-owned and/or operated by women, and/or required cash flow-based lending. So the question is, did KCB accomplish the objective of increasing lending to the target client and/or at terms that were softer, i.e., with reduced collateral requirements, lower interest rates, and longer loan terms? Did the DCA guarantee enable KCB to learn and gain confidence to make loans without guarantees? Did the guaranteed borrowers that performed well graduate to unguaranteed loans?

Q.1 Did KCB increase credit to the target sectors outside the DCA guarantee?

Yes, as noted, the targeted sectors under the 2006 and 2010 DCA guarantees were agriculture production and processing; manufacturing; tourism; merchandise/trade; second-tier MFIs; agriculture production/values addition; clean energy (i.e., solar, wind, biogas, and small hydroelectric power generation); commerce, constituency Development Fund projects, SACCOs, and construction. The evaluation was not able to secure data and/or a breakdown of the volume of lending to these target sectors outside the DCA guarantee. This was, however, one of the evaluation questions contained in the package sent to KCB H/Q. Financial data, obtained from KCB's Web site shows that the bank has continued to achieve growth in net loans and advances increasing from KES 198.7 billion in 2011 to KES 211.7 billion in 2012. According to the information provided, most of this growth was in its corporate, SMEs, agriculture, micro-credit, and construction sectors. These were among the sectors targeted by the DCA guarantee. Overall, KCB's objective was to increase its SME customer base to 150,000 accounts by 2012, through a rigorous and ambitious SME campaign dubbed "unlocking your potential." The bank aimed at achieving a lending portfolio of KES 10 billion for the sector by 2012 up from KES 6.3 billion in 2010. To support its SME loan book, KCB's target is to increase the SME deposit book to KES 30 billion by introducing innovative products and services geared toward bridging the gap in the local SME market. To grow its SME portfolio further, KCB has also received support from several other external funding sources, including a KES 9.6 billion ($105 million) loan from the International Finance Corporation.

Q2 Did KCB move into any new sectors/industries?

Yes, KCB did move to new sectors/industries outside those targeted under the 2006 and 2010 DCA guarantees. *Table 8* below shows the targeted sectors highlighted in blue and the sectors not targeted but which received loans from KCB under both the guarantees.

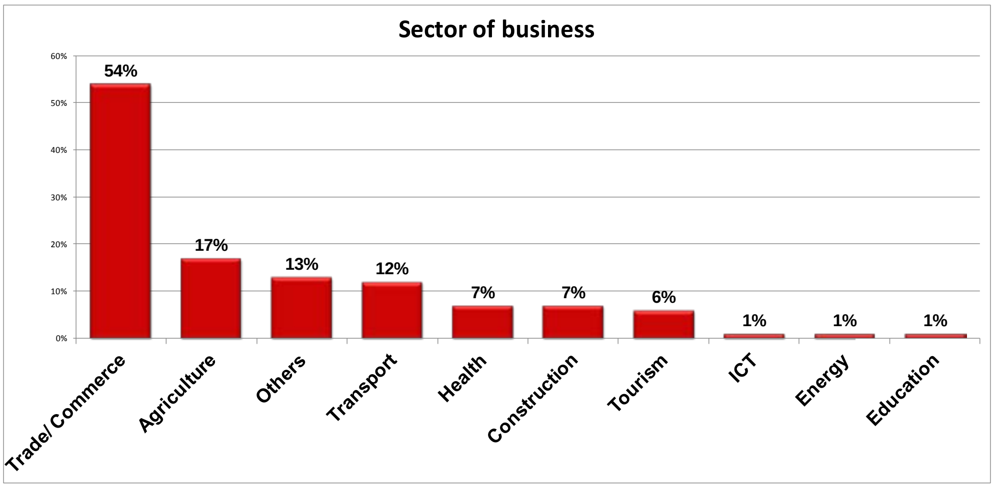
Under the 2006 DCA guarantee, the sectors funded that were not targeted under that guarantee included education, energy, fisheries and aquaculture, transport, and what the bank referred to as other services. The sectors not targeted but funded under the 2010 guarantee were education, housing, health, information and communications, transport, and forest wood. Overall, 69 percent of the credit under 2006 DCA went to targeted sectors and only 31 percent to non-DCA-targeted sectors. Although under the 2010 DCA 91 percent credit went to the targeted sectors with trade and commerce absorbing 89 percent of the credit, only 11 percent of the credit went to non-DCA-targeted sectors. As can be observed, improved management of the 2010 DCA guarantee by the SME unit at KCB H/Q ensured its adherence to target sectors. *Figure 5* below shows a breakdown of the sectors represented among the 69 borrowers interviewed by the evaluation. Among those interviewed by the evaluation, the sectors financed outside those targeted by the two guarantees included health, construction, ICT, and education.

Table 8: Additional Loans Extended by Sectors (targeted/non-targeted) and amounts disbursed

	2006 DCA Guarantee				%	2010 DCA Guarantee				%
SECTOR	**Targeted Sector**	**Total Loans**	**Women Loans**	**Total Disbursed**	**of Total Credit**	**Targeted Sector**	**Total Loans**	**Women Loans**	**Total Disbursed**	**of Total Credit**
Agriculture	✓	38	1	271,776	3	✓	20	6	191,373	3
Construction	No	28	1	228,764	3	✓	16	2	159,490	3
Infrastructure	No	0	0	0	0	✓	1	0	20,656	0
Manufacturing	✓	0	0	0	0	✓	0	0	0	0
Education	No	9	0	55,923	1	No	7	2	81,409	1
Energy	No	6	0	136,142	2	No	0	0	0	0
Fisheries and Aquaculture	No	2	0	11,495	0	No	0	0	0	0
Housing	No	0	0	0	0	No	1	0	12,151	0
Health	No	2	0	121,893	2	No	6	0	25,273	0
Information & Communication	No	30	0	259,301	3	No	5	2	19,392	0
Other Services	No	162	0	1,366,641	17	No	0	0	0	0
Tourism	✓	8	0	82,733	1	No	4	2	29,162	1
Merchandise/Trade/Commerce	✓	759	166	5,117,799	65	✓	773	224	5,102,112	89
Transport	No	24	0	168,663	2	No	13	1	67,922	1
Forest Wood	No	0	0	0	0	No	1	1	7,290	0
Clean Energy	No	0	0	0	0	✓	0	0	0	0
2nd Tier MFI's/MFIs	✓	0	0	0	0	✓	0	0	0	0
SACCO's	No	0	0	0	0	✓	0	0	0	0
CDF	No	0	0	0	0	✓	0	0	0	0
TOTAL		1,068	168	7,821,130	99		847	240	5,716,230	98

Source: *KCB Transaction Summary*

Figure 5: Sectors of Business Sampled by the DCA Evaluation Interviews



***Source**: DCA Evaluation*

Q.3 Did KCB move into new types of borrowers?

No, the new types of borrowers identified under the two DCA guarantees included second-tier MFIs, MFIs, and SACCOs. In its internal circular dated June 2, 2008, KCB highlighted the availability of loans to MFIs and SACCOs to a maximum of KES 20 million repayable over 48 months. No loans to these types of borrowers were recorded under either of the DCA guarantees. The DCA guarantees had identified these as key target sectors because they are a growing segment of the financial sector in Kenya that is highly constrained by lack of lending funds. Most SACCOs face a very high demand for loans from their members and are forced to seek additional funding from external sources. The challenge is that most SACCOs are not able to access external loans due to their low capital base, lack of adequate collateral, high cost of external funds, governance issues in some instances, and low risk rating. Information from the KCB Web site shows that the bank has more than 500 accounts for various co-operative societies and has established strategic partnership with some of the SACCOs. KCB normally requires collateral from these institutions to secure their facilities, which may be a challenge to the second-tier MFIs requiring such funding. Some of the large MFIs like Afya SACCO are able to adequately secure their facilities with the bank, and hence would not qualify for the guarantee support. Loans from KCB at prevailing rates of interest would also be too costly for the smaller MFI/SACCO clients. These institutions also prefer longer repayment periods than those that KCB is willing to give.

Q.4 Did KCB move into new types of loans?

***Loans to women (Grace loans)*:** The 2006 guarantee was to target MSMEs that were majority-owned and/or operated by women and required cash flow-based lending. This requirement was intended to mitigate the major constraint that most women face in their effort to borrow from commercial banks—the high collateral requirements. This is a great burden on prospective women borrowers since women do not have title deeds and other fixed assets that they can pledge. Because most banks make lending decisions largely based on the value of assets pledged by a borrower rather than a borrower’s expected revenues and cash flows, the DCA guarantee was to help KCB give women loans based on the cash flows. Loans extended to women borrowers under the two guarantees are shown in *Table 9*. Under the 2006 DCA, there were 167 loans to women, representing 15 percent of total loans, whereas under the 2010 DCA, there were 232 loans representing 22 percent of the total loans. The majority of the women borrowers were in trade and commerce for a total of 166 loans under 2006 DCA and 224 loans under the 2010 DCA.

Table 9: Loans to Female Borrowers Under 2006 & 2010 Guarantees

DCA Guarantee	2006			2010		
Sectors Funded	**Total**	**Women**	**Total**	**Total**	**Women**	**Total**
Agriculture	38	1	39	20	6	26
Construction	0	0	0	16	2	18
Other Services	162	0	162	0	0	0
Tourism	8	0	8	0	0	0
Trade/Commerce	759	166	925	773	224	997
Total	**967**	**167**	**1134**	**809**	**232**	**1041**
% of Total		**14.73**			**22.29**	

Source: *KCB Transaction Summary*

The KCB Grace loans were tailor-made for individual women entrepreneurs and women entrepreneurs in groups. Women were eligible for loans of up to KES 0.5 million for individual women entrepreneurs and up to KES 5 million for women entrepreneurs in groups. These loans had a six-month grace period and were repayable in 36 months. Unfortunately, the Grace loan scheme was discontinued by the bank due to poor management and follow-up by KCB staff during the six-month grace period that resulted in heavy defaults and loses for the bank. Grace loans constituted a large part of the 2006 DCA guarantee loans offset. The evaluation interviewed 20 women (nine from the 2006 guarantee and 16 from the 2010 guarantee) out of the total of 69 interviews conducted. In January 2008, KCB H/Q issued guidelines to all its branches on women loans. No cash flow-based lending was granted to women as had been envisaged under the 2010 DCA. Information received from KCB H/Q is that cash flow-based lending is still under consideration. The bank now uses a blend that includes stocks, title deeds, and cash flows.

The low number of women borrowers under the two DCAs could be due to the preference by women to borrow through their chama/groups system, SACCOs, or financial institutions that are more women-friendly such as Faulu Kenya, Kenya Women Finance Trusts, or Jamii Bora. Women respondents in particular consider KCB to be a rich man's bank. The women complained of many charges levied on loans, including some hidden costs. With the chama/groups, women know what the interest rate is, and the repayment never changes for the duration of the loan. Tradition and culture also play a big part in the role of women in Kenya, the extent to which they can hold bank accounts, run a business, or even borrow funds. It is common knowledge that women do not have assets that they can pledge as security to the bank, and when they seek to do so they are obliged to obtain clearance from their spouses and family members.

