

PARLIAMENT  
OF KENYA  
LIBRARY



REPUBLIC OF KENYA  
THE NATIONAL TREASURY AND PLANNING

---

THE PERFORMANCE REPORT FOR THE MSMEs CREDIT  
GUARANTEE SCHEME

---

December, 2021

PAPERS LAID	
DATE	20/2/22
TABLED BY	DEP MAJORITY
COMMITTEE	WTIP
CLERK AT THE TABLE	M. ADIIBORU

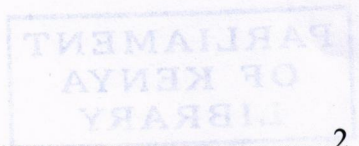


Table of Contents

A. BACKGROUND ..... 2

B. STATUTORY REPORTING REQUIREMENT ON CGS FOR MSMES ..... 3

C. CGS PERFORMANCE REPORT AS AT 31<sup>ST</sup> DECEMBER, 2021 ..... 4

    1. Risk classification of guaranteed facilities ..... 4

    2. Allocation to enterprises owned by women, youth and persons with disability ..... 5

    3. Allocation of credit guarantees by enterprise size ..... 6

    4. Allocation of credit guarantees to counties ..... 7

    5. Allocation of credit guarantees by economic sector ..... 10

    6. Trend of number of guaranteed facilities ..... 10

    7. Guarantee Utilization (Liquidity Position of the Scheme) ..... 11

D. CGS SUCCESSES ..... 12

    i. CGS Steering Committee ..... 12

    ii. CGS Operational Manuals ..... 12

    iii. Stakeholder Engagements ..... 12

    iv. PFI Capacity Building ..... 13

E. CHALLENGES IN CGS REPORTING ..... 13

F. CONCLUSION AND WAY FORWARD ..... 14

DATE	TABLED BY
COMMITTEE	CLERK AT THE TABLE

## **A. BACKGROUND**

Micro, Small and Medium Enterprises (MSMEs) are vital to Kenya's economic development and job generation, as stated in Vision 2030 and the Third Medium Term Plan (2018–2022). According to the KNBS 2016 MSME Survey, Kenya has over 7.4 million MSMEs, which employ over 14.9 million Kenyans across all sectors of the economy and account for roughly 40% of the country's GDP. Furthermore, MSMEs are a significant driver of inclusive economic growth since they cover a wide variety of activities in nearly all sectors of the economy.

Despite the critical role they play, MSMEs continue to face a variety of challenges. Most of the start-up companies do not survive their 4<sup>th</sup> birthday owing to constrained access to finance for capital and operational demands, market challenges, and weak business strategies. Further, MSMEs that access credit face unfavorable loan conditions due to a lack of sufficient collateral, high collateralization requirements, short payback periods, and high interest rates since they are viewed as risky by financial institutions. This is majorly due to information asymmetries and informal management techniques, both of which make them unappealing to lenders.

Furthermore, the Covid-19 Pandemic has had a disproportionate impact on many MSMEs. With lower turnover and interruptions in the market and supply chains, many MSMEs were and continue to be unlikely to obtain affordable and high-quality loans under traditional arrangements.

In light of the above, the National Treasury rolled out the Credit Guarantee Scheme (CGS) by entering into risk-sharing agreements with participating financial institution (PFIs) on 8<sup>th</sup> December, 2020, to support MSMEs to access quality and affordable credit. This is anticipated to help MSME businesses stay afloat and safeguard employment during and after the Covid-19 pandemic. The Credit Guarantee Scheme is anchored on the Public Finance Management (Amendment) (No.2) Act, 2020 and the Credit Guarantee Scheme Regulations, 2020. In 2020/21 financial year, the Parliament appropriated KShs. 3 billion as initial capital for purposes of the CGS.

The Credit Guarantee Scheme for MSMEs is currently being delivered through a risk sharing agreement between the Government and 7 participating banks. The seven banks are Absa, Cooperative, Credit, DTB, KCB, NCBA and Stanbic. The banks act as the intermediaries in provision of credit to qualifying MSMEs borrowers based on a pre-agreed Scheme Qualifying Criteria. Lending is done by the banks with due diligence in line with the Central Bank of Kenya Prudential Guidelines.

The maximum loan amount under the Scheme is KShs. 5 million with a tenor of 3 years and up to 5 months' grace period and discounted interest rate based on the MSMEs risk profile. The Scheme guarantees to pay the banks 50% of the outstanding principal amount, subject to a maximum of 25% of the principal amount, in case of default on qualifying credit facilities advanced to MSMEs. This provides an incentive for the banks to offer better credit terms for the qualifying MSMEs.



