



**Microfinance Investment Support Facility  
for Afghanistan (MISFA)**

**and**

**Ministry of Finance**

**and**

**Italian Ministry of Foreign Affairs**

**General Directorate for Development Cooperation**

**Project revision**

**Italian Support to Afghan Microfinance and Enterprises  
In Herat**

**ISAME Project**

**AFGHANISTAN**

**November 2014**

## REVISED PROJECT DOCUMENT

<b>Country:</b>	Afghanistan
<b>Project Title:</b>	Italian Support to Afghan Microfinance and Enterprises in Herat Province – (ISAME Project)
<b>Donor:</b>	Government of Italy
<b>Project Number:</b>	AID 9309
<b>Duration</b>	Three years
<b>Starting Date:</b>	October 18, 2014
<b>Completion Date:</b>	October 17, 2017
<b>Institutional counterpart:</b>	Afghan Ministry of Finance
<b>Executing Agency:</b>	Microfinance Investment Support Facility for Afghanistan (MISFA)
<b>Total Funding:</b>	Original budget disbursed: Euro 6,400,000 Total balance to date: Euro 5,688,819 Equivalent to AFN 392,202,689

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## ACRONYMS

<b>ACGF</b>	Afghanistan Credit Guarantee Foundation
<b>AFN</b>	Afghani (Currency)
<b>ANDS</b>	Afghanistan National Development Strategy
<b>ARI</b>	Acute Respiratory Infection
<b>CDC</b>	Community Development Councils
<b>CHW</b>	Community Health Worker
<b>DAIL</b>	Directorate of Agriculture Irrigation and Livestock
<b>DDA</b>	District Development Assemblies
<b>DFI</b>	Development Financial Institution
<b>DoWA</b>	Directorate of Women Affairs
<b>FINCA</b>	Foundation for International Community Assistance
<b>FMFB</b>	First Microfinance Bank
<b>GoIRA</b>	Government of the Islamic Republic of Afghanistan
<b>HFL</b>	Hope for Life (MFI)
<b>KfW</b>	Kreditanstalt für Wiederaufbau, meaning <i>Reconstruction Credit Institute</i>
<b>IFAD</b>	International Fund for Agricultural Development
<b>IP</b>	Implementing Partners
<b>ISAME</b>	Italian Support to Afghan Microfinance and Enterprise
<b>MAIL</b>	Ministry of Agriculture, Irrigation, and Livestock
<b>MUTAHID</b>	Development Finance Institution
<b>MFI</b>	Microfinance Institution
<b>MISFA</b>	Microfinance Investment Support Facility for Afghanistan
<b>MoF</b>	Ministry of Finance
<b>M&amp;S</b>	Monitoring and Supervision
<b>MRRD</b>	Ministry of Rural Rehabilitation and Development
<b>NABDP</b>	National Area-Based Development Program
<b>NATEJA</b>	Non Formal Approach to Training and Education in Afghanistan
<b>NGO</b>	Non-Governmental Organization
<b>NSDP</b>	National Skills Development Program
<b>NSP</b>	National Solidarity Program
<b>OXUS</b>	Microfinance & Development
<b>PAR</b>	Portfolio at Risk
<b>PRA</b>	Participatory Rural Appraisal
<b>SARD</b>	Support to Agriculture and Rural Development
<b>SME</b>	Small & Medium Enterprise
<b>TUP</b>	Targeting the Ultra-Poor
<b>VFU</b>	Veterinary Field Unit

## ABSTRACT

In March 2011 the Ministry of Finance of the Islamic Republic of Afghanistan (MoF) and the Microfinance Investment Support Facility for Afghanistan (MISFA) entered into an agreement to implement the Italian Support to Afghan Microfinance and Enterprises (ISAME) project.

The overall objective of the project was to contribute to poverty and social inclusion of the population in Herat, Farah, and Badghis provinces through the improvement of the microfinance sector.

However the microfinance and SME market in the Western region started declining since the project was first proposed. There were only a few microfinance organizations in Herat with the capacity to properly disburse loan funds and there were no service providers in the other two target provinces of the project, Farah and Badghis. In addition, one of the leading microfinance institutions, BRAC, with a significant footprint in the Western region of Afghanistan, had to exit the sector due to its portfolio quality and operational management issues.

As a result ISAME project intervention has been limited only to microfinance component through the MFI OXUS, training activities and operative costs for a total amount spent of Euro 833.061 out of a total disbursed budget of Euro 6.4 Mil.

In order to reactivate the ISAME Project, MISFA and MOF propose to align the Project revision with a program financed by the World Bank “Access to Finance”, which include a component defined “**Targeting the Ultra Poor**” (TUP). This new component has been first funded by IFAD and successfully piloted by MISFA in Bamyan and Badakhshan provinces.

MISFA will build synergies and coordination between IFAD, World Bank and Italian Development Cooperation, all funding TUP projects. The same procurement process will be conducted for all projects and there will be close oversight and quality control over all TUP activities. The households will be targeted under similar selection criteria that are available in the Operational Manual developed jointly by MISFA and the World Bank and give priority to women households.

The revision of the ISAME Project document includes the following main issues:

- The revised Project will have three components, such as:
  - Targeting Ultra Poor (TUP)
  - Microfinance
  - Small & Medium Enterprises (SME)

The first component, TUP is a new one, while the other two components were already part of the original ISAME Project.

Regarding the **microfinance** component, MISFA will operate through MFI partners including, FMFB, **OXUS**, **Muthaid** and **FINCA**. This increase in operative MFI partners will create the conditions to invest the allocated funds within the proposed Project duration.

Regarding the SME component, the commercial First Microfinance Bank (**FMFB**) is one of few banks specialized in financing SMEs window. A SME Credit Guarantee Facility has been implemented and managed by **DEG** (German Investment Corporation) in support to FMFB. Thus SME clients requesting loans to FMFB will benefit of this extra support of a Credit Guarantee Facility by DEG, including clients financed through ISAME funds. Other partners including OXUS, Mutahid, and FINCA have either established SME Departments or receiving TA and other support from MISFA to establish SME Departments. They will also utilize ISAME funds to disburse SME loans to their clients.

- The project will be implemented only in Herat province. Considering the precarious security conditions and the absence of operating MFIs in the other Provinces of the Western Region, the intervention will be geographically focused only on the Province of Herat, both urban and rural areas.
- The duration of the Project will be over the coming three years with expiry date on 17 October 2017.
- The total balance of the Project budget is in the amount of 392,202,689 AFN equivalent to approximately Euro 5,688,819.

All the innovations proposed for each of the three components (TUP, microfinance, SMEs) would create the conditions to achieve the Project objectives by the support to very vulnerable people through a comprehensive package including productive assets such as livestock, unbankable people through microfinance and small traders and producers through loans to SMEs.

The ISAME project may create links with other interventions of the Italian Development Cooperation in Herat province such as: Support to Agriculture and Rural Development (SARD), National Solidarity Program (NSP), National Area-Based Development Program (NABDP), projects in women vocational training implemented by Italian NGOs, Support to milk-dairy cooperatives and the Non Formal Approach to Training and Education in Afghanistan (NATEJA) program.

## **PROJECT DOCUMENT**

### **1. INTRODUCTION**

MISFA was established in 2003 at the invitation of the Afghan government — to get donor coordination right from the start and avoid the counter-productive efforts that have emerged from conflicting donor objectives in other post-conflict situations. It is the first facility of its kind, pooling diverse donor funding mechanisms and converting them into streamlined, flexible support to microfinance institutions (MFIs) in Afghanistan, tailored to local priorities and accompanied by technical assistance and strong performance monitoring.

MISFA is an apex institution to pool diverse donors funding mechanisms and to offer a streamlined flexible support to MFIs in Afghanistan. In 2006 MISFA was transformed into a not for profit company owned by the Ministry of Finance (MoF) and governed by an independent board of directors nominated by Afghan government and donors.

In March 2011 the Ministry of Finance of the Islamic Republic of Afghanistan (MoF) and the MISFA entered into an agreement to implement the Italian Support to Afghan Microfinance and Enterprises (ISAME) project. The overall objective of the project was to contribute to poverty and social inclusion of the population in Herat, Farah, and Badghis provinces through the improvement of the microfinance sector.

However the implementation challenges for the ISAME project began to reveal right after completion of its first year when one of the leading microfinance institutions with a significant footprint in the Western region of Afghanistan, the target region for ISAME, had to exit the sector due to its portfolio quality and operational management issues. The microfinance and SME market in the western region was also declined since the project was first proposed. There were only a few microfinance organizations in Herat with the capacity to properly disburse loan funds

and there were no service providers in the other two target provinces of the project, Farah and Badghis.

To ensure timely completion of the project, MISFA first suggested reallocation of the approved funds and then revision to the scope of the project, changing its focus from only three provinces in the western region to a nation-wide program. This has not been possible to agree and therefore the Parties decided to explore alternative solutions.

As a result of the recent discussions held between MoF, Italian Development Cooperation Office (IDCO) and MISFA, the ISAME Project document is hereto revised in line with the following main issues:

- The project will be implemented only in Herat province. Considering the precarious security conditions and the absence of operating MFIs in the other Provinces of the Western Region, the intervention will be geographically focused only on the Province of Herat, both urban and rural areas.
- The duration of the Project will be over the coming three years with expiry date on 17 October 2017.
- The total balance of the Project budget is in the amount of 392,202,689 AFN equivalent to approximately Euro 5,688,819.
- The revised Project will have three components, such as:
  - Targeting Ultra Poor
  - Microfinance
  - Small & Medium Enterprises

The first component, Targeting Ultra Poor is a new one, while the other two components were already part of the original ISAME Project.

