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Guaranteeing additionality?

A case study of loan portfolio guarantees and their impact in Kenya

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Abstract

Development guarantees (DGs) have been projected to mobilise considerably more private capital per public dollar relative to other instruments, but evidence on their development impact remains limited. This thesis addresses this gap through a case study of loan portfolio guarantees (LPGs) issued by the African Guarantee Fund (AGF) in Kenya, by examining the research question: *how and under what conditions does AGF's guarantee scheme generate additionality for Kenyan MSMEs, and what are the implications for guarantees as instruments in Danish development finance?*

Drawing on thematic analysis of interviews with AGF, their beneficiaries and development finance experts, the analysis applies New Institutional Economics, Strategic Alliance Theory, and a Financialization lens to examine the effects of DGs in practice. The findings confirm collateral constraints as the dominant market failure in the Kenyan MSME credit market and DGs as a viable corrective instrument. In terms of financial additionality, we find AGF's LPGs do enable formal access to finance for previously excluded borrowers. On development additionality we find that impact is conditional on PFI behaviour and technical assistance. We argue that these findings provide much-needed evidence for informing future DG facilities, including the upcoming DKK 12 billion Danish allocation to DG interventions.

Key words: Development guarantees, Loan portfolio guarantees, Additionality, Blended Finance, MSME Finance, Kenya

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List of Abbreviations

AFFAWA	Affirmative Finance Action for Women in Africa
AGF	African Guarantee Fund
CPE	Critical Political Economy
DAC	Development Assistance Committee
DG	Development Guarantee
DGF	Development Guarantee Facility
IFDK	Impact Fund Denmark
ILO	International Labour Organisation
LPG	Loan Portfolio Guarantees
MSMEs	Micro, Small and Medium-Sized Enterprises
M&E	Monitoring & Evaluation
MFA	Ministry of Foreign Affairs (Denmark)
MDB	Multilateral Development Bank
NIE	New Institutional Economics
ODA	Overseas Development Assistance
OECD	Organisation for Economic Co-operation and Development
PFI	Partner Financial Institution
PSI	Private Sector Instrument
RQ	Research Question
SAT	Strategic Alliance Theory
SIDA	Swedish International Development Cooperation Agency
SDGs	Sustainable Development Goals
SSA	Sub-Saharan Africa
TA	Technical Assistance

List of Definitions

Development Guarantee (DG)	A risk-sharing instrument in which a public or development actor commits to compensate a financial institution for part of its losses if a borrower or project defaults (Garbacz, 2021; Winpenny, 2005).
Loan Portfolio Guarantee (LPG)	A form of development guarantee in which a guarantor covers a defined share of losses across a portfolio of loans issued by a partner financial institution (Soumaré, 2022; World Bank, 2015).
Blended Finance	The strategic use of development finance for the mobilisation of private capital towards sustainable development in developing countries (OECD, 2018).
Mobilisation	The process through which public development finance attracts additional private investment that would not otherwise have been deployed (OECD, 2025b).
Financial additionality	The ability of an intervention to provide finance and/or improves financial conditions beyond what would have occurred under standard market terms (Winckler-Andersen et al., 2021).
Development additionality	The ability of an intervention to deliver development impact, such as employment creation or financial inclusion, that would not have occurred without it (Winckler-Andersen et al., 2021).
Access additionality	A subset of financial additionality referring specifically to whether previously excluded borrowers gain access to formal credit as a result of the intervention (authors own interpretation).
Terms additionality	A subset of financial additionality referring specifically to whether borrowers get credit on better terms relative to prior of the intervention (authors own interpretation).
Credit rationing	A situation in which lenders restrict loan supply even to borrowers willing to pay higher interest rates, typically as a response to information asymmetry and adverse selection in credit markets (Stiglitz and Weiss, 1981).
Information asymmetry	A condition in which one party to a transaction has less information than the other party about characteristics of the transactions (Stiglitz and Weiss, 1981)
Adverse selection	The tendency of market failures to produce outcomes in which entire categories of borrowers are excluded from credit markets, typically because lenders cannot distinguish between safe and risky borrowers at acceptable cost (Stiglitz and Weiss, 1981) (adapted to specific context of this thesis)

Collateral	An asset that a borrower offers to a lender as security for a loan. If the borrower defaults on the loan (fails to repay), the lender has the right to seize and sell the collateral to recover the outstanding loan amount.
Partner Financial Institution	A commercial bank or financial institution that has entered into a guarantee-agreement with a DG-issuing organisation, committing to extend credit to targeted borrower segments under the terms of the guarantee (authors own interpretation; adapted to specific context of this thesis)
Micro, Small and Medium-Sized Enterprises (MSMEs)	Firms defined by employee count, turnover, or asset size that fall below the threshold of large enterprises. In the African context, MSMEs are typically defined as firms with fewer than 250 employees, but definitions vary by country and institution (African Union, 2019; OECD, 2026a).
Market failure	The inability of a competitive market to achieve an efficient allocation of resources often due to imperfect information, and other market imperfections that prevent efficient behaviour (Besley, 1994)
Moral Hazard	A situation in which the allocation of risk between economic agents changes the behaviour of the agent who does not bear full consequences of their actions (Besley, 1994)
Asymmetric Dependence	A condition in strategic alliances in which partners are unequally dependent on one another, with the less dependent partner having more bargaining power and less incentive to comply fully with shared objectives (Casciaro and Piskorski, 2005; Parkhe, 1993).
Financialization	The increasing role of financial motives, financial markets, financial actors, and financial institutions in the operation of domestic and international economies (Epstein, 2005, p. 3).

1. Introduction

It is no longer a debated topic: the world is facing a development financing crisis. The annual development financing need towards 2030 is estimated at USD 3 to 4 trillion, and the gap only continues to grow (OECD, 2025a). Many traditional donors have cut their aid budgets, and the most recent OECD figures estimate a 23.1% decline in bilateral Overseas Development Assistance (ODA) between 2024 and 2025 (OECD, 2026b). As OECD Secretary General Cormann stated, this decline in ODA *"highlights the need to maximize impact of available resources, and to use them more effectively"* (OECD, 2026c, p. 1).

The concept of blended finance has emerged as a direct response (OECD, 2018). At its core, blended finance deploys public funds (such as ODA) to de-risk investments and projects thereby attracting much needed private capital. This shift is reflected in the Development Assistance Committee's (DAC's) own trajectory: in recent years, donors have started to move away from direct ODA transfers toward more catalytic blended finance instruments (OECD, 2025a).

Yet mobilising private capital is not straightforward, least of all in places where it is most needed (OECD, 2023). Private investors operate on a risk-return logic: they allocate capital where expected returns are proportional to expected risk. In much of Sub-Saharan Africa (SSA), however, political uncertainty, weak regulatory frameworks, and unstable financial markets inflate the perceived risk far beyond its reality (Amine et al., 2025; Bayliss, 2020; Hansen et al., 2020). This creates a paradox in which the regions and people most in need of investment are precisely those that conventional private finance tends to withhold from (Sial & Chandrasekhar, 2024).

Development guarantees (DGs) have emerged as one of the most direct responses to the challenge of mobilising private capital toward underserved segments in developing countries. In practice, DGs are financial instruments through which public or multilateral actors cover part of the risk of an investment, thereby lowering the risk profile sufficiently for private investors or banks to engage with markets or borrowers they would otherwise avoid.

While DGs operate across different levels of the development finance system - from protecting investors against political risk to covering credit risk for local banks (Barder & Talbot, 2015), it is the latter type, that sits at the centre of this thesis. Loan portfolio guarantees (LPGs) are a

widely used type of DG specifically designed to address the financing gap facing micro, small and medium-sized enterprises (MSMEs). In SSA, MSMEs make up over 90% of all businesses and are central to employment and economic growth (African Union, 2019). Yet the majority remain shut out of formal credit markets. One reason being that banks cannot easily verify the creditworthiness of small borrowers, and most MSMEs lack the land or property that banks require as collateral (Njue & Mbogo, 2017; Stiglitz & Weiss, 1981) Under an LPG, the guarantor covers a share of the bank's potential losses across a portfolio of loans, thereby reducing risk sufficiently for the bank to lend to borrowers it would normally not lend to.

DGs ability to unlock access to financing have led donors to scale up DG programmes as a targeted response to the increasing financing gap (Sial & Chandrasekhar, 2024). Denmark is a case in point: a pilot DG programme introduced in 2022 has since been scaled into a permanent Development Guarantee Facility (DGF) with a total DG frame of DKK 12 billion, reflecting a broader shift in how donor countries are choosing to deploy scarce public resources (Impact Fund Denmark, 2025). It is within this context that this thesis examines what it takes for a DG to generate development impact in practice.

Yet, despite DGs receiving growing attention in the field, the development impact of DGs remains poorly understood. Their potential has been assessed primarily through the lens of mobilisation rather than what happens after capital is deployed, and whether it actually reaches underserved borrowers remains an open question (Hansen et al., 2020; Winckler-Andersen et al., 2021). A growing body of critical scholarship further raises concerns that reliance on instruments like DGs reflects a broader reorientation toward attracting private capital rather than addressing what is developmentally needed (Bernards, 2024; Van Waeyenberge, 2015).

This thesis focuses on the ability of DGs to generate what researchers and policymakers call 'additionality': development impact that would not have occurred without the guarantee (Gillenwater, 2012). In the context of this thesis, a distinction is drawn between two types; 1) financial additionality - whether the DG unlocks finance that would otherwise not have been available; and 2) development additionality - whether that finance translates into real socio-economic outcomes such as job creation, business growth, and improved conditions for underserved groups (Winckler-Andersen et al., 2021).

To examine the additionality of DGs, this thesis draws on the case of the African Guarantee Fund (AGF), employing both New Institutional Economics (NIE), Strategic Alliance Theory (SAT) and Critical Political Economy (CPE) as our theoretical frameworks. Focusing specifically on AGF's LPGs in Kenya, the study asks:

Research Question: How and under what conditions does the AGF's guarantee scheme generate additionality for Kenyan MSMEs, and what are the implications for guarantees as instruments in Danish development finance?

The study is based on eleven semi-structured interviews with stakeholders involved in AGFs LPG operations and is supplemented by portfolio-level data on AGFs LPGs. The research question is examined through four analytical sub-questions including

1) *Are the market failure conditions that theoretically justify LPGs empirically present in the Kenyan MSME credit market?*
2) *How does AG''s LPG scheme translate into financial and development additionality in practice?*
3) *How does the AGF-PFI relationship impact LPG's ability to generate additionality?*
4) *What do the findings reveal about the design conditions necessary for guarantees to function as effective instruments within Danish development finance?*

Our findings contribute to the thin empirical literature on the development impact of DGs (Hansen et al., 2020) and aim to generate insights relevant to the design of Denmark's permanent DGF. The thesis proceeds as follows: Section 2 provides contextual background; Section 3 reviews relevant literature; Section 4 introduces the theoretical framework; Section 5 presents the methodology; Section 6 contains the analysis; Section 7 discusses broader implications and limitations; and Section 8 concludes.

2. Background for the thesis

This section provides the contextual foundations on which the literature review, theoretical framework, and analysis build. It proceeds in three parts: the MSME landscape and Kenya's credit market (2.1); DGs as a tool in development finance (2.2); and AGF as the case institution (2.3).

2.1 The context: MSMEs in the Kenyan Credit Market

MSMEs are the backbone of Kenya's economy, yet they face persistent and structural barriers in accessing finance. In Kenya, MSMEs contribute to 33% of GDP and employ over 80% of the private sector workforce (Grant Thornton, 2025). Following the 2022 election, MSMEs even obtained a dedicated State Department for advancing their terms on the Kenyan market (Government of Kenya, 2026).

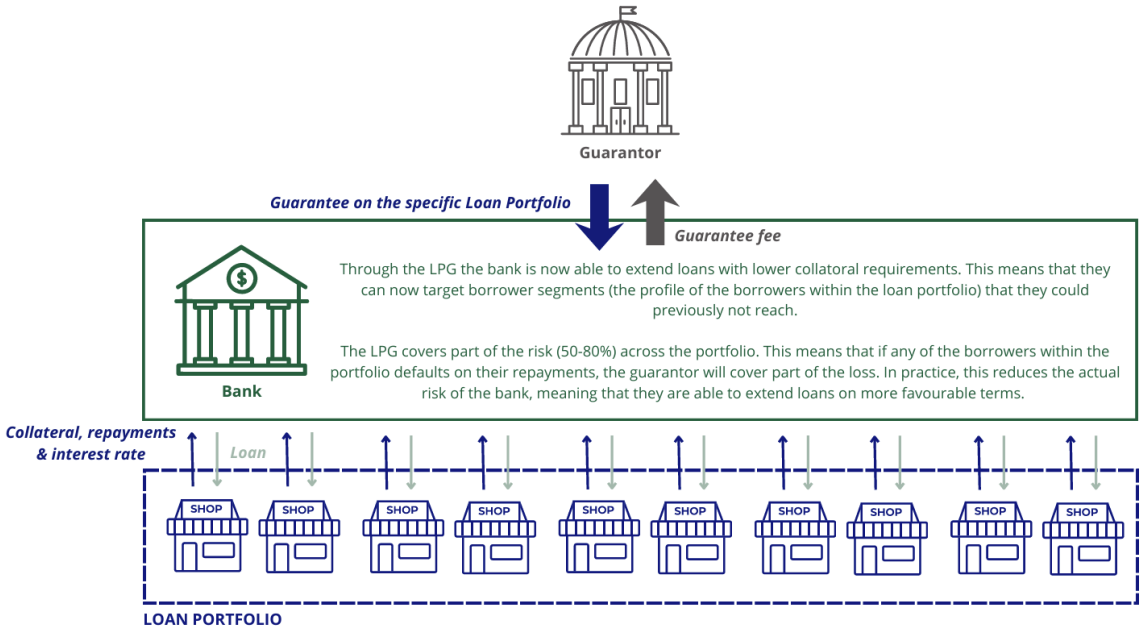
Despite their central role in the Kenyan economy, MSMEs remain systematically underserved by formal financial institutions, with an estimated financing gap of USD 19 billion (FSD Kenya, 2024). Indeed, access to finance is amongst the most frequently cited barriers to MSME growth. According to FSD Kenya (2024), there are approximately 7.4 million MSMEs in Kenya, the majority of which operate informally and without licenses. Survey evidence indicates that around 25% of all business owners report access to finance as a major barrier to growth (KNBS, 2024). For MSMEs specifically, this figure is likely to be even higher, due to their low asset base and their limited ability to pledge collateral (OECD, 2018).

