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Contractor Name:	Chemonics International, Inc.
USAID Cognizant Technical Office:	Office of Economic Opportunities, USAID/Jordan
Date of Report:	April 29, 2005
Document Title:	**Expanded Access to SME Finance: Establishing a USAID Development Credit Authority (DCA) Loan Portfolio Guarantee** Final Report
Author's Name:	Ms. Caroline Averch
Activity Title and Number:	Achievement of Market-Friendly Initiatives and Results Program (AMIR 2.0 Program) F/Preparation of Concept Papers, FMD Component, Work Plan No. 636.08

Expanded Access to SME Finance: Establishing a USAID Development Credit Authority (DCA) Loan Portfolio Guarantee

Final Report

April 29, 2005

Data Page

Name of Component: Financial Markets Development (FMD)

Authors: Ms. Caroline Averch

Practice Area: Financial Sector Services

Service Offering: SME Finance

List of Key Words Contained in Report:

- Access to Credit
- Small and Medium-Sized Enterprises (SMEs)
- Commercial Bank
- Receivables Financing
- Working Capital
- Term Loans
- Loan Tenor
- Excess Liquidity
- Loan Guarantee
- Banking Sector
- Development Credit Authority (DCA)
- Loan Portfolio Guarantee (LPG)
- DCA Action Package
- Guarantee Facility

Abstract

The Report presents the activities, outputs, and results of a consultancy to support USAID/Jordan in developing its inaugural Development Credit Authority (DCA) activity – a Loan Portfolio Guarantee (LPG) facility to stimulate greater access to credit by Small and Medium-Sized Enterprises (SMEs) in Jordan. The LPG, in combination with technical assistance and capacity building programs for both potential SME borrowers and bank Credit Officers, will catalyze the extension of credit at appropriate terms and competitive pricing for currently underserved SMEs to expand and upgrade their businesses.

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EXECUTIVE SUMMARY

Substantial excess liquidity in the financial sector, stable inflation and exchange rates, relatively strong local and international financial institutions, and a burgeoning capital market all contribute to making Jordan an optimal country for private sector financing of development projects. Nonetheless, SME lending remains short-term and not broadly accessible due to risk perceptions of financial institutions, information asymmetry, and limited term money in the financial system.

The proposed DCA Loan Portfolio Guarantee facility which was the focus of this consultancy will support increased SME access to medium and long term financing for the purchase of equipment and technology, as well as working capital. The DCA facility will provide the bank with a partial guarantee on multiple loans made to SMEs in all sectors and in all geographic areas of Jordan. Through more accessible working capital, targeted capital investment, and business development assistance, SMEs will increase their contribution to national economic growth by expanding their production, improving their efficiency, and hiring more employees.

USAID/Jordan's main objectives with this activity are to increase SME access to finance, thereby increasing incomes, creating employment and stimulating economic growth. Loans under the facility are not proposed for certain sectors, instead remain broadly defined to include activities that stimulate economic prosperity. Based on discussions with the Bank of Jordan, the activity intends to mobilize \$10 - \$15 million to Jordanian SMEs through market rate loans over the period of the guarantee.

USAID's most successful DCA activities have been those that are mutually reinforcing with ongoing technical assistance and policy reform initiatives. This DCA activity to increase access to credit for Jordanian SMEs has direct synergies and will coordinate closely with a number of USAID and other donor funded SME and Banker capacity building programs.

The guarantee will provide a demonstration effect that lending to SMEs is profitable, both to Bank of Jordan and the wider banking industry. The complementary support provided by the USAID and other training and technical assistance programs will mutually reinforce the guarantee facility to catalyze lending to Jordanian SMEs. As the guarantee facility is utilized and loans are placed, SME credit histories will be established, and it is expected that SME borrowers able to access credit without a guarantee either through Bank of Jordan or another lender. As DCA has seen in other countries, once other banks take notice of BOJ's successful penetration of the SME market it is anticipated that it will spur competition leading to more affordable credit for SMEs. Concurrently some portion of the excess liquidity in the financial sector will be absorbed and put to productive use.

Background

Genesis of the Activity

The Financial Markets Development (FMD) Initiative under AMIR 2.0 strives to strengthen Jordan's financial markets by leveraging unused capital for developing and modernizing financial institutions. This includes the development of new financial products that would facilitate the extension of credit by banks to SMEs.

USAID's Office of Development Credit (ODC) delivered a workshop on the Development Credit Authority in February 2005 for USAID/Jordan and participants from other USAID Missions around the world. Continuing the momentum from the workshop, USAID and the AMIR Program met with several banks to explore opportunities for utilizing DCA to stimulate SME financing. This consultancy focused on a smaller subset of that initial group of banks.

USAID/Jordan and the AMIR Program discussed with the banks the possibility of using a DCA guarantee to offer partial risk coverage for banks lending to SMEs that are involved in export related activities either directly or as suppliers to larger export related entities, and other SMEs with limited access to finance. USAID/Jordan and the AMIR Program had met several banks potentially interested in lending to SMEs in a manner that is new to Jordan. As the lack of extension of credit to SMEs by banks is a serious impediment to the development of the SME sector in Jordan, the additionality coming from a DCA Guarantee could have a significant positive development impact.

USAID's Development Credit Authority

USAID's Development Credit Authority (DCA) is a tool to leverage limited donor funds and build local private sector financial institutions in developing countries. DCA catalyzes domestic investment by offering loan guarantees that foster access to credit and longer term sustainable funding sources for financially viable development projects. In countries constrained by a lack of appropriate financial products, services, and markets, USAID's DCA is a key to unlock local credit markets, and limited donor funds are augmented by the unlimited potential of the private sector. DCA is the legal authority that allows USAID missions to issue partial loan guarantees to private lenders. In turn, these guarantees provide a way to encourage local capital funding of projects. DCA allows USAID to provide the most appropriate mixture of grant and credit assistance to achieve a particular development goal. By offering a guarantee on up to 50 percent of a lender's risk on loans made to single or multiple borrowers, the DCA encourages private lenders to extend financial services to credit-worthy but underserved markets. It also encourages those lenders to offer longer loan terms; reduce collateral requirements; lend at market-based interest rates; and, invest on a sustainable basis in local development efforts in lieu of or in addition to USAID and other donors. The DCA mechanism requires true private sector risk sharing with the lenders providing loans using their own capital. USAID also receives tremendous budget leverage with the actual cost to missions averaging 5 to 10 cents for every dollar loaned by a private bank. DCA is an extremely flexible mechanism and includes four different tools to enhance credit in a broad variety of situations and environments. These tools include loan guarantees, portable guarantees, loan portfolio guarantees, and bond guarantees.

Objective

The challenge of this consultancy was to meet with two to four banks that have expressed a serious interest in using the proposed DCA facility and work with them in designing a DCA portfolio guarantee program that would extend credit to SMEs. The consultancy assisted banks, the AMIR Program and USAID/Jordan in advancing the various inputs required for a DCA credit enhancement for the planned portfolio guarantee program.

Specific Tasks Undertaken

Background Reading

During this consultancy the consultant reviewed a number of relevant background documents in preparation for interviews with the banks and to understand the potential linkages between ongoing USAID and other technical assistance efforts. These documents included but were not limited to:

-Annual Reports

- Standard Chartered Bank
- Export and Finance Bank
- Bank of Jordan
- Cairo Amman Bank

-Available Credit Rating Agency and Investment Bank Reports

- Standard Chartered Bank
- Export and Finance Bank
- Bank of Jordan
- Cairo Amman Bank

-Information on the National Linkage Program.

-Chemonics International Inc., SME Access to Capital in Jordan Final Report, August 2004.

Interviews and Meetings

Meetings were conducted with relevant stakeholders and parties which would be involved either directly or indirectly in any DCA guarantee facility for SME lending. This included USAID, USAID-funded and EU-funded technical assistance programs, and potential commercial bank partners. As a Loan Portfolio Guarantee structure was used, whereby an identified lender has guarantee coverage for a pool of multiple unknown borrowers, only secondary source information was required for the potential SME borrowers, as presented in Appendix ID. Borrower Report for ODC Risk Assessment.

Meetings and coordination with USAID/Jordan and the AMIR Program's FMD and ECI Components dealt with the development objectives involved with using the DCA guarantee to enhance credit extension to SMEs, and possibilities for coordination with technical assistance programs. Meetings with the banks focused on learning more about their plans and capacity for moving into SME lending, their market segmentation, level of commitment, and other factors that would support the rationale for including them as a DCA partner bank. Multiple meetings with Bank of Jordan, the principal focus of this consultancy, covered the specific details of the process for establishing a DCA guarantee, requirements for partner banks, intended use of the guarantee, size of the expected portfolio guarantee, loan sizes and tenors, duration of the facility, claims procedures, and next steps. A detailed schedule of meetings is attached as Appendix IVC, and participants included:

- USAID/Jordan
- USAID/Office of Development Credit
- AMIR Program – FMD and ECI Components
- Bank of Jordan
- Standard Chartered Bank
- Export and Finance Bank
- National Linkages Program (SME Capacity Building)
- FOR-Jordan (SME and Banker Training)
- JUSBP (Business Development Service Center)
- EJADA (EU-funded SME and Banker TA)

The consultant and the AMIR FMD component leader coordinated with Jim Barnhart, Director of USAID/Jordan Economic Opportunities Office, to confirm with the US Treasury Financial Crimes Enforcement Network (FinCEN) that Bank of Jordan did not have any blemishes on its record related to money laundering or terrorism financing. The team then advocated for the incorporation of this information and the documentation of this due diligence step of into the final complete action package for the risk assessment team's review. USAID/Jordan is investing considerable effort and funds into anti-money laundering and terrorism financing prevention initiatives, and this is one way to demonstrate their concern and interest in the topic in a practical and meaningful way.

Outputs Produced

<u>USAID/Jordan</u>

- Powerpoint Presentation – *Stimulating Expanded SME Access to Finance in Jordan: Establishing a Development Credit Authority Loan Portfolio Guarantee*. Delivered at USAID/Jordan on April 28, 2005
- Draft of DCA Action Package for Bank of Jordan Loan Portfolio Guarantee
- Draft of DCA Monitoring Plan
- Borrower Report for ODC Risk Assessment
- Compilation of Financial Institution Information Required for Risk Assessment
- Detailed Schedule of Activities to Finalize DCA LPG with Bank of Jordan

Bank of Jordan
- Illustrative Term Sheet
- Sample Letter of Intent
- Comparison of DCA vs. EJADA Loan Guarantee Programs
- Summary of Key Information for Senior Management Committee Meeting

Standard Chartered
- Sample Letter of Intent
- Process and Notional Schedule for Future Participation in DCA for SME Lending
- Illustrative Term Sheet

AMIR
- Powerpoint Presentation – *USAID's Development Credit Authority: Overview and Applications for Jordan*. Delivered at AMIR for internal staff and JUSBP on April 25, 2005

Results Achieved

USAID/Jordan's inaugural $10-15 million DCA Loan Portfolio Guarantee facility is moving forward at a rapid pace, with all parties aiming to continue momentum to present the entire deal to the Credit Review Board on Thursday, June 2.

USAID/Jordan also remains interested in pursuing the development of a second and possibly third Loan Portfolio Guarantee for SME lending with Standard Chartered and Export & Finance Bank at the time their SME strategies are at a more advanced state of development.

Planned Follow-On Activities

A Scope of Work has been developed for the period 5 May to 5 June 2005 for follow on activities to continue AMIR support to USAID/Jordan on the Bank of Jordan SME LPG. Tasks covered in this SOW include but are not limited to: producing and facilitating follow up communications with the bank and USAID; responding to any USAID/ODC questions during the risk assessment process; and assisting in the preparation of the Mission for the presentation of the deal to the Credit Review Board.

There is a strong likelihood that Standard Chartered will have its SME lending strategy ready in mid-August or early September 2005 and be able to enter into more specific discussions on how the bank may want to avail itself of a DCA LPG. Additionally, AMIR will continue to dialogue with Export & Finance bank on this subject, expecting that their SME strategy will be finished by the end of calendar year 2005. SOWs for support to continuing these discussions and/or developing additional DCA LPG Action Packages will be developed at a later date as appropriate.

List of Appendices

Appendix I – USAID Documents

IA. Powerpoint Presentation – *Stimulating Expanded SME Access to Finance in Jordan: Establishing a Development Credit Authority Loan Portfolio Guarantee*. Delivered at USAID/Jordan on April 28, 2005

IB. Draft of DCA Action Package for Bank of Jordan Loan Portfolio Guarantee

IC. Draft of DCA Monitoring Plan

ID. Borrower Report for ODC Risk Assessment

IE. List of Financial Institution Information Required for Risk Assessment

IF. Detailed Schedule of Activities to Finalize DCA LPG with Bank of Jordan

Appendix II - Bank of Jordan Documents

IIA. Illustrative Term Sheet

IIB. Sample Letter of Intent

IIC. Comparison of DCA vs. EJADA Loan Guarantee Programs

IID. Summary of Key Information for Senior Management Committee Meeting

Appendix III - Standard Chartered Documents

IIIA. Sample Letter of Intent

IIIB. Process and Notional Schedule for Future Participation in DCA for SME Lending

IIIC. Illustrative Term Sheet

Appendix IV - AMIR Documents

IVA. SOW Activity Name: 636.08 Development Credit Authority (DCA)
SOW Title: F/Preparation of Concept Papers

IVB. Powerpoint Presentation – *USAID's Development Credit Authority: Overview and Applications for Jordan*. Delivered at AMIR for internal staff and JUSBP on April 25, 2005

IVC. Schedule of Meetings for Carrie Averch – 18 April – 28 April 2005

IVD. SOW Activity Name: 636.08 Development Credit Authority (DCA)
SOW Title: F/Credit Review Board Meeting Preparation

CHEMONICS INTERNATIONAL INC.

Electronic Document Submission Title Page

Contract No.:	278-C-00-02-00210-00
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USAID Cognizant Technical Office:	Office of Economic Opportunities USAID Jordan
Date of Product/Report:	April 29, 2005
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Author's Name:	Ms. Caroline Averch
Activity Title and Number:	Achievement of Market-Friendly Initiatives and Results Program (AMIR Program) F/Preparation of Concept Papers, FMD Component, Work Plan No. 636.08
Name and Version of Application Software Used to Create the File:	MS Word 2002 MS PowerPoint MS Excel
Format of Graphic and/or Image File:	N/A
Other Information:	N/A

Stimulating Expanded SME Access to Finance in Jordan

Establishing a Development Credit Authority Loan Portfolio Guarantee

April 28, 2005

Jordanian SMEs
The Credit Challenge

- Information asymmetry – no reliable comprehensive credit reference information system.
- SMEs have opaque financial statements, poor business plans, and limited traditional collateral/security to pledge.
- Very limited medium- and long-term funds in financial system so difficult for banks to lend for SME capital investment.
- Commercial banks are conservative and have focused on large corporates and easy T-bill returns.
- Limited capacity to properly analyze SME borrowers; evaluate, mitigate, and appropriately price risk.
- Legal environment not conducive to Receivables-based financing.

DCA Activities in Jordan

- February 2005: USAID DCA Workshop
- February – April 2005: USAID and AMIR meet with several banks to explore DCA opportunities for SME finance
- April 2005: Narrowed field to Bank of Jordan, Standard Chartered, and Export & Finance Bank
  - Bank of Jordan – current proposed DCA facility
  - Standard Chartered - 2-3 months until SME strategy ready
  - Export & Finance Bank - 4 months until SME strategy ready

DCA Activity Description

Bank of Jordan

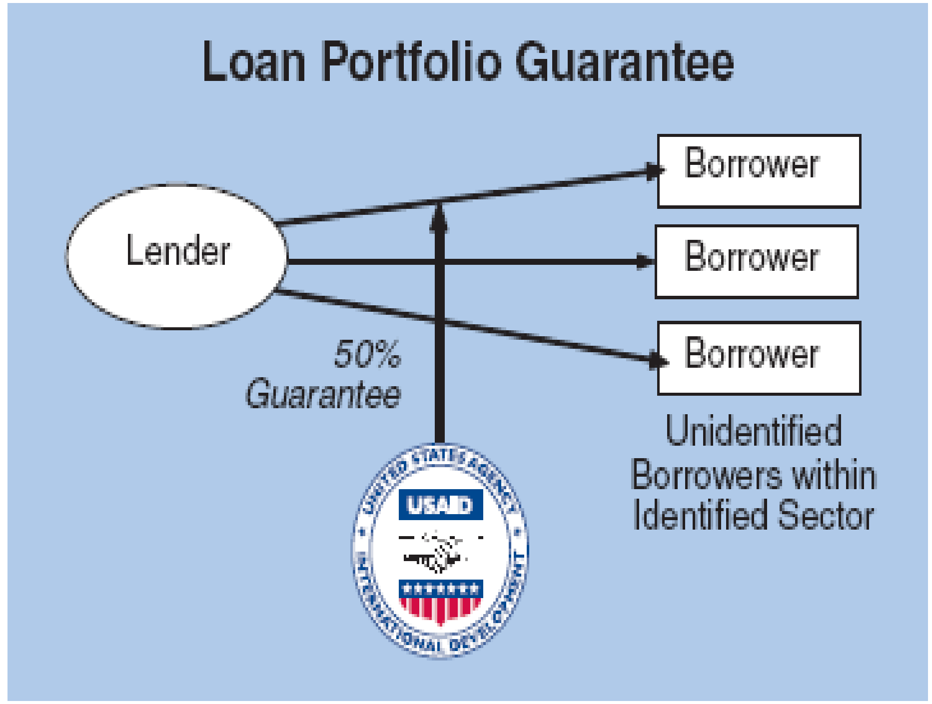
Type: Loan Portfolio Guarantee (LPG)

Facility Amount: $10 - $15 million (Jordanian Dinar equivalent)

Purpose: Provides the bank with a partial guarantee on multiple loans made to SMEs in all sectors in all geographic areas. SME loans will be for asset purchase, capital investment, and working capital.

Supports: SO 5 – Increased Economic Opportunity for Jordanians

Subsidy Cost: Est. $400,000 - $500,000



Bank of Jordan
An Ideal DCA Partner Bank

- Local Jordanian-owned bank
- SME lending is part of their long-term business strategy
- Wide branch network for outreach to SMEs across Jordan
- Not engaged in speculative activities
- Demonstrated Senior Management commitment:
  - Embedded EU-funded SME Advisor
  - Active participation in FOR-Jordan SME Credit Analysis training and requested in-house training
  - Recent DCA LPG for SME lending with USAID/WBG

Technical Assistance

USAID's most successful DCA activities are mutually reinforcing with ongoing technical assistance and policy reform initiatives.

Bank of Jordan's DCA LPG for SME lending will have direct synergies and coordination with these and other programs:

- AMIR's FMD and ECI Components
- National Linkages Program (SME Capacity Building)
- FOR-Jordan (SME and Banker Training)
- JUSBP (Business Development Service Center)
- EJADA (EU-funded SME and Banker TA)

Economic Justification

- **Correcting Credit Market Imperfections**
  - Limited SME access to appropriate and affordable financing options
  - LPG encourages analysis of new SME clients and learning
  - LPG will effectively reduce borrower collateral requirements
  - Loans at market rates to not distort existing financial markets
- **Additionality**
  - Banks need incentives + capacity building to lend to SMEs
  - LPG will not displace other private financing to this sector
  - No overlap with other donor and GOJ guarantee schemes
  - Close synergies with other USAID programs

Demonstration Effect

Demonstration Effect: Lending to SMEs is profitable.

A vision for measuring success:

- Guarantee facilities are utilized.
- SME credit history established.
- SME borrowers able to access credit without a guarantee.
- Competition and diversity leads to more affordable credit.
- Excess liquidity in the financial sector absorbed.

