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USAID Project No. 615-0263
Dollar Appropriation No.725/61014
Budget Plan Code: GSS5-95-21615-KG13

PROJECT GRANT AGREEMENT

BETWEEN

THE REPUBLIC OF KENYA

AND THE

UNITED STATES OF AMERICA

FOR

MICRO-PRIVATE ENTERPRISE DEVELOPMENT
[MICRO-PED]

DATED: August 30, 1995

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PROJECT GRANT AGREEMENT FOR MICRO-PRIVATE ENTERPRISE DEVELOPMENT

Dated: August 30, 1995

Between

The Republic of Kenya (hereinafter referred to as the "Grantee")

and

The United States of America, acting through the United States Agency for International Development ("USAID").

Article 1: The Agreement

The purpose of this Agreement is to set out the understanding of the parties named above ("Parties") with respect to the undertaking by the Grantee of the Project described below, and with respect to the financing of the Project by the Parties.

Article 2: The Project

SECTION 2.1. Definition of Project. The Project, which is further described in Annex 1, is designed to increase employment in Kenyan micro-enterprises, firms with fewer than ten employees. The project will improve the policy environment for micro-enterprises through conducting research, facilitating policy dialogue, increasing the capacity of the Government of Kenya to implement policy change and other activities. The project will increase employment in targeted sub-sectors through the provision of cost-effective services designed to alleviate constraints of micro-enterprises operating in these sub-sectors. The project will increase the sustainable delivery of financial services to micro-enterprises. The project will contribute to increased learning and institutional capacity in interventions to generate employment in micro-enterprises.

Annex 1, attached, amplifies the above definition of the Project. Within the limits of the above definition of the Project, elements of the amplified description stated in Annex 1 may be changed by written agreement of the authorized representatives of the Parties named in Section 8.2 without formal amendment of this Agreement.

SECTION 2.2. Incremental Nature of Project.

(a) USAID's contribution to the Project will be provided in increments, totalling $12,000,000 (Twelve Million U.S. Dollars), the initial one being made available in accordance with Section 3.1 of this Agreement. Subsequent increments will be provided subject to the availability of funds allocated to USAID for this purpose, and to the mutual agreement of the Parties, at the time of each subsequent increment, to proceed.

(b) Within the overall Project Assistance Completion Date ("PACD") stated in this Agreement, USAID, in consultation with the Grantee, may specify in Project Implementation Letters appropriate time periods for the utilization of funds granted by USAID under each individual increment of assistance.

Article 3: Financing

SECTION 3.1. The Grant. (a) To assist the Grantee to meet the costs of carrying out the Project, USAID, pursuant to the Foreign Assistance Act of 1961, as amended, agrees to grant the Grantee under the terms of this Agreement not to exceed Two Million Five Hundred Thousand United States ("U.S.") Dollars ($2,500,000) ("Grant"). (b) If at any time USAID determines that its contribution to the Project under this sub-section exceeds the amount which reasonably can be committed for project purpose during the current or following U.S. fiscal year, upon written notice to the Grantee, USAID may withdraw the excess amount, thereby reducing the amount of the Grant, as set forth on Subsection 3.1(a). Actions taken pursuant to this Subsection shall not reduce USAID's total estimated contribution to the project below that contained in Subsection 2.2(a), subject to the availability of funds allocated to USAID for this purpose and to the mutual agreement of the Parties, at the time of each subsequent increment, to proceed.

The Grant may be used to finance foreign exchange costs, as defined in Section 6.1 of this Agreement, and local currency costs, as defined in Section 6.2 of this Agreement, of goods and services required for the Project.

SECTION 3.2. Grantee Resources for the Project.

(a) The Grantee agrees to provide or cause to be provided for the Project all funds, in addition to the Grant, and all other resources required to carry out the Project effectively and in a timely manner.

(b) The resources provided by the Grantee and private sector participants in the Project will not be less than the equivalent of US $5.355 million, (US $101,000 -- all "in-kind", from the Grantee and $5,254,000 from the sub-grantees) including costs borne on an "in-kind" basis. This represents 31% of total Project costs.

(c) USAID will have individual separate agreements with sub-grantees.

(d) GOK will bear no responsibility for accounting for subgrantee funds.

SECTION 3.3. Project Assistance Completion Date (PACD).

(a) The PACD, which is September 30, 2000, or such other date as the Parties may agree to in writing, is the date by which the Parties estimate that all services financed under the Grant will have been performed and all goods financed under the Grant will have been furnished for the Project as contemplated in this Agreement.

(b) Except as USAID may otherwise agree in writing, USAID will not issue or approve documentation which would authorize disbursement of the Grant funds for services performed subsequent to the PACD or for goods furnished for the Project, as contemplated in this Agreement, subsequent to the PACD.

(c) Requests for disbursement, accompanied by necessary supporting documentation prescribed in Project Implementation Letters, are to be received by USAID or any bank described in Section 7.1 no later than nine (9) months following the PACD, or such other period as USAID may agree to in writing. After such period, USAID giving notice in writing to the Grantee, may at any time or times reduce the amount of the Grant by all or any part thereof for which requests for disbursement, accompanied by necessary supporting documentation prescribed in Project Implementation Letters, were not received before the expiration of said period.

Article 4: Conditions Precedent

SECTION 4.1. Conditions Precedent to First Disbursement.

Except as USAID may otherwise agree in writing, prior to any disbursement under the Grant, or to the issuance by USAID of documentation pursuant to which such disbursement will be made, the Grantee shall furnish or have furnished to USAID, in form and substance satisfactory to USAID a written statement setting forth the names and titles of persons holding or acting in the Office of the Grantee and of any additional representatives, and representing that the named person or persons have the authority to act as the representative or representatives of the Grantee, together with a specimen signature of each such person certified as to its authenticity.

SECTION 4.2 Additional Conditions Precedent

Prior to disbursement of USAID funds to the GOK for assistance to the Trade and Industry Unit of the Kenya Institute of Public Policy, Research and Analysis (KIPPRA), the Grantee shall furnish or have furnished to USAID in form or substance satisfactory to USAID written evidence that KIPPRA has been formed and Gazetted, a Director and key Economic Advisor are in place and office space for the Trade and Industry Unit has been allocated.

SECTION 4.3. Notification. When USAID has determined that the conditions precedent specified in each of Sections 4.1 and 4.2 have been met, USAID will promptly so notify the Grantee.

SECTION 4.4. Terminal Dates for Conditions Precedent.

(a) If all the conditions specified in Section 4.1 have not been met within 60 days from the date of this Agreement, or such later date as USAID may agree to in writing, USAID, at its option, may terminate this Agreement by written notice to the Grantee.

(b) If all the conditions specified in Section 4.2 have not been met within 1 year from the date of this Agreement, or such other date as USAID may agree to in writing, USAID, at its option, may cancel the portion of the Grant related to KIPPRA and may terminate this Agreement by written notice to the Grantee.

