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Tijara Provincial Economic Growth Program: An Assessment of Microfinance Program Reporting and Lending Institution's Operations

FINAL REPORT

January 5, 2010

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FINAL REPORT



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Contracted under 267-C-00-05-00508-00

Monitoring and Evaluation Performance Program, Phase II (MEPP II)

DISCLAIMER

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

TABLE OF CONTENTS

LIST OF ACRONYMS	ii
EXECUTIVE SUMMARY	1
INTRODUCTION	3
THE DEVELOPMENT PROBLEM AND USAID'S RESPONSE	4
PURPOSE OF STUDY	6
METHODOLOGY	6
ASSESSMENT FINDINGS.....	8
Monthly Reports.....	8
Summary Review of Tijara Monitoring and Evaluation System.....	18
Management Best Practices	19
CONCLUSIONS	25
ANNEX A: SCOPE OF WORK	26
ANNEX B: METHODOLOGY	30
ANNEX C: LITERATURE REVIEWED	34
ANNEX D: ILLUSTRATIVE M&E FIELD EVALUATION MISSION SCHEDULE	35
ANNEX E: DEFICIENCIES OR WEAKNESSES IN MANAGEMENT BEST PRACTICES.....	36
ANNEX F : SCHEDULE OF MEETINGS AND FIELD VISITS.....	38
ANNEX G : LOAN DATA VERIFICATION REPORTS.....	39

LIST OF CHARTS AND TABLES

Table I: Microfinance Institutions in Iraq as of August 2009.....	7
Chart 1: DATA FLOW AND SYSTEMS within the MFIs: Loan Application and Approval.....	11
Chart 2: DATA FLOW AND SYSTEMS from MFIs to TIJARA	12
Chart 3: DATA FLOW AND SYSTEMS from TIJARA to USAID/EGA.....	13

LIST OF QUOTES FROM KEY INFORMANT INTERVIEWS

Box 1. Shariah-Compliant Loan Products.....	23
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LIST OF ACRONYMS

AOTR	Agreement Officer Technical Representative
BFF	An Iraqi Microfinance Institution (Bright Future Foundation)
CBI	Central Bank of Iraq
CGAP	Consultative Group to Assist the Poor (World Bank)
COP	Chief of Party
COTR	Contracting Officer's Technical Representative
CPA	Coalition Provisional Authority
DQA	Data Quality Analysis
EGA	Economic Governance/Agriculture
ePRT	Embedded Provincial Reconstruction Team
FSS	Financial Self Sufficiency Ratio
FY	Fiscal Year
GoI	Government of Iraq
IBTCI	International Business & Technical Consultants, Inc.
IMFI	International Microfinance Institution
IR	Intermediate Result
LAR	Loans at Risk
LPF	Loan Performance Software
M&E	Monitoring and Evaluation
MBP	Management Best Practices
MENA	Middle East and North African Region
MEPP II	Monitoring and Evaluation Performance Program, Phase II
MIS	Management Information Systems
MFI	Microfinance Institution
MOU	Memorandum of Understanding
NGO	Non-Governmental Organization
OER	Operation Expense Ratio
OSS	Operational Self Sufficiency Ratio
PAR	Portfolio at Risk
PCMS	Performance Classification & Monitoring System
PEG	Provincial Economic Growth
PMP	Performance Management Plan
PRT	Provincial Reconstruction Team
Q	Quarter
RF	Results Framework
SANABEL	A network serving Microfinance Institutions in the Arab world
SEEP	The Small Enterprise Education and Promotion (Microfinance Network)
SO	Strategic Objective
SOW	Scope of Work
TEDC	An Iraqi MFI: Tal' Afar Economic Development Center
TDMN	An Iraqi MFI: Al Tadamun
USAID	United States Agency for International Development
USG	United States Government
USM	United States Military

EXECUTIVE SUMMARY

The Tijara Private Sector Development program and its predecessor Izdihar have been responsible for the birth of the Microfinance industry in Iraq, and more importantly the development of indigenous Iraqi microfinance institutions (MFIs). Together, they have expanded impressively the microfinance activities launched by the Coalition Provisional Authority in 2003.

The microfinance industry in Iraq has achieved notable accomplishments since 2003. This has been a critical element in promoting private sector development in general, and Iraqi small businesses in particular. Over the past two years, the Tijara program has helped introduce the systematic reporting of microfinance loan activities through the introduction of standard software now used by all grant recipients.

The United States Agency for International Development/Economic Governance and Agriculture (EGA) Office requested an assessment of the reporting and best practices employed by the microfinance institutions' (MFIs') on the Tijara program. The main objectives of this assessment are: (i) to review and validate the "Sustainable Microfinance" supporting documentation that Tijara uses to compile the monthly "Outreach and Collection Performance" report submitted to USAID/EGA; and, (ii) assess the management best practices of the local Iraqi MFIs.

A field verification on the veracity of the loan figures by two MFIs (Al Bashaer and Al Mosaned) was conducted to validate the figures in the monthly "Outreach and Collection Performance" report. The management best practices were assessed through a desk review of MFIs operational assessments, an interview with Tijara staff and a field interview with staff from four MFIs (Al-Aman, TEDC, Al Tadhmun and BFF).

The spot check verification with the two MFIs showed that the figures reported in the monthly outreach and collection performance report to USAID are accurate. For example, the comparison of the "Amount in \$ of loans disbursed" and the "Number of loans disbursed" to those reported in the "Outreach and Collection Performance" revealed that they were the same for Al Bashaer (August 2009) and for Al Mosaned (September 2009), and hence, the figures reported to USAID are accurate. However, given that this verification was not statistically representative, and cannot be generalized, some risks of errors and weaknesses identified from the analysis of the data flow should be addressed.

As evidenced by the data flow analysis, MFIs weaknesses stem mainly from various flaws identified in applying the existing credit and accounting manuals, policies and procedures and the presence of transcription risks in the processing of loan information. MFIs managers are also unable to monitor loan officers to adequately perform their duties on the basis of MFIs operational procedures.

Transcription risks came mainly from the manual process stages in the preparation and compilation of the monthly "*Outreach and Collection Performance*", the lack of real verification of compiled data, and, in general, the absence of a plan for data quality assessment both at Tijara and at the MFI levels.

Tijara is committed to and mainstreams MFI management best practices but this assessment revealed that the following deficiencies should be addressed to improve MFI management best practices:

- (1) the lack of appropriate follow-through by MFI management in addressing the recommendations of the operational assessments. Specifically, weak or absent internal control or audit, and inadequate management information systems (manual and computerized) to ensure the quality of data being reported to Tijara were frequently pointed out.
- (2) the absence of targeted capacity building for MFI board members and management, particularly in the areas of strategizing, operations, risk and delinquency.
- (3) the difficulties in developing Shariah-compliant loan products by MFIs; and
- (4) the overdependence on Tijara Technical Assistance and subsidized trainings;

Recommendations for Tijara

- Encourage MFIs to comply with MFI best practices in management information systems.
- Revise, update and adequately monitor the application of policies and procedures related to data, information management, and systems; and the clarification of Loan Officer's responsibilities.
- Specifically, mainstream a culture of internal control within MFIs and establish a clear internal control with more data checks to reduce transcription risks that should be linked to a comprehensive data quality assessment plan and Tijara M&E systems.
- Work with MFIs to define clearly planned activities that address the major deficiencies identified in the operational assessments.
- Develop specialized training for Board Members and Management that is custom-designed to meet their needs and the realities of doing business in Iraq.
- Encourage and assist MFIs to collaborate with the SANABEL network to acquire best practices, especially with regard to Shariah-compliant loan products.

Recommendations for USAID

- Ask Tijara to update its PMP.
- Consider incorporating within future Grant Agreements and Grant Amendments between Tijara and MFIs explicit guidance and requirements on DQA.
- Consider applying ADS Chapter 219.3.5.2, "Microfinance Institution Commitment to Attain Full Financial Substantiality" to MFIs in Iraq.
- Include a requirement for independent field verification that encompasses a data quality audit, confirmation of loan beneficiaries through direct interviews, and systematic interviews of unsuccessful loan applicants.

