Theme n° 3
How can we gain in order to serve on the long term?
Managing the costs

CCSP-Laos

MAIN Seminar
The levers of financial sustainability

A Case study

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1 – INTRODUCTION : THE CCSP AND ITS LAOTIAN ENVIRONMENT

At the end of 1996, the *Coopérative de Crédits pour le Soutien aux Petites Unités de Production* - CCSP-Vientiane - was the first private credit union with legal status in Laos.

Based on this initial successful experience, a number of new regional CCSPs were developed to form a network of CCSPs in Laos, with the support of the SIDI and the *Association de Soutien au Développement des Sociétés Paysannes* (ASDSP). The network now has 6 operating CCSPs and 3 more under construction.

In order to consolidate its position and the network's refinancing capacity, a study on the creation of a refinancing fund for the CCSPs is underway. The shareholders it will bring together are the local CCSPs and the international donors, such as the SIDI and its partners in Europe.

1.1 The context

According to the UN nomenclature, Laos is classified among the world's least-advanced countries with a per capita GDP estimated at less than US$ 300 per year. Eighty-five percent of its rural population is made up of scattered ethnic groups, living in a self-sufficient village economies.

In 1975, Laos joined the camp of the Communist countries, alongside Vietnam and Cambodia. After 4 years of a collectivized system, based on the Chinese and Soviet models, the economy was on the verge of collapse. Starting in 1979, was obliged to disengage from its collectivist path and prior to 1990 more than 3,000 collectivist co-operatives were disbanded. An individual family-based economy was then encouraged in place of the

collective co-operatives and price control of farm and manufactured products was abandoned.

After the constitution was adopted in 1991, a body of law on foreign investors, taxation and trade rights was passed, thereby enabling the country to evolve towards a market economy.

1.2 The initial ideas

It was against this backdrop that some officials from the Agriculture Ministry left the civil service to set up a group of local expert volunteers to carry out development actions under the name *association de soutien au développement des sociétés paysannes* (ASDSP).

After a dozen years' experience in development actions, including during their civil servant period, the staff of the ASDSP noted that most of the previous economic activities had trouble developing. Some of the reasons were:

- local businessmen are too poor and cannot dispose of enough savings to develop their economic activities;
- the merchant banks do not want to risk financing small producers or poor businessmen;
- under projects backed by international institutions or by the state, local initiatives are, before long, deadlocked by the presence of experts and state officials who are too interventionist.

1.3 A network of durable financing structures in the hands of local businessmen's groups

Based on the observations mentioned above, the staff of the ASDSP launched a challenge, summed-up by the following ideas and objectives:

- develop an economy of solidarity in Laos;
- create financing structures belonging to groups of local businessmen, farmers and craftsmen, in the villages, districts and suburban neighbourhoods, as a means to develop their economic activities, starting with the creation of the first CCSP in the capital, Vientiane, at the end of 1996;
- organize a network of ethics, mutual assistance and partnership amongst the CCSP, i.e. a **CCSP network**;
- create a refinancing structure in the CCSPs (a co-operative fund) that would bring together, as shareholders, the partners from the north (SIDI, Fondation Gillès, Alterfin, Nosereor, etc.), and the CCSPs in Laos;
- improve the performance and the profitability of the CCSPs, enabling them to buy, gradually, shares in the co-operative fund, in order to become the main network of local shareholders in the co-operative fund in Laos.

2 – A THREE-STAGE DEVELOPMENT STRATEGY

2.1 The creation of the basic structures:1996-2000

- Experiments were conducted with the granting of loans in 1996 in the region of Vientiane, the capital of Laos. Based on those positive results, an initial legal *savings and loan* structure recognized by the state was set up and became the first CCSP (*Coopérative de Crédits pour le Soutien aux Petites Unités de Production)*;

- The initial structure of the CCSP was bolstered through techniques and strategies enabling it to perform very well and be recognized as a leader in the area of solidarity financing. The technical means introduced are:
  - a series of training manuals in the Laotian language on credit management methods;
  - a micro-banking software package in Laotian for managing savings and loans, adapted to the level managerial staff in the villages and districts;
- Training was provided for managerial staff and a number of CCSPs were developed in the various provinces in order to meet the many needs of the rural zones in Laos: 6 CCSPs were set up between 1996 and 2000.
- A CCSP network was set up along the same ethics and the same vision of development, featuring an ethical network of exchanges, mutual assistance and development based on Laos village society.

