

Policy makers in other regions responded to the crisis in the microfinance sector by tightening legislation and introducing stricter regulation, while in ECA the general tendency in 2009 seemed to be to liberalize and streamline legislation to allow for a wider range of financial services and more conducive operating environments for MFIs. At the same time, the negative effects of the crisis on MFIs and clients prompted policy makers to delve deeper into issues of responsible and ethical finance and to tackle over-indebtedness.

The crisis also had broad repercussions for the financing of MFIs. Commercial lenders quickly retreated, whereas cross-border public investors' came forward. While total outstanding debt financing decreased for MFIs, cross-border funders continued to increase their commitments to microfinance either directly or through microfinance investment intermediaries (MIIs), signaling a long-term interest in the industry. However, much of the disbursed funding did not reach retail MFIs in 2009, as some were not able to absorb additional funding due to scaled-back growth plans and the performance of others made the investments too risky, resulting in high liquidity for MIIs. For institutions allowed to take deposits, deposits proved to be a reliable source of domestic funding, and unlike loan portfolios, savings portfolios increased.

On a positive note, a healthier sector is likely to develop now that industry actors are more willing to engage in responsible lending to both clients and MFIs, support portfolio growth with more adequate risk management, and have a greater understanding of target clients through tracking of social performance indicators. This report explores how *MFIs*, *policy makers*, and *funders* in ECA have begun to adjust to the new risks and challenges presented by the 2009 twin economic and financial crises. The report analyzes client outreach, product realignment, changing policy and funding trends, and social performance indicators.

## Market Overview

### A. Scope and Trends of Microfinance Services

#### Key Issues and Trends

- The ECA microfinance market experienced the most severe contraction in credit services worldwide in 2009.

- In 2009, some credit unions and some microfinance programs of downscaling banks closed, while more new nonbank financial institutions (NBFIs) in Central Asia were registered. The overall number of institutions remained at levels similar to that of 2008.
- Commercial banks realigned their product offerings in reaction to the crisis—banks in Central and Eastern Europe (CEE) and the Balkans shifted their focus from microfinance toward SME lending.
- Interim data through September 2010 demonstrate continued contraction in the Bosnian market and slow growth in Azerbaijan and Kosovo.
- Unlike loan portfolios, savings portfolios and deposit accounts increased in most subregions, with the exception of CEE. In the coming years there may be newcomers in the provision of deposit services, as several large NBFIs in Central Asia have received deposit licenses.

#### 1. Credit Services

Economies in the ECA region were severely affected by the global financial and economic crises. While most countries had gross domestic product (GDP) growth of over 5 percent in 2008, almost half of the region had negative growth in 2009. As the crises deepened in 2009, the region saw continued economic deterioration and an increase in poverty levels. In 2009, close to one-fifth of the population lived below national poverty lines—an increase of 4.5 percent from the prior year, representing almost 3 million more people (see Table 1). Poverty rates grew primarily in the Balkans and CEE, as these two subregions were most integrated with Western Europe's economy and, consequently, were most affected by the economic downturn.

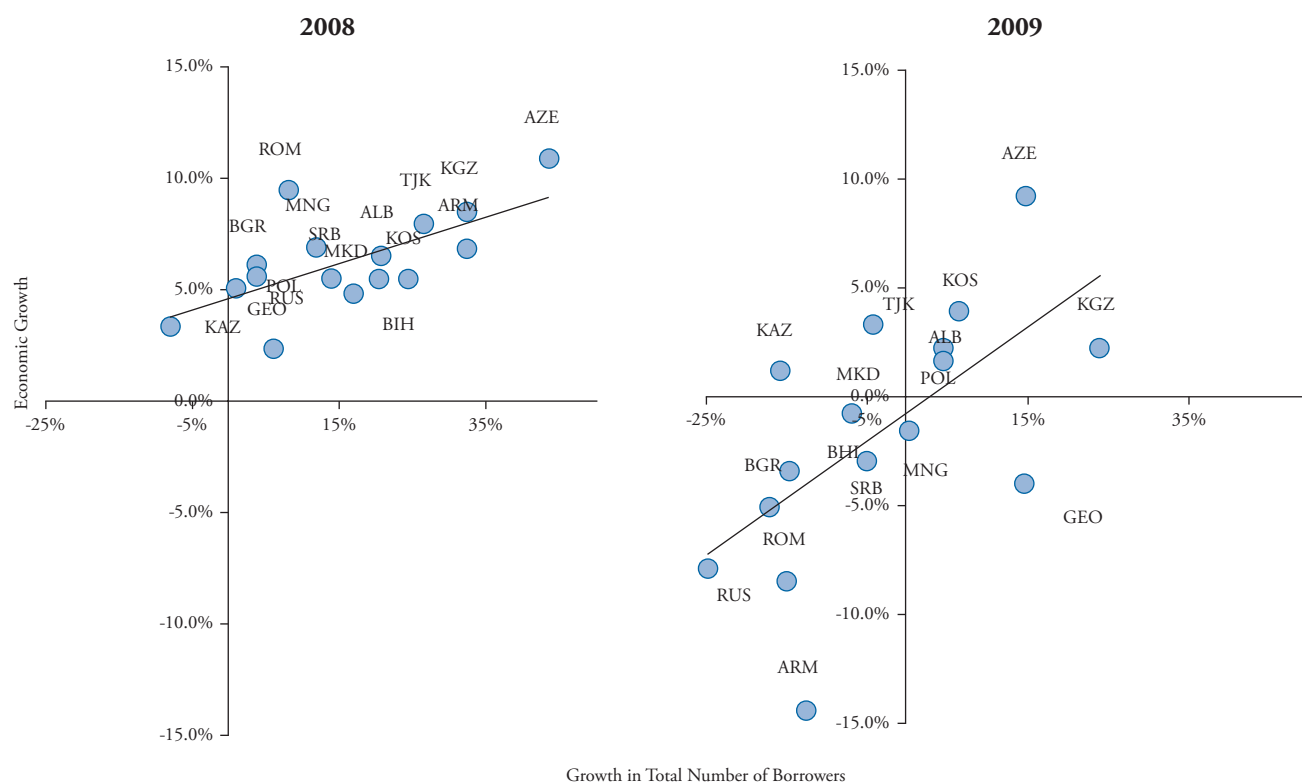
The crisis in the United States and Western Europe quickly spilled over to Russia and continues to have negative effects in Kazakhstan, whose financial systems are deeply integrated with those of the United States and Western Europe. Through their close trade ties with Western Europe, countries in CEE experienced crisis contagion. Countries that rely heavily on remittances from Western Europe (for the Balkans and CEE) and Russia and

**Table 1** Key Macroeconomic Indicators and Volume Figures, 2009

	2009	Compared to 2008
Countries	22	n/a
Population, mln	366.21	0.2%
Poverty rate	19.6%	4.1%
Number of people below poverty line, mln	71.66	4.5%
Average gross national income per capita, USD	7,034	-0.7%
Number of institutions providing microfinance services	8,012	-3.3%
Number of active borrowers, thous	8,576	-4.1%
Total loan portfolio, USD mln	12,095	-12.1%
Number of savers, thous	10,335	3.6%
Total savings portfolio, USD mln	8,596	21.9%
Lending penetration rate	12.0%	-8.2%
Savings penetration rate	14.4%	-0.5%

**Source:** CGAP-MIX MFI Survey 2009, World Bank Indicators, National Statistics Agencies. Results for gross national income per capita and poverty rates are weighted by the population size of each country. Product penetration rates are defined as total outreach over total population living below the poverty line, by country.

**Figure 1** Correlation between Economic Growth and Growth in Total Number of Borrowers, 2008-2009



**Source:** MIX Market 2007-2009 and World Bank indicators on GDP growth. Results are percentage changes of total amounts.

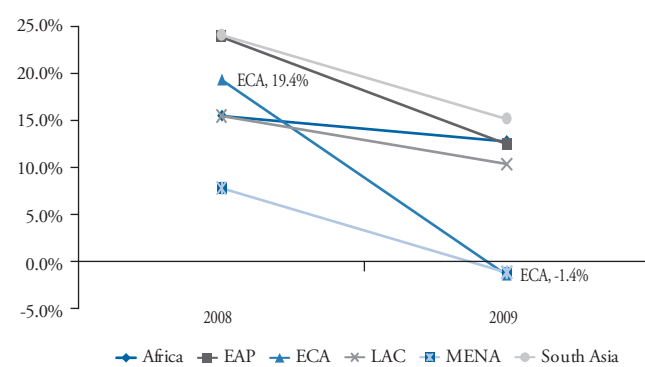
Subregion	Number of countries	Population, mln.	Average gross national income per capita	% of people living below national poverty line	Population below poverty line, mln.
Balkans	7	23.1	6,660	17.5	4.05
Caucasus	3	16.1	3,897	22.3	3.6
CEE	6	126.5	6,945	25.4	32.19
Central Asia	5	58.6	2,585	22.6	13.25
Russia	1	141.9	9,370	13.1	18.58
Total/Weighted average	22	366.21	7,034	19.6	71.66

Source: World Bank Indicators, National Statistics Agencies.

Kazakhstan (for the Caucasus and Central Asia) witnessed a sharp drop in volume of remittances, which decreased by 26 percent in 2009 versus 35 percent in 2008.<sup>2</sup> The combination of these events led to a contraction in the volume of microcredit. Demand from clients decreased as microenterprises had less business, and clients who depend on salaries or remittances for repayments saw these sources of income dry up. At the same time, supply decreased as MFIs were more cautious in their assessment of borrowers because of increased risk, with many preferring not to disburse loans to new clients. Figure 1 illustrates the correlation in ECA between growth in country GDP and growth in number of borrowers. In 2008, all but Kazakhstan had positive growth in outreach, whereas at the end of 2009, 10 markets had contracted in terms of number of borrowers. The only outlier is Georgia, where GDP shrank in 2008 as a result of the armed conflict with Russia, but microcredit services actually grew due to greater demand from clients as well as increased donor support for provision of financial services in the affected regions. Figure 2 shows that the contraction of microcredit services was the highest in ECA compared to that of all other regions.

Every part of the ECA region was hit by the crisis (see Figure 3). Credit services stagnated or contracted in the subregions of ECA most affected by the twin crises, such as the Balkans and CEE, which experienced the highest drop in number of borrowers—7 percent and 15 percent, respectively. Growth in outreach in Central Asia and the Caucasus was sluggish compared to 2008, but still positive—a trend driven by stable growth in markets such as Azerbaijan and Kyrgyzstan.

Figure 2 Growth Rates in Number of Borrowers, by Region 2007-2009



Source: MIX Market 2007-2009. Data are percentage changes of total amounts.

Market contraction was manifested not only in the decrease in microcredit services, but also in the structure and number of financial service providers in the sector. The total number of institutions remained similar to that of last year—about 8,000 (see Tables 3 and 4). However, there was a shift in institutional types—with greater numbers of NBFIs and decreasing numbers of credit unions and downscaling programs of commercial banks. Very small nonbank credit-only organizations continued to proliferate in Central Asia (20 percent more than in 2008) but that did not affect aggregate outreach much, as the average Central Asian NBFIs is very small with only 661 active borrowers.<sup>3</sup> At the same time, many credit unions in Poland, Ukraine, and Romania closed down as a result of the crisis. In Ukraine, there were 99 fewer credit unions in 2009 than in 2008. This was due

<sup>2</sup> See “Workers’ remittances and compensation of employees, received (current US\$)” at <http://data.worldbank.org/indicator/BX.TRF.PWKR.CD.DT>.

<sup>3</sup> For the purposes of this analysis about 1,000 MFIs registered in Kazakhstan were excluded from the statistics as they exist on paper only (otherwise Kazakhstan alone would account for 1,712 nonbank MFIs).



						8.0%			949	
						0.0%				

that once banks supported by EBRD repay their loans, they no longer report to EBRD, while some may still continue microlending activities.

A similar trend is observed among specialized microfinance banks. A large portion of their portfolio is allocated to the nonmicrofinance sector because they lend to corporations,

governments, and other financial institutions. ECA stands out globally in terms of the percentage of portfolios channeled into corporate lending (see **Figure 4**), especially by specialized microfinance banks. Corporate loan portfolios composed 54 percent of the total in 2009, up from 51 percent the previous year. Banks, particularly in the Balkans and CEE, moved from retail microfinance to SME

loans in 2009, with a 72 percent increase in the number of corporate loans versus an 11 percent decrease in retail loans. The annual reports of several ProCredit banks<sup>4</sup> state that small and very small businesses were most affected by the crisis and this, coupled with over-indebtedness among unregistered businesses, resulted in the banks' decision to focus on SME loans and to disburse fewer loans below US\$10,000. Within the retail loans sphere, MFIs lend to microbusinesses (microenterprise loans), but they are increasingly issuing loans for other household financing needs, such as consumer and mortgage loans.

Looking at the retail clients of ECA MFIs, consumer loans make up one-third of all loans—a trait observed only in the mature microfinance market of Latin America and the Caribbean (see Figure 5).

