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SACCOS DELINQUENCY MANAGEMENT AND INTERNAL CONTROL MENTORING

FINAL REPORT

March 2006

This publication was produced for review by the United States Agency for International Development. It was prepared by Thomas K. Shaw, a Consultant for Chemonics International Inc.

Rural SPEED

Rural Savings Promotion & Enhancement of Enterprise Development

SACCOS DELINQUENCY MANAGEMENT AND INTERNAL CONTROL TRAINING

FINAL REPORT

Rural SPEED
A USAID funded project
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Executive Summary

Since 1987, the Government of Uganda (GOU) has instituted major economic policy reforms to encourage the financial sector to become increasingly efficient, productive, and competitive. Uganda is well on its way to having a vibrant and reasonably deep financial services sector, with fifteen commercial banks, seven commercial credit institutions, four licensed and one potentially licensed micro-deposit taking institutions (MDIs), numerous microfinance institutions (MFIs), and member-owned savings and credit cooperatives (SACCOs). Despite recent growth and liberalized economic policies, only ten percent of the rural population has access to basic financial services. In addition, both the formal and the informal financial sectors still require structural changes to be able to provide the range and depth of financial services that individuals and businesses require.

USAID/Rural SPEED's objective is to deepen and strengthen Uganda's financial sector in response to this rural sector demand for financial services. The increased provision of financial services should leverage economic activity to complement other USAID/Mission programs in rural areas. The resulting increase in economic activity should aid the GOU in achieving the target economic growth rates proposed in Poverty Eradication Action Plan. The USAID/Rural SPEED project is supporting and executing activities in the following areas:

- Institutional Capacity Building; and
- New Product Development and Service Delivery

The principle activity accomplished under this consultancy was the organization of a three-day training workshop on delinquency management and a series of follow-up mentoring visits. The purpose of this workshop was to help participants from eighteen SACCOs understand delinquency, analyze and determine its causes, learn how to measure it, learn how to use ratio analysis, discuss strategies for controlling and preventing it, and to prepare for implementation a SACCO delinquency management plan. To achieve this, the training looked at:

- Loan delinquency (definitions);
- Delinquency warning signs;
- Causes of delinquency;
- Measuring delinquency;
- Compensating for loan loss risk and loan loss write-offs; and
- How to develop strategies for delinquency management

After completing the topics in the training guide, the participants prepared delinquency management plans for their SACCOs, based on a standard format. The delinquency management plans were then presented to the workshop participants for additional comments and suggestions. While some of the plans were well structured and well presented (Kyamuhunga and Masaka), there is still a need to improve and refine the plans. To address this concern, ten one-day mentoring visited were conduced to seven of the current USAID/Rural SPEED partner SACCOs and to three additional SACCOs, which are being considered for future partnership.

During these mentoring sessions the boards expressed a strong concern for better delinquency management, now that they fully understood the immensity of the issue. Additional assistance mentoring assistance is necessary to encourage and empower the boards to make the difficult decisions needed to bring delinquency to the recommended best practice benchmarks of PAR > 1 day ≤ 5% and PAR > 30 days ≤ 2%.

As such it is recommended that:

1. USAID/Rural SPEED should address a letter to each one of the partner SACCOs requesting a detailed copy of their revised delinquency management plan.

2. Once the revised delinquency management plans are received, USAID/Rural SPEED needs to make sure that it is monitoring their progress through periodic mentoring visits. This is extremely important. It will ensure that the boards stay focused on the tasks and do not become discouraged if the expected change is not quick in coming.

3. Of the three potential (new) SACCO partners visited, it is strongly discouraged that USAID/Rural SPEED selects Bugongi. This SACCO's board is too weak to make substantial changes in the project's remaining time period. The management is weak as well and there is no adequate information management system. While they can still be invited to training programs, if space is available, they should not become partners.

4. In addition, if Kajara is retained as a SACCO partner, they should be given the accounting and financial management training that they did not receive last year. It is very important that the board treasurer, accountant and manager understand and apply the proper accounting principles and practices to bring the entire financial management system up to best practice standards.

5. USAID/Rural SPEED needs to follow up on SACCO loan loss provisioning and loan write-off. Loan loss write-offs must be done for loans, which are more than 360 days past due. The technical note presented in Appendix J should be distributed to each SACCO and a follow-up visit scheduled

6. In order for SACCOs to produce loan loss ratios in a timely and accurate manner better software is required. Currently, SACCOs waste a lot of time on report compilation and have no time left for management.

   The current software, Financial Solutions, is grossly inadequate. Not only does it not do many of the operations that a MFI needs, it does others totally incorrectly. Its delinquency calculations are based on overdue installment principal and not outstanding principal for delinquent loans. This leads to an under-evaluation of actual risk by 25% or more and an over estimation of the number of delinquent loans, which are counted more than once, if several installments are past due.

7. The final missing piece for successful implementation of the delinquency management plan is the provision business analysis skills:

If the delinquency management plans are formalized and implemented, as discussed during the mentoring visits, then the SACCOs should be able to make dramatic reductions in delinquency by the end of 2006. Loan delinquency management is a complicated process and often takes six or more months to address effectively. The higher the current PAR ratios the longer it may take to address the underlying problems. Close supervision of progress will be necessary to keep the SACCOs focused on the issue until it is brought under control.

Background

Introduction

Since 1987, the Government of Uganda has instituted major economic policy reforms to encourage the financial sector to become increasingly efficient, productive, and competitive. Uganda is well on its way to having a vibrant and reasonably deep financial services sector, with fifteen commercial banks, seven commercial credit institutions, four licensed and one potentially licensed micro-deposit taking institutions, numerous microfinance institutions, and member-owned savings and credit cooperatives. Despite recent growth and liberalized economic policies, only ten percent of the rural population has access to basic financial services. Both the formal and the informal financial sectors still require structural changes to be able to provide the range and depth of services that individuals and businesses require.

Commercial lending and the majority of microfinance lending activities remain confined to urban and peri-urban areas due to the high cost and low return of rural outreach. In addition, interest rates remain high, adequate forms of collateral do not exist due to continuing disorganization within the land registry system and the financial and social costs of selling mortgaged land and properties after seizure. Furthermore, there is little accountability and proper supervision of Tier 4 institutions, such SACCOs, especially in the rural areas.

To stay true to the goals set in the GOU's Poverty Eradication Action Plan (PEAP), Uganda must achieve an annual economic growth rate of seven to eight percent to reduce overall poverty to ten percent by 2017. All citizens, especially the poorest, must benefit from economic growth and have access to financial services, such as savings and credit. The USAID/Uganda's 2002-2008 Strategy therefore calls for expanded, sustainable economic opportunities for rural sector growth, through promotion of a connection between productive strategies implemented by the private sector in rural areas and expansion of the financial services sector to these areas. USAID's Rural Savings Promotion and Enhancement of Enterprise Development (USAID/Rural SPEED) was thus designed to help achieve this goal.

USAID/Rural SPEED's objective is to deepen and strengthen Uganda's financial sector in response to this rural sector demand for financial services. The increased provision of financial services should leverage economic activity to complement other USAID/Mission programs in rural areas. The resulting increase in economic activity should aid the GOU in achieving the target economic growth rates proposed in Poverty Eradication Action Plan. The USAID/Rural SPEED project is supporting and executing activities in the following key areas:

A. Institutional Capacity Building
   - Savings Mobilization;
   - Agriculture Finance;
   - Non-agriculture Finance; and,
   - Bank//MDI/MFI/SACCO Linkages.
   -

B. New Product Development and Service Delivery

Underpinning all of USAID/Rural SPEED's strategy to achieve its key activities in rural areas are Uganda's numerous, but weak, SACCOs. USAID/Rural SPEED, other donor programs, and the GOU all view SACCOs as a critical element for extending savings services to rural people, multiplying and expanding rural savings and credit transactions through formal wholesale borrowing and depositing with commercial banks, and providing a locally-based, locally-knowledgeable rural financial intermediary capable of prudently lending for agricultural activities.

Unfortunately, Uganda's SACCOs have widely disparate organizational forms, management styles, policies and procedures, and financial systems. This is owing to the complex history of the SACCO sector in Uganda wherein SACCO models have been promoted based on multiple European, North American, African and local experiences. Weak management exists in the sector due both to intentional malfeasance and to weak management methods based on the lack of a standardized training regiment. One of the key weaknesses in management witnessed by USAID/Rural SPEED staff and consultants has been the lack of a basic standard system and methodology for tracking delinquent loans at the loan officer level, aging arrears at the management level and authorizing bad debt write-off at the board level.

This USAID/Rural SPEED consultancy will train 54 SACCO representatives in standard techniques for delinquency management and prudent practice for internal control including roles of management, policies, procedures and systems. Further, USAID/Rural SPEED will directly mentor ten partner organizations, through short term technical assistance and ongoing project support, in these very systems.

Scope of Work

The objective under the scope of work (SOW) was to train 54 SACCO[1] representatives (18 loan committee members, 18 loan officers and 18 general managers) on successful models of delinquency management and prudent practices for internal controls, roles of management; policies, procedures and systems. Further, ten one-day mentoring visits were provided to the SACCOs, which are partnered with USAID/Rural SPEED or which are currently under consideration for partnership. The training and mentoring is expected to serve as a foundation toward wider capacity building and for opening opportunities for these SACCOs to expand their respective businesses.

The principal tasks to be completed under this SOW engagement are as follows:

- Prepare in advance training documents including, policies, procedures, and systems from an existing successful rural SACCO movement.
- In Uganda, to meet with USAID/Rural SPEED and other professionals to review the systems currently used by Ugandan SACCOs and control systems promoted by USAID/Rural SPEED.
- Develop a three day training module to cover:
  - SACCO delinquency management strategies and internal control structures, procedures and controls including the roles of the board and the management.
  - Delinquency management procedures from the loan officer level through to the board level with practical classroom based applications.
  - SACCO portfolio tracking and interpretation including standard ratio analysis (this aspect is reinforcement of earlier training).

- Deliver this training module in Mbarara for 54 participants.
- Conduct an additional one day mentoring session, based on discussion and field visits for each of USAID/Rural SPEED's ten partner SACCOs.
- Prepare a final report noting institutions visited, contacts made and recommendations.

As such, the work plan dates for the assignment under the SOW are shown in Table 1.

[1] Of the expected 54 participants, only 52 actually showed up for the training.

Table 1 Consultancy Work Plan Calendar

FROM	TO	ACTIVITY
March 3, 2006	March 3, 2006	Preparation of workshop training manual in USA
March 5, 2006	March 5, 2006	Travel from Toledo to Amsterdam
March 6, 2006	March 6, 2006	Travel – Amsterdam to Entebbe
March 7, 2006	March 7, 2006	Preparation of workshop documents
March 8, 2006	March 8, 2006	Preparation of workshop documents and travel to Mbarara
March 9, 2006	March 11, 2006	Delinquency management workshop
March 13, 2006	March 18, 2006	SACCO mentoring visits
March 20, 2006	March 23, 2006	SACCO mentoring visits
March 24, 2006	March 25, 2006	Preparation of consultancy report
March 27, 2006	March 27, 2006	Presentation of report and revisions/Travel from Entebbe to Nairobi
March 28, 2006	March 28, 2006	Travel from Nairobi to Toledo

The total number of work days under the assignment was twenty-two (22), which includes international travel from and to the United States.

Activity Summary

Delinquency Management and Internal Controls Training Workshop

The objectives of the delinquency management and internal control workshop were to help the participants from eighteen SACCOs understand delinquency and its costs, analyze and determine its causes, learn how to measure it, learn how to use ratio analysis, discuss strategies for controlling and preventing it, and to prepare for implementation a SACCO delinquency management plan. The proposed individual delinquency management plans would then be presented to the Boards and discussed during the one-day mentoring visits.