Kenya's credit market compounds these challenges. Despite representing one of SSAs more developed financial sectors, it remains characterised by strong barriers to credit access particularly for MSMEs (World Bank, 2025). With high collateral requirements being a common way for Kenyan banks to compensate for risk, they frequently require borrowers to pledge assets above the value of their lending volume (Karumba and Wafula, 2012). However, most MSMEs lack sufficient or formally documented assets that satisfy these requirements (Njue and Mbogo, 2017), and the legal and administrative processes associated with registering collateral can be complex and time-consuming (ibid.). Borrowing costs further compound the barrier, with commercial bank lending rates typically being around 5 to 10 percentage points above the rate of the Central Bank of Kenya (Trading Economics, 2025). Faced with these barriers, MSMEs typically rely on informal sources of finance, with approximately 40% obtaining financing through family and friends (FSD Kenya, 2024).

2.2 The instrument: Guarantees as a tool in Danish Development Finance

A development guarantee is a risk-sharing instrument in which a public or development actor commits to compensate a financial institution for part of its losses if a borrower defaults (Winpenny, 2005; World Bank, 2015). This thesis focuses specifically on loan portfolio guarantees (LPGs), where a guarantor covers a defined share of losses across a portfolio of MSME loans issued by a partner financial institution (PFI), typically between 50-80% (see Figure 1). This partial coverage preserves the lender's incentive to assess borrowers carefully while enabling it to extend credit to borrowers it would otherwise consider too risky.

Figure 1: Illustration of a Loan Portfolio Guarantee

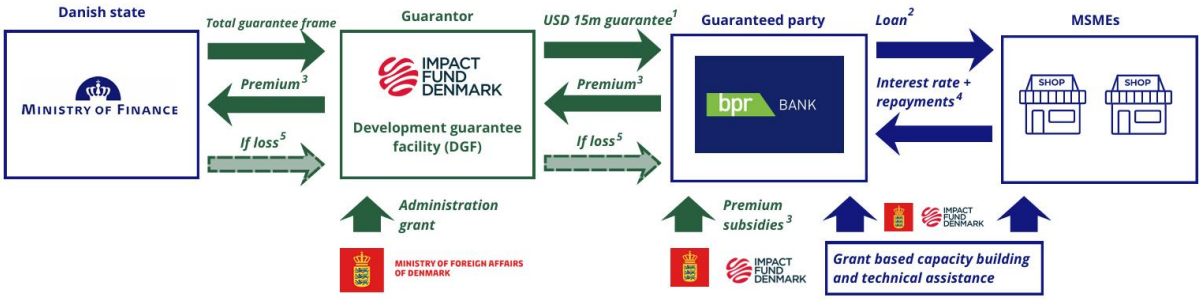


Source: authors own interpretation

Denmark's use of DGs as a dedicated bilateral instrument is relatively recent. Denmark has previously supported guarantee-issuing institutions through its development cooperation, yet DGs only became established as a distinct bilateral instrument through a pilot programme launched jointly with Sida in 2022 (MFA, 2023). Following the pilot, the Danish government decided in 2026 to establish a permanent guarantee facility (DGF) with a total frame of DKK 12 billion towards 2030 (MFA, 2026), administered by Impact Fund Denmark (IFDK) and expected to become operational in Q3 2026.

The pilot programme illustrates how the instrument is being applied across different contexts. Most relevant to this thesis is IFDK's LPG to the Rwandan commercial bank BPR (Impact Fund Denmark, 2026). The DG frame was initially USD 5.6 million, but was recently expanded to USD 15 million, and is designed to expand MSME lending in a market with credit challenges comparable to Kenya (Figure 2).

Figure 2: Illustration of how a guarantee works in practice (BPR Bank, Rwanda)



1 + 2: A DG covers part of BPR's risk that the borrower will not repay the loan amount
3: To access the DG, BPR pays a premium to the guarantor, which is the price of the DG. This premium can be subsidized using ODA.
4 + 5: If the MSME default on their loan repayments, the guarantor covers part of the loss to BPR.

Source: Internal Impact Fund Denmark material on Development Guarantees

2.3 The Case Institution: African Guarantee Fund

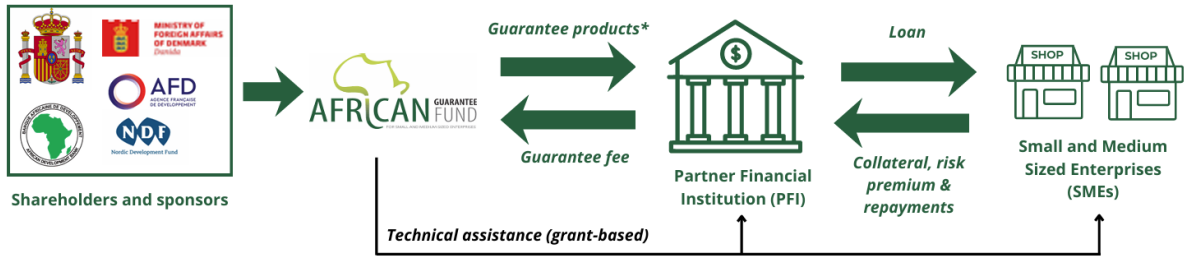
The African Guarantee Fund (AGF) represents the case institution of this thesis. It was selected because it is amongst the most established DG-issuing institutions on the African continent. Founded in 2011 with a mandate to address MSME financing constraints across Africa, AGF operates by providing DGs to PFIs and capacity development support to both lenders and MSMEs (MFA, 2018). Its scale, maturity, and Denmark's significant role as a founding shareholder makes it a particularly relevant case for examining the conditions under which DGs generate additionality.

AGF was founded by the African Development Bank, the Government of Spain through AECID, and the Government of Denmark through the Ministry of Foreign Affairs, initially capitalised with USD 50 million in share capital (MFA, 2018). Since its establishment in 2011, Denmark has been the largest contributor, with an ownership share of approximately 42%. This makes Denmark's development finance priorities directly relevant to how AGF's DG scheme is designed and evaluated.

Rather than lending directly to MSMEs, AGF operates as a risk-sharing intermediary, absorbing part of the credit risk on behalf of PFIs and thereby enabling them to extend finance

to borrowers they would otherwise consider too risky (see Figure 3). Since becoming operational, AGF has issued approximately USD 2.7 billion in guarantees, mobilising around USD 5.5 billion in MSME loans through more than 100 PFIs across Africa by the end of 2024 (AGF, 2025). Beyond its DG operations, AGF provides technical assistance (TA) to both PFIs and MSMEs, supporting lenders in developing MSME financing capabilities and helping borrowers improve their readiness to obtain formal financing.

Figure 3: African Guarantee Fund Structure and Operations



*AGF has several types of guarantees. Loan portfolio guarantees (75%), Bank Fundarising Guarantee (11%), Loan Individual Guarantee (14%) and Equity Guarantee (<1%). Above demonstrates the most common type of guarantee instrument.

Source: Adapted from AGF annual report, 2024

3. Literature review

This literature review maps three interconnected fields that together frame the analytical contribution of this thesis. The first situates the AGF case within broader debates about blended finance and mobilisation (3.1); the second examines how the literature defines and measures additionality in the context of DGs (3.2); the third identifies the theoretical gaps that this thesis seeks to address (3.3). Indeed, while the financial performance of DGs have received growing scholarly attention (Brown & Lee, 2017; IFAD, 2014; Winckler-Andersen et al., 2019), the literature remains predominantly policy-oriented. As noted by Hansen et al. (2020), *"there is a need for more detailed studies, including case studies, which can provide more information about how financial instruments work in practice"* (p. 35).

3.1 Blended Finance Literature

Blended finance has gained significant traction among policymakers, practitioners, and scholars as a potential response to the growing development financing gaps (Sharma et al., 2023). Broadly defined as *"the strategic use of development finance for the mobilisation of additional finance towards sustainable development in developing countries"* (OECD, 2018, cited in Winckler-Andersen et al., 2021, p. 6), it was presented following the 2015 Addis Ababa Action Agenda as a solution capable of simultaneously attracting private capital and generating development outcomes. Nonetheless, the evidence supporting these claims remains thin. The most systematic mapping effort identified only 33 relevant publications, most of them being grey literature rather than independent academic studies (Sánchez Torrente et al., 2020), and limited additional evidence on DGs impact has emerged since (EBRD, 2025).

Policy reports have most recently illuminated the limits of blended finance instruments. Private sector mobilisation has been way smaller than anticipated, with mobilised finance predominantly flowing to middle-income rather than lower-income countries (OECD, 2023). In response, policymakers have called for more catalytic instruments that maximise effect per unit of public expenditure (OECD, 2025a). Most recently, the updated OECD DAC guidance now explicitly requires donors to demonstrate both financial and development additionality for ODA eligibility (OECD, 2025b). This reflects a broader shift away from treating mobilisation alone as sufficient justification for concessional interventions in development (Sial & Chandrasekhar, 2024; Action Aid et al., 2026).

A growing strand of scholarship argues that the blended finance agenda represent a deeper reorientation of development finance around investor-friendly priorities rather than development needs (Bernards, 2024; Gabor, 2021). From this perspective, instruments like DGs risk privileging commercial market logic over development objectives. Concretely, this critique points to three limitations. First, leverage ratios measure the volume of private capital mobilised but say nothing about whether that capital reaches the most in-need or generates welfare improvements on the ground (Winckler-Andersen et al., 2021). Secondly, scholars have pointed to the social costs of debt-based instruments and raised concerns that these are rarely captured in standard evaluation frameworks (Aitken, 2013; Baylis et al., 2020). Finally, the concentration of blended finance in commercially attractive contexts means that the poorest and most fragile settings, where financing gaps are greatest, remain underserved (Action Aid et al., 2026). The implications of these critiques for the specific case of DGs are returned to in section 7.1.

3.2 The Impact of Development Guarantees

A few studies have examined the ability of DGs to create meaningful impact in developing countries (Boschi et al., 2014; Green, 2003; Gurmessa et al., 2021; Soumaré, 2021). The literature identifies three benefits associated with the instrument: limited fiscal costs, mobilisation of private capital, and additionality as the ultimate development effect (Barder and Talbot, 2015; Garbacz et al., 2021; Lee et al., 2018). However, assessing DG impact poses methodological challenges that go beyond those associated with more direct instruments (Hansen et al., 2020). Unlike grants, which involve direct transfers to which outputs can be traced, DGs operate through a complex causal chain: they modify the risk exposure of financial intermediaries, who may then alter their lending behaviour in ways that reach intended beneficiaries. Gurmessa et al. (2022) identify three attribution challenges specific to guarantees: 1) whether lending behaviour changed as a direct result of the guarantee; 2) whether those changes can be traced to firm-level outcomes; and 3) whether the DG's contribution can be isolated from co-deployed instruments such as TA. The literature suggests that current evidence on whether DGs truly cause additional investment is weak and inconclusive (Barder and Talbot, 2015; Gurmessa et al., 2022).

Several disaggregations of additionality can be found in the literature. This thesis focuses on two dimensions of additionality as defined by Winckler-Andersen et al. (2021). 1) Financial additionality, which concerns whether DGs mobilise private capital or expand access to finance

and 2) Development additionality, which concerns whether that finance generates measurable socio-economic outcomes such as employment, inclusion, or economic growth. Indeed, these definitions are much in accordance with the newly revised OECD Private Sector Instruments Reporting Directive (OECD, 2024).

3.2.1 Financial additionality: mobilisation or substitution?

In the context of this thesis, financial additionality asks whether the DG was the determining factor in a lending decision i.e. whether credit was extended because the DG was in place and would not have been extended in its absence (Gillenwater, 2012). Winckler-Andersen et al. (2021) argue additionality must be assessed both ex ante and ex post, and caution that without a credible baseline, additionality claims may be overstated. A recurring concern in the literature is whether financial institutions would have extended credit regardless thereby simply redistributing risk from the lender to the guarantor (Barder and Talbot, 2015; Sial & Chandrasekhar, 2021). This concern has been conceptualised by Vogel and Adams (1997) as substitution effects in which lenders improve terms for existing pool of borrowers instead of using the DG to reach new segments. This of course has direct implications for the financial additionality of DGs.

The empirical evidence on financial additionality remains mixed and context specific. Several case-specific evaluations of DG schemes show positive results, including Gurmessa et al. (2022), who identify increased lending to targeted groups under Ethiopian LPGs, and Taguchi and Yasumura (2021), who find that DGs correlate with increased private sector commitments. However, a cross-country study on LPGs finds limited additionality in new loans and find that few borrowers graduate to non-guaranteed lending (IFAD, 2014). Indeed, there seems to be a common concern in the literature that DGs often expand credit volumes without fundamentally altering financing conditions such as interest rates or collateral requirements which raises questions about DGs financial additionality in practice.

3.2.2 Development additionality and development outcomes

Development additionality asks whether DGs generate socio-economic outcomes that would not otherwise have occurred (Winckler-Andersen et al., 2021). It is conceptually distinct from financial additionality as increased capital flows do not necessarily translate into developmental outcomes (ibid.). Across the literature, scholars have argued that financial additionality is a necessary but insufficient condition for development impact, and that the two

must be assessed separately rather than assumed to follow from one another (Carter et al., 2018; Garbacz et al., 2021; IFAD, 2014). Hence, DGs must be assessed not only in terms of expanded lending, but also in terms of employment, inclusion of underserved groups, and firm-level growth.

Empirical evidence on development additionality is also limited in the literature. Winckler-Andersen et al. (2021) show that a Colombian DG scheme increased firm-level employment but had limited productivity effects, which may suggest that loans were used for working capital rather than long term investments. Likewise, a study on LPGs in Malawi showed improved MSME access to finance but that the most underserved segments remained unreached (Banda-Nyirenda et al., 2024). More positive findings come from Soumaré (2022), who identifies evidence that LPGs can contribute to economic growth by alleviating credit rationing, and an evaluation study from SIDA, who document positive employment effects in Guatemala and Bosnia (Carnegie Consult, 2016). Nonetheless, the literature remains clear that development additionality cannot be assumed, and that careful case-based analysis is best suited to guide evaluations of DGs (Hansen et al., 2020).

3.2.3 Measuring the impact of development guarantees

Moreover, the literature suggests that measuring additionality remains an unresolved challenge (Habbel et al., 2021; Carter et al., 2018). While financial additionality can be approximated through econometric analysis, development additionality requires tracing causal chains from financing to firm behaviour to measurable outcomes, which has proven difficult in less data-driven contexts (Hansen et al., 2020; Gurmessa et al., 2019).

While mobilisation metrics are comparatively well established (OECD, 2023), the measurement of development additionality remains less standardised and more context-dependent (Hansen et al., 2020). In this context, the IDB Office of Evaluation and Oversight (Pires et al., 2022) has raised concerns about the absence of a DG-specific measurement tool. Indeed, the most comprehensive framework - 16 principles for credit DGs developed by ILO, World Bank and FIRST Initiative (ILO, 2015) - is primarily oriented toward institutional governance rather than borrower-level development additionality. IDBs concerns are echoed by other scholars such as Carter et al. (2018) who highlight the “elusive quest for additionality,” and Barder and Talbot (2015) who underscore the necessity of control trials if DG-issuing institutions are to effectively evaluate the development impact of their DGs.

