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IKONGO DUE DILIGENCE

FINAL REPORT



July 2006

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Rural SPEED

Rural Savings Promotion & Enhancement of Enterprise Development

IKONGO DUE DILIGENCE

FINAL REPORT

The author's views expressed in this publication do not necessarily reflect the views of the United States Agency for International Development or the United States Government.

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TABLE OF CONTENTS

| | |
|---|----------|
| Executive Summary | i |
| Background | 1 |
| Introduction | 1 |
| Qualifiers | 1 |
| Governance Effectiveness And Strategy | 2 |
| Management Effectiveness | 3 |
| Product Development And Delivery..... | 3 |
| Asset-And-Liability Management | 3 |
| Accounting And Financial Management | 4 |
| Financial Sustainability | 4 |
| Rural Outreach..... | 4 |
| Prudence and Transparency in Product Pricing..... | 4 |
| Financial Transparency..... | 5 |
| Summary of Scores by Assessment Area | 6 |
| Conclusion | 7 |
| Appendix 1 Persons Interviewed..... | 8 |

EXECUTIVE SUMMARY

Ikongo SACCO is a relatively young institution whose operations and performance are still lacking in many areas. Despite this however, it has shown a good measure of maturity as far as governance and management is concerned. This has been translated into a steady and robust business growth.

This has been the first assessment of this nascent institution and despite critical operational issues that have undermined its good progress/ performance; it shows very strong indications of sustainable growth, viability, efficiency and outreach.

The SACCO has to address itself to the following areas: portfolio management, asset/ liability management, financial transparency and product pricing. Being a young institution, Ikongo has not had quite sufficient trainings to make it strong in those areas so once it is given the necessary technical support, it will make tremendous improvement. This explains its average health and performance.

BACKGROUND

Introduction

In June/ July 2006, The USAID- Rural SPEED Project contracted FRIENDS Consult Ltd to conduct a due diligence of Ikongo Rural Cooperative Savings & Credit Society Ltd in Bwera Township Kasese District. The objective of the due diligence was two-fold:

- i) To assess the governance/ operational position and performance of the SACCO in order to provide Rural SPEED with a fair view of the SACCO's progress since it became a partner, and point out areas of further training/ TA needs;
- ii) To train two MDI staff on the job, equipping them with the knowledge of the structure and usage of the tool.

The assessors held free and uninterrupted discussions, and had access to the SACCO documents and records in the course of the assessment. Below is a report covering all areas assessed.

This report is based on a one-day, limited due diligence and is in no way a substitute for external audit, internal audit or extended/in-depth due diligence in circumstances where any of these would be required.

QUALIFIERS

Does the SACCO have?

| | Yes | No |
|--|-----|----|
| 1. A Valid registration certificate from the Department for Cooperatives? ¹ | √ | |
| 2. Identifiable place of business where they carry out their activities? | √ | |
| 3. At least one full time staff? | √ | |
| 4. Financial services as its core business? No other business | √ | |
| 5. Active loans and savings operations? | √ | |
| 6. An active Board/ Committee Directors | √ | |

¹ An institution that is, at the time of the assessment, changing its form from NGO or any other into a cooperative has for this purpose be deemed to be registered as a cooperative society

RATERS**GOVERNANCE EFFECTIVENESS AND STRATEGY**

| ASSESSMENT QUESTIONS <i>Does the SACCO have...</i> | MAX SCORE | SCORE | REMARKS |
|---|------------------|--------------|--|
| Full control of its affairs resting on the membership, board and management, with no external superior authority? | 2 | 2.0 | AGM sits annually, is supreme organ. Board minutes show well laid out policy issues clearly discussed and decided on. No external control |
| An able board, with the right skills and dedication to move it forward? | 2 | 1.0 | C/man-Diploma (Theology), Vice C/man-Enrolled Nurse (2), Treasurer–Degree (Theology), 4-“O” – level board members, 1-Senior Two (S.II). |
| A clear governance structure? | 2 | 2.0 | AGM has ultimate authority. Board & audit committees elected by the AGM, Board appoints staff, constituted the loans committee and oversees the SACCO operations. Committees present include; audit (3), loans (3), human resources (3) & education (3) committees. Clear reporting relationships in place. Some mild element of founder members |
| Well laid out and followed responsibility and accountability practices for all organs & persons? | 2 | 1.0 | No well-articulated scope of work/ responsibilities of committees. Board to AGM accountability present, minuted & resolutions implemented promptly. Management to Board accountability inadequate; Reports from Mgmt to BOD lack financial and profitability analysis. Loans to Directors tracked & within acceptable limits. |
| A clear ownership structure? | 2 | 2.0 | Interviewed members demonstrated a high sense of ownership, share holders register in place & up-to-date, share certificates issued after full payment shares applied for; all members, however, vote at AGM. |
| A focus on the savings and credit business? | 2 | 2.0 | Savings and credit services to members is the core business of the SACCO |
| A strategic/ business plan, supporting the mission that is followed? | 2 | 2.0 | Ikongo SACCO has a business plan. Membership, savings, loans targets are embedded, followed and superceded. SACCO preparing a revised 5 year business plan |
| Beneficial linkages with external Partners | 2 | 2.0 | UCA Ltd, Rural SPEED, Princon, SUFFICE, AMFIU |
| Its by-laws, constitution, or such other internal governance guidance documents? | 2 | 2.0 | UCA Ltd generic by-laws in place, Generic operational & policy documents developed by UCA Ltd in present. |

