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Report No: PAD5269

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

PROJECT APPRAISAL DOCUMENT
ON A
PROPOSED GRANT

IN THE AMOUNT OF EUR 10 MILLION
(US$ 10.69 MILLION EQUIVALENT)

TO

UKRAINE

FOR

STRENGTHENING THE PARTIAL CREDIT GUARANTEE (PCG) FUND FOR SMALL FARMERS IN UKRAINE (STRENGTHENING THE PARTIAL CREDIT GUARANTEE FUND IN AGRICULTURE PROJECT)

July 28, 2023

Finance, Competitiveness And Innovation Global Practice
Europe And Central Asia Region

CURRENCY EQUIVALENTS

(Exchange Rate Effective May 31, 2023)

Currency Unit =	Ukrainian Hryvnia (UAH)
UAH 36.57 =	US$1
US$ 1.33 =	SDR 1

FISCAL YEAR
January 1 - December 31

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ABBREVIATIONS AND ACRONYMS

AM	Accountability Mechanism
AQR	Asset Quality Review
CGS	Credit Guarantee Scheme
CMU	Cabinet of Ministers of Ukraine
CPF	Country Partnership Framework
EBRD	European Bank for Reconstruction and Development
ECA	Europe and Central Asia
EIB	European Investment Bank
ERW	Explosive Remnants of War
ESMS	Environmental and Social Management Systems
ESRS	Environmental and Social Review Summary
ESS	Environmental and Social Standards
EU	European Union
EUR	Euro
FAO	Food and Agriculture Organization
FIF	Financial Intermediary Financing
FM	Financial Management
FX	Foreign Currency
GDP	Gross Domestic Product
GoU	Government of Ukraine
GRS	World Bank Grievance Redress Service
ha	hectares
HQ	Headquarters
IFC	International Financial Corporation
IFI	International Financial Institution
IUFRs	Interim Unaudited Financial Reports
LCR	Liquidity coverage ratio
M&E	Monitoring and evaluation
MAPF	Ministry of Agrarian Policy and Food
NBU	National Bank of Ukraine
NDC	National Determined Contribution
NPL	Non-performing loans
PCG	Partial Credit Guarantee
PCGF	Partial Credit Guarantee Fund in Agriculture
PDO	Project Development Objective
PFI	Participating Financial Institutions
PIT	Project Coordination Team
POM	Project Operational Manual
POS	Point of Sale
RE	Recipient-executed Trust Fund

SAR	State Agrarian Registry
SEA/SH	Sexual Exploitation and Abuse/Sexual Harassment
SME	Small and Medium Enterprise
SOBs	State-owned banks
SW	Staff weeks
TF	Trust Fund
UAH	Ukrainian Hrynvia
USAID	United States Agency for International Development
USD	United States Dollar
WB	World Bank
WBG	World Bank Group

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DATASHEET

BASIC INFORMATION

Country(ies)	Project Name	
Ukraine	Strengthening the Partial Credit Guarantee (PCG) Fund for small farmers in Ukraine (Strengthening the PCGF in Agriculture Project)	
Project ID	Financing Instrument	Environmental and Social Risk Classification
P180242	Investment Project Financing	Substantial

Financing & Implementation Modalities

[ ] Multiphase Programmatic Approach (MPA)	[ ] Contingent Emergency Response Component (CERC)
[ ] Series of Projects (SOP)	[√] Fragile State(s)
[ ] Performance-Based Conditions (PBCs)	[ ] Small State(s)
[√] Financial Intermediaries (FI)	[ ] Fragile within a non-fragile Country
[ ] Project-Based Guarantee	[√] Conflict
[ ] Deferred Drawdown	[ ] Responding to Natural or Man-made Disaster
[ ] Alternate Procurement Arrangements (APA)	[ ] Hands-on Enhanced Implementation Support (HEIS)

Expected Approval Date	Expected Closing Date
31-Mar-2023	30-Jun-2026
Bank/IFC Collaboration	Joint Level
Yes	Joint Project - involving co financing with IFC (loan, equity, budget, other) or staffing

Proposed Development Objective(s)

The Project development objective (PDO) is to operationalize the Partial Credit Guarantee Fund in Agriculture (PCGF) to help improve access to financing for small farmers in Ukraine.

Components

Component Name	Cost (US$, millions)
Capitalization of the PCGF for the provision of Partial Credit Guarantees to Eligible PFIs for Agricultural Loans	10.69

Organizations

Borrower:	Ministry of Agrarian Policy and Food
Implementing Agency:	Ministry of Agrarian Policy and Food Partial Credit Guarantee Fund

PROJECT FINANCING DATA (US$, Millions)

SUMMARY

Total Project Cost	106.25
Total Financing	100.00
of which IBRD/IDA	0.00
Financing Gap	6.25

DETAILS

Non-World Bank Group Financing

Trust Funds	10.69
Miscellaneous 1	10.69
Commercial Financing	85.49
Commercial Financing Guaranteed	42.74
Unguaranteed Commercial Financing	42.74

Expected Disbursements (in US$, Millions)

WB Fiscal Year	2023	2024	2025	2026
Annual	0.00	10.69	0.00	0.00

Cumulative	0.00	10.69	10.69	10.69

INSTITUTIONAL DATA

Practice Area (Lead)
Finance, Competitiveness and Innovation

Contributing Practice Areas

SYSTEMATIC OPERATIONS RISK-RATING TOOL (SORT)

Risk Category	Rating
1. Political and Governance	High
2. Macroeconomic	High
3. Sector Strategies and Policies	Moderate
4. Technical Design of Project or Program	Substantial
5. Institutional Capacity for Implementation and Sustainability	Substantial
6. Fiduciary	Substantial
7. Environment and Social	Substantial
8. Stakeholders	Substantial
9. Other	
10. Overall	Substantial

COMPLIANCE

Policy
Does the project depart from the CPF in content or in other significant respects?

[ ] Yes [✓] No

Does the project require any waivers of Bank policies?

[ ] Yes [✓] No

Environmental and Social Standards Relevance Given its Context at the Time of Appraisal

E & S Standards	Relevance
Assessment and Management of Environmental and Social Risks and Impacts	Relevant
Stakeholder Engagement and Information Disclosure	Relevant
Labor and Working Conditions	Relevant
Resource Efficiency and Pollution Prevention and Management	Relevant
Community Health and Safety	Relevant
Land Acquisition, Restrictions on Land Use and Involuntary Resettlement	Not Currently Relevant
Biodiversity Conservation and Sustainable Management of Living Natural Resources	Relevant
Indigenous Peoples/Sub-Saharan African Historically Underserved Traditional Local Communities	Not Currently Relevant
Cultural Heritage	Not Currently Relevant
Financial Intermediaries	Relevant

NOTE: For further information regarding the World Bank's due diligence assessment of the Project's potential environmental and social risks and impacts, please refer to the Project's Appraisal Environmental and Social Review Summary (ESRS).

Legal Covenants

Sections and Description
Schedule 2, Section I.A.2. of the Grant Agreement: The Recipient, through MAPF, shall, not later than one month from Effective Date, establish, and thereafter maintain at all times during Project implementation, a Project Coordination Team ("PIT"), with functions and responsibilities acceptable to the Bank as set forth in the Project Operational Manual.

Sections and Description
Schedule 2, Section I.A.3. of the Grant Agreement: The Recipient, through the MAPF, shall cause PCGF to hire, not later than one month from Effective Date, and thereafter maintain, at all times during Project implementation, one or more environmental and social specialists, as needed, with terms of reference and qualifications acceptable to the Bank.

Sections and Description

Schedule 2, Section I.C.1. of the Grant Agreement: No later than one month after the effectiveness of the Grant Agreement, the Recipient, through the MAPF, shall adopt the POM in form and substance acceptable to the Bank, containing detailed implementation and institutional arrangements for the Project.

Conditions

Type	Financing source	Description
Effectiveness	Trust Funds	The Grant Agreement shall not become effective until evidence satisfactory to the Bank has been furnished to the Bank that the conditions specified below have been satisfied: (a) the Recipient has signed the Subsidiary Agreement with the PCGF on terms and conditions satisfactory to the Bank; and (b) the Subsidiary Agreement referenced above in Section 5.01 (a) of the Grant Agreement and this Agreement have been duly authorized or ratified by all necessary governmental action.

Type	Financing source	Description
Disbursement	Trust Funds	No withdrawal shall be made: (a) for payments made prior to the Signature Date; or (b) under Category 2 until and unless the Bank has received adequate evidence that: (a) PCGF Internal Regulations are adopted and approved; (b) the PCGF Board and the PCGF Management Board are duly elected and appointed; (c) a risk manager and internal auditor are appointed to the PCGF; and (d) at least one PFI has signed a Participation Agreement with the PCGF; all in form and substance satisfactory to the Bank.

I. STRATEGIC CONTEXT

A. Country Context

1. **The 20-year-old moratorium on sales and purchases of farmland was lifted on July 1, 2021, opening the agricultural land market**. The approved law lifted the moratorium on land sales and allowed purchases by individuals up to 100 ha from July 1, 2021, and purchases by legal entities from January 1, 2024, with the right to buy agricultural land initially limited to Ukrainian citizens. Land transactions have been steadily growing since July 2021 as people are gaining confidence in the market. The area of agricultural land traded each month has been growing steadily in 2021, reaching over 71,000 ha/month in December 2021. Since the start of Russia's invasion of Ukraine, the volume of traded land dropped from over 43,000 ha in February 2022 to less than 7,000 ha in June 2022 and reached close to 17,000 ha in December 2022. Agricultural land prices appear to have remained largely stable in the first three months since the opening of the land market, averaging at UAH 33,000 per ha and increasing by 12 percent in 2022 to UAH 40,000.

2. **The land market opening is expected to have positive economic and social impacts**. First, the reform is expected to increase agricultural and overall economic growth through increased investments in land with clear rules on property rights. Second, the reform will transfer resources, in the form of increased land prices, to landowners and create collateralizable assets for rural investments. As landowners are mainly rural, older, less educated, and female, the reform would essentially transfer resources to the more vulnerable segments of the Ukrainian population. Third, the reform has the potential to revive local communities and enhance local services through the revenue streams generated by auctioning off state and communal land.

3. **The land reforms have already shown positive impact despite the difficult environment**. During the first 4 months of its operation, mandatory e-auctions for farmland in state and communal ownership, combined with transfer of public land ownership to local councils, doubled the leases paid. After a brief suspension at the start of Russia's invasion of Ukraine, land markets continue to operate at almost pre-invasion levels in the areas not directly affected by Russia's invasion of Ukraine. Moreover, in the context of the country's European Union (EU) accession, key elements of land reform implementation were adopted in a law in June 2022. A resolution of the Cabinet of Ministers of Ukraine (CMU) detailing a time-bound action plan to implement land reform priorities as laid out in the Anti-Corruption Strategy 2021-2025 (adopted by the Law No. 2322-IX from June 20, 2022) is overdue and expected to be approved in the first quarter of 2023.

4. **Before Russia's invasion of Ukraine began, the government of Ukraine (GoU) put in place key legal, regulatory, and supervisory elements of a commercially viable partial credit guarantee fund (PCGF), with a sound independent governance framework, which will support access to finance of small credit-constrained farmers**. The related legislation came into effect on November 24, 2021, and steps towards operationalization of the PCGF are progressing well. The Cabinet of Ministers of Ukraine (CMU) adopted resolution #125 dated February 16, 2022, on establishing the PCGF and adopting the PCGF Charter. Three other resolutions detailing the recruitment process, remuneration and eligibility criteria for independent PCGF Supervisory Board members were also adopted. The adopted PCGF Charter foresees that the PCGF Supervisory Board consists of five members, three of which shall be independent, and with its chairperson selected among its independent members. In August 2022, the National Bank of Ukraine (NBU), as the regulator of the PCGF, adopted a special regulation on PCGF activities, which includes a set of micro-prudential requirements for the PCGF. On February 6, 2023, the NBU licensed PCGF as a nonbanking financial institution focused on providing guarantees. Next steps will be the

recruitment of the PCGF Supervisory and Management boards.