Taken together, the literature reveals a fragmented evaluation landscape where both aspects of additionality remain under-specified with no standard reporting methodology, which raises concerns that mobilisation may be used as a proxy for development impact (Sial &Chandrasekhar, 2024).

3.3 Theoretical Perspectives and Gaps in the Guarantee Literature

Despite rapid expansion of DGs in development finance, theoretical engagement with how and why they work remains limited. Much of the literature is policy-oriented and evaluation-driven, focused on mobilisation volumes and portfolio performance rather than on the conditions that determine whether DGs generate their intended effects (Hansen et al., 2020). Two gaps are particularly significant for this thesis. First, whether the market failures DGs are designed to correct are actually present in developing country credit markets (Besley, 1994; Brown and Lee, 2017). Secondly, the field remains largely under-theorised with little to no research examining guarantees beyond neoliberal market logics. This thesis responds to both gaps by combining a theoretical framework drawn from NIE and SAT - supplemented by reflections from CPE - with a case-based analysis of AGF's LPG schemes in the Kenyan MSME credit market.

4. Theory and Analytical Framework

The analysis of DGs in this thesis is organised around three theoretical perspectives, each assigned a distinct analytical task. New Institutional Economics (NIE) provides the theoretical rationale for why DGs are deployed in credit markets that fail to meet MSME financing demands. Strategic Alliance Theory (SAT) provides the framework for examining whether the relational conditions between AGF and its PFIs are conducive to generating intended effects.

However, what neither theory addresses are whether the broader structural conditions within which DGs operate are conducive to development impact in the first place, or whether the growing reliance on market-based instruments reflects a deeper reorientation of development finance around investor-friendly priorities rather than developmental needs. This is the analytical space that the concept of financialization, drawn from Critical Political Economy (CPE), occupies in this thesis.

4.1 New Institutional Economics: The Rationale for Guarantees in Development

NIE emerged from dissatisfaction with explanations of economic performance that rely solely on prices and markets (Heidrich, 2021). While anchored in core neoclassical assumptions, NIE challenges the argument that markets operate under perfect information and costless contracting, questioning whether markets can reliably achieve efficient outcomes without institutional support (Stiglitz & Weiss, 1981). From an NIE perspective, economic outcomes are shaped not only by markets but by institutions. Institutions are defined by North (1990, p. 3) as *"the humanly devised constraints that shape human interaction"* and encompass both the formal and informal rules that structure incentives, reduce uncertainty, and enable economic exchange. Acemoglu and Robinson (2012) further categorise institutions along a spectrum from inclusive to extractive. Inclusive institutions promote economic prosperity by securing broad-based property rights and providing broad economic opportunities, while extractive institutions systematically exclude certain actors from participation. In the context of MSME finance, financial systems may function as extractive institutions when they exclude smaller firms from credit access, thereby providing a clear rationale for DGs as a corrective institutional mechanism.

4.1.1 Central concepts: credit market failures and DG responses

NIE is particularly relevant in credit markets, where three interconnected frictions generate systematic barriers to MSME finance.

The first friction is **transaction costs**, which can be defined as the costs of searching for information, negotiating contracts, monitoring performance, and enforcing agreements (Coase, 1937; Williamson, 1985). In credit markets, screening borrowers requires costly information gathering, monitoring loan use is burdensome, and enforcing repayment is uncertain. This is particularly true where law enforcement and financial reporting standards are weak - a context characterized by exclusive institutions (Acemoglu & Robinson, 2012). DGs are argued to partially compensate for these costs by reallocating risk and modify lender incentives (Cusmano, 2018).

The second friction is **information asymmetry** and **credit rationing**. Stiglitz and Weiss (1981) demonstrate that credit markets may fail to allocate resources efficiently even in competitive settings. They argue that as interest rates rise, adverse selection attracts riskier borrowers while moral hazard incentivises riskier behaviour, thereby reducing expected lender returns. Under such conditions, banks may prefer to limit [ration] credit rather than raising interest rates, which may exclude certain segments of borrowers (Besley, 1994). By reducing lenders' expected losses in the event of default, DGs may enable banks to extend credit to borrowers they would otherwise exclude (Boschi et al., 2014).

The third friction is weak property rights. Within NIE, enforceable property rights are considered a prerequisite for well-functioning credit markets, as they enable borrowers to pledge assets as collateral for obtaining loans (Acemoglu and Robinson, 2012). Yet in many developing country contexts, property rights are difficult to enforce (Besley, 1994; Manara and Pani, 2023). Meanwhile, many MSMEs lack the pledgeable assets that banks require, creating a barrier to credit that is then further compounded by high collateral rates combined with weak property rights. Here, the argument is that DGs can then partially substitute for collateral by providing lenders with an alternative form of security, thereby lowering the collateral needed for the individual borrower (Cusmano, 2018).

4.1.2 The limits of NIE: from design to relational dynamics

NIE provides a theory-based rationale for DGs as instruments that correct credit market failures. However, its analytical focus on design carries an implicit assumption: if collateral requirements are lowered, formal access to credit will be granted to those that could not access it under higher requirements. This assumption is complicated by a number of factors including moral hazard (San-Jose et al., 2022). If PFIs know that a portion of potential losses will be

covered by a guarantor, they may reduce the consistency in borrower screening, which ultimately undermines the additionality of the instrument (Hansen et al., 2020). As Nabli and Nugent (1989) caution, institutional design logic cannot be assumed to translate automatically into the behavioural outcomes it presumes. It is precisely this gap between DG design and PFI behaviour that SAT addresses.

4.2 Strategic Alliance Theory: The Relationship Dynamics between AGF and PFIs

SAT emerged from the field of international business strategy as a framework for analysing inter-organisational partnerships, how and why they form, how they are governed, and under what conditions they succeed or fail (Parkhe, 1993; Kale and Singh, 2009). SAT is increasingly relevant in blended finance contexts, where it remains contested whether private financial institutions are genuinely motivated to maximise development outcomes rather than commercial returns. As Bernards (2024, p. 94) notes, it is far from self-evident that private finance institutions *"are actually interested in maximising their opportunities to invest in development projects"*. SAT provides the theoretical framework necessary to avoid assuming that AGF and its PFIs share a common development intent. An assumption that, if incorrect, would fundamentally alter conclusions around the conditions for DGs to generate additionality.

4.2.1 Central concepts: asymmetric dependence, goal divergence and relational governance

The most central concept from SAT for this analysis is **asymmetric dependence** (Casciaro and Piskorski, 2005; Inkpen and Beamish, 1997). In any alliance, partners are rarely equally dependent on one another (Parkhe, 1993). The less dependent partner has more bargaining power and less incentive to comply fully with shared norms, because the cost of non-compliance is low. Inkpen and Beamish (1997) further demonstrate that as one partner's dependency decreases, the likelihood of instability increases. Not through outright non-compliance but through passive drift, where the less dependent partner continues to formally participate while operationally reverting to its own preferred practices (ibid.). In the DG context, if the guaranteed portfolio is insufficiently significant to the PFI to justify adapting internal processes, the alliance may persist in formal terms while failing to generate the behavioural change at the bank on which its development impact depends.

A related concept is **goal divergence** defined as the extent to which partners pursue different objectives within a shared arrangement (Doz and Hamel, 1998). Goal divergence becomes analytically significant when one partner's objectives can be achieved without fulfilling the obligations that serve the other partner's goals. This dynamic may be reinforced by what

institutional theory describes as decoupling (Meyer and Rowan, 1977), which is defined as the divergence between formal adoption of a practice and substantive behavioural change. In the context of DGs, this would be the case if financial institutions signal compliance to the guarantor while operationally continue business-as-usual lending to maximize their own interests.

In this regard, SAT distinguishes between **contractual governance** (formal rules, reporting requirements, and penalty mechanisms) and **relational governance** (the norms, trust, and shared understandings) that shape behaviour beyond formal obligations (Kale and Singh, 2009). Effective alliances typically combine both, with relational governance compensating for the limitations of contractual mechanisms alone. Where only formal contractual mechanisms are in place, the risk of passive drift increases. In the context of DGs, this suggests that it is the quality of the guarantor-PFI relationship, rather than the formal terms of the DG agreement, that determines whether the instrument generates its intended developmental effects.

4.2.2 The limitations of SAT and economic theory

While SAT and NIE together provide a theoretically grounded framework for analysing both the rationale for DGs and the relational conditions that determine whether they generate additionality, they operate primarily at the level of market mechanisms and inter-organisational dynamics. Both theories have an explanatory focus on the incentive structures that govern credit markets - and the conditions under which these generate or undermine additionality. This makes both theories well equipped to explain why DGs are deployed and whether the conditions for their effectiveness are present, but they are less equipped to address the broader structural conditions within which both credit markets and DG partnerships are embedded. (Sial & Chandrasekhar, 2024; Bernards, 2024).

4.3 Critical Political Economy: Positioning DGs within Financialization critique

Both NIE and SAT share a common limitation: they operate within the logic of market systems rather than questioning it. Neither theory asks whether market-based instruments can deliver genuine development transformation, or whose interests the growing reliance on such instruments ultimately serves. Drawing on CPE, this thesis employs the concept of **financialization** as a structural lens to raise these questions. Epstein (2005, p. 3) defines financialization as *"the increasing role of financial motives, financial markets, financial actors and financial institutions in the operation of the domestic and international economies".*

Drawing on Mader et al. (2019), this process operates across three interconnected levels relevant to this thesis.

At the **macro level**, financialization describes broad systemic changes in how economies operate, including how financial logics come to shape economic policies and global economic structures (Mader et al., 2019). In the context of development finance, this is visible in the reorientation of ODA away from traditional funding models and toward leveraging private capital flows - of which blended finance instruments like DGs are a direct expression (Van Waeyenberge, 2015; Bernards, 2024). At the **meso level**, financialization describes how organisations increasingly adopt financial instruments and metrics as the dominant framework for evaluating performance and strategy (Mader et al., 2019). In the context of development institutions, this is reflected in how donors increasingly assess interventions around mobilisation volumes rather than development outcomes (Global Focus, 2026). At the **micro level**, financialization describes the penetration of financial rationales into the everyday lives of individuals through credit, debt, and insurance (Mader et al., 2019). In the context of LPGs, this raises the question of whether previously excluded MSME borrowers who are incorporated into formal financial circuits are served on terms structured around developmental need or around the logic of markets (Aitken, 2013). Drawing on Lazzarato (2012), debt is understood not merely as a financial transaction but as a power relation in which the borrower is positioned as accountable to the creditor and to the financial logic within which that relationship is embedded. This dynamic is further sharpened by the concept of international financial subordination (IFS), which suggests that geopolitical domination is expressed through money and finance with deep historical roots in colonial legacies and the unequal integration of developing economies into global markets (Alami et al., 2023).

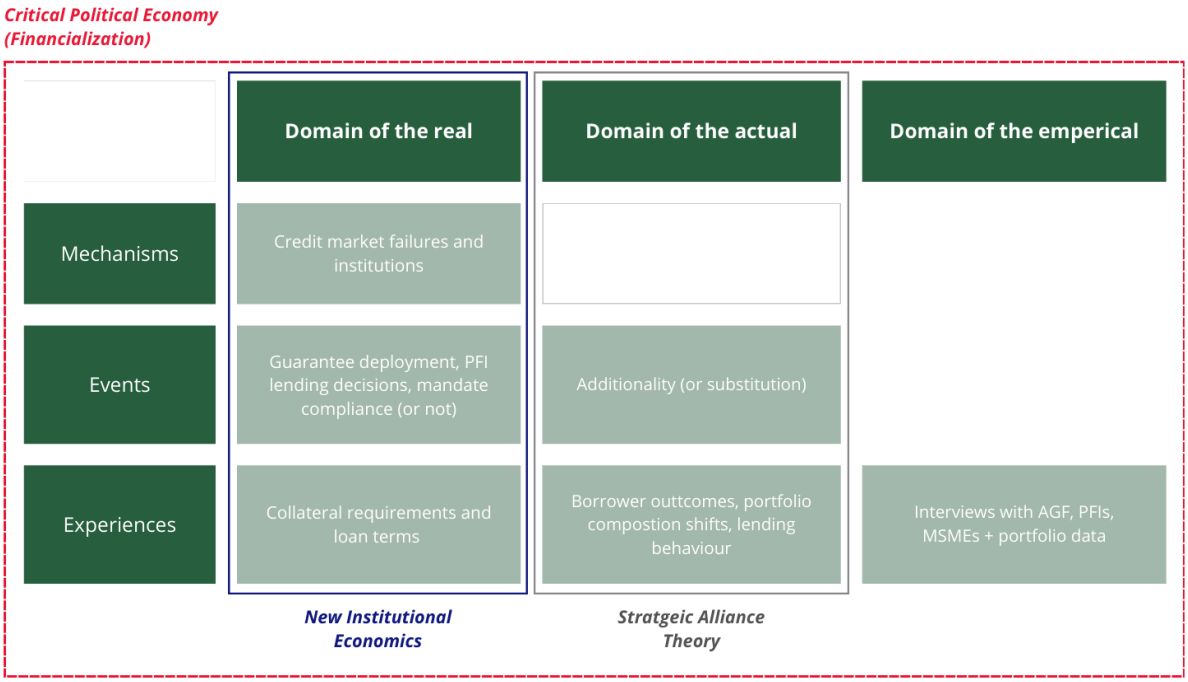
In the context of this thesis, financialization is understood not as the deliberate strategy of institutions or development actors, but as a tendency that development institutions are increasingly albeit unconsciously adopting. The key analytical implication is that when development objectives are pursued through instruments embedded in financial market logic, the criteria for success tend to shift from what is developmentally needed toward what is financially viable. The CPE lens is applied at the close of each analytical sub-section in Chapter 6, and the threads are drawn together in the discussion in section 7.1.

5. Methodology

5.1 Research Philosophy: Critical Realism

This thesis is grounded in a critical realist ontology, which holds that social reality consists of underlying structures and mechanisms that generate observable events and outcomes, but which cannot be directly observed and must be accessed through theoretical interpretation and empirical analysis (Bhaskar, 2018). Critical realism distinguishes between three domains of reality: 1) the real - the domain of structures and mechanisms that have causal powers regardless of whether they are activated; 2) the actual - the domain of events that occur when mechanisms are triggered; and 3) the empirical - the domain of observable experiences and outcomes (Knudsen, 2023.). This ontological position is particularly relevant for the present study, as it allows the analysis to move beyond observable lending outcomes to examine the underlying mechanisms that produce them (see figure 4)

Figure 4: Theoretical and ontological framework



Source: Adapted from Knudsen, 2013 (p. 12)

Critical realism is particularly well suited to the theoretical architecture of this thesis, which combines NIE, SAT, and CPE within a single coherent analytical design, avoiding both the determinism of positivist theories and the subjectivism of interpretivist approaches (Bhaskar, 2008).