Article 5: Special Covenants

SECTION 5.1. Project Evaluation. The Parties agree to establish an evaluation program as part of the Project. Except as the Parties may otherwise agree in writing, the program will include, during the implementation of the Project and at one or more points thereafter:

(a) evaluation of progress towards attainment of the objectives of the Project;

(b) identification and evaluation of problem areas or constraints which may inhibit such attainment;

(c) assessment of how such information may be used to help overcome such problems; and,

(d) evaluation, to the degree feasible, of the overall development impact of the Project.

SECTION 5.2. Exemption from Duty and Taxes. The Grantee agrees to except all agencies charged with the implementation of MICRO-PED from customs duties, Value Added Tax (VAT) and to exempt from income tax and National Social Security contributions all income or other emoluments received by non-Kenyan technical staff contracted under this activity. The Grantee also agrees to approve work permits for non-Kenyan technical staff employed for this activity.

Article 6: Procurement Source

SECTION 6.1. Foreign Exchange Costs. Except as USAID may otherwise agree in writing, disbursements pursuant to Section 7.1 will be used exclusively as follows.

(a) to finance the costs of goods and services required for the Project having, with respect to goods, their source and origin, and with respect to services, their nationality in Code 935 of the USAID Geographic Code Book as in effect at the time orders are placed or contracts entered into for such goods or services, except as provided in the Project Grant Standard Provisions Annex 2, Section C.1(b) with respect to marine insurance. All reasonable efforts will be used to maximize U.S. Procurement whenever practicable. Air travel and transportation to and from the U.S. shall be upon certified U.S. Flag carriers. Other air transportation financed under this Grant of property or persons, will be on carriers/holding U.S. certification, to the extent services by such carriers are available.

(b) to finance ocean transportation costs under the Grant only on vessels under flag registry of the countries included in AID Geographic Code 935 and the cooperating country, subject to 50/50 shipping requirements under the Cargo Preference Act and the regulations promulgated thereunder.

SECTION 6.2. Local Currency Costs. Disbursements pursuant to Section 7.2 will be used exclusively to finance the costs of goods and services required for the Project having their source and, except as USAID may otherwise agree in writing, their origin in the Republic of Kenya or in countries included in USAID Geographic Code 935 "Local Currency Costs." To the extent provided for under this Agreement, Local Currency Costs may also include the provision of local currency resources required for the Project.

Article 7: Disbursement

SECTION 7.1. Disbursement for Foreign Exchange Costs.

(a) In accordance with requirements of conditions precedent, the Grantee may obtain disbursements of funds under the Grant for Foreign Exchange Costs of goods or services required for the Project in accordance with the terms of this Agreement, by such of the following methods as may be mutually agreed upon:

(1) by submitting to USAID, with necessary supporting documentation as prescribed in Project Implementation Letters, (A) requests for reimbursement for such goods or services, or, (B) requests for USAID to procure commodities or services on Grantee's behalf for the Project; or,

(2) by requesting USAID to issue Letters of Commitment for specified amounts (A) to one or more U.S. banks, satisfactory to USAID, committing USAID to reimburse such bank or banks for payments made by them to contractors or suppliers, under Letters of Credit or otherwise, for such goods or services, or (B) directly to one or more contractors or suppliers, committing USAID to pay such contractors or suppliers for such goods or services.

(b) Banking charges incurred by Grantee in connection with Letters of Commitment and Letters of Credit will be financed under the Grant unless Grantee instructs USAID to the contrary. Such other charges as the Parties may agree to may also be financed under the Grant.

SECTION 7.2. Disbursement for Local Currency Costs.

(a) In accordance with requirements of conditions precedent, the Grantee may obtain disbursements of funds under the Grant for Local Currency Costs required for the Project in accordance with terms of this Agreement, by submitting to USAID, with necessary supporting documentation as prescribed in Project Implement77ation Letters, requests to finance such costs.

(b) The local currency needed for such disbursements may be obtained:

(1) by acquisition by USAID with U.S. dollars by purchase or from local currency already owned by the U.S. Government; or,

(2) by USAID, (A) requesting the Grantee to make available the local currency for such costs, and (B) thereafter making available to the Grantee, through the opening or amendment by USAID of Special Letters of Credit in favor of the Grantee or its designee, an amount of U.S. dollars equivalent to the amount of local currency made available by the Grantee, which dollars will be utilized for procurement from the United States under appropriate procedures described in Project Implementation Letters.

The U.S. dollar equivalent of the local currency made available hereunder will be, in the case of subsection (b) (1) above, the amount of U.S. dollars required by USAID to obtain the local currency, and in the case of subsection (b) (2) above, an amount calculated at the rate of exchange specified in the applicable Special Letter of Credit Implementation Memorandum hereunder as of the date of the opening or amendment of the applicable Special Letter of Credit.

SECTION 7.3. Other Forms of Disbursement. Disbursements of the Grant may also be made through such other means as the Parties may agree to in writing.

SECTION 7.4. Rate of Exchange. Except as may be more specifically provided under Section 7.2, if funds provided under the Grant are introduced into Kenya by USAID or any public or private agency for purposes of carrying out obligations of USAID hereunder, the Grantee will make such arrangements as may be necessary so that such funds may be converted into currency of Kenya Shillings at the highest rate of exchange which, at the time the conversion is made, is not unlawful in Kenya.

Article 8: Miscellaneous

SECTION 8.1. Communications. Any notice, request, document, or other communication submitted by either Party to the other under this Agreement will be in writing or by telegram or cable, and will be deemed duly given or sent when delivered to such party at the following addresses:

To the Grantee:
Mail Address:
Permanent Secretary
Ministry of Finance
P.O. Box 30007
Nairobi, Kenya

Alternative address for cables: Finance, Nairobi, Kenya.

To USAID:

Mail Address:
The Director
USAID Mission to Kenya
P.O. Box 30261
Nairobi, Kenya

Alternative address for cables: USAID/Kenya, AMembassy, Nairobi

All such communications will be in English, unless the Parties otherwise agree in writing. Other addresses may be substituted for the above upon the giving of notice. The Grantee, in addition, will provide the USAID Mission to Kenya with a copy of each communication sent to and from USAID/Washington.

SECTION 8.2. Representatives. For all purposes relevant to this Agreement, the Grantee will be represented by the individual holding or acting in the office of the Permanent Secretary, Ministry of Finance and USAID will be represented by the individual holding or acting in the Office of the Director, USAID Mission to Kenya, each of whom, by written notice, may designate additional representatives for all purposes other than exercising the power under Section 2.1 to revise elements of the Amplified Project Description in Annex 1. The names of the representatives of the Grantee, with specimen signatures, will be provided to USAID, which may accept as duly authorized any instrument signed by such representatives in implementation of this Agreement, until receipt of written notice of revocation of their authority.

SECTION 8.3. Standard Provisions Annex. A "Project Grant Standard Provisions Annex" (Annex 2) is attached to and forms part of this Agreement.

IN WITNESS WHEREOF, the Grantee and the United States of America, each acting through its duly authorized representative, have caused this Agreement to be signed in their names and delivered as of the day and year first above written.