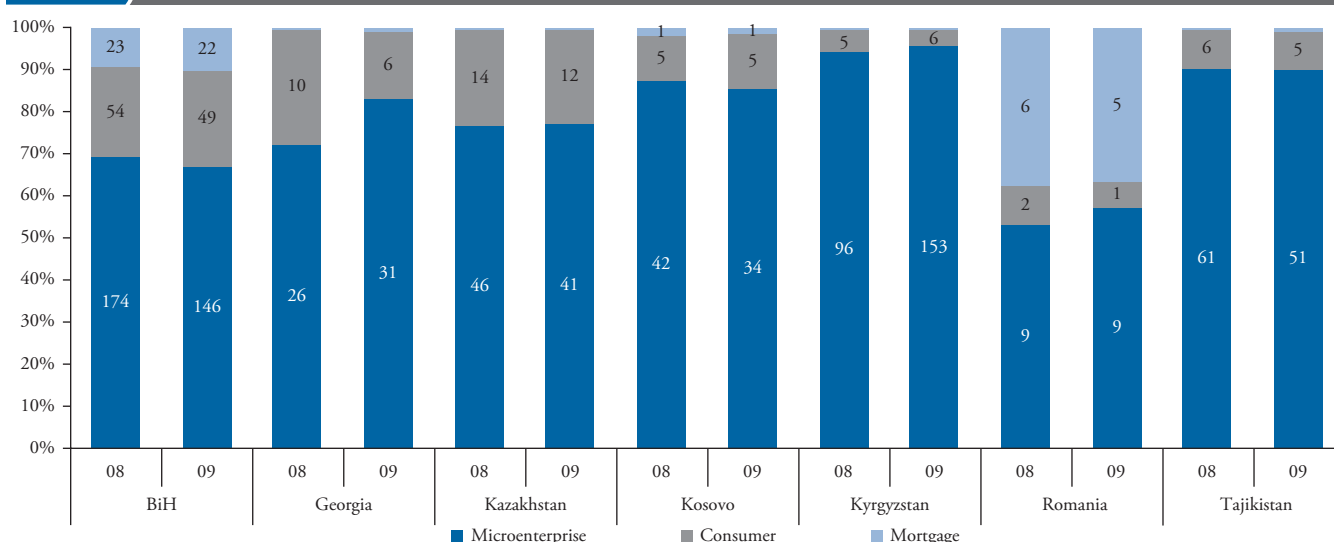
In several ECA markets, NBFIs decreased consumer lending in 2009. Figure 5 shows that in Georgia and Kazakhstan, consumer loans decreased in absolute amount, as well as a percentage of the MFI's outstanding loans. Georgian MFIs moved in this direction, since consumer loans presented higher risk for the institution in the aftermath of the armed conflict with Russia and the financial crisis. For example

one MFI, Crystal, reduced its portion of consumer loans by increasing prices and setting stricter loan conditions. In CREDO, the largest MFI in Georgia, clients were taking consumer loans in parallel with business loans, a practice CREDO began to monitor more closely and to restrict in some cases in the environment of higher credit risk. In Kazakhstan, ACF changed its main loan product from an individual to a group loan, thereby decreasing significantly the individual consumer loan portfolio, while another, Arnur Credit, decided to focus more on rural microbusiness loans than on loans for household purposes. In Bosnia and Herzegovina, both microenterprise and consumer loans decreased in amount, but microenterprise loans were more affected, perhaps due to the higher risk associated with lending to unregistered businesses.

To sum up, in 2009 MFIs adjusted to higher credit risk resulting from the financial crisis and from specific market events (e.g., over-indebtedness in Bosnia and Herzegovina, political instability in Georgia) by shrinking or slowing down the growth of their portfolios and re-evaluating their product offerings. Did this trend continue into 2010 once the worst repercussions of the crisis were over? Quarterly data<sup>5</sup> demonstrate a continuing deterioration in ECA's

Figure 5

Trends in Loan Products Offerings for Nonbank MFIs in ECA, 2008-2009



Source: MIX Market 2009. Data represent totals. Data labels represent the number of loans outstanding in thousands.

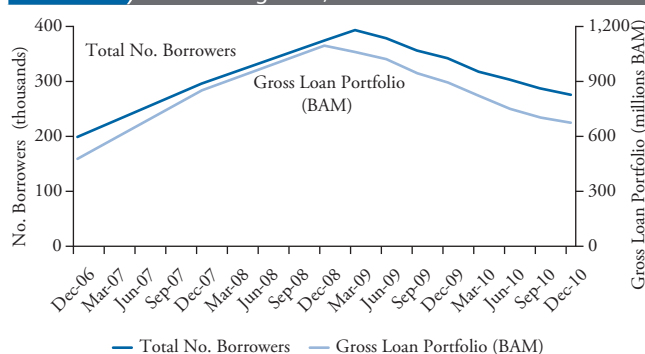
<sup>4</sup> See Annual Reports 2010 for ProCredit Bank — Bosnia and Herzegovina.

<sup>5</sup> As of the writing of this report MIX has collected interim data for the markets of Azerbaijan, Bosnia and Herzegovina and Kosovo.

biggest microfinance sector—Bosnia and Herzegovina (see Figure 6). Very high growth rates in this small market (the population is about 4 million) in 2006-2008 supported by a large influx of foreign as well as local debt investments led to over-indebtedness. The sector had a penetration rate of 15 percent in 2008, doubling from 7.8 percent in 2006. Globally, only Bangladesh had a higher penetration rate (25 percent). Multiple lending to clients and clients guaranteeing other clients' loans, compounded with the effects of the crisis, led the market to contract and portfolio at risk to triple. By December 2010, the loan portfolio of Bosnian MFIs had shrunk back to 2007 levels.

Kosovo and Azerbaijan, which were among the few sectors that did not contract in 2009, continued positive, though much slower, growth in 2010. NBFIs in Azerbaijan have slowed their growth as competition further intensified from the specialized micro- and SME-lending bank AccessBank and 11 other downscaling banks (see Figure 7). As we note later in the Financial Performance section, risk levels at these same banks continued to rise during the year. Cognizant of the problems created in Bosnia and Herzegovina when too many MFIs chased too few clients, NBFIs in Azerbaijan were looking for ways to assess the level of cross-indebtedness in the industry by sharing client lists, devising indicators to track through the national association, and preparing to meet the requirements for using the country's Central Credit Registry Service.<sup>6</sup> In

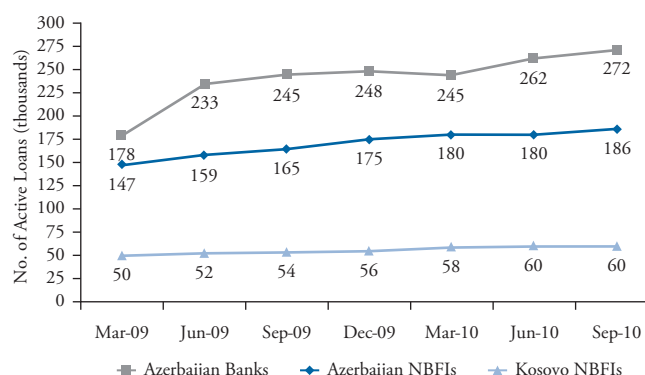
**Figure 6** Quarterly Trends in Outreach and Scale in Bosnia and Herzegovina, March 2009–December 2010



**Source:** Association of Microfinance Institutions in Bosnia and Herzegovina. Data represent totals.

<sup>6</sup> For more information see “Market Overview” of Azerbaijan Country Briefing at <http://www.mixmarket.org/mfi/country/Azerbaijan/report>.

**Figure 7** Quarterly Trends in Outreach and Scale in Bosnia and Herzegovina, March 2009–December 2010



**Source:** AMFA for Azerbaijan, AMFI for Bosnia and Herzegovina, and AMIK for Kosovo. Data represent totals.

Kosovo, another very small Balkan country with a strong microfinance sector (albeit one dominated by ProCredit Bank, which comprises 64 percent of the market), NBFIs outreach stagnated in 2010 amid rising risk levels and concerns about over-indebtedness.<sup>7</sup> Therefore, 2010 results for a few markets show that the trends observed in 2009 continued into the next year, as MFIs were still cleaning their portfolios; in sectors less affected by the crisis, MFIs were becoming more cautious, learning from the experience of neighboring markets.

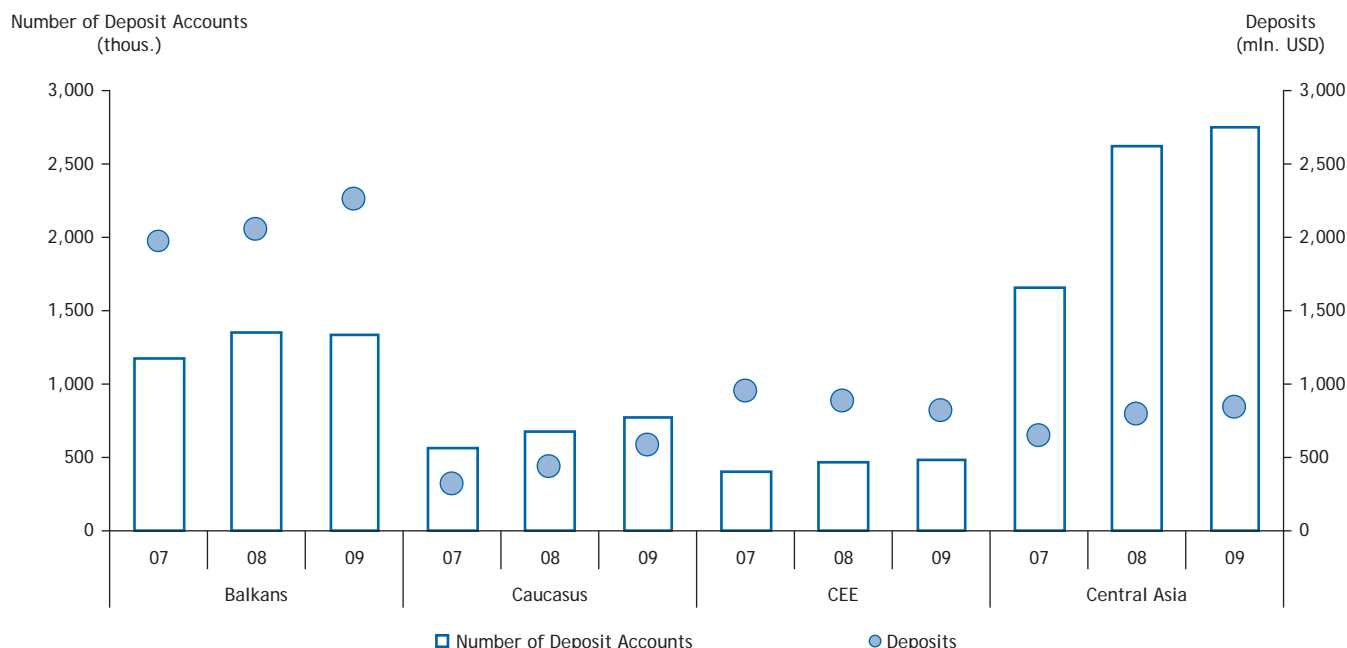
## 2. Deposit Services

In contrast to credit services, the volume of savings increased overall in 2009, although not uniformly across the region (see Figure 8). In 2009, deposit mobilization continued to be strong in the Caucasus and in all countries of the Balkans except Bosnia and Herzegovina. ProCredit Bank Bosnia saw a 25 percent decrease in volume of deposits, because of pay outs of large deposits to public companies and institutions. Retail deposits increased by 2.2 percent though, underscoring the reliability of a diversified deposit base. A similar situation was observed in CEE, where banks continued to experience a contraction in volume of savings that began in 2008.

<sup>7</sup> In a recent study by *responsAbility* “Over-indebtedness and Microfinance – Constructing an Early Warning Index” Kosovo is classified in the second most exposed to over-indebtedness category, i.e. the market exhibits relatively high level of early warning signals for over-indebtedness.



**Figure 8** Trends in Number of Deposit Accounts and Deposit Volume (USD mln.) for Banks, by Subregion, 2007-2009



**Source:** MIX Market 2007-2009. Data represent totals.

is contraction was due primarily to the withdrawal of term deposits by institutional investors and large retail customers. In Central Asia deposit accounts and savings volume for banks remained at similar levels to 2008, though Khan Bank, with 2.2 million depositors (among Khan Bank's deposits are children's welfare money accounts—a government-disbursed state allowance for children), covers practically the entire country of Mongolia, whose population is 2.7 million. Overall, the deposit base of ECA banks continued to be a stable source of funding. Where it has diminished, it did so at slower rates than that of the loan portfolio — the ratio of deposits-to-loans portfolio for the Balkans has been at or above 100 percent over the past three years, while in CEE it remained at about 70 percent, as in 2008.

## B. Policy Environment and Supporting Infrastructure

### Key Issues and Trends

- Financial inclusion agendas are reinforced rather than weakened, despite the crisis.

- Policy makers increasingly realize that they need to fill gaps in regulation to prevent quasi-deposit-taking (i.e., borrowing or investments from clients, the terms of which come close to those of typical retail deposit-taking).
- Consumer protection and consumer financial education are the most commonly cited reforms undertaken in the region.
- Over-indebtedness issues are found throughout the region, particularly in the most saturated markets, prompting policy makers and sector players to focus on issues of responsible and ethical finance.
- More research is necessary to understand whether government funding of microfinance is filling in gaps or undermining private sector players, especially in view of increased retail government funding of microfinance clients in some countries (e.g., Kazakhstan).
- Using nonbank financial service providers to provide branchless banking services is much

more challenging than it would appear on the surface, though development of alternative nonbank payment systems continues in several countries in the region.

### 1. Trends in Financial Inclusion

As the financial crisis of 2008-2009 hit the ECA region, industry stakeholders were concerned that this could thwart or suspend policy and regulatory reforms aimed at increasing low-income populations' access to finance. Despite these expectations, the financial inclusion agenda was reinforced rather than weakened as a number of countries in the region introduced substantial legislative changes or initiated important regulatory discussions. The following are some examples:

- In **Bosnia and Herzegovina** there is ongoing discussion with regard to two main themes:<sup>8</sup>
  1. Working out a smoother path for nongovernment organization (NGO) MFIs (microcredit foundations [MCFs]) to transform into commercial companies (microcredit companies [MCCs]).<sup>9</sup> This would be accomplished through consolidation of MCFs to limit the number of market players, since, per the current interpretation of the law, MCFs that establish MCCs are supposed to remain in the market and continue lending.
  2. Expanding the range of financial services allowed for both types of MFIs to include savings, money transfers, leasing, and card operations.
- In 2009, **Russia** adopted a new law, "On credit cooperation,"<sup>10</sup> to streamline and regulate activities of financial cooperatives—the most numerous microfinance service providers in the country—which before the law had existed in many different forms. In 2010, the Russian president approved

a new law, "On microfinance activity and microfinance organizations"<sup>11</sup> (effective from January 2011), to introduce the standardization of activities, performance indicators, and reporting of MFIs that are registered under the law, as well as to open up potential access to government support programs for all forms of MFIs.

- In **Serbia**, for many years the government had not allowed direct lending activities by any form of NBFI, and local MFIs had therefore been compelled to lend through commercial banks. Last year was marked by the initiation of a broad-based discussion among policy makers, the microfinance sector, and international development institutions that culminated in the development of a draft law, "On microlending companies," that allows MFIs to lend directly and was submitted to the Parliament at the end of 2010.<sup>12</sup>
- In 2009 and 2010, the National Bank of **Tajikistan** (NBT) worked on the development of a new draft law, "On microfinance organizations," that would replace the current microfinance law. The focus of the new legislation is on differentiated treatment of nondepository and deposit-taking MFIs, as well as standardization of disclosure requirements and preservation of the social mission of NGO MFIs.<sup>13</sup>

Overall, policy makers in the ECA region have been moving on a path to liberalizing legislation on microfinance—providing for a range of various nonbank forms and expanding the range of financial services allowed.