5. **In parallel, the State Agrarian Registry (SAR) has been launched successfully in mid-August 2022 and now has more than 80,000 farmers registered**. It is has been used to implement (i) a EUR 50 million program of cash grants to small farmers (< 120 ha and/or <100 cows) that was started in early September 2022 and was fully committed at the end of October; (ii) a program to provide grain storage to approximately 1400 large farmers (800-10,000 ha) implemented by the Food and Agriculture Organization (FAO) on behalf of Canada, Japan and the Minderoo Foundation; (iii) will be used by the United States Agency for International Development (USAID) for seeds and fertilizers and by FAO for implementing an EUR 6 million program implemented on behalf of the EU, aimed at the establishment of an investment matching grant scheme for farmers operating in specific value chains of Western Ukraine. Based on this experience, the Ministry of Agrarian Policy and Food (MAPF) intends to make use of SAR mandatorily for transparent processing of all types of state support, including guarantees. MAPF is also working on an automated data exchange between SAR, State Fiscal Service, and State Statistics Service, as a way to reduce transaction cost of supplying credit to small farmers and allowing smaller banks to compete with larger ones on an equal footing, ideally in a way that would allow farmers to graduate to full commercial financing in due course. The application to the PCGF by small farmers would be submitted through SAR, to which financial institutions will have access. It is recommended for SAR to be the preferred platform for PCGF loan applications and only making it an exclusive vehicle in case the operational interface is fully accessible for participating banks.

6. **Ukraine, in general, and the agricultural sector, in particular, is vulnerable to the impacts of climate change.** Increasing temperatures and more uneven precipitation patterns have led to more frequent and more severe drought periods in the last decade. Based on modeling using different scenarios, climate change impacts are expected to decrease the yields of many crops, such as barley, maize and sunflower, which are critical export goods. The frequency and intensity of extreme weather events, including heatwaves, thunderstorms, heavy precipitation, pluvial and river flooding, droughts, and hailstorms, are expected to rise with higher warming, negatively impacting agricultural productivity. Furthermore, the risk of diseases and pests as well as wildfires increases with climate change. There are options to mitigate the impacts by introducing climate-smart agriculture practices.[1]

B. Sectoral and Institutional Context

7. **While the financial sector is an essential building block for fostering private sector led sustainable growth, it was not fully equipped to play that role even prior to Russia's invasion of Ukraine.** The Ukrainian banking sector lacks depth and makes only a relatively small contribution to private sector development with a private sector loan-to-GDP ratio of 28.4 percent in 2020 compared to a 55.2 percent average in ECA region (excluding high-income countries). A large share of state-owned banks (SOBs) with a high percentage of nonperforming loan (NPL) ratio and elevated exposure to government bonds continues to undermine the efficiency of financial intermediation and credit growth to the private sector. Among the challenges to firm performance in Ukraine, access to finance has historically been one of the biggest growth obstacles and particularly problematic for smaller enterprises.

8. **Constrained access to finance for small farmers has been further exacerbated by Russia's invasion of**

[1] World Bank. 2021. Ukraine: Building Climate Resilience in Agriculture and Forestry.

Ukraine. Pre-invasion World Bank (WB) studies show that many small farmers (up to 500 ha) are underbanked and do not even have access to basic banking instruments. Banks tend to work with clients perceived as less risky, such as agricultural companies with farms larger than 500 ha. Pre-invasion constraints related to lack of collateral, credit history, and reliable financial accounts that would mitigate asymmetric information risks and enable financial institutions to better assess their creditworthiness. In the context of the land reform, the lack of long-term loans for small farmers risks having several adverse effects. First, it could prevent smaller farmers from investing in productivity-enhancing technologies, which could lead to missed opportunities for significant income and welfare gains. Second, it could result in excessive land concentration among wealthy individuals, especially in the second phase of the land reform. As a result of Russia's invasion of Ukraine, commercial banks have been cautious in intensifying their lending activity to enterprises while small farmers' demand for additional financing has increased.[2] High interest rates as well as collateral requirements remain the main factors deterring businesses from taking new loans.[3]

9. **Since the start of Russia's invasion of Ukraine, state programs have become the main engine of lending.** Amid the tightening of banks' credit conditions, the 5-7-9 Loan Program in combination with State Portfolio Guarantee Program were almost the only channels of corporate crediting. The 5-7-9 Loan Program was launched in 2020 and is based on a mechanism of (partial) compensation of interest rates. CMU expanded the program in early spring 2021. This included a lending program to agribusinesses at favorable terms (short-term loans up to 6 months, with full interest rate compensation, and an increased loan amount of UAH 60 million), with bigger enterprises also becoming eligible.[4] As part of the state guarantees on a portfolio basis, 6,969 loans worth UAH 33.48 billion were issued to agribusinesses.[5]

10. **Partial credit guarantees by the PCGF form an important and complementary support vehicle aimed at enabling small farmers to capitalize on the land reforms and leveraging private capital for financing support during Russia's invasion of Ukraine and reconstruction phase**. Despite the challenging environment resulting from Russia's invasion of Ukraine, the design features of the PCGF remain highly relevant in the Ukrainian context, where banks are highly liquid and increasingly risk averse. The establishment of the PCGF has been a key element of the broader land reform package envisaging loan maturities of up to ten years whose availability is currently limited in the market (including through state support programs). The GoU is committed to accelerating the PCGF operationalization and replacing the current temporary credit guarantee arrangements based on good governance, safeguards, financial and systems standards. In a next step, as the PCGF becomes fully operational, it will be important for the GoU to decide upon a concrete timeline for the consolidation of all guarantee programs in support of small farmers at the PCGF. At the same time, the 5-7-9 Loan Program, can play an important role in supplementing guarantees with additional interest rate compensation instruments.

[2] Preliminary results of a WB survey among 2000 farmers conducted in 2022 found that over 90 percent of farmers with a farm size between 50-500 ha want to borrow while close to 40 percent in that group have never received a loan. Almost all demand relates to working capital loans.

[3] A recent NBU survey (NBU Business Outlook Survey, Q3) found that more than half of agricultural companies stated that their borrowing needs will increase in the near future. High interest rates on loans remain the main factor deterring businesses from taking new loans, as indicated by about half of the survey respondents, and 40 percent of agricultural companies participating in the survey. Collateral requirements are another constraint for about a quarter of respondents and one-fifth of agricultural companies that consider applying for a loan.

[4] As of December 2022, the program accounted for 26 percent of the net hryvnia corporate portfolio.

[5] For agriculture companies, the state guarantee cannot exceed 80 percent of the individual loan compared to 70 percent for other SMEs.

C. Relevance to Higher Level Objectives

11. **Russia's invasion of Ukraine has fundamentally impacted the context for the current Country Partnership Framework (CPF) FY17-FY21 (Report 114516-UA, discussed at the Board on June 20, 2017).** However, by supporting small farmers, the project contributes to achieving Objective 3, which supports agricultural development and land reforms, within Focus Area 1, Make markets work, which is aimed at unlocking the potential of the private sector through institutional reform and key investments. Strengthening government/PCGF's capacity to exercise its functions in supporting agriculture also limits negative impact of Russia's invasion of Ukraine on achievement of the Twin Goals, eliminating extreme poverty and boosting shared prosperity, thereby achievement of all pillars of the CPF.

12. **The project is consistent with the country's climate strategies.** Prior to Russia's invasion, Ukraine had demonstrated commendable dedication to the implementation of mitigation measures to combat climate change. In 2016, Ukraine ratified the Paris Agreement and in 2021, it pledged an ambitious new National Determined Contribution (NDC2). This commitment set a goal for a nationwide net reduction in greenhouse gas emissions of 65 percent by 2030, relative to the levels recorded in 1990. Furthermore, the nation committed to attain carbon neutrality by 2060. The Ukrainian government, in January 2020, issued a preliminary proposal for Ukraine's Green Energy Transition until 2050. This proposition intended to raise the proportion of renewable energy in the national energy mix to 70 percent by 2050. The NDC mentions the importance of the agriculture sector and its susceptibility to climate change is recognized and actions on both the mitigation and adaptation aspect were included. Even in the face of Russia's invasion, Ukraine has reiterated these pledges. In addition to mitigation, the investments required for rebuilding will also have to take into account Ukraine's susceptibility to the effects of climate change. The current Russian invasion significantly escalates the climate risks in Ukraine and reduces its ability to address climate-related issues, especially in the agricultural sector.

II. PROJECT DESCRIPTION

A. Project Development Objective

PDO Statement

13. The Project development objective (PDO) is to operationalize the Partial Credit Guarantee Fund in Agriculture (PCGF) to help improve access to financing for small farmers in Ukraine.

PDO Level Indicators

- The PCGF is fully operational as an independent financial institution regulated by the NBU.
- Number of small farmers cultivating less than 500 ha of agricultural land access loans with the PCGF guarantee.
- Total amount of loans [UAH million] guaranteed by the PCGF for small farmers.

B. Project Components

14. **The project comprises one component on capitalization of the PCGF in the total amount of EUR 10**

million.[6] The component is designed as a recipient executed (RE) trust fund (TF). The project aims to contribute to the capitalization of the new PCGF, with a sound independent governance framework, which will support credit-constrained farmers and significantly improve sustainability of the current credit guarantees, thereby providing long-term benefits for agricultural development and food security. The contribution through the EU funded TF will be disbursed in two tranches. The first tranche of EUR 6 million will be disbursed as soon as the grant agreement becomes effective for the authorized capital of the PCGF to reach its legally foreseen amount of UAH 200 million. The second tranche (EUR 4 million) will follow once the PCGF is fully operational with its institutional, legal and operational framework acceptable to the WB. The second tranche will be disbursed once (a) PCGF Internal Regulations are adopted and approved; (b) the PCGF Supervisory Board and the PCGF Management Board are duly elected and appointed; (c) a risk manager and internal auditor are appointed to the PCGF; and (d) at least one PFI has signed a Participation Agreement with the PCGF; all in form and substance satisfactory to the Bank.

15. **The initial capitalization is expected to get other donors, including the European Union (EU), to consider providing more funds into PCGF as it becomes operational.** The passage of the 2022 State Budget Law on December 2, 2021, allocated UAH 200 million for the authorized capital of the PCGF, UAH 190 million of which have been re-allocated to other purposes as a result of Russia's invasion of Ukraine. Overall, a capitalization of EUR 100 million had been envisaged prior to Russia's invasion of Ukraine, comprising of EUR 50 million tentatively provided by the EU to be matched by a similar contribution of the GoU. Due to Russia's invasion of Ukraine, the EU contribution had to be revised downwards, while future possible contributions could not yet be secured. In addition to the EUR 10 million under the project, the WB Accelerating Private Investments in Agriculture Program (P166941) aims to support the government in providing matching funds for the capitalization of the PCGF in the amount of USD 9 million. Once the PCGF is operational, guarantees will be provided on a wholesale basis through participating banks based on clearly defined eligibility criteria. According to the NBU's regulation the total volume of guarantees provided by the PCGF may reach up to 4 times the capital of the PCGF. Eligibility criteria for small farmers will be defined further in the POM and ensure that they meet the Paris Alignment corporate commitment.

C. Project Beneficiaries

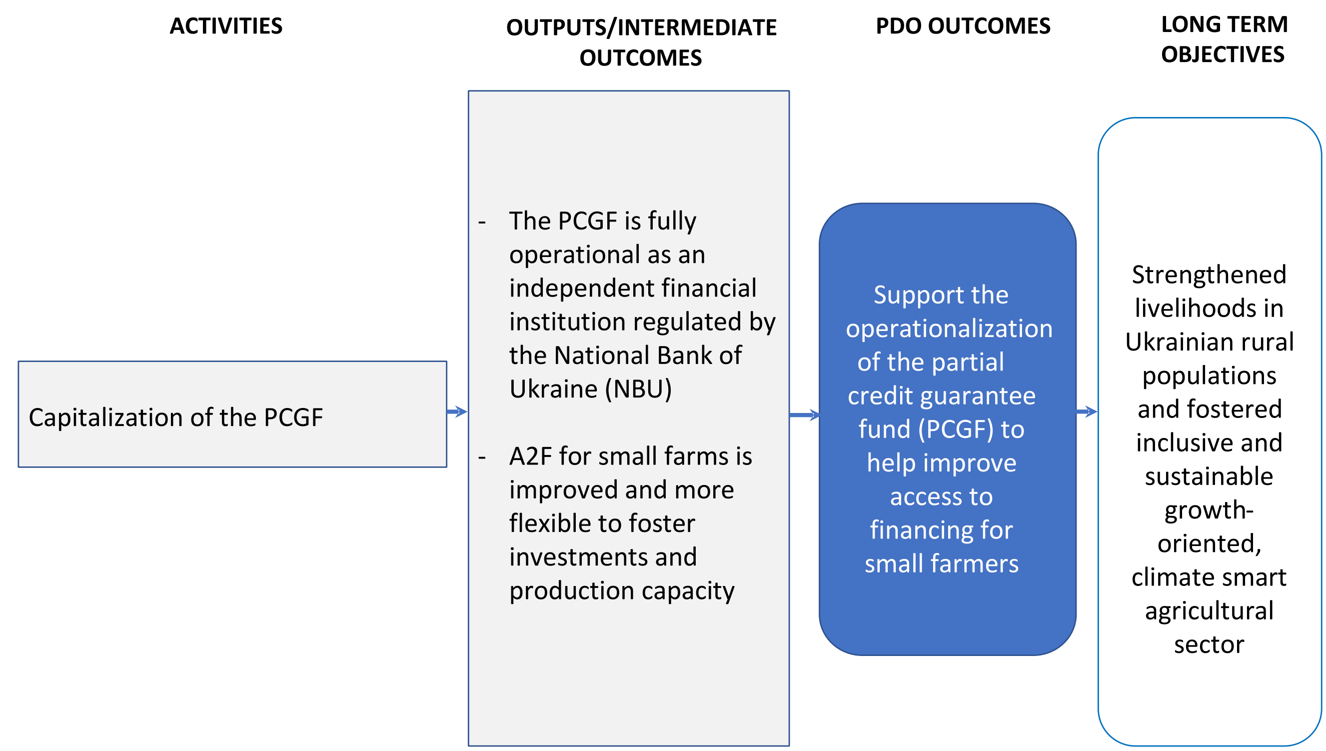
16. **The main project beneficiaries will be small farmers of less than 500 ha.**[7] Participating financial institutions (PFIs)[8] will also benefit from the project by reducing their exposure to credit risk and enabling them to increase their lending portfolio. Finally, the general population and employees of the financed beneficiary enterprises will indirectly benefit from increased economic activity and employment generated by the project.

