Ex post evaluation – Tajikistan

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Sector: Formal sector financial intermediaries (CRS code 24030)
Programme/Project: Financial sector programme I BMZ No. 2012 656 28* / 2012 702 48 (CM) and Financial sector programme II BMZ No. 2014 679 92 / 2014 702 36 (CM)
Implementing agency: Ministry of Economic Development and Trade

Ex post evaluation report: 2020

All figures in EUR million For detailed information see next page	Total (Planned)	Total (Actual)
Investment costs (incl. CM)	16.00	12.64
Counterpart contribution	0.00	0.00
Funding	16.00	12.64
of which BMZ budget funds	16.00	12.64

*) Random sample 2019

Summary: The financial sector programme supported the expansion of sustainable lending with the goal of improving the housing situation of private households with low to medium incomes in rural areas. Furthermore, the project was designed to strengthen the national financial system. Alongside providing refinancing resources to expand lending by banks and micro-finance institutions, FC also provided funds for a complementary measure: the private financial institutions were supported by a consultant to develop loan offers for specific target groups and to disburse loans efficiently and profitably to private households. For this purpose, the Ministry for Economic Development and Trade (MEDT) received a EUR 7 million grant for both Phase I and Phase II of the project to refinance qualified financial institutions (FI), and a grant of EUR 1.0 million for a complementary measure (CM).

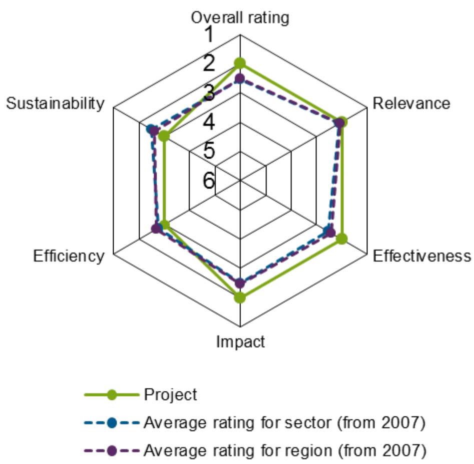
Development objectives: The aim of the FC measure was to expand the sustainable loan business of private financial institutions in Tajikistan with regard to housing finance (construction, purchasing, modernisation and extension) for the long-term and efficient use by the target group (outcome). The FC measure was intended to help promote the private sector by broadening and deepening the financial sector. Improving the supply of loans was intended to boost the housing situation of private households earning low to medium incomes (impact).

Target group: The direct target group of the FC measure was the partner finance institutions participating in the programme. The indirect target group comprised private households in rural regions carrying out housing investments.

Overall rating: 2 (both phases)

Rationale: The financial sector programme stands out due to being highly relevant. The funds provided were able to finance additional housing in rural areas. However, both sustainability and efficiency can only be rated as satisfactory, partly because of developments beyond the control of the programme.

Highlights: The development standard of the financial sector in Tajikistan is inadequate. Combined with difficult macroeconomic conditions, this means that housing finance in the classic sense, with relatively large amounts of credit and long maturities, was unable to take hold. Despite the grant funding provided, real interest rates remain high for ultimate borrowers. However, the additional housing created has made a lasting improvement to the living conditions of the rural population. The programme created a range of financing offers adapted to the given conditions, and was therefore met with a high level of satisfaction from the ultimate borrowers.



Rating according to DAC criteria

Overall rating: 2 (all phases)

Ratings:

Relevance	2
Effectiveness	2
Efficiency	3
Impact	2
Sustainability	3

Breakdown of total costs

(EUR million)	Project A (Planned)	Project A (Actual)	Project B (Planned)	Project B (Actual)
Investment costs (total)	7.00	7.00	7.00	4.56
Counterpart contribution	0.00	0.00	0.00	0.00
Funding	7.00	7.00	7.00	4.56
of which BMZ budget funds	7.00	7.00	7.00	4.56
Complementary measure (total)	1.00	0.98	1.00	0.10
Counterpart contribution	0.00	0.00	0.00	0.00
BMZ funds	1.00	0.98	1.00	0.10

Relevance

At the time of the project appraisal, the programme was highly relevant for the Tajik finance sector and the target group. When the project started, there was a liquidity squeeze in the local currency within the Tajik finance sector due to the macroeconomic conditions (this still applies today). The economy is heavily dependent on remittances from guest workers in Russia. This is why a large part of domestic deposits are denominated in foreign currencies. Commercial loans are also often denominated in foreign currency, which results in significant currency risks for borrowers. The high interest rates for local-currency loans made it impossible for many potential borrowers to carry out housing investments, especially since foreign-currency loans were generally not an option either, because of exchange-rate risks.

