MICROENTERPRISE INNOVATION PROJECT—MICROSERVE

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THE ORGANIZATION FOR WOMEN'S ENTERPRISE DEVELOPMENT

Institutional Assessment Report
Delivery Order No. 7

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Submitted to:
USAID

Submitted by:
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ABSTRACT

This report is an assessment of the Organization for Women's Enterprise Development in Honduras. The assessment and analysis were undertaken in support of the U.S. Agency for International Development's Microenterprise Innovation Project—Implementation Grant Program (IGP). The report reviews the microlending program of an IGP beneficiary in Honduras. The outline of the report was developed for field assessments of this sort and reviews the original financial indicators of the ODEF program, appraises its management information system, and assesses progress in meeting the grant's targets.

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ACRONYMS

FHIS	Honduran Fund for Social Investment
FOPRIDEH	Federation of Private Development Organizations
IDB	Inter-American Development Bank
IGP	Implementation Grant Program
MIS	Management information system
NGO	Nongovernmental organization
ODEF	Organization for Women’s Enterprise Development
PVO	Private voluntary organization
SFI	Sistemas Financieros Internacionales

EXECUTIVE SUMMARY

MicroServe's Implementation Grant Program (IGP) provides grants to U.S. private voluntary organizations, cooperatives, credit unions, and developing country organizations to develop indigenous organizations that serve microenterprises. The IGP seeks to increase the outreach and scale of local institutions' microenterprise services and improve their financial viability, financial reporting, and internal administration.

This report reviews the microlending program of an IGP beneficiary in Honduras, the Organization for Women's Enterprise Development (ODEF). A nongovernmental organization (NGO), ODEF is an affiliate of the Katalysis North/South Development Partnership, a California-based private voluntary organization that promotes microenterprise development in Central America. Katalysis received a three-year, $900,000 grant in October 1996 to strengthen ODEF. About $189,000 was earmarked for Katalysis's technical assistance and training costs, and the remaining $710,000 was to capitalize ODEF's credit fund ($651,159) and finance some of its operating costs ($58,841). Over the three years, Katalysis was expected to add matching funds of about $300,000.

Summary of findings. In January 1997, nearly five months after the grant was signed, two G/EG/MD advisors visited ODEF to review original financial indicators of the program, appraise its management information system, and assess progress in meeting the grant's targets. The advisors found substantial progress:

- During 1996 ODEF established 98 new community banks and closed 21, ending the year with 175 active banks having 4,068 members (73 percent women).
- Total value of loans disbursed in 1996 was U.S. $1.55 million (L 19,425,921),[1] with 56 percent going to community banks and 44 percent to individual borrowers.
- During 1996 the number of individual loans declined by 37 percent. A total $682,930 was loaned to 456 clients (54 percent women).
- Average loan size for community bank members was $127 and for individual borrowers $1,498. Women represented 72 percent of clients.
- Operating costs represented 20 percent of earning assets. ODEF was capable of covering 103 percent of the operating costs from interest and fee income. When imputed financial costs were added (i.e., the inflation rate or interbank rate, whichever is higher), ODEF was 64 percent financially self-sufficient.
- ODEF's technical and managerial capacity was well developed and had evolved to the point where Katalysis's external involvement in ODEF administration was minimal.

[1] The currency conversion rate at the time this report was prepared: U.S. $1.00 = 12.5 lempiras. Throughout this report, *$* refers to U.S. dollars.

Katalysis continues to provide specialized technical assistance when asked, but all other aspects of program administration are directed by ODEF staff.

Analysis of ODEF operations. Overall, ODEF is an effective source of financial services for many low-income clients in northeastern Honduras. However, it will need to upgrade financial planning and internal administration to reach its potential client mass (e.g., 20,000 clients) while controlling both loan delinquency and operating costs. In January 1997 ODEF had little liquidity, having less than 2 percent of assets in cash, checking, and savings accounts. Loans consumed another 74.8 percent of assets, followed by fixed assets (18.6 percent) and accounts receivable (7.7 percent). Loan delinquency was high: 14.1 percent of the outstanding portfolio.

The loan portfolio ratio (75 percent) is a bit low for an NGO financial intermediary, and it could be increased another 10 percent without risk if ODEF can better control delinquency. At the current delinquency rate of 14.1 percent, loan collection efforts likely consume valuable staff time. ODEF should also try to reduce the high ratios for fixed assets (18.6 percent) and accounts receivable (7.7 percent), since these generate no earnings. Finally, ODEF should be regularly monitoring and evaluating its financial condition (e.g., cash flow, income, and expenditures) to ensure sufficient liquidity to maintain its growth targets. Achieving these targets will require that ODEF overcome financing constraints that limit its ability to become 100 percent financial self-sufficient by the grant's end.

Summary of issues and options. Key issues identified include the following:

- **Management information and accounting.** Since July 1996, ODEF's internal control and management information systems have suffered as efforts focus on de-bugging a newly purchased software program. This process is expected to be completed in February 1997, when ODEF will need to reconcile all account balances. While the manual accounting and portfolio monitoring is adequate for the immediate future (with minor problems resulting from data input errors and slow, inaccurate reporting from several commercial banks), ODEF should complete installing the computer software program as soon as possible.

- **Financing growth.** ODEF does not possess sufficient resources to finance the 510 community banks targeted in the grant proposal. Obtaining a secure source of external funding to finance future growth represents perhaps the greatest obstacle. The search for new funding is complicated because local commercial banks require borrowers to pledge real collateral, and the fixed assets owned by ODEF (primarily the central office and the *Herencia Verde* training center) cannot be used. This was a provision of the agreement between ODEF and the municipality of San Pedro Sula. ODEF should continue investigating the possible use of collateral alternatives such as loan insurance as one way to access commercial bank financing.

- **Liquidity management.** In December 1996, ODEF had cash and bank deposits equivalent to 1.2 percent of total assets. This is far too little liquidity for a financial institution, and particularly one that is managing the internal account savings of affiliated community banks.

  Regarding savings, ODEF has been using a portion of the community bank guarantee deposits to finance its loan portfolio. Although such in-system financing is not deposit mobilization from the general public (which would violate banking legislation), ODEF should obtain written authorization from the government before continuing this practice.

While authorization is sought, ODEF should establish an interest-bearing investment account for depositing the community bank guarantee funds. In addition, ODEF should maintain a portion of the "restricted donations" and the short-term accounts payable in similarly liquid accounts. These resources should not be used to finance the loan portfolio.

- **Delinquency calculation method and provisioning.** ODEF now calculates its delinquency rate using the amount (value) of payments past due, reporting a 3.7 rate in December 1996. This calculation method underestimates the degree of risk to ODEF should a loan be uncollected. When delinquency is calculated using the portfolio-at-risk formula, the rate becomes 14.1 percent. ODEF should change the way it calculates and reports delinquency.

  In addition, ODEF is now creating loan loss reserves as a simple percentage (3 percent) of the loan portfolio. This procedure does not recognize the aging of the delinquent portfolio (e.g., 30, 60, and 90 days past due). ODEF should change the procedure and adopt a provisioning policy that more accurately reflects the risk of loss in the loan portfolio (see example on page 13 of Section III).

- **Nonfinancial services.** ODEF operates the Herencia Verde Agricultural Training and Learning Center to train community bank boards of directors and treasurers and promote organic growing techniques among small farmers. The center is dependent on grant funding. In 1996, it was able to cover only 6.9 percent of operating costs of about $100,000 from earned income (e.g., training fees, rent, and the sale of agricultural produce). Most of the grant funding will end in late 1998, when ODEF must decide if and how it will continue to operate the center. There appear to be several options:

  - Obtain additional operating grants and continue both the community bank and the small farmer outreach programs
  - Reduce the number staffing the center and reduce or eliminate the small farmer agricultural program
  - Rent the center to another agency (while possibly maintaining a separate training schedule for community bank board members and treasurers)
  - Close the center

- **Fixed assets.** ODEF's fixed assets represented about 18.6 percent of total assets. This ratio, due to donations of land and facilities from the municipality of San Pedro Sula, is much too high for a financial institution seeking self-sufficiency. Therefore, ODEF should minimize future investments in fixed assets, accelerate the depreciation schedule (where appropriate), and aggressively seek growth.