FOR REPUBLIC OF KENYA

BY: [signature]

NAME: B.K. Kiplagat

TITLE: PS - TREASURY

FOR UNITED STATES OF AMERICA

BY: [signature]

NAME: George Jones

TITLE: Director USAID

FOR UNITED STATES OF AMERICA

BY: _____

NAME: _____

TITLE: _____

Attachments:

Annex 1 - Project Description including illustrative budget table

~~Annex 2 - Project Grant Standard Provisions (HB 3, App 6-A 1).~~

AMPLIFIED PROJECT DESCRIPTION

ANNEX 1

I GENERAL PROJECT DESCRIPTION

0.1 PROJECT SUMMARY

The goal of the MICRO-Private Enterprise Development (MICRO-PED) Project is to create jobs for the 3.6 million people expected to enter the labor force by the year 2000. The Project focuses on micro enterprise development, support for firms with ten or fewer employees. The micro enterprise, or "informal" or "Jua Kali", sector provides the greatest opportunity for providing large number of jobs. The MICRO-PED project will be organized in three components, each addressing key constraints to micro enterprise growth:

1) The Policy Component will improve the policy and regulatory environment of micro enterprises.

2) The Sub-Sector Component will increase cost-effective delivery of non-financial services to targeted sub-sectors.

3) The Finance Component will increase sustainable delivery of financial services.

The Project will be implemented through a bilateral Project Grant Agreement with the Government of Kenya, and a variety of instruments as laid out under subsection 0.24.

0.11 CONSTRAINTS, OPPORTUNITIES AND STRATEGIES

Employment creation is one of the most significant challenges facing Kenya today. The Kenyan labor force, currently numbering more than 11 million people, is growing rapidly and is expected to reach 14.6 by the year 2000. Providing jobs for these 3.6 million workers constitutes today's employment challenge in Kenya. Employment is a central issue in the alleviation of poverty in Kenya, and employment is a key indicator of broad-based economic growth. Private enterprises show good prospects for creating jobs in the medium term, compared to small scale farms, which are reducing in size and productivity, and the public sector, which is also contracting. In contrast, private enterprise employment has been growing at an average annual rate of 12% over the last ten years. Within the private enterprise sector, micro enterprises (firms with less than 10 employees) are the most likely group of firms to provide widespread employment, a fact the Government of Kenya acknowledges. In 1993, micro enterprises constituted 75% of private enterprise employment and created 270,000 new jobs, compared to only 24,000 jobs created by larger firms. **Thus the GOAL of the MICRO-PED Project is to increase private enterprise employment, and the PURPOSE is to increase micro-enterprise employment.**

The micro and small enterprise sector is large and diverse, and the challenge for agencies hoping to stimulate employment growth in the sector is how to identify where the potential growth is, what constrains that growth and how to facilitate it. In assessing problems and opportunities facing micro enterprises, USAID/Kenya with REDSO/ESA and USAID/W assistance, engaged in a rigorous, participatory planning process involving sample surveys, focus group discussion with micro entrepreneurs, evaluations, consulting with partners, bringing in international experts, and years of one-to-one discussions between USAID staff and Kenyan business people. Emerging from this analysis are three major issues that drive the MICRO-PED interventions. First, many micro-enterprises are constrained by policy, regulatory and infrastructure issues. Second, many firms are faced with diminishing market opportunities, increasing competition, and problems with the cost and availability of inputs. Third, micro-enterprises do not have adequate access to credit. The MICRO-PED Project will implement strategies to overcome these constraints.

0.2 PLAN OF ACTION

Based on the above constraints and opportunity analyses, the MICRO-PED Project will be organized in three components, each addressing key constraints to micro enterprise growth: Policy, Sub-Sector Development and Finance Components. The Project will be implemented through a bilateral Project Grant Agreement with the Government of Kenya, and a variety of instruments committing funds directly to Kenyan and US private sector institutions.

0.21 Policy Component

Despite positive GOK policies towards the informal sector, surveys of micro enterprises and analyses by policy experts reveal that policy, regulatory and infrastructure issues represent significant constraints to micro enterprise growth. There is an "implementation gap" between stated policies and GOK actions on this issue. Having accomplished many major macro-economic and agricultural reforms, however, the GOK and the donor community are now focusing more on sector-specific policies, including micro enterprise policy. This creates an opportunity for USAID to contribute to the policy change process.

The output of this component will be an improved policy and regulatory environment. To achieve this target, activities will be organized around the major inputs needed to accomplish significant policy change:

1) A Policy Forum that will facilitate public-private sector dialogue, conduct appropriate research and support the GOK policy process,

2) Association development, to bring micro enterprises into the policy making process.

In addition, under this component, USAID/Kenya will engage in small research and experimental activities that inform general strategies for assisting micro enterprise and employment growth.

0.22 Sub-Sector Development Component

One of the major constraints facing micro enterprises is poorly functioning markets. Market constraints vary across sectors and solutions involve a variety of non-financial interventions. In order to strengthen micro enterprise markets, **the output of this component will be to increase the cost-effective delivery of non-financial assistance to targeted sub-sectors.** USAID/Kenya will select an Institutional Contractor (IC), a United States Private Voluntary Organization (USPVO), or a local NGO to implement the activity in partnership with Kenyan institutions. The implementing agency will combine two predominant approaches in sub-sector development: a broad analytical approach that assesses market weaknesses and identifies single interventions affecting large numbers of micro enterprises (e.g. technology or policy change); and an "incremental" approach that relies more on participation of targeted entrepreneurs and experienced NGOs to identify and address immediate felt needs of entrepreneurs. Success in strengthening markets will be evident in increased employment in the targeted sub-sectors.

0.23 Finance Component

Access to credit continues to be a major handicap facing the growth of micro enterprises in Kenya where demand far exceeds supply. The formal banking institutions have not developed appropriate instruments for supporting the micro enterprise sector although its contribution to employment creation and economic development in general has been widely acknowledged. Although micro enterprise lending in Kenya is significantly more developed than in any other African country, Kenyan micro enterprise lenders, mostly NGOs, have yet to reach levels of outreach and sustainability achieved in Latin America and Asia. This component will focus on increasing sustainable delivery of credit to micro enterprises. It will build on experiences gained under the Private Enterprise Development (PED) Project, and is likely to involve most of the NGOs who participate or have participated in that Project. The MICRO-PED Project will engage in three major activities to support the sustainable delivery of financial services to micro enterprises in Kenya:

* Assisting in the conversion of a credit-providing NGO into a formal financial institution;

* Granting funds to lending institutions that serve micro enterprises and have a reasonable chance of attaining institutional and financial sustainability by eventually raising funds through the private sector; and

* Facilitating the availability of technical assistance to micro enterprise lending institutions and programs in Kenya.

USAID will be taking a financial systems approach, aiming at supporting sustainable delivery of credit and savings facilities to the poor.

0.24 Implementing Mechanism

The MICRO-PED Project will be obligated through a Project Agreement with the Government of Kenya. Activities will be implemented through a combination of mechanisms as follows:

1. Policy Component: Project Implementation Letter with the GOK, 3 Grants or contracts with US and Kenyan policy organizations, and miscellaneous small actions by USAID/Kenya.

2. Sub-Sector Component: 1 Institutional Contractor, United States Private Voluntary Organizations (USPVO) or a local NGO who will issue grants and provide technical assistance and coordination for the activity.