5.2 Research Design: Qualitative Case Study

The empirical analysis is based on a qualitative case study of AGF's LPG scheme, with the unit of analysis being the scheme itself. More specifically, its design, its relational dynamics, and the conditions under which it generates additionality in the Kenyan MSME credit market. The case study design is appropriate for several reasons; First, the RQ seeks to provide explanatory and case-based knowledge rather than frequencies or distributions, making qualitative inquiry more appropriate than large-N quantitative approaches (Yin, 2018). Second, the case study allows the thesis to examine how DGs operate within a specific institutional context, providing a level of depth that broader comparative studies cannot provide (Deeg, 2007).

The selection of the AGF-Kenya case is a motivated choice rather than based on random selection. Kenya represents one of the more developed financial markets in SSA, with a relatively diversified ecosystem of financial institutions and a significant concentration of AGF PFIs. The persistence of MSME financing constraints, despite financial sector development makes, makes it a critical case for examining whether DGs can shift inflated perceived risk in the right direction.

5.3 Data Collection

This study employs a multi-source data collection in which semi-structured interviews function as the primary empirical material which is then supplemented by portfolio-level data. This approach reflects Bryman's (2016a) argument that qualitative research benefits from the use of multiple data sources to strengthen analytical depth and credibility.

5.3.1 Semi-structured interviews

The primary empirical material consists of eleven semi-structured interviews with actors involved in or affected by the AGF LPG scheme. Interviews were selected as the primary data collection method because the mechanisms this thesis seeks to examine - credit market frictions, PFI lending behaviour, and the relational dynamics of the AGF-PFI partnership - are not directly observable through quantitative data alone. Access to the institutional logics, experiences, and decision-making processes of the actors involved is necessary to understand how and why the DG generates or fails to generate additionality in practice (Hammett et al., 2015; Bryman, 2016a). The semi-structured format allows for a partially predetermined set of questions while retaining flexibility to follow up on emergent themes (Bryman, 2016c).

Participants were selected through a combination of purposive and snowball sampling (Bryman, 2016b). Initial contacts were identified purposively based on their institutional role within the AGF LPG scheme, ensuring perspectives were captured from across the full causal chain through which DGs operate. Subsequent contacts were identified through snowball sampling, as initial interviewees referred the researcher to additional relevant actors. The theoretical framework directly informed the sampling strategy: NIE concepts of credit market failures pointed toward PFI and MSME perspectives, while the SAT-informed focus on the AGF-PFI relational dynamic pointed toward AGF management and expert informants. An overview of the interviewed parties can be found below (Table 1).

Table 1: Data Sources

	Sources	Use of source
Qualitative data sources		
Interviews		
AGF representatives	AGF management (AGF I)	Primary
	AGF bank officer (AGF II)	
	AGF board member (AGF IIV)	
PFI representatives	PFI I	Primary
	PFI II	
MSMEs that obtained financing through AGF PFIs	MSME I	Primary
	MSME II	
Experts on DG instruments	Danish DG expert (Expert I)	Primary
	Danish DG expert (Expert II)	
	Professor I (Expert IIV)	
	Professor II (Expert IV)	
Relevant documents		
AGF annual report	3 (2022-2024)	Secondary
Programme Documents – Danish DGF	2 internal IFDK documents (pilot + permanent)	Secondary
Quantitative data sources		
AGF generated data[1]	1 internal AGF excel report	Secondary
World Bank data on Lending Interest Rates (%)[2]	indicator/FR.INR.LEND	Secondary
Trading Economics data on lending interest rates (%)	Country list on registered lending rate	Secondary
Bloomberg data on lending interest rates (%)	Indexes included [COUNTRY CODE]BANK Index and ILRN amongst others	Secondary
World Bank data on Defaulted Loans to Total Gross Loans (%)	indicator/FB.AST.NPER.ZS	Secondary
World Bank data on Domestic credit to private sector (% of GDP) against GDP	Indicator/FS.AST.PRVT.GD	Secondary

[1] AGF provided data includes data on their entire active DG portfolio (updated 31/12/2024). The original data set included different types of DGs, but data used for this thesis has been disaggregated to only loan disbursed through LPGs between 2016-2024 (totalling 23,583). An overview of the data with different disaggregation's can be found in appendix 3.

[2] World Bank data was used as the primary data source for lending interest rates. Where country specific data wasn't available, Trading Economics or Bloomberg data sources were used as substitutes.

Interviews were conducted iteratively, with initial interviews with AGF management and experts providing contextual grounding that shaped subsequent PFI and MSME interview guides. Interviews were conducted through a combination of in-person meetings and online calls, reflecting the geographical distribution of participants across Kenya and Denmark. Most interviews with AGF, PFIs and affiliated MSMEs were done in Nairobi, Kenya. All interviews were recorded with informed consent and subsequently transcribed. Information that can be used to identify interviewees is removed from quoted material where necessary to protect confidentiality.

5.3.2 Documentary and portfolio data

In addition to interview material, the study draws on documents provided by AGF, the Danish MFA, and IFDK, as well as portfolio-level data from AGF. AGF annual reports and internal portfolio data provide information on AGF-LPGs (see appendix 3). For the non-DG backed loan book, we have relied on external data sources for comparison (see Table 1). Across external data, weighted averages were used, where each country is weighted according to its share of AGF's active portfolio as reported in AGF's 2024 annual report (see appendix 3).

It should be noted that definitional equivalence across sources cannot be fully guaranteed, and this comparison provides only an indicative quantitative basis for triangulating the qualitative findings in this thesis. Loan-level data on the non-guaranteed portions of individual PFI loan books was not obtainable, as PFIs were unwilling or unable to share this. A more rigorous econometric assessment would require access to both ex ante and ex post borrower profiles across guaranteed and non-guaranteed portfolios, which was not obtainable. As Bryman (2016d) notes, documentary data in case study research serves to triangulate qualitative accounts rather than replace them, and it is in this spirit that the quantitative material is used throughout this thesis.

5.4 Analytical Approach

The empirical material is analysed through theory-informed thematic analysis, combining deductive codes derived from NIE, SAT, and financialization theory with inductive codes where interview material raises themes not anticipated by theory (see appendix 1). This reflects the critical realist position that empirical material may reveal mechanisms beyond those initially theorised (Bhaskar, 1978). Prior to coding, all transcripts were read in full to develop familiarity with the material. Codes were then applied systematically and refined iteratively, with related codes grouped into broader themes using Nvivo.

The coding scheme is structured around four analytical dimensions. The first, informed by NIE, focuses on transaction costs, information asymmetries, collateral constraints, and credit rationing as experienced by lenders and borrowers. The second, informed by SAT, focuses on the AGF-PFI relational dynamics - including portfolio significance, compliance monitoring, and evidence of goal divergence or passive drift. The third, informed by CPE and financialization theory, examines the broader political economy implications of the findings, including whether guarantee design reflects intermediary interests as much as borrower needs. The fourth is a cross-cutting additionality dimension capturing reference to new borrowers reached, substitution effects, employment, business growth, and credit graduation regardless of which theoretical framework it most directly relates to. Validity of findings is strengthened through triangulation across interview accounts, portfolio-level data, and external data sources (Bryman, 2016a).

5.5 Research Quality, Trustworthiness and Ethical Considerations

Producing credible and trustworthy findings requires both methodological rigour and transparent acknowledgement of the study's constraints (Bryman, 2016a). The trustworthiness of this study is assessed across four dimensions (Lincoln & Guba, 1985). Credibility is strengthened through multi-source triangulation and respondent validation, whereby interviewees were invited to review quoted material for accuracy prior to submission. Transferability and dependability are addressed through detailed documentation of the methodological approach, including the coding scheme in Appendix 1 and thick descriptions of all analytical stages (Tracy, 2010). Confirmability is partially constrained by several limitations: full anonymisation limits readers' ability to trace individual accounts; English was not the first language of most interviewees, introducing a risk that nuance was occasionally lost and AGF portfolio data was obtained through personnel aware of the research agenda and may reflect institutional framing. These constraints are mitigated by transparency in the presentation of findings and are discussed further in section 7.2, where we also reflect on the researcher's positionality.

All participants provided informed consent prior to interview, were informed of their right to withdraw, and were guaranteed anonymity in the presentation of findings. The researcher's professional affiliation with IFDK represents a significant positionality consideration that shapes both access and potential confirmation bias. Mitigation strategies and a fuller reflection on the implications of this positionality are also discussed in section 7.2.

6. Analysis

The forthcoming analysis is structured in four interconnected parts, each corresponding to a distinct analytical task derived from the RQ:

Overall RQ: How and under what conditions does AGF's guarantee scheme generate additionality for Kenyan MSMEs, and what are the implications for guarantees as instruments in Danish development finance?

1) *Are the market failure conditions that theoretically justify LPGs empirically present in the Kenyan MSME credit market? (Section 6.1 using NIE)*
2) *How does AGF's LPG scheme translate into financial and development additionality in practice? (Section 6.2)*
3) *How does the AGF-PFI relationship impact LPGs' ability to generate additionality? (Section 6.3 using SAT)*
4) *What do the findings reveal about the design conditions necessary for guarantees to function as effective instruments within Danish development finance? (Section 6.4)*

It is important to note that this thesis works from the premise that access to credit can enable development outcomes, which is the logic on which DGs as instruments are built. A financialization lens is applied briefly at the close of each analytical section to reflect on what this premise leaves unexamined. These reflections are not intended to refute the primary findings but to remain honest what is not covered in the thesis at hand. These reflections are drawn together in the discussion in section 7.1 as we examine the limitations of the study at hand.

6.1 Examining the NIE Rationale: Are Market Failures present and how do guarantees mitigate these?

This section examines whether the theoretical conditions justifying DGs are empirically present in the Kenyan MSME credit market. Drawing on NIE, as outlined in the theory section, the analysis identifies two interconnected market failures that make LPGs an appropriate instrument in Kenya. First, this section will examine information asymmetry and credit rationing, which together generate adverse selection that systematically excludes viable MSME borrowers (6.1.1). Following, we shall illuminate how the broader regulatory environment and weak property rights compound these barriers (6.1.2).

6.1.1 Information asymmetry, adverse selection and collateral-based exclusion

Systematic exclusion of MSME borrowers in the Kenyan credit market is generated by two mutually reinforcing market failures: information asymmetry and credit rationing. Information asymmetry refers to a situation in which lenders cannot adequately assess borrower creditworthiness due to an unequal distribution of information between the two parties (Stiglitz & Weiss, 1981). Credit rationing describes a situation in which lenders restrict loan supply to borrowers willing to pay higher interest rates, because they perceive them as too risky to lend to (ibid.). DGs are theoretically justified by their ability to correct both (Besley, 1994). In Kenya, the informational infrastructure necessary for lenders to assess MSME creditworthiness is structurally absent. The country lacks a formal credit registry (World Bank, 2026), and many MSMEs trade under personal names without formal business registration. This makes it close to impossible to properly assess business creditworthiness and suggests that information asymmetry is high in the Kenyan MSME credit market. PFI II captures the operational consequence:

"*most MSME applicants don't have financial documentation or history (...) so it was a very difficult segment to lend to***"** (PFI II)

As banks are often unable to distinguish between safe and risky borrowers at acceptable cost, they respond through adverse selection. Adverse selection is defined as the tendency of information asymmetry to generate outcomes in which entire categories of borrowers are excluded rather than individually assessed (Stiglitz & Weiss, 1981). This is where information asymmetry generates credit rationing: rather than conducting risk-adjusted assessments of individual firms and price the loans thereafter, banks restrict certain borrower segments instead. In Kenya, our interviewees collectively observe a tendency amongst banks to raise collateral levels above the value of the loan for certain borrower segments. One PFI representative (PFI I) informed us that collateral requirements frequently reach >150% of total loan value, thereby systematically excluding asset-poor but cash flow-generating businesses. Some banks even make blanket restrictions to the MSME borrower segment "*As a bank it was a policy that we didn't lend to that segment"* (PFI II).

The borrowers most affected are what an AGF board member describes as the *"missing middle"*(AGF IIV), firms too large for microfinance but too collateral poor for standard commercial lending. This is confirmed from both sides of the market: PFI I notes that several

excluded MSMEs had commercially viable proposals but insufficient collateral, while MSME I confirms the DG-backed loan represented *"our first time ever securing financing"* despite being able to demonstrate solid financial records. As a result of information asymmetry and credit rationing through high collateral requirements, the Kenyan MSME credit market seems to be characterised by adverse selection in which MSMEs become structurally excluded from accessing formal financing.

By absorbing part of the risk from a bank, a LPG makes the cost of uncertainty bearable enough that categorical exclusion is no longer the rational lender response (Besley, 1994). In simple terms, this means that LPGs can address the collateral barrier directly by lowering the collateral requirement for the MSME while simultaneously creating a bridging period during which MSMEs build the credit history that eventually makes them independently creditworthy. From a critical perspective, however, improving risk perception cannot transform the structural conditions producing exclusion in the first place. If Kenya's financial system has historically been organised around larger, more formalised economic actors, instruments like LPGs alone cannot address the underlying inequality between small and large capital owners (Alami, 2023) - a limitation we return to in section 7.1.

6.1.3 Regulatory environment and exclusive property rights

Regulatory requirements and weak property rights independently compound the collateral and information barriers identified above. Kenyan banks are not merely commercially risk-averse but also institutionally constrained. In Kenya, regulations require banks to lend against collateral, meaning high collateral requirements are a regulatory mandate rather than a bank preference (Karumba & Wafula, 2012). The LPG therefore operates not only as a collateral substitute but as a mechanism enabling banks to respond more inclusively to otherwise exclusive regulatory requirements, as one AGF representative confirms: *"the guarantee doesn't just help them lend more; it also frees up regulatory capital"* (AGF IIV)

Property rights infrastructure introduces a further layer of systemic exclusion. PFI I describe borrowers who own land but cannot pledge it as collateral because formal registration of legal ownership remains incomplete. This suggests that the barrier is not only asset poverty but also the institutional infrastructure surrounding asset ownership. Moreover, these challenges seem to be compounded by the unequal distribution of property rights along gender lines (Caswell et al., 2022). In Kenya, customary land tenure systems concentrate asset ownership in male

hands, thereby producing a structural exclusion that compounds the standard collateral barrier for women entrepreneurs (ibid.). PFI II confirms this pattern:

"*Women are trying to do business, but they cannot get financing because they do not have securities in their own names (…) it is either in the husband's name, the brother's name, or the father's name*" (PFI II)

Here, LPGs can create access to specific borrower segments, such as women-led businesses, through higher risk coverage ratio, thereby providing a solution to MSME credit constraints even for the most structurally excluded business owners. To summarize, we find that LPGs seem to be a viable response to enabling more inclusive lending practices despite operating in a context characterised by exclusive institutions.