2.2 Consolidation of the CCSPs and refinancing: now in progress

This second stage is designed to strengthen the development capacity of the CCSPs via the creation of a refinancing fund in partnership with the international donors, focussing on the following:

- The continuation of the training programme for CCSP managers and the attainment of the goal of 13 regional CCSPs (including the first CCSP in Vientiane).
- Create a global refinancing structure for all the CCSPs, with the first 13 CCSPs as local shareholders along with the international shareholders, the SIDI and its partners in Europe, other international donors, etc. with a initial capital of around US$ 600,000, of which 80% to 90% would be held by the international shareholders and 10% to 20% by the local shareholders.
- Attain a development impact vis-à-vis 5,000 members by the end of the year 2005.
- Since one of the leading objectives of the donors is to support the CCPS network in order to make progress towards autonomy, they plan to transfer 20% to 40% of their shares to the shareholders by the end of the year 2005.

2.3 Development of the network: 2005 and 2010

This stage consists of boosting the performance and profitability of the CCSPs, allowing the CCSP network to acquire a majority of the shares and to establish itself as the leading majority group of shareholders of the refinancing fund. The objectives to be reached will be:
- Develop the network of CCSPs beyond the 13 CCSPs planned in the initial strategy.
- Reinforce the performance and the profitability of the CCSPs and their socio-economic impact on their members so as to achieve the capacity to increase their equity capital and gradually acquire a majority of the shares of the refinancing fund.
- The final objective of the international donor partners will be achieved when a fully autonomous and durable refinancing structure is in the hands of the population through the CCSPs in Laos.

3 – ARRANGING THE CCSPS INTO A NETWORK OF FINANCING STRUCTURES CLOSE TO LOCAL BUSINESSMEN

The network is made up of small decentralized independent and profitable structures that are close to their customers or member businessmen. Each CCSP is intended to have a management capacity of 300 to 500 members or customers. Beyond that number, a new CCSP must be created.

Each CCSP can cover several villages. The members or customers of the CCSP must organize themselves in *solidarity groups* that act as guarantors for their borrower members. The solidarity groups operate under the following rules:

- In principle, each solidarity group should not have more than 10 members (any more would not be manageable by local businessmen);
- Each group should have a solidarity deposit and guarantee office able to fully cover one or two conventional loans of their group (a conventional loan would be a loan limited to the group's guarantee capacity). If this conventional loan limit is exceeded, the borrower must find other additional guarantees).
- The solidarity group must be recognized by the legal authority of the village (with the seal of the village);
- Every disputed loan must be resolved in the first instance within the solidarity group, and then in the administrative council of the village and only as a last resort by the district or provincial court.

The network of the CCSPs must be sufficiently large to be representative at provincial or national level, with a sufficient number of functional local structures enabling it to set up a refinancing fund in partnership with the international donors.

- So far, 6 CCSPs have been set up and 3 new CCSPs are being created. The development plan calls for 13 CCSPs by the end of the year 2002.
- The refinancing structure (the co-operative fund) is now under study.

4 – HOW CAN WE GROW IN ORDER TO SERVE ON THE LONG-TERM? A NETWORK BUILT ON THE QUEST FOR AUTONOMY

In our network in Laos, each CCSP is made up of poor businessmen without enough income to develop their own economic activities. That is why the founders of the network are counting on the following in the start-up:

- support from the donors to pay for the training of managers and contributions from the SIDI and its partners in Europe, for example.
- and an initial fund contributed by the members of each CCSP.

4.1 Disseminate the founding principle: autonomy

The key principle of the CCSP network is to transmit to the leaders of the local CCSPs a spirit of autonomy **from the outset**.

Taking the initiative in creating a CCSP

The local founding group must take the steps to obtain authorization from the local authorities in the village, district or province for the setting up of their CCSP and to operate savings and loan activities under legal conditions. An office will be supplied at the start by

the local founding group. In the beginning it might be the house of a member (rent will be paid later on with the revenue from the CCSP) The group should appoint at least one manager, who will be paid a part-time salary, based on a quarter monthly time, and later on will be paid full-time, along with salary supplements, depending on the growth of activities and profitability.

Operational autonomy

Three to six months after the start, the local CCSP must attain financial equilibrium, in other words, the monthly revenue must be more than monthly expenditure. Income from the collection of interest and other services offered by the local CCSP must cover the capital costs (interest paid out on borrowing from banks and on the savings of members), the rent, wages and other office costs.

An initial degree of financial autonomy

The equity capital (shares + savings and member deposits) must be between 15% and 20% of the portfolio at the end of the first year and between 20% and 25% at the end of the second year, and so on.