MANAGEMENT EFFECTIVENESS

| | | | |
|---|---|-----|--|
| Management staff with suitable qualifications and experience to manage the SACCO? | 2 | 2.0 | Manager has BBA (Acc) with two years credit experience, Accountant-Diploma(Acc) with 14yrs experience as Acc Assistant, Loans Officer-3yrs working exp, Cashier & Cr.O – Diplomas in business studies |
| A balance of focus between profit & development in the SACCO operations? | 2 | 1.0 | SACCO offers mainly member-based savings & portfolio management training. No development focused member training |
| Observable business growth? | 2 | 2.0 | Savings grew by 48%, loans-65% and membership-16% for the period Dec'05 – 30 April. Annualized, this would be 144% for savings, 195% for loans and 48%. Save for the membership growth, the other indicators are almost astronomical. Ikongo is young and hopefully this growth will stabilize at some lower but healthy levels. |

PRODUCT DEVELOPMENT AND DELIVERY

| | | | |
|--|---|-----|---|
| Variable and adaptable products? | 2 | 2.0 | Savings – voluntary & fixed deposits Loans–commercial, school fees loans, emergence loans, agricultural loans with varied rates and terms. |
| Documented operational policies and procedures | 2 | 2.0 | Accounting/financial mgt manual, credit manual, HR manual, credit manual in place. |
| Efficiency in service delivery mechanisms? | 2 | 0.5 | Loans committee sits once a month |

ASSET-AND-LIABILITY MANAGEMENT

| | | | |
|---|---|-----|---|
| Effective delinquency management? | 2 | 0 | Portfolio fairly aged with PAR > 30days at 36% |
| Safety of clients' deposits? | 2 | 1.0 | Ikongo SACCO has strong room (but with wooden doors), the till limit of 2 million is respected. No cash insurance cover. |
| Moderate gearing? | 2 | 2.0 | Debt: Equity ratio of 2:1 as at April, 2006 |
| Prudence in intermediation? | 2 | 0.5 | Savings/Cash cover of 16% as at April, 2006. Ikongo SACCO is undercapitalized, relying heavily on savings of members to lend, resulting in this over-intermediation |
| Proper assessment of borrowers & anti-concentration | 2 | 0.5 | Poor borrowers assessment (no cash flow assessment) |
| Clear documentation of loans, savings, other assets and liabilities | 2 | 2.0 | Loans are well documented, savings ledger promptly posted and documented, fixed deposit ledger is properly maintained, loans payable account with MSC well kept. securities poorly appraised and documented, fixed assets register poorly maintained, |

ACCOUNTING AND FINANCIAL MANAGEMENT

| | | | |
|---|---|-----|--|
| A proper bookkeeping system? | 2 | 1.0 | Double entry, cash based accounting system in place; cashbook in place & up-to-date; Depreciation not done, Fixed asset register poorly kept, No loan loss provision, No balanced off general ledger |
| A suitable accounting system? | 2 | 1.5 | Monthly financial reports up-to April, 06 in place, audit conducted by an independent auditor – Mark House |
| Proper financial management principles? | 2 | 1.0 | Annual budget in place but not tracked on monthly basis, budgetary controls and variance analysis not done. |
| Documented accounting & financial management manual | 2 | 2.0 | Accounting & financial management manual in place and followed. |

FINANCIAL SUSTAINABILITY

| | | | |
|---|---|-----|--|
| Measures of sustainability consistently monitored? | 2 | 0.5 | OSS and FSS not regularly monitored and their targets are not in the business plan |
| Good levels of operational and financial sustainability? | 2 | 0.5 | OSS of 106% before the loan loss provisions and depreciation charge. |
| Profitability and sustainability embedded in business plans | 2 | 1.0 | Sustainability not well embedded & articulated in the business plan. Profitability is articulated. |

RURAL OUTREACH

| | | | |
|------------------|---|-----|--|
| Rural operations | 2 | 2.0 | The SACCO is rural based located at Bwera Township in West Bukonzo County – Kasese |
|------------------|---|-----|--|

PRUDENCE AND TRANSPARENCY IN PRODUCT PRICING

| | | | |
|---|---|-----|---|
| All direct and indirect overhead costs taken into account in determining interest rates and fees | 2 | 1.0 | Direct & indirect costs not considered. SACCO needs to increase its operations and do a proper costing exercise |
| Market rates charged by competitors taken into account in determining interest rates and fees | 2 | 2.0 | Charges proposed by UCA Ltd & Princon with reference to other SACCO and competitors such as FINCA, PRIDE, CERUDEB, and Stanbic. |
| All interest rates and charges displayed and fully disclosed to the client before they decide to borrow | 2 | 0.5 | Entry costs displayed, however interest rates, charges, and fees are not displayed. Members know costs on loan application. SACCO urged to translate cost schedule into local language. |

