PD-ABP-036

97264

PROPOSED DESIGN

MICROENTERPRISE FINANCE ACTIVITY

FOR THE WEST BANK AND GAZA

FINAL REPORT

Submitted to USAID/West Bank and Gaza
By Management Systems International,

Stephen C. Silcox
Karl F. Jensen

CONTRACT NUMBER:
HNE-0159-C-00-3080-00

February 28, 1997

MANAGEMENT
SYSTEMS
INTERNATIONAL

600 Water Street, S.W.
Washington, D.C. 20024
USA

202/484-7170
Fax: 202/488-0754

TABLE OF CONTENTS

ANNEXES

SYNOPSIS OF ACTIVITY

The proposed budget provides a minimum of $3 million over a three year period. Of that total, $2.3 million would be spent on technical assistance and training, including long and short-term TA, training sessions for bank staff, workshops and conferences, study tours, research and evaluation, and MIS installation. The remaining $700,000 would be used to provide risk sharing capital to leverage capital from the participating bank(s) over the three year period. This is the minimum amount necessary to implement the activity and assumes that banks will participate in the activity without further financial incentives.

It is important to point out that very few banks worldwide have entered the microenterprise finance market without some financial incentives in addition to loan guarantee funds and technical assistance. Although the banks being considered as partners with USAID in this activity have an excess of liquidity, that factor alone has not provided sufficient incentive for banks in other parts of the world to engage in a microfinance activity. Likewise, the provision of technical assistance and training by USAID may not provide sufficient incentive for the banks to engage in a microfinance activity. Although it is hoped that these factors, coupled with a loan default guarantee fund, will be sufficient to entice one or two banks in the West Bank and Gaza to establish and implement a successful microfinance program, USAID should be prepared to offer further financial incentives to the banks if the banks show a reluctance to participate in the program.

The eventual final total budgeted for this activity will depend upon the negotiations to be undertaken in the next few weeks between USAID officials and the three potential banks which have indicated an interest in participating in the program.

The activity will establish microfinance programs in one or two existing commercial banks in the West Bank and Gaza and will concentrate on non-collateralized lending to established microenterprises of five or less employees with most initial loans starting between $1,000 and $2,000. The maximum loan will be for $10,000 and the average loan size after one to two years of program operation will range between $2,000 and $5,000. Most loans will be repaid in six months or less with a maximum loan period of 12 months. Almost all loans will be for working capital with loans for fixed assets being made only after the client has satisfactorily repaid at least four working capital loans. Saving services will also be offered to microenterprises. Special attention will be given to serving the needs of women entrepreneurs and at least 40% of the loans will be made to women entrepreneurs.

The **purpose** of the microfinance activity using commercial banks as lenders is:

> To increase access to credit for microenterprises, with special attention to women clients, and to develop long-term, sustainable sources of financial services for microenterprises through the formal financial system of the West Bank and Gaza

The **objectives** of this activity are:

1. To leverage USAID financial inputs with substantial capital from the participating banks to reach much greater numbers of microenterprises that could not be reached through NGO financed programs without significant infusions of donor loan capital.

2. To enhance the potential for rapid scale up of microloan numbers and amounts that will assist the banks to achieve early profitability in their microfinance programs.

3. To achieve a system of microfinance through the commercial bank sector which would have greater prospects for long-term, financial and institutional sustainability than the provision of microcredit through traditional NGO modes.

4. To provide microentrepreneurs with access to a wider range of banking services and to develop a long-term relationship between the banks and microentrepreneurs.

The Activity will have two components:

A Risk-Sharing Component to both share the risk of loan defaults between USAID and the participating banks and to leverage bank capital for microfinance. USAID will also provide financial support to participating banks for start-up costs to establish a microfinance program in each bank.

A Technical Assistance and Training Component which will provide both long-term and short-term technical assistance to the participating banks to

- advise them on the establishment and implementation of a microfinance program
- to provide training and study tours in best practices in microfinance
- to install a management information system for tracking loan portfolio performance and financial sustainability of the program and to train MIS operators
- to conduct research such as baseline studies for program impact and subsector analyses
- to perform a mid-term and end of activity evaluation

It is estimated, assuming minimum funding levels, that the bank(s) participating in the Activity could reach program profitability by the end of the first year of implementation and could have an active portfolio between 2,000 and 16,000 loans outstanding by the end of year three of the Activity, depending upon portfolio performance and loan capital extended by the bank(s).

<u>This Activity is dependent upon USAID reaching agreement with at least one existing commercial bank in the West Bank and Gaza to implement a microfinance program in substantial conformity with the above description of the Activity.</u>

BACKGROUND

The USAID/West Bank and Gaza Strategy (1996-2000) outlines a two-track approach for future USAID initiatives to increase access to financial services for the Palestinian private sector. This approach consists of:

1) Support grants to existing NGO microcredit projects in order to expand the volume of credit available to small borrowers in the near-term; and

2) Technical assistance and training to facilitate the development of microcredit programs run by commercial banks in order to develop a more sustainable and broad-based model for microcredit delivery in the longer term.

In September, 1996, USAID concluded grant agreements with Save the Children and UNRWA to enhance their capacity to deliver microenterprise loans in the West Bank and Gaza. Funds provided under these agreements are expected to result in 8,500 individual loans to Palestinians, over an eighteen month period and reach a level of 2,800 active loans (size of loan portfolio).

Also in 1996, USAID organized and financed a series of seminars and workshops to expose Palestinian bankers to microcredit practices and technology employed in other parts of the world, with an emphasis on successful programs developed with USAID assistance in Egypt. A select group of Palestinians were invited to attend a one-week training session on the operations and management of a microlending program at the Alexandria Business Association.

Subsequently, a USAID Program Management Specialist conducted meetings with representatives of several commercial banks to assess their interest in a potential USAID-financed program to introduce microlending operations at selected bank branches in the Palestinian territories. These discussions resulted in narrowing the number of potential banks to implement a microlending program to five.

This report is the result of a consultancy to assist the USAID/West Bank/Gaza Mission to design an activity to support the second track of microlending through commercial banks. It presents the conceptual design and details on how one or two banks would be selected to implement a microlending program in the West Bank and Gaza.

This report was written by Stephen C. Silcox & Karl F. Jensen, consultants for Management Systems International, Inc. in Washington, D.C. It was based on discussions held with selected bank officials, NGO staff operating microlending programs financed by USAID, other private sector representatives and USAID staff in late January and early February 1997. This design builds upon the Microfinance Sector Assessment performed for USAID by Silcox, Jensen and Olaf E. Kula for USAID in January and February 1996. Readers of this report desiring further information on the origins of this activity design should consult that assessment. The next section of this report summarizes and updates some aspects of that report.

NEED FOR MICROFINANCE IN THE WEST BANK & GAZA

Banks provide two important services to the community; savings services and loan provision. While the banks in the WB/G do provide both services, the balance is severely skewed. Total deposits as of September 1995 exceeded one billion US dollars, and loans were approximately $220 million.

There has been an apparent "mopping up" of savings from both residents and deposits from Palestinians overseas, but there has yet to be extension of lending within the area now controlled by the Palestinian Authority. Up until this point in time, no firm decisions have been made by the Palestinian Monetary Authority (PMA) on local reinvestment of deposits; generally funds held by Jordanian-owned banks are reinvested in government securities in Jordan or held to cover transactions with Israeli entities through Israeli correspondent banks.

There is currently a broad range of bank branches providing services in WB/G. However, there are precious few examples of banks lending to small and microenterprises.

Lending practices are conservative, with most loans being for overdraft facilities (72.09%). The remaining breakdown of loans includes term loans of 1-3 years (12.37%), other loans (12.43%) and discounted bills (3.11%) [Percentages from MAS Statistical Review with figures as of September 1995]. On the surface, lending is based on liquid collateral (cash), but underpinned by "name" lending, i. e., lending to members of families that are well known and respected in the area. Wealthier families with businesses recognized within the banking community have far greater access to banking services than poorer, less well known clients.

There is a clear need for the provision of working capital loans to microenterprises, mostly to purchase materials for processing or resale. These are currently not available from sources other than savings, family or informal moneylenders.

There are reasons to be hopeful that the banking system can be utilized in the future provision of credit to small and microenterprises. The relatively large number of banks and bank branches necessarily creates a competitive environment. Nearly all of the banking institutions interviewed indicated future plans for doing corporate lending, but there is a very limited market for this type of lending. However, at present, banking services for people with limited financial resources are largely confined to deposit taking. The strongest argument for pursuing bank-led intervention for microfinance is that banks have the infrastructure for handling cash, as well as providing aligned services, such as savings. <u>The major drawback at this point is that most bank officials have little, if any, familiarity with successful microfinance programs; consequently, as experience in other countries has shown, bank representatives will require considerable experience with or exposure to such programs to even consider such type of lending. This will require both on-going, daily technical assistance in the establishment and implementation of microfinance programs as well as visits to successful microfinance programs through banks elsewhere.</u>

A limited number of NGOs have recently launched programs that issue relatively small loans (initial loans in the US$ 200-300 range) for short terms (4-6 months) using internationally accepted microenterprise lending methodologies. These programs have been particularly successful at reaching women. USAID provided grants in 1996 to the two largest of these programs under Track 1 of USAID's microfinance initiative to assist them to expand their operations. (Save the Children received $1 million and UNRWA received $500,000.)

Estimates indicate that there are currently about two million residents in WB/G. Of that population, one half (those over 16 years of age) are assumed to be employable. About 35% of the total employable population is unemployed, but 25-30% of the employed population is reported as self-employed. Using this category of persons as a proxy for possible microentrepreneurs, the total microentrepreneurs in the WB/G would be conservatively estimated to number at least 150,000. Approximately 90% of existing private businesses in the WB/G have less than ten employees and at least 80% of existing businesses have less than 5 employees.

There is no data available at this time to calculate the upper bound for loan demand in the WB/G. Such information could be obtained using a baseline survey methodology or conducting a microenterprise survey using a variety of sampling techniques. Nevertheless, there is substantial evidence that the demand for microenterprise loans already greatly exceeds the level needed to reach sufficient scale for an microenterprise lending program to be sustainable. Both SCF and UNRWA have done initial assessments of potential demand for their women's solidarity group lending schemes for both the West Bank and Gaza. In Gaza alone, there are an estimated three thousand women operating retail activities with a fixed place of business in existing markets. According to UNRWA staff, the number of women in the WB/G who operate home-based businesses is higher than the number of those with market stalls. UNRWA staff estimate the demand among women microentrepreneurs in Gaza at a minimum of 5,000 borrowers.

Another conservative estimate of demand is to assume that at least 20% of the microenterprises in the WB/G would both be interested in and qualify for a microenterprise loan. This approach safely yields 30,000 potential borrowers. Given that there are slightly over three thousand outstanding microenterprise loans in all of the WB/G today, it is reasonable to assume that there is a considerable "credit gap" at interest rates sufficient to cover the costs of microenterprise lending.

PURPOSE AND OBJECTIVES OF THE MICROFINANCE ACTIVITY

The **purpose** of the microfinance activity using commercial banks as lenders is:

> To increase access to credit for microenterprises, with special attention to women clients, and to develop long-term, sustainable sources of financial services for microenterprises through the formal financial system of the West Bank and Gaza.

The **objectives** of this activity are:

1. To leverage USAID financial inputs with substantial capital from the participating banks to reach much greater numbers of microenterprises than can be reached through NGO-financed programs without significant additional infusions of donor loan capital.

2. To enhance the potential for rapid scale up of microloan numbers and amounts that will assist the banks to achieve early profitability in their microfinance programs.

3. To achieve a system of microfinance through the commercial banking sector which would have greater prospects for long-term, financial and institutional sustainability than the provision of microcredit through traditional NGO modes.

4. To provide microentrepreneurs with access to a wider range of banking services and to develop a long-term relationship between the banks and microentrepreneurs.

The system for monitoring the achievement of this purpose and objectives and suggested indicators are found in a later section of this report.

DESCRIPTION OF THE ACTIVITY

A. Clientele to be Served

The clientele served (or "target group") for the microfinance activity through commercial banks will have the following characteristics:

1. All microenterprises in the WB/G will be eligible to participate in this microenterprise lending program. Microenterprises will be defined as enterprises with ten or fewer employees.

2. Priority will be given to microenterprises with 5 or fewer employees.

3. Program design and implementation will ensure women's access to financial services.

4. Only established microenterprises which have been operating for more than six months will be eligible for microloans.

B. Financial Products to be Offered

The loan and savings products offered by the banks to eligible microenterprises will include the following:

1. Short-term, working capital loans of twelve months or less will be the principal loan product offered. At least 75% of the bank's loan portfolio for the first year will consist of loans of less than $2,000 for terms averaging six months or less.

2. Borrowers will be able to access medium-term investment capital (e.g., equipment loans with repayment periods of more than 12 months) only after satisfactorily repaying at least four working capital loans. (However, USAID may desire to limit its risk-sharing participation only to those loans for working capital.)

3. Loan clients will be encouraged, but not required, to establish savings accounts at the banks offering microcredit.

4. Loan and savings products will be developed which specifically address the needs and modalities of women-run microenterprises.

5. Banks will be encouraged to offer other financial services to microentrepreneurs as the banks acquire greater familiarity with the financial needs of microenterprises.

C. Lending Methodology to be Employed

The lending methodology to be employed by the banks will include the following key elements:

1. Loans will be made to individuals.

2. Lending will be based primarily on the character and experience of the individual rather than traditional forms of collateral. Alternative and informal types of collateral, such as peer guarantees and village leader co-signers, should be encouraged. The lending program will emphasize access to future working capital credit as the incentive for prompt repayment of existing loans, rather than the loss of collateral.

3. Interest rates on loans will be set high enough to cover all operational costs of the microfinance program, including the cost of funds lent, and provide for a reasonable profit.

4. Loan amounts will be incrementally increased for repeat borrowers. For example, a borrower who had repaid an initial loan of $1,000 for 3 months might receive a second loan of $1,500 for 3 months or $2,000 for 4 months.

5. All loans should be approved or rejected within as short a period of time as possible. Repeat loans should be approved or rejected within a shorter period of time than the original loans.

6. Loan officers will contact the microentrepreneurs at their place of business to offer the bank's financial products to them. Follow-up and monitoring on loans (including collections) will also be conducted at the microentrepreneur's site of business by the same loan officers responsible for the loan appraisal.

7. Financial products will be standardized as much as possible to reduce loan portfolio management costs.

IMPLEMENTATION PLAN

A. Institutional Delivery Structure

The institutional delivery structure for this is relatively simple and straightforward. It is graphically illustrated in the organizational chart on the next page, along with the technical assistance and training to be provided by USAID. The bank or banks selected from the three finalists for this activity will create an autonomous unit within their banks which will consist of field loan officers and one supervisory loan officer. All staff for the MFA would initially be on a term contract basis with the participating banks. The microfinance program shall function as a separate division of the bank for the first year or two of the program. At some future time, the bank might decide to make the MFA staff permanent employees of the bank and might also decide to integrate the microfinance program into regular bank operations.

Each of the banks implementing this Activity will need to have a sufficient number of branches through which their microfinance program can be executed. The banks carrying out this program will need to make some operational changes in order to effectively extend and recover microenterprise loans, but the following describes, in general, some of the main operational aspects of the program.

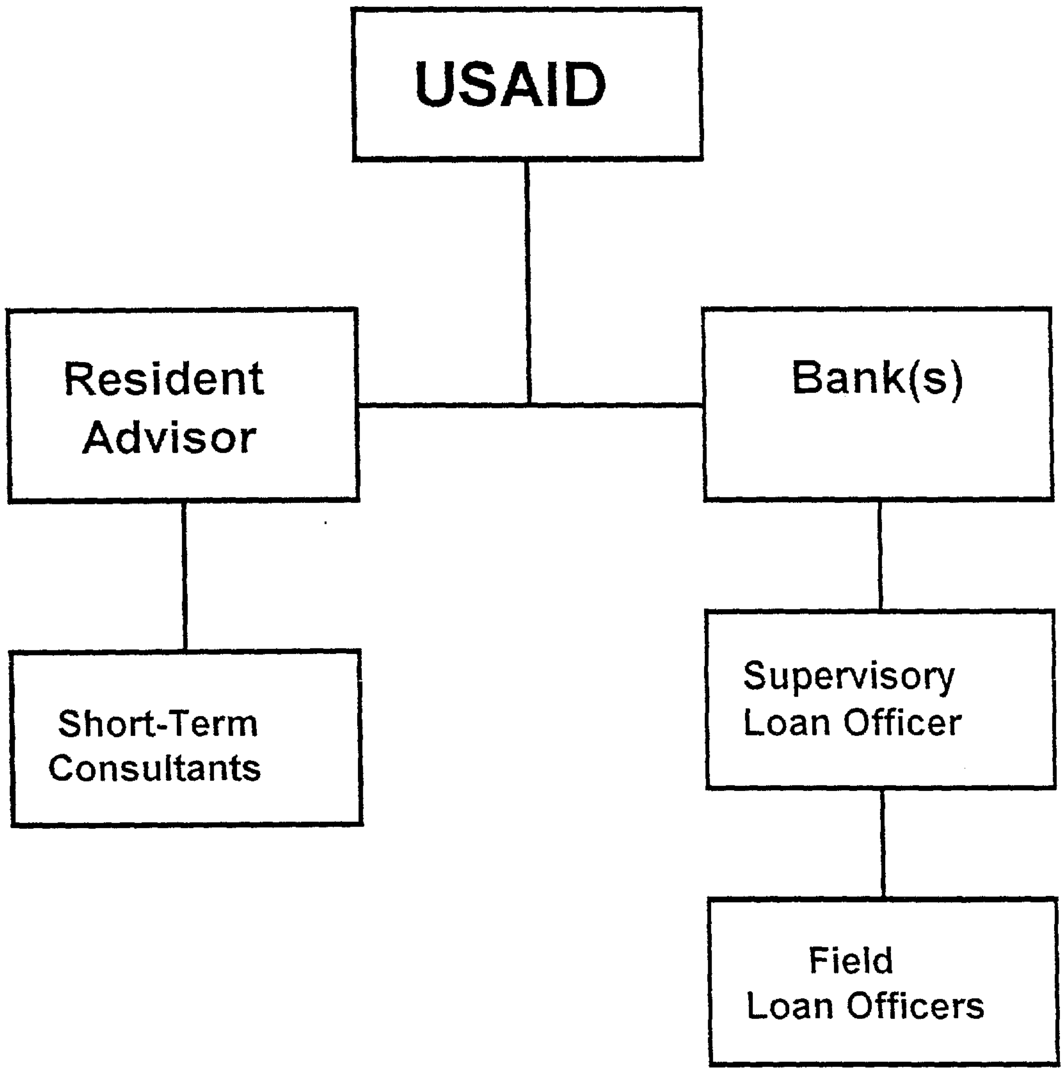
One of the keys to a successful microfinance program within a bank is the ability to identify clearly the costs and returns of that program. The formation of an autonomous unit within the bank can greatly assist in accomplishing this objective. An autonomous unit solely responsible for the performance of the microfinance activity can clearly identify the various costs of conducting the microfinance activity as well as the revenues and profits generated by the unit.

In addition, since microenterprise lending utilizes a new methodology than standard bank lending, operating this activity as through an autonomous unit can facilitate experimentation with new approaches and methodologies. The Supervisory Loan Officers and Field Loan Officers need to be actively involved with microenterprise borrowers. Although loan repayments will probably be made at the banks, most of the rest of the activities relative to program promotion, loan applications, loan appraisal, loan monitoring and follow-up will take place at the microentrepreneur client's place of business. This not only makes follow-up easier, it also allows for the loan officers to view other business activities in the area that might qualify for a loan. Successful microfinance programs involve having the loan officer transact most business and follow-up in or near the borrower's place of business. The loan officer's time spent within the bank office should be minimized in order to maximize his/her time spent with current and potential clients.

The Supervisory Loan Officer (SLO) will be the principal point of contact for the operation of the program in each participating branch. The SLO, while essentially operating as head of the autonomous microfinance unit, will be integrated into the participating bank's management structure. It is assumed that the SLO would report to not only the respective branch manager,

ORGANIZATIONAL CHART

MICROFINANCE ACTIVITY



but to senior management of the bank itself. His/her responsibilities will be to regularly report on the progress and growth of the activity, and to gain support of upper management for the microfinance activity. The supervisory officer will need to be well-informed on bank policies and directions, but is expected to play a major role in developing and maintaining the bank's focus on the importance of the microfinance activity. He/she will require previous experience working within a bank as well as excellent communications skills in both Arabic and English.

The participating banks will be required to identify and hire new loan officers on contract that are willing to spend the bulk of their respective workday in the community developing and supervising loans, rather than sitting behind a desk at the branch bank.

Many, but not all, successful microfinance programs use some type of monetary incentive system to encourage performance by loan officers and staff both in terms of the numbers of active clients serviced by the loan officers and in terms of loan portfolio quality, i.e., borrowers repaying loans on time. It is recommended that an incentive system be developed over the course of this activity, but not be made a precondition for bank participation in the activity. During the course of this consultancy, the potential for incentive compensation systems were discussed with bank staff and other relevant parties. Some bank staff expressed clear resistance to such a system, citing difficulties with using such a system within their general employee policies. However, if the microfinance portfolio performance performs as expected, the Resident Advisor might be able to convince the participating banks to experiment with an employee performance incentive system during the course of the activity. The Resident Advisor should encourage the banks to focus on how to improve the productivity and lower the per loan costs of the loan officers during the development of the microfinance program. This approach could aid in convincing the banks to experiment with incentive compensation systems.

The participating banks will develop policies and procedures to rapidly develop, review, and issue loans to eligible microenterprises. It is expected that the system developed will resemble the following delivery and recovery structure.

✓ Loan officers, the bulk of whose time is spent in the communities to be served, will identify potential borrowers through personal contact, and later, through references from existing borrowers.

✓ Standard loan applications will be straightforward and not require collateral, will be completed through direct interaction between the loan officer and the potential client. This will particularly facilitate loan applications from potential clients who are illiterate.

✓ Unless the bank has compelling reasons to disapprove the loan application, the loan will be approved, generally within two weeks of when the application is initially received. That application, when approved, will result in a simple and understandable loan agreement, an amortization schedule (with specific repayment dates that fit the business cycle of the borrower), and will initially be for a total period of no more than 2-6 months, with multiple payments within the period. The loan will be extended in cash, in the currency most suitable for the borrower, with repayments scheduled and occurring in the same currency. Discussions with an attorney in Ramallah indicated that the use of post-dated checks, similar to the procedures used by successful microfinance programs in Egypt, may be utilized as a technique to assure repayments.

✓ The bank issuing the loan will closely monitor the performance of the loan, with particular respect to timely repayment. This ability will be enhanced through the installation and use of an efficient management information system designed specifically for microenterprise finance. If payments are not made precisely on the day agreed to in the loan agreement with the borrower, immediate steps will be taken to help ensure that the loan amortization will either immediately be made by the borrower, or sanctions will be brought against the borrower. Loan officers will regularly visit borrowers with current and outstanding loans to not only review the state of the business, but to provide friendly and firm reminders of the repayment schedule agreed upon within the loan agreement.

✓ It is assumed that, based on experience to date in microenterprise lending in the West Bank and Gaza by the NGOs supported by USAID, most borrowers will pay on time and in full. It will be made explicit to the borrowers from the outset of their first loan application that any borrower who repays on time and in full will immediately be eligible for a subsequent or "repeat" loan. The bank issuing the initial loan must be prepared to immediately reissue a repeat loan, in most cases for a slightly larger amount, to any borrower that has met all the terms and conditions of the current, fully amortized loan.

✓ The bank may provide a basic orientation course to prospective and initial borrowers on how the credit program works and with details on specific aspects of the loans. This training will be directly related to the credit program. No other training or technical assistance for microentrepreneur clients is anticipated for the success of the microfinance activity.

B. Technical Assistance & Training

Technical assistance and training will be provided to bank staff as a critical component of the activity. As mentioned in section two of this report, the banks in the West Bank and Gaza have no direct experience in microfinance and will require both financial incentives as well as long-term, specialized technical assistance to agree to develop a microfinance program within their banks. A Resident Advisor will provide participating banks with broad-ranging advice on the establishment and implementation of microfinance programs within their banks and will be supplemented by selected short-term advisors as required.

The Resident Advisor will be provided office space at the headquarters of the participating bank or banks under this activity. His/her day-to-day interactions will be primarily with the Supervisory Loan Officer at each participating bank. The Resident Advisor will also have ready access to senior bank management, as required. He/she will be responsible for not only providing technical advice to the SLO and bank management, but assisting in the long term planning of loan extension and savings services, as well as identifying further training needs for the staff. By the end of contract with the Resident Advisor, all skills will have been transferred to the SLO.