4.2 Setting a rate of interest combining profitability and fairness

This spirit of autonomy automatically implies **a control over charges and revenue**, in other words, enough must be earned in order to cover the charges (see *operational autonomy* below), and to set aside reserves for a contingency provision and a margin to ensure its development.

Control over revenue also means control over fair interest rates that also ensure sufficient profitability for the structure and enough revenue for the customers. The CCSP network believes that its long-term viability depends on its ability to generate long-term and equitable profitability that will feed its own development and the creation of wealth for its customers and members.

The rates of interest on loans granted by the CCSPs are in general higher than those on loans granted by state banks but lower by more than 50% than the rates of interest charged by the loan sharks.

This rule for setting interest rates has been proposed and approved by the twice-yearly Assembly of Solidarity Groups of each CCSP's board of directors.

Today, given the newness of the network, a single rate of interest is defined by each CCSP, as follows:

- cost of capital (interest on borrowing) = 30%
- administrative costs (including wages) = 10%
- contingency provision = 2% to 5%
- margin = 5%

Total: 47% to 50 % per annum

The network of CCSPs sets profitability at 15% and if that margin is exceeded because of growth in the portfolio, then the CCSPs decrease the rate of interest on loans and in exchange the customers (CCSP members) must spend the extra cash resulting from the fall in interest rates on shares of the CCSP, which in turn increases the equity capital of the CCSPs.

4.3 Regularly assessing the network's performance

A monthly performance and profitability evaluation system helps to anticipate changes in each CCSP, month by month. Below is an example of an evaluation table of 3 regional CCSPs.

Real and monthly ratio	CCSP-Kasi	CCSP-Thatèng	CCSP-Nateuil
Year of start-up	Beginning 98	Beginning 99	January 2000
Ratio of June, 2000			
Monthly administrative costs/portfolio	2.83%	1.07%	1.34%
Return on portfolio: interest collected/expenditure	5.03%	3.96%	4.18%
Financial equilibrium: revenue/expenditure	146%	120%	101%
Financial autonomy: equity capital/portfolio	114%	16.59%	25.60%
Repayment rate (without arrears)	98%	99%	99%

Each of the 3 CCSPs achieved financial equilibrium as the total of monthly revenue exceeded the total of monthly expenditure: +46% for CCSP-Kasi, +20% for CCSP-Thatèng and +1% for CCSP-Nateuil.
In its first six months of operations, the CCSP-Nateuil reached financial equilibrium; only one salary was paid out for 20% of full-time. The woman in question only earned 50,000 kip per month (around US$45). On the other hand, the CCSP-Thatèng, which started a year and a half earlier with a portfolio of 202 million kip (US$30,000) spends 1 million kip (US$150) on two salaries. The salary increases in step with increases in revenue.

It is only at the first stages of autonomy that each CCSP can develop and increase its portfolio.

5 – DIFFICULTIES AND SOME LONG-TERM SOLUTIONS

Exchange-rate risks

One of the first difficulties encountered in poor countries is the unpredictability of monetary crises that can occur at any time, such as in Laos where the local currency has been devalued by 100% to 140% per year since the 1997 crisis.

The CCSP network is required to hold its borrowed funds in US dollars in order to ensure a return and to protect against exchange rate losses. Those funds are used as a guarantee to enable the CCSP network to borrow in local currency from a Laotian foreign trade bank.

Bank regulations

One major problem are the interest rate ceilings set by the state. The rate of interest applied by the CCSP should not, in principle, exceed by more than 3% the rate applied by state banks, resulting in a maximum of 27% since the rate applied by the state banks is 24%. It would be impossible for the CCSPs to apply that ceiling because a CCSP is not like a state bank that can apply subsidized interest rates and any deficit is made up by fresh funds from the state.

The CCSPs continue to apply a profitable rate of interest of around 50% per year. But the CCSP network is now negotiating with the Central Bank authorities to ease some of the more restrictive regulations.

Insufficient liquidities

The network of the CCSPs is still too young and too small to mobilize enough deposits and savings to finance loans. The successive devaluation of the local currency over the years does not encourage people, who are poorer and poorer, to save.

The funds offered by the international donors are available but there is still too much exchange-rate risk to transfer those funds into the local currency as the economic situation of the country is far from stable. But those resources are needed by our young CCSP network as a guarantee fund in order to obtain capital in the local currency from a bank with a large supply of money, such as the BCEL. Funds borrowed on the long-term could be transferred into the local currency with less risk because the repayment of those funds would be staggered over time and less risky than funds borrowed on the short or medium term.