## **2. GENERAL CONTEXT**

### **2.1 The Microfinance sector in Afghanistan**

The microfinance institutions and banks have the potential to provide increased access to finance Micro Small Enterprises (MSEs) and to Small and Medium Enterprises (SMEs) respectively, but the underdevelopment and the fragility of the financial system in Afghanistan have prevented them to do so on a significant scale.

In Afghanistan the banking sector is still fragile and underdeveloped and SMEs remain financially underserved. Only few banks have specialized SMEs financing window, mostly the commercial First Microfinance Bank (FMFB), which has a strong SME Department focusing on the SME market segment.

A SME Credit Guarantee Facility (with initial funding from USAID and the German Government) has been operating in Afghanistan since 2006 and is showing promising results. This Credit Guarantee Facility has been implemented and managed by DEG (German Investment Corporation), a German Government-owned development financial institution, part of KfW banking group.

According to the World Bank “Access to Finance” Project: “From 2003-08, growth of the microfinance sector was steady with 373,080 active borrowers (and around 450,000 clients) reported by March 2008 and a cumulative US\$204 million of loans disbursed by MISFA’s 16 microfinance partners. During that period, the main focus was to scale outreach of MFIs. The

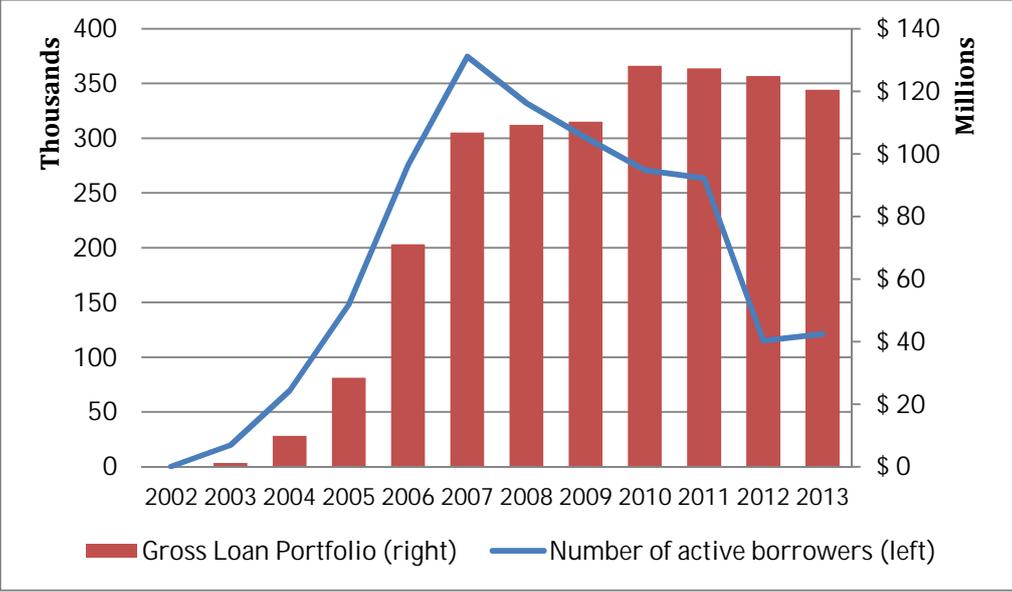
microfinance experience in Afghanistan was considered a unique success as it had managed to build a microfinance sector from scratch in five years.

However, the extremely rapid growth of the sector with fragile institutions led to a repayment crisis in 2008 (which is not unique to Afghanistan and also happened in countries such as Nicaragua, Bosnia and Herzegovina and Pakistan). The rapid client outreach had come at the expense of proper due diligence in lending, compliance with internal control processes and internal monitoring of performance. These factors, combined with cost inflation and a deteriorating security environment, contributed to a decline in portfolio quality of most MFIs.

Following this crisis, MISFA focused more attention on direct monitoring and supervision of MFIs to verify the accuracy of their reporting and supported a consolidation of the sector, as it appeared that a number of small MFIs were not viable. As of 2011, from the initial MISFA partner institutions, 2 of the weakest institutions exited the sector, 1 merged with FMFB – a sister organization, 2 institutions remained in country, but discontinuing as MISFA partners, 6 of the small MFIs had their operations merged into Mutahid (a new entity created by MISFA), 5 MFIs remained as independent institutions: FMFB, BRAC, ASA, Oxus and HFL.

However, in 2012, it emerged that BRAC and ASA had serious difficulties, which led to their exit (by March 2013) of the sector. MISFA currently has four partner MFIs: FMFB (which is a commercial bank), Oxus, HFL and Mutahid, representing 148,111 clients and 81,970 borrowers with US\$93.4 million in loans outstanding<sup>1</sup>. Figure 1 below shows the evolution of the microfinance sector (represented by MISFA partners) between 2003 and 2012. The sharp contraction in the number of clients in 2012 is caused by the exit of the microfinance sector of BRAC”.

**Figure 1: Evolution of Afghan microfinance sector 2003-2013**



Source: MISFA and AMA

MISFA has been working to strengthen its institutional capacity to serve the development finance sector based on the lessons learned from the recent issues at the sector. A 22 performance standards for partner institutions were developed and a dedicated monitoring and supervision department was established at MISFA to provide monitoring and supervision of its loans and grants to partners. Each assessment of partner institution is followed by developing of an action plan to be implemented by the partners. MISFA’s team conducts quarterly follow-up on implementation of the action plans. Partners are now required to hire only Central Bank approved

<sup>1</sup> FMFB is the leading institution, representing 88 percent of clients and loans outstanding.

audit firms to do their annual financial audits. Pre loan/grant disbursement assessment of partner institutions have now been institutionalized at MISFA. Grants to partners are earmarked for certain activities and disbursements are subject to partners’ meeting the agreed upon targets and benchmarks. MISFA currently has four active partners. The First Microfinance Bank, OXUS Afghanistan, Mutahid Development Finance Institution and Hope for Life Microfinance Afghanistan. MISFA is currently finalizing its funding agreement with FINCA, increasing the number of its partners to five. With the current set of few strong development finance partners and introduction of additional controls at MISFA and the partners, MISFA shall be able to properly manage its donor funds in the country.

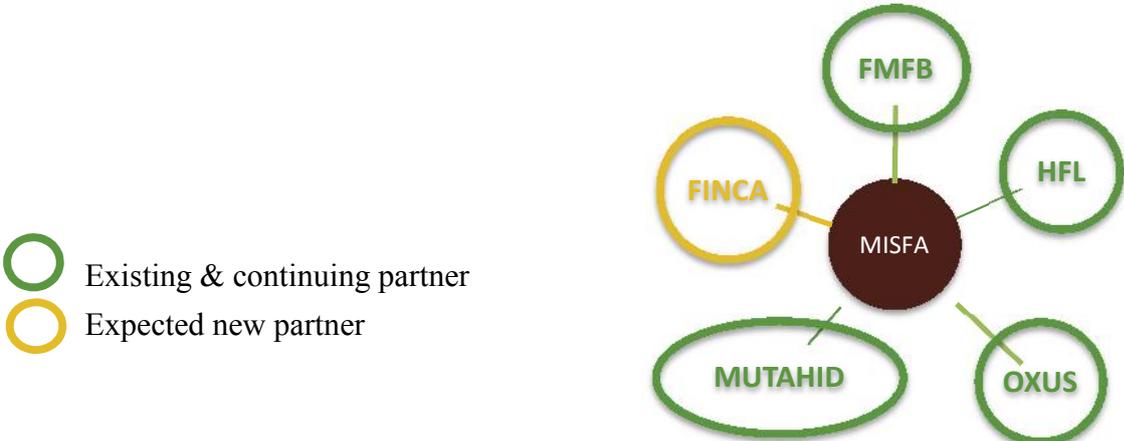
As of June 30, 2014, MISFA partners have a total of 144,332 active clients in 14 out of 34 provinces. The outstanding loan portfolio stands at 4.9 billion Afghanis (AFN), funding 80,866 active borrowers. Seventy three percent of the total borrowers are in urban and twenty seven percent in rural areas, where 23% of the total borrowers are women. The portfolio at risk more than 30 days (PAR>30 days) of the partner institutions is in the range of 2.5 percent, compared with the globally accepted PAR of 5 percent. About 21 percent of microfinance clients are women. The partner financial institutions provide services both in urban and rural areas through 60 branches with a total of 1,668 employees.