SECTION I
OVERVIEW OF ODEF'S HISTORY AND OPERATIONS

A. The Origins of ODEF

ODEF is the Katalysis partner in Honduras. Katalysis, established 1984 in Stockton, California, to help poor people become more self-sufficient, operates through partnerships with indigenous NGOs in Central America. In addition to Honduras, it has programs under way in Guatemala and Belize. Katalysis provides technical, institutional development, strategic planning, and financial support to its local partners, who in turn provide services to their low-income clients. Katalysis partners work in three principal areas: women's community banking, microenterprise development, and sustainable agriculture.

ODEF was created in 1985 to foster and support women's microenterprise development. In the first four years, ODEF's financial services were secondary to its community development activities. In 1985 ODEF made unsecured loans to five low-income clients. By 1989, though the loan program had grown to serve 210 low-income borrowers, costs were high and outreach limited. To broaden impact, ODEF introduced community banking, a lending method modeled after FINCA's village banking programs.

Lending methods. Community banking, or group credit with joint liability, is now ODEF's preferred lending method. ODEF views group lending as a way to reach poor clients while also greatly increasing the beneficiaries of the credit program. Community bank loans are much smaller than individual loans, and group members are jointly responsible for loan repayment, which reduces loan recovery difficulties. To date, ODEF continues to use both group and individual lending, but about 54 percent of loans disbursed in 1996 went to community banks and that portfolio is growing more quickly than individual lending.

Institutional problems in transitioning into a microcredit NGO. ODEF has passed through two major watersheds in attempting to become an efficient, businesslike NGO. First, in 1993, it fired more than 90 percent of the staff because they failed to accept ODEF's shift from a socially oriented institution to one delivering credit at what many staff considered to be high interest rates. Second, in 1994, it pruned underperforming banks from the community banking program. Among 48 community banks operating, ODEF purged 28 because of lax internal bank disciplines, ignored meetings and savings targets, and difficulties in loan recovery. It retained 20 community banks and retrained promoters and other credit division staff to focus on internal bank disciplines before completing loan applications.

Portfolio management and financing. During 1996 ODEF disbursed $1.55[2] million to 8,657 clients using a combination of individual and community bank loans. At year's end, the delinquency rate using the portfolio-at-risk formula was 14 percent, but the long-run loss rate declined from 7.6 to 4.3 percent. About 85 percent of the outstanding delinquency is within the individual loan

[2] The currency conversion rate at the time this report was prepared: U.S. $1.00 = 12.5 lempiras. Throughout this report, *$* refers to U.S. dollars.

portfolio—one reason ODEF plans to emphasize community banking over individual loans. ODEF aggressively pursues delinquent borrowers, using legal action if other means fail.

At present, ODEF is dependent on external grants and low-cost loans to finance its portfolio, and the weighted average cost of funds in 1996 was 18.6 percent. ODEF has sufficient funding available to finance the current portfolio of individual and community bank clients, but if growth is to continue (including an increase in the average loan size), ODEF must obtain additional sources of financing. This is perhaps the most critical challenge over the next few years.

B. Board of Directors

Composition. ODEF has an eight-member board of directors, comprised of a lawyer, a nurse, two agricultural engineers (livestock and crop specialities), a public administrator, a businesswoman, a political science teacher, and the ODEF executive director (who has a degree in economics). Board members are drawn from a pool (*asamblea*) of 16 individuals involved in creating the organization. They rotate board positions every several years, or whenever a member resigns.

Level of involvement. The board meets every three months but more frequently if major decisions are required. Day-to-day management is delegated to the executive director, and board oversight is limited to discussion of issues presented by the executive director at quarterly meetings. Typical topics include:

- Problems complying with the terms of agreements with donor agencies
- Changes in lending policies (e.g., a reduction in the individual loan terms from 24 to 12 months)
- Plans to increase staff salaries or to contract for external audits

Board/management relations appear to be good. Individual board members often visit the ODEF office, but they do not interfere with operations. The treasurer reviews financial statements if there is a real or potential problem, but such occasions are rare.

While involvement to date appears quite limited, the board has been active in specific instances. For example, it provoked the major reorganization in 1994 when many staff had difficulty accepting the shift to a business orientation that included tightened cost controls, higher interest rates, and legal action to recover delinquent loans. As described earlier, more than 90 percent of the staff were replaced to maintain the focus on long-term sustainability.

Considerations for the board of directors. At present, more active board involvement in day-to-day operations is not needed. The executive director supervises operations and maintains sound relationships with creditors and donor organizations, and she is supported by a dedicated, competent management team. However, ODEF should consider opening board membership to individuals and organizations beyond the original founders. For example, enlisting the participation of private business leaders, ANDI, or the Covelo Foundation would broaden the board's experience base and likely increase member participation.

ODEF should also strengthen external oversight by discontinuing the practice of permitting employees to fill board positions. At present, ODEF's executive director and two other staff members serve on the board. While this may strengthen board/management communication, it weakens independent monitoring. Further, the board should be provided with quantifiable indicators (monthly reports on income, expenditures, and portfolio performance) to assess performance quarterly (at minimum).

C. Financial Planning and Management

Past procedures. Before 1995 ODEF used a participatory process for financial planning and management. Each January, all staff would meet to review the past year's targets and results and set new targets (e.g., number of new banks to be formed in each region and number of new individual clients). Senior management then reviewed the past year's income and expenditure reports, set targets for the credit program and the Herencia Verde center, and allocated resources to be invested in each area.

Current procedures. In January 1996 ODEF changed that procedure when it prepared and adopted a five-year (1996-2000) business plan. The plan had two primary goals: consolidate the organization's finances and improve its capability to provide financial services to low-income borrowers (particularly women). Specific targets are as follows:

- Increase the number of beneficiaries by 500 percent
- Achieve 100 percent self-sufficiency (including training and community development costs)
- Increase capital 200 percent by using retained earnings
- Increase community bank lending to 90 percent of total loan portfolio value by 2000

Today, ODEF management meets in January, reviews the past year's progress in reaching these targets, evaluates the availability of financial resources, and takes any necessary action (e.g., increasing the number of promoters or seeking additional funding).

On a quarterly basis, annual budgets are prepared, and management reconciles projected figures with actual income and expenditures. In 1996, there was only one reconciliation of the annual budget because a new accounting software program had slowed the preparation of accurate financial statements. The deputy director and the credit department chief are keeping an eye on income and expenditures, but detailed monitoring will be impossible until the new software is online and all accounts have been balanced. Management expected most of the software problems to be resolved by February 1997, and fully operational the program will generate detailed income and expenditure reports.

Cash management. This is controlled by the executive director, her deputy, and the chief of the Credit Department. The principal source of cash is loan payments. However, ODEF discourages clients from making payments at the central office in San Pedro Sula. Robberies of local businesses are commonplace in the city, and ODEF seeks to avoid attracting the attention of the often wellarmed bandits. Borrowers are directed to make payments at branches of the six commercial banks having arrangements with ODEF for loans and/or community bank savings. However, some clients do make loan payments at ODEF's offices and ODEF has arranged with the Sogerin Bank for an armored car to collect cash deposits at the central office each afternoon. Daily collections typically range from $400 to $2,000.

ODEF contracts for an external audit yearly using international firms as required by the grant agreements with USAID, the Inter-American Development Bank, and other donors.

D. Competition

According to ODEF, Honduras has more than 954 offices providing financial services, including 494 bank agencies, 55 savings and loans, 200 finance company branches, 130 cooperatives, and 75 NGOs. Formal financial institutions such as banks and finance companies have little interest in ODEF's clientele and the organization's principal competition is NGO-sponsored programs. Among the international private voluntary organizations, Catholic Relief Services, FINCA, Freedom from Hunger, Save the Children, Opportunity International, Project Hope, and World Relief all sponsor village banking programs in different regions of Honduras.