INTRODUCTION

Louis Berger was awarded the Tijara Provincial Economic Growth Project (PEG) contract (267-C-00-08-00500-00-05 on January 23, 2008. Overall, the objective of the Tijara-PEG activity is to grow the Iraqi economy by promoting private sector development by increasing access to finance. There are two components to the project. Under Component One, Tijara provides business development services (BDS) targeted primarily through the Small Business Development Centers (SBDCs) Tijara additionally continues to assist the Government of Iraq (GoI) in its efforts to join the World Trade Organization and establish the National Investment Commission (NIC). Under Component Two, Tijara focuses on expansion of commercial lending through specialist microfinance institutions (MFIs) and commercial banks by identifying and reducing market lending risks; providing training and technical assistance; disseminating information, education, knowledge management and research; and, operating a grant facility. A complementary objective to Component Two is promoting the development of an accessible, demand-driven market for high quality capacity building services that are responsive to the differing needs of MFIs and their clients. The present assessment focused on this complementary objective.

The Provincial Economic Growth (PEG) staff began a dialogue with the Central Bank of Iraq (CBI) and other GoI authorities, to harmonize and integrate Non-Governmental Organization (NGO) MFIs into Iraq's formal financial system. While Iraq has a long history of informal finance such as family- or village-based rotating savings and credit societies, best-practice microfinance only began as an industry in 2003 under the Coalition Provisional Authority (CPA).

The microfinance industry has experienced impressive growth since its inception in 2003. Its growth in outreach to clients was as high as 78% per annum through December 2007. From December 2007 through January 2009 growth declined to a still impressive 64%. This decline is attributable to the stage of growth of the MFI industry, lack of MFI capital, limited institutional capacity, and a lack of enabling legislation to support the industry. Some major accomplishments include:

- Eleven emerging microfinance institutions are now functioning, nine of which are indigenous, and collectively constitute an outreach to over 51,318 clients (15% of which are women), and oversee an outstanding loan portfolio of \$77.3 million.
- Cumulative loan disbursements of \$344 million to over 149,334 clients.
- All MFIs are at or nearing operational self-sufficiency.
- Six operational assessments have been completed for two international and four Iraqi MFIs.
- A Performance Classification Monitoring System (PCMS) has been initiated to track the evolution of the MFIs as of December 2007.
- Financial systems verified and structured to improve data quality.

According to the initial scope of work, this assessment of Tijara's Microfinance Program included two phases. The Phase One objectives were to: (a) review and validate Tijara's supporting documentation for the monthly MFI reports; (b) assess Tijara's monitoring and evaluation practices with respect to the MFI program; and, (c) assess management practices of the local MFIs. The objectives of Phase Two were to confirm through direct interview the operations of the MFI with (d.) MFI loan officers and, (e) loan beneficiaries. After the debriefing of Phase One to USAID on November 9, 2009, Phase Two was implemented with the objective focused on verifying loan figures reported by Tijara through its monthly report to USAID.

THE DEVELOPMENT PROBLEM AND USAID'S RESPONSE

Problem Statement

Decades of war and the collapse of the Ba'athist government resulted in the devastation of the entire Iraqi economy, including its financial institutions and service industry. In order to facilitate a modern market economy and ensure sustainable economic growth it is imperative that banking and non-bank financial institutions are developed and strengthened. This includes the development of financial institutions that support equitable access to financial services and that serve, among others, the poor, women, and micro, small, and medium sized businesses.

Theory of the Intervention

The USAID Strategy is a key element in the United States' plan for democratic and free market development in Iraq. This strategy emphasizes responsiveness and sustainability through an expanded role in supporting focused political and economic stabilization through building national capacity and establishing the foundations for economic growth. These efforts will diminish the appeal of insurgency, help in fostering democratic institutions, and promote sustainable economic development. As a result, a stable, democratic, and prosperous Iraq will emerge.

In January 2006, USAID/Iraq approved a three-year Strategic Plan (2006-2008, extended through 2009) that represents an integrated approach along three broad tracks (i.e. security, economic, and political). This plan incorporates efforts made across the U.S. government and works in coordination with the Gol and the international community. It supports peace, economic expansion, and democracy through four Strategic Objectives:

1. Reduce incentives for participation in violent conflict (SO 7).
2. Expand private sector economic opportunities (SO 8).
3. Strengthen responsive and effective local government (SO 9).
4. Improve capacity of national government institutions (SO 10).

SO8 encompasses all USAID's activities related to the growth of Iraq's private sector. Under SO8, USAID aims to be an enabler of private sector growth (Intermediate Result (IR) 8.1); to

increase the capacity of the private sector (IR 8.2); and to strengthen the infrastructure necessary for a modern economy (IR 8.3). Activities related to the creation of financial, legal, and regulatory frameworks necessary for the growth of a functioning market economy are related to IR 8.3.

The microfinance activities of Tijara occur under IR 8.3. These activities are based on the belief that rapid and sustainable economic growth can occur only when the basic infrastructure for a modern market economy is in place. This infrastructure includes functioning banking and non-bank financial institutions that support equitable access to essential financial services that will benefit entrepreneurs as well as micro, small, and medium sized businesses. These activities correspond with and support the Embassy's FY09 Mission Strategic Plan, which includes "...reforming Iraq's cash-based economy by fostering new financial institutions, making capital available, encouraging business growth and home-owning."

The Design of Microfinance Program under Tijara PEG

The Tijara project provides financial and technical assistance for start-up, expansion, new product development and other forms of capacity-building of retail microfinance institutions to increase access to financial services for those currently excluded. The project launched several new indigenous MFIs in addition to continuing to support existing ones. This support includes training in accounting and modern loan administration, provision of technical assistance, and direct funding to expand services over the life of the project.

PURPOSE of STUDY

By taking into account the refocusing of Phase Two's initial objectives, the purpose of this assessment is to analyze the data flow and validate the veracity of loan figures provided in monthly microfinance reports that Tijara provides to EGA. It also assesses microfinance best practices of the local MFIs working with Tijara.

METHODOLOGY

The Iraqi MFI industry established by the USAID-funded Izidiyar and Tijara projects consists of three large international NGOs and seven indigenous NGOs operating throughout the country since 2003. As of August 2009, a total of \$ 343,533,252 in loans was disbursed to 149,334 beneficiaries by these MFIs. The loans disbursed by the indigenous MFIs total 13.9% (in value), distributed to 20,751 recipients (12.7%) since inception. This assessment focuses on the indigenous Iraqi MFIs. Table I presents these MFIs and identifies those selected during the assessment for the field data verification and interviews on MFI management practices. The following methods were employed to collect the data:

- Desk review of microfinance literature, USAID and Tijara documents, and reports on MFI grant recipients. IBTCI staff requested and reviewed all relevant documents and reports. (See list in Annex C)
- Interviews with Tijara staff. Questions were developed for these interviews (See Annex B):
- Key Informant Interviews with four MFI staff in Erbil on Management Best Practices. Questions were developed for these interviews (See Annex C)
- Field verification of loan figures in the loan recipient physical files kept by two MFIs.

Table I: Microfinance Institutions in Iraq as of August 2009

Name of MFI	Location of Head Office	Value of Loans disbursed in \$	Number of loans disbursed
<i>International NGOs</i>			
Relief International	Suleimianiya	22,421,405	15,704
ACDI/Voca (Al Tiqa)	Kirkuk	88,692,949	33,510
CHF International	Hilla, Babel	188,532,153	79,639
<u>Sub Total</u>	<u>3</u>	<u>299,646,507</u>	<u>128,523</u>
<i>Iraqi MFIs (Indigenous)</i>			
<i>Al Aman</i> ⁽²⁾	Kirkuk	6,193,965	2,981
<i>Al Bashaer</i> ⁽¹⁾	Mansour, Baghdad	10,535,350	6,470
<i>Al Mosaned</i> ⁽¹⁾	Tikrit, SalahdDin	2,524,750	1,150
<i>Al Takadum</i>	Al-Qaim, Fallujah & Ramadi	10,934,600	4,558
<i>TEDC</i> ⁽²⁾	Tala'far, Nenawah	3,861,750	1,682
<i>Al Tathamun</i> ⁽²⁾	Mosul, Ninawah	267,500	151
<i>BFF</i> ⁽²⁾	Erbil	9,568,830	3,759
<u>Sub Total</u>	<u>7</u>	<u>43,886,745 (13.9%)</u>	<u>20,751 (12.7%)</u>
Total	10	343,533,252	149,334

Source: Tijara Monthly Outreach Performance and Collection Report, August 2009

(1) : Field data verification for Al Bashaer and Al Mosaned.