During the three-day workshop, the following topics were discussed and examples given to provide a hands-on learning experience (see Appendix A for detailed program):

- Loan delinquency – definitions
- What is loan delinquency?
- What is the difference between loan delinquency and loan default?
- What are the effects of loan delinquency?
  - For the SACCO
  - For the SACCO members
  - For SACCO staff
  - For donor and support organizations
- What are some of the delinquency warning signs?
- What are the causes of delinquency?
- How do we measure loan delinquency?
- Compensating for loan loss risk
- Loan loss provisioning
- Loan write-offs and written-off loans register
- Pricing loan fees and interest rates
- Review of delinquency management findings from the September 2005 SACCO mentoring visits.
- Developing strategies for delinquency management
- Review loan policies and procedures
- Evaluating loan officers and loans committee members
- Training loan officers and loans committee members
- Doing business analysis before approving loans
- Improving collection methods
- Alternative collateral
- Charging higher interest rates on repeat loans to delinquent clients
- Loan rescheduling and refinancing
- Internal control systems

After completing the topics in the training guide, the participants worked on putting together an outline of a model delinquency management plan (Appendix B). Using this tool, the participants then returned to their respective groups to prepare a delinquency management plan for their SACCOs. On the final day of the workshop the delinquency management plans were then presented to the entire workshop for additional comments and suggestions. Two of the plans were well structured and well presented (Kyamuhunga and Masaka). The others still require additional work, once they return to their respective SACCOs. The debate on the delinquency management plans was active and helpful. It allowed certain group to revise the plans, based on comments for other SACCOs, before they gave their presentations and thus improved the final product.

At the end of the workshop, a written test was given to evaluate the participants' comprehension of the materials covered during the workshop. The test covered the primary topics presented and discussed during the training, as well as, calculation of portfolio at risk ratios and loan loss provisioning requirements. The test, with sample answers, can be found in Appendix C.

The average score for all participants was 28 points, out a possible 48 (58.33%), which is acceptable (Appendix D). The highest number of points scored was 45, which is excellent. In all, nineteen participants scored thirty (30) points or more; i.e., 63% or higher. This is a majority of the participants and is well distributed among the eighteen SACCOs. I believe that this indicates that all of the SACCOs can do the necessary analysis to prepare a practical delinquency management plan. They will, however, need mentoring support to ensure that they implement and evaluate those plans and to ensure that the expected decrease in PAR > 1 day and PAR > 30 days occurs.

After completing the test and written evaluation of the workshops, an oral review of the initial participants' expectations was conducted to see if the workshop had achieved its goals. The participants indicated that:

- Expectations had been met. They were going back as changed people. They had learned where to begin and what is expected. In addition, they had made friends during the workshop.
- They were going back with information about write-offs, delinquency and how to calculate it.
- It was now clear how to work out delinquency calculations.
- It had enlightened the participants about practical applications; and
- This training was very good and timely (really needed now).

The participants raised concerns on the suggestion that loan officers must not collect money (from the field) and on the applicability of charging a higher rate on repeat loans to previously delinquent clients. It was thought that it might be better simply to reduce the amount of the repeat loan. This, however, does not deal with the added cost of the delinquency, which is expected to reoccur with these repeat loans to previously delinquent borrowers.

Finally, the participants recognized the importance of a SACCO conducting a periodic review its loan policy because:

- In many cases the policies are outdates;
- Growing SACCO demand might indicates that loan policies need to be improved to better serve the changing needs of the members (new products);
- The SACCO needs to keep up with the competition; and
- If the Bank of Uganda adjusts its interest rates, then the SACCO will need to update its own interest rates.

The amended SACCO delinquency management plans were then taken back to the respective SACCOs for presentation, debate and approval of their Boards of Directors. For the ten USAID/Rural SPEED partner institutions, this step was facilitated during the mentoring visits. Finally, the team summary notes from day 1 (Appendix E) and day 2 (Appendix F) sessions, were distributed to the participants.

Mentoring Visits

The principle purpose of the one-day SACCO mentoring visits was to examine the delinquency problem and to explain, in detail, the proposed delinquency management plans, which were prepared during the workshop by each SACCO's team of participants. The idea was to discuss the proposed solutions and to explain, in practical terms and in detail, how the board and management will implement the proposed activities. In addition, the SACCOs were requested to complete the loan delinquency information (Appendix G), which was not brought to the workshop as expected. This information was then used to assess current delinquency rates and loan loss provision requirements. In some case it also helped to discuss the need for and justification of loan loss write-offs.

Before the delinquency management plans were presented to the board, a review of the September 2005 training and mentoring visits' delinquency findings and proposed solutions (Appendix H) were presented and discussed. This made it easier for the boards to understand and adopt the proposed delinquency management plans. The highlights of each of the mentoring visits are presented in chronological order below.

Kyamuhunga people Savings Co-operative, Ltd.

This mentoring visit took place on Monday, March 13, 2006. During the visit the following board and staff members were present:

Board Members	
Rusiimwa Grace	Board member
Barekye R. Archangel	Board member
Fr. Birungi Vincent	Treasurer
Batuna Yorokamu	Chairman
Mujuni Edward	Chairman loans committee
Staff	
Muhebwe Harriet Katiti	Manager
Bamwine Henry	Loan officer

According to the information from their Financial Solutions software, the loan delinquency ratios are not very high (PAR > 1 day is 8% and PAR > 30 days is 4.8%). Unfortunately, it was discovered that the recent software update does not age the loans correctly. It actually only ages the outstanding overdue installment principal instead of the entire outstanding principal. The figures in Table 2 are not correct and data was not available to correct the information to redo the table. Only the actual value for PAR > 1 days, which is 18.91%, was able to be calculated. This is a difference of almost 11% and makes the portfolio very risky. However, until the software is corrected the SACCO will continue to underestimate portfolio risk and not be able to sufficiently provision for the real delinquency risk, even though the management has been followed the recommended best practice methodology.

Table 2 Kyamuhumga SACCO Delinquency Statistics as of February 28, 2006

DAYS PAST DUE	NO. LOANS	OUTSTANDING PRINCIPAL	PORTFOLIO AT RISK	LOAN LOSS PROVISION	
				RATE	AMOUNT UGX
Current Loans	N.A.	470,876,363	0.00%	0%	-
1 - 30 Days	N.A.	16,303,035	3.19%	10%	1,630,304
31 - 60 Days	N.A.	4,758,629	0.93%	25%	1,189,657
61 - 90 Days	N.A.	5,644,554	1.10%	50%	2,822,277
91 - 120 Days	N.A.	6,449,144	1.26%	75%	4,836,858
121 - 180 Days	N.A.	7,819,933	1.53%	85%	6,646,943
> 180 Day	N.A.	-	0.00%	100%	-
SUB-TOTAL	N.A.	40,975,295			17,126,039
TOTAL	N.A.	511,851,658			
PAR > 1 Day			8.01%		
PAR > 30 Days			4.82%		

In reviewing the proposed delinquency management plan, the board suggested that the SACCO collect the signature specimens from the LOC chairpersons to be able to verify that the loan request forms and collateral pledges are actually signed by the LOCs. Working and exchanging information with the information can reduce the risk of borrowers using fake addresses and already pledged securities. Overall, the discussion with the board was very positive, although follow-up on progress in the implementation of the delinquency management plan should be done.

Kitagata Development Savings and Credit Cooperative

This mentoring visit took place on Tuesday, March 14, 2006. During the visit the following board and staff members were present:

<u>Board Members</u>

Mubangize Jane	Vice-chairperson
Kataryebwa Katta James	Treasurer
Muhoozi Eli	Chairperson loans committee
Mwesigye Bernard	Board member
Atwikirize Eldard	Loans committee member

<u>Staff</u>

Komujuni Harriet	Manager
Twinomugisha Nathans	Credit officer

Loan delinquency was quite high in this SACCO, with a PAR > 1 day at 25% and a PAR > 30 days at almost 20% (Table 3) at the end of December 2005. A lack of electricity has meant that the figures are not available for January and February 2006 but it is doubtful if the situation has improved very much since December. Since some of the delinquency is do to the late payment of government salaries to borrowers. The SACCO has formally requested a Salary Code number and authorization so that it can receive the members' salaries directly as deposits into the SACCO's bank account. While this will not eliminate delinquency due to late salary payment, it will ensure that the SACCO gets its money no matter when the government finally makes the payments.

Table 3 Kitagata SACCO Delinquency Statistics as of December 31, 2005

DAYS PAST DUE	NO. LOANS	OUTSTANDING PRINCIPAL	PORTFOLIO AT RISK	LOAN LOSS PROVISION	
				RATE	AMOUNT UGX
Current Loans	N.A.	263,383,506	0.00%	0%	-
1 - 30 Days	113	18,555,916	5.28%	10%	1,855,592
31 - 60 Days	75	13,355,991	3.80%	25%	3,338,998
61 - 90 Days	57	14,869,422	4.23%	50%	7,434,711
91 - 120 Days	19	8,022,799	2.28%	75%	6,017,099
121 - 180 Days	32	19,076,426	5.43%	85%	16,214,962
> 180 Day	36	14,260,882	4.06%	100%	14,260,882
SUB-TOTAL	332	88,141,436			49,122,244
TOTAL	N.A.	351,524,942			
PAR > 1 Day			25.07%		
PAR > 30 Days			19.80%		

The board is aware of the delinquency problem and welcomed both the recent workshop and the discussion of the delinquency management plan during the mentoring visit. Unfortunately, the initial plan was not well prepared by their workshop participants. As a result, we were required reviewed all of the components in model delinquency management plan with them. This led to a revised delinquency plan, which is shown in Appendix I

One of the ideas discussed was to introduce a system of color-coded loan performance identification cards. It was suggested that the color coding could help encourage borrowers to repay on time. The borrowers would be divided in three categories, good, average and bad. The color would also determine the interest rate charged on their loans; i.e., the most favorable rate for the good borrower and the highest rate for the bad borrowers. The following color coding was proposed:

- Blue card Good borrower 2%/month interest charge
- Yellow card Average borrower 3%/month interest charge
- Red card Poor (delinquent) borrower 4%/month interest charge

However, before implementing any proposal, a full business analysis must be conducted to see what effect the interest changes will have on SACCO income and sustainability. Furthermore, a formal written policy on the program must be developed to ensure that the selection is based on clear, objective criteria.

One worrying piece of information is that the SACCO has been selected to participate in a government agricultural lending program. This program has a predetermined interest rate of 0.9%/month (10.8% annual) from which the SACCO will be paid a service fee. Loans will have a phased disbursement schedule and the SACCO will have to conduct technical verification of the farming stages before disbursement. The SACCO does not have the resources or technical skills to do this. In addition, the interest rate will not allow for the SACCO to have a sufficiently high fee to cover its costs. This is not a good deal. The government must provide the technical supervision of the farmers and allow the SACCO to charge a fee, which will fully cover its costs.

2.1.1 Muhame Financial Savings and Credit

This mentoring visit took place on Wednesday, March 15, 2006. During the visit the following board and staff members were present:

Board Members

Kahindi Sam	Chairman
Nshemeire Audrey	Vice-chairperson
Freedom Katherine	Treasurer
Tusiime Titus	Secretary
Mubangizi Edison	Chairperson loans committee
Tugategire Joy	Board member
Mwesigwa Asaph	Board member
Katwiromunda Stephen	Board member
Rev. Kateebarirwe Adonia	Board member
Keereere Sebastion	Board member
Nuwagaba David	Supervisory committee member
Munyabwera Alfred	Supervisory committee chairperson
Tindyebwa Polly	Supervisory committee chairperson

Staff

Komujuni Hope	Manager
Twebaze Cresent	Loans officer

The delinquent amounts by age category were not correctly calculated by the SACCO management (Table 4). The figures actually represent the outstanding installment principal amounts for each ageing category. This is an incorrect method for calculating the delinquency, however, it was not noted until several days later that the calculation were not correct. It is estimated that the actual portfolio at risk ratios may be twice as high, or more, than those shown in the table. Without reentering all of the individual loan information into a new spreadsheet it would take too long to make the actual calculations. Even without the corrected figures the ratios are quite high, with PAR > 1 day at 19% and PAR > 30 days at more than 13%. It is important that someone from USAID/Rural SPEED returns to the SACCO to correct the error and ensure that the delinquency ratios are correctly calculated in the future. Otherwise, the SACCO will continue to underestimate and under-provision the loan delinquency risk.