Organizations offering comparable services. The Fundacion Covelo, FINCA, FUNADEH, IDH, CEPROD, ACAMO, and ASIDE provide credit to microentrepreneurs through village banks, solidarity groups, or individual loans. FINCA has a large program, while the others are about half the size of ODEF. Little geographic overlap or aggressive competition exists. As a promotional tool, ODEF says it offers a lower interest rate (34 percent) for first cycle loans than that of most other NGOs. There was no evidence that promoters have difficulty finding clients anxious to start new banks.

Cooperatives and credit unions. These operate in Yoro, El Progreso, and Santa Barbara. Most are small and either incapable or unwilling to extend services to poor clients (particularly women). Most of the credit unions are illiquid and only serve individuals who are known to them, have savings for deposit, and/or can pledge real assets as collateral. The agricultural cooperatives in Santa Barbara, Yoro, and El Progreso are typically crop-specific (e.g., basic grains, bananas, tobacco and coffee), and services are usually limited to in-kind financing for agricultural inputs and simple equipment. They do not finance small and microbusinesses.

E. Internal Organization

ODEF is organized into three departments:

- **Central Administration**
  - Provides program oversight
  - Administers the budget and prepares financial reports
  - Monitors field operations
  - Prepares project proposals and loan applications
  - Represents the organization with donors and other interested parties
  - Guides department heads

- **Credit**
  - Promotes all new community banks
  - Identifies individual clients and helps them submit loan applications
  - Regularly visits the banks and borrowers once loans are disbursed
  - Collects delinquent accounts
  - Trains and orientates community bank board members
  - Identifies candidates for agricultural training at Herencia Verde

- **Herencia Verde Agricultural Training and Learning Center**
  - Trains community bank boards of directors and treasurers

  - Conducts externally financed organic farming training program for subsistence farmers, drawn from communities where the community banks operate and typically not members of the banks

Staff total 54: executive director; deputy; seven accounting and administrative employees; 30 credit personnel, including promoters, analysts, and supervisors; and 15 Herencia Verde employees, including the director, administrator, two agricultural engineers, a community bank trainer, and support personnel.

F. Decentralization of Decision Making

Decision making is divided between the executive director and her deputy. The executive director makes all decisions concerning ODEF's growth strategy (e.g., where to promote new banks). She maintains relations with creditors and donor agencies and ensures that the terms of grant or loans agreements are met. The deputy director makes all administrative decisions, manages ODEF's human resources, and supervises accounting. The three department chiefs make operational decisions in their respective areas.

ODEF has a credit committee, comprised of two board members and the executive director, to review and approve all loan applications. The review of community bank applications is relatively straightforward and based on evidence of a good repayment record and ODEF's loan size policy for different cycles. Individual loan applications are reviewed more closely as they are typically for larger amounts; however, there is little detailed analysis of most applications. The minimum individual loan is $238 (L 3,000); the maximum, $4,762 (L 60,000).

G. External Risk

External risks to ODEF are largely limited to the uncontrollable factors of inflation and devaluation. For example, as inflation reduces the value of the lempira, clients will begin seeking larger loans to keep up with the rising price of commodities. ODEF is already short of liquidity, and it will become more difficult to satisfy the demand for larger loans while also continuing to grow and establish new community banks. This is one reason that ODEF should maintain a minimum capital growth rate equal to or better than the annual inflation rate.

Over the short term, ODEF should upgrade its financial planning capability and more regularly assess inflation's effect on earnings, expenses, and the loan portfolio. This planning should be complemented by closer monitoring and evaluation of ODEF's financial operations, particularly cash flow, loan administration, and operating costs.

SECTION II
MANAGEMENT INFORMATION AND ACCOUNTING SYSTEMS

Switch to new accounting software. In July 1996 ODEF began using an accounting software program (MAS/90) acquired from Sistemas Financieros Internacionales, a subsidiary of a U.S. firm that supplies credit unions.[3] Since September/October 1996, ODEF has used the software to prepare monthly financial statements and portfolio reports, but has had problems reconciling account balances and errors are common. Identifying these problem is complicated by ODEF's decision to discontinue manual accounting when it shifted to the as yet untried new software. Today, the lack of a parallel set of manually prepared accounts makes quickly finding errors difficult, whether input errors made by ODEF staff or mistakes made by commercial banks when processing loan payments.

For several months, ODEF has been unable to prepare accurate financial statements, age the delinquent loan portfolio, or reconcile all outstanding accounts. However, it appears that no major hidden accounting problems exist. For the reporting period, there was only a $312 difference in the balance of the $1.48 million loan portfolio. Nonetheless finding and correcting errors is time-consuming, and ODEF expected most of the software problems to be resolved by February 1997.

Financial reporting. ODEF's chart of accounts is relatively simple and was obtained from the Fundacion Covello, a local, USAID-funded, nonprofit organization that provides technical guidance to area NGOs. The chart of accounts was specifically developed for NGO financial intermediaries such as ODEF and permits preparation of financial statements by source of funds, a common requirement of donor organizations and creditors. While this chart of accounts is not the same as that used by commercial banks, it appears adequate for ODEF's types of operations.

The new accounting software permits the user to work online when processing client transactions with the cashier and immediately updates the accounting upon transaction completion. Once ODEF corrects the errors with the software, there should be no differences between the auxiliary books and the general ledger. Regarding commercial bank liquidations of client loan repayments, ODEF will not operate online and will need to use a batch input system. Data entry errors will likely be more common in this system.

Reports generated by the MIS. The management information system component of the software generates a series of reports:

- Client database, including variables such as gender, age, income, employment, geographic location, name of client's village bank (if appropriate), and the promoter who supervises the bank or individual account. The software permits sorting the data by any of these variables.

- Loan portfolio, including client balances, aging of accounts, a record of letters and repayment reminders sent, interest rates, and delinquency reports. All data can be sorted by source of funds.

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[3] SFI has been distributing and installing the software in Honduran credit unions for about five years and recently began selling it to NGOs.

- Fixed asset use and depreciation schedule.

- Accounting reports such as the general ledger, budget controls, reconciliations of account balances, and financial reports by source of funds.

Internal controls. The following are observations and recommendations for ODEF's internal control system:

- An independent reconciliation and review of bank accounts was most recently completed in December 1995. In 1996 reconciliations were made through the month of June, but they were not reviewed by someone other than the individual who made the reconciliation. Independent review of account balances is important for internal control. Regular reviews can help ODEF find errors and balance the accounts, important steps to be taken while installation of the software is being completed.

- There is a small difference between the individual loan account balances and the general ledger totaling $315 (L 3,935). This is probably due to input errors by ODEF accounting staff. Corrective steps should be taken soon.

- The deputy director completes many internal control functions. While hiring a full-time, internal auditor is unnecessary, ODEF should have its external auditor provide more detail on each account in the annual audit.

- Two individuals sign all ODEF checks. Segregation of functions is inadequate.

SECTION III
FINANCIAL STATEMENTS AND BASELINE DATA

The G/EG/MD assessment team constructed financial statements for year-end 1996 by using data provided by the accounting unit. Some adjustments may be necessary when the computer accounting system is fully operational and the external audit is complete, but the information presented here is thought to be fairly accurate estimates. Balance sheet and income statement data are presented in Annex A.

A. Balance Sheet

A1. Liquidity and Investment Funds

In December 1996, ODEF had 29 bank accounts among six commercial banks. The diversity of these accounts greatly complicates cash management, but donors and creditors require there be no mixing of funds. In addition, separate accounts are necessary to provide clients with several options for loan repayment in the six banks.

ODEF had 1.2 percent of total assets in cash and bank accounts. This is too little liquidity for a financial institution. ODEF is using a portion of the guarantee funds (as well as some restricted operating grant funds) to finance the loan portfolio, which has a minimum turnover of four months. While this is an efficient cash management policy, ODEF is risking that these resources will be unavailable when needed. We therefore recommend that ODEF introduce a liquidity policy that requires a separate bank account for the guarantee funds, the restricted donations, and all short-term accounts payable.