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Bank of Jordan DCA LPG Schedule & Next Steps

On schedule for June 2 Credit Review Board (CRB) Meeting

Next Steps – USAID

- April 28 – Submit Congressional Notification
- May 4 – Submit Action Package and Monitoring Plan to ODC
- May 10 – Negotiate legal agreement (ODC in consultation with Jerry + RLA)
- June 2 – Present the Action Package to the CRB
- June 15 – Prepare Certification and Legal Opinion (ODC in consultation with Jerry + RLA)
- July 1 – Sign Legal Agreement

Bank of Jordan DCA LPG Schedule & Next Steps

On schedule for June 2 Credit Review Board (CRB) Meeting

Next Steps – AMIR

- April 28 – Provide USAID with Draft Action Package
- May 3 – Refine facility ceiling / structure per outcome of BOJ committee meeting and Mission decision
- May 4 – Submit All Documents for Risk Assessment to ODC
- May – Liaise and facilitate as required with BOJ, respond to ODC questions, and help prepare presentation for CRB
- June 2 – Support Mission on presentation of the Action Package to the CRB

DCA LPG Monitoring

Options for non-ODC monitoring responsibilities

- In house: Mission assumes all monitoring responsibilities
- Project-based: AMIR assists USAID/Jordan and USAID/ODC with monitoring the guarantee facility
- Local firm: Some Missions contract out DCA monitoring functions to a small local firm.

Key Monitoring Activities

- Compliance
- Fee payments
- Semi-annual reporting
- Database on usage to monitor development indicators
- Processing claims payments

Other Potential DCA Partner Banks Standard Chartered

- Ongoing Dialogue with CEO indicates keen interest in SME LPG
- SME Strategy expected in mid-August 05 – not ready for this DCA Action Package but AMIR will continue support
- Interested in exploring DCA coverage for QIZ lending per Royal Court letter to Bankers Association
- Good corporate citizen and Innovator in Jordan:
  - Credit Card Introduction and public education
  - Credit Bureau Law advocacy
  - Credit Bureau conference and involvement of Central Bank

Standard Chartered is a USAID/DCA Partner Bank in:

- Uganda:
  -$4 million facility for SME lending fully utilized;
  -$6 million for *rural* SMEs;
  -$8 million for Warehouse Receipts lending.
- Zambia - $2 million facility for Warehouse Receipts lending.
- Ghana - $10 million facility established for SME lending.

Other Potential DCA Partner Banks SME Lending

- Export & Finance Bank
- Cairo-Amman Bank
- Housing Bank for Finance & Trade

Other DCA Applications for Jordan

SO 2: Enhanced Integrated Water Resources Management

- **Water:** (all DCA structures)
  - Wastewater treatment
  - Potable water and sewerage infrastructure
  - Irrigation
  - **Extra subsidy cost available to Mission specific to water
- **Municipal Finance:** (all DCA structures)
  - Water
  - Energy
  - Housing
  - Public works

SO 3: Improved Social Sector Development and Governance

- **Housing:** (all DCA structures)
  - Mortgage lending
  - Secondary markets
- **Education:** (LPG)
  - Student loans
  - Private schools
- **Health:** (LPG, LG)
  - Lending and equipment leasing for clinics
  - Hospitals
  - Midwives

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Other DCA Applications for Jordan

SO 5: Increased Economic Opportunity for Jordanians

- **Private Sector Development:** (LPG, LG)
  - Finance for competitive sectors, Pharmaceutical, Garment, Tourism
  - Business Associations Sustainability
- **Capital Markets**: (BG)
  - Corporate bond issues
  - Municipal bonds
  - Securities
  - Certificates of Deposit to increase longer term funds

All Mission SOs:

DCA could be a tool integrated into USAID/Jordan's program portfolio.

DCA Handouts

- Detailed DCA LPG Activity Schedule
- Sample Term Sheet
- Draft Action Package
- Draft Monitoring Plan

June 12, 2005

ACTION MEMORANDUM

TO: Lisa Fiely, Chief Financial Officer

FROM: David Ostermeyer, Chairman of the Credit Review Board

SUBJECT: CRB Recommendation for Approval of a Development Credit Authority Activity in Jordan

As described in the attached documents, USAID/Jordan intends to sign a loan guarantee agreement with the Bank of Jordan in Jordan in support of the Mission's SO Number 5 – Increased Economic Opportunity for Jordanians. To successfully implement this agreement, EGAT/DC and USAID/Jordan have designed a Monitoring Plan and agree to adhere to the responsibilities as outlined in that document. The Credit Review Board has reviewed this transaction and found that the risk has been appropriately assessed and that there is reasonable assurance of repayment of the obligations covered by these guarantees. Furthermore, the CRB has approved the subsidy cost to be associated with this activity and believes the Office of Development Credit has adequately provisioned for the risk entailed in this prospective agreement.

RECOMMENDATION

That the CFO sign below and thereby approve the findings of the Credit Review Board and the recommendation of the Chairman of the Credit Review Board with regard to this activity.

Approval:

_____________ ______
Lisa Fiely Date
CFO

Mission Approval:

________________ _____
Anne Aarnes Date
Mission Director

Attachments:

I. Project Information Sheet
II. Activity Description
III. Economic Justification
IV. Risk Assessment
V. Subsidy Cost Calculation
VI. Financial Statements & Additional Information
CC: CRB Members, RLA

Attachment VI: Financial Statements & Additional Information
U.S. Agency for International Development
SME Lending in Jordan (BOJ)

Project Identifier:	SME Lending in Jordan (BOJ)

Country	Jordan	**Mission/Bureau**	Jordan
Mission/Bureau Program Officer	Jerry Florkowski	**Investment Officer**	TBD
ODC Regional Officer	Alison Eskesen		
	Recommend Approval:	**Chief Risk Officer**	Kathleen Wu

Type	Loan Portfolio Guarantee	**Guarantee Number**	TBD
Lender(s) /Guaranteed Party (incl. contact information)	Bank Of Jordan, Jordan Head Office - P.O. Box 2140 Amman 11181 Jordan Tel: +962-6-569-6122		

Borrower(s)	Small and Medium Enterprises (SMEs) established and operating in Jordan.

Mission SO(s) Supported by Activity

SO Number 5 – Increased Economic Opportunity for Jordanians

The US Government's Economic Development Goal in Jordan is Broad-based, market-oriented growth accompanied by expanding investment, improving standards of living and enhanced economic opportunities for all Jordanians. USAID/Jordan's SO Number 5: Increased Opportunity for Jordanians supports three intermediate results:

1. Increased access to business services;
2. More effective identification and implementation of policy reforms; and
3. An improved environment for sustained policy reform.

Sector

SME Development – Private Enterprise

Activity Description *(one paragraph)*

This DCA loan portfolio guarantee (LPG) will facilitate access to working capital and longer term capital expenditure financing for small and medium enterprises (SME) which are currently underserved by the financial sector. The guarantee will complement technical assistance initiatives being undertaken by USAID to strengthen SMEs and the banking industry. Qualifying borrowers will include financially viable SMEs, defined as having 5 to 250 employees, operating in any sector of the economy, including those that are exporting or provide inputs to exporters.

Performance Indicators *(Please provide a list of key measures of the benefits and performance of this activity)*

1. Utilization of total authorized amount;
2. Number of new loans disbursed by the lender; and
3. Number of SMEs receiving loans.

Attachment VI: Financial Statements & Additional Information
U.S. Agency for International Development
SME Lending in Jordan (BOJ)

Target timeframe for obligation	June 2005
Subsidy funding source *(expiration date, type, source)*	FY 2005 ESF – expires September 2005

Max. Cum. Disbursements ($)	10,000,000	**Guarantee currency**	Jordanian Dinar, US Dollar, Euro
Term *(years)*	8	**Type of Risk sharing**	Pari passu
Interest Rate (%)	8-12% will vary by currency	**Guarantee percentage**	50%
Revolving?		**Guarantee ceiling** ($)	5,000,000
Initial Disbursement *(year)*		**Payment guaranteed**	Principal Only

Notes on transaction terms & claim requirements	

Commitment Fee ($)	1.25% or $62,500 – Non-reimbursable				
Utilization Fee (%) **p.a.**	1.00%	**Util. fee payment Basis**	Semi-annual	**NPV** ($)	

For Loan Portfolio Guarantees (LPGs)		**For Bond Guarantees**	
Est. number of sub loans	50	**Type**	
Est. avg., sub-loan maturity (years)	2	**Coupon** (%)	
Est. avg. size of sub-loans ($)	200,000	**Trustee**	
Max. auth. Portfolio Amount ($)	10,000,000	**Investors**	
Final year of loan disbursement	Year 7	**Secondary Investors**	

Subsidy Cost	$	%	**Net Defaults**	%	**Fees**	%	**Single effective rate**	.%

Risk Score		**Expected cum. Default rate**	%
Country	# (%)	**Borrower**	# (%)
Lender	# (%)	**Transaction**	# (%)

Key Risk Factors: *Brief list of key factors (e.g., nature of the lending activity, specific management concerns, sectoral concerns, etc.)*

- Performance of Bank of Jordan originating quality portfolio
- Recoveries on non-performing assets
- Limited capacity of SMEs in Jordan

Special conditions for approval:

Attachment VI: Financial Statements & Additional Information
U.S. Agency for International Development
SME Lending in Jordan (BOJ)

Background

The Hashemite Kingdom of Jordan is a democratic monarchy that faces the critical challenge of spurring economic growth and generating employment. According to Emerging Jordan 2004, "unemployment and poverty remain two of Jordan's most intractable problems." The Government of Jordan (GOJ) states the unemployment rate in 2003 at 16% of the labor force. However other estimates, which include underemployment and employment in the informal sector, place the unemployment rate between 25-30%. The poverty rate is approximately 30% according to the GOJ. USAID/Jordan supports the GOJ's long-term vision and strategy for increasing economic activity and job creation.

Small and medium enterprises (SMEs) are among the most active creators of new jobs and economic activity in developing economies. Growth in this sector is, however, typically inhibited by undercapitalization within the enterprise and limited access to capital from external sources. The limitation in access to capital arises as a result of the innate conservatism and restricted business models characteristic of Jordan's established capital sources – commercial banks – and a lack of development in the local intermediary financial institution (IFI) sector. Raising capital through equity or bond markets is not a viable alternative for SMEs in Jordan's still developing capital market environment.

According to a 2004 USAID report, *SME Access to Capital in Jordan*, an effective program to develop SME access to capital in Jordan should focus on the following measures: (i) the provision of incentives to commercial banks to support lending to SMEs through (a) provision of loan guarantees for 50 percent of the loan extended ....and (iv) the provision of technical assistance to SME owner-managers to develop know-how in the areas of cash-flow management, financial reporting and strategic business development. This guarantee will directly respond to these recommendations and address the needs of both SMEs and the banking sector in matching credit supply and demand.

USAID/Jordan has a combination of already established technical assistance programs that focus on small and medium-sized businesses and support increased trade. The Mission proposes to augment the development impact of these programs with a partial guarantee to facilitate SME financing for working capital and medium and long-term financing for capital investment.

Development Objective

Substantial liquidity in the financial sector, stable inflation and exchange rates, relatively strong local and international financial institutions, and a burgeoning capital market all contribute to making Jordan an optimal country for private sector financing of development projects. Nonetheless, SME lending remains short-term and not broadly accessible due to risk perceptions of financial institutions, information asymmetry, and limited term money in the financial system. A summary list of the factors constraining SME access to finance includes:

- Information asymmetry – no reliable comprehensive credit reference information system.
- SMEs have opaque financial statements, poor business plans, and limited traditional collateral/security to pledge.
- Very limited medium- and long-term funds in financial system so difficult for banks to lend for SME capital investment.
- Commercial banks are conservative and have focused on large corporate clients and low risk returns.

- Limited capacity to properly analyze SME borrowers; evaluate, mitigate, and appropriately price risk.
- Legal environment not conducive to Receivables-based financing.

The proposed guarantee will support increased SME access to working capital, and medium and long term financing for the purchase of equipment and technology. The DCA facility will provide the bank with a partial guarantee on multiple loans made to SMEs in all sectors and in all geographic areas of Jordan. Through more accessible working capital, targeted capital investment, and business development assistance, SMEs will increase their contribution to national economic growth by expanding their production, improving their efficiency, and hiring more employees.

USAID/Jordan's main objectives with this activity are to increase SME access to finance, thereby increasing incomes, creating employment and stimulating economic growth. Loans under the facility are not proposed for certain sectors, instead remain broadly defined to include activities that stimulate economic prosperity. Based on discussions with the Bank of Jordan, the activity intends to mobilize $10,000,000 to Jordanian SMEs through market rate loans over the period of the guarantee.

Technical Assistance

USAID's most successful DCA activities have been those that are mutually reinforcing with ongoing technical assistance and policy reform initiatives. This DCA activity to increase access to credit for Jordanian SMEs has direct synergies and will coordinate closely with these and other programs:

- USAID-funded National Linkages Program (SME Capacity Building)
- USAID-funded Financial Operations Results FOR-Jordan Project (SME and Banker Training)
- USAID-funded Jordanian-US Business Partnership (JUSBP) – now transforming to (Business Development Service Center)
- USAID's Achievement of Market-Friendly Initiatives and Results (AMIR) Program
  -Financial Markets Development Component
  -Enhanced Competitiveness Initiative Component
- EU-funded Euro-Jordanian Action for the Development of Enterprise (EJADA)
  (SME and Banker TA)

National Linkages Program.

USAID/Jordan has initiated the National Linkages Program, which dovetails with the GOJ's competitiveness program for SMEs (Jordan Upgrading and Modernization Programme's - JUMP). It also complements USAID funded technical assistance to the Aqaba Development Corporation, the Aqaba International Industrial Estate, and the Zarka Chamber of Industry. The National Linkages Program (NLP) facilitates backward linkages to assist SMEs grow and access the international market. NLP is demand-driven, focusing on the exporters' input needs and then assisting SMEs in becoming accredited suppliers to these large companies, thus creating the backward linkage. Backward linkages are inter-firm relationships, where large corporations regularly purchase intermediate goods and services as production inputs from one or more local SMEs in the production chain.

NLP will broker backward linkages with large Jordanian companies and local SME suppliers. NLP will also strengthen local SMEs through technology transfer and skills upgrading to ensure the consistent quality of inputs. NLP will conduct an audit of the SME supply company, identifying management and production inefficiencies, and will assist the SMEs upgrade their systems and processes to meet the exporters' needs. NLP will provide grants up to 30 percent of the cost to participating SMEs that want to upgrade equipment or invest in technology. The remaining 70 percent the SME must finance itself. It is anticipated that many SMEs will seek private financing for a portion of the 70 percent not covered by NLP for such equipment and technology purchases.

The ultimate success of NLP will lie in the ability of SMEs to implement their upgrading programs, especially in the area of new capital investment, key to achieving accredited supplier status with large exporters. Based on current loan tenors to SMEs, it is expected that most SMEs will face difficulty accessing medium-term financing for the purchase of new machinery, for increased stock levels, and for the acquisition of new technology. The proposed partial guarantee will facilitate the bank extending loan tenors of at least three years or more to SMEs.

FOR-Jordan Project

The goal of the FOR-Jordan Project is to improve the ability of Jordanian banks to safely and confidently lend to SMEs, and to increase the competitiveness of Jordanian SMEs. FOR-Jordan workshops will employ an integrated strategy to:

- Provide SMEs with tools and training with which to develop, implement, and measure financial and operational strategies

- Provide banks with tools and training for better risk assessment and management and introduce new lending methodologies appropriate for SMEs.

The project will be delivering multiple workshops for both SMEs and banks through September 2005. Workshops for SMEs focus on understanding the business' financial position, improving financial statements, and how to present a business plan to banks. For banks, training focuses on credit analysis, risk assessment, credit scoring, and non-financial analysis. Both groups are introduced to the Uniform Finanical Reporting System (UFRS). The UFRS is an IAS compliant reporting and internal management tool which allows a company to understand its financial performance and to present its financial position effectively to banks, potential suppliers, customers, and investors. The Credit Officer version of the UFRS is designed for bankers and financial analysts as a tool to convert financial information provided by companies into a common format, with which current and projected financial performance can be easily understood and converted into a credit score.

Bank of Jordan has already sent a number of its Credit Officers to FOR-Jordan's cost-shared bank training, and is in discussions with FOR-Jordan to arrange an in-house more customized training for Bank of Jordan staff only to increase the knowledge and skill set within the credit department about SME lending techniques. Pairing this type of technical assistance with the guarantee will contribute significantly to its successful utilization.

JUSBP

The Jordan-United States Business Partnership (JUSBP) is a USAID-funded economic development program providing financial assistance to private businesses in Jordan, focusing on Small and Medium-Sized Enterprises (SMEs). Designed to provide assistance to Jordanian companies, JUSBP conducts most of its work at the "firm level" to improve the business capabilities of client enterprises. This involves direct support for improvements in management, marketing, technology, production methods, quality assurance, financial management, and human resources, among other priorities. JUSBP, and its follow on the Business Development Service Center, will serve as a potential referral source for SME clients for BOJ.

A major thrust of JUSBP is to improve the ability of Jordanian companies to compete in international markets through expanded trade opportunities. As a U.S. assistance program, JUSBP emphasizes trade with the United States, particularly advantages that are available under the Jordan-United States Free Trade Agreement. JUSBP addresses these export priorities through the Export Fast Track Activity Program, EFTAP. The Global Trade and Technology Network (GTN), is also housed at JUSBP, offering a network of trade specialists to help companies with international trade transactions. JUSBP works in most economic sectors with private business associations that seek to develop the commercial interests of Jordan. The program provides assistance to these associations for business development, training, member services, trade enhancement, and networking with global associations and industry groups. JUSBP also established a comprehensive industrial and human resources training program with both private and public sector constituents, and offers a unique Internship Program "Maharat" for Jordanian university graduates. Other JUSBP initiatives include, Faculty-to-Factory, Increasing the Competitiveness of Jordanian Women Owned Businesses, Certified Manager Program and the Certified Trade Advisors.

AMIR

The AMIR Program is an innovative economic opportunity project funded by (USAID) and implemented in partnership with the Jordanian private sector and government. The current phase, launched in February 2002, builds on the impressive success of the original phase of the program, which from 1998 to 2002 promoted economic growth and prosperity in Jordan by developing a more favorable environment for business and investment. The current phase is broader in scope, engaging the government and the private sector through a series of expanded initiatives. In October 2004, program's work was re-organized, creating a new initiative to capitalize on linkages across the program. In partnership with the people and government of Jordan, the AMIR Program is creating a globally recognized economic success story through its work on four major initiatives. Out of the four, the Enhanced Competitiveness Initiative (ECI) and Financial Markets Development (FMD) are the components that will most integrally complement the DCA LPG for SME lending with Bank of Jordan.

The Enhanced Competitiveness Initiative (ECI) aims to improve Jordan's national competitiveness. "Competitiveness" refers to Jordan's ability to create robust, sustained economic growth, while improving the quality of life of its citizens through increased employment and incomes. Improving competitiveness involves creating a favorable environment for doing business, encouraging investment, developing enterprise, and upgrading human resources to improve the productivity of local firms. It requires a continuous and focused national effort that is undertaken by a partnership which includes the government of Jordan, the private sector, and civil society. ECI focuses on the following priority challenges: creating effective public institutions for economic policy development and implementation; organizing key private sector constituencies; providing business development services in underserved segments of the economy that demonstrate high potential; fostering public-private partnerships for economic policy formulation; and building business management capacities. Key Initiatives ECI is undertaking include: Business Association Strengthening; Business Development Services; Business Skills Development; Investment Promotion; and Public-Private Partnership Support.

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SME Lending in Jordan (BOJ)

The Financial Markets Development Initiative (FMD) works with Jordan's capital and financial markets institutions to develop a fair, efficient, liquid, and transparent market to inspire domestic and international investor confidence. During the first phase of the AMIR Program, the initiative focused on capital markets development in the areas of regulatory reform, institution building, and improving the efficiency and stability of Jordan's three capital market institutions: the Jordan Securities Commission (JSC), the Amman Stock Exchange (ASE) and the Securities Depository Center (SDC).

During the second phase of the program, this initiative is working to broaden and deepen Jordan's financial markets by leveraging unused capital for developing and modernizing financial institutions, accomplished through enhancing banking laws and bank supervision, developing equity market regulations, introducing new investment instruments, developing the government bond market and housing finance market, and expanding the investment portfolio of the social security fund. These approaches help to address the causes of illiquidity in long-term finance and harness Jordan's US$2 billion locked in low-yield investments that have little development impact. Key Initiatives and Entities FMD is working with include: Central Bank of Jordan; Capital Markets Development: Jordan Securities Commission, Amman Stock Exchange, Securities Depository Center; Pension Fund (Social Security Investment Commission); Jordan Mortgage Refinance Corporation; Banks and Financial Institutions; Chartered Financial Analyst Program; and Ministry of Finance.