As women do not own assets, they cannot freely approach the bank, which accounts for the low uptake of loans. Again, that is why women flourish under the chama/groups system where they are not required to produce any security except their savings/shares and guarantors. There is also the women's Enterprise Fund established in August 2007 that has extended more women access to finance for setting up business enterprises. The funds are channeled to the grassroots through multiple sources, including constituency development committees. As of 2010, some 166,610 women had benefited from the funds with investments in wholesale and retail trade, poultry, dairy farming, hair salons, basket weaving, transport, and communications.

Given the challenges cited above in particular, the USAID/DCA guarantee may have to rethink its strategy in supporting loans to women in the future. One option is through the KCB Microloans products that use a mechanism similar to that used by the chama and institutions considered women-friendly. An alternative is for the DCA to incubate similar guarantee facilities in the women-friendly institutions such as those mentioned above. Besides, KCB remains very conservative and is yet to rid itself of the tag as a government parastatal and modernize its business approach. The bank is still trapped in its historical performance and has been very slow to embrace the changing practices adopted by its competition, such as the Equity Bank, NIC Bank, the Faulu, Maisha Bora, and Kenya Women Finance Trust Fund. During discussions with KCB/HQ staff, the evaluation was informed that the DCA guarantee has enabled the bank to rethink the collateral approach and it has been exploring ways to break away from its tradition of secured loans by creating products that are cash flow-based.

***KCB SME product*:** The SME product was first launched by KCB in 2008—two years after the 2006 DCA guarantee was activated. To be eligible, SME enterprises are required to have total investments of less than KES 50 million and well-maintained accounts over a minimum of six months. SMEs can borrow up to KES 20 million that they can use to purchase whatever is needed to expand their business. This is up from the KES 5.0-million limit set before. KCB SME loans targeted those SMEs unable to borrow primarily due to the lack of tangible security. The loan can be used for expansion or purchase of machinery or to boost working capital. Securities accepted include title deeds (where applicable), chattel mortgage over machinery and equipment, log books, debenture over company assets, letters of undertaking, or confirmed letters of credit on supported guarantees. SME loans are repayable within a maximum time frame of three years.

***Biashara Club*:** KCB Biashara Club provides a range of value adding services to SMEs aimed at growing their businesses even further. Members who pay a KES 1,000 monthly fee can attend workshops on entrepreneurship and capacity building, have the opportunity to network and source for new customers for their businesses, receive business advisory services through SME management seminars and workshops in a variety of relevant topics, and participate in business trips to tap into new markets. The challenge to most clients as expressed to the evaluation is that they are unable to participate in these activities due to the high demands of their work. Most small businesses are very much dependent on the business owner. The evaluation noted that the level of education of the respective clients also affected their appreciation the Biashara Club and its various activities.

KCB Microloans: As an SME product follow-up, KCB established a microloans department in 2011. KCB Boresha Biashara loans are designed to finance MSMEs that require working or investment capital to improve their businesses. The security requirements are very flexible and include chattels on household items, shares, and business stock. The loan minimum is KES 5,000 and the loan maximum is KES 500,000. These loans have a flexible repayment term of up to 12 months. Eligibility criteria include the ability to repay and must have a minimum of one-year experience in the business to be financed. Given the above-cited classification, it seems that a good number of DCA loans would fall under the microloan category.

Q.5 Did KCB move into any new loan terms?

Loan terms to targeted sectors under the guarantee crucial to an SME are collateral requirements, loan tenor, and interest rates and other charges.

- *Collateral*

The high collateral requirements are caused by the imperfections of financial markets that make banks consider lending to be a risky business. Even where loans are secured, banks have had challenges making recoveries and enforcing contracts. The legal processes in Kenya are long, time-consuming, and costly, and the outcome is never assured. Consequently, under normal lending requirements, banks in Kenya—and KCB is no exception—impose a very high collateral requirement of up to 150 percent collateral coverage on lending. Most SMEs confronted with such a stringent requirement, high interest rates, and short repayment period are unable to borrow. They find alternative sources of finance that in most cases are even more expensive. The existence of the guarantee enabled KCB to soften its collateral requirements and to introduce alternative collaterals such as stocks, logbooks, treasury bills, life insurance, cash flows, and guarantees that were not previously considered as suitable collateral in the lending policy of the bank. *Table 10* shows how KCB was able to adjust its security requirement margins with the DCA guarantees, enabling more clients to qualify for loans and others to qualify for bigger loans.

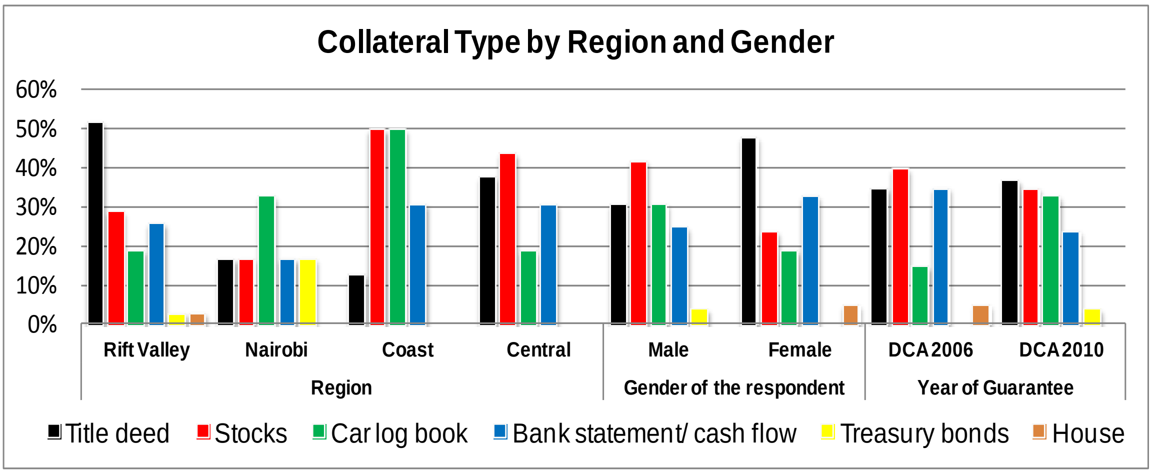
Table 10: KCB-Adjusted Collateral Margins with DCA Guarantees

Type of Security		Discounted Value % of CMV	With USAID Guarantee
Land	Urban Residential	75%	125%
	Urban Commercial/Industrial	65%	115%
	Urban Specialized	60%	110%
	Other Municipality and Township	60%	110%
	Other Municipality and townships - Specialized	50%	100%
	Rural	50%	100%
	Rural Specialized	40%	90%
Debentures	Plant Machinery and Equipment	20%	70%
	Debtors	60%	110%
	Stocks	15%	65%
Publicly quoted Stock and Shares		60%	110%
Life Policy (Surrender Value)		90%	140%
Cash, Treasury bills/Bonds		90%	140%
Pledge over Merchandise		50%	100%
Assignment of Receivables		65%	115%

Source: *KCB H/Q Circular of June 2007*

There was no uniformity on how these margins were applied by KCB branches. In places like Iten, Nandi Hills, and Mombasa where there is a serious issue of lack of title deeds, the branches used stocks and chattels mortgage on machinery and equipment to secure facilities. In Mombasa in one case involving a women borrower, the branch used rental income cash flow as security, coupled with guarantees. *Figure 6* below gives a synopsis of collateral preferences in the four regions visited by the evaluation.

Figure 6: Collateral by Type, Region, Gender, and Guarantee



Source: *DCA Evaluation*

The analysis carried out by the evaluation shows that in Nairobi, logbooks were the preferred form of collateral; in the Coastal Region, titles deeds and logbooks were preferred; in the Rift Valley, the majority of borrowers provided KCB with title deeds; and in Central Kenya, stocks were preferred. Where the value of the collateral was not adequate, the DCA guarantee would kick in and provide the 50-percent security margin required. The survey conducted by the evaluation shows that 48 percent of the women interviewed provided title deeds, where 42 percent of men provided stocks. See *Table 11* below. Where women are concerned, this defeats the purpose of the DCA guarantee, which was to lighten the collateral burden on women, who normally do not have title deeds to charge as security.

Table 11: Type of Securities Used to Secure Loans to Women Borrowers

Collateral – Type	Gender of the respondent	
	Male	Female
Title deed	31%	48%
Stocks	42%	24%
Car log book	31%	19%
Bank statement/ cash flow	25%	33%
Treasury bonds	4%	0%
House	0%	5%

Source: *Evaluation Field Reports*

An analysis of the mean collateral cover value of the 69 enterprises sampled shows that the collateral requirements on women borrowers was higher with a mean of 152 percent as compared to male borrowers with a mean of 111 percent. The need for higher collateral coverage for women borrowers shows that KCB considers women to be higher-risk borrowers than men. This is contrary to the trend in most MFIs and SACCOs where collateral requirements for women are much lower. It has been found that the loan repayment performance by women is far better than that of the male borrowers. The DCA guarantee provision was that KCB would provide women with cash flow-based loans due to constraints that they face in providing tangible securities. The lack of financial history by women within the banks is also an issue that constrains banks and forces them to demand tangible collateral. The evaluation noted that KCB did not give any cash flow-based loans to women as was anticipated. All the loans to women were secured with title deeds, stocks, or logbooks. As noted above, the lack of financial records and stable income flows by most SMEs is a factor that hinders cash flow lending by banks. *Table 12* below shows that the 2006 DCA guarantee loans had on average a higher collateral cover requirement of 172 percent, as compared to the 2010 DCA requirement of 100 percent. Again, this could be attributed to the confusion in the management of the 2006 DCA whereby the branch staff did not really follow procedure. There was much more adherence to the guarantee provisions under the 2010 guarantee than there was under the 2006 guarantee.

Table 12: Collateral Cover Margins Under the 2006 and 2010 Guarantee Loans

		Total	Rift Valley	Nairobi	Coast	Central	Male	Female	DCA 2006	DCA 2010
Loan Amount	Mean	983,507	871,935	1,169,667	1,223,688	889,688	1,081,917	758,571	969,000	989,429
Subject Lender: Collateral value - Prior	Mean	1,188,889	1,383,333	1,450,355	950,000	940,000	1,202,500	1,150,00	1,668,750	986,842
% Collateral Cover Prior		121	159	124	78	106	111	152	172	100

Source: *DCA Evaluation Field Reports*

- *Loan Tenor*

Review of KCB guidelines shows that the loan tenor allowed on term loans was three years, working capital up to 12 months, and for MFIs and SACCOs between two and four years. An analysis of KCB TSs shows that the tenor used by the bank on working capital and investment loans exceeded KCB H/Q guidelines. *Table 13* shows the minimum and maximum tenors as contained in the TS. Under the 2006 DCA, the minimum tenor for working capital was three years, whereas it was six months under the 2010 DCA. The difference was due to the better management of the 2010 DCA by the SME unit that eliminated the confusion between what constituted working capital vs. capital investment by KCB staff. DCA 2006 had a longer tenor for investment loans at 45 months as compared to the DCA 2010 tenor of 36 months. In both cases, working capital loans enjoyed a maximum tenor of 48 months. The normal practice is for investment loans to have a longer tenor than working capital.