A2. Loan Portfolio

In December 1996, the gross loan portfolio represented 74.6 percent of total assets. The value of the portfolio remained relatively the same between 1995 and 1996, but the number of loans disbursed grew by 77 percent while the average loan size declined by 45 percent. This indicates why ODEF plans to increase community bank lending while reducing the number and value of individual loans. There are an average of 23 members in each community bank.

Loan Portfolio Summary	1994	1995	1996
Cumulative value of loans disbursed	$652,410	$1,580,570	$1,554,073
Number of loans disbursed	1,390	4,140	7,313
Average loan size	$469	$382	$212

A2a. Credit Methodology

In 1996 ODEF disbursed loans totaling $1.55 million (L 19,425,921), with 56 percent going to community banks and 44 percent to individuals. Average loan size for community bank members was $127; for individuals, $1,498. Women represented 72 percent of clients.

Community banking program. This program targets individuals who are unable to access commercial credit because they lack collateral or a credit history. According to Katalysis, typical bank clients are women with an average annual income well below the poverty line ($474 annual) established by the Inter-American Development Bank (IDB). Community banks are formed by a minimum of 20 members and are maintained for three and a half years, or a total of nine cycles. Loan terms for each cycle range between four and six months. The maximum loan size for the first cycle is $95 per bank member, and loan amounts are increased by 20 percent each cycle according to need.

Bank members are expected to save at least 20 percent of each loan received. Upon reaching the end of the ninth cycle, members will have accumulated about $400, theoretically an amount sufficient to self-finance their microenterprises. A portion of member savings are used to establish a guarantee fund with ODEF against nonpayment of loans. In well-performing community banks, up to 50 percent of accumulated savings may be used for internal loans to members and nonmembers, often at higher interest rates than those charged by ODEF. In poorly performing banks, up to 70 percent of accumulated savings must be maintained in the guarantee fund.

The amounts and terms of the first loans are fixed and are the same for all bank members. However, individual loan terms may vary in the second and succeeding cycles as the performance of each borrower is evaluated. Members are required to make weekly payments to the community bank, and banks are expected to repay ODEF every two weeks. To make their loan payments, most community banks use the six commercial banks having agreements with ODEF.

Key Indicators of the Community Banking Program	1995	1996
Total number of community banks in operation	98	175
Total number of borrowers	2,413	4,068
Percentage of women	87%	73%
Total credit disbursed	$418,666	$871,223
Total number of loans disbursed	3,454	6,857
Average loan size	$121	$127

As mentioned earlier, community bank members are expected to graduate at the end of the ninth cycle, when they will have accumulated about $400 in savings and become capable of self-financing their businesses. As yet, no ODEF community bank has reached the ninth cycle. Some banks likely will continue through additional cycles, as happens in other village banking programs in Honduras. Also, community bank "graduates" that need larger loans can then apply to ODEF's individual loan program.

Individual loan program.[4] This program targets larger microenterprises and small businesses by offering loans larger than those provided by community banks. Loans range from $240 (L 3,000) to $4,800 (L 60,000). Small loans ($240 to $400) require two co-signers. Loans from $400 to $800

[4] ODEF also has a small ($70,000) home improvement loan program financed by CHF, but it represents less than 5 percent of the total portfolio.

require two co-signers and a pledge of collateral (e.g., television or refrigerator). Loans above $800 require property collateral. Exceptions to the collateral requirements are made when an applicant has a good credit history. The average loan term is 24 months, but ODEF soon plans to reduce this to 12 months to obtain greater portfolio rotation and reduce risk.

Key Indicators of the Individual Loan Program	1995	1996
Total number of borrowers	721	456
Percentage of women	72%	54%
Total credit disbursed	$1,161,904	$682,850
Average loan size	$1,612	$1,498

A2b. Loan Administration

ODEF has a written policy covering application procedures, maximum loan amounts, terms, collection policies, and other aspects of the credit program. The policy should be updated to reflect lending program changes such as greater focus on community banks and shorter terms for individual loans.

The organization also has a refinancing policy that permits a borrower to apply for a new loan upon repaying 75 percent of an outstanding loan balance. Refinancing applicants must demonstrate no history of loan delinquency. The policy is designed to help good clients obtain fresh financing before the original loan term expires. A portion of the new loan must be used to repay any outstanding balance on the prior loan.

As discussed in Section A2d on page 12, ODEF aggressively pursues delinquent clients, taking legal action if other efforts fail. Delinquent borrowers are levied a 3 percent surcharge on past due payments.

A2c. Loan Monitoring

Most ODEF individual and community bank clients make their biweekly or monthly loan payments using accounts in one of six commercial banks. ODEF views this as a good way to introduce their clients to the more formal, commercial banking system, as well as avoid handling too much cash in the main office. While this method is effective for managing cash, it hampers loan administration and delinquency tracking and reporting. Several banks are slow and at times inaccurate in reporting loan payments into the ODEF account. When errors occur, promoters must seek out borrowers and reconcile their individual receipts against the consolidated reports presented by the commercial banks.

Before introducing the new accounting software in July 1996, ODEF had a loan tracking system that reported loans by zone, agent, and source of funds. Use of this system was stopped in June 1995 when problems began to appear. Since then, ODEF has used manual tracking in which credit agents make regular checks of village bank and individual borrower records during site visits. While most ODEF clients use the banks to make their payments, some visit the central office and make payments to the cashier. At times this has made reconciling member payments with the accounting records more difficult. The practice has also exposed ODEF to losses. For example, a cashier was recently caught using client payments for her own use.

A2d. Recovery of Delinquent Accounts

ODEF has a firm policy regarding delinquent accounts and has a lawyer on retainer to take legal action when necessary. The organization's approach is designed to encourage payment without threatening delinquent borrowers. Once a loan becomes delinquent, a promoter visits the borrower to encourage repayment. Three visits are usually made over 30 days. If this fails, the credit department chief accompanies the promoter in another visit to the borrower. If another 30 days pass with no response, the lawyer visits the borrower. Normally, one lawyer visit is sufficient to obtain a payment or negotiate a new repayment schedule. If not, legal action is taken.

ODEF tries to avoid legal action because of the high costs and the long delays typically incurred. Nonetheless, in 1995 legal action was taken against six community banks to recover $644 and against 77 individual borrowers with delinquent loans totaling $19,370. Individual loans are much larger than community bank loans, and historically, they have had much higher delinquency rates. According to ODEF, this is one reason it is de-emphasizing individual loans and reducing loan terms for individual borrowers.

A2e. Loan Loss Provisioning

ODEF has a policy of maintaining loan loss reserves equivalent to 3 percent of the active loan portfolio. After 180 days, delinquent loans are written off, but collection efforts continue. The current policy does not differentiate between community banks and individual borrowers, but the following new policy was expected to be presented at the March 1997 board meeting:

Delinquency	Community Banks	Individual Loan Program
0-30 days	50% of overdue payments	0
31-60 days	75% of overdue payments	0
60-90 days	100% of outstanding balance	0
120-180 days	100% of outstanding balance	50% of overdue payments
More than 180 days	n/a	100% of outstanding balance

ODEF does not use a portfolio-at-risk formula to calculate loan delinquency rates. The current system measures delinquency by calculating the value of past due payments as a percentage of the total portfolio. This procedure ignores the potential risk of loss should a delinquent loan remain uncollected. At present, ODEF is reporting a delinquency rate of 3.7 percent, close to the acceptable range for NGO financial intermediaries. However, using the portfolio-at-risk formula yields a delinquency rate of 14.1 percent.

In addition to the calculation problems mentioned above, the new provisioning policy is not sufficient to address risk of potential loan loss. The policy should be changed for several reasons:

- No provisions exist for delinquent individual loans until four months have passed. This is too long.