### 2. Deposits and Quasi-Deposits

In many ECA countries, NBFIs without licenses to take deposits act as de facto deposit-taking financial intermediaries, often responding to customer demand.

<sup>8</sup> See [http://amfi.ba/images/stories/publikacije/mikrofinansije\\_2010eng.pdf](http://amfi.ba/images/stories/publikacije/mikrofinansije_2010eng.pdf)

<sup>9</sup> See, Eastern Europe and Central Asia Benchmarking Report, 2008.

<sup>10</sup> <http://www.cgap.org/gm/document-1.1.6144/Federal%20Law%20on%20Credit%20Cooperation%20of%202009.pdf>

<sup>11</sup> <http://www.cgap.org/gm/document-1.9.46017/Federal%20Law%20No.%20151-FZ%20on%20Microfinance%20and%20Microfinance%20Organisations.pdf>

<sup>12</sup> [http://icfp-serbia.org/assets/Uploads/Microfinansing\\_in\\_Serbia.pdf](http://icfp-serbia.org/assets/Uploads/Microfinansing_in_Serbia.pdf)

<sup>13</sup> See, NBT presentation at [http://www.mfc.org.pl/mfc\\_2010/prezentacje\\_2010.html](http://www.mfc.org.pl/mfc_2010/prezentacje_2010.html).

Policy makers are beginning to realize that gaps need to be filled in prudential regulation of nonbanks and the resulting consumer protection and systemic risk issues, though only a few countries have taken concrete measures thus far.

Regulators in **Moldova** undertook a careful analysis to decide how to regulate NBFIs that fund their activities with loans from natural persons. An overriding concern is how to provide an adequate regulatory/supervisory framework without hindering expansion of financial access and innovation. However, since the market penetration and portfolio value of these nonbank providers are rather low, additional research is necessary to see whether the risks they pose are worth the cost of creating additional regulation and supervision.

The new law “On microfinance activity and microfinance organizations” in **Russia** limits nonbank MFIs’ ability to accept loans from natural persons; only loans of RUB 1.5 million (about US\$50,000) or more will be allowed.

the development of consumers' rights, and implementation of specific measures is now underway. Last year, Ukraine also undertook a national financial literacy survey designed to lay the basis for a financial education framework, tools, and programs.

#### 4. *Over-Indebtedness Issues*

With the onset of the financial crisis, issues of microfinance borrower over-indebtedness arose in a number of countries in the ECA region.<sup>18</sup> Not only did high debt burdens adversely affect the financial conditions of microfinance clients, they also heightened the risk of discrediting microfinance as a socially oriented development tool designed to help low-income clients. How did policy makers and sector players react?

In **Azerbaijan**, the issue of borrower over-indebtedness became so severe that the local MFI association considered promoting a principle of "one lender, one client." Concerned about this issue, several banks and leading MFIs in the country, as well as

is unjustified, as it can be perceived as a disincentive for private sector players who would otherwise be interested in working in hard-to-reach areas. Also, it remains to be seen whether there is a viable exit strategy for the Fund in the medium or long term.<sup>22</sup>

## 6. Branchless Banking

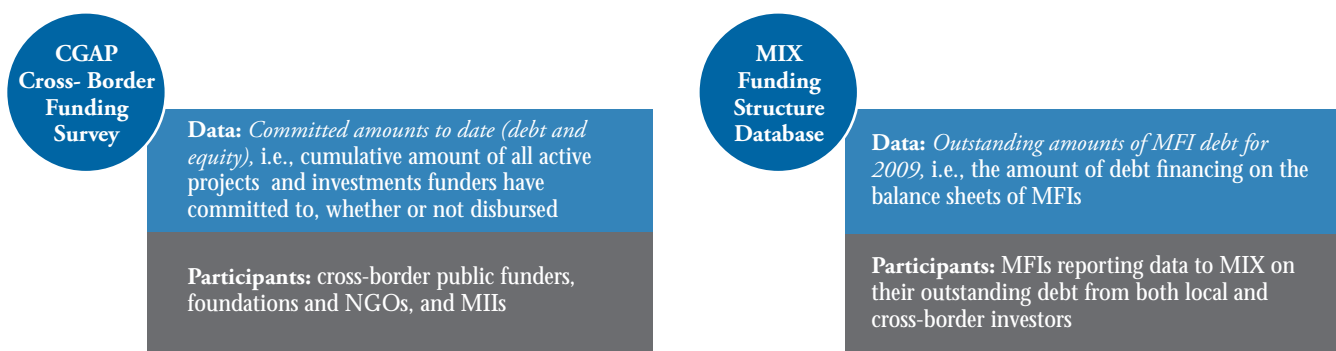
Despite the promise of branchless banking to provide cheaper access points and expand financial services to the unbanked, MFIs in the region have not turned to these solutions yet. With respect to other nonbanks that typically do not provide microfinance services (such as payment transfer companies), regulators have been struggling with several issues, including definitions of a range of allowable activities for agents, the delegation of rights and responsibilities (including for customer identity verification), other anti-money laundering and combating the financing of terrorism (AML/CFT) issues, the role of mobile network operators, the introduction of consumer protection, and the overall scope of supervision. Until these issues are resolved it will be difficult for traditional MFIs to enter in the branchless banking area. In the meantime, however, the expansion of branchless channels for payment services in several countries in the region is noteworthy (e.g., Russia, discussed in the prior year's report).<sup>23</sup>

## Funding of the Microfinance Industry in ECA

### Key Issues and Trends

- Debt continues to constitute the most significant source of funds in the balance sheets of ECA MFIs, while the share of equity in MFIs' funding structure decreased because of the erosion of capital due to losses in 2009.
- **Commitments** (i.e., cumulative amounts of funding for all active projects and investments, whether or not disbursed): Cross-border funders, mostly public lenders such as development finance institutions (DFIs), increased their funding commitments to ECA, though funding went primarily to MIIs<sup>24</sup> rather than to retail MFIs.
- **Outstanding debt:** Commercial lenders, such as local banks, retreated from troubled sectors while public investors such as DFIs and bilateral agencies increased their share of funding.
- At the end of 2009, liquidity of both MIIs and MFIs was higher than in 2008.

Figure 9 Data Sources



<sup>22</sup> For a discussion on the role of government in microfinance, see CGAP, *The Role of Government in Microfinance, Donor Brief* at [http://www.cgap.org/gm/document-1.9.2371/DonorBrief\\_19.pdf](http://www.cgap.org/gm/document-1.9.2371/DonorBrief_19.pdf).

<sup>23</sup> See also materials of the Fifth Krakow Forum on Policy, Law and Regulation for Inclusive Finance (8-10 October 2010) in the Policy Program section at <http://www.mfc.org.pl/pf2010.htm>.

<sup>24</sup> MIIs are investment entities that have microfinance as one of their core investment objectives and mandates. MIIs can provide debt, equity, or guarantees (directly or indirectly) to microfinance service providers. The main types of MIIs are microfinance investment vehicles (MIVs), holding companies, and others, such as peer-to-peer lending platforms.

- Foreign exchange risk is high for MFIs operating in countries with depreciating local currencies. Many MFIs disbursed loan products in hard currency, but there is also a positive correlation between credit risk and the percentage of assets in hard currency.

## A. Funding Structure of ECA MFIs

MFIs in ECA continue to rely primarily on debt financing to fund their portfolios, while equity levels decreased due to net losses that eroded capital (see **Figure 10**).

This is most evident for MFIs that are not financially sustainable (i.e., MFIs whose adjusted revenues in 2009 did not cover their financial, operational, and impairment loss expenses) where the capital-to-asset ratios decreased from 26 to 22 percent. Deposits fund a greater portion of the loan portfolio of banks; their share increased in 2009 due to an increase in the savings volume as mentioned earlier, while borrowings remained at similar levels.

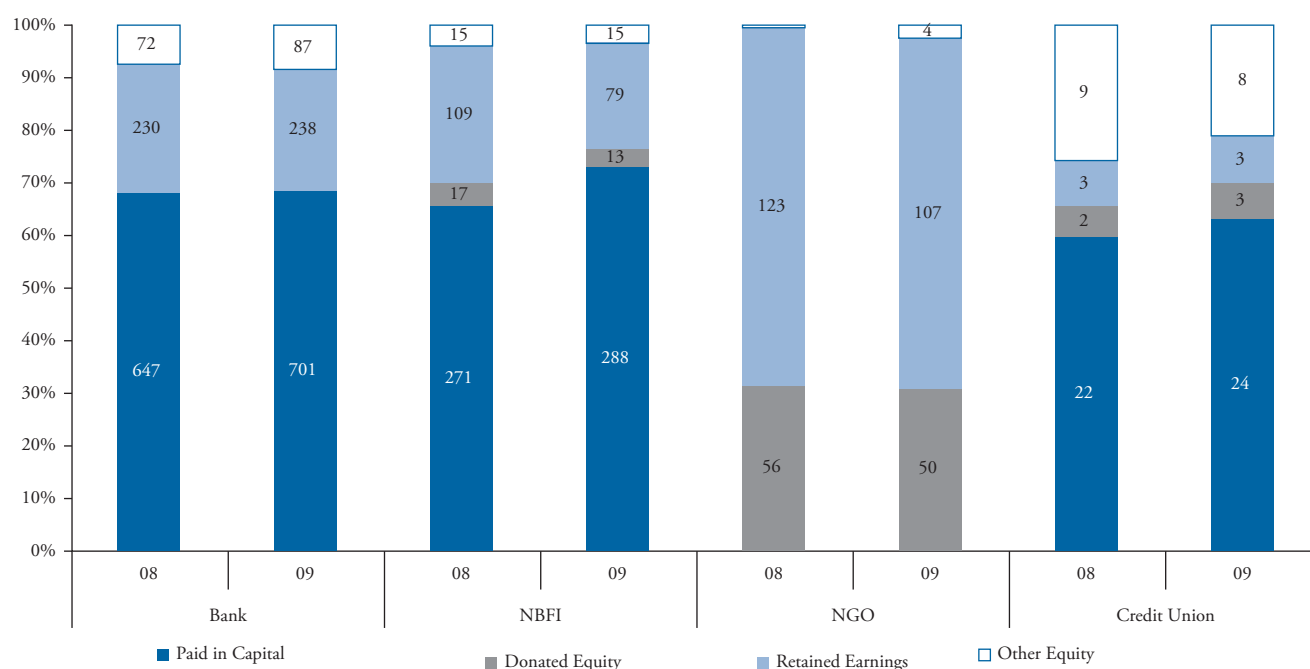
**Figure 11** demonstrates the decreasing role of donated equity, which constitutes only 4 percent of the total equity base of ECA MFIs, pertaining primarily to the equity structures of NGOs. Shareholder capital increased for both banks and NBFIs, but just five banks (all ProCredit Banks and the state-owned Mikrokreditbank in Uzbekistan) accounted for two-thirds of new equity investments.

## B. Cross-Border Funder Commitments and Trends in Outstanding Debt Financing

The microfinance industry in ECA is funded mainly by debt instruments, as demonstrated; 83 percent of debt outstanding in 2009 came from cross-border investors.

Therefore, understanding how cross-border investors adjusted their funding decisions in the aftermath

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**Figure 11** Trends in the Composition of Equity by Charter Type, 2008-2009

**Source:** MIX Market, 2008-2009. Data represent totals. Data labels represent corresponding amounts in USD mln.

understand their long-term horizon as well as the short-term realities of the funding landscape in ECA.

Table 6 Characteristics of Cross-Border Funders <sup>25</sup>		
	ECA	Global
Total Committed (million USD)	6,188	21,313
Growth (%)	22	17
Number of active funders	29 public funders	41 public funders
	11 foundations/NGOs	16 foundations/NGOs
	53 MIs	90 MIs

**Source:** CGAP Cross-Border Funding Surveys, 2010.

### At a Glance

As of December 2009, cross-border funders had committed close to US\$6.2 billion to microfinance in ECA, representing 29 percent of the total funding committed to microfinance globally, the largest share of all regions. ECA is the only region where public funding<sup>26</sup> grew faster than private funding<sup>27</sup> in 2009—by 26 percent (against 11 percent globally), while private funding grew by 14 percent (33 percent globally). Nevertheless, ECA still has a large inflow of private funding, receiving 30 percent of global funds. Fourteen DFIs active in the region represent 64 percent of total commitments to ECA; KfW and EBRD alone represent 42 percent.

- A vast majority of committed amounts (99 percent) are used to fund retail financial

<sup>25</sup> For the first time this year, we are presenting consolidated data from the CGAP Microfinance Funder Survey and the CGAP MIV Survey. To avoid double counting, CGAP made adjustments to both data sets. Therefore, these highlights cannot be compared to data and analysis from previous CGAP Funder and MIV Surveys without taking these adjustments into account.

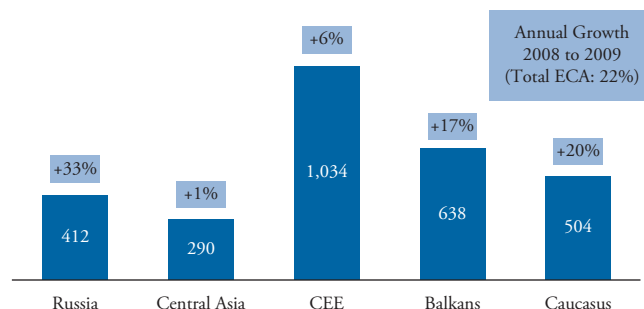


service providers, while capacity building funding continues to lag in ECA, with only US\$82 million committed, the smallest amount compared to other regions. Given persistent policy issues and lack of adequate market infrastructure, such as absence of national credit registries and limited foreign currency hedging tools, in many ECA countries it appears that this area deserves more funder attention.

- Structured finance (e.g., securitization, collateral debt obligations, convertible loans) is more widely used in ECA than in other regions; it represents 10 percent of direct commitments compared to less than 2 percent in other regions.
- ECA ranks first in terms of equity investments—DFIs invested US\$560 million in equity, 60 percent of which were to MIIs that reinvest in ECA in equity or debt and 40 percent directly into retail institutions.

The distribution of total funding commitments by subregion did not change, with CEE still having the largest portion, and Central Asia the smallest. As can be seen in **Figure 12**, the growth of funding in CEE and Central Asia was very modest; this decreased the respective portions of the total for these subregions.