[6] Another approximately USD9 million capitalization for the PCGF – as matching contribution to the grant funds - is foreseen in the 2023 Budget Code.

[7] In line with the Law of Ukraine 'On Partial Credit Guarantee Fund in Agriculture' the target group are small farmers which are defined as micro, small and medium-sized business entities and natural persons - entrepreneurs, the main activity of which is the production of agricultural products, which meet the requirements for micro-enterprises, small and medium-sized enterprises according to the Law of Ukraine "On Accounting and Financial Reporting in Ukraine" and which own and/or use agricultural land not exceeding 500 hectares, including land plots purchased with funds received on credit.

[8] Commercial banks.

D. Results Chain



E. Rationale for Bank Involvement and Role of Partners

17. **Constrained access to finance, which has been further exacerbated by Russia's invasion of Ukraine – calls for additional support for small farmers.** World Bank studies show that many small farmers (up to 500 ha) are underbanked and do not have access even to basic banking instruments prior to Russia's invasion of Ukraine. Banks mostly work with clients perceived as less risky (agricultural companies whose farms are larger than 500 ha). As a result of Russia's invasion of Ukraine, commercial banks have been cautious in intensifying their lending activity to enterprises while small farmers' demand for additional financing has increased. This situation required a public sector intervention and hence the PCGF is being established as an independent, legal institution. IFI/donor intervention to expand the capital base and strengthen institutional capacity of the PCGF is well-justified and will contribute to eliminating above-mentioned market failures.

18. **The World Bank is a globally recognized standard setter for public credit guarantee schemes**. The WB recently issued "Principles for Public Credit Guarantee Schemes for SMEs",[9] which sets standards for public credit guarantee schemes (CGS) on legal and regulatory, corporate governance, risk management, operational, monitoring and evaluation issues. The WB has worked on partial credit guarantees in a number of countries, including Mexico, Haiti, Croatia, Kosovo, and Moldova. These projects include both - capitalization and technical assistance.

[9] https://www.worldbank.org/en/topic/financialsector/publication/principles-for-public-credit-guarantee-schemes-cgss-for-smes.

19. **Financial intermediary financing is typically successful if priced in line with market principles, and with clear eligibility criteria.** In line with the WB Policy on IPF and associated Guidance on Financial Intermediary Financing, the project will use market principles to price financing to PFIs and firms to avoid market distortions and safeguard sustainability. To achieve additionality and sustainability while avoiding creating moral hazard, the design of the PCGF has incorporated best practices. In line with the Principles for Public Credit Guarantee Schemes for SMEs, the credit guarantee scheme is operated by an independent legal entity on the basis of a sound and clearly defined legal and regulatory framework. The PCGF has sound governance arrangements in place, including a majority independent Supervisory Board and is independently supervised (by NBU) on the basis of risk-proportionate regulation. It envisages the adoption of clearly defined and transparent eligibility and qualification criteria for small farmers and lenders; offers partial coverage to provide the right incentives for small farmers and lenders and aims to adopt an efficient, clearly documented, and transparent claim management process (see Annex 2 for further information).

20. **The proposed project is complementary to a wide range of other agribusiness support provided by the World Bank Group (WBG) and other development partners in Ukraine**. The WB supported the development and approval of the legislation to establish the PCGF through the Development Policy Loan (P172597) approved by the Board on December 17, 2021. Through the Swedish funded Ukraine Financial Sector Recovery and Resilience Project (P164701), the WB supported preparation of the PCGF Law and continues to support the authorities in operationalization of the PCGF. The International Financial Corporation (IFC) has also been closely involved in the PCGF's establishment and will support capacity building of banks and farmers in their work with the PCGF. Project activities are complementary to the Accelerating Private Investments in Agriculture Program (P166941), which aims to support the government in providing matching funds for the capitalization of the PCGF in the amount of USD 9 million. Credit lines and risk-sharing facilities supporting SMEs and private companies more broadly including the agricultural sector in the country are provided by the European Bank for Reconstruction and Development (EBRD)[10], European Investment Bank (EIB)[11], and IFC[12]. However, limited focus is placed by existing programs on underserved and smaller farmers with working capital and investment financing needs.

F. Lessons Learned and Reflected in the Project Design

21. **Lessons learned from similar WBG projects contributed to the project design.** These include recent experiences in Mexico, Haiti, Croatia, Kosovo, and Moldova. These projects in developing countries provided insight into the specific challenges for new or struggling partial credit guarantee schemes. Capacity constraints in risk management and monitoring and evaluation were among critical factors for functioning guarantee frameworks in the developing country context. As a result, they were included as an important part of the institutional capacity building activities that will be provided by the WB through complementary technical assistance.

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[10] Unfunded risk-sharing facilities in support of private companies in critical industries. The facilities will back up to 50 per cent of the credit risk of €200 million in newly originated financing which is being provided by OTP Leasing (€80 million), Credit Agricole (€50 million), ProCredit Bank (€40 million) and OTP Bank (€30 million), subject to a portfolio cap of 50 per cent.

[11] EIB provided EUR 400 million in loans to finance medium- and long-term investment needs and medium- and long-term working capital of enterprises in the agricultural sector of Ukraine's economy.

[12] In December 2022, IFC launched a new $2 billion package to support the Ukrainian private sector during Russia's invasion of Ukraine and initial reconstruction stage. The program, among other, will provide financing through financial intermediaries to on-lend to micro, small and medium enterprises and agribusinesses, and through trade finance guarantees.

22. **The project also benefited from international experience.** The WB's Principles for Public Credit Guarantee Schemes for SMEs were a useful framework for assessing the existing credit guarantee framework in Ukraine and support the design stage of the PCGF. Additionally, besides consultations with other IFIs, on determining the suitability of the partial credit guarantees as an instrument to support small farmers, the project also benefited from a literature review for global experience and benefited from Vienna Initiative's and EIB's regional studies.

III. IMPLEMENTATION ARRANGEMENTS

A. Institutional and Implementation Arrangements

23. **This project** focuses on the capitalization of the PCGF. Both MAPF and PCGF are implementing agencies. The project implementation team (PIT) will be composed from staff of both institutions. The project coordinator and financial management expert will be appointed from within MAPF. The environmental and social specialist will be hired by the PCGF. A subsidiary agreement will be signed to reflect the obligation of PCGF to comply with Bank policies and procedures (effectiveness condition). The PIT shall be fully established latest one month after grant effectiveness date.

B. Results Monitoring and Evaluation Arrangements

24. **During project implementation, project monitoring and evaluation (M&E) will be the responsibility of the PIT** and supervised by the WB project team, with periodic consultation with donors and facilitation of stakeholder participation. See Annex 1 for further information on the results framework.

C. Sustainability

25. **The project will support the establishment of a functional and sustainable PCGF.** This work has started before Russia's invasion of Ukraine. The WB supported the development and approval of the legislation to establish the PCGF through a Development Policy Loan approved by the Board on December 17, 2021. The WB Finance, Competitiveness, and Investment Global Practice is currently providing technical assistance to make the PCGF aligned with the 16 principles set forth by the WB for a sustainable, efficient, institutionally sound PCGF. In the medium term, it is envisaged that the PCGF will replace the existing system for the provision of government guarantees and create a sustainable institution for the long-term support to small-sized farms fitted to support the recovery process.

IV. PROJECT APPRAISAL SUMMARY

A. Technical, Economic and Financial Analysis

26. **The sub-projects to be funded under the project are not pre-identified and project costs are not pre-defined, thus a traditional economic/financial analysis is not conducted**. Nevertheless, the project is expected to increase availability and tenors from PFIs. The specific eligibility criteria, terms and conditions will be defined

in the project operational manual (POM). The POM shall be adopted latest one month after grant effectiveness date. In addition, by supporting finance for small farmers, the project is expected to have an impact on employment. The project will collect data on gender for analytical purposes.

27. **The main project beneficiaries will be small farmers of less than 500 ha.** PFIs will also benefit from the project by reducing their exposure to credit risk and enabling them to increase their lending portfolio. Finally, the general population and employees of the financed beneficiary enterprises will indirectly benefit from increased economic activity and employment generated by the project.

28. **Maximizing Finance for Development.** The project is expected to leverage significant private capital through PCGF guarantees. Once the anticipated initial capital of approximately EUR 10 million is fully paid in, with the proposed 1:4 leverage and 50 percent guarantee coverage, the PCGF will be able to facilitate up to EUR 80 million of financing for small farmers by PFIs.

29. **The rationale for public intervention in the provision of finance to small farmers is driven by the lack of alternatives in the short term.** Access to finance is constrained due to the macro-financial crisis resulting from Russia's invasion of Ukraine, but also constraints prior to Russia's invasion of Ukraine such as lack of collateral, credit history, and reliable financial accounts that would mitigate asymmetric information risks and enable financial institutions to better assess their creditworthiness.

30. **In addition, the project will continue to help the PCGF in its effective operationalization process.** The WB has been providing advisory work to the authorities, helping shape the legal and regulatory framework for the PCGF. The governance and risk management arrangements for the PCGF are critical, and the WB will be following the reform process closely during project implementation to ensure that reforms implemented are not reversed.

31. **The operation is aligned with the goals of the Paris Agreement on both mitigation and adaptation.** Overall, the projects activities and objectives are in line with the country's NDCs. There were no aspects of the project that clearly went against the county's ability to meet their nationally determined objectives, nor hinder their progress in doing so.

32. **Assessment and reduction of adaptation risks**: The main climate and disaster risk likely to affect the project investments is water scarcity. Climate change is predicted to result in more drought occurrences, both in terms of scope and length, according to trends and variations, negatively impacting agricultural productivity. The project design will take into consideration the uneven precipitation trends that threaten the outcomes of the project, specifically, climate change risks and vulnerability to droughts may be managed and mitigated through the project's second phase of implementing climate smart agriculture such as water management practices in the context of droughts and crop diversification to reduce climate vulnerability. These measures will improve environmental management and increasing the resilience of the targeted areas in the event of climate-related shocks. Through the enhancement of the farm's adaptation and resilience the project will lead to increased productivity and employment. Risks from climate hazards are considered low, given the operation is not financing any infrastructure and thus, no material risks to the operation exist.

33. **Assessment and reduction of mitigation risks**: The operation is not at a material risk of having a negative impact on the country's low-GHG-emissions development pathways. The operation also supports institutional capacity building of the PCGF, specifically risk management and monitoring and evaluation, which poses a low

climate risk in achieving the PDO. There may be a risk of carbon lock-in associated with financing to small farms. However, to mitigate the risk, eligibility criteria will be defined further in the POM and will ensure that no activities that fall under the Universally Non-Aligned list of the Paris Alignment corporate commitment are funded.

34. On mitigation, the operation has a low risk of preventing the Country's transition to low-carbon development pathways, given its contribution to increasing financing access to small scale farms and increasing their resilience to climate change via climate smart agriculture practices.

35. On adaptation, the operation will adequately reduce the physical climate risks by providing increased financing to small scale farmers, and the project's climate resilience and adaptation design considerations limit the exposure to a low level of residual risk.