Table 13: Loan Type and Tenor Under 2006 and 2010 DCA Guarantees

	2006 DCA Guarantee		2010 DCA Guarantee	
Type of Loan	Tenor on Months			
	Minimum	Maximum	Minimum	Maximum
Working Capital	3	48	6.5	48
Investment Loans	12	45	12	36

Source: *KCB Transaction Summary*

- *Interest rates*

During discussions with the DCA guarantee borrowers, the review noted that virtually all of them were not sure of the interest rate charged on their loans. They were not able to keep track of frequent changes in interest rates, especially because the bank does not always inform them when there are changes. Nevertheless, one thing they all complained about was high interest rates charged by money lenders. The interest rates mentioned by respondents ranged from a high of 27 percent to a low of 18 percent, as shown in *Table 14* below. In September 2012, KCB lowered its base lending rate from 22 percent to 19 percent in response to CBK's revision of its base lending rate by 350 basis points to 13 percent. The downward revision of base lending and mortgage rates was due to the improvement in the overall cost of credit and easing of inflationary pressures. Overall, the cost of credit is expected to improve further as the monetary policy indicators all point toward a stable economic environment in 2013.

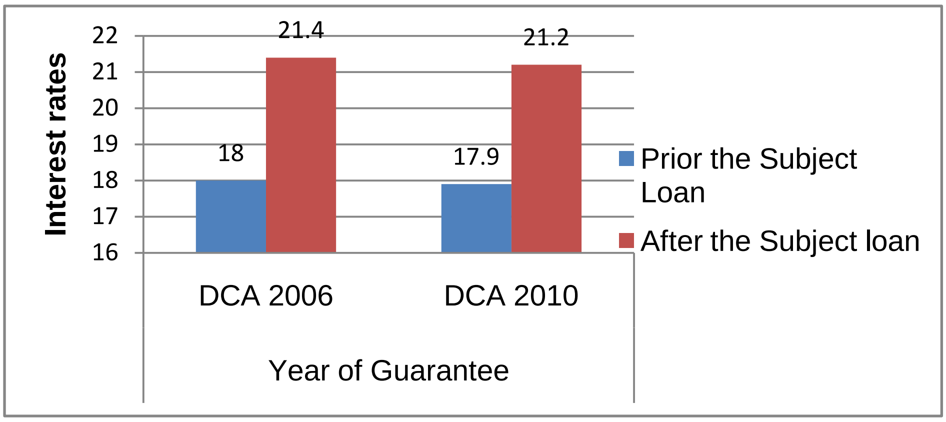
Table 14: Range of Interest Rates Charged on DCA 2006 and 2010

	Total	DCA 2006	DCA 2010
Minimum	18	18	18
Mean	21	20	21
Maximum	24	24	27

Source: *Evaluation Interviews*

To determine if KCB in any way improved its interest rate terms, the evaluation asked the 69 borrowers about their experience with loans prior to and after KCB's DCA-guaranteed loans. The outcome is analyzed in *Figure 7* below.

Figure 7: Average Interest Rates Prior to and After the DCA Guarantee Loans



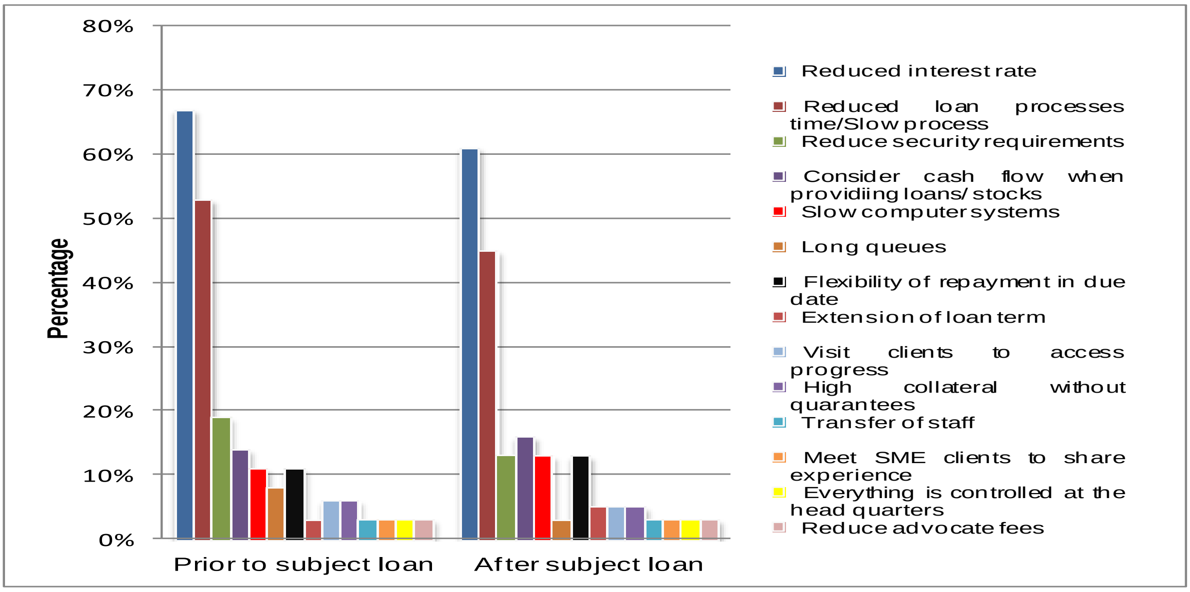
Source: *DCA Evaluation Field Reports*

Prior to the 2006 DCA loan, borrowers were paying interest rates of 18 percent and after the subject loans this rose to 21.4 percent. Prior to the 2010 guarantee, borrowers were paying an average of 17.9 percent and after the subject DCA loan this rose to 21.2 percent. These rates were very close to the mean rate charged by KCB of 20 percent under the 2006 DCA and 21 percent under the 2010 DCA. KCB largely used the market rates of interest. Except for Biashara Club members who received a 1-percent interest discount, DCA guarantee members did not receive any special interest rate consideration.

- *Recommendation of DCA Borrowers on KCB Terms:*

The evaluation sought opinions from the sampled borrowers on loan terms that they considered as the most pressing in the period prior and after the subject DCA loan. The summary of the responses is captured in *Figure 8*.

Figure 8: Borrower Recommendations on KCB Loan Terms



Source*: DCA Evaluation Field Reports*

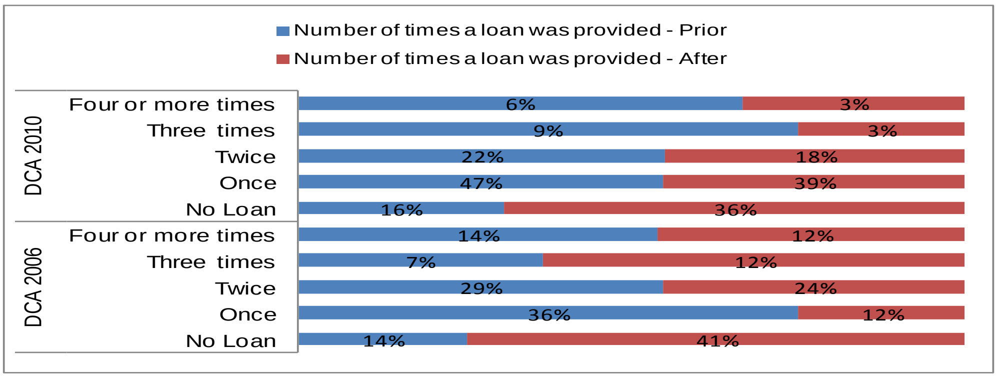
In both period scenarios, the four top issues that emerged were that KCB should i) consider reducing interest rates on loans, ii) reduce loan-processing times, iii) reduce security requirements, and iv) consider cash flow as a substitute/supplement for collateral when providing loans. Others mentioned are as presented in *Figure 8*. Overall interest spreads in Kenya are very high. According to CBK, as at January 2013, the average lending rate stood at 18.13 per cent, whereas the deposit rate was 6.51 per cent—leaving a clean interest margin of 11.62 per cent. Reasonable spread should be about 5 percent. Apart from the interest on the loan, all the borrowers have to pay processing fees and insurance cover that are added to the total cost. To stimulate economic activity CBK has started easing monetary policy, lowering the Central Bank Rate (CBR) to 9.5 percent as at the time of the evaluation, from a high point of 18 percent in 2012. Commercial banks have started to respond to CBK's action and have started reducing their average lending rate.

For a long time, the pricing of loans in Kenya has been a source of public debate with different players. Transparency in pricing is critical because borrowers have the right to know the exact price of products in the market. Non-transparent or opaque pricing prevents consumers from making informed decisions about borrowing. The CBK has in the past blamed insufficient market information for the low rate at which Kenyans have been taking credit and has been pushing the banks to be more transparent with customers on interest rates and other charges. CBK therefore requires that all banks publish any changes in their charges, including loan interest. Even where banks publish changes, most borrowers do not take note.

Q6. To what extent were the DCA guarantees responsible for improving access of partners' customers to credit outside the guarantees?

For first-time borrowers, the DCA guarantee provided them with the opportunity to establish a credit record, which greatly improved their chances to access credit outside the guarantees, within or outside KCB. In addition, for those that did not have the traditional type of collateral, the bank used stocks and other forms of collateral to secure their loans. *Figure 9* provides an analysis of the sampled 69 borrowers and the proportion of those with access to credit prior and after the DCA subject loan.

Figure 9: Additional Loans Extended to KCB Clients Outside the DCA Guarantee



***Source**: DCA Evaluation Field Reports*

Prior to the 2006 DCA guarantee, 14 percent of the sampled borrowers had not accessed loans (i.e., they were new borrowers), 36 percent of them had borrowed once, 29 percent twice, 7 percent three times, and 14 percent four times or more. These loans were either from KCB or other institutions, but mainly KCB. After the DCA subject loan, 41 percent of the 2006 DCA guarantee borrowers opted not to borrow again. Considering that the DCA 2006 guarantee loans are all fully repaid, this constitutes a large proportion of prospective repeat borrowers lost to KCB. It was noted that 12 percent had borrowed again once and 12 percent three times and 12 percent four to more times. More of the DCA 2010 guaranteed borrowers were willing to access credit a second, third, and fourth times. As seen from the table, 16 percent of the DCA 2010 guarantee borrowers were first-time borrowers, 47 percent had borrowed once, 22 percent twice, and 9 percent three times, and 6 percent four times. Of these, 36 percent of those interviewed had not borrowed again, 39 percent had borrowed once, and 18 percent three times. This showed a much improved scenario over the 2006 situation.

Unfortunately, borrower loans outside the guarantee became impossible when the guarantee expired. Those that applied for additional facilities were asked to bring tangible securities that they were still not in a position to produce. According to the customers interviewed, it takes time to build the assets such as land and buildings that are required by KCB. The borrower will require several loan cycles to build a strong financial base and reserves from which to acquire other investments that can be used as collateral by the bank. Several clients interviewed during the evaluation who had been turned down by KCB due to lack of collateral were in the process of moving, while others had already moved to other financiers. KCB still needs to develop skills for analyzing SMEs and develop security-free loan products.

In the Githuguri–Central Region, which is a dairy farming area, farmers complained that KCB loan products were not suited for the agricultural sector. The bank also lacked personnel who could address the issues and challenges faced by dairy farmers. There is a need also for KCB to have a clear operational manual on procedures and requirements under the DCA guarantees to ensure a speedy application processing and confirmation of the decision. It may also be worthwhile for those applications that do not satisfy the requirement to be rejected at the branch level, with only those with the highest probability of approval going to the HQ. This way the branches will not create unwarranted expectations by the client. Borrowers also complained that the setting of the loan repayment dates should take into account the business cycle of the borrower to avoid causing hardship in loan repayment. For example, for some businesses, setting loan repayment at the end of the month when salaries, rent, and other payments are due should be avoided. Borrowers who operate schools recommended that the loan repayment should follow the school calendar when the borrower's cash flow is at its peak.