**Figure 12** Commitments to ECA (USD mln), by Subregions and Annual Growth from 2008 to 2009



**Source:** CGAP Cross-Border Funding Surveys, 2010. Data represent total committed amounts in USD mln. Percentages labels represent the growth in committed amounts from 2008 to 2009.

highest growth rates of funding commitments were to Russia (in the form of a broad range of debt and equity investments in downscaling banks and MFIs), the Caucasus, and the Balkans.

Funder commitments to the region grew significantly despite negative growth at the level of MFIs. **Table 7** shows that commitments increased or remained stable in all countries except Kazakhstan (where EBRD no longer invests in downscaling banks), while the microlending portfolios dropped in 10 countries—particularly in

**Table 7** Commitments, by Country as of December 2009, and 2008-2009 Trends for Commitments and Loan Portfolio of Retail MFIs

	2009 Commitments, mln. USD	2008/2009 Growth	2009 Loan Portfolio, mln. USD	2008/2009 Growth
Albania	50 to 100	→	366	↑ 8%
Armenia	100 to 300	↑	390	↓ -32%
Azerbaijan	100 to 300	↑↑	588	↑↑ 22%
Belarus	50 to 100	→	68	→ 4%
Bosnia & Herzegovina	100 to 300	↑↑	833	↓ -17%
Bulgaria	300 to 500	→	640	→ 3%
Georgia	100 to 300	↑↑	454	↓ -5%
Kazakhstan	50 to 100	↓	1,343	↓ -7%
Kosovo	50 to 100	↑↑	830	↑ 25%
Kyrgyz	1.957	143.28	171.62	142.88

**Source:** Funding data are from CGAP Cross-Border Funding Surveys, 2010. Country allocation is available for 46 percent of ECA commitments. MFI data are from CGAP-MIX MFI Survey 2009, MIX Market, EBRD and WOCCU. Loan portfolio includes both retail and corporate loans.



Armenia, Bosnia and Herzegovina, Moldova, Montenegro, Russia, Tajikistan, and Ukraine. As mentioned earlier, contraction of the overall microlending portfolio for the sector was about 12 percent.<sup>28</sup> How can this be explained?

Funders report commitments, not disbursements, to the CGAP survey; commitments do not fluctuate in the same way as MFI portfolios. Commitments represent the cumulative amount of all active projects and investments, whether or not disbursed. For example, if a project entails disbursements of several tranches over five years, the full amount, not only the amount disbursed in the survey year, is counted as commitments. A closer look at new private funder commitments reveals that about 14 percent of additional funding did not reach the field, but rather created a liquidity surplus at the MII level. Most MIIs could not quickly adjust their instruments to fit the needs of struggling MFIs, nor could they accommodate the deteriorating performance profiles of MFIs in the midst of the crisis. Some MIIs even tightened their conditions in response to the crisis—thus making funding even less affordable.

As for public funder commitments, of the total US\$4.2 billion committed as of December 2009, only about US\$650 million was disbursed in 2009, with US\$500 million going directly to retail MFIs. Overall, most of the

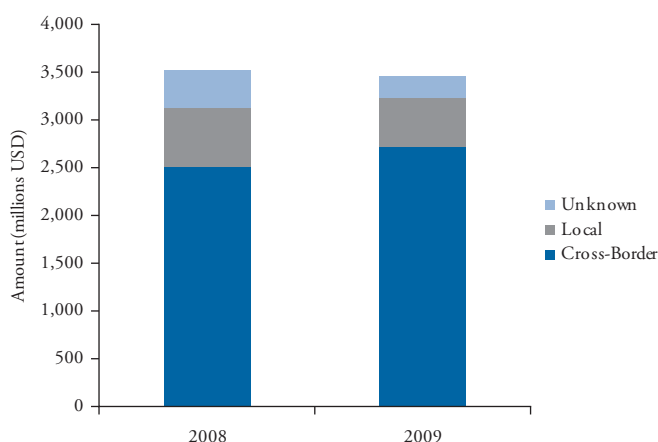
DFI funding was allocated to build on their existing large projects, and only a small part was dedicated to preventing liquidity shortages in the wake of the financial crisis.

us, even though total commitments grew, most of this funding was idle liquidity with MIIs—for which the volume of commitments increased significantly—and the funding available for the retail level did not materially change.

is confirmed by MIX Funding Structure Data, which contains information on the outstanding borrowings of MFIs from both local and cross-border investors. While total debt from local funders decreased in 2009, the portion of total debt from cross-border funders increased (see Figure 13).

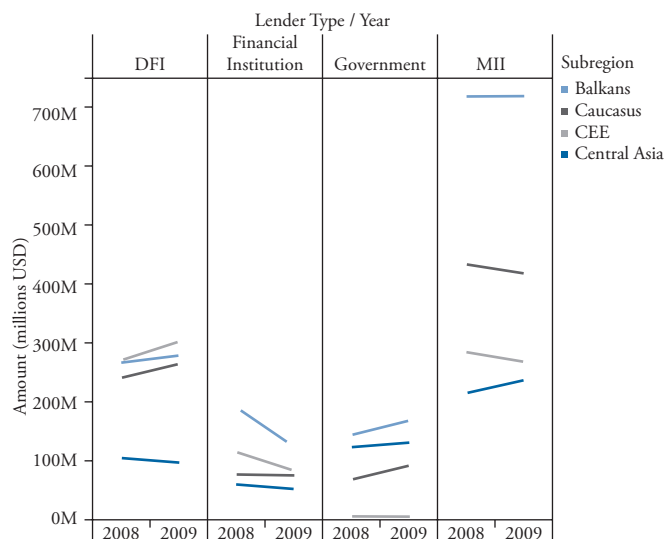
Trends in the funding landscape in the region show that the conventional wisdom about financing in times of crisis time holds true in the case of ECA microfinance. Purely commercial lenders, most often commercial banks, reduced their exposure to the sector (as many of them were also dealing with the effects of the crisis), while public investors' role in funding increased (see Figure 14). Debt from financial institutions decreased in every subregion and especially in the Balkans, where amounts outstanding were reduced by 35 percent to US\$123 million. is

**Figure 13** Trends in Outstanding Debt by Origin of Funder, 2008-2009



**Source:** MIX Funding Structure Data, 2008-2009. Data represent totals.

**Figure 14** Trends in Total Borrowings by Lender Types and Subregion, 2008-2009



**Source:** MIX Funding Structure Data 2008-2009. Results are totals. DFI = Development Financial Institution; MII = Microfinance Investment Intermediaries.

<sup>28</sup> Source: CGAP MFI Survey 2009, MIX, EBRD, and WOCCU.

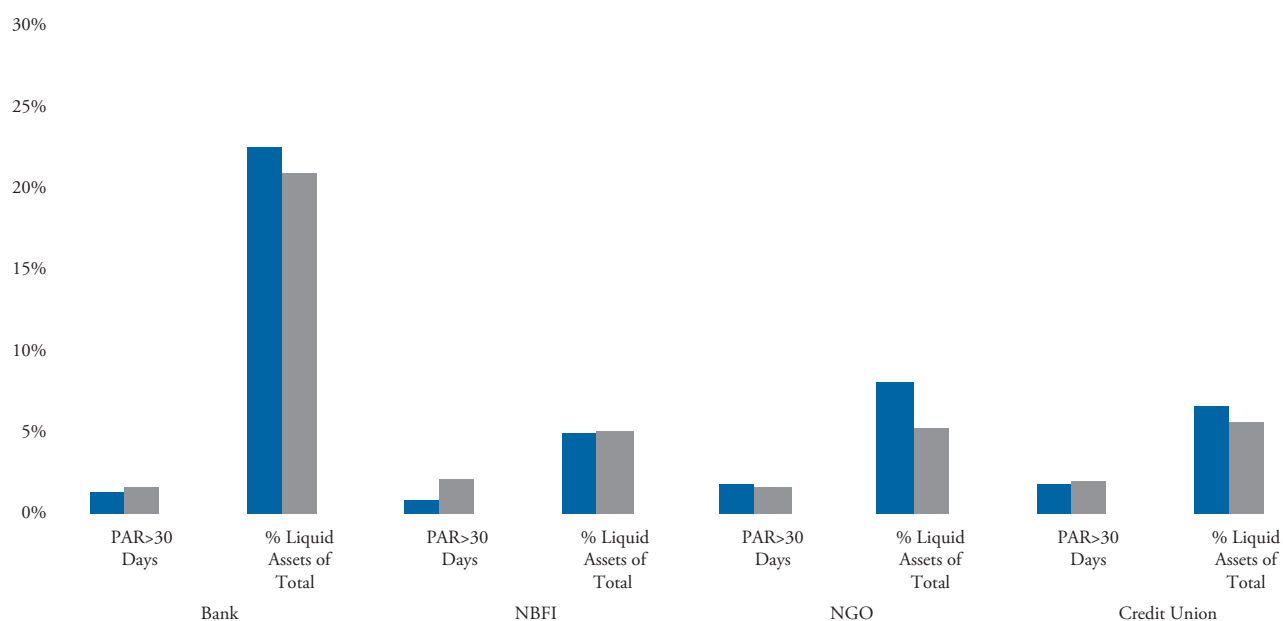
is due mostly to a change in the funding landscape in Bosnia and Herzegovina, where debt from commercial banks made up 19 percent of the total in 2008 versus 12 percent in 2009. Even though debt from banks was relatively long term, with a weighted average maturity of 34 months in 2008, close to half (US\$60 million) was due to be repaid in full in 2009. Indeed at the end of the year, local banks' portfolio in Bosnian MFIs had decreased by US\$56 million, demonstrating that hardly any of them wished to continue their exposure to the sector.

Debt financing from MIIs, which makes up almost half of funding in ECA, plateaued for most regions, increasing only in Central Asia (see **Figure 14**). As noted, MIIs had funds, but much remained as extra liquidity for two reasons: many MFIs seeking investment were too risky, while many investable MFIs did not have as much demand for funds as they were shrinking their portfolios or avoiding borrowing in hard currency due to foreign exchange risk (see **Box 1**). In contrast, funding from public funders, such as DFIs and governments (including both government institutions and bilateral agencies), increased on MFIs' balance sheets in almost every subregion. The Balkans and CEE—the two

markets most affected by the crisis—saw funding increase by 4 percent (US\$11 million) and 12 percent (US\$32 million), respectively. The increase of 9 percent (US\$21 million) in the Caucasus was due primarily to debt financing to the large banks in Azerbaijan, Armenia, and Georgia.

At the end of 2009, excess liquidity was a problem not only for MIIs, but also for MFIs. Generally, debt in ECA is fairly long term—about four years on average (even debt from banks had an average term of 24 months in 2008). At least 11 percent (or US\$453 million) was due to be repaid in full in 2009. MFIs were able to raise a similar amount throughout 2009. While cross-border disbursements dried up in the early months of 2009 and MIIs had excess liquidity, by the end of the year ECA MFIs themselves were overly liquid, with the nonearning liquid assets ratio doubling from 7 percent in 2007 and 2008 to 13 percent in 2009. **Figure 15** demonstrates a connection between rising risk levels and increasing liquidity. As delinquency shot up, many MFIs preferred to curb new disbursements and keep a greater portion of their assets as cash equivalents. Credit unions appear to be an exception—probably a result of the withdrawal of members' contributions.

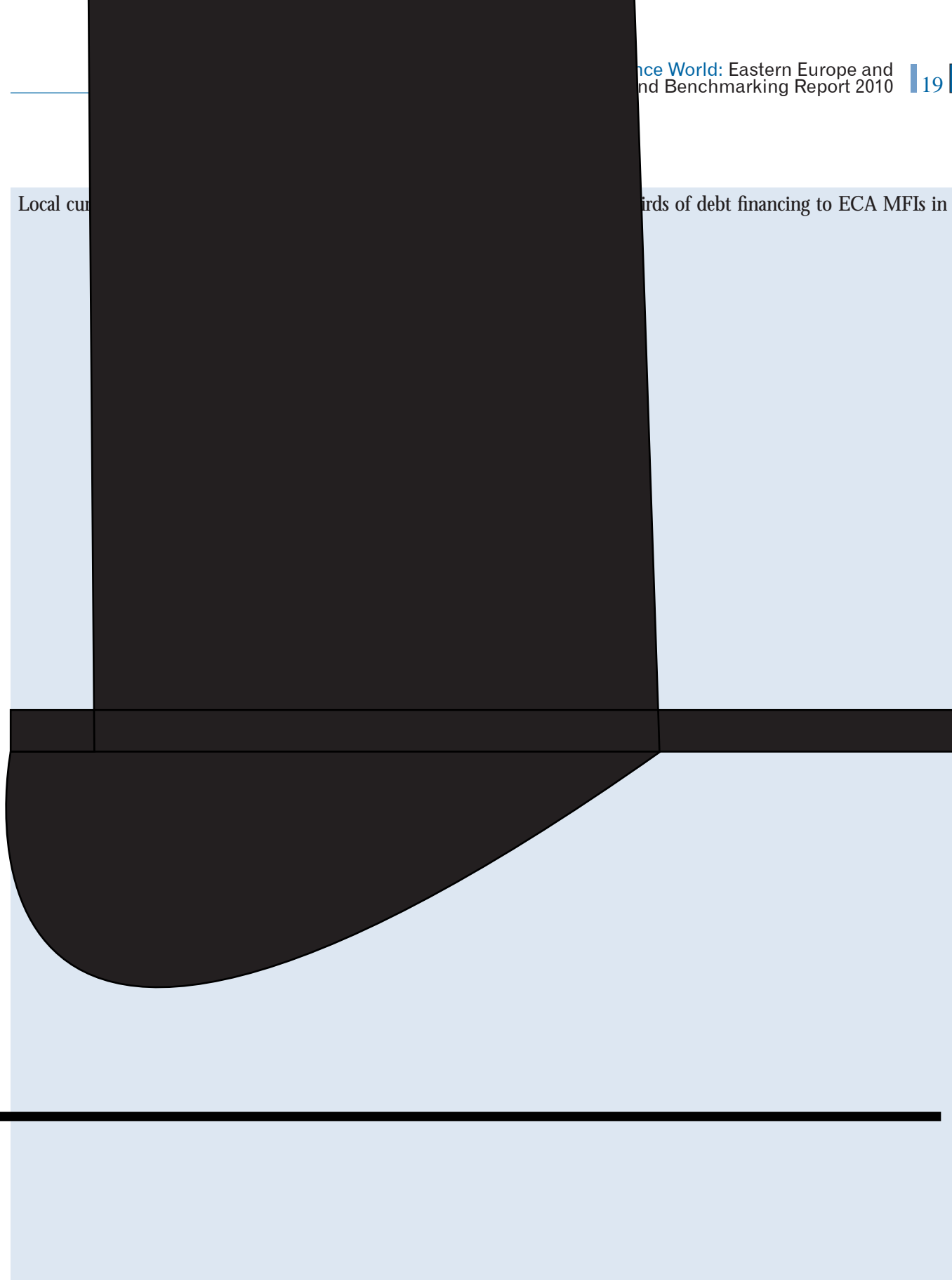
**Figure 15** Portfolio at Risk over 30 Days and Percentage of Nonearning Liquid Assets of Total Assets, by Charter Type, 2007-2009