## **B. STATUTORY REPORTING REQUIREMENT ON CGS FOR MSMEs**

Section 59A of the Public Finance Management Act, 2012, requires the Cabinet Secretary to prepare, at least once every year, a statement of the credit guarantees granted to qualifying MSMEs, together with a report of:

- “(a) the total value of credit guarantees given during that period;*
- (b) the total value of credit guarantees liquidated during that period;*
- (c) the total value of outstanding credit guarantees on the date of the report;*
- (d) the risk assessment of the credit guarantees or classes of guarantees;*
- (e) information on the total value of credit guarantees, disaggregated into the number of enterprises owned by women, youth and persons with disabilities which have been guaranteed;*
- (f) information on the total value of credit guarantees, disaggregated into the number of micro, small and medium enterprises guaranteed and by the respective regions; and*
- (g) any other relevant information prescribed by regulations for the purposes of this section.”*

The Public Finance Management (Credit Guarantee Scheme) Regulations 2020 expounds on the reporting requirements outlined in the Act. Regulation 20 states that the Scheme Manager shall prepare and submit to the Scheme Administrator regular reports on the credit guarantees given under the Scheme including financial and technical reports on guarantees made during the period including information on:

- (i) the products and sectors for which guarantees have been issued;**
- (ii) the number of beneficiary micro, small and medium enterprises;**
- (iii) the value of credit guaranteed;**
- (iv) the repayment periods;**
- (v) the guarantees which have been liquidated;**
- (vi) reports on repayments made on outstanding credit facilities and details of any outstanding payments;**
- (vii) reports on delinquent guarantees and the stage of recovery;**
- (viii) reports on the size and quality of the guaranteed portfolio;**
- (ix) reports on the liquidity position of the Scheme; and**
- (x) the risk assessment of the credit guaranteed.**

This report is prepared pursuant to Section 59 A of the Public Finance Management Act, 2012 and it covers the period from 8<sup>th</sup> December, 2020 to 31<sup>st</sup> December, 2021.



## C. CGS PERFORMANCE REPORT AS AT 31<sup>ST</sup> DECEMBER, 2021

Approximately KShs. 2.11 billion has been disbursed to 1,291 MSMEs under the CGS to date as reported by the banks through Central Bank of Kenya. In December alone, a total of KShs. 478.3 million was issued, up from KShs. 266.6 million disbursed in November. The total value of fully repaid facilities as at 31<sup>st</sup> December, 2021 is KShs. 219.3 million. The beneficiaries of the CGS so far is support a minimum of 9,000 jobs.

In terms of credit guarantees issued under the CGS as at 31<sup>st</sup> December 2021, a total of KShs. 526,898,836.5 has been extended to qualifying MSMEs. This represents the maximum amount that the Government may pay in case the whole guaranteed portfolio is defaulted. As at 31<sup>st</sup> December 2021, no credit guarantees had been liquidated under the CGS. The outstanding credit guarantees is KShs. 472,086,131.75.

A guarantee value of KShs. 54,812,704.75 has been released as a result of full repayment of guaranteed facilities. The repaid guarantee value can be reallocated to additional qualifying enterprises, implying that the credit guarantee achieves a higher leverage ratio in unlocking private sector credit for enterprises. This presents a unique advantage of using credit guarantee schemes to support MSME access to credit.

### 1. Risk classification of guaranteed facilities

The Credit Guarantee Scheme uses the Central Bank of Kenya risk classification of assets and provisioning outlined in the Central Bank of Kenya Prudential Guidelines (CBK/PG/04). For purposes of risk classification, the facilities are classified as either Normal, Watch, Substandard, Doubtful or Loss.

As at 31<sup>st</sup> December, 2021 CGS registered 1203 active facilities with a total outstanding principal amount of KShs. 1,965,620,655. A total of **1168** were classified as “**Normal**” as at 31<sup>st</sup> December, 2021 while **24** facilities were classified as “**Watch**” in the same period. These facilities represent a total outstanding principal amount of KShs **40,118,919** representing potential claims up to a maximum of KShs **9,520,712**.

As at 31<sup>st</sup> December, 2021 **10** guaranteed credit facilities were classified as “**Substandard**”. The outstanding principal amount for the ten loans is KShs. **17,120,157** and CGS’s liability for the same is up to a maximum of 25% of the initial principal amount. In this regard, KShs **4,070,164** is due for claim and processing in accordance with the set claims procedures. One (1) facility has been classified as “**Doubtful**” with an outstanding principal amount of **Kshs. 276,982** and CGS liability in case of a claim is **Kshs. 138,491**

“**Normal**” facilities are well-documented facilities granted to financially sound customers where no weaknesses exist, and are performing, and are expected to continue to perform, in accordance with contractual terms.

**“Watch”** facilities may not be past due but exhibit potential weaknesses which may weaken the asset or inadequately protect the institution’s position at some future date. Facilities whose installments have become due and remain unpaid for a period between 30 and 90 days are classified under “Watch.”

**“Substandard”** facilities are not adequately protected by the current net worth and paying capacity of the borrower and, therefore, the institution must look to secondary sources such as collateral, sale of fixed assets, refinancing or additional capital injections for repayment. Facilities whose installments have become due and remain unpaid for a period longer than 90 days are classified under “Substandard.” PFIs can lodge claims once facilities are “Substandard.”

