

Mikrofin

CARE Microfinance Case Study

Banja Luka, Bosnia and Herzegovina (BH)

September, 2001

Program context and regional operating environment

Mikrofin's microcredit program was originally started as Care International microcredit program in Bosnia and Herzegovina (BH) middle/end of 1997. The program became a part of the World Bank financed Local Initiatives (Microfinance) Project (LIP), which provided overall financing to the, on a competitive basis, selected NGOs including loan fund, operating costs and technical assistance financing.

In 1997, one and a half year after the war end, Bosnia and Herzegovina was a country shattered by four years of war with mass unemployment and population displacement. The unemployment rate was around 60 percent and had very serious economic and social implications on post-war economy. About 1.5 million people were both internally and externally displaced and represented about one third of the prewar population.

The only financial institutions providing financial services to the population and enterprises were state owned commercial banks. As of the lack of funds, its ownership structure and complicated policies and procedures commercial banks were not in position to provide any financial services to the micro and small entrepreneurs.

There was no any previous experience in microfinance neither in the country nor in the region and all microcredit programs have been started from the scratch. The Local Initiatives (Microfinance) Project was designed in 1996 as part of the World Bank's program to support the post-conflict reconstruction and economic recovery of Bosnia and Herzegovina with specific goal to provide financial services to the economically disadvantaged and war-affected people and assist them to make transition from dependence on humanitarian assistance to active employment.

Today, the microfinance sector in BH today comprises 17 institutions: 12 local and 4 international microcredit NGOs (known legally as "Micro Credit Organizations") and one specialized commercial microenterprise bank – the Microenterprise Bank, supported by IFC and EBRD. Together the World Bank/LIP-financed institutions comprise about 70 percent of the sector based on earning assets.

Program description

Care International/Mikrofin's microcredit program was started in October 1997. As of July 1, 1999 Care International microcredit program in Bosnia and Herzegovina was localized and locally registered NGO Mikrofin took over and became fully independent and responsible for the microcredit program.

The main goal of the microcredit program is to provide microcredits to the disadvantaged economically active people without access to the financial services provided by the commercial banks. Typical Mikrofin's client is economically active and low income person with profitable business activity or idea (start-up business).

This very clear objective along with the appropriate financing and institutional development led Mikrofin's microcredit program to a very high performance and outreach. In terms of the number of clients served Mikrofin's microcredit program is the largest microcredit program in the region.

As of June 30, 2001 Mikrofin disbursed 23,734 microcredits in total amount of DEM 59,406,500 (US\$ 25,851,392). The average loan size disbursed was DEM 2,503 (US\$ 1,089) or about 100% GDP. The portfolio outstanding was DEM 8,344,893 (US\$ 3,631,372) with 3,955 active clients. Average loan size outstanding was DEM 2,109 (US\$ 917%) or about 84% of GDP.

Methodologies

Mikrofin is applying two lending methodologies individual and group. While there was a tradition in individual lending in the region solidarity group lending appeared to be new method of delivering credits to the target clients. Care International and its Project Manager, with previous experience from Bolivia, played key role in the development of the solidarity group method.

Solidarity group methodology confirmed that it was possible to disburse microcredits to the number of micro entrepreneurs having no traditional collateral. Entering new markets Mikrofin is organizing orientation meetings with the potential clients presenting key elements of the solidarity group methodology and providing necessary instructions. Groups are usually formed of 3-5 people without family members being members of the same group. Group members must have different business and group leader is always person from the local community. Solidarity group methodology has been very “attractive” for a number of refugees and displaced persons who did not have any collateral and were not in position to access commercial bank’s financing.

Individual lending started in a later phase and first individual loans were disbursed to the clients who used to be members of the solidarity groups. In most of the cases individual loans are higher and collateralized.

All credit policies and procedures are comprised in the Credit Manual, which is part of the more comprehensive Operational Manual. Credit policies and procedures are clear and made available to the all credit staff.

Mikrofin is delivering its services through two core loan products, which are well suited to the target clients. After approval by the Credit Committee and contract signing with the client loans are disbursed through the commercial banks. Loan repayments are also collected by the banks and appropriate reports are sent to the Mikrofin’s Finance Department.

Two loan products are result of the two loan methodologies applied and orientation to the target clients.