- The use of past due payments to calculate the amount to be provisioned clearly understates the risk of loss. In addition, it postpones recognition of potential loss until six months have passed. ODEF could find itself having to write off 100 percent of an outstanding loan balance with one large provision. This could have a severe and disproportionate impact on the income statement. A more appropriate provision against loan loss on a monthly basis is as follows:

Delinquency	Community Banks	Individual Loan Program
0-30 days	50% of outstanding balance	10% of outstanding balance
31-60 days	75% of outstanding balance	25% of outstanding balance
60-90 days	100% of outstanding balance	50% of outstanding balance
120-150 days	100% of outstanding balance	75% of outstanding balance
180 days	n/a	100% of outstanding balance

A3. Fixed Assets

Fixed assets represent 18.6 percent of total assets, a high ratio for a financial intermediary. Nearly 12.2 percent of total assets (equivalent to $240,000) consist of the land and installations at ODEF's San Pedro Sula office and the Herencia Verde. The land in both locales was donated to ODEF by the municipality of San Pedro Sula, but by agreement, the assets cannot be sold nor used as collateral. Vehicles and motorcycles represent 4.2 percent of total assets.

ODEF has three branch offices, in El Progreso, Choloma, and Santa Barbara. The El Progreso and Santa Barbara offices are rented. The Choloma belongs to ODEF, and the organization has invested about $3,600 to maintain it. ODEF has accumulated depreciation reserves of $45,260 using a straight method of 10 percent per year for vehicles and office equipment, 12.5 percent per year for computers, and 6.67 percent per year for buildings.

ODEF should try to reduce the ratio of fixed assets to total assets. Fixed assets generate no earnings and ODEF needs more liquidity to finance a growing loan portfolio. Since the San Pedro Sula office and the Herencia Verde center cannot be sold, there are only two ways to reduce the fixed asset ratio: (1) increase the value of total assets through growth, or (2) accelerate depreciation of some assets using a more realistic time period. In the latter, for example, computers do not have an active life of eight years and should be depreciated over three to four years. Similarly, vehicles should be depreciated over five years instead of the 10 years now used.

A4. Other Assets

The other assets line item represents 7.7 percent of total assets. The largest component of the other asset account is interest receivable. ODEF uses accrual accounting to book the interest earned on loans as recommended by its external auditor, Price Waterhouse. Accrual accounting tends to inflate earnings by obscuring the risk of interest loss on delinquent loans, and the procedure should be changed. Financial institutions such as ODEF should use cash accounting, and they should only recognize interest earned when it is actually paid. This will avoid inflating both the income statement and the balance sheet.

B. Liabilities

B1. Savings

Honduran legislation prohibits ODEF from mobilizing savings. However, savings are mandatory for all ODEF community bank members, with borrowers required to save the equivalent of 20 percent of loan amounts each time they borrow. Member savings are deposited in a commercial bank account, managed by the community bank's board of directors and monitored by the ODEF credit promoter. Community banks are permitted to use their "internal accounts" to make loans, but this is not a common practice. Many banks are simply afraid to lend to outsiders and would rather maintain deposits in local bank branches where potential problems are avoided.

Community banks having delinquency rates above 5 percent (as measured by delinquent payments) are required to deposit up to 70 percent of their member savings with ODEF as a "guarantee fund." ODEF estimates that it now manages between 30 and 45 percent of total community bank savings in these guarantee funds. A competitive return is paid to the community banks, often 1 to 2 percent higher than commercial banks typically offer small savers. The high rate of interest paid is one reason that many community banks want to maintain a guarantee deposit with ODEF, regardless of whether it is required or not.

As noted earlier, ODEF is actually using a portion of the guarantee funds to finance the loan portfolio, a risky practice given the uncertainty surrounding the application of local banking legislation to NGO financial intermediaries. For example, one could argue that the savings of the community banks are internal to the ODEF system and do not represent deposit mobilization from the general public. This is a reasonable argument once used by emerging credit unions in the 1960s. However, ODEF should seek written clarification from the government if it plans to continue using some portion of the community bank guarantee funds to finance lending. In the meantime, ODEF should discontinue current practice and maintain community bank guarantee funds in a separate, relatively liquid investment account earning the best possible rate of return.

B2. External Sources of Financing

ODEF has obtained substantial external funding for its operations, including loans and grants from international organizations such as the IDB, CRS, CHF, and USAID, and from local organizations such as the Fundacion Covelo, the Honduran Fund for Social Investment (FHIS), and the Federation of Private Development Organizations (FOPRIDEH). Loan terms range from a highly subsidized IDB loan with a 40-year term, 10-year grace period, and 1-percent interest rate, to a loan from FHIS at near commercial rates (i.e., 30 percent). The weighted cost of funds to ODEF in December 1996 was 18.9 percent, significantly below commercial bank rates (between 34 and 40 percent). The external loans now possessed by ODEF include:

Creditor	Loan Amount (lempiras)	Annual Interest Rate
Procatmer Fund	L 6,162,742	26%
IDB	4,459,106	1%
PASI Fund (FHIS)	3,323,663	30%

Creditor	Loan Amount (lempiras)	Annual Interest Rate
Fundacion COVELO	1,952,638	19%
CHF	880,246	17%
FOPRIDEH	566,667	18%
Total	L 17,345,062	

ODEF tried to obtain local commercial bank financing in 1996, but all banks approached wanted real guarantees equal to 150 percent of the loan amount being sought. Since ODEF cannot use the land of its San Pedro Sula office or the Herencia Verde center for collateral, few options exist. ODEF is now negotiating credit insurance from a local company that, if approved, will have an annual cost of 3 percent of the loan amount insured. ODEF is not certain commercial banks will accept credit insurance in lieu of collateral, but it is making an attempt to mobilize additional external resources.

B3. Restricted Donations

In December 1996, ODEF had donations totaling $107,880 (equivalent to 5.5 percent of total assets) from international and local sources (e.g., the IDB and the Fundacion VIDA) to finance some of its future operating costs, as well as those of the Herencia Verde center.

ODEF is now 64 percent financially self-sufficient and appears well capable of meeting the project goal of 100 percent self-sufficiency by the end of the program. However, the Herencia Verde center presents a potential problem. In 1996, the center generated only about 6.9 percent of its operating costs from earned income, and remaining costs were financed with grants. The training center is a small, well-run facility used to train community bank board members and small farmers. It could become a drain on ODEF’s operations once the three-year operating grants from the Fundacion VIDA and Katalysis end.

Herencia Verde operating costs totaled about $100,000 in 1996. After the grant funding ends, ODEF hopes to finance the center from two sources: (1) fees charged for the use of the facilities and (2) income from the sale of eggs, chickens, fish, and vegetables. The center is close to completing construction of a hen house with a capacity for 1,500 chickens and has two small fish ponds and about two vegetable gardens. Under the best conditions, the center’s agricultural produce is unlikely to finance a significant portion of its operating costs. Therefore, ODEF will need to aggressively promote use of the training center by other paying clients, obtain new operating grants, or eventually, rent or close the center.

As an interim step, ODEF should assess the potential to reduce costs. For example, are 15 employees at Herencia Verde absolutely necessary? Salaries represent the largest single cost item, and reductions in staffing could be made without seriously affecting service. Finally, ODEF should consider the potential for establishing Herencia Verde as a separate entity. This would permit the center to seek independent sources of funds and specialize in agricultural training, allowing ODEF to specialize in financial services delivery.

B4. Other Liabilities

In December, the other liabilities line item was $75,310, or 3.8 percent of total assets. The largest single item in the account was the “guarantee funds” of the community banks. These totaled $57,280, or 76 percent of other liabilities.

