

DEG Horizons

Our business is developing.



FINANCIAL SECTOR DEVELOPMENT

is one of the areas where DEG is particularly involved. DEG supports institutional strengthening of the private financial sector in developing countries and the provision of investment capital for small and medium-sized enterprises.

RELIABLE ACCESS TO CAPITAL. HOW DEG PROMOTES THE FINANCIAL SECTOR.

The financial sector is an essential part of an efficient economic system. The main task of the financial sector and its institutions is to provide the economy with liquidity and to mobilize savings that are invested in the country. An important prerequisite here is that investors and companies have confidence in the stability of the financial sector. The main tasks of the sector and its institutions are to provide the economy with liquidity and to mobilize savings invested in the country. The financial sector in many developing countries is, however, not yet sufficiently well developed: the finance institutions are often beset with institutional weaknesses, banking supervision is in need of improvement and banks have hardly any long-term refinance facilities. Banks are very cautious because of the risks involved in this sector and, accordingly, long-term capital in particular is practically unobtainable. It is then often small enterprises that cannot borrow the funds they need for investment because they do not have adequate collateral. Moreover, the range of financial services available in developing countries is limited, so that products that are heavily in demand, such as mortgage loans or leasing finance, are not available.

DEG is a finance institution for promoting private enterprise in developing and emerging countries and has been actively engaged in the development of the financial sector since its establishment in 1962. It supports establishing a functioning diversified financial sector as the key sector in an economic system. DEG's activities are oriented according to the guidelines for financial sector development laid down by Germany's Federal Ministry for Economic Co-operation and Development

(BMZ). The BMZ's concept for the financial system development sector emphasizes the key significance of the financial system in the process of economic and social development. In many developing countries the financial system is still a bottleneck in the development process; they should be given support to establish efficient, integrated systems and functional institutions. Improving the access of all customer groups to financial services and bridging gaps in the types of finance available make important contributions to this. With its services specially tailored to private financial institutions, DEG takes the importance of the private sector in the development of the financial system into account.

DEG is involved at various levels. It plays a part in the setting up and institutional strengthening of private finance institutions and thus contributes to the stabilization of the sector. It does what it can to expand the range of financial services being offered. And it enables small and medium-sized enterprises in particular to have access to investment capital by providing long-term refinance to local banks. It also sends a signal to other investors by deliberately getting involved in less developed markets as well. DEG finance can be arranged in different ways to meet the requirements of the banks and the demands of the final borrowers – loans, lines of credit, guarantees for credit institutions as well as mezzanine finance and equity, for instance in private-equity funds. DEG's involvement of many years in supporting the financial sector is reflected in its portfolio: financial sector projects represent a 44%-share of the total volume of EUR 2.4 billion.



CAPITAL AND KNOW-HOW FOR STRENGTHENING FINANCE INSTITUTIONS.

The institutional strengthening of private finance institutions is one of DEG's main tasks in the development of the financial sector. It provides the institutions with long-term capital and provides them with advice based on years of financial expertise. In this way it can help stabilize financial sectors, especially where these are less developed.

DEG holds equity in ACLEDA, a bank in Cambodia that emerged from a local non-governmental organization. KfW played a decisive role in professionalizing ACLEDA in the 90s. DEG provided the institution with finance for the first time in 2000 in the form of equity financing. DEG increased its equity in ACLEDA last year after the bank had obtained its full banking licence. DEG has a say in the development of the bank through its seat on the supervisory board. ACLEDA is one of the few financial institutions in Cambodia that provides loans in local currency in a country where there is strong dollarization. It can offer the complete range of financial services via a nationwide network. This enables it to reach large parts of the population, which is mostly poor.

DEG is also actively supporting the stabilization of finance institutions in transition countries in central and eastern Europe. It is active in Georgia in a financial sector that is characterized by restructuring and the economic crisis at the end of the 90s. Longer term investment capital for enterprises is practically unavailable. DEG is currently involved in three banks in the country. They include the private Bank of Georgia, which was formally a state-owned bank. As a result of its equity share, DEG has an important say in the bank's business policy and at the same time its involvement sends out a positive signal for other investors in Georgia. DEG also has equity in a commercial bank, TBC Bank, and uses its seat on the board to exercise its supervisory and advisory functions.

CREDIT LINES FOR SME FINANCE.

Another objective of DEG's financial sector development is to enable small and medium sized enterprises (SME) to have access to long-term investment capital. To achieve this, DEG works together with local finance institutions and grants them lines of credit provided the funds are passed on to SME.

Kazakhstan's Kazkommertsbank received a line of credit in 1998 and a second line in 2002 to satisfy the capital needs of small and medium-sized enterprises. A lack of long-term finance is a major bottleneck in the development of the private sector in Kazakhstan. The country is very dependent on exports of oil and other raw materials and diversification is very important for the country's economy. The credit lines enable enterprises engaged in areas such as agriculture, building and construction and the food industry to obtain loans for their investments from their local banks.

Another example is a long-term loan DEG made available to the Turkish Garanti Bank. It was made explicitly available to provide investment capital for small and medium sized Turkish enterprises from the Marmara region that was affected by a devastating earthquake in August 1999 in which more than 15,000 people died. The local bank continually informs DEG about the lending of loans to final borrowers. With the help of the DEG finance, numerous Turkish companies from the region were able to obtain investment credits.