**2.2 Project Context**

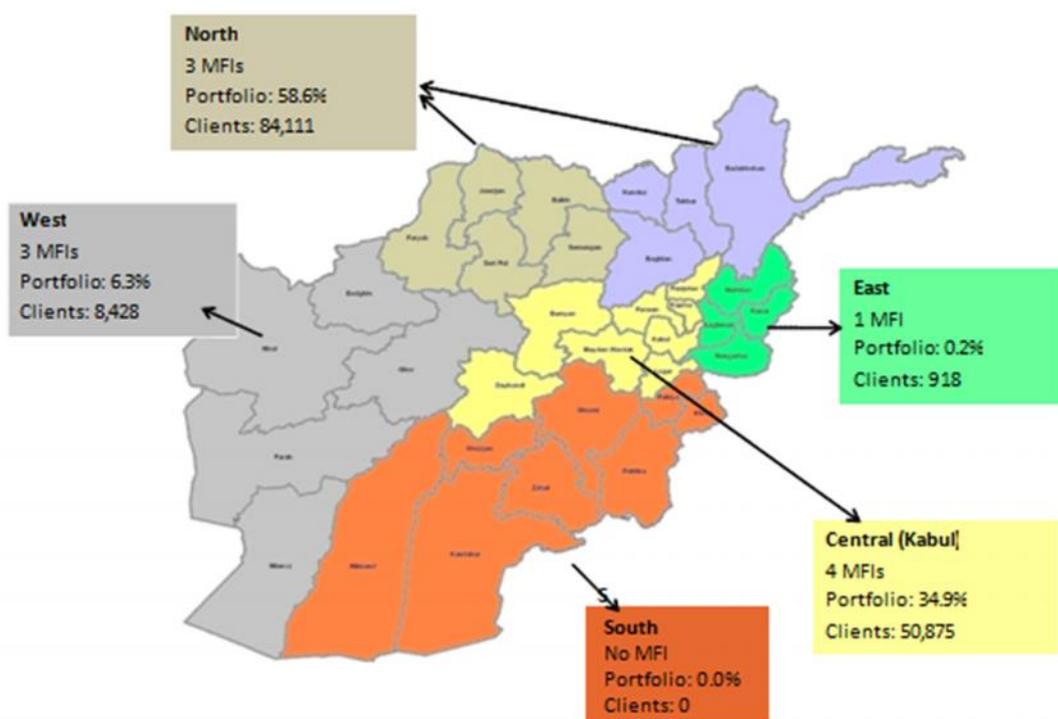
The policy of the Italian Cooperation Office is to include rural areas of the Western region. This would be in line with MISFA’s current plan, to implement Targeting the Ultra Poor (TUP) project in four districts of Herat province. The microfinance and SME components will concentrate in urban areas with the potential to reach out the rural districts as and when there is room for responsible expansion in those areas.

The following MISFA partners operate in Herat:

MFI	N° of Borrowers	Outstanding Portfolio	N° of Branches
FMFB	3,573	258,009,073	2
OXUS	820	36,661,000	1
Mutahid	96	9,923,980	1
FINCA	574	4,952,567	1
<b>Grand Total</b>	<b>5,053</b>	<b>309,546,620</b>	<b>5</b>



## MISFA (Existing only) Partners' Geographical Coverage (June 2014)



### 2.3 Targeting the Ultra Poor

Under the revised scope of work, a new component will be added to the ISAME project. This new component is called TUP (Targeting Ultra Poor).

MISFA's TUP programs first funded by IFAD and piloted by MISFA in Bamiyan and Badakhshan provinces. The pilot identified 1,200 rural households, through a participatory wealth ranking, who were found to be at the very bottom of the economic ladder. Under the MISFA pilot it was found that adopting a "graduation model" which combines support for immediate needs with longer term investments in training, financial services, and business development for a period of at least two year equips the ultra poor to help themselves move and remain out of extreme poverty. Given that often the ultra poor families are headed by women, 100% of the beneficiaries in both pilots were women.

MISFA will try to build synergy and coordination between IFAD, World Bank and ISAME funded TUP projects. The same procurement process will be conducted for all projects and there will be close oversight and quality control over all TUP projects. The households will be targeted under similar selection criteria that are available in the Operation Manual developed by MISFA and approved by the World Bank. Lessons learned from across the nine provinces, where TUP projects were piloted or are being implemented will be shared with all projects. There will be

joint project design workshops and coordination meetings as the projects move on. The TUP funded project under ISAME will be part of MISFA's larger program supported by IFAD and the World Bank. IFAD is funding TUP in Bamyan and Badakhshan. The World Bank will fund it in six additional provinces and the ISAME funds will be utilized to implement the TUP project in Herat.

While MFIs are moving towards higher loan amount, MISFA is addressing the needs of the very poor at the other end of the spectrum by implementing a program created for the ultra poor. Using the lessons learned on the successful implementation of the targeting the ultra poor (TUP) program, MISFA will expand it nationally by reaching out to different provinces. MISFA will be working with selected national NGOs to build their capacity in order to partner with MISFA in implementing the ultra poor program in various provinces.

Experience globally shows that combining interventions providing safety nets, livelihoods and social development and microfinance services at the household level over a period of two years results in higher and sustainable graduation rates out of extreme poverty. Safety net programs such as cash or asset transfers, food aid and or public works employment reach the extreme poor, while livelihood and microfinance program provide an effective and sustainable exit strategy that prepares them for improved income generation and market activities.

Findings from the Bamyan TUP pilot also confirm that this approach works in the Afghanistan context. It was found that in less than a year, 28 percent of household (100% headed by women) overcame extreme poverty, 92 percent of the household had increased access to food after involvement in the program, and an estimated 55 percent reported an increase in value of productive assets.

The pilot program which took on a multi-sectorial approach also reported a number of social benefits; for example, 87 percent reported changes in the attitude and behaviour of the communities where they live; 65 percent had improved housing conditions, 100 percent household vaccinate their children aged between 0-1 years and 38 percent reported using sanitized stab latrine. Though survey data are not available on the change in perception of the role of the women in the communities, but the over all results of the project suggest that such a change must have happened and shall be tracked in the future projects.

TUP program aims at sustainably "graduating" the ultra-poor from a safety net program to income generating activities and eventually linking them with microfinance programs and saving groups. In order to ensure that graduation is sustainable, the program will (i) provide households a two year package of asset/inputs and subsistence support; (ii) build their capacity to improve their incomes and achieve financial literacy; (iii) facilitate access to basic health care through community –based health workers; (iv) link them with existing saving groups and microfinance institutions for access to financial services.

Based on the successful implementation of the TUP program funded by IFAD, the World Bank has recently provided \$15 million to MISFA for further scale-up of the TUP to six additional provinces. The TUP projects are being implemented by MISFA partner NGOs under close oversight from MISFA.

The TUP sub-component under the ISAME project will be implemented in four districts (Karukh, Ghoryan, Enjeel and Zendajan) of Herat province. At the start of the project, MISFA will conduct a situational analysis and assessment of the province and may amend the list of the districts to ensure successful implementation of the TUP project in Herat. For further implementation arrangements please refer to the Operational Manual of the TUP program.

## 2.4 Microfinance

The microfinance program in Herat will enhance the support to low income people, promoting and strengthening the development and growth of a long-term, strong and healthy microfinance sector that provides high quality and efficient financial services. The microfinance program will be implemented through MFI partners including FMFB, OXUS, FINCA and Muthaid.

In Herat, MISFA has provided AFN39 million in loans and grants of ISAME funds to **OXUS** through the existing ISAME project, as AFN 30 million loan for microfinance and AFN 9 million grant for the support to set OXUS' branch in Herat.

Additional AFN 20 million loan was provided to OXUS for SME/MF component by MISFA through additional funds of other donors.

### Achievements:

With funding from ISAME, OXUS/Afghanistan expanded its branch in Herat Province. The branch currently employs 22 individuals including 5 female employees. It is currently serving **820 borrowers including 198 women borrowers (24%)**. Gross loan outstanding is AFN 36.6 million as of end of October 2014. **Cumulatively OXUS-Herat branch served 2,819 clients and disbursed total amount of AFN 214.3 million.**

OXUS-Herat branch offers five products with following features:

Name of Product	Loan Size, AFN	Loan Term	Upfront fee	Interest Rate (Flat per month)
Micro Business Loan (MBL)	10,000 - 29,999	6-12 Months	1.75%	2.4%-2.5%
Small Business Loan (SBL)	30,000 - 49,999	6-12 Months	1.75%	1.8%-1.9%
Micro Enterprise Loan (MEL)	50,000 - 199,999	6-12 Months	1.75%	1.6%-1.7%
SME	200,000 - 1,000,000	6-18 Months	1%	1.5%-1.6%
SME +	1,000,000 - 2,000,000	6-18 Months	1%	1.5%-1.6%

Sector wise concentration of OXUS-Herat branch portfolio as of Oct 2014 is as follows:

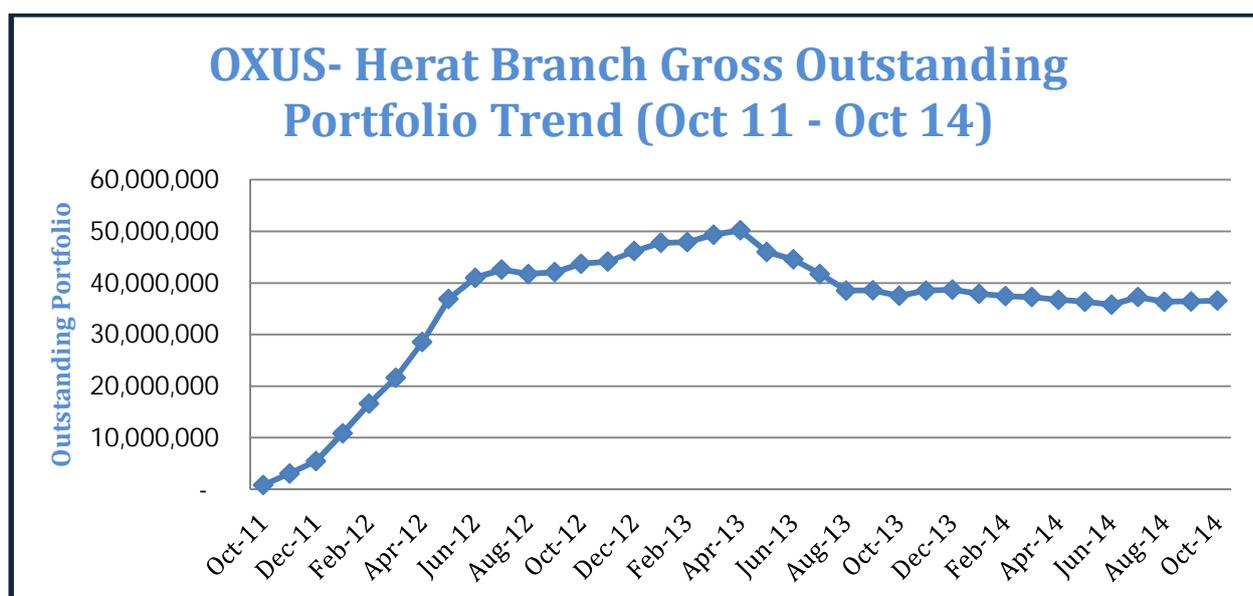
Sector	Active Borrowers	Outstanding Loan, AFN
Trade and Services	783	34,800,000
Manufacturing	35	1,800,000
Agriculture	1	33,000
Live Stock	1	28,000
<b>Total</b>	<b>820</b>	<b>36,661,000</b>