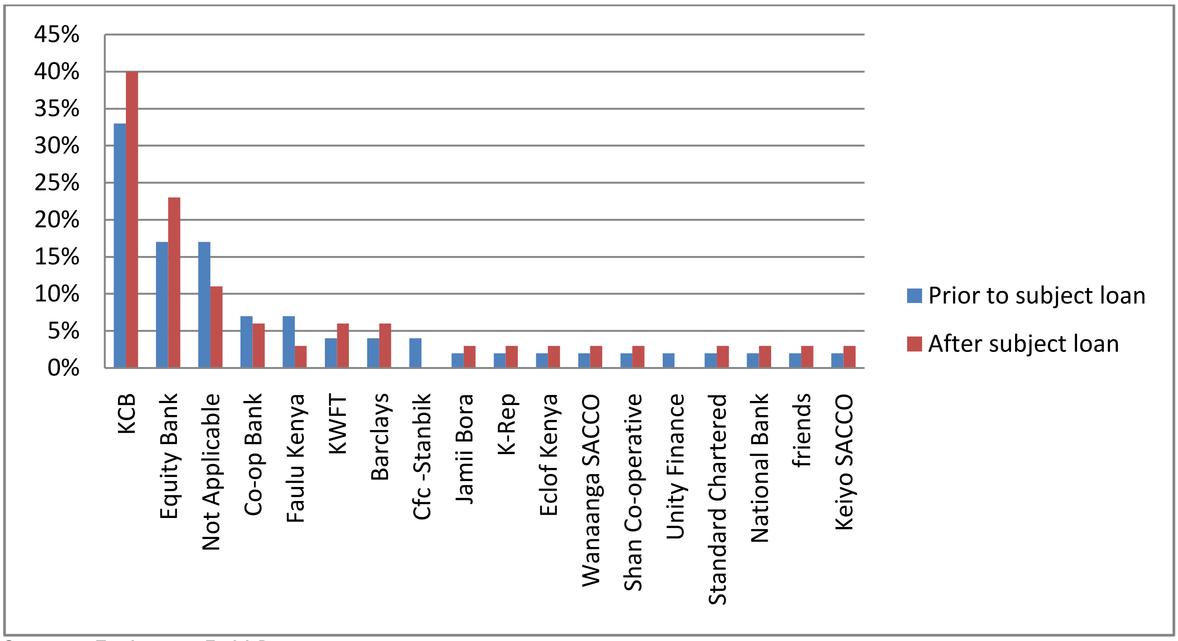
What emerged during the evaluation was that KCB services are not harmonized across all the branches. The quality of service depends on the respective branch managers and the staff. For example, in Mombasa the evaluation noted that clients from surrounding branches preferred to operate from the town center branch. The evaluation noted that the branch had a friendly and very professional atmosphere that appealed to a certain group of clients. These differences were noted across all the branches sampled by the review. It is important that a client visiting any KCB branch be confident of receiving the same quality of service to avoid migration of customers to those branches where the services were perceived to be better.

BORROWER BEHAVIOR CHANGE BEFORE AND AFTER THE GUARANTEE

Q1. Did borrowers seek loans before and after the guaranteed loan from the partner financial institution or other financial institutions? If so, were the requests successful?

As noted before, only eight DCA loan borrowers out of the 69 sampled were new borrowers. The rest had either borrowed from KCB or other institutions. *Figure 10* below gives a breakdown of the institutions mentioned by the 69 sampled borrowers with whom they had received loans prior to and after the DCA subject loan.

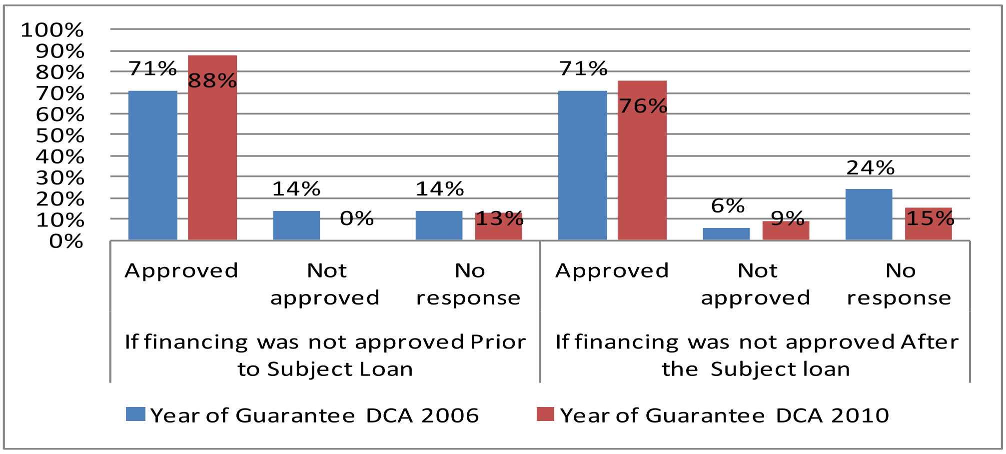
Figure 10: DCA Borrower Loans from Partner and Other Financial Institutions Prior to and After the KCB loan



***Source**: Evaluation Field Report*

In terms of approvals, most of those interviewed confirmed that their loans were approved either within KCB or by other institutions. The responses are reflected in *Figure 11* below. In the case of both DCAs, financing approvals improved after the subject loan, rising from 71 percent to 88 percent under the 2006 DCA and from 71 percent to 76 percent under the 2010 DCA. As mentioned, the evaluation noted that most clients (especially first-time borrowers) who had taken guaranteed loans with KCB had opted to move to other financial institutions. This is because they had failed to secure follow-up loans with KCB, as they were unable to satisfy KCB collateral requirements. Unlike KCB, information made available to the evaluation was that other banks were more flexible and willing to use other forms of collateral than KCB. Borrowers who had a good track record with KCB under the DCA loans were able to secure loans from other institutions easily. KCB staff are very aware of this and are quite concerned at the rate with which KCB is losing business to competition. There is a need for KCB to rethink its lending collateral requirements, especially for borrowers with a good track record.

Figure 11: Proportion of Interviewed Borrowers with Approved Loans



***Source**: DCA Evaluation Field Reports*

Q2. To what extent were the DCA guarantees responsible for improving the borrowers' willingness to seek credit?

As the terms with the DCA guarantee favored their businesses, 25 percent of those interviewed under the 2006 DCA and 55 percent under the 2010 DCA guarantee (especially the first-timers) were eager for a second loan with KCB. See *Figure 12* below. The use of stocks as collateral was new to KCB and was highly appreciated by KCB clients, and this even attracted considerable new business for the bank. Unfortunately, KCB was not able to sustain the DCA guarantee terms and soon resorted to its old collateral requirements. Consequently, many who had applied for follow-up facilities were not able to secure them due to changes in collateral requirements. The figure above shows that the proportion of those who received loan approvals after the subject loans among those interviewed increased under both DCA guarantees. This could be from KCB or other sources. In the Iten–Rift Valley region, the evaluation met a business woman who had been forced to scale down her school uniform business when she failed to secure a follow-up loan with KCB. The initial loan had been secured by her stocks, with a chattels mortgage over her sewing machines. The subsequent loan from KCB was small and could not sustain the expanded level of her business. She was very disappointed, although hopeful that KCB would eventually reinstate the old terms. She has no title to pledge, as this is one of those parts of Kenya where residents do not have title deeds.

From the discussions with KCB field staff, the evaluation noted that KCB's lending to SMEs had become very dependent on the cushioning provided by the DCA guarantee. Although there are plans to do so, the bank has not evolved similar loan products to enable them to lend any subsequent loans without the guarantee. Consequently, clients are frustrated and many have looked or are in the process of looking for alternative funding sources outside KCB. The evaluation visited one such client in Nairobi who had secured a KES 3-million loan with Jamii Bora Bank. He had an earlier loan of KES 1.5 million with the KCB Moi Avenue Branch under the 2010 guarantee. Unfortunately, KCB was unable to provide him with a follow-up loan due to inadequate securities.

RESULTS OF THE GUARANTEE – IMPACT LEVEL

DEMONSTRATION EFFECT OF THE DCA GUARANTEE

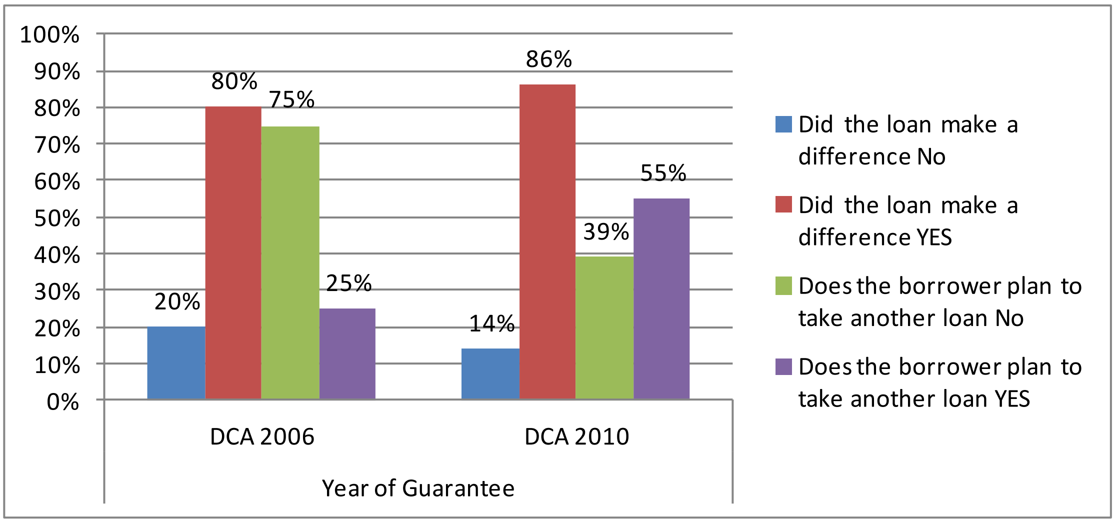
Q1. What role if any did the DCA guarantee play as a demonstration model?

By covering up to 50 percent of the net loss on the principal amount of loans made by its partners to help mitigate the risks associated with lending to new sectors or new borrowers, the DCA guarantee's ultimate goal was to demonstrate to KCB and other lenders the sustainability and profitability of the SME sector. By so doing, the guarantee would allow the lender/KCB to expand financial services to underserved economic sectors and social groups, which they had previously considered to be "High Risk."

Prior to the DCA guarantee, KCB was not a player in the SME market. But, with the market skills and confidence it gained through loans to DCA-guaranteed borrowers, the bank has continued to develop new SME products, partnered with other financiers, increased its deposit levels, and mobilized resources through rights issues in order to build its SME portfolio in addition to other lending activities. At the borrower level, DCA-guaranteed loans have had a big demonstrative effect on first-time borrowers. Those that successfully repaid their loans have the confidence to seek out even bigger loans from KCB or any other players on the market.