B. Fiduciary

(i) Financial Management

36. **FM/disbursement assessment has been carried out and FM and Disbursement arrangements were confirmed to meet the WB requirements**. Considering the relatively small size and simplicity of this operation, but in view of the current risks and uncertainties related to Russia's invasion of Ukraine, FM risk is Substantial after proposed risk mitigation measures. To mitigate the risk of delay of funds transfer or their misuse, MAPF will follow flow of funds procedures as described below. As MAPF will be the grant signatory, it will also have the power to sign withdrawal applications, that will be submitted to the WB via Client Connection. MAPF PIT will have a specialist in charge of FM / Disbursements in this project who will be in charge of disbursements as well as subsequent reporting. While MAPF has some experience in working with the WB through implementation of the Accelerating Private Investment in Agriculture Program (P166941), the WB will provide support as necessary during implementation of this grant.

37. **No designated account will be required for this grant**. MAPF will then prepare and sign two withdrawal applications (one for each tranche) to channel grant funds to its respective account in UAH in the State Treasury of Ukraine. These funds will be included in the State Budget of Ukraine, in the budget line 2801380 of MAPF "For Capitalization of PCGF". The WB would do the conversion of EUR to UAH and credit corresponding UAH amounts to the mentioned account. Further, MAPF would immediately (within three business days) transfer the funds received to its accounts opened in the State Treasury to the local account of PCGF opened in Ukrgasbank, with the purpose of PCGF capitalization. An existing account of PCGF already opened and operational in Ukrgasbank for the purpose of PCGF capitalization will be used for channeling of the grant funds. Onward transfer of funds from MAPF to PCGF accounts will be required to be completed within three days from their receipt into MAPF accounts. MAPF will then send an official confirmation of the grant funds reaching respective PCGF accounts, including copies of State Treasury and Ukrgasbank statements to confirm final receipt of the funds.

38. **No Interim Unaudited Financial Reports (IUFRs) will be required for this operation**. However, MAPF will provide confirmation letters to the WB that the funds have been received into its State Treasury account, and then credited to PCGF accounts opened in Ukrgasbank, following processing of each tranche. Each such letter will be accompanied by the bank statements confirming receipt of grant funds into MAPF State Treasury account and then into PCGF account in Ukrgasbank. Such alternative assurance procedures will be sufficient for this operation

considering its size and nature of the activities financed. The WB retains the right to request an independent audit of transactions financed by this grant. In that case, the PCGF would be obliged to provide an independent auditor's report within 6 months of such request.

(ii) Procurement

39. **Currently no recipient executed procurement is foreseen by the project.** It is expected that the project resources will be used as partial credit guarantees for the loans to small farmers. The Procurement Regulations for IPF Borrowers, dated July 2016 and revised November 2020 (Fourth Edition), (i.e., the new procurement framework) does not apply to loans made by eligible financial intermediaries to private borrowers. The project will be subject to the World Bank's Anticorruption Guidelines, dated July 1, 2016, revised January 2011 and July 2016 (Guidelines on Preventing and Combatting Fraud and Corruption in Projects financed by IBRD Loans and IDA Credits and Grants). Potentially, the project audit of the financial statements might be the only procurement to be carried out. In this case, the independent auditor will be selected based on the Terms of Reference acceptable to the Bank. The WB team will assist the Recipient as needed.

C. Legal Operational Policies

	Triggered?
Projects on International Waterways OP 7.50	No
Projects in Disputed Areas OP 7.60	No

D. Environmental and Social

40. **Potential environmental impacts are connected to purchase of land, purchase and use of agrochemicals (pesticides, fertilizers), establishment of irrigation systems and include impact on biodiversity, surface and ground water sources, soil quality, OHS and community health and safety impacts, as well as hazards related to Russia's invasion of Ukraine such as land contamination and explosive remnants of war (ERW).** Environmental risks are expected to be site-specific, temporary and can be readily addressed through standard mitigation measures and compliance with national laws, however, these risks may be exacerbated by Russia's invasion of Ukraine and hazards and threats related to Russia's invasion of Ukraine (such as aerial attacks and ERW). On the social side, project activities associated with the provision of credit guarantees for land purchase, working capital, and equipment installation and construction works for small and medium-scale agricultural activities are unlikely to involve some site-specific adverse risks and impacts on workers and communities which in most situations will be easily manageable. However, Russia's invasion of Ukraine poses significant contextual risks associated with worker and community health and safety and may induce incidents of harmful labor or further displacement of refugees using vacant land if inspection activities are not carried out. To address potential adverse environmental and social impacts, the Recipient will develop and adopt a fund-level Environmental and Social Management Systems (ESMS) to be followed by PCGF and PFIs.

41. **Project activities are likely to involve some site-specific adverse social risks and impacts on workers and communities which in most situations will be easily manageable but are rendered unpredictable by the contextual risks associated with the national emergency**. Russia's invasion of Ukraine poses significant contextual

risks that are beyond the control of the project such as risks associated with aerial bombardment, fighting or further displacement of refugees. Community and worker health and safety risks common to the activities being supported include risk of interaction with nearby communities during transport of equipment and machinery or during localized construction activities. Loans intended for the purchase of land need to be screened to ensure that any land acquisition occurs on a willing seller-willing buyer basis documented by legal transaction records on fully registered and notarized private land where the absence of dispute over ownership or use is confirmed. Sexual exploitation and abuse and sexual harassment (SEA/SH) risks are estimated to be low but preventative measures should be put in place. There is a risk that provision of credit financing may benefit those enterprises with existing financial capacity, and not reach rural new starters or those with insolvency records or cultural minorities and the elderly without access to information or awareness of the program. Small entrepreneurs may be more reluctant to apply and take on debt during the current crisis. Financial products and training tailored to smallholders is required, for example, for women-led business, community enterprise, borrowers lacking a credit history or lacking financial skills. The quality of management systems deployed by PFIs is likely to vary and a capacity building approach will need to be integrated into the bank TA activities to ensure that these systems are subject to due diligence review and updated for consistency with ESS9.

42. **Citizen Engagement.** As part of its M&E activities, PCGF/MAPF will conduct a client survey at mid-term with ultimate beneficiaries. The PCGF will discuss with the PFIs how to address the feedback provided by the ultimate beneficiaries and provide evidence of responses triggered by the feedback. The following indicator is included in the project M&E framework: “Percentage of project beneficiaries that report project sub-finance reflected their needs (end target is 80 percent)”.

43. **Gender.** In terms of monitoring, the following gender-disaggregated indicator is included in the project M&E framework as an intermediate indicator: “percentage of loans financed by the PCGF extended to women (end target is 10 percent).” This indicator will be monitored throughout the life of the project on semi-annual basis.

44. **Climate-focus.** In a second stage – conditional to receiving additional financing – it is envisaged to expand the scope of the project with a view of supporting climate smart agriculture.

45. **In accordance with WB OP 4.03, the requirements of OP/BP 7.50, Projects on International Waterways, and those of OP/BP 7.60, Projects in Disputed Areas, may be applicable to any WB-supported private sector activity in addition to OP/BP 4.03.** Since it is not expected that any activities under this project will involve international waterways or disputed areas, the policies will not be triggered. Any activity impacting international waterway or disputed territories will be excluded from the project.

V. GRIEVANCE REDRESS SERVICES

46. ***Grievance Redress.*** Communities and individuals who believe that they are adversely affected by a project supported by the WB may submit complaints to existing project-level grievance mechanisms or the WB Grievance Redress Service (GRS). The GRS ensures that complaints received are promptly reviewed in order to address project-related concerns. Project affected communities and individuals may submit their complaint to the WB independent Accountability Mechanism (AM). The AM houses the Inspection Panel, which determines whether harm occurred, or

could occur, as a result of WB non-compliance with its policies and procedures, and the Dispute Resolution Service, which provides communities and borrowers with the opportunity to address complaints through dispute resolution. Complaints may be submitted to the AM at any time after concerns have been brought directly to the attention of WB Management and after Management has been given an opportunity to respond. For information on how to submit complaints to the WB Grievance Redress Service, please visit http://www.worldbank.org/GRS. For information on how to submit complaints to the WB Accountability Mechanism, please visit https://accountability.worldbank.org.

VI. KEY RISKS

47. **The overall risk to achieving the PDO is rated Substantial due to Russia's invasion of Ukraine, with widespread and unpredictable security, political, social, and macroeconomic instability**. To account for this, project design has been kept lean, which would help mitigate some of the risks. However, the main risk remains related to the duration and severity of the current military aggression and its human, economic and macro impact as discussed below.

48. **Political and Governance risk is High**. Russia's invasion of Ukraine and the declaration of martial law on February 24, 2022, poses a huge risk to the political and governance landscape. The evolution and the potential impact on the ability of the Government and institutions to perform core functions remains highly uncertain as the military aggression continues.

49. **Macroeconomic risk is High**. Rising geopolitical tensions and Russia's invasion of Ukraine have led to a severe deterioration of the macroeconomic situation in the country. After restoring government control over Kyiv and Chernihiv regions in April 2022, the economic activity has started to gradually improve. Nevertheless, Ukraine's economy contracted by 29.1 percent in 2022. While thus far, the authorities have introduced and remained committed to broadly sound macroeconomic policies to avert the most immediate fiscal, monetary, and financial sector risks, Ukraine is continuing to face three macro-critical challenges stemming from the ongoing military aggression: (i) high fiscal financing needs and inability to mobilize domestic revenues; (ii) increasing reliance on monetary financing and deteriorating asset quality of the financial sector; and (iii) weaker external position.

50. **Sector Strategies and Policies risk is Moderate**. The GoU has the policies and mechanisms in place to support agricultural production and storage. The GOU is also focusing on increasing agrifood exports, committing to domestic investments, and coordinating investment and policy decisions with other countries and partners. The GoU is committed to accelerating the PCGF operationalization and replacing the current temporary credit guarantee arrangements based on good governance, safeguards, financial and systems standards. In a next step, as the PCGF becomes fully operational, it will be important for the GoU to decide upon a concrete timeline for the consolidation of all guarantee programs in support of small farmers at the PCGF.

51. **Technical Design of Project risks are Substantial**. Prior to Russia's invasion of Ukraine, the banking system was in relatively sound condition, and the overwhelming majority of banks remained liquid and operational. However, the loss of assets, collateral, and revenues will severely affect banks' profitability and solvency. During March-December 2022, the banking sector already accounted for USD 2.9 billion (UAH 105 billion) of loan loss provisions for expected credit losses related to Russia's invasion of Ukraine. Significant financial forbearance

measures have been implemented for financial institutions and enterprises. The full effect on the financial system will therefore only be better known in 2023 as the NBU implements a first asset quality review (AQR) since the start of Russia's invasion of Ukraine. The WB is providing technical assistance to NBU in the AQR implementation process and is closely monitoring the situation in the financial system. Moreover, PFIs interested in participating in the project need to meet a set of established eligibility criteria. PFIs will be selected by the PCGF based on their financial health, as well as their capacity to implement sub-projects. PFI selection is also subject to a no-objection process by the WB (to be reflected in the POM), while PFI financing agreement covenants between the PCGF and PFIs require compliance with local regulations thereby supporting the continued financial health of PFIs.

52. **Institutional Capacity for Implementation and Sustainability risks are Substantial**. In case of Russia's invasion of Ukraine being still ongoing over the next planting and harvest season, some damages to planting areas, farm equipment, or further damages to the available grain storage and infrastructure may be a result. This could mean a slower than hoped for return to liquidity of farmers and traders and reductions in investment appetite. The risks will be mitigated by investments in locations that are considered 'less risky'. Moreover, there is a substantial risk that the originally foreseen EUR 100 million capitalization for the PCGF will not be achieved as donor commitment as well as GoU's commitment to provide matching contributions to reach the amount is not yet fully confirmed.

53. **Environmental and Social Risks are Substantial.** Potential environmental impacts are connected to purchase of land, purchase and use of agrochemicals (pesticides, fertilizers), establishment of irrigation systems and include impact on biodiversity, surface and ground water sources, soil quality, OHS and community health and safety impacts, as well as hazards related to Russia's invasion of Ukraine such as land contamination and explosive remnants of war (ERW). Community and worker health and safety risks common to the activities being supported include risk of interaction with nearby communities during transport of equipment and machinery or during localized construction activities. Environmental and social risks are expected to be site-specific, temporary and can be readily addressed through standard mitigation measures and compliance with national laws, however, these risks may be exacerbated by Russia's invasion of Ukraine and hazards and threats related to Russia's invasion of Ukraine (such as aerial attacks). To manage these risks, the PIT for PCGF will establish a fund-level ESMS prior to the start of guarantees approval process. In addition to the ESMS, PFIs will conduct screening of eligible beneficiaries. Only those beneficiaries whose business activities are judged to be of substantial, moderate or low environmental and social risks will be eligible for project support. At the beneficiaries level, simple streamlined environment and social due diligence procedures that includes screening against the prescribed eligibility criteria and compliance with national laws can serve as underlying framework for addressing environmental and social risks and impacts.