A full description of the advisory services to be provided by the Resident Advisor and qualifications is found in the Statement of Work for the Resident Advisor in Annex 4. Other technical assistance will be coordinated by the Resident Advisor and will include at least 640 person/days of short term services in the fields of policy, sub-sector analysis, gender-related issues, marketing, training, investment, and bank-related development issues.

A Management Information System (MIS) software system developed with USAID financing in Egypt appears to be the most responsive to the needs of banks in West Bank/Gaza. The firm that developed the system, Environmental Quality International, has indicated a willingness to both install the system in at least three sites in WB/G, and provide training to local operators to ensure system quality and responsiveness. Specific adaptations to the environment in the West Bank and Gaza may be required.

Training of loan officers and key staff will be coordinated by the Resident Advisor. Periodic formal training sessions, with assistance by specialist short-term trainers, will be scheduled and funds are allocated for this activity. Periodic and formal training programs are not only useful for loan officers and staff, but are generally viewed as an incentive for performance.

In addition, funds have been allocated for taking selected bank management staff on study tours to inspect successful microfinance operations utilizing a banking model in other countries. Sufficient funds have been budgeted for travel of at least six senior level bankers (if two banks are selected to participate in the program), accompanied by the Resident Advisor, to view successful microfinance operations of banks in both Bolivia and Indonesia. It is recommended that USAID budget independently for key USAID officers to accompany the senior bank management staff on these study tours.

C. Optional Contract Mechanisms for Obtaining Technical Assistance and Training

USAID/West Bank/Gaza has two principal options for contracting for the technical assistance and training required for this Activity. Except for the installation of the USAID/Egypt financed MIS system which was developed for microfinance institutions in Egypt and which could be purchased on a sole source basis for installation in participating banks in the West Bank and Gaza , the two options are as follows:

1. An institutional contractor would be selected through full and open competition which would provide the services of the Resident Advisor as well as short-term technical

assistance and training. This option has the advantage of having one single contractor responsible for the coordination and provision of all TA and training for the Activity. Proposals in responses to a RFP could also suggest innovative approaches toward the implementation of the Activity. The principal disadvantage is the length of time which would be required to issue the RFP, make the selection and field the Resident Advisor.

2. A Personal Services Contractor could be selected to fill the position of the Resident Advisor and buy-ins to centrally funded microenterprise development contractors, such as those administered by the Office of Microenterprise Development in the Global Bureau, could be used for short-term TA and training. This option might result in lower costs, but could be more management intensive for USAID and hamper the ability of the Resident Advisor to coordinate all activities effectively. On the other hand, it would allow USAID/West Bank/Gaza to access specialized resources developed for the express purpose of disseminating lessons learned in the microenterprise development field.

While the Activity Design Team recommends that Option 1 be selected, both options are valid approaches to the acquisition of TA and training for the Microfinance Activity.

D. Activity Implementation Schedule

An Activity Implementation Schedule is presented on the next page. It provides an overview of the key activities to be undertaken in the establishment and implementation of a microfinance program within one or two participating banks. Any RFP issued for technical assistance to implement the Microfinance Activity should encourage the proposals to expand this implementation schedule and illustrate how the potential contractor would provide innovative mechanisms to implement the Activity.

WEST BANK/GAZA MICROFINANCE ACTIVITY IMPLEMENTATION SCHEDULE

(3 Years)

ACTIVITY	Qtr 1	Qtr2	Qtr 3	Qtr 4	Qtr 5	Qtr 6	Qtr 7	Qtr 8	Qtr 9	Qtr 10	Qtr 11	Qtr 12
1 Negotiation & Final Selection of Bank(s)	XXX											
2 Finalize Microfinance Activity Design & Funding	XXX											
3 Issue RFP for Institutional Contractor	XXX											
4 Evaluate and Select Contractor		XXX										
5 Field Resident Advisor			XXX									
6 Select First Bank Branches			XXX									
7 Short Term Specialist Services			XXX		XXX		XXX		XXX		XXX	
8 Establish Program Start-up Details			XXX									
9 Hire and Train Local Bank Staff			XXX			XX		XX		XX		
10 Initial MIS Installation			XXX									
11 Loan Extention				XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX
12 Receive MIS Reports				X	X	XXX	XXX	XXX	XXX	XXX	XXX	XXX
13 Project Evaluation								XXX				XXX
14 Modify MIS as Necessary					XXX				XXX			
15 Identify Additional Branches					XXX			XXX		XXX		

FINANCIAL PLAN

A. Description of Key Financial Components and Explanatory Notes

The proposed budget provides a minimum of $3 million over a three year period. Of that total, $2.3 million would be spent on technical assistance and training, including long and short-term TA, training sessions for bank staff, workshops and conferences, study tours, research and evaluation, and MIS installation. The remaining $700,000 would be used to provide risk sharing capital to leverage capital from the participating bank(s) over the three year period. This is the minimum amount necessary to implement the activity and assumes that banks will participate in the activity without further financial incentives.

It is important to point out that very few banks worldwide have entered the microenterprise finance market without some financial incentives in addition to loan guarantee funds and technical assistance. Although the banks being considered as partners with USAID in this activity have an excess of liquidity, that factor alone has not provided sufficient incentive for banks in other parts of the world to engage in a microfinance activity. Likewise, the provision of technical assistance and training by USAID may not provide sufficient incentive for the banks to engage in microfinance activity. Although it is hoped that these factors, coupled with a loan default guarantee fund, will be sufficient to entice one or two banks in the West Bank and Gaza to establish and implement a successful microfinance program, USAID should be prepared to offer further financial incentives to the banks (such as those discussed in Option 2 below) if the banks show a reluctance to participate in the program.

The eventual final total budgeted for this activity will depend upon the negotiations to be undertaken in the next few weeks between USAID officials and the three potential banks which have indicated an interest in participating in the program.

Key Assumptions:

1. Bank Program Start-up Operational Support: Scenario I shows USAID support for operations in one branch (or bank) for the first year; Scenario II shows USAID support for operations in two branches (or two banks) for the first year. Alternatively, USAID may decide to fund only a portion of the start-up costs for the programs, but continue that support for the three years of the project on a declining basis.

2. Loan Uptake Projections: These two scenarios assume that all loan capital will be provided by the participating banks with some type of risk-sharing by USAID in guaranteeing funds to the banks for loan defaults. Scenario One assumes a total of $4.4 million in loan capital during the three years of the activity. This scenario would result in a loan portfolio of active loans totaling 1,750 at the end of the three years. Scenario Two assumes a total of $40 million in loan capital during the three years of the activity. This scenario would result in a loan portfolio of active loans totalling 16,000 at the end of three

years. As these scenarios demonstrate, the total number of active loans at the end of the activity will be directly related to the amount of capital the bank is willing to contribute to the program.

3. Loan Uptake Projections: Default, set at .75% per annum, is accounted for in the profit and loss column. It is impossible to predict actual default in advance, but this figure is generated from the NGO experience in WB/G to date (0%), and from other experience in mature programs in Egypt..

4. Loan Uptake Projections: Profit and Loss is simply a mathematical calculation, based on costs, defaults, and return on interest. No base cost of capital is utilized, but rather a mark-up on whatever the cost of capital is by the bank issuing the loans.

Explanatory Notes

1. Although this budget includes the cost of shipment of household effects and a vehicle for the Resident Advisor, the current bilateral agreement between USAID and the Government of Israel does not provide for these shipments. However, upon the advice of the Mission Controller, these have been retained in the budget in case the bilateral agreement with Israel is changed to permit these shipments.

2. Short-term Technical Assistance has been roughly estimated, but actual timing and detailed description of the short term TA will have to be determined by the Resident Advisor in conjunction with the Mission.

3. Salary and support of loan officers to initiate the program is based on estimates from a former banking employee working for USAID. It is assumed that USAID will provide operational support for a percentage of salaries, transport costs, purchase of cellular telephones, and office space for the first year or two of implementation.

4. It is assumed that further exposure of key management staff in the participating banks to successful banking models for microenterprise finance will be beneficial. Funds have been allocated, for study tours to Banco Sol in La Paz, Bolivia (including a side trip to meet with key staff in the Office of Microenterprise Development in Washington, DC, and to Bank Rakyat Indonesia (BRI) in Indonesia.

5. Installation of a good management information system is a key to success of the Activity. A proven model has been developed in Egypt (with AID funding) and could be installed in the participating banks in West Bank/Gaza. That cost for this component is based on a quote from the firm that developed and implemented the system in Egypt and includes training of at least six operators.

6. A special Research and Evaluation line item has been budgeted in order to provide funds for both foreseen and unforeseen research that could be beneficial to the success of the

Activity or assist in promoting its successes. Potential sub-sector analysis and baseline data surveys are described in section nine of this report. The budget also provides for a mid-term and final evaluation of the Activity.

7. The budget includes funds for regular meetings and workshops by and for the NGOs providing microfinance with grants from USAID and for the banks participating in the Microfinance Activity.

B. Budget for Technical Assistance and Training

TECHNICAL ASSISTANCE COMPONENT

MicroFinance Finance Project
West Bank and Gaza

Cost Estimate

SUMMARY

I. US Source - Long Term	$513,804
II. US Source - Short Term	$340,000
III. Initial Bank Support	$348,320
IV. MIS Development/Installation	$50,000
V. Research/Evaluation	$300,000
VI. Training/Conferences	$100,000
VII. Overseas Visitations (7 Persons)	$76,000
Sub-Total	$1,728,124
Overhead at 70% of I & II	$597,663
Total TA and Support	$2,325,786

International Travel Cost Estimate

MicroEnterprise Finance Project
West Bank & Gaza

Destination	Airfare	No. of Days	Number of People	Per Diem	Total Per Diem	Total Cost
La Paz	4,700	5	7	110	3,850	36,750
Washington, DC		5	7	166	5,810	5,810
Jakarta	3,500	5	7	195	6,825	31,325
Training Fees	300		7			2,100
			Estimated SubTotal			$75,985

Assumption:
Travel to La Paz and Washington would be on same trip

TECHNICAL ASSISTANCE COMPONENT (Long Term)

MicroEnterprise Finance Project

West Bank/Gaza **Cost Estimate**

U.S. Source	Long Term			
I.				
	A. Resident Advisor	$	# of Mon.	Total
	1. Salary (Monthly)	7,200	36	259,200
	2. Post Differential	720	36	25,920
	3. DBA Insurance	340	36	12,234
	4. Medivac Insurance	17	36	600
	5. Temporary Qrts. Allowance	10,000	1	10,000
	6. Living Qrts. Allowance	2,050	35	71,750
	7. Education Allowance (2XAnnual)	24,700		74,100
	8. Air Fare			
	8.a. 2 RT for Team Leader (Annual)	6,000		18,000
	8.b. 1 RT, 3 Family Members (Annual	9,000		27,000
	9. HHE and Vehicle Shipping			15,000
			Sub-Total	513,804

Long Term Salary and Support Sub-Total	$513,804

TECHNICAL ASSISTANCE COMPONENT (Short Term)

MicroEnterprise Finance Project

West Bank & Gaza

Cost Estimate

U.S. Source	Short Term					
		Daily	No. of	Per	No. of	
II.	Specialty	Rate	Days	Diem	Days	Cost
	A. Policy	$330	80	$245	100	$26,745
	B. Management Info. Systems	330	80	245	100	26,745
	C. Sub-Sector Analysis	300	80	245	100	24,345
	D. Gender Issues	300	80	245	100	24,345
	E. Marketing	300	80	245	100	24,345
	F. Training	280	80	245	100	22,745
	G. Investment	330	80	245	100	26,745
	H. Banking	330	80	245	100	26,745
			640		Sub-Total	$202,760
					DBA Ins.	8,516
					Medivac In	724
					Local Trav.	20,000
		Salary and Per Diem Sub-Total				$232,000
	I. Air Fares	Cost/RT	No. of RT			Cost
		3,000	36			$108,000
			Air Fare Sub-Total			$108,000

Short Term Salary and Support Sub-Total	$340,000

C. Estimated USAID-Financed Bank Program Start-Up Support Costs

ESTIMATED SUPPORT COSTS (Local)

MicroEnterprise Finance Project
West Bank & Gaza

Scenario 1

10 Loan Officers (1 Bank)

	$/Month	Total Mo.	Total Cost
1. Supervisory Loan Officer (1)	1,667	12	20,000
2. Loan Officers (10)	933	120	112,000
3. Operational Support (Travel/Transport/Off.)	230	132	30,360
4. Phone Purchase (11)			8,800
5. Office Space (if required)	250	12	3,000

Estimated Salary and Support Costs	$174,160

Scenario 2

20 Loan Officers (2 Banks or 2 Branches)

	$/Month	Total Mo.	Total Cost
1. Supervisory Loan Officers (2)	1,667	24	40,000
2. Loan Officers (20)	933	240	224,000
3. Operational Support (Travel/Transport/Off.)	230	264	60,720
4. Phone Purchase (22)			17,600
5. Office Space (2) (if required)	500	12	6,000

Estimated Salary and Support Costs	$348,320

Assumptions in Both Scenarios:

A. AID Support for One (1) Year

B. Costs Based on 1997 Data

D. Loan Uptake Projections

Loan Uptake Projection
Profit & Loss Scenario 1
MicroEnterprise Finance Project
West Bank/Gaza Total Program
(All in US $)

	Qtr 1	Qtr 2	Qtr 3	Qtr 4	Qtr 5	Qtr 6	Qtr 7	Qtr 8	Qtr 9	Qtr 10	Qtr 11	Qtr 12
FIXED COSTS												
Salary	33,000	33,000	33,000	33,000	36,300	36,300	36,300	36,300	39,930	39,930	39,930	39,930
Overheads	11,840	1,440	1,440	1,440	1,584	1,584	1,584	1,584	1,742	1,742	1,742	1,742
VARIABLES												
Avg. Loan Size	1,000	1,200	1,400	1,600	1,800	2,000	2,200	2,500	2,500	2,500	2,500	2,500
Interest Rate Mark-Up	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%
Avg. # Loans Outstanding	75	200	300	450	550	600	750	1,000	1,200	1,500	1,750	1,750
Total Amount Outstanding	75,000	240,000	420,000	720,000	990,000	1,200,000	1,650,000	2,500,000	3,000,000	3,750,000	4,375,000	4,375,000
Default	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%
Interest Income	1,875	6,000	10,500	18,000	24,750	30,000	41,250	62,500	75,000	93,750	109,375	109,375
Income	1,734	5,550	9,713	16,650	22,894	27,750	38,156	57,813	69,375	86,719	101,172	101,172
Cost	44,840	34,440	34,440	34,440	37,884	37,884	37,884	37,884	41,672	41,672	41,672	41,672
Profit/Loss	(43,106)	(28,890)	(24,728)	(17,790)	(14,990)	(10,134)	272	19,929	27,703	45,046	59,499	59,499

Assumptions:

Bank Loan Capital Investment $4,400,000
10 Loan Officers & 1 Supervisor

Loan Uptake Projection
Profit & Loss Scenario 2
MicroEnterprise Finance Project
West Bank/Gaza Total Program
(All in US $)

	Qtr 1	Qtr 2	Qtr 3	Qtr 4	Qtr 5	Qtr 6	Qtr 7	Qtr 8	Qtr 9	Qtr 10	Qtr 11	Qtr 12
FIXED COSTS												
Salary	66,000	66,000	66,000	66,000	72,600	72,600	72,600	72,600	79,860	79,860	79,860	79,860
Overheads	23,680	2,880	2,880	2,880	3,168	3,168	3,168	3,168	3,485	3,485	3,485	3,485
VARIABLES												
Avg. Loan Size	1,000	1,200	1,400	1,600	1,800	2,000	2,200	2,500	2,500	2,500	2,500	2,500
Interest Rate Mark-Up	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%
Avg. # Loans Outstanding	100	250	500	2,000	3,000	4,000	5,000	8,000	10,000	12,000	15,000	16,000
Total Amount Outstanding ($)	100,000	300,000	700,000	3,200,000	5,400,000	8,000,000	11,000,000	20,000,000	25,000,000	30,000,000	37,500,000	40,000,000
Default	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%	0.75%
Interest Income	2,500	7,500	17,500	80,000	135,000	200,000	275,000	500,000	625,000	750,000	937,500	1,000,000
Income	2,313	6,938	16,188	74,000	124,875	185,000	254,375	462,500	578,125	693,750	867,188	925,000
Cost	89,680	68,880	68,880	68,880	75,768	75,768	75,768	75,768	83,345	83,345	83,345	83,345
Profit/Loss	(87,368)	(61,943)	(52,693)	5,120	49,107	109,232	178,607	386,732	494,780	610,405	783,843	841,655

Assumptions:

Bank Loan Capital Investment $40,000,000
20 Loan Officers & 2 Supervisors

MONITORING AND EVALUATION PLAN

A. Suggested Activity Indicators & Targets

(The Activity Design Team met with Peter Malnak, the USAID Project Development Officer responsible for the Performance Monitoring System for USAID/West Bank/Gaza, and Richard McLaughlin, consultant, during this consultancy to discuss indicators for tracking Intermediate Results (IR) dealing with greater access to credit. Agreement was reached on specific indicators which would better reflect the achievement of this IR. The following indicators and targets are suggested and may be refined prior to their incorporation in the IR framework.)

This suggested indicators and targets for this activity include the following (all targets are to be achieved by the end of the Activity in three years, unless otherwise stated):

Purpose Level

Purpose: To increase access to credit for microenterprises, with special attention to women clients, and to develop long-term, sustainable sources of financial services for microenterprises through the formal financial system of the West Bank and Gaza

Indicators:
- Increased numbers of active loans to microenterprises with a substantial portion going to women entrepreneurs
- Increased loan value of active loans to microenterprises with a substantial portion going to women entrepreneurs
- Increased profits to banks from microenterprise loans under $10,000

Targets:
- An active portfolio of (To be Determined after negotiations with banks) loans to microenterprises by all participating banks, of which at least 40% would be to women
- An active portfolio totalling (TBD) million of loans to microenteprises by all participating banks of which 40% would be to women
- Profits to the banks totaling at least (TBD) million, or averaging (TBD) million per quarter at the end of the activity

Objective Level

Objective #1: To leverage USAID financial inputs with substantial capital from the participating banks to reach much greater numbers of microenterprises that could not be reached through NGO financed programs without significant infusions of donor capital.

Indicator: An increase in the use of bank-generated capital for loans to microenterprises

Target: At least $(TBD)million of the capital for outstanding loans to microenterprises comes from bank-generated capital.

Objective #2: To enhance the potential for rapid scale up of microloan numbers and amounts that will assist the banks to achieve early profitability in their microfinance programs.

Indicator: A substantial increase in the number of loans to microenterprises by the end of the second year of the Activity

Target: (TBD) total active loans by all participating banks by the end of the second year

Objective #3: To achieve a system of microfinance through the commercial banking sector which would have greater prospects for long-term, financial and institutional sustainability than the provision of microcredit through traditional NGO modes.

Indicator:
- A significantly greater number of active loans to microenterprises held by participating banks compared to NGOs providing microfinance
- Achievement of break-even and substantial profitability of microfinance for banks before NGO microfinance programs currently in operation

Targets:
- Participating banks would have a microenterprise loan portfolio twice as large as NGO programs in the West Bank and Gaza
- Participating banks would achieve break-even at the end of Year Two of Activity implementation and achieve minimum profits twice as large as existing NGO programs by the end of the Activity.

Objective #4: To provide microentrepreneurs with access to a wider range of banking services and to develop a long-term relationship between the banks and microentrepreneurs.

Indicator:
- Participating banks increase numbers of microentrepreneurs holding savings accounts with the banks as well as receiving loans.
- Participating banks provide additional loans to past participants in the microfinance program above and beyond the loan ceilings of the microenterprise finance program
- Participating banks develop new banking products for microenterprises

Targets:
- At least 25% of the recipients of microloans have savings accounts with the same banks at the end of the three year period of the activity.
- At least 10% of the microentrepreneurs receiving microfinance loans receive loans higher than the $10,000 ceiling for microloans from the

participating bank

- At least two new banking products are developed for microenterprises by the end of the activity.

B. Bank Responsibilities

Participating banks will be responsible for all reporting on their microfinance programs to USAID. Some reports will be submitted on a quarterly basis and others on an annual basis. Reporting content and formats will be agreed upon by USAID and the selected banks and incorporated into the agreement between the parties. These reports will track loan portfolio performance, outreach and the financial sustainability of the microenterprise program of each participating bank. A sample reporting format for loan portfolio performance and outreach is shown on the next page.

C. Resident Advisor Responsibilities

The Resident Advisor will be responsible for assisting the management of the participating banks in the preparation of the reports for which the banks are responsible. He shall coordinate the installation of the computerized management information system in each participating bank and ensure that the appropriate bank staff are effectively trained in the operation of the system and can produce the appropriate reports. Although another contractor, obtained through a separate contract will be responsible for the installation of the system and for training bank staff, the Resident Advisor will supervise these aspects of the work to be performed by the independent contractor.

In addition, the Resident Advisor shall be responsible for a monthly report to USAID in a format to be agreed upon at the time a contract is signed and will provide information on progress toward the achievement of the purpose and objectives of the Activity as well as the status of various sub-activities.

D. Mission Management Responsibilities

The USAID Mission shall be responsible for monitoring the performance of the Resident Advisor and other contractors and monitoring the performance of the participating banks. This monitoring shall entail review of the various reports, regular progress meetings with the Resident Advisor and bank staff as well as special meetings dealing with aspects of Activity implementation. The Private Enterprise Officer shall have prime responsibility for these monitoring functions but may delegate many of them to the Project Management Specialist attached to that office. The Strategic Objective Team responsible for this Activity shall have regular quarterly meetings to review Activity progress.

Sample Reporting Format

MicroEnterprise Lending Program West Bank and Gaza
Monthly Portfolio Report

TOTAL LOANS	Number this Mo.	%	Amount this Month	%	Number this Year	%	Amount this Year	%	TOTAL to DATE	%
New Loans	8	67%	14,000	74%	17	77%	30,000	75%	45,000	82%
Repeat Loans	4	33%	5,000	26%	5	23%	10,000	25%	10,000	18%
Total	12	100%	19,000	100%	22	100%	40,000	100%	55,000	100%
LOAN LENGTH										
<4 Months	5	42%	2,250	12%	7	32%	4,000	10%	9,000	16%
4-6 Months	3	25%	8,900	47%	7	32%	12,000	30%	15,000	27%
6-8 Months	3	25%	2,850	15%	7	32%	18,000	45%	24,000	44%
8-10 Months	0	0%	0	0%	0	0%	0	0%	0	0%
10-12 Months	1	8%	5,000	26%	1	5%	6,000	15%	7,000	13%
Total	12	100%	19,000	100%	22	100%	40,000	100%	55,000	100%
GENDER										
Female	8	67%	15,000	79%	16	73%	30,000	75%	37,000	67%
Male	4	33%	4,000	21%	6	27%	10,000	25%	18,000	33%
Total	12	100%	19,000	100%	22	100%	40,000	100%	55,000	100%
LOAN SIZE										
<1,000	5	42%	1,800	9%	4	18%	2,500	6%	3,000	5%
1,000-1,500	2	17%	2,800	15%	5	23%	5,000	13%	6,000	11%
1,500-2,000	2	17%	3,800	20%	7	32%	10,500	26%	20,000	36%
2,000-3,000	2	17%	5,600	29%	4	18%	10,000	25%	10,000	18%
3,000-4,000	0	0%	0	0%	0	0%	0	0%	3,000	5%
4,000-5,000	1	8%	5,000	26%	1	5%	5,000	13%	6,000	11%
>5,000	0	0%	0	0%	1	5%	7,000	18%	7,000	13%
Total	12	100%	19,000	100%	22	100%	40,000	100%	55,000	100%
BUSINESS DESCRIPTION										
Trade	5	42%	3,800	20%	6	27%	4,000	10%	5,000	9%
Manufacturing	2	17%	5,600	29%	3	14%	7,000	18%	8,000	15%
Processing	2	17%	2,800	15%	5	23%	5,000	13%	7,500	14%
Transportation	0	0%	0	0%	3	14%	1,200	3%	2,000	4%
Tourism	2	17%	1,800	9%	3	14%	5,000	13%	6,000	11%
Service	0	0%	0	0%	1	5%	1,000	3%	12,000	22%
Agriculture	1	8%	5,000	26%	1	5%	5,000	13%	6,000	11%
Other	0	0%	0	0%	0	0%	11,800	30%	8,500	15%
Total	12	100%	19,000	100%	22	100%	40,000	100%	55,000	100%

Note: The Same form would be submitted for repeat borrowers

Sample Reporting Form

MicroEnterprise Lending Program West Bank/Gaza
Monthly Delinquency Report

Amount Outstanding of TOTAL ACTIVE L	Number	%	Amount	%
On-Time	44	88%	35,000	82%
1-7 Days	4	8%	2,800	7%
7-21 Days	1	2%	3,000	7%
21-35 Days	0	0%	0	0%
35-60 Days	0	0%	0	0%
60-90 Days	1	2%	1,700	4%
Total Outstanding	50	100%	42,500	100%

Total Amount with Late Payments	7,500
Total Amount Outstanding	42,500
Portfolio At Risk	18%

OTHER MICROFINANCE PROGRAMS IN THE WEST BANK/GAZA

A. The International Finance Corporation of the World Bank Group

The only other microfinance program in the West Bank & Gaza that poses a potential threat to the success of the USAID Microfinance Activity is that of the International Finance Corporation.