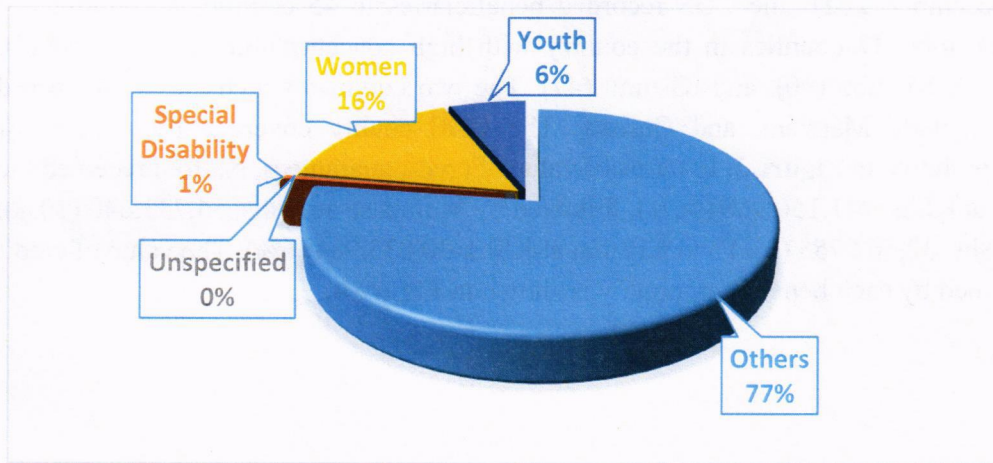
**“Doubtful”** facilities have all the weaknesses inherent in a substandard loan plus the added characteristic that the loan is not well secured. These weaknesses make collection in full, on the basis of currently existing facts, conditions, and value, highly questionable and improbable. Facilities whose installments have become due and remain unpaid for a period longer than 180 days are classified under “Doubtful.”

**“Loss”** facilities are considered uncollectible or if the collections are of such little value that their continuance recognition as bankable assets is not warranted. These facilities must have been due and unpaid for over 360 days.

## **2. Allocation to enterprises owned by women, youth and persons with disability**

As at 31<sup>st</sup> December 2021, 23% of the total number of guaranteed facilities had been disbursed to businesses owned by women, youth and persons with disabilities (PwDs) as reported by the banks through CBK. Women beneficiaries were 206, youth beneficiaries were 81 while PwDs were 6. However, in terms of value of credit guarantees the proportion extended to enterprises owned by women, youth and PwDs was 16.44%, suggesting that this category of borrowers receives on average smaller volumes of credit facilities. Women received KShs. 64,813,226.65 of the total credit guarantees extended, youth received KShs. 19,875,233.75 while PwDs received KShs. 1,937,500.00.

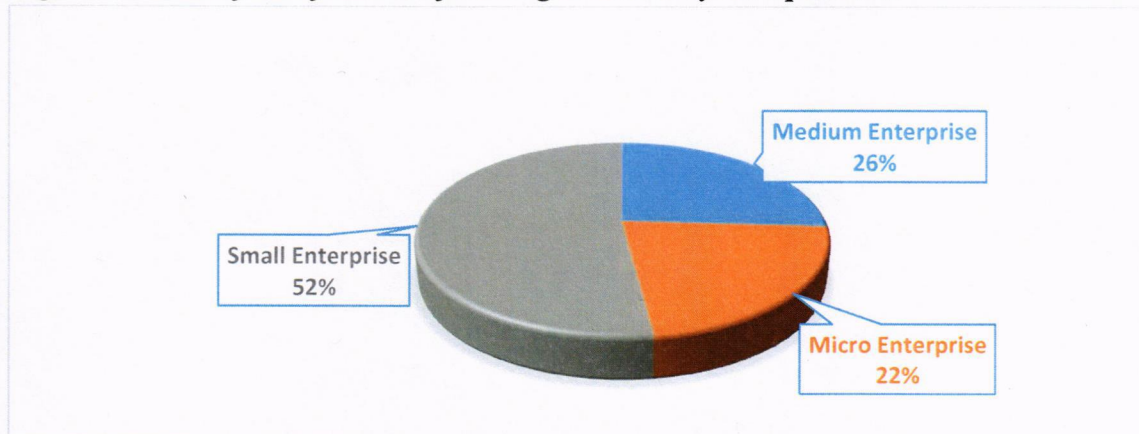
**Figure 1: Share of number of beneficiaries of credit guarantees by women, youth, PwDs and others**



### 3. Allocation of credit guarantees by enterprise size

All the three sizes of enterprises (micro, small, and medium) have benefitted from CGS facilities as reported by the banks through CBK. Of the 1291 facilities issued, small enterprises received 672, medium enterprises received 334 while micro enterprises received 285. In terms of value of facilities, small enterprises received KShs. 284,975,780.86, medium enterprises received KShs. 183,818,222.25 while micro enterprises received KShs. 58,104,833.50. The proportion of credit guarantees allocated to micro enterprises can be attributed to the average size of their loans being smaller than either of small and medium enterprises. The application of the legal definition of micro, small and medium enterprises has been a challenge whereby an enterprise can be micro by one criterion and small by another. The Scheme is consulting relevant Government Institutions on the application of this legal definition, noting that if the definition was administered in the strict sense it would lock out many MSMEs. The share of the facilities by enterprise size is illustrated in **Figure 2**.