3. Finance Component: 3-5 Grants to Kenyan lending institutions and 1 Institutional Contract or Grant to a USPVO for technical assistance.

The implementing mechanisms were determined by an analysis of different options, which included a cost comparison, an assessment of the administrative burden to USAID/Kenya and REDSO/ESA, an examination of the opportunities for USAID/Kenya substantial involvement in activities, and an evaluation of the potential sustainability of interventions. Potential implementing partners were consulted and their input taken into account. This implementation arrangement will likely include three USAID personal services contractors (2 FSN and 1 USPSC).

0.3 DEFINITION OF SUCCESS

Micro enterprise employment is expected to increase from an annual growth rate of 13% to one of 18%. Changes in the policy environment will be measured through a qualitative policy matrix. In the targeted sub-sectors, some 280,000 jobs will be generated each year. Through support to financial institutions, an

addition 40,000 people will have access to loans and 2 institutions will become financially sustainable. Systems to monitor these indicators will be integrated into Project management by building the capacity of partner organizations.

0.4 BUDGET

The Project has a five year life of Project and USAID funding of US $12 Million, subject to the availability of funds. Counterpart contribution from the GOK and private sector institutions will amount to 31% of total Project funds, which amount to $17.355 million.

The allocation of USAID funds among components is as follows:

1. Policy:	$ 1.95 million
2. Sub-sector:	$ 4.20 million
3. Finance:	$ 4.50 million
4. USAID Support	$ 0.90 million
5. Evaluations/Audits	$ 0.45 million

1.0 COMPONENT ONE: POLICY AND ENABLING ENVIRONMENT

The output of this component will be an improved policy and regulatory environment. To achieve this target, activities will be organized around the major inputs needed to accomplish significant policy change:

1) Establishing a Policy Forum that will facilitate public-private sector dialogue, conduct appropriate research, and supporting the GOK policy process, and

2) Association development, to bring micro enterprises into the policy making process.

In addition, under this component, USAID/Kenya will engage in small research and experimental activities that inform general strategies for assisting micro enterprise and employment growth.

1.1 Policy Forum:

The Policy Forum will bring together stake holders from the private sector, academia, researchers, non-government organizations and other groups to work together towards implementing policy changes. Participants will direct the research agenda, contribute to the research, and meet in public forums several times per year to focus on particular policy issues. The goal is that participants will take responsibility for ensuring that policy change is implemented. These participants will include a cross-section of leaders from small and large business owners, micro enterprises association executives and board members, representatives from formal sector

organizations and larger businesses, university researchers, business consultants, representatives of the NGO community, representatives of the donor community, and others. Every effort will be made to link this forum with other emerging cooperating groups in the sector. Specifically, the forum proposes to work closely with the Small Scale Jua Kali Enterprise Program Steering Committee, coordinated by the Office of Vice President and the Ministry of Planning and National Development, in two ways. One is in identifying a research agenda that reflects priorities, and ensures topics are relevant and not duplicative of other initiatives. The other is for the Steering Committee to act as a primary recipient of the research recommendations which will provide input into the deliberations of the committee. In selected instances when the GOK demonstrates a limited capacity to carry out agreed reforms, the policy forum may, if necessary, provide technical assistance and support to the relevant ministries of the GOK to support policy implementation.

The Forum will be housed in a research institution, based in Kenya and yet to be identified, which will receive a Grant or contract to manage the Policy Forum activities of the Policy Component. Much of the research will be sub-contracted to a combination of Kenyan and international policy specialists. The institution housing the Forum and the research will be a neutral entity where both public and private sector stake holders can meet and work together on a common agenda for implementing policy reform. Specific criteria will be used to select an institution that can provide an effective secretariat for the Policy Forum and manage its activities.

The policy research, most of which will be funded by the Project, will serve as the basis for policy dialogue. The general approach should include:

* Focusing on priority issues,
* Analyzing in greater detail the effects of particular existing laws and regulations on micro enterprises,
* Identifying barriers to the implementation of current policy,
* Suggesting alternative policies, and
* Developing clear and specific strategies for implementing policy change.

At least one study will focus on policy issues particular to women entrepreneurs. In addition, the Policy Forum will be responsive to policy issues affecting other activities in the Project, for example financial, technology and sector-specific policies.

The Government is a critical actor in implementing policy change. Although much of the policy research will be undertaken by independent organizations, the capacity of the GOK to analyze and implement policy change is a key element in reforms taking place. This component will support efforts to strengthen the GOK policy analysis and implementation capability. Support for increasing analytical capability will be targeted to the Trade and Industry Unit of the proposed Kenya Institute for Public Policy Research and Analysis (KIPPRA), housed within the Ministry of Planning and National Development. This assistance, in collaboration with the European Union and Africa Capacity Building Foundation, will include the financing of long-term technical assistants, training and short-term consultants, and limited capital and operating expenses for a period of four years. The sustainability of this activity will develop from the GOK planning to finance future expenses through the GOK budget, and through planned consultancies and sale of publications. In addition to assistance to KIPPRA, short-term technical assistance may be allocated to various Ministries to assist in such activities as developing regulations or streamlining procedures, and other policy change activities, on an as-needed basis.

1.2 Association Strengthening:

To be effective, policy dialogue must include both the policy makers <u>and</u> the private sector players affected by policies, in this case, micro enterprises. In order to ensure that micro entrepreneurs themselves participate in policy dialogue, there is a need to strengthen representative micro enterprise associations. Kenyan micro enterprise associations are young and have yet to succeed in providing quality services to large memberships.

Associations will be strengthened primarily through training. Other interventions may emerge as associations grow and develop proposals for other activities. Courses will be developed by a consultant or organization with extensive experience in micro or small business association development, working in collaboration with a Kenyan business training institution who will ultimately carry out the training. One of the courses will focus on management improvement for associations while the other will emphasize constructive skills for representing members and engaging in effective policy dialogue. Building capability in the small business membership organizations is a long-term program. Although training can be accomplished relatively quickly, it will take time for such organizations to develop additional strength and become effective representatives of micro enterprises.

1.3 Strategy Support

In addition to these focused activities, USAID/Kenya will engage in several small research and experimental activities designed to develop and inform the development community about new approaches to employment creation. These activities will emerge during Project implementation, but potential areas to be explored include:

a) Data collection and analysis to explore micro enterprise contribution to economic growth and the quality of micro enterprise jobs,

b) Analysis of gender constraints in micro enterprise development examining the causes and exploring solutions to women's disadvantaged position in the sector,

c) Targeted or experimental assistance to stimulate demand for micro enterprise products through stimulating wider macro-economic growth (e.g. through assistance to the Capital Markets Authority), and through increasing effective linkages to the agricultural sector, and

d) Investments in developing better monitoring tools and linking latest techniques and data to the national data reporting systems.

These and other areas of Strategy Support will be managed directly by USAID/Kenya.