Individual lending loan product has following characteristics:

- loan sizes range from DEM 2,500.00-15,000.00 (US\$ 1,089-6,527),
- repayment terms are: from 2-18 months
- interest rates are from 2% to 2,5% a month calculated on declining balances,
- up-front fee is from 1-2% calculated on the loan amount.

Solidarity group lending loan product has following characteristics:

- loan sizes range from DEM 500,00-1,500.00 (US\$ 217.00-652.00),
- repayment terms are: from 2-7 months,
- interest rate is 2,5% a month calculated on declining balances,
- up-front fee is from 1% calculated on the loan amount.

Mikrofin does not collect any savings.

Institution framework

Mikrofin is currently organized as Citizens Association, which is local legal form of Non Governmental Organization. This institutional form requires court registration, Statute, General Assembly of founders and Board of Directors. Because Law on microcredit organizations has been recently adopted Mikrofin plans to register as non-profit and non-deposit specialized microcredit organization as soon as possible.

Mikrofin does not have ownership structure and will not have it as long as registered as Microcredit Organization, too.

Future plans and evolution shall depend on the legal framework and institutional forms available. If possible Mikrofin would change its legal status into the institutional form which will allow Mikrofin to convert to a for-profit form.

Mikrofin has developed a solid base for future growth and institutional development. Computerized loan tracking and accounting systems provide accurate and timely reports. Branch network, which includes five Branch Offices is well developed. All internal policies and procedures are documented in a form of a comprehensive Operational Manual. Most importantly Mikrofin has young but well trained and skilled staff. The senior management team consists of the General Director, the Credit Director, and the Finance Director. The team is very solid with respect to day-to-day operations, and shares a clear vision in terms of Mikrofin's competitive advantages, competition and strategy. Credit Officers handle either individual or group loans. Credit Officers appear highly motivated and have a strong client orientation. To date, Mikrofin has maintained strong cohesion among staff and a high degree of transparency in operations. Any future changes of the institutional form will require adequate staff recruitment and training.

As of June 30, 2001 Mikrofin capitalized DEM 2,068,443 (US\$ 900,105) as a result of grants received (DEM 1,160,087 or US\$ 504,824) and retained earnings (DEM 908,355 or US\$ 395,280). In terms of the funding liabilities (about DEM 6,697,660 or US\$ 2,914,560) 54% represent World Bank/Local Initiatives Project funds, 42% funds provided by Care International and 4% short term loan. Funds provided by both World Bank/Local Initiatives Project and Care International are under the subsidized rates.

Mikrofin is today operationally and financially self sustainable institution covering all its operating expenses including financial expenses and loan loss provision by its operating incomes.

Program and portfolio summary information

From its start Mikrofin's microcredit program has been oriented to the low income clients. This is characterized with small outstanding balances, high disbursements in terms of both number of loans and value and high number of female clients served, compared with other microcredit programs in the country.

At the same time Mikrofin successfully managed its expenditures and revenues, which led to a high profitability ratios and full operational and financial sustainability after four years of operation.

After first funds received in October 1997 and staff/loan officers training Mikrofin disbursed its first group loans in February 1998.

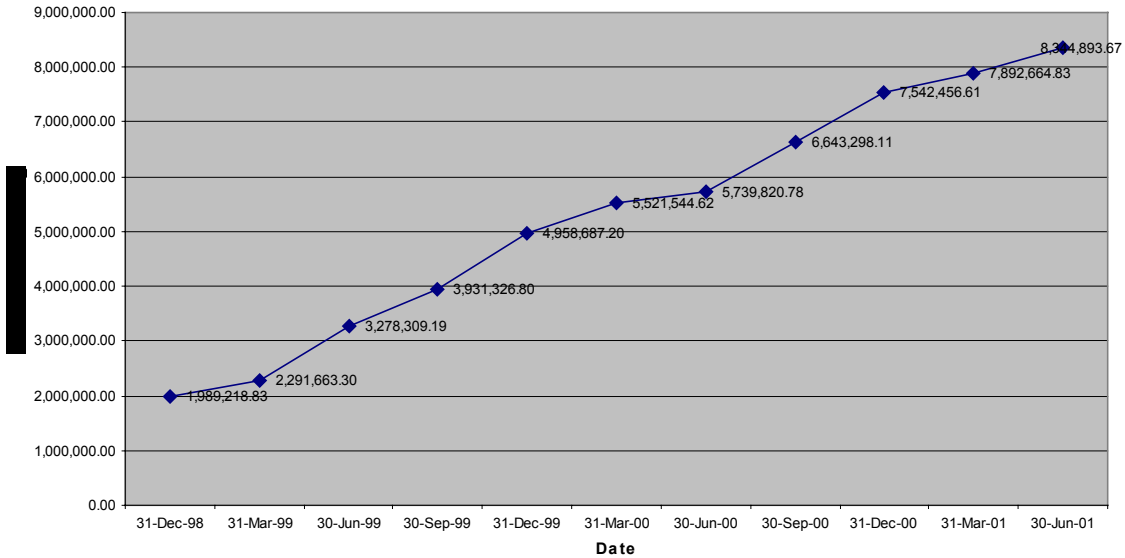
Due to the:

- relatively small average loan size disbursed, about 100% GDP,
- solidarity group methodology,
- increase of the overall institutional capacities including developments/improvements of the systems,
- growth of the operations in the existing regions,
- expansion to the new regions,
- increase of both funding liabilities and capital, and
- short average repayment term (around 6 months),

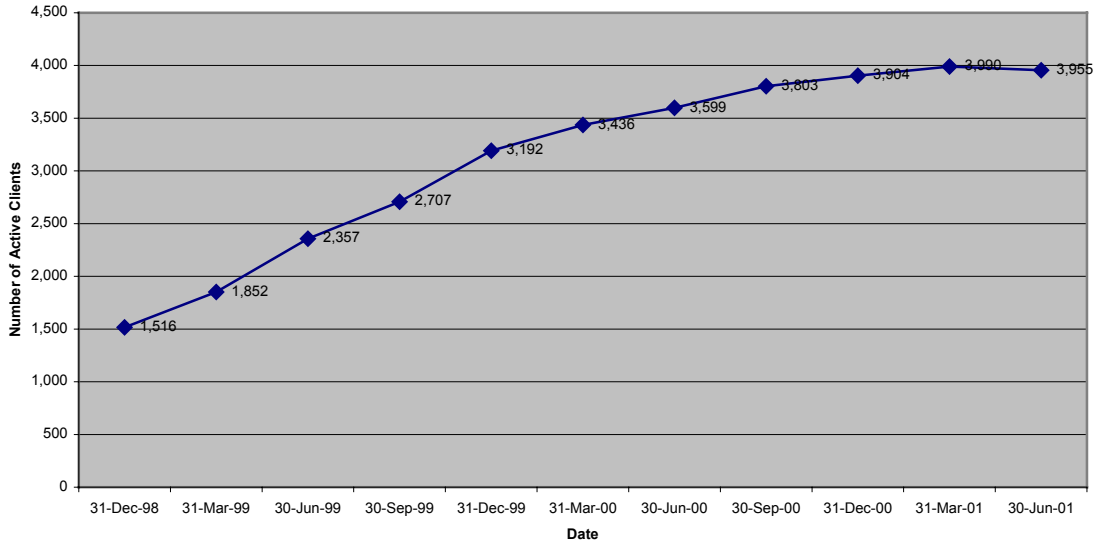
Mikrofin significantly increased its scope of work and outreach over the past four years. Growing trends were very high, which is normal for very young institution and particularly if majority of financing is provided by donors. Financing provided by the World Bank/Local Initiatives Project and Care International including fund's transfers in periodical tranches influenced directly institutional growth and caused some jumps in more or less harmonious growing trends.

Graphs bellow are showing institutional growth in terms of some key elements (portfolio, number of active clients).

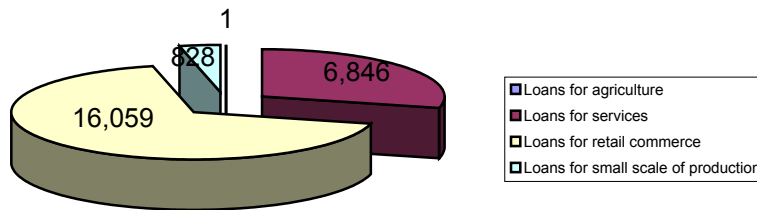
Portfolio outstanding trend line



Number of Active Clients trend line



Mikrofin’s clients use their loans to finance its business activities in: services, trade and small scale production. Dominant activities financed by Mikrofin are trade and services.