Promoting lending to borrowers in rural areas was consistent with the country's strategy, which recognised the lack of housing loan offers to finance the purchase, construction, extension and renovation of private homes as a significant bottleneck in the process for improving the target group's poor housing and living conditions, especially in rural areas. Housing construction in Tajikistan was chronically underfunded and there was a great need to renovate existing housing. The aims of the programme were also consistent with the German development cooperation priority of sustainable economic development in Tajikistan, as part of which the performance capacity of financial intermediaries and their funding opportunities in particular were to be strengthened.

Established microfinance banks largely in private ownership were selected to participate in the project. Only these institutions were able to provide sufficient access to the rural population. This is partly because larger institutions are not active in rural areas, but also because they do not engage in disbursing relatively small loans. This selection was consistent with the objective of the programme to provide housing finance products, and as a result of this, housing in rural areas. The public implementing agency MEDT forwarded FC's euro grant to the FIs under favourable conditions as local-currency loans, stipulating that these loans were to be disbursed to ultimate borrowers in the local currency for housing purposes. The respective FI was responsible for working out the exact conditions for the ultimate borrowers, but with refinancing rates of 6% and 8%, the interest rate was capped at 28% p.a., not to be exceeded. The maximum interest rate corresponded to the highest average loan interest rate disclosed by the National Bank of Tajikistan in the five years before the project started. The theory of change, which was designed to help the rural population invest in housing thanks to the better lending conditions by comparison, seems plausible from today's perspective too. This is why the programme was very relevant for the Tajik finance sector and the rural population, even in the context of there being no national housing programmes or public promotional institutions.

Relevance rating: 2 (both phases)

Effectiveness

The target achievement at outcome level can be summarised as follows using the indicators below:

Indicator	Status PA, target PA	Ex post evaluation
The entire housing loan portfolio net of the FC refinancing funds grows by an average of 5% p.a.	Target value: average growth of 5% p.a.	Achieved (37% p.a. average growth for 2015–2018 for the entire housing loan portfolio).
The FIs participate in the housing finance with additional funds totalling 15% of the total volume.		Achieved, the counterpart contribution was raised in the onlending agreements with the respective FIs to 40% and adhered to.
The Portfolio at Risk over 30 days of the housing loan portfolio does not exceed 5% at any of the participating FIs in any year.		Achieved. FI1: 1.71% FI2: 0.18% FI3: 0.88% FI4: 2.31%[1]
The FC refinancing funds of the housing component were paid out in full 2 years after the initial disbursement.		Achieved

In the years after the project was launched the FIs enjoyed impressive growth. The annual growth rates of all the loan portfolios were in the double-digit range. However, this growth could not be maintained as the economic situation deteriorated. In fact, some FIs are now registering a marked decline in the sizes of their loan portfolios (even though the housing loan portfolios have bucked this trend and grown continuously) and are battling against the difficult macroeconomic conditions, which is also visible in the significant deterioration in the quality of risk for the overall portfolios. Based on the evaluation we view the continuous growth in the housing loan portfolios, which goes against the general trend, as positive and sustained. Housing finance products in local currency were introduced successfully at all of the participating FIs. Prior to this, there were no special products for housing finance, and so normal consumer loan products were used in this context in some cases. Thanks to the training of loan officers and the support given to the evaluations and cost analyses of housing projects, the complementary measure helped the FIs expand their product portfolio and offer home loans in rural areas to a significant extent.

We rate the effectiveness as good on account of the convincing results at outcome level, including the sound risk quality of the housing loan portfolio.

Effectiveness rating: 2 (both phases)

[1] For comparison: The overall PAR30 of the participating FIs was 14.63%, 6.41%; 3.00%, 3.04%. The share of non-performing loans in the entire banking sector is still high at 30%.

Efficiency

The funds were made available to the implementing agency, the Ministry for Economic Development and Trade, in the form of a grant. Under a quick and efficient procedure the ministry forwarded the funds on to the FIs in the form of loans. The FIs repay these loans to a special revolving fund over time, which then channels the money back into the financial sector as investments – with a particular focus on financing small and medium-sized enterprises (SMEs). This ensures the money repaid is used in a manner that benefits development, and justifies the use of grant funds. A repeated use approach for housing loans would have been desirable from the perspective of the programme, but the applied solution is justified for efficiency reasons since the revolving fund ensures the counterpart funds of all FC financial sector projects are used in Tajikistan. The use and design of the revolving fund is not part of the programme evaluated here.

In principle, all FIs received the refinancing funds from MEDT in the local currency at interest rates of 8% p.a. and for terms of up to 10 years. There was no differentiation between the FIs. If evidence was provided that the loans created a certain number of additional square metres of housing, a rebate was given, bringing the interest rate down to 6%. The conditions for the onlending of the funds from the implementing agency MEDT to the FIs were not altered or continuously checked during the term of the programme, which would have made sense given the fluctuations in the national interest rate and would have increased the level of ambition of the FIs.