Table 4 Muhame SACCO Delinquency Statistics as of February 28, 2006

DAYS PAST DUE	NO. LOANS	OUTSTANDING PRINCIPAL	PORTFOLIO AT RISK	LOAN LOSS PROVISION	
				RATE	AMOUNT UGX
Current Loans	N.A.	418,058,105	0.00%	0%	-
1 - 30 Days	N.A.	29,250,360	5.67%	10%	2,925,036
31 – 60 Days	N.A.	14,613,853	2.83%	25%	3,653,463
61 – 90 Days	N.A.	9,382,996	1.82%	50%	4,691,498
91 - 120 Days	N.A.	7,896,336	1.53%	75%	5,922,252
121 - 180 Days	N.A.	9,144,725	1.77%	85%	7,773,016
> 180 Day	N.A.	27,876,460	5.40%	100%	27,876,460
SUB-TOTAL	N.A.	98,164,730			52,841,726
TOTAL	772	516,222,835			
PAR > 1 Day			19.02%		
PAR > 30 Days			13.35%		

In addition, there was some confusion in the purpose of the mentoring visit. The board had been called for the AGM preparatory meeting and thought that the mentoring visit was simply a briefing on the delinquency management training. While the letter had been clear that the purpose was to work with the board on the proposed delinquency plan prepared during the workshop, they were unable to focus more than two hours of time on the plan. In addition, the chairperson of the loans committee was on his way from Kampala (he is a Master student at the university) and only arrived at 11:00 A.M. While I believe that the two hours of discussions were well received and helpful to the board, the time was not sufficient to fully discuss how the proposed delinquency plan will be implemented.

One issue raised during the meeting, and not accepted by the board, was to continue to allow loan officers to make collections in the field. I believe that they have finally realized that this must no longer occur, however, it needs to be put into the collections policy in writing, once the review of the loans policy is implemented.

Shuuku Credit and Savings Cooperative

This mentoring visit took place on Thursday, March 16, 2006. During the visit the following board and staff members were present:

<u>Board Members</u>

Tuwahirwa Wilson	General Secretary

<u>Staff</u>

Tukamushaba Miriam	Manager
Mubangizi Deo	Senior Loan Officer
Ahimbisibwe Albert	Loan Officer

Loan delinquency is significant but not as high as in other SACCOs. The PAR > 1 day was 11.32% and the PAR > 30 days was 7.68% (Table 5) at the end of February 2006. Most of the delinquency is in the 1 – 30 days, 31 – 60 days and 61-90 days categories, which should be easier to manage. However, Shuuku finally wrote of 37,664,867 UGX in loans past due more than 360 days, at the end of February. This was an important effort that was needed to portray the accounting records accurately and fairly. It has taken five months, since the accounting training, to create sufficient loan loss provisions to achieve this.

Table 5 Shuuku SACCO Delinquency Statistics as of February 28, 2006

DAYS PAST DUE	NO. LOANS	OUTSTANDING PRINCIPAL	PORTFOLIO AT RISK	LOAN LOSS PROVISION	
				RATE	AMOUNT UGX
Current Loans	N.A.	327,310,111	0.00%	0%	-
1 - 30 Days	109	13,453,500	3.64%	10%	1,345,350
31 – 60 Days	101	12,844,000	3.48%	25%	3,211,000
61 – 90 Days	73	8,599,500	2.33%	50%	4,299,750
91 - 120 Days	30	4,047,500	1.10%	75%	3,035,625
121 – 180 Days	11	2,844,500	0.77%	85%	2,417,825
> 180 Day	0	-	0.00%	100%	-
SUB-TOTAL	324	41,789,000			14,309,550
TOTAL	N.A.	369,099,111			
PAR > 1 Day			11.32%		
PAR > 30 Days			7.68%		

The only additional problem noted was that the SACCO accountant did not create a clear audit trail for the process. This came from a misunderstanding of the administrative part of the accounting process. There is also some confusion on the calculated loan loss provision amount used in reports and the actual amount in the account. The SACCO was not keeping a ledger card for these transactions. They were simply subtracting the amounts from the income statement and the balance sheets. In light of this, I was able to a simple training so that the account could understand the process. In addition, Appendix J was prepared to provide a detailed explanation of the process. This technical note should be distributed to all of the SACCOs. The loan loss provision account is currently under funded, after the write offs. The actual amount is 11,217,947 UGX, which needs to be brought up to at least 14,309,550 UGX.

While the time with the accountant and loan officers was quite useful, the time was the board was less so. Only the board secretary showed up for the session. As it turns out, only four board members were invited. The others either did not show up or were not invited by the manager. I am not sure why the information was misunderstood but it means that the rest of the board does not understand the contents and implications of the delinquency management plan. The board secretary was very sharp and seems to understand the implications; however, it may be very difficult for him to communicate all of the information to the other board members. At the very least, the SACCO management must hold another (full) board meeting in the near future to present the amended plan to them for approval and buy-in.

Kajara SACCO

This mentoring visit took place on Friday, March 17, 2006. During the visit the following board and staff members were present:

Board Members	
Kundyomunda Jomo T.	Chairman
George Kashereka	Vice-chairperson
Kinono George	Treasurer
Kakeeto A Bata Sande	Secretary
Owaarwe Deborah	Board member
Tumusiime Alice B.	Board member
Staff	
Nasasiirwe Privah	Manager
Mucunguzi Savio	Loan officer

While the PAR > 1 day and the PAR > 30 days ratios are both quite high at 15.79% and 8.03% (Table 6), their loan loss provision account has more than sufficient funds (54,666,229 UGX) to cover the portfolio risk requirements (21,128,201 UGX). This is a good sign and indicates that they are sufficiently well positioned to deal with the delinquency; however, they need to work on collection strategies.

Table 6 Kajara SACCO Delinquency Statistics as of February 28, 2006

DAYS PAST DUE	NO. LOANS	OUTSTANDING PRINCIPAL	PORTFOLIO AT RISK	LOAN LOSS PROVISION	
				RATE	AMOUNT UGX
Current Loans	N.A.	299,592,376	0.00%	0%	-
1 - 30 Days	48	27,626,122	7.76%	10%	2,762,612
31 - 60 Days	11	7,210,357	2.03%	25%	1,802,589
61 - 90 Days	6	6,570,000	1.85%	50%	3,285,000
91 - 120 Days	9	3,700,000	1.04%	75%	2,775,000
121 - 180 Days	6	3,900,000	1.10%	85%	3,315,000
> 180 Day	12	7,188,000	2.02%	100%	7,188,000
SUB-TOTAL	92	56,194,479			21,128,201
TOTAL	N.A.	355,786,855			
PAR > 1 Day			15.79%		
PAR > 30 Days			8.03%		

Their delinquency management plan lacked a lot of detail. We therefore discussed all of the elements and I believe that they can revise the plan and make it much better. Their plan discusses more individual actions than strategic ones but should lead to the same result. They are expecting to implement a number of actions, such as, new warning letters and a quicker frequency for sending them out, pre-disbursement training for members and guarantors, and the production of loan ageing report. It is doubtful, however, that they will make quick progress on loan ageing since they do not have a working computer or software, although they do have a brand new HP 1320 printer.

In addition, they did not participate in the accounting and financial management training last year, which they really need to make improvements in reporting. I would suggest that USAID/Rural SPEED arrange for them to be trained by Friends Consult, if they are available. This training could include any other of the new partner SACCOs, which did not receive the training last year. I was impressed with the manager, who seems to have a good grasp of the problems and possible solutions to their delinquency. This is certainly a SACCO worth considering for partnership with USAID/Rural SPEED.

Ebirungi Birugo Mutuutu SACCO

This mentoring visit took place on Saturday, March 18, 2006. During the visit the following board and staff members were present:

Board Members

Kashaija Abert	Board member
Muramira Deus	Treasurer
Muwonge Stephen	Chairman
Kazibwe Rose	Vice-chairperson
Mwije Jennifer	Board member
Mitsindi Catherine	Audit committee member
Babyeyaka Pheobe	Board member
Tabaaro Richard	Board member
Kakuru Charles	Board member
Atukwatse G. B.	Secretary
Bushaija Edward	Chairman audit committee

Staff

Mugume Joseph	Manager
Muhwezi John Bosco	Loan officer

The PAR > 1 day and the PAR > 30 days ratios are both extremely high at 24.63% and 16.93% (Table 7). In addition, the loan loss provisioning has been totally inadequate to cover most of the portfolio risk and is not even sufficient to write off all 42 loans delinquent more than 360 days (5,854,800 UGX). It is currently 2,765,898 UGX and is provisioned only at the end of each financial year. While I have strongly recommended that they start providing the loan loss provision account at a rate of 1,500,000 UGX per month, it will still take them at least 16 months to achieve their goal. By that time the portfolio may be even worse. They currently need a loan loss provision value of 21,220,265 UGX to cover the risk in their portfolio.

Table 7 Ebirungi Birugo Mutuutu SACCO Delinquency Statistics as of Feb. 28, 2006

DAYS PAST DUE	NO. LOANS	OUTSTANDING PRINCIPAL	PORTFOLIO AT RISK	LOAN LOSS PROVISION	
				RATE	AMOUNT UGX
Current Loans	N.A.	136,602,900	0.00%	0%	-
1 - 30 Days	118	13,945,250	7.69%	10%	1,394,525
31 - 60 Days	76	9,413,700	5.19%	25%	2,353,425
61 - 90 Days	52	4,768,000	2.63%	50%	2,384,000
91 - 120 Days	31	3,266,100	1.80%	75%	2,449,575
121 – 180 Days	36	4,028,400	2.22%	85%	3,424,140
> 180 Day	59	9,214,600	5.08%	100%	9,214,600
SUB-TOTAL	372	44,636,050			21,220,265
TOTAL	N.A.	181,238,950			
PAR > 1 Day			24.63%		
PAR > 30 Days			16.93%		

While I believe that the management may be capable of making improvements, I am worried about the board. They are very weak and it is not clear that there is sufficient time to assist them. They were fairly participative during our mentoring session but lack a lot of information and knowledge as to what to do. The loans officers are still collecting money in the field. We discussed this issue in great detail and I now hope that they will change. The do have a computer but use some locally created software (from a person in Kampala) and would really need something much better if they are to have up-to-date information for real-time management of the delinquency problem. Their software only works for savings and accounting purposes. There is nothing for loans, which are still handled manually.

The manager indicated that he wanted to make the loans committee a permanent structure; i.e., that they are at the office every day. We strongly discouraged this since it will mean more costs and would send a signal to all of the other board members that everyone should be paid. I believe that the board members understand this and will not allow it to happen.

They were open to new types of collateral, in addition to property, and on requiring pre-disbursement training for guarantors. While I was pleased with the outcome of the meeting, I am still concerned that the board will need a lot of strengthening before it can adequately manage delinquency. Thus the task will fall mostly on the SACCO management.

They need to focus more on saving mobilization and on increased share capital requirements to develop their financial well-being. They want to open new branches, without having prepared a market survey or developed a cost effective business plan. It is not sufficient to have members that are distant from the SACCO office to justify a new branch. I had the impression that this is a copycat idea from other local SACCOs, which have branches or have recently created branches.

Nyarwanya Savings and Credit Society

This mentoring visit took place on Monday, March 20, 2006. During the visit the following board and staff members were present:

Board Members	
Mgabiirwe Gard	Chairman
Kijunjuure Africano	Vice-chairman
Biryabarema Geoffrey	Board Member
Muhoozi Gard	Board Member
Rukundo Benon	Board Member - Security
Bananuka John Bosco	Board Member
Kigango Aine	Board Member
Staff	
Kigango Fred	Manager
Oryoroba James	Accountant
Tagobya Prosper	Loan Officer
Africa Abaasi	Driver

While I have prepared the table using the information provided by the SACCO accountant, it is doubtful if the figures are correct (Table 8). When we requested the number and amount of all loans past due > 360 days (21 and 11,654,000 UGX), both the number of delinquent borrowers and the amount outstanding exceeded the figure that had been provided for the > 180 days category (9 and 6,137,300 UGX). Since it was impossible to sort out the errors (no computerized loan system), it was requested that the figures be verified and recalculated by the accountant and sent to USAID/Rural SPEED later in the week. Given that the actual figures were uncertain I have replaced the > 180 days past due figure with the verified > 360 days past due figure. All that is certain is that delinquency ratios are critically high and extremely damaging to the SACCO's performance.