At the time the Microfinance Sector Assessment was conducted in January and February of 1996, conversations with World Bank representatives revealed little interest on their part in becoming involved in microenterprise finance. In fact, the general attitude expressed at that time was to cede that activity to USAID. However, during the course of 1996, IFC and World Bank officials decided to provide financing for what is called a microenterprise project.

According to the design document, this proposed project will provide finance for microenterprises (defined as enterprises with ten or fewer employees) for loan amounts ranging from $500 to $30,000 with repayment periods ranging from one month to five years. Loans would be used to finance fixed assets and associated working capital for new operations, expansions and rehabilitations. At least 20% of project funding would be dedicated to loans of less than $10,000. Microentrepreneurs would be required to have viable cash flows. Market-based interest rates would be charged.

Project funding would total $23 million, including a trust fund credit from IDA of $5 million, a quasi-equity investment from the IFC of $7.5 million, a total contribution to the project of $7.5 million shared by the three participating banks (Jordan National Bank, Arab Bank and the Commercial Bank of Palestine) as loan capital, and $3 million from the IFC for technical assistance. All loans to microenterprises would be funded 37.5% by the participating bank, 37.5% by the IFC and 25% by the credit provided by the IDA. This makes the effective risk-sharing participation by the bank to be 37.5%, with the balance assumed by the IFC and the IDA credit. The IDA credit and the IFC quasi-equity investment effectively provide soft loans to the banks to onlend to microenterprises.

Technical assistance would be provided to the banks in the form of a resident advisor for each participating bank, training for loan officers, study tours to successful microenterprise programs elsewhere, and an automated loan screening and monitoring system. Technical assistance will also be provided by business support agencies to microenterprises on various aspects of business development.

Mr. Silcox of this activity design team held a telephone conversation was held with Tamara Lansky, the IFC representative responsible for the design of the IFC project, while the team was in Jerusalem. This was followed up with a meeting in Washington a few days after Mr. Silcox returned to the United States. During those conversations, Ms. Lansky stated that traditional collateral may be used to secure loans under the IFC program, with some exceptions. When questioned about the potential for duplication between the IFC-sponsored and USAID-financed activities, she was sensitive to this issue and expressed a willingness to explore ways to collaborate with USAID to eliminate duplication and confusion between the two activities. When it was explained that the USAID activity would concentrate on loans below $5,000, Ms. Lansky stated that she was willing to approach World Bank staff on the possibility of putting a floor of $5,000 on IFC-financed microenterprise loans. It was agreed that this suggestion could help to eliminate duplication between the two activities, but that other alternatives should be explored as well in the next few weeks to eliminate potential conflict or duplication between the two activities. She was particularly sensitive to the potential for conflict between the USAID-financed Resident Advisor and the IFC-financed bank advisors, particularly if one or more of the banks participate in both the USAID and the IFC activities. Mr. Silcox suggested that the IFC and USAID might reach an informal agreement to attempt to resolve any problems which might develop in this regard in the future.

B. Other Donors

Current activity by other donors in the microenterprise finance area is limited to additional support for the microlending activities of UNRWA and Save the Children.

The European Union provides support to the Palestinian Development Fund, an amalgamation of three Palestinian NGOs previously providing agricultural and small and medium enterprise credit to Palestinians which were reviewed in the Microfinance Sector Assessment in February 1996. At that time, representatives of those three NGOs and a representative of the European Union stated that previous bad experience with microlending had led them to the decision to provide credit only to small and medium enterprises.

Although the PDF is not now engaged in microlending, one of the members of the Board of Directors who attended a workshop on microlending organized by USAID in 1996 was inspired by that workshop to investigate the potential for engaging in microlending with USAID support. The Activity Design Team met with him to discuss his interest. At the conclusion of that meeting, he was informed that the likelihood of USAID providing finance to another NGO for microlending at this time was not very good. He indicated that he might explore other sources of finance and the Activity Design Team wished him well. If he is successful in finding a donor interested in supporting a microlending activity by the PDF, there may be potential overlap between USAID's microfinance activities through NGOs; but it is very unlikely that efforts by the PDF would impinge upon the success of USAID's support to banks to develop long-term, sustainable access to credit for microenterprises through the formal financial sector.

UNRESOLVED ISSUES & FURTHER RESEARCH REQUIRED

A. Risk-Sharing Options for USAID and the Participating Banks

Through the course of this design of a microfinance activity, three basic options for entering into agreements with commercial banks on risk-sharing of loan capital were identified. The first option - the provision of a grant to the participating banks of loan capital - was dropped after discussion with USAID staff. The remaining two options are presented below with the advantages and disadvantages of each.

Option #1: A loan guarantee program, with slight modifications, could be included under the Loan Portfolio Guarantee (LPG) Program administered by the USAID Global Private Enterprise Bureau. This could easily take place with at least one bank, the Jordan National Bank, which is already a participant in the LPG program. Alternatively, new agreements could be entered into with other banks that are willing to serve the microenterprise market, but are not currently participants of the LPG.

Advantages:

+ AID would only have to fund the technical assistance, training, and support costs discussed within this document. No funds beyond this amount (currently estimated at slightly larger than $2.3 million), would need to be expended from Mission funds.

Disadvantages:

-- The only bank that appears to be willing to lend to microenterprises and is a functional partner of the LPG to date is Jordan National Bank. Other banks that might be willing to lend to the sector might not choose to participate in the LPG program. The other two finalists for the USAID Microfinance Activity are the Bank of Jordan and the Arab Bank. The Activity Design Team was told that they both refused to participate in the LPG program earlier due to the fee structure for the program.

-- The LPG involvement in lending to microenterprises has thus far been largely limited to issuing guarantees to US-based NGOs or to banks to lend to NGOs for onlending to microenterprises. The experience of most banks with the LPG program is primarily with lending to small businesses (generally in the $20,000 - $250,000 range) with collateral requirements, rather than to microenterprises with no collateral. The LPG has been modestly successful in encouraging WB/G banks to extend loans to small businesses. However, to date the LPG appears to have been utilized primarily to "top up" collateral requirements for small businesses.

Option #2 A loan guarantee fund financed directly by USAID/West Bank/Gaza would be placed with participating banks in an interest-bearing account. This account would serve as a collateral fund for participating banks, allowing up to one-half of non-recoverable principal of defaulting microenterprise loans to be initially withdrawn from the account to cover bank losses. This percentage could be decreased on a phased basis as the banks acquire experience with the microfinance program and their loan clients. At the end of the agreement period, USAID would determine the ultimate disposition of the funds.

Advantages:

+ The funds could be put in place rapidly with the participating bank, and microfinance lending should occur fairly rapidly following staff training.

+ The banks would not necessarily need to be participants in the LPG program, but might be enticed to join the program later, which should generate even larger amounts of loan capital to be available to the microenterprise sector without additional Mission funding.

Disadvantages:

-- The negotiating process would need to include at least the notional final disposition of the funds, which has not been fully agreed upon within the Mission at this time. Should the Mission come to final agreement on the position as to whether or not remaining (unencumbered) funds would revert to AID or remain with the banks, this issue should not be difficult to resolve during negotiations with the banks.

B. Role of the USAID Resident Advisor vis-a-vis the IFC Bank Advisors

Although there are legitimate concerns relative to the potential for duplication or, at worst, conflict between the USAID Resident Advisor and the IFC Bank Advisors working at the same bank, there are a number of points which argue against a potential conflict between the two.

For example, the two advisors will be working with essentially different programs. The IFC loan product is primarily for small businesses, generally for those with medium term requirements (1-5 years), and requiring loan capital in excess of $10,000. This loan product is slightly different from the traditional loans that the banks are currently making and could, in fact, enhance the growth of the small business sectors in the West Bank/Gaza. However, it is doubtful that these loans would significantly conflict with the loan products to be promoted by the USAID Microfinance Activity.

It appears that the IFC Bank Advisors will be working with a different clientele and market than is envisioned under the USAID Microfinance Activity. The USAID-financed Resident Advisor will assist the bank(s) in establishing and closely monitoring an entirely new market for the banks;

microenterprises that have a need for short-term working capital with multiple repayments during the course of a loan that will probably be no more than six months in length. Current estimates show that most loans will be in the $1,000-2,000 range without pledged collateral. The new clientele will initially be unfamiliar with banking processes; the banks will initially be unfamiliar with the new clientele. However, the role of the Resident Advisor will be to provide (or facilitate) training for management and staff that will allow that staff to move into the microenterprise finance market.

Even though there is the possibility of an IFC Bank Advisor and the USAID Resident Advisor working at the same bank headquarters, the programs they would work with are targeted at different sectors of the economy. In fact, during interviews with bank officials by the Activity Design Team, bank officials expressed the opinion that the IFC project was not directed at the same clientele and would not use the same methodology as the proposed USAID Microfinance Activity.

C. Baseline Data for Impact Evaluation of the Activity

A management information system will be put in place with all banks participating under this Activity which will collect data and report on portfolio and financial performance of the banks. However, USAID has a need to gather impact data that will not show up within those reports. Impact data generally attempts to establish that microfinance activities result in increased net family income and other similar effects. It is proposed that research be carried out within this Activity (probably through household surveys) that would establish baseline data in the areas anticipated to be affected by microfinance activities. That baseline data will be important initially to assist AID in gaining a better understanding of the financial situation of the target market of microentrepreneurs in West Bank/Gaza. Subsequent impact data could be gathered from both clients that receive financial services under this Activity and from those microentrepreneurs that did not receive loans from the USAID Microfinance Activity.

D. Sub-sector Analysis

It is suggested that during the course of this activity sub-sector analyses be conducted in selected sub-sectors. Sub-sector analysis involves the study of particular sub-sectors of economic activity, such as clothing production, fruit and vegetable marketing, handicraft production, or vehicle repair. Sub-sector analysis provides information on the start-to-finish aspects of the particular sub-sector, identifying not only particular constraints in the market flow, but also identifying opportunities for improvements that can be achieved. It is recommended that sub-sector analysis be undertaken once lending is underway and significant borrower markets are identified.

NEXT STEPS

A. Bank Negotiations

The next step for the USAID Mission is to decide on the type(s) of risk-sharing arrangements to be utilized during negotiations with banks in the West Bank and Gaza and then to engage the banks in negotiations. The final selection of banks from among the three finalist banks (Jordan National Bank, Arab Bank and Bank of Jordan) should be carried out through a competitive system so that USAID West Bank & Gaza can make an objective selection of the banks best suited to carry out this Activity.

USAID should select either one or two banks for participation in the Microfinance Activity. Technical services could be provided more easily to one bank and would permit activity resources to be more focussed. However, two banks would provide competition between banks which could assist in achieving activity objectives more rapidly and could also allow for USAID to focus resources on the most successful bank after the initial two years of activity.

In order for a commercial bank to qualify for assistance from USAID/WB&G, it should be required to make an application with information regarding the following items. The USAID Project Management Specialist under the Private Enterprise Officer may assist the applicant banks in developing their applications to ensure that AID requirements are being met.

The following issues should be addressed in an agreement between USAID and the banks participating in a microfinance program for the West Bank and Gaza. These and are divided into two categories - Negotiable and Non-Negotiable Items. The Non-Negotiable Items are those that provide the minimum framework for a microfinance program. The Negotiable Items are those which, although important, provide some room for variance between the optimum program desired by USAID and the program which the bank(s) are willing to accept.

For the Negotiable Items, USAID should negotiate the best possible package with one or two banks. It is important to point out, however, USAID's support to the participating banks should be uniform. In other words, USAID should not offer one package of assistance to one bank and a different package to a another bank. This would create dissension among the banks and would provide an easy excuse for the bank receiving the lesser assistance to perform with less enthusiasm and blame programmatic failures on USAID's differing treatment of the banks.

Non-Negotiable Items

1. Target Clientele

All microenterprises in the WB/G will be eligible to participate in this microenterprise lending program. Microenterprises will be defined as enterprises with ten or fewer employees. Priority will be given to microenterprises enterprises with 5 or fewer employees. Program design and implementation will ensure women's access to financial services. Only established microenterprises which have been operating for more than six months will be eligible for microloans.

2. Financial Products

Short-term, working capital loans of twelve months or less will be the principal loan product offered. At least 75% of the bank's loan portfolio for the first year will consist of loans of less than $2000 for terms averaging six months or less. Borrowers will be able to access medium-term investment capital (e.g., equipment loans with repayment periods of more than 12 months) only after satisfactorily repaying at least four working capital loans. The maximum loan size will be initially set at $10,000 and the bank shall focus on loans of less than $5,000. Loan clients will be encouraged, but not required, to establish savings accounts at the banks offering microcredit. Loan and savings products will be developed which specifically address the needs and modalities of women entrepreneurs.

3. Lending Methodology

Loans will be made to individuals. Lending will be based primarily on the character and experience of the individual rather than traditional forms of collateral. Alternative and informal types of collateral, such as peer guarantees and village leader co-signers, should be encouraged. The lending program will emphasize access to future working capital credit as the principal incentive for prompt repayment of existing loans, rather than the loss of collateral. Interest rates on loans will be set high enough to cover all operational costs of the microfinance program, including the cost of funds lent, and provide for a reasonable profit. Recognizing that most loans will be for working capital, all loans should be approved or rejected within as short a period of time as possible. Repeat loans should be approved or rejected within a shorter period of time than the original loans. Loan amounts will be incrementally increased for repeat borrowers. For example, a borrower who had repaid an initial loan of $1000 for 3 months might receive a second loan of $1500 for 3 months or $2000 for 4 months. Loan officers will contact the microentrepreneurs at their place of business to offer the bank's financial products to them. Follow-up and monitoring on loans (including collections) will also be conducted at the microentrepreneur's site of business by the same loan officers responsible for the loan appraisal.

4. **Commitment to Profitability of Microlending**

The bank must be committed to the profitability of its proposed microlending program. This should be evidenced in bank projections of initial estimates of loans numbers with rapid increases in loan numbers and volume over the first two years and in the corresponding interest rates charged to cover costs of program operations. (This is to assure that the participating banks are not engaging in the program only for political or public relations reasons.)

5. **Risk-Sharing on Loan Defaults**

The bank will commit to share an appropriate portion of the risk on defaulting loans.

6. **Autonomous Unit**

The bank shall establish an autonomous unit within the bank which will be responsible for the microlending program.

7. **Staffing**

The bank will provide sufficient staff to conduct the program including Field Loan Officers and a Supervisory Loan Officer. These staff will be newly hired when the program commences in order to assure that the employees are committed to the program and its methodology and to assure that their background and experience is suitable for this new activity.

8. **Resident Advisor**

The bank will agree to accept the services of a Resident Advisor, to be financed by USAID, who will provide technical assistance to the bank in the establishment and implementation of the microfinance program.

9. **Office Space**

The bank will agree to provide suitable office space for the microfinance program staff and Resident Advisor, either directly in each branch bank or in a nearby office building to facilitate communication and integration within the bank's operations.

10. **Reporting**

The bank will provide quarterly and annual reports to USAID which will report on the activities of the microfinance program within the bank. A format for these reports will be developed in collaboration with the Resident Advisor and based on experience elsewhere.

Negotiable Items

A. Geographic Coverage

The banks should indicate the areas which they intend to serve and identify which initial branch or branches of the banks would provide the financial services to the microenterprise clientele. Within those areas, clear identification of the number of borrowers and savers targeted for services should be indicated, either by month or by quarter. Preference shall be shown to those banks which target urban areas that have enterprise densities which would permit early scale up of operations at least cost.

B. Profitability Projections

Banks demonstrating more rapid achievement of profitability will be given higher preference.

C. Leverage of USAID Funds with Bank Capital

Banks indicating a willingness to provide higher amounts of their own capital and to provide greater numbers (with corresponding and appropriate volumes) of loans will be given preference.

D. Risk-Sharing on Loan Defaults

Banks should express its commitment to share the risk on defaulting loans. The bank(s) agreeing to accept higher risk on defaulting loans will be given preference. (In the absence of a compelling reason, USAID should not accept a risk of greater than 50%, on the principal only, of the defaulting loans.)

E. Staffing

Although USAID will be prepared to provide financial support for initial program startup costs, the bank(s) which require less financial assistance for these costs will be given preference.

F. Incentive Systems

Banks willing to adopt an incentive payment system for loan officers and other employees engaged in the microfinance program will be given preference.

G. Resident Advisor

The bank(s) demonstrating a better understanding of the role of the Resident Advisor and how they will use his/her skills and integrate him/her into the bank's management structure will be given preference.

The negotiation points and criteria for selection presented above may be expanded to include other items. These are the basic issues which should be addressed. Following negotiations with the banks, an agreement should be entered into which specifies the agreement between USAID and the participating bank(s) in detail.

B. Formalization of Activity Design

USAID will need to finalize the Microfinance Activity Design in conjunction with an agreement with either one or two banks to implement the Activity, since without the agreement of at least one bank, the Activity cannot move forward. At this point, USAID will have to make some tentative decisions on different aspects of the Activity which are not contingent upon agreement with the banks. Key items in this category include the total funds available for the Activity and specific line items, contractual mechanisms to obtain technical assistance, and the length of the Activity.

The visit by John Moran of the USAID Global Bureau to the West Bank and Gaza the week of the 23rd of February appears to have assisted the Mission in moving forward on the selection of the risk-sharing mechanism with the banks. Mr. Silcox of the Activity Design Team met with him in Washington the week before his arrival in Tel Aviv to discuss the issues to be resolved in the activity design to provide him with background information before he arrived. It may be necessary to obtain further consulting services to complete negotiations with the banks if Mr. Moran is unable to achieve closure on the agreements with the banks. Although the Regional Legal Advisor can provide assistance in reviewing the proposed agreement between USAID and the banks, local legal services to draft the final agreement with the banks may also be necessary to assure that any agreement is consistent with the current laws applicable to the West Bank and Gaza and is written in Arabic.

Mr. Silcox also met with Elisabeth Rhyne, the Director of the Office of Microenterprise Development in the Global Bureau of USAID in Washington. She provided comments on the activity design - particularly in regard to the issues to be negotiated with the banks. Her comments were incorporated into this final report.

ANNEXES

ANNEX 1

Scope of Work

Design of a Microenterprise Activity in West Bank/Gaza

Background

The USAID/West Bank and Gaza Strategy (1996-2000) outlines a two-track approach for future USAID initiatives to increase access to financial services for the Palestinian private sector. This approach consists of:

1) Support grants to existing NGO microcredit projects in order to expand the volume of credit available to small borrowers in the near-term; and

2) Technical assistance and training to facilitate the development of microcredit programs run by commercial banks in order to develop a more sustainable and broad-based model for microcredit delivery in the longer term.

In September, 1996, USAID concluded grant agreements with Save the Children and UNRWA to enhance their capacity to deliver microenterprise loans in the West Bank and Gaza. Funds provided under these agreements are expected to result in 8,500 individual loans to Palestinians, over an eighteen month period.

Also in 1996, USAID organized and financed a series of seminars and workshops to expose Palestinian bankers to microcredit practices and technology employed in other parts of the world, with an emphasis on successful programs developed with USAID assistance in Egypt. A select group of Palestinians were invited to attend a one-week training session on the operations and management of a microlending program at the Alexandria Business Association.

Subsequently, a USAID Program Management Specialist conducted meetings with representatives of several commercial banks to assess their interest in a potential USAID-financed program to introduce microlending operations at selected bank branches in the Palestinian territories. The program, as outlined in these discussions, would include the following elements:

*USAID funding for the procurement and installation of the Management Information System and associated software currently in use in Alexandria;

*USAID funding for staff training, as necessary and appropriate;

*USAID funding for a Resident Advisor to be situated at the bank(s) regional headquarters to oversee the introduction of microlending operations;

*a USAID guarantee for some proportion of the loan capital allocated for microenterprise borrowers.

The commercial bank representatives were generally supportive of this program concept but each raised a number of specific questions concerning elements of the program design (see attached Memoranda).

General Objectives

The general objectives of this consultancy are: 1) to analyze the activity concept in order to provide complete answers to the specific questions cited below; 2) to validate the feasibility of the activity and assess the likelihood of achieving the desired developmental outcomes; 3) to describe each element of the proposed activity in detail (e.g. bank structures, staff functions, volume of loans over time and the role of USAID technical and financial assistance); 4) to estimate activity costs and recommend an appropriate sequencing of activity elements; 5) to draft Memoranda of Agreement between participating banks and USAID, as necessary and appropriate; and 6) to draft terms of reference for activity implementation contractor(s).

Specific Questions

The consultants will prepare a detailed written response to the following specific questions:

1. Are the commercial banks prepared to invest the necessary resources to introduce a microlending component in their branches? Which banks are most amenable? Which branches of those banks?

2. What are the prospects for sustainability of microlending facilities within participating banks? What factors will determine whether the bank(s) commitment to the program is sustainable over time? What are the perceived risks and how can they be mitigated?

3. Which elements of the Alexandria Business Association operations can/should be transferred to the West Bank and Gaza? How might the Alexandria model be modified to reflect conditions prevailing in the Palestinian territories?

4. What kind and intensity of training will be necessary to introduce the Alexandria operations to the participating banks in the West Bank and/or Gaza? What level of resources will be required and how should training activities be sequenced and managed?

5. What should be the roles and responsibilities of the Resident Advisor and to whom should he/she report? What qualifications should he/she possess? How should the relationship be structured among the Advisor, USAID and the bank?

6. How should the guarantee facility be structured? When should it be phased-down or withdrawn?

7. How should the activity be implemented? Which contracting mode would be most appropriate?

8. Are there substantive differences between the banking environment in Gaza and the West Bank that would suggest a need to modify the proposed activity to adapt to the area targetted?

9. How should the activity be monitored and evaluated? What kinds and frequency of reports should be generated?

10. What optional elements, if any, should USAID consider during the course of activity implementation?

11. How should the commercial bank(s) interact with NGO microcredit programs?

12. What role, if any, should the USAID activity play in marketing the microcredit facility to potential borrowers? How might demand for microcredit expand over time and should the activity expand accordingly?

Timing and Level of Effort

Two consultants are required for a period of three weeks in-country. Six day workweeks are authorized. This consultancy should begin not later than Monday, January 27, 1997.

Up to five person days are authorized in the United States to finalize the deliverables.

Deliverables

The consultants will deliver a draft report responding to the specific questions cited above, at the beginning of their third week in-country. Prior to their departure, the consultants will conduct an oral debriefing to review the findings contained in the draft report before an audience to be selected by USAID.

A final report, incorporating responses to substantive and editorial comments received during the draft report review will be provided no later than ten working days after the field work is completed.

The consultants will also provide the following specific products as separate documents or as appendices to the final report no later than ten working days after the field work is completed: 1) a draft Memorandum of Agreement for use with participating banks; 2) a draft activity budget and timeline; 3) draft terms of reference for an activity implementation contract; 4) a draft activity training plan; and 5) draft terms of reference for the Resident Advisor.

Ten (10) hardcopies of these reports and specific products will be delivered to USAID/West Bank and Gaza along with one or more diskettes containing all text, tables and annexes.

Logistics

The consultants will be responsible for all logistical aspects of this consultancy including, but not limited to: transportation, secretarial support, printing and duplication, communications, hotel accomodations and computer access.

Consultant Qualifications

A Microcredit Specialist with a minimum of ten years practical experience in the design and implementation of microfinance projects in developing countries. This consultant should be fully-versed in all aspects of USAID policy relating to microcredit and have participated in USAID-funded microcredit design or evaluation activities. He/she should also have past professional experience in either the West Bank and Gaza, in Egypt, or ideally, in both areas.

A Microcredit Training Specialist with a minimum of five years practical experience in the design and implementation of training programs to enhance the delivery of credit to small borrowers. This consultant should also have past professional experience in the West Bank and Gaza, in Egypt, or in both areas. He/she should be able to prepare operating budgets for training programs and possess experience in the financial analysis of training activities. He/she should also have previous professional experience in the monitoring and evaluation of microcredit programs in developing countries.

Reporting Arrangements

The consultants will report to the Director of the Private Enterprise Office of USAID/West Bank and Gaza, or his designee.