EJADA

The EU-funded Euro-Jordanian Action for the Development of Enterprise Program (EJADA) is dedicated to facilitate the integration of the Euro-Mediterranean free trade area through its work to modernise and upgrade Jordanian industry, while improving the competitiveness of small & medium size enterprises (SMEs) and their environment. EJADA's aim is to broaden the scope of activities and knowledge base by operating through four specialised yet diverse components that work directly and indirectly with Jordanian SMEs. EJADA's four components are designed to provide an integrated set of services for SMEs, but each has a distinctly different role, which are: Direct Support to SMEs; Financial Support Services; Vocational Training and Human Resources Development; Policy Support and Institutional Strengthening. As part of its Financial Support Services Component, EJADA sourced an advisor to BOJ to assist the bank with the development of its SME strategy.

EJADA has a Loan Guarantee Scheme which is run by the Jordan Loan Guarantee Corporation. Under this scheme up to 70% of the lending risk of banks which lend to SMEs is covered by a special fund (up to €6 million) financed by EJADA. Loans between JD28, 500 and JD 428,500 for new investment in premises, machinery and equipment are eligible for the scheme, where the borrower can demonstrate a viable business plan and an ability to meet repayments.

BOJ has participated in EJADA's loan guarantee scheme but has placed only 4 loans under their 70%-30% risk sharing arrangement. The bank believes that even with the reduced coverage percentage offered by the USAID DCA facility, they find it more attractive an incentive and will actively utilize the facility. For EJADA's loan guarantee scheme, credit analysis, due diligence, and credit approvals are undertaken in close coordination on a loan-by-loan basis with EJADA, and EJADA has the final approval on credit decisions. BOJ feels that its credit teams will better increase their capacity in undertaking the entire process on their own, with targeted technical assistance and training as needed, using the DCA mechanism.

Additionally, the EJADA guarantee program is much narrower in its qualifying borrower pool, limiting lending to the manufacturing and services sectors, fixed asset purchase loans only, and the tenor must be between three to eight years. Since this DCA activity is restrictive on the loan size and tenor only by the maximum, and leaves the sectors and credit decision process to the bank, Bank of Jordan is eager to work with USAID through this DCA guarantee facility.

Proposed Guarantee Structure

The proposed Loan Portfolio Guarantees will be for 8 years and have a total facility ceiling of USD $10,000,000. It will be under a single legal agreement with the Bank of Jordan. This DCA loan portfolio guarantee (LPG) will facilitate access to working capital and longer term investment and asset purchase financing for small and medium enterprises (SMEs) currently underserved by the financial sector. The guarantee will complement technical assistance initiatives being undertaken by USAID to strengthen SMEs and the banking industry. Qualifying borrowers will include financially viable SMEs, defined as having 5 to 250 employees, operating in any sector of the economy, including those that are exporting or provide inputs to exporters. While USAID believes that many of the borrowers will come from the technical assistance provided by NLP and other technical assistance partners as described above, the Mission has elected not to limit borrowers to only those participating in a USAID- or other donor-funded programs, to encourage the bank to utilize the guarantee facility to explore the SME market and continue to do so in a sustainable manner after the guarantee period.

Bank Partner

Bank of Jordan (BOJ) was established in 1960 by a group of Jordanian businessmen. It is the third largest bank in Jordan in terms of assets with a 4.5% share of deposits and a 5.5% share of loans at the end of 2002. It offers a range of retail and corporate banking products, complemented by some treasury and investment services. It is a domestic commercial bank, the third largest in Jordan, with an expanding network of over 71 outlets and 28 ATMs. It also has 5 branches in Palestine with that branch network engaging as of summer 2004 in another USAID DCA LPG for SME lending through the USAID/West Bank and Gaza Mission. Bank of Jordan's major shareholder is the Fakhoury Group, a prominent business family group. BOJ's Vision and Mission present the values of the bank's management which is progressive within the Jordanian context.

Vision. "To be the pioneering bank in Jordan, and in any other country in which we are present; a leader in fulfilling the financial and banking needs and expectations of our customers, continuously developing and enhancing our service to build a lasting and distinguished relationship with them."

Mission. "We will be energetic in our quest to become our customers' strongest and closest partners, to maintain our position as their bank of choice. We will fulfill our customers' needs and anticipate their expectations by offering an advanced range of value-added services and solutions that help our customers achieve their ambitions for a prosperous future. We will be transparent and fair in our dealings, and will conduct ourselves professionally and with a motivated team spirit. We will strive to raise the standard of our organization, and will work together to be a positive and practical role model in the continuing development of our community."

The bank experienced a 12% growth rate in its net direct credit facilities during 2004, ending at JD 398.8 million ($282,350,400), and total customer deposits increased over 2004 to JD 761.2 million ($538,929,600). SME lending will fall under the Bank of Jordan's Commercial Credit Department. The total outstandings for the Commercial Credit Department as of March 30, 2005 are at JD 57 million ($40,356,000) with 4218 borrowers. Sectoral breakouts include mining (.95%), construction (9.8%), light industry (8.9%), agriculture (3.3%), small trading (25.3%), transportation (5.6%), tourism (2.06%), services (36.9%), retail (6%), and other (1.19%).

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Many factors indicate that Bank of Jordan will be a committed and valuable USAID DCA partner bank, including:

- BOJ is a local Jordanian-owned bank.
- SME lending is part of their long-term business strategy.
- BOJ has a wide branch network for outreach to SMEs across Jordan.
- BOJ, unlike many other banks in Jordan is not engaged in speculative activities – for instance, other large commercial banks have been offering large trading on margin accounts for customers day trading on the Amman stock exchange.
- BOJ Senior Management has made a significant and ongoing commitment to moving systematically into the SME market and working with USAID. They have demonstrated this by: continuing to benefit from the assistance of an embedded EU-funded SME Advisor; actively participating in FOR-Jordan SME Credit Analysis training and requested in-house training; and establishing a recent DCA LPG for SME lending with USAID/West Bank and Gaza.

Attachment III: Economic Justification
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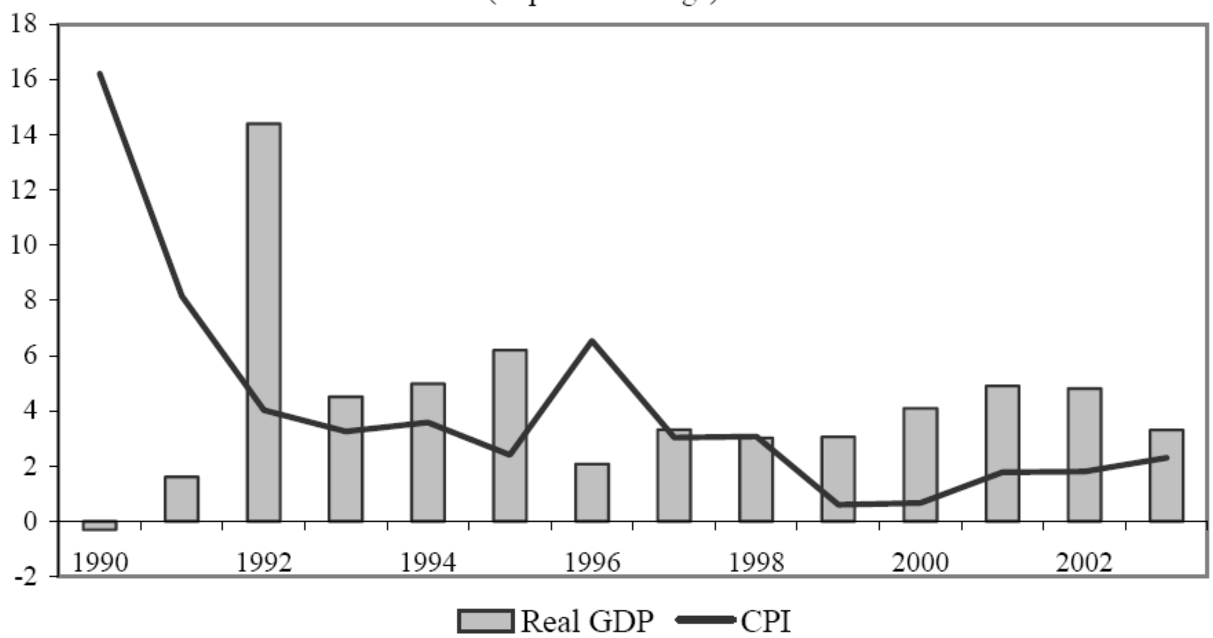
SME Lending in Jordan (BOJ)

Economic Growth Rate

International confidence in Jordan's economy remains high with recent upgrades in the soveriegn rating by Moody's and Capital Intelligence in September 2003. According to Emerging Jordan 2004, "Moody's highlighted trade liberalization, fiscal reform, and privatization as three areas where the government has made particular progress." This is despite the disruption in economic growth as a result of Iraq war, which curbed tourism and placed into question Jordan’s historical access to free Iraqi oil.

Jordan has a population of about 5 million, and a per capita gross national income estimated at about US$1,800 in 2002—higher than the average for lower-middle-income countries (US$1,400) but less than the average for countries in the Middle East and North Africa (US$2,200). Jordan’s economy is closely tied to those of other countries in the Middle East. Three notable features are: remittances from Jordanians working in other countries, especially in the Gulf states, are an important source of national income (equivalent to15–20 percent of GDP); the region is the primary destination for Jordanian exports and in turn supplies the bulk of Jordan’s energy requirements; and Jordan receives substantial aid from countries in the region. Economic performance has been marked by successful disinflation and fluctuations in real GDP growth over a wide range (Fig. 1). (International Monetary Fund and Jordan: Issues Paper. Prepared by the Independent Evaluation Office. November 19, 2004.)

Figure 1. Real GDP Growth and CPI Inflation
(In percent change)



Source: Central Bank of Jordan

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SME Lending in Jordan (BOJ)

Banking and Financial Markets

Domestic liquidity grew by 12.4% against 7.0% over the period 2002 to 2003. Moreover,
the CBJ's foreign reserves continued to rise remarkably. They rose by US$ 1.2 billion in 2003, to reach, by the year's end, a balance of US$ 4.7 billion; an amount that is enough to finance more than 9 months-worth of the Kingdom's imports of goods and services. The CBJ made several reductions in interest rates during 2003 trying to create a downward influence on market interest rates. These reductions came in light of the reductions in international interest rates and to stimulate domestic economic activity. Banks responded positively to this trend by lowering both the lending and deposit interest rates. However, reductions in the deposit interest rate have far exceeded the reduction in lending rates.

The financial sector in Jordan includes 19 commercial banks, 2 Islamic banks, and 4 public or joint ownership banks, and 26 insurance companies. Total deposits at licensed banks increased in 2003 by JD 601.7 million, or 6.4%. This rise was mainly concentrated in deposits of private sector (resident), which grew by 14.4%. On the other hand, credit facilities extended by licensed banks grew by a modest rate of 2.6% as a consequence of the heightened uncertainty that prevailed in the region. (Central Bank of Jordan Annual Report 2003)

Market imperfections

Currently, the majority of lending in Jordan to SMEs is in the form of overdraft accounts. As stated by some private sector banks, their clients prefer overdraft accounts despite higher interest costs because there is no amortization schedule to which they are tied. However, the Central Bank has regulated that by 2007 no more than 20% of a bank's portfolio can be in overdraft accounts. Thus, banks will be forced to offer term loans. While most banks have noted that working capital loans to SMEs is viable and somewhat available to a limited group of SMEs, overwhelmingly they are hesitant to extend tenors. Most banks noted that 3-year financing to SMEs is extremely restricted, despite having significant liquidity. Jordan is dealing with a systemic dearth of long term funds in the system, but it is hoped that the guarantee will stimulate the bank to explore solutions such as the issuance of longer term Certificates of Deposit to correct that mismatch to be able to offer longer tenor loans on a sustainable basis.

Factors constraining SME access to finance includes:

- Information asymmetry – no reliable comprehensive credit reference information system.
- SMEs have opaque financial statements, poor business plans, and limited traditional collateral/security to pledge.
- Very limited medium- and long-term funds in financial system so difficult for banks to lend for SME capital investment.
- Commercial banks are conservative and have focused on large corporates and easy T-bill returns.
- Limited capacity in the banking sector to properly analyze SME borrowers; evaluate, mitigate, and appropriately price risk.
- Legal environment not conducive to Receivables-based financing.

Bank of Jordan will use the DCA guarantee to make loans to new SME clients identified through the aforementioned technical assistance programs, through their current client base, and through their branch network. They are at the point of finalizing their SME Strategy developed in cooperation with an EU-funded advisor, which will include some new product development and piloting for this market, timing for which coordinates very well with the expected establishment of the guarantee facility. Concurrently, BOJ will continue to explore options for building capacity within the bank to understand and analyze SME businesses, and with the guarantee BOJ will be able to reduce borrower collateral requirements, although they will continue to price loans according to risk at market rates.

Additionality

The proposed guarantee does not crowd out private lending to SMEs because there is almost no bank lending beyond three years to SMEs, and there is limited receivables-based financing for working capital. While there are some EU and GOJ guarantee funds to encourage the banking sector to lend to SMEs, their structure, narrow parameters for qualifying borrowers, burdensome administrative procedures, and inteference in the credit decision making process makes them unattractive to the banks and they are not making use of them. Hence there is no overlap between the DCA facility and any other guarantee fund.

Without the guarantee, Bank of Jordan would not move forward with lending to the a broader array of SMEs or with developing longer term loan products for SMEs. The guarantee complements and enhances Bank of Jordan's ongoing investments in exploring the SME lending market including training, technical assistance, and the development of new financial products. Additionally, while BOJ has made a timid step towards extended loan tenors, the guarantee will increase their comfort level in lending for more than 3 years, and they do have some existing client demand for 5 year loans they have not been able to meet yet due to their risk perception.

The guarantee will provide a demonstration effect that lending to SMEs is profitable, both to Bank of Jordan and the wider banking industry. The complementary support provided by the USAID and other training and technical assistance programs will mutually reinforce the guarantee facility to catalyze lending to Jordanian SMEs. As the guarantee facility is utilized and loans are placed, SME credit histories will be established, and it is expected that SME borrowers able to access credit without a guarantee either through Bank of Jordan or another lender. As DCA has seen in other countries, once other banks take notice of BOJ's successful penetration of the SME market it is anticipated that it will spur competition leading to more affordable credit for SMEs. Concurrently a portion of the excess liquidity in the financial sector will be absorbed and put to productive use.

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Provided by the Office of Development Credit

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Provided by the Office of Development Credit

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Bank of Jordan - SME

Provided by the Office of Development Credit.

DEVELOPMENT CREDIT AUTHORITY (DCA) MONITORING PLAN

BANK OF JORDAN – LOAN PORTFOLIO GUARANTEE FOR SME LENDING

Monitoring is a coordinated effort between the Mission and the Office of Development Credit (EGAT/DC). Monitoring responsibilities are divided into Development and Financial activities.

The mission is solely responsible for Development Monitoring of the loan portfolio guarantee (LPG), whereas the responsibility for Financial Monitoring throughout the period of the activity, is shared with both EGAT/DC and the Mission.

USAID/Jordan will be assisted in its Development Monitoring and Financial Monitoring responsibilities by the Achievement of Market-Friendly Initiatives and Results (AMIR) Program through July 2006. The AMIR Program will support USAID approximately two person days/month for the first 3 months, decreasing to one person day/month for the remaining 9 months. Support will include:

- Working with USAID and the bank to promote clear understanding of compliance with the legal agreement, reporting requirements, the definition of qualifying borrowers, and field any other questions or issues that may arise;
- Monitoring bank to ensure fee payment when due;
- Liaising with the bank to ensure proper and timely semi-annual and annual reporting through the internet CMS reporting system;
- Developing and maintaining a data base of DCA usage by the bank;
- Processing claims applications from the bank and follow up with USAID/Washington until the point of claim payment;
- Monitoring DCA portfolio for potential problem loans and potential defaults;
- Working with bank to ensure appropriate collections practices for any claims;
- Encouraging participating bank utilization by facilitating communication and coordination between the bank and appropriate SME strengthening programs, bank training programs, and other initiatives to assist the bank in understanding the SME sector;
- Preparing quarterly summary reports and any ad hoc reports as required;
- Conducting annual site visit if occurring within the timeframe allotted; and
- Training the follow-on entity on DCA and the monitoring role.

DEVELOPMENT MONITORING

This DCA guarantee facility will contribute to the achievement of USAID/Jordan's SO Number 10 – Increased Economic Opportunity for Jordanians. The US Government's Economic Development Goal in Jordan is broad-based, market-oriented growth accompanied by expanding investment, improving standards of living and enhanced economic opportunities for all Jordanians. Three intermediate results support SO Number 10 - Increased Opportunity for Jordanians. These include:

1. Increased access to business services;
2. More effective identification and implementation of policy reforms; and

3. An improved environment for sustained policy reform.

The DCA LPG specifically complements and reinforces IR1: Increased Access to Business Services, in that access to financial services is equally as important as other non-financial aspects of business services such as management capacity building, to facilitating business growth and expansion. The indicators the Mission will use to monitor the guarantee on an ongoing basis are:

1. Percentage utilization of total authorized amount;
2. Number of new loans disbursed by the lender; and
3. Number of SMEs receiving loans.

The Mission will also request that EGAT/DC forward the synthesized information compiled through the Credit Management System (CMS) Annual Data Questionnaire (ADQ) that all guaranteed parties complete annually to obtain qualitative measures of the impact of DCA guarantees. The type of information collected in the ADQ is described further in Section iii.

FINANCIAL MONITORING

Financial Monitoring activities include ensuring that fees are paid, reporting requirements are met, documenting completion of conditions precedent (when applicable), making site-visits, and closing out the facility upon expiration. The EGAT/DC Portfolio Management (PM) team takes primary responsibility for Financial Monitoring. EGAT/DC will create and manage source files for all DCA facilities and be the primary resource for financial reporting on DCA activities within the Agency.

The coordinated effort in monitoring requires that the Mission and EGAT/DC staff work as a team. The Mission establishes and maintains the primary relationship with the partner financial institution (FI), or guaranteed party, and acts as the liaison between the FI and the EGAT/DC in Washington. The liaison role is supported by the EGAT/DC Project Development (PD) team Relationship Manager who together with the Mission ensure:

- Frequent contact with the FI's management.
- Timely and compliant submission of required documents and reports.
- Prompt remittance of USAID origination and utilization fee payments from FIs.
- Communication with EGAT/DC Portfolio Management if problems arise or certain conditions change that either reduce or improve the financial stability of the FI or the Borrowers.

This monitoring plan outlines detailed requirements for Financial Monitoring activities. A monitoring plan may include additional monitoring duties if deemed necessary by Mission Officer(s) responsible for a DCA activity and/or EGAT/DC Relationship Managers. These additional duties may arise due to the particular structure of the guarantee facility, the status of the guaranteed party or the desired development outcomes. The duties detailed below are performed throughout the life of the guarantee facility. Each monitoring activity must be conducted according to this monitoring plan. The EGAT/DC PM team will ensure that the DCA files in Washington are maintained to document all monitoring activities as outlined in this plan.

i. REPORTING

For examples of any of the following reports, templates should be included as an attachment to the legal agreement signed between USAID and the guaranteed party. Prior to signing this agreement, Missions should contact EGAT/DC for examples/templates.

a) TRANSACTION REPORT (TR)

Most LPGs require the guaranteed party to submit a Transaction Report (TR) for each loan that is placed under guarantee coverage. A TR is a data sheet containing information about the loan and the borrower. In the case of large volume LPGs, TRs can be structured to be extremely concise with only key data required, such as the loan date, borrower name, loan amount, loan purpose. Guaranteed parties submit TRs to the Mission and to EGAT/DC through an Internet-based system – Credit Management System (CMS). CMS will only track the basic information of a TR. If there is specific performance compliance data to check, e.g. asset size of borrower, the guaranteed party may still be required by the Mission to submit paper or electronic TRs. The frequency of submitting TRs varies. They can be entered in CMS in "real time" as the loans are placed under coverage. Alternatively, Missions may decide to allow banks to submit TR data with QLS information on a semiannual basis.