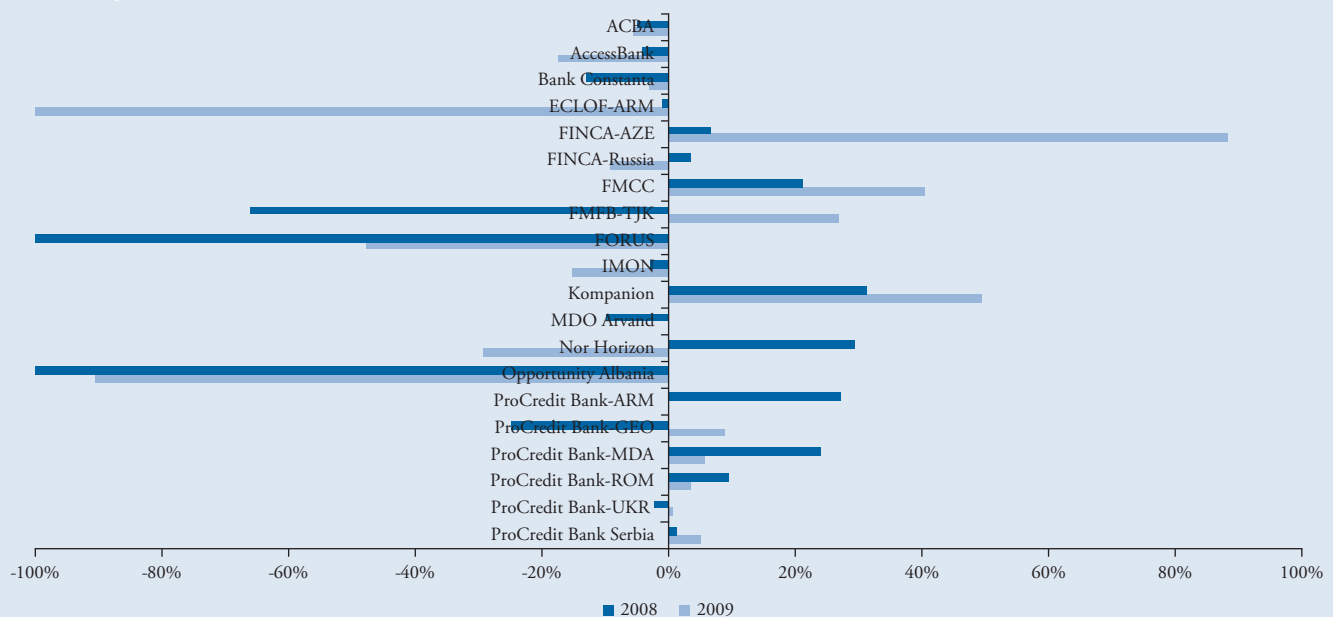


**Source:** MIX Market, 2007-2009. Data represent medians.

Local cur

ards of debt financing to ECA MFIs in

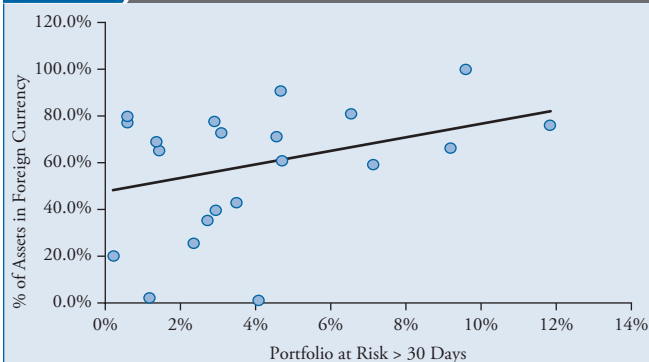


**Figure B** Net Foreign Currency Exposure for Selected ECA MFIs, 2008-2009

**Source:** MIX Market 2008-2009. Data represent totals.

**Note:** Foreign Currency Exposure is defined as (Total Assets in Foreign Currency – Total Liabilities in Foreign Currency)/Total Equity.

**Figure C** demonstrates a clear positive relationship between portfolio at risk and the percentage of assets in foreign currency (assuming the portfolio is the largest asset of an MFIs). For example, IMON International in Tajikistan, for which foreign exchange losses constituted 11 percent of its net income in 2009, found that the most significant determinant of higher incidence of delinquent loans was the currency in which the loan was issued. The portfolio at risk for Tajik somoni-denominated loans was 0.5 percent versus 4 percent for USD-denominated loans. In 2010, the MFIs decreased the percentage of the portfolio in indexed loans from 78 percent to 70 percent, which, other things being equal, corresponds to a decrease of 0.25 percent in portfolio at risk.<sup>30</sup>

**Figure C** Correlation between Foreign Exchange Risk and Credit Risk, 2009

**Source:** MIX Market, 2009. Data represent percentages of total assets and total portfolio.

Cross-border investors also began to explore ways to alleviate foreign exchange risk for MFIs in ECA. Many fund managers and DFIs are reluctant to have open currency positions, but the alternative of MFIs passing on the risk to end clients as indexed loans is not desirable either as credit risk is likely to rise and the MFIs may suffer reputation risk due to nontransparent costs associated with their products (assuming local currencies depreciate relative to hard currencies). Consequently, to mitigate foreign exchange risk, investors have started to work with MFIs to mobilize the expertise of intermediaries such as MFX Solutions (a microfinance-dedicated currency hedging facility) and TCX (a special purpose fund providing market risk management products to its investors to hedge currency risk.)

<sup>30</sup> See presentation “IMON International’s Experience” under Managing Risks Track at 2010 SEEP Annual Conference Session Materials. <http://seepnetwork.org/Pages/AC2010/SessionMaterials.aspx>

## Financial and Social Performance of Retail MFIs

### A. Financial Performance

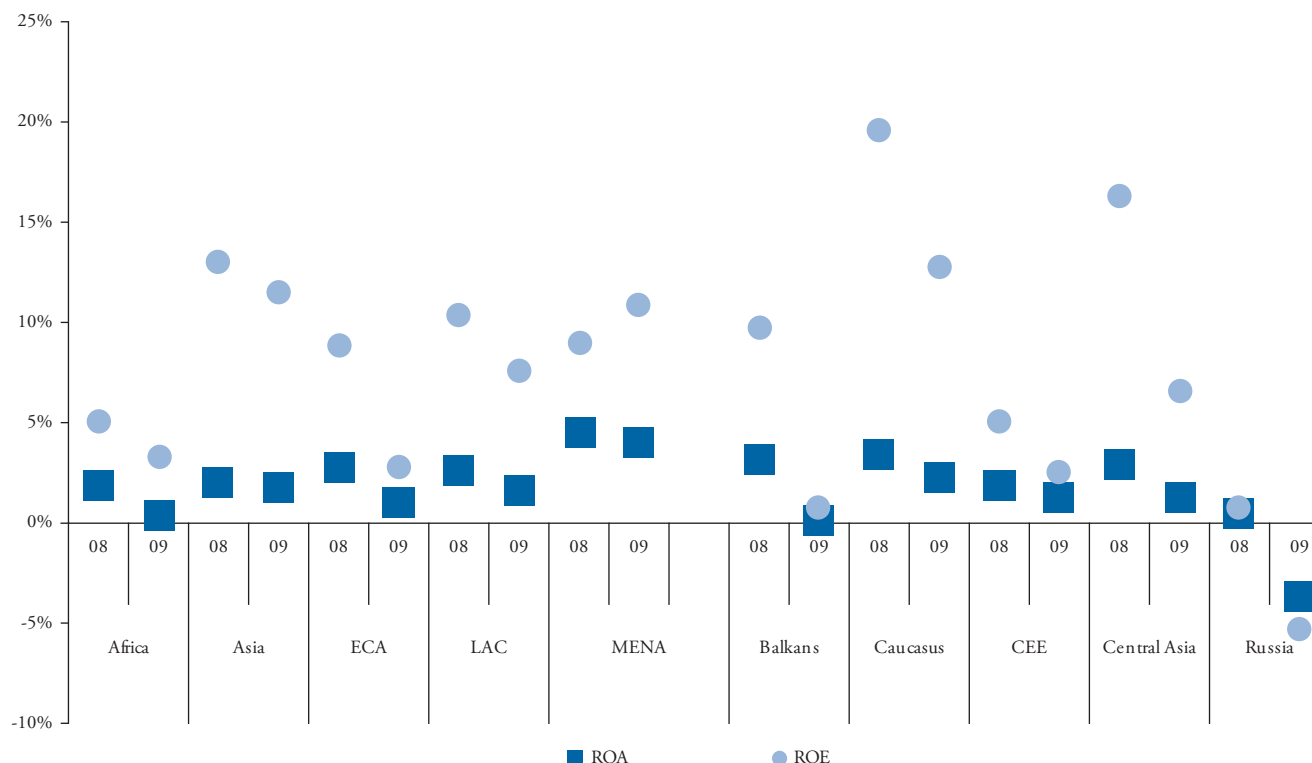
#### Key Issues and Trends

- High credit risk resulted in the doubling of impairment loss expenses, lower revenues, and negative returns.
- Credit risk more than doubled across subregions in 2009. Data from 2010 indicate that high delinquency continued to be an issue, although portfolio at risk levels in Bosnia and Herzegovina have started to decline in recent months.
- Operating expenses were lower in 2009 than in 2008 as a consequence of decreasing personnel expenses, even while the number of staff remained stable.

MFIs with large volumes of delinquent loans had lower revenues due to unrecovered repayments and increases in loan loss provision expenses, finishing the year with barely breakeven or negative bottom lines. As **Figure 16** demonstrates, in 2008 the microfinance sector in the ECA region was one of the more profitable globally, whereas in 2009, return on assets and equity were among the lowest. On the subregional level, returns diminished everywhere, with the most dramatic drops experienced in the Balkans (driven by Bosnia and Herzegovina, where 10 out of 13 MFIs were unprofitable) and Russia.

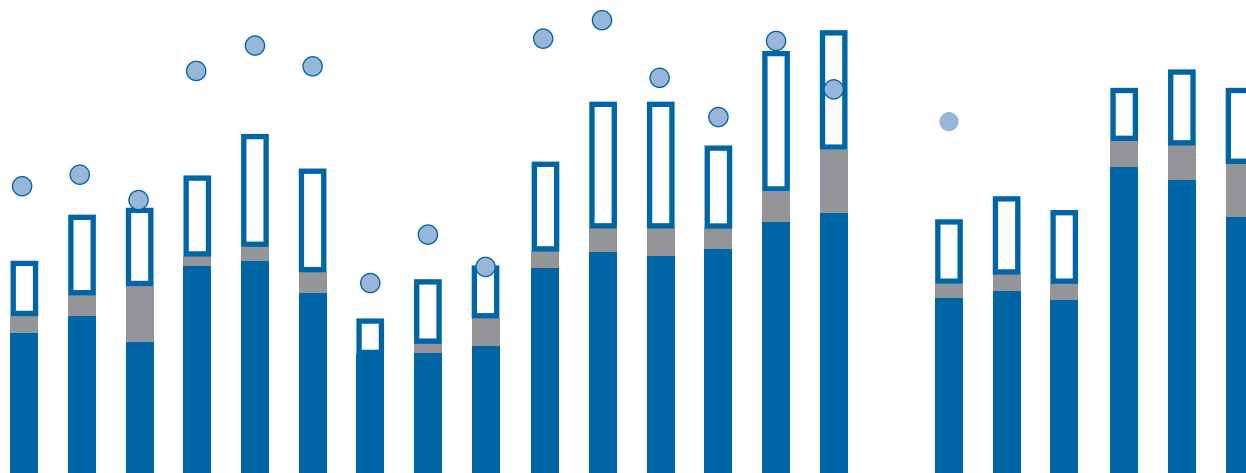
Analysis of returns shows that lower revenues and higher impairment loss expenses squeezed margins, while financial and operating expenses stayed the same or decreased (see **Figure 17**). A decrease in revenues across the sector was due to a combination of lower repayment rates as well as a higher percentage of nonearning liquid assets. In 2008, loan portfolios were 88 percent of total assets, but in 2009 this decreased to 80 percent.

**Figure 16** Trends in Adjusted Return on Assets (ROA) and Adjusted Return on Equity (ROE), by Global Region and ECA Subregion, 2008-2009



**Source:** MIX Market 2008-2009. Data represent medians.

Figure 17 Composition of the Return on Assets Indicator, by Subregion and Sustainability, 2007-2009

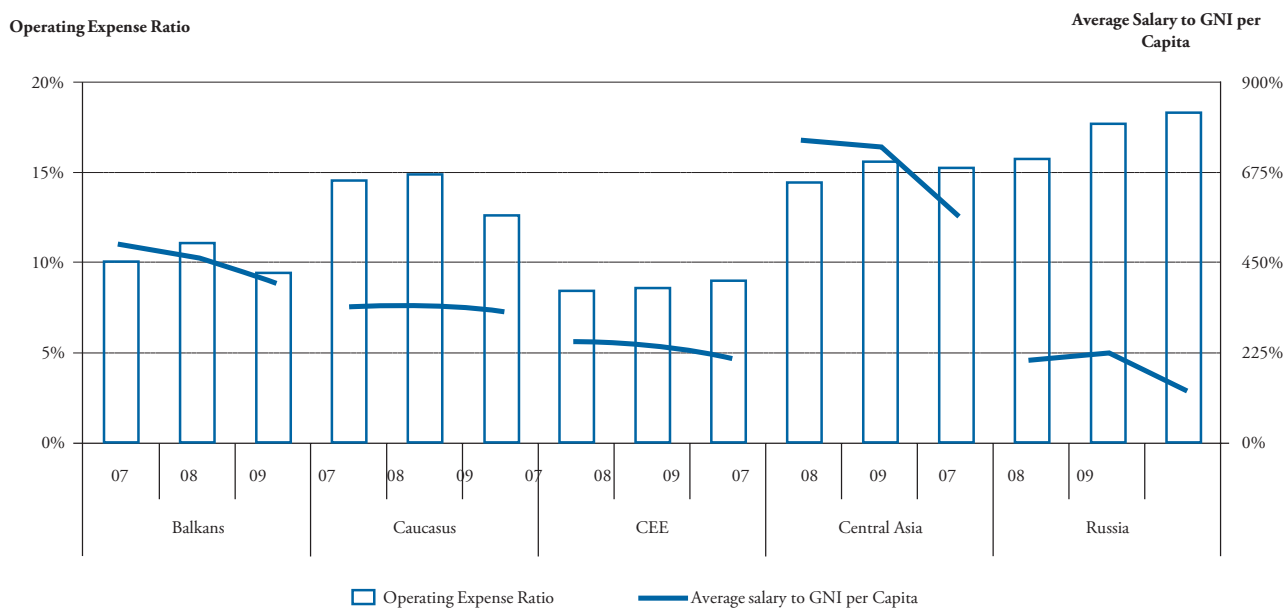


**Source:** MIX Market 2007-2009. Data represent medians.

Financial expenses remained at similar levels to 2007, demonstrating that even in an advanced market such as ECA the cost of funding does not adjust quickly to rising risk levels.

