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PROVINCIAL ECONOMIC GROWTH PROGRAM

STATE OF IRAQ'S MICROFINANCE INDUSTRY



October 2012

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COVER PHOTO: Sulaymaniyah cobbler Kaywan Maruf Hama Saeed used two microfinance loans totaling \$5,000 to buy virgin wool for the traditional Kurdish shoes and clothes he makes. "Kurds appreciate quality and authentic products when it comes to shoes and clothes," he smiles. "I'm the only retailer on the street that doesn't worry about Chinese imports."

STATE OF IRAQ'S MICROFINANCE INDUSTRY

All data and information in this report is current as of June 2012

The USAID-*Tijara* Provincial Economic Growth Program is made possible by the support of the American people through the U.S. Agency for International Development (USAID). USAID-*Tijara* is implemented by The Louis Berger Group, Inc.

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LIST OF ABBREVIATIONS

ATM	Automated teller machine
AusAid	Australian Agency for International Development
BFF	Bright Future Foundation
BOD	Board of Directors
BOP	Bottom of the pyramid
CAGR	Compounded annual growth rate
CBI	Central Bank of Iraq
CGAP	Consultative Group to Assist the Poor
CMOC	Civil military operations center
COSIT	Central Organization for Statistics and Information Technology
DFID	Department for International Development, United Kingdom
DIG	Development Innovations Group
GAAP	Generally accepted accounting principles
GB	Government banks
GDP	Gross domestic product
GLP	Gross loan portfolio
GoI	Government of Iraq
ICBG	Iraqi Company for Bank Guarantees
ICF-SME	Iraqi Company for Financing SMEs
ICT	Information and communications technology
IDP	Internally displaced person
IFC	International Finance Corporation
IQD	Iraqi dinar
IMF	International Monetary Fund
JSC	Joint stock company
KRG	Kurdistan Regional Government
LLC	Limited Liability Company
MBB	Micro Banking Bulletin
MENA	Middle East and North Africa
MFI	Microfinance Institution
MIM	Ministry of Industry and Minerals
MIX	Microfinance Information eXchange Market
MOLSA	Ministry of Labor and Social Affairs
MoU	Memorandum of understanding
MSME	Micro, small and medium enterprise
NBFI	Non-Banking Financial Institution
NGO	Non-Governmental Organization
OPIC	Overseas Private Investment Corporation
PB	Private Banks
PCMS	Performance Classification and Monitoring System
PDS	Public distribution system
PPP	Purchasing power parity
PRT	Provincial reconstruction team
RI	Relief International
SBDC	Small business development center
SME	Small and medium enterprise
TEDC	Tallafar Economic Development Center
TDMN	Al-Tadhamun
ToT	Training of trainers
UN	United Nations
UNHCR	United Nations High Commissioner for Refugees
UNIDO	United Nations Industrial Development Organization
UNOPS	United Nations Office for Project Services
USAID	United States Agency for International Development
USG	United States Government
VCF	Value chain financing
WB	World Bank

PREFACE

USAID-*Tijara* is pleased to present the third annual State of the Iraqi Microfinance Industry Report.

A microfinance industry that is based on international best practices standards is relatively new to Iraq and to the wider Middle East and North Africa (MENA) region. Established in Iraq in the latter half of 2003, the industry has 12 international and indigenous microfinance institutions (MFIs) operating in all 18 provinces of the country. The industry through the end of June 2012 disbursed just under \$959.3 million in loans to 403,765 clients since inception. As of that date there was an outstanding loan portfolio of just under \$143.9 million with 93,627 active clients. The industry continues to enjoy very high rates of loan repayment, notwithstanding ever-present security challenges.

We are pleased to report that there is growing emphasis on more inclusive lending that focuses on reducing poverty. The industry increasingly is using the solidarity group lending (SGL) methodology, which USAID-*Tijara* introduced and now promotes as a tool for outreach to the poor and women who have been previously excluded from the finance sector. Through this methodology, there is over \$14.9 million outstanding to almost 23,077 individual group members, one-third being women. Additionally, we are pleased to report that USAID-*Tijara* also introduced the Iraqi Vulnerable Groups Support Initiative (IVGSI) to facilitate outreach to vulnerable and minority groups (VMGs) who have been unable to access funding because of their vulnerable or minority status. This initiative is not only facilitating outreach to the target groups through our grant funding, but has also motivated partner institutions to increase financial services to those groups through their own funding. As a result, this has created a multiplier effect of the grant funding which will be further increased when the funds repaid by the clients are reused to make more loans.

All MFIs have adopted internationally-compliant reporting standards and have also developed effective rules of operation guided by the industry-wide Code of Conduct and Ethics which was instituted in 2010. As noted in our previous report, the MFIs have also implemented more modern management information systems and are now effectively tracking client outreach, financial information and trends. The Central Bank of Iraq (CBI) and the NGOs Directorate are increasingly engaged in supporting the industry's role in the finance sector and in considering the regulation and supervision of the industry when appropriate legislative framework is formulated.

The development of the Iraq microfinance industry largely is attributable to the efforts of the U.S. Agency for International Development (USAID). Over the past seven years, USAID, through its implementing partner USAID-*Tijara*, has supported the industry at the macro, meso and micro levels through targeted interventions aimed at integrating microfinance institutions into the formal financial system. Such interventions include capacity building of industry participants and product innovation as well as enhanced transparency and reporting.

At the meso level, USAID-*Tijara* is pleased to report that what began as an idea to establish the Iraq Microfinance Network (IMFN) back in 2008, recently culminated in official registration of the IMFN on April 26, 2012, making it a legal entity which will operate as the coordinating body for the microfinance industry. The IMFN will play a key role in shaping and advancing an inclusive microfinance industry, while also strengthening the microfinance sector in the country. It is expected to play a vital role in sustaining Iraq's inclusive microfinance sector especially after USAID-*Tijara* concludes its mission in Iraq in January 2013.

On behalf of all industry participants we thank the Government of Iraq, especially the CBI and the NGOs Directorate, the U.S. Embassy and USAID for their support for microfinance in Iraq.

We welcome you to review this report to gain an understanding of Iraqi microfinance as well as future trends that are likely to impact its growth. We are proud to be increasingly involved as a catalyst and a driving force in developing and advancing inclusive microfinance sectors together with the microfinance practitioners both in Iraq and across the MENA region.

Sincerely,

DONAL COTTER



CHIEF OF PARTY, USAID-TIJARA

EXECUTIVE SUMMARY

Microfinance institutions (MFIs) in Iraq have emerged as effective, demand-driven credit-only institutions offering clients an alternative to inaccessible banking institutions on the one hand and exploitative traditional money lenders on the other. With early-stage donor funding from USAID to help overcome the challenges of Iraq's post-conflict environment, MFIs have achieved significant scale, depth of outreach to the poor and women and financial and institutional sustainability with consequent desired socio-economic impact over the past eight years. The microfinance industry continues to grow and solidify its important role in Iraq's financial sector.

The microfinance sector in Iraq includes 12 NGO-MFIs operating in all 18 provinces. Since 2009, the overall regulatory environment for the sector has improved with the issuance of the NGO (non-governmental organization) Law. The law enables MFIs to continue as quality financial service providers for women, youth, micro and small entrepreneurs and economically challenged people in Iraq. The greatest accomplishment to date for USAID-*Tijara* has been the Central Bank of Iraq's (CBI) recognition of microfinance as an effective source of credit for micro, small and medium-scale enterprises (MSMEs) and therefore an important component of the finance sector.

The microfinance industry has achieved a respectable rate of growth and socio-economic impact on those it serves. Despite concerns that Iraq is not ready for microfinance, the sector has cumulatively disbursed 403,765 loans amounting to over \$959.3 million with outstanding portfolio of \$143.9 million held by 93,627 active clients as of June 2012. The industry holds an impressive 99% repayment rate and a portfolio at risk (PAR) greater than 30 days of just 1.3%. Despite high levels of activity, growing efficiency and greater depth of outreach, this fast growing industry has only scratched the surface of the potential market in Iraq and with less than 1% market penetration, it is attracting more donors and a growing list of stakeholders.

USAID, through its implementing partner, USAID-*Tijara*, has scaled-up initiatives at the macro, meso and micro levels to create an inclusive financial sector in Iraq. The United Nations Capital Development Fund (UNCDF) introduced the sector development approach to microfinance industry which later was adopted globally. This approach includes operations at the three levels listed below indicating the objective at each level:

Macro level: Strengthened and secure economic, legal, and regulatory infrastructure that provides and supports an enabling environment that favors microfinance industry growth and sustainability.

Meso level: Strengthened technical and institutional infrastructure that advocates, promotes and supports a more inclusive financial sector.

Micro level: Creation of viable and sustainable MFIs that have strengthened capacities and that offer diversified products and services, especially for vulnerable groups like the poor, women and youth.

At the macro level, the greatest accomplishment has been the CBI's recognition of microfinance as an effective and important component of the financial sector. USAID-*Tijara* is continuing its leadership and is also intensifying its efforts in coordinating and communicating with other donors in ensuring an enabling environment more conducive for expanding and deepening the outreach of quality financial services especially for the poor and women. As a result of this leadership and interventions, the Iraqi microfinance industry will benefit from an improved enabling environment.

At the meso level, an important milestone in the microfinance industry was achieved in April this year when the Iraq Microfinance Network (IMFN) was formally registered. USAID-*Tijara* introduced the idea of a network that would take its role to support the microfinance industry in the post *Tijara* period and all the MFIs in Iraq met in a forum on August 8, 2010, and deliberated on the benefits of a network and its possible role, structure, and management, and the services it should render. The forum then made a decision to form and make operational the IMFN and an informal Board was constituted to oversee the process and apply for registration with the NGOs Directorate under the NGO Law. With assistance of USAID-*Tijara*, the by-laws of IMFN were prepared and approved by the members comprised of all the 12 MFIs. The application for registration was submitted on Feb 12, 2012, at the NGOs Directorate and all the efforts made culminated with the formal registration and issuance of the Certificate on April 26, 2012. The IMFN is now an independent institution with legal status to operate as the coordinating body which will play a key role in shaping and advancing an inclusive microfinance industry while also further strengthening the microfinance sector in the country.

At the micro level, USAID-*Tijara* and its predecessor USAID-Izdihar, have played a significant role in nurturing the microfinance sector through grant support and capacity building initiatives designed to ensure that the MFIs have the capacity and knowhow to create opportunities for considerable growth and expansion to proactively and effectively meet the large unmet demand for inclusive financial services in Iraq. Institutional development, through both grant funding and capacity building, has been the pillar of the progress that has been achieved

CHAPTER I

by Saeed Lateef

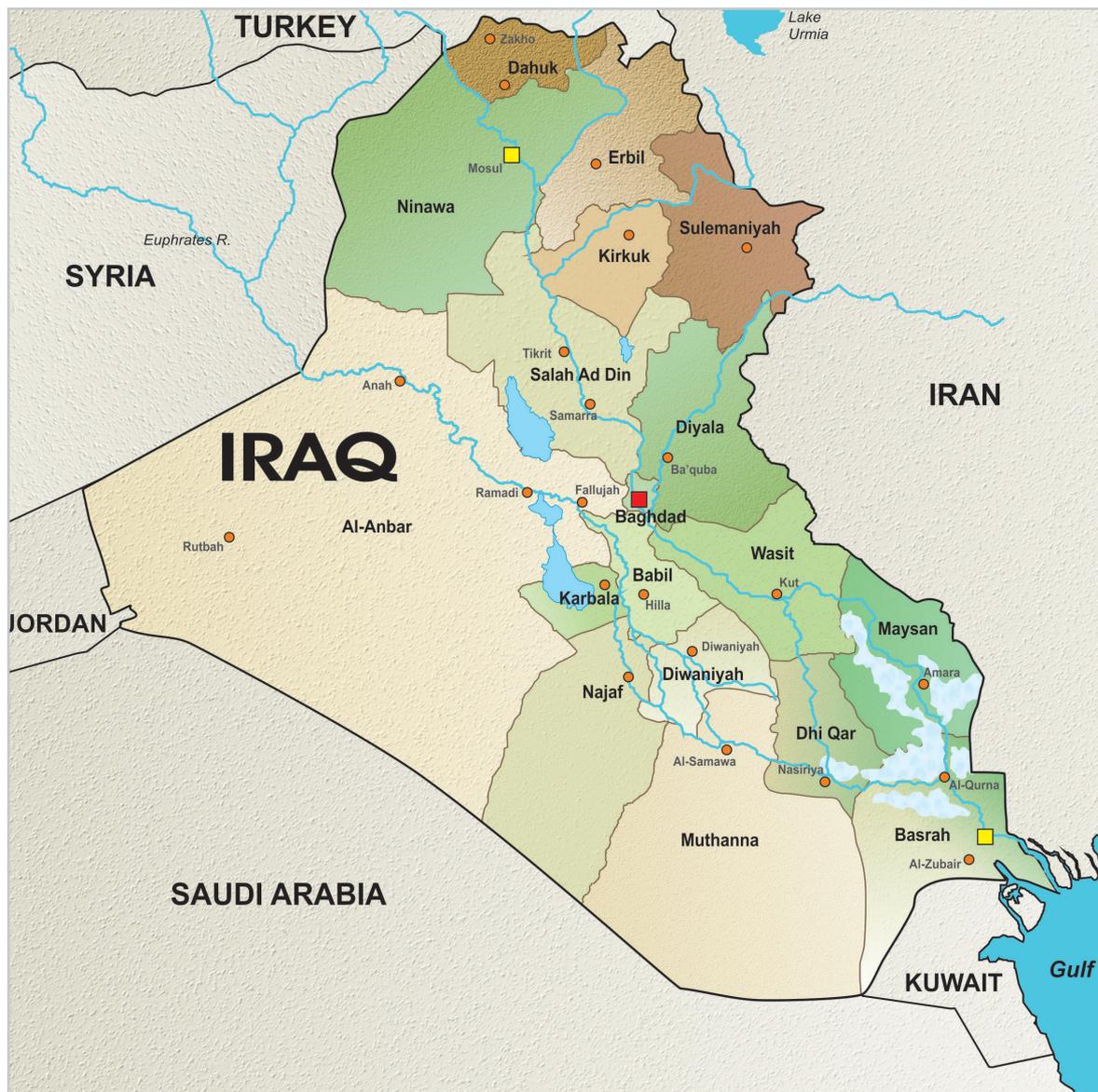
THE IRAQI MICROFINANCE INDUSTRY OVERVIEW

Falafel is great, but the real money is in burgers. That's why Nassriya vendor Rahim Abdul-Ameer Jassim asked CHF for \$4,000 loan to buy a grill. Increased sales now cover all his expenses, pay for four employees and leave a tidy net profit of \$300 at the end of the month.

1.1 IRAQ

Iraq is bordered by Jordan to the west, Syria to the northwest, Turkey to the north, Iran to the east, and Kuwait and Saudi Arabia to the south. Iraq has a population of 32 million, of which 66% lives in urban settlements. Compared to the Middle East and North Africa (MENA) region, socio-economic indicators for Iraq are mixed. Poverty and human conditions in Iraq worsened in the 1990s and have only marginally improved in recent years. GDP per capita (PPP) is \$3,900, which is 161st in the world rankings¹. An estimated 25% of the population lives below the poverty line of \$2.20 per person per day². Average life expectancy at birth is 68 years, compared to 72 years in the MENA region. Overall unemployment (percentage of total labor force) is between 16.2-17.5% for men, and 22.5% for women³. Public service delivery continues to be unreliable; only 12.5% of people whose dwellings are connected to the public network report that their supply of water is stable. As for electricity in Iraq, output averages about 8,500 MW falling far short of demand which is typically more than 14,000 MW⁴.

Iraq has been categorized as a middle-income country since the 1970s due to developing good infrastructure, efficient education and healthcare systems. However, over the past three decades, wars, dictatorship and international sanctions have crippled Iraq's economy. The economy showed resilience in 2004, but annual growth rate is still too slow to rebuild this security-challenged country. According to World Bank classification in July 2011, Iraq was categorized as a lower middle-income country falling in the range of GNI per capita of \$1,006-\$3,975⁵.



1 <https://www.cia.gov/library/publications/the-world-factbook/geos/iz.html>

2 <http://data.worldbank.org/indicator/SI.POV.2DAY>

3 <http://data.worldbank.org/indicator/SL.TLFTOTL.IN>

4 http://en.wikipedia.org/wiki/Electricity_sector_in_Iraq

5 <http://chartsbin.com/view/2438>

TABLE 1: INDICATOR: IRAQ (LOWER MIDDLE INCOME COUNTRY)

Indicators	Iraq	MENA
Total Population (million)	32.0	331.3
Total Population Annual Growth Rate (%)	3.0	1.8
Literacy (% of population aged 15+)	78	78
Percentage of Population Living in Rural Areas	34	42
Life Expectancy at Birth (Years)	68	72
GNI per Capita PPP (\$)	3,370	8,045
GDP Growth Rate (%)	0.8	4.2

Source: World Bank

1.2 IRAQI FINANCIAL SECTOR

The Iraqi financial sector is comprised of a variety of institutions, which include the Central Bank of Iraq (CBI), commercial banks, specialized banks, insurance and finance companies. These institutions operate within formal financial markets and are supported by a financial infrastructure consisting of payment and settlement systems within applicable legal and regulatory framework. The financial sector also includes 12 USAID-*Tijara* partner microfinance institutions, which are NGO-MFIs by their legal status. The sector faces several challenges in meeting the needs of the developing economy⁶, including domination by the banking system, with most assets held by state-owned banks; weak financial infrastructure which impedes access to finance, and a still developing SME and microfinance industry which is far from reaching its full potential.

TABLE 2: IRAQI FINANCIAL SECTOR⁷

Commercial Banks	Non- Banking Financial Institutions and Financial transfer and Investment Companies	Insurance Companies	Microfinance Institutions (MFIs) NGOs
State Owned Banks (7) Private Commercial Banks (23) Islamic Banks (9) Foreign Banks (7)	Financial Institutions (32) Financial Companies (10)	State Owned Companies (3) Private Companies (18)	Local Iraqi MFIs (10) International MFIs (2)

The commercial banks, both public and private, dominate the financial system. Currently, there are 46 commercial banks including specialized Islamic and foreign banks with a network of 774 branches throughout Iraq. As Iraq stabilizes, its banking system is growing both in size and focus. Stability of the Iraqi dinar (IQD) and reducing inflation are at the core of this impressive progress. Most banks' income is generated from fee-based services including financial transfers, however, thriving private banks are increasing intermediation. The volume of commercial bank lending, both corporate and consumer, has doubled since January 2008.

The performance of financial institutions has also been promising in the recent past. The Iraqi Company for Bank Guarantees (ICBG) was established in 2006 with a \$5 million grant from the United States Agency for International Development (USAID). ICBG is Iraq's premier provider of loan guarantees to privately-owned banks for loans targeted to Iraqi small and medium enterprises. ICBG guarantees up to 75% of loans to SMEs granted by these banks. The operations of ICBG also focus on institutional development and capacity building in the banks, as well as its own organization, while marketing and implementing the guarantee program. The Company's outreach is extended throughout Iraq through the participating bank network; such outreach allows access to credit for small and medium enterprises in all the provinces of Iraq. ICBG had approved over 3,800 loans worth almost \$46 million as 2011 came to a close. Sixteen banks are signatories to ICBG's loan guarantee program. The Iraqi Stock Exchange (ISX), founded in 2004, had 84 companies listing their shares as of July 2012. This compares well with other regional exchanges in terms of the number of listed companies. The banking sector is the largest on the bourse, which also lists industrial, agricultural, and insurance firms. The total market value of shares listed on the exchange is around \$3 billion and the daily trade volume averages from \$2 million to \$3 million. Twelve MFIs, two international and ten local, as of June 2012 have disbursed 403,765 loans valued at over \$959.3 million since inception, mostly to MSMEs. USAID-*Tijara* is providing capital and technical support to these MFIs, thus enabling them to offer an array of quality financial products and services on a sustainable basis. As of end June 2012, twelve MFIs had an outstanding portfolio of \$143.9 million with 93,627 active clients, of whom 21% were women.

⁶ <http://www.iraq-businessnews.com/2011/09/26/republic-of-iraq-financial-sector-review/>

⁷ http://siteresources.worldbank.org/INTMENA/Resources/Financial_Sector_Review_English.pdf

I.3 MICROFINANCE IN THE MENA REGION

Around 26% or 96.2 million of 370 million people in the Arab region live on less than \$2 per day. The supply of microfinance services in the region is encouraging, especially when we consider that there is a lack of adequate formal financial services by banks and formal financial institutions. It is critical for these institutions to increase the outreach of their services in order to have a good measure of success in reaching more clients that have previously been excluded from formal financial services. Nonetheless, the region has reduced the gap between demand and supply in the recent past due to impressive growth in the depth and breadth of quality financial services, except in a few countries in the region which suffered from global economic recession.

The MENA region recorded the third highest median in outreach and scale following closely on the heels of Asia and Latin America (LAC) regions. With the exception of Morocco, the regional industry's outreach and gross loan portfolio grew at 29% and 40% respectively in 2008 and at 27% and 29% respectively in 2009. In the Iraqi microfinance industry, active clients and loan portfolio grew at 27.7% and 28.4% respectively in 2010 and 15.1% and 20.0% respectively in the year 2011. Morocco was the only exception in the region where the industry recorded a decline in active clients and loan portfolio for the second consecutive year since 2008 due to increased delinquency of up to 10% PAR > 30 days for the industry and with one of the four larger institutions experiencing up to 30% PAR > 30 days. The Moroccan crisis prompted microfinance industry players across MENA to be more cautious in creating a balance between growth and risk. The MFIs in the region revised their outreach growth plans and implemented precautionary measures such as tightening their credit processes, strengthening management, and placing a greater emphasis on loan recovery, including the use of legal action to pursue delinquent borrowers in order to avoid and mitigate the risks.

Despite the contraction in active clients and in outstanding loan portfolio, the Moroccan microfinance industry is still the largest in the region in gross loan portfolio which is almost three times that of Egypt, which has surpassed it in number of active clients. The main reason for this disparity is that Egypt uses solidarity group lending (SGL) methodology to a greater extent and therefore focuses on reaching the poor through small loans. In comparison Iraq's outreach is less than one tenth of that for Morocco and for Egypt although its gross loan portfolio is at a much higher proportion in view of its high average loan size. Review of the data in Table 3 clarifies the size of the microfinance industry in the ten MENA countries for which the Mix Market has reported the latest numbers for 2009.

TABLE 3: MFIs FROM 10 COUNTRIES REPORTING DATA AT MIX MARKET FOR 2009

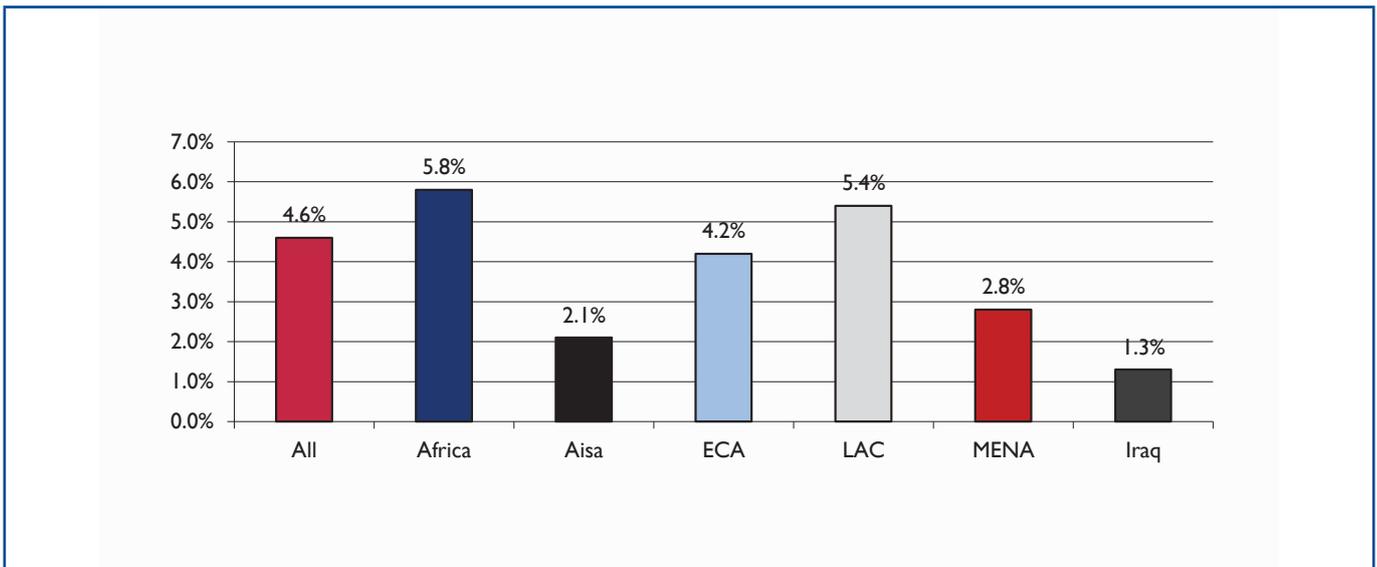
Country	MFIs	Number of Active Borrowers	Gross Loan Portfolio (GLP)	Average Loan Balance
Egypt	13	1,100,541	\$216,688,450	\$197
Morocco	10	915,839	\$609,943,100	\$666
Jordan	8	159,081	\$134,262,829	\$844
Tunisia	1	123,041	\$41,355,997	\$336
Palestine	8	34,057	\$89,202,509	\$2619
Lebanon	3	31,671	\$29,274,281	\$924
Yemen	6	28,714	\$3,593,486	\$125
Syria	2	21,327	\$18,181,266	\$852
Sudan	3	20,155	\$3,867,094	\$192
Iraq ⁸	12	93,627	\$143,932,639	\$1537
Total	66	2,528,053	\$1,290,301,651	\$510

Source: MIX Market – 2009 Benchmarks

Portfolio quality plays a vital role in determining the sustainability of a microfinance institution in particular and the industry in general. The MFIs in MENA maintained high portfolio quality despite deterioration in the Moroccan industry in 2008 and 2009. The region's overall portfolio quality was above the median, with the second lowest PAR > 30 days in the world at 2.8% after Asia which recorded PAR > 30 days at 2.1%. The Iraqi microfinance industry performs the best in the MENA region with only 1.3% PAR >30 days as of June 30, 2012.

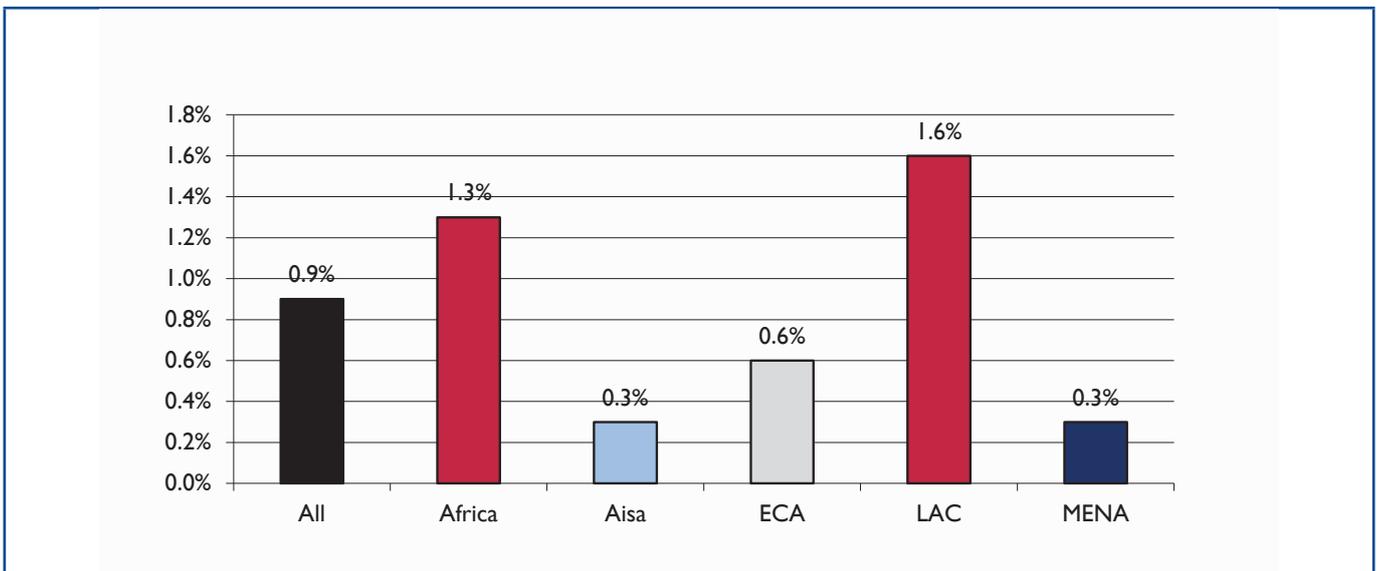
⁸ Iraq numbers are updated to June 2012 as per USAID-Tijara's consolidated industry report

FIGURE 1: PORTFOLIO AT RISK > 30 DAYS



Source: MIX Market

FIGURE 2: WRITE OFF RATIO

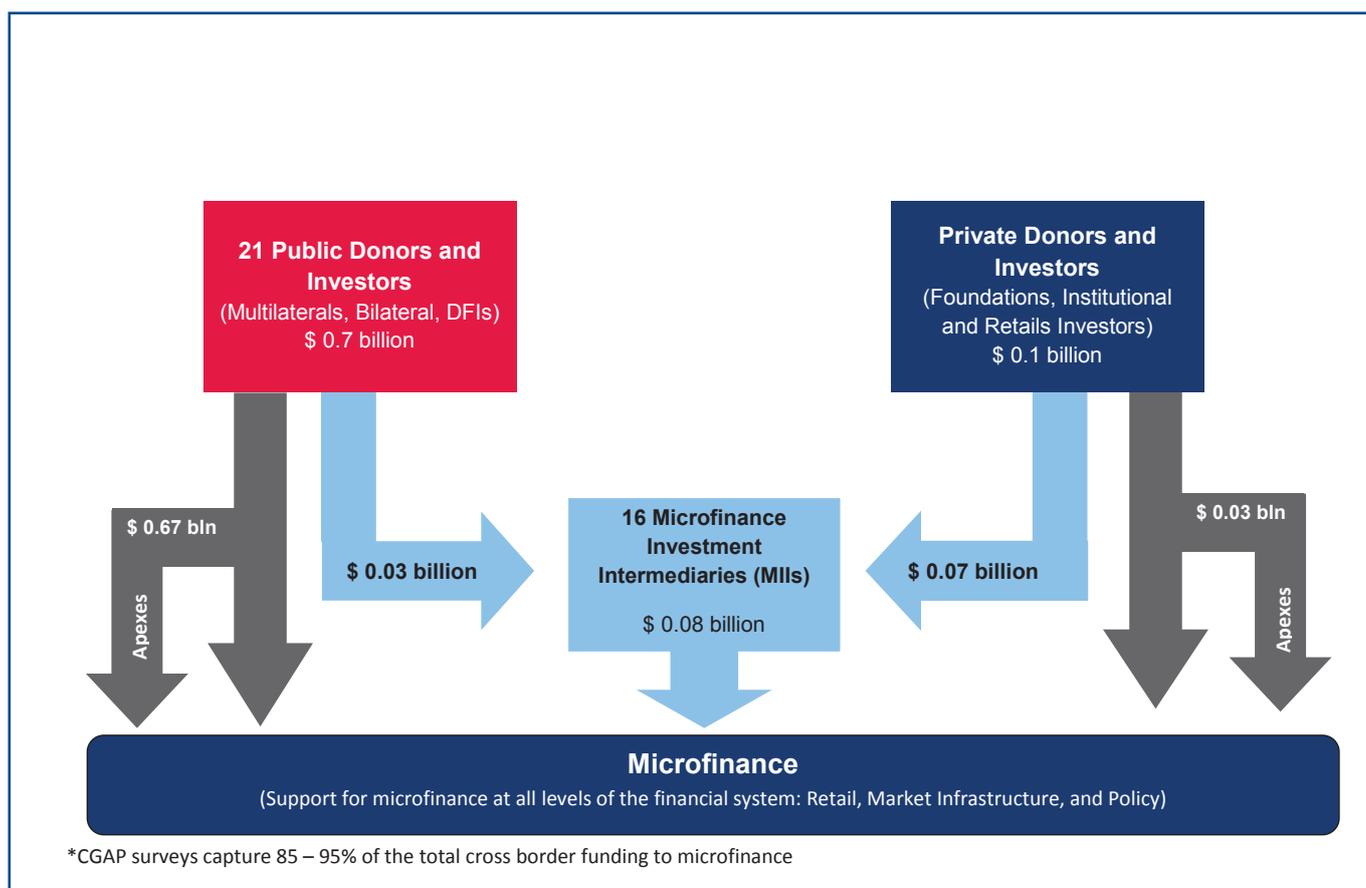


Source: MIX Market

Microfinance institutions in MENA, like anywhere else, have three different sources of funding: deposits, debt, and equity. The legal and regulatory framework in a few countries such as Sudan, Syria and Yemen allows microfinance institutions to mobilize savings. The rest of the MENA country microfinance industries face restrictive regulations with regard to savings deposit mobilization. Donated equity has mainly been through various sources of funding throughout the region. The capital-to-asset ratio of the region is the highest (45%) compared to a global median of 23%. This means that institutions in the region have much unutilized capacity to leverage their capital for greater outreach. However, increasing debt financing and decreasing dependence on donated equity is a recent positive development.