The introduction of stock as collateral had a very positive effect on the bank's ability to attract and lend to those young entrepreneurs in trade and commerce that did not have title deeds to pledge. In Iten-Rift Valley, the evaluation met with a young electronic shop owner who had borrowed KES 1.0 million using stocks as collateral. He had also introduced four of his friends to the bank who were able to secure loans. Unfortunately, the failure of KCB to give them additional facilities with the expiration of the DCA guarantee has discouraged them. By reverting back to full security requirements, KCB is likely to erode all the gains it has achieved in financing SMEs. Information provided to the evaluation is that the bank is in the process of developing a partially secured lending product that is awaiting approval for lending to SMEs. Apart from the DCA guarantee, the Financial Sector Deepening program has partnered with a number of Kenyan banks (ABC Bank, Chase Bank, and NIC Bank) to develop and grow the use of supply chain finance products tailored to SMEs and to get the banks to understand and mitigate the risks associated with SME financing. *Figure 12* below shows how the borrowers interviewed view the impact of DCA guaranteed loans. As can be observed from this figure, more than 80 percent of those interviewed agree that the two DCA guarantees made a difference to their lives. Asked if they planned to take additional loans, 75 percent of those interviewed under the 2006 DCA and 39 percent under the 2010 DCA were reluctant to do so. *Figure 12* shows the impact of the DCA guarantee on borrowers as measured by the effect of the loan on their businesses and their willingness to borrow again.

Figure 12: Impact of DCA Guaranteed Loan on Borrowers

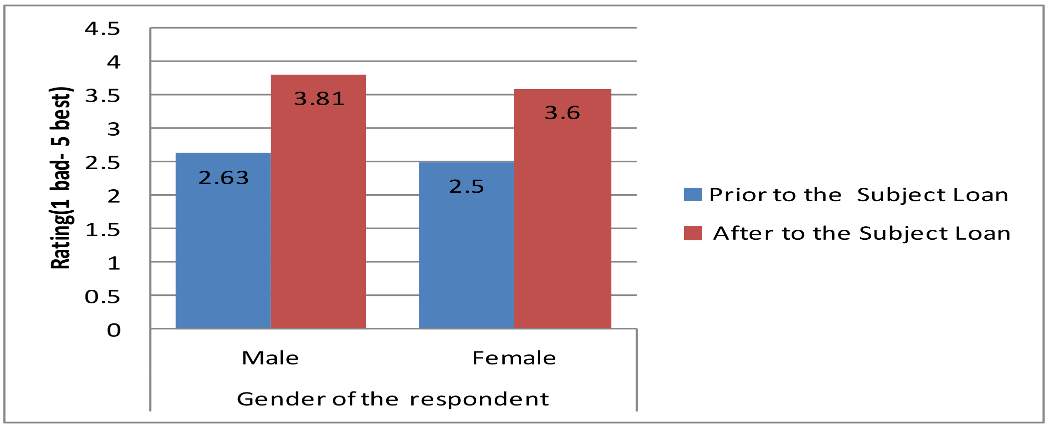


Source: *DCA Evaluation Field Reports.*

SOCIAL IMPACTS ON DCA BORROWERS

Quality of Life: One of the borrower evaluation questions sought to gauge how and if the DCA-guaranteed subject loan had impacted the borrower's quality of life. Their assessment of the changes in their quality of life is represented in *Figure 13* below.

Figure 13: Impact of the DCA Guarantees on Quality of Life

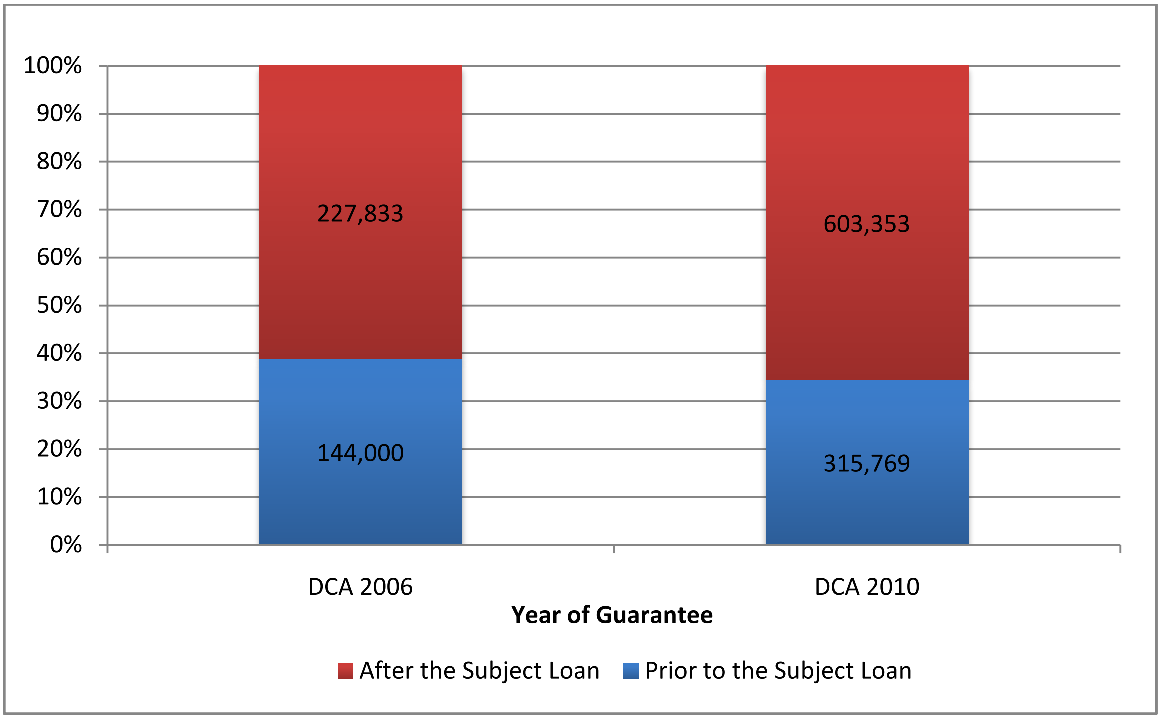


Source: *DCA Evaluation Field Report*

This was a very difficult part of the questionnaire to administer and for the borrowers to quantify. The change in quality of life is relative and the same criteria will not apply across all the respondents. The evaluator, however, took time to explain to the respondents what the question meant to help them gauge any perceived change in their social status prior and after the subject loan. It was difficult for some borrowers to identify if there had been any change in their quality of life. Others were able to record a change in the quality of life even with that one loan such as a better house, better schools, or improved diet. Overall, as shown in the figure above, both men and women recorded a change in quality of life after the subject loan.

Savings: Results of the borrower questionnaire also revealed that the borrower level of savings on average improved in the period after the subject loan with the improvement being higher under the 2010 DCA guarantee. Under the 2006 DCA guarantee, borrower savings rose by 37 percent, whereas savings rose by 48 percent under the 2010 DCA. See *Figure 14* below.

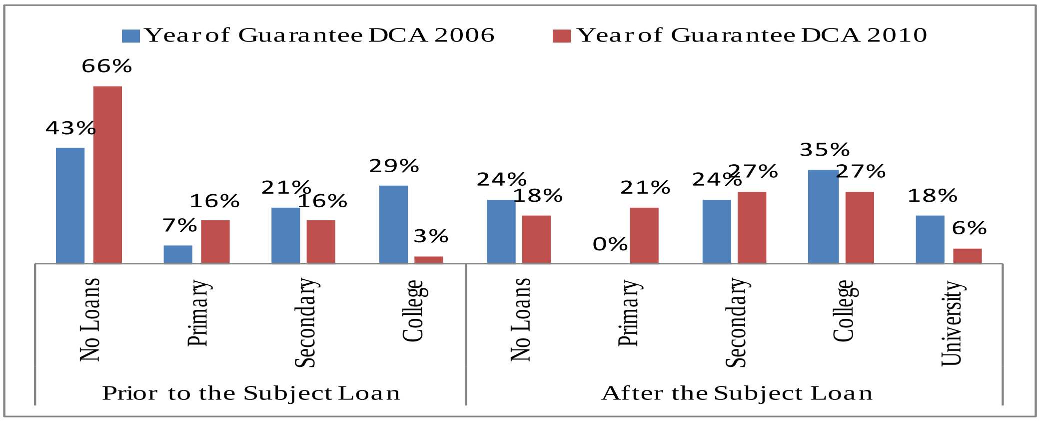
Figure 14: Average Value of Saving in Any Formal Account 2006 and 2010 DCA



Source: *DCA Evaluation Field Reports*

Education Levels: A good measure of impact is the level of education attained by borrower's children over the period prior and after the subject loan. With improved businesses, profits, and savings, DCA borrowers were able to send more children to institutions of higher learning. *Figure 15* below shows the levels of education attained. It is noted that after the subject loan, both DCA 2006 and 2010 borrowers reported having children at university level. As reported by respondents, college-level enrollment rose from 29 percent to 35 percent for DCA 2006 borrowers and from 3 percent to 27 percent for 2010 DCA borrowers.

Figure 15: Education Levels Attained by DCA 2006 and 2010, Prior to and After the Subject Loan



***Source**: DCA Evaluation Field Reports.*

SUMMARY AND RECOMMENDATIONS

SUMMARY OUTPUT LEVEL

The two DCA guarantees enabled KCB to launch into the SME sector without the fear of incurring heavy losses and to develop a clear strategy for its future involvement in the sector. Although the guarantees did not achieve the financial additionality (only 12 percent of borrowers were first-timers), it helped KCB's marginal clients raise their borrowing levels with the bank. In this regard, it is the view of the evaluation that the DCA guarantees acted as a major marketing tool for KCB's own funds. Unfortunately, the bank did not use the opportunity offered by the guarantee to develop similar products to enable it to sustain its SME lending under the same DCA guarantee terms. KCB has resorted to high collateral requirements and is likely to lose most of the DCA borrowers who are unable to meet its normal lending collateral requirements. On the economic additionality front, DCA borrowers were able to grow their businesses and improve profitability with the DCA-guaranteed loans. On average, the enterprises surveyed improved their sales and profitability levels.

SUMMARY OUTCOME LEVEL

The DCA guarantee enabled KCB to establish an SME unit that had not existed before. Although the bank has been slow to act, it is exploring alternative ways of securing loans such as cash flow-based loans, stocks, logbooks, and chattels that traditionally were unacceptable forms of collateral for the bank. KCB is, however, very slow to change and still thinks in terms of high collateral, whereas its competition has moved to providing collateral-free loans. The bank also focused on providing working capital and channeled very little of the DCA-guaranteed loans into investment capital. Although the DCA guarantee inspired more borrowers to seek loans with KCB, the bank needs to fine-tune its loan processing to meet changing market practices and borrower expectations in Kenya. Failure to do so will see all its gains from the DCA guarantee disappear.

SUMMARY IMPACT LEVEL

KCB is yet to venture into the non-security loan market as it is still in the process of developing appropriate instruments. Prior to the DCA guarantee, KCB was not a player in the SME market. The DCA guarantee, however, gave the bank the confidence to attempt to move into such new markets. The guarantees enabled the bank to gain experience in working with SMEs such as with the Grace loans that specifically targeted women. KCB has since developed a clear strategy and improved collaboration with other financiers in a bid to grow its SME portfolio and become a major player in the sector. Among the 69 borrowers sampled, from the borrower perspective, the loans under the DCA guarantees were able to facilitate growth in their businesses and enabled them to achieve some impressive positive social impacts (e.g., employment creation, new business creation, better education for children). DCA guarantees had a big demonstrative effect on first-time borrowers by giving them the confidence to seek additional loans from the bank or elsewhere. The guarantee ultimately demonstrated to KCB the existing potential and showed that funding SMEs can be a profitable business.