Missions and EGAT/DC will review CMS data, or paper/electronic TRs if required, to ensure that the guaranteed party submits TRs that are compliant with the legal agreement. The loan is assumed to be approved for guarantee coverage unless USAID contacts the guaranteed party to further clarify the proper enrollment of loans under coverage.

b) QUALIFYING LOAN SCHEDULE (QLS)

Most DCA activities require that the guaranteed party submit a Qualifying Loan Schedule (QLS) every six months.[1] Typically, these QLS reports correspond with guarantee periods from October 1 – March 31, and then April 1 through September 30. The QLS is a status report on all new loans placed under coverage, outstanding loans, and loans taken off coverage during the past six months. The summary level figure of each QLS that is most important from the utilization and USAID risk exposure perspective is the ending principal balance. This is relevant for all guarantee types – LPGs, loan or bond guarantees.

EGAT/DC ensures financial compliance of every QLS and it will report any non-compliance to the Mission for resolution or directly discuss these issues with the guaranteed party if previously agreed to by the Mission. QLS non-compliance may occur frequently if the guaranteed party does not fully understand reporting procedures or the legal agreement terms and conditions. In some cases, several email and/or telephone communications may be necessary to resolve non-compliance issues. Furthermore, a Mission or EGAT/DC site visit to or meeting with the guaranteed party may be required if the issues remain unresolved for more than 60 days. Once in compliance, the QLS serves as a platform to assess appropriate fees, judge the overall risk exposure, document the overall effectiveness of the program, and/or predict future claims.

For LPGs, QLS reports are submitted via the Internet-based Credit Management System (CMS). For other loan and bond guarantees, the guaranteed party will submit either electronic or paper

[1] The current standard for loan and bond guarantee reporting requirements are annual, corresponding with the amortization or repayment of the loan/bond.

reports, which typically include updated amortization or repayment schedules, as stipulated in the legal agreement. EGAT/DC will ensure those reports are properly entered into CMS for management reporting and utilization fee billing purposes. Missions, guaranteed parties and EGAT/DC will have simultaneous access to CMS to view data and to identify either compliant or non-compliant issues.

ii. FEES

Each DCA activity requires that the guaranteed party remit payment of two types of fees. As stated above, it is the responsibility of the Mission and the EGAT/DC Relationship Manager with support from the EGAT/DC PM team to ensure timely and accurate payment of fees.

a) Origination Fee – One time fee paid upfront. The guaranteed party typically has thirty (30) days from the signing of the legal guarantee agreement to pay this fee. A bill will not be submitted to the Mission or to the guaranteed party. Payment must be made as instructed in the legal agreement. See legal agreement for further information. In regards to the majority of PGs, the identified borrower(s) will pay the origination fee as stipulated in its commitment letter, which serves as the obligating document for this type of guarantee.

b) Utilization Fee – Annual fee that is paid every six months. The fee is based on an average outstanding principal balance during a semiannual period. This is typically calculated by averaging the ending principal balance of the current and previous QLS reports submitted by the guaranteed party. Once QLS report balances are confirmed as compliant by EGAT/DC in CMS, EGAT/DC will contact Riggs Bank to ensure a bill, a "Notice of Payment Due" (NPD) is sent to the guaranteed party with the total amount to be paid. The guaranteed party has thirty (30) days to pay the utilization fee after it receives the NPD. See legal agreement for further information. In regards to PGs, the commitment letter will not entail any utilization fees, which would be paid by the eventual guaranteed party that provides a loan to the borrower. Also, for bond guarantees, utilization fees are typically paid upfront in one lump sum at the time of bond disbursement. This fee is calculated as a net present value of future fees based on forecasted outstanding amounts during the bond guarantee term.

iii. ANNUAL DATA QUESTIONNAIRE (ADQ)

Through CMS, EGAT/DC will request that guaranteed parties complete an ADQ by June 30 every year. CMS will generate emails to the key contacts of all guaranteed parties on or around June 1 to request that they complete the ADQ before the end of the month. ADQ guidance in CMS will recommend that the guaranteed party spend no more than 30 minutes on the ADQ to ensure that this request is not overly burdensome

The purpose of this questionnaire is to obtain qualitative measures of the impact of DCA guarantees. Examples of the questions asked in the ADQ are:

- Collateral. Please describe if your institution has been able to lower its collateral requirements for Qualifying Borrowers because of the USAID guarantee.

- Loan Terms. Please describe if the USAID guarantee has resulted in your institution's ability to lengthen the repayment term (duration or tenor) for loans to Qualifying Borrowers?
- Other. What other impact has the USAID guarantee had on your ability to provide loans to Qualifying Borrowers? (For example, have you been able to make loans to these types of borrowers without the guarantee?)
- Example of a "success story" of the tangible benefits realized by one of the borrowers who productively utilized funds from a DCA guaranteed transaction.

iv. CLAIMS

The following list highlights how DCA claims are processed:

- Guaranteed party submits claim(s) for defaulted loan(s) to the Mission under a covered DCA facility. When the Mission receives the claim, it should forward the documentation to EGAT/DC Portfolio Management (PM) team along with any additional information relevant to this particular guarantee.
- EGAT/DC PM team reviews claim for compliance and prepares paperwork for claim approval. Any necessary correspondence with guaranteed party will be cleared by the respective the Mission Officer responsible for the DCA activity and the EGAT/DC Relationship Manager.
- EGAT/DC PM team arranges for clearances by Mission Officer, Relationship Manager prior to submitting to EGAT/DC Director for approval.
- Once approved, EGAT/DC PM team commits and obligates funds from the appropriate DCA Financing Account via Phoenix.[2]
- Upon obligation of the claim amount to be paid, the PM team then notifies FM/LM to instruct the Mission Controller to pay the claim.
- The Mission Controller then makes the claim payment, and obtains reimbursement through FM/LM via the Intra-governmental Payment and Collection (IPAC) system.
- EGAT/DC PM team follows up with email/phone contact to Mission Controller to confirm that claim payment has been made available to the guaranteed party.
- FM/LM notifies the EGAT/DC PM team when evidence of the Controller's transaction has been received. EGAT/DC PM team may then need to adjust the obligation amount due to exchange rate differences.

v. RECOVERIES

The EGAT/DC PM team (with potential field support from the Mission Officer responsible for the DCA activity in case of late responses) will send out annual letters by the first week of June of each year to all FIs that have received a claim payment from USAID. The letter, signed by the EGAT/DC Director or EGAT/DC PD Relationship Managers, will request that the FI submit a Schedule of Net Recoveries [see template below] by June 30 that identifies all claim payments made to a FI and requests updated data and certification on recoveries received by the FI on these defaulted loans.

[2] When a DCA guarantee is initially established, the subsidy funds are transferred to the DCA Program Account. As the guarantee is utilized, the subsidy is disbursed proportionally to the DCA Financing Account, where fee payments from guarantee parties are also applied. The combination of subsidy and fees for guarantees obligated within the same fiscal year is the source of funds for claim payments to guaranteed parties.

SCHEDULE OF NET RECOVERIES								
<Bank Name> <Loan Portfolio Guarantee Number XXX> < as of DATE >								
Defaulted Loan/ Borrowers Name	Date of Qualifying loan	Date of Claim payment	Amount of Claim in USD	Recoveries Received as of <DATE>	Amount of Recoveries Collected by Bank	Date of Recoveries	Amount of Recoveries due to USAID	Expected Date Recoveries to be remitted to USAID

* To be completed by USAID
* To be completed by the financial institution

vi. MISSION SITE VISITS AND EGAT/DC BIENNIAL REVIEWS

Based on OMB Circular A-129, Mission Officer(s) responsible for a DCA activity are required to conduct and report on site visits to the guaranteed party, while the EGAT/DC PM team must conduct biennial reviews of the guarantee. Structures and guidelines for these visits and reviews are provided in the following two tables. Due to the similar nature of the reports described below, the EGAT/DC PM team will coordinate its biennial review with appropriate Mission staff.

Mission Site Visit	
Frequency:	Annually from date agreement is signed, particularly for guarantees with substantial loan volume, signs of deterioration in guaranteed loan(s), high default rates.
Responsible Entity:	Mission Officer responsible for the DCA activity or designee
Responsibilities:	Meet with partner Financial Institution management, establish status of project and determine compliance and performance issues.
Report Outline:	**Preparation**: Summary of telephone/email communication with PM team prior to site visit to understand unresolved monitoring and compliance issues and to review the most current utilization data. **Unresolved Issues**: Discussion of issues from Section I with FI and clarification of how issues are to be resolved. **Country Status**: Update on any country-wide issues that the FI believes is affecting its loan portfolio and/or DCA utilization – economic changes, exchange rate fluctuations, legal/political changes. **Bank Status**: Update on current situation with the financial institution being guaranteed – e.g., personnel, policy or strategy changes, bank performance, merger & acquisition activities. **Borrower Site-Visit**: If possible, request at least one visit to a borrower that received a DCA-guaranteed loan. Summary of visit should include details of: the loan amount, purpose of the loan, loan term, justification for using the DCA guarantee, how it was repaid, and the resulting benefits for the borrower. **USAID Support**: Discussion with FI if USAID can provide any further guidance or assistance in order to promote utilization of and proper reporting on the guarantee. **Conclusion**: Summary of follow-up action items
Delivery of report:	Mission Officer will send completed report via email to EGAT/DC PM team within 30 days of the anniversary of guarantee and EGAT/DC PM team will review the report and ensure that it is appropriately filed. In lieu of this report, the Mission Officer will send EGAT/DC an email to justify that the visit was not necessary. This email will also be filed accordingly.

EGAT/DC Biennial Review	
Minimal Frequency:	Biennially (once every two years) from date agreement is signed or coordinated with a country visit for other purposes
Responsible Entity:	EGAT/DC PM team (with support from Relationship Manager) or designee. If a Mission or its contractor prefers to be responsible for the biennial review, EGAT/DC PM team will review and provide feedback on the biennial report as outlined below.
Responsibilities:	To produce the following report at a minimum of once every two years for a DCA guarantee.
Report Outline: Note: Since the Biennial Report is similar to the Mission On-site Visit Report, EGAT/DC will coordinate its Biennial Review with the Mission to ensure that the FI is not overburdened with similar questions from two different USAID entities.	**Pre-Review Information Gathering**: Review of files to ensure files are current. Analyze recent reporting, fee and claim information to identify any issues that require follow-up with the FI. Data to be summarized and analyzed are: utilization ratios, fees billed and paid, claims net of recoveries as a percent of subsidy + fees, and reporting timeliness. **Unresolved Issues**: Discussion of issues from Section I with FI and clarification of how issues are to be resolved. Also, reminder to FI that have received claim payments of requirement to share recoveries. **Country Status**: Update on any country-wide issues that the FI believes is affecting its loan portfolio and/or DCA utilization – economic changes, exchange rate fluctuations, legal/political changes. **Bank Status**: Update on current situation with the financial institution being guaranteed – e.g., personnel, policy or strategy changes, bank performance, merger & acquisition activities. **Borrower Monitoring**: {if on-site} request to see credit files at the FI on a random selection of at least two borrowers. If possible, request at least one visit to a borrower that received a DCA-guaranteed loan. Summary of visit should include details of: the loan amount, purpose of the loan, the loan term, justification for using the DCA guarantee, how it was repaid, and the resulting benefits for the borrower. **EGAT/DC Support**: Discussion with FI and Mission if EGAT/DC can provide any further guidance or assistance in order to promote utilization of and proper reporting on the guarantee. Conclusion: Summary of follow-up action items
Delivery of report:	EGAT/DC PM team will review this report and ensure that it is appropriately filed. If this report is part of trip report conducted by an EGAT/DC staff member, it will be copied and placed in the appropriate DCA file.

vii. AUDITS

When a guaranteed party submits a claim for payment, the EGAT/DC PM team will monitor the level of claims against the following three criteria:

NOMINAL CHECK	Do cumulative paid and pending claims exceed the equivalent of US$ 25,000?
PORTFOLIO CHECK	Do cumulative paid and pending claims (converted to total loan values) exceed 10% of Cumulative Utilization?
SUBSIDY CHECK	Are cumulative paid and pending claims as a percent of "subsidy plus fees received" above 50%?

Although this three-tiered criteria checklist is primarily applicable to LPGs, which may receive a series of claim payment requests from the guaranteed party, the same guidelines should be utilized for other forms of DCA guarantees. Data related to these three criteria will be included in the summary page provided in the claim package developed by the EGAT/DC PM team. If at least two out of the three criteria result in positive answers, the EGAT/DC PM team will convene to discuss the possibility of an internal review of the guaranteed party's TRs and QLSs. The PM team will then coordinate next steps with the respective Relationship Manager from the EGAT/DC PD team. The Mission will be contacted as necessary, and additional documentation may be requested from the guaranteed party. The PM team, with guidance from the PD team and the Mission, may request a site visit to inspect the credit files of the guaranteed party.

In the event irregularities are found during the EGAT/DC PM team desk or on-site review, an audit should be conducted by an experienced, independent auditor. The EGAT/DC Risk Management (RM) team will coordinate the planning and review of this auditor's performance. The RM team will also conduct this audit with appropriate Mission guidance. Results of this audit will be disseminated between the PM team and the RM team as well as the Relationship Manager to decide on next steps with this DCA guarantee.

The guaranteed party will be required to repay any amounts deemed to have been paid based on disallowed transactions (e.g., unqualified borrowers). If the guaranteed party is judged to have committed fraud, provided erroneous information, or is perceived as unable to carry out the activities and responsibilities of the guarantee, the USAID Office of General Counsel may advise to terminate the agreement following consultations with the Mission and relevant EGAT/DC staff.

viii. BUDGET

- One (1) designated responsible Officer: 2% of time, **$1,038 per year** for each year during which loans may be placed under coverage. This is based on an annual salary of $51,903.
- One (1) FSN in the Financial Management Office: 2% of time, **$626 per year** for each year during which loans may be placed under coverage. This is based on an annual salary of $31,284.
- Year 1 of the Guarantee: AMIR Support: 7% of one person's time, **$2,894 per year**, for the first year during which loans may be placed under coverage, based on an annual salary of $41,340.
- Years 2-8 of the Guarantee: USAID TBD Project Support: 7% of one person's time, **$3,534 per year** on average for years 2 through 8 of the guarantee period during which loans may be placed under coverage. This calculation is based on an annual salary of $41,340 for Year 1, with an assumed annual increase of 5% per year.

Total Annual Cost for Mission: **$8,092 (estimated average)**

USAID/W EGAT/DC travel to COUNTRY: $3,450 per trip, 1 trip for every two years is $1,725 per year. Estimated staff time costs for EGAT/DC to monitor this DCA guarantee are:

- EGAT/DC PD and PM team: 7 days per year, $3,500 annually for each year during which loans may be placed under coverage. This is based on an average salary of EGAT/DC personnel of $93,600 and a benefits package of $37,500.
- EGAT/DC PM monitoring contractors: $2,000 annually based on ongoing contract.

Total Annual Cost for EGAT/DC: $7,225

ASSESSMENT OF THE SME SECTOR IN JORDAN
IN PREPARATION FOR A DEVELOPMENT CREDIT AUTHORITY
LOAN PORTFOLIO GUARANTEE

Submitted by: **the Achieving Market-Friendly Initiatives and Results (AMIR) Program at the request of USAID/Jordan**

May 2005

ASSESSMENT OF THE SME SECTOR IN JORDAN IN PREPARATION FOR A DEVELOPMENT CREDIT AUTHORITY LOAN PORTFOLIO GUARANTEE

Introduction

This assessment of SME sectors in Jordan has been completed in anticipation of the establishment of a new DCA Loan Portfolio Guarantee to stimulate lending to SMEs in Jordan, which may be expanded in the near future to multiple banks. It is based on secondary source information, and the final product will be incorporated into the DCA risk assessment of the project conducted by the Office of Development Credit. Any recommendations contained within may be used to better structure the proposed lending program to the needs of SMEs. The assessment analyzes key drivers of financial performance, factors that affect creditworthiness, and factors mitigating or exacerbating risk related to the debt repayment capacity of SMEs in Jordan. Since the guarantee is open to lending to SMEs in all sectors of the economy, three sectors have been selected solely for the purposes of this assessment: construction, tourism, and the industrial sector as characterized by the garment industry, which are representative of the mix of sectors in the DCA partner bank's portfolio.

Background

The proposed DCA Loan Portfolio Guarantee facility will support increased SME access to medium and long term financing for the purchase of equipment and technology, as well as working capital. The DCA facility will provide the bank with a partial guarantee on multiple loans made to SMEs in all sectors and in all geographic areas of Jordan. USAID/Jordan's primary objectives with this activity are to increase SME access to finance, thereby increasing incomes, creating employment and stimulating broader economic growth. The LPG, in combination with technical assistance and capacity building programs for both potential SME borrowers and the partner bank, will catalyze the extension of credit at appropriate terms and competitive pricing for currently underserved SMEs to expand and upgrade their businesses.

Economic Overview

Jordan is a small Arab country with inadequate supplies of water and other natural resources such as oil. Debt, poverty, and unemployment are fundamental problems, but King Abdallah, since assuming the throne in 1999, has undertaken some broad economic reforms in a long-term effort to improve living standards. In the past three years, the Government of Jordan (GOJ) has worked closely with the IMF, practiced careful monetary policy, and made substantial headway with privatization. The government has also liberalized the trade regime sufficiently to secure Jordan's membership in the WTO (2000), a free trade accord with the US (2000), and an association agreement with the EU (2001). These measures have helped to improve productivity and have put Jordan on the foreign investment map. The US-led war in Iraq in 2003 dealt an economic blow to Jordan which was dependent on Iraq for discounted oil (worth $300 - $600 million a year). Several Gulf nations provided temporary aid to compensate for the loss of this oil, but Jordanian government has been forced to raise retail petroleum product prices and the sales tax base. Jordan's export market, heavily dependent on exports to Iraq, was also affected by the war but recovered quickly while contributing to the Iraq recovery effort. The main challenges facing Jordan are reducing dependence on foreign grants, reducing the budget deficit, and creating investment incentives to promote job creation and the encouragement of tourism.[1]

Recently, however, several of Jordan's key economic indicators have shown signs of improvement due to structural reforms implemented by the Government of Jordan (GOJ) with the help of the U.S. and other donors since 1999. The Qualified Industrial Zones and U.S.-Jordan Free Trade Agreement, for example, increased annual U.S.-bound exports by almost five-fold since 2001. Despite the negative economic impact of the war in Iraq, Jordan's GNP continues to grow, having achieved a rate of 7.5% in 2004. Jordan was accepted into the World Trade Organization in 2000, and completed a three year IMF structural adjustment program in 2002. These positive developments, combined with continuation of a relatively stable monetary and fiscal environment and a sound microeconomic and regulatory structure means that Jordan is poised for rapid economic growth.

Challenges

The critical economic challenges facing Jordan are modest economic growth rates, insufficient international competitiveness, persistent poverty, high unemployment, sagging *per capita* incomes and economic structural imbalances. All of these factors threaten Jordan's ability to generate new economic opportunities for its citizens and limit private sector trade and investment. In short, Jordan must grow its economy at sustained "real" rates above 5% annually in order to address the pressing poverty and unemployment problems. Moreover, the Jordan Vision 2020 exercise estimates that Jordan's economy must grow at a rate of 8.4% annually in order to achieve its national goal of doubling of gross domestic product *per capita* by 2020.[2] USAID/Jordan's Strategic Objective 10 – Increased economic opportunity for Jordanians – addresses these issues, and the proposed DCA guarantee will contribute to this end.

Jordan has been steadily improving on all macro-economic fronts from 2001 to date. The two indices that fall below the rest, dragging the overall rating down are the rankings for Country Credit Rating and the Technology Index. Historically, the most deeply rooted problems in Jordan are: poor access to finance, particularly the limited venture capital availability; the lack of marketing and branding strategies for firms; the lack of specialized research and training facilities coupled with a poor work ethic; the low capacity for innovation; and the poor port infrastructure.[3]

Exports

In the quantity of exports category, Jordan ranks at 35/104. In the quality of exports however, which is split into the two indices of "nature of competitive advantage" and "value chain presence", Jordan ranks at 42/104, and 46/104 respectively. This is partially due to the fact that firms compete directly with lower-end products that benefit from large economies of scale in East Asia rather than targeting higher value-added products and so are unable to compete effectively. The lack of value-chain presence also means that the value-added reaped

[1] CIA Factbook online
[2] Jordan Vision 2020
[3] Global Competitiveness Report 2003, Jordan Analysis

by Jordan (whether in the final stages of packaging, or the refinement of certain natural resources) is not achieving its true potential.[4]

Table (13): Quality of Exports Rankings

	1998	2000	2002	2004
Nature of Competitive Advantage	40/53 25th	52/59 12th	35/80 56th	42/104 60th
Value Chain Presence	-	31/59 47th	42/80 48th	46/104 56th

Source: Global Competitiveness Report

The GOJ through the JUMP program has identified the selected strategic sectors which have the most competitiveness potential – manufacturing products and providing services for export. Some examples of these in the Jordanian economy include: computer software development; shared services and back office data processing; customer contact call centers; financial services; professional and technical consulting services, and educational and medical services.[5] SMEs are active in almost all of these subsectors, although this analysis focuses on the three mentioned above.