6.1.4 Sub conclusion - NIE rationale empirically supported

The market failure conditions that theoretically justify LPGs have been shown to be empirically present in the Kenyan MSME credit market. They operate in mutually reinforcing ways: information asymmetry and credit rationing generate adverse selection that excludes viable but asset-poor borrowers, while regulatory mandates and weak property rights deepen these barriers. The AGF-LPG scheme provides a credible corrective mechanism for each. By substituting for missing collateral, creating a bridging period for MSMEs to build independent creditworthiness, and freeing up regulatory capital to enable more inclusive lending it directly mitigates the identified market failures. As a result, we argue that the NIE rationale for the instrument is both theoretically and empirically justified in the Kenyan context.

Nonetheless, it is worth noting, that confirming the NIE rationale means accepting its framing - one in which MSME exclusion appears as a correctable deviation from an otherwise functional credit market. The market failures documented here are not random institutional gaps but features commonly found in financial systems integrated into global markets on historically unequal terms (Alami et al., 2023). Whether DGs can meaningfully address conditions of this kind, or whether they require more fundamental structural change, is a question the NIE framework is not designed to answer and is therefore one we shall return to in section 7.1.

6.2 The development Effect of Loan Portfolio Guarantees

Having established that the market failure conditions justifying LPGs are empirically present in the Kenyan MSME credit market, this section examines the extent to which AGF's LPGs generate additionality in practice. As mentioned in the literature review, financial additionality is understood as the ability to unlock financial resources not available under standard market terms, and development additionality as the ability to create development impact that would not have occurred without the intervention (Winckler-Andersen et al., 2021). The section below covers both aspects of additionality by examining whether the LPGs unlocks credit for previously excluded borrowers, whether that credit translates into measurable development outcomes, while also illuminating whether the instrument can be deliberately designed to advance specific development objectives.

6.2.1 Financial additionality and improved loan terms

The AGF-LPG scheme generates financial additionality primarily by enabling access to formal credit for previously excluded MSME borrowers through collateral substitution. In practice, financial additionality can take two forms: the mobilisation of private capital not otherwise present, and the unlocking of credit for borrower segments not otherwise served (Gillenwater, 2012). This analysis focuses on the latter, as the mobilisation dimension is already well covered in existing literature. Indeed, one expert interviewee stated it quite clearly *"It does not make sense to mobilise private capital if it does not also lead to development results"* (Expert IV).

Recognising that a quantitative analysis of ex ante and ex post loan terms and borrower profiles would have been the optimal approach, data availability has not permitted this. Nonetheless, interview evidence from PFIs, consistently suggests that banks would not have extended credit to their MSME customer base without the LPG. PFI I states that since acquiring the facility they have lent to a great number of clients who *"could not access financial facilities without this guarantee"*, adding that *"probably 70-80% of this would have been affected by collateral requirements"*. PFI II independently confirms there are customer segments they *"definitely"* could not have reached without the LPG, providing triangulated supply-side evidence that the LPG enables access to previously excluded borrowers.

Both MSMEs interviewed confirm that the DG-backed loan represented their first time securing formal financing. This suggests that the LPG was not just used to cover PFI risk on existing borrowers but rather used to expand the PFI borrower pool to MSME profiles not previously part of their borrower portfolio. MSME II provides an explicit counterfactual:

"*because the company was still growing, still young, we didn't have much assets per se, so it would mean the company wouldn't be here today*" (MSME II)

Nonetheless, across interviewees it is evident that the LPGs enables access to finance for previously excluded groups through collateral substitution rather than pricing improvement. Portfolio level data from AGF suggests collateral requirements decrease by as much as 70-80 percentage points (median change = 52 percentage points) under the LPG while interest rates remain largely unchanged or even above market ranges (Table 2). The financial additionality generated is therefore best characterised as *access additionality* rather than *terms additionality*. By substituting for collateral, the LPG dismantles the adverse selection mechanism that previously excluded viable borrowers entirely, but without reducing the cost of credit.

Table 2: Interest rate and collateral rate comparison

	AGF portfolio		Regional average *(without DG)*		OECD economies
	Pre DG	Post DG	Own analysis	Open source	
Median interest rate	N/A	20.1%	17%	+20%	6.1%
Collateral requirement (% of loan value)	94%	42%	N/A	73-90%	N/A

Source: AGF portfolio data is based on median values covering all LPGs across Africa[3]. See appendix 3 for further disaggregation of data.

6.2.2 Development additionality and sustainability of effect

As mentioned earlier, development additionality refers to the ability of a given intervention to deliver development impact that would not have occurred without it (Winckler-Andersen et al., 2021). While attribution challenges make it difficult to isolate the LPG's contribution specifically (Gurmessa et al., 2022), the analysis provides qualitative case-based evidence of DGs development impact under the AGF programme.

[3] On regional average, the "own analysis" is based on data from World Bank, Trading Economics and Bloomberg and calculated using weighted average. Moreover, the regional average interest rates has been increased with 2 percentage points according to OECD report (OECD, 2026) on average spread from market interest rate to MSME interest rate. All weighted inputs are based on AGF portfolio shares across African regions (2016-2024). Values under "Open source" is based on averages calculated by Global Economy Data (2026), while "OECD economies" is based on data on developed economies is from OECD (2025c)

A common indicator of development impact in blended finance is job creation (Winckler-Andersen et al., 2021). According to AGF's annual report (AGF, 2025), its DGs have since inception created more than 0.5 million jobs in SSA across 44,000 MSMEs. In our data, both MSME interviewees report substantial firm-level employment growth. MSME I traces employment impact beyond the directly supported firm explaining that through a payment system for smallholder farmers in their supply chain, they were able to reliably pay out salaries that allowed suppliers to cover school fees and farm expenses up front. This suggest that indirect job-creation from AGFs LPGs is likely even higher than recorded in their annual report as current Monitoring and Evaluation (M&E) frameworks does not account for second-order effects. That being said, both indirect and direct causal attribution remains difficult to track under DGFs, as the IFDK expert acknowledges:

"*the causal chain from access to finance, to increased lending, to increased investment, to increased employment - it's quite difficult to track all the way down*" (Expert II)

Another common indicator of development results for blended finance instruments is business growth. Here, MSME II reports a fifteenfold increase in annual turnover, attributing this directly to the financing received through AGF. Moreover, both MSMEs describe trust-building effects with suppliers and buyers that multiply direct financial impact into broader market integration, and underline that their consistent repayment has built credit histories that will improve their ability to obtain future financing. Indeed, a critical question for development additionality is whether DG-backed borrowers are able to graduate to independent creditworthiness once the DG is withdrawn. The empirical data on this is mixed. As demonstrated in Table 3, 98.8% of AGF's guaranteed loan book finances working capital rather than fixed assets, meaning graduation through asset accumulation cannot be assumed at the AGF portfolio level.

Table 3: Loan purpose

	AGF portfolio	Includes
Working capital	98.8%	Stock supply, contract financing, equity release and purchasing of other goods
Fixed assets	1.2%	Purchase of vehicle, machinery or property acquisition, construction of buildings and other value-adding acquisitions

Source: Data is based on AGF portfolio data covering all LPGs across Africa. Subsets are based on researchers own interpretation of working capital versus fixed assets as loan purpose is not aggregated in original data (N=3341 different loan purpose entries).

Nonetheless, dependency on the DG for continued credit access is not the same as an absence of development additionality, since the employment, business growth, and market relationships already represent real development outcomes regardless of whether guaranteed lending continues. From a financialization perspective, it is worth noting that the metrics used to assess development additionality - employment creation and business growth - reflect a particular framing of development in which market participation are treated as a primary development outcome (Aitken, 2013). Measuring development additionality through business metrics alone may therefore leave important dimensions of borrower welfare unexamined - a reflection we shall return to in section 7.1.

6.2.3 Policy objectives in focus

The DGs can be designed to direct credit towards borrower segments facing compounding exclusion, representing a distinct dimension of development additionality. Within AGF, this operates through differential coverage ratios: general MSME lines receive 50% coverage while women-led and green businesses receive 70%. As such, AGF uses the coverage rate of the DG as a commercial incentive to make targeted segments more attractive to lend to. As established in section 6.1, women entrepreneurs face a structural property rights exclusion making standard collateral provision challenging regardless of business viability. It is exactly such kinds of compounded exclusion that the DG can be designed to address.

From the borrower side, MSME I confirms that this has worked in practice. By accessing finance under the AFAWA (Affirmative Finance Action for Women in Africa) programme, this women-led business, was able to obtain formal financing for the first time:

"I think the thing that drew me in personally was the AFAWA angle, because they support women-led businesses. I felt like this was designed for a business like ours" (MSME I)

This suggests that additionality is not only generated through the differential coverage ratio but through the signalling effect of a named programme, changing both lender and borrower behaviour simultaneously. The Danish MFA expert adds that differential coverage rates can indeed be used to advance certain policy priorities. In our conversations, they noted that a key advantage of the DGs is that they can be shaped to align with specific policy priorities "*whether that's a focus on women, youth, green, refugees, or a particular geographic area"* (Expert I). This demonstrates that the DG is not merely a market correction tool, but can actively translate

donor priorities into commercial bank behaviour without requiring direct public investment in targeted sectors.

It is worth noting, however, that pursuing policy objectives through commercial incentives means their realisation depends on whether those objectives can be made financially attractive to PFIs. As Mawdsley (2018, as cited in Bernards, 2024) observes, converting development outcomes into market incentives requires work shaped by the logic of what private capital finds attractive, a limitation we return to in section 7.1.

6.2.4 Sub conclusion - conditional levels of additionality

Taken together, our analysis suggests that AGF's LPG scheme does translate into both financial and development additionality in practice, but this additionality is conditional rather than automatic. The LPGs enable access to formal credit for previously excluded borrowers through risk/collateral coverage but generate *access additionality* rather than *terms additionality*. As such, we find that the LPGs remove the structural barrier to credit without changing its cost. This access translates into measurable development outcomes in employment creation and business growth, and the instrument can be deliberately designed to target borrower segments facing compounding exclusion. As such, the additionality potential is real, but as one expert interviewee notes, effectiveness is further dependent on

"*incentives being more closely linked to development additionality and impact, rather than being primarily tied to financial or intermediary indicators*" (Expert IIV)

From a financialization perspective, three questions remain unexamined. Firstly, whether access to high-cost credit constitutes genuine development benefit when borrowing terms remain unchanged. Second, whether employment and growth metrics adequately capture development effects. And finally, whether policy objectives embedded in commercial logics can indeed generate development outcomes.

6.3 The Conditions under which Guarantees Generate Additionality

Section 6.1 has demonstrated that the market failure conditions justifying DGs are empirically present in the Kenyan MSME credit market. Section 6.2 has shown that AGF's DGs does seem to generate both financial and development additionality, but that it should not be automatically assumed as a consequence of the DG intervention. In this regard, our interviewees pointed to the relational dynamics between AGF and PFIs as a critical determinant of whether additionality materialises in practice. It is this relational condition, and the governance mechanisms through which it operates, that this section examines through the lens of SAT.

6.3.1 Portfolio share and asymmetric independence

The dependence between AGF and its PFIs is fundamentally asymmetric, and this asymmetry has significant explanatory power over whether the LPG generates its intended development outcomes. According to SAT, actors within any alliance are rarely equally dependent on one another, which creates an asymmetry in the relationship that ultimately shape alliance outcomes (Parkhe, 1993). In the context of LPGs, AGF is critically dependent on PFIs to fulfil its core mandate, as one AGF expert confirms:

"AGF's main mission is to facilitate access to financing for MSMEs (...) but the PFIs need to utilise our guarantees to provide financing to MSMEs" (AGF I)

This suggests that without PFI deployment, the LPG becomes redundant. Meanwhile, the PFI, by contrast, can continue its core lending operations independently of AGF. A key indicator of this asymmetry is the share of the PFI's total loan book that is guaranteed. As Table 4 illustrates, the median guaranteed portfolio represents just 0.77% of total PFI lending volume, a finding confirmed qualitatively by the IFDK expert, who estimates the guaranteed portfolio represents *"probably below 1% of their total portfolio"*. From a SAT perspective, a partner representing less than 1% of total lending volume has limited structural leverage to shape institutional behaviour, as the cost of non-compliance is simply too low relative to the operational adjustments required to fully internalise the developmental mandate.

Table 4: Portfolio share

# of PFIs with LPGs	146 (total = 255)
Median loan book per PFI	USD 808.37 m
Median guaranteed loan book	USD 6.22m
Portfolio share	0.77%

Source: Data is based on AGF portfolio data covering all loan portfolio guarantees across Africa using calculations based on different subsets. Data on non-guaranteed loan books is retrieved externally.

This asymmetry is further compounded by a partial misalignment of objectives i.e. what SAT would coin as goal divergence. Our interviewees signal that AGF's primary objective is developmental whereas the PFI's primary objective is commercial. This suggests that portfolio share alone therefore cannot determine LPG effectiveness, as passive drift or decoupling from the PFI will remain a risk. What matters then is whether governance mechanisms are in place to ensure strategic alignment despite asymmetric dependence, which is the focus of the following sub-sections.

6.3.2 Mechanisms that counteract the asymmetric dependence hypothesis

We find that three mitigating mechanisms can partially compensate for the asymmetric dependence described above. The first and most fundamental operates through the financial architecture of the instrument itself. Under a proportional risk-sharing structure, the PFI retains meaningful exposure on every guaranteed loan, thereby ensuring that non-compliance carries a direct financial cost. One AGF representative confirms this structure *"makes substitution extremely difficult"* (AGF IIV). Claims data from the AGF portfolio support this (Table 5), illustrating that defaults across the AGF portfolio are substantially lower than the regional average on non-guaranteed lending. In essence, this suggests that moral hazard behaviour from PFI is relatively contained, as passive drift away from PFI alliance obligations would likely include less systemic borrower screening and thus a higher number of defaults.

Table 5: Non Performing Loans (NPLs)

	Face value NPL (USD m)	% of total loan book
AFAWA	5.8	1.3 %
Green loans	1.1	1.5 %
Gross book AGF	109.7	2.4 %
Regional Average	N/A	9.2 %

Source: Data is based on AGF portfolio data covering all LPGs across Africa using calculations based on different subsets. The regional average is based on World Bank Data weighted average of 29/44 AGF portfolio countries from 2017-2024.