RECOMMENDATIONS:

Key Recommendations for USAID

1. In future, USAID/Kenya may wish to consider setting up these guarantees as revolving funds to help the bank generate more than one cycle of loans. To avoid a situation where guarantee borrowers are unable to secure follow-up loans, it is recommended that KCB and USAID/DCA agree on a time frame for developing and testing new products in order to avoid a situation where the bank is overly dependent on DCA guarantees.

2. USAID/DCA in collaboration with KCB should work out a cost-sharing mechanism with borrowers whereby local financial consulting organizations/business service providers can support SMEs in improving their operations and preparing the required statements.

3. USAID/DCA should in future put more emphasize on supporting real sectors of the economy (e.g., agriculture, manufacturing), which are the economy movers, hence the need for long-term capital investments.

4. To encourage KCB and any other DCA partners to support long-term capital investment, the evaluation would recommend that USAID consider specifying the proportion of the guarantee that would support different loans (working capital vs. capital investment).

5. For women-owned businesses, USAID/DCA should consider working with institutions that are more experienced in developing loan products that address the specific needs of women-owned businesses such as the Kenya Women Finance Trust Fund, FAULU Kenya, K-Rep, and Jamii Bora Bank.

Key Recommendations for KCB

1. KCB should improve financial literacy among its borrowers and ensure that borrowers are aware of the interest rate being charged on their loans.

2. KCB should develop good loan products for capital investment and build staff skills and capacity to appraise and manage long-term investment loans for economic development.

3. KCB needs to improve the ability of its staff to analyze the risks associated with SME loans and avoid terming everything as working capital.

4. KCB should improve its capacity to deal with agricultural-related loans with seasonality regimes that are different from normal bank loans.

5. KCB should expedite and roll out loan products that would address the constraints of DCA guarantee borrowers to avoid frustration among its clients who fail to secure follow-up loans, resulting in them shifting to other institutions.

6. KCB may wish to consider decentralizing the loan approval limit as its SME and microloans portfolio grows to avoid delays in securing approval from H/Q.

7. KCB staff have to appraise and finance client requirements appropriately to avoid them borrowing short to fund long-term investment (housing), which is bound to create a mismatch in cash flows and compromise client ability to service loan obligations.

ANNEX A: Revised DCA Evaluation Framework

EVALUATION QUESTIONS INPUT LEVEL	DATA SOURCES	INDICATORS	ANALYSIS METHOD
INPUT LEVEL -Guarantee Design and Development			
1. What was the motivation for the 2006 and 2010 DCA Guarantees with KCB? Who originated the effort?	Scope of Work USAID Reports	Level of SME lending in KCB at the time of DCA 2006 origination Volume of Loans disbursed by KCB Changes in Loan Processing behavior of lenders Change in behavior of borrowers	Interviews with KCB HQ Staff , USAID projects – KEMCAP, KARF and FIRM
2. Was Technical Support provided to KCB by USAID and/or borrowers to accompany the guarantee	Scope of work, USAID/Kenya, USAID project contractors, KCB HQ Staff and Borrowers	No. of KCB staff trained No. of borrowers supported KCB systems improved	Guided interviews with KCB HQ staff, USAID contractors and borrowers
3. Did the structure of the Guarantee help KCB achieve the intended goals	KCB Transaction Summary	Volume of loans generated by KCB	Review of KCB Data
4. Did the structure of the Guarantee Encourage KCB to lend more for working capital purposes rather than investment	DCA Guarantee Agreements	Proportion of Loans to Working Capital and Investment Capital	DCA Reports
OUTPUT LEVEL – FINANCIAL ADDITIONALITY			
a) Did KCB re-orientate its SME lending strategy in line with the DCA guarantee targets? b) How did KCB find borrowers? Did it market the DCA guarantee loan? If so how?	KCB reports and strategy, records, KCB Borrower Interviews with KCB staff at HQ and Branches	• More lending to SME sector by KCB • No. of new and additional borrowers achieved	Review of KCB Data Qualitative analysis of borrower Questionnaires

OUTPUT LEVEL ECONOMIC ADDITIONALITY			
How did DCA guarantee influence the borrowers economic additionality (e.g. sales, Profit, Job creation**s**	Interviews with KCB Borrowers	Volume of Sales generated % Profit Generated No. of new Jobs created	Analysis of evaluation questionnaires Statistical Analysis
OUTCOME LEVEL LENDER BEHAVIOUR CHANGE			
A. Given the high utilization of both guarantees: 1) **D**id the KCB increase credit to the target sectors **outside** the DCA guarantee? **2)** Did KCB move into **any new sectors/Industries**? (Did KCB work within the **scope of Sectors** in the DCA Guarantee Agreement? If not, Why?) 3) Did KCB move into any new **type of borrowers**? (Did KCB lend MSMEs that are owned/ operated by women, and/or require cash flow-based lending) 4) Did KCB move into any new **type of loans**? (Did KCB develop new loan products as a result of the guarantee's TA support?) **5)** Did KCB move into new **loan terms**? **6)** To what extend did DCA guarantee improve access of KCB customers to credit outside the Guarantee?	KCB transaction report summary, KCB records, Interviews with KCB staff at HQ and Branches, KCB borrowers and USAID Kenya partner projects	Quantitative comparison over time of KCB loan portfolio characteristics disaggregated by: • No of loans to targeted sectors within/outside the DCA Guarantee • New by Sectors/industries • Type of borrowers before and after the guarantee • New types of Loans (No. of cash flow-based loans approved by KCB) • Better pricing of loans • Types of loans before and after the guarantee • KCB loan terms before and after the guarantee e.g. tenor, collateral, • Changes in loan processing culture • Number of loans approved	Analysis of the KCB transaction report summary, compare indicator values pre/versus/post-guarantee and change in indicator value over time Qualitative analysis of interview notes with borrowers and bank documents (on lending strategy)

OUTCOME LEVEL BORROWER BEHAVIOUR CHANGE	DATA SOURCES	INDICATORS	ANALYSIS METHOD
1) Did the borrowers seek loans before and after the guarantee loans from KCB or other financial institutions? If so, were the requests successful? 2) To what extent were the DCA guarantees responsible for improving the borrower's willingness/access to seek credit outside and/or within KCB?	KCB Borrowers interviews	• No. of borrowers with repeat loans under/or outside the guarantee • No. of borrowers with loans with loans with other lenders • Additional sales due effect of the loan • Improved profitability as a result of the loan • No. of jobs created due to guarantee loan	Qualitative and quantitative analysis of interviews with KCB clients under the DCA guarantees Analysis interview questionnaire administered to sampled KCB borrowers
IMPACT LEVEL: Long Term Changes in Market practices or perception towards targeted sectors			
a) What additional insights can you provide that access for loans improved for the targeted sector. b) What role if any, did DCA-KCB loan guarantee play as a demonstration model?	USAID Kenya Projects KCB Reports	• No. of other banks desiring to replicate the DCA-KCB guarantee model • Increase in No. of Banks with loan products to the SME sector • Growth in SME sector in Kenya	Review SME sector performance data/information, growth and trends Requests by other banks to be considered for similar guarantee products by USAID
EXOGENOUS FACTORS: That influences Outputs, Outcomes and Impact			
Enabling Environment, Post Election Violence, 2008 financial market crisis, completion, Technical Assistance and other donors	Monetary Authorities reports	Inflation rate, lending rates, exchange rates, food prices, GDP	Review monetary performance reports, sector reviews and commentaries

ANNEX B: Kenya Sector-Gross Domestic Product (2005-20011)

(Constant 2001 prices –KES million and Percentage Change)

YEARS	2005		2006		2007		2008		2009	2010		2011	
SECTORS ACTIVITIES	KES millions	%	KES millions	%	KES millions	%	KES millions	%	%	KES millions	%	KES millions	%
Agriculture and Forestry	299,798	6.9	312,926	4	320,423	2	307,354	-4	-2.6	299,431	6	318,586	1.5
Fishing	5,751	9.6	6,249	9	6,181	-1	5,363	-13	3.8	5,565	3	5,713	3.1
Mining and Quarrying	5,335	2.7	5,554	4	6,272	13	6,453	3	-4.5	6,163	10	6,763	7.1
Manufacturing	115,698	4.7	122,953	6	130,673	6	135,291	4	1.3	137,060	5	143,263	3.3
Electricity and Water	27,751	-1	27,288	-2	29,769	9	31,341	5	-3	30,397	10	33,335	-3
Construction	35,401	7.5	37,649	6	40,405	7	43,735	8	12.7	49,270	5	51,486	4.3
Wholesale and Retails Trade	106,095	5.6	118,361	12	131,754	11	138,044	5	3.9	143,460	8	154,942	7.3
Hotels And Restaurants	15,572	13	17,894	15	20,814	16	13,298	-36	42.8	18,993	4	19,796	5
Transport and Communications	122,317	9	136,306	11	156,845	15	161,615	3	6.4	171,994	6	182,181	4.5
Financial Intermediations	45,030	6.9	47,170	4	50,306	2	51,659	-4	-2.6	55,375	6	60,379	1.5
Real estate, renting, business services	65,882	3.4	68,447	4	70,860	4	73,503	4	3	75,674	3	78,089	3.6
Public administration	46,722	-1	45,974	-2	45,031	-2	45,317	1	1.6	46,031	2	47,085	2.5
Education	72,999	0.7	73,188	0	76,257	4	80,771	6	2.7	82,952	5	86,651	4.9
Other services	77,017	3	79,980	4	82,575	3	85,120	3	3.2	87,850	2	89,772	4
FISIM	-11,261	4.3	-11,835	5	-12,174	3	-10,484	-14	13.9	-11,945	-6	-11,260	5.2
All industries at basic prices	)30,106	5.2	1,088,103	6	1,155,991	6	1,168,382	1	2.6	1,198,270	6	1,266,782	3.8
All industries excl. agriculture	730,308	4.6	775,177	6	835,568	8	861,027	3	4.4	898,839	6	948,195	4.6
Taxes on products	145,143	11	161,367	11	180,855	12	188,882	4	3.8	196,117	6	207,981	7.9
GDP at market prices	1,175,248	5.9	1,249,470	6	1,336,846	7	1,357,263	2	2.7	1,394,387	6	1,474,763	4.4

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ANNEX C1: Borrower Evaluation Questionnaire

General Borrower Information								
CMS Transaction Report ID		Date of Review				Name of Borrower/Establishment		
Sector						Type		
Shareholder/Owner						Town/Location		
Name/title of person/s met								
Address		Email Address/Phone Number (If any)						
General Info on Business		Bank Contact						
Loan Amount		Loan USD equivalent at X = 1 USD						
Start date of loan		Loan term in Months				Time to approve and disburse loan (Months)		
Loan type		Purpose of loan						
Loan is in good standing? If not, list outstanding issues								
Bank relationship								
Borrower Company Information								
Sector of Business (Check all that apply)	Fisheries and Aquaculture		Health		Information & Communication Technologies		Tourism	
	Trade/Commerce		Transport		Energy		Agriculture	
	Education		Construction		Other (Please specify)			
Is the business at least 50% woman-owned?		Woman-ownership percentage						
Total number of employees		Male			Female			

Notes on employee breakdown			
Business Capital “Equity”		**Capital USD equivalent**	

Borrower’s assessment of primary credit constraint (Notes)	
High collateral	
Unfavorable tenor terms offered	
High interest rate	
Lenders’ lack of knowledge about business sector/opportunity	
Other (Explain)	