According to the CGAP Funding Survey 2010, there are 45 funders active in the region, of which 21 are public funders, eight are foundations/NGOs, and 16 are microfinance investment intermediaries (MIIs). Total commitments to the microfinance sector in MENA were \$800 million, representing 4% of total cross-border funding to microfinance sectors in the world. These commitments recorded a slow growth rate of 4% compared to 17% globally. In view of its unfavorable and restrictive legal and regulatory environment, the region did not attract a large number of donors and in fact records the lowest number of private funders and other investors despite excellent portfolio quality and the potential of its untapped financial sector. However, as a result of measures taken by the governments and microfinance players in the region to create enabling legal environments, private funding grew by 80% in 2009 compared to 33% globally.

FIGURE 3: COMMITMENTS TO MICROFINANCE FOR MENA AS OF DECEMBER 2009: \$0.8 BILLION*



Source: CGAP

As the depth of outreach increases, the array of financial products and services is diversified and microfinance service providers are integrated more into the formal financial sector. In addition, there is also a need to adapt policy and legal frameworks that facilitate the operations of microfinance service providers in offering quality services to the economically challenged people in the region. Over the past two years, new initiatives have been taken in many countries to regulate microfinance sectors. Syria, Yemen and Egypt have approved laws and regulations for the industry while the Central Bank of Iraq (CBI), with the assistance of USAID-Tijara, has issued SME Finance Companies ordinance to support commercialization of the sector. This ordinance will also pave the way for transformation of NGO-MFIs into non-banking financial institutions (NBFIs) when the additional necessary legal and regulatory framework is formulated/amended to facilitate such transformations since the current legislation and its interpretation by the authorities does not allow NGO MFIs' transformation into NBFIs.

The microfinance industry can only reach its full potential if it is integrated into a country's formal financial sector, where it would be prudentially supervised to ensure adherence to best practice standards. However, for the industry to get there, the stakeholders, i.e. the authorities, donors and practitioners will need to act in concert in deciding when, and how, this takes place. This is the time to bring the microfinance sector into the mainstream financial sector in the MENA region. Low levels of investment (international, domestic and social) to the region can be attributed to the lack of: a) appropriate regulations and b) an enabling legal framework. Clear legal and regulatory financial regimes reduce some inherent operational and institutional risks and, consequently attract more foreign commercial and social investments into the microfinance industry. Many countries in the region have either not introduced specialized microfinance laws or have less favorable enabling environments. The differences in stakeholder understanding of an enabling legal and regulatory framework for inclusive sustainable financial services are narrowing. As a result of the ongoing efforts by the stakeholders in the MENA region, the microfinance sector will attract an increased inflow of funds and capital from diversified investors, thus helping microfinance institutions to meet their double bottom line goals.

1.4 THE IRAQI MICROFINANCE INDUSTRY

The Iraqi microfinance industry based on internationally accepted standards of best practice was established in 2003 and has since made great achievements despite significant challenges of a post-conflict economy. The sector is comprised of 12 NGO-MFIs operating in all 18 provinces. Since 2009, the overall regulatory environment for the sector has improved with the issuance of the NGO (non-governmental organization) Law which enables MFIs to continue as quality financial service providers for women, youth, micro and small entrepreneurs, and economically challenged people in Iraq. Thus far, the sector has achieved an ambitious rate of growth and socio-economic impact on those it serves. With 403,765 loans disbursed to entrepreneurs across Iraq since inception and with a total cumulative disbursement of \$959.3 million as at the end of June 2012, the microfinance industry is coming of age rapidly and evolving from a stabilization intervention to an independent industry incorporating globally prescribed best practices and supported by multiple stakeholders.

Challenges in Post-Conflict Iraq

Overcoming constraints to Income Generating Activities and to Self-Employment

Major conflicts directly undermine economic growth by destroying lives, property, and infrastructure, and indirectly by diverting resources to military activities at the expense of productive investment in physical and human capital. Conflict also disrupts essential public services, impairs fiscal and administrative capacity for postwar recovery, and leaves a legacy of debt that encumbers future budgets. Iraq has faced these problems⁹. The process of recovery has been challenging with dependency on a state-run economy, which results in a significant disadvantage to self-employment. USAID, through its economic development initiatives under *Tijara* (Arabic: Trade) and its predecessor *Izdihar* (Arabic: Prosperity), continues to play a key role in facilitating the culture of entrepreneurship in Iraq and in unleashing the potential of the private sector. Available statistics indicate that these efforts are succeeding in making a difference and changing lives of the poor and women and disadvantaged minorities.

Security

The Iraqi Government has been strengthening security, but it remains fragile. This is evidenced by the spike in suicide attacks after withdrawal of US troops in December 2011. The security situation discourages a larger international presence in Iraq and negatively affects the microfinance sector. It is generally understood and accepted that it is very difficult for microfinance to grow in a conflict situation as institutions are unwilling to lend where there is risk that the client might not pay or even worse might not be around to make the payment. Nevertheless, the commitment of USAID continues unabated especially in conflict-prone communities within Iraq, which are benefiting through the various initiatives funded by USAID.

Refugees' Status and MFIs' Support for IDPs

The United Nations High Commissioner for Refugees (UNHCR) estimates that more than 4.7 million Iraqis left their homes as a result of the conflicts that have plagued the country. Of these, it is estimated that 1.6 million are internally displaced. Many have returned home as security has improved, but displacement remains a concern. MFIs are providing critical micro-loans to internally displaced persons (IDPs) by incorporating flexibility of loan criteria such as removing the requirement that a client must have lived in the same neighborhood for at least two years in order to qualify for a loan. USAID-*Tijara* has developed initiatives, which its partner MFIs are now implementing to help IDPs and other minorities overcome the disadvantage of lack of capital and be able to set up income generating activities. One of these initiatives is the Iraqi Vulnerable Groups Support Initiative (IVGSI) which targets vulnerable groups including IDPs and other marginalized communities.

Financial Sector Development

The level of financial intermediation in Iraq has been improving with credit to the economy increasing from 4.1% of GDP in 2008 to 6.5% in 2009 and to 9.1% in 2010 according to a World Bank report. The banking system is dominated by two of the large state-owned banks, Rafidain and Rasheed. These two banks account for about 91% of total assets. The composition of the financial sector is indicated in Table 2 under Section 1.2 above. Capital markets, besides government securities, are almost nonexistent. There is a serious skills deficit as well as inadequate planning in respect of development of human resources for all levels at banks, and especially so for the middle management level.

Bankers in Iraq lack experience lending to MSMEs, thus limiting the level of financial intermediation required for good growth. Many banks are relatively new, with inadequate skills for analyzing credit risk and for conducting cash-flow analyses. Other obstacles include loans with repayment terms that are too short to accommodate longer term investments and collateral requirements in excess of 150% of loan amounts. USAID's intervention in

⁹ Iraq Economic Recovery Report February 2009

the SME sector led to the creation of : a) an SME guarantee facility, **the Iraqi Company for Bank Guarantees (ICBG)** that guarantees SME loans, and b) the **Iraqi Company for Financing SMEs (ICF-SME)**, an NBF established in 2009 to provide on-lending capital to banks for SME borrowers. Experience indicates that banks cooperating with USAID projects in Iraq have a more diversified portfolio, with over 50% of loans to SMEs as safe investments for wealth creation.

MFIs hold their funds in state-owned banks due to security risks of handling cash, however, there are tremendous inefficiencies in doing so and clients often face logistical challenges, including liquidity constraints. It is expected that as Iraq transitions into a more secure environment and as the Iraqi dinar stabilizes in the short term, local currency will take precedence over U.S. dollars. The microfinance sector will be faced with exchange rate challenges as MFIs shift from US\$ to IQD. These challenges are already hitting the sector with a recent requirement for MFIs to disburse in IQD, however, the impact of the exchange differences arising is expected to be low since the IQD has been fairly stable against the US dollar. No impact is expected on clients since they will receive their loans and repay back in IQD.

Development of Skilled Human Resources

The United Nations embargo between 1991- 2003 created a ‘brain drain’ of those Iraqis who would have been qualified to provide a human resource pool to the financial sector. Further, a substandard system of higher education in Iraq is a challenge for institutional, economic and human development. Information technology skills and qualified professionals remain in severe short supply. To help build the Iraqi microfinance sector, USAID has taken the lead in providing training in critical areas including board governance and oversight, internal controls and risk management, strategic business planning etc. Furthermore, training has been carried out for developing the industry infrastructure of certified trainers in over eight areas of expertise, including financial analysis, delinquency and risk management and human resource management.

Overcoming Challenges in Developing Microfinance Activities in Iraq

Many challenges had to be overcome in implementing successful microfinance in Iraq. Some of the major challenges that had to be overcome are clearly evidenced in the following case in Anbar Province in the South-West, which was a classic and typical of experiences elsewhere in the country. The challenges included:

- i) Selling microfinance as a tool for improving the livelihoods of the communities and alleviating poverty – conventional microfinance was viewed as an undesirable foreign practice that was against Islamic principles.
- ii) Overcoming tribal sensitivities – the Province has several communities that were keen to fight for their specific rights over the others.
- iii) Security – this was one of the provinces ravaged by conflict and upheaval.

USAID-Tijara had to be rather innovative in overcoming these challenges and took several measures to do so. The decision was made to set up Al Takadum microfinance institution with three branches, each operating in the main town of each of the three districts in Anbar Province. On the question of selling microfinance to the communities, action was taken first to develop the Al Murabaha loan product, which is sharia compliant in line with Islamic principles which reject interest charge as “haram” i.e. “forbidden”. Under the Al Murabaha loan the institution buys and sells an asset to the borrower at a margin and therefore no interest is reflected on the transaction and the client just repays to the MFI the full amount of the cost plus the margin as his/her cost of the asset. In addition to this it was important to develop loan products which met the needs of the communities. In view of the damage in the Province due to conflict, the home improvement loan proved to be very popular and convinced the communities of the benefits of accessing the services of Al Takadum. Additionally the housing loan was packaged to meet other needs of the communities by factoring in those other needs to be covered under the housing loan. Once this was done, the effort was made to work with Council members and Administration officials and other community leaders for their support and thereafter it was possible to convince the sheiks and religious leaders to declare fatwas directing that microfinance services are sharia compliant and would assist the communities in improving their lives. Once this was achieved, it was then possible to build clientele for Al Takadum.

With regard to overcoming tribal sensitivities, action was taken to structure the Board of Al Takadum to have equal representation from the three districts and to agree on rotation of the board chair so that each district had its representative chair the board meetings on a rotational basis. Furthermore the board members needed to be trained in good governance according to best practices. This was done through USAID-Tijara’s training programs on improving microfinance governance including institution of a Board Audit Committee.

With regards to security it was critical to work with Al Takadum’s board and management to get their commitment and to hire committed staff. In fact loan officers had to be very brave to go out and develop clients and form groups under the solidarity group lending methodology. Some staff in fact faced real threats of attack

because of what was perceived by extremists as association with foreigners.

Despite the challenges, through the above solutions and the commitment of the board and management, Al Takadum is now one of the more successful Iraqi MFIs and compares favorably with leading MFIs of its size and stature around the world. The institution has disbursed over \$53.2 million in loans to 27,320 clients since inception just over four years ago and currently has an outstanding portfolio of almost \$11.6 million with 10,903 active clients as at June 30, 2012. The institution's success is evidenced by the USAID-Tijara's award of the "Best Governed MFI partner" for two years in a row.

1.5 POVERTY IN IRAQ

According to Iraq's National Strategy for Poverty Reduction and the World Bank, Iraq has an estimated poverty rate of 23%¹⁰ or 7.36 million people living below the poverty line of \$2.20 per day. Additionally, there is a large proportion of the non-poor living just above the poverty line and since the poverty gap is 4.5%, even a small reduction in economic growth would substantially increase poverty rates. Poverty rates are much higher in the southern and central Iraqi provinces and are lowest in Kurdistan Region (KRG).

TABLE 4: POVERTY RATES ACROSS PROVINCES IN IRAQ¹¹

Provinces	Location	Population	Number of Poor	Poor %
Baghdad	Capital	7,826,397	1,029,102	13
Babil*	Central	1,808,951	753,837	42
Karbala	Central	972,467	362,957	37
Najaf	Central	673,603	166,244	25
Diwaniyah	Central	1,084,871	384,060	35
Wasit	Central	1,166,434	410,575	35
Diyala	North	1,709,340	572,282	33
Ninawa	North	3,078,974	716,287	23
Salah ad Din	North	1,304,938	526,643	40
Kirkuk	North	987,977	97,932	10
Dahuk	North - KRG	553,662	52,081	9
Erbil	North - KRG	1,689,406	58,099	3
Sulaymaniyah	North - KRG	2,074,069	69,229	3
Basrah	South	2,094,788	680,140	32
Maysan	South	902,684	230,999	26
Muthanna	South	673,603	332,489	49
Dhi-Qar	South	1,770,244	572,976	32
Al-Anbar	West	1,627,592	344,069	21
Total		32,000,000	7,360,000	23

In November 2009, the Iraqi Ministry of Planning and Development Cooperation released the National Strategy for Poverty Reduction in Iraq for 2010 – 2014, prepared by the High Committee for Poverty Reduction Policies in Iraq. The strategy seeks to reduce poverty during this time period from the current poverty rate of 23% down to 16% by 2014.

To do so, microfinance is seen as part of the solution. The Iraqi economy consists of a vast number of MSMEs and informal sector activities that are the main source of livelihood for the majority of people. Lack of capital is a serious constraint to MSME development. People lack savings and may be indebted. Formal banking services are very limited. Developing MSMEs is seen by many as a solution for much needed job creation and reconstruction. Microfinance offers small-scale, affordable credit (loan sizes from \$500- \$5,000) and is seen as one of the keys to this solution. The approach towards developing financial services in Iraq has so far attempted to deal with the entire market segment of MSMEs, using the enterprise as the unit of analysis, rather than the poverty level of the individuals who own these firms. The enterprises are therefore funded on the merits of their potential rather than

¹⁰ Based on Confronting Poverty in Iraq 2011 Report by World Bank and Government of Iraq

¹¹ <http://musingsoniraq.blogspot.com/2011/01/state-of-iraqs-provinces.html> (Populations in Provinces adjusted to total population of 32million)

on the basis of their owner's standing in society. However, as the incidence of poverty at the household level becomes clearer through studies undertaken by the UN and the Government of Iraq to develop poverty measurement index, the focus on household levels will enable a broader strategy on inclusiveness and overall impact.

1.6 MICROFINANCE IMPRINTS IN IRAQ

Microfinance based on best practice standards in Iraq began in 2003 mainly as a tool to assist the victims of war and violence, and to help stabilize insecure areas. It has now become the sole provider of sustainable financial services for the poor and those excluded from the formal financial sector, including MSMEs. MFIs such as CHF International, Al-Thiqa (set up and supported by ACDI/VOCA), and Relief International (RI) established operations in Iraq in 2003, 2004 and 2006 respectively, through funding received from U.S. Government sources¹². Their operations, however, were limited to the less-violent areas in Iraq and to the semi-autonomous non-violent Kurdistan Region in Northern Iraq.

USAID-Izdihar¹³, a private-sector development and employment generation project funded by USAID from 2004 to 2008 and implemented by The Louis Berger Group, Inc., collaborated with the U.S. and coalition military forces in late 2006 to establish indigenous MFIs in each province. The goal was to ensure the presence of at least one MFI in each province to enable private sector growth. In supporting MFI development, USAID envisioned local institutions serving communities through strategies for delivering locally acceptable loan products, thereby filling an unmet market gap left by the larger players.

At that time security concerns impacted all economic development activities in Iraq. To alleviate these concerns, the military established civil-military operations centers (CMOCs) to provide oases of stability in otherwise violent regions. Allowing the MFIs to operate from CMOCs provided a relatively safe operational environment, lowering the risk for conducting financial operations that might otherwise have been impossible. Building relationships between MFIs and the military also served to provide the latter with information on economic activity in the areas of their operations.

USAID-Izdihar developed strategic partnerships with the Civil Affairs Section of the U.S. military to provide parallel funding streams for operational and loan capital. While the military (and later Provincial Reconstruction Teams or PRTs) paid operational costs of the local MFIs, USAID-Izdihar provided loan capital grants and intensive technical assistance. The MFI Al-Bashaer was established in 2006 in Baghdad, followed by Al-Aman in Kirkuk the same year. Building upon these models, USAID-Izdihar assisted in establishing local MFIs in Anbar Province (one of the most violence-prone provinces) as well as in Salah ad Din and Ninawa Provinces.

The U.S. military's role in developing Iraq's microfinance sector has been significant. PRTs, which were small civil-military units, served as intermediaries with local MFIs in conflict-prone regions, and helped to promote microfinance services within local communities. The PRTs were discontinued in second half of 2011 as US forces prepared their withdrawal from Iraq in December 2011.

In November 2006, the first-ever Iraq Microfinance Summit brought practitioners, donors, and other interested supporters from all over the world together to take stock of the Iraqi microfinance industry, outline the issues facing the industry and discuss donor objectives achieved through microfinance. This led to a consensus on six key strategies that collectively formed the Iraq Microfinance Strategy for the industry's future growth.

¹² Initial capital was provided by U.S. Coalition Forces, significantly augmented by support from USAID on a continuous basis.

¹³ Izdihar was a USAID funded private sector growth and employment generation project implemented by The Louis Berger Group and its joint venture partners in Iraq to support microfinance, SME lending, trade policy, investment promotion and business development services. The project worked at the federal and provincial levels in collaboration with the Central Government, Provincial Governments, Provincial Reconstruction Teams (PRTs), Military and other local NGOs. This multidisciplinary program ended in March 2008. A follow-on USAID program (named *Tijara*) is continuing the initiatives undertaken by the Izdihar project, building on the successes and addressing sector level challenges through a sector development approach.

2012 Status: Looking Back at the Iraq Microfinance Strategy 2006 Priorities

Priority 1: Clearly Defining What Microfinance Means in Iraq

Microfinance includes the provision of diverse range of loan products to the poor and MSMEs across all 18 provinces in Iraq. Loan size ranges from \$500-\$25,000 with more than 80% of current loan portfolio representing loans for income generating activities.

Priority 2: Enhancement of the Legal Framework

The Iraqi Government NGOs Directorate and Central Bank of Iraq have recognized the importance of extending financial access for the poor and those who are excluded from the mainstream financial system. CBI issued SME Finance Companies Ordinance, which underscores the enabling environment for microfinance in Iraq.

Priority 3: Capacity Building and Training

Over 784 microfinance practitioners have been trained on microfinance-related skills and knowledge. They include 12 certified Master Trainers in six CGAP modules on Financial Analysis, Human Resources Management, Delinquency Management and Interest Rate Settings, Product Development, Operational Risk Management and Accounting. SMFC has also introduced modules on Governance, Internal Audit, and Strategic business planning to help manage the risks and returns.

Priority 4: Transparency, Standards and Reporting

All Iraqi MFIs track their performance and report to donors and stakeholders using the Performance Monitoring Tool (PMT), which compiles performance results across each MFI's branches based on internationally acknowledged disclosure and reporting standards. USAID-Tijara has a Performance Monitoring System (PMS), a centralized database to which all respective PMT databases are exported, and then consolidated to generate overall industry performance ratios and indicators. The PMS also informs the Performance Classification Monitoring System (PCMS). The PCMS shows the evolution of MFIs and how they compare with their peers in the Middle East and North Africa (MENA) region based on type of institution (indigenous or international), number of borrowers, loan amounts outstanding, average loan size, portfolio-at-risk (PAR) for loans past due for more than 30 days, operating expense ratio (OER), case load, operational self-sufficiency (OSS), and financial self-sufficiency (FSS). Each of these indicators is assigned a score in order of importance to determine the overall category of the MFI and eventually the class into which it is categorized vis-à-vis its peer MFIs in the MENA region.

Priority 5: Developing a Microfinance Network

With the issuance of the NGO law, allowing the sector to legally register a national microfinance network, USAID-Tijara brought Iraq MFIs to a forum to institutionalize the network. The Iraqi MFIs adopted a Code of Conduct and Ethics for the sector as part of the network's ongoing initiatives. As a formal network, this entity will cater for the capacity building, advocacy, information dissemination and transparency needs of the industry. The Iraq Microfinance Network (IMFN) was formally registered and issued with the requisite certificate on April 26, 2012: it is now an independent institution with legal status to operate as the coordinating body which will play a key role in shaping and advancing an inclusive microfinance industry while also further strengthening the microfinance sector in the country. USAID-Tijara continues to support IMFN through technical and grant assistance to enable it to lead the microfinance industry upon close out of Tijara in January 2013.

Priority 6: Increasing Bank Linkages

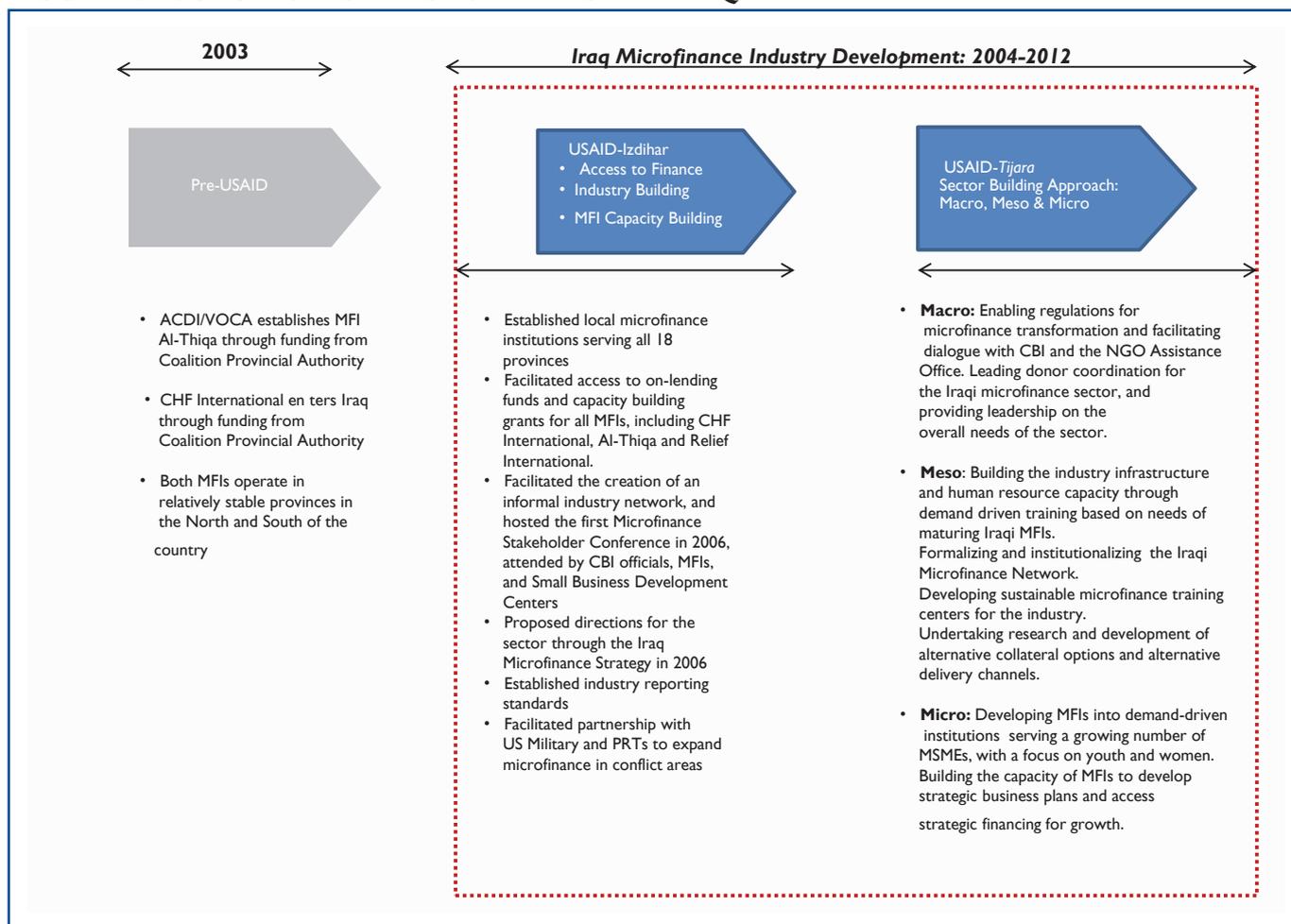
As the banking sector matures, government entities could enable access to low cost debt capital for MFIs through the two big state owned banks, however, based on the overall financial sector health in the country, linkages between the MFIs and banks will require more time.

Recent government pronouncements show that microfinance is gaining recognition among policy makers as an effective tool to enable economic growth and reduce poverty. In 2007, the GoI established microfinance programs with heavily subsidized annual interest rates (2% in 2007 and 0% in 2008). The government microfinance

program was started in mid-2007 by the Ministry of Labor and Social Affairs (MOLSA) as a pilot program and then expanded to all the provinces in Iraq except the Kurdistan Region. A similar program was developed by the Ministry of Industry and Minerals (MIM) for industrial SMEs. These government programs offer funds at an artificially low cost and create an unreasonable benchmark among potential borrowers, with some diverting their resources into lobbying in an attempt to qualify for these schemes. Furthermore, the modality of government disbursed loan funds is not timely for approved clients and additionally the unreasonable requirement of a one-time repayment of the total loan at the end of one year instead of industry recommended frequent repayments on a weekly or monthly basis greatly increases the risk of default. Even as economic theory suggests that a more flexible repayment schedule would benefit clients, microfinance practitioners emphasize that the fiscal discipline imposed by frequent repayment is critical to preventing loan default¹⁴.

Iraq's rapidly growing microfinance industry reached a milestone in March 2010 when the total number of microfinance branches and satellite offices across Iraq reached 100. By the end of June 2012, the number of outlets had increased further to 109. This underscores the success Iraq's MFI sector has achieved in its drive to provide wider access to quality financial services across the country.

FIGURE 4: EVOLUTION OF MICROFINANCE IN IRAQ



In March 2010, the NGOs Directorate approved a new law that moved beyond the previous one in which microfinance activities were implicitly referred to as illegal. The new law raises issues regarding interest rates and taxation rules for revenue generating NGOs; however, the NGOs Directorate has demonstrated a strong commitment to engaging with the microfinance sector and the NGO-MFIs to assist in providing financial services to low-income Iraqis. Potential partnerships with government ministries such as MOLSA and MIM are taking shape as MFIs continue to demonstrate competency at delivering sustainable financial services for the poor.

¹⁴ Repayment Frequency and Default in Microfinance, Harvard University Press, 2009

FIGURE 5: MICROFINANCE OUTREACH ACROSS IRAQ AS OF JUNE 2012

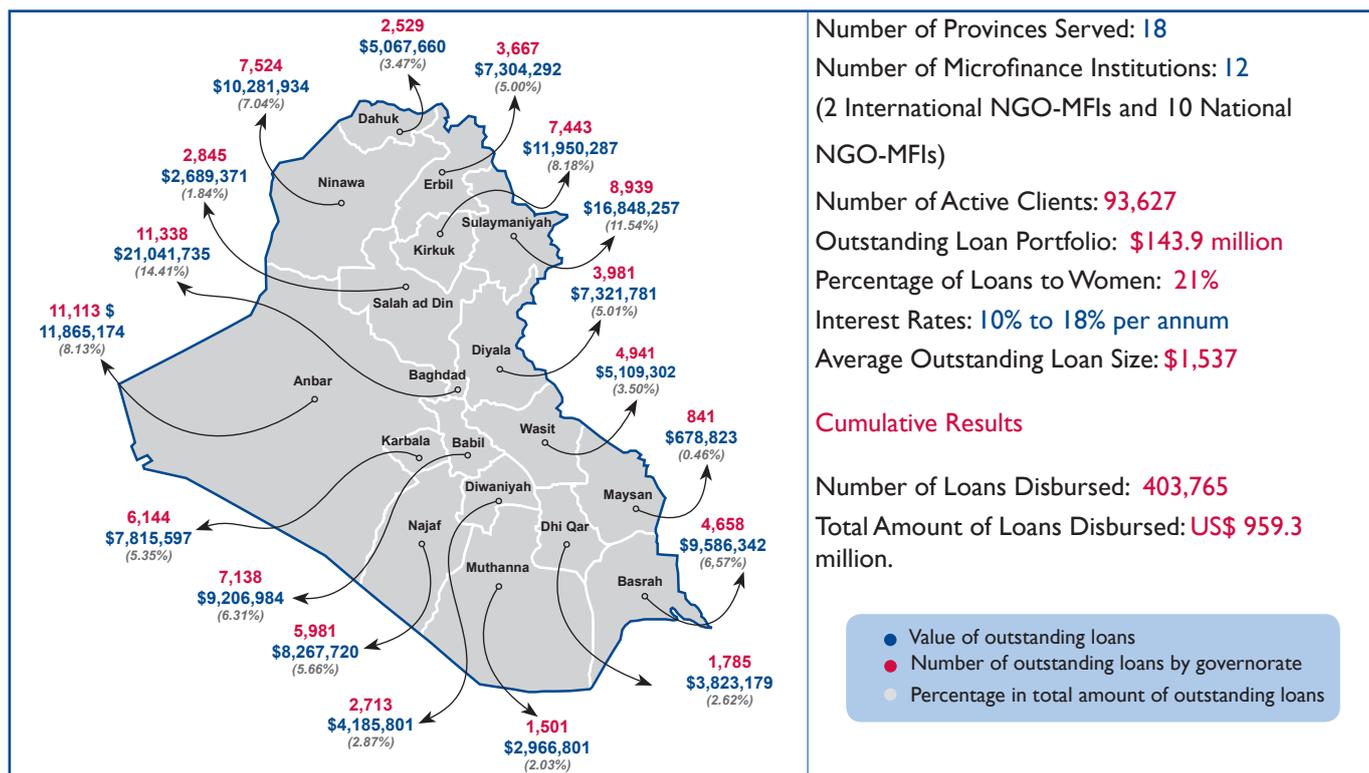


TABLE 5: POVERTY ADDRESSED BY MFIs IN IRAQ AT JUNE 30, 2012

Province	Number of Poor ¹⁵	No. Poor Clients Served by MFIs	% Poor Clients Reached by MFIs	No. of Poor ¹⁶ Indirectly Reached	% of Poor Reached
Baghdad	1,029,102	11,151	1.08	78,057	7.58
Babil, Hilla	753,837	7,053	0.94	49,371	6.55
Karbala	362,957	5,988	1.65	41,916	11.55
Najaf	166,244	5,765	3.47	40,355	24.27
Diwaniyah	384,060	2,736	0.71	19,152	4.99
Wasit	410,575	5,015	1.22	35,105	8.55
Diyala , (Ba'qubah, Khanaqeen, Kifri)	572,282	3,934	0.69	27,538	4.81
Ninawa, Mosul, Tala'afar	716,287	7,339	1.02	51,373	7.17
Salah ad din	526,643	2,667	0.51	18,669	3.54
Kirkuk	97,932	7,346	7.50	51,422	52.51
Dahuk	52,081	2,437	4.68	17,059	32.75
Erbil	58,099	3,688	6.35	25,816	44.43
Sulaymaniyah	69,229	8,805	12.72	61,635	89.03
Basrah	680,140	4,669	0.69	32,683	4.81
Maysan	230,999	838	0.36	5,866	2.54
Muthanna, Samawa	332,489	1,503	0.45	10,521	3.16
Dhi-Qar, Nassriya	572,976	1,790	0.31	12,530	2.19
Anbar	344,069	10,903	3.17	76,321	22.18
Total	7,360,000	93,627	1.27	655,389	8.90

¹⁵ Musings On Iraq The State Of Iraq's Provinces05291012.htm (adjusted)

¹⁶ Based on a factor of 7 as the accepted family size in Iraq

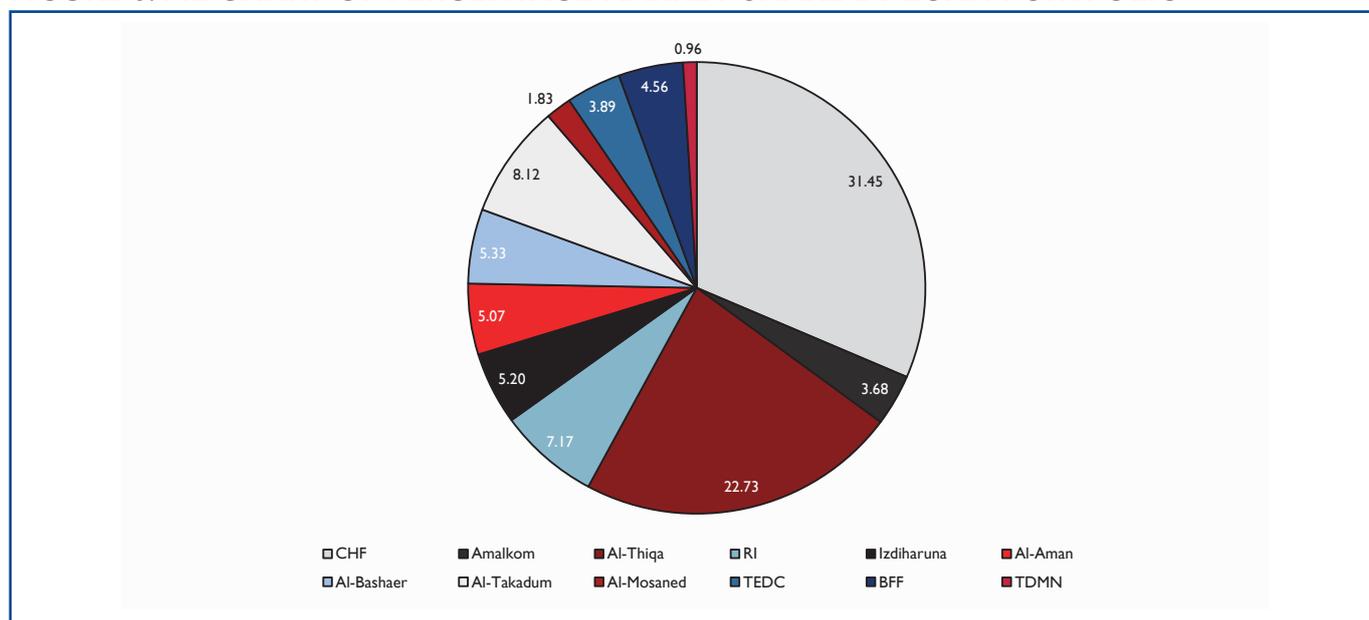
As Iraq stabilizes and innovation emerges, the microfinance sector is maturing. Innovation will emerge in the use of alternative collateral options and alternative delivery channels such as leveraging the expansive outreach of the country's mobile telephone network of over 20 million subscribers. Iraqi MFIs are recognized as providing valuable community service with their proximity to clients. Together, the 12 MFIs provide financial access to 93,627 active clients as of June 30, 2012, representing MSMEs in the country. MSMEs are generally more labor-intensive than capital-intensive and have relatively high production costs largely because raw materials are purchased in smaller quantities; their owners lack adequate technical experience in production, accounting, administration and stock control and most are unregistered and family operated. The entrepreneur usually gets the small amount of finance needed from savings or from family. In view of their small size and lack of acceptable collateral, MSMEs are viewed by formal credit providers as risky and therefore they face a major challenge in accessing additional capital to grow. Since the informal credit providers typically lend at rates that may jeopardize their survival (the differential could be as high as 40 points or even higher), the MSMEs are now turning to the Iraqi MFIs for their funding needs thereby accessing needed funds to enhance their operations and grow. It is therefore critical that the microfinance industry be supported by all stakeholders to continue this important contribution to growth of the economy.