(2) : Field interviews on management best practices for Al-Aman, TEDC, Al Tathamun and BFF.

ASSESSMENT FINDINGS

Monthly Reports

Each month *Tijara* provides USAID with a comprehensive report in the form of an excel worksheet that includes information on all MFI operations including financial information and performance indicators for each MFI. These indicators are in line with the standard recommended by CGAP and used by MFIs. Each MFI -- whether a locally owned MFI or an MFI run by international NGOs, uses the same reporting format to provide a monthly "Outreach and Collection Performance" report to *Tijara*. These reports are based on the data flow and systems that link *Tijara* to the MFIs. Therefore, the quality and validity of the reports are based on the data flow and systems. A description of the data flow and systems is described in the following paragraphs.

Data Flow and Systems Linking *Tijara* to the MFIs¹

Step 1: Getting started: Vetting the loan application. After a client completes a loan application, including providing information about the guarantor, the loan officer determines how much credit should be approved. If the client is new, the loan officer must first visit the applicant's business location to ascertain the viability of the enterprise. Before making any computations, the loan officer first checks if the client's name appears on the blacklist found in the Iraqi microfinance website (www.IMFI.Org). However, this tool is not used comprehensively by the MFIs according to *Tijara* and MFIs interviewed in Erbil.

When the client and the loan officer complete the required Loan Application Form, the loan officer consults with the supervisor to decide whether or not to formally interview the applicant and discuss the proposal before submitting the application to the credit committee. If the loan applicant appears to satisfy the eligibility requirements, the supervisor and the loan officer schedule a site visit with the applicant. The application verification, analysis, and appraisal process continues until a well-informed credit decision is made to either approve or reject the loan application.

Step 2: Approving the loan. The Credit Committee reviews each loan application in detail and makes its judgment according to the policies delineated in *Tijara*'s credit policy manual. The authority to approve or reject a loan application resides with the Credit Committee. In reaching a decision, Credit Committee members use their own personal insight, experience, or privileged information concerning the applicant; consider the nature of the project to be financed; assess any other relevant information such as market conditions, feasibility, legal implications, and collateral issues. In general, credit approval and lending decisions are based

¹ MFIs refer to both local MFI and International MFI as described in the body of this report.

on an overall analysis of each applicant's loan application where each factor in the approval consideration is weighted equally.

Step 3: Entering a new loan into the system. This process differs from one MFI to another. At this stage, the client information should be entered into the LPF system as specified in the 'standard credit manual'. However, most of the MFIs do not follow this manual. They only enter the data into the system from the loan file documents after the loan has been approved and disbursed.

Step 4: Entering approved loans into the Loan Performer (LPF) Software Program. The LPF is a microfinance management information system for recording basic client data as well as accounting and portfolio information for the MFI. LPF handles shares, savings deposits, and loan tracking as well as accounting. MFIs have centralized data entry. Data entry is only done at the MFI's Head Office as branch offices send hard copies of the client and loan details to the main offices to be entered into LFP through their respective loan officers. According to the credit policy manuals, branches should keep a copy of the loan files and all original hard copies are sent to the MFI headquarter for filing. Each week, each MFI sends the LPF database to *Tijara* for internal audit purposes, including validation and ensuring that the data are consistent with *Tijara's* policies and procedures contained in the accounting manuals. It should be noted that some MFIs are still using excel sheets in parallel with the LPF to track the loan portfolio and to double-check the accuracy with the LPF data.

The MFIs make regular backups that are sent by email to *Tijara* for review and validation. At *Tijara* headquarters, the LFP data are stored on a drive named 'share drive' that is used as a repository for backing-up and securing data. Data can also be transferred between the MFIs and *Tijara's* headquarters using CDs and flash drives. Each MFI has responsible senior personnel who manage system access rights and assign user-defined system privileges to the staff depending on their need and responsibilities in their respective institutions. Once data are entered into LPF any further changes made to the data are backed-up and can be traced.

Step 5: Integrity of the data. Each MFI has a dedicated *Tijara* Program Manager who oversees the operations of the institution, including assuring that principles and practices related to data capture, storage, and retrieval are adhered to. The *Tijara* Program Manager also routinely checks the accuracy, integrity, and validity of the data entered into the LPF system against the manual records. *Tijara* staff performs regular monthly site visits to MFIs and, among other tasks, checks the accuracy of the data that has been entered. Every month, both MFI's portfolio and accounting reports are separately checked as well as the integrated general ledger to ensure that it reconciles with transactions from all the sub-ledgers.

Step 6: MFI reports on information from the LPF. Each MFI prepares a monthly report in excel format using the data and indicators generated from the LPF to *Tijara's* Senior Financial Analyst entitled: "Outreach and Collection Performance" report. This is a manual operation in which the information from the LPF is transcribed into the excel sheet.

Step 7: Tijara consolidation of MFI reports. The MFI monthly reports are consolidated and compiled into a worksheet by *Tijara's* Senior Financial Analyst who is in charge of MFI reporting and compliance. The analyst mainly uses checks and balances which are built into the reporting templates to validate the accuracy of the data contained in the monthly report. The checking includes, for example, the total outstanding at the end of the reporting period, which must be equal to the sum of total outstanding loans by sector for the same period. The analyst does not receive any LPF databases, neither does she check the accuracy of the "Outreach" reports using the databases. Finally, the verified monthly and quarterly reports are submitted to the *Tijara* Monitoring and Evaluation Director, who then prepares and submits the consolidated monthly "Outreach" report to USAID. The M&E Director's staff cuts and pastes data from the MFI monthly reports vetted by the Senior Financial Analyst into the consolidated monthly report that is sent to USAID/EGA. In the consolidated report new grand totals are tallied.

Charts 1 to 3 map pictorially how the data starting from the loan application reach the monthly "Outreach and Collection Performance" report sent to USAID/EGA. This review identifies points of weakness in the data flow process. Process weaknesses are shown graphically in the diagrams using the lightning bolt symbol. Chart 1 tracks data flow from loan applicants to MFI branches; Chart 2 from MFI branches to their head office and from MFI head office to *Tijara*; and Chart 3 from *Tijara* to USAID/EGA. Inserted text boxes assess the validity, reliability and timeliness of data reported, and verify the consistency of data at different levels.