Portfolio quality has always been very high with PAR after 30 days below 1%. Following factors contributed to this very high portfolio quality:

- good credit analysis,
- clear and documented loan approval procedures,
- good MIS system providing accurate and timely reports on late payments including ageing,
- clear procedure in terms of the “treatment” of the late payments,
- appropriate loan officer’s incentive system based on the loan officer’s portfolio quality among other factors,
- clients motivation through the higher follow up loans and simpler loan approval procedure.

Microfinance sector in BH developed very rapidly over the past four years. It comprises today 17 institutions: 12 local and 4 international microcredit NGOs (known legally as “Micro Credit Organizations”) and one specialized commercial microenterprise bank – the Microenterprise Bank, supported by IFC and EBRD.

As international NGO with the previous experience in microfinance Care International played one of the key roles in the development of the microfinance sector in BH. This was of significant importance during the initial phase of the development of the microfinance sector. There was no previous experience in microfinance in this region and Care's presence, including very qualified international Program Manager, contributed a lot to the development of the microfinance sector in BH.

Mikrofin took over from Care International as of July 1, 1999. This way program was localized and local staff became fully responsible for the microcredit program. Care International continued to provide financing and kept two positions in the Board of Directors. Mikrofin continued, very successfully, further institutional development and represents one of the leading microcredit organizations in BH serving low income clients and bottom end of the small and micro entrepreneurs.

Lessons learned

Mikrofin was and is focused on provision of financial services to low-income clients and entrepreneurs who do not have access to loans provided by commercial banks. This specific type of lending required important efforts in institutional development and staff training. The World Bank Local Initiatives Project provided significant amount of all types of the technical assistance through hiring of very qualified international microfinance experts. The technical assistance was very often tailored to the specific needs of the growing microcredit organizations. In addition to this Mikrofin, individually, organized some staff training (especially for the new hired loan officers) or sent its staff to the regional training centers for additional training. The staff training is considered as one of the key success factors.

On time localization of the microcredit program, after two years, provided both Care International and Mikrofin with the credibility in the local community to continue implementation of other projects in case of Care International and to further develop microcredit program in case of Mikrofin. Care International policy in this regard was very clear from the very beginning and localization was one of the important goals of the microcredit program. The only international full time employee on the microcredit program was Project Manager and rest of the staff was hired locally. The development of the skills and capacities of the local staff made localization of the microcredit program very easy, simple and straightforward.

Development of a very clear and strict lending policies and procedures together with the appropriate staff/loan officers training led to a very high portfolio quality. Clear institutional mission/vision shared among employees and development of the appropriate loan products to the target clients enabled Mikrofin to serve a specific market niche. This was very important in the initial phase of the institutional development.

Problems or issues Care International/Mikrofin faced during the evolution of the microcredit program could be divided in to two groups: external and internal.

One of the first external problems Care International has faced starting its microcredit program in BH was fact that country just came out of the four year war. Not only the country itself but the economy were totally destroyed. Hundreds of thousands of people were unemployed, displaced, refugees. Some political factors and almost "resistance" to the international NGOs, especially in the Republic of Srpska of Bosnia and Herzegovina, caused additional difficulties.

According to the existing local laws NGOs were not allowed to provide any type of financial services. This made loan disbursements by Care International and Mikrofin difficult and management was under the constant pressure of "doing something illegal". At the same time the process of development of "Law on microcredit organizations" was very slow as of number of reasons: long process of drafting the Law, number

of stakeholders were involved (World Bank, USAID, Ministries of Finance, international and local lawyers, Banking Agencies), permanent personal changes in the Ministries of Finance and Governments.

Although the World Bank played the key and extremely positive role in the development of the microcredit sector in BH in some cases its internal rules represented limitations. Acting as most of donors World Bank imposed some criteria and conditions, which in some cases, represented barriers to the development of the microcredit organizations. This is in a first place related to the limitation to the amount of the operating costs of microcredit organizations. Secondly, fund disbursement procedure was very often very slow and made microcredit organizations create waiting lists of the clients in some cases.