Table 8 Nyarwanya SACCO Delinquency Statistics as of Feb. 28, 2006

DAYS PAST DUE	NO. LOANS	OUTSTANDING PRINCIPAL	PORTFOLIO AT RISK	LOAN LOSS PROVISION	
				RATE	AMOUNT UGX
Current Loans	N.A.	205,697,814	0.00%	0%	-
1 - 30 Days	N.A.	15,312,000	5.96%	10%	1,531,200
31 - 60 Days	N.A.	3,247,600	1.26%	25%	811,900
61 - 90 Days	N.A.	4,193,200	1.63%	50%	2,096,600
91 - 120 Days	N.A.	8,721,400	3.40%	75%	6,541,050
121 - 180 Days	N.A.	7,947,600	3.10%	85%	6,755,460
> 180 Day	N.A.	11,654,000	6.93%	100%	11,654,000
SUB-TOTAL	N.A.	51,075,800			29,390,210
TOTAL	N.A.	256,773,614			
PAR > 1 Day			22.28%		
PAR > 30 Days			16.32%		

The actual value of the Loan Loss Provision account is 1,788,398 UGX, which is significantly less than the calculated risk adjusted amount of 29,390,210 UGX. There are 11,654,000 UGX in loans greater than 360 days past due. All of these should be written-off; however, the SACCO is not earning enough income each month to this quickly. We have recommended that the SACCO try to provision by between 1,500,000 UGX and 2,000,000 UGX per month for the next year (12 months) in order to bring the loan loss provision account up to the recommended level. At this rate, it will only be able to write off the current loans past due > 360 days in about 7 months. Perhaps the application of the suggestion in the delinquency management plan can help reduce the delinquency over the same period, whereby they will not need much more provisioning. Without careful supervision this is unlikely to occur. It will take a sustained effort to manage the loan write-off situation.

The board appears to be motivated and wanting to perform well; however, they are very weak. In addition, the SACCO uses external loans (MSCL) instead of member savings to finance its portfolio. Furthermore, while most loans are given under a group guarantee mechanism, the guarantee is not real. Group members and other guarantors are not willing to pay for delinquent members. It is simple a signature on a piece of paper. The SACCO appears reluctant, especially the board, to use the courts to foreclose on collateral (property). This must begin immediately.

Rubabo People Cooperative Savings and Credit Society

This mentoring visit took place on Tuesday, March 21, 2006. During the visit the following board and staff members were present:

<u>Board Members</u>

Tuhaise Peter	Chairman
Biryatwita Bonny	Vice-chairman
Masheija Jolly	Treasurer
Ndyanimanya Jackson	Chairman loans committee
Ndyamwijuka Jovent	Board member/loans committee
Kiiza Beebwe Emily	Board Member
Muhanji B. Celeb	Board Member
Musiimenta Ludia	Board member
Wenamanya Margaret	Supervisory Committee

<u>Staff</u>

Turyahabwe Esau	Manager
Turinawe Christopher	Loan officer/Accountant
Byaruhanga Happiness	Loan officer

The information on delinquency ratios was not available when we arrived. After a long discussion, the board chairman said that they must be prepared by Friday, 24 March 2005 at noon and faxed to USAID/Rural SPEED offices in Kampala. While they did not arrive as expected on Friday, it did make it after close of business and was thus available on Monday morning to be included in the report.

Our impression, that delinquency is very high, was confirmed with the figures (Table 9) that were sent. PAR > 1 day is 29.3% and PAR > 30 days is 23.9%. In addition, the value of loans > 180- days dues is 54,563,542 UGX, all of which needs to be provisioned at 100%. This SACCO has a critical situation with delinquency since the loan loss provision account has only 29,842,072 UGX, when it should be 69,947,937 UGX. If this SACCO does not take drastic steps to recover these delinquency loans is it likely to become technically insolvent very soon if it has not reached that stage already. This board needs a strong wake up call.

Table 9 Rubabo SACCO Delinquency Statistics as of Feb. 28, 2006

DAYS PAST DUE	NO. LOANS	OUTSTANDING PRINCIPAL	PORTFOLIO AT RISK	LOAN LOSS PROVISION	
				RATE	AMOUNT
Current Loans	N.A.	245,648,100	0.00%	0%	-
1 - 30 Days	14	18,481,700	5.32%	10%	1,848,170
31 – 60 Days	13	11,278,800	3.25%	25%	2,819,700
61 – 90 Days	143	8,588,700	2.47%	50%	4,294,350
91 – 120 Days	130	8,562,900	2.47%	75%	6,422,175
121 - 180 Days	0	-	0.00%	85%	-
> 180 Day	197	54,563,542	15.72%	100%	54,563,542
SUB-TOTAL	497	101,475,642			69,947,937
TOTAL	497	347,123,742			
PAR > 1 Day			29.23%		
PAR > 30 Days			23.91%		

Furthermore, the SACCO management was not well prepared to present the delinquency management plan during our visit. This was discussed by the board and the management was told to revise the plan. The board has set a date for a full board meeting next week to review and discuss, more thoroughly, the delinquency issues and a better prepared plan. However, our discussions during the mentoring session were able to highlight all of the issues that should be included in the plan. It further led to the proposal of a number of activities, which should be implemented under the revised plan.

During the discussions, it was finally agreed that the loan officers should not longer collect payments in the field. The SACCO will find another way of getting the members to come and pay at the office, where the loan was disbursed. In addition, it seems that there is a strong need to conduct some form of pre-disbursement training for guarantors, as well as, implementation of a more rapid response to seizing and selling pledged collateral.

Bugongi SACCO

This mentoring visit took place on Wednesday, March 22, 2006. During the visit the following board and staff members were present:

Board Members

Mpuriirwe Francis	Chairman
Nyehangane Daniel	Treasurer
Tugume Wilson	Vice-chairman
Kirabira	Secretary
Mrs. Rwamugundu Molly	Secretary loans committee
Mugisha Kateire	Loans committee
Asiimwe Jolly	Board member
Nuwagira Nice Byamukama	Board member
Kamugisha Nekemia	Chairman audit committee
Bamutsimbire T. Willy	Secretary audit committee

Staff

Ashaba Denis	Manager
Mugizi Edward	Loan officer

Loan delinquency is a significant problem here and there are doubts about the accuracy of the figures. They are still considering the delinquent principal from installments and not the total outstanding principal. Thus individual loans are in several age categories. This would suggest that delinquency for PAR > 30 days is much higher than the 7.98% rate shown in Table 9. The PAR > 1 day is also likely to be affected because there are installment, which are not yet due for delinquent loans and have therefore been shown in the database as current. I would not be surprised if the actual PAR > 1 day is 25% or more. Their software, however, will not provide the information since they seem to be using a simple Excel spreadsheet and not a specific loan's management software.

Table 9 Bugongi SACCO Delinquency Statistics as of Feb. 28, 2006

DAYS PAST DUE	NO. LOANS	OUTSTANDING PRINCIPAL	PORTFOLIO AT RISK	LOAN LOSS PROVISION	
				RATE	AMOUNT UGX
Current Loans	N.A.	248,463,750	0.00%	0%	-
1 - 30 Days	164	16,098,850	5.60%	10%	1,609,885
31 - 60 Days	85	8,065,350	2.81%	25%	2,016,338
61 - 90 Days	46	4,289,100	1.49%	50%	2,144,550
91 - 120 Days	27	1,657,300	0.58%	75%	1,242,975
121 - 180 Days	15	946,400	0.33%	85%	804,440
> 180 Day	23	7,975,300	2.77%	100%	7,975,300
SUB-TOTAL	360	39,032,300			15,793,488
TOTAL	N.A.	287,496,050			
PAR > 1 Day			13.58%		
PAR > 30 Days			7.98%		

The most disturbing aspect of our mentoring session was that the several board members kept falling asleep. This was the most ineffective and weak board that I have visited so far. I believe that I did most of the talking since they did not even have a copy of their delinquency plan. They had to use my copy for presentation. Although the decision is up to the USAID/Rural SPEED team, I do not think that this SACCO is a viable choice as a partner. The defaulting members are taken to court but the collateral is not seized and sold. They are very much more afraid of “hurting” their “poor” members than they are worried about saving the SACCO. Only the chairman seemed to have a good idea of what was going on and what needs to be done. This, however, is not sufficient.

Masaka MF (Mamidecot)

This mentoring visit took place on Thursday, March 23, 2006. During the visit the following board and staff members were present:

Board Members	
Kayiso Mayanja Gerald	Secretary
Nalubega Geraldine	Chairperson loans committee
Hajati Muzeeyi Lukiya	Board member
Mayanja Reillus	Board member
Kasujja Methodius	Board member
Staff	
Zabasajja N. Joe	Manager
Kavuma Cyprian	Loan officer

Once again, this SACCO was not able to provide accurate information on loan delinquency but for an entirely different reason. Their version of the Financial Solutions software does not function properly for loans. It appears to double count loans, even those that are already paid off. Since the volume of loans outstanding is considerable (over 844,000,000) in addition to more than 5,000 clients, it is impossible to have the time to resolve this manually. This SACCO is definitely the best candidate for the first installment of whatever software is finally selected since they will have need all of the options and reports. If it works in their SACCO then it will work in the other partner SACCOs. The board is motivated and willing to move forward, although our mentoring session was more of a teaching lesson by me. It has motivated them to hold another meeting to more clearly define their delinquency management plan, especially to indicate who is responsible for which activities and by when must they be completed.

Conclusions and Recommendations

The most frequent comment made by the SACCO boards, during the mentoring sessions, was that the issue of loan delinquency is extremely important and the current training welcomed. Previously, the delinquency issue was perceived as a minor concern. They did not understand the full impact that this delinquency problem will have in the future survival of their SACCOs. In addition, most had no idea how serious the problem was, since they were not calculating the portfolio at risk ratios nor were they interpreting the results to make better management decisions. Presenting the finding from last year's training and mentoring helped give them a wake up call in what needs to be addressed to manage delinquency before it is too late. However, simply recognizing the problem is not sufficient. The boards must make sure that the changes are implemented and that the continued their performance is frequently evaluated. It is therefore recommended that:

1. USAID/Rural SPEED should address a letter to each one of the partner SACCOs requesting a detailed copy of their revised delinquency management plans.
   a. The letter should provide a 2 or 3 week delay (maximum) for the reception of their detailed response.
   b. The letter should reference the revised delinquency management plan outline, which is found in Appendix B, as the model. A copy of this should be sent with the letter.
   c. The letter should also request revised loan delinquency ageing information to verify the current information, which seems to be incorrect in some cases and simply doubtful in others. Please note that where the error is computer generated (due to Financial Solutions) there will not be a real solution until there is better software available.
   d. The letter should further state that USAID/Rural SPEED will be monitoring the SACCO's progress in implementing its plan.
   e. There must be reasonable and realistic progress as a condition for continued USAID/Rural SPEED assistance.

2. Once the revised delinquency management plans are received, USAID/Rural SPEED needs to make sure that it is monitoring their progress through periodic mentoring visits. This is extremely important. It will ensure that the boards stay focused on the tasks and do not become discouraged if the expected change is not quick in coming.

3. Of the three potential (new) SACCO partners visited, it is strongly discouraged that USAID/Rural SPEED selects Bugongi. This SACCO's board is too weak to make substantial changes in the project's remaining time period. The management is weak as well and there is no adequate information management system. While they can still be invited to training programs, if space is available, they should not become partners.

4. In addition, if Kajara is retained as a SACCO partner, they should be given the accounting and financial management training that they did not receive last year. It is very important that the board treasurer, accountant and manager understand and apply the proper accounting principles and practices to bring the entire financial management system up to best practice standards.

5. USAID/Rural SPEED needs to follow up on SACCO loan loss provisioning and loan write-off. Loan loss write-offs must be done for loans, which are more than 360 days past due. The technical note presented in Appendix J should be distributed to each of the SACCOs and a follow-up visit scheduled to ensure that the process is implemented properly. Having a proper audit trail is very important. While this problem was only noted in one SACCO (Shuuku) it is likely that others have addressed the accounting procedures incorrectly, as well. In many cases the much needed loan loss write-offs have not yet been done so this technical note can serve as a template to properly write off loans, when the SACCO has sufficient loan loss provisions set aside.