Another mechanism concerns PFI-selection prior to DG deployment. One DG expert noted:

"you can't change the strategy of a bank with a guarantee. You need to find a bank that already has the right strategy (...) we can help them go faster and further, but we can't create strategic intent that isn't there" (Expert II)

This introduces a pre-entry dimension to the strategic alignment problem that conventional SAT framing does not capture. During the interviews, it was clear that different levels of institutional buy-in from the two PFIs was affecting their use of the LPGs. Despite operating under identical DG terms with similarly marginal guaranteed portfolios, PFI I demonstrated more institutional commitment and active deployment of the DG, while PFI II engages more transactionally. Instrument design alone cannot explain this difference, but pre-entry strategic alignment may be able to. Nonetheless, it is worth noting that PFIs who are strategically aligned prior to the alliance-building may already be extending credit to underserved borrowers, raising questions about additionality in itself.

A third governance mechanism is AGF's formal contractual governance structure, through which PFIs submit quarterly financial reports and annual sustainability reports on guaranteed portfolios. While AGF management describes this as an important accountability mechanism, the data reveals that *"AGF (...) has almost never rejected a claim or raised non-compliance concerns"* (AGF I). This suggests that formal contractual governance functions primarily as a reporting requirement rather than an active enforcement mechanism. This reinforces the finding that relational governance carries the primary weight of ensuring development compliance in the AGF-PFI relationship.

6.3.3 Capacity development as an enabler for sustainable impact

Most importantly, we find that technical assistance (TA) functions as the primary mechanism through which AGF pursues active behavioural change at the PFI level, beyond what coverage ratio, PFI selection and contractual governance can achieve. At AGF, TA corresponds on average to approximately 10% of the total financial engagement with a given PFI, with USD 1.8 million disbursed across 43 PFIs in 2024 (AGF, 2025). All DGs within AGF are as a starting point accompanied by TA, designed around a prior diagnostic assessment of each PFI's specific capacity gaps rather than as generic training.

The most direct connection between TA and strategic alignment concerns what one AGF representative identifies as the internal championing problem:

"*If the staff member who understands guarantees isn't the one talking to the business development team on the ground, the guarantee just doesn't get used. That's why capacity development is so important***"** (AGF II)

TA addresses this by building the internal human capital necessary for operational compliance regardless of portfolio size by creating awareness of the DG across loan officers. This can be argued to be a form of relational governance, through which AGF ensures that there is institutional buy-in.

TA also addresses the demand side of the credit market by preparing MSMEs to be credit-ready. Both AGF and PFIs confirms, and one interviewee stated that the TA component serves *"partly to train loan officers, and partly to ensure a pipeline of borrowers who come to the bank with proper business cases"* (AGF I). One important insight that could be taken up further in future research is the demand for localized TA. According to one expert interviewee TA *"only works properly if it is in-country and on-site"* (Expert IIV) suggesting that TA must be appropriately designed to the context in which it is implemented.

The findings therefore suggest that TA functions as an enabling condition rather than a supplementary component. As a result, we find that TA must be non-negotiable component of the DG intervention and further designed to serve the specific needs of both PFIs officers and intended borrower-beneficiaries while retaining the necessary level of relational compliance.

6.3.4 Sub conclusion - strategic alignment as a condition

Taken together, the analysis reveals that the AGF-PFI relationship significantly shapes LPGs' ability to generate additionality, with three conditions emerging as analytically important. First, proportional risk-sharing aligns PFI financial interests with portfolio quality through the instrument's own architecture. Second, pre-entry strategic alignment between AGF and the PFI determines the baseline commitment level from which all governance mechanisms must work. Third, TA functions as the primary relational mechanism through which AGF can enable behavioural change within PFIs. As such, because of asymmetric dependence between AGF and its PFIs, the conditions under which the DG is deployed ultimately determine whether it generates additionality.

From a financialization perspective, the mechanisms identified above work primarily by aligning commercial incentives with developmental objectives rather than subordinating commercial logic to developmental need. Moreover, the conditions that generate additionality in the AGF case are time-consuming, resource-intensive, and difficult to scale. Thereby risking TA to be treated as optional rather than essential. A concern we return to in section 7.1.

6.4 Overall conclusion and Implications for Danish Guarantee Schemes

Taken together, our analysis has demonstrated that AGF's LPG scheme does generate additionality for Kenyan MSMEs, but this additionality is conditional rather than automatic and dependent on a specific set of conditions that cannot be assumed to be in place. The market failure conditions justifying the instrument are empirically present and the LPGs is well-matched to their nature, confirming that the instrument is theoretically and empirically justified in the Kenyan context.

However, three qualifications are essential. First, we find that the LPGs generates *access additionality* rather than *terms additionality* - it removes the structural barrier to credit without changing its cost. Second, development additionality is real but contingent on PFI behaviour rather than automatic - a condition revealed by the asymmetric dependence between PFIs and AGF. Third, both forms of additionality depend on proportional risk sharing, pre-entry strategic alignment, and TA as an enabling rather than supplementary component. Development additionality cannot therefore be assumed to follow automatically from financial additionality, and the depth of development effects depends heavily on how strategically the PFI integrates the AGF mandate into its lending approach.

While the answers to sub-questions 1-3 are provided in sections 6.1.4, 6.2.4, and 6.3.4, the findings from the AGF-Kenya case directly address sub-question 4 by revealing three design implications for DGs to function as effective instruments within Danish development finance:

1) *Instrument design must reflect the specific nature of the market failure it is addressing*. The dominant market failure in the Kenyan context is collateral-based credit rationing rather than liquidity shortage or interest rate distortion. As one expert describes, the DG is *"extraordinarily capital-efficient compared to traditional aid"* (Expert II) precisely because it addresses risk constraints rather than liquidity gaps. However, this efficiency is only realised if the instrument is designed to the specific exclusion mechanisms present in the target market.
2) *Proportional risk sharing should be a non-negotiable design principle.* The findings confirm that proportional risk sharing between the guarantor and the PFI is one of the deepest governance mechanisms available, aligning PFI financial interests with portfolio quality through the instrument's own architecture. The differential coverage ratios applied within AGF, 50% for general MSME lines and 70-75% for women-led

and green businesses, illustrate how this principle can simultaneously target specific policy priorities.

3) *TA must be treated as a required component of the guarantee rather than a supplementary one.* Without targeted capacity building, PFI loan officers may lack the knowledge necessary to deploy the DG effectively, and MSMEs may lack the financial documentation required to meet minimum creditworthiness criteria. The DG and TA should therefore be treated as inseparable components of a single intervention applied in tandem.

Taken together, these three implications suggest that the DG is the correct instrument for the identified market failures, but that its ability to generate additionality is conditional. The AGF case demonstrates that additionality is achievable: creditworthy MSMEs accessing formal credit for the first time, measurable employment creation, and early graduation pathways toward independent creditworthiness. However, these outcomes depend on PFIs that actively integrate the DG into their lending strategy, loan officers who understand how to deploy it, and MSMEs that arrive with sufficient financial documentation. As one expert summarises: *"I think it's an incredible instrument (...) But the argument that you can use your ODA in a very cost-efficient way (...) is only strong if the conditions are right"* (Expert II).

7. Discussion

This discussion reflects on what our findings mean beyond the immediate empirical context. Reflecting on our more critical pointers throughout the analysis, section 7.1 examines what the study leaves unexamined by drawing on the financialization lens to ask what a more critically oriented inquiry would have looked like. Section 7.2 addresses limitations of the study at hand including researcher positionality and section 7.3 presents an agenda for future research inquiries.

7.1 Reflecting on the Study: Theoretical Limitations and a More Critical Perspective

Any empirical study is shaped by the analytical choices made before data is collected and this thesis is no exception. The primary analytical frameworks, NIE and SAT, take the instrument on its own terms, accepting that expanding access to formal credit within existing financial market structures can enable development outcomes.

Several more critical, yet substantive reflections have been left unexamined by the analysis. The first concerns the risk-return asymmetry embedded in DG instruments. LPGs have been critiqued for transferring risk from private institutions to public balance sheets while leaving returns with commercial institutions (Action Aid et al., 2026). This is precisely what CPE scholars mean when they describe the financialization of development as empowering the extractive operations of financial capital (Bernards, 2024). DGs reduce risk for private financial actors without requiring them to reduce returns.

This raises a fundamental question about whether the instrument serves development objectives or primarily subsidises commercial bank risk management (Barder and Talbot, 2015). The empirical findings of this thesis lend weight to this concern: with asymmetric dependence between AGF and PFIs, the commercial logic of PFIs risks redirecting DG interventions "*towards an investment finance structure rather than a development finance logic"(Expert IIV).* According to CPE, this is not a design failure that can be fixed through strategic alignment, but rather a structural tendency of deploying a development instrument within institutions whose primary orientation is return generation.

The second thread concerns the premise that access to formal credit constitutes development benefit. Throughout the analysis, the cost of credit under the DG was found to remain broadly unchanged. Drawing on Lazzarato (2012), debt is not simply a financial transaction but a power

relation in which the borrower is positioned as accountable to the creditor and to the financial logic of the exploitative market. Similarly, Aitken (2013) documents how the rapid expansion of financialised micro-credit between 2004 and 2010 generated widespread over-indebtedness among poor borrowers. This exploitative nature of debt was found to be a result of commercial pressures and investor returns taking precedence over development objectives (ibid.). While LPGs differ from microfinance in important ways, the underlying risk is similar: when commercial logic gains precedence over developmental intent, previously excluded borrowers may find themselves incorporated into financial circuits that generate debt obligations rather than economic opportunities. Whether access to high-cost credit on unchanged terms (what this thesis has coined as *access additionality* rather than *terms additionality*) constitutes real development benefit for previously excluded MSMEs is therefore a question the primary analysis is not designed to answer, but indeed one that future research could benefit from.

Furthermore, a more critically oriented study would have started from a different premise: not whether DGs are efficient within existing financial market structures, but whether those structures are themselves conducive to the kind of development transformation that DGs are meant to support. Such a study would have asked why financial exclusion is so pervasive across the MSME segment in Kenya, tracing their roots to the path dependent nature of African banking systems and the ongoing dynamics of IFS that continue to shape who can access formal credit today (Alami et al., 2023; Lazzarato, 2012). In addition, a more critically oriented approach would have likely asked whether the governance conditions this thesis identifies as necessary for additionality is likely to be prioritized when programmes scale toward mobilisation targets, or whether the structural pressures toward efficiency and volume tend to crowd such conditions out (Sial & Chandrasekhar, 2024). As one expert notes,

"Unless we rethink how we structure guarantees and partnerships, we won't see fundamentally different results" (Expert IIV)

While these critiques are not reflected in our interviews with AGF, PFIs nor MSMEs, several expert interviewees lend weight to above concerns. Indeed, the critiques above represent genuine research gaps that is beyond the scope of this thesis, but which may guide future research inquiries on DGs as development instruments. Nonetheless, what the AGF case does contribute to is a detailed account of the specific conditions under which additionality is

achievable - and a demonstration that even within existing financial market structures, the gap between what DGs can deliver and what they tend to deliver by default is significant. That gap is explained by asymmetric dependence and governance conditions that are demanding, resource-intensive, and structurally at odds with the scale logic of the blended finance agenda.

7.2 Other Research Limitations

Several methodological limitations must be acknowledged transparently as they shape what can and cannot be concluded from the findings presented in this thesis (Tracy, 2010). The most fundamental limitation concerns the lack of counterfactual empirical data. Establishing additionality requires knowing what would have happened in the absence of the DG - a counterfactual that has not been achievable in our qualitative case study. The same logic applies to the weight this thesis has placed on TA as an enabling condition for additionality. Because all PFIs within AGF receive both LPG(s) and TA simultaneously, it is impossible to isolate the effect of each component, and no valid control group exists. The analysis therefore documents contribution rather than attribution: the findings illuminate the mechanisms through which additionality is generated rather than establishing a precise causal chain between the instrument and observed outcomes (Bhattacharjee, 2017b). This constraint is not unique to this study. Winckler-Andersen et al. (2021) identify counterfactual construction as a fundamental challenge in development finance evaluation, and the qualitative case study design adopted here is precisely suited to examining mechanisms rather than estimating causal effects (Bhattacharjee, 2017b).

A related limitation concerns the MSME sample. As MSMEs were accessed through PFIs, they likely represent successful borrowers in terms of demonstrating additionality i.e. borrowers who did not have access to formal financing before, applied for the guarantee-backed loan, were approved, and are now actively repaying. In addition, our sample size of only 2 MSMEs constitute an important limitation. Nevertheless, the thesis does not claim to represent the full population of MSMEs in Kenya and acknowledge that above limitation is often a curse related to snowball sampling (Bhattacherjee, 2017). Indeed, MSME accounts were used to triangulate PFI and AGF claims rather than to make representative generalisations, and findings are therefore presented as indicative rather than conclusive throughout.

Moreover, the generalisability of findings is constrained by the case selection. Findings cannot necessarily be generalised to more fragile contexts, less developed financial systems, or DG

programmes lacking AGF's TA infrastructure. However, as noted by Tracy (2010), generalisability is rarely an appropriate quality criterion for qualitative research. More relevant is the resonance of findings, which refers to the extent to which the mechanisms identified can inform understanding in other contexts (ibid.). On this basis, the governance conditions identified as necessary for additionality are likely to apply with even greater force in less favourable contexts, making the findings a conservative rather than optimistic estimate of what is required for DGs to generate additionality.

Another important limitation of this thesis is researcher positionality. According to Haraway (1988), positionality refers to the recognition that knowledge is always generated from a specific, embodied, and socially situated perspective. This is an evident limitation given that the researcher is professionally employed by IFDK, which holds approximately 40% of shares in AGF and is projected to be the primary DG-issuing institution in Denmark (MFA, 2026). This affiliation shaped the study in several ways. While it provided privileged access to AGF data and related interviewees, that would otherwise have been difficult to obtain, it also introduced a significant risk of confirmation bias (Schumm, 2021). In this case, the author of this thesis likely has an unconscious preference to interpret findings in ways that affirm the developmental effectiveness of DGs given the researcher's professional stake in both.

It is worth noting here that across interviews, the author disclosed their IFDK affiliation while framing the study explicitly as independent academic research conducted in a student capacity. This was done to limit bias in interviewees responses, while also acknowledging that full non-disclosure would risk breaching informed consent (Bilgen et al., 2021). This middle-ground approach nonetheless carries its own limitations. It cannot be ruled out that some interviewees, particularly AGF or PFI representatives with an existing relationship to IFDK as a shareholder, adjusted their accounts upon learning of the affiliation. This risk is acknowledged as a constraint on the credibility of interviewee responses.

Several mitigation strategies have been employed to address this risk. The financialization lens reflected upon throughout the analysis explicitly incorporates critical perspectives that challenge rather than affirm the developmental mandate of development finance institutions and their instruments. As recommended by Tracy (2010), the thesis has prioritised transparency in the presentation of findings, including where evidence contradicts the expected positive narrative (i.e. lending interest rates). Moreover, triangulation with available quantitative data

ensures that conclusions are not drawn from any single actor's account, and the limitations section at hand acknowledges rather than undermine the most significant constraints on what can be concluded given the positionality of the author.