Key performance indicators of the branch are as of October 2014 are:

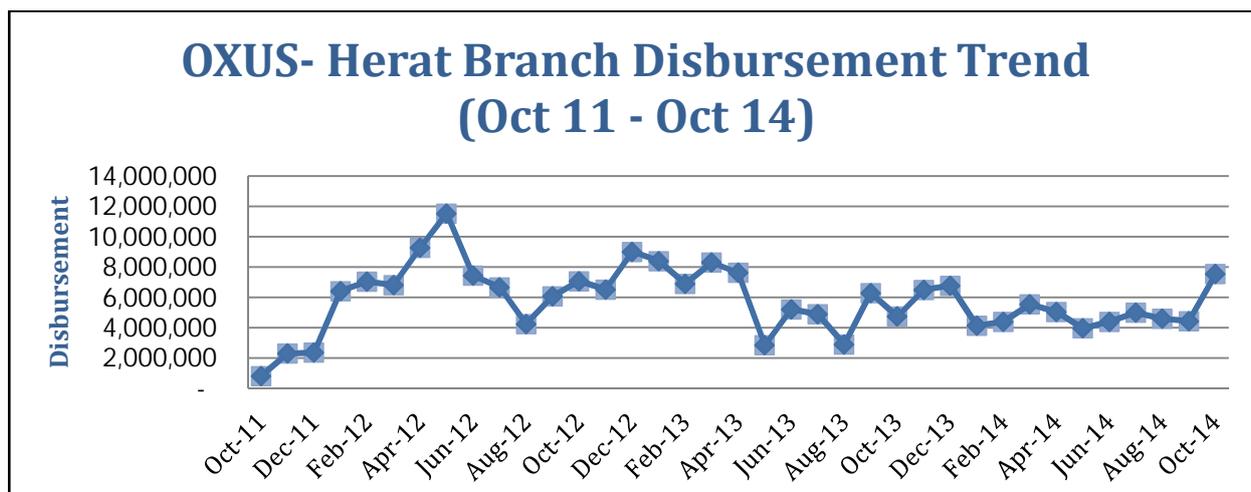
Performance Indicators (OXUS Branch in Herat)	October 2014
Amount of Loans Disbursed – Cumulative (AFN)	*214.3 million
Number of Loans Disbursed – Cumulative (AFN)	2,819
Active Borrowers (male and female)	820
Number of Women Borrowers (Active)	198
Value of Loans Outstanding (AFN)	*36.6 Million
Loans Outstanding Per Borrower (AFN)	44,708
Portfolio at Risk (PAR30)	5%
Number of Employees	22

\*These include ISAME funds

Outstanding Portfolio from inception (October 2011) till Oct 31, 2014 is as follows:



Disbursement trend for Herat branch from inception to Oct 31, 2014 is as follows:



The average loan size amounts to AFN 76,023 (USD 1,334 @AFN 57 / USD). This is due to larger loan sizes reflected in below table:

Products	Total amount - AFN	Number of loans	Average size - AFN
Individual Loan	17,690,000	114	155,175
Micro Business Loan	2,579,052	125	20,632
Micro Enterprise Loan	50,303,091	336	149,712
Small Personal Loan	12,265,000	301	40,748
Small Business Loan	85,424,386	1,868	45,730
<b>Totals</b>	<b>168,261,529</b>	<b>2,744</b>	<b>61,320</b>
Small Medium Enterprise	39,947,667	66	605,268
Small Medium Enterprise+	1,500,000	1	1,500,000
SME Loan	4,600,000	8	575,000
<b>Totals</b>	<b>46,047,667</b>	<b>75</b>	<b>613,969</b>
<b>Grand Total</b>	<b>214,309,196</b>	<b>2,819</b>	<b>76,023</b>

### ISAME Contribution Quantification:

Out of a total of 2,819 OXUS's clients, **2,744 have been clients for microcredits** (97%) during the period October 2011 – October 2014 financed by the ISAME initial loan funds of AFN 30 million. The total disbursements for microfinance amounted to **AFN 168,261,529** (out of total AFN 214.3 million).

It is estimated that, out of a cumulative 2,744 microfinance clients served through ISAME funds, 658 have been women clients (considering an average of 24%). The average of microcredit loans is in the amount of AFG 61,320 equivalent to approximately Euro 796.

### Next steps:

Through this Project revision ISAME funds will be utilized to expand the existing products of OXUS, Muthaid, FMFB and FINCA. It will also support new products including Mutahid's Sharia-compliant product. Mutahid's Sharia-based product (*Mutabaha*) is currently funded by IFAD. *Mutabaha* is an Islamic Finance concept governed by Shari'ah principles. It is a contract between the Development Financial Institution (DFI) Mutahid and each client, by which Mutahid DFI purchases goods and then sells them to the client at a cost that includes a profit margin. The contract requires specific instalment payments to Mutahid DFI. This arrangement avoids charging interest, which is forbidden under some interpretations of Islamic law.

*Sharia* compliant products could be another innovative window for the ISAME fund utilization. Microfinance clients in Herat province have long been demanding to have access to Sharia-compliant loans. Since then MISFA has been in the process of piloting Sharia-compliant loan products, designed and developed based on client demand. Under the ISAME project, MISFA partners will work on the next phase of this innovation, the tweaking, adjustments and implementation stage. Before the sharia-compliant loan products could be systematically scaled up, practitioners must have a better operational understanding of their application. This would include understanding the price-effectiveness trade-offs acceptable to customers, creating proof-of-concept prototypes, and designing a branding, marketing and distribution strategy.

FINCA, recently has been discussing designing new and innovative rural agricultural product, so that will be another funding channel to reach out to rural poor clients. The new agriculture product of FINCA could also be funded under the ISAME project.

It is to be noted that each MISFA partner has products specifically developed for women, in order to improve their access to microfinance.

In order to find out relevant financial resources for the TUP component, MISFA proposed to revise and reduce the budget lines allocated to Operative Costs and Training (see chapter 3.5 "The budget"). Anyhow, the capacity building needs and operative costs of partner institutions are covered through other sources.

Further, the revised geographical focus will be only Herat province and mainly in the urban area.

## **2.5 Small and Medium Enterprise (SME) Loans**

The original scope of work, in terms of products, of the SME sub-component of the ISAME project will remain unchanged. However, the geographic focus will only be in Herat Province and mainly in the urban area.

It is evident that none of the MFIs in Afghanistan has been able to reach operational sustainability in the last ten years with its microfinance product lines alone. Increasingly, institutions are offering higher loan amounts and have begun establishing SME product lines within their operations to help them reach sustainability and to provide much needed credit support to the “missing middle”—the small business owners. In order for MFIs to set up SME lending in a sustainable manner, using a proven methodology that is contextualized for Afghanistan, MISFA will provide technical assistance to help establish sound SME departments.

One of the MISFA partners implementing the SME sub-component of the ISAME project will be FMFB/Afghanistan. The partner currently has a guarantee facility with DEG (Deutsche Investition – und Entwicklungsgesellschaft mbH) for its SME lending. The guarantee fees range depends on risk ratio of the loans. The loss coverage/sharing ratio under this facility is 72:28, meaning 72% of the credit losses will be paid by DEG and 28% will be borne by FMFB.

The SME loans disbursed by FMFB under the ISAME project in Herat will also be guaranteed by DEG and in future by the Afghanistan Credit Guarantee Foundation (ACGF), which is supposed to take over the same role carried out by DEG, unless the DEG/ACGF/FMFB agreement will be otherwise for unforeseen reasons. Other partners will include other MFI partners with established SME Departments. They include FINCA, OXUS, and Mutahid.

## **2.6 On-lending contacts to MFIs and repayment fund**

Relations between MISFA and MFIs are regulated through on-lending contracts. Conditions for on-lending contracts will be discussed between MISFA and relevant MFIs. Presently, conditions for micro credit and SME funds are 5-7% annual interest depending on the status of the partners<sup>2</sup>, and 5 year grace period and a 5 years repayment period. Funds reimbursed by local financial institutions to MISFA will be placed in the MISFA accounts for further support of the microfinance/SME sector via on-lending facilities or capacity building grants. Considering that the grace period may overtake the project’s expected duration (3 years), the MoF undertakes to keep the Embassy of Italy informed about the repayments’ level and outcome after completion of this Project.

## **2.7 Conditions to Borrowers and repayment rate**

Conditions to the final borrower are set in the contracts and depend on the financial product. However, for microcredits, the normal conditions are a 1.25-2% monthly rate over a 6-24 month loan period, while the loan’s value may vary between US\$ 100 – 7,000. Loans are mostly utilized to promote small business opportunities creating or sustaining an average of 1.5 jobs per loan. Micro credits target socially vulnerable groups and women, which make up to 20% of the clients.

Conditions for SMEs greatly vary according to the market. These loans have a range between US\$ 3,000 – 300,000, though most MFIs foresee a maximum loan of US\$ 50,000.