6. In order for SACCOs to produce loan loss ratios in a timely and accurate manner better software is required. Currently, SACCOs waste a lot of time on report compilation and have no time left for management. It is always better to have a computer generated report, which is then analyzed and used to make management decisions, than to spend hours preparing a manual report that is not used. The current software, Financial Solutions is grossly inadequate. Not only does it not do many of the operations that a MFI needs, it does others totally incorrectly. Its delinquency calculations are based on overdue installment principal and not outstanding principal for delinquent loans. This leads to an under-evaluation of actual risk by 25% or more and an over estimation of the number of delinquent loans, which are counted more than once if several installments are past due. In one case, Masaka MF, the program double counts loans in the ageing categories and even enters fully paid loans as delinquent. This issue has still not been addressed by the service provider after more than six months of waiting.

7. The final missing piece for successful implementation of the delinquency management plan is the provision business analysis skills:
   a. First, the loan officers should be trained on how to collect sufficient information to be able to prepare a simple balance sheet and income statement for each client's business.
   b. Second, the loan officers should be trained on analyzing the businesses based on the balance sheet and income statement information.
   c. Third, the loan officers should be trained on how to put together a technical evaluation of a number of different business activities; i.e., a value chain assessment and minimal standards for these business activities to be able to borrow and repay loans in the agricultural, services and trade sectors.
   d. Fourth, the loans committee should be trained on how analyze the business information presented by the loan officers to make decisions on loans sizes and terms for those business activities, which are approved.

If the delinquency management plans are formalized and implemented, as discussed during the mentoring visits, then the SACCOs should be able to make dramatic reductions in delinquency by the end of 2006. Loan delinquency management is a complicated process and often takes six or more to address effectively. The higher the current PAR ratios the longer it may take to address the underlying problems. Close supervision of progress will be necessary to keep the SACCOs focused on the issue until it is brought under control.

Appendix A Training Workshop Programme

From	To	Description	Time
Day 1 – Thursday 9 March 2006			
08:30	09:15	Introduction: • Introduction of the participants • Presentation of the programme and selection of daily summary teams • Presentation of the training objectives • Selection of training disciplinarian • Questions/issues not covered that need to be included in the programme	 10 min 15 min 10 min 5 min 5 min
09:15	10:45	Session 1 – Loan Delinquency - Definitions • What is loan delinquency? • What is the difference between loan delinquency and loan default? • What are the effects of loan delinquency? • What are the delinquency warning signs? • What are the causes of delinquency?	90 min
10:45	11:15	Tea Break	30 min
11:15	1:05	Session 2 – Measuring loan delinquency • Portfolio at Risk (PAR) ratios • Loan loss ratio • Loan loss reserve ratio • Risk coverage ratio • Effective repayment rate	110 min
1:05	2:20	Lunch	75 min
2:20	4:05	Session 3 – Compensating for Loan Loss Risk • Loan loss provisioning • Loan Write offs and Written-off loans register • Pricing loan fees and interest rates	105 min
4:05	4:25	Tea Break	20 min
4:25	5:30	Session 4 – Review of delinquency management findings from the September 2005 mentoring to SACCOs	65 min
17:30		End of Day	
Day 2 – Friday 10 March 2006			
08:30	08:50	Review of Day 1 Topics • Presentation of Day 1 Summary by a team of participants • Questions & answers	 10 min 10 min
08:50	10:45	Session 5 - Developing Strategies for Delinquency Management • Review loan policies and procedures • Evaluating loan officers and credit committee members • Training loan officers and credit committee members • Doing business analysis before approving loans • Improving collection methods • The use of alternative types of collateral • Charging higher interest rates on repeat loans to delinquent clients • Loan rescheduling and refinancing	70 min
10:45	11:05	Tea Break	20 min
11:05	1:00	Session 6 – Analyzing Delinquency in the 18 participating SACCOs (Work in groups) • Review of SACCOs' PAR and other ratios • Analysis of loan loss provision value • Loan policies problems • Current collection strategies and problems	45 min
1:00	2:10	Lunch	70 min
2:10	2:30	Session 7 – SACCO Internal Control Systems • Supervisory Committee • Board of Directors	20 min
2:30	2:55	Session 8 – Creating a Delinquency Management Plan	25 min
2:55	4:00	Session 9 – Individual SACCO Delinquency Management Plans	65 min
4:00	4:30	Tea Break	30 min

4:00	5:30	Session 9 (cont.) – Individual SACCO Delinquency Management Plans	90 min
5:30		End of Day	
Day 3 – Saturday 11 March 2006			
From	**To**	**Description**	**Time**
08:30	08:50	Review of Day 2 Topics - Presentation of Day 2 Summary by a team of participants - Questions & answers	 10 min 10 min
8:50	10:40	Presentation of individual delinquency management plans (15 minutes each) 1. Kitagata DFS, Ltd. 2. Shuuku SACCO 3. Nyarwanya SACCO 4. Rubabo SACCO 5. RUSCA, Ltd. 6. Maska MF (Mamidecot) 7. Ikongo Rural Development Co-op 8. Rukoma SACCO	110 min
10:40	11:10	- Tea Break	
11:10	1:12	Presentation of individual delinquency management plans (15 minutes each) 9. Bugongi Village Bank 10. Kajara Peoples SACCO 11. Buyanja SACCO 12. Ebirungi Birugomututu 13. Kinkizi Development Financial Services 14. Victoria Basin Saving & Microfinance Cooperative Trust Ltd 15. Kyamuhungs Peoples SACC	122 min
1:12	2:10	Lunch	58 min
2:10	2:57	Presentation of individual delinquency management plans (15 minutes each) 16. Muhame FS Co-op 17. Ankole Farmers and Traders, Ltd. 18. Kamukuzi Village Trust	47 min
2:57	3:41	Written Test on Training	44 min
3:41	4:05	Written and Oral Evaluation	24 min
4:05		End of Training	

Appendix B Model Delinquency Management Plan

1. Objective

- To reduce loan delinquency over the next (time frame to be specified) months to:
  - PAR > 1 day to be ≤ 5%
  - PAR > 30 days to be ≤ 2%

2. Presentation of the current situation as of (provide date)

- PAR > 1 day =;
- Total number of loan > 1 day past due;
- Value of loan outstanding > 1 day past due;
- PAR > 30 days = ;
- Total number of loan > 30 days past due;
- Value of loan outstanding > 30 days past due;
- PAR 1 – 30 days =;
- PAR 31 – 60 days =;
- PAR 61 – 90 days =;
- PAR 91 – 120 days =;
- PAR 121 – 180 days =;
- PAR > 180 days =;
- Loan loss ratio =;
- Loan loss reserve ratio =;
- Risk coverage ratio =;
- Effective repayment rate =;
- Number of loans > 360 Days;
- Value of loans > 360;
- Current value of loan loss provision account; and
- An explanation of what the numbers mean.

3. Review of the loan policy and procedures

- Take a sample of at least 5 delinquent loans and compare the entire loan request and approval documents to the loan policies;
- Note anything that does not fit with the policies or any problems caused by the policies;
- Take a sample of at least 5 good loans and compare the entire loan request and approval documents to the loan policies;
- Note anything that does not fit with the policies or any problems caused by the policies;
- Make recommendations for changes to the board;
- Once the changes are approved implement them; and
- After 3 – 6 months review the changes to see if they have accomplished the objective of reducing delinquency.

4. Review the loan collection policy

- Who is doing what?
- When does it occur?
- What are the steps required to finally get the loan collected (warning, seizure of collateral, sale of collateral)?
- How much does it cost the SACCO to collect a delinquent loan?
  - Work time x number of staff x salary & benefits;
  - Fuel and maintenance or transport costs;
  - Printing documents, reports, etc.;
  - Percentage of general overhead used to follow up delinquency; and
  - Fees paid (lawyers, court brokers, policy, magistrates, etc.).

5. Evaluate the loan officers and loan committee

- On the quality of the loan appraisal;
- On how well the loan documentation is completed and how complete it is (ledger cards, forms, postings up to date);
- On PAR ratios: PAR > 1 day, PAR > 30 days, total # of loan > 1 day past due, Value of loan outstanding > 1 day past due, Total number of loan > 30 days past due, Value of loan outstanding > 30 days past due, PAR 1 – 30 days, PAR 31 – 60 days, PAR 61 – 90 days, PAR 91 – 120 days, PAR 121 – 180 days, and PAR > 180 days;
- Number of loans disbursed during the period;
- Value of loans disbursed during the period;
- Value of loans outstanding at the beginning and end of the period;
- Total number of clients;
- Relationship with the public; and
- Work attitude.

6. Provide training to build capacity

- Training for the loan officers and loan committee members on the revised loan policies and procedures;
- Training for the loan officers and loan committee members on the revised collection procedures and forms;
- Training for the loan officers and loan committee members on the business analysis of loan requests; and
- Training for the loan officers and loan committee members on the revised collateral policy.

7. Implementation Timetable

- Provide a detailed timetable to reach the set objectives.

8. Evaluation of progress

- Short evaluation each month; and
- Full evaluation after 3, 6 and 9 months.

Appendix C Delinquency Management Training Test Correction

Question 1. Define loan delinquency (2 points)

Loan delinquency is a situation that occurs when a loan payment is past due; i.e., the scheduled payment has not been made on or before the date stated in the loan agreement.

Question 2. Give the formula for the Portfolio at Risk (PAR) ratio > 1 day. (2 points)

PAR ≥ 1 day: (Value of the outstanding loan balance in arrears ≥ 1 day, at the end of the period) / (Value of loans outstanding, at the end of the period)

Question 3. Explain the difference between loan delinquency and loan default? (3 points)

Loan delinquency occurs when one loan payment is one day late. Loan default occurs when a borrower cannot or will not pay his or her loan.

Question 4. What are three effects of loan delinquency on the SACCO as an institution? (3 points)

The effects of loan delinquency on the SACCO are:
- Less income because of less interest income
- Less clients because of less financial resources
- Increased operating expenses
- Higher recovery costs
- Decreased capital base
- Decreased sustainability due to lower income
- Ever increasing delinquency
- Poor image of the institution
- Less cash flow in the SACCO
- Decline in the earning rate
- Loss of trust in the SACCO
- Decreased amount and rate of loan disbursements

Question 5. What is the recommended frequency for loan loss provisioning? (1 point)

The recommended loan loss provisioning frequency is monthly to accurately reflect the risk in the SACCOs portfolio during that month.

Question 6. What are the five Cs used to evaluate a loan request? (5 points)

The five Cs are:
- Character
- Capacity
- Capital
- Conditions
- Collateral

Question 7. Using the information below, calculate the following: (10 points)

Value of loans outstanding zero days past due		435,000,000
Value of loans outstanding past due	1 – 30 days	3,245,000
Value of loans outstanding past due	31 – 60 days	1,300,000
Value of loans outstanding past due	61 – 90 days	987,550
Value of loans outstanding past due	91 – 120 days	43,500

Value of loans outstanding past due	121 – 180 days	123,900
Value of loans outstanding past due	>180 days	19,850

Please show all of your calculations:

a. Value of the gross loan portfolio (outstanding): **440,719,800**

(435,000,000 + 3,245,000 + 1,300,000 + 987,550 + 43,500 + 123,900 + 19,850) = **440,719,800**

b. PAR > 1 day = **1.3%**

(3,245,000 + 1,300,000 + 987,550 + 43,500 + 123,900 + 19,850)/ 440,719,800 x 100 = 5,719,800/440,719,800 x 100 = 1.3%

c. PAR > 30 days = **0.56%**

(1,300,000 + 987,550 + 43,500 + 123,900 + 19,850)/ 440,719,800 x 100 = 2,474,800/440,719,800 x 100 = 0.56%

d. PAR 121 – 180 days = **0.03%**
123,900/440,719,800 x 100 = 0.03%

e. What is the total value of delinquent loans? = **5,719,800**
(3,245,000 + 1,300,000 + 987,550 + 43,500 + 123,900 + 19,850) x 100 = 5,719,800

Question 8. Based on the information contained in question 7 calculate the amount of loan loss reserve, which is necessary to compensate for loan loss risk? Please show all of your calculation. (7 points)

1 – 30 days	3,245,000	x	10%	=	324,500
31 – 60 days	1,300,000	x	25%	=	325,000
61 – 90 days	987,550	x	50%	=	493,775
91 – 120 days	43,500	x	75%	=	32,625
121 – 180 days	123,900	x	85%	=	105,315
>180 days	19,850	x	100%	=	19,850
			Total	**=**	**1,301,065**

Question 9. At what stage should the SACCO write off a delinquency loan? Please justify your answer. (2 points)

Loan write-offs need to occur once a loan becomes delinquent for one year (360 days or 12 months). Loan write-offs should be done monthly, as the specific loans become 360 days past due.