The setting up of the future refinancing fund (co-operative fund), with a sufficiently large initial capital contribution from the international donors would be a good solution to ensure durable financing with lower risks on the long-term..

6 – DETAILED COMPARISON OF 3 CCSPS: KASI, THATENG AND NATEUIL

Evaluation of the performance of the CCSP-KASI

exchange rate: 7750 kip/$	at July 31, 2000
Number of villages involved	
Number of solidarity groups	
Number of members	120
Number of salaried managers	2
Number of active borrowers	70
Number of outstanding loans	70
Average amount of loans	1,766,389
Portfolio at end of period (see T6)	123,647,252
Average portfolio per manager	61,823,626
Average number of borrowers per manager	35
Loans from banks or donors	31,698,134
Shares	3,695,000
Capital transferred from the former credit union	105,497,805
Accumulated results in reserve	7,764,203
Members' savings	24,048,658
TOTAL EQUITY CAPITAL	**141,005,666**
Equity capital/borrowing	445%
Equity capital/portfolio	114%
Real ratio from January to July	
Administrative costs (administration + salaries + taxes)/portfolio: from July 1, 2000	17.40%
Portfolio return in % (interest received/portfolio): from July 1, 2000	32.16%
Operational autonomy % (revenue/expenditure): from July 1, 2000	128%
Financial autonomy in % (capital equity/portfolio)	114%

Rate of repayment	98%
Real ratio for the month of July	
Administrative costs for the month/portfolio	2.83%
Portfolio return in % (monthly interest received/portfolio)	5.03%
Operational autonomy % (monthly revenue/expenditure)	146%
Financial autonomy in % (capital equity/portfolio)	114%
Rate of repayment	98%
Cost of capital borrowed by the CCSP (already included in monthly expenditure)	30%
Annual rate of interest on loans granted by CCSP	60%

Nota bene::

Kasi reached its operational autonomy because its revenue greatly exceeded its expenditure (see Ratios above)

Evaluation of the performance of the CCSP-Thatèng (in KIP)	
Exchange rate: 7600 kip/$US	**at June 30, 2000**
Number of villages involved	
Number of solidarity groups	15
Number of members	130
Number of salaried managers	3
Number of active borrowers	120
Number of outstanding loans	120
Average amount of loan	1,691,121
Portfolio at end of period	202,934,478
Average portfolio per manager	67,644,826
Average number of borrowers per manager	40
Loans from banks or donors	**173,500,000**
Share capital	1,080,000
Accumulated results in reserve	6,428,385
Members' savings	26,165,307
Total equity capital (capital + savings)	**33,673,692**
Equity capital/borrowing	19.41%
Equity capital/portfolio	16.59%
Real monthly ratio: June, 2000	
Monthly administrative costs/portfolio in %	1.07%
Monthly return on portfolio in % (monthly interest received/portfolio)	3.96%
Monthly operational autonomy in % (revenue/monthly expenditure)	120%
Financial autonomy in % (equity capital/portfolio)	16.59%
Rate of repayment	99%
Cost of capital borrowed by CCSP (already included in monthly expenditure)	32%
Annual interest rate on loans granted	48%
***Nota bene*:**	
Operational autonomy was readily achieved because the revenue surpassed the expenditure by about 20% monthly	

Evaluation de la performance de la CCSP-Nateuil (EN KIP)	
Exchange rate : 7600 kip/$	**at March 31, 2000**
Number of villages involved	
Number of solidarity groups	2
Number of members	17
Number of salaried managers	1
Number of active borrowers	15
Number of outstanding loans	15
Average amount of loan	721,955
Portfolio at end of period	10,829,328
Average portfolio per manager	10,829,328
Average number of borrowers per manager	15
Loans from banks or donors	**10,000,000**
Share capital	170,000
Members' savings	2,602,700
Total equity capital (capital + savings)	**2,772,700**
Equity capital/borrowing	27.73%
Equity capital/portfolio	25.60%
Real monthly ratio for March, 2000	
Monthly administrative costs/portfolio in %	1.34%
Monthly return on portfolio in % (interest received / portfolio)	4.18%
Monthly operational autonomy (monthly revenue/expenditure)	101%
Financial autonomy in % (equity capital/portfolio)	25.60%
Rate of repayment	99%
Cost of capital borrowed per year (already included in monthly expenditure above)	32%
Rate of interest on loans granted by CCSP	48%
Nota bene: the CCSP-Nateuil reached operational autonomy in the first six months; March revenue was 1% more than expenditure.	