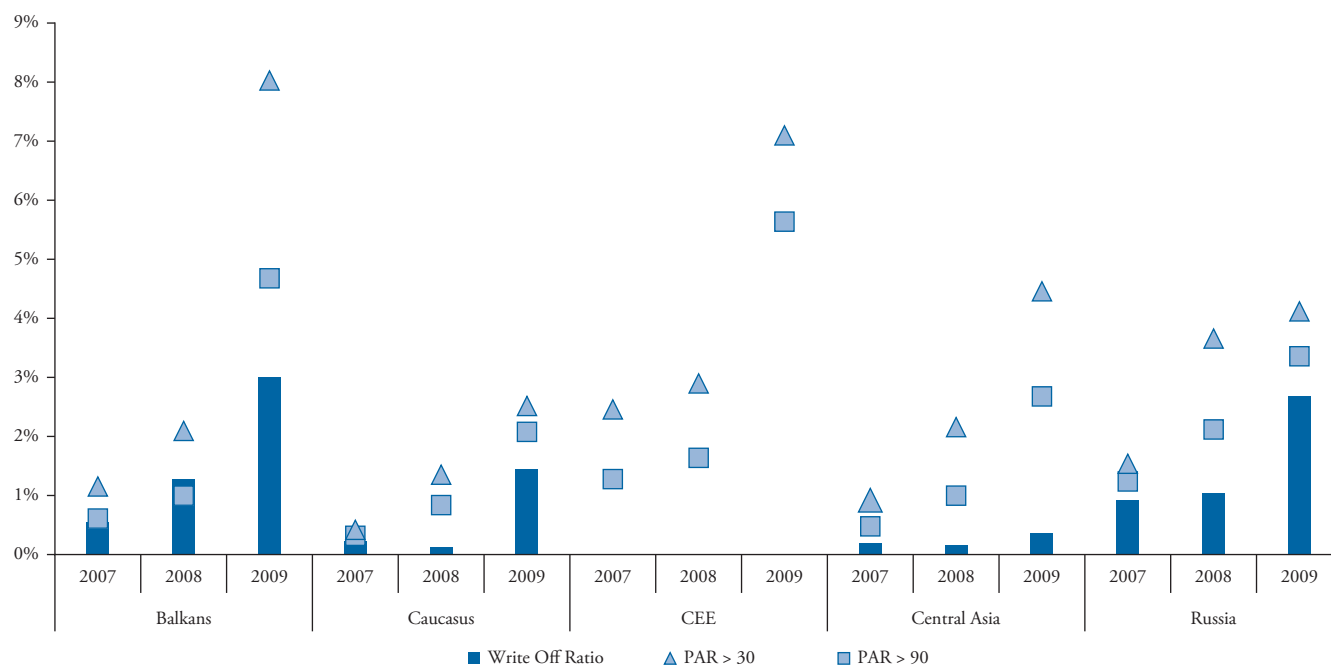
Many MFIs, especially in the Balkans and the Caucasus, reduced operating expenses in 2009. A decrease in personnel expenses, which make up the larger part of operating costs, was the main driver behind this. Salaries as a percentage of gross national income (GNI) per capita decreased (see **Figure 18**), with sharp downward movements in the Balkans, Central Asia, CEE, and Russia. As reporting on social performance indicators demonstrates (see Social Performance section) since incentives are often aligned with growth and portfolio quality metrics, it is likely that monetary incentive-based compensations were reduced in this challenging year of negative growth and high delinquency.

**Figure 18** Operating Expense Ratio and Average Salary to GNI per Capita, by Subregion and Charter Type, 2007-2009



**Source:** MIX Market 2007-2009. Data represent medians.

**Figure 19** Trends in Delinquency and Risk Coverage Ratios, by Subregions, 2007-2009



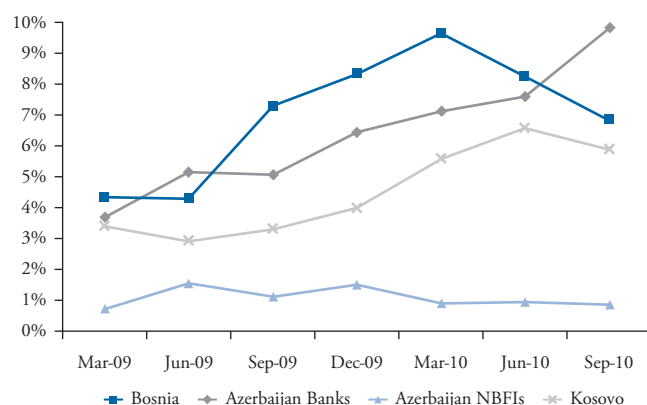
**Source:** MIX Market 2007-2009. Data represent medians.

trend MFIs are monitoring closely, especially in relation to concerns about cross-indebtedness with other MFIs and downscaling banks.

Quarterly data for 2010 indicate that portfolio-at-risk levels were still on the rise for most of the year, though there are some encouraging trends. In Bosnia and Herzegovina in the second part of the year, delinquency began to decrease, although it was still much higher than March 2009 levels. In Azerbaijan, NBFIs were able to maintain good portfolio quality, but portfolio at risk of their competitors, downscaling banks, is much higher and may be indicative of future challenges for the sector. However, it also demonstrates that providers wholly dedicated to microfinance in this particular market exhibit better risk profiles than banks that have product lines for microlending within larger portfolios. Risk was also rising in Kosovo (due to a combination of increasing market saturation and a lagging effect of decreased remittances from Western Europe, which are often critical to loan repayments at a household level). Similarly to Bosnian MFIs, Kosovo MFIs began to reduce portfolio-at-risk levels in the latter half of 2010. It is a positive trend that nonbank providers in these three markets exhibited downward credit risk trends in 2010, which may signal sector recovery.

Figure 20

Quarterly Trends in Portfolio at Risk > 30 Days for Azerbaijan, Bosnia and Herzegovina, and Kosovo, March 2009–September 2010



Source: AMFA for Azerbaijan, AMFI for Bosnia and Herzegovina, AMIK for Kosovo.

## B. Social Performance<sup>31</sup>

### Key Issues and Trends

- A majority of ECA MFIs have identified social performance as a component of their institution's strategic plan.
- Poverty alleviation is a common development goal. However, poverty outreach is not a commonly tracked indicator, and only a small proportion of ECA microfinance clients are below the poverty line.
- ECA MFIs demonstrated good alignment between their operations and mission regarding outreach to rural clients. However, there is still a large unmet demand in rural and remote sections of countries.
- Good practices have emerged in terms of implementation of consumer protection policies, especially those regarding policies on preventing over-indebtedness and training staff on client protection.

### 1. Translating Social Mission in Measurable Outcomes

Social performance measures how well an institution translates its social mission into practice.<sup>32</sup> For the first time in the series of this report we are delivering consolidated results for social performance indicators of ECA MFIs. The following analysis provides a first look into the social goals of ECA MFIs and how well they are able to report on these goals.<sup>33</sup> The data show many MFIs still have difficulties reporting on the actual outcomes related to their mission. This is work in progress.

<sup>31</sup> According to the Social Performance Task Force (<http://sptf.info/>), social performance, or the social bottom line, is about making an organization's social mission a reality. This may include serving larger numbers of poor and excluded people; improving the quality and appropriateness of financial services; creating benefits for clients; and improving social responsibility of an MFI.

<sup>32</sup> Retail providers with a double or triple bottom line have an explicit social mission that they strive to translate into results at the client level (e.g., people's empowerment, reducing vulnerability, poverty alleviation, job creation, and economic development). They are committed to protect clients, to behave ethically, and to positively effect change in client's lives. Social performance reporting measures how well providers translate their social mission into policies, systems, and practices in outcomes and concrete results on the ground.

<sup>33</sup> As of 31 January 2011 social performance indicators are available on the MIX Market profile of each MFI that reports.



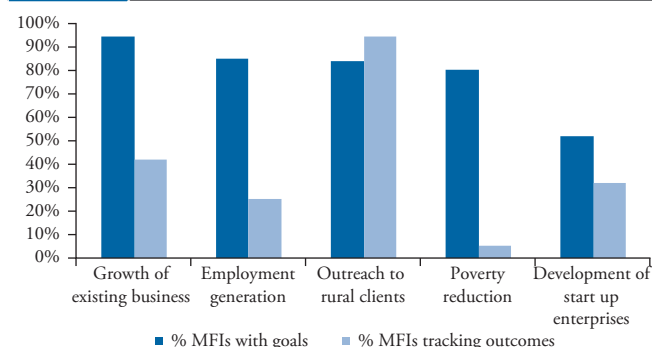
A majority of the 81 ECA MFIs reporting on social performance are NBFIs (68 percent), followed by banks and NGOs (14 percent), and cooperatives (4 percent). Banks appear considerably under-represented in the sample. Banks serve 47 percent of total borrowers (both corporate and retail) in the region, as reported to MIX Market, but those reporting on social performance represent a far lower percentage. The two countries with the highest rates of reporting are Azerbaijan and Tajikistan. In these countries, strong national associations support MFIs, while international investors, who provide 70 to 80 percent of debt financing in the areas in question, further incentivize reporting.

Social performance reporting reveals that there is work still to be done to track how actual outcomes align with MFI missions. Ninety-four percent of the MFIs reporting from ECA list “growth of existing business” as a development goal and indicate a strong focus on low-income clients. However, less than half of these same MFIs were able to report the number of enterprises financed during the past two years, and only 26 percent track employment in financed enterprises.

Similarly, less than a third of the MFIs in the sample were able to report on poverty statistics, even though a majority cited poverty alleviation as a development goal. Eighty-four percent of MFIs stated that their target market is low-income clients, although less than half specifically target the poor. This limited focus on targeting seems to contradict the fact that poverty alleviation is one of the top development goals reported by MFIs. Furthermore, a mere 17 percent mention the poor in their mission statement.

The 25 MFIs that reported on poverty outreach figures show a median of 8 percent of clients below national poverty lines. Six of the MFIs reporting poverty outreach figures were FINCA affiliates using FINCA’s Client Assessment Tool (FCAT), an index that documents expenditures on six social metrics: household food security, health care, housing, education, empowerment, and social capital.<sup>34</sup> Data for MFIs using FCAT show a median of 5 percent of clients below the national poverty line and 4 percent below the US\$2 a day poverty line. Almost none of the

Figure 21 Development Goals and Outcomes Tracking



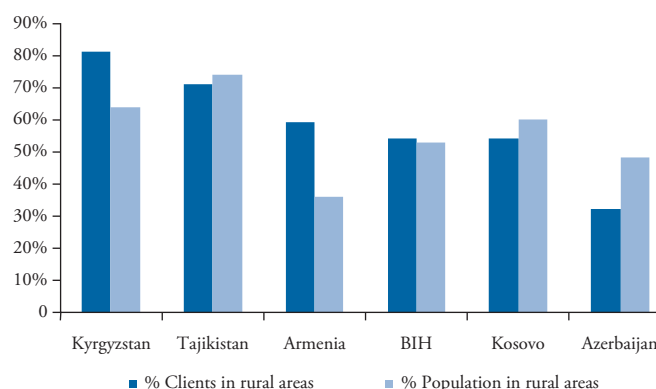
Source: MIX Market, 2008-2009.

**Note:** MFIs tracking outcomes refers to the ability of reporting indicators related to the development goals. In the case of “poverty reduction” it refers to the ability of MFIs to report the number of clients who are above the poverty line after three years in the program.

MFIs in ECA was able to report changes in the poverty status for their clients.

ECA MFIs demonstrated better alignment between their operations and their mission regarding outreach to rural clients<sup>35</sup> (see Figure 22). Twenty-eight percent of MFIs reported having branches where there are no other financial institutions, and clients served in these areas are only 3 percent of total clients.

Figure 22 Outreach to Clients in Rural Areas

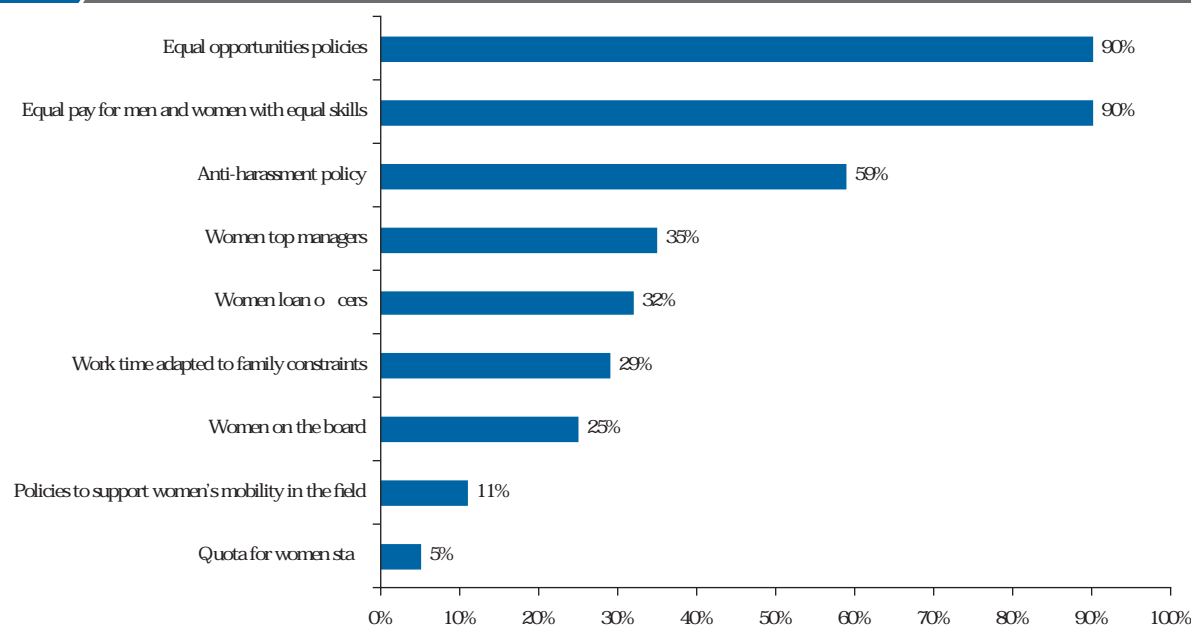


Source: MIX Market, 2009. Data represent medians.