**Figure 2: Share of beneficiaries of credit guarantees by enterprise size**

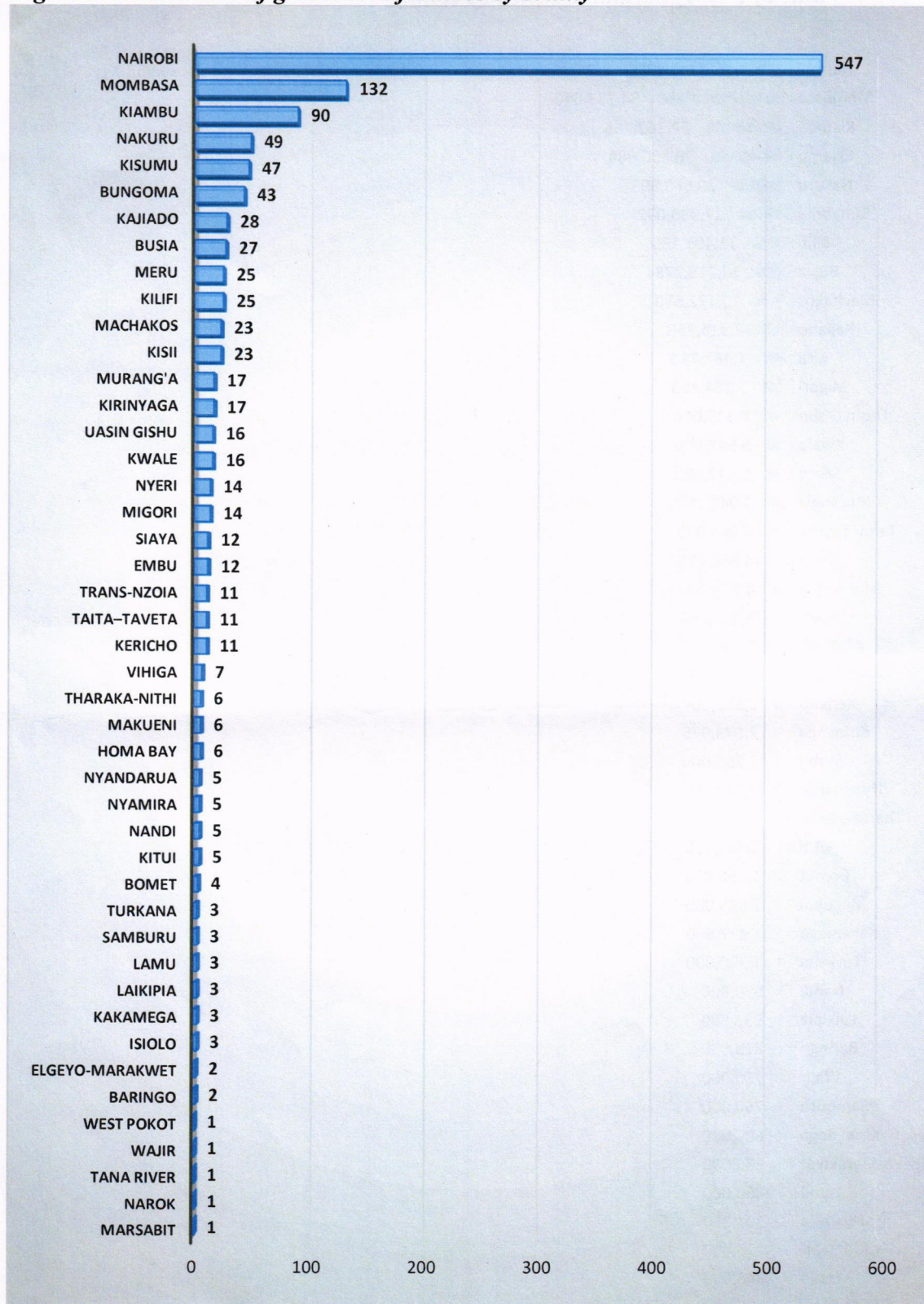




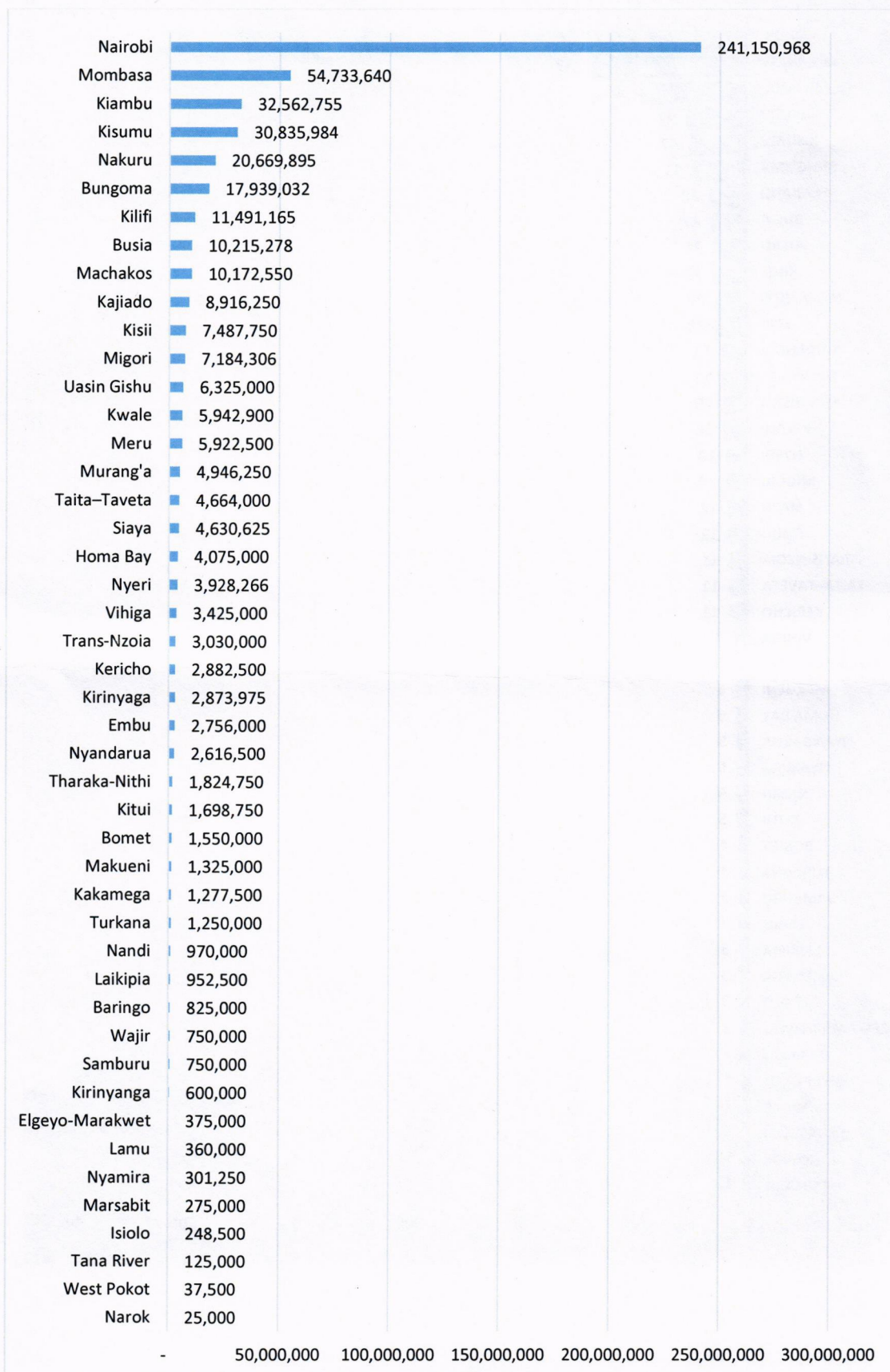
#### 4. Allocation of credit guarantees to counties

As at 31<sup>st</sup> December, 2021, the CGS recorded beneficiaries in 45 counties accounting for 93.75% of the total 47 counties in the country with high concentration in Nairobi (547), Mombasa (132), Kiambu (90), and Kisumu (47). The two counties which are yet to record beneficiaries include Mandera, and Garissa. The CGS county coverage by number of beneficiaries is shown in **Figure 3**. In terms of value of credit guarantees, Nairobi received the highest share at KShs. 241,150,968 (46%), followed by Mombasa at KShs. 54,733,640 (10%), Kiambu at KShs. 32,562,755 (6%) and Kisumu at KShs. 30,835,984 (6%). The value of credit guarantees issued by each beneficiary county is shown in **Figure 4**.