Chart 1: DATA FLOW AND SYSTEMS within the MFIs: Loan Application and Approval

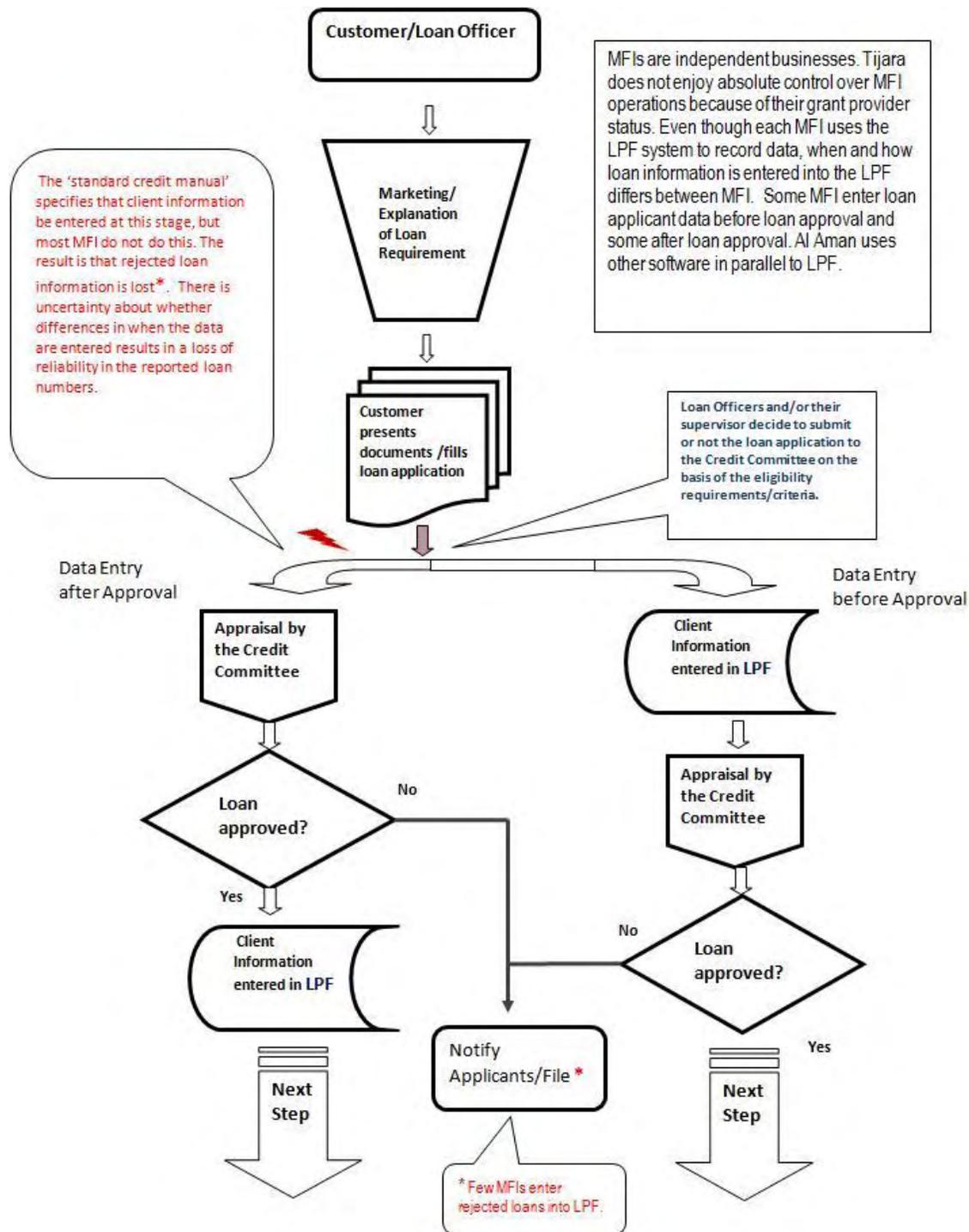


Chart 2: DATA FLOW AND SYSTEMS from MFIs to TIJARA

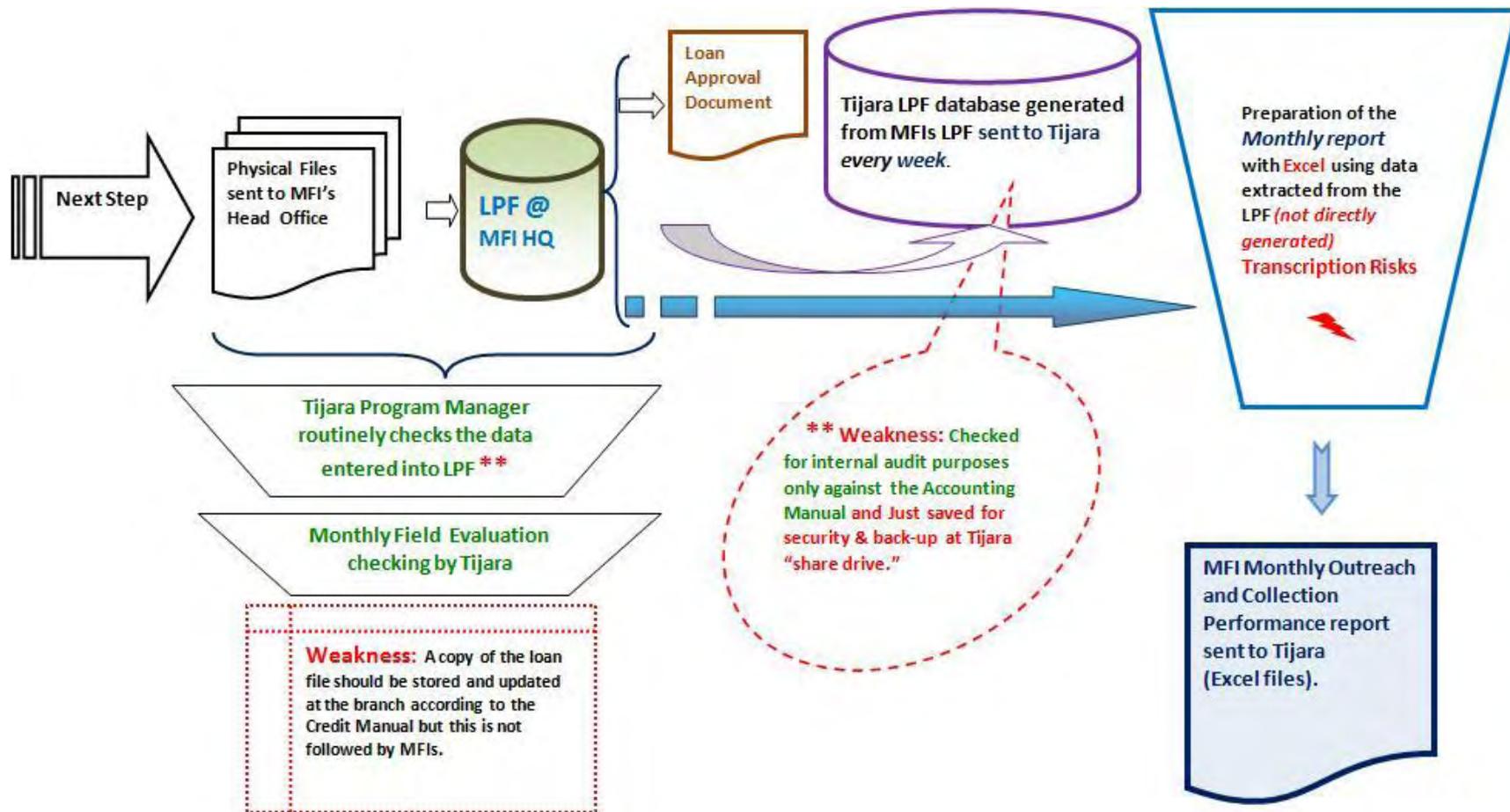
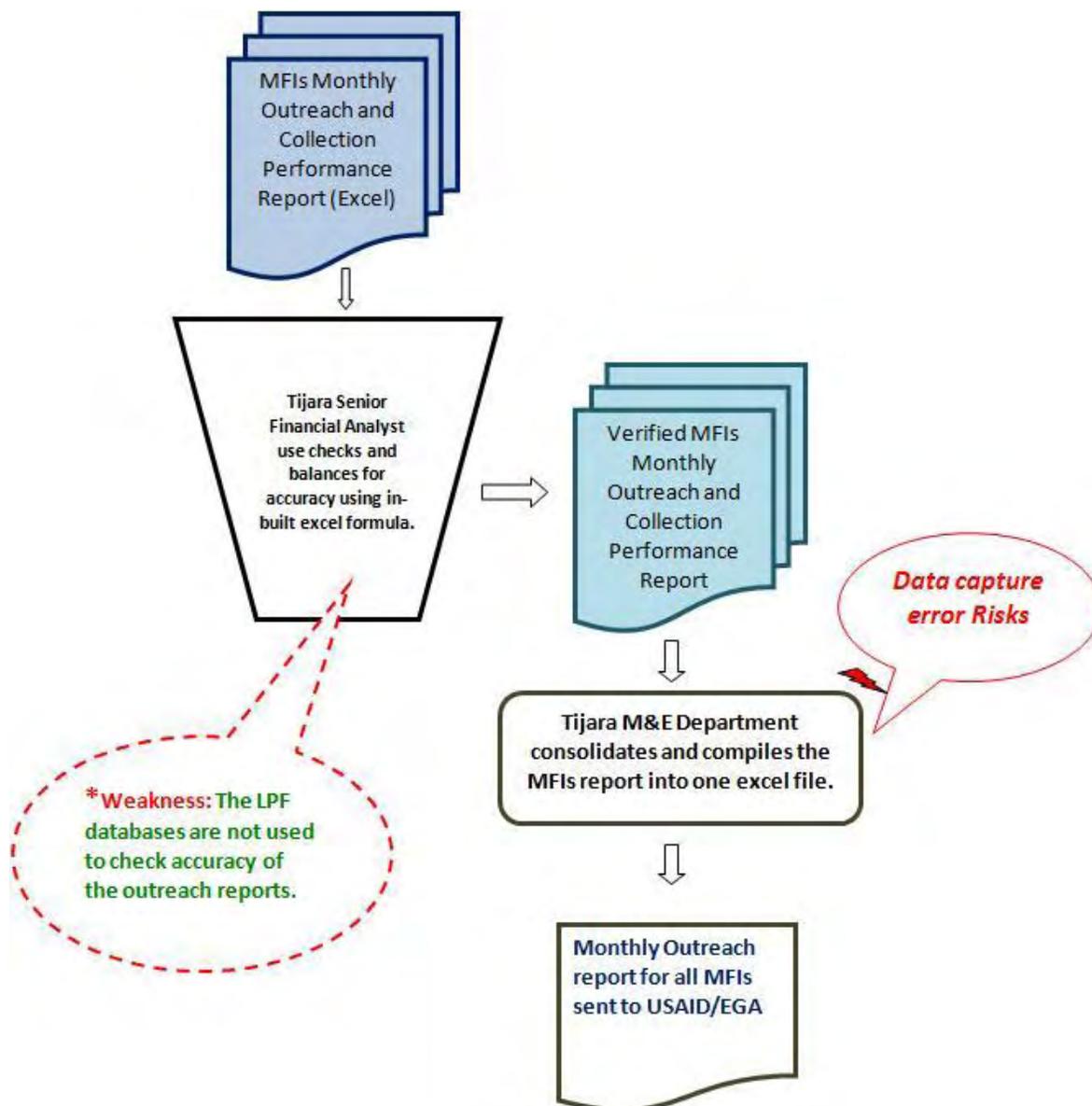