Comparative Analysis (Statistical)

Loan Access	**Prior to Subject Loan**								**After Receiving Subject Loan (As of most recent year completed)**								
Number of times a loan was provided	Once		Twice		Three times		Four or more times		Once		Twice		Three times		Four or more times		

Source of credit:										
	Avg. Int. Rate	Collateral Value	Personal or Group Guarantees	Tenor (Months)	Time Obtaining Loan	Avg. Int. Rate	Collateral Value	Personal or Group Guarantees	Tenor (Months)	Time Obtaining Loan (Months)
Subject Lender										
Family/Friends										
Another Cooperative / SACCO										

Another MFI										
Another Commercial Bank										
Other										
Additional Source of Credit Questions										
Please specify the other financial institution that provided financing										
Please specify the type of collateral required (fixed assets, land, cash,etc.) by each institution										
If financing was not approved, please specify the reason										
Who initiated the loan process? (Lender, Borrower, TA provider, etc.)										
Access to Credit for the Following Purposes (Pre and Post Loan) – Check all applicable and specify the institution that provided the loan										
Working Capital / Income Generation										
Physical Infrastructure										
Training / Skills Building										
Upgrades & Maintenance of Assets										
New Business Creation										
Other (Please Specify)										

Distance Of Nearest Formal Credit Institution		
Cooperative / SACCO		
MFI		
Commercial Bank		
Other (Specify)		
Financial Inclusion		
Mobile Phones (Number)		
Value of Savings Account/s in Formal System		
Holds Insurance Policy of Any Kind (Yes/No)		
Basis of Prior Loan Denial (Narrative)		
Impression of Bank (Narrative)		
Employment Generation	**Year Prior to Loan**	**Most Recently Completed Year (2012)**
Borrower/Business Employment Metrics		
Total number of employees		
Monthly salary expense (Wages)		
Business Sustainability	**Year Prior to Loan**	**Most Recently Completed Year (2012)**

Borrower/Business Sustainability Metrics		
Est. Production Volume (if applicable)		
Est. Gross Sales		
Est. Net Profit		
Local Sales (% of total sales)		
Export Sales (% of sales)		
Social Impact Metrics		
Highest Education Level Attained by Children		
Value of Home (client perception/est)		
Expenditure on Savings/Burial Societies		
Quality of Life Rating (1=Bad 5=Best)		
Access to USAID Technical Assistance (Yes/No)		
Quality of USAID Rating (1=Bad 5=Best)		
Positive Competitive Factors (Notes)		

Competitive Threats (Notes)	
Borrower's assessment of the bank. Would the borrower recommend another client to the subject bank? Any recommendations in terms of loan processing, collateral requirement, or other factors?	
Access to USAID TA (Notes)	
DCA Assessment By Interviewer: **Did the Loan Make a Difference? Does the borrower plan to take another loan from the bank or another institution?**	

ANNEX C2: KCB Interview Protocol

- *Input Level (DCA Guarantee Design and Structure):*

a) What prompted/motivated KCB to partner with USAID under the DCA guarantee? Who initiated the partnership?
b) How has the DCA guarantee benefited KCB? Did the program meet with your expectations in terms of expected results?
c) In your view, what aspects of this collaboration have worked well and why? And are there aspects of this collaboration that have not worked well and why? How do you think these should be dealt with by KCB and/or by USAID to improve future programs?
d) What aspects / conductions of the DCA proved to be challenging/constraints, during the implementation phase of the Guarantee? e.g. grace period of the loans? How did KCB deal with them?
b) Did the DCA guarantee help increase access to finance among the disadvantaged women-owned SME's? How did KCB deal with this issue?
c) In your view, is the DCA guarantee approaches to the issues of access to finance for target sectors in Kenya right or do you think the DCA guarantee would have achieved more with a different approach? Which one?
d) Would you suggest ways in which the DCA guarantee can be adjusted/re-oriented to better address the needs of the business community in Kenya?
e) What political, social, cultural and economic obstacles have you experienced if any, and how did they affect your work? Positively/Negatively?
f) How best do you think the program can in future improve its interventions in relation to these aspects?
g) What would you say are the major strengths and/or weaknesses in the DCA guarantee approach?

OUTPUT LEVEL:

a) Did the DCA help KCB to increase credit to the target sectors outside the DCA guarantee? i.e., using KCB's own resources? To what extent?
b) Did the guarantee enable KCB to increase the type of loans and type of borrowers in its portfolio e.g., lending to MFIs, SACCOs, women owned businesses, new unexplored sectors e.g., energy
c) How did the DCA guarantee affect KCB's rules of engagement with the clients i.e., did KCB change its loan terms to targeted sectors under the guarantee? If Yes How? If No, Why?
d) It seems KCB did not work within the scope of Sectors agreed in the DCA Guarantee Agreement? E.g., 2006 DCA target sectors were: SMEs engaged in agriculture production and processing, manufacturing, tourism, and commerce and trade and second tier MFIs including women –owned businesses. ***The sectors funded by KCB were construction, education, energy, fisheries and aquaculture, health, information and communication, transport.*** Was there a subsidiary agreement to the revision of the sectors to be funded?
e) Under 2006 DCA, Claims made by KCB against the guarantee amounted to US$558,538. What was the failed "Grace Loan" product? **Has KCB made any recoveries on the *280 loans, which were subject of the claims made against the guarantee by KCB***
f) The 2010 DCA reached 100 percent utilization within a year of the obligation date. What was the cause of this upsurge in loan uptake? What lessons has KCB leant from this that can educate future programs?
g) **Under 2010 DCA:** Agriculture production/values addition, clean energy, commerce, constituency Development Fund Projects, construction and manufacturing; MFIs, and SACCOs. At least 20 percent to clean energy sector areas of solar, wind, biogas, and small hydroelectric power generation. The analysis shows that no loans were made by KCB on 4 key targeted sectors. These were: clean energy, which was allocated 20 percent of the guarantee, second Tier MFIs, MFIs,

SACCOs and CDF projects. What was the ***cause of KCB's failure to loan to these sectors, which were considered important under the two DCA guarantees***

h) Both DCA 2006 & 2010 had only two loan products: working capital and investment capital. The transactions summary shows that over 90 percent of loans were for working capital purposes (trade & commerce), and only a few for investment capital. Why such a big difference? Is there no demand for investment capital?
i) What was KCB's experience in lending to MSMEs that are owned/ operated by women? Did the bank make any cash flow-based lending to women owned businesses (DCA 2010) examples

OUTCOME LEVELS:

a) How effective was the TA support to facilitating the DCA implementation by KCB? What, in your view could have been done better if at all?
b) Apart from USAID, what other partnerships is KCB involved in?
c) Has the bank experienced any challenged/difficulties managing resources from multiple partners? Explain? What solution have been effected or need to be effected?
d) Did the technical assistance from USAID help KCB improve its operations in targeted sectors/borrowers under the DCA guarantee
e) Did KCB re-orientate its lending SME strategy in line with the DCA guarantee targets?
f) How did KCB find borrowers? Did it market the DCA guarantee loan? If so how?
g) Did the DCA guarantee change the way KCB assess the loan applicant in terms of collateral requirements and loan tenor? If so How?
h) Did KCB approve any cash flow-based loans to women owned/operated SMEs
i) Did KCB develop new loan products as a result of the guarantee's with the help of the TA support?
j) Did the terms offered under the DCA guarantee encourage more borrowing
k) Did the structure of the guarantee encourage KCB to lend more for working capital purposes rather than investments?
l) Did more KCB clients access loans as a result of the guarantee

IMPACTS AND SUSTAINABILITY:

a) Has KCB dealt with other guarantees similar to the DCA guarantee, and how do you compare their impacts on your work?
b) What positive impacts have been generated through the DCA guarantee's support and how will these be sustained?
c) Any negatives impacts? What mitigative measures have been put in place against such?
d) Is DCA guarantee a relevant and appropriate intervention in dealing with issues of empowerment and access to credit for marginal sectors and borrowers in the business communities in Kenya especially in the energy sector, women, MFI's, SACCOs etc?
e) Have you introduced any new loan products to the market under the DCA guarantee? (Please specify in terms of Sector, type(loan/ Savings) and Market segment)
f) What key measures did KCB undertake to ensure the success of the DCA guarantee e.g. special training of the employee, marketing of the products, this?
g) Are you aware if the DCA Guarantee has had any effect on how other banks operate especially in the SME sector? How?
h) Will KCB continue working with DCA guarantees in future?

LESSONS LEARNED:

a) If you were to restructure your partnership with USAID DCA guarantee, what would you do differently next time?
b) What lessons good or bad have you learned from this corporation?
c) Were there exogenous factors outside KCB's control that influenced Outputs, Outcomes and Impact of the two DCA guarantees 2006 and 2010? How did KCB deal with these?
d) Any recommendations /suggestions for future initiatives such as these?

CLOSING REMARKS AND APPRECIATION

ANNEX D: Final Fieldwork Plan

No. of Days	DATE	DAY	TIME	PROPOSED ACTIVITY	LOCATION
1	03/21/2013	**Thursday**	10.00	Meeting with Linda – DAI • Review of the Evaluation Work Plan and meetings scheduling • Sampled list of KCB borrowers/Clients to be interviewed in the field • Review the Borrower Questionnaire and support to be provided by DAI • Logistics and facilitation • 26 Clients under DCA 2006 not included in the KCB Transactions Report Summary • Agree on Non-DCA banks to be consulted • Any other issues that may *arise.*	Nairobi
2	03/26/2013	**Tuesday**	9.00 2.0	Meeting with KCB, to agree on final list of branches /borrowers to be interviewed. Seek clarification on evaluations questions/ request for additional information / data. Meeting with DAI (Mark) to review the roles played by the KEMCAP and *KARF projects*	KCB H/Q Nairobi DAI Offices Nairobi
3	03/27/2013	**Wednesday**	9.00 11.30 2.00	Meet KCB Branches & Borrowers in Nairobi ,, ,,	Nairobi
4	03/28/2013	**Thursday**	,,	Meet KCB Branches & Borrowers in Nairobi	Nairobi
	03/29/2013	**Friday**		**EASTER HOLIDAYS** **(Travel by Road to Eldoret by Road)**	
	03/30/2013	**Saturday**			
-	03/31/2013	**Sunday**			
	04/01/2013	**Monday**			
5	04/02/2013	**Tuesday**	9.00 11.30 2.00	Meet KCB Branches & Borrowers in Eldoret	Eldoret
6	04/03/2013	**Wednesday**	,,	Meet KCB Branches & Borrowers	Eldoret
7	04/04/2013	**Thursday**	9.00 - 11.30 2.00	Morning Meet 1 or 2 Borrowers **(Travel to Nakuru by Road)**	Eldoret
8	04/05/2013	**Friday**	9.00 -	Meet KCB Branches & Borrowers ,,	Nakuru