**Figure 3: Distribution of guaranteed facilities by county**



**Figure 4: Value of credit guarantees issued by county**

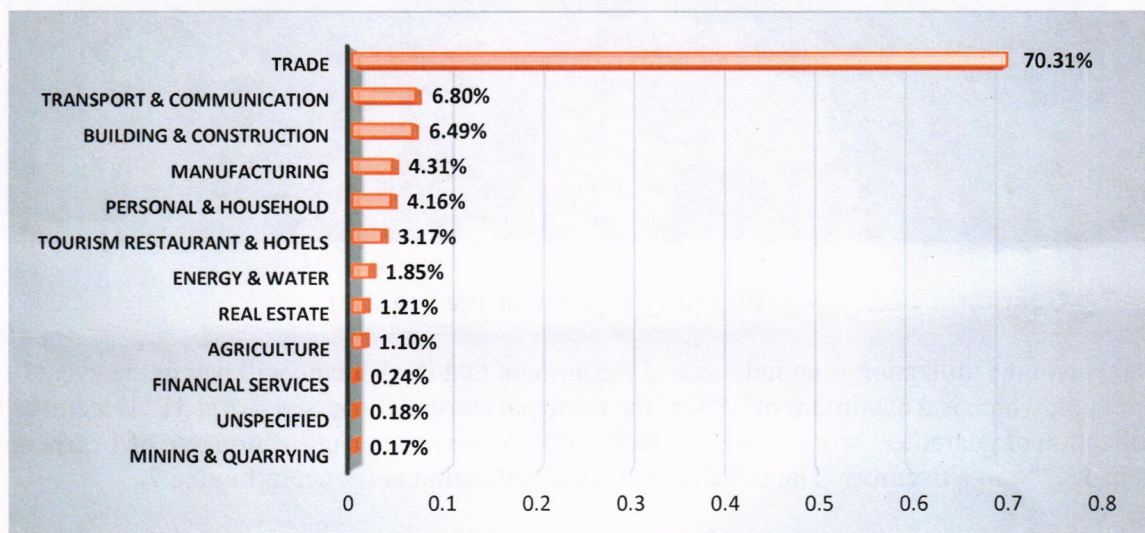




## 5. Allocation of credit guarantees by economic sector

The facilities placed under the scheme have been distributed across eleven (11) sectors. Trade Sector continues to lead with 70.31% of the total facility value up from 66.91% in the previous month, which is still higher than the sector limit of 40% as per the CGS Agreement. This is followed by Transport and Communication (6.80%), Building and Construction (6.49%) and Manufacturing (4.31%). A disproportionately small number of credit facilities has been allocated to Agriculture (1.10%) and Financial Services (0.24%) sectors. This could be attributed to the definition of sectors in the banking industry. For instance, agriculture is restricted to on-farm activities and excludes MSMEs in the value chain. The National Treasury is working with the relevant Government agencies to address low uptake in Agriculture including designing sector specific product. The share of the facilities by sector is illustrated in **Figure 5**.

