Independent evaluation of AfDB assistance to small and medium enterprises (2006–2013)

Khaled Samir Hussein,
Principal Evaluation Officer, African Development Bank

This evaluation was conducted to inform the Bank's future assistance to Small and Medium Enterprises (SMEs). The purpose of the evaluation is three-fold: 1) assess the relevance, effectiveness and sustainability of Bank assistance to SMEs; 2) evaluate how efficiently the Bank's structure and procedures have supported the design and delivery of operations; and, 3) identify potential areas for improvement.

Findings

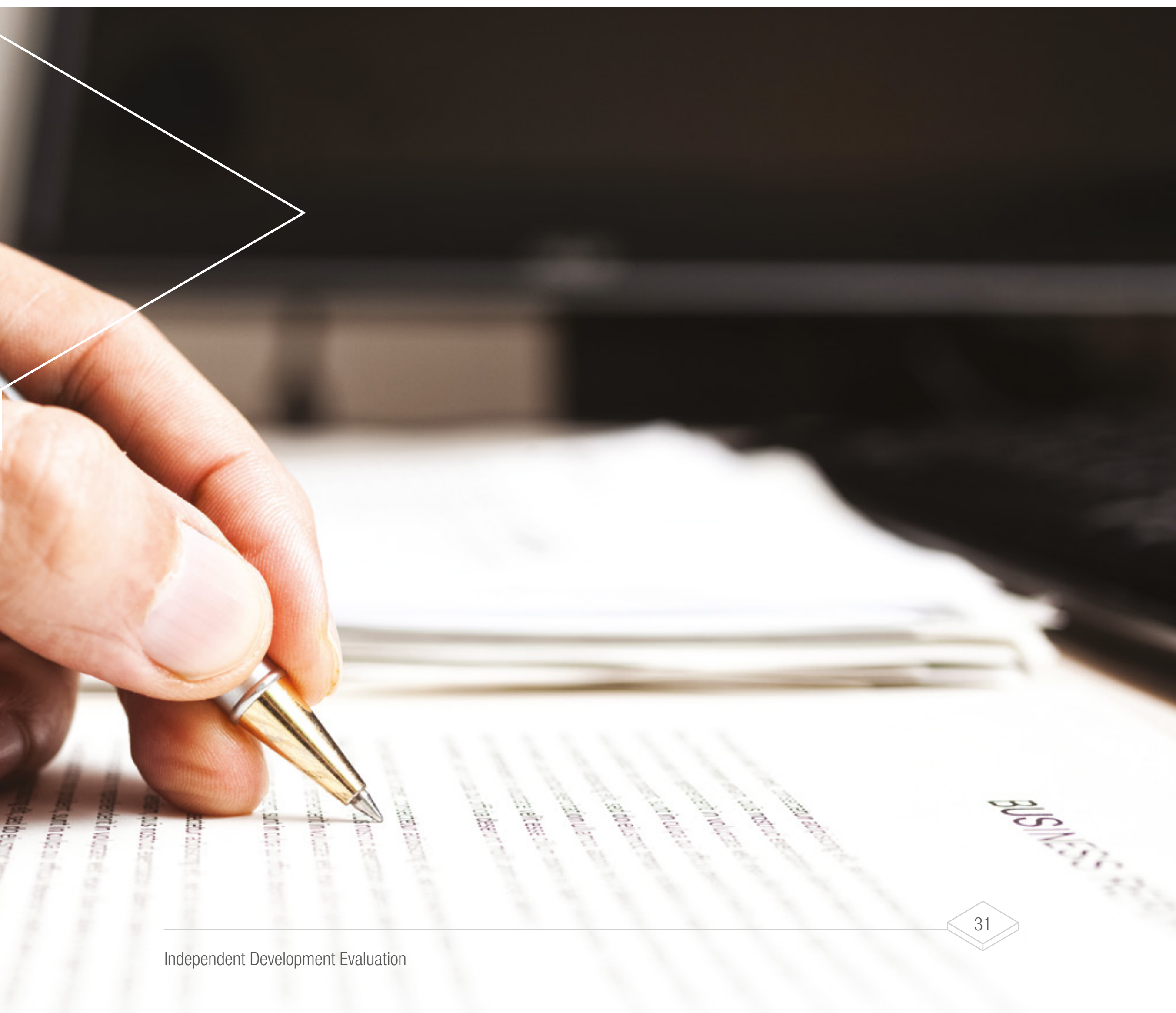
- **Relevance of the Bank's strategic orientation is rated as satisfactory.** The importance of SME development in Africa has long been recognized by the Bank, and SME development has been a recurrent theme in strategic and policy documents. However, no dedicated SME strategy exists and SME assistance lacks a unified conceptual framework. This is partly reflected by the absence of a harmonized definition of SME, often preventing proper identification of target groups. The themes addressed by the Bank are highly relevant for SME development. However, when compared with other MDBs, the Bank is more focused on improving conditions for SME finance, and pays less attention to other areas of interventions (such as investment climate reform, financial market infrastructure, market access). One persistent gap in the Bank's product mix is the limited use of local currency lending, which limits its ability to effectively reach SME beneficiaries.
- **Relevance of SME assistance operations is rated moderately satisfactory.** The relevance of SME assistance operations is often undermined by weaknesses in design. In some cases, there was a limited appreciation of client's financial needs, which resulted in project cancellations. Financing agreements often did not appropriately specify eligibility criteria for sub-loans. This provided ample room for risk-averse banks, a substantial subset among recipients of the Bank's SME assistance, to utilize loan proceeds for safer corporate lending. As a result, a significant share of Bank assistance was nominally targeted at SMEs, but in practice can be better described as generic private-sector development assistance. However, since 2013 the SME focus has been considerably strengthened, and operations channeled through the ASMEP (Africa Small and Medium Enterprise Program) and the African Guarantee Fund are much more aligned with SMEs' financing needs. Another positive feature has been the frequent combination of investment and technical assistance operations, although the latter were not always squarely focused on SMEs.
- **Effectiveness of SME assistance operations is rated moderately satisfactory.** Due to design weaknesses, the Bank's ability to reach SMEs was limited, with the majority of projects performing well below target. Out of the sample of 17 operations for which detailed data are available, 10 missed their targets by more than 25 percent, three performed on target, and four over performed. These projects provided financing to 1,800 firms. While 90 percent of these beneficiaries can indeed be reasonably characterized as SMEs, they received less than 40 percent of the US$622 million disbursed. The rest went to large enterprises, each receiving on average about US$2 million, compared with an average of US$150,000 for SMEs. Only a few financial intermediaries expanded their SME portfolio and even fewer introduced new financial products for SMEs. On the positive side, the majority of projects performed well in financial terms, experiencing little or no defaults. The effects of the Bank's