No. of Days	DATE	DAY	TIME	PROPOSED ACTIVITY	LOCATION
			2.00		
9	04/06/2013	**Saturday**	9.00 11.30 2.00	Meet KCB Branches & Borrowers ,, **(Late Afternoon Travel to Nairobi by Road)**	Nakuru
-	04/07/2013	**Sunday**		**Travel to Mombasa by Road**	
10	04/08/2013	**Monday**	9.00 11.30 2.00	Meet KCB Branches & Borrowers	Coast
	04/09/2013	**Tuesday**	**NO WORK - PUBLIC HOLIDAY**		Coast
11	04/10/2013	**Wednesday**	9.00 11.30 2.00	Meet KCB Branches & Borrowers	Coast
12	04/11/2013	**Thursday**		Drive from Mombasa to Machakos, Meetings with KCB staff	Coast/Central Regions
13	04/12/2013	**Friday**	9.00 11.30 2.00	Meet Borrowers in Machakos Travel to Nairobi	Central
	04/13/2013	**Saturday**	**NO FIELD WORK**		
	04/14/2013	**Sunday**			
14	04/15/2013	**Monday**	9.00 11.30 2.00	Meet with KCB Githuguri & Borrowers	Central
15	04/16/2013	**Tuesday**		Travel to Thika KCB Branch/Meetings with borrowers whole day	

ANNEX E: Evaluation Deliverables and Revised Final Frame

Revised List of Deliverables Dates

In order to answer the evaluation questions, the Consultant will develop the following deliverables:

- By February 18, customize the DCA Evaluation Framework to the Kenya Commercial Bank evaluation. The framework/methodology should reflect the specific objectives of the multibank guarantee described in the Action Packages and Legal Agreements. It will also detail the measurements of how success in meeting those objectives has or has not been achieved.
- By February 18, provide a list of quantitative and qualitative indicators.
- By February 18, provide desktop analysis and work plan.
- From o/a March 21 to April 15, conduct a site visit to Kenya to obtain primary source information from sources listed in the Revised Evaluation Framework.
- By May 7, provide for E3/DC review a draft evaluation report including the following chapters:
    - -Executive Summary
    - -Methodology and Indicators
    - -Exogenous factors that may have influenced guarantee performance
    - -Results of the guarantee at the input level
    - -Results of the guarantee at the output level for lender and borrower
    - -Results of the guarantee at the outcome level (behavior change for lender and borrower during and after the guarantee)
    - -Results of the guarantee at the impact level (market demonstration impact)
    - -Conclusions and Findings
    - -Recommendations
    - -Bibliography

8. By May 14, obtain comments on the draft evaluation report from E3/DC
9. By May 18, submit to E3/DC a final draft of the evaluation report.
10. By May 22, provide E3/DC with a draft 4-page "Impact Brief" for comment.
11. By May 27, obtain comments on the 4- page "Impact Brief" from E3/DC.
12. By May 31, (or 3 working days after receiving comments from E3/DC), submit to E3/DC a final draft of the 4-page "Impact Brief."

13. Provide a Brownbag presentation (optional), including a PowerPoint presentation, (specific date TBD) to E3/DC and other relevant USAID personnel to present key evaluation findings. At the time of the Brownbag presentation also make available copies of the 4-page Impact Brief.

These deliverables will be used by E3/DC to develop action items that will improve guarantee development and management

ANNEX F: List of Interviewees

NAME	REGION OFFICE and CLIENT ID	CONTACTS
Abraham Kipkoech Kipruto	Nandi Hill Branch KCB	722636367
Acme Hospitality Limited	KCB 615-DCA-06-007	722653225
Agnes Abonyo Ogunde	KCB 615-DCA-10-12	722796681
Albert Chorono	Nakuru Branch KCB	721322808
Ali Kassim Msalaam	KCB 615-DCA-06-007	722626689
Amina Soud Mohammed	KCB 615-DCA-10-12	720854964
Arther Githiru Ndonye	KCB 615-DCA-10-12	733969650
Benjamin Kurgat	Eldoret Main branch KCB	720710808
Charles Kiara	Machakos Branch KCB	722333669
Charles Muturi	KCB 615-DCA-10-12	720818144
Charles Omondi Agak(Chaalam general Contractors)	KCB 615-DCA-06-007	722427566
Daniel Murithi	KCB 615-DCA-10-12	722231115
Danvan Muiruri Njuguna	KCB 615-DCA-10-12	720320233
David Mwaruma	KCB 615-DCA-10-12	720320233
Dennis Amwai	Kikuyu Branch KCB	720563135
Dennis Muithya Pius	Regional Office Coast KCB	722641456
Diesel Petrolium ltd(Collins Boinet)	KCB 615-DCA-06-007	720673687
Dominic Kamau Waithike	KCB 615-DCA-10-12	722514864
Dorothy Jomeli	KCB 615-DCA-10-12	723346203
Edith Mungala	Treasury Square branch KCB	722258023
Elizabt Musau	KCB 615-DCA-10-12	711924187
Emmanuel Kosgey	KCB 615-DCA-06-007	713135555
Emmy Chepugetich	KCB 615-DCA-10-12	724536348
Ester Wangui Chege	KCB 615-DCA-10-12	722960764
Evans Munungi	River road Branch KCB	720352857
Feisurai Abudalla	KCB 615-DCA-10-12	722626684
Geoffrey Karanja	KCB 615-DCA-10-12	722728056
George Nganga Nguge	KCB 615-DCA-10-12	729998908
Gertzel Shirachi	KCB 615-DCA-10-12	714794560
Glory Chemicals	KCB 615-DCA-10-12	722270624
Grace Chepkoech	KCB 615-DCA-10-12	722967631
Hannah Muthoni Waititu	Central Region Office KCB	722676442
Hannington Gatara	KCB 615-DCA-06-007	723487769
Harron Chege Kimaru	Githunguri Branch	721806184
Harron Mutamba	KCB 615-DCA-10-12	721366782
Hillary Kibet Mutai	KCB 615-DCA-06-007	721499766
Invoilata Adhiambo Obala	KCB 615-DCA-10-12	725315197
James Wanaina Mbugua	Eldoret Main branch KCB	720673687
Jane Sang	KCB 615-DCA-10-12	723234845
Jeanette Auma Ochieng	KCB 615-DCA-06-007	721631814
Jennifer Maiyamu Mue	Njoro Branch KCB	725728188
John Saina	KCB 615-DCA-10-12	726587402

NAME	REGION OFFICE and CLIENT ID	CONTACTS
Johnson Kinyanjui Chege	Moi Avenue KCB	735628972
Joseph Kivuva	KCB 615-DCA-10-12	722778027
Joseph L. Kipyoto.	KCB 615-DCA-10-12	720317112
Joseph Njoroge	Limuru Branch KCB	722445651
Josiah T. Mugwe	Treasury Square branch KCB	722626689
Juma Mwangi	KCB 615-DCA-10-12	722620093
Kaka Pemwa Enerprises (Patrick Elija and Silus Chiponda)	Kiambu Branch KCB	725289757
Kevin Kariuki	Eldoret Main branch KCB	722611017
Linda A. Kagota	USAID Kenya FIRM	726677392
kipkemoi Toromo	KCB 615-DCA-06-007	722472774
Lucy Waitherero Mwangi	KCB 615-DCA-10-12	722402460
Lydia Njeri Munge	KCB 615-DCA-06-007	729257340
Martin Kibiwott Tanui	KCB 615-DCA-06-007	725283671
Mary C. Jibet jane	KCB 615-DCA-10-12	722763302
Mary Wanjala	KCB 615-DCA-06-007	722880606
Maureen Mariga	KCB 615-DCA-10-12	725802257
Maxwell Ndundi Guracha	KCB 615-DCA-10-12	722883371
Moses Chemtoi	KCB 615-DCA-10-12	722437478
Moses Kimani Keriche	KCB 615-DCA-06-007	722437478
Moses Wamwea	KCB Head Office	726658069
Mwangi Virginia	Thika Branch KCB	720911996
Nathan Kyalo	KCB 615-DCA-10-12	710726564
Nelson Gathogo Waiganjo	KCB 615-DCA-06-007	726587402
Ngowan Bookpoint(John Ngoru)	KCB 615-DCA-10-12	733796773
Nicholas Muindi and Dorothy Katana Muindi	Moi Avenue KCB	736125244
Olipa Ongeri	KCB 615-DCA-10-12	721846742
Paul K. Kipkorir	KCB 615-DCA-06-007	723755482
Peter Kiptanui	KCB 615-DCA-10-12	727701415
Peter Muiruri Githuka	KCB 615-DCA-10-12	733787991
Peter Nmbiyu Kibunja	KCB 615-DCA-06-007	722570919
Rhoda Aswani Busolo	KCB 615-DCA-10-12	728337659
Richard Cheruiyoit Koril	KCB 615-DCA-06-007	726459855
Robert Francis Nungu	KCB 615-DCA-06-007	738056702
Rwale Boutique (Ruth Achieng)	Iten Branch KCB	729206000
S.K.cheboi	Mvita branch KCB	722866420
Salma Amin	KCB 615-DCA-10-12	722808124
Sammy Kaniaru	KCB 615-DCA-10-12	726678021
Sammy Mwangi Kiguru	KCB 615-DCA-10-12	722949611
Sammy Ndichu Mbugua	KCB 615-DCA-10-12	722949611
Samwel Kuria Kariuki	KCB 615-DCA-10-12	727727461
Samwel Muli Kariuki	KCB 615-DCA-06-007	722302108
Serah Njeri Wachira	KCB 615-DCA-10-12	722626689
Shabiri Odhiambo Agutu	Mombasa Town Center KCB	721278834

NAME	REGION OFFICE and CLIENT ID	CONTACTS
Shauri Dena	KCB 615-DCA-06-007	723115816
Solomon Nzioka Philip	KCB Head Office	722321282
Soo M. Jacinta	KCB 615-DCA-10-12	720579631
Stephen Kiplimo Tunui	KCB 615-DCA-10-12	721251537
Stephen Wachiro Nguro	Great Rift region Office KCB	723770846
Steve Wafula	Eldoret West Branch KCB	720224405
Susan koech	KCB 615-DCA-10-12	717180780
Tabitha Wairimu Ndugu	KCB 615-DCA-10-12	723903058
Thomas K. Keror	KCB 615-DCA-10-12	721937381
Timothy Githiora Ndungu(Vantage Motors parts)	Regional Office Nairobi KCB	722639481
Victor Mbaabu	KCB 615-DCA-10-12	722673372
Zaki Ali Said	KCB 615-DCA-10-12	723917264

ANNEX G: References

1. Kenya commercial bank Transaction summery report LPG 615-DCA-06-007
2. KCB Transaction summery report LPG 615-DCA-06-007-1
3. Kenya commercial bank Transaction summery report LPG 615-DCA-10-12
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9. Kenya KCB 615-DCA- 06-007
10. Work order number: 012 Kenya Commercial Bank DCA guarantee Evaluation 2006 & 2010
11. Central Bank of Kenya annual report 2011-2012
12. Kenya National & Statistics Bureau Quarterly GDP Reports
13. http://www.kcbbankgroup.com/ke/
14. Financial Sector Deepening Program (FSD) Report 2011-12
15. World Bank: Kenya Economic Update / December 2012 Edition No. 7
16. Action Packages (this explains the mission's priorities, the development rationale for doing a DCA guarantee, and the risk assessment (using CAMELS analysis) for determining the overall risk score and how much subsidy (loan loss reserve) the Mission would have to pay for the DCA guarantees)
17. Legal Agreements (contracts between USAID and KCB that define the terms and detail the specific Qualifying Borrower/Qualifying Project/Maximum Amount Per Borrower definitions)
18. Monitoring Plans (responsibilities of the Mission and DCA office and important indicators the Missions wishes to track)
19. CMS Database system found here: https://cms.usaid.org/