<u>Labor force</u>

Male participation in Jordan's work force is at 64.2% for the entire population (taken from the Human Resource Indicators, 2002), whereas the female rate is only at 12.3%. This figure is especially low; however, recent manufacturing experiences such as the textile industry have been increasing the role of women in the workplace. Meritocracy in Jordan's private companies remains relatively low, as does productivity-linked pay.[6] However, many GOJ, USAID, and other donor technical assistance programs are addressing the need to raise the level of performance and management in Jordanian firms to a world-class standard, both to benefit the local economy, and as a marketing tool to attract foreign investment.

SMEs in Jordan

"Jordan has staked much of its future economic prosperity on the development of a sophisticated network of technology-based SMEs. This comes as no surprise at a time when the country is faced with the twin challenges of anticipating a grim future for its traditional labor-intensive industries….while striving to prevent the 'brain drain' of an increasing number of highly skilled graduates."[7]

Jordan's business sector is dominated by small, family-owned enterprises and medium sized firms that have not been able to transform into larger, more competitive companies. In part, this is due to a conservative commercial banking system that has yet to provide the high level of capital required to generate adequate levels of growth, investment and employment that are needed to offset Jordan's high population growth rate. However, SMEs also have many needs for capacity expansion in the areas of business planning, financial management, accounting, marketing, and other key business skills which must be addressed. As a result,

[4] Ibid.
[5] "Business Plan 2003-2007 for the Jordanian Upgrading and Modernisation Program (JUMP)".
[6] Global Competitiveness Report 2003, Jordan Analysis
[7] "Size Matters: Why SME Financing in Jordan is Inadequate", by Gabi Afram, Business Jordan, April 2005.

with a few exceptions, Jordanian firms lag behind global competitors in the areas of manufacturing, information technology, and financial services. External auditing is not a common practice for the small-sized businesses, and somewhat more common for medium sized firms.

Backward and forward linkages

The nascent National Linkages Program within JUMP is focusing attention on sectors having with the largest capacity to source components and services within the domestic market in Jordan, including: Large Capital Intensive Companies; Heavy Engineering; Electronics and Electrical Appliances; Electrical Engineering; and Construction. These industry sectors require a wide diversity of components and other intermediate inputs, many of which can be supplied by domestic companies a sizeable portion of which in Jordan are SMEs. Experience has shown that SME supplier companies, implementing a program of upgrading for the purpose of making linkages with larger firms, need funding to purchase technology; purchase new equipment; extend premises; and increase working capital. Local commercial banks often impose relatively onerous collateral and other requirements. And prefer to provide project funding through overdraft facilities, rather than long-term debt, so Jordanian firms find it difficult to fund expansions. Most successful backward linkage programs provide some form of preferential access to finance, and the proposed DCA guarantee will help overcome some of those constraints.[8]

Legal & Regulatory Environment / Corporate Governance

According to the World Bank's definition, a country's corporate governance framework "should recognize the rights of stakeholders as established by law and encourage active co-operation between corporations and stakeholders in creating wealth, jobs, and the sustainability of financially sound enterprises. The corporate governance framework should assure that the rights of stakeholders that are protected by law are respected."

Much progress was made in Jordan's regulatory environment in the 1990s, since the creation of the Jordan Securities Commission, the Amman Stock Exchange, and the Securities Depository Center. The powers of each of the three bodies were strengthened by the Securities Law of 2002 and subsequent regulation. The Controller of Companies also plays an important role by enforcing many basic corporate governance provisions of the Company Law. A recent World Bank assessment found little evidence of corporate governance scandal, and relatively good disclosure practices. The development of modern board practices is at an earlier stage, although Jordan is advanced in its early adoption of the institution of the audit committee.

The World Bank's assessment report identifies several key next steps that focus on implementation, including: (i) developing a Code of Corporate Governance that focuses on the role, duties, and functions of the board; (ii) focused enforcement of the disclosure provisions, with continued emphasis on a review of content; (iii) revision of the Company Law to bring the policy framework into greater compliance with the OECD Principles, and (iv) a review of the regulatory jurisdictions of the three main regulatory bodies that oversee corporate governance. Together, these measures will bring Jordan into the mainstream of the

[8] "Analysis and Recommendations for the Establishment of a Backward Linkage Program in Jordan", AMIR, May 2000.

worldwide corporate governance reform movement and provide new opportunities for issuers to implement international good practice.

In bankruptcy, employees have priority over creditors. Creditors can veto capital reductions, and have other rights in line with similar income countries in the region. The bankruptcy framework exhibits heavy court involvement, with both weak creditor and debtor rights, and significant delays, however, outcomes in this area are quite consistent with other economies of the region at similar levels of development.

There are no voluntary codes of practice or recommendations on relations with stakeholders. There is an article in the CL stating that the board of directors will exert their efforts to maximize the wealth and the profit of the company. Stakeholders have no specific right to access information or take part in corporate decision making processes. In their annual report, companies must disclose their organizational structure, hiring policy, number of employees, qualification categories, turn-over ratio, and training programs. Bondholder association rights to information are only vaguely defined in the law. Changes in firm creditor rating are announced promptly as material facts.[9]

Financial Assessment

The Country Credit Rating is taken from *Institutional Investor*. According to *Institutional Investor*, the best rating, 100, would represent the countries with the strongest debt service capacity and the lowest possibility of defaulting on their debt. A rating of 0, the worst rating, would represent countries with the weakest debt service capacity and the greatest possibility of default. In other words, these ratings are proportional to expected collection. Jordan's rating has improved from 38.6 in 2003. In terms of the hard data, Jordan ranks as follows:

Table (7): Country Credit Ratings 2003 (used in 2004 GCR):

Country	Credit Rating
Singapore	86.4
Finland	92.3
Israel	58.0
Iceland	76.3
Jordan	41.2
Taiwan	75.2
Ireland	90.9
Egypt	42.1

Source: Institutional Investor

Jordan scored low on financial sector competitiveness for financial market sophistication (48/104), ease of access to loans (46/104), and most significantly the lack of "venture capital availability" (71/104). Venture capital funds for financing start-ups which are considered high risk projects are almost non-existent – the existing incubator facilities are not venture capital funds so SMEs have extremely limited access to equity capital.[10] Raising capital

[9] "Report on the Observance of Standards and Codes (ROSC)", Corporate Governance Country Assessment, Jordan, World Bank, June 2004
[10] Global Competitiveness Report 2003, Jordan Analysis

through equity or bond markets is not a viable alternative for SMEs in Jordan's still developing capital market environment. (Strauss) Recently the Central Bank of Jordan set out regulation that by 2007 no more than 20% of a bank's portfolio can be in overdraft accounts, thereby the extension of term loans should begin to increase.

Availability of Capital for SMEs

"Many of the country's smallest, youngest, and fastest growing businesses still find it difficult to get sufficient financing".[11] Currently, the majority of lending in Jordan to SMEs is in the form of overdraft accounts. As stated by some private sector banks, their clients prefer overdraft accounts despite higher interest costs because there is no amortization schedule to which they are tied. While most banks have noted that working capital loans are somewhat available to a very limited group of SMEs, overwhelmingly they are hesitant to extend tenors. Most banks noted that 3-year financing to SMEs is extremely restricted, despite having significant liquidity.

Despite its excess liquidity, Jordan's banking sector is dealing with a systemic dearth of long term funds in the system, but it is hoped that a DCA guarantee will stimulate the bank to explore solutions such as the issuance of longer term Certificates of Deposit to correct its asset/liability mismatch to be able to offer longer tenor loans on a sustainable basis. Factors constraining SME access to finance include:

- Information asymmetry – no reliable comprehensive credit reference information system.
- SMEs have opaque financial statements, poor business plans, and limited traditional collateral/security to pledge.
- Very limited medium- and long-term funds in financial system so difficult for banks to lend for SME capital investment.
- Commercial banks are conservative and have focused on large corporate clients and government security investments.
- Limited capacity in the banking sector to properly analyze SME borrowers; evaluate, mitigate, and appropriately price risk.
- The current Jordanian legal environment not conducive to receivables-based financing.

Commercial bank credit is the first external source of capital to which an SME should be able to turn for financing its growing working capital or equipment financing needs. Jordan has the advantage of a relatively healthy banking sector, with numerous banks which are well-established and liquid. These banks are active in lending to the larger corporate sector, in project financing, and in retail lending to individuals, for example via home mortgage lending and other forms of consumer credit which are now growing rapidly. The banks typically invest excess liquidity in Government bills and bonds, and in other investment instruments. There is no lack of loanable funds in the commercial banking sector in Jordan.

[11] "Size Matters: Why SME Financing in Jordan is Inadequate", by Gabi Afram, Business Jordan, April 2005.

However, typical of many developing economies, commercial bank lending to the SME sector is deficient. This lack of lending to SMEs is primarily a reflection of the banks' innate conservatism in asset creation and lack of incentives or inclination to date to develop credit programs aimed at the SME sector. This is in part, but not entirely, a matter of risk appetite on the banks' part. It is also due to a lack of know-how within the banks on the specific techniques used successfully elsewhere in lending to SMEs efficiently and in a way which keeps risks at an acceptable level. [12]

Many sophisticated technology-oriented SMEs that have the highest potential for growth and job creation have extreme difficulty in accessing credit since their core value is intellectual property which is an intangible asset.[13] Receivables financing is also undeveloped in Jordan as a mechanism for expanding access to capital by SMEs. This form of financing requires the acceptance and use by SMEs, their customers and financial institutions, of instruments which represent evidence of debt and sources of cash flow against which a financial institution can provide financing to the SME. The legal environment (enforceability of the instrument against the SMEs customer as well as against the SME) is key to a successful use of receivables financing to expand SME access to capital from this source, turning sales into cash for the SME.[14]

Interest Rates

The private sector is not keen on the interest rate spread banks are making, indicating that when available, loans are expensive for businesses. The banks set the rate based on their break-even point given their demand for loans. The higher the amount of loans supplied, the lower the interest rate is able to fall. Although banks often aggressively advertise to find new clients, given the lack of low-risk loans demanded (and low number of loans given to SMEs with little credit history), banks are unable to lower the rates sufficiently. If a larger volume of credit were disbursed, then the breakeven interest rate could be spread more evenly over those amounts, and therefore the average interest rate would fall.[15]

Table (8): Interest Rate Spread

	1998	2000	2002	2004
Jordan	19/43	44/59	56/102	58/104
Egypt	27/43	21/59	35/102	51/104

Source: Global Competitiveness Report

In terms of ease of access to loans, there are several factors influencing this decision. A large number of SMEs in Jordan, have no financial records. Moreover, many lack the ability to provide a detailed feasibility study when applying for a loan, and with the risk-averse nature of the management of many Jordanian banks, this makes credit access more difficult.

[12] AMIR Program Report, "SME Access to Capital in Jordan", Stephen Strauss, August 2004.
[13] "Size Matters: Why SME Financing in Jordan is Inadequate", by Gabi Afram, Business Jordan, April 2005.
[14] AMIR Program Report, "SME Access to Capital in Jordan", Stephen Strauss, August 2004.
[15] Global Competitiveness Report 2003, Jordan Analysis

CONSTRUCTION

Jordanian SMEs are active in the construction sector and are apt to participate in backward linkages arrangements providing supply to larger domestic purchasers. Real value added for the Jordanian construction sector continued to grow at a slower pace for the second year in a row, as its growth rate amounted to 5.5% for 2003 compared to 8.8% in 2002, attributable to price increases of reinforcement steel and misdistribution of quantities of cement sold, with large contracting companies purchasing large quantities of cement thus reducing the quantities available in the market for smaller contractors.

The number of construction companies registered in 2003 rose by 16 from the year before, to 59 companies. By contrast, their capital dropped sharply from JD 4.3 million in 2002 to JD 2.9 million this year. The number of construction permits issued climbed in 2003 by 5.2% against only 0.9% in 2002, and the licensed building areas increased by 11% compared to 20.3% in 2002. Licensed building areas designated for residential purposes were the majority in 2003 (80%) of the total licensed building areas of 8,108.8 thousand square meters. Credit facilities extended by licensed banks to the construction sector increased in 2003 by 5.2% to JD 804.5 million at the end of the year against an increase of 4.9% during 2002, thus representing 15.3% of the total credit facilities extended by licensed banks.[16]

SWOT Analysis – Construction Sector	
Strengths • Global real estate market is increasing, and national is stable so continuous investment • Basic framework for mortgage lending in place • Iraq situation causing influx of people requiring accommodations and offices	**Opportunities** • Growth in hotel development with tourism increase • Residential building expanding in new Amman developments • Foreign Direct Investment
Weaknesses • Relatively small amount of developable land for either agriculture or industry • Criteria and process for environmental clearance burdensome • Site development approval requires interactions with multiple GOJ agencies • Lack of utilities outside urban areas	**Threats** • Lack of enabling policies and skill sets for proper land valuation • Registration process / ownership regs not attractive to international construction operations

[16] Central Bank of Jordan, Annual Report, 2003.

TOURISM

Tourism is a key driver of Jordan's economy as the single largest employer and the second highest producer of foreign exchange, contributing over JD 600 million in revenue, or a current 7.5% of Jordan's GDP annually. The WTO reports that Jordan is one of the few countries in the Middle East to have recorded growth in tourism, and this growth neared 9.8% in 2002. During the first four months of 2004, the number of tourists visiting Jordan increased by an impressive 43.4% compared to the same period in 2003, comprising visitors from other Arab countries as well as Europeans and Americans. Despite these promising near-term numbers, though, tourism is still viewed as a high-risk venture in Jordan, and lags behind in comparison to other Middle Eastern countries. The WTO indicates that nine of the 30 top emerging destination countries are in the Middle East North Africa region. All of them are Arab countries – but Jordan is not among them.

According economic data in the Central Bank of Jordan 2003 Annual report, the "trade, restaurants and hotels" sector value added grew, at constant basic prices, by 4.5% compared with 2.1% in 2002. As for the tourism sector in particular, its performance was impacted in 2003 by the uncertain conditions in the region, especially in the first half of the year, leading to a reduction in the growth rate of its value added at current prices from 8.6% in 2002 to 3.6% in 2003.

Credit facilities extended by licensed banks to tourism sector declined slightly during 2003 by 0.4% compared with a growth of 1.5% in 2002 to reach JD 172.8 million by the year end, thus representing 3.3% of total credit facilities extended by licensed banks. Similarly, credit facilities extended to this sector by the IDB retracted by 2.1% compared to their level at the end of last year to reach JD 32.9 million at the end of 2003.[17]

SWOT Analysis – Tourism Sector	
Strengths • Four main tourism centers well known • Large number of sites to develop • New National Tourism Strategy • Good internal roads and international airports • Political stability • High domestic and regional Arab country demand	**Opportunities** • New product and site development – adventure tours, cultural and nontraditional tourism, tourism linked to medical services visits and conferences • GOJ efforts to attract FDI • As incomes increase so does environmental protection, thereby increasing tourism appeal • Hotels increasing in number and quality
Weaknesses • Lack of reliable statistical data for planning • International perceptions of regional stability • Lack of skilled labor • Weak promotion and marketing • Limited Foreign Direct Investment (FDI)	**Threats** • Instability in the region causing 2001-like decline in global and regional tourism industry • Natural resource linked – limited water and petroleum, i.e. hotels use significant amounts of water

[17] Central Bank of Jordan, Annual Report, 2003.

INDUSTRIAL SECTOR / GARMENT INDUSTRY

Industry in General

There was a marked slowdown in the industrial sector's performance between 2002 and 2003 but its relative importance to GDP remained at almost the same level - 20.0%. The sector's slump is attributable to the reduction in domestic and external demand for many of the sector's products. The decline in the manufacturing industrial production index has not been uniform, with production indices of food products and beverages, fertilizers, cement, "wearing apparel and textiles", and "detergents and soaps" dropping, and production indices of tobacco products, pharmaceuticals, and refined petroleum products increasing. Production from Qualifying Industrial Zones (QIZs) is comprises part of the value added for manufacturing sector.

Available data show an increase in both the number of registered industrial companies and their capital, with the number of newly registered industrial companies reached 426 with a total paid-up capital of JD 12.5 million in 2003. Credit facilities extended by licensed banks to the industrial sector declined by a narrow margin of 0.6% at the end of 2003, comprising 16.7% of total credit facilities extended by licensed banks. By contrast, credit facilities extended to the industrial sector by the Industrial Development Bank (IDB) increased by 0.7%, compared to their level at the end of 2002 to JD 76.7 million at the end of 2003.[18]

Garment Industry

The targets for the Euro-Jordanian Action for the Development of the Enterprise (EJADA)-produced national strategy and action plan to enhance the competitiveness of the garment industry in Jordan for the period 2004-2010 include: total investments of JD 620 million; jobs created – 88,000, new companies established 1,006, and total exports of JD 2,128 billion. It is assumed that some portion (not defined specifically in their report) of that 1,006 new companies will be SMEs. The national strategy assumes that 60% of the financing needs out of the total required investment would be provided by bank loans. The additional 40% is anticipated to come from equity capital should a number of GOJ tax incentives and other enabling environment factors foster an increase in equity availability.[19]

[18] Central Bank of Jordan, Annual Report, 2003.
[19] "The Financing Strategy, Garment Industry", EJADA.

SWOT Analysis – Garment Industry	
Strengths • Does not require sophisticated technology • Efficient infrastructure and telecommunications available • IT is well promoted and integrated • Export and investment-friendly policy	**Weaknesses** • Shortage of skilled labor • Free zone formulas concentrated on QIZ rather than diversified • Lack of SME-supportive financing policies promoting access • Customs clearance period and inland transit time
Opportunities • EU and US Imports of garments from developing countries • Production costs of Asian countries increasing • Advantages of QIZ agreement include • Possible to export to Europe free of duties for products fully produced in Jordan using local inputs	**Threats** • Dismantling of MFA • Leading exporting countries of garments implementing upgrading programs to increase competitiveness • QIZs having business relations with Israel which could be affected by regional instability • Lack of diversification of exports concentrated toward US market

Recommendations

The DCA guarantee facility should be paired with technical assistance and capacity building to complement both the lender and borrower actors in this guarantee facility to facilitate utilization and ensure that risks in lending to SMEs in particular sectors and industries are mitigated. Loan products will have to be developed by the bank to meet medium term loan demand, and tailored to the specific needs and cashflows of businesses within whichever sector or industry the SME borrower is operating in.

ASSESSMENT OF THE SME SECTOR IN JORDAN
IN PREPARATION FOR A DEVELOPMENT CREDIT AUTHORITY
LOAN PORTFOLIO GUARANTEE

Annex A – Economic Indicators for SME Sectors

Main Indicators of Construction Sector
2000-2003

	2000	2001	2002	2003
Value added at current prices (JD million)	203.3	231.0	251.7	279.3
Growth rate at constant prices (%)	1.1	12.5	8.8	5.5
The deflator of the construction sector (1994=100)	86.1	86.9	87.1	91.6
Outstanding credit facilities extended by licensed banks (JD million)	744.9	728.9	764.9	804.5
Number of registered construction companies	74.0	67.0	43.0	59.0
Capital of registered construction companies (JD million)	4.9	3.5	4.3	2.9
Quantity of cement sales to domestic market (in thousands of tons)	2,188.7	2,417.7	2,656.3	2,774.4
Number of permits (thousand)	17,925	21,248	21,433	22,555
Licensed area for building (thousands of sq.m.)	4,921.5	6,071.9	7,306.8	8,108.8

Sources : - Monthly Statistical Bulletin / Central Bank of Jordan.
- Jordan Cement Factories Company.