C. Institutional Capital

Institutional capital totaled $415,641 (L 5,195,516), or 21 percent of total assets. Capital was comprised of donor contributions of $251,280 (L 3,141,011), and retained earnings totaled $164,360 (L 2,054,505), or 39.5 percent of total capital. Donor contributions are as follows:

Donors	Contributions	
	U.S. $	lempiras
Municipality of San Pedro Sula	$ 100,209	L 1,252,609
Fundacion VIDA	77,110	963,874
CRS	24,671	308,397
Katalysis	15,223	190,291
Fundacion COVELO	10,320	129,006
IDB	10,436	130,452
Fondo PROCATMER	6,877	85,965
USAID	6,433	80,417
Total	$ 251,279	L 3,141,011

About 70 percent of the grant capital is represented by the land and buildings of ODEF’s San Pedro Sula office and the Herencia Verde center. Donor capital contributions in 1996 grew by only 7 percent, suggesting a possible reduction in donor funding and reinforcing the need for ODEF to seek alternative financing sources.

ODEF retains all year-end earnings in capital accounts. While there is no specific target for leverage, ODEF had a 4.7 leverage ratio of capital to total assets in December 1996.

D. Income Statement

D1. Revenue

The credit program generates more than 90 percent of operating income. ODEF uses a flat interest rate (34 to 36 percent for community banks and 32 percent for individual loans) and accrual accounting. In addition to the interest rate, ODEF charges clients a 2 percent commission. Accrual accounting inflates total income, particularly when delinquency exists. ODEF should consider using cash accounting (i.e., only recording interest income when it is actually received).

The principal source of ODEF revenue was the interest paid on loans as shown below:

Sources of Revenue	Amount		% of Total Income
	U.S. $	lempiras	
Interest on loans	$ 422,661	L 5,283,264	80.3%
Commissions	28,481	356,009	5.4%
Delinquent charges	21,478	268,484	4.1%
Other financial income	5,885	73,562	1.1%
Total financial income	478,505	5,981,319	90.9%
Nonfinancial income	48,038	600,479	9.1%
Total income before donations	526,543	6,581,798	100.0%

The other nonfinancial income line item ($48,038) primarily consists of charges for paperwork and legal stamps and other costs required by the government. This is equivalent to a 1 percent charge on loan amounts. ODEF also charges borrowers a loan insurance fee equivalent to 0.9 percent for individual borrowers and 1 percent for community banks.

The loan insurance guarantees the family of a borrower that they will not have to repay loan balances if the client dies. ODEF absorbs the insurance risk for loan amounts up to $800 (L 10,000), and for larger loans, contracts insurance coverage from a private firm. Continuing this policy is quite risky. For example, if 10 borrowers with $800 loan balances should die in one year, ODEF would have to absorb an $8,000 loss. ODEF should consider contracting re-insurance to dilute such a risk.

D2. Local Interest Rates

According to ODEF management, commercial banks charge an average of 40 percent for loans, but lend only to well-known clients or those who meet their collateral requirements. Finance companies can charge up to 8 percent a month, but again they lend only to larger clients who possess collateral. The inflation rate is about 26 percent in Tegucigalpa and 30 percent in San Pedro Sula. Formal financial institutions have little (if any) interest in financing ODEF's clientele.

To encourage commercial banks to lower loan interest rates, during 1997 the Honduran Government is planning to reduce the legal reserve requirement from 37 to 34 percent. While the banks are unlikely to significantly lower lending rates, ODEF should closely monitor local financial markets to remain competitive with other NGO-sponsored credit programs.

D3. ODEF Interest Rate Policy and Calculation Method

ODEF charges annual rates ranging from 32 percent for individual loan clients to 34 to 36 percent for community banks. The following demonstrates how individual loans are calculated by using the example of a L 12,000 loan with a 24-month term and a 32-percent interest rate:

$$\frac{\text{Principal (X) Interest Rate (X) Time}}{\text{12 months}} = \frac{12{,}000 \times 0.32 \times 24}{12} = \text{L } 7{,}680$$

Monthly payment:

$$\frac{\text{Principal + Interest}}{\text{Time}} = \frac{12{,}000 + 7{,}680}{24} = \text{L } 820$$

The effective interest rate is 59.29 percent, in between the rates charged by commercial banks and finance companies. At present, this rate is sufficient for ODEF's operations, but it should be reviewed if the situation changes (e.g., the cost of funds increases).

The borrower of the L 12,000 actually receives L 11,532, after discounts are made for the following:

Total loan amount	L 12,000	
Less:		
Commission (2% of loan)		L 240
Paperwork (1% of loan)		L 120
Insurance (0.9% of loan)		L 108
Total deductions	L 468	
Actual amount disbursed	L 11,532	

A flat interest rate is also charged on community bank loans. The rate is 34 percent for first cycle loans and 36 percent for succeeding cycles with biweekly payments.

Community bank members make weekly loan payments to their bank, and the bank makes biweekly payments to ODEF. The following illustrates the calculation for the weekly payment of a community bank client with a L 1,000 loan having a four-month term and a 34-percent annual interest rate:

$$\frac{\text{Principal (X) Interest Rate (X) Time}}{\text{12 months}} = \frac{1{,}000 \times 0.34 \times 4}{12} = \text{L } 113.33$$

Weekly payments:

$$\frac{\text{Principal + Interest+ Obligatory Savings (20\%)}}{\text{Time}} = \frac{1{,}000+113.33+200}{16} = \text{L } 82.08$$

ODEF's loan portfolio yield in December 1996 is calculated as follows:

$$\frac{\text{Revenue generated by loan portfolio (interest, commissions and delinquency charges)}}{\text{Average loan portfolio during period}} = \frac{\text{L } 5{,}907{,}757}{\text{L } 16{,}164{,}580} = 36.55\%$$

D4. Operating Expenses: Cost of Funds

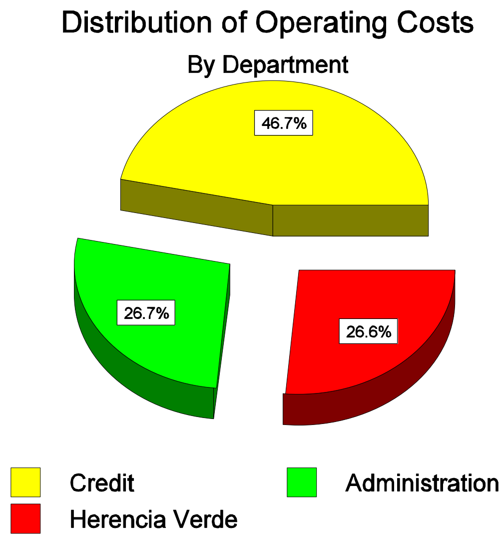
In 1996, ODEF paid $170,825 (L 2,135,309) on an average external debt totaling $1,288,889 (L 16,111,111) for an average financial cost rate (e.g., interest paid as a percentage of the average loans payable) of 13.2 percent. This means that ODEF is operating with a low cost of funds, which likely will change as finding alternative financing sources, including commercial rate loans, becomes necessary. Nonetheless, the 40-year term and low interest rate of the IDB loan provides ODEF a cushion to soften the average cost of future external loans.

Operating costs as a percentage of average assets have declined from 38.4 percent in 1994, to 23.7 percent in 1995, to 16.1 percent in 1996. The 1996 figure is quite good for an NGO financial intermediary working with small credit users. That the operating ratio has declined over the last three years illustrates both the growth of assets and improved efficiency in providing for borrower follow-up. Operating costs in 1996 were distributed as follows:

Line Item	Amount (lempiras)	Percentage
Salaries and other personnel costs	L 2,215,409	61.6%
Professional fees	166,259	4.6
Depreciation	248,123	6.9
Maintenance of fixed assets	416,541	11.6
Other costs	552,574	15.3
Total	L 3,598,906	100.0%

Salaries. Salaries and related staff costs represented 61 percent of total operating costs. Salaries are competitive with other NGOs, but below the wages of comparable staff at commercial banks.

Staff/client ratios vary and depend greatly on whether the banks and individual borrowers are in rural or urban locales. Promoters and supervisory field staff manage an average of 22 community banks or 130 individual borrowers. The ratio of individual borrowers to staff appears low (i.e., best practice recommends an average of 220 per credit agent), but ODEF is reducing lending to individuals and increasing its community bank portfolio. Staff are promoting creation of new banks while also following up on the outstanding portfolio. Promoters typically attend 25 to 35 urban banks, but in rural areas they can only attend a maximum of 25 due to the distances involved and the difficulty in moving from one town to another.