*Figure 5: Share of credit guarantees by economy sector*

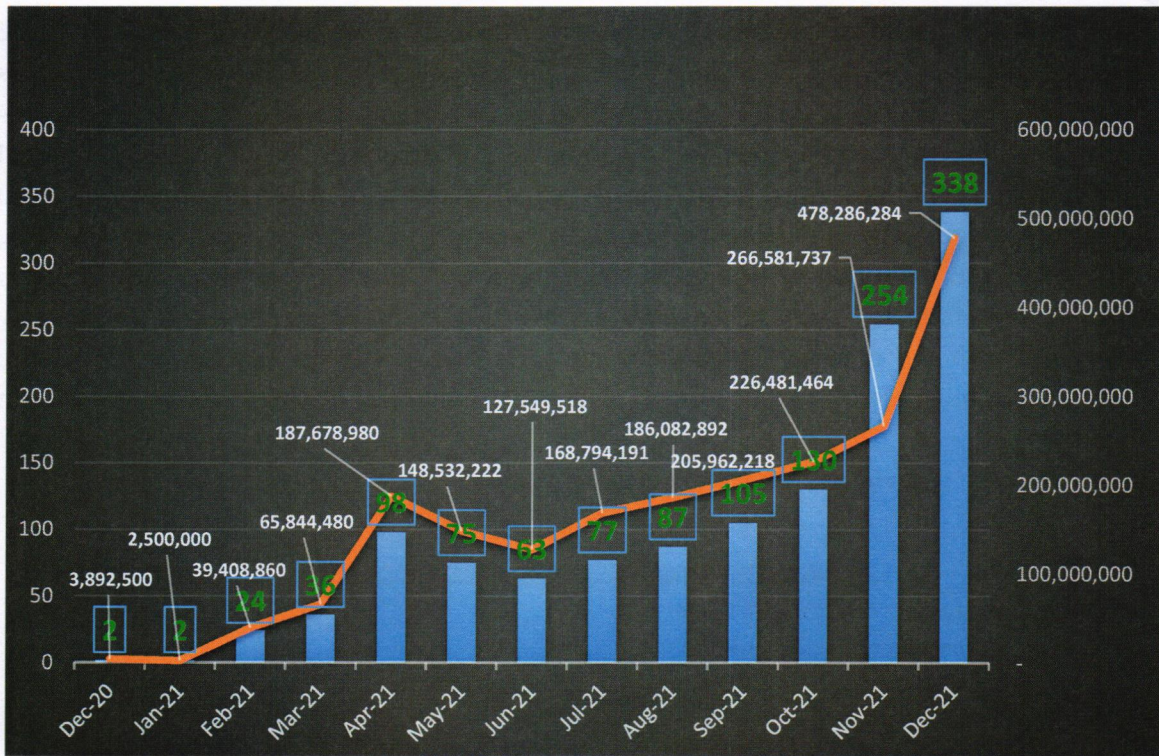


## 6. Trend of number of guaranteed facilities

In the period, December 2020 to January 2021, PFIs were establishing internal structures and systems to facilitate the implementation of the Scheme explaining the low utilization of guarantees in those months. Disbursements of guaranteed facilities increased in the months of February (37), March (47), and April (118). CGS recorded a decline in the number of guaranteed facilities in the months of May (71) and June (61). Nonetheless, the number of guaranteed facilities increased in the months of July (74), August (93), September (119), October (122) and November (251) with December recording the highest CGS performance in terms of number and value of facilities since inception. The trend of number and value of facilities by month is shown below in **Figure 6**.



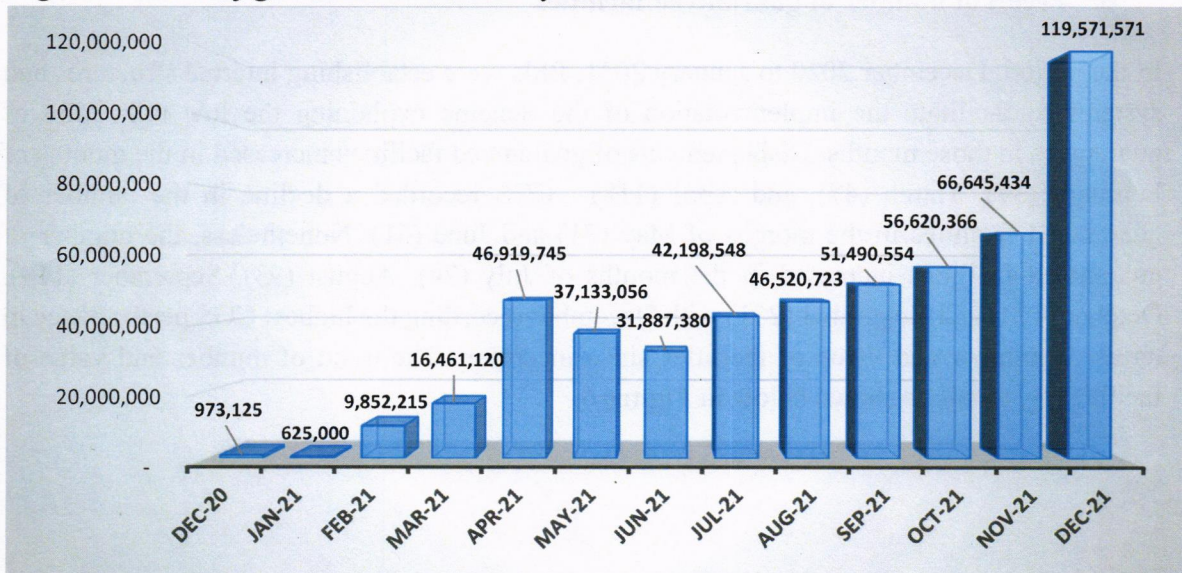
**Figure 6: Trend of facilities by month**



**7. Guarantee Utilization (Liquidity Position of the Scheme)**

The guarantee utilization is an indicator of the amount that the Scheme will pay in the event of a default, which is a maximum of 25% of the principal amount disbursed. As at 31<sup>st</sup> December, utilization of guarantees stood at KShs 526,898,837 representing a utilization rate of 17.6% up from 15.7% in November. The trend of guarantee utilization is shown in Figure 7.

**Figure 7: Trend of guarantee utilization by month**



## **D. CGS SUCCESSES**

Since its inception, the Scheme has achieved the following milestones:

### **i. CGS Steering Committee**

The CGS has a fully constituted Steering Committee comprising of the following members:

- i. PS, National Treasury, Chairperson
- ii. PS or PS's alternate/State Department for Industrialization
- iii. Attorney General or Attorney General's alternate
- iv. Governor, Central Bank of Kenya
- v. 3 independent members with experience in finance/banking, insurance and entrepreneurship

The Steering Committee has held five meetings since inception and provided the required oversight on the management of the Scheme in line with the CGS Regulations, 2020.

### **ii. CGS Operational Manuals**

The CGS technical team developed five manuals to guide the operations of the Scheme. The manuals are necessary to guide the discharging of CGS obligations in accordance with the law as well as the credit guarantee agreements. The CGS received and considered comments from stakeholders before finalization of the manuals. Subsequently, the five manuals were approved by the Steering Committee for use by the Scheme, and include:

- i. CGS Operations Manual;
- ii. CGS Risk Management and Compliance Manual;
- iii. CGS Monitoring and Evaluation Manual;
- iv. CGS Claims Procedure Manual; and
- v. CGS Finance and Accounting Procedure Manual.