Nonetheless, these measures cannot eliminate positionality bias entirely (Tracy, 2010). The RQ framing, the theoretical frameworks selected, and the interpretive choices made throughout the analysis are inevitably shaped by the researcher's institutional position (Bilgen et al., 2021). What can be said is that a conscious effort has been made to generate findings that are ethically presented rather than institutionally convenient - and that the critical reflections embedded throughout the analysis represent a genuine attempt to hold DGs and their limitations in view rather than to generate an evaluation that solely serves the interests of DG-issuing institutions.

7.3 Future Research Agendas

The findings and limitations of this thesis point toward several directions for future research, spanning both methodological and empirical dimensions.

The most immediate methodological gap concerns causality. Future research should seek to address this through quantitative research inquiries - for instance, comparing MSME outcomes across PFIs with and without DG arrangements, or tracking borrower trajectories before and after DG deployment where data permits. A particularly valuable contribution would be a study that directly engages MSME applicants who were denied credit, allowing for a more rigorous assessment of the counterfactual and a fuller account of who the DGs do and do not reach.

A related empirical gap concerns the role of TA as a distinct component of the intervention. Because all PFIs studied in this thesis receive both a DG and TA simultaneously, it is impossible to isolate the contribution of each. A study that compares additionality outcomes across PFIs receiving DGs with and without TA support would provide much-needed evidence on whether TA is a conditional element for DG schemes to be truly additional.

Furthermore, the financialization lens applied throughout this thesis has flagged three structural questions that future research should take up more directly. First, whether financial exclusion mechanisms for MSMEs reflects structural features of how developing country financial systems have been historically positioned within global financial hierarchies (Simba et al., 2024). Secondly, and as already touched upon in the micro credit space by Aitken (2013), it

would be interesting to examine further whether access to credit through DGs incorporate borrowers into financial circuits that expose them to unsustainable debt obligations. Longitudinal studies tracking MSME welfare outcomes beyond the lifetime of the DG would be particularly valuable here. Finally, whether the broader trajectory of blended finance has shaped donor incentives and impact frameworks would be interesting to delve further into. Comparative studies across development programmes employing different kinds of instruments would shed important light on this question.

8. Conclusion

This thesis has demonstrated that development guarantees can generate additionality for Kenyan MSMEs, but only under conditions that cannot be assumed to be in place. Examining how and under what conditions AGF's guarantee scheme generate additionality for Kenyan MSMEs, and what this reveals for guarantees as instruments in Danish development finance, the analysis has advanced our empirical understanding of DGs as development instruments in a field that has long relied on evaluative reports generated by the very institutions deploying them.

The first principal finding is that the market failure conditions that theoretically justify DGs are empirically present in Kenya's MSME credit market. Collateral-based lending and information asymmetries create adverse selection that systematically exclude viable MSMEs from accessing formal finance, and AGF's LPG scheme addresses these frictions in ways that are consistent with the rationale for DG instruments. This finding matters because it confirms that the instrument is deployed in a context where it is appropriate, which has revealed itself as a precondition for additionality that cannot be taken for granted across all DG deployments.

The second and most central finding is that additionality is conditional rather than automatic. The analysis identifies four overarching conditions that determine whether a DG generates genuine development impact. First, the DG must be deployed in a context where the market failure it is designed to correct is both present and addressable through risk-sharing, rather than through alternative instruments better suited to the specific constraints of that market. Second, both financial and development additionality depend on whether PFIs internalise their developmental mandate and adjust lending behaviour accordingly rather than using the guarantee to de-risk existing borrowers. Where PFIs treat the DG as a risk management tool rather than a market expansion instrument, risk substitution rather than additionality is the likely outcome. Third, TA emerges as an important enabling condition for additionality, supporting PFIs in strengthening their capacity to serve underserved borrowers over time. Moreover, the findings suggest that the DG and TA components of AGF's scheme should not be seen as separate instruments but rather be applied in tandem. Fourth, strategic alignment between PFIs and the guarantor cannot be assumed. This has revealed an important finding that carries direct implications for future DGF designs. Specifically, it corroborates previous literature recommending partial rather than full risk coverage as a non-negotiable design

principle. Indeed, proportional risk-sharing is one of the few governance mechanisms capable of directly minimizing moral hazard behaviour from the PFI.

This relates to the third finding, which concerns the relational dynamics of the guarantor-PFI alliance. Applying SAT to this relationship reveals that asymmetric dependence create conditions in which moral hazard behaviour from the PFI may limit the development effects of the DG. Ensuring institutional buy-in and relational governance through for example TA is therefore essential to limit goal divergence and keep PFI behaviour aligned with developmental intent. These finding shifts attention from instrument design to instrument governance, suggesting that the conditions for additionality are as much relational as they are technical.

Taken together, these findings carry concrete implications for the design of Denmark's permanent DGF. Firstly, DG deployments should be preceded by rigorous market diagnostics to confirm that the DG is the most appropriate instrument for the specific context. Such diagnostics can also establish the ex-ante baseline against which additionality can later be assessed, ensuring that M&E frameworks are grounded in an empirically documented counterfactual from the outset. Secondly, DG agreements should include clear additionality conditions rather than relying on PFI goodwill. Thirdly, our findings suggest that TA should be treated as a core component of the facility rather than an optional add-on with dedicated funding. Finally, the alliance management and monitoring mechanisms that sustain PFI compliance over time should be treated as a deliberate design feature of any DGF rather than assumed to emerge organically.

Beyond Denmark, the findings of this thesis speak to bilateral donors more broadly who are considering LPGs as instruments in their development financing. Indeed, we do not intend to signal that LPGs (or other types of DGs for that matter) can substitute more traditional grant-based instruments. Furthermore, we want to assert that LPG deployment should not be driven solely by the pressure to mobilise private capital, but rather by their ability to act as temporary instruments to increase access to finance for underserved groups. The conditions identified in this thesis provide a practical framework for donors seeking to move beyond the assumption that DGs work and toward an evidence-based understanding of when and why they do.

This thesis has examined one institution in one market over one period. The mechanisms identified are analytically transferable (Tracy, 2010), but whether DGs are also effective

instruments in fragile contexts, less developed financial systems, or contexts lacking PFIs with AGF's institutional maturity remains an open question. More broadly, this thesis contributes to a field that has long relied on evaluative reports generated by the very institutions deploying DGs. By bringing together NIE, SAT, and a financialization lens within a single analytical framework, this thesis has demonstrated that the question of whether DGs work cannot be separated from the question of additionality. Moreover, as perfectly articulated by one expert interviewee

"*The potential of guarantees may not be overestimated, however, what is underestimated is simply how difficult it is to assess how guarantees work, where they work and under what conditions*" (Expert IV)

This thesis has attempted to shed light on the additionality of DGs and while our findings reveal that effects are conditional, they are not pessimistic: DGs are legitimate when deployed in contexts where the right market failures are present, where institutional relationships are actively governed, and where development impact is treated as the primary accountability standard rather than as a by-product of mobilisation. Whether the upcoming DKK 12 billion Danish DGF can sustain those conditions at scale remains the central question. As one expert interviewee cautions, precision about *"when and how an instrument is used matters more than enthusiasm for the instrument itself"*. The same applies to DGs, and this thesis has been an attempt to bring important knowledge into just that.

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9. Appendices

Appendix 1: Interview guides[4]

African Guarantee Fund	
Theme	**Questions**
Introduction	Could you briefly introduce your role at AGF and your involvement with guarantee operations in Kenya?
	How would you describe AGF's role within the Kenyan SME finance ecosystem?
Rationale for Guarantees	What do you see as the main barriers preventing Kenyan SMEs from accessing finance?
	To what extent are collateral requirements, information asymmetries, or regulatory constraints key barriers?
	Why are guarantees considered an appropriate instrument to address these constraints?
Impact of guarantees	To what extent do AGF guarantees enable lending to SMEs that would otherwise not have received financing?
	In practice, do guarantees primarily affect: access to credit, collateral requirements, loan tenor, pricing, or lending volumes?
	How important are guarantees in actual credit approval decisions within PFIs?
	Do MSMEs financed under guarantees later "graduate" to non-guaranteed financial products?
Relationship with PFIs	How does AGF typically select partner financial institutions? And what characteristics make a PFI a strong strategic fit for AGF?
	Have you observed significant differences in outcomes across PFIs despite similar guarantee structures?
	How does AGF balance risk sharing while ensuring PFIs retain incentives for sound lending practices? And what governance or monitoring mechanisms are used to mitigate these risks?
	What role does technical assistance (TA) play alongside guarantees?
Monitoring and evaluation	How does AGF assess whether a guarantee programme has been successful? Which indicators are used to track development intend?
	How does AGF assess whether a guarantee programme has been successful?
	To what extent is it possible to establish whether lending would have happened without the guarantee? Are the effects lasting, or mainly linked to ongoing AGF engagement?
Closing	What design features are most important for an effective guarantee programme?
	Is there anything you think is particularly important to understand about guarantees in practice that we have not discussed?

[4] Interview questions varied slightly depending on the specific profile of the interviewee in question.

Partner Financial Institutions	
Theme	**Questions**
Introduction	To start, could each of you briefly introduce your role in the Trade Finance / MSME Business team and how you engage with MSME lending?
	As a team, how are you involved in loans that are backed by development guarantees (such as AGF)?
MSME lending context	Before working with guarantee-backed lending, which MSME segments or transaction types were most challenging for [BANK NAME] to finance, and why?
	From your perspective, how does the presence of a guarantee affect your assessment of risk when lending to MSMEs?
	Have guarantees changed transaction costs in practice - for example, screening, monitoring, or structuring deals?
MSME credit worthiness	Based on your experience, have MSME clients with AGF-guaranteed loans shown improvements in their internal credit ratings over time? - If yes, what typically drives these improvements (repayment history, financial reporting, transaction volume, formalisation)?
	Do you observe cases where MSMEs initially financed under a guarantee later qualify for non-guaranteed financial products? If so, how common is this? And over what time horizon does it typically occur?
Additionality and behavioural change	Are guarantees enabling [BANK NAME] to reach MSME clients or transactions that you would otherwise not have served?
	Do guaranteed MSME clients receive different loan terms compared to non-guaranteed clients (e.g. pricing, tenor, collateral)?
	In your view, would these loans likely have been issued without the guarantee? Why or why not?
Guarantees and capacity building	Have you or your colleagues participated in any guarantee-related training or technical assistance (e.g. risk management, ESG, gender-lending)? And has this influenced how you approach MSME clients?
	Do you see these efforts as complementing the guarantee itself, or as more separate?
Relationship with AGF	To what extent do externally funded guarantees shape [BANK NAME]'s MSME or trade-finance strategy, if at all? If such guarantees were phased out, do you think [BANK NAME] would continue lending to the same MSME segments?
	Do AGF or other partner priorities influence which sectors, MSME profiles, or transaction types are prioritised under guaranteed lending?
	What performance or impact indicators does [BANK NAME] track for guaranteed MSME loans? And how do you report on these to AGF?
Closing	Is there anything you think is particularly important to understand about how guarantees operate in practice within trade finance and MSME banking at [BANK NAME]?

Small and Medium Sized Enterprises (MSMEs) in Kenya	
Theme	**Questions**
Company background	Can you briefly describe your company (sector, size, years in operation)?
	How would you describe your company's growth trajectory so far?
	Before receiving this loan, how did you typically finance your operations? ie. savings, informal lending, other bank loans
	What were the main challenges you faced when trying to access finance?
Loan Experience & Access to Finance	When did you start banking with [BANK NAME]? And what kind of loan agreement do you have?
	Can you describe the process of applying for this loan? Were there any specific conditions that were particularly difficult to meet?
	How would you describe the collateral requirements? And How would you describe the interest rate and repayment terms?
	Did you feel the bank perceived your business as high-risk, medium-risk, or low-risk? Why?
Use of Loan & Business Impact	How did you use the loan?
	What changes did the loan enable in your business? Investment in equipment, expansion, hiring or working capital?
	Did the loan affect your productivity, revenue, or profitability?
	Did it affect your relationships with suppliers or customers?
Counterfactual and additionality	If this loan had not been available, what would you have done? Would you have obtained financing elsewhere? On similar terms?
	Did the loan allow you to undertake activities that would otherwise have been postponed or cancelled? What kinds?
Relationship with the bank and future financing	Has your relationship with the bank changed since receiving this loan?
	Do you feel your business is now perceived differently by financial institutions?
	Have you accessed other financial products since this loan?
	Do you expect to rely on similar financing in the future?
Closing	What was the most important effect of this loan for your business?
	What challenges still remain in accessing finance for businesses like yours? If you could change one thing about MSME lending in Kenya, what would it be?

Expert interview	
Theme	**Questions**
Introduction	Could you start by briefly describing your professional background and how guarantees have featured in your work - both in the Swedish and Danish development finance contexts?
	In your experience across these two institutional settings, have you noticed significant differences in how guarantees are designed, deployed, and evaluated and if so, what do you think accounts for those differences?
The political rationale	From your experience working with guarantee instruments, what do you see as the primary justification for using guarantees rather than other instruments such as concessional loans or grants to expand MSME access to finance?
	In your view, do guarantees effectively address the specific barriers that prevent commercial banks from lending to MSMEs or do you think these barriers are more structural?
	If not already covered; Do you think the market failure conditions that justify guarantees theoretically are actually present in the contexts where they are deployed - for instance in Kenya?
Additionality	Based on your experience, to what extent do you think guarantees actually expand credit access for borrowers who would otherwise remain excluded?
	Do you observe cases where MSMEs initially financed under a guarantee later qualify for non-guaranteed financial products? If so, how common is this? And over what time horizon does it typically occur?
	How do you assess the distinction between financial additionality - expanding credit volumes - and development additionality - generating measurable outcomes such as employment or firm growth? - In your view, is financial additionality a reliable proxy for development impact?
	From what you have seen, do borrowers typically graduate from guarantee-backed lending to accessing credit independently over time, or does the guarantee tend to become a permanent feature of the lending relationship?
Guarantor-PFI relationship	How do you usually see the relationship between the guarantor and the bank play out? - What role does TA play?
	In your experience, how do commercial banks typically respond to guarantee mandates in practice? - Do you think they genuinely adapt their lending behaviour to reach underserved borrowers, or do they tend to use guarantees primarily as a risk management tool on their existing portfolio?
	What governance mechanisms have you seen work effectively in ensuring that partner financial institutions comply with the developmental intent of guarantee schemes - and where do you think these mechanisms tend to break down?
Danish Guarantee Facility - Design and Policy	Denmark has relatively recently established a permanent guarantee facility through IFDK, partly drawing on Sida's prior experience. In your view, what are the most important lessons from the Swedish experience that should inform how Denmark designs and manages its guarantee facility?
	How do you assess the current design of the Danish guarantee facility in terms of its potential to generate genuine development additionality - as opposed to primarily mobilising private capital or managing overall risk profiles for PFIs?
	What has been the biggest challenge in the design of the new guarantee facility?
	How does DFIs (issuing guarantees) perform their due diligence on PFIs? How do you make sure that the guarantee is actually used for its intended purpose?
Closing	Looking at the trajectory of guarantee use in development finance more broadly - do you think guarantees are living up to their promise as catalytic instruments, or is there a risk that the mobilisation narrative is obscuring development impact?
	Is there anything you think is particularly underappreciated or overlooked in current debates about guarantee effectiveness that you would want to flag for my thesis?