Beneficiaries: The beneficiaries of the policy component will be all micro entrepreneurs, their employees and the unemployed people that will find jobs as a result of a growing micro enterprise sector. Policy reform will benefit many small businesses as well. A focus on licensing and deregulation will benefit urban businesses more, since these problems are more significant in urban areas, and a focus on infrastructure would benefit rural businesses more. At least one policy activity will specifically benefit women.

2.0 SUB-SECTOR COMPONENT

One of the major constraints facing micro enterprises is poorly functioning markets. Market constraints vary across sectors, and solutions involve a variety of non-financial interventions. In order to strengthen micro enterprise markets, **the output of this component will be to increase the cost-effective delivery of non-financial assistance to targeted sub-sectors.** Success will be evident in increased employment in the targeted sub-sectors.

The strategy of this intervention is to focus on high potential group of micro enterprises that operate in similar markets, or sub-sectors, such as the dairy sub-sector, identify particular constraints facing micro enterprises operating the sub-sector, and carry out cost-effective, non-financial interventions to alleviate these constraints. For example, micro enterprises may be constraints from trading in fresh milk because they lack refrigeration. An intervention might be to introduce large coolers adapted to the carts many micro entrepreneurs use to transport milk. Specific sub-sectors and interventions will be designed during Project implementation, but there are several operating principles that implementing organizations will subscribe to in carrying out sub-sector interventions. These principles reflect the combination of two approaches so far developed in the field of sub-sector development: a broad "analytical" approach that analyses markets weaknesses and identifies single interventions that affect large numbers of micro enterprises ("leveraged" interventions), such as technology or policy change; and an "incremental" approach that relies on NGOs to engage micro entrepreneurs in defining constraints and interventions, and focusses on the immediate felt needs of business people. This approach is still new, so strategies will evolve and lessons learned will be documented and shared.

USAID/Kenya has already identified two broad sectors that show high potential for employment creation: agri-businesses and metal related firms. The agribusiness sector, made up largely of fruit and vegetable traders, restaurants, and food processors, was selected because of its large size, high participation of women, and linkages to agriculture. In contrast, the metals sector is small, but individual firms grow quickly, most employees are either paid employees or apprentices, and the sector is instrumental in the development of the transport and machine/tool markets in Kenya, which in turn facilitate growth in all sectors. These two different sectors were also selected, in part, to learn lessons about intervening in dramatically different types of markets. These sectors represent broad categories. However, in order to identify specific constraints and interventions, more specific "sub-sectors", such as dairy or non-motorized transport, will have to be selected during Project implementation. The implementors may also identify reasons why other sectors should be considered in addition to or instead of these, but information to date indicates that the agri-business and metals sectors have a strong potential for increasing micro enterprise employment (Kristjianson & Wangia, 1995; Masinde 1995).

USAID will select an Institutional Contractor (IC), a US Private Voluntary Organization (PVO) or a local NGO to implement the sub-sector activities in partnership with Kenyan institutions. The Implementing Agency will develop a specific process for

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implementing this component, and this process may evolve andchange as lessons are learned during implementation. Based on consultation with experts and with potential Kenyan partners, the following process is suggested:

1. **Staffing:** The Implementing Agency should have one international and one Kenyan professional.

2. **Seminars:** To launch the activity, and as a coordination and monitoring instrument throughout the Project, the Implementing Agency will hold seminars with players in the broad sectors already selected as high potential - agri-business and metals.

3. **Selecting Interventions and Implementing Organizations:** After the initial seminar, and throughout the Project as additional constraints emerge, Kenyan Implementing Organizations (IOs) will propose interventions to be funded by the Project. Proposals will be selected according to a set of criteria to be developed during implementation

4. The Implementing Agency may also **solicit proposals** for additional activities.

5. **Institutional Development:** The Implementing Agency will conduct institutional analysis on likely IOs prior to awarding grants. This analysis will determine institutional capabilities and needs. Institutional development objectives will then be built into the expected outputs of the grant, and key activities (such as training, management consultants, MIS systems, and capital equipment) will be funded in the grant.

6. **Institutionalization:** By the end of year 1, the Implementing Agency will make a plan for institutionalizing the activities in which it is engaged, if applicable.

This six step process is illustrative of an approach that incorporates the operating principles, but the process may be modified as experience suggests the most effective, sustainable approaches. In addition, there may be exceptional circumstances under which cross-sectoral program would be financed, for example if such a program would increase knowledge about constraints and opportunities in different sectors or if such interventions provide valuable lessons learned about sustainable delivery of non-financial services.

Beneficiaries: Sub-sector Development will mainly assist micro entrepreneurs and employees in the agri-business and metals sectors. The agribusiness sector has a high proportion of women

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and rural entrepreneurs, and many workers who are unskilled and unpaid and, thus, poorer than workers in many other sectors. Inaddition, development of the agri-business sector will benefit farmers. In contrast, the metals sub-sector is mainly urban, and predominantly comprised of skilled men, who are well paid and who receive significant training on the job. Employment created in the agribusiness sector is, thus, more likely to reach the poor in large numbers, but jobs created in the metals sector are more likely to be high quality jobs.

3.0 COMPONENT THREE: FINANCIAL ASSISTANCE

Access to credit continues to be a major handicap facing the growth of micro enterprises in Kenya where demand far exceeds supply. The formal banking institutions have not developed appropriate instruments for supporting the micro enterprise sector although its contribution to employment creation and economic development in general has been widely acknowledged. Micro enterprise lenders, mostly NGOs, have yet to reach levels of outreach and sustainability achieved in Latin America and Asia. This component will focus on increasing sustainable delivery of credit to micro enterprises. It will build on experiences gained under the Private Enterprise Development (PED) Project, and is likely to involve most of the NGOs who participate or have participated in that Project.

The MICRO-PED Project will engage in three major activities to support the sustainable delivery of financial services to micro enterprises in Kenya:

* Assisting in the conversion of a credit-providing NGO into a formal financial institution;

* Granting funds to lending institutions that serve micro enterprises <u>and</u> have a reasonable chance of attaining institutional and financial sustainability by eventually raising funds through the private sector; and

* Facilitating the availability of technical assistance to micro enterprise lending institutions and programs in Kenya.

Under this component there will be several other minor activities. First, USAID will facilitate dialogue between Banks and NGOs to encourage NGO borrowing from banks. USAID/W loan portfolio guarantee funds, which are administered through another Project, may be instrumental in developing these relationships. Second, USAID may fund small, experimental initiatives to develop additional loan products to serve clients who are not being served by current products. Third, USAID may fund the development of innovative training curricula in private sector

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organizations that offer training to micro enterprise lending institutions.