Question 10. What are the two most important questions to be asked about a loan request? (2 points)

The two most important questions are:
- **Can** the member repay the loan?
- **Will** the member repay the loan?

Question 11. When does a loan go "bad?" Why? (2 points)

A bad loan goes bad the day it is disbursed.

Question 12. Name two of the steps that are taken in developing a SACCO delinquency management plan. (2 points)

The steps that are taken to develop a delinquency management plan are:

- Objectives
- Present (current) situation
- Review the loan policy
- Review the collection policy
- Evaluate loan officers and loan committee
- Training/capacity building for loan officers and loan committee members
- Implementation timetable
- Evaluate the implementation of the plan – review progress

Question 13. What are two effects of loan delinquency on SACCO members? (2 points)

The effects of loan delinquency on the SACCO members are:

- Less financial discipline
- Less trust of the SACCO
- Less motivation to repay
- Less savings deposited
- Less possibly for repeat loans or new loans to new members
- Less possibility for larger loans
- May not able to withdraw savings on demand due to lack of cash
- May not receive dividends
- Possible loss of savings
- Collateral seized and sold
- Must pay delinquent surcharge (penalty)
- Members leave the SACCO

Question 14. Name two warning signs, which indicate that loan delinquency, is a problem in the SACCO? (2 points)

The warning signs are:

- Loan portfolio is decreasing
- Decreased number of loans disbursed per month
- Decrease in the loan recovery percentage
- Increase in loan recovery expenses
- Increase in loan write-offs
- Large or increasing volume/number of loans granted or renewed with loan policy exceptions
- Large or increasing volume/number of collateral exceptions
- Large or increasing number of loans that are delinquent for extended periods without any payments or communication from the borrowers
- Lines of credit with balances in excess of the maximum approved amount
- Loan values that are greater than the value of the collateral
- Large concentration of loans to individuals or groups of related borrowers granted with or without board approval
- Loans to SACCO officials, employees and their relatives that are outside of the stated policies
- Growth in the loan loss provisioning at a rate that is significantly greater than the percentage growth in loans
- Loss of income from loan interest
- Significant increases in the number or value of problem loans, as a percentage of loans
- Numerous loan extensions and/or refinancing requests made and granted
- Personnel assigned to loan collection lack the attitude, personality and training needed to collect loans

Question 15. Name three causes of loan delinquency. (3 points)

Causes of delinquency are:

- Inadequate or inexistent loan policies and procedures
- Poor application of loan policies and procedures
- Inexperienced or poorly trained loan officers
- Inexperience or poorly trained loans committees
- Inadequate or inexistent loan analysis and approval standards
- Poor application of loan approval (underwriting) standards
- Poor loan appraisal/assessment
- Poor loan follow-up
- Inadequate or non-existent collection policies and procedures
- Poor application of collection policies and procedures
- Too many large loans
- Too much concentration of loans to one or several business types
- Timing of the business cash flow does not correspond to the loan repayment schedule
- Too many or too large insider loans; i.e., loans to SACCO staff, board and committee members, and/or their immediate families
- Too much emphasis in granting loans to all members regardless of their ability to repay
- Lack of capacity of the borrowers to absorb/use the loan properly
- Undue influence from board members;
- Inside lending to staff that does not follow policy
- Loans given based on “who you know” and not on repayment capacity
- Corrupted loan officers
- Lack of or inadequate pre-disbursement training
- Multiple borrowing for different institutions
- Inbuilt dishonesty
- Political interference
- Natural disasters such as fire, flood, storms, etc.
- Divergence of funds from the intended (approved) loan purpose to another activity

Appendix D Delinquency Management Workshop Test Results

No.	Name	SACCO	Position	Points Available	Points Scored	Percentage
1	Muhebwa Harriet Katiti	Kyamuhunga Peoples Coop	Manager	48	45	94%
2	Twebaze Cresent	Muhame FS Ltd	Deputy Loan Officer	48	44	92%
3	Muhwezi John Bosco	Ebirungi Birugo Mutuutu	Loan Officer	48	38	79%
4	Bakengana Zebia	Ikongo	Chairperson Loans Com.	48	38	79%
5	Muhindo Isaac Baaile	Ikongo	Manager	48	38	79%
6	Sabiiti Job	RUSCA	Loan Officer	48	36	75%
7	Kukiriza Ronald	Kamukuzi Village Trust	Loan Officer	48	35	73%
8	Banwine Henry	Kyamuhunga Peoples Coop	Loan Officer	48	35	73%
9	Zabasajja N. Joe	Masaka MF (Mamidecot)	Manager	48	35	73%
10	Mugisha Isreal K.	Shuuku SACCO	Chairperson Loans Com.	48	35	73%
11	Nsaaiirwe Privah	Kajara SACCO	Manager	48	35	73%
12	Byamugisha Benson	Buyanja	Loan Officer	48	33	69%
13	Muwnguzi Savio	Kajara SACCO	Loan Officer	48	33	69%
14	Twinomukisha Nathans	Kitagata DFS Ltd	Loan Officer	48	33	69%
15	Mubangizi Edison	Muhame FS Ltd	Chairperson Loans Com.	48	32	67%
16	Konwjuni Harriet	Kitagata DFS Ltd	Manager	48	31	65%
17	Kakembo Lwingstone	Victoria Basin SACCO	Loan Officer	48	31	65%
18	Tinbdimuzara Charles	Rukoma	Manager	48	30	63%
19	Tukamushaba Miriam	Shuuku SACCO	Manager	48	30	63%
20	Ahimbisibwe Albert	Shuuku SACCO	Loan Officer	48	30	63%
21	Ashaba Denis	Bugongi	Manager	48	29	60%
22	Wenamanya Margaret	Rubabo	Chairperson Loans Com.	48	29	60%
23	Byaruhanga Happiness	Rubabo	Loan Officer	48	27.5	57%
24	Muhindo Samuel	Ikongo	Loan Officer	48	27	56%
25	Agabirwe Rosette	Kamukuzi Village Trust	Manager	48	27	56%
26	Tagobya Prosper	Nyarwanya	Loan Officer	48	27	56%
27	Buhire Elly Bruce	Ankole	Loan Officer	48	26	54%
28	Kiuhere Mark	Kinkizi Development FS	Loan Officer	48	26	54%
29	Mujuni Edward	Kyamuhunga Peoples Coop	Chairperson Loans Com.	48	25	52%
30	Mugizi Edward	Bugongi	Loan Officer	48	24	50%
31	Mutabari Euasaph	Buynaja	Manager	48	24	50%
32	Kavuma Cyprian	Masaka MF (Mamidecot)	Loan Officer	48	23	48%
33	Turinawe Christopher	Rubabo	Accountant	48	23	48%
34	Mujuni Geoffrey	Rukoma	Loan Officer	48	23	48%
35	Muramira Deus	Ebirungi Birugo Mutuutu	Chairperson Loans Com.	48	22	46%
36	Asiimwe Denis	Kamukuzi Village Trust	Chairman Loans Com.	48	22	46%
37	Kirembeka Benon	Victoria Basin SACCO	Manager	48	22	46%
38	Rutara James	Rukoma	Chairperson Loans Com.	48	21	44%
39	Tugume Wilson	Bugongi	Chairperson Loans Com.	48	20	42%
40	Kataba James	Kinkizi Development FS	Chairperson Loans Com.	48	20	42%
41	Nalubega Geraldine	Masaka MF (Mamidecot)	Chairperson Loans Com.	48	20	42%
42	Tibarimu F. Xavier	Buyanja	Chairperson Loans Com.	48	17	35%

43	Mwesuma	Victoria Basin SACCO	Board Member	48	17	35%
44	Rev. Tusingwire Reuben	Kinkizi development FS	Manager	48	15	31%
45	Kashereka George	Kajara SACCO	Chairperson Loans Com.	48	13	27%
46	Kijunjuure Africano	Nyarwanya	Chairperson Loans Com.	48	11	23%
			Average		**28**	

Appendix E Summary Notes

Day 1 Topics

THURSDAY 9 MARCH 2006

Prepared by Team 1 Group Members:
1. Komujuni Harriet
2. Ndyamuba Amon
3. Bamwine Henry
4. Joseph
5. Bakengana Zebia
6. Twebaze Cresent
7. Kijunjuure Africano
8. Moramira Deus
9. Mukwezi John Bosco
10. Tugume Wilson
11. Privah Nasasiirwe
12. Muhebwa Harriet Katiti

Delinquency is a situation, which occurs when a loan payment is not paid on time. Loan default is the failure to repay the loan.

Signs of delinquency:
- Decrease in loan portfolio;
- Decrease in interest on loans;
- Loan loss provisioning keep on increasing;
- Recovery expenses are increasing; and
- Increase in loan write-offs.

Causes of delinquency
- Poor loan appraisal;
- Poor loan policies;
- Inexperienced credit officers and loan committee;
- Poor follow-up; and
- Too much inside lending.

Effects on SACCO
- Capital base goes down;
- High recovery cost;
- Low cash inflow; and
- Loss of trust in a SACCO.

Delinquency on SACCO Member
- Decreased interest hence low dividend;
- Leads to a loss of collateral security;
- Penalties on delinquent loans; and
- Reduces members' capacity to save.

On SACCO staff:
- Poor customer relationships;
- Staff may opt to leave the SACCO;
- Poor remuneration; and
- Low salary increments.

On Donors:
- Donor support is pulled out;
- Loss of trust; and
- Hard condition, when one is seeking a grant.

How to measure Loan Delinquency
- Measured in terms of portfolio quality;
- Done in terms of different ratios;
- It is categorized in 7 steps;
  - Category 1 0 days
  - Category 2 1 – 30 days
  - Category 3 31 – 60 days
  - Category 4 61 – 90 days
  - Category 5 91 – 120 days
  - Category 6 121 – 180 days
  - Category 7 over 180 days

The ratio is measured as follows: (Value of the outstanding loan balance in arrears for that category) / (Value of loans outstanding, at the end of the period)

The best practice standard is:

PAR ≥ 1 day: ≤ 5%
PAR > 30 days: ≤ 2%

Loan loss ratio is the rate at which a SACCO is writing off its bad loans. The formula is: (Value of loans written off during the period) / (Average gross portfolio)

Effective repayment rate is: (All payments received during the period, including arrears recovered) – (loan prepayments)] / (Scheduled amount of payments due during the period, including arrears; i.e., what was supposed to be paid)

Loan loss provisioning is the money put aside to cater for ban loans. It is calculated by:

$$\frac{\text{PAR amount due (by category) x risk percentage per category}}{\text{Outstanding loans}}$$

Compensating for loan loss:

1. Loan writ-off after a year
   - Should be done monthly, not to overstate assets
   - Open a register for written off loans

2. Pricing loan fees
   - Here every institution should ensure that their break-even point is where income covers costs.
   - Steps determine interest rate
   - Estimate the portfolio yield.
   - Consider rates of similar institution
   - Project income considering delinquency
   - Look at the effect on customers

Follow-up exercise:

Lastly we looked at observation made from different SACCOs.

Recommendations made:

- Review of policies and procedures
- Evaluation of loan officers and loan committee
- Also recommended that a member should not get a loan with an instalment that is greater than 30% of the unadjusted monthly income.
- Provisions and write-offs should be done monthly
- In addition to land other securities should be added
- Guarantors should physically appear in the office when the loan is disbursed

The day was closed with a prayer led by Reverend.