ANNEX 2

LIST OF PERSONS INTERVIEWED

U. S. GOVERNMENT

USAID/Washington

Elisabeth Rhyne, Director, Office of Microenterprise Development, USAID Global Bureau
John Moran, Director, Loan Portfolio Guarantee Program, USAID Global Bureau
Gregg Baker, Chief Economist, ANE/SEA/EA

USAID/West Bank/Gaza

Chris Crowley, Director
David Rhoad, Deputy Director
Rosalie Fanale, Program Development Officer
Brad Wallach, Private Enterprise Officer
Peter Malnak, Project Development Officer
Johnny Zeidan, Private Sector Program Manager
Richard McLaughlin, Consultant

BANKS

Jordan National Bank

Hanna Ghattas, Regional Manager
Malek Khadder, Deputy Regional Manager

Arab Bank

Joseph Nesnas, Assistant VP, Head of Project Finance Department

Cairo Amman Bank

Yousef Bazian, Assistant General Manager, Regional Manager
Fayez Husseini, Assistant Manager

Bank of Jordan

Atiyeh Shananier, Assistant General Manager, Regional Manager
Susan Khoury, Manager, Ramallah Branch

39

Commercial Bank of Palestine

Khaled Ghabeish, General Manager
Abdallah Khalil, Manager, Ramallah Branch

NGOS

Save the Children Federation

Pat Conners,

Palestinian Development Fund

Hani Abu-Dayyeh, Board Member

CONSULTANTS & ATTORNEYS

Aziz, Fuad and Raja Shehadeh

Fuad Shehadeh, Advocate

Massar Associates

Bashar Masri, General Manager

INTERNATIONAL FINANCE CORPORATION

Capital Markets Division

Tamara Lansky, Investment Officer

ANNEX 3

ANSWERS TO QUESTIONS IN SCOPE OF WORK

DESIGN OF A MICROENTERPRISE ACTIVITY

FOR THE WEST BANK & GAZA

WITH DIRECT LENDING THROUGH COMMERCIAL BANKS

1. **Are the commercial banks prepared to invest the necessary resources to introduce a microlending component in their branches? Which banks are most amenable? Which branches of those banks?**

Discussions with the five banks identified by the USAID Program Management Specialist as showing the most interest in establishing a microlending program resulted in the narrowing down of those with the most potential to three banks - Jordan National Bank, Arab Bank and Bank of Jordan. Of the three, the first two had management personnel who received exposure to microenterprise lending principles through the USAID-sponsored microenterprise finance workshops in 1996. Top management of the Bank of Jordan were clearly interested in microlending, but only middle management personnel had participated in the USAID-sponsored workshops. Time did not permit the Activity Design Team to meet with many branch managers of the banks. However, selection of the branches where the microfinance program would begin should be decided upon by the top management of the banks selected by USAID for participation in the microfinance activity, in collaboration with the Resident Advisor.

2. **What are the prospects for sustainability of microlending facilities within participating banks? What factors will determine whether the bank(s) commitment to the program is sustainable over time? What are the perceived risks and how can they be mitigated?**

First and foremost, it should be kept in mind that success of this activity is not certain. Microenterprise programs run exclusively through banks with no NGO involvement are very rare. Prospects for sustainability are good if the selected banks follow the policies and procedures exemplified by successful microenterprise programs elsewhere and consistent with the design of this activity. The rationale for attempting this activity is due to the conditions cited in the Microfinance Sector Assessment of February 1996 which are favorable for this kind of program in the West Bank & Gaza. The Activity Design Team has developed projections of loan activity and a budget for program expenses that illustrate to potential for financial sustainability of the

41

microfinance activity. If the participating banks follow this model, or something similar, the chances for success are good. Nevertheless, it should be kept in mind that these projections provide a starting point for negotiations with the three banks identified. The bank negotiations should be a competitive process with final agreement being made with that bank or those banks that provide USAID with the most attractive offer. The final agreement with the banks should reflect sufficient detail to assure that both the banks and USAID are in agreement about the key issues of the activity.

Principal factors which will determine sustainability over time include the following:

- Strong, long-term commitment by the participating banks to the success and profitability of the activity and to the principles of microfinance developed in other countries and exemplified in USAID's Guiding Principles for Microenterprise Finance Programs
- Rapid scaling up of operations to achieve break-even early in the program
- Development of a cadre of well-trained and experienced loan officers who are both competent to judge risk and evaluate borrowers as well as to monitor loan repayments on a regular basis
- Enforcement of prompt repayments
- Rapid approval of repeat loans
- Charging interest rates that fully recuperate program costs (including the cost of funds) plus a reasonable margin of profit
- Development of other activities and services for loan clients that increase the bank's interest in the clients for additional profits (e.g., savings programs)

Key perceived risks in dealing with banks encompass the following:

- Interest in the activity only to alleviate criticism of bank's reluctance to loan funds to small and microenterprises in the West Bank & Gaza without excessive collateral requirements
- Interest in the activity mainly to receive donor funds
- Changing the "mentality" of bankers who generally consider microentrepreneurs to be poor risks and this type of loan program as a charitable or social activity, not as a profit making opportunity
- Inability to adopt bank policies and procedures to fit microenterprise program principles
- Continuing to rely on collateral to secure loans
- Lack of follow-up of loan repayments and excessive reliance on a guarantee fund
- Substantial staff turnover creating program continuity problems

Measures proposed to mitigate these risks consist of the following:

- Provision of funds to share in the risk of banks in program implementation for sufficient time to demonstrate the program's success
- Funding a portion of the start-up operational costs for the bank to establish the program
- Provision of both long-term resident and short-term technical assistance and training to

42

assure that the bank's both feel comfortable in implementing the program and are exposed to best practices in microfinance elsewhere

- Provision of an effective, already proven, MIS system with hardware, software and related training
- Agreement by the bank to set up an autonomous division for the microlending operations, to provide office space for program staff and the Resident Advisor, an employee compensation package to attract and retain good employees as well as to cover transportation costs for client and promotion visits, and to provide appropriate program reports to USAID on a monthly, quarterly and annual basis.

3. <u>Which elements of the Alexandria Business Association operations can/should be transferred to the West Bank and Gaza? How might the Alexandria model be modified to reflect conditions prevailing in the Palestinian territories</u>?

First, it is important to point out that this activity design does not follow the ABA model, since that model uses an NGO in conjunction with a bank, as do most microenterprise finance models worldwide. One can state that the proposed activity to implement the program directly through the banks will conduct many of the same functions that ABA uses and employ similar methodologies in terms of microlending principles and operations. In fact, the proposed activity will more closely resemble the model of the National Bank of Development in Egypt. Such things as the ABA operations manuals, MIS and other aspects of their program can be adapted for use in the Palestinian territories, but the overall approach used by ABA is very different from the approach used in the proposed activity for the banks in the West Bank & Gaza. The BRI model in Indonesia could be considered a more appropriate model, since it utilizes banks directly with no NGO participation. The aspects of the ABA and NBD models in Egypt are relevant in that the economies, culture and language are similar.

4. <u>What kind and intensity of training will be necessary to introduce the Alexandria operations to the participating banks in the West Bank and/or Gaza? What level of resources will be required and how should training activities be sequenced and managed</u>?

The workshops conducted for banks and NGOs in the West Bank and Gaza over the past year were only partially successful in that they provided some limited exposure to successful microlending programs for bank personnel. Senior bank management only participated in the one day sessions in Ramallah or Gaza. More junior and middle management bank staff visited the ABA program in Alexandria. Thus, one of the main objectives of the workshops - to identify one or two "champions" of microenterprise finance was not achieved. Although the workshops whetted the interest of a few bank managers and this was reflected in the interest shown by the three banks mentioned in the answer to Question #1, none of the bankers interviewed last week by the team believed that microlending was profitable enough to undertake a program on his/her

43

own. In fact, some of the bankers interviewed expressed the opinion that the Egypt-type program might not work in the West Bank & Gaza due to special conditions here. This means that more efforts and time will be needed to change the traditional "banker mentality" and to convince them that a program can function here with modifications to models from Egypt and elsewhere.

The Activity Design Team recommends that the technical assistance required to convince the bankers of the profitability of the program and to assist in the establishment and implementation of the program should incorporate of the following:

- A Resident Advisor with broad experience in microfinance development programs using banks as an integral part of the programs. He/she should serve for a minimum of three years with options for annual extensions, based on a determination by USAID. A Draft Scope of Work for the Resident Advisor is attached.

- Short-Term Technical Assistance in specific areas will be required, as identified by the Resident Advisor during the course of activity implementation. Illustrative TA might include specialists in MIS development, loan product development, sub-sector analysis, gender issues, marketing, policy issues and investment.

- Intensive initial training of the program staff for each bank will be necessary to expose them to successful microlending principles and operational procedures and to train them in the approach to microlending to be employed by their respective bank(s). This should include study trips to successful programs in other countries for the Supervisory Program Officer in each bank and one or two key senior bank management staff. Training of field Loan Officers should be conducted in the West Bank & Gaza, bringing in training staff from other countries, as needed.

5. What should be the roles and responsibilities of the Resident Advisor and to whom should he/she report? What qualifications should he/she possess? How should the relationship be structured among the Advisor, USAID and the bank?

The principal objective of the Resident Advisor is to advise the management and staff of the banks participating in the MF Project on all issues, policies and implementation of their respective microenterprise finance programs. Since the banks implementing the project will have had little or no experience with loans of these types, the Resident Advisor will be responsible for both convincing the bank management of the feasibility of these loans as well as to assist program staff in the establishment and implementation of microfinance lending programs and bring lessons to bear from other successful microfinance programs elsewhere. He/she will report to a designated senior officer of each participating bank and be supervised by the Private Sector Officer and the Microenterprise Program Officer of USAID/West Bank/Gaza.

The Resident Advisor should have over five years prior experience in managing or advising on microfinance programs in developing countries and over ten years total experience in development programs in developing countries, preferably in the Middle East. He/she should possess at least a Bachelor's Degree in Finance or a related field, although a Master's Degree is preferred. Excellent communications and writing skills are required. Knowledge of successful microfinance programs in the Middle East and elsewhere in the world is required and experience in running training programs would be a plus. A background in banking institutions and Arabic language capability is preferred. The Resident Advisor must be capable of working closely with bank personnel and advising them on all topics relevant to the establishment, implementation an evaluation of a microfinance program.

6. How should the guarantee facility be structured? When should it be phased-down or withdrawn?

USAID should fund a risk-sharing fund to leverage bank resources for microlending which could be in the form of a loan default guarantee facility or in another form. The facility would be phased out over the life of the activity with a declining percentage of USAID funds at risk as the participating banks acquire experience with the program and the microentrepreneur clients' repayment history. The design of the guarantee facility will need to be determined during final activity design and in consultation with the LPG program. Three options have emerged through discussions with West Bank/Gaza bankers and with John Moran of the USAID Loan Portfolio Guarantee Program for the structure of this facility:

a) A direct grant to each participating bank that would be used to reimburse the bank on a portion of the principal of defaulting loans during the life of the activity on a declining ratio agreed upon in advance by the banks and USAID. At the end of the project, the funds would revert to the bank for microlending purposes.

b) A loan guarantee program included under the Loan Portfolio Guarantee Program (LPG) administered by the USAID Global Private Enterprise Bureau. This could take the form of an amendment and increase in funds to existing participants in the LPG (Jordan National Bank), or a new agreement with new bank participants.

c) A loan guarantee fund placed either with the participating banks in an interest-bearing account or in another bank in the West Bank/Gaza that could be drawn upon for defaulting loans similar to the LPG, but with special terms and conditions different from the LPG and with a clear understanding that only a portion of the principal on defaulting loans are guaranteed. This would be funded by USAID/West Bank/Gaza with Activity Funds, but might also include participation by the LPG. At the end of the activity, USAID would determine the final disposition of these funds.

45

The LPG has been modestly successful in encouraging WB/G banks to extend loans to small businesses. However, to date the LPG appears to have been utilized primarily to "top up" collateral requirements for small businesses. Entry into the microfinance area will be a completely new experience for the banks and the Activity Design Team believes that this will require measures beyond the traditional guarantee program approach.

7. How should the activity be implemented? Which contracting mode would be most appropriate?

USAID/West Bank/Gaza has two principal options for contracting for the technical assistance and training required for this Activity. Except for the installation of the USAID/Egypt financed MIS system which was developed for microfinance institutions in Egypt and which could be purchased on a sole source basis for installation in participating banks in the West Bank and Gaza , the two options are as follows:

- An institutional contractor would be selected through full and open competition which would provide the services of the Resident Advisor as well as short-term technical assistance and training. This option has the advantage of having one single contractor responsible for the coordination and provision of all TA and training for the Activity. Proposals in responses to a RFP could also suggest innovative approaches toward the implementation of the Activity. The principal disadvantage is the length of time which would be required to issue the RFP, make the selection and field the Resident Advisor.

- A Personal Services Contractor could be selected to fill the position of the Resident Advisor and buy-ins to centrally funded microenterprise development contractors, such as those administered by the Office of Microenterprise Development in the Global Bureau, could be used for short-term TA and training. This option might result in lower costs, but could be more management intensive for USAID and hamper the ability of the Resident Advisor to coordinate all activities effectively. On the other hand, it would allow USAID/West Bank/Gaza to access specialized resources developed for the express purpose of disseminating lessons learned in the microenterprise development field.

While the Activity Design Team recommends that the first option be selected, both options are valid approaches to the acquisition of TA and training for the Microfinance Activity.

8. Are there substantive differences between the banking environment in Gaza and the West Bank that would suggest a need to modify the proposed activity to adapt to the area targeted?

Experience to date with existing programs in the West Bank and Gaza (namely the Save the Children and UNRWA programs) do not indicate any difference in loan methodology between the

West Bank and Gaza. Although the economies of both areas differ considerably, the lending principles and operations of the microfinance programs are not significantly different. There could be differences in the types of microenterprises financed, and these could be determined both through practice and through the application of subsector analysis early in the implementation of the program.

9. <u>How should the activity be monitored and evaluated? What kinds and frequency of reports should be generated?</u>

Successful microenterprise finance programs require almost instantaneous access to portfolio performance, and the ability to regularly review the financial performance of the units issuing the loans. This activity will provide funding to provide hardware and software, along with local staff training, to ensure data that is accessible to management, staff, as well as to the donor agency. A sophisticated series of programs have been developed with USAID support in Egypt. It is recommended that this system, which produces information in both Arabic and English, be adapted to fit the situation in West Bank/Gaza.

The minimum data required for reporting to USAID is specified in the USAID Guiding Principles for Selecting and Supporting Intermediaries for Small and Microenterprise Finance. The data required for this activity is broken down into the following categories:

a) **<u>Portfolio Performance</u>** - The banks will require data on loan performance to be available within the same business day that loan issuance or repayment is expected to occur. Microenterprise loans are tailored to the business cycle of the borrower, primarily for working capital, which means that repayments are made on a daily, weekly, or monthly basis (short-term and high-rollover). The Management Information System (MIS) must reflect this cycle of rapid loan issuance and short loan periods with multiple repayments. This information should be both timely and easily accessible to loan officers and management so that 1) if amortization payments have been fully met by the borrower, repeat loans can occur rapidly, and 2) if a payment has been missed, the responsible loan officer can take corrective measures immediately. A summary of this information, which would be submitted to AID on a monthly basis, is shown as an attachment. This information can track outreach and gender issues as well.

b) **<u>Institutional Financial Performance</u>** - The key to long term sustainability of microfinance services is that the banks receive sufficient profit from their microlending operations to justify continuing services. Participating banks will be required to provide income and expense information to USAID on a quarterly basis as well as an annual audit with a balance sheet and a profit and loss statement. A Loan Uptake Projection is attached which shows the likely outcome (profitability) of lending to microenterprises in West Bank and Gaza. These variables will be tested during the actual implementation of the project. (All costs are based on information received from local sources.)

41

USAID officers will use the monitoring data to track progress in this activity. In addition, it is recommended that USAID finance an outside evaluation in the third year of the activity in order to determine the success of the activity and potential areas for strengthening for follow-on activities.

10. What optional elements, if any, should USAID consider during the course of activity implementation?

USAID should provide funds for additional research which might be necessary during the life of the activity. This is always helpful in providing a source of funds to study specific activity components or related issues which could either assist in the success of the activity or in focussing attention on specific elements that might apply to other USAID activities in the West Bank/Gaza or elsewhere.

It is recommended that USAID should focus on microfinance provision and not finance any training or technical assistance to microenterprises in the field of business skills training, production, marketing, or vocational training as a part of this Activity. Experience elsewhere has demonstrated that training of this sort does not necessarily provide any added benefit to a microfinance program through banks. Initial orientation sessions with prospective or initial loan clients of the banks may be provided by the banks. A number of successful microfinance programs use this type of training to acquaint their clients with the operation of the credit program and to educate them as to the proper use of credit.

11. How should the commercial bank(s) interact with NGO microcredit programs?

The participating banks shall actually be engaged in competition with NGO microcredit programs, although this will not become evident until a year or more of operations. USAID should, as much as possible, encourage the participating banks and the NGOs which have received microfinance activity grants to cooperate and share information about common problems, successes and failures. Since this activity is an experiment and may not succeed, USAID should be on the lookout for possible linkages between the banks and the NGOs that might provide opportunities for greater collaboration and symbiotic relationships. The intent of this activity is to experiment with different institutional mechanisms to establish long-lasting and sustainable sources of finance for microenterprises. USAID should remain open to evolving opportunities and relationships to achieve that objective, rather than to be limited by ideological straitjackets or biases toward one particular institutional mechanism.

It is suggested that USAID promote and facilitate a forum for the periodic sharing of information and experiences among both the banks and NGOs receiving funding from USAID for microenterprise finance. This forum might also include other banks and NGOs active in the field with support from other donors or organizations.

12. **<u>What role, if any, should the USAID activity play in marketing the microcredit facility to potential borrowers? How might demand for microcredit expand over time and should the activity expand accordingly?</u>**

The responsibility for marketing microcredit rests on the banks and the NGOs providing these services. USAID's role should be to support their initiatives. If the demand for microcredit expands and those institutions are unable to meet that demand, USAID should look for opportunities to supplement the supply of funds or institutions providing microcredit. For example, should the activity succeed in achieving profitability for the participating banks, but those banks find their lending limited by a shortage of capital or liquidity, USAID might encourage other banks to engage in microlending in order to expand the supply of capital available to the sector. Another alternative would be to assist the banks to increase their funds for lending through the development of savings programs that encourage clients and their relatives to place more deposits with the microlending facility.

USAID should be prepared to build on the successes of the microfinance activity through additional funding of promising initiatives. The development of sustainable microfinance institutions in the West Bank and Gaza does not have a two or three year horizon. Although USAID may wish to limit their commitment to a specified time frame, it should recognize that the development of sustainable microenterprise finance institutions is a long-term objective. In fact, experience elsewhere has shown that, over time, successful microfinance programs attract more donor interest and funding to assist in program expansion and the achievement of national impact. This is not a turn-key project with a fixed timeframe for success, but rather the beginning of an activity with the potential for a long-term solution to finance for microenterprises. USAID should be prepared to support further growth if the initial efforts bear fruit.

49

ANNEX 4

DRAFT STATEMENT OF WORK

RESIDENT ADVISOR

WEST BANK/GAZA MICROENTERPRISE FINANCE PROJECT

BACKGROUND

USAID/WEST BANK/GAZA is funding a Microenterprise Finance (MF) Project which will provide financial and technical support to selected banks in the West Bank and Gaza which are committed to establish and implement microenterprise finance programs in their banks. The project will provide risk sharing funds and a portion of the startup operational costs to the banks as incentives to encourage them to enter this new area of finance. In addition, USAID will provide technical assistance and training to bank management and program staff during the initial years of the project. The Resident Advisor will be the principal provider and coordinator of this technical assistance and training.

The MF Project will target microenterprises in the West Bank and Gaza with five employees or less and will provide non-collateralized loans ranging from $500 to 10,000, with an expected average size loan of between $1000 and $2000 to start, to finance working capital costs with terms averaging 6 months or less. Repeat loans of gradually increasing amounts will be given to bank clients repaying loans on time.

OBJECTIVE

The principal objective of the Resident Advisor is to advise the management and staff of the banks participating in the MF Project on all issues, policies and implementation of their respective microenterprise finance programs. Since the banks implementing the project will have had little or no experience with loans of these types, the Resident Advisor will be responsible for both convincing the bank management and staff of the feasibility of these loans as well as to assist them in the establishment and implementation of microfinance lending programs and bring lessons to bear from other successful microfinance programs elsewhere.

SPECIFIC TASKS

The Resident Advisor shall be responsible for the following tasks:

1. Advise the participating banks in all aspects of start-up of their programs, including budgeting, projections, staffing, and policy formulation.

2. Advise the participating banks on best practices in microenterprise programs based on world-wide experience to date and recommend appropriate training and technical assistance for bank management and MF program staff. This includes recommendations on study tours to other countries with successful MF programs.

3. Advise the participating banks on the establishment and implementation of the monitoring and loan performance tracking systems for each participating bank and assist in the preparation of reports to USAID.

4. Monitor and assess progress made by each participating bank in the implementation of its MF program.

5. Coordinate training and short-term technical assistance to participating banks on MF provided from other USAID-financed sources.

6. Advise the participating banks on various implementation issues including outreach, gender concerns, interest rates and program sustainability.

TERM AND LOCATION OF ASSIGNMENT

The Resident Advisor shall serve for an initial term of three years with optional additional years as determined by USAID.

The Resident Advisor shall have an office in each participating bank in the West Bank or Gaza (provided by each bank) and shall spend equal time among all participating banks in the microfinance project.

51

QUALIFICATIONS

The Resident Advisor should have over five years prior experience in managing or advising on microfinance programs in developing countries and over ten years total experience in development programs in developing countries, preferably in the Middle East. He/she should possess at least a Bachelor's Degree in Finance or a related field, although a Master's Degree is preferred. Excellent communications and writing skills are required. Knowledge of successful microfinance programs in the Middle East and elsewhere in the world is required and experience in running training programs would be a plus. A background in banking institutions and Arabic language capability is preferred. The Resident Advisor must be capable of working closely with bank personnel and advising them on all topics relevant to the establishment, implementation an evaluation of a microfinance program.

SUPERVISION & REPORTING

The Resident Advisor will report to a designated senior official of each participating bank and shall be supervised by the Private Sector Officer and the Microenterprise Program Officer of USAID/West Bank/Gaza. He/she shall provide monthly reports to USAID/West Bank/Gaza with content and format to be determined by USAID.

ANNEX 5

TASKS/RESPONSIBILITIES

SUPERVISORY LOAN OFFICERS & FIELD LOAN OFFICERS

The basic tasks and responsibilities of the Supervisory Loan Officers and the Field Loan Officers who will be employed by the participating banks under the USAID-financed Microenterprise Finance Activity in the West Bank and Gaza are listed below. Others may be added.

Supervisory Loan Officer

The Supervisory Loan Officer (SLO) will be responsible for the following basic tasks:

1. Identify and recruit potential Field Loan Officers (FLO) for the Microenterprise Finance Activity (MFA) and serve as the principal supervisor for the FLOs. This task will involve daily communication with the FLOs regarding all aspects of their work.

2. Provide assistance to the FLOs in setting targets for new and repeat borrowers and ensure that those targets are met, with revisions upwards or downwards as necessary.

3. Ensure that portfolio performance information generated by the Management Information System (MIS) is accurate and readily available to FLOs, with particular attention to loan repayments coming due or which re delinquent. The SLO will have overall responsibility for the MIS and must ensure that all data are updated on a constant basis and that new and/or different reports are generated as the MFA grows.

4. Take the initiative to follow-up on any borrowers who have missed loan repayment, in concert with the responsible FLO. This may often require visits to the borrower's place of business.

5. Keep bank management fully apprised of portfolio performance, both in terms of current and planned activities and targets, and, in general, act as the leader of the MFA within the respective bank or branch.

6. Have prime responsibility to ensure that new loan applications are rapidly processed and that repeat loan applications are fully processed by the final payment date of the active loan.

Field Loan Officer

The Field Loan Officer (FLO) will be responsible for the following basic tasks:

1. Identify and recruit new microentrepreneurs to the MFA through direct, physical outreach in the areas assigned. The FLO shall be fully versed in both savings and loan facilities available from the bank as well as specific products available for microentrepreneurs.

2. Develop loan applications together with the microentrepreneurs, specifically adapting the loan package and conditions to the business being served.

3. Complete any required paperwork associated with loan applications, ensuring that all required documentation is submitted along with the loan applications.

4. Under the leadership of the SLO, ensure that loan applications are rapidly processed by the bank, and that issuance of the loan approval and disbursements occur in a timely manner.