54. **Fiduciary risk is rated Substantial**. The risk associated with FM is assessed as Substantial. Despite the relatively simple project design and implementation arrangements, project risk is affected by increased inherent risks, such as MOF/MAPF/PCGF being affected by Russia's invasion of Ukraine in a way that would prevent them from processing the disbursements as well as documenting and reporting them. There is some risk of delay or disruption in full and correct execution of the two tranches that contribute to capitalization of the PCGF.

55. **Stakeholders' risk associated with the implementation of the Project is rated as Substantial**. Project implementation success depends on commercial banks remaining in operation for the duration of Russia's invasion of Ukraine. It also depends on personnel management by line ministries and the PCGF and their prompt actions. Prior to Russia's invasion of Ukraine the banking system was in a relatively good condition. Liquidity

remains at high levels, given a relatively stable deposit base and refinancing support from the NBU. At the same time, loss of assets, collateral, and revenues will severely affect banks' profitability and solvency. While some banks will be able to recover capital themselves through their future profits, others will likely need to be recapitalized by their shareholders.

VII. RESULTS FRAMEWORK AND MONITORING

Results Framework
COUNTRY: Ukraine
Strengthening the Partial Credit Guarantee (PCG) Fund for small farmers in Ukraine (Strengthening the PCGF in Agriculture Project)

Project Development Objectives(s)

The Project development objective (PDO) is to operationalize the Partial Credit Guarantee Fund in Agriculture (PCGF) to help improve access to financing for small farmers in Ukraine.

Project Development Objective Indicators

Indicator Name	PBC	Baseline	End Target
Operationalization of the PCGF			
The PCGF is fully operational as an independent financial institution regulated by the National Bank of Ukraine (NBU) (Text)		No	Yes
Number of small farmers cultivating less than 500 ha of agricultural land access loans with the PCGF guarantee (Number)		0.00	800.00
Total amount of loans [UAH million] guaranteed by the PCGF for small farmers (Number)		0.00	2,000.00

Intermediate Results Indicators by Components

Indicator Name	PBC	Baseline	End Target
Capitalization of the PCGF			
Number of banks partnered with the PCG Fund and lending financial resources to small farmers (Number)		0.00	5.00
Investment loans (including land purchase) guaranteed by the PCGF (as percentage of total guaranteed loans) (Percentage)		0.00	50.00
Percentage of loans financed by PCGF extended to female farmers (Percentage)		0.00	10.00
Citizen engagement: Farmers that report Project finance reflected their needs (%) (Percentage) (Percentage)		0.00	80.00
Portfolio Quality: Portfolio at risk (%) (Percentage)		0.00	10.00

Monitoring & Evaluation Plan: PDO Indicators

Indicator Name	Definition/Description	Frequency	Datasource	Methodology for Data Collection	Responsibility for Data Collection
The PCGF is fully operational as an independent financial institution regulated by the National Bank of Ukraine (NBU)	All steps in the agreed upon roadmap have been finalized acceptable to the Bank.	Semi-annual	Roadmap	Analysis of roadmap	PIT
Number of small farmers cultivating less than 500 ha of agricultural land access loans with the PCGF guarantee		Semi-annual	Progress reports	Analysis of loan data	PIT
Total amount of loans [UAH million] guaranteed by the PCGF for small farmers		Semi-annual	Progress reports	Analysis of project loans	PIT

Monitoring & Evaluation Plan: Intermediate Results Indicators					
Indicator Name	**Definition/Description**	**Frequency**	**Datasource**	**Methodology for Data Collection**	**Responsibility for Data Collection**
Number of banks partnered with the PCG Fund and lending financial resources to small farmers		Semi-annual	Progress reports	Analysis of progress report	PIT
Investment loans (including land purchase) guaranteed by the PCGF (as percentage of total guaranteed loans)	Investment loans (including land purchase) guaranteed by the PCGF (as percentage of total guaranteed loans) amounts to at least 50 percent.	Annual	Progress report/SAR	Analysis of data from SAR/progress reports	PIT
Percentage of loans financed by PCGF extended to female farmers		semi-annual	Progress reports	Analysis of loan data	PIT
Citizen engagement: Farmers that report Project finance reflected their needs (%) (Percentage)		Project mid-term	Report on summary of survey findings	Survey of beneficiary farmers	PIT
Portfolio Quality: Portfolio at risk (%)		Semi-annual	Progress reports	Analysis of loan data	PIT/PFIs

ANNEX 1: Implementation Arrangements and Support Plan

COUNTRY: Ukraine
Strengthening the Partial Credit Guarantee (PCG) Fund for small farmers in Ukraine

1. **This project** focuses on the capitalization of the PCGF. Both MAPF and PCGF are implementing agencies. The PIT will be composed from staff of both institutions. The project coordinator and financial management expert will be appointed from within MAPF. The environmental and social specialist will be hired by the PCGF. A subsidiary agreement will be signed to reflect the obligation of PCGF to comply with Bank policies and procedures (effectiveness condition). The PIT shall be fully established latest one month after grant effectiveness date.

2. **PFIs interested in participating in the project need to meet a set of established eligibility criteria.** The eligibility criteria for PFIs reflect ongoing compliance with a selected set of regulators' prudential requirements and are in line with the criteria designed and applied by the WB in similar line of operations. PFIs will be selected by the PCGF based on their financial health, as well as their capacity to implement sub-projects. PFI selection is also subject to a no-objection process by the WB (to be reflected in the POM), while PFI financing agreement covenants between the PCGF and PFIs require compliance with local regulations thereby supporting the continued financial health of the PFIs. If PFIs do not effectively implement the project including adherence to the eligibility criteria, they may be substituted for other eligible PFIs.

3. **FM/disbursement assessment has been carried out, and FM and Disbursement arrangements were confirmed to meet the Word Bank requirements**. Considering the relatively small size and simplicity of this operation, but in view of the current risks and uncertainties related to Russia's invasion of Ukraine, FM risk is Substantial after proposed risk mitigation measures. To mitigate the risk of delay of funds transfer or their misuse, MAPF will follow flow of funds procedures as described below. As MAPF will be the grant signatory, it will also have the power to sign withdrawal applications, that will be submitted to the World Bank via Client Connection. MAPF PIT will include a specialist in charge of FM / Disbursements in this project who will be in charge of disbursements as well as subsequent reporting. MAPF has some experience in working with the WB through implementation of the Accelerating Private Investment in Agriculture Program (P166941), however WB support will also be provided as needed during implementation of this grant.

4. **No designated account will be required for this grant.** MAPF will then prepare and sign two withdrawal applications (one for each tranche) to channel grant funds to its respective account in the State Treasury of Ukraine in UAH. These funds will be included in the State Budget of Ukraine, in the budget line 2801380 of MAPF "For Capitalization of PCGF". The WB would do the conversion of EUR to UAH and credit corresponding UAH amounts to the mentioned account. Further, MAPF would immediately (within three business days) transfer the funds received to its accounts opened in the State Treasury to the local account of PCGF opened in Ukrgasbank, with the purpose of PCGF capitalization. An existing account of PCGF already opened and operational in Ukrgasbank for the purpose of PCGF capitalization will be used for channeling of the grant funds. Onward transfer of funds from MAPF to PCGF accounts will be required to be completed within three days from their receipt into MAPF accounts. MAPF will then send an official confirmation of the grant funds reaching respective PCGF accounts, including copies of State Treasury and Ukrgasbank statements to confirm final receipt of the funds.

5. **No Interim Unaudited Financial Reports (IUFRs) will be required for this operation**. However, MAPF will provide confirmation letters to the World Bank that the funds have been received into its State Treasury account, and then credited to PCGF accounts opened in Ukrgasbank, following processing of each tranche. Each such letter will be accompanied by the bank statements confirming receipt of grant funds into MAPF State Treasury account and then into PCGF account in Ukrgasbank. Such alternative assurance procedures will be sufficient for this operation considering its size and nature of the activities financed. The World Bank retains the right to request an independent audit of transactions financed by this Grant. In that case, PCGF would be obliged to provide an independent auditor's report within 6 months of such request.

6. **Strategy and approach for implementation support.** The following implementation support strategy is proposed, considering the risks and mitigation measures related to the project:

- **Technical support.** WB implementation support will include (Senior) Financial Sector Specialists based in the WB office in Kyiv and Vienna as well as at WB Headquarters (HQ) to guide the PIT during project implementation. Implementation support missions will be conducted at least twice per calendar year.

- **FM.** During project implementation, the WB will supervise FM arrangements. A WB-accredited Senior FM specialist, temporarily based in Vienna, will assist with the project implementation support.

- **Procurement.** A procurement specialist will carry out supervision and will participate in project implementation support missions, respond to just-in-time requests, and provide ongoing guidance to the PIT as needed.

- **Environmental and Social Safeguards (E&S).** Implementation support will be provided as needed by WB E&S specialists on environmental and social safeguards standards, based in Vienna and WB HQ.

Table 1. Implementation support plan and resource requirements

Time	Focus	Skills Needed	Resource Estimate
Year 1	Task management	Project management (Vienna, Kyiv & HQ based)	6 staff weeks (SWs)
	Procurement	Procurement specialist (Vienna based)	1 SWs
	FM supervision	FM specialist (Vienna based)	2 SWs
	Safeguards	Safeguards specialists (Vienna & HQ based)	3 SWs
Year 2-3	Task management	Project management (Vienna & HQ based)	4 SWs
	Procurement	Procurement specialist (Vienna based)	1 SWs
	FM supervision	FM specialist (Vienna based)	2 SWs
	Safeguards	Safeguards specialists (Vienna & HQ based)	3 SWs

ANNEX 2: Assessment of Financial Sector and Financial Intermediary Financing (FIF)

COUNTRY: Ukraine
Strengthening the Partial Credit Guarantee (PCG) Fund for small farmers in Ukraine

1. **The project is expected to comply with FIF technical guidance when Russia's invasion of Ukraine ends and the national emergency is lifted**. While a definitive timeline is impossible to estimate, this is not envisaged in the immediate emergency phase and prior to the full operationalization of the PCGF.

2. **Before Russia's invasion of Ukraine began, the GoU put in place key legal, regulatory, and supervisory elements of a commercially viable PCGF.** The design included among others governance, legal and supervisory elements in line with good practices from the 16 Principles advocated by the WB. In line with the Law of Ukraine 'On Partial Credit Guarantee Fund in Agriculture' the target group of the PCGF are small farmers which are defined as micro, small and medium-sized business entities and natural persons - entrepreneurs, the main activity of which is the production of agricultural products, which meet the requirements for micro-enterprises, small and medium-sized enterprises according to the Law of Ukraine "On Accounting and Financial Reporting in Ukraine" and which own and/or use agricultural land not exceeding 500 ha, including land plots purchased with funds received on credit. Loans can be guaranteed up to 50 percent with a maximum maturity of 10 years. On February 6, 2023, the PCGF has been licensed as a non-bank financial institution to be supervised by the NBU. Once the anticipated initial capital of EUR 10 million is fully paid in, with the proposed 1:4 leverage and 50 percent guarantee coverage the PCGF will be able to facilitate up to EUR 80 million of financing for the small farmers by PFIs. In terms of purpose, loans can be provided for investment financing and working capital. The pricing of the guarantee will cover both default risks and administrative costs to ensure its financial sustainability. PFIs will also apply market-based pricing policies when extending loans. Table 1 provides information on the Assessment of the compliance of the PCGF with the Principles for Public Credit Guarantee Schemes for SMEs.

3. **As the PCGF was not established yet, the Government decided to use a bridge financing arrangement providing credit guarantees for agricultural loans through its state program managed by Ukreximbank**. As part of these state guarantees on a portfolio basis since December 2020, 17,614 loans totaling UAH 57.46 billion have been issued by 27 participating banks.[13] The program is administered by Ukreximbank. 6,969 loans worth UAH 33.48 billion were issued to agribusinesses. For agribusinesses the state guarantee cannot exceed 80 percent of the individual loan compared to 70 percent for other SMEs. The GoU is committed to accelerate the PCGF's full operationalization and replace the current temporary credit guarantee arrangements based on good governance, financial and systems standards. In a next step, as the PCGF becomes fully operational, it will be important for the GoU to decide upon a concrete timeline for the consolidation of all guarantee programs in support of small farmers at the PCGF.