3.1 Conversion of an NGO into a Formal Financial Institution

MICRO-PED will assist the major credit NGO in Kenya, Kenya Rural Enterprise Program (K-REP) through the critical stage of transition from an NGO to a formal financial institution. This will include strengthening K-REP's capacity to extend and collect loans on a widespread basis, establish savings instruments attractive to depositors, attract domestic investors, explore the possibilities of attracting funds from the capital markets of Kenya, and provide quality training to its employees. K-REP, the major player under the PED Project, is a dominant player in micro enterprise finance in Kenya and has the most concrete plans for attaining sustainability, to convert to a commercial bank in 1997. K-REP has demonstrated the potential to expand its program and realize a sustainable credit program for micro enterprises. The transition to becoming a bank will require increasing profitability by consolidating current activities to reduce delinquency and then expanding existing credit delivery services to achieve economies of scale. This expansion, and the capital requirements of registering as a Bank, will require a significant injection of technical assistance to develop savings instruments and structures and to comply with Central Bank of Kenya regulations. When K-REP registers the Bank, K-REP will establish a Trust which will effectively own the K-REP equity and reinvest profits back into the bank, or into K-REP NGO activities. K-REP is following the model of USAID-supported BANKOSOL in Bolivia and has a working relationship with the institution to assist in the transition. In the past, K-REP offered significant technical and financial assistance to other micro enterprise lending schemes. However, with its expanded programs and plans to become a Bank, K-REP will no longer be in a position to play a key role, as it did under PED, in supporting the growth of other micro enterprise lenders, who are increasingly representing competition.

K-REP has already initiated this transition process. A key Project assumption is that K-REP is capable of completing the process with minimal direct involvement of USAID/Kenya. However, K-REP will require assistance in two key areas: technical assistance/training and capitalization. Funding for technical assistance and training will be provided to K-REP and K-REP will independently procure the necessary technical services to assist it in this conversion process. TA is likely to be needed in the following areas: chartering and compliance procedures; organizational expansion, including the expansion of the loan portfolio and establishment of savings instruments; and capital market linkages.

Although K-REP is developing plans for attracting new funds from sources as large as institutional investors and as small as depositors that have passbook savings of US$25, there will be a need for equity investment by USAID in the short term. Depending on the detailed lending projections submitted to USAID by K-REP, USAID will place funds for loan capital on an incremental basis in K-REP, either directly or through another investment mechanism.

Prior to the provision of any funds to K-REP for it to carry out the listed activities, K-REP will be required to demonstrate to USAID/Kenya that it meets the selection criteria explained under Section B below. This requirement will be incorporated in the agreement instruments as condition precedent. Thereafter, USAID/Kenya will establish performance indicators that K-REP will meet as a requirement for receiving continued support under this Project.

3.2 Grants to Selected Micro Enterprise Lending Institutions

In addition to the provision of credit to micro and small enterprises by K-REP, the Project will also provide funds through other, carefully-selected and supervised lending institutions that serve micro enterprises. The type of institution and the loan product may vary, but the likely candidates are the NGOs currently involved in fairly extensive micro enterprise lending programs in Kenya using the group-lending methodology. Experience in Kenya and other countries indicates that only a few institutions will achieve sustainability and widespread outreach. The MICRO-PED Project will focus its resources on such institutions. NGOs desiring grant assistance from USAID/Kenya to continue and/or expand their credit programs will be required to compete for funds based on strict performance criteria. Funds, which will be directly administered by USAID, will be granted for:

1. Loan funds at existing branches that meet the performance criteria. USAID may fund new branches if <u>all</u> other branches perform as indicated below.

2. Recurrent and capital expenditure associated with branch operations. This may include "headquarters" costs as appropriately allocated to the funded branches.

3. Institutional development activities such as a monitoring information system for accounting and loan tracking, monitoring and evaluation plans, financial models, strategic plans, training and staff development systems, other forms of non-recurrent technical assistance, etc.

As indicated earlier, strict performance criteria will be applied to the NGO seeking USAID assistance. It is becoming increasingly important that micro finance services be provided to the poor through specialized institutions that emphasize the attainment of financial viability. Doing so is one of the most important preconditions to achieving exponential growth. MICRO-PED will build on its successful experience, while refining its lending strategies. One such refinement will be to introduce performance criteria and channel funding to successful branch operations. In doing so, USAID will assess past performance at the branch level--including on-time repayments of at least 95%, loan portfolio at risk of less than 15%, satisfactory branch sufficiency ratio, and acceptable cost per shilling lent. In order to target those NGOs that promise financial sustainability, criteria at the institutional level will also be applied. Such criteria may include an average repayment and cost per shilling lent rate for all branches at an acceptable level, an MIS system that is functional, a system of determining clearly-defined profit centers or branches, and a clear plan for achieving high outreach and financial sustainability.

It is envisioned that channelling funds to better performing NGOs will increase the impact of USAID investment and increase incentives for better performance throughout the micro enterprise lending sector. Based on USAID experience, there is not a large pool of micro enterprise lending NGOs with financial sustainability potential in Kenya. A few that are likely to satisfy the selection criteria have participated in the PED Project. These include five potential partners from which to select.

1. **Promotion of Rural Initiatives and Development Enterprises (PRIDE) Kenya** has received direct funding from USAID and through K-REP. The program has established an expansive branch network for credit delivery to micro enterprises in Kenya, has plans for expansion and show potential for becoming financially sustainable in the long run.

2. **Kenya Women Finance Trust (KWFT)** has been a beneficiary of USAID funding through K-REP. Its credit program although small in outreach has been performing well and has potential for growth.

3. **The National Council of the Churches of Kenya (NCCK)**, a membership church organization with both social and development objectives, implements a national credit scheme with funds from USAID/K-REP and EZE (a German affiliation of protestant churches). One branch is performing very well, but others have significant issues.

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4. **Presbyterian Church of East Africa (PCEA) Chogoria Hospital** manages an Enterprise Development Project with funding from USAID/K-REP. Although PCEA Chogoria is a regional program, it has achieved impressive results and has potential to increase outreach within the hospital's catchment area.

5. **Tototo Home Industries**, based on the coast, focuses on income generation for low income people, particularly women. The credit program, funded by USAID/K-REP, has reached very poor people, but with lower repayment rates than other schemes.

All these organizations, and there are several others in Kenya that have not received USAID support, primarily use a group lending model based on the Grameen Bank and adopted to Kenya by K-REP.

3.3 Technical Assistance

While the NGOs which are expected to participate in micro enterprise credit have demonstrated considerable skill in lending to micro enterprises, it is recognized that the illustrative selection criteria will not be easy for NGOs to meet and maintain without some outside technical assistance. The Project will, therefore, provide funds for technical assistance (TA) in two ways.

The first will be providing TA funding under the grants to NGOs participating in the above component. Such funds will be used for procuring TA of their choice from their preferred source. This demand-driven approach will enhance the ability of these NGOs to build links with other sources of technical assistance which will continue beyond the Project period, an important factor in sustaining such institutions.

Second, the Project technical assistance team, which is likely to include one international and one Kenyan professional dedicated to micro enterprise credit, will assist NGOs in identifying areas in which they need assistance. In the interest of increasing performance standards throughout the market, assessment services will be made available not only to NGOs who apply for and receive grants from USAID/Kenya but to other NGOs that are active in the micro enterprise finance sector. The main activities for the TA team will be to:

1) Refine the illustrative selection criteria to incorporate up-to-date information and data.

2) Conduct assessments of lending operations and institutional development issues. Such assessments will, determine areas where NGO programs need to be improved and where technical assistance may be required, and may determine eligibility for funding under the Project. The NGOs will be involved in drawing up the terms of reference for the assessments.