5. Regularly visit with the borrowers at their places of business to ensure that loan performance is optimal. These visits give the FLO the opportunity to observe and assess any unforeseen problems that might occur during the course of the loan period, as well as giving the impression to the microentrepreneur that the bank is serious about loan repayments and collections.

6. Promote the MFA through face-to-face meetings with potential borrowers in the same neighborhood as active borrowers and through public meetings to explain the loan and savings program.

7. Make direct and immediate visits to any borrower who misses a payment and to communicate to the borrower the penalties and ramifications of delinquent payments.

8. Make suggestions to bank management, through the SLO, on ways to both improve the bank products for microenterprises and to improve the operational performance of the MFA.

ANNEX 6

DRAFT MEMORANDUM OF AGREEMENT

FOR USE WITH PARTICIPATING BANKS

This annex suggests a format and presents the principal points which should be included in the final memorandum of agreement between USAID/West Bank & Gaza and the participating banks. Decisions as to the final form of the memorandum of agreement will depend upon the results of USAID's negotiations with the banks, legal review by the USAID Regional Legal Officer and a local attorney, and review by the USAID Contracting Officer.

Format

The Memorandum of Agreement should follow the same basic format as the attached "Application for Microenterprise and Small Business Loan Portfolio Guarantee" which is used by the USAID Global Bureau for their Loan Portfolio Guarantee Program. That document contains most of the points which any USAID agreement would need to include in order to be consistent with U.S. Government laws and regulations. That document also contains related forms which could be modified to apply to the specific risk-sharing arrangement decided on by USAID/West Bank/Gaza and the participating banks. Those forms will likewise need to be revised to delete points which are not part of the specific agreement between USAID/West Bank/Gaza and the participating banks and to add other points which are not addressed by those forms.

Points to be Addressed

1. Target Clientele

All microenterprises in the WB/G will be eligible to participate in this microenterprise lending program. Microenterprises will be defined as enterprises with ten or fewer employees. Priority will be given to microenterprises enterprises with 5 or fewer employees. Program design and implementation will ensure women's access to financial services. Only established microenterprises which have been operating for more than six months will be eligible for microloans.

2. Financial Products

Short-term, working capital loans of twelve months or less will be the principal loan product offered. At least 75% of the bank's loan portfolio for the first year will consist of loans of less than \$2000 for terms averaging six months or less. Borrowers will be able to access medium-term investment capital (e.g., equipment loans with repayment periods of more than 12 months) only after satisfactorily

55

repaying at least four working capital loans. The maximum loan size will be initially set at $10,000 and the bank shall focus on loans of less than $5,000. Loan clients will be encouraged, but not required, to establish savings accounts at the banks offering microcredit. Loan and savings products will be developed which specifically address the needs and modalities of women entrepreneurs.

3. Lending Methodology

Loans will be made to individuals. Lending will be based primarily on the character and experience of the individual rather than traditional forms of collateral. Alternative and informal types of collateral, such as peer guarantees and village leader co-signers, should be encouraged. The lending program will emphasize access to future working capital credit as the principal incentive for prompt repayment of existing loans, rather than the loss of collateral. Interest rates on loans will be set high enough to cover all operational costs of the microfinance program, including the cost of funds lent, and provide for a reasonable profit. Recognizing that most loans will be for working capital, all loans should be approved or rejected within as short a period of time as possible. Repeat loans should be approved or rejected within a shorter period of time than the original loans. Loan amounts will be incrementally increased for repeat borrowers. For example, a borrower who had repaid an initial loan of $1000 for 3 months might receive a second loan of $1500 for 3 months or $2000 for 4 months. Loan officers will contact the microentrepreneurs at their place of business to offer the bank's financial products to them. Follow-up and monitoring on loans (including collections) will also be conducted at the microentrepreneur's site of business by the same loan officers responsible for the loan appraisal.

4. Commitment to Profitability of Microlending

The bank must demonstrate its commitment to the profitability of its proposed microlending program. This should be evidenced in attached loan projections drafted by the bank of initial estimates of loans numbers with rapid increases in loan numbers and volume over the first two years and in the corresponding interest rates charged to cover costs of program operations.

5. Commitment to Use of Bank Funds for Loan Capital

The bank must commit to use it's own funds for loan capital for the Activity, in accordance with the loan projections specified in item 4 above.

6. Risk-Sharing on Loan Defaults

The bank will commit to share an appropriate portion of the risk on defaulting loans. The agreement will specify the amount to be shared by USAID and the modalities for the operation of the risk-sharing, including total amounts to be funded by USAID.

7. **Autonomous Unit**

The bank shall establish an autonomous unit within the bank which will be responsible for the microlending program.

8. **Geographic Coverage**

The banks will indicate the areas which they intend to serve and identify which initial branch or branches of the banks would provide the financial services to the microenterprise clientele.

9. **Staffing and USAID Support of Initial Program Start-Up Costs**

The bank will commit to provide sufficient staff to conduct the program including Field Loan Officers and a Supervisory Loan Officer. These staff will be newly hired when the program commences in order to assure that the employees are committed to the program and its methodology and to assure that their background and experience is suitable for this new activity. USAID will specify the amount of initial program start-up costs for which it will provide support funds.

10. **USAID-Financed Technical Assistance and Training**

The agreement will specify the various types of technical assistance and training to be financed and provided by USAID to assist the bank in the establishment and implementation of the Microenterprise Finance Activity.

11. **Resident Advisor**

The bank will agree to accept the services of a Resident Advisor, to be financed by USAID, who will provide technical assistance to the bank in the establishment and implementation of the microfinance program.

12. **Office Space**

The bank will agree to provide suitable office space for the microfinance program staff and Resident Advisor, either directly in each branch bank or in a nearby office building to facilitate communication and integration within the bank's operations.

13. **Reporting**

The bank will provide quarterly and annual reports to USAID which will report on the activities of the microfinance program within the bank. A format for these reports will be developed in collaboration with the Resident Advisor and based on experience elsewhere.

UNITED STATES AGENCY FOR INTERNATIONAL DEVELOPMENT (USAID)

APPLICATION FOR MICROENTERPRISE AND SMALL BUSINESS LOAN PORTFOLIO GUARANTEE

This application is comprised of the following five parts:

PART I	Summary
PART II	Information on the Financial Institution and Guarantee Coverage
PART III	Signatures of Financial Institution
PART IV	Financial Information to be Submitted by the Financial Institution
PART V	Standard Terms and Conditions
	Annexes

Please complete Parts II, III and IV of the application (only the blue colored pages) and submit, together with the documents described in Part IV, directly to:

Credit and Investment Staff
Bureau for Global Programs, Field Support and Research
United States Agency for International Development
Room 550 SA-2
Washington, D.C. 20523-0231 U.S.A.
(Attn.: LPG Program)

Acceptance by USAID of this application shall constitute an agreement between the Financial Institution and USAID for a Microenterprise and Small Business Loan Portfolio Guarantee upon the standard terms and conditions set forth in Part V.

PART I

SUMMARY[1]

PURPOSE OF THE GUARANTEE:

The purpose of the Microenterprise and Small Business Loan Portfolio Guarantee ("Guarantee") is to assist in mobilizing credit through the formal financial sector for qualifying microenterprises and small businesses in USAID-assisted countries on the basis of a risk sharing arrangement.

GUARANTEE COVERAGE:

The Guarantee covers up to fifty percent (50%) of a Financial Institution's net loss on the principal amount of Loans (Part V, Section 10.01[g]) made to qualifying microenterprises and small businesses, up to a mutually agreed upon Guarantee Limit not to exceed US$3,000,000. The Guarantee Limit, stated in U.S. Dollars, is the maximum amount that USAID will pay in the Local Currency equivalent to a Financial Institution under the Guarantee. If, for example, a Guarantee Limit of US$1,000,000 is approved by USAID, a Financial Institution could place up to US$2,000,000, the Maximum Covered Portfolio, in Qualifying Loans under Guarantee coverage, assuming a Guarantee Percentage of 50%. In the event of losses on the principal amount of these loans, USAID would pay to the Financial Institution 50% of the amount of such losses, up to a maximum of US$1,000,000 in the Local Currency equivalent.

QUALIFYING LOANS:

A Qualifying Loan is any type of new or net additional Local Currency credit, including commercial loans, lines of credit, overdrafts, commercial letters of credit, guarantees or Financial Leases, extended by a Financial Institution to a qualifying microenterprise or small business. A Qualifying Loan may finance, with certain exceptions (Part V, Section 2.01[b]), any productive or commercial activity in the country in which the Guarantee is operative. The total principal amount of Qualifying Loan(s) made to any one Borrower may not exceed the Local Currency equivalent of US$5,000 for microenterprise loans or US$150,000 for small business loans. (See Part V, Section 2.01 (Criteria for a Qualifying Loan) for complete information pertaining to the eligibility criteria.)

TERM OF THE GUARANTEE:

The term of the Guarantee is for a maximum of five (5) years, unless earlier terminated by USAID (Part V, Sections 4.02[c], 6.03, 6.05, 9.02, 9.03 and 9.04), and is effective as of the date of the USAID Guarantee Commitment (Part V, Section 3.01). Each Guarantee Period is a six-month period, except as provided in Part V, Section 10.01[f].

---

[1]This Summary provides a brief overview of the Microenterprise and Small Business Loan Portfolio Guarantee Program. The Standard Terms and Conditions which govern the Program may be found in Part V of this Application.

59

FEES:

A standard Facility Fee equal to 1/2 of one (1) percent will be charged upon the amount of the Guarantee Limit. This is a flat, front-end fee payable no later than thirty (30) days after the date of the USAID Guarantee Commitment. A Utilization Fee will be charged upon the average amount of Qualifying Loans outstanding during each Guarantee Period and adjusted in accordance with the level of Guarantee coverage. This fee, to be agreed upon by USAID and the Financial Institution, is payable semiannually. Fees are payable in Local Currency or in U.S. Dollars at the Financial Institution's option. **Failure to pay the Facility Fee or the Utilization Fee within the applicable periods set forth in Part V, Article VI, may result in USAID termination of the Guarantee.**

CLAIMS:

The Financial Institution may submit a claim on a Qualifying Loan only when it has either: (1) certified to USAID that it has written off the entire outstanding balance (including principal and interest) of the Qualifying Loan as a bad debt expense or (2)(a) certified to USAID that it is unable, because of a legal impediment or significant impracticality, to take the action described in (1) above, and (b) certified to USAID that it has established a specific provision in its allowance for bad debts. The claim must be made no earlier than three months after the Financial Institution has made a demand for full payment upon the Borrower and no later than six months after the expiration or earlier termination of the Guarantee. Claims will be paid promptly in Local Currency by the USAID Payment Representative after USAID has approved the claim for payment. (See Part V, Article V (Claim Procedures) for further details.)

REPORTING REQUIREMENTS:

The Financial Institution must maintain a record of all Qualifying Loans placed under (and removed from) Guarantee coverage. This information is to be submitted to USAID on a quarterly basis in the form of the Qualifying Loan Schedule, be kept up-to-date and be available for review by USAID at all times. The Financial Institution must also complete a Transaction Report for each Qualifying Loan placed under Guarantee coverage. All such reports must be received by USAID/Washington, along with the Qualifying Loan Schedule and Certification, no later than 30 days after the end of each Quarter. Forms for the Qualifying Loan Schedule, Certification and Transaction Report are set forth in Part V, Annexes B, C and D. **Failure to comply with these reporting requirements may result in USAID termination of the Guarantee.**

The Financial Institution shall submit a Baseline Questionnaire describing its microenterprise and/or small business lending activities. This information must be updated yearly thereafter as of September 30, if the Financial Institution's Application is approved by USAID.
(See Part IV, Section VII).

APPLICATION PROCEDURES:

1) The Financial Institution completes and submits Parts II, III (in duplicate) and IV of the Application, together with the documents described in Part IV, to USAID.

2) Upon receipt, USAID promptly reviews the Application. USAID reserves the right to request clarification as well as additional documentation from the Financial Institution.

Cc

3) USAID then notifies the Financial Institution of its acceptance or rejection of the Application. If the Application has been accepted, USAID issues a Guarantee Commitment, which serves to formally notify the Financial Institution of certain agreed upon conditions which apply to the operation of the Guarantee. The amount of the Facility Fee and the Utilization Fee, and procedures for payment of such fees, are also stipulated in the USAID Guarantee Commitment. (See Part V, Section 3.01).

CONFIDENTIALITY:

Proprietary information disclosed by the Financial Institution in conjunction with the submission of this Application and designated as such will be treated by USAID as confidential commercial information in accordance with applicable U.S. laws.

(End of Part I)

61

PART II

INFORMATION ON THE FINANCIAL INSTITUTION AND GUARANTEE COVERAGE

FINANCIAL INSTITUTION

(To be completed by the Financial Institution)

1. Name of the Financial Institution:

____

2. Address of the Financial Institution:

____
____
____

Telephone no: ______________________________

Telex no: ______________________________

Telefax no: ______________________________

Attn.: ______________________________

3. The Financial Institution is:

(a) organized and existing under the laws of:

____

(b) organized as a (describe legal status; e.g., bank, trust company, finance company):

____
____

(c) doing (describe type of activity):

____
____
____

(Sections 4 - 9 continued on next page)

62

PART II

INFORMATION ON THE FINANCIAL INSTITUTION AND GUARANTEE COVERAGE

GUARANTEE COVERAGE

(To be selected and completed by the Financial Institution after discussions with USAID)

4. Maximum Covered Portfolio. The total principal amount of Loans (determined for each Loan by the amount of Loan commitment) that may be placed under the Guarantee at any one time is the Local Currency equivalent of: $______________________________.

5. Guarantee Percentage. The amount of coverage (percentage of Loss of Qualifying Loans) is (up to 50%): ________%

6. Guarantee Limit. The U.S. Dollar limit of the Guarantee (not to exceed $3 million) is: $______________________________. (This amount is the maximum amount that USAID will pay under the Guarantee to the Financial Institution in Local Currency equivalent, and must equal the Maximum Covered Portfolio multiplied by the Guarantee Percentage.)

7. Currency of Fee Payment. The Facility Fee and the Utilization Fee will be payable in the currency of: ______________________________

8. Loans placed under Guarantee coverage by the Financial Institution will be:

   (a) made in the Country of ______________________________

   (b) made in the Local Currency of ______________________________

9. The term of the Guarantee is _____ years from the date of the USAID Guarantee Commitment (can be for no more than five (5) years).

(End of Part II)

PART III

SIGNATURES OF THE FINANCIAL INSTITUTION
(to be completed in duplicate)

(a) **Application by the Financial Institution**

(i) **Signing Officer**

This application is made by the undersigned authorized officer of the Financial Institution, who hereby certifies on behalf of the Financial Institution that the facts stated and representations made by it in this Application are true to the best of his/her knowledge and belief and do not omit any material facts relevant to such facts stated and representation made.

Financial Institution

By: Signature ______________________ Date ____________
Name (please print) ______________________
Title (please print) ______________________

(ii) **Certifying Officer**

The undersigned officer of the Financial Institution hereby certifies that the individual signing above is the said duly qualified and acting officer of the Financial Institution having full power and authorization to make this application on behalf of the Financial Institution.

By: Signature ______________________ Date ____________
Name (please print) ______________________
Title (please print) ______________________

(b) **Acceptance by USAID:** Upon acceptance by USAID, which is made by the USAID Guarantee Commitment (Part V, Section 3.01), this application shall constitute an agreement by the Financial Institution and USAID upon the Standard Terms and Conditions set forth in Part V hereof.

(c) **Required Statement:** USAID has advised the Financial Institution that U.S. law governing the issuance of a USAID guarantee requires the recipient of a guarantee, or any person under consideration for receipt of a guarantee, to make and file a statement regarding the use or non-use of influence in obtaining the guarantee. Accordingly, the Financial Institution makes and subscribes to the following statement by signing above:

If any funds have been paid or will be paid by the Financial Institution to any person for influencing or attempting to influence an officer or employee of any agency, a member of the United States Congress, an officer or employee of Congress, or an employee of a Member of Congress in connection with a commitment providing for USAID to guarantee a loan, the Financial Institution shall complete and submit Standard Form-LLL "Disclosure Form to Report Lobbying," in accordance with its instructions.

Submission of this statement is a prerequisite for making or entering into this transaction imposed by Section 1352, Title 31, U.S. Code. Any person who fails to file the required statement shall be subject to a civil penalty of not less than $10,000 and not more than $100,000 for each such failure.

64

PART III

SIGNATURES OF THE FINANCIAL INSTITUTION
(to be completed in duplicate)

(a) **Application by the Financial Institution**

(i) **Signing Officer**

This application is made by the undersigned authorized officer of the Financial Institution, who hereby certifies on behalf of the Financial Institution that the facts stated and representations made by it in this Application are true to the best of his/her knowledge and belief and do not omit any material facts relevant to such facts stated and representation made.

Financial Institution

By: Signature ______________________ Date ____________
Name (please print) ______________________
Title (please print) ______________________

(ii) **Certifying Officer**

The undersigned officer of the Financial Institution hereby certifies that the individual signing above is the said duly qualified and acting officer of the Financial Institution having full power and authorization to make this application on behalf of the Financial Institution.

By: Signature ______________________ Date ____________
Name (please print) ______________________
Title (please print) ______________________

(b) **Acceptance by USAID:** Upon acceptance by USAID, which is made by the USAID Guarantee Commitment (Part V, Section 3.01), this application shall constitute an agreement by the Financial Institution and USAID upon the Standard Terms and Conditions set forth in Part V hereof.

(c) **Required Statement:** USAID has advised the Financial Institution that U.S. law governing the issuance of an USAID guarantee requires the recipient of a guarantee, or any person under consideration for receipt of a guarantee, to make and file a statement regarding the use or non-use of influence in obtaining the guarantee. Accordingly, the Financial Institution makes and subscribes to the following statement by signing above:

If any funds have been paid or will be paid by the Financial Institution to any person for influencing or attempting to influence an officer or employee of any agency, a member of the United States Congress, an officer or employee of Congress, or an employee of a Member of Congress in connection with a commitment providing for USAID to guarantee a loan, the Financial Institution shall complete and submit Standard Form-LLL "Disclosure Form to Report Lobbying," in accordance with its instructions.

Submission of this statement is a prerequisite for making or entering into this transaction imposed by Section 1352, Title 31, U.S. Code. Any person who fails to file the required statement shall be subject to a civil penalty of not less than $10,000 and not more than $100,000 for each such failure.

65

PART IV
DOCUMENTS TO BE SUBMITTED BY THE FINANCIAL INSTITUTION

I. Documents/Information.

A. Articles of Incorporation.

B. Annual audited statements, with footnotes, for the preceding three (or available) years. Annual reports are acceptable if they include audited statements with footnotes.

C. i. List of registered owners (by name and percentage of ownership),
ii. List of registered owners which are local or foreign governments (by name and percentage of ownership), and
iii. List of principal officers and directors.

D. A copy of standard financial lease agreement, including clauses covering purchase option arrangements and similar terms, if leases are to be included under the USAID Guarantee.

II. Asset Quality (amounts shown must agree to audited financial statements or a reconciliation to audited statements must be provided).

A. Provide approximate percentage of the Loan portfolio ("Loan" is defined in Part V (Standard Terms and Conditions), Section 10.01[g]) by type as follows:

Amortizing (scheduled payments of principal and interest)	____%
Demand (scheduled payments of interest only)	____%
Authorized Overdrafts	____%
Other (describe)	____%
Total	100%

B. Schedule of past due loans (as defined on page IV-4 as of financial year-end for the past three years). If a period other than 30 days is used by your institution, please state the period used, (i.e., 60 days, 120 days, 6 months): ____________________

Year	19__	19__	19__
Balance Outstanding of Past Due Loans			
Total Outstanding Loans (per audited statements)			

C. Schedule of non-performing loans (as defined on page IV-4 as of financial year-end for the past three years). If a period other than 90 days is used by your institution, please state the period used, (i.e., 180 days, 9 months): ____________________

Year	19__	19__	19__
Balance Outstanding of Non-Performing Loans			
Total Outstanding Loans (per audited statements)			

66

NOTE: If records are only kept for past due or non-performing loans, but not both, only the appropriate schedule (B or C above) need be completed. If a definition is used other than the definitions provided at the end of this form, describe it in detail.

D. Describe policy for Provisions for Bad Debts, including any quantitative guidelines used and explain role, if any, of external auditor and/or supervisory authority.

E. Describe method of provisioning indicating a) if loans are written off against a previously established provision (general provisions) or b) if specific provisions against loans are provided for, but not written off, when judged uncollectible or if both methods are used.

F. Schedule of General Provisions, as of financial year-end for the past three years, with totals agreeing to audited statements.

Year	19__	19__	19_
Beginning Balance			
Transfer to the Provision			
Gross Charge-offs			
Other Entries (describe)			
Ending Balance			

G. Schedule of Specific Provisions, as of financial year-end for the past three years, with totals agreeing to audited statements.

Year	19__	19__	19__
Beginning Balance			
Increases in Specific Provisions			
Decreases in Provision (improved)			
Other Entries (describe)			
Ending Balance			

H. Describe policies with regard to suspension of interest and/or non-accrual of interest including quantitative guidelines, if any, with regard to loans in arrears and what requirements, if any, are mandated by the supervisory authority.

I. Schedule of contingent liabilities and other off-balance-sheet items, as of latest audited year-end:

1. Direct Credit Substitutes (guarantees, standby letters of credit, acceptances not on balance sheet, etc.)	
2. Transaction Related Contingent Items (performance bonds, bid bonds, warranties, etc.)	
3. Self-liquidating/Trade Related Items (documentary credits, commercial letters of credit)	
4. Formal Credit Commitments	
5. Other Significant Off-Balance Sheet Items (describe)	

III. Capital Adequacy

A. Describe capital requirements, either statutory or regulatory, for your type of financial institution (bank, finance or leasing company, etc.).

B. Schedule of capital elements (as of latest financial year-end).

Core Capital:

Paid-in Shares (common stock)	
Share Premiums (surplus)	
Statutory Reserves	
Retained Profits	
Total Core Capital	

Supplementary Capital:

Undisclosed Reserves (approved by supervisory authority)	
Asset Reevaluation Reserves	
Unencumbered General Provisions	
Other (describe)	
Total Supplementary Capital	

68

IV. Profitability

Schedule of income and expense as of financial year-end, past three years (with totals agreeing to audited statements).

Year	19	19	19
Interest Income			
Interest Expense			
Provisions for Bad Debts			
Non-interest Income			
Non-interest Expense			
Extraordinary Items (describe)			
Pre-tax Income			
Taxation			
Net Income			
Dividends			

V. Liquidity

A. Specifically describe mandatory liquidity ratios or other liquidity requirements, either statutory or regulatory, imposed by the supervisory authority for your class of financial institution.

B. Describe internal policies, guidelines, and/or specific ratios used by management to ensure sufficient liquidity.

VI. Microenterprise and Small Business Lending

A. Provide a brief statement of current credit policy for lending to microenterprises and/or small businesses.

B. Indicate whether you have a small business and/or microenterprise lending unit. If so, please provide a description of such unit, including matters such as staffing and procedures.

C. Provide a description of microenterprises and/or small business loans presently extended, including:

Definition of microenterprise and/or small business;
Total number of loans;
Number of loans made to women;
Value of the loans in local currency; and,
General description of business of borrowers by sector.

69

D. Provide a projection of the microenterprise and/or small business loans to be made under the guarantee, including:

a general description;
number of loans; and,
value of the loans in local currency.

E. Provide a statement of your standard collection procedures.

F. Provide a statement of your loan loss reserve policy.

G. Provide a statement of your bad debt write-off policy.

Definitions

The following World Bank definitions of "past due" and "non-performing" contain elements now widely used in many banking systems.

Past due (Overdue). Loans (as defined in Part V (Standard Terms and Conditions), Section 10.01[g]) are considered to be past due when: a) principal or interest is due and unpaid for 30 days or more; or b) interest payments equal to 30 days interest or more have been capitalized, refinanced, or rolled-over. Overdrafts and other credit extensions with pre-established repayment programs are considered past due when any of the following conditions exist: a) advances exceed the customer's borrowing line for 30 consecutive days or more; b) the customer's borrowing line has expired for 30 days or more; c) interest is due and unpaid for 30 days or more; or d) the account has been inactive for 30 days and deposits are insufficient to cover the interest capitalized during the period. The principal balance outstanding (and not the amount of delinquent payments) is used in calculating the aggregate amount of past due obligations.

Non-performing means that an asset is not generating income. Loans or advances (and potentially other assets) are considered to be non-performing when: a) principal or interest is due and unpaid for 90 days or more; or b) interest payments equal to 90 days or more have been capitalized, refinanced, or rolled-over. Overdrafts or other credit extensions without pre-established repayment programs are considered non-performing when any of the following conditions exist: a) advances exceed the customer's borrowing line for 90 consecutive days or more; b) the customer's borrowing line has expired for 90 days or more; c) interest is due and unpaid for 90 days or more; or d) the account has been inactive for 90 days and deposit are insufficient to cover the interest capitalized during the period. The principal balance outstanding (and not the delinquent payments) is used in calculating the aggregate amount of non-performing obligations.