4. **Implementation arrangements**. The WB is currently providing technical assistance to support operationalization of the PCGF. Basis is an agreed upon roadmap (see Table 2) of steps that need to be taken. Once achieved to the satisfaction of the Bank the PCGF can be considered fully operational. More concretely, the second tranche of EUR 4 million will be disbursed once (a) PCGF Internal Regulations are adopted and approved; (b) the PCGF Supervisory Board and the PCGF Management Board are duly elected and appointed; (c) a risk manager and internal auditor are appointed to the PCGF; and (d) at least one PFI has signed a Participation Agreement with the PCGF; all in form and substance satisfactory to the Bank.

[13] As of December 2022.

5. The project will use implementation arrangements consistent with FIF guidance. The project will use a standard due diligence review process based on financial performance (portfolio quality, capital adequacy, acceptable audits and liquidity), governance and regulatory compliance. The project operational manual will include the due diligence system, technical information on products, and a description of the partial guarantee system.

6. **Institutional, legal and regulatory framework**. The GoU designed a new government partial guarantee system for agricultural loans- the PCGF. A legal and regulatory system has been fully developed and is currently being operationalized that will meet the 16 principles set forth by the WB for a sustainable, efficient, institutionally sound PCGF. The legal basis for the PCGF is already created and it is anticipated to be operational in line with the Bank requirements by mid-2023. The PCGF is licensed and supervised by the NBU. This project will provide EUR 10 million into the capital of the PCGF, matched by the Government with envisaged support of the WB Accelerating Private Investment in Agriculture Program (P166941), which will bring the capitalization to approximately EUR 20 million. Overall, a capitalization of EUR 100 million had been envisaged prior to Russia's invasion of Ukraine, comprising of EUR 50 million tentatively provided by the EU which would be matched by a similar contribution of the GoU. Due to Russia's invasion of Ukraine, the EU contribution had to be revised downwards, while future possible contributions could not yet be secured. Once operational, guarantees will be provided on a wholesale basis through participating banks based on clearly defined eligibility criteria.

Table 1. Assessment of the compliance of the PCGF with the Principles for Public Credit Guarantee Schemes for SMEs[14]

Principles	Assessment
Legal and Regulatory Framework	
1. The CGS should be established as an independent legal entity on the basis of a sound and clearly defined legal and regulatory framework to support the effective implementation of the CGS's operations and the achievement of its policy objectives.	**Complied with.** The PCGF was established in 2022 as a separate legal entity under public law. The PCGF is subject to the regulatory framework for non-bank financial institutions and its operational rules are specifically regulated by the NBU under the Resolution "On the regulation of the PCGF's activities" No.184 dated August 19, 2022.
2. The CGS should have adequate funding to achieve its policy objectives, and the sources of funding, including any reliance on explicit and implicit subsidies, should be transparent and publicly disclosed.	**In progress.** Overall, a capitalization of EUR 100 million had been envisaged prior to the Russia's invasion of Ukraine, comprising of EUR 50 million tentatively provided by the EU which would be matched by a similar contribution of the GoU. Due to Russia's invasion of Ukraine, the EU contribution had to be revised downwards. The PCGF is expected to receive a total of approximately EUR 20 million in capital in 2023.
3. The legal and regulatory framework should promote mixed ownership of the CGS, ensuring equitable treatment of minority shareholders.	**Partially complied with.** As of today, the sole shareholder of the PCGF is the state. At the same time the Law of Ukraine "On Partial Credit Guarantee Fund in Agriculture" No. 1865-IX dated November 04, 2021 (PCGF Law) in paragraph 3 Article 1 regulates, that the PCGF can have other shareholders, which may be international financial organizations and other legal entities. The minimum share of the state in the authorized capital of the PCGF is 51 percent.
4. The CGS should be independently and effectively supervised on the basis of risk-proportionate regulation scaled by the products and services offered.	**Partially complied with.** The PCGF falls under the regulatory and supervisory framework of the NBU. The PCGF is subject to the regulatory framework for non-bank financial institutions and its operational rules are specifically regulated by the NBU under the Resolution "On the regulation of the PCGF's activities" No.184 dated August 19, 2022.
Corporate governance and risk management	
5. The CGS should have a clearly defined mandate supported by strategies and operational goals consistent with policy objectives.	**Partially complied with.** PCGF has a clear mandate – as stipulated in the PCGF Law – in supporting access to finance of small farmers in Ukraine[15]. The PCGF's Charter provides that the only activity of the PCGF is the provision of partial credit guarantees for loan obligations of small farmers. The envisaged strategy and business plans are yet to be developed.
6. The CGS should have a sound corporate governance structure with an independent	**Partially complied with.** PCGF's corporate governance is aligned with the standard structure for limited liability

[14] *Principles for public credit guarantee schemes for SMEs (English).* Washington, D.C.: World Bank Group. http://documents.worldbank.org/curated/en/576961468197998372/Principles-for-public-credit-guarantee-schemes-for-SMEs

[15] According to the PCGF Law, the target group are small farmers which are defined as micro, small and medium-sized business entities and natural persons - entrepreneurs, the main activity of which is the production of agricultural products, which meet the requirements for micro-enterprises, small and medium-sized enterprises according to the Law of Ukraine "On Accounting and Financial Reporting in Ukraine" and which own and/or use agricultural land not exceeding 500 hectares, including land plots purchased with funds received on credit.

	and competent board of directors appointed according to clearly defined criteria.	companies established by the legislation in Ukraine. The PCGF is regulated and supervised by the NBU, adding an additional layer of oversight. Members of the Management Board and Supervisory Board are not appointed yet. Nevertheless, a structured and transparent appointment process that adheres to explicit policies and procedures that seeks to ensure a majority independent Supervisory Board is implemented in the PCGF Law and secondary legislation, namely in the Resolutions of the Cabinet of Ministers of Ukraine: – “On Approval of the Procedure for the Competitive Selection of Independent Members of the Board of the Partial Credit Guarantee Fund” No. 508 dated May 03, 2022; – “On Approval of the Procedure for the Competitive Selection of an Executive Search Company to Select Candidates for Offices of Independent Members of the Board of the Partial Credit Guarantee Fund in Agriculture and the Executive Search Company to Recommend Remuneration for Members of the Board of the Partial Credit Guarantee Fund in Agriculture” No. 621 dated May 24, 2022; – “On Approval of the Procedure for the Competitive Selection of an Executive Search Company to Select Candidates for Offices of Independent Members of the Board of the Partial Credit Guarantee Fund in Agriculture and the Executive Search Company to Recommend Remuneration for Members of the Board of the Partial Credit Guarantee Fund in Agriculture” No. 621 of May 24, 2022.
7.	The CGS should have a sound internal control framework to safeguard the integrity and efficiency of its governance and operations.	**In progress.** According to Article 16 of the PCGF Law, the Fund should have an internal audit in place. The internal auditor of the Fund shall be appointed and dismissed by the Supervisory Board and shall report to the Supervisory Board. The internal auditor of the Fund shall submit the internal audit reports to the Supervisory Board of the Fund twice a year. The Fund’s internal audit reports are subject to approval by the Supervisory Board.
8.	The CGS should have an effective and comprehensive enterprise risk management framework that identifies, assesses, and manages the risks related to CGS operations.	**In progress.** According to the PCGF Law, the Supervisory Board is responsible for: • development and approval of risk management strategy and policy, risk management procedures, as well as the list of risks and their limits and • monitoring the performance of the risk management system. Therefore, the risk management framework will be established after the appointment of the Supervisory Board in line with relevant NBU regulations.
	Operational Framework	

9. The CGS should adopt clearly defined and transparent eligibility and qualification criteria for SMEs, lenders, and credit instruments.	**In progress.** According to the PCGF Law, the Supervisory Board is responsible for: • approval of the regulations on the procedure for providing guarantees by the Fund; • determination of additional criteria regarding the creditworthiness of business entities that are entitled to a partial guarantee by the Fund; • establishment of criteria for financial institutions to whom the loan obligations are guaranteed. Therefore, the eligibility and qualification criteria for small farmers, participating financial institutions, and loans will be designed after the appointment of the Supervisory Board.
10. The CGS's guarantee delivery approach should appropriately reflect a trade-off between outreach, additionality, and financial sustainability, taking into account the level of financial sector development of the country.	**In progress.** The PCGF aims to take these principles into account in its delivery approach.
11. The guarantees issued by the CGS should be partial, thus providing the right incentives for SME borrowers and lenders and should be designed to ensure compliance with the relevant prudential requirements for lenders, in particular with capital requirements for credit risk.	**In progress.** Under the PCGF law the only activity of the PCGF is the provision of partial guarantees for loan obligations of small farmers. The PCGF provides guarantees in the amount of up to 50 percent of the outstanding principal amount for the term of the loan agreement, but not more than for 10 years. The amount of uncovered guarantees provided may not exceed more than four times the amount of the regulatory capital of the PCGF.
12. The CGS should adopt a transparent and consistent risk-based pricing policy to ensure that the guarantee program is financially sustainable and attractive for both SMEs and lenders.	**In progress.** Under the NBU Regulation "On the approval of the Regulation on licensing and registration of financial service providers and the conditions for their activities in the provision of financial services" No. 153 dated December 24, 2021 the PCGF is obliged to prepare and submit a business plan, which must contain information about the applicant's business model and, in particular, the pricing policy. The pricing of the guarantee will cover both default risks and administrative costs to ensure its financial sustainability. PFIs will also apply market-based pricing policies when extending loans.
13. The claim management process should be efficient, clearly documented, and transparent, providing incentives for loan loss recovery, and should align with the home country's legal and regulatory framework.	**In progress.** Detailed internal regulations and guidelines are currently being developed.
Monitoring and Evaluation	
14. The CGS should be subject to rigorous financial reporting requirements and should have its financial statements audited externally.	**Partially complied with.** The PCGF's financial statements follow the accounting standards for non-bank financial institutions, as prescribed by NBU, and will be audited by reputable external auditors.

15. The CGS should periodically and publicly disclose nonfinancial information related to its operations.	**Partially complied with.** The annual reports include operational data and will be publicly disclosed.
16. The performance of the CGS—in particular its outreach, additionality, and financial sustainability—should be systematically and periodically evaluated, and the findings from the evaluation publicly disclosed.	**Partially complied with.** The PCGF was only established in 2022 and has not been subject to an external evaluation yet. That said, PCGF plans to implement this principle.

Table 2. Roadmap for establishing the PCGF

			Before 01.11.2022	11.2022	12.2022	I quarter 2023	II quarter 2023	III quarter 2023	IV quarter 2023
1.		**Legislation adoption**							
1.1.		Adoption and coming into effect of the Partial Credit Guarantee Fund (PCGF) law	+						
1.2.		Resolution of the CMU "On Establishing the Partial Credit Guarantee Fund in Agriculture" No. 125 of February 16, 2022;	+						
1.3.		Resolution of the CMU "On Approval of the Procedure for the Competitive Selection of Independent Members of the Board of the Partial Credit Guarantee Fund" No. 508 of May 03, 2022;	+						
1.4.		Resolution of the CMU "On Approval of the Procedure for the Competitive Selection of an Executive Search Company to Select Candidates for Offices of Independent Members of the Board of the Partial Credit Guarantee Fund in Agriculture and the Executive Search Company to Recommend Remuneration for Members of the Board of the Partial Credit Guarantee Fund in Agriculture" No. 621 of May 24, 2022;	+						
1.5.		Resolution of the CMU "On the approval of additional requirements for candidates for the position of Independent Member of the Board of the Fund for Partial Guarantee of Loans in Agriculture" No.669 of June 10, 22.	+						
1.6.		Order of the CMU "On approval of the composition of the Nomination Panel for the election of PCGF's independent Board members" No.930-p dated October 21, 2022	+						
1.7.		Order of the CMU "On the approval of the composition of the competitive commission for the selection of the personnel selection company, which selects candidates for the positions of independent members of the supervisory board of the Partial Guarantee Fund of Credits in Agriculture, and the personnel selection company, which recommends the amount of remuneration for the members of the Supervisory Board of the	+						