TABLE 6: MARKET SERVED BY IRAQI MFIs

Microfinance Institutions	Gross Loan Portfolio ((GLP	Percentage Market Share by (%) Portfolio
Al Aman	\$7,297,975	5.07
Al Bashaer	\$7,675,300	5.33
Al Mosaned	\$2,637,395	1.83
Al Tadamun	\$1,379,576	0.96
Al Takadum	\$11,682,240	8.12
Al Thiqa	\$32,718,236	22.73
Amalkom	\$5,297,077	3.68
Bright Future Foundation (BFF)	\$6,568,213	4.56
CHF International	\$45,265,018	31.45
Relief International	\$10,319,338	7.17
Izdiharona	\$7,486,410	5.20
Tallafar Economic Development Center (TEDC)	\$5,605,861	3.89
Total	\$143,932,639	100

USAID seeks to provide a deeper understanding of microfinance and provide a basis for a policy level consensus on the business, prospects, and contributions of microfinance in Iraq's economic development. With over 403,765 loans made to micro and small enterprises since 2004, the MFI sector is poised to play a greater role in the overall development of MSMEs at both the retail industry and policy levels.

FIGURE 6: PIE CHART OF PERCENTAGE MARKET SHARE BY LOAN PORTFOLIO



Microfinance Enables Better Lives in Northern Iraq

Attracted by political stability and financial opportunities, hundreds of Kurds are returning to Northern Iraq to build new livelihoods thanks to microfinance loans from USAID-Tijara funds through Bright Future Foundation.



by David Devoss

Iranian Kurd Fatima Ahmad left Iran because of discrimination. Today, her Soron beauty salon clears a monthly profit of \$400 on revenues of \$800 thanks to two microfinance loans worth \$4,000.

According to the Kurdish Regional Government's Bureau of Migration and Displacement, 250 Kurdish families or about 1,500 people leave Iran every year to reestablish themselves in their ancestral homes. They are joined annually by 2,400 Kurds from Europe who return under International Organization for Migration's (IOM's) voluntary repatriation program.

Many of the returnees settle in Soron, a mountain town in the province of Erbil. The city has 125,000 residents, 64% of whom are returnees from Iran. Between 1974 and 1989 more than one million Kurds fled Iraq to escape persecution from Saddam Hussein. Now Kurds are returning so rapidly that Soron's population is expected to grow by 50,000 over the coming decade.

Although she was born in Iran, Fatima Ahmad could not obtain Iranian citizenship because her parents were Iraqi Kurds. "I was alive but had no life," she explains. "I couldn't own property or get a passport. I couldn't even travel inside the country without police permission."

So four years ago Fatima, then 25, stuffed everything she had into one suitcase and walked into Iraq, eventually arriving in Soron. "In 2009 I received a microfinance loan of \$2,400 and opened this beauty shop," she says. "I average 15 customers a week, which gives me monthly revenues of \$800, half of which is profit." Recently, Fatima got a second loan of \$1,600 and used the money to buy higher quality cosmetics. "One thing I know for certain," she says. "I never would have gotten a microfinance loan in Iran."

Nearly all of the merchants speak Farsi at the Kirkuki market in Soron. Pictures of Isfahan decorate the coffee and sheesha bar operated by Ruzgar Yahya, 31. Taken to Iran when they were children, Ruzgar and his three brothers returned to Kurdistan in 2004 because of the safety provided by American troops. Today, thanks to four microfinance loans totaling \$7,000, they have four shops in the market and together employ 15 people. "USAID funded microfinance loans allow a dozen families to lead productive lives," says brother Farhad Yahya.



by David Devoss

Farhad and Ruzgar Yahya fled Iran in 2004 along with their two brothers. The Kurdish family now owns four shops in Soron thanks to microfinance loans totaling \$7,000. Ruzgar's sheesha bar is popular with Kurdish migrants from Isfahan.

Fatima Ahmad and the Yahya brothers received their loans from the Bright Future Foundation(BFF), one of 12 microfinance institutions receiving technical assistance and grants from USAID-Tijara. USAID established Iraq's microfinance industry to help aspiring Iraqi entrepreneurs who lacked the credit and connections necessary to apply for a bank loan. People like Amina Mohammad, 31, an impoverished seamstress who is raising five nieces and nephews who were orphaned when Amina's sister died.

In 2000, Amina left Iran with only enough money to buy a pedal-powered sewing machine. In 2009, she finally learned about BFF and applied for a \$1,000 microfinance loan which she used to purchase an electric sewing machine. "I can make more money with an electric machine because it sews sequins," she confides with a smile. Amina works with her sewing machine every night making clothes for the children and traditional Kurdish dresses. "Women see a dress they like on TV and then call me to duplicate it." Recently, however, she has been supplementing her \$500 monthly income from sewing by spending her days on the streets of Soron, working as a loan officer for the Bright Future Foundation.

"Amina is a very honest, hard working person who people find easy to talk to," says Ali Suhail, BFF's supervisor of loan officers. "She is exactly the sort of person we need in the Iraqi microfinance industry."



"I never could have received financing in Iran," says seamstress Amina Mohammad. "The government there won't give Kurds ID cards, much less bank loans."

CHAPTER 2



by David Devoss

THE IRAQI MICROFINANCE INDUSTRY: EMERGING TRENDS

Korsheed Hamed Hafdullah, 48, owns a yogurt factory in Dahuk. A \$2,500 microfinance loan from the Bright Future Foundation allowed him to buy plastic containers from Turkey that hold his yogurt.

Informal Definition of MSMEs

in Iraq:

Micro Enterprises

Loan Size: Below \$5,000

Number of Employees: 1-2

Small Enterprises

Loan Size: \$5,001 - \$250,000

Number of Employees: 3-9

Medium Enterprises

Loan Size: Over \$250,000

Number of Employees: 10-29

Note: The loan size takes precedence in defining the category of enterprise with regard to businesses that are usually classified under MSMEs. Therefore, this should be understood in the context of MSMEs referred to in this publication. Small and medium enterprises in terms of number of employees are based on guidelines provided by Iraqi Government's Central Organization for Statistics and Information Technology (COSIT).

Iraq's microfinance sector is dynamic.

In 2011, financial products diversified, outreach to the poorest deepened, a greater percentage of women was reached, operational efficiency continued to improve and the government demonstrated a greater commitment to creating an enabling environment for sustainable microfinance services by Iraqi MFIs.

Iraqi MFIs continue to exhibit scalability and scope as they broaden access and diversify their markets through client segmentation. This is characterized by three main types of average loan sizes: \$500 (very-poor clients), up to \$5000 (micro-enterprise clients) and \$5,001 - \$25,000 (small enterprise clients).

This report identifies seven major trends and notes how those trends will shape outcomes in the years to come, e.g. MFIs achieving commercial viability stage of growth and deepening outreach to poorer clients. MFIs are progressively mainstreaming into the formal financial sector, signified by diversifying sources of capital (from debt, equity and donors), the development of an enabling environment, and the adoption of the Microfinance Code of Conduct and Ethics. All of these are facilitating the mainstreaming of MFIs and making the overall financial sector ever more inclusive.

TREND 1: MFIs REACHING OUT TO POORER AND VULNERABLE CLIENTS

In 2011 the microfinance industry continued to build on achievements made previously and continued to play a greater role in deepening outreach to poorer clients including women, especially in southern and central Iraq where poverty is greater. Since the introduction of the solidarity group lending (SGL) methodology among four Iraqi MFIs in 2009, the minimum microfinance loan size reduced to \$500 thereby facilitating access to financial services for those clients without the minimum collateral required by MFIs as security for individual loans (see Chapter 4 for further discussion on collateral options in Iraq). With 23%¹⁷ of Iraq's population living under \$2.20 per day, the market potential is large. With USAID-Tijara's technical assistance, MFIs continue to further refine their downscaling strategies in order to capture this market more effectively to achieve their overall mandate of enabling financial inclusion for those at the bottom of the pyramid. One of the key downscaling strategies is the introduction of poverty loans through the Solidarity Group Lending (SGL) methodology which provided opportunity for MFIs to lower their loans from an average of \$2,500 - \$3,000 down to \$500 - \$800 and thereby reach the poor and women previously excluded. These efforts have been expanded further and facilitated through additional initiatives introduced by USAID-Tijara which include the Iraq Youth Initiative (IYI) and the Iraq Vulnerable Groups Support Initiative (IVGSI) and have also been directed to women headed households thereby making it possible to reach these disadvantaged populations previously excluded from the finance sector. Additionally, MFIs are developing new products, alternative collateral options and delivery channels to promote and facilitate lending to these groups.

TREND 2: MFIs ARE MORE CLIENT-RESPONSIVE AND ENTERING THE MAINSTREAM FINANCIAL SECTOR

MFIs are now entering the mainstream financial sector domain as part of their operations and they are accommodating clients by providing larger loan sizes ranging from \$5,000-\$25,000 for small businesses. These business financial services for small enterprises can contribute to economic development through employment generation, which increases stability in the current high unemployment environment in Iraq. Demand for such finance is increasing as MSMEs grow and since collateral requirements of banks are restrictive and thereby cause financing gaps for MSMEs in Iraq, MFIs whose collateral requirements are less stringent are graduating their clients

¹⁷ Based on the 2006/07 Household Socio Economic Survey, Central Organization for statistics and Information Technology (COSIT), Government of Iraq

and stepping in to provide such financing. Additionally, the MFIs are now using alternative collateral options and also offering new products (including agricultural loans and micro-insurance) which are fulfilling the needs of this important part of the finance market and thereby creating opportunities for growth of the economy. Furthermore, MFIs are responding to the need for Islamic loan products of which demand and market share is growing. These developments indicate the important role MFIs are taking and the contribution they are making in the finance sector in Iraq and generally for growth of the economy.

TABLE 7: COMPARING MFIs AND COMMERCIAL BANKS IN IRAQ

Indicators	MFIs	Banks
Number	12 MFIs	State (7); private banks(39)
Number of Branches	109 outlets	State (391) ; private banks (383)
Loan Size	\$500 - 25,000	For SME's about \$15,000 at disbursement
Interest Rate	10% to 18%	Presently in the 10% - 13% range
Repayment Period	12 months	Loans typically under two years
Collateral Requirements	1) Government Employee guarantees 2) Solidarity Group: peer to peer	Usually physical collateral if > \$10-15K
Services Offered	1) MSME Loans 2) Agri-business Loans 3) Housing Loans 4) Trade Loans 5) Taxi Loans	Overdraft, trade finance, deposits and money transfers, loans and guarantees.
Loan Processing Time	2-3 Days	Highly variable, usually 30 to 60 days, but in some cases much less and in others much more.

Substantial funding continued to flow into the country for SMEs, and has been mainly directed to MFIs, which have proven competency of offering the 'right' type of services required by the small enterprises in the country. The development of SMEs is recognized as an integral factor to unleashing the Iraqi entrepreneurial spirit. These enterprises need access to capital and MFIs will be key partners in providing such capital for facilitating financial inclusion for these businesses.

TREND 3: IRAQI MF INDUSTRY IS "INVESTMENT READY" AIDED BY ENABLING REGULATIONS

Since 2004, USAID and other US Government Agencies have provided over \$114 million in grant funding for loan and operational capital to MFIs. Other donors have in recent years provided additional funding bringing the total funding to the industry to \$122.4 million as of June 30, 2012.

The microfinance sector in Iraq is fast gaining global recognition as an "investment-ready" destination among bilateral and multilateral donors and other more commercially oriented development investors that are expressing an interest to invest in the industry. This recognition is being facilitated by enabling regulations issued by the CBI. It is fitting that the CBI and the NGOs Directorate have continued to increasingly interact with MFIs in the country and also with the regional microfinance stakeholders as part of USAID's sector building interventions at the macro policy level.

As Iraqi Government ministries MOLSA and MIM review their success/failure of the subsidized loan program through technical feedback from USAID-Tijara, the government will work towards streamlining its interventions at the policy level and is likely to partner with Iraqi MFIs to extend sustainable financial services to the target population (the poor and women, including Iraqi vulnerable groups, who have been previously marginalized from the sector). USAID has continued to play a leading role in providing timely financing to Iraqi MFIs for scaling-up outreach through a holistic sector development approach, and it is poised to play an instrumental role in ensuring coordination among donors and capital providers to appropriately address gaps and continue building microfinance best practices in Iraq. It is worthy of note that Iraqi MFIs have set very high performance standards that give confidence to donors and international investors thereby enhancing the global recognition that is opening up possibilities for additional investments into the sector.

TREND 4: IRAQI MF INDUSTRY ADOPTS INTERNATIONAL BEST PRACTICES FOR CLIENT PROTECTION

In 2010, Iraqi MFIs, supported by USAID-*Tijara*, drafted and adopted the Microfinance Code of Conduct and Ethics. This marked the emerging leadership among MFIs to take stock of the sector and promote good ethical practices. The Code adopts principles of client protection¹⁸ prescribed by Consultative Group to Assist the Poor (CGAP), which include transparent pricing, appropriate loan collection behavior, ethical staff behavior and privacy of client data. Further to development of this important Code for client protection, the MFIs are reducing their interest rate as they achieve scale of outreach and also as they respond to improved efficiency and greater competition. With adoption of best practices, MFIs also developed their reporting to MIX Market (Microfinance Information eXchange) which was one of the key accomplishments of the sector in 2011. This achievement is indicated by their accurate, timely and transparent reporting, measured by MIX Market classification whereby two out of 12 MFIs were awarded 4 Diamond Ratings, eight with three Diamond and the remaining two with two Diamond Ratings. USAID-*Tijara* continues to encourage partner MFIs to report to MIX Market to ensure transparency and visibility of the MFIs on the international stage, which helps to improve their profile to stakeholders, particularly potential investors, and the general public.

TREND 5: IRAQI STAKEHOLDERS BECOMING MORE KNOWLEDGEABLE ABOUT MICROFINANCE

USAID-*Tijara* has continued its leadership and efforts to coordinate and communicate with regulatory authorities in Iraq, like the NGOs Directorate and the CBI and with other donors such as the World Bank and UNDP to synergistically create an enabling environment that is more conducive for expanding and deepening the outreach of quality financial services. These efforts are directed towards enhancing the legal and regulatory framework to support further expansion and growth of the MFIs to help in meeting part of the demand for inclusive financial services. In the process, stakeholders are becoming more knowledgeable about the various measures taken by USAID-*Tijara*, such as: a) Sharing of the consolidated quarterly industry report with the NGOs Directorate and the CBI, b) Organizing Stakeholders' participation in Sanabel Network Conference, CGAP Policy Forum and other learning events, and c) Developing a relationship with the NGOs Directorate such that the Directorate has become proactive in sharing information relevant for MF industry. As a result of USAID-*Tijara*'s leadership and interventions, the Iraqi microfinance industry is already benefiting from an improved enabling environment with recognition and acceptance by the authorities (CBI and NGOs Directorate) as an important component of the finance sector; however, some challenges, which include unclear tax rules and required additional legislation to allow the current NGO MFIs to transform into NBFIs, still remain.

TREND 6: IRAQI MFIs INTEGRATING INTO NATIONAL, REGIONAL AND GLOBAL NETWORKS

The Iraq Microfinance Network (IMFN), which started as an idea by USAID-*Tijara* in August 2010, was formalized and issued with a Certificate of Registration on April 26, 2012. This made it an independent institution with legal status to operate as the coordinating body, which will play a key role in shaping and advancing an inclusive microfinance industry while also further strengthening the microfinance sector in the country. After registration, the IMFN held its first general assembly meeting at which all the 12 member MFIs were represented and which was witnessed by USAID-*Tijara* and the NGOs Directorate. With its formalization, the IMFN will be the focal point and the meso-level institutional means by which USAID-*Tijara* will be able to transition its support for and presence within the industry. When that happens upon *Tijara*'s scheduled close-out in January 2013, the IMFN will be the link between the microfinance industry and national stakeholders and also with regional and global networks and it will be expected to play a vital role in sustaining an inclusive microfinance sector in the country. All Iraqi MFIs, in addition to being members of the IMFN, are also members of Sanabel, the Microfinance Network of Arab Countries. This connection with the IMFN and Sanabel will ensure that Iraqi MFIs have the opportunity to take advantage of the educational and industry development initiatives that are channeled through these networks by various donors and stakeholders. In addition, the MFIs have also been benefiting from the SEEP Network initiatives in trainings and relevant publications. These linkages will ensure that Iraqi MFIs stay abreast of international microfinance best practices and be able to maintain the high performance standards already achieved.

¹⁸ <http://www.cgap.org/p/site/c/template.rc/1.26.4943/>

TREND 7: IRAQI MFIs ARE “DRAWING UP” ROADMAPS FOR THEIR FUTURE DEVELOPMENT

USAID-*Tijara* has worked with its partner MFIs over the years to develop sustainable financial institutions that offer inclusive financial services to Iraqi micro, small and medium size entrepreneurs including the poor and women. In the process it has conducted operational assessments of all the institutions and identified their weaknesses and made appropriate recommendations for improvement. Furthermore, USAID-*Tijara* has conducted workshops on good governance for the partner MFIs and thereby helped to institutionalize robust governance systems for effective governance and oversight. Subsequently USAID-*Tijara* has helped seven of the partner MFIs, which do not have international representation, to prepare their strategic business plans (SBPs). Strategic business planning is one of the key management activities that can help an MFI achieve the mission of poverty alleviation while also pursuing a path that leads to long term sustainability. It is therefore critical that Iraqi MFIs, whose mission is to provide inclusive financial services especially for the poor and women while also working towards long term sustainability, should have a procedure for preparing SBPs that guide their operations to achieve their stated objectives. This procedure should also include the preparation of detailed financial and operational budgets that identify and guide management on the factors and plans that are essential for the institution’s success. Those factors include design of diversified financial products which meet clients’ needs as well as plans for growth of outreach that lead to institutional sustainability. Comprehensive SBPs effectively managed and implemented by MFIs can be a source of confidence for stakeholders and investors. These initiatives by USAID-*Tijara* are part of the steps taken to develop a sound microfinance industry comprised of MFIs with good governance and oversight systems and plans enabling them to offer inclusive financial services that ensure long term sustainability.

Note to update Transformation of NGO MFIs trend status

In last year’s report, transformation of MFIs into NBFIs was noted as one of the trends expected to shape the microfinance industry in the future, however, subsequent to the publication, the CBI and the NGOs Directorate made a categorical clarification that under the current legal framework, it will not be possible for NGO MFIs to transfer their capital and assets to either LLCs or JSCs, the expected model of operation for NBFIs. This clarification made it clear that transformation of the partner MFIs will not be possible within the lifetime of USAID-*Tijara* program, which is scheduled to close out in January 2013. In spite of this, USAID-*Tijara* will continue its leadership and intensify efforts to coordinate and communicate with other donors such as the World Bank and UNDP to synergistically mold an enabling environment more conducive for expanding and deepening the outreach of quality financial services especially for the poor and women.

Sustainable Microfinance “Breathes” New Life into Halabja, a Booming City Rising from the Ashes

The goal of USAID-*Tijara* is to create strong, sustainable institutions that will continue to thrive after the *Tijara* program ends. The success of this policy already can be seen in the work the Cooperative Housing Foundation is doing to revive Halabja, a bustling Kurdish city in southeastern Sulaymaniyah Province.

One of 12 microfinance institutions receiving advice and technical support from USAID-*Tijara*, CHF has provided 336 microfinance loans worth \$768,000 to the people of Halabja. An additional 32 loans totaling \$54,700 are outstanding. The loans, underscore the economic viability of CHF and the ability of Iraq’s microfinance institutions to breathe life into impoverished corners of the country.

Twenty-five years ago, Halabja did not appear to have much of a future at all. On March 16, 1988, it was bombed by Saddam Hussein’s cousin Gen. Ali Hassan al-Majid and then blanketed with poison gas. About 5,000 Kurds were killed while an additional 6,000 were left to suffer life threatening injuries. To make the devastation complete, Ali then systematically reduced Halabja to rubble and forced survivors to move to a location where the streets were shaped to resemble the letters in Saddam’s name. The genocidal attack forever earned him the sobriquet, “Chemical Ali.”

But the town of Halabja refused to die. Today, ninety percent of the people forced to leave have returned. Entrepreneurs are starting small businesses thanks to CHF microfinance loans. At the end of the day many go home to new houses built with \$25,000 construction grants from the Kurdish Regional Government.

Dilawar Yasin Mahmud was a newborn baby when his parents carried him away from gas clouds smelling like sweet apples. “My father used wet blankets to protect my mother from the gas,” Dilawar says. “My family survived but my father’s lungs were ruined. He had difficulty breathing until the day he died.”

Dilawar opened a neighborhood mini market at age 16, but his business did not grow until he received a \$1,800 loan from CHF that allowed him to buy a freezer. Dilawar’s ability to sell ice cream set his store apart from the competition and before long children were insisting their parents shop with him.

“The freezer gives me a competitive advantage,” he smiles. “If people want ice cream on a hot summer day they have to come to me.”

CHF’s role in bringing Halabja back to life is not lost on Kuran Adham Rahim, the town’s 40-year old mayor. “CHF provides funds to start or expand a business without all the complexity of a bank loan,” he says. “Microfinance is making it easier for our economy to grow.”



Dilawar Yasin Mahmud sells ice cream from a freezer purchased with an \$1,800 microfinance loan from CHF.



Yadgar Ibrahim Ali used microfinance loans worth \$9,500 to open a photography studio and buy a digital printer.

Two CHF loans collectively worth \$9,500 enabled wedding photographer Yadgar Ibrahim Ali, 29, to open a studio on Halabja’s main street and purchase a digital printer from Japan. “A successful photography studio must have quality equipment,” he confides. “People come to me for crisp, quality negatives instead of driving to Sulaymaniyah.”

Yadgar is optimistic about Halabja’s future. The moment his second loan is repaid he plans to apply for a third. “I’ll use it to hire a second employee and buy an even larger printer,” he smiles.



CHAPTER 3

by David Devoss

BUILDING AN INCLUSIVE FINANCIAL SECTOR IN IRAQ

Dahuk factory owner Farzand Abdul Aziz Mohammed, 42, manufactures Fiberglass splash guards for residential and commercial kitchens and bath rooms. He used an \$8,800 loan from the Al-Thiqa Small Business Loan Fund to buy countertop templates and 33 different shades of pigment color Fiberglass.

3.0 WORKING FOR GROWTH OF IRAQ'S MICROFINANCE INDUSTRY

USAID-*Tijara*'s work with its partner MFIs has helped them address their challenges for growth. MFIs have been able to focus on opportunities to enhance their range of products and delivery systems thereby contributing to improving the environment for inclusive financial services that ensure the poor and women previously excluded will henceforth have access to funds they need for their small businesses. USAID-*Tijara* is continuing to use the consensus global financial sector development approach for building an inclusive financial sector at the three hierarchical levels viz macro, meso and micro. This approach also ensures that USAID is simultaneously accomplishing the five priority areas for the financial sector development as agreed with USAID/Iraq at the 2011 stakeholders' conference. The five areas include:

1. Developing, registering and operationalizing the Iraq Microfinance Network (IMFN) such that it will perform advocacy, capacity building and information clearinghouse role to promote transparency and sustainability in the MF sector.
2. Good governance in partner MFIs through effective performance of fiduciary, supervisory and management development responsibilities.
3. Development of diverse financial products and flexible collateral options through suitable delivery channels to facilitate greater outreach especially to the poor and women.
4. Assisting the policy makers in reforming the legal and regulatory regimes for a robust and inclusive financial sector.
5. Creating effective dialogue among key stakeholders (Gol, KRG, CBI, other donors and investors etc.) to make coordinated efforts in developing an inclusive financial sector.

Using the sector development approach, USAID-*Tijara* will continue its interaction at the macro level by working with relevant Iraqi government authorities in helping MFIs achieve the key objective of deepening and increasing outreach of inclusive financial services, especially for the poor and women, across both urban and rural areas throughout Iraq.

At the meso level, the objective of registering the Iraq Microfinance Network (IMFN) has been achieved and IMFN is now officially recognized as the network institution that will increasingly take over direct support of its constituent members upon close-out of the USAID-*Tijara* program.

At the micro level, work to build on progress made in previous years is continuing and it is helping individual MFIs achieve greater operational effectiveness and efficiency. This is done through follow up to ensure implementation of recommendations made by USAID-*Tijara* in its operational assessment reports for all MFIs, and also through enhancing the capabilities of the MFIs' governing boards of directors, and through development and implementation of their strategic business plans for long term growth and profitability. This work, by USAID-*Tijara* to enable its partner MFIs, is expanding financial inclusion for the target 1.1 million households living below the poverty line of U.S. \$2.20 per day as the institutions apply international standards of best practice for delivering sustainable financial services to the poor.

3.1 VALUE CHAIN INTERVENTIONS FOR SCALING-UP FINANCING TO MICRO, SMALL AND MEDIUM ENTERPRISES

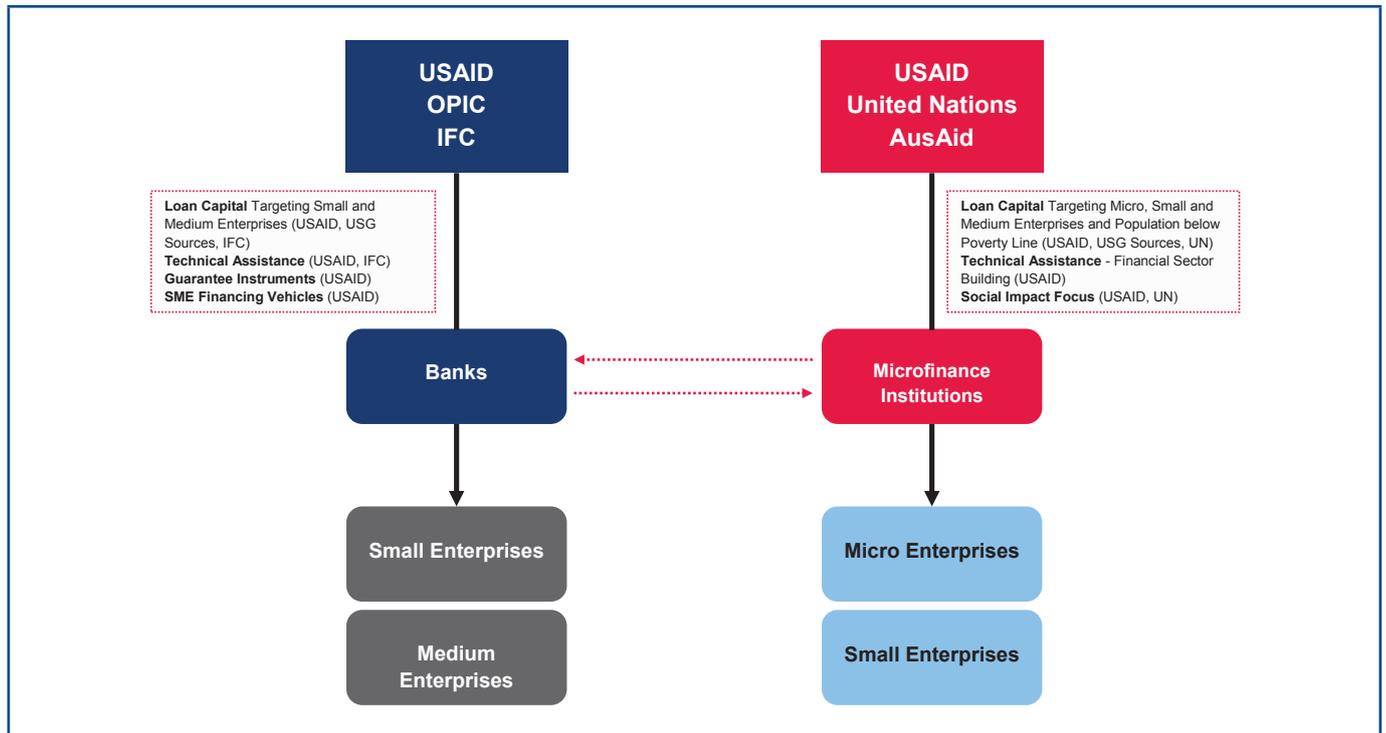
MSMEs are recognized as integral contributors to economic growth through several pathways that go beyond job creation, such as entrepreneurship, economic dynamism, linkages in value chains and societal development. MSME growth is positively associated with economic growth. For these enterprises to grow, industry dynamism and linkages within value chains are important.