SME assistance are difficult to gauge, partly due to the lack of information. In the case of the 15 operations for which accurate data on employment were available, a crude before-and-after comparison suggests an increase in employment of some 25,000 people, of which about 15,000 were in SMEs and the remainder in large enterprises.

- **The additionality of the Bank's intervention is rated as moderately satisfactory.** Provision of long-term resources enabled financial intermediaries to match the demand for term credit (medium to long-term lending). The Bank was also an important investor in a dozen equity funds, contributing to their commercial viability. However, the Bank rarely played a catalytic role. Most intermediaries were recipients of or were concurrently receiving substantial support from other MDBs/DFIs. In the case of equity funds, the Bank was rarely a first-round investor, and again other MDBs/DFIs also provided substantial funding. Non-financial additionality is rather modest. The majority of banks receiving credit lines from the Bank were also supported with technical assistance, but these interventions did not significantly influence project results.
- **Sustainability** – Little can be said about sustainability due to the limited number of completed projects and the paucity of development results sustained. Therefore, it was not possible to rate this criterion.
- **Efficiency of the organizational set-up and procedures are rated as moderately satisfactory.** Over the study period (2006–2013), the average time required to process an investment operation was about 10–12 months, i.e. about twice the average approval time at the International Finance Corporation and the European Bank for Reconstruction and Development. Similarly, the Bank had about twice as many approval gates, with a particularly laborious project clearance process. Finally, there is limited sharing of experience between the various units involved in SME-related work. However, some improvements were recently introduced for operations undertaken in the framework of the ASMEP, which provides a streamlined approval procedure. No particular issues emerged regarding disbursements of investment operations, whereas problems were found with technical assistance operations, with the

complexity of procurement procedures being the subject of criticism from clients. The Private Sector and Microfinance Department of the Bank, responsible for investment operations and related technical assistance, handled the bulk of SME assistance operations.