Chart 3: DATA FLOW AND SYSTEMS from TIJARA to USAID/EGA



Step 8: Validity and Reliability of data. The following procedures, actions and processes are intended to ensure that the data reported by MFIs are valid and reliable:

At the MFI level:

- Existence of policies and procedures for data reporting to Tijara: e.g. roles of loan officers in data entry, system access rights in the credit and accounting manuals;
- Traceability of changes in the LPF system;

- Separate verification of portfolio and accounting reports and comparison of general ledgers with individual ledgers.

At Tijara level:

- Regular monitoring and verification of the data in the LPF by the Program Manager;
- Weekly checking for internal audit purposes against the Accounting Manual;
- Monthly field evaluation visits to the MFI;
- Checks and balances of the MFI outreach and performance reports are performed for internal consistency using in-built formula checks.

Step 9: Timeliness of data collection. As specified in the Grant Agreement, there is evidence of operational planning for MFIs in the form of a time schedule for data collection and analysis, data entry and reporting. Tijara's in-house MFI operational assessments also serve as a key tool in monitoring the MFI management information and systems including the timeliness of data processing.

Risks

Despite the presence of the monitoring and control systems mentioned above, several risks were identified on the basis of: 1) the desk review of MFI operational assessments; and, 2) the analysis of the data flow process and the checks carried out on data accuracy with two MFIs (Al Bashaer and Al Mosaned).

Desk Review of MFI operational assessments. The MFI assessments noted several weaknesses with regard to information systems and their management, and specifically in data processing and reporting. Specifically, the policies and procedures regarding MFI data reporting to Tijara are inefficient and inadequately monitored at MFI level. Data quality may be adversely affected by the following weaknesses identified during the MFI operational assessments and in the review of MFI management best practices detailed in Annex D:

- Management knowledge and application of the policies and procedures;
- Weak internal control or capacity in internal control;
- Weak management capacity to track loan officers' duties associated with an absence of clear responsibilities and a lack of incentives to do their tasks; non-familiarity with certain key basic indicators; and; failure of loan officers to perform their duties appropriately such as timely loan filing data entry or conducting follow-up visits to loan recipients after disbursements.
- Infrequent verification due to the remoteness of branches; and

- Weak adherence to security procedures (software-data filing/storage).

Analysis of data flow and data accuracy checks. MFIs are independent businesses and they are not fully liable to Tijara as they may have other sources of funds. The following occurrences are related to this fact:

- Most of the MFIs do not record rejected loans into the LPF whether they enter the data into the LPF before or after loan approval as specified by the Standard Credit Policy Manual. There is uncertainty about whether or not differences in when the data are entered result in loss of reliability in the reported loan numbers. In addition, the result is a loss of information that could be used for more informed decision-making by MFIs and Tijara's management in order to increase their performance and outreach.
- Copies of loan files are not kept at the branch as specified by the Standard Credit Policy Manual. As a result, there is a missed opportunity for improving internal control within the MFIs.
- One MFI, AI Aman still uses double systems (Excel and LPF in parallel) to track their loan portfolio for the sake of "double-checking accuracy". In light of the good capability of the LPF system in capturing and processing client information, this appears to have limited utility.
- Though data verification and accuracy occurs during Tijara staff's field evaluation site visits, there is a lack of access to the LPF system by Tijara. Access would allow them to directly triangulate reporting of the LPF data submitted by the MFIs to Tijara.

The data and portfolio indicators in the "*Outreach and Collection Performance*" reported by MFIs are not directly produced from the LPF into the "excel reporting templates" but instead go through some manual entry processes. Hence, risks of mistakes in data capture may occur. Some loans had been approved and were later returned because they were considered *haram*. The process of subtracting these loans from the LPF is not clear and appears deficient. The LPF database in the shared drive at Tijara serves only as back-up for security purposes. It is not used to verify the accuracy of data reported in the "*Outreach and Collection Performance*" reports that form part of Tijara's monthly consolidated reporting to USAID.

There is a lack of systematic monitoring of loan recipients, such as interviewing them randomly to identify possible 'ghost' loans recipients. Hence, the validity of the data submitted by the MFI relies totally on what the MFI reports to Tijara. Tijara's M&E should systematically interview loan recipients as part of a sample audit of beneficiaries.

Sustainability of the MFI is a concern of USAID. Adherence to the stated USAID policy under ADS chapter 219.3.5.2, "Microfinance Institution Commitment to Attain Full Financial Substantiality," is not found in the existing Grant Agreements with MFIs. The ADS policy states that missions must obtain a written commitment from microfinance institutions to attain full financial sustainability on that institution's financial service activities within seven years of the initial provision of USAID assistance, prior to entering an agreement. This omission should be reconciled.

Data quality issues are only indirectly addressed in the Grant Agreement between MFIs and Tijara. These issues are planned for future discussion and agreement with the MFIs after the award of the grant.

Field data verification. Following a visit by IBTCI to one MFI for the purpose of examining loan documentation first hand, IBTCI tasked an Iraqi accountant firm to examine loans at two MFIs (Al Bashaer and Al Mosaned). The accountants were tasked to count from the loan recipients' physical files the number of loans disbursed while adding up the amount of all loans disbursed during the month considered.

Each loan contract agreement was examined and was the source of the information on loan amounts disbursed. The results are compared to the figures reported in "*Outreach and Collection Performance*" report to USAID. The two MFIs were randomly selected without any particular reason or consideration. The methodology is considered as a spot check in parallel to the data flow and reporting review. In this spirit, seeing that the two MFIs do not constitute a representative sample of all Tijara MFIs and the review only represents a specific point in time (months/years), the conclusions are applicable to two out of five possible local MFIs, and should be considered indicative.

The auditor counted the number of loans disbursed and added up the amount of all loans disbursed during the month of August 2009 (Al Bashaer) and September (Al Mosaned). The results are compared to the figures reported in "*Outreach and Collection Performance*" report to USAID for those same months. For both MFIs, no differences were found. The "Value of loans in \$" and the "Number of loans disbursed" compiled by the accounting firm at the verification match exactly the figures reported by Tijara to USAID in the Monthly Outreach Reports.

The figures in the "Outreach and Collection Performance" report to USAID for Al-Bashaer (August 2009) and Al-Mosaned (September 2009) are accurate. However, while there is no reason to doubt the results of this verification, and in light of the fact that this verification was not statistically representative and cannot be generalized, the following recommendations are provided in light of the key weaknesses identified from the analysis of the data flow.