3) Organize workshops and seminars on such topics as managing delinquency, increasing outreach, developing new loan products, MIS system development, mobilizing savings, etc.

4) Compile a database of technical assistance sources that NGOs can access, and

5) Strengthen a network of NGOs involved in micro enterprise lending to perform the above functions, if such a network emerges. The micro enterprise lending NGOs will take responsibility for forming and supporting the network. If the network emerges, the TA team will assist. If it performs well, the TA team will turn over its functions to the network. If not, other strategies for achieving sustainability will be developed during implementation.

Beneficiaries: Borrowers in successful lending schemes tend to be entrepreneurs located in densely population and high potential areas due to the economies of scale in such areas. Women are over-represented as borrowers and an evaluation of K-REP implied that loans were reaching firms that were growing at below average rates, i.e. poorer firms, and assisting them to reach average growth rates, in terms of employment. Thus, the program is increasing employment in needy firms. In addition, the K-REP evaluation showed that household income of entrepreneurs was increasing, as were assets and standards of living. So, the families of entrepreneurs, and probably employees, benefit as well.

4.0 EXPECTED RESULTS

(SEE ATTACHED LOGFRAME)

5.0 COORDINATION AND COLLABORATION

USAID will actively participate in the various forums involving Small Enterprise Development (SED) activities. Such involvement will ensure that other donors, GOK, non-government organizations and other initiatives are well known and understood by others. In many cases, these meetings have resulted in identifying issues and commonalities that require concerted donor actions needed in on-going or future investments. It is envisaged that the primary coordination mechanisms will include:

1. Frequent individual meetings with a sub-group of donors and others involved in specific initiatives, e.g., microenterprise policy, policy constraints affecting the small-scale sector, and association development;

2. Regularly scheduled SED meetings in which donors, Government and others exchange ideas and information on such programs; and

3. Participation in the reconstituted SSJKE Program Steering Committee, chaired by Office of the Vice President and Ministry of Planning and National Development.

II RESPONSIBILITIES OF THE PARTICIPANTS

III ILLUSTRATIVE FINANCIAL PLAN

'000s US Dollars	USAID	GOK	PRIVATE SECTOR	TOTAL
POLICY	1,950	101	29	2,080
SUB-SECTOR	4,200		1,225	5,425
FINANCE	4,500		4,000	8,500
USAID SUPPORT	900			900
EVAL & AUDIT	450			450
TOTAL	12,000	101	5,254	17,355

1/ Subject to the availability of funds to A.I.D. for this purpose, and to the mutual agreement of the parties to proceed at the time of each subsequent increment.

2/ Either party may unilaterally, with written notice to the other, adjust line items in this budget to a maximum of 15% per line item, of the last obligating agreement or amendatory obligation thereto, provided, however, that the total obligated amount as shown in the budget is not exceeded.

IV FINANCING METHODS

For the activities implemented by the GOK, USAID will make direct payments to suppliers of goods and services through contracts, purchase orders, etc., which exceed KSH 100,000 and all foreign exchange disbursements. USAID will provide funds on a

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reimbursement basis for all local currency transactions where direct payment is not possible, generally those under KSh 100,000. Reimbursement will occur on the basis of vouchers submitted to USAID.

V EVALUATION

USAID will conduct a mid-term and final evaluation of the Project. The GOK and private partners will participate in these evaluations by contributing to the development of the scopes of work, facilitating evaluators access to information, reviewing and commenting on evaluation findings and facilitating the implementation of evaluation recommendations pertinent to GOK activities.

ANNEX A

PROJECT DESIGN SUMMARY

LOGICAL FRAMEWORK

PROJECT DESIGN SUMMARY
LOGICAL FRAMEWORK

Life of Project: FY 95 - FY 00
Total U.S. Funding $12 million
Date Prepared March 8, 1995

Project Title and Number: MICRO PRIVATE ENTERPRISE DEVELOPMENT (MICRO-PED)
615-0263

NARRATIVE SUMMARY	OBJECTIVE INDICATORS	MEANS OF VERIFICATION	IMPORTANT ASSUMPTIONS
Program or Sector Goal: To increase private enterprise employment	Measures of Goal Achievement: Increase 5-year trend annual private enterprise employment growth rate from 12% to 17% (Percent women: 38%)	Means of Verification: USAID & GOK Surveys	Assumptions for Achieving Goal: GOK continues structural adjustment and economic liberalization.
Project Purpose: To increase micro enterprise employment	End of Project Status: Increase 5-year trend annual micro enterprise employment growth rate from 13% to 18% (40% women)	Means of Verification: USAID & GOK Surveys	Assumptions for Achieving Purpose: Continued GOK policy of support to the informal sector.

Outputs:	Magnitude of Outputs:	-Means of Verification	Assumptions for Achieving Outputs:
1. Improve the policy and regulatory environment affecting micro enterprises	1. Changes in policy and regulations targeted in a micro-enterprise policy matrix	3. Policy Matrix; Special studies; Evaluations.	The GOK is responsive to initiatives for policy change; participates fully in the Policy Forum; enables legal assistance work to continue in Kenya.
2. Increase employment in targeted sub-sectors through expansion of cost-effective business services	2a. Average annual increase in employment in targeted sub-sectors: -AGRIBUSINESS: 210,000; 41% women -METALS: 24,000; 1% women	2a. USAID & GOK Special Studies	The GOK is responsive to sector level policy change.
	2b. Increased cost effectiveness of non-financial service delivery (cost/job created or cost/firm assisted comparable to financial programs; a percent reduction in cost/job created or cost/firm assisted)	2b. Implementing Organizations' reports on cost of service & amount charged for services; Occasional firm surveys showing use & impact of services; Evaluations.	Assisted institutions receive sufficient funds from other sources so that they remain strong enough to carry out MICRO-PED activities without significant institutional support.
	2c. Increased cost-recovery of value-added, non-financial service provision to 50% on average	2c/d. Implementing Organizations' reports on number of beneficiaries; USAID & GOK special Studies.	
	2d. Number/Percent of firms using non-financial services in targeted sectors.		
	2e. Demonstrable improvement in institutional strength of service deliverers.	2e. Implementing Organization Reports using an Institutional development matrix; Evaluations.	
3. Increase sustainable delivery of financial services	3a. 40,000 micro entrepreneurs will have received credit (60% women);	3a/b Financial Institutions' reports. Evaluations.	Central Bank registers and regulates micro enterprise lenders;
	3b. 2 micro enterprise finance institutions achieve full financial sustainability and develop the ability to raise funds through savings or commercial Bank loans; 2 other micro enterprise institutions achieve break-even status, covering the cost of operations.		Banks avail savings facilities and lending facilities to NGO lenders.
	3c. Demonstrable improvement in the institutional strength of participating financial institutions.	3c. Financial Institutions' reports using an institutional development matrix; Evaluations.	