Iraq's National Development Strategy encourages the establishment of MSME projects and develops appropriate financing mechanisms for them. In Iraq, funding for micro enterprises is provided by microfinance institutions, informal lenders and family members. Lending to MSMEs is just beginning, promoted predominantly by donors through banks and now including MFIs as financiers. Banks have traditionally viewed MSMEs as risky due to their vulnerability to market fluctuations, their relatively short operating history and their lack of audited accounts. Ability to lend to the SMEs is hindered by:

- A deficit in skills, both managerial and technical, in the banking industry
- A legal/regulatory infrastructure that does not facilitate transactions, e.g., no modern bankruptcy law
- Inadequate information technology (IT) infrastructure
- Lack of an awareness of market economics
- Lack of credit bureaus

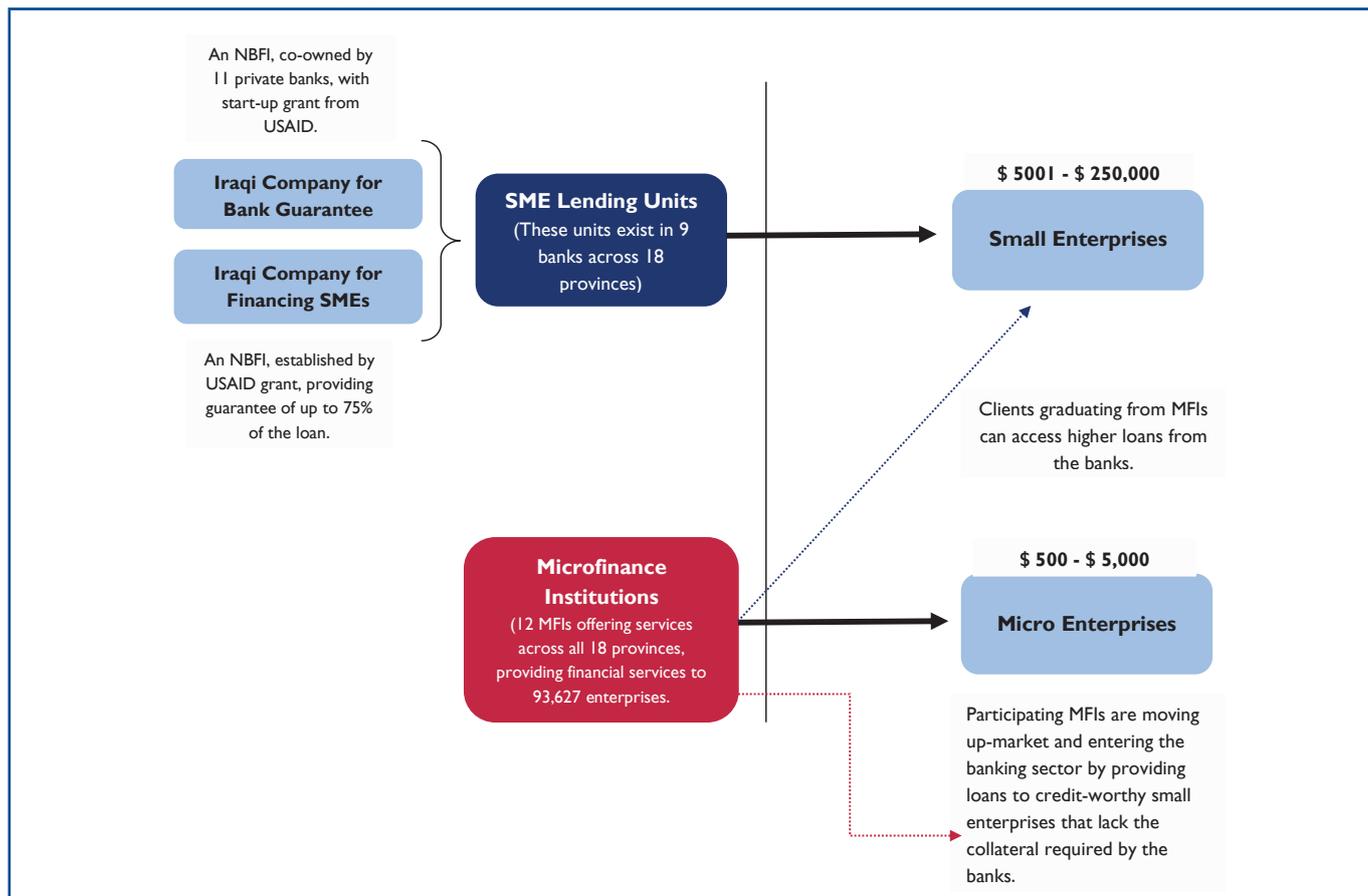
Support for MSMEs is largely missing within government initiatives. However, donors such as USAID, the World Bank, International Finance Corporation (IFC), Overseas Private Investment Corporation (OPIC) and the U.N. have been active in facilitating financing.

FIGURE 8: DONORS INTERVENTION FOR MSME FINANCING



In order to build sustainable financing interventions for MSMEs, USAID has actively promoted the development of a broader ecosystem that looks at value chain financing for MSMEs. Through USAID-*Tijara* and its implementing partners, two non-banking financial institutions (NBFIs) were established in 2006 and 2009, namely the Iraqi Company for Bank Guarantees (ICBG) and the Iraqi company for financing SMEs (ICF-SME). Co-owned by a group of private sector banks and financed through USAID grants, these institutions provide the necessary confidence to banks for extending loans ranging from \$5,001 to \$250,000 to MSMEs in Iraq. ICBG also provides on-site support to bankers on credit analysis and loan administration through its extensive training programs focused on replacing asset-based lending with modern cash-flow based lending.

FIGURE 9: USAID ENABLING ACCESS TO FINANCING FOR MICRO AND SMALL ENTERPRISES



As new donors enter the market and increase their collaboration with ongoing initiatives undertaken by USAID, the focus on MSMEs will scale-up. Furthermore, key challenges such as technical capacity of banks and MFIs and even government will be addressed in order to facilitate broader financial sector reform for inclusive economic growth. MFIs are increasing their outreach to micro enterprises and in addition to this some of them have been moving ‘up market’ to provide financial services to small enterprises since 2009.

Focus on MSMEs will grow beyond financing interventions. Such growth will include a broader value chain that is sector specific in order to increase MSMEs’ capacity and relevant options. For example, USAID-Tijara launched the Iraqi Youth Initiative (IYI) in 2010, which provides training, consultative business planning support to start-ups, and facilitates financing through a three-way partnership between small business development centers (SBDCs), MFIs and young entrepreneurs. In 2012 further initiatives were launched specifically targeting Iraqi vulnerable groups and women as more detailed under 4.5 and 4.6 in chapter four.

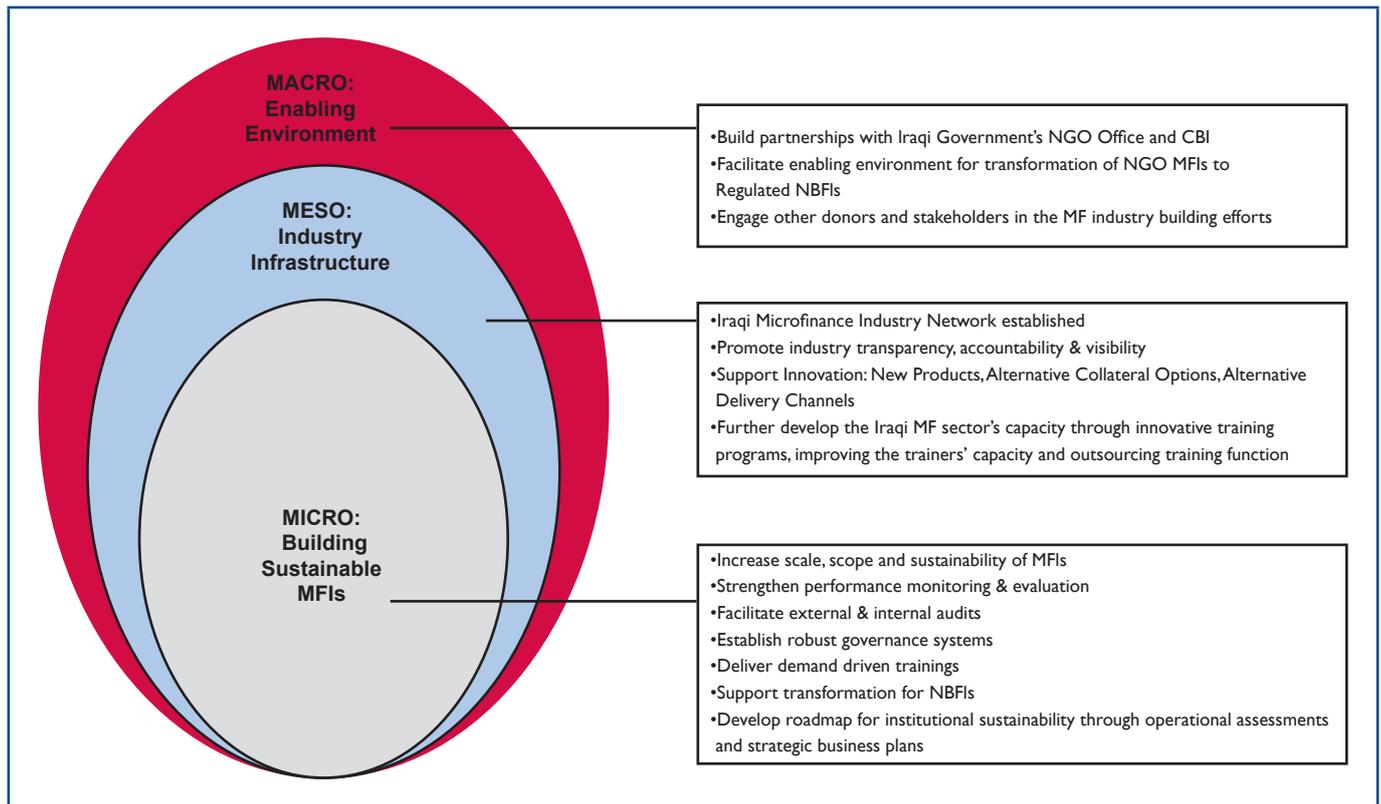
A broader MSME development strategy is being implemented, which seeks to leverage banks and MFIs as financial intermediaries for the Iraqi MSMEs. The strategy emphasizes sector specific development in order to create the required volume and network of entrepreneurs for strengthening their linkages to markets and relationships with suppliers and buyers.

3.2 USAID LEADS SECTOR DEVELOPMENT APPROACH IN IRAQI MICROFINANCE INDUSTRY

As the Iraqi microfinance industry grows, USAID and its implementing partner, USAID-Tijara, have together taken the lead in augmenting the sector development approach for achieving inclusive financial services for greater impact on the poor and other target populations.

At the policy level, the NGOs Directorate and CBI are now engaging Iraqi MFIs and other stakeholders working in the sector. All 12 MFIs in Iraq are registered as NGOs and continue to expand their services to reach out to the poor and women as they work towards achieving financial inclusion for disadvantaged populations in the country.

FIGURE 10: NEW ERA OF SECTOR DEVELOPMENT APPROACH IN IRAQI MICROFINANCE SECTOR



3.3 MACRO: BUILDING AN ENABLING REGULATORY ENVIRONMENT

The legal and regulatory policy environment for microfinance is improving. The CBI and the NGOs Directorate have accepted and given recognition of microfinance as an effective source of credit for micro, small and medium-scale enterprises (MSMEs). This is an important step and USAID continues to lead the effort for their support in the sector through greater understanding of the need for an enabling regulatory environment that facilitates growth of the microfinance industry. USAID has served as the coordinating agency for organizing stakeholder discussions with regulators. Various consultations have taken place with the CBI, led by USAID, regarding the need to adopt guidelines for the microfinance sector in Iraq. OPIC and CGAP have contributed to such discussions and CBI has already issued the MSME Finance Companies ordinance on NBFIs based on its overall objective of promoting sustainable growth, employment and prosperity in Iraq. USAID-Tijara will continue to take relevant necessary action for further progress to be made towards an inclusive financial sector. The details of the two government authorities involved in supervision and monitoring of the finance sector are given as follows:

- i) The NGOs Directorate
- ii) The Central Bank of Iraq

3.3.1 Iraqi Government NGOs Directorate

The NGOs Directorate understands the types of microfinance activities in which NGO-MFIs should engage as a result of continuous interaction and regular communication. USAID and USAID-Tijara have hosted stakeholder meetings with the NGOs Directorate, together with MFIs. The purpose of the meetings was to open lines of communication with the NGOs Directorate, and to introduce it to basic principles of microfinance, and the unique characteristics and challenges of the Iraqi microfinance industry and to seek its understanding and support.

Concern remains about the interest rates MFIs charge clients although the prevailing rates are considerably lower compared to globally acceptable microfinance interest rates in the region and beyond. Other issues that have been reviewed include client poverty levels, grant use and application to MFIs, geographical areas of coverage, and future meetings and dialogue. The stakeholder meetings helped establish more strategic relationship among NGOs Directorate and MFIs paving the way to create a more inclusive sustainable financial sector in Iraq.

The new NGO law allows for a variety of microfinance related activities, such as creating a microfinance industry network and opening multiple branches across the country. There are, however, several ambiguities that could continue to constrain MFIs including:

i) Taxation of revenue generating NGOs

According to the new law, an NGO can be exempted from paying taxes after receiving status as a “public utility” NGO, which is approved by a Council of Ministers, however, MFIs as revenue generating NGOs cannot apply for such a status. A high tax burden reduces incentives for MFIs to continue operating as NGOs. Additionally, newer MFIs will face reduced surplus margins because of added start-up costs. This could reduce future profitability and sustainability of new institutions and thereby discourage further entry.

ii) Dissolving the NGO and transferring assets to a successor organization of similar legal status

According to the new law, in case of dissolution of any NGO the assets shall be transferred to an organization with similar mandate and activities.

3.3.2 Central Bank of Iraq

The Central Bank of Iraq (CBI) recognizes the lack of depth in outreach for achieving the goal of financial inclusion given the largely underdeveloped banking sector in the country. In late 2010, the CBI issued the MSME Finance Companies ordinance to enable such companies to set up and provide needed financial services for MSMEs. However, the law does not allow NGO-MFIs to transform into NBFIs. The ability of NGO-MFIs to transform into NBFIs would allow sustainable MFIs to become more accountable as regulated entities and access a broader spectrum of capital which would enable them to increase their outreach. While the CBI does not endorse interference in interest rates charged by MFIs, the regulations make reference to “concessionary” rates. This is not clear and thus far the MFIs have been able to charge reasonable rates although these are lower than usual microfinance rates charged in MENA and other regions.

The capitalization requirements under the MSME Finance Companies law for creating an SME financing company are IQD two billion (\$1.7 million) as a joint stock company (JSC) and IQD one billion (\$850,000) as an LLC. In addition, the ordinance permits SME financing companies to provide only loans to MSMEs as other financial services such as savings are not permitted.

TABLE 8: MICROFINANCE SECTOR IN IRAQ: COMPARATIVE LEGAL AND REGULATORY FRAMEWORK

Institutional features	NGO – MFIs	MSME Finance Companies
Regulatory Status	<ul style="list-style-type: none"> Registered by Iraqi NGOs Directorate Not supervised or regulated by Central Bank of Iraq (CBI) 	<ul style="list-style-type: none"> Incorporated by Registrar of Companies Licensed and supervised by CBI as MSME – Finance Company
Legal Form	<ul style="list-style-type: none"> Non- Governmental Organization (NGO) 	<ul style="list-style-type: none"> Limited Liability Company (LLC) or Joint Stock Company (JSC)
Ownership Structure	<ul style="list-style-type: none"> No owners or shareholders At least three founding members Maximum 25% foreigners, resident in Iraq, may become members 	<ul style="list-style-type: none"> LLC: Minimum 1 shareholder and maximum of 25 shareholders JSC: Minimum 5 shareholders Foreign shareholders allowed
Capital Structure	<ul style="list-style-type: none"> No capital requirements 	<ul style="list-style-type: none"> LLCs: One billion IQD JSCs: Two billion IQD
Profit Status	<ul style="list-style-type: none"> Non-profit organizations; Profit from operations cannot be distributed to employees, directors or managers 	<ul style="list-style-type: none"> Commercial, for profit organizations; dividend can be paid to shareholders
Financing from commercial banks: local and foreign	<ul style="list-style-type: none"> Not allowed for on-lending purposes 	<ul style="list-style-type: none"> Bank borrowing up to 300% of paid-up capital (for LLCs and JSCs) Credit bonds up to 50% of the paid up capital may be issued (for JSCs only)

Institutional features	NGO – MFIs	MSME Finance Companies
Grants from donors	<ul style="list-style-type: none"> • Yes, grants are treated as revenue for the NGOs 	<ul style="list-style-type: none"> • Yes, subject to prior approval from Ministry of Planning and Development Cooperation. • All grants must be converted as shareholder capital
Provision of loans to target clients: the poor	<ul style="list-style-type: none"> • Not prohibited in the law 	<ul style="list-style-type: none"> • Allowed
Prudential Supervision	<ul style="list-style-type: none"> • No 	<ul style="list-style-type: none"> • Yes, by Central Bank of Iraq
Corporate Governance	<ul style="list-style-type: none"> • General Assembly • Board of Directors • Board sub-committees may be formed under the by-laws • Board members should meet basic criteria defined in NGO law and NGO's bylaws 	<ul style="list-style-type: none"> • General Assembly • JSCs: Board of Directors • LLCs: Advisory Board • Board sub-committees on risk management, audit and compliance • Board members should meet professional criteria set by CBI
Audit	<ul style="list-style-type: none"> • Only for NGOs with annual budget exceeding 75 million dollars by a public accountant. • By Board of Supreme Audit if NGO Office believes that NGO's accounts are manipulated or inaccurate. 	<ul style="list-style-type: none"> • By a CBI approved auditor • Inspection of records by CBI
Reporting to Regulator	<ul style="list-style-type: none"> • A financial report including a detailed description of the source of the NGO's funds and financial transactions. • A report of the NGO's activities including a briefing on the projects implemented by NGO during the year 	<ul style="list-style-type: none"> • Annual report containing: • Sources of finance. • Statement of outstanding loans and statement of pledged loans. • Prevailing interest rate(s) charged on credit products. • Purpose of loans and strategic alignment of loan purpose to the Company's missions. • Lending and collateral policies and procedures. • A statement of loan-loss provisions.
Taxation	<ul style="list-style-type: none"> • Yes ,except public utility NGOs 	<ul style="list-style-type: none"> • Yes
Dissolution	<ul style="list-style-type: none"> • Net assets transferred to successor organization with similar objectives 	<ul style="list-style-type: none"> • As per the Companies Law
Loan Loss Reserve	<ul style="list-style-type: none"> • Although not required by law, NGO-MFIs set aside 2-5% of outstanding loans as loan loss reserves 	<ul style="list-style-type: none"> • The Company will set aside financial allocations to overcome risks facing the Company, determined by the CBI
Consumer Protection	<ul style="list-style-type: none"> • Not required by the law. However, NGO-MFIs adhere to a Code of Conduct and Ethics adopted by the microfinance industry promoting transparent pricing and consumer protection principles 	<ul style="list-style-type: none"> • The CBI requires that the loans to target clients are used for purposes stated in the loan contract

3.4 MESO: BUILDING THE MICROFINANCE INDUSTRY INFRASTRUCTURE

The Iraqi microfinance industry infrastructure has evolved in the recent past and a variety of important initiatives at the meso level have strengthened technical and institutional infrastructure for an inclusive financial sector. USAID-*Tijara* has led some of the initiatives as follows:

- i) Transparent reporting systems,
- ii) Human resources training for the microfinance sector,
- iii) Establishment of the Iraq Microfinance Network (IMFN),
- iv) Development of a broader microfinance platform for coordinating with donors and global microfinance industry and for increased knowledge sharing that enhances knowhow and skills that facilitate progress towards achieving the goal of financial inclusion within Iraq.

3.4.1 Transparency and Accountability

MFIs have come a long way in accurately tracking, recording and reporting the performance data necessary to monitor and manage progress. Donor agencies require credible information on the results and impact of microfinance activities in which they are investing. The accurate and consistent reporting of performance is crucial in providing the data necessary for effective management decisions that take the MFIs to sustainability, which is increasingly important as a means to diversify funding sources.

Since 2010, all Iraqi MFIs have been consolidating data across branches and reporting using the automated MIS, which is comprised of their own loan tracking system and the Performance Monitoring Tool (PMT). The PMT compiles performance results across each MFI's branches based on internationally acknowledged disclosure and reporting standards. All respective PMT databases of the MFI partners are exported to a centralized database, the Performance Monitoring System (PMS), which is managed by USAID-*Tijara*. They are then consolidated to generate overall industry performance ratios and indicators. The PMS also informs the Performance Classification Monitoring System (PCMS).

Iraqi MFIs are increasingly interested in learning how they are performing in comparison to their peers at similar maturity levels across the MENA region. There is also a need to begin asserting a place for the industry as an integral part of the overall financial system in Iraq. To assist the industry in tracking its own progress and to report to funders and stakeholders more broadly, the PCMS was designed and tested by USAID-*Tijara*. The PCMS shows the evolution of MFIs and how they compare with their peers in the MENA region based on type of institution (indigenous or international), number of borrowers, loan amounts outstanding, average loan size, portfolio-at-risk (PAR) for loans past due for more than 30 days, operating expense ratio (OER), case load, operational self-sufficiency (OSS), and financial self-sufficiency (FSS). Each of these indicators is assigned a score in order of importance to determine the overall classification category of the MFI and eventually the class into which it is categorized vis-à-vis its peer MFIs in the MENA region.

The goal of the PCMS at the industry level is for the industry to be able to self-regulate by:

- Producing and presenting accurate and regular information on industry performance to stakeholders (clients, donors and potential commercial funders and investors)
- Setting accurate benchmarks (actual performance averages)
- Monitoring and documenting progress against benchmarks over time
- Providing feedback to individual MFIs on their performance against peer group averages
- Setting minimum standards for future performance as a means of accreditation

TABLE 9: CLASSIFICATION GRADE OF IRAQI MFIs**D: Start-up stage**

Up to 500 borrowers having outstanding loans of up to \$1 million. Portfolio at risk (PAR) and operational expense ratios (OER) tend to be high, while loan officer productivity and operational and financial self-sufficiency ratios are low.

C: Consolidation stage

MFIs consolidate and solidify performance by growing their portfolio up to 1,500 clients with loans of up to \$5 million outstanding. PAR and OER reduce while loan officer productivity and viability indicators increase.

B: Expansion stage

In the expansion phase, MFIs grow to reach up to 5,000 clients with an outstanding portfolio of up to \$15 million. PAR, OER and loan officer productivity ratios will reach industry standard levels, while viability indicators will be just below break-even point (85% – 99%)

A: Commercial viability stage

For commercial viability, MFIs will realize a surplus and generally perform and achieve international microfinance performance benchmarks. There is a portfolio of over 5,000 clients with more than \$15 million outstanding. PAR will be below two percent. OER will decrease to below 12% and loan officer caseload will generally be above 200. Viability ratios (OSS and FSS) will both exceed 100%.

Source: http://www.imfi.org/files/PCMS_ReportDec09.pdf

Tracking performance data has enabled the industry to document growth and development and also facilitate comparison of national performance benchmarks to international performance averages, for example by linking them to the global Microfinance Information Exchange (MIX) Market database¹⁹.

3.4.2 Building the Human Resource Capacity

USAID-*Tijara* has continued to play a critical role in building the institutional as well as the human resource capacity of the maturing Iraqi microfinance industry. A major part of this infrastructure development is the training of qualified Iraqis to become microfinance trainers so they can transfer skills to other Iraqi MFIs.

In 2006, USAID-Izdihar began developing 11 Iraqi microfinance trainers chosen from over 100 applicants to become CGAP-certified Iraqi microfinance trainers. As of 2011, eight First Generation MF Trainers remain serving the Iraqi microfinance industry as leaders, including several who are MFI chief executives.

Since 2009, over 784 Iraqis employed by or associated with Iraqi MFIs, USAID-*Tijara*-supported SBDCs, and other key stakeholders such as government departments have been trained through 66 events up to June 30, 2012. These events have included workshops and conferences in topics essential to institutional growth and financial sector mainstreaming. Trainers were also trained as Master Trainers of Trainers (MTOTs) in early 2010 by an International Training firm and they are currently available to support the industry as needed.

3.4.3 Iraq Microfinance Network (IMFN)

USAID-*Tijara* has supported the development of a sustainable microfinance industry in Iraq. It advocated reform and development of the microfinance industry by promoting training and standardized MFI reporting to enable performance monitoring.

Based on the NGO Law which allows for the creation of a national microfinance network, USAID-*Tijara* supported the institutionalization of the Iraq Microfinance Network and an initial step was taken whereby all the Iraqi MFIs agreed to a Code of Conduct and Ethics for the sector. The Code focuses on such areas as transparency, client protection, and respect for religion, among others.

The IMFN was officially registered in April this year and it held its first General Assembly and Board meeting soon thereafter on May 8, 2012. The network will support a number of programs and initiatives for the industry and for its constituent members, the Iraqi MFIs. Additionally, it will monitor and advise on policy, coordinate donors and direct the sector towards best practices and sustainability. Most importantly, the network will serve as a unified voice for the Iraqi microfinance sector to lobby government for a more favorable legal and regulatory environment. The Iraqi microfinance knowledge portal (www.imfi.org) will be transferred from USAID-*Tijara* to the network as IMFN becomes institutionalized and takes responsibility for the microfinance industry upon conclusion of USAID-*Tijara*'s term.

¹⁹ <http://www.themix.org>

3.4.4 Knowledge Sharing

USAID continues to provide platforms for building cooperation among Iraqi MFIs, and also promote collaboration, partnership and healthy competition on interest rates and client services. In all 18 provinces, the MFIs have developed expertise keeping in view market characteristics, clients’ needs, services delivery mechanisms, and loan products leading to demand driven quality products and services. Al-Takadum in Anbar, which has demonstrated competency in Islamic finance (Al-Murabaha), often hosts site visits for other MFIs that are facing increased resistance to conventional microfinance loan products from religious leaders in their areas of operations. MFIs also extend full cooperation for any USAID-Tijara technical assistance experts’ inquiries in areas that would lead to improved impact for the broader microfinance sector.

3.5 MICRO: BUILDING THE ROADMAP TOWARDS INSTITUTIONAL SUSTAINABILITY

Rapid client and portfolio growth changed the dynamics of the microfinance industry. MFIs gained increasing independence as demand-driven institutions and they are becoming more recognized as effective development institutions reaching out to the poor and to those excluded from the mainstream financial sector.

Based on the classification system mentioned under table 9 above, 10 MFIs are under Category A, the Commercial Viability Stage, while two MFIs are under Category B, the Expansion Stage. This is a significant increase from 2009 when eight of the MFIs were in Category A while the rest were under Category B. The improvement reflects the MF sector’s merit to be included in the mainstream financial sector.

Category A-Commercial Viability Stage		Category B-Expansion Stage
Al Aman	Bright Future Foundation	Al Tadamun
Al Bashaer	CHF International	Al Takadum
Al Mosaned	Relief International	
Al Thiqa	Izdiharona	
Amalkom	Tallafar Economic Development Center	

Compared to globally used standards of Tier I, II and III MFIs, ten MFIs fall under the category of Tier II while the remaining two fall under Tier III. MFI tiers are defined using the CGAP endorsed portfolio size parameters:

- Tier I: GLP > \$50 Million
- Tier II: GLP > \$3 Million and < \$50 Million
- Tier III: GLP < \$3 Million

Tier I: GLP>\$50 million	Tier II: GLP > \$ 3 million and < \$ 50 million		Tier III: GLP< \$ 3 million
None	Al Aman	Bright Future Foundation	Al Mosaned
	Al Bashaer	CHF International	Al Tadamun
	Al Takadum	Relief International	
	Al Thiqa	Izdiharona	
	Amalkom	Tallafar Economic Development Center	

At the micro level of sector development in Iraq, the progress already made thus far is reviewed below. This and also the other key areas requiring attention as the microfinance industry grows towards long term sustainability are reviewed as follows:

- Growth of the Microfinance Industry
- Women Clientele
- Portfolio Quality and Financial Performance
- Growing Efficiency in Loan Operations

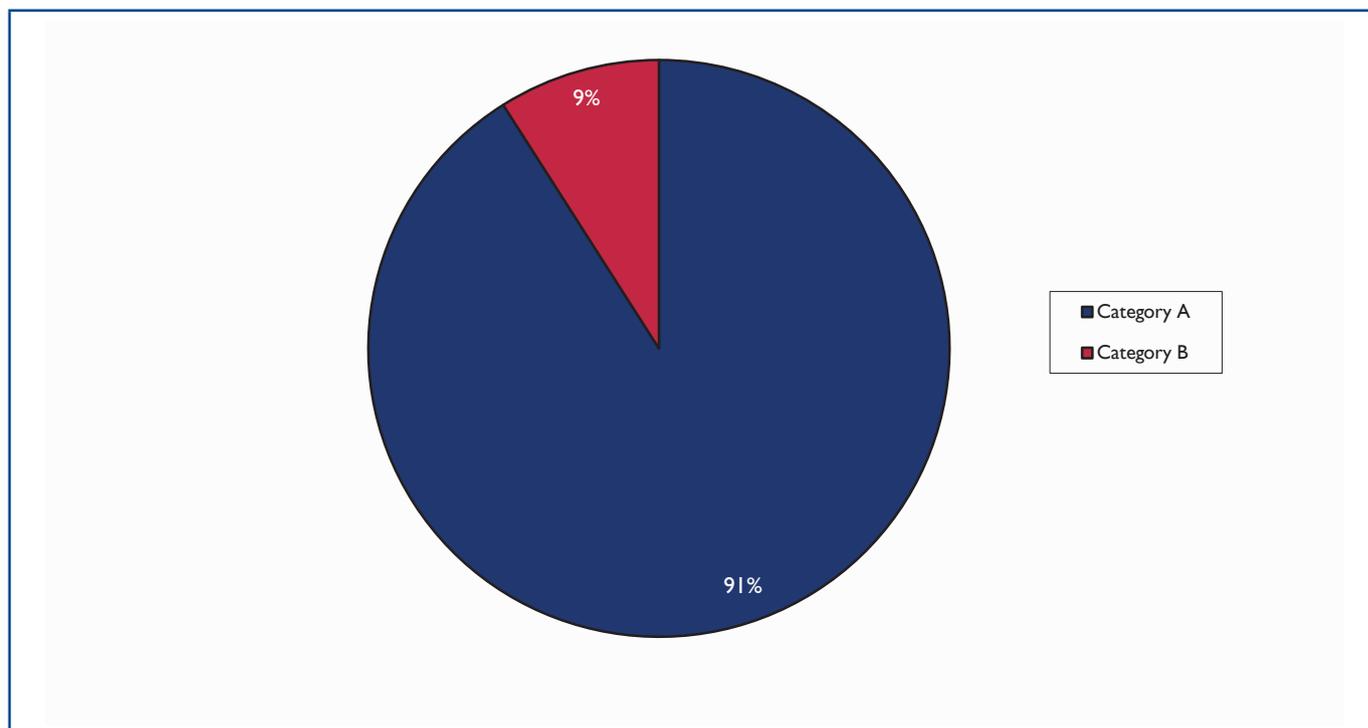
3.5.1 Growth of Microfinance Industry

The Iraqi microfinance industry experienced high Compound Annual Growth Rates (CAGR) in outstanding loan portfolio over the years. Setting the base at December 2006, the rate was 63.9% through 2009, but this decreased to 54.2% in 2010 and then to 46.7% in 2011. Even with the rate decreasing due to growth of portfolio base, this is impressive growth and indicates the large market demand. Meeting market demand however is constrained by the low availability of capital resources. It will therefore be critical for the microfinance industry to access the required resources in order to maintain the good growth already achieved. This will require concerted efforts by the authorities, mainly the CBI and the NGOs Directorate, to create a legal and regulatory environment conducive to giving donors and investors the incentive to channel funds into the industry. The year-on-year growth rates for both outstanding loan portfolio and number of active clients are shown in the following table:

	December 2009	December 2010	December 2011	June 2012 ²⁰
Active Clients	58,852	75,182	86,554	93,627
Year-on-Year Client Growth	52%	27.7%	15%	16.4%
Outstanding Loan Portfolio (\$)	\$82,855,717	\$106,406,242	\$127,733,002	\$143,932,639
Year-on-Year Portfolio Growth	48.2%	28.4%	20%	25.4%

The decline reflected over the years is partially due to the introduction of the solidarity group lending (SGL) methodology to Iraq in 2009. This methodology facilitates loans to the poor and women without the requirement of physical collateral. In order to attract low-income clients, SGL introduced a reduced minimum loan size of \$500. This meant that MFIs would need to disburse about three to four loans under SGL to match the one loan done under the individual loans. As a result, the outstanding loan portfolio has leveled off as the average loan size has declined. Simultaneously, the continuing unstable security situation and limited number of new investors constrain the MFIs' ability to grow at a faster pace. Iraqi MFIs also face challenges in accessing qualified human resources. They have high attrition rates as MFIs continue to lose trained staff members to more secure, stable and higher paid opportunities with government, international development contractors, private business firms and even institutions outside Iraq.