VII. Baseline Questionnaire

Attached are two (2) Baseline Questionnaires, one of which is to be completed by the Financial Institution when applying for the Loan Portfolio Guarantee, and yearly thereafter (September 30). Please select the Baseline form relevant to the type of Guarantee being requested. Form (a) is for a Microenterprise facility. Form (b) is for a small business facility.

70

Form (a) - MICROENTERPRISE BASELINE DATA QUESTIONNAIRE

Bank Name: Country:

Name of Preparer: Title of Preparer: Date:

---

1. How many branches (please circle one) are/will be using the Guarantee?

2. What is your definition of a "Microenterprise?"

3. Does your Bank have a microenterprise lending program? _____Yes _____No

   If yes, how long has the program been in existence?

   How many employees work on the microlending program?

4. What is the size of your microenterprise loan portfolio[1], including loans made with and without the guarantee?

	Current Year	Last Year	Two Years
Number of Loans			
Total Amount of Loans (in local currency)			

5. How many loans in your microenterprise loan portfolio have been made to women-owned businesses and what is the total amount of these loans?

	Current Year	Last Year	Two Years
Number of Loans			
Total Amount of Loans (in local currency)			

6. For your current portfolio, specify the average term (loan life) for amortizing microenterprise loans: ______

   In percentage terms, what portion of the micro-loan portfolio is comprised of:

   Term Loans ____________
   Revolving Credits ____________

7. In percentage terms, what is your average collateral requirement relative to loan value?

   Microenterprise Business Loans ____________
   Loans to Larger Borrowers ____________

8. Do you use cash flow analysis when calculating the borrower's ability to repay the loan?
   _____Yes _____No

[1] Microenterprise loans are defined as less than the local currency equivalent of US$ 5,000.

71

Form (b) - SMALL BUSINESS BASELINE DATA QUESTIONNAIRE

Bank Name: Country:

Name of Preparer: Title of Preparer: Date:

---

1. How many branches (please circle one) are/will be using the Guarantee?

2. What is your definition of a "small business?"

3. Does your Bank have a small business lending program? ____Yes ____No

   If yes, how long has the program been in existence?

   How many employees work on the small business lending program?

4. What is the size of your small business loan portfolio[1], including loans made with and without the guarantee?

	Current Year	Last Year	Two Years
Number of Loans			
Total Amount of Loans (in local currency)			

5. How many loans in your small business loan portfolio have been made to women-owned businesses and what is the total amount of these loans?

	Current Year	Last Year	Two Years
Number of Loans			
Total Amount of Loans (in local currency)			

6. For your current portfolio, specify the average term (loan life) for amortizing small business loans: ________

   In percentage terms, what portion of the small business loan portfolio is comprised of:

   Term Loans ____________
   Revolving Credits ____________

7. In percentage terms, what is your average collateral requirement relative to loan value?

   Small Business Loans ____________
   Loans to Larger Businesses ____________

8. Do you use cash flow analysis when calculating the borrower's ability to repay the loan?
   ____Yes ____No

[1] Small Business Loans are defined as loans not exceeding the local currency equivalent of US$ 150,000, to borrowers whose assets (excluding land, business and equipment) are less than the local currency equivalent of US$250,000.

12

PART V
STANDARD TERMS AND CONDITIONS

These Standard Terms and Conditions are part of an agreement for a Microenterprise and Small Business Loan Portfolio Guarantee ("Guarantee") made and entered into by and between USAID and the Financial Institution by application of the Financial Institution for a Microenterprise and Small Business Loan Portfolio Guarantee (the "Application") and acceptance of the Application by USAID

ARTICLE I
The Guarantee

Section 1.01. The Guarantee. Subject to these Standard Terms and Conditions, USAID shall pay to the Financial Institution an amount in Local Currency equal to the Guarantee Percentage of the loss of principal incurred by the Financial Institution on Qualifying Loans, as defined in Article II, up to the Guarantee Limit.

ARTICLE II
Qualifying Loans

Section 2.01. Criteria for a Qualifying Loan. A Qualifying Loan is a Loan (see Section 10.01[g]) granted by the Financial Institution to a Borrower that meets all of the following criteria:

[a] The Borrower must meet all of the following criteria:

[1] If the Borrower is an individual, the Borrower must be a national or permanent resident of the Country (Part II, Section 8). If the Borrower is a corporation or other business entity, it must be majority-owned by [i] nationals or permanent residents of the Country and/or [ii] corporations or other business entities that are owned by such nationals or residents;

[2] the Borrower must be 100% privately owned, controlled and operated;

[3] the Borrower's principal place of business must be in the Country;

[4] the Borrower must be a "microenterprise" for that portion of the Guarantee Portfolio allocated to loans to microenterprises, or a "small business enterprise" for that portion of the Guarantee Portfolio allocated to loans to small business enterprises as defined by USAID in the USAID Guarantee Commitment, (Section 3.01) or as otherwise agreed to in writing by USAID and the Financial Institution.

[b] The Loan may finance any private productive or commercial activity conducted principally in the Country, and which is legal in the Country, excluding the following:

[1] the production, processing or marketing of sugar, palm oil, cotton, or citrus for export;

[2] the purchase, manufacture, importation, distribution or application of pesticides;

[3] the production, processing or marketing of luxury goods, including such items as gambling equipment, alcoholic beverages, jewelry, and furs;

[4] activities related to abortion or involuntary sterilization;

[5] police, other law enforcement, or military activities;

74

[6] the production, processing or marketing of materials for explosives, surveillance equipment, or weather modification equipment;

[7] any activity which would result in any significant loss of tropical forests or involve the extraction of commercial timber in primary tropical forests;

[8] the purchase of goods or services which are shipped from or produced in Brazil, Cuba, Iraq, Iran, Liberia, Libya, Nigeria, Serbia, Somalia, Sudan, The Gambia, North Korea, People's Republic of China, Syria, and Vietnam (as such list of countries may be amended from time to time by written notice from USAID to the Financial Institution, provided, however, that no such notice shall be effective with respect to any Loan made by the Financial Institution prior to such notice), or are produced by corporations or other entities that are more than fifty percent (50%) owned by nationals or permanent residents, or Governmental Authorities, of those countries;

[9] an activity reasonably likely to involve the relocation or expansion outside of the United States of an enterprise located in the United States if non-U.S. production in such relocation or expansion replaces some or all of the production of, and reduces the number of employees at, said enterprise in the United States; and

[10] an activity the purpose of which is the establishment or development of any export processing zone or designated area where the labor, environmental, tax, tariff, and safety laws of the country would not apply, without the prior written approval of USAID.

[c] The Loan may not finance the purchase or lease of motor vehicles manufactured outside the United States.

[d] The total principal amount of Loans to any one Borrower outstanding at any one time under Guarantee coverage (Section 4.01) may not exceed the Local Currency equivalent -- calculated at the Exchange Rate determined by the Financial Institution at the time the Loans are made -- of [1] Five Thousand U.S. Dollars ($5,000) for the portion of the Guarantee Portfolio allocated to microenterprise loans, or [2] One Hundred Fifty Thousand U.S. Dollars ($150,000) for the portion of the Guarantee Portfolio allocated to small business enterprise loans, or such other U.S. Dollar amount as may be specified by USAID in the USAID Guarantee Commitment (Section 3.01), or as may be otherwise agreed to in writing by USAID and the Financial Institution.

[e] If the Borrower is an existing customer of the Financial Institution, the Loan must be additional to the credit already being provided by the Financial Institution and must not be a renewal or extension of a pre-existing Loan.

[f] The Loan must be made at a market rate of interest, and no portion of the Loan may be financed, directly or indirectly, with subsidized funds.

[g] At least fifty percent (50%) of the commercial risk of the Loan must be retained by the Financial Institution at all times, and no portion of the Loan may be guaranteed by a Governmental Authority or a donor organization (other than USAID), provided, however, that this subsection [g] shall not apply to conventional forms of collateral or guarantees obtained by the Financial Institution for the Loan.

[h] The Loan must be placed under Guarantee coverage (Section 4.01) within ten (10) business days after the Loan has been disbursed (for term loans) or approved (for lines of credit and all other credit facilities). A Loan may be removed from Guarantee coverage, but no Loan once removed from Guarantee coverage may thereafter be placed again under Guarantee coverage without the written consent of USAID.

[i] The total principal amount of Loans outstanding under Guarantee coverage at any one time -- calculated at the Exchange Rate determined by the Financial Institution at such time -- shall not exceed the Maximum Covered Portfolio (Part II, Section 4), and no new Loans shall be placed under Guarantee coverage when the total principal amount of Loans then outstanding under Guarantee coverage exceeds the Maximum Covered Portfolio.

Section 2.02. Repayment. The Financial Institution shall have no right to obtain payment under the Guarantee with respect to any Loan that is not a Qualifying Loan in compliance with Section 2.01. If the Financial Institution obtains payment under the Guarantee for a non-complying Loan, the Financial Institution shall be immediately liable to repay to USAID the full amount of the payment obtained plus interest accruing from the date of the payment at the rate of one percent (1%) per month, or at the maximum legal lending rate per month in the Country, whichever is less.

ARTICLE III
Acceptance

Section 3.01. Acceptance of the Application: USAID Guarantee Commitment. The Guarantee shall have no force and effect until USAID accepts the Application made by the Financial Institution. Acceptance by USAID shall be made by a written notice from USAID substantially in the form of Annex A ("USAID Guarantee Commitment") and signed by an authorized officer of USAID. The USAID Guarantee Commitment serves to formally notify the Financial Institution of certain agreed upon conditions which apply to the operation of the Guarantee. USAID shall have the right, at its sole discretion, to accept or reject the Application. USAID may request further documentation from the Financial Institution prior to accepting or rejecting the Application. The Guarantee shall become effective as of the date of the USAID Guarantee Commitment ("Effective Date").

ARTICLE IV
Guarantee Coverage, Reporting

Section 4.01. Guarantee Coverage. The Financial Institution shall place a Qualifying Loan under Guarantee coverage by [a] making appropriate entries on the Qualifying Loan Schedule (Annex B to these Standard Terms and Conditions), which shall be kept up to date at all times, and by [b] completing a Transaction Report for such Loan (Annex D to these Standard Terms and Conditions). The Financial Institution shall remove a Qualifying Loan from Guarantee coverage by making appropriate entries on the Qualifying Loan Schedule. A Qualifying Loan placed under Guarantee coverage shall remain under Guarantee coverage unless removed from Guarantee coverage or, as provided in Article IX hereof, until the expiration or earlier termination of the term of the Guarantee.

Section 4.02. Reporting.

[A] Quarterly Reporting. No later than thirty (30) days after the end of each Quarter, USAID/Washington must receive from the Financial Institution {1} a copy of the Qualifying Loan Schedule in effect on the last day of the Quarter just ended, completed in accordance with the instructions provided therein, together with a Certification in the form of Annex C to these Standard Terms and Conditions, and {2} a completed Transaction Report in the form of Annex D to these Standard Terms and Conditions for each Qualifying Loan entered into during such Quarter. If the required information is submitted to USAID/Washington within the applicable period by facsimile transmission, the Financial Institution must also provide the original documentation to USAID/Washington in due course.

[B] Annual Reporting. No later than one hundred eighty (180) days after the end of its fiscal year, the Financial Institution shall submit to USAID audited annual financial statements including, or together with, the information requested in Sections II(A), II(B), II(C), II(F), II(G), II(I),

16

III(B), AND SECTION IV AND VII OF PART IV OF THE APPLICATION.

[C] FAILURE TO PROVIDE REQUIRED REPORTS. IF THE FINANCIAL INSTITUTION SHOULD FAIL TO PROVIDE THE REQUIRED REPORTS TO USAID WITHIN THE APPLICABLE PERIOD, THE GUARANTEE SHALL TERMINATE AS OF THE COMMENCEMENT OF THE IMMEDIATELY PRECEDING GUARANTEE PERIOD, UNLESS USAID AND THE FINANCIAL INSTITUTION AGREE OTHERWISE IN WRITING.

ARTICLE V
CLAIM PROCEDURES

SECTION 5.01. CLAIM REQUIREMENTS. NO CLAIM ON A QUALIFYING LOAN MAY BE SUBMITTED TO USAID UNLESS ALL OF THE FOLLOWING REQUIREMENTS ARE MET:

[A] AS A CONSEQUENCE OF THE BORROWER'S DEFAULT, THE TOTAL OUTSTANDING PRINCIPAL OF THE QUALIFYING LOAN HAS BECOME IMMEDIATELY DUE AND PAYABLE, AND THE FINANCIAL INSTITUTION HAS MADE A DEMAND UPON THE DEFAULTING BORROWER FOR FULL PAYMENT OF ALL AMOUNTS DUE.

[B] THE FINANCIAL INSTITUTION HAS PURSUED ALL REASONABLE AND DILIGENT COLLECTION EFFORTS AGAINST THE BORROWER (AND ANY OTHER PERSON THAT MAY BE LIABLE ON THE QUALIFYING LOAN) TO MAKE FULL PAYMENT OF ALL AMOUNTS DUE.

[C] AFTER SUCH COLLECTION ACTIVITIES, THE FINANCIAL INSTITUTION HAS EITHER {1} CERTIFIED TO USAID THAT IT HAS WRITTEN OFF THE ENTIRE OUTSTANDING BALANCE (INCLUDING PRINCIPAL AND INTEREST) OF THE QUALIFYING LOAN AS A BAD DEBT EXPENSE; OR {2} CERTIFIED TO USAID THAT IT {A} IS UNABLE, BECAUSE OF A LEGAL IMPEDIMENT OR SIGNIFICANT IMPRACTICALITY, TO TAKE THE ACTION DESCRIBED IN {1} ABOVE, AND {B} HAS ESTABLISHED A SPECIFIC PROVISION FOR POSSIBLE LOAN LOSSES.

[D] THE CLAIM HAS BEEN SUBMITTED TO USAID NO EARLIER THAN THREE (3) MONTHS AFTER THE FINANCIAL INSTITUTION'S DEMAND FOR FULL PAYMENT, AS REQUIRED BY SUBSECTION [A] OF THIS SECTION, AND NO LATER THAN SIX (6) MONTHS AFTER THE EXPIRATION OR EARLIER TERMINATION OF THE GUARANTEE, PROVIDED, HOWEVER, THAT NO CLAIM MAY BE SUBMITTED TO USAID IF THE DATE OF THE FINANCIAL INSTITUTION'S DEMAND FOR FULL PAYMENT UNDER SUBSECTION [A] OF THIS SECTION OCCURS AFTER THE EXPIRATION OR EARLIER TERMINATION OF THE GUARANTEE.

SECTION 5.02. SUBMISSION OF CLAIM. THE FINANCIAL INSTITUTION SHALL MAKE A CLAIM BY SUBMITTING TO USAID FOR EACH QUALIFYING LOAN A LETTER IN THE FORM OF ANNEX E.

SECTION 5.03. APPROVAL OF CLAIM FOR PAYMENT. THE FINANCIAL INSTITUTION SHALL NOT BE ENTITLED TO PAYMENT ON A CLAIM UNTIL USAID APPROVES THE CLAIM FOR PAYMENT BASED ON ITS REVIEW OF THE CLAIM AS SUBMITTED. USAID RESERVES THE RIGHT TO REQUEST CLARIFICATION OF AND FURTHER DOCUMENTATION ON ANY CLAIM SUBMITTED FOR PURPOSE OF APPROVING A CLAIM FOR PAYMENT.

SECTION 5.04. PAYMENT OF CLAIM. UPON APPROVAL OF A CLAIM FOR PAYMENT, USAID SHALL ADVISE THE USAID PAYMENT REPRESENTATIVE TO PAY TO THE FINANCIAL INSTITUTION THE APPROVED AMOUNT OF THE CLAIM IN LOCAL CURRENCY. USAID SHALL GIVE THE FINANCIAL INSTITUTION WRITTEN NOTICE THAT SUCH PAYMENT ADVICE HAS BEEN GIVEN. USAID SHALL HAVE THE RIGHT TO WITHHOLD PAYMENT OF AN APPROVED CLAIM AMOUNT IF ANY GUARANTEE FEES AND ANY OTHER AMOUNTS HEREUNDER ARE DUE AND OWING TO USAID.

SECTION 5.05. LIMITATION ON CLAIM PAYMENTS. THE TOTAL AMOUNT OF ALL PAYMENTS ON CLAIMS DURING THE TERM, OR ANY RENEWAL TERM, OF THE GUARANTEE (ARTICLE IX) SHALL IN NO EVENT EXCEED THE GUARANTEE LIMIT. FOR THESE PURPOSES, U.S. DOLLAR EQUIVALENTS SHALL BE CALCULATED AT THE EXCHANGE RATE IN EFFECT ON THE DATE OF EACH PAYMENT, AS DETERMINED BY USAID.

11

ARTICLE VI
FEES

SECTION 6.01. GUARANTEE FEES. IN CONSIDERATION FOR THE GUARANTEE, THE FINANCIAL INSTITUTION SHALL PAY TO USAID:

[A] THE FACILITY FEE; AND
[B] THE UTILIZATION FEE.

SECTION 6.02. FACILITY FEE. USAID SHALL CALCULATE A STANDARD FACILITY FEE EQUAL TO 1/2 OF ONE (1) PERCENT UPON THE AMOUNT OF THE GUARANTEE LIMIT, AND SHALL SPECIFY THE AMOUNT OF THE FACILITY FEE IN THE USAID GUARANTEE COMMITMENT (SECTION 3.01). THE FACILITY FEE SHALL BE PAYABLE NO LATER THAN THIRTY (30) DAYS AFTER THE DATE OF THE USAID GUARANTEE COMMITMENT.

SECTION 6.03. FAILURE TO PAY FACILITY FEE. IF THE FINANCIAL INSTITUTION SHOULD FAIL TO PAY THE FACILITY FEE WITHIN THE APPLICABLE PERIOD, THE GUARANTEE SHALL TERMINATE AS OF THE EFFECTIVE DATE (SECTION 3.01).

SECTION 6.04. UTILIZATION FEE. AFTER REVIEW OF THE QUALIFYING LOAN SCHEDULE FOR THE GUARANTEE PERIOD LAST ENDED, USAID SHALL CALCULATE A UTILIZATION FEE BASED UPON THE AVERAGE AMOUNT OF QUALIFYING LOANS OUTSTANDING DURING SUCH GUARANTEE PERIOD AND ADJUSTED IN ACCORDANCE WITH THE LEVEL OF GUARANTEE COVERAGE. FOR PURPOSES OF CALCULATING THE AVERAGE U.S. DOLLAR VALUE OF QUALIFYING LOANS OUTSTANDING IN THAT PERIOD, THE EXCHANGE RATE DETERMINED BY USAID SHALL BE USED. USAID SHALL SPECIFY THE UTILIZATION FEE DUE FOR SUCH ENDED GUARANTEE PERIOD IN A WRITTEN NOTICE TO THE FINANCIAL INSTITUTION. THE UTILIZATION FEE SHALL BE PAYABLE NO LATER THAN THIRTY (30) DAYS AFTER THE DATE OF SUCH NOTICE. USAID MAY CHARGE A UTILIZATION FEE FOR EACH GUARANTEE PERIOD OCCURRING DURING THE INITIAL AND ANY RENEWAL TERMS OF THE GUARANTEE.

SECTION 6.05. FAILURE TO PAY UTILIZATION FEE. IF THE FINANCIAL INSTITUTION SHOULD FAIL TO PAY THE UTILIZATION FEE FOR ANY ENDED GUARANTEE PERIOD NO LATER THAN THE APPLICABLE THIRTY (30) DAY PERIOD, THE GUARANTEE SHALL TERMINATE AS OF THE COMMENCEMENT OF THAT GUARANTEE PERIOD, UNLESS USAID AND THE FINANCIAL INSTITUTION AGREE OTHERWISE IN WRITING.

SECTION 6.06. MANNER OF PAYMENT. ALL PAYMENTS OF AMOUNTS OWING TO USAID UNDER THE GUARANTEE SHALL BE STATED IN U.S. DOLLARS, AND PAYABLE IN THE CURRENCY OF FEE PAYMENT (PART II, SECTION 7). IF PAYABLE IN LOCAL CURRENCY, PAYMENT SHALL BE IN AN EQUIVALENT AMOUNT OF LOCAL CURRENCY CALCULATED AT THE EXCHANGE RATE DETERMINED BY USAID. PAYMENTS SHALL BE MADE TO THE USAID PAYMENT REPRESENTATIVE IN THE MANNER SPECIFIED BY USAID IN THE USAID GUARANTEE COMMITMENT (SECTION 3.01). THE FINANCIAL INSTITUTION SHALL PROMPTLY NOTIFY USAID OF SUCH PAYMENTS (E.G., BY TELEFAX) AFTER EACH SUCH PAYMENT IS MADE.

ARTICLE VII
REPRESENTATIONS, WARRANTIES, COVENANTS

THE FINANCIAL INSTITUTION HEREBY REPRESENTS AND WARRANTS AS FOLLOWS:

SECTION 7.01. ORGANIZATION, EXISTENCE. THE FINANCIAL INSTITUTION IS A CORPORATION OR OTHER INSTITUTION DULY ORGANIZED AND VALIDLY EXISTING WHERE INCORPORATED OR CHARTERED, AND HAS FULL POWER, AUTHORITY AND LEGAL RIGHT TO CARRY OUT ITS BUSINESS AS CURRENTLY CONDUCTED, TO EXECUTE, DELIVER AND PERFORM THIS GUARANTEE AND ALL OTHER DOCUMENTS WHICH THIS GUARANTEE CONTEMPLATES WILL BE EXECUTED BY THE FINANCIAL INSTITUTION.

SECTION 7.02. AUTHORIZATION, BINDING EFFECT. THE EXECUTION, DELIVERY AND PERFORMANCE BY THE FINANCIAL INSTITUTION OF THIS GUARANTEE HAVE BEEN DULY AUTHORIZED BY ALL NECESSARY ACTION OF THE FINANCIAL INSTITUTION, AND THIS GUARANTEE CONSTITUTES A LEGAL, VALID AND BINDING OBLIGATION OF THE FINANCIAL INSTITUTION ENFORCEABLE IN ACCORDANCE WITH ITS TERMS.

SECTION 7.03. GOVERNMENTAL APPROVALS, ETC. NO APPROVAL, PERMIT, LICENSE, AUTHORIZATION, CERTIFICATE OR CONSENT OF ANY GOVERNMENTAL AUTHORITY IS REQUIRED FOR THE FINANCIAL INSTITUTION TO ENTER INTO THIS GUARANTEE, EXCEPT SUCH AS HAVE BEEN HERETOFORE OBTAINED AND ARE IN FULL FORCE AND EFFECT.

SECTION 7.04. FACTS AND CIRCUMSTANCES. THE FACTS AND CIRCUMSTANCES OF WHICH THE FINANCIAL INSTITUTION HAS INFORMED USAID, OR CAUSED USAID TO BE INFORMED, IN THE APPLICATION OR OTHERWISE IN THE COURSE OF REACHING AGREEMENT WITH USAID ON THIS GUARANTEE, ARE ACCURATE AND COMPLETE, AND INCLUDE ALL FACTS AND CIRCUMSTANCES (INCLUDING ANY ACTIONS, PROCEEDINGS, INVESTIGATIONS OR CLAIMS AGAINST OR AFFECTING THE FINANCIAL INSTITUTION NOW PENDING BEFORE ANY COURT, ARBITRATOR OR GOVERNMENTAL AUTHORITY) THAT MIGHT MATERIALLY AFFECT THE GUARANTEE AND THE DISCHARGE OF THE FINANCIAL INSTITUTION'S OBLIGATIONS UNDER THIS GUARANTEE.

SECTION 7.05. FURTHER DISCLOSURE. THE FINANCIAL INSTITUTION SHALL INFORM USAID IN A TIMELY MANNER OF ANY SUBSEQUENT FACTS AND CIRCUMSTANCES THAT MIGHT MATERIALLY AFFECT THE GUARANTEE OR THE FINANCIAL INSTITUTION'S DISCHARGE OF ITS OBLIGATIONS UNDER THE GUARANTEE, OR THE TRUTH AND ACCURACY OF ANY OF THE REPRESENTATIONS MADE IN SECTIONS 7.01 THROUGH 7.04 HEREOF.