		Partial Guarantee of Credits in Agriculture” No. 941-p dated October 21, 2022							
1.8.		Resolution of the CMU “On making changes to the Charter of the Partial Credit Guarantee Fund in Agriculture ” No. 1219 dated October 28, 2022	+						
1.9.		The Resolution of the NBU "On the regulation of the PCGF's activities" No.184 dated August 19, 2022	+						
1.10.		Resolution of the CMU “On making changes to the Charter of the Partial Credit Guarantee Fund in Agriculture” No.334 dated April 18, 2023	+						
1.11.		Order of the CMU “On appointment of the state representatives in the Board of the Partial Credit Guarantee Fund in Agriculture from the state” No.476-p dated May 30, 2023	+						
1.12.		Order of the CMU “On appointment of the independent Board members in the Partial Credit Guarantee Fund in Agriculture” No.490-p dated June 02, 2023	+						
2.		**Approval of the budget program passport (Article 20(8) of the Budget Code of Ukraine)**	+						
3.		**PCGF Creation**	+						
3.1.		The legal entity has undergone the state registration and was registered with the tax authority	+						
3.2.		The seal has been produced	+						
3.3.		The bank account has been opened	+						
3.4.		Forming the initial authorized capital	+						
3.5.		Amendments to the State Budget of Ukraine for 2022 to ensure the formation and payment of the authorized capital of the Fund/amendments to the Statute	+						
4.		**Developing internal policies and procedures**							
4.1.		Drafting a Model Contract with an executive search agency that creates a short list of independent PCGF Board members (Article 8(8))			+				
4.2.		Drafting a Model Contract with an executive search agency that recommends remuneration for PCGF Board members (Article 8(9))				+			
4.3.		Drafting a Model Contract between the PCGF and an independent				+			

		PCG Board member (Article 8(24))							
5.		**Electing the Supervisory Board and the Board of the PCGF**							
5.1.		Making a decision to start hiring process	+						
5.2.		**Selecting an executive search agency to create a short list of independent members of the PCGF Board. Signing a contract with the executive search agency**							
5.2.1.		Nomination Panel's decision to hold the contest			+				
5.2.2.		Ministry's publication of the contest announcement			+				
5.2.3.		Receiving bids			+				
5.2.4.		Handing over bids to the Nomination Panel			+				
5.2.5.		Stage 1 — the Nomination Panel verifies the candidates' conformity with criteria			+				
5.2.6.		Stage 2 — the Nomination Panel reviews applications and chooses the best offer				+			
5.2.7.		The Ministry prepares and submits to the Cabinet of Ministers of Ukraine a draft decision to appoint an executive search agency and a draft service contract with the executive search agency				+			
5.2.8.		Negotiating the entry into the service contract with the executive search agency				+			
5.2.9.		Signing the contract and publishing information about final results of the contest				+			
5.3.		**Selecting an executive search agency to recommend the remuneration for Board members. Signing a contract with the executive search agency**							
5.3.1.		Nomination Panel's decision to hold the contest				+			
5.3.2.		Ministry's publication of the contest announcement				+			
5.3.3.		Receiving bids				+			

5.3.4.		Handing over bids to the Nomination Panel				+			
5.3.5.		Stage 1 — the Nomination Panel verifies the candidates' conformity with criteria				+			
5.3.6.		Stage 2 — the Nomination Panel reviews applications and chooses the best offer				+			
5.3.7.		The Ministry prepares and submits to the Cabinet of Ministers of Ukraine a draft decision to appoint an executive search agency and a draft service contract with the executive search agency				+			
5.3.8.		Negotiating the entry into the service contract with the executive search agency				+			
5.3.9.		Signing the contract and publishing information about final results of the contest				+			
5.4.		The executive search agency issues a short list of candidates					+		
5.5.		**Electing independent Board members**							
5.5.1.		The Cabinet of Ministers of Ukraine (CMU) requests international associations of guarantee institutions to nominate two representatives for the Nomination Panel	+						
5.5.2.		The CMU appoints three CMU representatives and two representatives of guarantee institutions for the Nomination Panel	+						
5.5.3.		The Nomination Panel elects independent Board members from the short list					+		
5.6.		The CMU appoints its representative to the Supervisory Board					+		
5.7.		The second executive search agency recommends the remuneration for both dependent and independent members of the Management Board				+			
5.8.		The shareholder meeting appoints independent members of the Management Board, approves the remuneration of both dependent and independent members of the Management Board							
5.9.		The PCGF enters into contracts with independent Board members							
5.10.		The Regulator endorses dependent and independent Board members							
6.		**The Shareholder Meeting approves**							
6.1.		The Core (Strategic) Lines of PCGF Operation (Article 7(1)(3))							

6.2.		The Development Strategy presented by the Board (Article 7(1)(4))							
7.		**Key decisions/action to be taken at the Board meeting**							
7.1.		Approve internal charters/regulations:							
7.1.1.		an internal charter of the PCGF Management Board (Article 8(11)(10))							
7.1.2.		an internal charter of the PCGF Board (Article 8(11)(10))							
7.1.3.		an organizational and staffing chart of the PCGF (Article 8(11)(6))							
7.1.4.		the number of members in the Management Board (Article 8(11)(12))							
7.1.5.		a model contract with the Chair and members of the Management Board (Article 8(11)(13))							
7.1.6.		an internal regulation on the Investment Policy (Articles 8(11)(11) and 13(2))							
7.1.7.		the risk management strategy and policy, risk management procedures, and the list of risks and their threshold levels (Article 8(11)(3))							
7.1.8.		a Charter of the internal audit function (Article 9(12)(12))							
7.1.9.		criteria for selecting an external auditor (Article 8(11)(14))							
7.1.10.		an internal regulation on the internal control system and the risk management system (Article 8(11)(11))							
7.1.11.		an internal Information Disclosure Policy (Article 8(11)(23))							
7.1.12.		an internal policy governing the eligibility criteria for private financial institutions (Articles 8(11)(21), 14(3))							
7.1.13.		an internal policy governing the eligibility criteria for borrowers (minimum loan underwriting standards) (Articles 8(11)(20), 14(2))							
7.1.14.		the specification of the maximum amount of guarantees per financial institution in the current year (Article 13(7))							
7.1.15.		the PCGF Development Strategy for three years (Article 8(11)(1))							
7.2.		**Appointment of the personnel**							

7.2.1.		Management Board							
7.2.2.		Risk Manager							
7.2.3.		Internal Auditor							
8.		**The Management Board is to make decisions on**							
8.1.		the allocation of duties among members of the Management Board							
8.2.		the recruitment of the personnel							
8.3.		the office space and procurement of office equipment							
8.4.		the development of a web portal					+		
8.5.		the scope of information to be disclosed on the web portal							
9.		**Licensing**							
9.1.		The approval of Guarantee and Suretyship Issue Rules by the PCGF Management Board together with sample contracts A partnership agreement between the PCGF and a private financial institution							
9.2.		Registration with the Register of Financial Institutions (up to 30 days, as agreed upon with the NBU)	+						
9.3.		PCGF Licensing (up to 30 days)				+			
10.		**Financial institutions**							
10.1		The selection of financial institutions							
10.2		The signing of a general framework agreement with financial institutions							
10.3		Training							
11.		**Guarantees**							
11.1.		Start of provision of partial guarantees for credit obligations of agricultural producers							

ANNEX 3: Financial Sector Trends

COUNTRY: Ukraine
Strengthening the Partial Credit Guarantee (PCG) Fund for small farmers in Ukraine

Situation prior to Russia's invasion of Ukraine

1. **Ukraine's financial system is dominated by banks, with significant state ownership.** Banks account for 88.6 percent of total financial system assets;[16] around 47 percent are state-owned, 31 percent are foreign, and 22 percent private banks. The Ukrainian banking sector lacks depth, with a private sector loan-to-GDP (gross domestic product) ratio at 28.2 percent in 2020, compared to a 57.5 percent average in the Europe and Central Asia (ECA) region (excluding high-income countries). Furthermore, the nonbank sector is underdeveloped and requires further strengthening of the regulatory and supervisory framework and financial system infrastructure. The private sector loan-to-GDP ratio stood at 28.4 percent in 2020 compared to a 55.2 percent average in ECA region (excluding high-income countries). Local businesses have repeatedly emphasized that limited access to finance is one of the biggest growth obstacles, and it is particularly problematic for SMEs. Sector concentration is in the normal range for a competitive market – the five-bank concentration stands at 56 percent of banking assets, but state-owned banks (SOBs) account for around half of banking sector assets.

2. **Following measures adopted in the aftermath of the 2014–2015 crisis, the Ukrainian banking system was in relatively good condition; but it faces heightened operational, credit, market, profitability, solvency and liquidity risks as a result of Russia's invasion of Ukraine**. Due to stringent regulatory and supervisory measures, systemwide capital adequacy stood at 18 percent and the aggregate nonperforming loan (NPL) ratio at 30 percent at end-2021 (down 11 percentage points compared to a year earlier). Bank profitability and liquidity were high; all 13 systemically important banks had liquidity coverage ratios (LCRs) of more than 150 percent (as of January 1, 2022), at least 50 percent above the required minimum. About a third of the loan portfolio and deposit liabilities are denominated in foreign exchange (FX), a key source of vulnerability in case of sustained currency depreciation and/or economic contraction. Another important vulnerability relates to possible negative feedback loops between Ukraine's fiscal accounts and the banking system given its large exposure to the government sector. See Table 1 for detailed information.

Table 1. Evolution of banking sector soundness

	2013	2014	2015	2016	2017	2018	2019	2020	2021
Capital adequacy ratio (%)	18.3	15.6	12.3	12.7	16.1	16.2	19.7	22.0	18.01
NPLs as share of total loans (%)	12.9	19.0	28.0	30.5	54.5	52.9	48.9	41.0	30.0
Liquid assets to total assets (%)	20.6	26.4	33.0	48.5	53.9	51.1	72.3	69.1	69.2
ROA (%)	0.3	-4.2	-5.5	-12.5	-1.8	1.6	4.7	2.8	4.5
ROE (%)	1.7	-32.0	-65.5	-122.2	-15.3	14.6	37.6	21.7	37.9
Customer deposits to total (non-interbank) loans (%)	73.3	64.5	71.2	80.5	84.6	81.8	103.1	139.0	140.3
FX-denominated loans to total	34.7	47.7	57.9	51.4	47.5	46.5	41.2	39.1	32.0

[16] This figure does not include collective investment institutions and pension funds.

loans (%)									
Share of state bonds in bank assets (% of total assets)	7.0	7.9	7.0	19.4	26.1	29.9	24.5	31.7	28.6

Sources: NBU; World Bank staff calculations. *Note:* ROA = return on assets; ROE = return on equity.

Post Russia's invasion of Ukraine

3. **While the payment system has been operating smoothly since the start of Russia's invasion of Ukraine, recent strikes on infrastructure have temporarily impacted banks' operations**. According to NBU, around 87 percent of bank branches were operational as of end January 2023. The share of working branches has decreased compared to the peak of early 2023 due to the return of scheduled power outages. Mykolayiv's and Kherson's shares of working branches are improving after restoring government control over the right bank of the Dnipro river, although the pace has slowed in Kherson due to constant artillery shelling. NBU is implementing a plan – jointly with banks - to ensure continuity of the banking system amid possible long-term blackouts. Systemically important banks have identified a list of 760 regular branches located in Kyiv and in 275 settlements in 22 oblasts, which will provide financial services to clients even in conditions of long-term power outages. These branches are currently being furnished with all the necessary equipment and communication channels designed for continuous operation when there is no power. Plans are being implemented to ensure the resupply of these branches with additional staff, cash register equipment, ATMs, and cash. In addition, several measures have already been taking including the cashback option at point of sale (POS) – essentially allowing cash withdrawal at merchants alongside a purchase - as well as preserving data security by transferring banks' IT systems to cloud-based solutions.

4. **Banks, at an aggregate level, are very liquid.** Since the beginning of Russia's invasion of Ukraine, bank deposits have increased by 32.3 percent in UAH equivalent (or by UAH 463 billion), which is partly attributed to Hryvnia depreciation. Hryvnia retail deposits have surged by 40.6 percent, stabilizing in 2023. FX retail deposits have fully restored after an outflow at the beginning of Russia's invasion of Ukraine, demonstrating a slight increase by 3.9 percent net of FX effect over the last four months. The FX term deposits increase was, mainly due to an increase in term deposits driven by NBU measures to allow conversion of Hryvnya into FX at banks' exchange rates (normally better than street rate) provided the FX funds are deposited for at least three months. Hryvnia corporate deposits resumed growth in August and edged up at the end of the year, resulting in a 25 percent increase since February 24. Corporate FX deposits have increased by 6.5 percent since the start of Russia's invasion of Ukraine. The overall growth of deposits is concentrated in SOBs, while other banks, as a group, experienced a slight decline in deposit funding. End-January 2023, NBU announced that it would continue to keep its policy rate unchanged at 25 percent and would increase reserve requirements further in two steps.