FIGURE 11: SHARE OF OUTSTANDING LOAN PORTFOLIO BY MFI CLASSIFICATION



²⁰ The growth to June 2012 is annualized to reflect the true comparison

FIGURE 12: SHARE OF ACTIVE CLIENTS BY MFI CLASSIFICATION

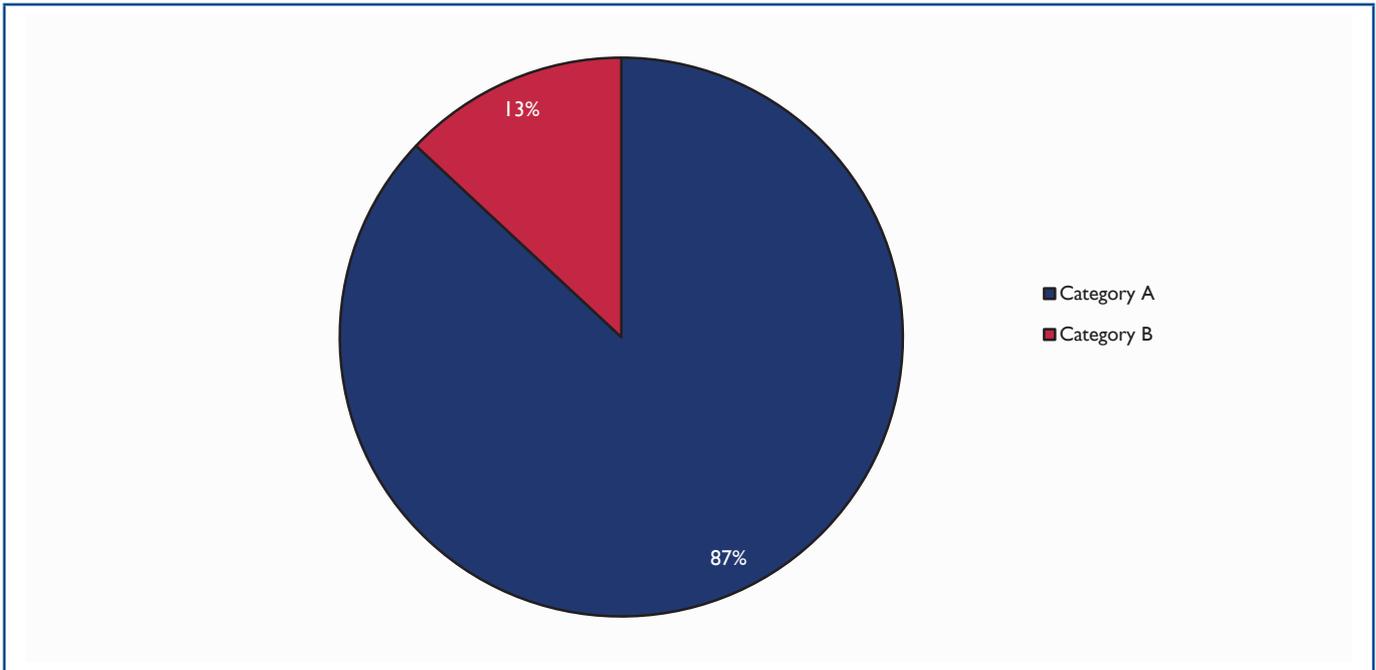


FIGURE 13: GROWTH IN LOAN PORTFOLIO (USD), CUMULATIVE AND OUTSTANDING

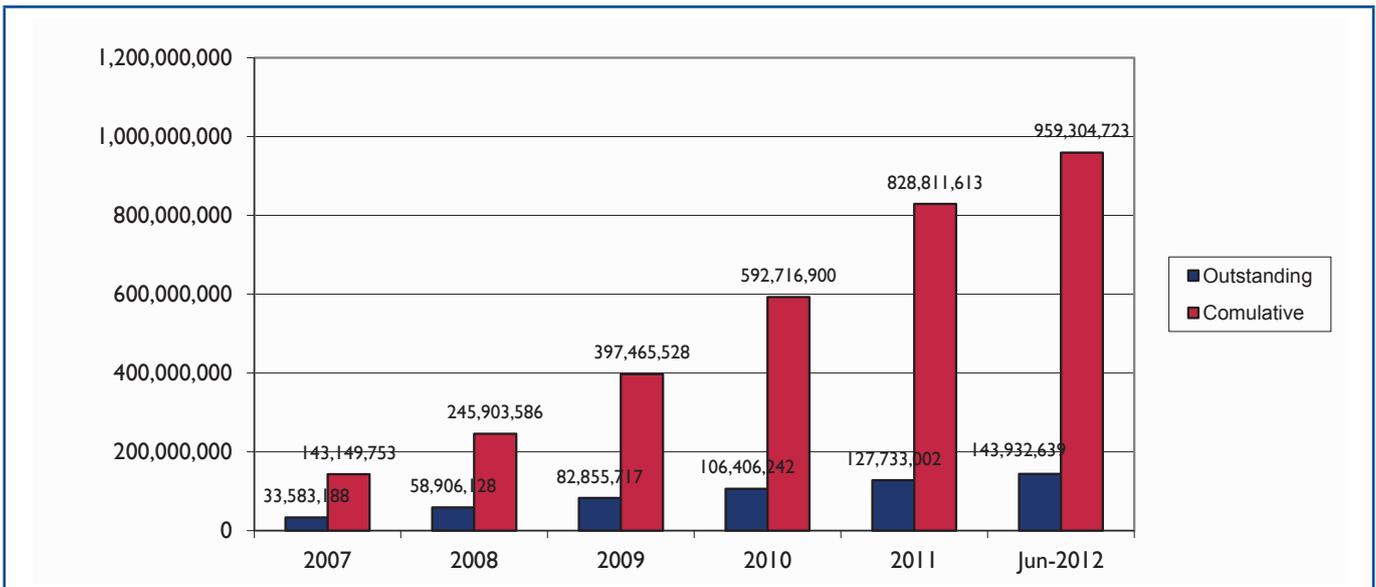


FIGURE 14: GROWTH IN CLIENT OUTREACH (NUMBERS), CUMULATIVE AND OUTSTANDING

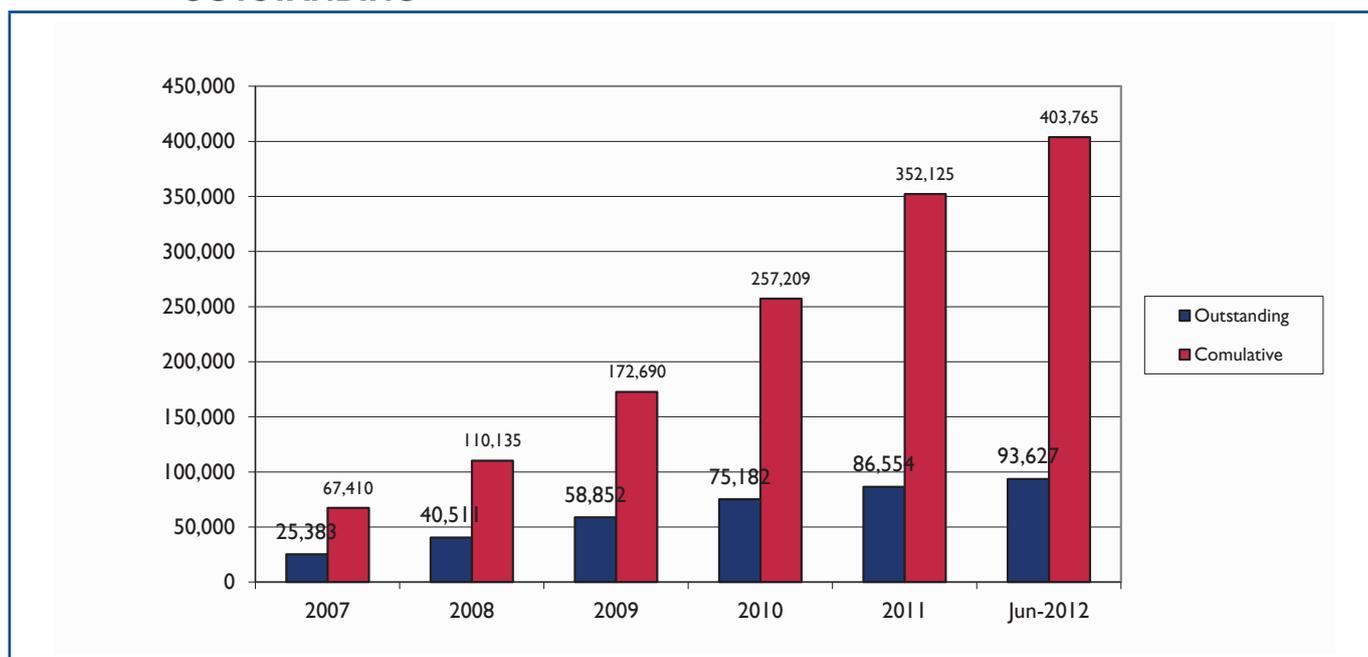


TABLE 10: IRAQI MFIs AVERAGE GROWTH COMPARED TO MENA AVERAGES

Indicators	MENA Averages (MBB)	Iraqi MFIs Averages
Number of Active Borrowers	13,161	7,802
% of Women Borrowers	67.6%	21%
Gross Loan Portfolio per MFI (\$)	\$6,229,943	\$11,994,387
Average Loan Balance per MFI (\$)	\$363.83	\$1,537

3.5.2 Women Clientele

Across the world, women entrepreneurs contribute significantly to the economic growth and sustainable livelihoods of their families and communities. Inclusive financial services, including microfinance, help empower women from poor households by giving them access to critical economic resources. As a result, this positively influences female clients’ decision-making power and thereby enhances their families’ and their own socio-economic status. Currently, 70% of the world’s women are poor. They have been disadvantaged in access to credit and other financial services and this limits their ability to effectively contribute to the informal economy and local economic development.

Commercial banks and formal financial institutions often focus on men and formal businesses, often male-owned, neglecting women who make up a large and growing segment of the informal economy. The collateral requirements often are so stringent that women fail to get loans and other financial services due to lack of the required collaterals. Microfinance however, often targets women and in some cases, elsewhere in the world, women are exclusively targeted. The ripple of women’s microfinance can turn into a wave that leads not only to enhanced empowerment and decision-making, but also to powerful institutions able to take on complex new tasks serving the whole of society.

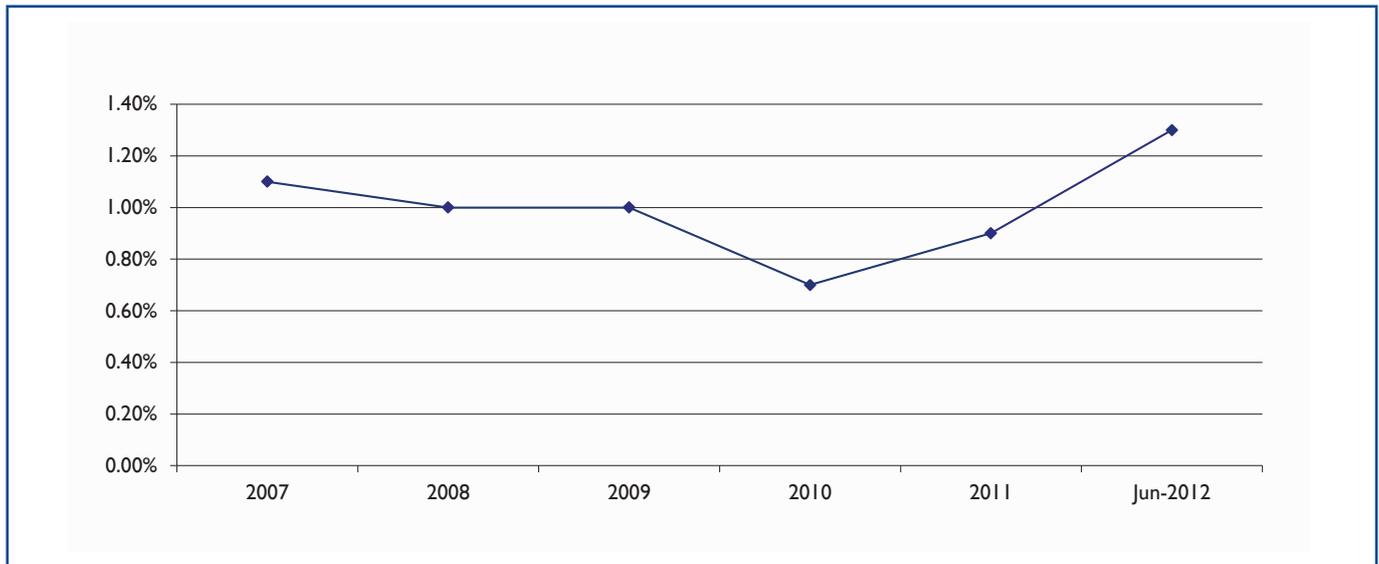
One in ten Iraqi households is headed by a woman. More than 80% of these women are widows. Women make up 17% of the country’s labor force, compared to 81% of men. The low participation rate of women is partially attributed to illiteracy, lack of access to capital, and conservative social and cultural traditions. Since 2003, women have been proving their entrepreneurial skills by successfully running their MSMEs. Women who access quality financial services demonstrate higher success rates compared to men both in terms of repayment and positive socio-economic impact on their families. Thus, outreach to women has been a priority of the microfinance industry. As a proportion of total active clients, the percentage of women has increased from 13% in March 2007 to 16% in December 2010 and to 21% in June 2012. It is expected that the percentage of female clients will continue to grow as MFIs have demonstrated a commitment to increasing these clients by hiring female loan officers and targeting women groups using the SGL methodology. Female loan officers represent 19% of all loan

officers among Iraqi MFIs, a proportion that continues to grow each year as MFIs attempt to extend their outreach to women, however, based on the limited economic and social mobility of women in Iraq, the microfinance sector has yet to unleash the entrepreneurial potential of Iraqi women.

3.5.3 Portfolio Quality and Financial Performance

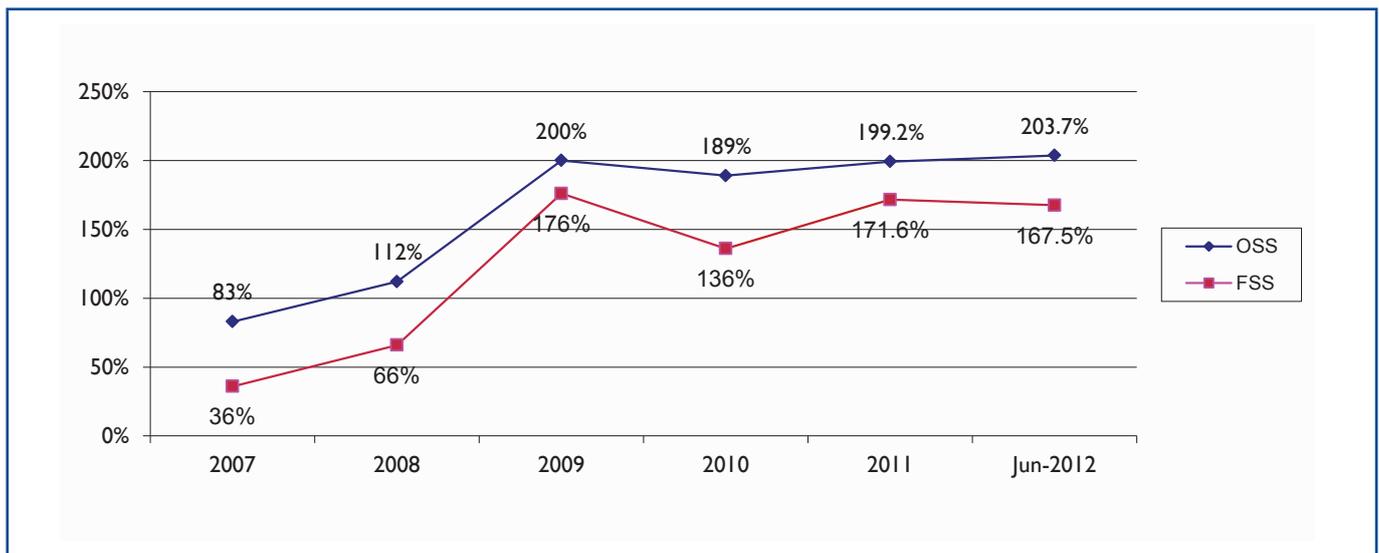
All of the Iraqi MFIs currently have a healthy loan portfolio with PAR > 30 days at just 1.3%. This performance is better than the MENA average of 2.8% and illustrates the better quality maintained by the Iraqi MFIs in spite of the security challenges in the country. The Grade A MFIs (listed in Table under paragraph 3.5 above) also have better credit/risk analysis systems as well as better collection methods. As a result, they have been able to maintain good portfolio quality.

FIGURE 15: PORTFOLIO AT RISK > 30 DAYS ACROSS THE YEARS



The operational and financial self-sufficiency for MENA was 123.5% and 121.3% respectively, according to 2010 Arab Microfinance Benchmarking Report, compared with OSS of 203.7% and FSS of 167.5% in Iraq. Rates of both indicators, operational and financial sustainability, have continued to increase as the Iraqi MFIs increase their outreach and efficiency. The higher returns in Iraq are mainly due to higher margins since Iraqi MFIs do not incur financial costs of borrowing incurred by other MENA countries. This subject of financial costs is discussed further in section 3.5.4 below.

FIGURE 16: OPERATIONAL AND FINANCIAL SELF SUFFICIENCY



3.5.4 Growing Efficiency in Loan Operations

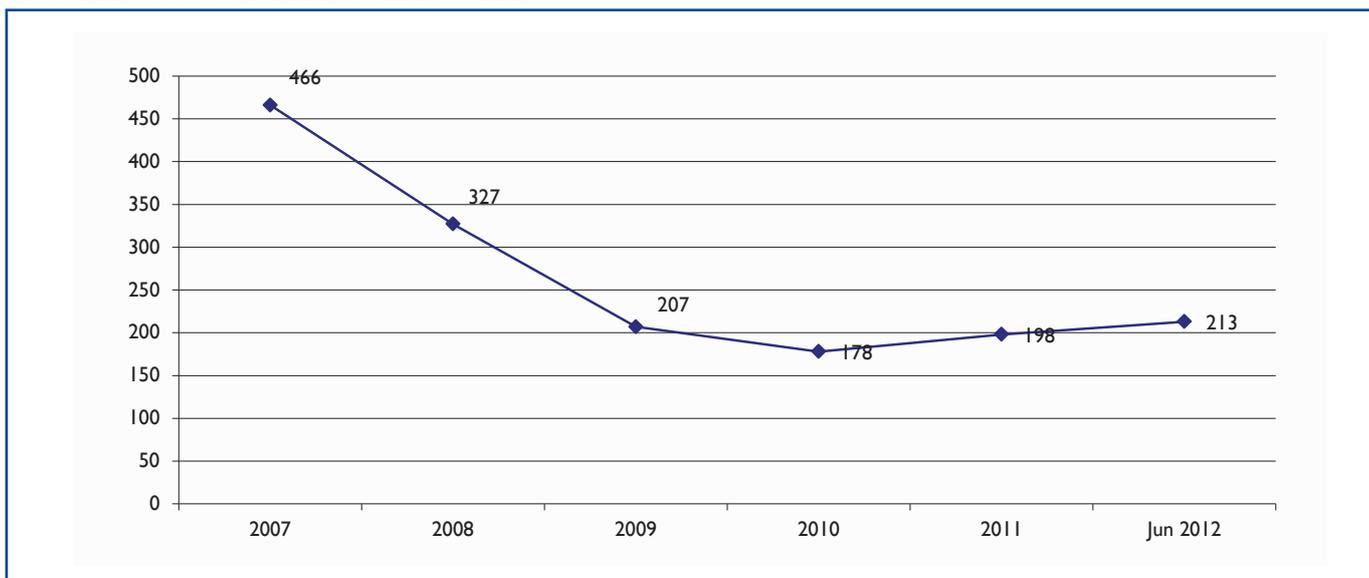
During 2009 and 2010, Iraqi MFIs continued to be highly efficient in their loan operations, a trend that corroborates their increasing scale of operations. The operating cost ratio at 12.7% has improved dramatically

from the ratio of 13% in 2009 and 28% in 2008. The cost per borrower improved from \$207 in 2009 to \$178 in 2010 but then increased to \$198 in 2011 as cost of inflation increased. The following sections and the related charts indicate the progress made in efficiency of the Iraqi MFIs.

In a country characterized by ongoing conflict and insecurity, operating costs are far higher in Iraq compared to other countries in the region. For example, the average monthly salary of a loan officer (including built-in incentive schemes) in Iraq is \$843. This is very high compared with India and Bangladesh where the average is about \$100.

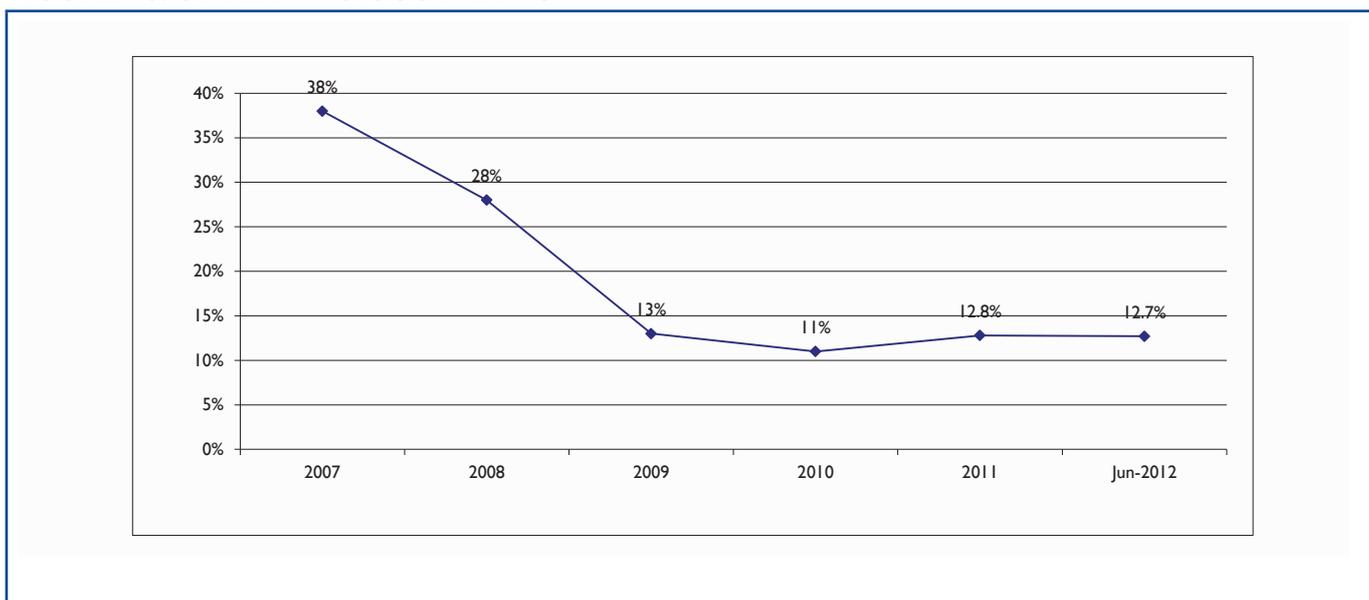
In addition, Iraq hires extra support staff, mainly for security, and that increases personnel costs to a much higher level than in other regional countries. While most loan officers typically use bicycles or motorcycles in other countries for field work, due to weather and security conditions, those in Iraq are forced to use cars, which are more costly. Despite such costs, Iraqi MFIs were showing a healthy reduction in cost per borrower over time as their experience and outreach grew but the situation stabilized and then the costs increased in 2011 as general costs and inflation increased.

FIGURE 17: COST PER BORROWER



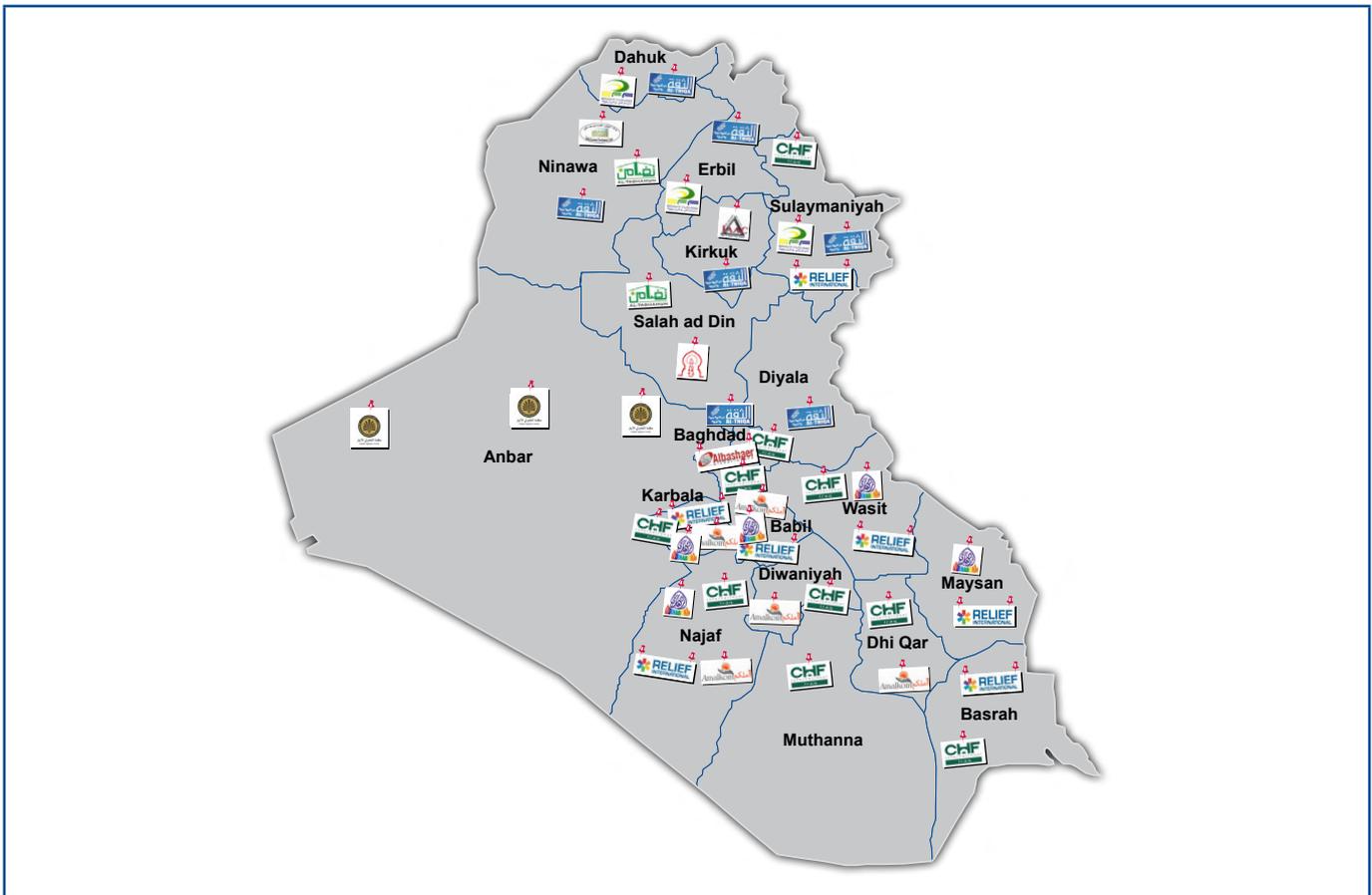
The reduction in the operating costs is due mainly to effects of scale as overhead costs are distributed over a larger portfolio base. Furthermore, improved standardization and increasing use of technology are also contributing to higher efficiency of Iraqi MFIs. Overall, this marks the progress due to merging of demand-driven, sustainable and competitive markets with quality financial services.

FIGURE 18: OPERATING COST RATIO



MFIs are moving from serving one province to now operating in multiple provinces, thereby increasing the competition in the sector, and consequently leading to improved services and lower borrowing costs for targeted clients.

FIGURE 19: GEOGRAPHICAL PRESENCE OF MFIs ACROSS 18 PROVINCES IN IRAQ



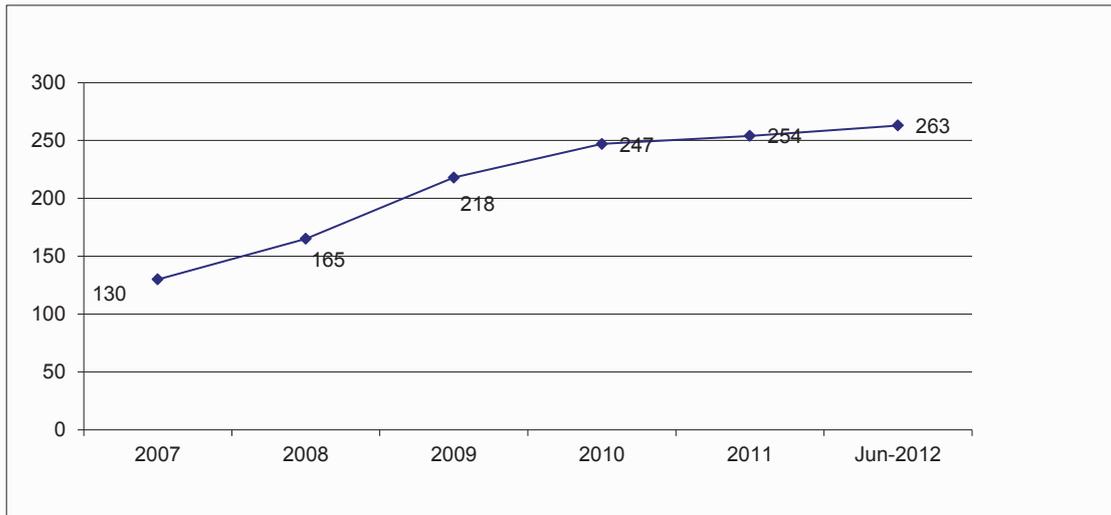
The financial cost ratio for Iraqi MFIs is negligible. Currently, there are no providers of debt capital in the Iraqi microfinance sector, domestic or international. Banks are unwilling to lend to MFIs. They themselves are receiving technical and financial support from international donors such as the IMF, USAID and the Iraqi Government to restructure the financial services infrastructure in the country. Grant capital for lending is provided predominantly by USAID, with 55% of total on-lending capital of \$99.5 million provided as loan capital. In 2009, 2010 and 2011, UNIDO, UNOPS, UNDP, Kiva and AusAID contributed combined approximately \$6.4 million for microfinance lending in Iraq. It is obvious that when donor funding is no longer available, Iraqi MFIs will have to source commercial funding for their continued expansion plans. This will lead to additional costs and they will need to adjust their lending rates in order to maintain their margins to ensure long term sustainability.

Interest charged on loans is the main source of internally generated income for Iraqi MFIs. Since MFIs do not bear financial costs, annual interest rates charged range from 10%-18% and are high enough to cover operational costs. Comparatively, the MENA average interest rate is 24%.

Iraqi MFIs continue to demonstrate higher cost efficiencies than their MENA peers, particularly analyzed on the basis of average number of clients per loan officer. The MFI Al-Aman records 398 clients per loan officer, followed by Al-Thiqa at 371 clients per loan officer. On average Iraqi MFIs record 263 clients per loan officer compared to the MENA average of 202.

Loan officers are the major link between MFIs and their clients. They are central for service delivery and they mediate and process transactions between MFIs and clients and thus implement policies of MFIs in ways that demonstrate deep understanding and compassion for successful lending. Therefore, if the case load per loan officer is above what is appropriate considering the local market, lending methodology, and product type, then lower portfolio quality, higher delinquency, and less sustainable delivery of services would be the results, which are certainly not desirable, however, Iraqi MFIs have demonstrated the ability to balance quantity and quality and have thereby achieved desirable results.

FIGURE 20: CASE LOAD PER LOAN OFFICER IN IRAQI MICROFINANCE INDUSTRY



Al Takadum Microfinance Organization Supports Micro and Small scale Enterprises in Al Anbar Province with Murabaha Loans

Mahmood Shihab Ahmed is a 46 years old businessman who operates a nut packing and packaging enterprise in Fallujah City, Al Anbar Province. In May 2011, Mahmood heard about Al Takadum’s Murabaha loan program from a friend who is one of the MFI’s very satisfied and successful clients. Mahmood was keen to start his own business to earn a living to support his wife and five children. Therefore, he applied for a loan of \$6,000 and was able to buy nut packaging machines and stocks of nuts and set up a nut packing and packaging enterprise.



One year later, he is able to manage his improved living standards and he is very happy with the success of his business which is growing day by day.