SECTION 7.06. RECORDS, INSPECTIONS AND AUDIT. THE FINANCIAL INSTITUTION SHALL

[A] MAINTAIN OR CAUSE TO BE MAINTAINED, IN ACCORDANCE WITH GENERALLY ACCEPTED ACCOUNTING PRINCIPLES AND PRACTICES CONSISTENTLY APPLIED, BOOKS AND RECORDS RELATING TO THIS GUARANTEE, ADEQUATE TO SHOW THE FINANCIAL INSTITUTION'S COMPLIANCE WITH THESE STANDARD TERMS AND CONDITIONS. SUCH BOOKS AND RECORDS WILL BE AUDITED REGULARLY IN ACCORDANCE WITH GENERALLY ACCEPTED AUDITING STANDARDS, AND MUST BE MAINTAINED (EXCEPT AS USAID MAY OTHERWISE AGREE IN WRITING) UNTIL THREE YEARS AFTER THE EXPIRATION OR TERMINATION OF THE GUARANTEE;

[B] AFFORD AUTHORIZED REPRESENTATIVES OF USAID THE OPPORTUNITY AT ALL REASONABLE TIMES TO INSPECT THE FINANCIAL INSTITUTION'S BOOKS, RECORDS, AND OTHER DOCUMENTS (INCLUDING, BUT NOT LIMITED TO, THE ORIGINAL QUALIFYING LOAN SCHEDULE AND ANY BORROWERS' FILES) RELATING TO THE GUARANTEE TO VERIFY THAT LOANS SUBJECT TO GUARANTEE COVERAGE ARE BEING MADE AND RECOVERIES PURSUED AND APPLIED IN ACCORDANCE WITH THESE STANDARD TERMS AND CONDITIONS; AND

[C] PROMPTLY PROVIDE SUCH OTHER INFORMATION AND REPORTS AS USAID MAY REASONABLY REQUEST.

SECTION 7.07. COMPLETE RESPONSIBILITY OF THE FINANCIAL INSTITUTION FOR TAXES. THE FINANCIAL INSTITUTION SHALL PAY ALL TAXES, IN WHATEVER FORM AND HOWSOEVER IMPOSED, INCLUDING ANY INTEREST AND PENALTIES, IF ANY, ON OR WITH RESPECT TO THE GUARANTEE, AND SHALL INDEMNIFY USAID AGAINST ANY SUCH TAXES THAT MAY BE IMPOSED UPON USAID IN CONNECTION THEREWITH. PAYMENTS OF ALL AMOUNTS HEREUNDER SHALL BE MADE FREE AND CLEAR OF AND WITHOUT REDUCTION FOR SUCH TAXES.

SECTION 7.08. RECOVERIES.

[A] [1] ALL RECOVERIES FROM THE DEFAULTING BORROWER FROM ANY SOURCE (INCLUDING THOSE RELATING TO THE QUALIFYING LOAN AND TO ANY OTHER LOAN MADE TO THE BORROWER BUT NOT COVERED BY THE GUARANTEE) RECEIVED BY THE FINANCIAL INSTITUTION AFTER THE DATE OF ITS CLAIM SHALL BE APPLIED, FIRST, TO REIMBURSE THE FINANCIAL INSTITUTION FOR ACTUAL AND REASONABLE EXPENSES INCURRED IN CONNECTION WITH ITS COLLECTION EFFORTS, PROVIDED, THAT SUCH EXPENSES WERE NOT PREVIOUSLY DEDUCTED IN

19

DETERMINING THE FINANCIAL INSTITUTION'S LOSS UNDER SECTION 10.01[H] HEREOF. WITH RESPECT TO THE REMAINING AMOUNTS ("NET RECOVERIES"), THE FINANCIAL INSTITUTION SHALL PAY TO USAID, WITHIN THIRTY (30) DAYS OF RECEIPT OF SUCH NET RECOVERIES (OR IMMEDIATELY AFTER USAID'S PAYMENT OF THE FINANCIAL INSTITUTION'S CLAIM IF RECEIPT OF SUCH NET RECOVERIES OCCURS PRIOR TO SUCH PAYMENT), AN AMOUNT EQUAL TO THE GUARANTEE PERCENTAGE (PART II, SECTION 5) OF SUCH NET RECOVERIES, UP TO THE AMOUNT OF THE CLAIM AS PAID BY USAID.

[2] IN THE EVENT THAT THE FINANCIAL INSTITUTION HAS LOANS OUTSTANDING TO THE DEFAULTING BORROWER THAT ARE NOT COVERED BY THE GUARANTEE, NET RECOVERIES FROM THE DEFAULTING BORROWER SHALL BE APPLIED TO THE DEFAULTED QUALIFYING LOAN AND THE NON-COVERED LOANS, RESPECTIVELY, ON A PARI PASSU BASIS.

[3] PAYMENTS MADE TO USAID UNDER THIS SECTION SHALL BE MADE IN THE CURRENCY OF FEE PAYMENT. IF MADE IN U.S. DOLLARS, SUCH PAYMENTS SHALL BE CALCULATED AT THE EXCHANGE RATE USED IN EFFECT ON THE DATE OF EACH PAYMENT AS DETERMINED BY USAID.

[B] AFTER THE DATE OF ITS CLAIM, THE FINANCIAL INSTITUTION SHALL CONTINUE TO PURSUE THE COLLECTION ACTIVITIES DESCRIBED IN SECTION 5.01[B] HEREOF FOR ITSELF AND, WITH RESPECT TO THE NET RECOVERIES PAYABLE TO USAID UNDER SUBSECTION [A] HEREOF, AS AGENT FOR USAID, SO LONG AS COMMERCIALLY REASONABLE.

[C] AT USAID'S REQUEST (WHICH MAY BE MADE AT ANY TIME ON OR AFTER THE DATE USAID PAYS THE CLAIM), THE FINANCIAL INSTITUTION SHALL EXECUTE AN ASSIGNMENT IN FAVOR OF USAID, IN FORM AND SUBSTANCE ACCEPTABLE TO USAID, OF THE FINANCIAL INSTITUTION'S RIGHT [1] TO RECEIVE THE SHARE OF NET RECOVERIES DUE TO USAID UNDER SUBSECTION [B] AND/OR [2] TO PURSUE COLLECTION OF SUCH NET RECOVERIES.

ARTICLE VIII
TRAINING, EVALUATIONS, COLLATERAL

SECTION 8.01. USAID TRAINING, EVALUATIONS, COLLATERAL. THE FINANCIAL INSTITUTION RECOGNIZES THAT THE PURPOSE OF THE GUARANTEE BY USAID IS TO ENCOURAGE GREATER SMALL BUSINESS LENDING AND, TO THAT END, THE FINANCIAL INSTITUTION AGREES TO COOPERATE REASONABLY IN SMALL BUSINESS LENDING SEMINARS, TRAINING PROGRAMS, PROMOTIONAL PROGRAMS AND EVALUATIONS (INCLUDING EVALUATIONS OF THE OVERALL DEVELOPMENTAL IMPACT OF THE GUARANTEE AS IT RELATES TO WOMEN) CONDUCTED, SPONSORED OR SUPPORTED BY USAID. COOPERATION SHALL INCLUDE MAKING APPROPRIATE MANAGERIAL OR OTHER STAFF AVAILABLE FOR PARTICIPATION IN SUCH SEMINARS, PROGRAMS AND EVALUATIONS. THE FINANCIAL INSTITUTION ALSO RECOGNIZES THE IMPORTANCE OF USING FLEXIBLE LENDING TECHNIQUES AND CREDIT CRITERIA, INCLUDING CASH-FLOW ANALYSIS, FOR THE EXPANSION OF LENDING TO THE SMALL BUSINESS SECTOR. ACCORDINGLY, THE FINANCIAL INSTITUTION AGREES TO WORK WITH USAID TO REDUCE ITS EMPHASIS ON COLLATERAL REQUIREMENTS TO THE MAXIMUM EXTENT PRACTICABLE (CONSISTENT WITH REASONABLE COMMERCIAL PRACTICES) AND TO EXPLORE ALTERNATIVE METHODS OF CREDIT ASSESSMENT.

ARTICLE IX
EXPIRATION, TERMINATION, REDUCTION, RENEWAL

SECTION 9.01. TERM. THE TERM OF THE GUARANTEE IS FOR A MAXIMUM OF FIVE (5) YEARS FROM THE EFFECTIVE DATE (SECTION 3.01), AS AGREED TO BY USAID AND THE FINANCIAL INSTITUTION IN PART II, SECTION 9, UNLESS EARLIER TERMINATED UNDER SECTIONS 4.02[C] ("FAILURE TO PROVIDE REQUIRED REPORTS"), 6.03 ("FAILURE TO PAY FACILITY FEE") AND 6.05 ("FAILURE TO PAY UTILIZATION FEE"), OR 9.02 AND 9.03 HEREOF.

SECTION 9.02. TERMINATION BY USAID FOR MATERIAL BREACH. USAID MAY TERMINATE THE GUARANTEE OR, AT ITS SOLE ELECTION, SUSPEND AND AT ANY TIME THEREAFTER TERMINATE THE GUARANTEE, AT ANY TIME PRIOR TO

80

THE END OF ANY GUARANTEE PERIOD BY WRITTEN NOTICE TO THE FINANCIAL INSTITUTION UPON THE OCCURRENCE OF ANY MATERIAL BREACH OF THESE STANDARD TERMS AND CONDITIONS BY THE FINANCIAL INSTITUTION, INCLUDING, BUT NOT LIMITED TO, FAILURE TO FURNISH DOCUMENTATION, MISREPRESENTATION, BREACH OF COVENANT, INSOLVENCY OR BANKRUPTCY, OR THE OCCURRENCE OF ADVERSE EVENTS (INCLUDING SIGNIFICANT LOSSES UNDER THIS GUARANTEE).

SECTION 9.03. TERMINATION BY USAID FOR CONVENIENCE. USAID RESERVES THE RIGHT TO TERMINATE THE GUARANTEE ANY TIME FOR ANY REASON BY WRITTEN NOTICE TO THE FINANCIAL INSTITUTION; PROVIDED, HOWEVER, THAT IN THE EVENT OF TERMINATION UNDER THIS SECTION, ALL QUALIFYING LOANS OUTSTANDING UNDER GUARANTEE COVERAGE UP TO THE DATE OF NOTICE OF SUCH TERMINATION SHALL REMAIN COVERED UNTIL THE TERM OF THE GUARANTEE SHALL OTHERWISE EXPIRE OR BE TERMINATED.

SECTION 9.04. EFFECT OF TERMINATION. NO TERMINATION OR SUSPENSION UNDER SECTIONS 4.02[C], 6.05, 9.02, 9.03, OR 9.05, EXCEPT FOR MISREPRESENTATION UNDER SECTION 9.02, SHALL HAVE AN EFFECT ON THE VALIDITY AND ENFORCEABILITY OF ANY CLAIM IN WHICH A DEMAND FOR FULL PAYMENT UNDER SECTION 5.01[A] OCCURRED PRIOR TO SUCH TERMINATION.

SECTION 9.05. REDUCTION. AT ANY TIME AFTER THE FIRST TWO GUARANTEE PERIODS OF THE INITIAL TERM OF THE GUARANTEE, USAID MAY, AT ITS OPTION, BY WRITTEN NOTICE TO THE FINANCIAL INSTITUTION, REDUCE THE MAXIMUM COVERED PORTFOLIO (PART II, SECTION 4) TO EQUAL THE MAXIMUM AMOUNT OF QUALIFYING LOANS OUTSTANDING UNDER GUARANTEE COVERAGE AT ANY ONE TIME DURING ANY THREE CONSECUTIVE GUARANTEE PERIODS, PROVIDED, HOWEVER, THAT THE AMOUNT OF THE MAXIMUM COVERED PORTFOLIO SHALL NOT BE REDUCED BELOW THE TOTAL PRINCIPAL AMOUNT OF QUALIFYING LOANS THEN OUTSTANDING UNDER GUARANTEE COVERAGE. IN THE EVENT OF ANY SUCH REDUCTION, USAID SHALL MAKE A PROPORTIONAL REDUCTION IN THE GUARANTEE LIMIT (PART II, SECTION 6). IN THE EVENT THE MAXIMUM COVERED PORTFOLIO IS REDUCED TO ZERO, THE GUARANTEE FACILITY SHALL BE DEEMED TERMINATED.

ARTICLE X
DEFINITIONS

SECTION 10.01. TERMS. THROUGHOUT THESE STANDARD TERMS AND CONDITIONS, TERMS, WHEN CAPITALIZED, SHALL HAVE THE MEANING ASSIGNED TO THEM IN THE APPLICATION (INCLUDING THIS PART V), OR AS FOLLOWS:

[A] "USAID PAYMENT REPRESENTATIVE" SHALL MEAN THE PARTY OR PARTIES DESIGNATED BY USAID IN THE USAID GUARANTEE COMMITMENT (SECTION 3.01), OR OTHER WRITTEN NOTICE TO THE FINANCIAL INSTITUTION, TO RECEIVE AND MAKE PAYMENTS FOR USAID AS CALLED FOR BY THESE STANDARD TERMS AND CONDITIONS.

[B] "BORROWER" SHALL MEAN THE BENEFICIARY OF A LOAN ADVANCED BY THE FINANCIAL INSTITUTION. IF FINANCIAL LEASES ARE A FORM OF CREDIT AUTHORIZED IN THE USAID GUARANTEE COMMITMENT (SECTION 3.01), "BORROWER" SHALL INCLUDE THE LESSEE OF SUCH LEASES.

[C] "EXCHANGE RATE" SHALL MEAN THE HIGHEST RATE OF EXCHANGE FOR THE CONVERSION OF U.S. DOLLARS TO LOCAL CURRENCY WHICH AT THE TIME IS NOT UNLAWFUL IN THE COUNTRY, AND DETERMINED IN THE MANNER PROVIDED HEREIN.

[D] "FINANCIAL LEASE" SHALL MEAN A LEASE OF NEW MACHINERY AND EQUIPMENT WITH THE FOLLOWING TERMS AND CONDITIONS:

[1] THE TOTAL OF LEASE PAYMENTS (PRINCIPAL PORTION ONLY) MUST BE EIGHTY-FIVE PERCENT (85%) OR MORE OF THE ASSET COST TO THE FINANCIAL INSTITUTION.

[2] IF THERE IS A PURCHASE OPTION AT THE EXPIRATION OF THE LEASE, THE OPTION PRICE MUST BE NOMINAL.

[3] The lease does not require the Financial Institution to provide for the servicing, repair or maintenance of the leased property, to renew any license or registration of the leased property, or to purchase insurance covering the leased property unless the cost of such insurance is for the account of the Borrower.

[4] In the judgment of USAID, the intent of the lease is for the lessee to own the asset at the end of the lease contract.

[e] "Governmental Authority" shall mean the government of the Country or any other country, any agency or instrumentality thereof, or any entity owned or controlled thereby.

[f] "Guarantee Period" shall mean each of the consecutive periods occurring from the Effective Date (Section 3.01) until the term of the Guarantee expires or is earlier terminated under the applicable provisions of Article IV, Article VI or Article IX. The first Guarantee Period begins on the Effective Date and ends on the date specified by USAID in the USAID Guarantee Commitment (Section 3.01). Each subsequent Guarantee Period, with the possible exception of the last period, is a six (6) month period commencing on the date following the expiration of the immediately preceding period. Unless the Guarantee is earlier terminated, or unless otherwise agreed to by USAID and the Financial Institution, the last Guarantee Period expires at the end of the five (5) year term of the Guarantee.

[g] "Loan" shall mean any type of local currency credit, including commercial loans, lines of credit, overdrafts, commercial letters of credit, guarantees or Financial Leases, unless limited by USAID in the USAID Guarantee Commitment (Section 3.01) or otherwise agreed to in writing by USAID and the Financial Institution.

[h] "Loss" shall mean the loss of principal, only, after deduction of all recoveries from the defaulting Borrower from any source (as described in Section 7.08[a][1]) received by the Financial Institution prior to the date of its claim, less actual and reasonable expenses incurred in connection with its collection efforts up to such date.

[i] "Maximum Covered Portfolio" shall mean the total amount of Qualifying Loans placed under Guarantee coverage, minus any claimed losses. For example, the Maximum Covered Portfolio on a US$6,000,000 facility with claimed losses of US$500,000 would be US$5,500,000.

[j] "Quarter" shall mean each of the consecutive periods occurring from the Effective Date (Section 3.01) until the term of the Guarantee expires or is earlier terminated under the applicable provisions of Article IV, Article VI or Article IX. The first Quarter shall be coterminous with the first Guarantee Period. Each subsequent Quarter, with the possible exception of the last, is a three (3) month period commencing on the date following the expiration of the immediately preceding Quarter. The Quarters are defined as follows:

January 1 through March 31;
April 1 through June 30;
July 1 through September 30; and
October 1 through December 31.

87

ARTICLE XI
MISCELLANEOUS

SECTION 11.01. GOVERNING LAW. THIS GUARANTEE SHALL BE GOVERNED BY THE LAWS OF THE UNITED STATES AND THE DISTRICT OF COLUMBIA.

SECTION 11.02. AMENDMENT, ASSIGNMENT. THIS GUARANTEE MAY BE AMENDED ONLY IN WRITING SIGNED BY AUTHORIZED REPRESENTATIVES OF BOTH PARTIES. THIS GUARANTEE MAY NOT BE ASSIGNED IN WHOLE OR IN PART BY THE FINANCIAL INSTITUTION WITHOUT THE PRIOR WRITTEN CONSENT OF USAID.

SECTION 11.03. JURISDICTION. THE FINANCIAL INSTITUTION CONSENTS TO JURISDICTION IN THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLUMBIA AND AGREES THAT, UNLESS WAIVED BY USAID, ANY ACTION BROUGHT TO RESOLVE ANY BREACH, DEFAULT, DISPUTE OR INTERPRETATION OF THIS GUARANTEE SHALL BE COMMENCED IN THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLUMBIA. THE FINANCIAL INSTITUTION AGREES NOT TO CLAIM, IN ANY SUCH LEGAL ACTION, THAT THE DISTRICT OF COLUMBIA IS AN INCONVENIENT PLACE FOR TRIAL. THE FOREGOING SHALL NOT, HOWEVER, LIMIT THE RIGHT OF USAID TO SERVE LEGAL PROCESS IN ANY MANNER PERMITTED BY LAW OR AFFECT THE RIGHT OF USAID TO BRING ANY ACTION OR PROCEEDING AGAINST THE FINANCIAL INSTITUTION OR ITS PROPERTY IN THE COURTS OF THE COUNTRY OR IN ANY OTHER COURTS HAVING JURISDICTION.

SECTION 11.04. COMPLETE AGREEMENT. THE STANDARD TERMS AND CONDITIONS OF THIS PART V, ANNEXES A (IN THE FORM EXECUTED BY USAID), B, C, D AND E HERETO, AND PARTS I, II, III AND IV AS INCORPORATED BY REFERENCE INTO THIS PART V CONTAIN THE COMPLETE AGREEMENT BETWEEN USAID AND THE FINANCIAL INSTITUTION AND SUPERSEDE ALL PRIOR AGREEMENTS AND UNDERSTANDINGS, WHETHER WRITTEN OR ORAL, RELATING TO THE SUBJECT MATTER HEREOF. IN THE EVENT OF ANY INCONSISTENCY BETWEEN THE PRINTED PROVISIONS OF THIS AGREEMENT, THIS PART V SHALL PREVAIL.

SECTION 11.05. CONFIDENTIALITY. PROPRIETARY INFORMATION SUBMITTED TO USAID AND DESIGNATED AS SUCH BY THE FINANCIAL INSTITUTION AS PART OF THE APPLICATION OR PURSUANT TO THESE STANDARD TERMS AND CONDITIONS SHALL BE TREATED BY USAID AS CONFIDENTIAL COMMERCIAL INFORMATION IN ACCORDANCE WITH APPLICABLE U.S. LAWS.

END OF STANDARD TERMS AND CONDITIONS:
ANNEXES A - E FOLLOW

ANNEX A
FORM OF USAID GUARANTEE COMMITMENT

DATE: ______________________

FISCAL YEAR: 19 ____

GUARANTEE COMMITMENT

[NAME OF FINANCIAL INSTITUTION]
[STREET ADDRESS]
[CITY, COUNTRY]

SUBJECT: SMALL BUSINESS LOAN PORTFOLIO GUARANTEE
PROJECT NO. 940-3005.[__]
GUARANTEE COMMITMENT NO. [____________]

DEAR :

I AM PLEASED TO INFORM YOU THAT THE AGENCY FOR INTERNATIONAL DEVELOPMENT (USAID) HAS ACCEPTED YOUR APPLICATION FOR THE SMALL BUSINESS LOAN PORTFOLIO GUARANTEE ("GUARANTEE") DATED ______, 19__, UNDER THE FOLLOWING CONDITIONS AND LIMITATIONS:

MAXIMUM COVERED PORTFOLIO: US$ ______________
GUARANTEE PERCENTAGE: ______%
GUARANTEE LIMIT (USAID COMMITMENT): US$ ______________

FROM OUR DISCUSSIONS WITH YOU, WE UNDERSTAND THAT YOU INTEND TO ALLOCATE THE GUARANTEE PORTFOLIO BETWEEN MICROENTERPRISE AND SMALL BUSINESS LOANS APPROXIMATELY AS FOLLOWS: ______________
____

THIS NOTICE IS ALSO TO ADVISE YOU OF THE FOLLOWING:

1. <u>FEES:</u>

<u>FACILITY FEE:</u>

[A] A FACILITY FEE OF US$______ IS DUE AND PAYABLE NO LATER THAN THIRTY (30) DAYS AFTER THE DATE HEREOF. THE FACILITY FEE IS EQUAL TO _____% OF THE GUARANTEE LIMIT STATED ABOVE.

[B] PAYMENT IS TO BE MADE IN U.S. DOLLARS, THE CURRENCY OF FEE PAYMENT.[1] PAYMENT IS TO BE MADE IN THE LOCAL CURRENCY AMOUNT DETERMINED BY YOUR USAID PAYMENT REPRESENTATIVE ON THE DATE OF YOUR PAYMENT.[2]

1-2 ONLY ONE OF THESE TWO SENTENCES IS TO BE INCLUDED IN THIS PARAGRAPH.

84

UTILIZATION FEE:

[A] A UTILIZATION FEE WILL ALSO BE CHARGED FOR THE GUARANTEE. YOU WILL RECEIVE A SEPARATE NOTICE OF PAYMENT DUE FOR SUCH FEE AFTER THE EXPIRATION OF EACH GUARANTEE PERIOD. (SEE SECTION 5 BELOW.)

[B] THE UTILIZATION FEE IS EQUAL TO ___% PER ANNUM OF THE AVERAGE U.S. DOLLAR VALUE OF QUALIFYING LOANS PLACED UNDER GUARANTEE COVERAGE DURING A SIX-MONTH GUARANTEE PERIOD.

2. REPORTS

IN ACCORDANCE WITH THE TERMS AND CONDITIONS OF THE GUARANTEE, YOU ARE REQUIRED TO COMPLY WITH THE FOLLOWING REPORTING REQUIREMENTS.

[A] QUARTERLY REPORTING. NO LATER THAN THIRTY (30) DAYS AFTER THE END OF EACH QUARTER, USAID/WASHINGTON MUST RECEIVE FROM YOU {1} A COPY OF THE QUALIFYING LOAN SCHEDULE (AS FURTHER COMPLETED IN ACCORDANCE WITH ITS INSTRUCTIONS) IN EFFECT AS OF THE LAST DAY OF THE ENDED QUARTER, TOGETHER WITH A CERTIFICATION, AND {2} A TRANSACTION REPORT FOR EACH QUALIFYING LOAN ENTERED INTO DURING SUCH QUARTER. IF THE REQUIRED INFORMATION IS SUBMITTED TO USAID/WASHINGTON WITHIN THE APPLICABLE PERIOD BY FACSIMILE TRANSMISSION, YOU MUST ALSO PROVIDE THE ORIGINAL DOCUMENTATION TO USAID/WASHINGTON IN DUE COURSE.

THE QUARTERS ARE DEFINED AS FOLLOWS:

JANUARY 1 THROUGH MARCH 31;
APRIL 1 THROUGH JUNE 30;
JULY 1 THROUGH SEPTEMBER 30; AND
OCTOBER 1 THROUGH DECEMBER 31.

[B] TRANSACTIONAL REPORTING. YOU ARE REQUIRED TO SUBMIT TO USAID A TRANSACTION REPORT AT THE TIME EACH QUALIFYING LOAN THAT WAS PLACED UNDER GUARANTEE COVERAGE IS REMOVED FROM GUARANTEE COVERAGE.

[C] ANNUAL REPORTING. NO LATER THAN ONE HUNDRED EIGHTY (180) DAYS AFTER THE END OF YOUR FISCAL YEAR, YOU ARE REQUIRED TO SUBMIT TO USAID AUDITED ANNUAL FINANCIAL STATEMENTS INCLUDING, OR TOGETHER WITH, THE INFORMATION REQUESTED IN SECTIONS II(A), II(B), II(C), II(F), II(G), II(I), III(B), IV, AND VII (BASELINE) OF PART IV OF THE APPLICATION.