Recommendations

An adequate information system is critical to the success of any organization and includes all the systems (both manual, physical, and computerized) used to generate the information that guides management action and decisions. From weaknesses identified during the MFI operational assessments, there is a lack of personnel and/or staff capacity to adequately manage information systems. Tijara should require MFIs to put in place internal controls built-in within MFI information systems with the specific objectives to report timely, reliable, accurate, user-friendly, secure, and cost effective data, and meet the needs of various users. To this end, Tijara should do the following:

- Revise, update and adequately monitor the consistent application of policies and procedures related to data collection and information management systems. This includes clarification of Loan Officer responsibilities, ensuring familiarity with key indicators, and developing an incentive system for good performance.
- Structure clear controls and/or audits that are internalized within MFIs and link it to M&E. Make internal control a priority by making sure that supervisory checks and balances are in place and systematically conducted to avoid mal-data entry and data mismatch.
- Ensure all manual, physical, and computerized systems are suitably linked and secure to allow timely and accurate reporting and sharing of data and information that guides management action and decisions.
- Have the Senior Financial Analyst or the M&E Department use the LPF database to verify the figures included in the monthly *Outreach and Collection Performance* reports.
- Encourage MFIs to comply adequately with MFI best practices in management information systems despite the fact that they are “independent” and not fully liable to Tijara.

In addition to the recommendation for Tijara, it is recommended that USAID do the following:

- Ask Tijara to update its PMP and stress the need to address data quality to give assurance that: (a) data quality assessments are conducted properly; and, (b) reported results are appropriately verified in accordance with the established agency guidance.
- Consider incorporating in future Grant Agreements and Grant Amendments between Tijara and MFIs explicit guidance and requirements on DQA. This should be finalized and agreed to before the award.
- Verify the status of the application of USAID policy under ADS chapter 219.3.5.2, “Microfinance Institution Commitment to Attain Full Financial Substantiality” and consider applying it to MFIs in Iraq. If not applicable, a waiver may be required.
- Include a requirement for independent field verification that encompasses a data quality audit, confirmation of loan beneficiaries through direct interview, and systematic interviews of unsuccessful loan applicants.

Summary Review of Tijara Monitoring and Evaluation System

Tijara's PMP is the core document for the M&E system. The PMP monitors the achievements of program operations. It is a blueprint that details how Tijara will collect and analyze performance information to track progress toward planned results. The microfinance component of the project is within SO 8 (Private Sector Economic Opportunities Established) and IR 8.3 (Infrastructure for Modern Economy Strengthened). Indicator 8.3 is the number and dollar value of loans made through MFIs and banks. Although there are three sub-indicators associated with the microfinance program, Indicator (Sub-IR) 8.3.1.1 is the only one related to this evaluation. Indicator 8.3.1.1 tracks the progress made by MFIs in establishing best practices in their back offices and management systems. In addition, Tijara uses different monitoring, assessment and reporting tools to disseminate progress and the achievements of MFIs. These include:

1. Field evaluation site visits
2. Operational assessments
3. Performance Monitoring Tool (PMT)
4. Performance and Classification Monitoring System (PCMS)

Field Evaluation site visits. Throughout the year, the Field Evaluation Specialist conducts site visits to each MFI several times per quarter to verify monthly data the MFIs provide to Tijara and verify documents that support the distribution of loans (See Annex E: Illustrative M&E Field Evaluation Mission Schedule). Verification activities include supervisor interviews, loan officer monitoring, field visits to borrowers, and filing and reporting system reviews. The Field Evaluation Specialist also tracks the progress MFIs made toward implementing recommendations from any previous assessments.

Operational Assessments. Operational assessments were conducted to tailor technical assistance to the diverse needs of Iraqi MFIs that differ from one another in skill levels, training, and maturity. To this end, Tijara Baghdad staff conducted seven operational assessments from May 2008 to April 2009 for the more mature MFIs (over one year old). They included the following MFIs: Al-Aman (Aug. 2008, April 2009), Al-Bashaer (March 2009), Al-Takadum (March 2009), and the Tal'afar Economic Development Center (TEDC) (Oct. 2008). These assessments had two purposes. First, they were designed to assist the MFIs by grading each in the seven PCMS reporting areas and providing each MFI with a technical plan to improve their operational performance. As their operational skills improved MFIs were able to access increased Tijara funding. Second, the assessments were to determine MFI capability to achieve goals and objectives, to service their clients, and to assure custodianship of the resources allocated to them.

The assessments included interviews with MFI Executive Directors, Loan Officers, and clients; as well as reviews of various documents related to the PCMS's seven reporting areas. Each area was rated on a 5-point Likert scale. At the end of each assessment report the MFI was

appraised and given a grade. A set of recommendations were listed and discussed with MFI management. As the MFI implemented these recommendations they were able to obtain Tijara funding.

Performance Monitoring Tool (PMT). The PMT is a data platform that Tijara is localizing and rolling out to the MFIs to streamline the reporting process in 2009. The PMT simplifies and automates the monitoring process. The goals of the PMT are to: (1) ease the reporting burden on MFIs and on Tijara in order to produce one rather than several reports that are compiled on a monthly and quarterly basis; and, (2) reduce the risk of human error in the current excel-based reporting system.

Performance and Classification Monitoring System (PCMS). The PCMS tracks the evolution of MFI performance in areas of outreach, self-sufficiency, portfolio health, operating efficiency, and portfolio yield. In the PCMS, Iraqi MFIs are rated and verified vis-à-vis their peer institutions in the MENA region. The PCMS, along with the completion of MFI assessments, allows Tijara to analyze MFI suitability in consideration for Tijara grants. MFI data are recorded in monthly reports and are fed into the PCMS. Based on internationally acknowledged standard reporting ratios for microfinance, the PCMS compiles performance results from all participating MFIs on a monthly and quarterly basis, then feeds back the results to the participating MFIs. PCMS also disseminates compiled performance data to donor agencies, lenders, and eventually Central Bank of Iraq (CBI). The PCMS consists of the following:

- An institutional coding tool indicating ownership and age. Only the database manager and the MFI know which data belongs to which MFI. The purpose of the tool is to present accurate, industry-wide performance data to stakeholders. It is not intended to be used to expose particular MFIs.
- A set of Good Practice Microfinance Performance ratios that reflect scale and depth (size); quality within the areas of delinquency management (Portfolio at Risk); cost control (operational expense ratio); productivity (loan officer case load); and sustainability (operational and financial self-sufficiency ratios).
- A minimum performance standard matrix for each category of MFI (A-D), with ranges of performance into which MFIs can plot and score their own performance to arrive at a category of maturity. The four grades are: D: Start Up Stage; C: Consolidation Stage; B: Expansion Stage; A: Commercial Viability Stage.

Management Best Practices

To find out if Tijara MFIs follow management best practices in microfinance, we reviewed Tijara's approach in mainstreaming management best practices through: 1) interviews with Tijara staff; 2) a review of Tijara documents related to management best practices; 3)

identification of challenges related to management best practices based on the review of the operational assessments; and, 4) interviews with four MFIs.

Tijara Approach to MFI Management Best Practices

There is much evidence that Tijara is committed to and mainstreams MFI best practices, particularly with regard to MFI management practices. The CGAP and the Microfinance Gateway are the two main sources used by Tijara for updating microfinance best practices. Tijara's main reference is a document entitled "*Izdihar Microfinance Best Practices*" that was developed by the previous microfinance project Izdihar In June 2007. Tijara employed this document to mainstream microfinance best practices and to create a set of industry norms in Iraq. Practices pertaining to technical and methodological aspects of the program are described in the document and contextualised to reflect the conflict-environment in Iraq.

Tijara's approach to mainstreaming microfinance best practices is focused on analyzing key opportunities and constraints for access to financial services from the following perspectives²:

- *Macro (policy, legal, and regulatory constraints),*
- *Meso (financial infrastructure audit, ratings, and networks), and*
- *Micro (MFIs and other financial service providers/promote best practices)*

This approach also seeks to define a clear exit strategy before the project will end, how to address gaps in the supportive infrastructure, and how to build and strengthen human and institutional capacities.