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<sup>2</sup> MISFA’s interest rate for non-dividend distribution partners is 5% and for dividend distribution partners is 7%.

### 3. JUSTIFICATION AND RATIONALE

#### 3.1 Problems/Issues to be addressed

In only three years, the TUP project funded by IFAD and MISFA's core activities of microfinance and SME lending have significantly improved the lives of thousands of rural and urban families in Afghanistan. However, there is a need and a great window of opportunity to:

- Improve the lives of more ultra poor families and graduate them out of ultra poverty.
- **strengthen** the capacities, systems and networks put in place;
- **scale up** the microfinance and SME lending initiatives and innovations;
- Continue to **innovate** based on better knowledge of markets and good practices on the ground.

#### 3.2 Stakeholders and Target Beneficiaries

##### *TUP Stakeholders*

The TUP stakeholders are Herat Provincial Government, MFIs, NGOs, Community Development Councils (CDCs), District Development Assemblies (DDAs), DAIL and Veterinary Field Units (VFUs), Schools, saving groups and health providers. Direct beneficiaries include approximately **1725 households, corresponding in total to about 12.075 beneficiaries** in four rural districts of Herat (average of 7 family members in rural areas). Based on lessons learnt from the pilot TUP project, it is expected that at least 80% of beneficiaries will be women.

##### *Other partners for SME and Microfinance*

Other partners of the SME and Microfinance are Provincial government, Business development associations, cooperatives, DDAs.

Direct beneficiaries for microfinance include: **2,744** clients received loans by OXUS Herat branch since October 2011 to October 2014. Approximately 658 were women clients (considering an average of 24%). Considering that a family in urban area has an average of 6 members, out of 2,744 household clients the **total beneficiaries of microfinance component are approximately 16.464**. At present 820 are outstanding clients.

Within the continuation of microfinance activities additional **2,396** clients are expected to receive loans by OXUS, Mutahid and FINCA, which implies approximately **14.376 beneficiaries** (average of 6 members per family).

The estimation **beneficiaries of 60 SME clients will be approximately a total of 1620** (60 clients x 4,5 workers x 6 family members).

Given that the women's access to microfinance is an on-going and long-term process in Afghanistan, and notwithstanding the gender measures that will be taken in order to ensure women's full participation in the program, in this case the percentage of women clients is expected to be around 25-30%, in line with previous MISFA experience.

#### 3.3 Project Justification

Given the successful implementation and the evident impact on the first batch of TUP beneficiaries in Bamyan province, where 400 Ultra Poor Households were targeted, MISFA received funding to scale it up to two districts of Badakshan that is Khash and Faizabad, where 800 household ultra poor families were targeted. This project has been successfully completed at the end of July 2014. After this breakthrough in serving the poorest of the poor, IFAD approved

additional funding for Shuhada district and the remaining villages of the Faizabad in Badakhshan province. Further, the World Bank approved new funding to scale up the TUP project in six additional provinces over the next five years.

Following are statistics which shows the improvements in the life of the TUPs after the implementation of the project in Badakhshan province.

- 75 % of the beneficiaries have overcome extreme poverty and 13% came above the poverty line, while 12% of them were very poor, and 13% of them reported average level of income.
- 73% of the household income is sufficient to meet their needs.
- 99% of the beneficiaries have access to cash income.
- 99% of the beneficiaries have improved housing conditions.
- 97% of the beneficiaries were linked with the government and other NGOs have a presence in the area.
- 93 % of the beneficiaries linked with financial institutions, 360 households have joined saving groups, and 380 households opened a bank account in Faizabad, which resulted in making a saving of AFN 2,306,680.
- 58 children of TUP households enrolled in public schools
- 588 households have been using sanitize slab latrines, while before the project the households were using open space or traditional latrine.
- 100% of the beneficiaries have vaccinated their animals against common disease, which resulted in a reduction in the mortality of animals by 94%.
- 100% of the beneficiaries got national identity cards.

Though survey data are not available on the change in perception of the role of the women in the communities, but the over all results of the project suggest that such a change must have happened and shall be tracked in the future projects.

At present MISFA has only five partners compared to a few years back when sixteen MFI partners were operative. This reduction in number of MFIs allows concentrating more on the oversight, capacity building and quality control of the MFIs, and that will bring added value to the operations of the microfinance institutions. In addition to this, MISFA partners now have innovative and more customised products. For instances, the rural agriculture and livestock, the Sharia-compliant products and their wider acceptability in the market will have remarkable impact on the disbursement of fund to the clients.

### **3.4 MISFA contribution to the Project**

MISFA will take full responsibility for the implementation and supervision of the project. MISFA's Monitoring and Supervision Department will carry out monitoring and supervision missions to ensure the project is implemented properly and the targets achieved as included in the project description. MISFA's Public Information and Communication will document and disseminate success stories and other news of the project. The Finance and Administration Department will provide appropriate support function to facilitate the implementation of the project and work closely with the partners on an as needed and required basis. MISFA's senior management will dedicate considerable time to the ISAME project and its implementing partners.

MISFA senior management will dedicate considerable time to the ISAME project and its MFI partners involved.

MISFA will build synergies and coordination between IFAD, World Bank and ISAME funded TUP projects. The same procurement process will be conducted for all projects and there will be close oversight and quality control over all TUP projects. The households will be targeted under similar selection criteria that are available in the Operational Manual developed jointly by MISFA and the World Bank and give priority to households whose head is a woman. Lessons learned from across the nine provinces, where TUP projects were piloted or are being implemented will be shared with all projects. There will be joint project design workshops and coordination meetings as the projects move on.

### **3.5 Gender issues**

Traditionally the position of women in Afghanistan has been low compared to men. Women are generally poorer, have low education, inadequate access to health services, and suffer from traditions and customary laws. Thus, empowerment of women is one of the main issues in Afghanistan. Microfinance and particularly the TUP services are considered as an entry point against poverty, generally targeting poor men and women and a vehicle toward empowering women.

The argument behind Microfinance Institutions (MFIs) targeting women is that, women are good credit risk, are less likely to misuse the loan and are more likely to share the benefits with others in their household, especially their children and with regards to access to education and health. This women's increasing role in the household economy will lead to their empowerment.

Empowerment of women is a challenge since traditionally Afghan women have been marginalized and still subjected under the control of men.

Due to their low education level, knowledge and skills on how to manage their work and lack of required collaterals, women have no access to formal credit and other financial services.

Microfinance and TUP aim at improving men and women economic situation by putting financial resources and assets in their hands.

Economic independence results in higher bargaining power for women in their households and communities, and subsequently results in higher prestige and self-esteem, synchronous with potential to empower.

The project is seen as contributing not only to poverty reduction and financial sustainability, but also to a series of links to economic empowerment, increased well-being, social and political empowerment for men and women.

MISFA envisages that for the three Project components (TUP, microfinance and SMEs) a share of at least 60% of the direct beneficiaries will be women. Specifically, gender monitoring, sex-disaggregated data, and evaluation indicators to systematically measure the here below changes will be designed for each type of intervention, ensuring that all indicators and information on beneficiary-targeted actions are broken down by sex, within the Indicator Monitoring System set by MISFA for this project.

Although it is difficult to measure the exact impact and indicators of access to financial resources and assets on different dimensions, it is important to distinguish between the functions of microfinance and TUP program and the potential it carries to improve the livelihoods of vulnerable people and empowerment of women.

Indicators of Empowerment could be measured in various dimensions such as:

- *Board/staff diversity*

Percentage of women board members, staff, senior management, middle management and front-line staff in MISFA's partners. This is of paramount importance given the general

reticence of women to talk to men, especially in rural areas. The presence of female staff could help presenting MISFA's products to women and enhance their access to microcredit.

- *Percentage of active loans to women (Microfinance)*

Microfinance component: disaggregated data on percentage of active loans to women.

- *Percentage of active loans to women (SMEs)*

SME component: disaggregated data on percentage of active loans to women entrepreneurs. Percent of clients analysed through market research, by gender.

- *Percentage of active grants to women (TUP)*

TUP component: disaggregated data on percentage of active grants to women. Percent of women clients who attend financial education programs

Aside from quantitative data collected through gender-disaggregated indicators that have been already developed by MISFA for TUP projects, qualitative information will be gathered in order to assess the impact of each project component on women in terms of their empowerment. Indeed, previous researches have shown that targeting women without adequate support networks and empowerment strategies can merely shift all the burden of household debt and household subsistence onto women. Those indicators will try to help have a better understanding of the support strategies that are needed to ensure a real impact of the project into women's conditions. Some examples of qualitative indicators for TUP projects, are as follows:

- *Control over Savings and Income:*

This variable refers to the ability of the client/beneficiary to exercise greater control over the savings and income within the household economic portfolio. Thus the term control is used here to refer to increased control of savings and income within the household. It is measured in terms of an increased role in and/or bargaining power in decisions regarding the decision to save and use of income earned and/or generated from business activities

- *Increased in ownership of assets:*

This variable refers to legally or socially authorized household/individual ownership of property or assets: that is, to when, under either modern law or customary law, the household/individual is recognized to own property or assets in their individual capacity. It is measured in terms of individual/household ownership of properties or assets approved either under modern or customary law.

- *Participation in decision making:*

When women start receiving and using financial support to make a positive contribution to the household and the community the perception toward them starts to change. Changes include both in the self-perception of the women as well as changes in the perceptions that others have on those women. Increases in the women's self-esteem and self-confidence can lead to a more active role for the women in decision-making both with the household and within the community.