Day 2 Topics

FRIDAY 10 MARCH 2006

Prepared by Team 2 Group Members:

13. Tukamushaba Miriam
14. Turinawe Christopher
15. Zabasajja Joseph
16. Kirembeka Benon
17. Tindimuzara Chance
18. Mugizi Edward
19. Kashereka George
20. Atuheire Marx
21. Komujuni Hope
22. Nalubega Geraldine
23. Baake Isaac
24. Tagobya Prosper
25. Kavuma Cyprian
26. Muhindo Samuel
27. Mucunguzi Savio
28. Welenamanya Marg
29. Denis

1. Developing strategies for delinquency management:

Why do we review the policies?

- Some of the policies may be outdated;
- Growth in SACCO results in a need to review policies to serve the changing needs of members; and
- To keep up with competitors.

2. Evaluation of the loan request in terms of the 5 “Cs”:
   - Character of the member;
   - Capacity to run the business;
   - Capital invested in the business;
   - Conditions that may affect the loan; and
   - Collateral, which the member pledges.

3. To be effective the policies must:
   - Select good borrowers;
   - Provide loan sizes and terms in relation to the borrower’s present capacity to pay; and
   - Provide incentives to repay – like penalty fees for late payments.

4. Evaluating loan officers and credit committee members:
   - The SACCO should be able to identify the performance delinquency rate by loan officer;
   - The loan officer's poor performance may be a sign of insufficient training and possibly fraud;
   - Loan officer performance should be evaluated at least once a year.

5. Training loan officers and credit committee members:
   - If the evaluation of the above indicates that there is a need for improvement, then the training should be provided; and
   - Training ensures that they fully understand the policies and procedures.

6. Doing business analysis before approving loans:
   - The committee must look at the member's business by looking at the income statement and balance sheet;
   - The income statement for the period of the loan request should be realistic; and
   - All the expenses must be included in the income statement.

7. Improving collection methods:
   - To achieve high repayment rates involves asking people for money and some management staff have a personal difficulty with this;
   - Giving money away (loans) is much easier than getting it back; and
   - If a loan becomes delinquent the following procedures must be followed:
     - <u>One day late</u>: Give a notice to the member
     - <u>One week late</u>: Issue a warning letter to a delinquent member
     - <u>Two weeks late</u>: A second warning letter should be issued to the borrower and the guarantor. Guarantors should be informed that their savings will be seized; and
     - <u>One month late</u>: Withdraw the overdue amount from the borrower's savings to pay the loan. Then apply the court procedures.

8. The use of alternative types of collateral
   - All loan application must have one or more forms of guarantee;
   - The best form of guarantee is savings but this is not sufficient to cover the full value of the loan; and
   - Spouses should not sign as guarantors.

9. Charging higher interest rates on repeat loans to previously delinquent borrowers (repeat loans)
   - It's the best way to discourage delinquency; and
   - If this is not done the institution loses money.

10. Loan rescheduling and refinancing
    - Its not the solution for delinquency; and
    - It may encourage delinquency because it rewards the borrower for falling behind in repayment.

11. Measuring loan delinquency
    - Practical application of PAR > 1 day and PAR > 30 days
    - Various institutions presented their PAR > 1 day and PAR > 30 days
    - This was further practically applied to the 4 ratios as follows:
      - <u>Loan Loss Ratio</u> = (Value of loans written off during the period) / (Average gross portfolio);
      - <u>Loan Loss Reserve Ratio</u> = (Loan loss reserve) / (Gross loan portfolio);
      - <u>Risk coverage ratio</u> = (Loan loss reserve) / (portfolio at risk > 30 days); and
      - <u>Effective repayment rate</u> = (All payments received during the period, including arrears recovered) – (loan prepayments)] / (Scheduled amount of payments due during the period, including arrears)

12. Internal control system
    - Looked at Board of Directors and Internal Audit Committee
    - Has to analyze actual ratios and their variability over the past few months;
    - To ensure that PAR > 1 day is ≤ 5% and PAR > 30 days is ≤ 2%
    - Conduct review of the loan policies and procedures to identify weaknesses and possible modification.
    - Conducting a review of the loan officers' performance
        - Might be due to a failure of application of procedures
        - Should be replaced if not performing
        - Prepare performance improvement plans to meet targets.
    - Conducting a review of the credit committee performance
        - To determine if credit committees weaknesses are due to failure to apply policies and procedures.
        - To prepare improvement plan
    - Each SACCO was requested to design a delinquency management plan, which possesses:
        - Objectives
        - Presentation of current situation (in ratios and numbers);
        - Review of the loan policy and procedures (for example: pick 5 delinquent loans to compare to policy)
        - Review of collection policy
            - Who is doing what?
            - When does it occur?
            - Steps to be done to collect money.
            - How to improve the above.
        - Evaluation of the loan officers and credit committee members
        - Capacity building
        - Implementation time table
        - Review of the progress

Appendix F Information prepared by Rural SPEED for Mentoring Visits

1. Ratios

Ratios	December 2005	January 2006	February 2006	Financial Year End 2005 (if different from Dec. 2005)
Total Gross Loan Portfolio				
Actual Loan Loss Provision/Reserve Value				
PAR 1- 30 days				
PAR 31- 60 days				
PAR 61- 90 days				
PAR 91- 120 days				
PAR 121- 180 days				
PAR > 180 days				
PAR ≥ 1 day				
PAR ≥ 30 day				
Value past due loans 1- 30 days				
Value past due loans 31- 60 days				
Value past due loans 61- 90 days				
Value past due loans 91- 120 days				
Value past due loans 121- 180 days				
Value past due loans > 180 days				
Number of past due loans 1- 30 days				
Number of past due loans 31- 60 days				
Number of past due loans 61- 90 days				
Number of past due loans 91- 120 days				
Number of past due loans 121- 180 days				
Number of past due loans > 180 days				
Loan Loss Ratio				
Loan Loss Reserve Ratio				
Risk Coverage Ratio				
Effective repayment rate				

2. In addition, the SACCO needs to prepare, if possible, the number (detail) of loans, which are 360 days or more over due for preparation of a loan write-off calculation.

3. We will need summary loan data by past due category for loan officers, in order to calculate their PAR ratios.

4. We need to have a copy of the loan policy available.

5. We need to have a copy of any collection policy, which is not contained in the loan policy.

Appendix G Review of Delinquency Management Findings from the September 2005 SACCO Mentoring Visits

In September 2005, nine one-day mentoring visited were conducted at USAID/Rural SPEED partner SACCOs. The general observations found during these visits were:

- None of the institutions were calculating their portfolio at risk rates. SACCOs did not know how delinquent loans were without looking at each and every loan ledger card.
- Loans are approved based character and collateral. There is no business analysis of cash flows, income statements and balance sheets.
- There has not been any recognition that loan delinquency begins the day the loan is disbursed. The institutions react to the excuses given by clients and not on better information to judge how the loan will be and is actually invested in the business.
- Loan loss provisioning is not done monthly. It is not based on the actual portfolio risk.
- Loan loss write-off is not being done as required under the generally accepted accounting principles for loans delinquent more than 12 months. Loan write-off is not done because the institutions believe that writing off a loan equals forgiveness, which is not the case. Loan loss write-offs are simply an accounting procedure to remove the loans from the balance sheet and to transfer them to a “Written-off Loan” register.
- In some cases the loans policies are not adhered to by either the loan officers or the loans committee leading to previously delinquent clients receiving repeat loans and becoming delinquent again.
- The loan policies are not reviewed on a periodic basis. Many are the same as they were when the institutions were created.
- Co-signers/guarantors are rarely informed of the loan delinquency immediately and do not understand their liability (obligation) to pay if the client is delinquent. Members simply sign the forms without understanding the implications.
- Most loan collateral is land (property), however, it is difficult if not impossible to seize and sell land in rural communities.
- Some loan officers collect delinquent repayments in the field. This is both a risky and a dangerous idea for the institution. Field repayment, even with receipts can lead to embezzlement or being falsely accused of receiving payments, when the client did not give it to him. It also encourages delinquent clients to continue to wait for the loan officer to come to collect the next delinquent payment. It is a costly procedure for the institution.

In light of these weaknesses, it was recommended that:

► The board and management review the loan polices and procedures at least once a year and if possible every six months. Where the policies are found to be lacking or inappropriate they must be added or changed.

► The loan officers are evaluated to see if they are correctly applying the policies. If they are not then they should be warned and given a chance to change. If change does not occur within a reasonable time then they should be replaced.

- The loan committee members are evaluated to see if they are correctly applying the policies. If they are not then they should be warned and given a chance to change. If change does not occur within a reasonable time then they should be replaced.

- The delinquent loans in the portfolio should aged into the six age categories and the portfolio at risk rates calculated for each age category, for PAR > 1 day and for PAR > 30 days, at the end of each month. This information must be communicated to the board.

- The loan loss provisioning be done monthly based on the risk percentages.

- All loans greater than 12 months past due be written off and transferred to a “Written-off Loan” register. The board would then be responsible to follow up on these loans and not the loan officers. While this amount may be too much to do in one month, it can be phased in between now and 31 December 2005. That way the accounting will be correct at the beginning of 2006.

- Training on business analysis of loans should be conducted to teach loan officers and loan committee members how to properly evaluate business loans. This training should include formats for simple balance sheets, income statements and cash flow statements for the businesses. The amount of information required will be dependent upon the loan amount requested. The larger the amount, the more information required. It is important to increase the expenses by 20% and decrease the income by 20% during the analysis, to take into account that the fact that small businesses, without proper accounting records, generally overestimate income and underestimate expenses. If this change of 40% still gives a positive result, then the loan is likely to be successful. In addition, the monthly installment amount should not exceed 30% of the total unadjusted income. If it is 50% or more, then the business is likely to be delinquent on one or more installment.

- Higher rates of interest are charged on repeat loans to previously delinquent clients, after a 6-9 month waiting period. Additional collateral or co-signers/guarantors should be required.

- Co-signers/guarantors are required to come to the office with the client before the loan is disbursed to ensure that they fully understand their liability as a co-signer/guarantor. In addition, they need to be informed immediately when a loan payment is delinquent and must pledge either one or more shares or savings, which can be seized immediately if the loan becomes delinquent.

- When land is given as collateral, the institutions should require some form of additional guarantee, which will cover one or two installments and which can rapidly be seized and sold if the client is delinquent. This will deliver the message that the institution is serious about collecting the loan and ensure that some money is recovered before the court process to seize and sell the land occurs.

- New delinquent loan collection strategies need to be developed to reduce the number and amount of delinquencies.

- No loan officer should ever collect money from clients, no matter what the reason. If field collection is necessary the manager or the accountant should do the collections.

Appendix H Kitagata revised Delinquency Management plan

1. Objective

- To reduce loan delinquency over the next 9 months to:
  - PAR > 1 day to be ≤ 5%
  - PAR > 30 days to be ≤ 2%

  This will be based on a target of a 3% per month reduction April to August and then the rest of the way by December to achieve the benchmarks.

2. Presentation of the current situation as of 31 December 2005

- PAR > 1 day = 25.1%
- Total number of loan > 1 day past due = 332
- Value of loan outstanding > 1 day past due = 88,141,436
- PAR > 30 days = 19.8%
- Total number of loan > 30 days past due = 219
- Value of loan outstanding > 30 days past due = 69,585,520
- PAR 1 – 30 days = 5.28 %
- PAR 31 – 60 days = 3.8%
- PAR 61 – 90 days = 4.23%
- PAR 91 – 120 days = 2.28%
- PAR 121 – 180 days = 5.43%
- PAR > 180 days = 4.06%
- Loan loss ratio = 3.2%
- Loan loss reserve ratio = 3.47%
- Risk coverage ratio = 13.8%
- Effective repayment rate = 80.3%
- Current value of loan loss provision account = 12,186,869

3. Review of the loan policy and procedures

- Take a sample of at least 5 delinquent loans and compare the entire loan request and approval documents to the loan policies;
- Note anything that does not fit with the policies or any problems caused by the policies;
- Redesign the forms that the LOCs sign, provide them with exercise books and pens to help them keep track of borrowers pledged collateral;
- Make recommendations for changes to the board;

4. Review the loan collection policy

- Design new reminding and warning letters to be sent to both the delinquent client and the guarantors;
- Follow up more with guarantors even after two weeks
- Work on alternative collaterals such as cows, vehicles (log books), computers, radios, televisions, bicycles and furniture.
- To pay bonuses to loan officers who exceed the new targets

5. Evaluate the loan officers and loan committee

- On the quality of the loan appraisal;
- On how well the loan documentation is completed and how complete it is (ledger cards, forms, postings up to date);
- On PAR ratios;
- Number of loans disbursed during the period;
- Value of loans disbursed during the period;
- Value of loans outstanding at the beginning and end of the period;
- Total number of clients;
- Relationship with the public; and Work attitude.