Main Indicators of Tourism Sector

2000 - 2003

	2000	2001	2002	2003
Number of arrivals (million)	4.6	5.2	5.5	5.3
Gross tourism income/GDP at current basic prices (%)*	10.0	9.1	9.7	9.4
Value added of tourism sector at current prices (JD million)**	260.0	252.3	274.1	284.0
Value added/GDP at current basic prices (%)	5.1	4.6	4.8	4.6
Outstanding credit facilities extended by licensed banks (JD million)	155.2	171.0	173.5	172.8
Outstanding credit facilities extended by the IDB (JD million)	32.5	33.5	33.6	32.9
Number of hotels	452	472	461	458
Number of rooms (thousand)	17.5	19.2	19.4	19.7
Room occupancy ratio (%)	39.5	30.5	32.0	33.7
Employees in hotels (thousand)	9.8	11.4	10.3	10.5
Employees in tourism sector (thousand)	21.5	22.9	21.5	22.1

Sources : - Monthly Statistical Bulletin / Central Bank of Jordan.
- Ministry of Tourism and Antiquities.
- Industrial Development Bank.

* : Gross tourism income according to the balance of payments data.

** : CBJ estimates.

Main Indicators of the Industrial Sector
2000-2003

	2000	2001	2002	2003
Value added at current prices (JD million)	969.4	1,013.3	1,111.0	1,178.3
Growth rate at constant prices (%)	3.9	5.8	12.3	3.2
The deflator of the industrial Sector (1994=100)	111.7	110.3	107.7	110.7
Industrial exports (JD million)*	964.4	1,216.8	1,415.4	1,518.4
"Mining & quarrying" & manufacturing industrial production index	107.1	120.1	127.6	116.2
Number of registered industrial companies	315	384	358	426
Capital of registered industrial companies (JD million)	8.5	7.6	6.7	12.5
Outstanding credit facilities extended by licensed banks (JD million)	784.1	806.3	885.1	879.4
Outstanding credit facilities extended by the IDB (JD million)	88.4	80.4	76.2	76.7

Sources : - Monthly Statistical Bulletin / Central Bank of Jordan.
- Industrial Development Bank.

* Domestic exports excluding agricultural exports.

**ASSESSMENT OF THE SME SECTOR IN JORDAN
IN PREPARATION FOR A DEVELOPMENT CREDIT AUTHORITY
LOAN PORTFOLIO GUARANTEE**

Annex B – Resources Used

i. USAID Documents (listed chronologically)

- AMIR Program Report, "Analysis and Recommendations for the Establishment of a Small Enterprise Component in the National Linkage Program in Jordan", David Lovegrove, October 2004.
- AMIR Program Report, "National Linkages Program Communication Strategy", September 2004.
- AMIR Program Report, "SME Access to Capital in Jordan", Stephen Strauss, August 2004.
- AMIR Program Report, "Jordanian Partner Evaluation/Selection & Mini Sub-Sector Analyses and Selection", Alison Hong, May 2004.
- AMIR Program Report, "National Linkages Program Design Update", The Services Group, January 2004.
- AMIR Program Report, "Investment Promotion Sectoral Strategy 2004-2006: Garment Sector", Al-Jidara Investment Services, November 2003.
- AMIR Program Report, "Jordan Investor Targeting Strategy 2003, An Assessment of Jordan's Competitiveness in Attracting FDI Relative to other Middle East/North African Countries", Charles Krakoff and Al-Jidara Investment Services, July 2003.
- AMIR Program Report, "The 2002 Investor Roadmap of Jordan", The Services Group (TSG) and Al-Jidara Investment Services, December 2002.
- AMIR Program Report, "Analysis and Recommendations for the Establishment of a Backward Linkage Program in Jordan", The Services Group (TSG), May 2000.
- AMIR Program Report, "Investor Promotion Strategic Plan and Investor Service Guidelines", The Services Group (TSG), June 1998.

ii. EJADA Documents (listed chronologically)

- Strategy and Action Plan to Enhance the Competitiveness of The Garment Industry in Jordan", Final Report, Tahar Ben Amor, December 2002.
- "The Financing Strategy, Garment Industry", EJADA.

iii. Ministry of Planning and International Cooperation Documents (listed chronologically)

- "Jordan's Competitiveness Book, Confronting the Competitiveness Challenge", Ministry of Planning and International Cooperation, Jordan National Competitiveness Team, 2003.

iv. Other Documents (listed chronologically)

- "Size Matters: Why SME Financing in Jordan is Inadequate", by Gabi Afram, Business Jordan, April 2005.
- Central Intelligence Agency Factbook, Jordan, 2005.
- "Report on the Observance of Standards and Codes (ROSC)", Corporate Governance Country Assessment, Jordan, World Bank, June 2004.
- Central Bank of Jordan, Annual Report, 2003.
- "Business Plan 2003-2007 for the Jordanian Upgrading and Modernisation Program (JUMP)".
- "USFTA Opportunities Survey", Jordan United States Business Partnership (JUSPB), December 2001.
- Global Competitiveness Report 2003, Jordan Analysis found at http://www.competitiveness.gov.jo/.

Required Lending Institution(s) Information for USAID Development Credit Authority Loan Portfolio Guarantee Facility Assessment

1. CVs of senior management team (principal officers and directors)
2. Organization chart
3. List of registered owners by name and percentage of ownership (if publicly listed, note % held by public)
4. Present, past use of DCA guarantee, if any (N/A)
5. Audited financial statements (with footnotes) and annual reports for past three years, plus most recent interim financial report. Please see #11.
6. Three to five year business plan, if available
7. Rating by a recognized rating agency, if available
8. CAMEL rating/analysis by the central bank, if available
9. Additional information as requested by the Risk Management Team per specifics of the project
10. Detailed description of the lender's asset quality classification policies.
11. In addition, please fill in the following tables if applicable, if this information is not available in the audited financial statements of the bank:

Classification*	2004	2003	2002
Gross loans			
a. Performing			
b. Special Mention			
Total performing loans (a + b)			
c. Sub-standard			
d. Doubtful			
e. Loss			
Total non-performing loans (c + d + e)			
Accrued interest as % of total non-performing loans			

*If the lender uses a different set of classification standards than those above, please provide a breakout of performing and non-performing loans per the lender's classification standards.

Information reported to central bank	2004	2003	2002
Risk-weighted assets			
Capital adequacy ratio (CAR)			
Liquidity ratio			

Activity Schedule for Completing DCA LPG for BOJ SME Lending

Details	Date	Status	Comments
Mission Prepares Concept Paper	February 6, 2005	Completed and Approved by ODC RM	
Mission (through AMIR) prepares DCA analyses and initiaties discussion with RLA (USAID/Jordan Legal Officer)	April 17 - April 30	Underway	
Sample Termsheet Drafted	April 17 - April 30	Completed and being presented to BOJ Sr. Mgmt. on May 2	with ODC RM on April 25. Further modified by the incorporation of BOJ comments on April 26.
Mission (through AMIR) prepares Action Package	April 17 - April 30	Underway	Will be finalized for Mission by no later than April 30
ODC RM sending Jerry subsidy cost estimate to include in CN	April 26, 2005	Completed for $10 million non-revolving facility	This may be modified should the ceiling or revolving nature of the facility change
Program Officer from Mission Prepares Congressional Notification and submits	April 28, 2005	Underway	
Bank of Jordan sending AMIR entire package of FI information for Risk Assessment	April 28, 2005		
Bank of Jordan Senior Management Meeting will provide approval in principle for BOJ Jordan facility	May 2, 2005		
Mission will review Action Package and Monitoring Plan and forward to ODC RM	May 4, 2005		
All Risk Assessment materials will be handed over to USAID/ODC in Washington	May 4, 2005		Financial Institution information and Borrower Research for LPGs.
Paul Freedman, in consultation with Jerry and Legal Officer, negotiate legal agreement in Washington with BOJ	May 10, 2005		Mr. Hamdan, Assistant GM of BOJ will be in Washington, DC May 4 - 17.
ODC Prepares Risk Assessment and final Subsidy Calculation	May 15, 2005		It is anticipated that the risk assessment will be completed off-site as a desk review.
CRB receives entire completed Action Package one week prior to meeting	May 26, 2005		
CRB Reviews Action Package and Recommends Approval	June 2, 2005		
CFO Approves Subsidy Cost	June 9, 2005		
Funding Transfer Occurs	June 15, 2005		
Certifications and legal opinions on lender related to AML / Anti-terrorism and drug financing	July 15, 2005		
Guarantee Agreement Signed and Project Obligated	July 1, 2005		

SAMPLE USAID GUARANTEE TERM SHEET – SME LENDING[1]

GUARANTEE PURPOSE: The USAID Guarantee is intended to stimulate term and working capital financing for small and medium-sized enterprises (SMEs) in Jordan. Such financing will include up to the Jordanian Dinar equivalent of Ten Million U.S. Dollars ($10,000,000) in loans disbursed by Bank of Jordan (herein referred to as the "Bank".) The USAID Guarantee is backed by the full faith and credit of the United States Government.

PARTIES TO GUARANTEE AGREEMENT: The Guarantee Agreement shall be entered into between the Bank and USAID.

1. Maximum Authorized Amount. The aggregate principal amount of loans that may be lent by the Bank and partially guaranteed by USAID shall not exceed the Jordanian Dinar equivalent of Ten Million U.S. Dollars ($10,000,000).

2. USAID Guarantee Percentage. Fifty Percent (50%) of the Bank's net loss of principal.

3. Guarantee Ceiling (Maximum USAID liability). The Jordanian Dinar equivalent of Five Million U.S. Dollars ($5,000,000).

4. Term of Loan Portfolio Guarantee. 8 years.

5. Claim Requirements. No claim under the USAID Guarantee shall be honored unless the Bank certifies to USAID and USAID thereafter reasonably determines that all of the following requirements are met:

(a) The entire amount or a portion of the loan has become due, and the Borrower has failed to pay such principal amount;
(b) The Borrower has failed to meet the Bank's written demand for repayment of the principal amount due on the loan within thirty (30) days of receipt of the demand;
(c) The Bank has pursued reasonable collection efforts in accordance with applicable law and standard commercial practice in Jordan; and
(d) After such collection activities, the Guaranteed Party has either (i) certified to USAID that it has written off the entire outstanding balance (including principal and interest) of the Qualifying Loan as a bad debt expense, or (ii) certified to USAID that it (A) is unable, because of a legal impediment or significant impracticality, to take the action described in (i) above, and (B) has established a specific provision of funds (which is evidenced on its balance sheet or income statement) for possible loan losses associated with the default by the Defaulting Borrower, and the amount of such provision equals or exceeds 20% of the amount of defaulted principal.

6. **Post-Claim Reimbursement Requirements**. After USAID has paid a claim with respect to the guaranteed loans, the Bank shall continue to pursue reasonable collection activities against the Borrower and shall reimburse USAID 50% of such post-claim recoveries, after deducting its reasonable expenses incurred in collection efforts and accrued and unpaid interest on the Loans.

7. **USAID Guarantee Fees.**

(a) **Origination Fee**. One and one-quarter percent (1.25%) of the Guarantee Ceiling (which is $62,500). This fee is payable by the Bank under the terms of a Guarantee Commitment Agreement between the Bank and USAID.
(b) **Utilization Fee**. One percent (1%) of the outstanding principal amount that is guaranteed by USAID. This fee shall be payable semi-annually on guaranteed portion of the total amount outstanding under coverage on the portfolio.

8. Qualifying Borrowers. Small- and medium-sized enterprises (SMEs) operating in Jordan. SMEs are defined by USAID/Jordan as enterprises with 5 to 250 employees. It is anticipated maximum loan size will be 354,000 Jordanian Dinars (USD $500,000), and maximum loan term will be 60 months. For loans over this size, the Bank may petition USAID for a justified exception. Currency of loans will be matched to the currency of revenue generated by the borrower, including Jordanian Dinars, US Dollars, and Euros.

[1] This term sheet is for discussion purposes only and does not represent a binding commitment from USAID.

SAMPLE LETTER OF INTENT FOR USAID DCA LPG

[On Bank of Jordan Letterhead]

April 24, 2005

Mr. Khush Choksy
Component Manager
Financial Markets Development
Achievement of Market-Friendly Initiatives and Results (AMIR) Program
Salem Center, Sequleyah Street, Al-Rabiyeh
P.O. Box 940503 Amman 11194 Jordan
kchoksy@amir-jordan.org

Dear Mr. Choksy:

Pursuant to our ongoing discussions with USAID/Jordan and the AMIR Program, Bank of Jordan would like to formally confirm its interest in participating in a USAID Development Credit Authority (DCA) Loan Portfolio Guarantee Facility to offer partial risk coverage for lending to small and medium-sized enterprises (SMEs).

Bank of Jordan has a long-term strategic interest in expanding our lending to SMEs, as demonstrated by the attendance of our Credit Officers at the FOR-Jordan Bank Training Program, our ongoing engagement of a European Union-funded SME Finance Advisor, and our preliminary SME business strategy prepared with this Advisor's assistance. Additionally, Bank of Jordan is eager to begin lending to SMEs in West Bank under a new DCA Loan Portfolio Guarantee with USAID/West Bank and Gaza.

We believe a USAID DCA Loan Portfolio Guarantee will assist us in increasing our lending to SMEs in Jordan and complement our overall efforts to move into this market in a systematic way.

We look forward to collaborating with USAID/Jordan and AMIR to develop the guarantee facility, and to engaging new SME bank clients through this program.

Sincerely,

Mohammed Anwar Hamdan
Assistant General Manager

Comparison of USAID Development Credit Authority Loan Portfolio Guarantee Facility with EJADA Loan Guarantee Program

1. Partial Risk Coverage

USAID: USAID's DCA Facility will share 50% of the Bank's net loss of principal in a pari pasu arrangement, for loans to SMEs meeting Qualifying Borrower criteria. (see Sample Term Sheet). For post-claim recoveries, the Bank may reimburse USAID 50% of recoveries after deducting its reasonable expenses incurred in collection efforts, and accrued and unpaid interest on the Loans.

EJADA: EJADA's guarantee will cover 70% of the Bank's net loss of principal.

2. Qualifying Borrowers

USAID: Small- and medium-sized enterprises (SMEs) operating in Jordan in any sector, defined by USAID/Jordan as enterprises with 5 to 250 employees. SME Borrowers may be receiving technical assistance from any programs in Jordan including, but not limited to the National Linkages Program (NLP), FOR-Jordan, Jordanian-US Business Partnership (JUSBP), EJADA. The Bank may also lend to SMEs that are not participating in any technical assistance programs as long as they meet the other basic criteria.

EJADA: SMEs employing 5 to 250 people, in the manufacturing and services sectors only, excluding retailing, property development, securities investment, and banking. SMEs must have participated in EJADA's SME strengthening technical assistance program.

3. Loan Size and Terms

USAID: It is anticipated maximum loan size will be 354,000 Jordanian Dinars (USD $500,000), and maximum loan term will be 5 years. For loans over this size, the Bank may petition USAID for a justified exception. There is no minimum size or minimum term. Currency of loans will be matched to the currency of revenue generated by the borrower, including Jordanian Dinars, US Dollars, and Euros.

EJADA: Loan range is JD 28,500 - 428,500 ($605,000). Loan terms are between 3 and 8 years.

4. Facility Ceiling

USAID: The aggregate principal amount of loans that may be lent by the Bank and partially guaranteed by USAID shall not exceed the Jordanian Dinar equivalent of Ten Million U.S. Dollars ($10,000,000). This ceiling is for Bank of Jordan only and is not being shared among other banks.

EJADA: Euro 24 million ceiling is shared across 16 banks in Jordan, with Bank of Jordan's portion of that being below $10 million.

5. Fees

USAID: The USAID DCA facility requires that Bank of Jordan pay an origination fee one time upon the activation of the facility, and a utilization fee on the guaranteed portion of the outstanding amount. The fees as proposed in the illustrative term sheet are included below, and these fees are subject to negotiation between USAID and Bank of Jordan.

(a) **Origination Fee**. One and one-quarter percent (1.25%) of the Guarantee Ceiling (which is $62,500). This fee is payable by the Bank under the terms of a Guarantee Commitment Agreement between the Bank and USAID.
(b) **Utilization Fee**. One percent (1%) of the outstanding principal amount that is guaranteed by USAID. This fee shall be payable semi-annually on guaranteed portion of the total amount outstanding under coverage on the portfolio.

EJADA: Bank of Jordan is required to pay a fee up to 1.5% per annum of the value of its outstanding loan guarantee. Currently Bank of Jordan is paying a 1% utilization fee.

6. Credit Approval Process

USAID: Credit analysis, due diligence and credit decisions are undertaken by the bank according to their standard Credit Policies and Procedures. Loans are placed under coverage at the time of disbursement, and must meet criteria for Qualifying Borrowers.

EJADA: Credit analysis, due diligence, and credit approvals are undertaken in close coordination on a loan-by-loan basis with EJADA. EJADA has the final approval on credit decisions.

USAID DCA Loan Portfolio Guarantee for SME Lending
Bank of Jordan
Summary of Anticipated Guarantee Parameters

- Maximum Cumulative Disbursements: $10,000,000
- Guarantee Ceiling: $5,000,000
- Duration of Guarantee: 8 years
- Final Year of Loan Disbursement Under Coverage: Year 7
- Expected Interest Rate: 8 – 12% (will vary by currency)
- Currency of Loans Placed Under Coverage: JD, USD, Euro
- Estimated Number of Loans: 50
- Estimated Average Loan Maturity: 4 years
- Estimated Average Loan Size: USD 200,000

SAMPLE LETTER OF INTENT FOR USAID DCA LPG

[On Standard Chartered Jordan Letterhead]

April 24, 2005

Mr. Khush Choksy
Component Manager
Financial Markets Development
Achievement of Market-Friendly Initiatives and Results (AMIR) Program
Salem Center, Sequleyah Street, Al-Rabiyeh
P.O. Box 940503 Amman 11194 Jordan
kchoksy@amir-jordan.org

Dear Mr. Choksy:

Pursuant to our ongoing discussions with USAID/Jordan and the AMIR Program, Standard Chartered Jordan would like to formally confirm its interest in participating in a USAID Development Credit Authority (DCA) Loan Portfolio Guarantee Facility offering partial risk coverage for lending to small and medium-sized enterprises (SMEs).

We believe a USAID DCA Loan Portfolio Guarantee will assist us in increasing our lending to SMEs in Jordan and complement our broader efforts to move into this market in a systematic way.

We look forward to collaborating with USAID/Jordan and AMIR to develop the guarantee facility, and to engaging new SME bank clients through this program.

Sincerely,

Christopher Knight
Chief Executive, Levant

Developing a USAID Guarantee for SME Lending with Standard Chartered
Illustrative Process and Timeline

Week of May 16, 2005

Standard Chartered Risk Manager from Dubai to meet with Khush Choksy, Component Manager, Financial Markets Development, AMIR program.

May to August 2005

Standard Chartered conducting market research and developing SME lending strategy.

August 15, 2005

Expected finalization date of SME lending strategy. Standard Chartered will share strategy, which will remain in confidence, with USAID and AMIR Program. Discussions will continue and a working definition will be established for the specific subset of qualifying SME borrowers the bank intends to use the guarantee coverage for.

September 2005

- Development of the loan portfolio guarantee parameters; agreement on process moving forward; concurrence reached on guarantee ceiling, intended use of guarantee coverage, qualifying borrowers; Action Package (the document initiating the guarantee process) prepared and submitted to USAID/Jordan.

- <u>Letter of Intent</u>: Standard Chartered should send a letter indicating interest and commitment to lending to SMEs and participating in a USAID guarantee facility. A sample letter of intent is attached that should be tailored to reflect the bank's interests in using the guarantee coverage.

- <u>Term Sheet</u>: USAID/AMIR will draft an illustrative term sheet for discussion purposes with Standard Chartered. A very preliminary template version is attached.

- <u>Required Documentation</u>: Standard Chartered will collect the standard set of required information required from all banks participating in a USAID guarantee facility (attached). Most of this information can be taken from your annual report although some may need to be synthesized from other reports.

- Legal Agreement Negotiated

November 2005

Guarantee is activated, and loans may be placed under coverage.

SAMPLE USAID GUARANTEE TERM SHEET – SME LENDING[1]

GUARANTEE PURPOSE: The USAID Guarantee is intended to stimulate term and working capital financing for small and medium-sized enterprises (SMEs) in Jordan. Such financing will include up to the Jordanian Dinar equivalent of X Million U.S. Dollars ($X) in loans disbursed by Standard Chartered Jordan (herein referred to as the "Bank".) The USAID Guarantee is backed by the full faith and credit of the United States Government.