<sup>34</sup> For more information on FCAT, visit [www.finca.org](http://www.finca.org).

<sup>35</sup> Outreach to rural clients refers to settled places outside towns and cities, such as villages and hamlets, where most livelihoods are farm-based.

Figure 23 Gender Dimension of MFIs



**Source:** MIX Market, 2009. Results show percentage of MFIs with gender development goals.

Compared to the distribution of countries' populations in rural and urban areas, MFIs that reported on their outreach in rural areas have relatively more clients in rural areas than the average population in Kyrgyzstan and Armenia. However in the other countries we do not see this bias from the figures.

*Gender-oriented goals* are not prominent among ECA MFIs: only half reported "gender equality" as a development goal, and women represent a relatively small proportion of clients (42 percent) compared to other regions.<sup>36</sup> Thirty-two percent of MFIs reported offering some form of women's empowerment service<sup>37</sup> beyond financial services.

The tendency in ECA not to prioritize gender development goals is reflected in the human resource structure of MFIs. Although the vast majority of human resource policies promote equal opportunities, women appear

under-represented in senior management positions (Figure 23).

## 2. Policies and Procedures in Place to Manage Social Performance

Most ECA MFIs are establishing policies and procedures to manage their social performance that include social responsibility to staff, to clients, and to the community. In fact, the majority of MFIs reported that social performance issues have been identified as components of their institution's strategic and business plans, and 70 percent perform some sort of training on social performance topics. The most common training topics are mission orientation, development goals, over-indebtedness prevention, and communication with clients about prices.

Establishing a social performance committee is only a first step, however, as few MFIs (11 percent) have established a standing social performance committee that regularly reviews social performance issues.

Staff incentive schemes in ECA mainly reward portfolio quality and the ability to attract new clients, while only 24 percent reward staff on the basis of quality interaction with clients. Average staff turnover is

<sup>36</sup> Data for fiscal year 2009 across regions show that women borrowers represent a median of 62 percent of borrowers in Latin America, 89 percent in Asia, 64 percent in Africa, and 56 percent in Middle East and North Africa.

<sup>37</sup> Women's empowerment services specifically identified in the social performance standards report are as follows: business training for women, leadership training, women's rights education, and counseling for women—victims of violence.

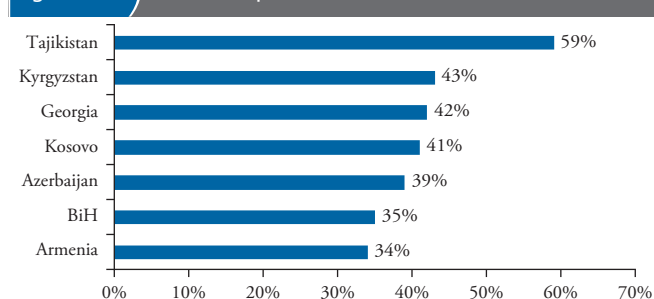
16 percent, and a majority of staff are permanent. Overall, MFIs report responsible human resources practices, the majority of which include practices to ensure staff safety, a clear salary scale based on market salaries, pension contribution, and anti-discrimination policies.

Client dropout rates<sup>38</sup> in the region were 36 percent in 2009, and the majority of MFIs in Armenia, Bosnia and Herzegovina, and Kyrgyzstan reported having clients who were also borrowing from other institutions (see Figure 24). Around 40 percent of ECA MFIs reported regularly monitoring client exit and most of them use interviews of exiting clients for market research purposes. The great majority of MFIs also reported using market research to identify the needs of clients and potential clients.

Overall, MFIs reported paying considerable attention to consumer protection principles, especially those regarding

policies on preventing over-indebtedness and training of staff on client protection. Fifty-one institutions in the region have endorsed the Smart Campaign. However, only 20 percent of the MFIs reporting have all the consumer protection principles in place.

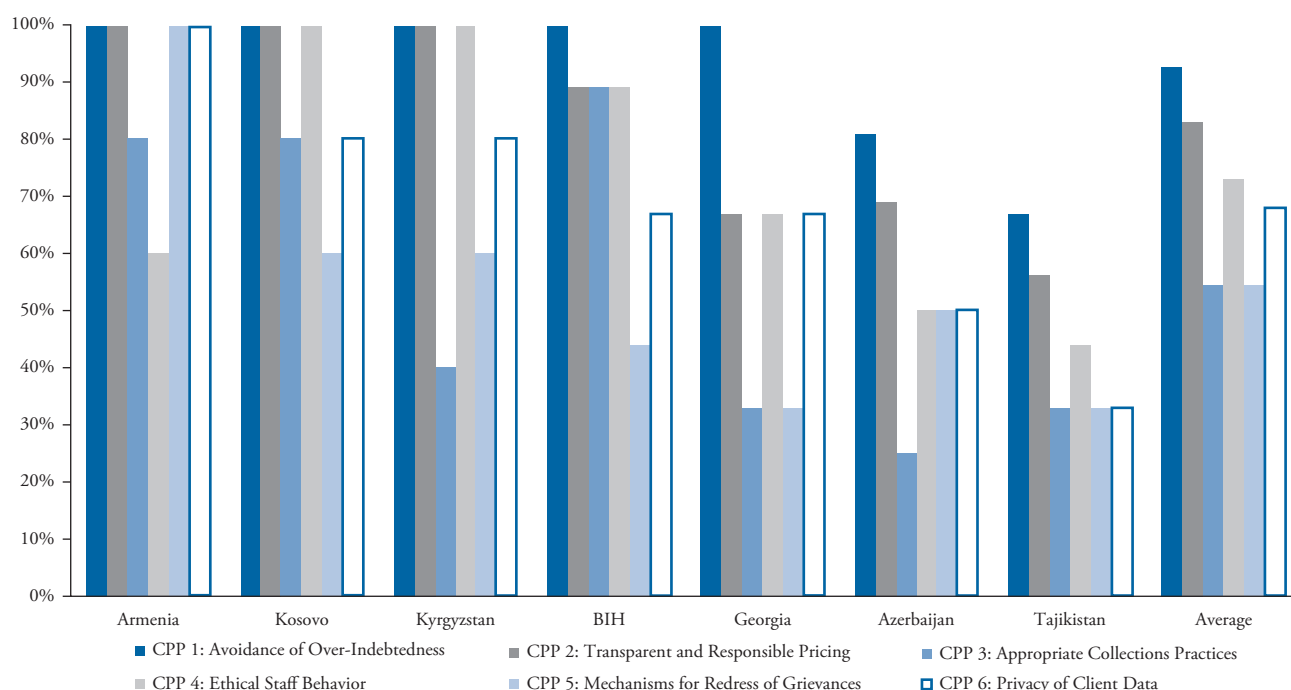
Figure 24 Client Dropout Rate, 2009



Source: MIX Market, 2009. Data represent medians.

Figure 25 Consumer Protection Principles (CPP) in Select ECA Countries

% of MFIs with CPPs



Source: MIX Market, 2009. Data represent averages.

<sup>38</sup> The formula used to calculate dropout rate is (clients at beginning of the period + new clients - clients at the end of the period)/clients at the beginning of the period.

A loan approval process that evaluates borrower repayment capacity is the most popular measure that MFIs reported using to address potential over-indebtedness. Nevertheless, only 39 percent of MFIs offer financial education for clients, and only half have established a mechanism to handle client complaints or have a code of ethics that spells out acceptable and unacceptable debt collection practices. Where credit bureaus do not exist for MFIs, such as in Azerbaijan, MFIs exchange information among themselves to verify clients' indebtedness (see also the Policy Environment section). As previously highlighted, regulatory reforms can play an important role in preventing over-indebtedness, and the implementation of consumer protection and consumer financial education and the establishments of a Central Credit Registry with mandatory reporting requirements are all important steps that several countries in the region are already undertaking.

Just as social performance management and reporting is on the rise in the industry as a whole, ECA MFIs are demonstrating an increasing commitment to tracking and reporting social performance data in an effort to know their customers better and to assess how effectively they are serving them. In addition to taking some financial performance management steps, such as reducing their dependency on hard currency loans and prioritizing portfolio quality over growth, that MFIs have undertaken as a response to the economic crisis, MFIs are also starting to adapt their internal policies and systems to better track social performance indicators, creating specific positions for managing social performance topics, and using social audits to better assess the management of their organizations.

## Looking Ahead

The year 2009 was marked by significant challenges in the ECA microfinance sector, which was hit the hardest of all regions worldwide as a result of financial and economic crises. Microfinance loan portfolios contracted across the region, and MFIs' financial performance deteriorated. MFIs in ECA showed the lowest profitability indicators

worldwide and the worst portfolio quality since the inception of the sector.

Despite the negative trends outlined, the crisis highlighted several important developments that hold promise for recovery:

- Even though microloan portfolios contracted, savings were resilient and even grew—proving their reliability as a domestic funding source.
- The financial inclusion agenda among policy makers was reinforced, with the topics of consumer protection and consumer financial education, as well as responsible and ethical finance, coming to the forefront.
- Funders increased their commitments to the region, though funding distribution and instruments have not yet been adjusted to the new realities of the sector.
- Finally, improved social performance management and indicator tracking will undoubtedly help MFIs in the region deal with some of the new risks and challenges that have emerged as a result both of the crisis and the maturing of the sector.

How long will it take for the sector in ECA to return to its precrisis state? What lessons will MFIs learn from the crisis, and will they come out of it stronger than before? Which types of institutions will fill the niche of the banks withdrawing from microfinance, and will some banks return? How will funders accommodate for the changing needs of the sector? Will policy measures taken in response to the crisis yield the results desired? All of these issues will be subject of our further research.

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## Data and Data Preparation

Five different data sets are drawn on to present the analysis of the microfinance sector in this report:

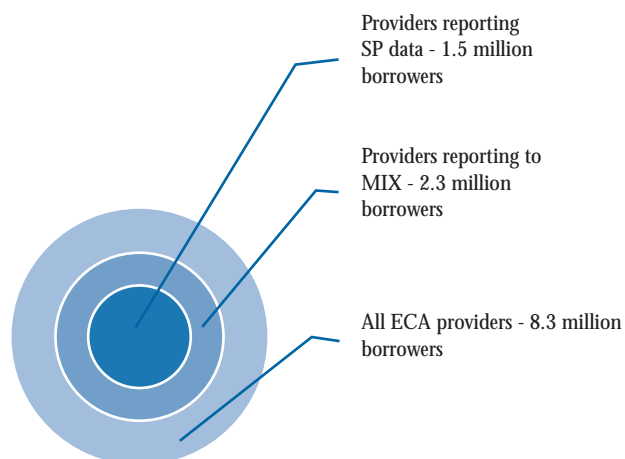
- CGAP-MIX 2010 MFI Survey: Covering over 8,200 institutions in the region. Given the large sample size, this survey contains only basic volume data, such as the number of borrowers and savers and loan portfolio size. This data set provides the most complete landscape description of microfinance in the ECA region in 2009, drawing on data from associations, regulators, donors, and publicly available data to compile aggregate statistics for all types of microfinance providers.
- CGAP 2009 Microfinance Funder Survey data: Conducted annually, this survey provides market intelligence to the industry on the microfinance portfolio of leading donors and investors.
- MIX data set for 217 MFIs in 2009 and a balanced panel data set of 122 MFIs for 2007-2009. These institutions were selected based on their ability to provide transparent, detailed reporting. The report

analyzes this sample to review trends in outreach and scale and in financial performance. For benchmarking purposes, MIX collects and prepares MFI financial and outreach data according to international microfinance reporting standards. Raw data are collected from the MFI, inputted into standard reporting formats, and cross-checked with audited financial statements, ratings, and other third-party due diligence reports, as available. Performance results are then adjusted, using industry standard adjustments, to eliminate subsidy, guarantee minimal provisioning for risk, and reflect the impact of inflation on institutional performance. This process increases comparability of performance results across institutions.

- MIX Funding Structure Database for 2009: One-hundred-and-forty MFIs provided detailed information on their individual borrowings, including source, original currency, beginning and maturity date, and interest rate of the loan. While each MFI's information is confidential, MIX creates aggregate analysis on the types of lenders, cost, and maturity of retail debt in ECA.
- MIX social performance data collection: The report assesses the various aspects of social performance management as reported by 81 MFIs (out of 217) from ECA to MIX in 2008 and 2009. It provides a framework for analyzing the current state of social performance practice in the region, based on the social performance indicators selected by the Social Performance Task Force and highlights current challenges in data collection and reporting.

Together, these data sets represent the most detailed and comprehensive collection of financial performance, outreach, product line, and funding structure information for MFIs in the region. The performance of the sample analyzed in this report is overall representative of the general trends in Eastern Europe and Central Asia, as the sample of 217 MFIs covers 60 percent of the total loan portfolio for ECA as presented in **Table 3**, with

Figure 26 Number of Borrowers in Data Sets on MFIs, mln



100 percent coverage for microfinance banks and 74 percent coverage of NBFIs and NGOs. The relationships among the MFI data sets are presented in **Figure 26**. Data for all of the individual institutions included in the report are publicly available online and regularly updated at [www.mixmarket.org](http://www.mixmarket.org).