ODEF starting salaries for promoters range from $80 to $96 monthly, with an increase after a two-month trial period. After two years, monthly promoter salaries average between $136 and $152, which is considered competitive with other NGO operations. ODEF experimented with hiring "experienced" staff from other similar programs, but most were unable or unwilling to adapt to ODEF policies and operating procedures. The organization now has a policy of hiring recent high school graduates and training them. This has worked well. There is no formal incentive program for ODEF staff, but an end-of-the-year bonus is given to all staff if financial results are positive.

As noted earlier, ODEF's depreciation method should be changed to reflect the real expected life of vehicles and computer equipment.

SECTION IV
REASONABLENESS OF YEAR 1 TARGETS

The three-year USAID grant to Katalysis is expected to permit the Organization for Women's Enterprise Development to reach full financial self-sufficiency by October 1999. Approximately $651,000 from USAID and $265,000 from Katalysis will be used to increase ODEF's capital. By the end of the grant, ODEF is expected to have 510 community banks operating with about 12,408 members as well as 231 individual clients.

In December 1996, ODEF was ahead of schedule in meeting the year 1 targets of the grant agreement (outlined in Table 1 on page 23). During the year, ODEF disbursed $871,223 to 6,857 village bank clients, doubling its village bank portfolio. In addition, 456 individual clients received $682,850 in credit, a 40 percent reduction in individual lending over 1995. The shift from individual to community bank lending was one goal of the program. ODEF was also capable of covering 103 percent of operating costs from earned income and had reached the year 1 target of 61 percent financial self-sufficiency, with seven months to spare.

Loan delinquency. At 14.1 percent, loan delinquency was much higher than the 3 percent target, and the long-run loss rate (4.3 percent) was higher than the 2.5 percent target. The difference is primarily due to ODEF's use of delinquent payments rather than the portfolio-at-risk to calculate and report its delinquency rate. The same error was found in the 1995 Katalysis grant proposal, which listed delinquency as 3.68 percent, not the actual 14.97 percent. Most delinquent accounts were 30 to 60 days past due, at which point recovery was much better due to the use of a lawyer. As the program grows, ODEF will need to closely monitor the quality of its loan portfolio by addressing the real risk of loss. Finally, as noted in Section III (pages 12-13), ODEF needs to adopt a provisioning policy that avoids inflating loan portfolio value while assuring sufficient reserves to write down unrecoverable loans.

Program financing. Finally, the most significant issue likely to affect ODEF's ability to meet the grant targets is availability of sufficient financing. According to the proposal, by the end of the grant ODEF plans to have 510 community banks operating with an outstanding portfolio of $1,051,266 (L 14,192,096) and a separate individual loan portfolio of $382,500 (L 5,163,754). Total financing projected necessary was $1,433,766.

This projection has two key problems:

- The projected exchange rate used for year 3 of the grant (L 13.5 = $1.00) is not realistic given the rate was L 12.6 = $1.00 in January 1997, almost two and a half years before the grant ends.

- Katalysis projected a loan average of $85 per community bank member, which is below the maximum loan size for first-cycle borrowers ($95).

It seems more likely the average member in the 510 community banks will be in his or her fifth cycle. This would require a loan portfolio of about $3,102,000.

In December 1996, ODEF had a loan portfolio of $1,468,307 (L 18,500,670), including 175 community banks and 1,485 individual borrowers. Little was available to finance additional lending, though ODEF will need a minimum $1.6 million in additional capital to finance the 510 community banks and additional resources to finance the individual loan portfolio. As noted earlier, obtaining a secure source of financing should be a priority over the next year.

Formulas:

$$\frac{\text{Net Result (L 751,976)}}{\text{Total Revenue (L 6,581,798)}} = 0.114 \qquad \frac{\text{Total Revenue (L 6,581,798)}}{\text{Total Assets (L 24,731,355)}} = 0.266 \qquad \frac{\text{Total Assets (L 24,731,355)}}{\text{Equity (L 5,195,516)}}$$

Profit Margin times Turnover = 4.76

=

Return on Assets times Leverage

= 3%

Return on Equity = 14.4%

Table 1. Summary of Year 1 Targets (October 1996-September 1997) and Values as of December 1996 (Lempiras)

	Baseline Year Dec. 1995	Projected Year 1	Actual Dec. 1996	% Variance
Activities				
1. Amount of loans, start of year *	4,713,243	14,057,124	13,828,491	-1.6%
2.a. Amount of loan, end of year, CBs	2,108,569	4,352,283	5,089,250	16.9%
2.b. Amount of Loans, end of year, ILP	11,948,555	12,903,344	13,411,420	3.9%
2.c. Total Loans Outstanding *	**13,828,491**	**17,255,627**	**18,500,670**	**7.2%**
3. Average amount of loans outstanding	9,270,867	15,656,376	16,164,581	3.2%
4.a. No. loans outstanding, end year, CBs	2,156	4,906	7,172	46.2%
4.b. No. loans outstanding, end year, ILP	978	435	1,485	241.4%
4. Total No. loans outstanding, end of year	**3,134**	**5,341**	**8,657**	**62.1%**
5.a. Average loan size (CB program)	978	887	710	-20.0%
5.b. Average loan size (IL program)	12,217	29,663	9,031	-69.6%
5. Average loan size	**4,412**	**3,231**	**2,137**	**-33.9%**
6. Delinquency (portfolio at risk) **	14.97%	3.00%	14.14%	371.4%
7. Long-run loss rate **	7.6%	2.5%	4.3%	75.7%
Interest Rates				
8.a.a. Nominal interest rate charged/CBs	28.0%	34.0%	34.0%	
8.a.b. Nominal interest rate charged/ILP	28.0%	32.0%	32.0%	
8.b.a. Annual effective rate/CBs	47.0%	57.0%	57.0%	
8.b.b. Annual effective rate/ILP	47.0%	53.0%	53.0%	
9. Local interbank lending rate	32.3%	30.0%	34.0%	
10. Inflation rate	29.5%	25.0%	30.0%	
Client Revenues				
11.a. Interest income (CBs)	not available	1,519,768	not available	n/a
11.b. Interest income (ILP)	not available	4,135,154	not available	n/a
11.c. Total interest income from clients	**2,037,253**	**5,654,922**	**5,551,748**	**-1.8%**
12. Fee income from clients	356,546	599,759	356,009	-40.6%
13. Total client revenues	**2,393,799**	**6,254,681**	**5,907,757**	**-5.5%**
Nonfinancial Expenses				
14. Administration, including salaries	3,197,054	4,381,259	3,350,774	-23.5%
15. Depreciation of fixed assets	0	316,797	248,123	-21.7%
16. Loan loss provisions	452,755	469,661	95,616	-79.6%
17. Total nonfinancial expenses	**3,649,809**	**5,167,717**	**3,694,513**	**-28.5%**
Adjusted Financial Expenses				
18. Adjusted financial expenses	**2,994,490**	**4,696,913**	**5,495,957**	**17.0%**
Totals				
19. Expenses	**6,644,299**	**9,864,630**	**9,190,470**	**-6.8%**
20. Return on operations	**36.03%**	**63.41%**	**64.28%**	**101.4%**

* Adjusted to reflect audited portfolio balance in December 1995.

** The delinquency rate for 1995 was stated as 3.68 percent, but that was based on delinquent payments rather than using the portfolio-at-risk formula required by G/EG/MD. The assessment team recalculated the actual amount of loans delinquent for 30 or more days for 1995 and 1996, and arrived at adjusted rates of 14.97 and 14.14 percent. The same procedure was used to obtain the adjusted long-run loss rates.

KEY: CBs = community banks; ILP = individual loan program.