PARTIES TO GUARANTEE AGREEMENT: The Guarantee Agreement shall be entered into between the Bank and USAID.

1. Maximum Authorized Amount. The aggregate principal amount of loans that may be lent by the Bank and partially guaranteed by USAID shall not exceed the Jordanian Dinar equivalent of X Million U.S. Dollars ($X).

2. USAID Guarantee Percentage. Fifty Percent (50%) of the Bank's net loss of principal.

3. Guarantee Ceiling (Maximum USAID liability). The Jordanian Dinar equivalent of (½ above) U.S. Dollars ($X).

4. Term of Loan Portfolio Guarantee. X years.

5. Claim Requirements. No claim under the USAID Guarantee shall be honored unless the Bank certifies to USAID and USAID thereafter reasonably determines that all of the following requirements are met:

(a) The entire amount or a portion of the loan has become due, and the Borrower has failed to pay such principal amount;
(b) The Borrower has failed to meet the Bank's written demand for repayment of the principal amount due on the loan within thirty (30) days of receipt of the demand;
(c) The Bank has pursued reasonable collection efforts in accordance with applicable law and standard commercial practice in Jordan; and
(d) After such collection activities, the Guaranteed Party has either (i) certified to USAID that it has written off the entire outstanding balance (including principal and interest) of the Qualifying Loan as a bad debt expense, or (ii) certified to USAID that it (A) is unable, because of a legal impediment or significant impracticality, to take the action described in (i) above, and (B) has established a specific provision of funds (which is evidenced on its balance sheet or income statement) for possible loan losses associated with the default by the Defaulting Borrower, and the amount of such provision equals or exceeds 20% of the amount of defaulted principal.

6. **Post-Claim Reimbursement Requirements**. After USAID has paid a claim with respect to the guaranteed loans, the Bank shall continue to pursue reasonable collection activities against the Borrower and shall reimburse USAID 50% of such post-claim recoveries, after deducting its reasonable expenses incurred in collection efforts and accrued and unpaid interest on the Loans.

7. **USAID Guarantee Fees.**

(a) **Origination Fee**. Between 0.5-2% of the Guarantee Ceiling (which is $X). This fee is payable by the Bank under the terms of a Guarantee Commitment Agreement between the Bank and USAID.
(b) **Utilization Fee**. Between 0.5-2% of the outstanding principal amount that is guaranteed by USAID. This fee shall be payable semi-annually on guaranteed portion of the total amount outstanding under coverage on the portfolio.

8. Qualifying Borrowers. Small- and medium-sized enterprises (SMEs) operating in Jordan. SMEs are defined by USAID/Jordan as enterprises with 5 to 250 employees. It is anticipated maximum loan size will be X Jordanian Dinars (USD $X), and maximum loan term will be X months. For loans over this size, the Bank may petition USAID for a justified exception. Currency of loans will be matched to the currency of revenue generated by the borrower, including Jordanian Dinars, X, and X.

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[1] This term sheet is for discussion purposes only and does not represent a binding commitment from USAID.

Annex B
Short Term Consultancy Agreement Scope of Work

Activity Name: 636.08 Development Credit Authority (DCA)
SOW Title: F/Preparation of Concept Papers
Modification No: Original
SOW Date: Wednesday, March 23, 2005
SOW Status: Draft
Task and Consultant Name:
F/ Preparation of Concept Papers
CA Caroline Averch

I. Specific Challenges Addressed by this Consultancy

The Financial Markets Development (FMD) Initiative under AMIR 2.0 strives to strengthen Jordan's financial markets by leveraging unused capital for developing and modernizing financial institutions. This includes the development of new financial products that would facilitate the extension of credit by banks to SMEs.

USAID's Development Credit Authority (DCA) is a tool to leverage limited donor funds and build local private sector financial institutions in developing countries. DCA catalyzes domestic investment by offering loan guarantees that foster access to credit and longer term sustainable funding sources for financially viable development projects. In countries constrained by a lack of appropriate financial products, services, and markets, USAID's DCA is a key to unlock local credit markets, and limited donor funds are augmented by the unlimited potential of the private sector. DCA is the legal authority that allows USAID missions to issue partial loan guarantees to private lenders. In turn, these guarantees provide a way to encourage local capital funding of projects. DCA allows USAID to provide the most appropriate mixture of grant and credit assistance to achieve a particular development goal. By offering a guarantee on up to 50 percent of a lender's risk on loans made to single or multiple borrowers, the DCA encourages private lenders to extend financial services to credit-worthy but underserved markets. It also encourages those lenders to offer longer loan terms; reduce collateral requirements; lend at market-based interest rates; and, invest on a sustainable basis in local development efforts in lieu of or in addition to USAID and other donors. The DCA mechanism requires true private sector risk sharing with the lenders providing loans using their own capital. USAID also receives tremendous budget leverage with the actual cost to missions averaging 5 to 10 cents for every dollar loaned by a private bank. DCA is an extremely flexible mechanism and includes four different tools to enhance credit in a broad variety of situations and environments. These tools include loan guarantees, portable guarantees, loan portfolio guarantees, and bond guarantees.

USAID/Jordan and the AMIR Program are reviewing the possibility of using a DCA guarantee to enhance bank lending to SMEs that are involved in export related activities either directly or as suppliers to larger export related entities. USAID/Jordan and the AMIR Program have met several banks that may be potentially interested in lending to SMEs in a manner that is new to Jordan. As the lack of extension of credit to SMEs by banks is a serious impediment to the development of the SME sector in Jordan, the additionality coming from a DCA Guarantee could have a significant positive development impact.

The challenge of this consultancy is to meet with two to four banks that have expressed a serious interest in using the proposed DCA facility and work with them in designing a DCA portfolio guarantee program that would extend credit to SMEs.

II. Objective

The objective of this consultancy is to assist banks, the AMIR Program and USAID/Jordan in advancing the various inputs required for the DCA credit enhancement for the planned portfolio guarantee program.

III. Specific Tasks of the Consultant

Under this Scope of Work, the Consultant(s) shall perform, but not be limited to, the tasks specified under the following categories:

A. **Background Reading Related to Understanding the Work and Its Context**. The Consultant shall read, but is not limited to, the following materials related to fully understanding the work specified under this consultancy:

- Annual Reports of the following Banks:
    - Standard Chartered Bank
    - Export and Finance Bank
    - Bank of Jordan
    - Cairo Amman Bank
- Any reports by credit rating agencies or other investment banks reports on:
    - Standard Chartered Bank
    - Export and Finance Bank
    - Bank of Jordan
    - Cairo Amman Bank
- Information on the National Linkage Program.
- Chemonics International Inc., SME Access to Capital in Jordan Final Report, August 2004.
- Any other related material

B. **Background Interviews Related to Understanding the Work and Its Context**. The Consultant shall interview, but is not limited to, the following individuals or groups of individuals in order to fully understand the work specified under this consultancy:

- Standard Chartered Bank
- Export and Finance Bank
- Bank of Jordan
- Cairo Amman Bank
- USAID/Jordan.
- USAID (DCA Office)
- AMIR Program.
- Other organizations and individuals as deemed necessary.

C. **Tasks Related to Accomplishing the Consultancy's Objectives**. The Consultant shall use his/her education, considerable experience and additional understanding gleaned from the tasks specified in A. and B. above to:

- Meet with USAID/Jordan and AMIR Program to discuss the development objectives involved with using the DCA guarantee to enhance credit extension to SMEs.

- Meet with USAID/Jordan and other State/USAID Projects to discuss any potential areas of collaboration between the DCA program and work of the consultant and other State Department/USAID Projects.

- Meet with the banks that have been identified as potential DCA lenders and work together with the banks, AMIR Program and USAID/Jordan to prepare a DCA action package for the loan portfolio program. This will include details on the intended use by banks, portfolio guarantee facility size and duration.

The substance of, findings on, and recommendations with respect to the above mentioned tasks shall be delivered by Consultant in a written report in the format described in sections IV., V., and VI. Of Annex A – Standard Short Term Consultancy Agreement Information.

IV. Time frame for the Consultancy. Unless otherwise specified in writing, the time frame for this consultancy is specified by the expenditure start and end dates shown in Annex C.

V. LOE for the Consultancy. The days of level of effort are allocated by location in Annex C.

Consultant ___________________ Chemonics __________________

Annex C

Scope of Work Level of Effort Allocation

As of 03/23/2005

Project Action:	F/Preparation of Concept Papers
Action Number:	3151
Scope Of Work:	F/Preparation of Concept Papers
Scope Number:	1389
Description:	The objective of this consultancy is to assist banks, the AMIR Program and USAID/Jordan in advancing the various inputs required for the DCA credit enhancement for the planned portfolio guarantee program.
SOW Start Date:	04/25/2005
SOW End Date:	05/25/2005
Scope of Work Document:	No Document
Last Uploaded:	

Level of Effort

Name	**Start**	**End**	**US**	**Field**	**3rd**	**Travel**	**Total**
Caroline Averch	04/25/2005	05/25/2005	2	12	0	2	16

Consultant ____________________ Chemonics ___________________

USAID's Development Credit Authority

Overview and Applications for Jordan

April 25, 2005

The Credit Challenge

Banks in developing countries and many emerging markets have a low level of financial intermediation:

- Mobilization of deposits and investment capital is limited and not put to productive use.
- Banks hold much of their portfolio in liquid, extremely low-risk assets (i.e. government T-bills).
- Underdeveloped Capital Markets preclude long-term investment, and lead to limited and prohibitively expensive term loans, consumer credit, mortgage lending, and student loans.

One Solution to the Credit Challenge

DCA mobilizes local capital and encourages private financial institutions to:

- reduce their excess liquidity and provide access to credit to underserved markets.
- improve capacity to assess and manage risk.
- provide longer term lending.
- reduce inappropriate collateral requirements.
- offer market-based interest rates.
- invest in local development efforts in lieu of and/or in addition to USAID and other donors.

DCA Overview

•**Guarantees**: DCA allows USAID to issue partial loan guarantees to private sector lenders, pledging to cover the lender's risk of borrower default up to 50% of loan principal.

•**Another Tool**: DCA is an additional tool like contracts or grants, to advance USAID Mission SOs or other USAID development objectives.

DCA Overview

Leverage: DCA projects represent public-private partnerships and leverage substantial private sector resources – historic ratios have averaged 25:1.

- USAID sets aside a loan loss reserve between 3-9% of the guarantee facility value to cover potential claims.
- The guaranteed party pays a commitment fee (.5-2%) and a utilization fee (.25-2%) to offset this amount.
- A $10 million guarantee facility could cost a USAID Mission approximately $400,000 =
  $1 USAID: $25 private sector lending its own money.

Rationale for DCA

•Enhances the Impact of development programs through cost-effectiveness and additionality.

•Offers a Private Sector led Sustainability Strategy: private local capital investing in local development initiatives provides an exit strategy for projects and USAID Missions.

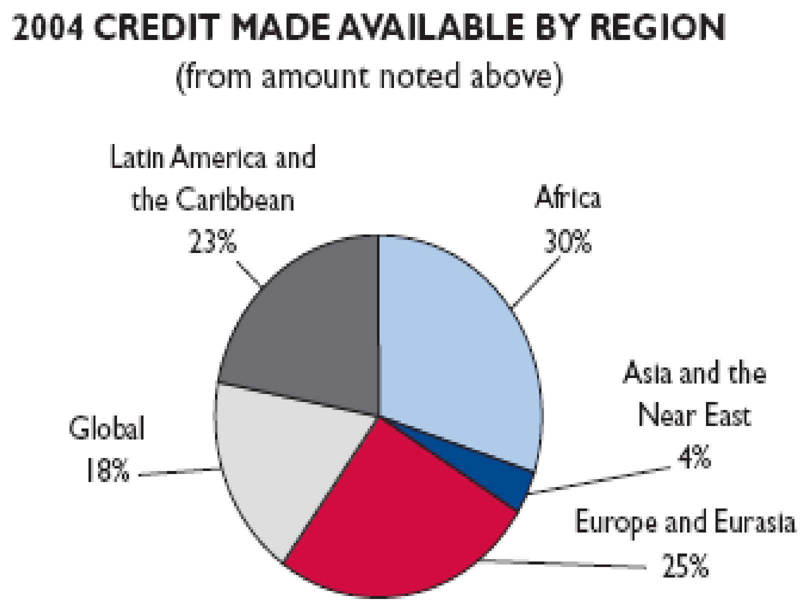
•Engages the private sector in a symbiotic and cost-effective partnership model, contributing to GDA goals.

•Provides a demonstration effect to lenders that development projects / borrowers are creditworthy and a profitable market.

•As more lenders enter the market, competition leads to better terms for borrowers.

Summary of 2004 Guarantees

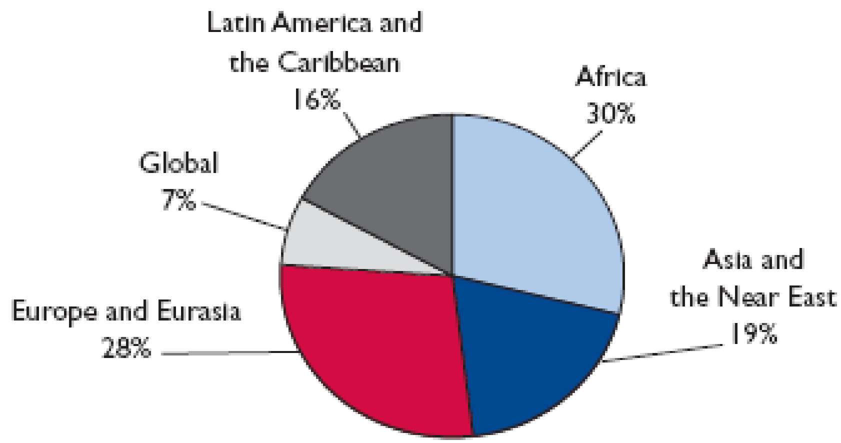
- Number of Guarantees: 36
- Total Credit Made Available: $278,733,334
- Amount Guaranteed: $102,916,667
- Cost to USAID: $10,285,880
- Number of Countries: 22



Entire DCA Portfolio: 1999-2004

- Number of Guarantees: 114
- Total Credit Made Available: $855,799,334
- Amount Guaranteed: $335,249,667
- Cost to USAID: $28,106,780
- Number of Countries: 36

TOTAL CREDIT MADE AVAILABLE BY REGION
(from amount noted above)



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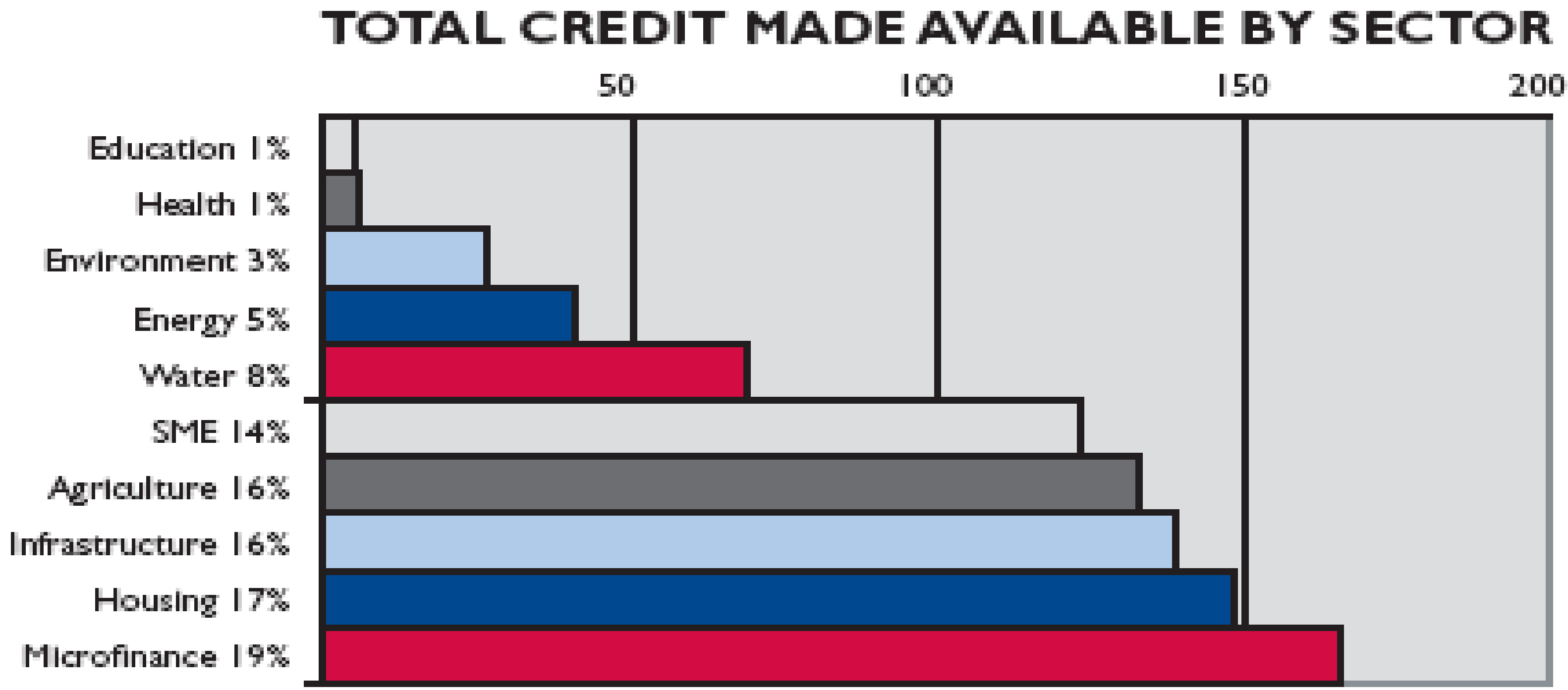
Total DCA Usage by Sector



DCA Guiding Principles

Mission Driven: DCA is a demand-driven initiative. USAID Missions and Bureaus have primary responsibility for designing, authorizing and implementing activities that support development objectives.

Support for SOs. DCA must be used for activities in support of USAID Strategic Objectives (it is part of a Mission's overall strategy and often done in conjunction with TA and policy reform efforts).

DCA Guiding Principles

Where can it be used? DCA is available for all USAID-presence countries (with a few exceptions), and all sectors in which USAID works.

True Private Sector Risk-Sharing. USAID covers no more than 50% of a lender's risk, with at least half of the default risk covered by a private sector lender.

- Reduces Moral Hazard
- Leverages Resources of Local Banks

Private Sector Only. Borrowers and lenders must be non-sovereign.

Financial Viability. Each activity funded under DCA must be financially viable (i.e. sufficient cash flows to meet all operational costs and service all the debt).

DCA Guiding Principles

Market Imperfections. DCA will be used to address market imperfections. Assistance shall be made at market rates so as not to distort existing financial markets.

Additionality. DCA must not be used unless it is probable that the transaction would not go forward without it, taking into consideration whether such financing is available for the term needed and at a reasonable cost.

Demonstration Effect: DCA seeks to demonstrate to local banks that the new lending is profitable and thus to encourage future lending without guarantees.

DCA Guarantees May Not…..

•Guarantee other donor-backed funds or guarantee facilities such as EJADA's SME guarantee facility, rediscounted government credit lines, or EBRD SME credit lines.

•Guarantee sovereign debt.

•Provide guarantees in countries that do not yet have a country risk rating like East Timor.

•Guarantee equity investments – DCA can only enhance debt instruments (loans, bonds, debt securities, etc.). But it can guarantee a loan to a socially responsible investment fund.

•Guarantee financing for illegal activities per standard USAID regulations.

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DCA – 4 Flexible Tools

DCA’s flexibility allows structuring to enhance credit in a broad variety of situations and environments:

- Loan Portfolio Guarantee
- Bond Guarantee
- Loan Guarantee
- Portable Loan Guarantee

Guarantee Facilities range from <$1 - $100 million.