Internal problems or challenges were related to the overall institutional development and funding. As other microcredit programs in BH Care International/Mikrofin microcredit program was growing very fast in terms of portfolio outstanding and number of active clients, in terms of staff and branch network, etc. The development of the key institutional factors such as Business plans, staff hiring and training, systems was very often caused by this growth. Normally this process should be vice versa.

As mentioned above delays in funding caused some internal difficulties in terms of cash and liquidity management and loan disbursement.

Mikrofin has developed solid institutional base for the future institutional growth and development. In order to position itself as a good and permanent institution in the financial sector Mikrofin will have to develop a plan to build greater depth in its management team. This will be necessary especially in case Mikrofin decides to change its institutional form in future and to convert to a for-profit form. This will also require appropriate changes to the Board of Directors.

Secondly the competition among microcredit organizations shall increase in the near future and some commercial banks might decide to enter the microcredit sector, too. Mikrofin should consider its future market position and prepare itself to address these market challenges.

Thirdly, alternative or commercial sources of funding should be sought. In terms of funding Mikrofin is currently relying on the World Bank/Local initiatives Project, Care International and its own capital. Further institutional growth and development will require more diversified sources of funding including commercial borrowing in order to make Mikrofin more independent.

Balance Sheet with June 30, 2001

ASSETS	
Cash	7,933.93
LID Portfolio Bank Account	54,702.39
Other Bank Accounts	37,850.33
Interest-bearing Deposits	-
Loans Outstanding	
LID Loans Outstanding: Current	3,695,455.45
LID Loans Outstanding: Non-Performing	-
LID Loans Outstanding: Rescheduled	-
Total LID Loans Outstanding	3,695,455.45
Other Loans Outstanding: Current	4,648,260.75
Other Loans Outstanding: Non-Performing	1,177.47
Other Loans Outstanding: Rescheduled	-
Total Other Loans Outstanding	4,649,438.22
Total Loans Outstanding: LID and Other	8,344,893.67
(LID Loan Loss Reserve)	0.00
(Other Loan Loss Reserve)	-167,651.31
(Total Loan Loss Reserve: LID and Other)	-167,651.31
Net LID Loans Outstanding	3,695,455.45
Net Other Loans Outstanding	4,481,786.91
Net Loans Outstanding (LID and Other)	8,177,242.36
Accounts Receivable	21,044.90
Other Current Assets	-
TOTAL CURRENT ASSETS	8,298,773.91
Long-term investments	-
Property and Equipment	855,217.19
(Accumulated Depreciation)	-138,724.30
Net Property and Equipment	716,492.89
TOTAL LONG-TERM ASSETS	716,492.89
TOTAL ASSETS	9,015,266.80
LIABILITIES AND NET WORTH	
LIABILITIES	
LID Loan	3,737,893.32
Short-term debt	150,000.00
Client Savings: passbook	-
Client Savings: time deposits	-
Deferred Revenue	-
LID Payable Cost of Capital	15,360.50
Other Payables	233,802.85
TOTAL CURRENT LIABILITIES	4,137,056.67
Long-term debt	2,809,767.07
Other Long Term Liabilities	-
TOTAL LONG TERM LIABILITIES	2,809,767.07
TOTAL LIABILITIES	6,946,823.74
CAPTIAL	
Grant Capital	1,160,087.28
Shareholder Capital/Paid In Capital	-
Excess (Deficit) of Income over Expenses (prior years)	490,294.34
Excess (Deficit) of Income over Expenses (current year)	418,061.44
TOTAL CAPITAL	2,068,443.06
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TOTAL LIABILITIES AND CAPITAL	9,015,266.80