Appendix 2: The Code Book

Description: *Each code is assigned to one of six analytical dimensions corresponding to the three-fold structure of the thesis. Within each dimension, codes are organised into themes and sub-codes. The codebook also includes a cross-cutting additionality dimension that captures evidence relevant to both financial and development additionality regardless of which theoretical framework it most directly relates to.*

Dimension I: NIE - Market Failure Conditions in the Kenyan Credit Market *To examine whether the conditions of the Kenyan MSME credit market empirically warrant guarantees as an institutional response.*			
Theme 1.1 Transaction costs in MSME lending			**21**
Sub-code	*Description*	*Illustrative example*	*Frequency*
1.1.1 Information gathering costs	References to the cost or difficulty of obtaining borrower information prior to lending	*"Because they are not formally registered, it is really difficult to obtain information on their credit history" (PFI I)*	12
1.1.2 Monitoring costs	References to the cost or difficulty of monitoring loan use after disbursement	*"We now have [Person 2] and her team who are supposed to monitor the facilities" (PFI II)*	3
1.1.3 Enforcement costs	References to the cost or difficulty of enforcing contract obligations incl. collateral registration	*"In Kenya it's crazy. At times it can even take a year" [to charge a property] (SME I)*	6
Theme 1.2 Information Asymmetry and Credit Rationing			**33**
Sub-code	*Description*	*Illustrative example*	*Frequency*
1.2.1 Inadequate borrower information	References to lack of reliable financial information about MSME borrowers	*"Most MSMEs do not have audited accounts or formal financial records" (PFI I)*	14
1.2.2 Adverse selection concerns	Reference to banks restricting loan volumes or excluding clients	*"Anyone below one year, as a bank, we took a policy not to lend to them" (PFI II)*	11
1.2.3 Guarantee as information substitute	References to the guarantee reducing the need for full borrower information	*"Having AGF gives us a more balanced view of the customer's business… not just looking at collateral, we're also looking at cash flow strength" (PFI I)*	8
Theme 1.3 Collateral Constraints and Property Rights			**48**
Sub-code	*Description*	*Illustrative example*	*Frequency*
1.3.1 Insufficient collateral	References to MSMEs lacking adequate collateral to meet lending requirements	*"The main issue is always collateral - most MSMEs simply do not have enough" (PFI II)*	15
1.3.2 Weak property rights	References to difficulties with land registration, title verification, or collateral enforcement	*"in Kenya, the time to perfect a security is an Achilles heel for SME financing needs" (PFI II)*	12
1.3.3 Guarantee as collateral substitute	References to the guarantee reducing or replacing collateral requirements	*"With the AGF guarantee in place we can be more flexible on our risk calculations" (PFI I)*	21
Theme 1.4 Institutional Environment			**11**
Sub-code	*Description*	*Illustrative example*	*Frequency*
1.4.1 Regulatory fragmentation	References to inconsistent or overlapping regulatory frameworks affecting lending	*"Banks are overly protected/over-insured as they don't release equity" (AGF III)*	6
1.4.2 Weak complementary institutions	References to gaps in supporting infrastructure incl. both political and economic institutions	*"the problem is often that markets are not developed enough to assess risk in a reasonable way. Markets are small, not very liquid, and it can be hard to exit investments" (Expert IV)*	5

Dimension II: SAT - Relational Dynamics and Goal Divergence *To examine whether the structural dynamics of the AGF-PFI relationship is conducive to additionality or whether PFI behaviour is characterised by moral hazard*			
Theme 2.1 Portfolio Share and strategic significance			**26**
Sub-code	*Description*	*Illustrative example*	*Frequency*
2.1.1 Guaranteed portfolio size	References to the AGF-guaranteed portfolio within PFI lending	*"guaranteed portfolio probably below 1% of total loan book at [bank name]" (expert II)*	8
2.1.2 Pre-entry strategic alignment	References to AGF selecting PFIs that already share its developmental mandate.	*"You can't change the strategy of a bank with a guarantee, you need to find a bank that already has the right strategy" (expert II)*	9
2.1.3 Internal champion effect	References to whether a specific staff member or team within the PFI understands and champions the guarantee, affecting utilisation rates	*"If the staff member who understands guarantees isn't talking to the business development team, the guarantee just doesn't get used" (expert IV)*	6
2.1.4 Multiple DG providers	References to PFIs managing relationships with several guarantee providers simultaneously, impacting AGF's relative influence.	*"PFIs range from Access Bank to small tier-3 institutions - large banks have multiple DFI relationships"(AGF IIV)*	3
Theme 2.2 Goal divergence			**37**
Sub-code	*Description*	*Illustrative example*	*Frequency*
2.2.1 Commercial versus developmental objectives	References to tension between the PFI's commercial mandate and AGF's developmental mandate	*"At the end of the day we are a commercial bank and need to manage our risk" (PFI II)*	10
2.2.2 Internal credit assessment frameworks	References to internal risk-scoring models or criteria that shape lending decisions	*"Our credit committee applies the same criteria regardless of whether a guarantee is in place (…) so the risk rating is the same, but we can allow for a higher risk appetite with guaranteed products" (PFI I)*	10
2.2.3 Loan officer behaviour	References to how individual loan officers handle guaranteed versus non-guaranteed applications	*"Part of the issue is that staff who understand guarantees aren't always talking to the business development team" (AGF II)*	5
2.2.4 AGF (in)dependence on PFIs	References to AGF's reliance on PFIs to deploy guarantees and reach SMEs, limiting AGF's ability to enforce behavioural change.	*"AGF's main mission is to facilitate access to financing for MSMEs (...) but the PFIs need to utilise our guarantees to provide financing to MSMEs" (AGF I)*	5
2.2.5 PFI (in)dependence on AGF	References to PFIs' ability to operate without significant reliance on the guarantee, reducing AGF's negotiating leverage.	*"AGF has been one of several trade finance partners since 2017"* (PFI I)	7
Theme 2.3 Moral Hazard at alliance level			**7**
Sub-code	*Description*	*Illustrative example*	*Frequency*
2.3.1 Reduced screening incentives	References to the guarantee reducing the rigour of borrower screening	[No strong evidence found across PFI interviews. Both PFIs emphasise standard credit criteria are maintained]	0
2.3.2 Guarantee used on existing borrowers	References to the guarantee being applied to borrowers who would have received credit regardless	*"there's no point paying for a guarantee you don't need" (Expert II)*	2

2.3.4 Passive drift/under-utilization of facility	References to formal participation in the alliance without substantive behavioural change	*"Banks were requesting guarantee facilities but only drawing down a fraction of them" (AGF IIV)*	5
Theme 2.4 Governance and monitoring			**33**
Sub-code	*Description*	*Illustrative example*	*Frequency*
2.4.1 Contractual compliance mechanisms	References to formal reporting requirements, eligibility criteria, and penalty mechanisms	*"We submit quarterly reports to AGF on the guaranteed portfolio" (PFI II)*	9
2.4.2 AGF monitoring capacity	References to AGF's ability to assess PFI compliance and/or lending behaviour	*"It happens, but very rarely. Recently an AGF investigation found a PFI falsely presenting a default" (AGF IIV)*	2
2.4.3 Relational governance quality	References to trust, communication, and ongoing dialogue between AGF and PFIs	*"We have a good working relationship with the AGF team" (PFI II)*	6
2.4.4 Technical assistance as an alignment mechanism	References to capacity building or technical assistance as a mechanism for maintaining strategic alignment	*"CD plays three major roles - risk mitigation, market development, and impact enhancement" (AGF II)*	12
2.4.5 Enforcement actions	References to AGF sanctioning or challenging PFI behaviour	*"We push back on underutilised facilities" (AGF I)*	4
Theme 2.5 Effect of guarantee at PFI level			**14**
Sub-code	*Description*	*Illustrative example*	*Frequency*
2.5.1 Risk appetite expansion	References to AGF's reliance on PFIs to fulfil its developmental mandate	*"the guarantee enables lending to 1-3 year businesses that would previously be excluded" (PFI I)*	9
2.5.2 Negotiating dynamics	References to how terms of the guarantee relationship are negotiated and by whom	*"The terms are largely set by AGF but we have some flexibility in how we deploy the portfolio" (PFI II)*	5
Dimension III: CPE and financialization of development *To examine the broader political economy implications of the empirical findings for Danish development finance. Applied primarily at the discussion level.*			
Theme 3.1 Risk and return distribution			**11**
Sub-code	*Description*	*Illustrative example*	*Frequency*
3.1.1 Public risk absorption	References to public or donor institutions bearing downside risk	*"Socialising risk - removing it from private actors while banks still capture interest income - is a legitimate critique." (Expert IV)*	2
3.1.2 Private return capture	References to commercial institutions capturing returns without proportional risk exposure	*"The cost of the facility remains the same, no interest rate concession is per say passed to SME borrowers" (PFI II)*	3
3.1.4 Risk of guarantee dependence	References to borrowers failing to graduate from guarantee-backed to independent lending	*"If we were to cease it, customers who haven't reached the threshold would be greatly affected" (PFI II)*	6
Theme 3.2 Financialization of development			**24**
Sub-code	*Description*	*Illustrative example*	*Frequency*
3.2.1 Mobilisation over impact concerns	References to mobilisation ratios being prioritised over demonstrated development impact	*"There's a misalignment between the political narrative on guarantees and the evidence we actually have - particularly on development additionality" (Expert IV)*	10

3.2.2 Danish policy objectives	References to Danish development finance goals and how guarantees serve or underserve them	*"12 billion DKK facility (…) we can target specific priorities (…) whether that's a focus on women, youth, green, refugees, or a particular geographic area". (Expert I)*	4
3.2.3 Instrument versus structural transformation	References to whether guarantees address underlying financial system constraints or merely work around them	*"Unless we rethink how we structure guarantees and partnerships, we won't see fundamentally different results" (Expert IIV)*	5
3.2.4 Power relations in guarantee design	References to whose interests shape how guarantee terms and mandates are defined	*"Organisationally, we are moving increasingly towards an investment finance structure rather than a development finance logic " (Expert IIV)*	5
Dimension IV: Cross cutting additionality assessment *To capture evidence relevant to both financial and development additionality regardless of which theoretical framework it most directly relates to.*			
Theme 4.1 Financial additionality			**43**
Sub-code	*Description*	*Illustrative example*	*Frequency*
4.1.1 New borrowers reached	References to MSMEs accessing credit for the first time through the guaranteed portfolio	*"This was our first time ever securing external financing" (SME I)*	12
4.1.2 Improved collateral terms	References to the guarantee enabling lower collateral requirements	*"so the guarantee addresses a collateral gap - credit criteria remains unchanged and pricing unchanged, only collateral flexibility changes" (PFI II)*	14
4.1.3 Improved interest rates terms	References to the guarantee enabling lower interest rate	[No evidence of interest rate concession from any PFI interview]	0
4.1.4 Counterfactual credit access	References to whether the borrower would have received credit in the absence of the guarantee	*"Around 70–80% of guaranteed portfolio could not have been served without the guarantee" (PFI I)*	9
4.1.5 MSME credit volume effects	References to overall changes in MSME lending volumes attributable to the guarantee	*"Our MSME portfolio has grown since we partnered with AGF"(PFI I)*	8
Theme 4.2 Development additionality			**42**
Sub-code	*Description*	*Illustrative example*	*Frequency*
4.2.1 Employment effects	References to job creation or retention attributable to guaranteed lending	*"We were able to hire three additional staff after receiving the loan" (SME I)*	8
4.2.2 Business growth	References to firm expansion, increased revenues, or new market entry	*"The loan allowed us to purchase new equipment and increase our production capacity" (SME II)*	10
4.2.3 Financial inclusion	References to reaching underserved groups including women, youth, or informal sector businesses	*"A significant share of our guaranteed portfolio goes to women-owned enterprises" (PFI I)*	12
4.2.4 Credit graduation	References to borrowers moving from guaranteed to non-guaranteed lending	*"Some customers have grown to where they can stand by themselves [i.e. without the guarantee]"(PFI II)*	6
4.2.5 Long-term sustainability	References to whether development outcomes are sustained beyond the guarantee period	*"PFIs are reducing collateral requirements over time – their perception of MSME is changing"*	6

Appendix 3: Overview of Qualitative findings

3.1 Overview of difference between original data set from AGF and data used for thesis

	Frequencies	
	Original data set	**Data set used for thesis[5]**
# of loans	80,431 (LPGs = 79.954)	23,583
# of PFIs	255	110
Guaranteed amount	USD ~ 2.5 bn	USD ~ 0.7 bn
# of AFAWA loans	13276	6476
# of green loans	456	102

3.2 Overview of interest rates and collateral rates pre and post guarantee

	Pre-guarantee	**Post-guarantee**	**%-change**
Median interest rate	N/A	24.46%	N/A
Average interest rate	N/A	20.0%	N/A
Median collateral rate	94.41%	42%	55.04%
Average collateral rate	108%	53%	51%

3.3 Status on guarantee backed loans

	Based on all LPGs from original data set	
	Frequency	**Percentage**
Loans repaid	63,135	79%
Loans ongoing	14,144	18%
Loans defaulted	2,675	3%

3.4 Regional portfolio weight and related indicators

Regions	AGF portfolio weight	**Interest rate[6]**	**NPL rate[7]**
Central Africa	21%	15.80%	15.37%
East Africa	37%	20.30%	7.82%
North Africa	1%	11.91%	12.20%
Southern Africa	7%	21.82%	8.38%
WAEMU	30%	12.49%	N/A
WAMZ	4%	19.30%	10.06%
Regional average	**21%**	**16.99%**	**9.24%**

[5] All non-LPG-guarantees were taken out of the data provided from AGF. Furthermore, loan lines, where data was not exhaustive for all columns, was also omitted. Additionally, loans issued prior to 2016 were omitted.
[6] Based on data from World Bank, Trading Economics and Bloomberg using Lending Interest Rates accounting for a 2%-points interest rates spread as OECD MSME Score Card (OECD, 2026).
[7] Based on World Bank data on Defaulted Loans to Total Gross Loans (%) using indicator/FB.AST.NPER.ZS