### **iii. Stakeholder Engagements**

The scheme has engaged various stakeholders on credit guarantee scheme as follows:

#### **a) Sensitization of Ministries, Departments and Agencies on CGS**

CGS technical team conducted a virtual conference on credit guarantees, focusing on participants from Government Ministries, Departments and Agencies on 10th November 2021. The meeting was attended by 58 officials from various MDAs. Participants raised important comments, suggestions for enhancing the impact of CGS as well as offers for partnership and collaboration in the implementation of the CGS. A detailed record of the meeting with MDAs has also been prepared. CGS had also engaged State Department for Culture & Heritage and the State Department for Public Works and explored mechanisms to incorporate MSMEs in the creative and construction industries into the CGS.

- b) **PFI**s: CGS initiated a series of interactions with the PFI's to ensure compliance with the legal and operational requirements of the Scheme. During the sessions, the PFI's shared their experiences and challenges that contributed to low uptake of CGS facilities. Based



on the feedback from the PFIs, a set of recommendations have been forwarded for consideration by the Steering Committee in a bid to enhance the impact of the CGS.

- c) **African Women’s Studies Centre, University of Nairobi (AWSC):** The CGS Unit has partnered with the AWSC that hosts the Women Economic Empowerment (WEE) Hub to explore ways for improving access to guaranteed credit by women owned/led enterprises. The CGS technical team together with the WEE Hub are currently undertaking a study on the possible explanations for the low uptake of guarantees among women entrepreneurs. The findings will be useful in guiding targeted interventions to increase uptake of credit guarantees.
- d) **Kenya Bankers Association (KBA):** The CGS has been working closely with KBA to increase CGS awareness among bankers and MSMEs. KBA was a key partner during the design phase of the credit guarantee product. KBA hosts various webinars with the industry practitioners and MSMEs where the CGS is invited to pitch and make presentations. One of such webinars was held on 26<sup>th</sup> November 2021 themed “Boosting MSMEs Competitive Edge.”
- e) **Development partners:** FSD-Kenya supported the CGS feasibility study and is currently supporting acquisition of a credit guarantee monitoring system. Based on their experience in implementing credit guarantees locally and internationally, USAID and AGF have also continued to provide technical assistance to the implementation of the CGS. The National Treasury is in discussions with the World Bank, IFAD and KfW who have expressed interest in providing targeted credit guarantee products through the CGS. These partnerships are expected to ramp up the coverage and increase the impact of the CGS in the economy.

#### iv. PFI Capacity Building

The National Treasury conducted a targeted training for PFIs from 25<sup>th</sup> to 29<sup>th</sup> October 2021. The objective of the training was to increase the uptake of credit guarantees and minimize the risk of moral hazard in CGS implementation. The session provided the CGS and PFIs with feedback and lessons to improve the performance of the Scheme.

### E. CHALLENGES IN CGS REPORTING

- i. **Sector classification-**the definition of economic sectors in the banking industry may be contributing to misclassification of some MSMEs. For instance, some enterprises involved in health care services, education and agricultural value chain are being classified as trade.
- ii. **Informality of MSMEs:** Most MSMEs are informal and hence are not tax compliant and most of these enterprises are not registered by the relevant Government Agency as required by Regulation 10 of the CGS Regulations.
- iii. **Definition of micro, small and medium enterprises-**most of the enterprises do not fully fulfil the definition criteria set out in the PFM Act, 2012, and the MSE Act, 2012. Consequently, an enterprise could be micro by number of employees while according to turnover it could be classified as small or medium enterprise.

- iv. **COVID-19 pandemic:** The COVID-19 pandemic resulted into slowdown of economic activities which may have to low uptake of the guaranteed facilities.
- v. **Moral hazard:** The challenge to create awareness on the credit guarantee while safeguarding the CGS from the risk of moral hazard.

## **F. CONCLUSION AND WAY FORWARD**

The CGS performance report demonstrates how the Government has leveraged on private sector resources to provide credit to MSMEs while advancing its development objectives. Through the scheme, the PFIs have been able to lend KShs. 2.11 billion to MSMEs. Furthermore, participating banks are implementing the Scheme through their existing branch networks and infrastructure allowing them reach out to MSMEs in more counties compared to other government initiatives. This is evidenced by the outreach to 45 counties, outreach to women and youth and to both micro, small and medium enterprises.

The following actions are necessary to ensure that the Scheme achieves its founding objectives:

- i. In order to address the challenge of sector classification, the National Treasury is working with CBK to enhance detailed reporting including subsector and nature of business.
- ii. To promote the formality of MSMEs, the CGS continue engaging the relevant Government Agencies (Business Registration Services and Kenya Revenue Authority) to explore on various ways of increasing penetration of informal MSMEs, for registration and tax compliance.
- iii. The National Treasury to engage with relevant Government Institutions to address the challenge of MSMEs classification as per the law.