Tijara mainstreams management best practices through the following mechanisms and actions:

- *Regular update with MFI best practices:* Tijara staff regularly updates knowledge on management best practices through attendance at international conferences and trainings in microfinance. Tijara's sustainable microfinance program works closely with other components of the USAID program (e.g., EG II) and other stakeholders (e.g. CGAP, Microfinance networks in the MENA region SANABEL, SEEP).
- *Addressing best practices at the quarterly MFIs conferences:* Management best practices are discussed during the MFI quarterly conference organized by Tijara. Based on our interviews with Tijara staff and minutes of the conference, many topics related to bottlenecks and practical issues related to the application of management best practices were raised and discussed by participants. These conferences are excellent forums that enable MFIs to share management

² Interview with Tijara Microfinance Team Leader

experience at the operational level, and obtain useful recommendations to improve performance.

- *Analysis of management best practices from MFI operational assessments:* Tijara analyzed the best practices of MFIs during their operational assessments. Tijara found a series of deficiencies or weaknesses that impact MFI management practices, and hence credit operations. These findings and our reviews are summarized in Annex F of this report.

Issues are identified and recommendations are provided to MFIs based upon these operational assessments. Tijara follows-up on whether or not MFIs address these issues during site visits. Though Tijara is satisfactorily implementing the recommendations to establish benchmarks for the disbursement of grants, it appears that at least some MFIs do not have written plans with benchmarks on how to address the recommendations.

Recommendations

Once the MFI agrees on recommendations in the operational assessment, Tijara should work with them to define planned activities and timelines to address major deficiencies with timing, inputs, responsibilities, and resources required (e.g., Technical assistance (TA), capacity development, materials/software). The MFI board and management should review such plans on a regular basis to ensure compliance. TA packages with follow-up by Tijara should be linked to an exit plan.

Interviews of MFIs in Iraq on Management Best Practices

Four MFIs were interviewed. Tijara had assessed two of them through operational assessment exercises: Al Aman (August 2008, and March 2009) and TEDC (October 2008). The two others were BFF and Al Tadamun (TDMN). BFF is not required to report to Tijara since it has not yet received a Tijara grant. BFF is currently benefiting from Tijara's training, technical assistance, participation in the quarterly conference, and plans to apply for a Tijara grant. The main objective of interviews was to validate initial findings from the operational assessment desk review on MFI management best practices, and to identify other weaknesses in MFIs' management best practices.

Findings

From the rapid self assessment surveys, none of the MFIs raised major challenges with regard to management best practices. However, they did mention policies and procedures or reporting documents that they do not currently have or do not report on. These include: Board minutes of meetings, annual budget, staff capacity, human resource development plan, information systems, marketing strategy, and audited financial reports.

In general, the MFIs are aware of management best practices, and specifically the document on management best practices produced by the previous Izdihar project- except for BFF. However, staff from MFIs indicated that the document was not translated into Arabic and, as a result, they were not entirely familiar with its contents.

The Boards of all four MFIs are functional and appear to be proactive in addressing important issues raised and finding solutions. Executive Managers employ management best practices picked up as a result of their experienced backgrounds, trainings, and access to current information on management best practices.

Local traditions, religious factors, socio-cultural factors, and the security situation- as well as the lack of a legal and regulatory framework governing the MFI industry -- all have a marked influence on how international management best practices for MFIs can be applied in Iraq. Management best practices tools and materials are so generic as to be easily dismissed by MFIs. Targeted capacity building for MFI Board and Management appears to be insufficient.

Although all of the MFI staff said that they are addressing the lack of, or the unsuitability of ,the existing internal controls vis-à-vis the best practices, this function appears not to be a priority for them -- although some interviewees raised the difficulty of finding the person with the right skills for the position.

For their future growth, all MFI staff cited clearly their critical needs in staff and institutional capacity building and stressed the importance of Tijara technical assistance. In remarks they included weaknesses in strategizing, operational management, risk management, accounting, and delinquency management. BFF and Al Aman have started to address capacity building on their own, through in-house training provided by their own experienced staff as trainers.

From the interviews with the MFIs in Erbil, each MFI encounters different issues related to Shariah-compliant loan products. These differences are reflected in interview responses (See Box 1).

Box 1. Shariah-Compliant Loan Products.

Al Aman: “International MFI best practices is not compliant with Shariah law”

Though Al Aman was successful in developing Shariah-compliant loan products with fees charged to facilitate its operational and financial sustainability, Al Aman stated that the need to abide with Islamic law for lending remains a key challenge related to MFI best practices.

BFF: “We let our clients go by themselves to get approval in getting loans from their local religious leaders, we cannot help them”

Since BFF clients do not have a particular religious leader, approval to get loans is left to the potential clients and takes greater effort and time to engage with their local religious leaders (Imams or Sheiks) in order to institute support in their communities. This could become a constraint for BFF to meet its increasing demand of microfinance services.

Al Tadamun: “One of our Board members, who is an advisor to the Prime Minister, does our marketing; he is exploring market opportunities in three areas around the Mosul Office”.

There is a lack of marketing strategy for the MFIs. Al Tadamun (TDMN) mentioned that the big challenge is to develop the Islamic loans in these very conservative areas.

Except BFF, which still uses software developed by CHF, the three MFIs interviewed are using the LPF. Their MIS is not connected to their branches and they found this to be a big constraint in enabling them to address issues related to distance and security, and to better increase their performance.

Most loan officers reported that they often come across “illusion projects.” Loan officers take the time necessary to identify such projects, and this leads to a delay in loan processing that was identified during the operational assessments.

Recommendations

Though some strengths are cited above, a number of key constraints that may adversely affect MFI management best practices also have been identified. These interviews helped in better understanding issues identified through the desk review of the operational assessments (See Annex G) and in refining our recommendations:

- The development of a specialized training that is custom-designed to the realities in Iraq for MFI Board and Management is recommended. It should focus on management best practices essentials and should use direct and accessible language. Further, the trainings should be applied through an ongoing process of coaching and consultancy services provided to each MFI.
- Using the MFI operational assessments to establish benchmarks for the disbursement of grants in relation to implementation of the recommendations is very valuable. However, we also recommend that MFIs produce a clear planned approach and written, time-bound activities addressing each of the weaknesses identified during the assessment.
- Internal control is a matter of duty and credibility; it is critical to establish a culture of control and the accompanying tools or systems within MFIs. Sound financial management and control enhances MFI abilities to serve clients, ensure timely disbursements, and attract additional funds from microfinance funders.
- In light of the complexity of the situation in Iraq (insecurity and socio-cultural factors), a rigorous marketing strategy may not be needed for Iraqi MFIs. MFIs should invest more efforts in developing new products and improving service delivery through a continuous process based on regular feedback from clients and staff. An example of how this might work is provided by Al Aman, which has been successful in working with local government, religious and community leaders in order to design various types of loans that meet the needs of the poor and women.
- Tijara and MFIs should proactively use the SANABEL network to acquire international experience and best practices on Shariah-compliant loan products.
- MFIs need to put in place clear guidance, criteria and tools to help loan officers identify and reject bad and illusion projects early.

CONCLUSIONS

Significant growth in microfinance has been achieved in Iraq through USAID programs Izdihar and Tijara since their inception in 2003. Indicators of outreach and operational self sufficiency evidence these notable achievements, and there is no doubt of positive results of microfinance access for Iraqi entrepreneurs.

This assessment highlights some challenging aspects related to the ongoing and progressive development of MFIs in Iraq in connection to portfolio and financial reporting and microfinance management best practices. Overall, they are related to flaws in existing systems, policies and procedures -- and their effective application. Management information systems for ensuring data quality are inadequate and should be clearly structured into MFIs and linked to monitoring, evaluation and reporting. Internal control is often weak or lacking, and since managing risks is an essential function of MFIs, it is important to establish a culture of control -- and invest in accompanying resources and tools accordingly.

Specifically, human resource capacity, especially for Board Members, Operation Managers, and Loan Officers, is very important and critical. Strengthening capacity will contribute to more efficient operational and financial systems, and improved policies and procedures in order to better serve clients, report more accurately, and make informed management decisions.

At current growth rates, the MFIs will find it increasingly difficult to manage performance unless an internalized and targeted approach to these issues is adopted. The issues and recommendations highlighted in this paper will serve to improve MFIs effectiveness, strengthen their institutional sustainability, and increase their outreach.