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Inputs:	Implementation Target:	Means of Verification:	Assumptions for Achieving Inputs:
Overall: $12 Million USAID funds	Overall: See implementation schedule	Financial and Administrative Reports	USAID/Kenya Operational Year Budget remains stable or increases
1. Policy Component:	1)		
a) Technical Assistance and funds for operating and conducting research for the Policy Forum, and support to the GOK.	a) $1.25 million for TA, operations and research, and GOK support.		Availability of relevant implementing institutions; GOK commitment.
b) TA and training for associations	b) $0.20 for TA training		
c) Services and activities for strategy support.	c) $0.50spend on strategy support activities		
2. Sub-sector Component			
a) Technical Assistance to facilitate sub-sector development, strengthen institutions and programs and issue grants/contracts	a) $1.70 million for TA		Implementing Organizations have sufficient operational funds.
b) Grants/contracts for sub-sector development activities.	b) $2.5 Million in Grants and Contracts		
3. Finance Component	a) $3 Million in grants, with a $3 Million match		
a) Grants to NGO lenders & KREP	b) $1.50 million for TA		Sufficient NGO lenders meet and maintain performance criteria.
b) Technical Assistance			

NOTES ON INDICATORS:

1. **Private Enterprise and Micro Enterprise Employment Growth Rates:** USAID/Kenya projected employment to the year 2000 based on USAID's Baseline Survey of Micro and Small Enterprises (GEMINI), and World Bank and GOK estimates of growth in employment in small scale agriculture, the public sector, and private sector firms with more than 10 employees (see Background Analysis - Annex E). These estimates project a 12% average annual growth rate for private enterprise employment and a 13% average annual growth rate for micro enterprises, between 1993 and the year 2000. With the policy reform, sub-sector development and financial assistance provided under MICRO-PED, USAID hopes to increase the trend growth rate in micro enterprise employment to 18%, which would result in an average annual private enterprise employment growth rate of 17%, all other projections remaining the same. Eighteen percent is considered optimistic but realistic, given the extraordinary increase in micro enterprise employment by 20% in 1992 and 24% in 1993. The last two years are believed to be high levels that would naturally swing back. To get an 18% average annual rate, these high growth rates would need to be maintained, which would require a significant change in the operating environment, MICRO-PED will contribute to this changing environment.

In 1993, women represented 40% of micro enterprise employment and 23% of other private enterprise employment. Because of the projected shift towards more employment in micro enterprises, USAID/Kenya also projects that the portion of women in private enterprise employment as a whole will increase from 35% to 38%.

2. **Sub-sector Employment Growth Rates:** The National Baseline Survey of Small and Micro Enterprises (GEMINI) estimated the employment breakdown in different sub-sectors, and the distribution of new employment generated in different sectors. The agricultural sector provided 45% of micro enterprise employment in 1993, and 41% of all new jobs generated that year came from agri-businesses. The metals sector provided only 1% of employment in 1993, but generated 4% of new jobs in micro enterprises. Based on these proportions, USAID/Kenya estimated the amount of employment, that would be provided by these two sectors, if our targets will be met. The agribusiness sector should generate some 250,000 new jobs annually from 1993 to the year 2000. The metals sector, a much smaller sector, should add around 24,000 jobs per year. Women comprise 41% of employees in agri-businesses and 1% of employees in the metals sector. These ratios are expected to stay the same. MICRO-PED will contribute significantly to this employment change.

3. **Improving the Policy Environment: Policy Matrix:** USAID/Kenya has developed an effective qualitative policy matrix for the Kenya Export Development Support Project. To date, USAID/Kenya has not felt comfortable with quantitative indices for measuring policy

because they subjectively transform qualitative data into quantitative data. Rather, in addition to the use of a detailed qualitative matrix, USAID/Kenya has selected indicators that can be quantified (for example the percent of the budget spend on infrastructure) to represent some categories of policy change for specific purposes, like the Annual Program Impact report. The Policy Forum team will develop the specific measurement tool in year 1. The tool will reflect specific policy objectives, but may evolve as some objectives are reaches and other identified throughout the Life of Project.

4. **Increasing the cost-effectiveness of non-financial services:** This indicator will be developed more fully during project implementation when grant agreements and contracts are signed. Some interventions will be one-time, "leveraged" interventions such as association development, or the development of technology or training curricula. These funds are not expected to be recovered, but are expected to have very low cost/benefit ratios. Other interventions, however, will be for providing value-added services. These may have higher cost/benefit ratios, but in the long run, the aim is to develop financially sustainable service delivery. However, given the state of the art in delivery of non-financial services, the target for MICRO-PED is that firms pay 50% of the cost of value-added services during the life of project.

5. **Institutional Development:** In order to focus on and monitor institutional development, project implementors under the Finance and Sub-sector Development components will develop a qualitative Institution Development Matrix for assessing needs, setting targets, and monitoring progress. It will include such things as: Strategy, structure, operations, financial systems and sustainability, personnel policies, management information and impact monitoring systems, and leadership.

6. **Number of Borrowers:** With a USAID investment of $4 Million, matched by an NGO investment of $4 million, there will be some $8 Million available for additional lending activities. An average loan size of $400 is typical if there are a substantial number of second borrowers. This is roughly double the number of borrowers that received finance under the Private Enterprise Development Project. The project will also track the current number of borrowers, a figure that will be established when grants are agreed.

7. **Sustainability:** Financial sustainability of micro enterprise lenders will be measured by the ability of organizations to cover their operational and capital costs. It is expected that two financial institutions will progress to achieving full financial sustainability (covering implicit capital costs) and in addition will access funds through the private sector in the form of savings mobilization and commercial bank loans. This will significantly expand outreach as well. Two other financial institutions are

expected to break even (cover operational costs) during the period. One institution, K-REP, is approaching break-even and has plan for becoming a bank by mobilizing and lending savings. Another, PRIDE, is performing well and rapidly expanding outreach such that is has strong potential to do the same. Kenya Women's Finance Trust has the appropriate institutional setting and is performing well, but outreach is low so it would be a reasonable target to hope for break-even in this case. The other three potential participants are less likely to reach break-even, but with technical assistance and performance incentives, at least one should gain momentum.

ANNEX 1
ATTACHMENT I
PROJECT NO . 615-0263

'SUMMARY OF PROJECT COSTS BY EXPENSE CATEGORY AND SOURCE OF FUNDING
'(in 000 ' US Dollars.)

EXPENSE CATEGORY 1 /	Prior Obligation AID $	GOK (Equiv)	PRIV SEC (Equiv)	This Obligation AID $	GOK (Equiv)	PRIV SEC (Equiv)	Cumulative Budget AID $	GOK (Equiv)	PRIV SEC (Equiv)	Planned Life of Project funding. AID $	GOK (Equiv)	PRIV SEC (Equiv)
Policy Component	0	0	0	195	101	29	195	101	29	1950	101	29
Sub-sector Component	0	0	0	600		175	600	0	175	4200	0	1225
Finance component	0	0	0	1525	0	1355	1525	0	1355	4500	0	4000
USAID Support	0	0	0	180	0	0	180	0	0	900	0	0
Evaluation & Audits	0	0	0	0	0	0	0	0	0	450	0	0
TOTAL	0	0	0	2500	101	1559	2500	101	1559	12000	101	5254

1 / Subject to the availability of funds to USAID for this purpose , and to the mutual agreement of the parties to proceed at the time of each subsequent increment.