5. **Access to finance has been subdued as a result of Russia's invasion of Ukraine as banks' risk averseness rose and demand lowered.** Local currency retail loans have been declining since the start of Russia's invasion of Ukraine, and corporate loans in hryvnia have been decreasing since mid-June. Retail loans have been declining since the early days of Russia's invasion of Ukraine (by 38 percent in UAH and 48 percent in FX), as well as corporate loans in FX (by 29 percent). Corporate loans in UAH are 6 percent below levels prior to Russia's invasion of Ukraine, declining 14 percent since mid-June. The state program "5-7-9", which was broadened in April, has driven the short-lived growth of crediting at the beginning of Russia's invasion of Ukraine. The loan portfolio under the program increased since the beginning of Russia's invasion of Ukraine by UAH 78.1 billion, making up 26 percent of the hryvnia net corporate loan portfolio, of which SOBs issued 52 percent, however, since June, the issuance of new loans has significantly slowed.

6. **Asset quality is being significantly impacted by Russia's invasion of Ukraine**. The banking system was in relatively sound condition prior to Russia's invasion of Ukraine, and the overwhelming majority of banks remained liquid and operational. However, the loss of assets, collateral, and revenues will severely affect banks' profitability and solvency.

During March-December 2022, the banking sector already accounted for USD 2.9 billion (UAH 105 billion) of loan loss provisions for expected credit losses related to Russia's invasion of Ukraine, which is 34 times the amount posted in the same period of 2021. Since the start of Russia's invasion of Ukraine, four banks have been declared insolvent – two subsidiaries of Russian state-owned banks and two local private banks. From the preliminary baseline scenario estimates of the RDNA, potential credit losses suffered by the banking sector could reach USD 8.1 billion, resulting in more bank failures. The Deposit Guarantee Fund's resources will not suffice to deal with these expected failures. Significant regulatory forbearance measures have been introduced, including deferral of sanctions on banks that breach minimum regulatory requirements during martial law. Audits of banks' statements for 2021 and regular annual stress-tests/AQR have been postponed.

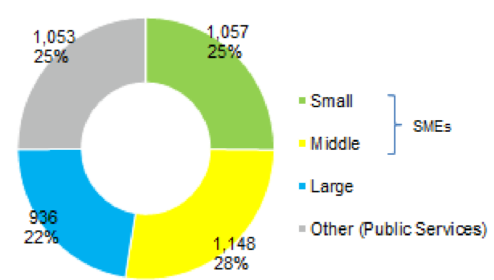
ANNEX 4: Access to Finance

COUNTRY: Ukraine

Strengthening the Partial Credit Guarantee (PCG) Fund for small farmers in Ukraine

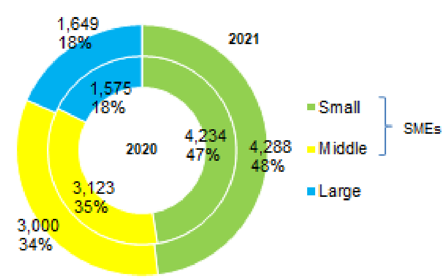
1. **In recent years, Ukraine has prioritized the development of SMEs, recognizing their growing importance for the economy and employment.** In 2017, the Government adopted a "Strategy for Small and Medium-sized Enterprise Development in Ukraine until 2020," with the goal of creating more favorable conditions for opening, operating, and growing SMEs. SMEs already play an important role in the Ukrainian economy. As noted above, out of all businesses registered in Ukraine large enterprises constitute less than 1 percent, whereas the universe of micro, small, and medium size enterprises and private entrepreneurs comprised over 99 percent of registered businesses (Table 1) and in 2020 generated nearly 50 percent of GDP and employed near 45 percent of all employed (Figures 1 and 2).[17] However, compared to peer countries, the density of formal micro, small, and medium size enterprises per 1,000 people in Ukraine (7.5) is far lower than in Romania (23.7), Turkey (30.1), Bulgaria (47.4), or Kazakhstan (61.3), indicating there is much room for expansion of the SME sector.[18] Although the number of small enterprises working in agriculture is only 4 percent, the sector is of greater importance for medium enterprises – 13 percent. Small and medium enterprises combined, play a large role in value addition in the sector with a share of 86 percent in agriculture (Table 2).

Figure 1. Enterprise value added in GDP 2020, UAH billion



Source: Ukrstat

Figure 2. Officially employed in private sector in 2020-21, thousands



Source: Ukrstat

[17] Ukrstat, Economic statistics / Economic activity / Activity of enterprises

[18] Micro, small, and medium size enterprises Economic Indicators Database, 2019.

Table 1. Distribution of enterprises by economic activity in 2020

	Large	Medium	Small
Share in total enterprises	0.03%	0.93%	99%
	Distribution by economic activity		
Industry	*50%*	*28%*	*6%*
Trade	*30%*	*18%*	*43%*
Agriculture	*7%*	*13%*	*4%*
Transportation and storage	*6%*	*7%*	*5%*
Information and communication	*2%*	*2%*	*11%*
Construction	*2%*	*5%*	*3%*
Professional, scientific, technical activities	*1%*	*3%*	*7%*
Administrative and support services	*1%*	*5%*	*3%*
Real estate activities	*0%*	*2%*	*5%*
Other	*1%*	*17%*	*13%*
	100%	***100%***	***100%***

Source: Calculated based on Ukrstat
Note. Legal entities and private entrepreneurs

Table 2. Value added by enterprise size[19] in 2020

	Large	Medium	Small	Total	*out of which SME*
Transportation and storage	*58%*	*28%*	*14%*	*100%*	*42%*
Industry	*50%*	*39%*	*11%*	*100%*	*50%*
Information and communication	*41%*	*38%*	*22%*	*100%*	*59%*
Trade	*26%*	*31%*	*43%*	*100%*	*74%*
Agriculture	*14%*	*46%*	*40%*	*100%*	*86%*
Construction	*12%*	*40%*	*48%*	*100%*	*88%*

Source: Calculated based on Ukrstat
Note. Only in the form of legal entities

2. **Among the challenges to firm performance in Ukraine, access to finance has historically been one of the biggest growth obstacles and particularly problematic for SMEs.** The Government has recognized this and "improving access to finance" was one of the key strategic directions in the SME Development Strategy. In the 2013 Enterprise Survey, only 16.2 percent of firms identified access to finance as a major constraint to business operation, but this percentage grew to 46.3 percent in 2019. Only 22.1 percent of respondents had a bank loan/line of credit, compared to 37.1 percent for the ECA average in 2019. Few firms use bank loans for investment or working capital purposes, only 16.3 percent and 21.5 percent respectively. According to the SME Finance Forum, 56.8 percent of SMEs in Ukraine are either fully or partly credit constrained. The SME Policy Index[20] in 2020 also demonstrates poor progress in facilitating access to finance for SMEs since the last Small Business Act assessment in 2016, though other pillars (institutional framework, public procurements, SME skills, internalization

[19] UkrStat for this type of statistical report shows only limited number of sectors with large number of players, excluding those sectors, where only few enterprises dominate.
[20] OECD et al. (2020), SME Policy Index: Eastern Partner Countries 2020: Assessing the Implementation of the Small Business Act for Europe, SME Policy Index, European Union, Brussels/OECD Publishing, Paris, https://doi.org/10.1787/8b45614b-en.

etc.) experienced significant progress. According to a USAID Competitive Economy Program[21] in 2020, access to finance was identified as a major obstacle for growth, behind complex legislation, corruption, and insufficient demand.

3. **SMEs continue to be constrained by loan tenor.** Historically, firms have noted difficulty in accessing loans with maturities above one year for investments[22], and the situation has not changed much. Sources of long-term capital investments are not highly diversified, and self-financing is the primary source (69 percent) of capital investment for enterprises. It is even higher for agriculture sector – 91 percent. Bank loans represent only a small share (5 percent) of investment financing of firms (9 percent of agriculture firms).[23] Analysis of NBU data as of December 2021[24] shows that the SME loan portfolio is dominated by short-term loans; 60 percent of loans to non-financial firms had maturities of less than 1 year, and only 14 percent had a maturity of more than 5 years. The situation has deteriorated since 2020, when 17 percent of the loans had a more than 5 years maturity. Long-term agriculture loans are quite rare, and the share of more-than-5 years loans in the sector is only 4 percent at the end of 2022.

4. **SME sector has been directly impacted by Russia's invasion of Ukraine; however, the full scale of the impact on financial viability will be reflected in 2023.** Recent data from the NBU highlighted that around a third businesses completely stopped or almost stopped operations since the outset of Russia's invasion of Ukraine. The most important obstacles for businesses were driven by Russia's invasion of Ukraine: rising prices on raw materials, difficulties with transportation, shrank demand, lack of working capital.[25] The implemented financial forbearance measures are expected to delay or avoid business exits. However, the full effect on the financial system will be better known in 2023, when, the scale of business exits will become clearer and deterioration of credit quality for SMEs will be reflected in banks' balance sheets. For exporting SMEs, the consequences are likely to continue longer before disrupted export supply chains recover in and outside Ukraine.

5. **Russia's invasion of Ukraine exacerbated challenges for businesses in Ukraine, including financing needs of SMEs.** The share of small and middle enterprises that name limited availability of loans a constraint for further growth is not that big (9 and 11 percent, vs 6 and 9 percent at end-2021), compared to current issues – military actions (85 percent), low demand (37 and 44 percent) and high raw materials prices (39 and 41 percent). Still, the number of businesses which expect their borrowing needs to rise in the nearest future is high – 46 percent, 10 pp higher than a year ago. Among agriculture companies the expectations are even higher – 51 percent vs 26 percent at end-2021, and about 56 percent intend to take a loan in the nearest future, which is 10 pp higher than at end-2021. On the other hand, banks have significantly tightened their lending conditions since the start of Russia's invasion of Ukraine. High loan rates remain the main factor deterring businesses from taking out new loans (for about half of respondents, and 40 percent for agricultural companies). Collateral requirements are another constraint for about a quarter of Ukrainian businesses and one-fifth for agricultural companies wanting to apply for a loan. Preliminary results of a World Bank survey[26] among 2000 farmers conducted in 2022 found that over

[21] Report on the assessment of state policy implementation of SMEs development in Ukraine 2019 (Ukrainian), USAID Competitive Economy Program, Results are published in "Big Problems of a Small Business" Systemic Report, Business Ombudsman Council. https://boi.org.ua/media/uploads/system_bigproblemssmalbusiness/3_2020_system_ua.pdf
[22] Senechal T, 2016, Market Assessment of Trade Finance Facilities in Ukraine
[23] Ukrstat, Capital investments by sources of financing by types of economic activity for 2021
[24] NBU Financial Sector Statistics, Loans to SMEs, September 2020, https://bank.gov.ua/en/statistic/sector-financial/data-sector-financial#2fs
[25] NBU Monthly Macroeconomic and Monetary Review, Q32022/ Q42021,
https://bank.gov.ua/admin_uploads/article/%D0%9C%D0%9C_2022-10_eng.pdf?v=4
[26] The survey was conducted by the World Bank's research department with implementation support by the Kyiv International Institute of Sociology (KIIS) and Kyiv School of Economics (KSE)

90 percent of farmers with a farm size between 50-500 ha want to borrow while close to 40 percent in that group have never received a loan.

6. **Amid the tightening of banks' credit conditions, the state program Accessible loans 5-7-9 percent in combination with State Portfolio Guarantee Program, were almost the only channels of corporate crediting.** In 2021, loans granted under the program accounted for 18 percent of the net hryvnia corporate portfolio, and as of December 2022 – 26 percent. CMU expanded the 5-7-9 Loan Program in early spring. This included a lending program to agribusinesses at favorable terms (short-term loans up to 6 months, with full interest rate compensation, and an increased loan amount of UAH 60 million), with bigger enterprises becoming eligible. As of December 2022, the program accounted for 26 percent of the net hryvnia corporate portfolio. In 2022, lending took place almost exclusively through the program. By mid-December 2022, UAH 161 billion in loans under 52,000 loan agreements had been approved in all areas. The total amount of outstanding loans was about UAH 95 billion. As part of the state guarantees on a portfolio basis, 17,614 loans totaling UAH 57.46 billion have been issued by 27 participating banks since December 2020.[27] 6,969 loans worth UAH 33.48 billion were issued to agribusinesses. For agriculture companies the state guarantee cannot exceed 80 percent of the individual loan compared to 70 percent for other SMEs.

[27] As of December 2022.