ANNEX A

ODEF BALANCE SHEET AND INCOME STATEMENT DATA

Organization for Women's Enterprise Development

Balance Sheet

	1993	1994	1995	1996
Cash & Banks	0	15,903	2,000	2,000
Investments	1,649,935	970,890	1,107,520	286,463
Loan Portfolio	908,185	4,202,325	13,529,189	17,942,354
Fixed Assets	825,257	1,421,344	3,997,990	4,590,507
All Other Assets	99,411	596,328	1,142,505	1,910,031
Total Assets	**3,482,788**	**7,206,790**	**19,779,204**	**24,731,355**
Savings	0	0	0	0
Subsidized Loans	636,500	2,930,454	14,976,272	17,245,950
Commercial Loans	380,884	1,319,440	579,206	941,386
Deferred Liabilities	292,951	1,112,982	0	1,348,503
Other Liabilities	15,545	87,611	0	0
Sub-Total Liabilities	**1,325,880**	**5,450,487**	**15,555,478**	**19,535,839**
Restricted Donations	249,030	0	0	
Donations to Capital	885,815	1,701,611	2,921,196	3,141,011
Accumulated Results	1,022,063	54,692	1,302,530	2,054,505
Sub-Total Equity	**2,156,908**	**1,756,303**	**4,223,726**	**5,195,516**
Total Liabilities & Equity	**3,482,788**	**7,206,790**	**19,779,204**	**24,731,355**

Income Statement

	1993	1994	1995	1996
Earned Income	436,385	1,184,811	3,284,552	6,581,798
Cost of Funds	144,468	172,075	1,042,239	2,135,309
Gross Margin	291,917	1,012,736	2,242,313	4,446,489
Operating Expenses	2,051,327	2,051,735	3,201,857	3,598,897
Loan Loss Provisions	0	257,021	452,755	95,616
Net Result	**(1,759,410)**	**(1,296,020)**	**(1,412,299)**	**751,976**
Extraordinary Income	2,340,890	1,616,199	1,541,536	639,472
Net Income	581,480	320,179	129,237	1,391,448

BALANCE SHEET

O.D.E.F.

	12/31/93	% Total Assets	12/31/94	% Total Assets	12/31/95	% Total Assets	12/31/96	% Total Assets
ASSETS								
Cash	0	0.00%	15,903	0.21%	2,000	0.01%	2,000	0.01%
Deposits in Other Financial Institutions	1,649,935	47.37%	949,721	12.72%	1,107,520	5.60%	286,463	1.16%
Loans Outstanding	1,029,794	58.25%	4,713,243	41.14%	13,828,491	41.14%	18,500,670	74.81%
Less Allowance for Bad Debts	(121,609)	-3.49%	(153,467)	-2.05%	(299,302)	-1.51%	(558,316)	-2.26%
Loans Outstanding (Net)	908,185	26.08%	4,559,776	61.05%	13,529,189	68.40%	17,942,354	72.55%
Accounts Receivable	95,514	2.74%	482,821	6.46%	1,067,484	5.40%	1,910,031	7.72%
Other Assets	3,897	0.11%	45,144	0.60%	75,031	0.38%	0	0.00%
Fixed Assets (Net)	825,257	23.70%	1,415,290	18.95%	3,997,980	20.21%	4,590,507	18.56%
Total Assets	**3,482,788**	**100.00%**	**7,468,655**	**100.00%**	**19,779,204**	**100.00%**	**24,731,355**	**100.00%**
LIABILITIES								
Notes Payable	1,017,384	29.21%	4,249,894	56.90%	14,980,186	75.74%	17,245,950	69.73%
Other Liabilities	308,496	8.86%	107,114	1.43%	575,293	2.91%	2,289,889	9.26%
Total Liabilities	1,325,880	38.07%	4,357,008	58.34%	15,555,479	78.65%	19,535,839	78.99%
INSTITUTIONAL CAPITAL								
Donations	1,134,845	32.58%	1,696,550	22.72%	2,921,196	14.77%	3,141,011	12.70%
Retained Earnings and Other Reserves	1,022,063	29.35%	1,415,097	18.95%	1,302,529	6.59%	2,054,505	8.31%
Total Institutional Capital	2,156,908	61.93%	3,111,647	41.66%	4,223,725	21.35%	5,195,516	21.01%
Total Capital	2,156,908	61.93%	3,111,647	41.66%	4,223,725	21.35%	5,195,516	21.01%
Total Liabilities and Capital	**3,482,788**	**100.00%**	**7,468,655**	**100.00%**	**19,779,204**	**100.00%**	**24,731,355**	**100.00%**

INCOME STATEMENT

O.D.E.F.

Income:	12/31/93	% Total Income	12/31/94	% Total Income	12/31/95	% Total Income	12/31/96	% Total Income
Interest on Loans (Less Rebates)	245,905	56.4%	890,588	75.2%	1,944,681	66.1%	5,283,264	80.3%
Delinquent Penalty Interest Income	0	0.0%	33,519	2.8%	92,572	3.1%	268,484	4.1%
Commissions / Fees - Loans	30,111	6.9%	147,149	12.4%	356,546	12.1%	356,009	5.4%
Net Income - Loans	*276,016*	*63.3%*	*1,071,256*	*90.4%*	*2,393,799*	*81.4%*	*5,907,757*	*89.8%*
Interest on Savings Deposits	0	0.0%	0	0.0%	64,366	2.2%	73,562	1.1%
Other Income	160,369	36.7%	113,555	9.6%	483,910	16.4%	600,479	9.1%
Total Income	436,385	100.0%	1,184,811	100.0%	2,942,075	100.0%	6,581,798	100.0%
Expenses:								
Financial Expenses								
Interest on Notes Payable	144,468	33.1%	172,075	14.5%	1,042,239	35.4%	2,135,309	32.4%
Other Financial Costs	0	0.0%	0	·0.0%	0	0.0%	0	0.0%
Total Financial Expenses	144,468	33.1%	172,075	14.5%	1,042,239	35.4%	2,135,309	32.4%
Operating Expenses								
Operating Expenses	2,051,327	470.1%	2,289,026	193.2%	3,197,054	108.7%	3,598,897	54.7%
Total Operating Expenses	2,051,327	470.1%	2,289,026	193.2%	3,197,054	108.7%	3,598,897	54.7%
Bad Debt Provisiones	0	0.0%	257,021	21.7%	452,755	15.4%	95,616	1.5%
Income from Operations	(1,759,410)	-403.2%	(1,533,311)	-129.4%	(1,749,973)	-59.5%	751,976	11.4%
Other Income / Expenses								
Donations	2,340,890	536.4%	1,926,345	162.6%	1,637,405	55.7%	639,472	9.7%
Net Income	581,480	133.2%	393,034	33.2%	(112,568)	-3.8%	1,391,448	21.1%

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ANNEX B
LIST OF MICROSERVE PUBLICATIONS

1. “Microfinance Training Course Evaluation and Completion Report,” April 19, 1996.

2. “Assessment of Microenterprise Support Institutions for USAID Sri Lanka: The Micro Enterprise Support Activity,” by Cary Wingfield Raditz, June 25, 1996.

3. “Microfinance Workshop for the West Bank and Gaza Completion Report,” by Dale W. Adams and Fernando Cruz-Villalba, July 29, 1996.

4. “Evaluación de la Propuesta de Constitución del Fondo Financiero Privado para el Fomento de Iniciativas Económicas,” by Miguel A. Rivarola, October 1996.

5. “Evaluación y Análisis de la Foundación para la Producción (FundaPro),” by Mario Dávalos, October 1996.

6. “Consideration of a Merger between the Sartawi Foundation and the Agrocapital Foundation,” by Ken L. Peoples, November 1996.

7. “Women’s Enterprise Development Project: Mid-Term Evaluation Report,” by Meliza H. Agabin, Jeanne Koopman, and Harunur Rashid, December 1996.

8. “Revisión del Sistema de Informática del Centro de Fomento a las Iniciativas Económicas,” by Robert Boni, April 1997.

9. “The Organization for Women’s Enterprise Development: Institutional Assessment Report,” by Oscar Oswaldo Oliva V. and Barry Lennon, June 1997.