Mahmood has been able to support his family in making progress to a better life by meeting all their needs and also paying other family monthly budget expenses. He is now economically self-sufficient and plans to expand his business with additional Murabaha loans from Al Takadum. Mahmood is grateful for Al Takadum’s help and expressed his appreciation by commenting: “It seemed very difficult for me to rebuild my life and own a nuts shop and Al Takadum organization gave me a golden opportunity that paved the road for my dreams to come true.”

Micro Loans Energize Diwaniyah



by Saeed Lateef

Five micro loans totaling \$38,000 helped Saad Abdul Ridah Hassan build four retail shops, a wholesale warehouse and a city-wide distribution network in Diwaniyah

Saad Abdul Ridah Hassan grew up poor in Diwaniyah, an impoverished town of 450,000 about 100 miles south of Baghdad. At age seven he began selling newspapers to motorists stopped at traffic lights. It took 17 years for him to scrape together enough money to rent a tiny space for a stationery shop at the city's Al-Tujar Market.

Saad's life took a remarkable turn when the Amalkom MFI, funded by USAID-Tijara, opened an office in town. The MFI in Diwaniyah loaned the ambitious entrepreneur \$3,000 to expand his shop. Saad paid the money back and received a second micro loan for \$4,500 that allowed him to open a store selling decorative house wares and Arabic-themed gifts.

Retail diversity resulted in increased revenues. Saad petitioned for a third loan which he used to start a men's clothing store.

A subsequent loan of \$10,000 went to enlarge his three shops and lease a fourth retail space that he stocked with costume jewelry.

As a general rule, Iraqi retailers mark up the wholesale price of the goods they sell by 100%. After deducting rent, salaries and miscellaneous expenses, they normally take home a 25% profit.

Experience told Saad that some Asian imports, notably clothes and jewelry, could be sold at even higher margins. But would opening a second clothing store offer the maximum return on investment?

Saad consulted USAID-supported Amalkom and decided to borrow \$14,000 to stock a warehouse that would be the hub of a city-wide distribution network. Says Saad: "Asian imports bought in bulk would give me a second wholesale revenue stream and maximize my retail profit margins."

Saad, now 32, has used five microloans totaling \$38,000 wisely. Today, he nets \$15,000 a month on gross sales of \$30,000 and has hired five employees. It is a major accomplishment in a country that just eight years ago had a centralized state economy largely devoid of private sector entrepreneurs.

CHAPTER 4



MICROFINANCE PRODUCTS AND SERVICES

Alah Hassan Mohammed is a 46-year old Diwaniyah artist with a passion for calligraphy. Alah now operates a calligraphy shop in Diwaniyah's Al-Tujjar Market because of 11.5 million IQD equivalent to \$9,500 microfinance loan from CHF, one of 12 microfinance institutions working with USAID-Tijara.

4.0 DIVERSIFYING PRODUCTS FOR GROWTH

Iraqi MFIs are diversifying their products as they work to expand their outreach in order to achieve improved operational efficiencies that pave the way for higher margins that lead to higher surpluses. Product diversification is also important because it enables the poor, as well as women and others excluded from the formal financial sector, to have access to financial services. Through the diversification, MFIs can fill the gap of serving the more economically challenged and socially excluded clients.

There are three main lending methodologies in the Iraqi microfinance sector: individual, solidarity group and Islamic. In departure from much of the global microfinance practice, the Iraqi microfinance industry started lending through individual loans and Al-Murabaha Islamic finance. As security improved in 2009 and more accurate data on poverty rates became available, the solidarity group lending (SGL) methodology was introduced under the auspices of USAID-*Tijara*. The SGL methodology has enabled MFIs to reach out to the poor and women as it is structured to offer loans as low as \$500 as compared to an average of about \$1,500 and above for individual loans for which physical collateral is a requirement. Also, SGL does not require physical collateral as group members just need to cosign guarantees for each other and then they can access the loans. The SGL has facilitated outreach to previously excluded groups such as poor and women and other groups marginalized from the mainstream financial sector.

FIGURE 21: % SHARE OF ACTIVE CLIENTS BY LENDING METHODOLOGY

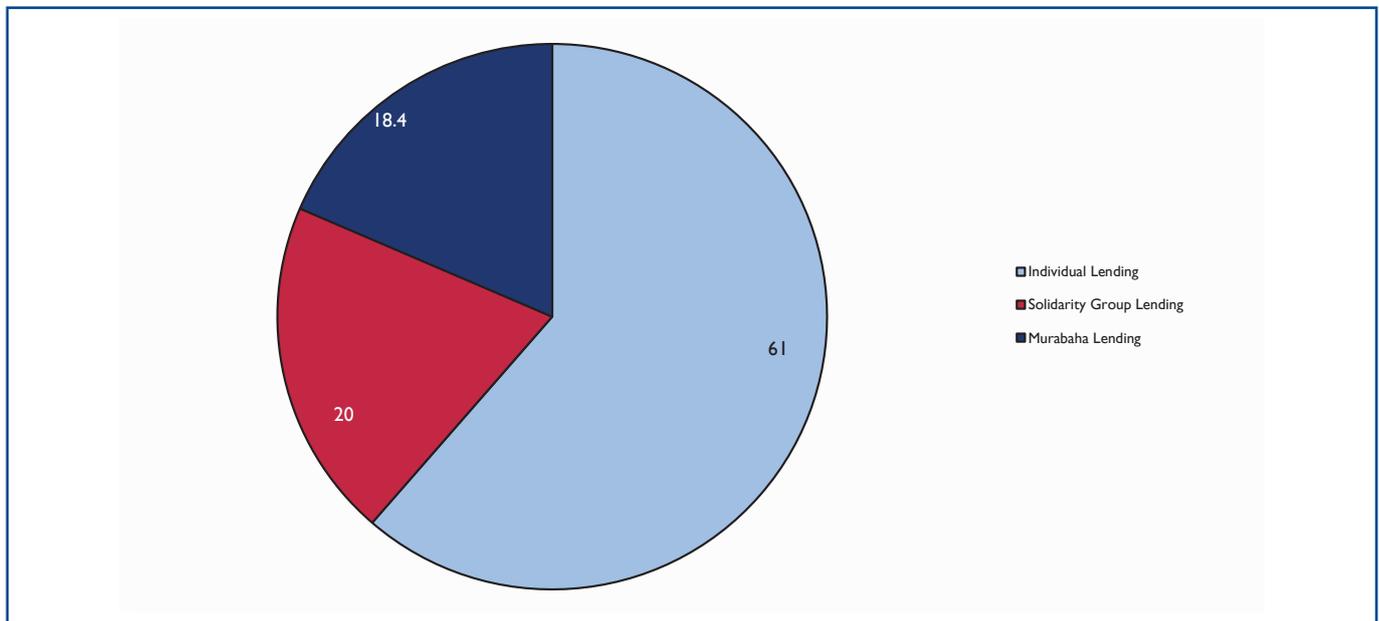
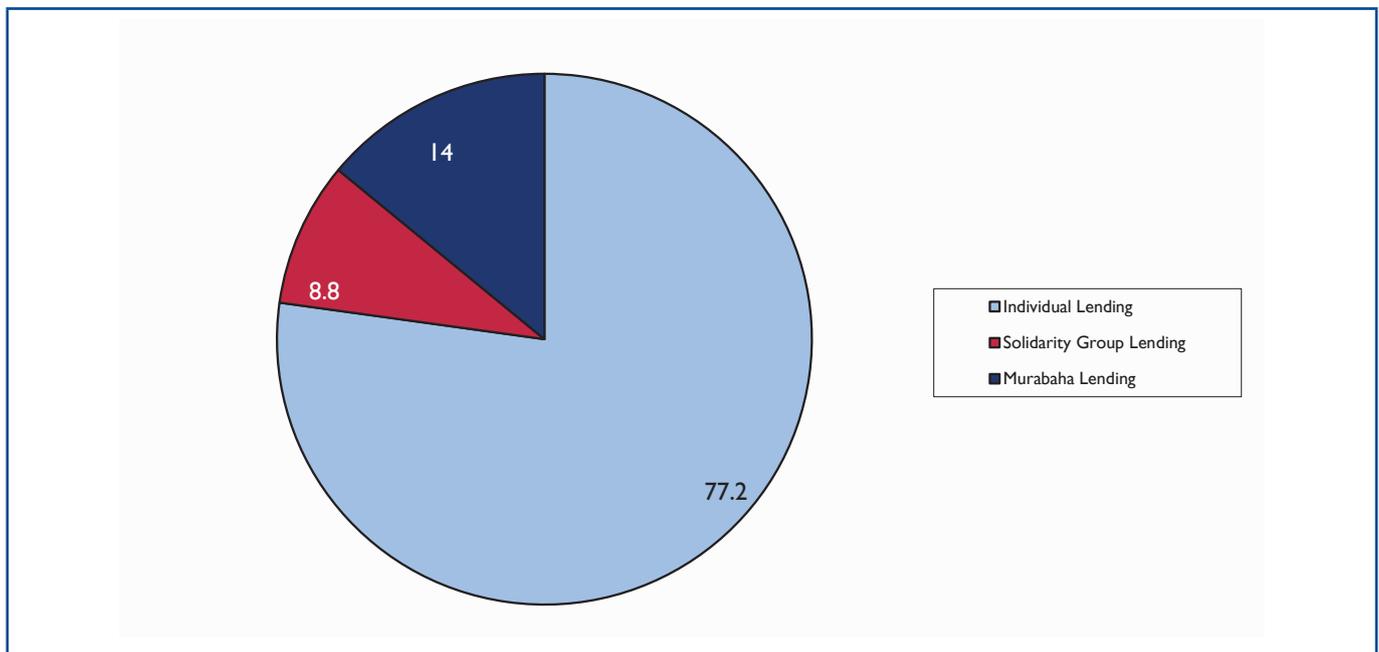


FIGURE 22: % SHARE OF LOAN PORTFOLIO BY LENDING METHODOLOGY



4.1 SOLIDARITY GROUP LENDING (SGL) METHODOLOGY

In SGL, group members (average of 3-5 per group) receive loans and then make regular monthly payments. Group members provide a mutual guarantee of loan repayment, which is adequate for MFIs that offer the product in order to reach the disadvantaged target groups, including the poor and women. SGL has three principal goals:

- Providing services to more of the poor and women who lack collateral or formal guarantees required by financial institutions;
- Attaining operational and financial self-sufficiency; and
- Reaching large numbers of vulnerable groups especially women and youth.

Successful SGL programs have a strong commitment to management efficiency and strive to be responsive to the market needs. Loans offered through the SGL methodology are usually targeted to very poor semi-urban and rural settlements and vulnerable clients segments such as women and youth. These loans are used for micro and small enterprises, agriculture inputs, and cottage industries. Iraqi MFIs are enhancing their outreach to the target groups through SGL.

Group lending is concentrated in southern and central provinces where poverty is more prevalent and group cohesion is high. Outreach to women using individual loans is 18% while that for group loans is 32%, demonstrating the growing success of SGL in reaching out to disadvantaged groups.

Poor people seldom have the collateral or connections necessary for bank financing. As a result, in 2009, Iraq's MFIs under the direction of USAID-*Tijara* began making solidarity group loans to market vendors, neighborhood retailers and beginning entrepreneurs in the food preparation and services sectors. Group loans provide for group members to vouch for one another instead of having to find a government employee to co-sign their note, a usual loan requirement. As of June 30, 2012, more than 64,664 Iraqis have taken the first step toward financial independence thanks to nearly \$64 million in group loans.

In Najaf, 11,347 borrowers, 31% of them women, have borrowed close to \$9,853,340 to start or expand their small businesses. The funds that have helped them become businessmen and businesswomen are supplied by local microfinance institutions Amalkom, Izdiharona and Relief International.

USAID-*Tijara* partner MFI Amalkom in Najaf Province reaches out to the poor through Solidarity Group Lending Methodology

Partner MFI Amalkom has implemented poverty lending through Solidarity Group Lending (SGL) methodology. The MFI has an interesting success story of a group comprising two women and one man that has been positively impacted in view of funding through SGL methodology. Sabeeha Nasser Mhanna Al Mayali (Group leader) is a 52 year old married woman who keeps farm animals in order to support her four dependents.



Sabeeha and her group members Shekreyye and Faeq in the background with her children

Shekreyye Ktouf Abbas is a 48 year old married woman who also keeps farm animals as a means to support her two dependents. Faeq Mahdi Mohaisin is a 40 year old married man working in delivery services. Sabeeha could not afford to purchase adequate feed for her cows and she also did not have proper tools needed for dairy production. Then she learnt about the group-lending product offered by Amalkom and she contacted her neighbors Shekreyye and Faeq who were also short of funding to develop their own income generating activities. Together they formed a working group as required under Amalkom's SGL methodology and applied for a loan for which they were financed.

They invested their respective loan amounts in improving their income generating activities and have reported improved income as a result of the funding from Amalkom. Sabeeha improved her income by 53% while Shekreyye increased hers by 81% and Faeq improved his by 38%. These are satisfied clients who have been positively impacted through SGL methodology.

4.1.1 Solidarity Group Lending in Iraq: Challenges and Recommendations

Challenges

- Five-members or more in groups are difficult to manage and may result in repayment problems.
- Small loan size reduces the motivation that attracts and facilitates easy group formation.
- Socio-cultural restrictions limit the freedom of women to run their own businesses and deal directly with institutions and banks.
- Demand for loans exceeds the reflows from repayments, negatively affecting new loan disbursement.
- Keeping up with demand and expansion is difficult since donors do not include reserve funds in the grants.

Recommendations

- Increase program exposure through the direct marketing and mass product introductions by staff in neglected areas especially in rural and minority communities.
- Teach youth and women on how to better manage their businesses.
- Expand efforts to reach vulnerable client segments such as women and youth by designing products that meet their needs.
- Convince donors to consider including reserve funds in grants to enable MFIs to keep up with demand and expansion.

4.2 SHARIA COMPLIANT LENDING

Sharia-compliant or Islamic-based lending refers to a system of credit provision that is consistent with Islamic law (Sharia) principles. This system reflects Islam’s teachings on wealth distribution, social and economic justice and especially prohibits interest charge on loans as it is considered “haram” or forbidden. Islamic finance researchers and practitioners agree that it is complementary to microfinance in terms of market innovation, asset orientation, core concerns, and equitable objectives. The table below compares factors under both Islamic and conventional microfinance.

	Islamic Finance	Microfinance
New-market Innovation	Reaches previously under-banked population	Focus on uplifting the poor
Asset orientation	Finance based on worthiness of ventures and assets, and not based on wealth	
Core concern	Routed in sharia-compliance	Fair access to capital
Equitable	Models advocate: <ul style="list-style-type: none"> - Financial inclusion - Entrepreneurship - Risk-sharing through partnership financing 	

Under Murabaha lending, the MFI literally buys goods and resells them to the microenterprises for the cost of the goods plus a markup to cover administrative costs. The MFI essentially becomes a facilitator/goods trader to enable a client to acquire assets/goods needed for his/her business. The borrower often pays for the goods in equal installments over an agreed repayment period. This model is easier for borrowers to understand and simplifies loan administration and monitoring. The MFI owns the assets/goods until the last installment is paid. Murabaha microfinance products and lending methodology has been widely adopted in Afghanistan, Pakistan, Yemen, Sudan, Iran, Indonesia, and Iraq. These countries have majority Muslim populations and according to their Islamic beliefs and teachings, interest (riba) is forbidden (haram). Therefore, clients in these countries prefer loans that are Sharia-compliant. Demand for Islamic financial products, including microfinance, is increasing in the MENA region. Iraqi MFIs have responded to the market demands in a professional and innovative manner and are likely to be future leaders in Islamic microfinance.

MFIs offering Islamic microfinance have prospered due to increased demand for Sharia-compliant products in Iraq. The demand for such products, however, exceeds the current ability to supply. Together, the five MFIs providing Al-Murabaha financing serve less than 1% of a total market potential of 820,000 households in the country.

The Islamic microfinance Al-Murabaha portfolio grew at a rate of 24% compared to the average industry growth rate for all lending of 20%. Despite this high growth rate, the amount of Islamic lending to total lending, now just 10%, needs to be proactively increased moving forward in order to drive down costs for Islamic MFIs.

Al-Murabaha lending presents an enormous, yet under-realized, opportunity for the microfinance sector in the country mainly because:

- Compliant with religious sentiments

As a Sharia-compliant product, Al-Murabaha lending is acceptable in all provinces and in many communities. It is praised as an important service by religious sheikhs and imams whose consent is important for continuing the offer and provision of quality financial services that facilitate greater MFI outreach to the poor and women.

- No limit on mark-ups charged for Al-Murabaha loans

There is increased attention on the issue of interest rates MFIs are charging. Al-Murabaha loans incorporate a mark-up on the procurement cost of assets/goods delivered to MFI clients. The methodology presents a unique opportunity for the Iraqi microfinance sector to become more profitable, taking advantage of this opportunity of no mark-up limits.

Murabaha is a popular and flexible Sharia-compliant financing structure introduced into Iraq by the USAID-*Tijara* and the Iraq Microfinance Network. It is recognized as a financing scheme for start-ups and small companies whose businesses involve the sale and purchase of commodities. Murabaha involves a financing party, usually a microfinance institution, which purchases tangible assets from a seller and then re-sells the items to the microfinance client at a predetermined profit margin or mark-up. In Iraq, Sharia-compliant financing requires the buyer to settle the marked-up purchase price by way of installments over an agreed period, which is typically one year.

Women employees energize super Nova

At 20¢ a piece, Hemmin Omar Ali's Super Nova chewing gum is not cheap. But Iraqi children buy it nonetheless since each foil packet also contains a biographical trading card bearing the likeness of celebrities like Johnny Depp, Rihanna and Brazilian soccer star Ronaldo. Kids who collect seven cards in the right numerical sequence can win a prize.



by David Devoss
Hemmin Omar Ali, 33, used a \$5,000 microfinance loan to create a company that sells \$200,000 worth of chewing gum a month. A second \$10,000 loan is allowing him to diversify into the potato chip business.

Hemmin's business took off in 2011 when he received a \$5,000 loan from Relief International, one of 12 microfinance institutions supported by the USAID-*Tijara* Provincial Economic Growth Program. He used the money on machinery that numbers each card and heat seals the foil packets. By the end of the year he had 32 female employees, four delivery trucks and monthly sales of \$180,000 in Iraqi Kurdistan region.

During the first quarter of 2012 he doubled the size of his factory, added 34 additional women and hired a Baghdad distributor. The move boosted monthly revenue to \$200,000 of which \$38,000 was pure profit.

He then spent 40% of his net on prizes that included Sony PlayStations, iPhones and Xboxes. What is the secret to Super Nova's success? "Hiring women," says Hemmin without hesitation. "Put 25 men in a small factory and half will start fighting while the rest go outside to smoke."

Recently, Hemmin received a second USAID-supported loan of \$10,000. He plans to use the money to produce Sharakam (My City) potato chips. "All the chips sold in Sulaymaniyah now come from Iran," he explains. "A bag with 50-gr of chips sells for IQD 311 or 36¢. "My chips will be made from Iraqi potatoes and come in 75-gr bags that sell for one dinar less. Iraqi people will buy them because they are locally produced. I'll also have the advantage of being able to produce a higher quality product," Hemmin smiles, referring to his previous success with gum. "Truthfully, my chewing gum doesn't taste as good as Wrigley's."

Murabaha Financing in Anbar Province: Lessons drawn from Al-Takadum Organization

The Anbar Province where USAID-*Tijara* MFI partner Al Takadum operates is one of the most security-challenged environments of MENA. Established in 2007, Al-Takadum faced considerable resistance from religious leaders who perceived microfinance as “haram” or forbidden. The MFI management team held 23 meetings with tribal and religious sheikhs to build consensus on the Al-Murabaha model of microfinance. During this course, the team travelled across the province to dialogue with local communities, many of whom were members of Sunni awakening councils.

Today, Al Takadum has three branches in Al-Qa'im, Fallujah, and Ramadi serving 10,903 clients and has financed the re-establishment of MSMEs and home improvement in the midst of insurgency. Al-Takadum's vision in enabling financial access to the people of Anbar Province was to replace violence with economic opportunities, and to empower the large numbers of widows and destitute women.

Al-Takadum is a market leader in Sharia-compliant Al-Murabaha microfinance in Iraq. An external audit revealed the MFIs' financial and field operations are in compliance with GAAP and CGAP best practices. In order to replicate its success and leadership in Islamic principles-based lending, Al Takadum is raising grant funding to establish a training center on Islamic finance for the microfinance sector in order to demonstrate practical and successful localized strategies for Al-Murabaha and other Sharia-compliant financial products in the near future.

Al Takadum believes in meaningful dialogue to further develop Anbar Province and Iraq and to build demand-driven quality financial services for the communities it serves.

4.3 INDIVIDUAL LENDING METHODOLOGY

Microfinance in Iraq was launched through individual lending methodology. This was different from the global practice whereby microfinance institutions start by offering financial services through the solidarity group lending methodology and then move to individual lending methodology subsequently. The departure from the normal global practice was mainly due to the high risk security situation in the country at the time. It was not easy to form groups and the principles of group formation and management by loan officers, and also free operation of micro and small enterprises normally operated by group members would have been very difficult if not impossible in such an environment. The processing of individual loans and the operations of enterprises financed therefrom did not have such constraints. Therefore, the loan methodology of choice as more MFIs came onto the scene was the individual lending methodology. As noted above, when the security situation improved, solidarity group lending was introduced in 2009 under the auspices of USAID-*Tijara*. The composition of the industry statistics clearly reflects the bias towards individual lending which comprises 90% of the total portfolio of the MFIs at June 30, 2012.

4.4 MFIs' ARRAY OF LOAN PRODUCTS

MFIs in Iraq offer a diverse range of lending products and target a variety of clientele profiles. The loans have been tailored to the needs of clients as the MFIs have gained more experience in serving the market. The range of products currently offered is reflected in table 10 below.

One of the popular products has been the home improvement loan which was developed with technical assistance from USAID-*Tijara*. This product has enabled the MFIs to meet their clients' needs to improve their existing homes.

Unlike traditional housing finance from commercial banks which involves mortgages and prolonged loan processing, home improvement through microfinance can be extended quickly with easier terms and simpler guarantees. Home improvement loans allow MFIs to reduce their risks by financing housing through a microenterprise product, while maintaining low delinquency rates and expanding their markets. As of end June 30, 2012, Iraqi MFIs had disbursed 17,445 home improvement loans of \$28 million to address the high demand and need to improve, refurbish, and extend existing homes.

TABLE 10: LOAN PRODUCTS

Loan Type	Loan Size (Range)	Interest Rate (Range)
MSME Start-up Loans	\$100 – 5,000	10% – 16%
MSME Loans	\$500 – 5,000	10%– 15%
SME Loans	\$5,001 – 25,000	10% – 15%
Agri-business Loans	\$500 – 25,000	10% – 16%
Home Improvement Loans	\$500 – 25,000	10% – 16%
Trade Loans	\$3,000	10% – 18%
Taxi Loan	\$500 – 25,000	10% – 18%
Consumer-Oriented Loans	\$500 – 2,000	10% – 12%
Lap top loans for students	\$500 – 2,000	10%

Interest rates charged by the Iraqi microfinance industry are among the lowest across the globe and regionally, particularly compared to more mature industries such as those in Morocco and India. However, MFIs may have to raise interest rates when they start incurring capital costs as they move towards more commercially oriented sources of funds in the next few years. Increasing scale and outreach will enable MFIs to lower interest rates and increase efficiencies without disrupting their relationships with clients, unless future capital costs are excessive.

Formal savings services are not available to the poor in Iraq and MFIs are not permitted to offer either voluntary or compulsory savings for their member clients, although a large proportion of them save informally with relatives or at home. Credit unions and savings cooperatives, generally seen in all microfinance sectors around the globe, have not yet formally developed in Iraq. In the near future, subject to enabling legal and regulatory environment, MFIs could commence mobilizing client savings as a form of collateral and to deepen and diversify their financial service product offerings to remain competitive.

4.5 IRAQI VULNERABLE GROUPS SUPPORT INITIATIVE (IVGSI)

In March this year, USAID-*Tijara* introduced the Iraqi Vulnerable Groups Support Initiative (IVGSI), which was designed to support and improve the livelihoods of groups of Iraqi families that are vulnerable to terrorist attack by virtue of their membership in an ethnic or religious minority group. Under the initiative, minority status is defined with respect to a family's home community, since a person may be a minority in their home community, but later flee to a community where their religious or ethnic group is in the minority. In addition, the initiative targets female-headed households and youth. This initiative has been implemented by USAID-*Tijara*'s MFI partners that were specifically selected by virtue of their existing and future capability to set up operations in the locations where the Iraqi Vulnerable and Minority Groups (IVMGs) reside. USAID-*Tijara* SMFC allocated a capital of \$3,750,000 to the three selected partners: Al Thiqa, BFF and Izdiharouna. These partner MFIs have been disbursing loans ranging from \$500-5,000 and averaging \$3,000 per loan. At this average, the grant initiative is projected to reach about 1,250 vulnerable clients. As of June 2012, these partner MFIs have disbursed over \$2.4 million of the grants allocated and are expected to fully disburse the balance by October 2012. In addition to the grant allocation, the partners have been motivated to use their own funds in reaching additional clients from these groups thereby greatly enhancing the impact of the grant funds. The initiative has reached 1,377 borrowers to date, 807 through the IVGSI grant funds and an additional 570 through the MFIs' own funds. At this rate of disbursement, the impact of outreach of the grant funds will be over 170% just from the initial disbursements. Incremental impact is expected when the MFIs disburse the repaid funds to the same vulnerable groups as agreed.

4.6 WOMEN'S EMPOWERMENT INITIATIVE

USAID-*Tijara*, in conjunction with its MFI partner Izdiharouna, is implementing a "women empowerment initiative" designed to exclusively target women who do not have traditional collateral required by banks and financial institutions and have therefore lacked the means to access credit services. Izdiharouna offers loans through SGL, individual lending and Islamic lending methodologies to the targeted women entrepreneurs. Women in Iraq, under the current cultural, political and social conditions, have had to bear with many limitations and restrictions on their ability to access financial and credit services that would have enabled them to engage in income generating activities. The grant will enable Izdiharouna to give opportunity to women to access credit services and apply for loans that they need to create or expand their businesses. All that is required in order to access the facility is that

the applicant be a woman needing a loan to develop or expand her business that is assessed to be viable. This grant offers additional opportunities for women in addition to those opportunities already created through other grants implemented by USAID-*Tijara* such as IVGSI noted under section 4.5 above and ensures further progress in inclusive financial services.

4.7 IRAQI YOUTH INITIATIVE FOR YOUNG ENTREPRENEURS' ACCESS TO FINANCE

The Iraqi Youth Initiative (IYI) is also implemented through USAID-*Tijara*. The goal is to create a variety of opportunities for youth, primarily recent graduates, to enter new professions, establish businesses, earn salaries and profits, and generate additional employment. IYI is an innovative combination of institutional resources designed to ensure that young clients benefit from an effective, holistic approach. IYI is developed specifically to generate employment opportunities at the maximum possible rate. It has three major focus activities:

- Access to finance for youth previously not available called Young Entrepreneurs' Access to Finance (YEOF),
- Creating self-employment opportunities, and
- Bridging the gap between employers seeking skilled staff and potential employees as indicated in the market assessments conducted by USAID-*Tijara*.

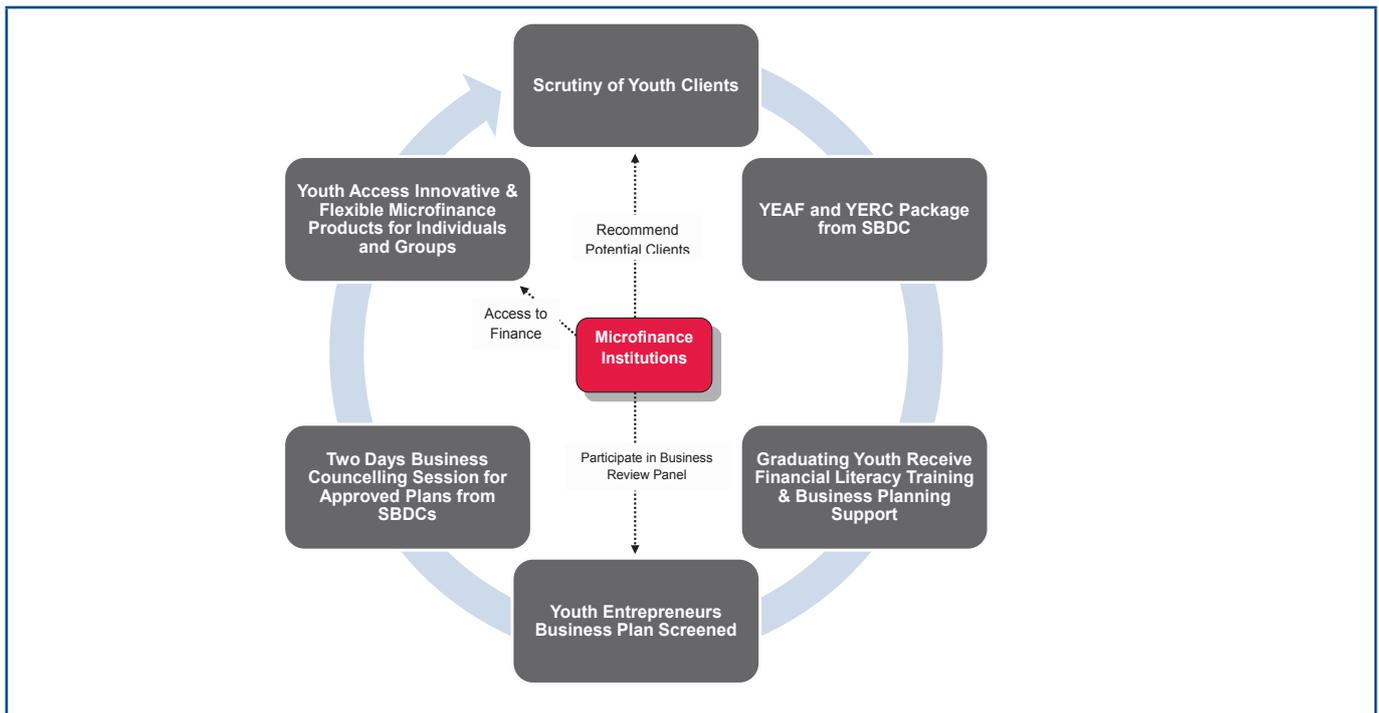
The YEOF was designed with the objective of developing and expanding demand-driven financial services for Iraqi youths 18-35 years old. The activity facilitates access to finance for youth by introducing loan products that enable young entrepreneurs to create businesses after receiving general business and financial literacy training through classroom and small group counseling sessions that develop skills in their respective business sectors. The trainings have helped qualify the youth to apply for loans from participating MFIs based on the quality and substance of the business plans they submit as part of their applications.

YEOF's loan products have offered more flexible loan terms and conditions without compromising the overall credit culture in the industry. The products offer a 15-month loan repayment period instead of one year, and grace periods of up to three months. Collateral requirements are more flexible and depend mainly on reputation/background checks undertaken by the MFI in addition to the motivation to repay as part of the broader IYI objective of instilling positive and results-oriented entrepreneurial vigor among participating youth. As of the end of June 2012, 1,603 loans had been disbursed amounting to \$5,229,200 through which new enterprises have been created nationwide (12% of loan funds allocated to women) creating over 3,189 permanent jobs (14% of which have been filled by women).

Finding that first job is always difficult for young adults. It is especially difficult in Iraq where adults have to cope with unemployment of 13 to 30 percent depending upon the community. But prospects for youth employment improved in a dozen communities with the introduction of the Iraqi Youth Initiative. The program teaches business skills to ambitious youths aged 18 to 35 at USAID-*Tijara*'s network of 12 Small Business Development Centers (SBDCs).

Young adults who exhibit entrepreneurial skills are encouraged to write a detailed business plan and then they are referred to one of the seven USAID-*Tijara* partner microfinance institutions (MFIs) supporting the initiative. These MFIs are prepared to give loans averaging \$3,000 to deserving candidates. Ongoing mentoring by Initiative staffers, and also by the SBDC and MFI, ensures implementation of the business plan and the timely repayment of the loan.

FIGURE 23: YOUTH FRIENDLY LENDING METHODOLOGY AND PRODUCTS ENABLE ACCESS TO FINANCE FOR IRAQI YOUTH



4.8 ALTERNATIVE COLLATERAL OPTIONS FOR GREATER OUTREACH

Collateral plays three roles in the microfinance sector: a) it demonstrates the commitment of the borrower to honor his/her contract prior to disbursement of the loan, b) it focuses the mind of the borrower in terms of responsibility during the life of the loan, and c) it offsets loss in the event of default²¹. Borrowers prefer collateral that is easily available and minimizes impact on the household and transaction costs. Lenders prefer collateral that can be liquidated in a timely manner, is marketable, minimizes transaction costs, and provides protection of loan capital.