- *Self-esteem:*

This variable refers to how one values oneself and how one feels that others value one's self and one's contributions. It is measured in terms of whether women make any major contributions to a) their household, and b) their community; and c) how women evaluate themselves compared to men and other groups in the society.

Monitoring will be done on the following: impact on decision-making, on self-confidence of women, on their status at home, on family relationships and the incidence of domestic violence, on their involvement in the community.

Their success can pave the way for them to become respected and valued members of the community.

- *Participation in activities outside home:*

This variable refers to participation of women in the activities outside their home. It is measured in terms of participation in different meeting and activities outside home.

Though, it is not funded under this project, MISFA and its MFI partners continue to revisit their products to address the needs of female clients (segmentation) and further develop and/or upgrade their gender appropriate financial products.

## **4. PROJECT FRAMEWORK**

MISFA's work is integrally linked to the Afghanistan National Development Strategy (ANDS), a comprehensive vision for the nation's security, governance, economic growth and poverty reduction. A key part of the 2020 Vision for Afghanistan is: "A society of hope and prosperity based on a strong, private sector led market economy, social equity, and environmental sustainability."

### **4.1 General Objective**

To contribute to poverty reduction and social inclusion of the population in the Province of Herat through the expansion and development of microfinance and SME sector and to support the most vulnerable people, with particular attention to empowerment of women.

### **4.2 Specific Objectives**

To support MISFA activities in order to improve financial conditions of vulnerable people and SMEs through the provision of specific lines of credit and productive assets, by strengthening the MFIs and NGOs network in order to broaden the offer of financial services in the Province of Herat.

### **4.3 Expected Results**

- Result 1:** Increased number of receivers of micro-credit, belonging to vulnerable groups and women.
- Result 2:** Improved SMEs in terms of increased access to credit and employment generation created.
- Result 3:** Improved financial income of TUP households that received productive assets to develop sustainable income generating initiatives.
- Result 4:** Improved operative capacity and sustainability of the MFI and NGO network.

#### **4.4 Activities**

##### ***4.4.1 Activities for Result 1:***

**Activity 1.1:** Microcredit to vulnerable people provided by MFI partners.

##### ***4.4.2 Activities for Result 2:***

**Activity 2.1:** Provision of credits to SMEs by the MFI partners.

##### ***4.4.3 Activities for Result 3:***

**Activity 3.1:** Activities in support to TUP people in four districts of Herat.

##### ***4.4.4 Activities for Result 4:***

**Activity 4.1:** Providing capacity building to the MFIs and NGOs partners.

**Activity 4.2:** Management support for implementation of the ISAME Project.

**TABLE 1: Project Framework for TUP Component**

<b>Objectives in words</b>	<b>Indicators</b>	<b>Means of verification</b>
<b>Goal or Impact</b>		
The incidence of extreme poverty reduced in the selected districts of Afghanistan.	<ul style="list-style-type: none"> <li>– Extreme poverty incidences reduced in the targeted ultra poor households</li> <li>– Reduced malnutrition in children under-five years of age.</li> <li>– Reduced child and maternal morbidity and mortality</li> </ul>	<ul style="list-style-type: none"> <li>– Outcome survey</li> <li>– Research papers</li> <li>– Baseline survey</li> <li>– End-of-program impact assessment</li> <li>– MISFA donor reports (every six months)</li> </ul>
<b>Purpose or Outcome</b>		
Helping 1725 families lift themselves out of extreme poverty.	<ul style="list-style-type: none"> <li>– 90% of TUP graduates access the existing development services without facilitation from TUP.</li> <li>– Diversified and strengthened asset bases of ultra poor and poor households.</li> <li>– 80% women from participating ultra-poor and poor households aware of their social rights and entitlements.</li> </ul>	<ul style="list-style-type: none"> <li>– Baseline, midterm and end-of-program impact assessment</li> <li>– MISFA donor reports (every six months)</li> </ul>
<b>Outputs</b>		
1. A total of 1725 TUP households supported to successfully develop sustainable income generating activities.	<ul style="list-style-type: none"> <li>– 80% of TUP members can articulate their future plans for diversified income sources.</li> <li>– 80% of TUP members use productive assets.</li> <li>– At least 80% of TUP graduates’ families</li> </ul>	<ul style="list-style-type: none"> <li>– MISFA donor reports (every six months)</li> <li>– Assessment reports</li> </ul>

	<p>enjoy at least two meals a day.</p> <ul style="list-style-type: none"> <li>– 80% of TUP members have improved their housing conditions.</li> <li>– 80% of the beneficiaries linked to the market</li> <li>– 80% of the beneficiaries started savings.</li> </ul>	
2. Essential preventive, basic curative and primitive health care services ensured for 1725 ultra-poor households	<ul style="list-style-type: none"> <li>– Increased health-seeking behavior for illnesses and a corresponding decrease in self-treatment</li> <li>– Increased households from 32% to 42% having and using slab latrines.</li> <li>– Increase eligible couples using modern contraceptives from 11% to 30%.</li> <li>– Increase from the existing rate to 90% of children aged 0-1 years who are fully vaccinated.</li> <li>– Increase in Tuberculosis (TB) detection rate from 76% to 80% and treatment success rate of 92%</li> </ul>	<ul style="list-style-type: none"> <li>– MISFA donor reports (every six months)</li> <li>– Assessment reports</li> </ul>
3. Awareness and confidence of ultra-poor and poor people to achieve their rights and entitlements enhanced/ access social justice strengthened.	<ul style="list-style-type: none"> <li>– All births, marriages and deaths are registered. All victims of physical assault, rape and other forms of violence receive medical care support.</li> <li>– At least 60% of women understand and can recall their fundamental rights and act on those that are most relevant to them (e.g., age of marriage, divorce).</li> </ul>	<ul style="list-style-type: none"> <li>- MISFA donor reports (every six months)</li> <li>- Assessment reports</li> </ul>
4. Advocacy, communication and social mobilization campaigns to	<ul style="list-style-type: none"> <li>– Changes in attitudes and behavior of the community members towards ultra poor and women.</li> </ul>	<ul style="list-style-type: none"> <li>- MISFA donor reports (every six months)</li> </ul>

influence policy makers and the general public in favor of the ultra-poor successfully implemented.	<ul style="list-style-type: none"> <li>– Other development partners sensitized and motivated to change their policies, programs and practices in favor of the rural poor.</li> <li>– One published article on ultra poor issues per year; 2 stories on the ultra poor broadcast on print and electronic media per year.</li> </ul>	<ul style="list-style-type: none"> <li>- Assessment reports</li> </ul>
5. Effective monitoring, research and evaluation systems operational and results effectively disseminated.	<ul style="list-style-type: none"> <li>– Potential champions for the ultra poor in government, NGOs, business, politics and media have improved understanding of ultra poor issues and the TUP program.</li> </ul>	<ul style="list-style-type: none"> <li>- MISFA donor reports (every six months)</li> <li>- Assessment reports</li> </ul>

### Activities

<b>Output 1 : TUP Incomes</b>	<b>Output 2: Essential Health Care</b>	<b>Output 3: Social awareness</b>	<b>Output 4: Advocacy, Communication And Social Mobilization</b>
Targeted Ultra Poor (TUP) members selected through a rigorous Participatory Rural Appraisal (PRA) process.	Staff recruitment (including at least 60% of women) and deployment	Capacity building including training and refresher courses of Community Health Worker (CHW).	Workshops, roundtables and meeting at Provincial to national levels
TUP members receive enterprise development and life skills training	Training of staff, health workers and community health workers. At least 80% of beneficiaries will be women	Organize local community leader workshops	College and university students and media persons visit TUP program at field level
TUP members receive assets worth AFN around 30,000 to 35,000 engage in enterprise development	Develop TRAINING materials	Yearly review and consultative meetings	
TUP members receive a stipend tailored according to personal capacity and circumstances and chosen	Provide health and nutrition education	Consultation forum and special meeting with local and national administration	

enterprise			
	Provide health care services including family planning, antenatal care, immunization, basic curative treatment, TB.	Network with law implementation committee; CDC; Local Shura; Village Poverty Reduction Committee.	
TUP members receive hands-on training and support through weekly/fortnightly home visit.	Community based treatment of Acute Respiratory Infection (ARI) for children under-5	Medical care support	
	Establish referral linkage with Government Institutions (GoIRA) and other private facilities.	Social reintegration for violence victims/survivors	
	Financial assistance (subsidies) provided for mild and severe morbidity for the ultra-poor.		
<b>Output 5 Monitoring, Evaluation and Research (MER)</b>	<b>Output 6: Program management</b>		
Design and implementation of monitoring system.	Staff recruited (including 60% women) and trained and offices equipped.		
Strengthening of capacity for producing quality reports and production of same.	Timely and thorough review of the program.		
Design, implementation and dissemination of impact assessment study's findings	Revisions in approach based on evidence of learning systems.		