Income Statement with June 30, 2001

FINANCIAL INCOME	
Interest income on Loan Portfolio	1,079,594.30
Loan fees and service charges	157,000.00
Penalties on Loans	97.40
Total loan income	1,236,691.70
Income from investments	
Income from other financial services	-
Total other financial income	
Total Financial Income	1,236,691.70
Other income	13,134.76
FINANCIAL COSTS OF LENDING FUNDS	
Interest on borrowed funds	139,519.75
Interest paid on deposits	-
Total Financial Costs	139,519.75
GROSS FINANCIAL MARGIN	1,110,306.71
Provision for Loan Losses	16,545.35
NET FINANCIAL MARGIN	1,093,761.36
OPERATING EXPENSES	
Salaries and Benefits	419,667.22
Office Supplies	8,544.11
Comunication	10,569.22
Rent&Utilities	69,974.52
Fuel	10,538.26
Travel Costs	2,494.73
Other Costs	5,864.09
Vehicle Maintenance	6,591.84
Depreciation	31,129.46
Training	37,001.20
Bank Fee	73,325.27
Total Operating Expenses	675,699.92
NET INCOME FROM OPERATIONS	418,061.44
NON FINANCIAL INCOME	
LID Operating Grant Income	-
Other Operating Grant Income	
Non-financial services income	-
EXCESS (DEFICIT) OF INCOME OVER EXPENSES	418,061.44

Financial Ratios with June 30,2001

Outreach and Institutional Indicators	
No. of active clients	3,955
No. of loans disbursed	4,835
Amount of loans disbursed	14,400,000
Average initial loan size disbursed	2,348.04
Average loan size disbursed	2,978.28
% loans to women	42.52%
% loans to DPs/returnees	34.27%
No. of staff	44
No. of branch offices	5

Portfolio Indicators/Ratios	
Total loan portfolio outstanding	8,344,894
Loan loss reserve ratio	2.01%
Portfolio at risk (> 30 days)	0.01%
% write-offs	0.50%

Profitability ratios	
Adjusted Return on Assets	3.58%
Adjusted Return on Equity	16.61%
Yield on Portfolio	32.11%
Operational Self-Sufficiency	150.26%
Financial Self-Sufficiency	113.95%

Efficiency Ratios	
Operating Costs Ratio	21.37%
# of active clients/Loan Officer	165
Total Gross Portfolio Outst./Loan Officer	347,703.90

Financial Structure	
Outstanding Gross Portfolio/Total Assets	92.56%
Cash and Bank Accounts/Total Assets	1.01%
Total Equity/Total Earning Assets	24.99%

Clients Stories

Client's name: Kondic Branko

Methodology: Solidarity group

Activity: Production of all types of keys

Credit cycle: VI

I have heard about MIKROFIN from my colleague who had received a loan from MIKROFIN. I have to say that from the very beginning I have seen difference in the way and system of work with us. Somehow I have felt that we have understood each other. I received the first loan in 1998 (10.03.1998). The group guarantee was suited to us because we had no bank guarantee. Practically, our knowledge and our work are the only guarantee for the loan. MIKROFIN, previously CARE has recognized and accepted that fact and I have received my first loan in amount of 1,500 DEM. I have bought a machine I am using now. That machine has provided me development and chance to feed my family. Since I was satisfied with loan conditions I have continued to receive further loans and now I am in the sixth cycle, loan amount I have received is 2,500 DEM. Finally, I am very satisfied and happy because such institutions exists at the market.



Client's name: Srdic Miroslav

Methodology: Solidarity group

Activity: Shoemaker

Credit cycle: III

The first loan I received from MIKROFIN was in the spring of the last year (18.04.2000). I needed to buy some raw material and used sewing machine. Since there is no bank at the market which would like to finance us this was the first time that somebody wanted to help us. So far, mainly we had to find a solution in the way we know. This is exactly what we need, the bank for us, for craftsmen. There was no guarantee problem although it was hard to find people to guarantee for as well as people who will guarantee for you. But everything has gone well and now I receive third loan in amount of 3,000 DEM. Gradual increase of loan amount suites to me although I thought it was a big problem at the very beginning. Finally, if my work goes well I will continue to be client of MIKROFIN.



Client's name: Kne`evi} Sretko

Methodology: Individual

Activity: Repair of electronic devices

Credit cycle: II

I am the owner of service shop "SREJA &CO ELECTRONICS". My cooperation with MIKROFIN was started in January last year when I received the first loan in amount of 4,500 DEM. Since I have arranged to attend course for licensed repair of devices PANASONIC and SONY I needed money to pay the course. My ideas had been understood by MIKROFIN that has approved my application for loan. The course was good and I got the license that provided a significant expansion of my activities. At this moment I am using the loan amount of 9,000 DEM, and I am able to introduce new services in my business. Since I intend to develop my own business and to provide new services, and since my payments to MIKROFIN were on time I believe in the future support of MIKROFIN to my business.