It was envisaged during the appraisal that the FIs would disburse the funds to the ultimate borrowers based on their own cost analyses. Sufficient competition was expected in the sector so that only a maximum interest rate of 28% p.a. was determined. At the time of the appraisal, the interest rates for available credit products ranged up to 35% p.a. Apart from the interest rate ceiling mentioned above, the FIs had sole discretion over the specific conditions governing the disbursement of the loans to the ultimate borrowers. Most of the FIs did not link these conditions to the specific creditworthiness of their clients. Moreover, it was found that the FIs tended to disburse loans at the maximum possible interest rate of 28% p.a. at the start of the programme, regardless of the actual term of the loan. It was also determined that there was no sufficient competition between the institutions in many rural areas. The ultimate borrowers also displayed low financial literacy as well as high loyalty to the FIs, which created little motivation to make housing loan products less expensive.

Given the low refinancing rates for the FIs in the project, they were able to use part of the high interest margin created in this way as a cross-subsidy to make other financing components from their own funds less expensive or more affordable for the borrowers. This produces a significant gearing effect for the FC funds.

However, it must be noted that most individual loans only covered a small part of the given project (up to roughly 60% of the total). The FIs revealed that the clients had to pay additional charges because of informal transaction costs (e.g. mandatory mortgage for loans exceeding the equivalent of roughly USD 6,000). This meant that lower loan amounts were often selected. Given the high real interest rates of around 20%, loans were only taken out in many cases once all other options had been exhausted (relatives, remittances from Tajik guest workers in Russia).

The margin between the loan interest rates and the refinancing rates in the evaluated project is very high. This is partly due to the rural character of the programme, which led to a less favourable processing and administrative cost structure at the FIs. However, we also assume that inefficiencies in the finance sector, high risk costs, a low level of competition and a lack of general financial literacy among the ultimate borrowers were additional factors behind the high interest rate. Given the design of the loans (no real estate as collateral, relatively low amounts and short terms) they mostly resembled microfinance and are therefore considered incremental housing loans (repeated borrowing for further building phases).

In spite of the rapid provision and disbursement as well as the significant gearing of the FC funds we only rate the efficiency of the programme as satisfactory given the high interest margin.

Efficiency rating: 3 (both phases)

Impact

All of the FIs observe the basic principles of managing financial transactions responsibly. A random examination of the loan files revealed no cases in which the loans were not used for the stated purpose.

It should be noted that all of the ultimate borrowers who were surveyed very much appreciated the opportunity to take out a housing loan. It was often necessary to keep the loan amounts relatively low due to the lack of documents on collateral for the property and the limited creditworthiness. To carry out housing projects it was therefore necessary to draw several loans one after the other. Moreover, the increased transaction costs for land registry extracts, for example, reduced the willingness of the ultimate borrowers to commit to higher loan amounts that required some form of collateral. The typical costs reported by the ultimate borrowers and FIs for producing documents were much higher than the official figures cited by MEDT corresponding to the maximum amounts that the local authorities are supposed to charge.

Given the macroeconomic conditions that were beyond the scope of the programme, the gradual disbursement approach seems to be a sensible and tailored (or the only) opportunity to finance housing projects for the envisaged target group. This is countered by the elevated risk of non-performance if the financing of the entire project is not secured from the very beginning.

The FC refinancing funds were forwarded to borrowers who had to use them explicitly for projects in rural areas outside of the large urban centres. The FIs selected the individual borrowers, and the defined target group (households with low to medium incomes) was reached. The borrowers assigned to the FC refinancing benefited from the slightly lower interest rates (when compared to consumer loans before the introduction of the programme). Moreover, the bank disbursed other loans under the same conditions using its own funds. Some 6,575 loans have been disbursed so far, with another 5,463 borrowers supported with the co-financing agreed with the FIs. The average loan size is 22,783 somonis, which at the current exchange rate amounts to around EUR 2,100. Roughly 49% of all loans were used for new constructions or extensions, 43% for renovations and 8% to buy existing homes. One significant objective of the measure was to create more housing. Since no indicator was formulated for this during the appraisal, the additional housing created was surveyed during the evaluation. The data for this was available since the FIs were able to benefit from an interest rebate from the implementing agency if proof of the additional housing created (compared to the renovation of existing housing) was provided. In this case, the interest rate payable was reduced from 8% p.a. to 6% p.a. The fulfilment of the requirements for the rebate mechanism was documented and checked by the implementation consultant.

Overall, we rate the impact of the programme as good.