**TABLE 2 Project framework for Microfinance, SME and TUP components**

	<b>Logic of the intervention</b>	<b>Indicators objectively verifiable</b>	<b>Sources of verification</b>
<b>GENERAL OBJECTIVE</b>	To contribute to poverty reduction and social inclusion of the population in the Province of Herat through the expansion and development of microfinance and SME sector and to support the most vulnerable people, with particular attention to empowerment of women.	<ul style="list-style-type: none"> <li>Number and total amounts of on-lending contracts between MISFA and MFIs aimed at vulnerable people and SMEs.</li> </ul>	<ul style="list-style-type: none"> <li>Project assessments and internal/external evaluations by Italian cooperation staff.</li> <li>Independent evaluation at the end of three-year project</li> <li>Reports by the Italian Cooperation project staff.</li> <li>Provincial report and statistics.</li> <li>MISFA Quarterly Donor Report</li> </ul>
<b>SPECIFIC OBJECTIVE</b>	To support MISFA activities in order to improve financial conditions of vulnerable people and SMEs through the provision of specific lines of credit and productive assets, by strengthening the MFIs and NGOs network in order to broaden the offer of financial services in the Province of Herat.	<ul style="list-style-type: none"> <li>Number and amounts of on-lending contracts between MFIs and clients (vulnerable people and SMEs) during and at end of the project implementation (disaggregated data).</li> <li>Amount of the revolving fund re-used by MFIs for vulnerable people and SMEs.</li> <li>Number of women and vulnerable people that received productive assets for income generation activities (TUP).</li> <li>Average and total amount of small grants for TUP.</li> </ul>	<ul style="list-style-type: none"> <li>MISFA specific data and information.</li> <li>MISFA annual external financial audits.</li> <li>MFIs/Banks annual financial audits.</li> <li>Report by Italian Cooperation Project staff.</li> <li>Independent assessments.</li> <li>Monthly portfolio Monitoring report by MFIs.</li> <li>MISFA annual external financial audits.</li> <li>External certified audit at end of three-year project.</li> <li>Reports by the Italian Cooperation Project staff.</li> </ul>
	<b>Logic of the Intervention</b>	<b>Indicators objectively verifiable</b>	<b>Source of verification</b>
<b>RESULTS</b>	1. Increased number of micro-credit borrowers, belonging to vulnerable groups and women.	<ul style="list-style-type: none"> <li>Number of clients and total amount of micro-credits.</li> <li>Number and total amount of micro-credits for women and their percentages out of total.</li> <li>Number of Islamic products provided.</li> <li>Percentages of repayments.</li> <li>Amount of the Revolving fund reinvested to vulnerable groups and women.</li> </ul>	<ul style="list-style-type: none"> <li>MISFA' Specific Data And Information.</li> <li>MISFA external annual audits.</li> <li>MISFA partners annual external audits.</li> <li>Direct observations and Italian Cooperation Project reports.</li> <li>Data and statistics on loans to women.</li> </ul>
	2. Improved SMEs in terms of increased access to credit and employment generation created.	<ul style="list-style-type: none"> <li>Number of contracts between the MFIs and SMEs</li> <li>Number of SMEs business plan approved and rejected.</li> <li>Repayments to MFIs.</li> <li>Amount of Revolving fund reinvested to SMEs.</li> <li>Number of SMEs expanded.</li> <li>Number of jobs created within SMEs.</li> </ul>	<ul style="list-style-type: none"> <li>MISFA quarterly donor reports.</li> <li>MISFA external annual audit.</li> <li>MISFA partners annual external audits.</li> <li>Direct observations and Italian Cooperation Project reports.</li> <li>Data and statistics on SMEs using existing formats.</li> </ul>
	3. Improved financial income of TUP households that received productive assets	<ul style="list-style-type: none"> <li>Number of beneficiaries and total value of productive assets.</li> <li>Number and total value of productive assets for women and their</li> </ul>	<ul style="list-style-type: none"> <li>MISFA quarterly donor reports.</li> <li>MISFA external annual audit.</li> </ul>

	to develop sustainable income generating initiatives.	<p>percentages out of total.</p> <ul style="list-style-type: none"> <li>• Average value of productive assets.</li> <li>• Number of local NGOs operative for TUP component.</li> <li>• Project portfolio managed by each local NGO for TUP component.</li> </ul>	<ul style="list-style-type: none"> <li>• MISFA partners annual external audits.</li> <li>• Direct observations and Italian Cooperation Project reports.</li> <li>• Data and statistics on assets distributed to women and vulnerable groups.</li> </ul>
	4. Improved operative capacity and sustainability of the MFI and NGO network.	<ul style="list-style-type: none"> <li>• Number of MFI and NGO operative within the ISAME project.</li> <li>• Number of MFI that reached its operational sustainability.</li> <li>• Number of professional staff of each MFI compared to its portfolio.</li> </ul>	<ul style="list-style-type: none"> <li>• MISFA' Specific Data And Information.</li> <li>• MISFA external annual audits.</li> <li>• MISFA partners annual external audits.</li> <li>• Direct observations and Italian Cooperation Project reports.</li> <li>• Data and statistics on MFI network</li> </ul>
	<b>DESCRIPTION</b>	<b>FINANCIAL INSTITUTION</b>	<b>COSTS in AFN</b>
<b>ACTIVITIES</b>	Microfinance: microcredit to vulnerable people provided by MFI partners.	Italian Grant to the Afghan Government (art. 15, law 49/87)	70,789,353
	SMEs: Provision of credits to SMEs by the MFI partners.		70,000,000
	TUP: Activities in support to TUP people in four districts of Herat.		205,413,335
	Training: Providing capacity building to the MFIs and NGOs.		10,000,000
	Operative costs: management support for implementation of the ISAME Project.		36,000,000

**TABLE 3: Work plan for TUP component**

S/No	Activities	Months (36 months)																																					
		1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23	24	25	26	27	28	29	30	31	32	33	34	35	36		
1	Meeting with provincial government and community elder (DDA/CDC)	█																																					
2	Hiring of project staff	█																																					
3	Setting up of field offices	█																																					
4	Community mapping and household listing through PRA/poverty ranking/ Selection of beneficiaries		█	█	█																																		
5	Start of stipend					█	█	█	█	█	█	█	█	█	█	█	█	█																					
6	Skills training for beneficiaries					█	█																																
7	Purchasing and distribution of assets							█	█	█																													
8	Field visit by POs (Health, Livelihood, Social, & Live stock )			█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	
9	Follow-up and mentoring for graduating beneficiaries; mainstreaming activities	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	

**TABLE 4: Work plan for Microfinance and SME components**

S/No	Activities	Months (36 months)																																					
		1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23	24	25	26	27	28	29	30	31	32	33	34	35	36		
1	Agreement with MFIs	█											█															█											
2	Loan disbursement to MFIs	█			█			█			█			█			█			█				█				█			█					█			
3	Gap assessment of MFIs											█													█														█
4	Follow up			█				█				█					█					█				█				█					█				█
5	Monthly Progress Report	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	█	

## **4.5 Impact**

The expected impact of the project is to fight poverty and increase income generation through various tools targeting the ultra poor, and micro, small and medium enterprises in Herat.

## **4.6 Sustainability**

MISFA, as an apex development finance institution has been able to develop into a sustainable institution, in spite of recent difficulties of the microfinance sector over the last few years. MISFA is also supporting the development of sustainable microfinance institutions in Afghanistan. As of June 2014, one partner institution has reached Operation Self Sufficiency (while a second institution is close to reaching Operation Self Sufficiency).

The Targeting Ultra Poor Program aims to provide the required support to the ultra-poor households to ultimately reach sustainable livelihoods after 36 months of support.

Project sustainability will also be ensured through the linkages with other initiatives funded by the Italian Cooperation in Herat, and namely Support to Agriculture and Rural Development (SARD), National Solidarity Program (NSP), National Area-Based Development Program (NABDP), projects in women vocational training implemented by Italian NGOs, Support to milk-dairy cooperatives and the Non Formal Approach to Training and Education in Afghanistan (NATEJA) program.

In order to increase the number of women having access to microfinance and SMEs loans, it can be envisaged to put MISFA's IP (Implementing Partners) in contact with NGOs carrying out vocational training program for women in the province. Indeed, those skilled women, who most of the time also receive literacy and numeracy trainings, most of the time don't have access to financial products. To this end, the collaboration of NSDP (National Skills Development Program of Ministry of Labour) could be asked to:

- 1) present MISFA's partner products during vocational training classes;
- 2) put MISFA partners in contact with women who are planning to create or expand their business through the Employment Service Centre to be created by NSDP in Herat.

## **4.7 Risks and Assumptions**

The main risks, which may impede the implementation of the project, are the following:

### ***Security Situation in Afghanistan***

This security situation is still precarious in any region of Afghanistan. The staff of MISFA will be based in Kabul, but will conduct regular visits to provincial and district offices of the partners. The partners will adopt a flexible approach to adapt the changes in the security situation. All efforts will be made to maintain support to local partners.

### ***Political instability***

The political situation is closely related to the security situation, and subject to changes. These changes can be associated within situational changes, which can affect the panel of stakeholders, policy priorities, and coordination mechanisms. The project will aim to build

ownership of established strategies and structures, and allow margins for flexibility, so as to make them more resilient to changes in the political situation.

***Policy changes***

With the rising importance of structural adjustment within the government, policy changes might be contemplated during project duration. Policy changes may occur also by the other institutions / agencies involved in the project implementation. In that case, the project will take in due consideration such policy changes and act accordingly on the basis of decisions mutually agreed upon by the parties.

## **5. IMPLEMENTATION AND MANAGEMENT ARRANGEMENTS**

### **5.1 Implementation strategy, methodology and mechanism**

#### **Targeting the Ultra Poor (TUP)**

Monitoring, data analysis and other necessary steps to improve implementation are conducted on a monthly basis. The Monitoring Department of MISFA will be responsible to do the monitoring based on a set of indicators at different levels of project performance. The TUP project staff and supervisors will undertake data gathering at different levels of the program. Data collection forms and formats have been prepared for this purpose. The objective will be to standardize the data collection exercise and ensure the collected data can be analyzed and compared. The following record will constitute the basic monitoring data: performance reports, training reports, project progress report among others. The managers at all levels of the project will be responsible for ensuring that the necessary data is collected, analyzed and recorded. Participatory approaches will be encouraged at all stages. All the collected data will be gender-disaggregated. A set of qualitative data will also be developed (see par. 3.5) in order to assess the impact of activities on women. To this end, female monitoring staff will also be recruited.