- Appropriateness of monitoring and evaluation arrangements are rated as moderately unsatisfactory. The monitoring and evaluation of SME assistance operations is challenging, requiring design of appropriate measuring tools and the collection of a significant mass of data. The matter is further complicated by the two-tiered structure of most SME operations, which in principle requires information from both immediate beneficiaries (banks, equity funds, etc.) and ultimate beneficiaries (the SMEs). Tools for measuring the performance of SME assistance operations were developed in the framework of the ASMEP. However, serious problems persist in data collection, with client financial institutions showing little inclination to provide data in a timely manner and Bank staff sometimes hesitating to put pressure on clients.



Where do we go from here?

1. **Develop a comprehensive conceptual framework** (e.g., dedicated strategy) for SME assistance, accompanied by a revamping of analytical work, which could provide useful inputs both for policy formulation and for the design of specific operations.

2. **An official definition of SME should be adopted by the Bank** so that the target groups are clearly defined. The definition of SME put forward by the ASMEP, based on size, is a good starting point, as it differentiates between small and medium firms and countries at different levels of development. In the case of operations with financial intermediaries, the Bank may consider complementing the size-based definition with one based on loan size, which is likely to be more easily handled by PFIs.

3. **Expand the utilization of local currency financing,** which is currently envisaged under the ASMEP, and the Bank should definitely make efforts to translate this into concrete action.

4. **Improve the design of investment operations,** with a more accurate assessment of PFIs' financial needs, with the primary objective of drastically reducing cancellations. This should be accompanied by a more realistic assessment of PFIs' propensities and abilities to effectively serve SME clients, with the setting of more realistic targets.

5. **Diversify the range of client PFIs and countries of operations,** which is already envisaged by the ASMEP, and the Bank should definitely deploy efforts to translate this into concrete action.

6. **Strengthen eligibility conditions to ensure that SMEs are effectively reached.** In the case of PFIs, eligibility conditions must be clearly specified so that on-lending (a financial intermediary lending money borrowed from another organization) is aligned with the intended objectives.

7. **Improve the relevance of technical assistance and facilitate its implementation.** Technical assistance initiatives should be tailored to the specific needs of each intermediary and be more consistently aligned with the objectives of the associated lending or investment operations. In addition, to avoid delays in the deployment of technical assistance, the Bank should consider a simplification of procurement procedures to better match the capabilities of beneficiaries.

8. **Improve coordination among services involved in SME assistance** by establishing mechanisms (e.g., community of practice) to achieve a greater integration among the various Bank services concerned. This could be done through the creation of a community of practice, linking all the staff involved in SME-related operations and facilitating the sharing of experiences and best practices.

9. **Simplify project approval procedures by** building upon the experience gained through the simpler procedures exhibited in the ASMEP: reduce the number of project approval; streamline approval procedures based on no-objection mechanisms or on the delegation of powers to senior management.

10. **Improve the collection of information on project achievements** by requiring PFIs to provide at a minimum: (i) the number and basic features of the sub-loans; (ii) detailed data on the composition of their portfolio, with a separate indication of the number and value of operations with SMEs (based on a uniform definition of SMEs); and (iii) data on non-performing operations, again with a separate indication of the relevant parameters for SMEs. PFIs should also be required to collect information on client SMEs for at least some basic variables (turnover, employment, exports).

11. **Establish a system to monitor and report on development results.** Such systems are currently standard in most MDBs (e.g. the Development Outcome Tracking System in the International Finance Corporation, and the Transition Impact Monitoring System in the European Bank for Reconstruction and Development).

Author's Profile

Khaled Samir Hussein is a Principal Evaluation Officer in the Independent Development Evaluation Department of the African Development Bank. Previously, he worked with the Islamic Development Bank and the Egyptian Ministry of Foreign Trade. His evaluation work focuses on AfDB's private sector interventions, particularly the thematic areas of financial intermediation, small and medium enterprise (SME) development and public private partnership (PPP). Khaled holds a B.A. in Economics and Computing and an M.S. in Finance and Risk Management from the ICMA Centre, University of Reading in the United Kingdom.