FINANCIAL TRANSPARENCY

| | | | |
|----------------------|---|---|---|
| General Ledger | 6 | 4 | <ul style="list-style-type: none"> • MSCL loans payable properly documented and recorded, • Share holders register up-to-date, properly maintained and reconciled with general ledger, • Fixed assets register poorly maintained and improvements proposed • Bank reconciliation not regularly done |
| Customer savings | 6 | 6 | <ul style="list-style-type: none"> • Savings and withdrawal are prompt, • Five clients' savings deposit slips and passbooks traced and reconciled with savings ledgers • Traced and agreed five member withdrawal slips and passbooks to their ledger and cash tills • No interest paid on savings |
| Loan/ Credit Ledger | 6 | 4 | <ul style="list-style-type: none"> • Reconciled three loan clients to loan ledgers • MSCL loan payable well maintained but no cheque numbers reflected • Interest income is calculated and posted on cash-basis • Loan ledger maintained and up-to-date but deliberately poorly aged |
| Income | 6 | 3 | <ul style="list-style-type: none"> • Interest income properly & prudently recognized • LLR & depreciation are not provided for & therefore income overstated • Interest and non-interest incomes recognized on cash basis |
| Expenditure | 6 | 3 | <ul style="list-style-type: none"> • Traced rent expense to waste sheets & income statements • Security properly posted and reconciled to the income statements & expenditure registers • Salary costs properly posted and reconciled off to the GL account. |
| Loan loss provisions | 6 | 2 | Loan aging is done of recent on monthly basis but loan provisioning is not done at all. |

SUMMARY OF SCORES BY ASSESSMENT AREA

| ASSESSMENT AREA | MAX SCORE | SCORE |
|--|------------------|--------------|
| Governance Effectiveness and Strategy | 18 | 16 |
| Management Effectiveness | 6 | 5 |
| Product Development and Delivery | 6 | 4.5 |
| Asset-and-Liability Management | 12 | 6 |
| Accounting and Financial Management | 8 | 5.5 |
| Financial Sustainability | 6 | 2 |
| Outreach | 2 | 2 |
| Prudence and transparency in product pricing | 6 | 3.5 |
| Financial Transparency | 36 | 22 |
| TOTAL | 100 | 66.5 |

SCORE INTERPRETATION GUIDELINES

| SCORE | INTERPRETATION |
|--------------|---|
| Over 80% | A promising institution with a nearly all the requisite structures and systems in place thus there is potential for high performance in most areas |
| 70-79 | A fairly promising institution with most of the requisite structures and systems in place, though in need of improvement. Performance and impact could be greatly enhanced through focused and well targeted technical and/ or financial assistance |
| 60-69% | <i>Average institutional health and performance. Careful discretion needs to be exercised in determining whether or not the institution is suitable</i> |
| 50-59 | Poor health and performance. Deep rooted weaknesses are likely to hinder any potential impact of BDS, technical or financial assistance. |
| Below 50% | Just a non-starter; do not enter the relationship. |

CONCLUSION

For its age and location, Ikongo Rural Savings and Credit Cooperative Society is doing well in areas like governance and reasonably well in management effectiveness and service delivery. However, it needs to improve in a number of areas like asset/liability management (delinquency management particularly), product pricing, financial transparency and sustainability. The 66.5% overall score makes the SACCO, according to the Tool interpretation guidelines, one with “average institutional health and performance. Careful discretion needs to be exercised. Targeted technical assistance would help in the identified weak areas of:

- Documentation of the roles and responsibilities of the different governance organs
- Slow speed of service delivery
- Poor delinquency management
- Inadequate deposit/ cash safety provisions
- Over-intermediation of deposits
- Inadequate borrower assessment, especially in regard to their ability to service the loans (cash flow assessment)
- Unsystematic accounting for fixed assets and depreciation
- Loan loss provisioning
- Sustainability tracking
- Improper costing and pricing of products
- Bank reconciliation and related book keeping aspects

APPENDIX 1 PERSONS INTERVIEWED

| | |
|---------------------------------------|-------------------------|
| Phillip Kanakalere | Board Secretary |
| Rev. Canon Ivan Bwambale Sibithondere | Treasurer |
| Damalie Tibwiita | Board members |
| Kanyanya Tom | Board members |
| Kule Edmond | Board members |
| Basiima K. Emeny | Member, audit committee |
| Muhindo Benjamin | SACCO Manager |
| Some staff and members | |

TRAINEES (BOTH FROM UML)

Andrew Gidudu
 Wilfred Bwambale of Uganda Microfinance Limited

The trainees rated the tool highly, expressed immense enthusiasm and demonstrated high comprehension levels in their ability to use the tool.