CAPITAL FOR INVESTMENT FUNDS WITH IMPORTANT DEVELOPMENTAL IMPACT.

Another field where DEG is active is financing private-equity corporations that provide capital for investments that have a positive developmental impact, such as healthcare or training. An example is the Emerging Africa Infrastructure Fund, which was initiated by the UK Government's Department for International Development; together with other providers of development finance DEG has introduced mezzanine finance in the form of subordinated loans. This has mobilized private finance institutions, which provided senior loans. The fund finances private infrastructure projects – energy and water supply, telecommunications and the transport industry – in sub-Saharan Africa. An example is a mobile phone project that is currently providing a telecommunications infrastructure for 12 African countries, including Tanzania, Gabon, the Republic of the Congo, Malawi and Nigeria.

DEG has equity in an IT fund of South Africa's Ethos Holding. The development of information technology and telecommunications is important, not least for the economic development of the region. Providing capital for up-and-coming local IT enterprises via the IT fund can make a contribution. DEG is also co-financing a company in South Africa, Edu Loan, whose loans enable working people on low-income to participate in university training programmes. The workers obtain small amounts of credit so that they can finance their training and further education; a specially developed repayment scheme ensures that the borrowers are well able to discharge their responsibilities.

EXTENDING THE RANGE OF FINANCIAL SERVICES AVAILABLE.

In less diversified financial sectors, DEG promotes a broadening of the range of financial services offered, especially to enable less financially strong enterprises to have access to products that are in demand but not available locally. Leasing finance is a good example; companies do not have to use their own funds to acquire the leased item, which itself provides the securities, so that small enterprises with little capital and collateral are in a position to use modern machinery and equipment. However, this product, which would be particularly useful in developing countries, is not widely available there. DEG is refinancing leasing companies in countries such as Thailand, Romania and Turkey. It is thus paving the way for them to finance their leasing business with matching maturities.

In many developing countries it is above all low-income groups that have inadequate access to mortgage loans. To improve housing finance, DEG invests in special institutions that offer such products: in Romania, for example, where DEG co-financed the country's first mortgage bank, Domenia Credit, in 2002, together with the IFC and other partners; or the Egyptian Housing Finance Corporation, in which it holds equity. Egypt's first private mortgage bank was set up with the support of India's HDFC, with which KfW and DEG have cooperated for a long time. Established in 1977 as India's first mortgage finance institution, it is now the country's largest provider of finance for house-building.



NEW FINANCIAL-SECTOR PROJECT COMMITMENTS.

Last year, DEG provided finance amounting to EUR 219 million for 35 projects in the financial sector, which is equivalent to 43% of all new commitments in 2003. On a product basis, most of these commitments were for long-term loans followed by equity and equity funds, mezzanine finance and guarantees.

Loans for medium-sized agricultural businesses in Latin America

DEG awarded a long-term loan to the regional Latin American Agribusiness Development Corporation (LAAD). This company gives medium-sized, export-dedicated enterprises in agriculture and food access to investment finance that they would otherwise be practically unable to obtain. This allows investments to be realized even in countries like Ecuador and Bolivia, which are regarded as high risks, thereby promoting employment in the agricultural sector.

Guarantee for bond issued by a Mexican mortgage bank

In addition to offering credit for house-building companies, the Mexican mortgage bank Crédito y Casa S.A. (CyC) also offers mortgage loans to families with medium and small incomes – loans that are in great demand. CyC has issued a bond to put its refinancing on a broader footing. By guaranteeing to support the bond securitization transaction, DEG contributed to securing the market placing of the bond. The improved refinance means CyC can grant additional credit to

finance simple housing. As a result, this new kind of bond provides an alternative for institutional investors in Mexico, who until now have practically only been able to invest in government bonds.

Equity in an East African investment company

The investment company Industrial Promotion Services Kenya Ltd. (IPSK) acquires equity in the industrial sector and in infrastructure projects; it has a say in the strategic orientation of the enterprises in which it holds equity. The Aga Khan Fund for Economic Development (AKFED), with which DEG has cooperated for over 20 years on various projects, is IPSK's majority shareholder. IPSK is planning to enlarge its equity portfolio in Kenya and expand into Tanzania and Uganda. DEG participated in providing the increase in capital required. Through its seat on the board of directors it plays an active role in determining IPSK's business policy and evaluating and selecting projects. IPSK is making an important contribution to African enterprises that would otherwise not have had access to investment capital.

DEG

- DEG has been financing and structuring the investments of private companies in developing and transition countries for more than 40 years.
- DEG invests in profitable projects that contribute to sustainable development in all sectors of the economy, from agriculture to infrastructure and manufacturing to services. We also focus on investments in local capital markets in order to facilitate reliable access to capital locally.
- So far, we have worked together with more than 1,100 companies. By providing 5.6 billion euros of finance, we have achieved a total investment of 37 billion euros.
- Our aim is to establish and expand private enterprise structures in developing and transition countries, and thus create the basis for sustainable economic growth and a lasting improvement in the living conditions of the local population.

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