**For definitions of MIX indicators and ratios visit** <http://www.themix.org/sites/default/files/Indicator%20Definitions.pdf>

**To see the data of individual MFIs analyzed in this report, visit** <http://www.mixmarket.org/mfi/region/Eastern%20Europe%20and%20Central%20Asia>

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## ANNEX II: Benchmarks

### Eastern Europe and Central Asia Benchmarks

Year (All figures are "medians")	2009 ECA	2009 Balkans	2008 Balkans	2007 Balkans	2009 Caucasus	2008 Caucasus	2007 Caucasus
<b>INSTITUTIONAL CHARACTERISTICS</b>							
Number of MFIs	189	33	33	33	28	28	28
Age	9	10	9	8	10	9	8
Total Assets	5,581,701	49,257,139	50,435,740	39,025,663	18,558,920	16,583,335	9,472,712
Offices	7	22	22	20	9	11	10
Personnel	38	148	148	121	159	156	123
<b>FINANCING STRUCTURE</b>							
Capital/Asset Ratio	27.3%	22.7%	24.8%	27.0%	24.3%	23.5%	23.7%
Debt to Equity	2.66	3.41	3.03	2.71	3.11	3.29	3.23
Deposits to Loans	0%	0%	0%	0%	0%	0%	0%
Deposits to Total Assets	0%	0%	0%	0%	0%	0%	0%
Portfolio to Assets	82.0%	85.4%	91.8%	90.3%	80.5%	86.1%	83.8%
<b>OUTREACH INDICATORS</b>							
Number of Active Borrowers	2,386	14,900	12,863	12,403	11,504	10,687	9,422
Percent of Women Borrowers	40.3%	42.3%	41.2%	39.0%	35.1%	40.1%	42.4%
Number of Loans Outstanding	247,900.0%	14,900	13,320	12,709	11,509	10,690	9,422
Gross Loan Portfolio	3,819,853	42,423,194	41,314,440	36,383,126	12,669,561	13,735,320	8,084,041
Average Loan Balance per Borrower	2,037	2,343	2,679	2,444	1,157	1,122	980
Average Loan Balance per Borrower/GNI per Capita	61.7%	73.0%	69.8%	71.2%	33.5%	38.8%	37.6%
Average Outstanding Balance	1,971	2,343	2,521	2,444	1,131	1,052	980
Average Outstanding Balance/GNI per Capita	58.1%	65.0%	65.9%	64.8%	79.8%	72.7%	78.9%
Number of Voluntary Depositors	0	0	0	0	0	0	0
Number of Voluntary Deposit Accounts	0	0	0	0	0	0	0
Voluntary Deposits	0	0	0	0	0	0	0
Average Deposit Balance per Depositor	2,375	353	1,416	1,335	2,135	858	1,328
Average Deposit Balance per Depositor/GNI per Capita	61.0%	8.0%	34.0%	39.0%	59.5%	26.0%	49.0%
Average Deposit Account Balance	1,617	1,535	1,416	1,335	742	742	1,114
Average Deposit Account Balance/GNI per Capita	40.5%	34.0%	34.0%	39.0%	23.0%	23.0%	41.0%
<b>MACROECONOMIC INDICATORS</b>							
GNI per Capita	4,236	4,236	4,510	3,780	2,658	3,350	2,580
GDP Growth Rate	-2.0%	-3.0%	6.0%	6.8%	-4.0%	6.8%	13.7%
Deposit Rate	8.0%	4.0%	4.4%	4.0%	10.3%	10.4%	9.5%
Inflation Rate	5.6%	0.9%	7.4%	2.9%	2.2%	10.0%	9.2%
Financial Depth	37.4%	57.8%	57.8%	65.9%	22.1%	22.1%	22.0%
<b>OVERALL FINANCIAL PERFORMANCE</b>							
Return on Assets	1.1%	0.2%	3.2%	3.7%	2.3%	4.3%	4.5%
Return on Equity	3.0%	0.8%	9.7%	11.9%	12.8%	19.6%	17.1%
Operational Self-Sufficiency	109.8%	101.6%	116.3%	123.6%	118.7%	121.8%	129.6%
Financial Self-Sufficiency	107.9%	101.2%	116.3%	123.6%	118.3%	121.0%	129.6%
<b>REVENUES</b>							
Financial Revenue/Assets	22.0%	19.1%	20.9%	20.1%	28.4%	29.8%	27.9%
Profit Margin	7.3%	1.2%	14.1%	18.4%	15.5%	17.4%	22.8%
Yield on Gross Portfolio (nominal)	27.0%	22.0%	23.0%	21.9%	33.1%	34.0%	32.5%
Yield on Gross Portfolio (real)	21.4%	20.9%	15.9%	18.0%	29.6%	10.2%	19.6%
<b>EXPENSES</b>							
Total Expense/Assets	21.9%	19.1%	17.7%	14.9%	23.0%	23.1%	22.1%
Financial Expense/Assets	5.9%	5.4%	5.5%	3.9%	7.2%	7.8%	5.6%
Provision for Loan Impairment/Assets	1.9%	3.7%	1.5%	1.0%	1.5%	1.0%	0.7%
Operating Expense/Assets	11.3%	9.4%	11.0%	10.0%	12.6%	14.9%	14.5%
Personnel Expense/Assets	6.2%	4.8%	5.9%	6.3%	7.8%	9.3%	8.1%
Administrative Expense/Assets	4.9%	4.3%	4.6%	4.1%	5.3%	5.9%	5.8%
Adjustment Expense/Assets	1.9%	0.2%	1.2%	0.7%	1.7%	4.5%	3.1%
<b>EFFICIENCY</b>							
Operating Expense/Loan Portfolio	14.7%	11.8%	12.5%	12.4%	14.9%	16.7%	16.6%
Personnel Expense/Loan Portfolio	7.5%	6.5%	7.1%	7.0%	9.3%	10.4%	9.4%
Average Salary/GNI per Capita	307.0%	399.0%	459.5%	493.5%	326.0%	337.5%	337.0%
Cost per Borrower	286	295	287	253	200	206	161
Cost per Loan	254	295	286	261	189	191	155
<b>PRODUCTIVITY</b>							
Borrowers per Staff Member	59	96	104	128	94	92	88
Loans per Staff Member	61	96	104	128	94	98	88
Borrowers per Loan Officer	151	193	209	209	266	229	197
Loans per Loan Officer	151	196	211	209	266	254	197
Voluntary Depositors per Staff Member	0	0	0	0	0	0	0
Deposit Accounts per Staff Member	0	0	0	0	0	0	0
Personnel Allocation Ratio	40.0%	54.7%	55.1%	56.7%	38.5%	39.3%	38.3%
<b>RISK AND LIQUIDITY</b>							
Portfolio at Risk > 30 Days	4.2%	8.0%	2.1%	1.3%	2.5%	1.3%	0.3%
Portfolio at Risk > 90 Days	2.7%	4.6%	1.0%	0.6%	2.1%	0.8%	0.2%
Write-off Ratio	0.6%	2.9%	1.2%	0.5%	1.4%	0.1%	0.2%
Loan Loss Rate	0.5%	2.9%	1.0%	0.3%	0.7%	0.0%	0.1%
Risk Coverage Ratio	67.2%	76.7%	84.5%	145.8%	86.8%	113.2%	215.7%
Non-earning Liquid Assets as a % of Total Assets	10.4%	11.7%	6.0%	5.8%	16.5%	8.1%	6.9%



Year (All figures are "medians")	2009 CEE	2008 CEE	2007 CEE	2009 Central Asia	2008 Central Asia	2007 Central Asia	2009 Russia*
<b>INSTITUTIONAL CHARACTERISTICS</b>							
Number of MFIs	25	25	25	28	28	28	19
Age	13	12	11	7	6	5	10
Total Assets	3,790,836	3,988,036	3,336,303	9,682,486	8,033,526	5,999,617	1,810,005
Offices	1	1	2	16	9	8	1
Personnel	5	5	5	195	168	116	8
<b>FINANCING STRUCTURE</b>							
Capital/Asset Ratio	34.8%	36.1%	37.8%	26.0%	23.2%	25.1%	16.2%
Debt to Equity	1.87	1.77	1.65	2.86	3.08	2.62	5.10
Deposits to Loans	0%	0%	0%	0%	0%	0%	76.2%
Deposits to Total Assets	0%	0%	0%	0%	0%	0%	68.4%
Portfolio to Assets	85.89%	88.38%	81.25%	77.94%	87.34%	87.64%	88.0%
<b>OUTREACH INDICATORS</b>							
Number of Active Borrowers	366	368	329	8,178	10,458	7,070	439
Per cent of Total Assets	0.7334183865985	0.7334183865985	0.7334183865985	0.7334183865985	0.7334183865985	0.7334183865985	0.7334183865985

## The Balkans

Table 5 Macedonia								
Population	2,042,484							
Provider	Legal Status	Number of Institutions	Retail Borrowers	Retail Portfolio, USD	Avg. Loan Balance, USD	Retail Depositors	Retail Deposits, USD	Avg. Deposit Balance, USD
Foundation	NGO	1	2,962	3,855,842	1,302	0	0	
Saving House	Credit Union	2	11,526	48,994,012	4,251	19,617	7,838,817	400
Specialized Microfinance Bank	Bank	1	28,127	56,308,781	2,002	132,046	126,659,337	959
<b>TOTAL</b>		<b>4</b>	<b>42,615</b>	<b>109,158,635</b>	<b>2,562</b>	<b>151,663</b>	<b>134,498,154</b>	<b>887</b>

Source: MIX Market.

Population	624,213							
Provider	Legal Status	Number of Institutions	Retail Borrowers	Retail Portfolio, USD	Avg. Loan Balance, USD	Retail Depositors	Retail Deposits, USD	Avg. Deposit Balance, USD
Nonbank Financial Intermediary	NBFI	1	40,104	86,399,031	2,154	0	0	
<b>TOTAL</b>		<b>1</b>	<b>40,104</b>	<b>86,399,031</b>	<b>2,154</b>	<b>0</b>	<b>0</b>	

Table 9 Azerbaijan								
Population	8,781,100							
Provider	Legal Status	Number of Institutions	Retail Borrowers	Retail Portfolio, USD	Avg. Loan Balance, USD	Retail Depositors	Retail Deposits, USD	Avg. Deposit Balance, USD
Credit union	Credit Union	48	9,432	14,953,157	1,585	9,432	4,607,616	489
Downscaling Bank	Bank	12	37,445	120,729,123	3,224			
Nonbank Credit Organization	NBFI	16	179,003	151,961,189	849	0	0	
Specialized Microfinance Bank	Bank	1	96,211	177,311,250	1,843	64,342	59,228,750	921
<b>TOTAL</b>		<b>77</b>	<b>322,091</b>	<b>464,954,719</b>	<b>1,444</b>	<b>73,774</b>	<b>63,836,366</b>	<b>865</b>

Source: AMFA, EBRD, MIX Market, WOCCU. Notes: Deposits for credit unions are membership fees not voluntary deposits.

Table 10 Georgia								
Population	4,260,333							
Provider	Legal Status	Number of Institutions	Retail Borrowers	Retail Portfolio, USD	Avg. Loan Balance, USD	Retail Depositors	Retail Deposits, USD	Avg. Deposit Balance, USD
Downscaling Bank	Bank	3	6,551	53,961,023	8,237			
Microfinance Organization	NBFI	8	76,014	52,590,533	692	0	0	
Specialized Microfinance Bank	Bank	2	69,521	103,397,633	1,487	396,453	170,330,769	430
<b>TOTAL</b>		<b>13</b>	<b>152,086</b>	<b>209,949,190</b>	<b>1,380</b>	<b>396,453</b>	<b>170,330,769</b>	<b>430</b>

Source: Central Bank of Georgia, EBRD, MIX Market.

## Central and Eastern Europe

Table 11 Belarus								
Population	9,663,000							
Provider	Legal Status	Number of Institutions	Retail Borrowers	Retail Portfolio, USD	Avg. Loan Balance, USD	Retail Depositors	Retail Deposits, USD	Avg. Deposit Balance, USD
Credit Union	Credit Union	14	1,047	630,563	602	1,047	585,824	560
Downscaling Bank	Bank	7	5,924	67,497,607	11,394			
<b>TOTAL</b>		<b>21</b>	<b>6,971</b>	<b>68,128,170</b>	<b>9,773</b>	<b>1,047</b>	<b>585,824</b>	<b>560</b>

Source: EBRD, WOCCU.

Table 12 Bulgaria								
Population	7,585,131							
Provider	Legal Status	Number of Institutions	Retail Borrowers	Retail Portfolio, USD	Avg. Loan Balance, USD	Retail Depositors	Retail Deposits, USD	Avg. Deposit Balance, USD
Cooperative	Credit Union	17	3,294	15,587,325	4,732	0	0	
Nonbank Financial Intermediary	NBFI	3	3,529	10,228,676	2,898	0	0	
Specialized Microfinance Bank	Bank	1	42,195	182,452,206	4,324	220,291	340,867,647	1,547
<b>TOTAL</b>		<b>21</b>	<b>49,018</b>	<b>208,268,207</b>	<b>4,249</b>	<b>220,291</b>	<b>340,867,647</b>	<b>1,547</b>

Source: MIX Market.



Table 17 Kazakhstan									
Population	15,888,000								
Provider	Legal Status	Number of Institutions	Retail Borrowers	Retail Portfolio, USD	Avg. Loan Balance, USD	Retail Depositors	Retail Deposits, USD	Avg. Deposit Balance, USD	
Credit Partnership	Credit Union	181	3,377	976,713,486	289,265	0	0		
Government Development Institution	Government Fund	1	18,899	43,140,384	2,283	0	0		
Microcredit Organization	NBFI	649	94,920	303,458,282	3,197	0	0		
<b>TOTAL</b>		<b>831</b>	<b>117,195</b>	<b>1,323,312,152</b>	<b>11,292</b>	<b>0</b>	<b>0</b>	<b>0</b>	

Source: MIX Market, Statistical Agency of the Republic of Kazakhstan.

Table 21 Uzbekistan								
Population	27,767,100							
Provider	Legal Status	Number of Institutions	Retail Borrowers	Retail Portfolio, USD	Avg. Loan Balance, USD	Retail Depositors	Retail Deposits, USD	Avg. Deposit Balance, USD
Credit Union	Credit Union	103	52,965	121,792,000	2,299	153,063	100,131,000	654
Downscaling Bank	Bank	2	7,478	37,409,306	5,003			
Microcredit Institution	NBFI	32	9,574	3,853,000	402	0	0	
Specialized Microfinance Bank	Bank	1	42,051	63,753,095	1,516	50,000	24,993,171	500
<b>TOTAL</b>		<b>138</b>	<b>112,068</b>	<b>226,807,401</b>	<b>2,024</b>	<b>203,063</b>	<b>125,124,171</b>	<b>616</b>

Source: EBRD, MIX Market, UNDP Uzbekistan.

# Eastern Europe and Central Asia Microfinance Analysis and Benchmarking Report, 2010

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