#### **Microfinance**

MISFA has five existing partners at national level i.e. FMFB, OXUS, HFL, Mutahid DFI and FINCA. MISFA enters into funding agreement on a yearly basis with its partner DFI's for providing on-lending loan and grants for various purposes. While making credit decisions, MISFA considers results of:

- Annual assessment of partners
- Current year actual performance review
- Overall sector performance

All new applicants for funding are subjected to a rigorous organizational assessment, which will also verify the availability of qualified female staff. Depending on assessment results and business plan review, MISFA credit committee approves, rejects or approves with conditions.

#### **Small and Medium Enterprises**

MISFA's SME Program was initiated in October 2006. Under this program, MISFA is developing SME lending by partnering with local financial institutions, including banks and microfinance institutions (MFIs). Although OXUS and Mutahid have a SME window, only FMFB will be used for implementing ISAME SME loans, as FMFB will benefit of the SME Credit Guarantee Facility provided by DEG. Partners are required to submit monthly reports, which are reviewed and consolidated. All stakeholders are included in distribution list for consolidated report. MISFA on-lending funds are not segregated into SME and microfinance. Partners are entitled to decide the focus with respect to product mix that they offer. The availability of products especially conceived for women will also be assessed. The results of data collection and analysis could also be used to further develop these products in order for them to meet current women's needs.

## 5.2 The Budget

The original budget of Euro 6,400,000 (100% untied) and the following budget revision and a Project no-cost extension was requested by MOF-MISFA and approved by the Government of Italy in February 2012, as per the here below table:

	<b>ISAME PROJECT COMPONENTS</b>	<b>Original budget in Mil. Euro</b>	<b>Approved budget revision in Mil. Euro</b>
1	MICROFINANCE CREDITS	2,0	2,8
2	SMEs CREDITS	2,1	1,3
3	TRAINING	0,4	0,4
4	OPERATING COSTS	1,9	1,9
	<b>TOTAL in Mil. EURO</b>	<b>6,4</b>	<b>6,4</b>

Following an external financial audit carried out by Ernst&Young for the ISAME project in May 2014, hereto is a table on the financial status of the project. In consideration that MISFA receives funds by MOF in Afghani currency, the ISAME Balance Receivable has been updated according to the exchange rate of September 2014, as follows:

<b>N.</b>	<b>Description of ISAME balance</b>	<b>Amounts in Euros</b>	<b>Amounts in Afghani</b>	<b>Exchange rate</b>	<b>Amounts in Euro</b>
1	Total Project Budget	<b>6,400,000</b>			
2	Funds Disbursed to MISFA	<b>3,718,340</b>	<b>240,720,681<sup>3</sup></b>	<b>64.74</b>	<b>3,718,340</b>
3	Funds Disbursed by MISFA (Loans/Grants to Partners)		<b>53,931,327</b>	<b>64.74</b>	<b>833,061</b>
4	Unspent Balance of ISAME Funds with MISFA (= 2 – 3)		<b>186,789,354</b>		<b>2,885,279</b>
5	Interest Earned by MISFA from Unspent Balance of the ISAME Funds		<b>8,930,037</b>	<b>73.27</b>	<b>121,880</b>
6	ISAME Balance with MISFA (= 4 + 5)		<b>195,719,391</b>		<b>3,007,158</b>
7	ISAME Balance Receivable (= 1 – 2)	<b>2,681,660</b>	<b>196,483,298<sup>4</sup></b>	<b>73.27</b>	<b>2,681,660</b>
<b>8</b>	<b>Total ISAME Unutilized Funds (Balance with MISFA + Receivables) or (= 6 + 7)</b>		<b>392,202,689</b>		<b>5,688,819</b>

<sup>3</sup> MISFA receives funding in Afghani. The exchange rate of the disbursement date for each transaction has been applied here.

<sup>4</sup> Exchange rate: Euro 1.00 = 73.269 AFN (DAB's rate for 07 September 2014)

The proposal of ISAME budget revision is as follows:

N°	ISAME PROJECT COMPONENTS	Original budget in Euro	Approved budget revision in Euro	Revised budget proposal in Euro	Balance proposal Sept. 2014 in Euro	Additional accrued bank interests in Euro	Total balance proposal Sept. 2014 in Euro	Exchange rate*	Total balance proposal Sept. 2014 in Afghani
1	MICROFINANCE CREDITS	2.000.000	2.800.000	1.556.863	1.093.462		1.093.462	64,74	70.789.353
2	SMEs CREDITS	2.100.000	1.300.000	1.081.269	1.081.269		1.081.269	64,74	70.000.000
3	TARGETING ULTRA POOR - TUP			2.681.660	2.681.660	121.880	2.803.540	73,27	205.413.335
4	TRAINING	400.000	400.000	356.793	154.467		154.467	64,74	10.000.000
5	OPERATING COSTS	1.900.000	1.900.000	723.415	556.081		556.081	64,74	36.000.000
	<b>TOTALS</b>	<b>6.400.000</b>	<b>6.400.000</b>	<b>6.400.000</b>	<b>5.566.939</b>	<b>121.880</b>	<b>5.688.819</b>		<b>392.202.688</b>

N.B. (\*) the exact average exchange rate for previous transactions is Euro 1,00 = 64,7387493 Afghani

N.B. (\*\*): updated exchange rate, Euro 1,00 = 73,26928 Afghani (07/09/2014)

### **5.3 Management and Operational Support Arrangements**

MISFA will hire an implementing partner for implementation of the TUP project through a transparent procurement process that will also take into account availability of female staff. MISFA will also enter into financing agreements with partner development finance institutions for implementing the microfinance and SME lending components of the ISAME project.

MISFA's role following awarding the contracts will include disbursing funds and monitoring and reporting on project activities throughout the life of the ISAME project. The entire partnership relations will be managed by MISFA's Program and Finance and Administration departments.

## **6. OVERVIEW, MONITORING, MANAGEMENT INFORMATION, AND REPORTING**

### **6.1 Oversight and Review**

MISFA has a dedicated department for Monitoring and Supervision for its microfinance partners and Targeting the Ultra Poor Program. MISFA developed 22 performance standards for microfinance that serve as benchmark for all our assessments and reviews. Following monitoring activities are conducted on a regular basis:

- Assessment of the existing partner institutions on a yearly basis, Gaps identified is shared with management and action plan for addressing is built with timelines in collaboration with partner management.
- MISFA also follows up on the implementation status of action plans once a year.
- All organizations applying for MISFA funding are subject to pre-assessment before entering into any funding agreement.
- Branch reviews and client verifications.

### **6.2 Knowledge Sharing**

Documenting the lessons learned by MISFA during the past decade is an objective of MISFA. There is a wealth of knowledge, best practices and lessons learned that must be captured from the evolution of MISFA, including managing the crisis phase of the microfinance sector, the consolidation process, successful implementation of TUP, transition from a project to a financial institution with stronger governance structures, and the various success factors relevant to an apex institution.

Capturing and organizing all these important knowledge and information and establishing MISFA's institutional memory in an organized, easy to refer to manner, is a strategic priority. Such knowledge would be useful for MISFA's future advocacy efforts, as well as its internal and sector wide capacity development initiatives. In addition, MISFA's experiences, while unique to Afghanistan, may nevertheless be useful to microfinance practitioners in other conflict areas.

MISFA's Knowledge Management strategy will establish permanent, technology and practice based instruments for capturing knowledge and informational tools, not only from within MISFA, but from across the development finance sector, with the long-term goal of developing a knowledge-based resource center within MISFA.

MISFA is planning to establish a dedicated knowledge management department with funding from another project to serve the purpose.

### **6.3 Communication and visibility**

Performance, achievements, outcomes and impact of the project will be communicated at two levels:

#### **6.3.1 Communication and visibility at local level:**

- **Regular Interaction:** Project staffs regularly interact with local government such as governor's office, Directorate of Rural Rehabilitation and Development (MRRD), Directorate of Agriculture, Irrigation and Livestock (DAIL), Community Development Councils (CDCs), District Development Associations (DDAs), Directorate of Women Affairs (DoWA) and other organizations and regularly update them on project's status.

#### **6.3.2 Communication and visibility at National & International Level:**

MISFA communicates project's status and achievements at National and International level through the tools described below:

- **Bi-monthly Newsletter:** MISFA publishes bi-monthly e-newsletters showcasing its achievements and new initiatives.
- **Case Stories:** it is an effective way of communicating project's impact on the lives of beneficiaries and clients, including women. MISFA regularly writes case stories of the project beneficiaries and widely distributes it through email, and in hard copies in the relevant events.
- **Annual Report:** MISFA's achievement throughout the year is communicated through publishing annual report at the end of each year. Annual Reports are widely distributed to relevant ministries, Donors, NGOs and other stakeholders in hard copies.
- **Documentaries:** MISFA produces documentaries of its projects as well. The documentaries will be displayed at different occasions to different range of people mainly government agencies, donors, implementing partners etc.
- **Impact Studies:** depending the availability of funds, a third party will be hired to study the impact of the project after the completion.

### **6.4 Reporting Schedule**

MISFA partners are required to submit Monthly Performance Report (MPR), which contains financials (Statement of financial position and Statement of comprehensive

income) and operational information (outreach, portfolio quality and other key ratios). These reports are reviewed and consolidated by MSD and are reported to donors on monthly basis. Additionally MISFA updates its donors through providing donor quarterly reports and specifically will provide an annual audited financial report on ISAME project.

## **7. ANNEXES**

- TUP Operational Manual is attached.
- Financial audit of ISAME Project carried out by Ernst & Young.