Traditional collateral options in Iraq include:

- The co-signature of one who earns an Iraqi Government salary; in the event of default, 20% of his/her monthly salary is deducted to satisfy a guaranteed loan. This option has proved to be very effective; however, it has an inherent risk in case of any change in political structure and stability in the country.
- Solidarity group lending – peer monitoring: With this form of guarantee, 3-5 unrelated persons co-sign and borrow as a group. In the event one defaults, the other group members satisfy the outstanding loan balance.

These guarantees, however, were limiting MFIs from achieving market potential. Over 90% of the outstanding portfolio of \$143.9 million at June 30, 2012, and 75% of the 93,627 active clients at that date are guaranteed through the first collaterals mentioned above. The rest (both in terms of outstanding portfolio and active clients) are guaranteed using the SGL methodology. Over-reliance on government employees to use their salaries as collateral increases risk to MFIs. It was therefore important that viable alternative collateral options be developed to enable MFIs to diversify their risks and reach borrowers that do not have access to government employees.

With technical assistance of USAID-*Tijara*, alternative collateral options were developed and piloted by some of the MFIs. These alternative collateral options have helped the MFIs to diversify risks associated with lending to the poor and women and vulnerable segments of the population. In general, these developments are facilitating uniform access to credit for lifting those under the poverty line to becoming productive citizens in the growing private sector in Iraq. Some of the benefits emanating from the alternative collateral options are as follows:

- Increasing outreach - exploring new markets and target groups like youth and women who do not have access to traditional collaterals like guarantors.
- Overcoming the limitation of guarantors and thereby enabling MFIs to mitigate risks by diversifying collateral options.
- Improving the brand image of MFIs in the eyes of all stakeholders.

²¹ Balkenhol B and Schutte H, "Collateral, Collateral Law, and Collateral Substitutes", Social Finance Programme, Working Paper No. 26, 2001, Employment Sector, International Labour Office, Geneva, pg 7

Business Training and a Microfinance Loan Help a Struggling Carpenter in Muthanna Province Start His Own Business

Some people dream big with visions of fancy cars and foreign vacations. Ali Majeed Flaih's dream was just to keep his family from starving.

The son of a Muthanna carpenter, Ali grew up watching his father produce handmade furniture for neighbors. The family never had much. And after his father died several years ago, Ali realized the family really had nothing at all. There were no savings, real property, credit history or influential friends. "My dream was to make enough money to feed my family and be able to set something aside so that one day I might be able to marry and have a family of my own."

In 2011, Ali heard about the Iraqi Youth Initiative, a USAID-Tijara program designed to help unemployed young Iraqis find their first job or start a business of their own.

After attending a week's business training at the Samawa Small Business Development Center, Ali realized he did not want to be a salaried employee since temporary jobs in Samawa come and go like zephyrs from Arabia.

He also realized that producing handmade furniture never could be viable economically. "I needed to produce more doors, dressers and desks in large numbers and the only way to do that was to mechanize."



Ali Majeed Flaih used a microfinance loan to hire two employees and buy a number of power tools for his Samawa carpentry shop.



Ali Majeed Flaih uses imported hardwood to make office doors, desks and cabinets.

Armed with a business plan developed during his training, Ali went to Amalkom, a microfinance institution that since its inception in January 2010 has disbursed loans of more than \$17 million in seven southern Iraq provinces and created over 13,000 jobs. After receiving a loan of \$2,200, Ali began making his modest shop a bit more modern. He bought power saws, sanders, drills and a router.

As word spread that Ali completed jobs quickly, he started receiving many more orders. This turn of events improved his revenues significantly. However, instead of declaring the increased revenue as profit, Ali - now age 24 - reinvested the money into the business and hired two employees.

Ali concedes he has not yet saved enough money to marry and start a family of his own, but he no longer has to work just for food and shelter. "I could not have started a real business without my Amalkom loan," he says and adds with an air of expectation, "I still have dreams. They are just bigger than they were before."

CHAPTER 5

by Saeed Lateef



THE MICROFINANCE INDUSTRY: FUTURE DIRECTIONS FOR GROWTH

'One Man's trash is another man's treasure' certainly is true in Iraq's Ninawa Province where Mosul ironmonger Bashar Mohammed Saeed turns discarded scrap metal into forged drain covers and other recyclables thanks to a microfinance loan from the Al-Tadhamun Economic Development Center.

5.0 THE MICROFINANCE INDUSTRY FUTURE LEADERSHIP

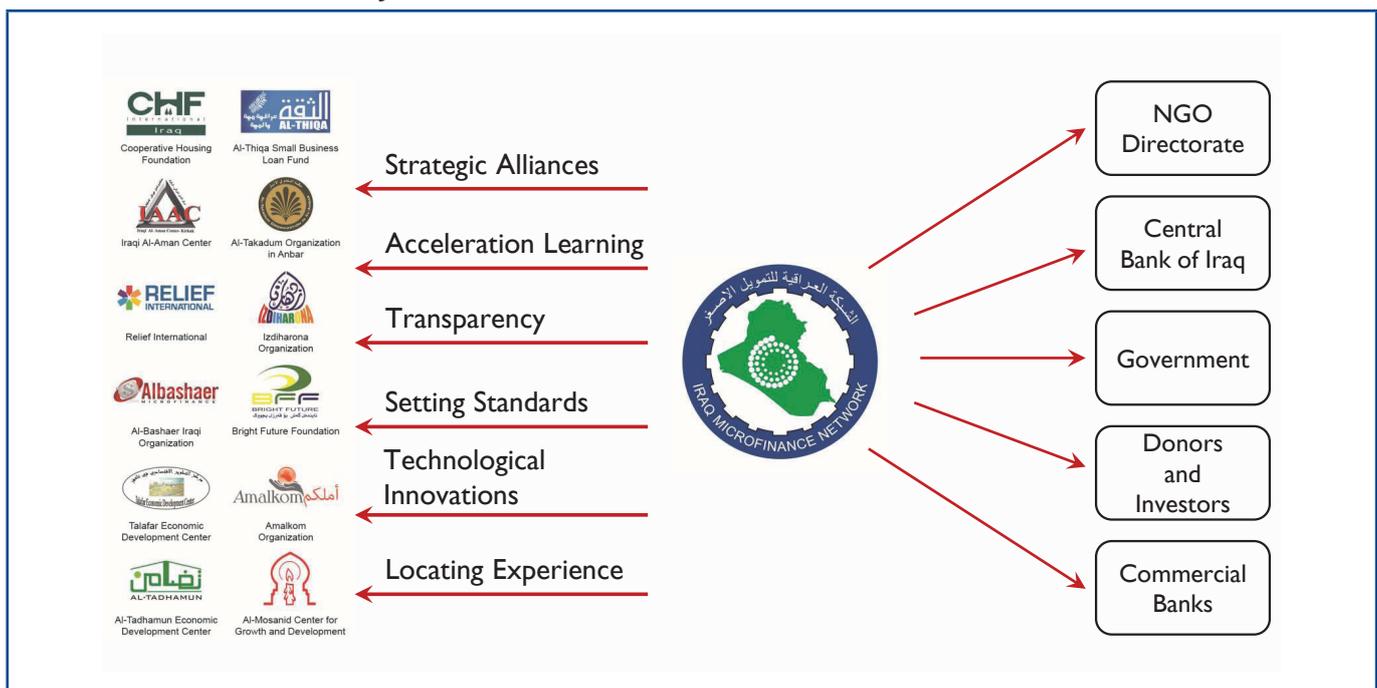
USAID will continue to play a strategic role in leading the Iraqi microfinance sector in its next phase of maturity. The ability of the industry to leverage drivers of growth and prioritize initiatives at the sector level will determine the sector’s success in reaching out to Iraq’s 7.4 million poor. USAID, through its implementing partner USAID-*Tijara*, together with other stakeholders including the 12 MFIs, has made good progress in development of the microfinance industry as indicated in earlier chapters.

USAID-*Tijara* has already helped build technical and industry infrastructure to create an enabling environment for inclusive sustainable microfinance sector in Iraq. One of the key examples is the Iraq Microfinance Network (IMFN). The USAID-*Tijara* Sustainable Microfinance Component (SMFC) has been performing most of the activities of the IMFN to date. These activities have been designed to develop a sustainable microfinance sector in Iraq. SMFC has pursued a sector development approach (already explained in earlier chapter) for the Iraqi microfinance industry. A list of activities currently carried out by SMFC to develop the microfinance industry in Iraq is given as follows:

- Serving as an information clearing house on the sector;
- Disseminating and promoting best practices;
- Attracting and encouraging coordination among donors;
- Facilitating linkages between MFIs and other development organizations;
- Providing and/or facilitating access to training for MFIs;
- Fostering transparency through performance monitoring;
- Advocating for a more favorable enabling policy environment; and
- Encouraging a long-term outlook in the industry.

The IMFN was registered in April and institutionalized in May 2012 as noted above. It is being operationalized through the support of USAID-*Tijara* and will gradually take responsibility for implementing the above listed activities as approved and prioritized by its BOD and General Assembly. USAID-*Tijara* will focus on strengthening the IMFN through grant support and human resource capacity building to implement the strategic business plan and activities approved by its board. This will ensure smooth transfer of roles and responsibilities to IMFN when USAID-*Tijara* closes out at the end of its term in January 2013.

FIGURE 24: FUTURE ROLES PERFORMED BY THE IRAQ MICROFINANCE NETWORK (IMFN); THE USAID-TIJARA CREATED MF INDUSTRY SUPPORT INFRASTRUCTURE.



5.1 KEY DRIVERS FOR GROWTH

5.1.1 Market Potential

The growth opportunities for the Iraqi microfinance industry will attract the entry of more actors seeking investment opportunities. Social motivations linking MFIs with key stakeholders such as MFI promoters, donors and policy makers will influence this drive for larger outreach to achieve massive scale. Client segmentation and demand on the one hand and specific loan products with enabling features such as alternative collateral options and linkages to markets on the other will facilitate scale and financial deepening.

- **Untapped depth:** Reaching out to vulnerable and economically-challenged communities by MFIs marketing their services through formal and informal networks will spread awareness about microfinance among potential clients. Innovative marketing techniques will need to be carefully applied to the specific needs of clients and the fragmented market where MFIs operate and face strong competition. Direct marketing, products and services that meet clients' needs and also advertising to potential markets and to entrepreneurs should prove to be effective. Additionally, MFIs need to form alliances with community-driven programs and local events to engage with potential clients on the services offered and should also address challenges of access to finance for the target groups. USAID-Tijara SMFC team regularly visits partner MFIs to provide on-site technical assistance on microfinance-related activities. Field visits to clients are an important feature of these visits. The SMFC team identified specific challenges clients are facing to access financial services. MFIs have been advised on how to address the challenges to provide inclusive products and services, and initiatives that facilitate this objective have been introduced and launched.
- **Under-served rural markets:** Approximately 10.8 million people live in rural Iraq, with agriculture and livestock as their predominant economic activity²². Over 90% of the current microfinance portfolio, however, is concentrated in urban areas. MFIs will need to increasingly move to rural areas as they are able to incorporate suitable loan products for the agricultural sector and fine-tune SGL group formation practices based on local contexts. Their success, however, in providing financial services for the rural poor will be contingent upon an improved security situation as well as the MFIs' ability to develop loan products and services that target rural-based activities and enterprises that sell and/or offer agricultural inputs, post-harvest storage facilities, irrigation equipment, food processing and value chain development programs.

5.1.2 Technology

Technological advancement has brought a wide range of opportunities through which MFIs can benefit. Advancement in MIS, ICT and Electronic Payment Systems has availed opportunities for MFIs to improve their efficiency and manage risks thereby increasing their outreach and profitability. USAID-Tijara has provided the technical and financial support that has enabled its partner MFIs to acquire and implement the necessary MIS software systems that enable them to take advantage of the above mentioned opportunities.

The MFIs benefit from the above technologies in the following ways²³:

- Informed decision making
- Increased flexibility
- Lower operating cost
- Increased transparency
- Accurate reporting
- Improved client service and convenience
- Rural outreach

Use of technology is also helping the Iraqi microfinance sector increase its outreach to vulnerable groups, including the poor and women. The microfinance industry is improving efficiencies and should realize the listed benefits through use of the technology effectively both at the head office and at the field operations levels. The use of technology, especially its potential for microfinance in Iraq, and also the benefits to be realized should motivate the MFIs to adopt these systems.

²² <http://www.tradingeconomics.com/iraq/rural-population-wb-data.html>

²³ Funding Microfinance Technologies, CGAP Donor's Brief No. 23, April 2005

5.1.3 Timely Availability of Trained Human Resources

A critical driver for growth will be the ability of Iraqi MFI managements to successfully lead the industry. As microfinance becomes increasingly commercialized and integrated into the broader financial system, growth and market interaction will bring about more opportunities and challenges to the MFIs. The knowledge and skill set of MFI managements and staff should match the new challenges and opportunities. USAID has been intensively involved in capacity building and in technical assistance to ensure MFIs are adopting industry best practices. This has proved successful as the industry has adopted best practices and is growing in stature and receiving recognition within the MENA region and globally.

With improvement of their financial position, an increasing number of MFIs have started to finance their own capacity building programs. Participants in capacity building programs range from field staff to Boards of Directors. The programs include experience sharing, formal short-term training on microfinance and long-term academic programs. Iraqi MFIs have so far maintained the balance between offering attractive remuneration to their staff and keeping their administrative costs low enough to sustain their operations. Like any other industry, the Iraqi microfinance sector is witnessing the turnover of some staff members like loan officers and a few senior level employees. This has encouraged MFIs to focus on developing a robust middle management through initiatives that meet their expectations and allow for effective knowledge transfer to new employees thereby facilitating continuity of their operations.

5.1.4 Enabling Environment

In addition to establishing and strengthening partner MFIs in the country, USAID-*Tijara* has played a key role in implementing USAID's strategic focus in poverty alleviation and job creation in Iraq's high risk conflict environment. This role has entailed all of the key aspects of development of the microfinance industry including advocacy for an enabling environment by engaging a number of stakeholders in the industry. The stakeholders have included the CBI, NGOs Directorate and other government agencies and ministries. These stakeholders have recognized the important role of MFIs in the financial sector and are increasingly engaged in supporting this role and in taking into account the regulation and supervision of the industry when appropriate legislative framework is formulated. Policymakers' increased understanding of the dynamics of the microfinance sector and the role of MFIs helps them develop appropriate legal and regulatory environment that facilitates and enables MFIs to grow and also achieve their dual mission of poverty alleviation and long-term sustainability. USAID-*Tijara* is encouraged by the positive response in recognition of the role of the microfinance industry and will continue its engagement for the resolution of the challenges.

5.2 PRIORITIES FOR SUSTAINABILITY

5.2.1 Ensure Institutional Growth Capacities and Risk Management Systems

While following ambitious growth trajectories, MFIs also need timely and complimentary investments into human resources, technology, systems and processes. Iraqi MFIs have thus far done a commendable job of managing high portfolio sizes of excellent quality. Investments in human resources, technology, systems and processes will have a great impact on the availability of future growth capital. Building on the success of the industry infrastructure in Iraq, MFIs still need technical assistance on operational growth management and risk management systems. Institutional capacities and strengths will be key in their ability to reach scale and maintain sustainability.

5.2.2 Strengthened Governance for effective oversight and risk management

To ensure a steady and healthy growth and development of risk management systems in MFIs, USAID-*Tijara* has organized technical assistance trainings for strengthening MFIs' governance systems. A thorough governance risk assessment was conducted in all Iraqi MFIs and weaknesses and associated risks were identified and the required risk mitigation systems are being put in place. All MFIs' BODs have been trained on good governance through the trainings organized by USAID-*Tijara* and many of them have reorganized their governance structures to enhance their capabilities to manage institutional growth and improve their risk management systems.

5.2.3 Client Focus: Putting Customers at the Core

The success of microfinance measured on social and commercial terms is built on the bankability of its clients and the ability of MFIs to offer services previously unavailable to the poor and women and other marginalized and vulnerable groups. As MFIs grow and become more commercialized, it is important that their clients' interests remain at the core of their institutional decisions. Iraqi MFIs, with the assistance and support of USAID-*Tijara*, have

introduced a number of new products which are suitable for marginalized segments of the community. Youth loan products, which are designed to create access to finance for unemployed youth, plus loans to vulnerable groups and to women are some of the recently introduced loan products. While some loan products are designed to satisfy current clients' demand, Iraqi MFIs are aggressively working towards introduction of new loan products to ensure the inclusiveness of their financial services thereby enhancing the outreach of Iraqi microfinance industry. Some of the measures being implemented are:

- **Client demographics:** MFIs need to categorize their client segments based on demographic characteristics like age, gender, geography, education, profession or enterprises and align their products and services accordingly. Increasing competition among Iraqi MFIs, and the endeavor to build on and sustain their market segments, has persuaded many MFIs to widen their client base by reaching out to more clients who were previously excluded from the mainstream finance sector.
- **Client needs and product diversification:** MFIs that both understand client needs and address them more effectively through viable business models should benefit from greater client retention. Products currently offered by MFIs are limited to credit, however, these can be augmented with new products such as micro-insurance. When the legal and regulatory framework in Iraq allows, savings mobilization could be a source of collateral and client insurance fund that helps mitigate the MFI's risks.
- **Client protection and responsible financing:** In 2010, the Iraqi microfinance industry, with the help of USAID-*Tijara*, developed and signed a pro-client Code of Conduct and Ethics. This Code endorses ethical principles and a commitment to benefit low-income Iraqis. The Code is a governing document that will continue to provide guidance to the Iraqi microfinance industry on ethical lending and consumer protection principles. Endorsed by all MFIs, the Code obligates the MFIs to uphold values such as high quality and sustainable financial services, transparency, respect for religion, fair lending and collection practices, privacy of client information and integration of social values into all business decision making. Further to the Code, the Iraqi microfinance industry has embarked on introducing social performance management within all MFIs. The IMFN will spearhead the effort to ensure social performance management is embraced by all MFIs for impact measurement and for customer protection and responsible financing.
- **Credit bureaus:** The IMFN aims to facilitate establishment of a credit bureau for the Iraqi microfinance sector in order to provide information on microfinance clients' credit history and basic information about loan providers. Credit bureaus not only provide information on delinquent clients, but also protect clients against unfair lending practices. A good credit bureau also should help identify over-indebted clients, as this is a growing concern in the microfinance industry. MFIs need to share information on client histories to minimize risks of lending and help maintain healthy portfolios. Credit bureau consultation also helps reduce transaction costs and increase institutional efficiency by rapidly identifying clients with poor repayment histories. Government, donors, technical assistance providers, and MFIs must work together to develop an effective policy and institutional framework for client information sharing, while still protecting client confidentiality. USAID-*Tijara* introduced a central data repository where negatively performing clients are reported in a secure blacklist system on the Iraqi Microfinance Knowledge Portal (www.imfi.org). Authorized users can search the database of blacklisted borrowers. No loan or other financial data is stored in the database. The system is a rudimentary credit bureau serving the MFIs' needs to identify delinquent and defaulting clients pending implementation of a credit bureau by the CBI, currently being developed with assistance of the Financial Sector Development project. The IMFN will gradually take over the role of hosting and administering the blacklist system.

5.2.4 Access to Capital: Diversified Sources of Funds

The major sources of funding for microfinance institutions to finance their growth have traditionally come by way of savings deposits from clients, debt financing from commercial sources, and equity financing from donors and other stakeholders. The main source of funding for Iraqi MFIs has been donor funding mainly from USAID and other US Government agencies. Other donors include DfID, UNOPS, UNIDO, UNDP and AusAID. As of June 2012, USAID funded projects such as Izdihar, *Tijara* and Inma had contributed 53% of donated equity to Iraqi microfinance institutions while the rest of the capital has been provided through the other sources. USAID-*Tijara* has been actively engaging stakeholders such as the CBI, NGOs Directorate, and MFIs to create an enabling legal and regulatory environment for an inclusive sustainable microfinance sector. As a result of these efforts, the CBI issued the SME Finance Companies law. The law provides guidelines and requirements for set up and operations of for-profit NBFIs. This law should have provided a window of opportunity for NGO MFIs to transform into for-profit legal entities but that window was abruptly shut when the CBI and NGOs Directorate categorically clarified that under the current legal framework, it will not be possible for NGO MFIs to transfer their capital and assets

to either LLCs or JSCs. The transfer was prohibited to ensure there would be no distribution of grant capital in future as it belongs to the Iraqi people. Therefore, transformation of NGO MFIs to private LLCs remains a major challenge pending formulation of the legislation that would facilitate such change. In the meantime, USAID-*Tijara* and the IMFN will continue to work with the authorities on enhancing the legal and regulatory framework to support further expansion and growth of the MFIs to help in meeting the demand for inclusive financial services. USAID-*Tijara* will continue its leadership and intensify its efforts to coordinate with other donors such as the World Bank and UNDP to synergistically mold an environment more conducive for incentivizing investors to provide funding that will enable Iraqi MFIs to expand their inclusive financial services.

When appropriate legislation is formulated thereby creating an enabling environment, the more mature MFIs should then be incentivized to transform into for-profit companies. In doing so, it is hoped that different financing options such as debt, equity and guarantees will be used as MFI investment vehicles. The Iraqi microfinance sector needs financing vehicles that provide low-cost accessible on-lending capital and also promote best practices and self-sufficiency.

5.2.5 Value Chain Financing

Value-chain financing has emerged as a tool to help businesses access essential financing that enables them to meet market demand while increasing their efficiency and strengthening their position with suppliers and buyers. It is especially beneficial for farmers and small-scale rural and urban businesses. Value chain finance helps improve productivity and quality by creating and strengthening market linkages between supply and demand markets while also reducing transaction costs and enhancing social impact. MFIs can introduce innovative approaches to value chain finance to serve both micro and small scale producers, thereby enabling them to leverage relationships with suppliers and buyers in urban markets.

Small scale farmers are gaining increased attention as part of the government's mandate to promote inclusive economic growth throughout Iraq. In early 2010, the Ministry of Agriculture approved over 2,000 loans of approximately \$15,000 each for small scale farmers²⁴. Isolated business interventions may not result in the desired outcome. Various businesses involved in activities from harvesting to distribution of outputs to the end user should be strong enough to absorb the increased farm products so that the farmers get reasonable return from their farming businesses. MFIs' ability to develop value chain capacity and to structure new financing products focused on the series of activities within the value chain determine the success of their contribution in the improving livelihoods of the farmers and will enable them to create greater value for the poor. The value chain and agricultural financing has also been considered as an approach to improve food security and nutrition to the poor and vulnerable groups such as women and children. Low-income communities suffer from increased food prices and security issues; Iraqi rural communities are no exception to this phenomenon. Agriculture and rural finance will increase rural household income, create jobs, and enhance food security.

USAID-*Tijara* partner MFIs have been providing agricultural loans to cater to the capital needs of the rural communities. Response to this product has been promising and its impact has been positive. Success of the agriculture loan product encourages MFIs to work through the value chains to improve rural livelihoods and enhanced food security in the country through offering quality financial services that enable realization of benefits from increased customer base and diversified loan products.

²⁴ <http://www.iraq-business-news.com/?p=2617>

AGRICULTURAL LOANS FROM TALLAFAR ECONOMIC DEVELOPMENT CENTER GIVE HOPE TO NINAWA FARMERS

The Tal'afar Economic Development Center (TEDC), a microfinance institution operating in Ninawa Province supported by the USAID-*Tijara*, offers a variety of agricultural lending products that allow farmers to more carefully plan their crop yields and survive periods of bad weather and price fluctuations.

Since inception in January 2008, TEDC has helped over 13,000 Ninawa residents secure more than \$27.7 million in critically needed financing. Among the most grateful beneficiaries, however, are some 296 farmers who have received \$995,950 to help them harvest crops, buy pesticides and fertilizer and hire more than 150 farm workers.

Tal'afar Economic Development Center (TEDC) disburses Agriculture Loans to help Small-Scale Farmers in Ninawa

Access to quality financial services, especially for rural small-scale farmers is a challenge anywhere in the world. Such farmers face numerous obstacles. Mostly they lack the capital needed to invest in the irrigation technology needed to boost productivity and profits. This certainly is the case for small-scale farmers in Ninawa Province. They cannot access the financial services they need from the three banks in the province. Their situation is made even more dire due to limited access to guarantee choices required by MFIs to give them access to credit services. However, USAID-*Tijara's* Ninawa province partner microfinance institution, Tal'afar Economic Development Center (TEDC) overcame many of these obstacles when it launched its "Agricultural Loan" product. Agricultural loans provide tremendous relief to small scale farmers. TEDC disburses agricultural loans to small-scale rural farmers to help them meet their farming needs. Agriculture is a key component of Ninawa's economy, particularly cereal production, with 39% of the 2.4 million people living in rural areas. Of the nearly one half million living in the province below the poverty line of U.S. \$2.2 per day, over 80% are in rural areas.



Qasim Mohammed Younis tends his flock on the high plains of Ninawa.

The agricultural loan product offered by TEDC is innovative in that it has a longer repayment period, offers a grace period of three months and provides loan sizes of up to \$5,000. Innovation comes from repayments scheduled according to the seasonal outputs of farmers. It also comes from how the loan can be guaranteed – one guarantor or co-signer with means (and not necessarily a salaried government worker), witnessed by two others. This product adds to TEDC's already impressive menu of loan products it offers small-scale manufacturers, traders and service providers. The MFI's performance and profitability have continued to increase.

Since it was established in July 2007, The TEDC has disbursed over \$27.7 million to 13,273 clients as of June 30, 2012, and as of that date it had a portfolio of over \$5.6 million with 4,803 active clients and near perfect loan recovery.

One of the farmers, Mr. Qasim Mohammed Younis, who received a loan stated, "I needed money to dig a tube well to solve the problem of water scarcity for my livestock. I tried to get a loan from one of the banks in my district but they did not help. Through TEDC, I can use the \$5,000 to make these investments to improve my family's income. I can also start saving to buy a small truck so that I can sell my dairy products in the city."

Grain Mill Enterprise Through Microfinance



Despite electrical outages, Noor Khether, Hala Kwan Jasim, Scott Jassim and Fethiye Mahdi Awad produce two tons of flour a day at their Al-Qa'im grain mill.

Al-Romana village is a tiny Euphrates River community close to Iraq's Syrian border. People born in Al-Romana rarely leave, preferring a traditional life where neighbors take care of each other. Recently, six simple women, four of them linked by marriage to the same man, left their 26 children to visit the Al-Takadum Microfinance Organization in Al-Qa'im 15-km away. They wanted to start a grain mill, they told the loan officer, so they could grind the wheat grown by their family and others. "We live in an agricultural area with a lot of wheat but no mill," says Scott Jassim Mohammed, a mother of ten who is president of the group. None of the women had formal education.

The loan agreement would have to be formalized with a mark rather than a signature. But that did not prevent Al-Takadum from giving them a \$4,500 loan. The six women have proved themselves to be successful business partners. Nearly all of the area's wheat farmers use their mill. The women work six days a week and produce two tons of flour a day. They take a percentage of the flour they produce and sell it to locals at prices below those in the grocery store. This year their average weekly revenue is IQD 420,000 or \$350. They have made every payment to Al-Takadum on time and are considering applying for a second loan.

"Our lives have changed with this mill because for the first time ever we have money," says Scott. "Our only problem is that the electricity keeps going off. If we can get a second loan from Al-Takadum we'll buy a generator."

CHAPTER 6

by Saeed Lateef

MICROFINANCE INDUSTRY STATISTICS

Romeel Nazar operates a bakery in the Northern Iraq city of Erbil. Every day, from 5 a.m. to 2 p.m., Romeel and his four employees bake hundreds of pieces of flat bread in two tandoor ovens. Romeel's biggest problem was keeping employees since kneading dough is hard work. So last year he went to Erbil's Bright Future Foundation, and borrowed 3.6 million IQD or \$3000 to buy an electric mixer. "My employees are much happier," he smiles. "We finish baking quicker and nobody complains anymore."