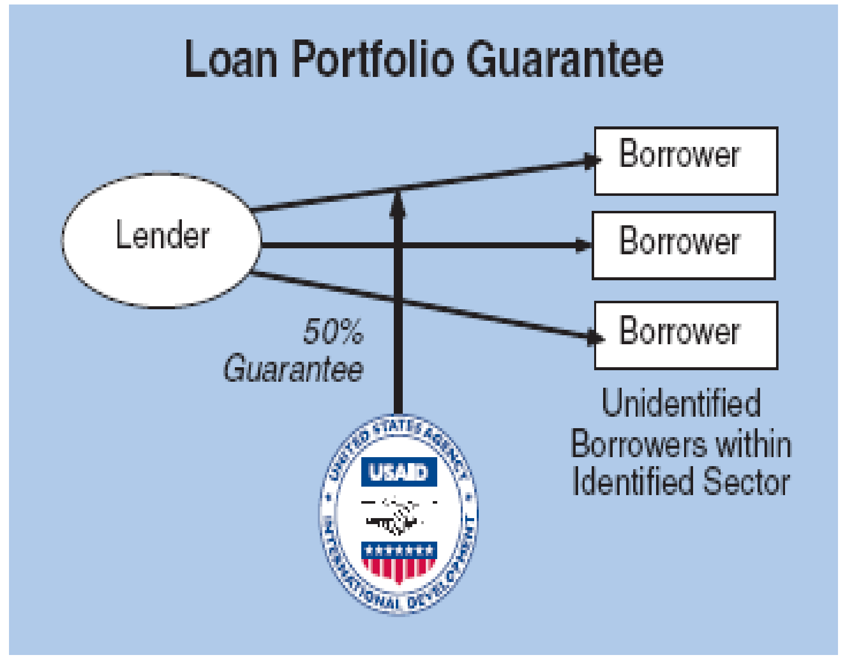
Loan Portfolio Guarantee (LPG)

Jordan

Type: Loan Portfolio Guarantee

Amount: $10,000,000
(Jordanian Dinar equivalent)

Purpose: Provides a financial institution with a guarantee on multiple loans made to SMEs in all sectors in all geographic areas.



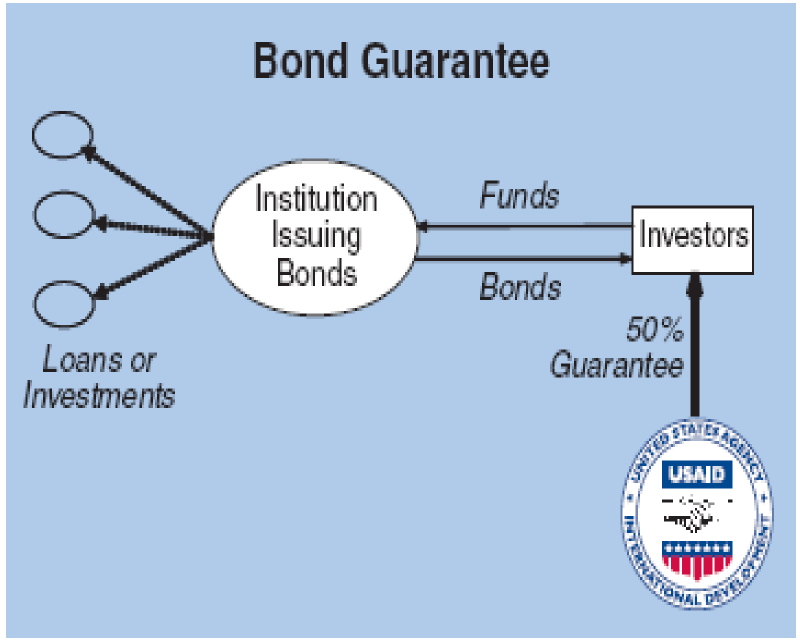
Bond Guarantee (BG)

India

Type: Bond Guarantee

Amount: $6,400,000 (Indian Rupee equivalent)

Purpose: Provides a partial bond guarantee for a pooled funding vehicle to finance water infrastructure projects in 7 small municipalities.



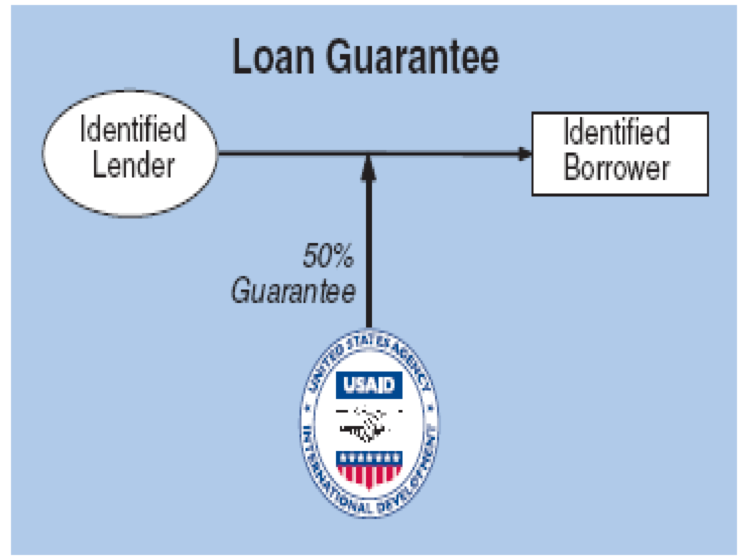
Loan Guarantee (LG)

South Africa

Type: Loan Guarantee

Amount: $4,800,000
(SA Rand equivalent)

Purpose: Provides a financial institution with a guarantee for a construction loan to a private company building mixed use housing / retail space in inner-city Joburg open to all socio-economic brackets.



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Portable Guarantee (PG)

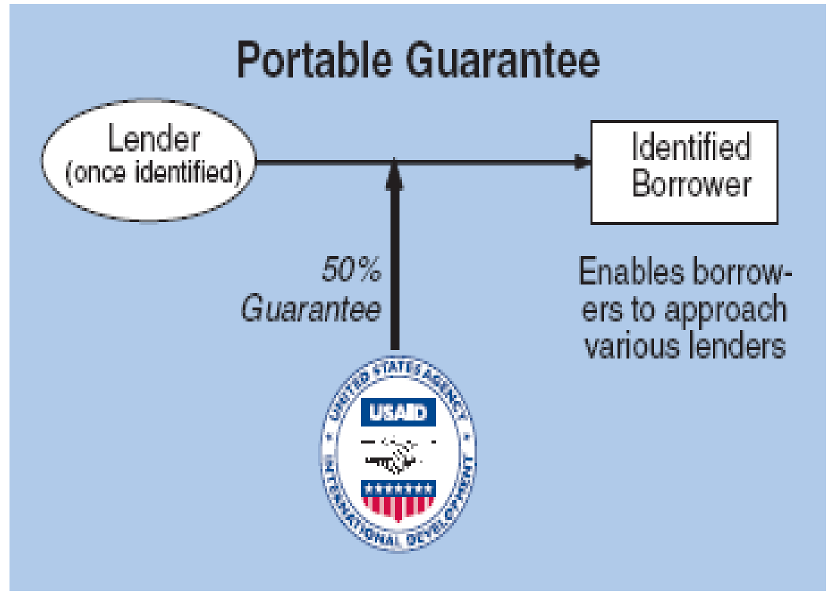
Morocco

Type: Portable Guarantee

Amount: $1,000,000
(Moroccan Dirham equivalent)

Guarantee Ceiling: $500,000

Purpose: Increase an MFI’s capital, enabling it to provide additional financing to micro-enterprises in Morocco. The MFI can select from any lender with a minimum credit rating.



DCA Applications for Jordan

- **SME:** Increasing SME access to finance – LPG
- **Private Sector Development:** Stimulating finance for competitive sectors like ICT, Tourism, etc. – LPG or LG for larger companies
- **Capital Markets**: Enhancement for new instruments or new users of standard instruments, supporting the development of secondary markets for housing finance, securities, etc. – BG
- **Water:** wastewater treatment, irrigation, potable water and sewerage infrastructure – all structures
- **Municipal (local gov.) Finance:** Water, energy, housing, transportation, public works – all structures
- **Housing:** Support for primary and secondary markets to increase home ownership – all structures
- **Education:** Increasing access to student loans – LPG
- **Health:** Increasing lending and equipment leasing for clinics, hospitals, midwives - LPG or LG

What Constitutes Success?

- Guarantee facilities are used – Loans are made and lenders learn about a new market.
- Credit ratings and credit histories established.
- Borrowers in target sectors, market segments able to access credit without a guarantee.
- Competition and diversity in financial products and services leads to more affordable credit.
- Liquidity in the financial sector absorbed – banks, pension funds, insurance companies investing.
- Financially viable projects are being financed by the private sector as the norm.

Meetings for Carrie Averch

Monday: April 18, 2005

Name	Title	Institution	Email Address	Tel. No.	Time
Mr. Khush Choksy Mr. Brad Fusco Ms. Asma Abu-Taleb Ms. Suhair Khatib	FMD Team Leader ECI Team Leader FMD Business Operations Advisor Business Development Services Subcomponent Manager/ECI	AMIR Program AMIR Program AMIR Program AMIR Program	kkchoksy@amir-jordan.org bfusco@amir-jordan.org aabutaleb@amir-jordan.org skhatib@amir-jordan.org	550 3050	09:30 am.
Mr. Mohammed Hamdan Mr. Khush Choksy Mr. Brad Fusco Ms. Asma Abu-Taleb Ms. Suhair Khatib	Assistant General Manager FMD Team Leader ECI Team Leader FMD Business Operations Advisor Business Development Services Subcomponent Manger/ECI	Bank of Jordan AMIR Program AMIR Program AMIR Program AMIR Program	mhamdan@bankofjordan.com.jo	569 6123	10:30 am.
Mr. Steve Wade	Program Director	AMIR Program	swade@amir-jordan.org	550 3050	3:00 pm.

Tuesday: April 19, 2005

Name	Title	Institution	Email Address	Tel. No.	Time
Mr. Rashad Bibars		FMI – FOR-Jordan Project *Meeting at AMIR Office			10:00 am
Mr. Mohammed Hamdan Mr. Khush Choksy Ms. Suhair Khatib	Assistant General Manager FMD Team Leader BDS Subcomponent Manager/ECI	Bank of Jordan	mhamdan@bankofjordan.com.jo	569 6123	11:00 am
	Credit Manager – Commercial Lending Division Credit Officers	Bank of Jordan			12:00 pm

Wednesday: April 20, 2005

Name	Title	Institution	Email Address	Tel. No.	Time
Mr. Christopher Knight Mr. Khush Choksy Ms. Suhair Khatib	Chief Executive, Levant FMD Team Leader Business Development Services Subcomponent Manger/ECI	Standard Chartered Bank AMIR Program AMIR Program	Christopher.Knight@jo.standardchartered.com	560 7201	10:00 am.
Mr. Brendan Russell	Component Manager, Financial Support Schemes	EJADA	http://www.ejada.jo/services/financial/index.htm		11:30am
Mr. Ali Al-Husary Ms. Asma Abu-Taleb Ms. Suhair Khatib	Chairman & CEO FMD Business Operations Advisor Business Development Services Subcomponent Manger/ECI	Export and Finance Bank AMIR Program AMIR Program	ali@efbank.com.jo	510 0200	01:00 pm.
Dr. Jim Barnhart Mr. Jamal Al-Jabiri Mr. Don Richardson Mr. Jerry Florkowski Mr. Steve Wade Mr. Khush Choksy Mr. Brad Fusco	Director, Economic Opportunities Office Cognizant Technical Officer Senior Private Sector Advisor Deputy Financial Management Officer Program Director FMD Team Leader ECI Team Leader	USAID AMIR Program AMIR Program AMIR Program	jbarnhart@usaid.gov JAl-jabiri@usaid.gov drichardson@usaid.gov jflorkowski@usaid.gov	590 6625	02:15 pm.

Thursday: April 21, 2005

Name	Title	Institution	Email Address	Tel. No.	Time
Holiday					

Sunday: April 24, 2005

Name	Title	Institution	Email Address	Tel. No.	Time
Suhair Brad Nahla Riyad Rima Mohammed		National Linkages Program *Meeting at AMIR Office			10:00 am

Monday: April 25, 2005

Name	Title	Institution	Email Address	Tel. No.	Time
	DCA Presentation for AMIR, JUSBP, other USAID contractors, Water Office	AMIR Program (Citadel)			9:00 am.
Khush Choksy	Telecon with Alison Eskesen, ODC Relationship Manager for USAID/Jordan and Jerry Florkowski	AMIR Program		(202) 712-5323	4:30 pm.

Tuesday: April 26, 2005

Name	Title	Institution	Email Address	Tel. No.	Time
Mr. Mohammed Hamdan Mr. Khush Choksy Mr. Brad Fusco	Assistant General Manager FMD Team Leader ECI Team Leader	Bank of Jordan AMIR Program AMIR Program	mhamdan@bankofjordan.com.jo	569 6123	10:00 am.
Mr.		Standard Chartered Bank		560 7201	04:00 pm. at AMIR

Wednesday: April 27, 2005

Name	Title	Institution	Email Address	Tel. No.	Time
Mr. Steve Wade Mr. Brad Fusco Mr. Khush Choksy	Program director ECI Team Leader FMD Team Leader	AMIR Program AMIR Program AMIR Program		550 3050	03:00 pm.

Thursday: April 28, 2005 (Presentation to USAID/Jordan)

Name	Title	Institution	Email Address	Tel. No.	Time
Ms. Anne Aarnes	Mission Director	USAID		590 6625	10:00 am.
Dr. Jim Barnhart	Director, Economic Opportunities Office		jbarnhart@usaid.gov		
Mr. Jamal Al-Jabiri	Cognizant Technical Officer		JAl-jabiri@usaid.gov		
Mr. Don Richardson	Senior Private Sector Advisor		drichardson@usaid.gov		
Mr. Jerry Florkowski	Deputy Financial Management Officer		jflorkowski@usaid.gov		
Mr. David Barth	USAID Lawyer				
Mr. Steve Wade	Program Director	AMIR Program			
Mr. Khush Choksy	FMD Team Leader	AMIR Program			
Mr. Brad Fusco	ECI Team Leader	AMIR Program			

Annex B
Short Term Consultancy Agreement Scope of Work

Activity Name: 636.08 Development Credit Authority (DCA)
SOW Title: F/Credit Review Board Meeting Preparation
Modification No: Original
SOW Date: Thursday, April 28, 2005
SOW Status: Final
Task and Consultant Name: F/Credit Review Board Meeting Preparation
CA Caroline Averch

I. Specific Challenges to be Addressed by this Consultancy

The Financial Markets Development (FMD) Initiative under AMIR 2.0 strives to strengthen Jordan's financial markets by leveraging unused capital for developing and modernizing financial institutions. This includes the development of new financial products that would facilitate the extension of credit by banks to SMEs.

USAID's Development Credit Authority (DCA) is a tool to leverage limited donor funds and build local private sector financial institutions in developing countries. DCA catalyzes domestic investment by offering loan guarantees that foster access to credit and longer term sustainable funding sources for financially viable development projects. In countries constrained by a lack of appropriate financial products, services, and markets, USAID's DCA is a key to unlock local credit markets, and limited donor funds are augmented by the unlimited potential of the private sector. DCA is the legal authority that allows USAID missions to issue partial loan guarantees to private lenders. In turn, these guarantees provide a way to encourage local capital funding of projects. DCA allows USAID to provide the most appropriate mixture of grant and credit assistance to achieve a particular development goal. By offering a guarantee on up to 50 percent of a lender's risk on loans made to single or multiple borrowers, the DCA encourages private lenders to extend financial services to credit-worthy but underserved markets. It also encourages those lenders to offer longer loan terms; reduce collateral requirements; lend at market-based interest rates; and, invest on a sustainable basis in local development efforts in lieu of or in addition to USAID and other donors. The DCA mechanism requires true private sector risk sharing with the lenders providing loans using their own capital. USAID also receives tremendous budget leverage with the actual cost to missions averaging 5 to 10 cents for every dollar loaned by a private bank. DCA is an extremely flexible mechanism and includes four different tools to enhance credit in a broad variety of situations and environments. These tools include loan guarantees, portable guarantees, loan portfolio guarantees, and bond guarantees.

USAID/Jordan and the AMIR Program met with several banks to discuss an SME loan portfolio guarantee. Bank of Jordan and Standard Chartered Bank emerged as the two most likely banks as they are in the process of establishing a comprehensive SME lending program.

Consultant ___________________ Chemonics __________________

At the current time, the AMIR Program and USAID/Jordan have decided to focus on only the Bank of Jordan as a candidate for a DCA loan portfolio guarantee in the immediate future, given the USAID/Jordan timetable for preparing the action package and obtaining the subsidy cost approval. Standard Chartered Bank is in the process of putting together a SME strategy and we will continue a dialogue with them.

The challenge of this consultancy is to work with the AMIR Program, USAID/Jordan and the USAID/DCA Office in Washington, D.C. to finalize the Bank of Jordan action package and monitoring plan and assist USAID/Jordan in preparing for the Credit Review Board meeting.

II. Objective of this Consultancy

The objective of this consultancy is to assist the AMIR Program and USAID/Jordan in finalizing the DCA Guarantee for the Bank of Jordan and participating in the Credit Review Board Hearing.

III. Specific Tasks of the Consultant

Under this Scope of Work, the Consultant(s) shall perform, but not be limited to, the tasks specified under the following categories:

A. **Background Reading Related to Understanding the Work and Its Context**. The Consultant shall read, but is not limited to, the following materials related to fully understanding the work specified under this consultancy:

- DCA Concept Paper prepared for Bank of Jordan.
- Bank of Jordan and other information for risk assessment.
- USAID Guarantee Term sheet for SME lending by Bank of Jordan.
- SME sector reports and other information provided by EJADA Program and JUSBP.
- National Linkages Program Information.
- Any other related material

B. **Background Interviews Related to Understanding the Work and Its Context**. The Consultant shall interview, but is not limited to, the following individuals or groups of individuals in order to fully understand the work specified under this consultancy:

- Bank of Jordan, (Via telephone and in person)

- USAID/Jordan, (Via telephone)
- USAID/Office of Development Credit (ODC)
- AMIR Program, (Via telephone)
- Other organizations and individuals as deemed necessary.

C. **Tasks Related to Accomplishing the Consultancy's Objectives**. The Consultant shall use his/her education, considerable experience and additional understanding gleaned from the tasks specified in A. and B. above to:

- Support and facilitate USAID/Jordan's finalization of the Action Package and help coordinate its submission to the ODC Relationship Manager.

- Finalize Monitoring Plan for USAID/Jordan and submit for final Mission approval and forwarding to the ODC Relationship Manager.

- Facilitate Washington-based meetings related to finalization of the Risk Assessment, negotiation of the legal agreement, and related topics.

- Assist USAID in preparing for the Credit Review Board Meeting.

- Participate in Credit Review Board Meeting as required.

The substance of, findings on, and recommendations with respect to the above mentioned tasks shall be delivered by Consultant in a written report in the format described in sections IV., V., and VI. Of Annex A – Standard Short Term Consultancy Agreement Information.

IV. Time frame for the Consultancy. Unless otherwise specified in writing, the time frame for this consultancy is specified by the expenditure start and end dates shown in Annex C.

V. LOE for the Consultancy. The days of level of effort are allocated by location in Annex C.

VI. Consultant Qualifications. The Consultant shall have the following minimum qualifications to be considered for this consultancy:

<u>Educational Qualifications</u>

- Bachelor or Master degree in business of finance

Work Experience Qualifications

- Work experience related to USAID credit enhancements and SME Finance. At least two years of experience related to USAID DCA guarantees.

Annex C

Scope of Work Level of Effort Allocation

As of 05/18/2005

Project Action:	F/Credit Review Board Hearing Preparation
Action Number:	5466
Scope Of Work:	Credit Review Board Hearing Preparation
Scope Number:	2381
Description:	The objective of this consultancy is to assist the AMIR Program and USAID/Jordan in finalizing the DCA Guarantee for the Bank of Jordan and participating in the Credit Review Board Hearing.
SOW Start Date:	05/05/2005
SOW End Date:	06/05/2005
Scope of Work Document:	(120) 636.08_Credit Review Board Hearing Preparation _F1_042805_CA.doc
Last Uploaded:	28 Apr 2005 09:28

<u>Level of Effort</u>

Name	Start	End	US	Field	3rd	Travel	Total
Ms. Caroline Averch	05/05/2005	06/05/2005	10	0	0	0	10

Consultant ___________________ Chemonics __________________