The achievement of the objective at impact level can be illustrated by means of the new indicator:

Indicator	PA target value	Ex post evaluation
Additional square metres of housing with direct FC refinancing	36,850 sqm	Achieved, 37,847 sqm

Impact rating: 2 (both phases)

Sustainability

Given the programme's favourable refinancing conditions in the Tajik currency of the somoni, the FIs were able to offer housing loans at moderately reduced interest rates (compared to consumer loans before the programme started). Thanks to the lasting impact of the additional square metres in built housing, the programme has a long-term positive impact on the living standards of the given ultimate borrowers and their housing situation. The FIs were trained to provide support to ultimate borrowers with regard to the sustainable planning of housing projects, and together with the implementation consultant they ensured the funds were used appropriately. The financed housing projects are sustainable and fulfil the basic national quality standards.

However, given the interest rates of between 24% p.a. and 28% p.a. and assuming an average national inflation rate of between 5% p.a. and 8% p.a. since 2014 (as reported by the Asian Development Bank), the real interest rates in the programme have settled at around 20% p.a. Yet traditional housing loans are characterised by higher volumes and longer terms compared to consumer loans, and with real interest rates of 20%, neither of these characteristics can be sustained in the long term. No borrower will opt for long loan terms as the overall burden caused by the repayments and the interest is not feasible. However, shorter terms are only an option if the loan amount is reduced accordingly to make the monthly charge bearable. This leads to the scenario described above that several small loans often had to be taken out one after the other in order to implement a construction project.

Furthermore, it is highly likely that the interest rates for housing loans in Tajik somoni will become more expensive again as soon as the FIs no longer have this favourable refinancing available. The IFC reportedly wants to build on the success of the programme and provide additional funds to the sector once the programme ends. However, these developments are not yet confirmed and so they are not taken into account in this ex post evaluation. What is more, the FIs repay the loans to the national refinancing fund that focuses exclusively on SMEs, so the funds do not benefit the housing sector on a lasting basis. It would seem sensible to review the objectives of this refinancing fund.

Based on the favourable refinancing in the local currency under the project, the FIs were able to offer relatively low-interest loans and massively expand the options on offer. The building projects that this enabled have a lasting positive effect on the housing situation of the borrowers. Once the favourable FC refinancing is no longer available, the range of loans will presumably narrow and the related conditions will become more expensive. When the programme funds are used up it is therefore possible that the housing loan portfolio will contract, but none of the FIs indicated they wanted to completely abandon this product in the future.

Regardless of this, it should be noted that the complementary measure (CM) has triggered a lasting effect at the FIs by creating expertise and establishing loan processes to finance housing. This has created professional risk management at the FIs, and some of the staff trained with CM funds are now experts at the FIs and continue to pass their knowledge on.

Given that the impact of the FIs on the supply of loans is likely to be temporary, the sustainability of the programme is only rated as satisfactory.

Sustainability rating: 3 (both phases)

Notes on the methods used to evaluate project success (project rating)

Projects (and programmes) are evaluated on a six-point scale, the criteria being **relevance, effectiveness, efficiency** and **overarching developmental impact**. The ratings are also used to arrive at a **final assessment** of a project's overall developmental efficacy. The scale is as follows:

Level 1	Very good result that clearly exceeds expectations
Level 2	Good result, fully in line with expectations and without any significant shortcomings
Level 3	Satisfactory result – project falls short of expectations but the positive results dominate
Level 4	Unsatisfactory result – significantly below expectations, with negative results dominating despite discernible positive results
Level 5	Clearly inadequate result – despite some positive partial results, the negative results clearly dominate
Level 6	The project has no impact or the situation has actually deteriorated

Rating levels 1-3 denote a positive assessment or successful project while rating levels 4-6 denote a negative assessment.

Sustainability is evaluated according to the following four-point scale:

Sustainability level 1 (very good sustainability): The developmental efficacy of the project (positive to date) is very likely to continue undiminished or even increase.

Sustainability level 2 (good sustainability): The developmental efficacy of the project (positive to date) is very likely to decline only minimally but remain positive overall. (This is what can normally be expected).

Sustainability level 3 (satisfactory sustainability): The developmental efficacy of the project (positive to date) is very likely to decline significantly but remain positive overall. This rating is also assigned if the sustainability of a project is considered inadequate up to the time of the ex post evaluation but is very likely to evolve positively so that the project will ultimately achieve positive developmental efficacy.

Sustainability level 4 (inadequate sustainability): The developmental efficacy of the project is inadequate up to the time of the ex post evaluation and is very unlikely to improve. This rating is also assigned if the sustainability that has been positively evaluated to date is very likely to deteriorate severely and no longer meet the level 3 criteria.

The **overall rating** on the six-point scale is compiled from a weighting of all five individual criteria as appropriate to the project in question. Rating levels 1-3 of the overall rating denote a "successful" project while rating levels 4-6 denote an "unsuccessful" project. It should be noted that a project can generally be considered developmentally "successful" only if the achievement of the project objective ("effectiveness"), the impact on the overall objective ("overarching developmental impact") and the sustainability are rated at least "satisfactory" (level 3).