MICROFINANCE INSTITUTIONS IN IRAQ AS OF JUNE 2012

Indicators		CHF	Amalkom	
Age		8 Y, 11 Mo	2 Y, 5 Mo	
Start Date		July'03	January' 10	
HQ		Babil	Babil	
Operating Area		Babil, Baghdad,Sulaymaniyah, Basrah,Al-Midaina,Karbala, Samawa, Najaf, Diwaniyah, Nassriya , Kut and Erbil	Hilla, Karbala, Najaf, Diwaniyah, Nassriya, Baghdad, Semawa, Basra	
No. of Offices		13 main offices and 1 satellite office	6 main offices	
Total # of staff		320	47	
Total # of Loan Officer		95	20	
Female LO		11	12	
Case Load		209	324	
Loan Portfolio as of 30th June 2012				
Loans Outstanding	Total Outstanding \$	45,265,018	5,297,077	
	Total Outstanding #	19,816	6,477	
	Female %	16%	37%	
	Individual \$	45,265,018	1,880,850	
	Individual #	19,816	697	
	Female %	16%	12%	
	Group #	-	3,416,227	
	Group Members	-	5,780	
	Group #	-	1,891	
	Female %	-	39%	
PAR> 30 days		0.1%	0.5%	
Average loan Size	Total Outstanding	\$2,284	\$818	
	Individual	\$2,284	\$2,698	
	Group	-	\$591	
Outstanding Loan Structure	Business Loans	Service	24.2%	39.2%
		Production	4.8%	4.3%
		Trade	58.3%	53.2%
		Total	87.3%	96.7%
	Agribusiness Loan	1.7%	3.3%	
	Home Improvement	9.8%	-	
Loans Disbursed Since inception	Total \$	401,603,058	17,139,150	
	Total #	137,331	16,887	
	Female %	14%	26%	
	Individual \$	401,603,058	3,108,350	
	Individual #	137,331	766	
	Female %	14%	13%	
	Group \$	-	14,030,800	
	Group Members	-	16,121	
	Group #	-	5,268	
	Female %	-	27%	
Outstanding Growth % past 12 months		5%	67%	
No. of jobs created		56,820	12,901	
Received fund as of 30th June 2012				
USAID/ Izdihar- Tijara (Loan Capital)		\$3,500,000	\$6,324,798	
USAID/ Izdihar -Tijara (Operation Capital)		\$3,207,865	-	
USAID/ Inma (Loan Capital)		-	-	
USAID/ Inma (Operation Capital)		-	-	
Total USAID		\$6,707,865	\$6,324,798	
Loan Capital Others		\$25,269,908	\$950,000	
Operation Capital Others		\$6,482,120	\$50,000	
Total Others		\$31,752,028	\$1,000,000	
Grand Total		\$38,459,893	\$7,324,798	
% USAID Contribution to Total		17%	86%	
Financial Ratios June 2012				
Operational Self Sufficiency (OSS)		124.3%	103.8%	
Financial Self Sufficiency (FSS)		120.1%	88.2%	
Operation Expense Ratio (OER)		21.8%	18.3%	
Yield		27.6%	25.9%	
MENA Benchmarks		MENA Medium	MENA Small	
Operational Self Sufficiency (OSS)		102.3%	114.1%	
Financial Self Sufficiency (FSS)		102.3%	107.3%	
Operation Expense Ratio (OER)		16.7%	19.1%	
Yield		30.2%	40.7%	

Indicators		RI	Izdiharuna	
Age		5Y, 11 Mo	4 Y	
Start Date		July'06	June'08	
HQ		Suleimaniya	Suleimaniya	
Operating Area		Sulaymaniyah, Kut,Karbala, Amara, Basrah, Hilla, Najaf, Erbil, Kirkuk	Iskandarea,Kut ,Sadda, Hilla,Najaf, Karbala ,Amara, Basra, Suleimaniya, Baghdad	
No. of Offices		8 main offices and 4 satellite offices	9 main offices and 4 satellite offices	
Total # of staff		104	75	
Total # of Loan Officer		30	34	
Female LO		11	8	
Case Load		339	230	
Loan Portfolio as of 30th June 2012				
Loans Outstanding	Total Outstanding \$	10,319,338	7,486,410	
	Total Outstanding #	10,180	7,828	
	Female %	31%	25%	
	Individual \$	4,978,414	4,770,134	
	Individual #	3,548	3,426	
	Female %	21%	21%	
	Group \$	5,340,924	2,716,276	
	Group Members	6,632	4,402	
	Group #	2,595	1,437	
	Female %	37%	27%	
PAR> 30 days		2.7%	3.6%	
Average loan Size	Total Outstanding	\$1,014	\$956	
	Individual	\$1,403	\$1,392	
	Group	\$805	\$617	
Outstanding Loan Structure	Business Loans	Service	23.4%	34.2%
		Production	1.9%	1.5%
		Trade	40.2%	51.5%
		Total	65.5%	87.2%
		Agribusiness Loan	6.2%	7.8%
	Home Improvement	27.2%	4.5%	
Loans Disbursed Since inception	Total \$	63,752,651	39,069,218	
	Total #	39,789	30,645	
	Female %	28%	22%	
	Individual \$	37,704,865	21,614,765	
	Individual #	18,848	11,439	
	Female %	21%	20%	
	Group \$	26,047,786	17,454,453	
	Group Members	20,941	19,206	
Group #	7,410	6,112		
	Female %	34%	24%	
Outstanding Growth % past 12 months		20%	40%	
No. of jobs created		6,032	3,617	
Received fund as of 30th June 2012				
USAID/ Izdihar- Tijara (Loan Capital)		\$4,145,156	\$4,323,000	
USAID/ Izdihar -Tijara (Operation Capital)		\$2,254,764	\$150,000	
USAID/ Inma (Loan Capital)		-	\$1,000,000	
USAID/ Inma (Operation Capital)		-	\$271,742	
Total USAID		\$6,399,920	\$5,744,742	
Loan Capital Others		\$3,038,125	\$1,136,154	
Operation Capital Others		\$200,000	\$363,846	
Total Others		\$3,238,125	\$1,500,000	
Grand Total		\$9,638,045	\$7,244,742	
% USAID Contribution to Total		66%	79%	
Financial Ratios June 2012				
Operational Self Sufficiency (OSS)		102.3%	189.0%	
Financial Self Sufficiency (FSS)		90.8%	171.1%	
Operation Expense Ratio (OER)		19.6%	13.9%	
Yield		26.9%	36.1%	
MENA Benchmarks		MENA Small		
Operational Self Sufficiency (OSS)		114.1%		
Financial Self Sufficiency (FSS)		107.3%		
Operation Expense Ratio (OER)		19.1%		
Yield		40.7%		

Indicators	Al-Thiqa	TEDC		
Age	8 Y , 5 Mo	4 Y, 5 Mo		
Start Date	January'04	January'08		
HQ	Kirkuk	Tal'afar/ Nenawa		
Operating Area	Kirkuk, Baghdad(Waziriya), Diyala Ba'quba (Khanateen, Kifri, Kalar), Erbil, Dahuk, Sulayimaniyah, Al-Hamdaniya (Basheqa)	Tal'afar, Sinjar, Al-Eyadiya, Al-Qahtania, Shimal		
No. of Offices	8 main offices and 5 satellite offices	1main office and 4 satellite offices		
Total # of staff	151	27		
Total # of Loan Officer	42	13		
Female LO	7	1		
Case Load	371	369		
Loan Portfolio as of 30th June 2012				
Loans Outstanding	Total Outstanding \$	32,718,236	5,605,861	
	Total Outstanding #	15,561	4,803	
	Female %	17%	11%	
	Individual \$	32,055,771	5,326,956	
	Individual #	14,408	4,308	
	Female %	17%	12%	
	Group \$	662,465	278,905	
	Group Members	1,153	495	
	Group #	343	149	
Female %	15%	3.00%		
PAR> 30 days	0.3%	0.2%		
Average loan Size	Total Outstanding	\$2,103	\$1,167	
	Individual	\$2,225	\$1,237	
	Group	\$575	-	
Outstanding Loan Structure	Business Loans	Service	34%	7.1%
		Production	0.1%	-
		Trade	28%	64.2%
		Total	62%	71.2%
		Agribusiness Loan	8%	4.0%
		Home Improvement	224,175.927%	24.8%
Loans Disbursed Since inception	Total \$	224,175,927	27,739,900	
	Total #	76,700	13,273	
	Female %	17%	14%	
	Individual \$	221,406,277	27,410,950	
	Individual #	73,429	12,778	
	Female %	17%	14%	
	Group \$	2,769,650	328,950	
	Group Members	3,271	495	
	Group #	969	149	
Female %	14%	3%		
Outstanding Growth % past 12 months	27%	21%		
No. of jobs created	64,950	10,345		
Received fund as of 30th June 2012				
USAID/ Izdihar- Tijara (Loan Capital)	\$7,187,380	\$2,723,650		
USAID/ Izdihar -Tijara (Operation Capital)	\$3,503,801	\$25,000		
USAID/ Inma (Loan Capital)	\$3,988,658	-		
USAID/ Inma (Operation Capital)	\$80,254	-		
Total USAID	\$14,760,093	\$2,748,650		
Loan Capital Others	\$8,655,848	\$753,050		
Operation Capital Others	\$3,735,183	\$44,000		
Total Others	\$12,391,031	\$797,050		
Grand Total	\$27,151,124	\$3,545,700		
% USAID Contribution to Total	54%	78%		
Financial Ratios June 2012				
Operational Self Sufficiency (OSS)	305.4%	385.9%		
Financial Self Sufficiency (FSS)	194.1%	294.0%		
Operation Expense Ratio (OER)	7.3%	5.1%		
Yield	30.3%	20.2%		
MENA Benchmarks	MENA Medium	MENA Small		
Operational Self Sufficiency (OSS)	102.3%	114.1%		
Financial Self Sufficiency (FSS)	102.3%	107.3%		
Operation Expense Ratio (OER)	16.7%	19.1%		
Yield	30.2%	40.7%		

Indicators		AI-Tadhamun	AI-Aman	
Age		3Y, 5 Mo	5 Y, 11 Mo	
Start Date		January'09	July'06	
HQ		Mosul	Kirkuk	
Operating Area		Mosul, Tilkaif, Al-Shirqat, Al-Shikhan)	Kirkuk, Taza, Daquq, Al-hawija,	
No. of Offices		1 main office and 3 satellite offices	1 main office and 3 satellite offices	
Total # of staff		21	27	
Total # of Loan Officer		8	12	
Female LO		-	-	
Case Load		128	398	
Loan Portfolio as of 30th June 2012				
Loans Outstanding	Total Outstanding \$		1,379,576	7,297,975
	Total Outstanding #		1,023	4,771
	Female %		5%	25%
	Individual \$		1,379,576	7,009,207
	Individual #		1,023	4,283
	Female %		5%	25%
	Group \$		-	288,768
	Group Members		-	488
	Group #		-	158
Female %		-	26%	
PAR> 30 days		16.1%	0.1%	
Average loan Size	Total Outstanding		\$1,349	\$1,530
	Individual		\$1,349	\$1,637
	Group		-	592
Outstanding Loan Structure	Business Loans	Service	14.4%	28.3%
		Production	1.4%	12.3%
		Trade	73.5%	23.1%
		Total	89.3%	63.7%
		Agribusiness Loan	4.2%	-
		Home Improvement	4.9%	36.3%
Loans Disbursed Since inception	Total \$		5,159,690	32,931,012
	Total #		2,418	15,615
	Female %		4%	20%
	Individual \$		5,159,690	32,596,576
	Individual #		2,418	15,127
	Female %		4%	20%
	Group \$		-	334,436
	Group Members		-	488
Group #		-	158	
Female %		-	26%	
Outstanding Growth % past 12 months		36%	41%	
No. of jobs created		1,719	12,875	
Received fund as of 30th June 2012				
USAID/ Izdihar- Tijara (Loan Capital)		\$1,975,000	\$3,897,180	
USAID/ Izdihar -Tijara (Operation Capital)		-	-	
USAID/ Inma (Loan Capital)		-	-	
USAID/ Inma (Operation Capital)		-	-	
Total USAID		\$1,975,000	\$3,897,180	
Loan Capital Others		\$445,738	\$366,999	
Operation Capital Others		\$50,000	\$379,609	
Total Others		\$495,738	\$746,608	
Grand Total		\$2,470,738	\$4,643,788	
% USAID Contribution to Total		80%	84%	
Financial Ratios June 2012				
Operational Self Sufficiency (OSS)		135.1%	356.1%	
Financial Self Sufficiency (FSS)		118.3%	293.9%	
Operation Expense Ratio (OER)		11.1%	7.0%	
Yield		30.4%	28.8%	
MENA Benchmarks		MENA Small		
Operational Self Sufficiency (OSS)		114.1%		
Financial Self Sufficiency (FSS)		107.3%		
Operation Expense Ratio (OER)		19.1%		
Yield		40.7%		

Indicators	Al-Takadum			Total Al-Takadum		
	Al-Qaim	Falluja	Ramadi			
Age	4 Y, 10 Mo	4 Y, 7 Mo	4 Y, 6 Mo	4 Y, 10 Mo		
Start Date	August'07	November'07	December'07	August'07		
HQ	Anbar / Al-Qaim	Anbar/ Falluja	Anbar/ Ramadi	Anbar		
Operating Area	Al-Qaim, Anah, Rawa, Al-Obadi	Falluja, Amarya Al-Falluja, Al-Karma, Saqlawia	Ramadi, Heet, Hadiithah, Habanea, Rutba	Al-Qaim, Falluja, Ramadi		
No. of Offices	1 main office and 3 satellite office	1 main office and 3 satellite offices	1 main office and 4 satellite offices	3 main offices and 10 satellite offices		
Total # of staff	26	32	49	107		
Total # of Loan Officer	8	17	19	44		
Female LO	0	2	1	3		
Case Load	389	221	212	248		
Loan Portfolio as of 30th June 2012						
Loans Outstanding	Total Outstanding \$	2,816,167	3,696,583	5,169,490	11,682,240	
	Total Outstanding #	3,113	3,757	4,033	10,903	
	Female %	33%	10%	12%	17%	
	Individual \$	1,990,982	3,236,351	4,482,304	9,709,637	
	Individual #	1,627	2,784	2,857	7,268	
	Female %	27%	10%	11%	14%	
	Group \$	825,185	460,232	687,186	1,972,603	
	Group Members	1,486	973	1,176	3,635	
	Group #	386	308	338	1,032	
	Female %	39%	10%	16%	24%	
PAR> 30 days	1.0%	1.0%	9.0%	4.7%		
Average loan Size	Total Outstanding	\$905	\$984	\$1,282	\$1,071	
	Individual	\$1,224	\$1,162	\$1,569	\$1,336	
	Group	555	473	\$584	\$543	
Outstanding Loan Structure	Business Loans	Service	-	29.3%	33.2%	23.9%
		Production	-	0.3%	1.6%	0.8%
		Trade	91%	31.2%	53.9%	55.6%
		Total	91%	60.8%	88.7%	80.4%
		Agribusiness Loan	6%	3.2%	9.9%	6.8%
	Home Improvement	3%	36.0%	1.4%	12.8%	
Loans Disbursed Since inception	Total \$	12,207,350	17,710,065	23,380,100	53,297,515	
	Total #	6,467	10,369	10,484	27,320	
	Female %	30%	10%	13%	15%	
	Individual \$	11,206,850	17,071,065	22,560,300	50,838,215	
	Individual #	4,981	9,393	9,297	23,671	
	Female %	21%	10%	12%	13%	
	Group \$	1,000,500	639,000	819,800	2,459,300	
	Group Members	1,486	976	1187	3,649	
	Group #	386	309	342	1,037	
	Female %	39%	10%	17%	24%	
Outstanding Growth % past 12 months	84%	24%	16%	30%		
No. of jobs Created	4,880	6,096	8,249	19,225		
Received fund as of 30th June 2012						
USAID/ Izdihar- Tijara (Loan Capital)	\$2,425,000	\$3,340,000	\$3,225,000	\$8,990,000		
USAID/ Izdihar -Tijara (Operation Capital)	-	-	-	-		
USAID/ Inma (Loan Capital)	-	-	-	-		
USAID/ Inma (Operation Capital)	-	-	-	-		
Total USAID	\$2,425,000	\$3,340,000	\$3,225,000	\$8,990,000		
Loan Capital Others	\$610,000	-	\$1,648,125	\$2,258,125		
Operation Capital Others	\$180,134	\$206,403	\$133,030	\$519,567		
Total Others	\$790,134	\$206,403	\$1,781,155	\$2,777,692		
Grand Total	\$3,215,134	\$3,546,403	\$5,006,155	\$11,767,692		
% USAID Contribution to Total	75%	94%	64%	76%		
Financial Ratios June 2012						
Operational Self Sufficiency (OSS)				85.6%		
Financial Self Sufficiency (FSS)				79.8%		
Operation Expense Ratio (OER)				19.9%		
Yield				19.6%		
MENA Benchmarks				MENA Small		
Operational Self Sufficiency (OSS)				114.1%		
Financial Self Sufficiency (FSS)				107.3%		
Operation Expense Ratio (OER)				19.1%		
Yield				40.7%		

Indicators		BFF	Al-Bashaer
Age		4 Y, 6 Mo	5 Y, 10 Mo
Start Date		December'07	August'06
HQ		Erbil	Baghdad
Operating Area		Erbil, Dahuk, Sulaymaniyah , Koisanjaq, Soran, Rania	Baghdad
No. of Offices		3 main offices and 3 satellite offices	13 offices and 2 satellite offices covering all Baghdad
Total # of staff		59	52
Total # of Loan Officer		20	27
Female LO		6	5
Case Load		214	198
Loan Portfolio as of 30th June 2012			
Loans Outstanding	Total Outstanding \$		7,675,300
	Total Outstanding #		5,345
	Female %		22%
	Individual \$		7,675,300
	Individual #		5,345
	Female %		22%
	Group \$		-
	Group Members		-
	Group #		-
PAR > 30 days		0.4%	2.4%
Average loan Size	Total Outstanding		\$1,436
	Individual		\$1,436
	Group		-
Outstanding Loan Structure	Business Loans	Service	17.7%
		Production	0.6%
		Trade	51.6%
		Total	69.8%
		Agribusiness Loan	0.0%
	Home Improvement	30.2%	
Loans Disbursed Since inception	Total \$		42,069,150
	Total #		21,105
	Female %		19%
	Individual \$		42,069,150
	Individual #		21,105
	Female %		19%
	Group \$		-
	Group Members		-
Group #		-	
Female %		-	
Outstanding Growth % past 12 months		12%	31%
No. of jobs created		532	20,961
Received fund as of 30th June 2012			
USAID/ Izdihar- Tijara (Loan Capital)			\$4,323,084
USAID/ Izdihar -Tijara (Operation Capital)			-
USAID/ Inma (Loan Capital)			-
USAID/ Inma (Operation Capital)			-
Total USAID			\$4,323,084
Loan Capital Others			\$2,275,934
Operation Capital Others			\$1,146,185
Total Others			\$3,422,119
Grand Total			\$7,745,203
% USAID Contribution to Total			56%
Financial Ratios June 2012			
Operational Self Sufficiency (OSS)		94.2%	228.3%
Financial Self Sufficiency (FSS)		85.9%	196.9%
Operation Expense Ratio (OER)		16.2%	9.4%
Yield		19.1%	30.1%
MENA Benchmarks		MENA Small	
Operational Self Sufficiency (OSS)		114.1%	
Financial Self Sufficiency (FSS)		107.3%	
Operation Expense Ratio (OER)		19.1%	
Yield		40.7%	

Indicators		AI-Mosaned	Total	
Age		3 Y, 7 Mo		
Start Date		November'08		
HQ		SalahAldin		
Operating Area		Tikrit, Al-Daur, Samarra, Baiji		
No. of Offices		1 main office and 3 satellite offices	109	
Total # of staff		25	1015	
Total # of Loan Officer		11	356	
Female LO		2	66	
Case Load		239	263	
Loan Portfolio as of 30th June 2012				
Loans Outstanding	Total Outstanding \$	2,637,395	143,932,639	
	Total Outstanding #	2,634	93,627	
	Female %	25%	21%	
	Individual \$	2,357,294	128,976,370	
	Individual #	2,142	70,550	
	Female %	19%	18%	
	Group \$	280,101	14,956,269	
	Group Members	492	23,077	
Group #	158	7,763		
Female %	54%	32%		
PAR > 30 days		2%	1.3%	
Average loan Size	Total Outstanding	\$1,001	\$1,537	
	Individual	\$1,101	\$1,828	
	Group	\$569	\$648	
Outstanding Loan Structure	Business Loans	Service	16.3%	26.9%
		Production	11.5%	3.0%
		Trade	51.9%	45.6%
		Total	79.7%	75.5%
	Agribusiness Loan	2.8%	4.3%	
Home Improvement	17.5%	19.6%		
Loans Disbursed Since inception	Total \$	14,002,520	959,304,723	
	Total #	7,279	403,765	
	Female %	23%	18%	
	Individual \$	13,669,920	895,546,748	
	Individual #	6,786	339,101	
	Female %	21%	17%	
	Group \$	332,600	63,757,975	
	Group Members	493	64,664	
Group #	158	21,261		
Female %	54%	27%		
Outstanding Growth % past 12 months		18%	20%	
No. of jobs Created		6,861	216,838	
Received fund as of 30th June 2012				
USAID/ Izdihar- Tijara (Loan Capital)		\$2,047,395	\$49,436,643	
USAID/ Izdihar -Tijara (Operation Capital)		\$46,805	\$9,188,235	
USAID/ Inma (Loan Capital)		-	\$4,988,658	
USAID/ Inma (Operation Capital)		-	\$351,996	
Total USAID		\$2,094,200	\$63,965,532	
Loan Capital Others		-	\$45,149,881	
Operation Capital Others		\$310,446	\$13,280,956	
Total Others		\$310,446	\$58,430,837	
Grand Total		\$2,404,646	\$122,396,369	
% USAID Contribution to Total		87%	52%	
Financial Ratios June 2012				
Operational Self Sufficiency (OSS)		232.7%	203.7%	
Financial Self Sufficiency (FSS)		199.9%	167.5%	
Operation Expense Ratio (OER)		9.5%	12.7%	
Yield		23.8%	26.5%	
MENA Benchmarks		MENA Small	Average	
Operational Self Sufficiency (OSS)		114.1%	108.2%	
Financial Self Sufficiency (FSS)		107.3%	104.8%	
Operation Expense Ratio (OER)		19.1%	17.9%	
Yield		40.7%	35.5%	

CODE OF CONDUCT AND ETHICS SIGNED BY IRAQI MICROFINANCE INDUSTRY REPRESENTATIVES



USAID | IRAQ
FROM THE AMERICAN PEOPLE



CODE OF ETHICS & CONDUCT FOR MICROFINANCE INSTITUTIONS (MFIs)

PREAMBLE

"Without firm commercial foundations, microfinance cannot become the profitable business that it needs to be in order to survive," said Elizabeth Littlefield, CGAP CEO. "But without firm ethical principles and a commitment to benefit poor people's lives first and foremost, it will no longer be microfinance"

Introduction

Microfinance is a powerful instrument against poverty. When poor people have access to financial services, they can earn more, build their assets, and cushion themselves against external shocks. Poor households use microfinance to move from everyday survival to planning for the future; they invest in better nutrition, housing, health, and education. Comprehensive impact studies have demonstrated that: (i) microfinance helps poor households meet basic needs and protect against risks; (ii) the use of financial services by low-income households is associated with improvements in household economic welfare and enterprise stability or growth; (iii) by supporting women's economic participation, microfinance helps to empower women, thus promoting gender-equity and improving household well-being; (iv) for almost all significant impacts, the magnitude of impact is positively related to the length of time that clients have been in the program

The microfinance sector in Iraq commenced operations in 2003 and since then has achieved remarkable outreach with the support of donors and the entrepreneurial spirit of the Iraqi people. As the sector continues to formalize and MFIs move towards transformation from NGOs to formalized non-banking institutions under the Central Bank of Iraq (CBI), it is imperative that MFIs are guided by a broadly established and recognized best practices code of ethics and conduct.

This document states core values for microfinance (Section A), a voluntary mutual code of conduct for microfinance institutions to abide by these values (Section B) and a process of compliance (Section C). All microfinance institutions, which receive funding and/or technical assistance from USAID-Tijara, unanimously and wholeheartedly agree to abide by the core values and the code of conduct as set out hereunder.

SECTION A - Core Values in Microfinance

A.1 INTEGRITY

Our mission is to service low-income clients—women and men—and micro, small and medium enterprises (MSMEs), providing them short term and/or long-term access to financial services, that are client focused, designed to enhance their well-being, and delivered in a manner that is ethical, dignified, transparent, equitable and cost effective.

A.2 QUALITY OF SERVICE

We believe that our clients deserve fair and efficient microfinance services. We will provide these services to them in as convenient, participatory and timely manner as possible. We'll treat our clients with respect and dignity, with no discrimination nor apartheid (Belief, Creed, Race, and Religion), empathizing with them most especially in times of crisis.

A.3 TRANSPARENCY

We shall give our clients complete and accurate information and educate them about the terms of financial services offered by us in a manner that is understandable by them.

A.4 RESPECT FOR RELIGION

We will respect the local religion of the communities in which we serve to ensure that our services to our clients do not hurt the sentiments of any community. We will work with communities through meaningful dialogues to ensure alignment, and as much as possible, seek cooperation with Religious Leaders.

A.5 FAIR PRACTICES

We are committed to ensure that our services to our clients are not unethical and deceptive. In providing microfinance services, we are committed to fair practices, which balance respect for clients' dignity and an understanding of a client's vulnerable situation, with reasonable pursuit of recovery of loans.

A.6 PRIVACY OF CLIENT INFORMATION

We will safeguard personal information of clients, only allowing disclosures and exchange of such information to others who are authorized to see it, with the knowledge and consent of clients.

A.7 INTEGRATING SOCIAL VALUES INTO OPERATIONS

We believe that high standards of governance, participation, management and reporting are critical to our mission to serve our clients and to uphold core social values of respect and community wealth creation.

A.8 FEEDBACK MECHANISM

We shall provide our clients formal and informal channels for their feedback and suggestions for building our competencies to serve our clients better.

SECTION B - Voluntary Mutual Code of Conduct

To ensure that all our activities and dealings with clients are in compliance with the above core values, we all agree to adopt the code of conduct as elaborated hereunder:

B.1 APPLICATION OF THE CODE:

"This code applies to all categories of member microfinance institutions - irrespective of their constitution (public, private etc.) - whose principal activity is microfinance and related services.
* This code comes into effect from August 8, 2010 unless otherwise indicated.

B.2 WE AGREE TO:

* Promote and strengthen the microfinance movement in the country by bringing sustainable microfinance services to the low-income people of Iraq.
* Build progressive, sustainable and client-centric microfinance institutions in the country to provide integrated financial services to our clients.
* Promote cooperation and coordination among microfinance institutions and other agencies to achieve higher operating standards and avoid unethical competition in order to serve our clients better.

B.2.1 INTEGRITY

We agree to:

* Act honestly, fairly and reasonably in conducting microfinance activities.
* Conduct our microfinance activities by means of fair competition, not seeking competitive advantages through illegal or unethical microfinance practices. No officer, employee, or other person acting on our behalf shall take unfair advantage of anyone by manipulation, concealment, abuse of privileged information, misrepresentation of material facts or any other unfair practice.
* Prominently display the core values and code of conduct on the notice board of head office and all branches, and put systems in place to ensure compliance.
* Ensure that our staff and any other person acting for us on our behalf, are trained or oriented to put these values into practice.

B.2.2 TRANSPARENCY

We agree to:

* Disclose to clients all the terms and conditions of our financial services offered in the language understood by the client.
* Disclose the source of funds, costs of funds and use of surpluses to Board Member and Donor to provide competitive services to clients.
* Provide information to clients on the rate of interest levied on the loan, method of deducting interest, terms of repayment, and any other information related to interest rates and other charges.
* Provide adequate information on alternative financing mechanism such as Islamic Finance as applicable and work towards making available such products for our clients.
* Provide periodical statements of our accounts to the clients.
* Work towards providing our annual audited financial statement to the Mix Market (www.themix.org).

B.2.3 FAIR PRACTICES

We are committed to follow fair practices built on dignity, respect, fair treatment, persuasion and courtesy to clients. We agree to:

* Provide micro finance services to low income clients irrespective of gender, race, caste, religion or language.
* Ensure that the services are provided using the most efficient methods possible to enable access to financial services by low income households at reasonable cost.
* Recognize our responsibility to provide financial services to clients based upon their needs and repayment capacity.
* Interact with the clients in an acceptable language and dignified manner and spare no efforts in fostering clients' confidence and long-term relationship.
* Maintain decency and decorum during the visit to the clients' place for collection of dues.
* Avoid inappropriate occasions such as bereavement in the family or such other calamitous occasions for making calls/visits to collect dues.
* Scrupulously avoid any demeanor that would suggest any kind of threat or violence.
* Emphasize using alternative collaterals which includes various forms of peer assurance such as lending through groups and group guarantees at the neighborhood level, or other forms of collateral.

B.2.4 GOVERNANCE

We agree to:

* Observe high standards of governance, ensuring fairness, integrity and transparency by inducing persons with good and sound reputation, as members of Board of Directors. We shall ensure that the majority of the directors are independent directors and/or duly elected representatives of the community we serve, and that we will involve the Board in all policy formulation and other important decisions.
* Ensure transparency in the maintenance of books of accounts and reporting/ presentation and disclosure of financial statements by qualified auditors.
* Put in our best efforts to follow the Audit and Assurance Standards issued by the Iraqi Audit Association.
* Place before the Board of Directors, a compliance report indicating the extent of compliance with this Voluntary Mutual Code of Conduct, specifically indicating any deviations and reasons therefore, at the end of every half financial year.

B.2.5 FEEDBACK/ GRIEVANCE MECHANISMS

We agree to:

* Establish effective and efficient feedback mechanism.
* Take steps to correct any errors and handle complaints speedily and efficiently.
* Provide, where a complainant is not satisfied with the outcome of the investigation into her complaint, he/she shall be notified of his/her right to refer the matter to the interim Compliance Committee facilitated by USAID-Tijara and in the future by the Iraqi Microfinance Network.

B.2.6 WORKING RELATION WITH DONORS/FUNDERS

We agree to:

* Build an environment based on mutual respect towards a common vision and goal.
* Attempt to harmonize our plans and operations with our funding agencies and loan fund providers framework, areas of priority, procedures and other relevant information.
* Ensure that the relations and transactions are transparent. Deception and misrepresentation will be avoided at all times, such as overstating client outreach and loan portfolios, double funding, diversion of grants and loans to unrelated activities.
* Maintain commitment to signed grants agreements conditions, and keep the mutually agreed upon the parameters of success of funded projects through evaluations that are participatory in nature.

B.2.7 WORKING RELATION WITH GOVERNMENT/CENTRAL BANK OF IRAQ

We agree to:

* Establish an environment of openness, mutual respect and engagement to improve and build inclusive financial sector in Iraq.
* Continued dialogue and communications with Government and CBI on policy reform recommendations for the conducive development of microfinance institutions and the sector.
* Commitment to comply with government laws and provide respective authorities with requested reports in an accurate and timely manner.

SECTION C - Compliance Mechanism

C.1 The 14 Iraqi Microfinance Network, in consultation with each other and facilitated by USAID-Tijara, will establish a Compliance Committee to oversee the implementation and compliance of the Code of Ethics and Conduct. The Committee will be represented by one nominated senior management personnel from each institution. In the long term, the MFIs, with support from USAID-Tijara, will establish the Iraqi Microfinance Industry Network, which will provide overall guidance and adherence to the Code and help in resolving any disputes.

C.2 The Board of the member microfinance institutions should adopt the ethics and the code of conduct on an annual basis.

C.3 In case of complaint received by the interim Compliance Committee (and in the future by the Iraqi Microfinance Network) regarding non-compliance with the code by any member microfinance institution, the committee shall take the following steps:

- * Assist in compliance.
- * Failing which:
 - I. Formally write to the chief executive of that member microfinance institution to respond to the complaint within 30 days.
 - II. If the chief executive of that member microfinance institution fails to respond within 30 days of the receipt of the communiqué, the matter will be formally communicated to the board of that microfinance institution in writing to seek a response.
 - III. If the board does not respond within the 15 days of the receipt of the communiqué, the membership of that microfinance institution shall be suspended till further decision of the committee.
 - IV. If the committee decides it is necessary to expel the microfinance institution from membership, it shall then take the appropriate decision and if they decide to expel the member, the name of the expelled member will be published on the imfi.org website.

USAID-Tijara Representative

Doral Cotter
Chief of Party

Mohammed Junaid
Team leader
Sustainable Microfinance

Baghdad- Iraq
August 8, 2010

Iraqi Microfinance Institution Members

Executive Manager
Al Aman

Executive Manager
Al Moesned

Director of Business and Operations
CHF International

General Manager
Al Thiqa

Branch Manager
Al Takadum Fallujah

Chief Executive Officer
Al Bashaer Iraqi Organization for Microfinance

Executive Manager
Al Tadhamun

Branch Manager
Al Takadum Al Qaim

Executive Manager
Tala'far Economic Development Center (TEDC)

Chief of Party
Relief International

Branch Manager
Al Takadum Ramadi

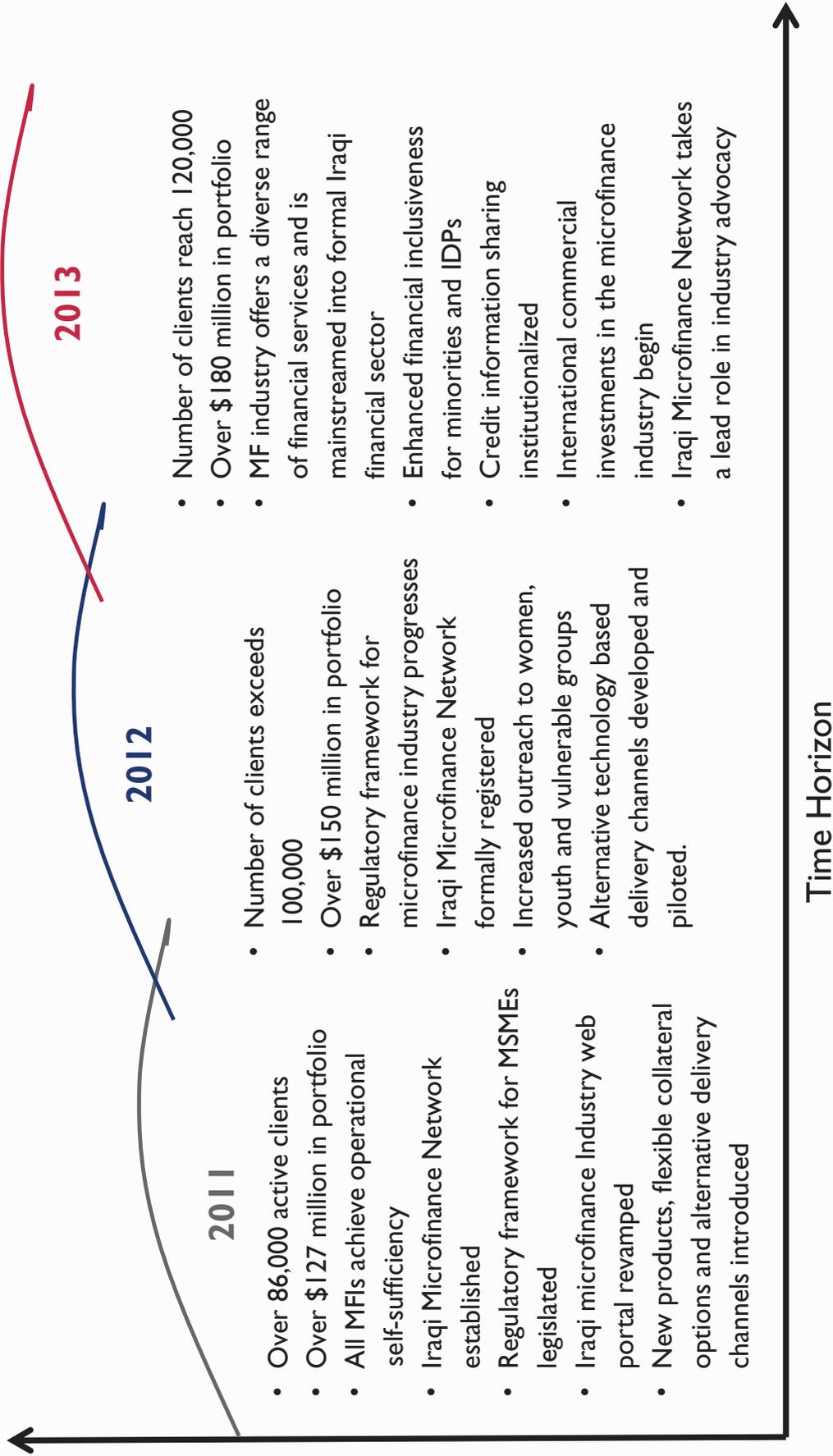
Executive Manager
Izziharona

General Manager
Bright Futures Foundation (BFF)

Senior Manager
Amalkom



Iraqi Microfinance Industry – Looking Forward



IRAQ'S MICROFINANCE NETWORK INSTITUTIONS



IRAQ FACES THE FUTURE