FORMS FOR THE ABOVE-MENTIONED QUALIFYING LOAN SCHEDULE, CERTIFICATION AND TRANSACTION REPORTS ARE INCLUDED IN PART V, ANNEXES B, C, AND D OF THE GUARANTEE APPLICATION. FOR YOUR REFERENCE, ADDITIONAL COPIES OF THESE FORMS ARE ATTACHED HEREWITH.

3. USAID PAYMENT INSTRUCTIONS.

PLEASE REMIT PAYMENTS OF THE FACILITY AND UTILIZATION FEES DIRECTLY TO USAID. FOR PURPOSES OF MAKING THESE PAYMENTS, YOUR USAID PAYMENT REPRESENTATIVE IS:

____
____
____

95

PLEASE ADVISE US OF YOUR PAYMENT BY TELEFAX. FOR THESE PURPOSES, SEND YOUR TELEFAX TO:

CREDIT AND INVESTMENT STAFF
BUREAU FOR GLOBAL PROGRAMS, FIELD SUPPORT AND RESEARCH
AGENCY FOR INTERNATIONAL DEVELOPMENT
TELEFAX NO.: (202)663-2149 OR (202)663-2373

4. GUARANTEE PERIODS.

PLEASE BE ADVISED THAT YOUR FIRST GUARANTEE PERIOD ENDS ON ________ __, 199__. EACH SUBSEQUENT GUARANTEE PERIOD, WITH THE EXCEPTION OF THE LAST PERIOD, IS A SIX (6) MONTH PERIOD COMMENCING ON THE DATE FOLLOWING THE EXPIRATION OF THE IMMEDIATELY PRECEDING PERIOD. STANDARD REPORTING PERIODS ARE APRIL 1 THROUGH SEPTEMBER 30, AND OCTOBER 1 THROUGH MARCH 31. UNLESS THE GUARANTEE IS EARLIER TERMINATED OR RENEWED, THE LAST GUARANTEE PERIOD WILL EXPIRE AT THE END OF THE FIVE (5) YEAR TERM OF THE GUARANTEE.

5. MICROENTERPRISE.

THE DEFINITION OF "MICROENTERPRISE" FOR [COUNTRY] IS AS FOLLOWS:

____
____
____

6. SMALL BUSINESS ENTERPRISE.

THE DEFINITION OF "SMALL BUSINESS ENTERPRISE" FOR [COUNTRY] IS AS FOLLOWS:

____
____
____

NO LOAN MADE BY YOU WILL BE A QUALIFYING LOAN COVERED BY THE GUARANTEE UNLESS IT IS MADE TO A MICROENTERPRISE OR SMALL BUSINESS ENTERPRISE, IN ACCORDANCE WITH THE ALLOCATION OF THE GUARANTEE PORTFOLIO AGREED TO BY USAID AND THE FINANCIAL INSTITUTION. (SEE PART V, SECTION 2.01 OF YOUR APPLICATION FOR ALL CRITERIA OF A QUALIFYING LOAN).

SINCERELY,

[NOT EFFECTIVE UNTIL FULLY COMPLETED AND SIGNED BY AN AUTHORIZED USAID SIGNATORY]

____
CREDIT AND INVESTMENT STAFF
BUREAU FOR GLOBAL PROGRAMS, FIELD SUPPORT AND RESEARCH

86

ANNEX B

QUALIFYING LOAN SCHEDULE FOR: ______________________________ (FINANCIAL INSTITUTION)

REPORTING PERIOD: ____________________ THROUGH ____________________

GUARANTEE PERIOD: ____________________ THROUGH ____________________ PAGE NUMBER ________

(1) Name of Borrower	(2) Date of Qualifying Loan (mm/dd/yr)[1]	(3) Type[2]	(4) Date Placed Under Coverage[3] (mm/dd/yr)	(5) Maturity Date (or Review Date for Lines of Credit) (mm/dd/yr)	(6) Amount of Qualifying Loan[4]		(7) Date Removed From Guarantee Coverage (mm/dd/yr)	(8) Days In Arrears	(9) Principal Balance At End Of Reporting Period In Local Currency[5]
					In Local Currency	In U.S. Dollars			

TOTALS (Column 6) TOTAL(Column 9)

[1]For Term Loans, date of loan disbursement; for Lines of Credit or other credit facilities, date of approval.
[2]"T" = term loans; "L" = lines of credit or overdraft facilities; "O" = other types of credits.
[3]Must be placed under coverage within ten (10) business days of column 2 date.
[4]Should not exceed the local currency equivalent of US$150,000. For lines of credit or other credit facilities, report the full amount of the credit facility.
[5]For Term Loans, principal balance outstanding; for Lines of Credit or other credit facilities, see following page. Do not include interest or fees.
Total of Column 9 should not exceed the Maximum Covered Portfolio at any time.

See reverse side for further instructions.

ANNEX B (Supplemental)

INSTRUCTIONS FOR THE QUALIFYING LOAN SCHEDULE

Maintaining the Schedule and Guarantee Coverage
(Columns 1 through 7)

The Qualifying Loan Schedule (or QLS) is to be completed in cumulative, chronological order as Qualifying Loans are placed under guarantee coverage. A Qualifying Loan is placed under Guarantee coverage by making the appropriate entries in Column 1 through 6 on the QLS form and, also by completing a Transaction Report for that Loan. A Qualifying Loan is removed from coverage by entering the appropriate date in Column 7 of the QLS.

Each page must be numbered in accordance with the chronological order of the QLS. The original page(s) are to be completed, held by the Financial Institution, kept up to date at all times and made available to USAID in accordance with Part V of the LPG Application, the Standard Terms and Conditions, Article IV, Section 4.02, "Reporting". Please duplicate this form when additional pages are needed.

Reporting Ending Principal Balances
(Column 9)

For Term Loans, the Financial Institution should report the the outstanding principal balance at the end of the Reporting Period, e.g. March 31 or June 30 or September 30 or December 31.

For Lines of Credit or other credit facilities, the Financial Institution may select either of the following two methods for reporting balances. Please note that once the bank has chosen a particular method, it must continue to use that same method until the facility is removed from Guarantee coverage.

> **Method 1:** The Financial Institution will list the full amount of the Line of Credit or other credit facility in Column 6. The Ending Principal Balance reported in column 9 should equal this amount, regardless of the amount outstanding at the end of the Reporting Period.
>
> **Method 2:** The Financial Institution will list the full amount of the Line of Credit or other credit facility in Column 6. The Ending Principal Balance reported in Column 9 will equal only the actual amount outstanding under the Line of Credit or other credit facility at the end of the Reporting Period.

Treatment of Claims made on Lines of Credit or other Credit Facilities: Method 1 and Method 2
Regardless of whether a Financial Institution selects Method 1 or Method 2 for reporting the Ending Principal Balance of a Line of Credit or other credit facility in Column 9 of the QLS, the USAID Guarantee applies only to the actual loss sustained by the Financial Institution (up to the amount reported on the QLS), which must be certified to USAID in the form of Annex E.

Reporting to USAID at the End of Each Quarter
(Columns 8 through 9)

At the end of each Quarter, the Financial Institution should photocopy the pages of the QLS and update, as appropriate, Columns 7 through 9. This completed photocopy must be submitted to USAID/Washington not later than 30 days after the end of the Quarter.

ANNEX C

CERTIFICATION FOR QUALIFYING LOAN SCHEDULE

Bureau for Global Programs, Field Support and Research
U.S. Agency for International Development
Room 550 SA-2
Washington, D.C. 20523-0231

Attention: Credit and Investment Staff

Ref: Microenterprise and Small Business Loan Portfolio Guarantee

Attached is the Qualifying Loan Schedule for the three month Reporting Period
____________________ through ____________________.

______________________________ ("Financial Institution") hereby certifies that, as of the date hereof, the Loans identified in the attached Qualifying Loan Schedule are Qualifying Loans covered by the Small Business Loan Portfolio Guarantee made in favor of the Financial Institution by the United States of America, acting through the U.S. Agency for International Development ("USAID").

____
Financial Institution

By: ______________________________
Signature

____
Name (please print)

____
Title (please print)

____
Date

ANNEX D

TRANSACTION REPORT

1. Name of Financial Institution: ____________________

2. (a) Borrower Name: (check one): ☐ Mr. ☐ Mrs. ☐ Ms. ____________________

   (b) Business Address:

   ____

   ____

   (c) The Borrower is: (check one): ☐Permanent Resident of ____________ (country)
   ☐National

   (d) Description of Borrower's business (Please be specific):

   ____

   ____

   (e) Size and Composition: Annual Sales: ____________________

   Total Assets: ____________________
   (excluding land, buildings, and machinery)

   Ownership (check one): ☐ Individual(s) ☐ Corporation

	Ownership (percentage)	Management (excluding ownership) (in numbers)	Full-time Employees (in numbers)
Men			
Women			

3. Qualifying Loan

   (a) Amount (in Local Currency): ____________________
   (For Financial Leases, only, enter the principal amount of the lease)

   (b) Qualifying Loan Date[1]: ____________________

[1] For Term Loans, date of disbursement; for Lines of Credit or other credit facilities, date of approval.

90

(c) Type of Credit (please check the appropriate box):

- ☐ Term Loan — Maturity Date: ______________________
- ☐ Line of Credit/Overdraft — Review Date: ______________________
- ☐ Other — Expiry Date: ______________________

(d) Purpose of the Qualifying Loan (please describe in full detail):

____

____

(e) Would the Financial Institution have made the loan to this Borrower without the USAID Guarantee? Yes__ No__

If Yes, what additional benefit did the USAID Guarantee provide?

____

____

If No, what effect did the USAID Guarantee have on the bank's decision to make the loan?

____

____

(f) Collateral/security as percentage of the amount described in (a) above: ________% (excluding the USAID Guarantee)

(g) Is the Borrower a first-time borrower of the Financial Institution? Yes ___ No ___

If Yes, has the borrower ever obtained credit from the formal sector? Yes ___ No ___

(h) Why has the bank placed this loan under guarantee coverage?

(Please check the appropriate item)

- ☐ Start-up Company
- ☐ No Credit History or Previous Borrowing History
- ☐ Inadequate Collateral or Equity Contribution
- ☐ Inadequate cash flows
- ☐ other (please specify)______________________________

ANNEX E
FORM OF CLAIM

[Letterhead of Financial Institution]

Credit and Investment Staff
Bureau for Global Programs, Field Support and Research
U.S. Agency for International Development
Room 550 SA-2
Washington, D. C. 20523-0231
Attn.: Director - LPG Program

RE: Qualifying Loan to (Name of Borrower)

Dear Sir or Madam:

Reference is made to the Small Business Loan Portfolio Guarantee (the "Guarantee") made effective in our favor by the USAID Guarantee Commitment issued on ______ _, 19_ by the United States of America, acting through the Agency for International Development.

Pursuant to the Guarantee, we hereby submit a claim for the amount in Local Currency of ______. This claim results from our Loss on the referenced Qualifying Loan, and is calculated on Exhibit A hereto. In addition to Exhibit A, we submit a copy of the Qualifying Loan Schedule that is now (or was last) in effect, which includes the Qualifying Loan on which this claim is made, together with a Certification (Part V, Annex C) therefor.

(Please indicate method [1] or [2] with a ✓ in the appropriate box)

☐ [1] **We hereby certify that we have written off the entire outstanding balance of the Qualifying Loan (including principal and interest) as a bad debt expense.**

☐ [2] **We hereby certify to USAID that we are unable to write off the entire outstanding balance of the Qualifying Loan (including principal and interest) as a bad debt expense because of the following legal impediment or significant impracticality:**

____

and that we have made a specific provision in our allowance for bad debts.

We hereby acknowledge our obligations [i] to notify USAID in the event of our receipt of Net Recoveries on the Qualifying Loan, [ii] to pay USAID a percentage of such Net Recoveries and [iii] to make a written assignment to USAID of our right to pursue and receive such Net Recoveries, all as provided in Part V (Standard Terms and Conditions), Section 7.08.

We hereby certify that the referenced Qualifying Loan, when made, met all of the criteria set forth in Part V, Section 2.01 and that this claim meets all of the requirements of Part V, Section 5.01.

Sincerely yours,

By: ______________________ ______________________
Signature Name (please print)

______________________ ______________________
Title (please print) Date

92

EXHIBIT A
ANNEX E (Continued) - STATEMENT OF LOSS

1. Borrower
   (a) Name: ____________________

   (b) Address (principal place of business): ____________________
   ____

   (c) Borrower is a (Check one): ☐ National ☐ Permanent Resident of: ____________________ (Country)

   (d) On the date of the Qualifying Loan, was the Borrower

   (i) a "small business enterprise" or a "microenterprise," as defined by USAID (Part V, Section 2.01(a)(4))? Yes ___ No ___

   (ii) 100% privately owned, controlled and operated? Yes ___ No ___

   (e) Purpose of the Qualifying Loan (please describe in detail): ____________________
   ____
   ____

   (f) On the date of the Qualifying Loan, state (in Local Currency) the total principal amount of each other Qualifying Loan and each other credit of the Borrower:
   Other Qualifying Loans covered by the Guarantee: ____________________
   ____

   Credits not covered by the Guarantee: ____________________
   ____

   (g) Was any portion of the Qualifying Loan financed, directly or indirectly, with subsidized funds or guaranteed by a Governmental Authority or any other donor organization (except USAID)? Yes ___ No ___

   (h) U.S. Dollar amount of Maximum Covered Portfolio (Part II, Section 4) on the date on which the Qualifying Loan was placed under Guarantee coverage? $__________

2. Dates:
   (a) of the Qualifying Loan ____________________

   (b) on which the Qualifying Loan was placed under Guarantee coverage ____________________

   (c) on which demand for full payment was made, as required by Part V, Section 5.01[a]) ____________________

   (d) of write-off or provision (Part V, Section 5.01[c]) ____________________

   (e) of this claim ____________________

(Sections 3-5 continued on the next page)

EXHIBIT A to ANNEX E (Continued)

STATEMENT OF LOSS

3. The Financial Institution has made the following efforts to induce or compel the Borrower (or any other person that may be liable on the Qualifying Loan) to make full payment of all amounts due on the Qualifying Loan: ____________________

____

____

4. On the date of the demand for full payment required under Section 5.01[a], state (in Local Currency) the total principal amount of each other Qualifying Loan and each other credit of the Borrower:

   Other Qualifying Loans covered by the Guarantee ____________________

   Credits not covered by the Guarantee ____________________

5. The Financial Institution's Loss on the Qualifying Loan, and the amount of its claim, is calculated in Local Currency as follows:

   (a) principal balance (excluding net recoveries) of the Qualifying Loan on date of this claim ____________________

   (b) net recoveries on date of this claim (Part V, Sections 7.08(a)(1), 10.01(h))

      (1) recoveries from all sources ____________________
      (2) less actual and reasonable collection expenses ____________________
      (3) net recoveries [Line (1) less line (2)] ____________________

   (c) Loss (principal balance less net recoveries) ____________________

   (d) Guarantee Percentage __________%

   (e) Financial Institution's share of Loss ____________________

   (f) Amount of claim ____________________

(End of Part V)

94

ANNEX 7

DRAFT TERMS OF REFERENCE

FOR AN ACTIVITY IMPLEMENTATION CONTRACT

(These Terms of Reference assume that the services of an Institutional Contractor would be obtained through a free and open competition to implement all of the technical assistance and training aspects of the Microenterprise Finance Activity. Should the USAID Mission to the West Bank and Gaza hire a Personal Services Contractor for the Microfinance Resident Advisor position, it would probably make more sense to obtain the requisite short-term assistance and training through existing Indefinite Quantity Contracts, such as MicroServe or others, since the level of effort for the short-term assistance alone would be too low to interest an Institutional Contractor.)

Background

The USAID/West Bank and Gaza Strategy (1996-2000) outlines a two-track approach for future USAID initiatives to increase access to financial services for the Palestinian private sector. This approach consists of:

1) Support grants to existing NGO microcredit projects in order to expand the volume of credit available to small borrowers in the near-term; and

2) Technical assistance and training to facilitate the development of microcredit programs run by commercial banks in order to develop a more sustainable and broad-based model for microcredit delivery in the longer term.

In September, 1996, USAID concluded grant agreements with Save the Children and UNRWA to enhance their capacity to deliver microenterprise loans in the West Bank and Gaza. Funds provided under these agreements are expected to result in 8,500 individual loans to Palestinians, over an eighteen month period and reach a level of 2,800 active loans (size of loan portfolio).

Also in 1996, USAID organized and financed a series of seminars and workshops to expose Palestinian bankers to microcredit practices and technology employed in other parts of the world, with an emphasis on successful programs developed with USAID assistance in Egypt. A select group of Palestinians were invited to attend a one-week training session on the operations and management of a microlending program at the Alexandria Business Association.

Subsequently, a USAID Program Management Specialist conducted meetings with representatives of several commercial banks to assess their interest in a potential USAID-financed program to introduce microlending operations at selected bank branches in the Palestinian territories. These discussions resulted in narrowing the number of potential banks to five.

In early 1997, the Microenterprise Finance Activity (MFA) was designed in order to assist the commercial banking sector in the West Bank and Gaza to establish and implement microfinance programs for microenterprises.

The **purpose** of the MFA using commercial banks as lenders is:

> To increase access to credit for microenterprises, with special attention to women clients, and to develop long-term, sustainable sources of financial services for microenterprises through the formal financial system of the West Bank and Gaza.

The **objectives** of the MFA are:

1. To leverage USAID financial inputs with substantial capital from the participating banks to reach much greater numbers of microenterprises than can be reached through NGO- financed programs without significant additional infusions of donor loan capital.

2. To enhance the potential for rapid scale up of microloan numbers and amounts that will assist the banks to achieve early profitability in their microfinance programs.

3. To achieve a system of microfinance through the commercial banking sector which would have greater prospects for long-term, financial and institutional sustainability than the provision of microcredit through traditional NGO modes.

4. To provide microentrepreneurs with access to a wider range of banking services and to develop a long-term relationship between the banks and microentrepreneurs.

General Objectives of this Request for Proposals for Technical Assistance and Training

The general objectives of this Request for Proposals (RFP) for technical assistance and training are as follows:

1. To provide on-going, resident, technical assistance to the banks participating in the MFA to assist them in establishing and implementing a microfinance program within their banks.

2. To bring lessons learned from successful microfinance programs elsewhere in the region and in the world to bear on the microfinance programs within the West Bank and Gaza.

3. To coordinate short-term technical assistance and training, as needed, for the development of the MFA in the West Bank and Gaza.

4. To assist in the development of a Microfinance Forum within the West Bank and Gaza in order to encourage the various parties active in microfinance to share their experiences.

Specific Tasks

The specific tasks required by a contractor to implement the RFP are as follows:

1. To field a Microfinance Resident Advisor (MRA) to provide on-going assistance to the banks for three years. The MRA will work closely with bank management to acquaint them with the best practices of microfinance programs elsewhere and to counsel them on the establishment and operations of their microfinance program. He/she will also provide assistance on a daily basis to the Supervisory Loan Officer and the Field Loan Officers of each bank/branch involved in the MFA.

2. The Contractor will coordinate all short-term technical assistance and training to the banks. This will require the identification of short-term technical assistance and training needs, preparation of statements of work for the consultancies, and the recruitment and supervision of qualified staff to conduct the consultancies. An illustrative list of potential areas for short-term assistance is presented below.

   - Policy Issues
   - Management Information Systems
   - Sub-Sector Analysis
   - Gender Issues
   - Marketing
   - Training Program Development
   - Investment of Funds
   - Banking Policies and Procedures

3. The Contractor will design and implement a Study Tour by key officials of banks participating in the MFA to three or four successful microenterprise finance programs elsewhere in the world which utilize commercial banks as the principle implementors of the program.

4. The Contractor will assist in the establishment and development of a Management Information System within each participating bank which will track loan portfolio performance and financial aspects of the microfinance program in each bank. This assistance may involve coordination of efforts with another Contractor with previous microfinance MIS experience in the region obtained directly by the USAID Mission for the West Bank and Gaza to put the MIS in place.

5. The Contractor will be responsible for the establishment of a Microfinance Forum in the West Bank and Gaza which will serve as a forum for sharing of experiences among all parties in the West Bank and Gaza active or interested in microfinance programs. These parties shall include banks, NGOs, legislators, and any others interested in microfinance.

Term of the Contract

The initial term of the contract to accomplish the objectives of this RFP will be for three years. USAID may extend the contract for additional optional years, if required and funding is available.

98

ANNEX 8

DRAFT ACTIVITY TRAINING PLAN

Training for bank staff in microfinance principles and procedures will be an integral part of the Microenterprise Finance Activity (MFA). The training will consist of three types - On-the-Job-Training, Study Tours and periodic short-term training courses. Specific details on each of these is given below.

On-the-Job Training

This training will be provided primarily by the Microfinance Resident Advisor (MRA). He/she will provide training and technical assistance to the management staff, Supervisory Loan Officers (SLOs) and Field Loan Officers (FLOs) on an ongoing basis. This training will be more intensive during the early stages of the program or when the microfinance program expands to new branches. However, it will continue over the course of the MFA on a regular basis. Since implementation of a microfinance program enters new phases as time goes along, there is a need for additional training to be conducted as new problems emerge or as the loan portfolio increases in size. There are stages of development of microfinance programs, as with other programs, and training must keep up with the new challenges each stage presents.

Study Tours

A kick-off study tour is envisioned early during the implementation of the MFA for senior staff of the participating banks. This will involve a visit to successful microfinance programs elsewhere in the world, particularly to some programs which utilize commercial banks as the principal implementors of microfinance programs. The final selection will be made later, but some possible candidates include BRI in Indonesia, Banco Sol in Bolivia, and NBD in Egypt. Other study tours for the SLOs and FLOs to programs closer to the West Bank and Gaza may be arranged during the course of the implementation of the MFA. The programs in Egypt are likely candidates for these study tours.

Short-Term Training Courses

From time-to-time, short-term training course will be necessary for bank staff in order to deal with specific problems occurring during the implementation the MFA. These training needs will be identified by the Microfinance Resident Advisor, some in advance and others as they occur during MFA implementation. There will be a need for initial training of SLOs and FLOs as they are hired and before they begin implementation of the microfinance program. This type of training will be repeated for new hires as the program expands to other branches. In addition, some refresher courses for existing SLOs and FLOs with new, advanced material may also be conducted from time to time. An illustration of the structure and content of the initial training course on microfinance principles and operations is presented below.

Illustrative Initial Training Course in Microfinance Principles and Operations

Training of new loan officers in a new program will take specialized effort. The following training activity will occur after the SLOs and FLOs have been recruited and given a short-term contract. No long term contracts should be issued until after the new recruits have had a chance to prove themselves as competent and willing to carry out their assignments.

Initial Training Course for Loan Officers

Week 1: The first week of employment should be familiarization with the overall banking operations of the respective bank. The training could be largely carried out by the branch manager and staff of the bank to which the SLO and FLOs are assigned.

Week 2: This week would be largely classroom training to be led by a short term consultant under the overall technical assistance contract. The first four days would be exposure to microenterprise loan design and development. The final day would be training in using a survey instrument that would elicit information from a perspective customer. The survey document would gather information on the perspective client's type and level of business activity, with particular attention to current levels of operation and to figure out what loan assistance would be required for business expansion.

Weeks 3 - 4: These weeks would be aimed at the carrying out the survey, with a recap of progress made on the final day of each week. Each new FLO should be expected to complete at least 10 surveys each week. The FLOs would meet on the final day of each week to exchange experiences from the survey exercise, and to critique each others survey results. This exercise not only familiarizes the FLOs with the microenterprise market, but allows them to "advertise" the launching of the microenterprise finance activity.

Week 5: The final week of training would again be largely classroom training carried out by both a short term consultant and the Supervising Loan Officer. Particular attention would be paid to properly filling out the loan applications and gathering any other documentation required under the microfinance activity. It would also include review of data generated under the management information system to ensure that the FLOs have a clear understanding of the critical information regarding loan and savings data of any and all borrowers within their respective portfolios. The person(s) responsible for the MIS would take part in helping the FLOs to understand what data is required from them.

180

As the activity expands, new loan officers will be added. Training for the expanded staff will largely follow the steps above, although the survey training would be replaced by pairing the new loan officer with an existing and experienced FLO to allow her/him to see how loan supervision and extension is carried out on a daily and weekly basis. Many successful microfinance activities actually divide up an existing loan officer's portfolio with a new loan officer so that the new FLO starts out with some experienced borrowers, and allows the experienced loan officer to expand the program to new borrowers.

101