6. Provide training to build capacity

- Training for the loan officers and loan committee members on the revised loan policies and collection policies;
- Include the guarantors in the pre-disbursement trainings
- Train the 109 LOCs on their roles and responsibilities in the loans collateral and recovery process and to show them how to maintain the suggested collateral registration books.

7. Implementation Timetable

- 3% reduction in PAR per month in April to June
- 3% reduction in PAR per month in July and August
- October to December remaining reduction in PAR > 1 day.

8. Evaluation of progress

- Short evaluation each month; and
- Full evaluation after 3, 6 and 9 months.

Appendix I Loan Loss Provisioning and Writing-Off Bad Loans

Putting aside reserves to provide for the risk of losing some or all of the value of “bad” loans is a simple procedure, known as loan loss provisioning. The provision for loan losses represents the value of both known and potential losses due to poor loan performance; i.e., delinquent borrowers. The loan loss provision account is a contra-asset account, within the asset part of the balance sheet. This means that the account has a credit balance instead of a debit balance, which asset accounts normally have. The effect of this contra asset account is to reduce the value of gross loans outstanding by the amount of the estimated loan losses. This ensures that the total value of assets does not overstate the value of the outstanding loans.

Loan loss provisioning must be done **monthly** to accurately reflect the potential losses at the end of each month. Monthly provisioning represents a best practice approach to managing the risk of non payment of loans within the SACCO’s portfolio. Even if there is an unexpectedly large increase in the amount needed in the loan loss provisions account, this amount should be expensed during that month so that the value of the loan portfolio will not be overstated and such that the balance sheet is fully and fairly disclosed.

In order to calculate the value needed, each month, in the loan loss provision account, a calculation must be done based on the risk within the portfolio. First, the SACCO must age the loan portfolio; i.e.., to divide the outstanding loans into seven (7) age categories. These categories are:

Category 1 on time loans

These are all loans, which are current; i.e. the installments have been paid either early or on time. They are zero (0) days past due.

Category 2 PAR 1 - 30 days:

These are loans, which have installments that are 1 to 30 days past due.

Category 3 PAR 31 - 60 days:

These are loans, which have installments that are 31 to 60 days past due.

Category 4 PAR 61 - 90 days:

These are loans, which have installments that are 61 to 90 days past due.

Category 5 PAR 91 - 120 days:

These are loans, which have installments that are 91 to 120 days past due.

Category 6 PAR 121 - 180 days:

These are loans, which have installments that are 121 to 180 days past due.

Category 7 PAR > 180 days:

These are loans, which have installments that are more than 180 days past due.

Once the SACCO has calculated the value of outstanding loans (principal balance) for each of these ageing categories, then those values can be used to calculate the amount of provisioning that is necessary. As the number of days a loan is past due increases, so does the risk of default (non payment). The risk of loss is always considered with respect to the entire outstanding loan principal amount and not the past due installment amount. Using the past due installment amount significantly underestimates the risk to the SACCO. Delinquency on the current installment indicates a probable delinquency on future installments since most delinquent borrowers cannot pay two or more installments at a time to catch up on payments. Thus they are likely to continue to be late throughout the loan repayment period and the entire outstanding principal is at risk.

This increased risk of loss, as the loan becomes more delinquent, is generally expressed as a percentage. This percentage is used to calculate the amount of loan loss provisioning, which is required to cover the risk by ageing category. The SACCO best practice standards recommend that provisioning be calculated as follows (Table 1):

Table 1 Loan Loss Provisioning Rates

Category	Loan Delinquency	Provisioning Rate
1	0 days past due	0%
2	1–30 days past due	10%
3	31–60 days past due	25%
4	61–90 days past due	50%
5	91–120 days past due	75%
6	121–180 days past due	85%
7	> 180 days past due	100%

Based on the provisioning rate, the formula for calculating the required amount of loan loss provisions is as follows:

Total required value for the loan loss provision account =

(Value category 2 x 10%) + (Value category 3 x 25%) + (Value category 4 x 50%) + (Value category 5 x 75%) + (Value category 6 x 85%) + (Value category 7 x 100%)

Table 2 provides an example of aging and of how to calculate the amount of loan loss provisions, which are required.

Example 1: In January 2006 the value of loans outstanding in the SACCO was as follows:

Table 2 Loan Ageing for January 2006

Loan Delinquency	Outstanding Principal	Provisioning Rate	Provision
1–30 days	21,030,000	10%	2,103,000
31–60 days	14,405,000	25%	3,601,250
61–90 days	8,044,000	50%	4,022,000
91–120 days	6,146,000	75%	4,609,500
121–180 days	1,243,500	85%	1,056,550
> 180 days	39,719,867	100%	39,719,867
Total	90,588,367		47,343,617

Once the total value of the loan loss provisioning account is known then the SACCO can calculate the amount needed for the current month’s provisioning expense.

Amount of monthly loan loss provision expense =

(Total required value for the loan loss provision account) - (Current Value (end of last month) of Loan Loss Provision Account)

If the amount in the Loan Loss Provision account was 41,678,900 at the end of December 2005, then the amount of loan loss provisioning expense for January 2006 should be:

47,343,617 – 41,678,900 = 5,664,717.

The SACCO would then pass the following operations in the December journal on the last day of the month; i.e., 31-01-06

	DEBIT	CREDIT
Loan Loss Expense Account	5,664,717	
Loan Loss Provision Account		5,664,717

The operation on the Loan Loss Provision account ledger card would be as follows:

Table 3 Loan Loss Provision Account Ledger Card

Date	Ref. No.	Description	Debit	Credit	Balance
31-12-05		Balance in LLP		41,678,900	41,678,900
31-01-06	554	LL Provisioning for Jan.		5,664,717	47,343,617

In addition to monthly loan loss provisioning, loan write-offs need to occur once a loan becomes delinquent for one year (360 days or 12 months) or more. Loan write-offs should be done monthly, as the specific loans become 360 days past due. It is too late to do this at the end of the financial year. This is simply an accounting procedure to ensure that gross loan portfolio is not overstated in the balance sheet. Please note that this is not a forgiveness of debt. While from an asset point of view, the loan no longer exists, it does not mean that loan recovery measures stop.

It is important that a memorandum account and written-off loans register be created to list the written off loans for future collection. While this is not part of the double entry accounting system, it will allow the SACCO to follow up on written-off loans.

Example 2: During the February 2006, the SACCO decided to write off all of the loans, which were greater than 360 days past due; i.e., in the > 180 days ageing category. The number of loans written off is 111, with a total value of 39,719,867. It should be noted that the procedures for writing of a loan are as follows:

Step 1 The accountant recognizes that the loan became past due more than 360 days during the month of February.

Step 2 The accountant completes the "Authorization to Write-Off Loan Principal" for each of the 111 loans, one by one.

Table 4 Authorization to Write-Off Loan Principal Form

SAVINGS AND CREDIT COOPERATIVE SOCIETY, Ltd.

(Full Address and Logo)

Authorization to Write-Off Loan Principal

1. Date: ____________________________
2. Member Name: ____________________________
3. Member Account No.: ____________________________
4. Loan No.: ____________________________
5. Principal outstanding (past due): ____________________________
6. Amount requested to be written-off: ____________________
7. Requested by (full name, title and signature): _________________________
8. Reason why the loan principal should be written off:

____

Approval

I, ___________________________, in my position as **Chairman of the Board** hereby authorize the ________SACCO Manager to write off the loan principal for the above mentioned SACCO member and loan account in the amount of: ________________

Name Date Signature

Step 3 The accountant presents the completed loan loss write-off authorization request forms to the manager, who must also approve the request. The SACCO must decide if the manager will sign on the form or not.

Step 4 The manager presents the requests at the next board meeting or calls a special board meeting to discuss the proposed loan write-offs.

Step 5 The board approves or rejects the proposals. If the board approves the write-off, the form is signed by the chairman and returned to the manager.

Step 6 The manager gives the approved forms to the account, who prepares an internal transfer voucher for each written off loan.

Step 7 If one of the individual loans, No. 2678, was for 287,000, then the journal operation would be as follows:

	DEBIT	**CREDIT**
Loan Loss Provision Account	287,000	
Loan Principal for Loan Account No. 2678		287,000

Step 8 Once all 111 loan write-offs have been entered into the journal, then the total principal amount written off against the loan loss provision account is entered in the Loan Loss Provision ledger card. Since the amount is subtracted from the loan loss provision account the calculation is:

47,343,617 - 39,719,867 = 7,623,750

The entry would be shown as follows:

Table 5 Loan Loss Provision Account Ledger Card after Loan Write-Offs

Date	Ref. No.	Description	Debit	Credit	Balance
31-01-05		Balance in LLP		41,678,900	41,678,900
31-01-06	554	LL Provisioning for Jan.		5,664,717	47,343,617
28-02-06		Write off of 111 loan	39,719,867		7,623,750

After the loan loss write-offs operations are completed, the SACCO must age the outstanding loans and calculate value of the Loan Loss Provision account, as follows:

Table 6 Loan Ageing for February 2006

Loan Delinquency	Outstanding Principal	Provisioning Rate	Provision
1–30 days	13,450,500	10%	1,345,350
31–60 days	12,844,000	25%	3,211,000
61–90 days	8,599,500	50%	4,299,750
91–120 days	4,047,500	75%	3,035,625
121–180 days	2,844,500	85%	2,417,825
> 180 days	0	100%	0
Total	41,718,000		14,309,550

Once the total value of the, loan provisioning account is known, then the SACCO can calculate the amount needed for the current month's provisioning expense:

Given that the amount in the Loan Loss Provision is currently 7,623,750, the February loan loss provisioning expense should be:

14,309,550 – 7,623,750 = 6,685,800

The SACCO would then pass the following operations in the February journal:

	DEBIT	**CREDIT**
Loan Loss Expense Account	6,685,800	
Loan Loss Provision Account		6,685,800

The operation on the Loan Loss Provision account ledger card would be completed as follows:

Table 7 Loan Loss Provision Account Ledger Card - February 2006

Date	Ref. No.	Description	Debit	Credit	Balance
31-01-05		Balance in LLP		41,678,900	41,678,900
31-01-06	554	LL Provisioning for Jan.		5,664,717	47,343,617
28-02-06		Write off of 111 loan	39,719,867		7,623,750
28-02-06	556	LL Provisioning for Feb.		6,685,800	14,309,550

This completes the operations for the month. The operations will be repeated in the following month if other loans become delinquent more than 360 days during that month.

Finally, the loan loss provision account is provisioned each month, based on the portfolio at risk calculation unless the amount in the loan loss provision account is greater than the risk calculated value.

Appendix A Loan Loss Authorization Request Form

SAVINGS AND CREDIT COOPERATIVE SOCIETY, Ltd.

(Full Address and Logo)

Authorization to Write Off Loan Principal

1. Date: ______________________________
2. Member Name: ____
3. Member Account No.: ____
4. Loan No.: ____
5. Principal outstanding (past due): ____________________________________
6. Amount requested to be written-off: ____________________________________
7. Requested by (full name and title): ____
8. Reason why the loan principal should be written off: ____________________________________

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Approval

I, ____, in my position as **Chairman of the Board** hereby authorize the _____________________SACCO Manager to write off the loan principal for the above mentioned SACCO member and loan account in the amount of:

____________ ____________ __________________________________

Name Date Signature