ANNEX A: Scope of Work

USAID/Iraq Tijara Provincial Economic Growth Project Validation of Project Reporting (October 12, 2009)

I. Objective of the Study

The purpose of this scope of work (SOW) is to validate reports received by the Economic Governance and Agriculture Office (EGA) on the status of Microfinance Institutions (MFI) funded under the Tijara program. The EGA seeks to draw a picture of the local MFIs in terms of operations and functioning as well as to provide an independent verification of the reports that it has been receiving. The assessment has two phases. The first phase is an assessment/validation of Tijara's monthly report to EGA on MFI in Iraq and examines documentation at the project implementation level. The second phase focuses on microfinance loan beneficiaries and is a confirmation that project beneficiaries for each of the local MFI did receive and utilize loans that were received from local MFI grant recipients. Implementation of the second phase of this assessment is conditional on findings of the first phase assessment.

Specifically the objective of this assessment is to:

- Review and validate Tijara's supporting documentation for the monthly MFI reports.
- Assess Tijara's monitoring and evaluation practice with respect to the MFI program.
- Assess management best practices of the local MFI.
- Under phase two, confirm through direct interview with MFI loan officers the operations of the MFI.
- Under phase two, confirm loan beneficiaries through direct interview.

II. Background

Overall, the objective of the Tijara - PEG activity is to grow the Iraqi economy by promoting private sector development by increasing access to finance. Under Component One, Tijara will provide business development services by providing targeted BDS primarily through the Small Business Development Centers (SBDCs) and other local organizations identified by the project. In addition, Tijara will continue to assist the Government of Iraq (GoI) in its efforts to join the World Trade Organization and standing up the National Investment Commission (NIC), which were begun during the Izdihar project. Under Component Two, Tijara will focus on expansion of commercial lending through microfinance institutions and banks by identifying and reducing market lending risks; providing training and technical assistance; disseminating information, education, knowledge management and research; and operating a grant facility. This SOW focused on the Microfinance element of Tijara's project Component Two.

The purpose of the Tijara Microfinance Component is to expand inclusive access to sustainable financial services provided by microfinance institutions and banks. A complementary objective promotes the development of an accessible, demand-driven market for high-quality capacity building services responsive to the differing needs of MFIs and their clients. Tijara provides training and technical assistance to the MFIs. The Microfinance Component began a dialogue with the Central Bank of Iraq (CBI) and other GoI authorities, to harmonize and integrate NGO MFIs into Iraq's formal financial system. While Iraq has a long history of informal finance such as family- or village-based rotating savings and credit societies, best-practice microfinance began emerging as an industry only in 2003 under the Coalition Provisional Authority.

Growth in outreach to clients over the past six years was as high as 78% per annum through December 2007. From December 2007 through January 2009 growth declined to a still impressive 64%. The decline is attributable to the stage of growth of the MFI industry, lack of MFI capital, limited institutional capacity and a lack of enabling legislation to support the industry.

Some major accomplishments through August 2009:

- Eleven emerging microfinance institutions, nine of which are indigenous, collectively with an outreach to over 51,318 clients (15% of which are women), and an outstanding loan portfolio of \$77.3 million.
- Cumulative loan disbursements of \$344 million to over 149,334 clients.
- All MFIs are at or nearing operational self-sufficiency.
- Five operational assessments completed for two international and three Iraqi MFIs.
- A Performance Classification Monitoring System was initiated to track the evolution of the MFIs as of December 2007.
- Financial systems were verified and structured to improve data quality.

This assessment is intended underwrite the veracity of these figures and statements, the processes used to confirm performance and to validate the loan beneficiaries.

III. Methodology

Phase One:

- Document review of Tijara MFI reports to EGA
- Document review of materials received by Tijara that support the monthly reports prepared for EGA.
- Document review of Tijara M&E plans, methods and reports.
- Key informant interviews with Tijara COP, M&E staff, microfinance staff (and others responsible for the monthly report).
- Key informant interviews with 3 International MFI management staff to understand and walk through reporting systems and M&E.

Phase Two:

- Key informant interviews with 9 local MFI management staff.
- Key informant interviews with MFI loan officers from each of the nine local MFI.
- Develop, pretest and pilot test a survey instrument suitable for interviewing loan recipients.
- For each local MFI, implement a random survey of recent loan recipients (fulfillment less than one year ago).

IV. Existing Sources of Information

EGA will make available all relevant program documents to enable the MEPP II team to conduct the assessment. Of specific interest are the monthly MFI reports, RIG reports on Tijara, special studies, and MFI guidelines that EGA wishes Tijara to follow. EGA will facilitate, through Louis Berger (the Tijara implementing partner), the provision of contact information for key informant interviewees, including local MFI management, loan beneficiaries and other relevant stakeholders.

Specific reference materials to be provided are:

1. Latest Tijara PMP.
2. Contract modification 2 and/or any later modifications.
3. Tijara Year 2 Workplan
4. MFI monthly reports.
5. Iraq Microfinance Industry Performance Reports (latest).
6. Database of loan recipients from which random samples of loan beneficiaries can be drawn for each of the local MFI

V. Team Composition

MEPP II is to conduct this DQA using existing in-country M&E specialists. However, in collaboration with MEPP II, EGA will determine whether external experts in microfinance are needed to complete this assessment.

VII. Schedule and Logistics

Task	Notional Duration³
Phase one document review	1 week
Phase one key informant interviews.	1 week
Develop preliminary findings under phase one and provide briefing to EGA	1 weeks
Phase two key informant interviews	2 weeks
Phase two survey of loan recipients	4 weeks
Draft report	1 week
Receive USAID comments and integrate them into final report	2 weeks
Total Time	10 - 12 weeks

³ Some tasks run concurrently.

VIII. Reports

The MEPP II team will be expected to provide a briefing to USAID no later than November 5, 2009 for Phase one findings. A briefing on Phase two, should it proceed, will occur no later than 30 November. A draft final report on findings and recommendations shall be provided no later than December 10, 2009. The study report will be the following format:

1. One page summary of report findings and recommendations
2. Executive summary not to exceed more than five pages.
3. Main body of the report findings and recommendations not to exceed 20 pages.
4. Relevant annexes or appendices may be unlimited.
5. Report will be formatted in accordance with USAID publication, "Constructing an Evaluation Report," dated April 14, 2006.

The final report will be provided to USAID no later than seven working days after receipt of USAID's comments on the draft report. It is anticipated that USAID review will require up to two weeks with comments to be returned to the team for final editing of the report. The final report will include, as an appendix, USAID's response to the report recommendations.

ANNEX B: Methodology

Assessment of the Microfinance program reporting and Lending Institution's operations (Tijara)

PHASE I

Phase I will respond to three questions: The main objective of Phase I is to assess the M&E system of Tijara in terms of quality of data and reporting to USAID and MFIs best practices.

Q1: Is the monitoring and evaluation of the microfinance component done/implemented appropriately and integrated within the *existing* Tijara M&E systems (PMP)?

Methodology:

- Desk review of the latest Tijara PMP, Performance Data Table, Tijara Monthly report
- Interview with Tijara M&E Director on Tijara M&E systems
- Review of Tijara's M&E policies, procedures and systems and how they implement it.
- Analysis of the M&E systems as related to Tijara "Sustainable Microfinance" program

Key Interview Questions:

- What resources, procedures and systems are Tijara using for managing and reporting to USAID?
- Describe your M&E process? Are there methods incorporated into the system to allow TIJARA to triangulate information?

Q2: Are the monthly reports submitted by Tijara to USAID/EGA valid, i.e. document-based, reliable, and consistent over time?

Methodology:

- Desk review of the latest monthly report (August and September 2009)
- Interview with Tijara staff who participates in the preparation of the monthly report.
- Analysis of the MFI reports submitted by MFIs to Tijara that are used to prepare the monthly reports; Tracing and analyzing the data to its primary source.
- Review of the policies, procedures and systems followed up by MFIs in the submission of the MFI monthly reporting.
- Review of the process within Tijara for the production of the monthly report.

Key Interview Questions:

What resources, procedures and systems are Tijara using for managing and reporting data to USAID?

How Tijara ensures that MFIs reports used for the preparation of the monthly reports are submitted on time, complete, and mistake free? -- Oversight, guidance and support to MFIs?

Is there quality control process/procedure related to the data processes and reporting at MFIs? At Tijara?

Data validity: (mainly data entry errors): How do you validate the data from MFIs? Do you have a system/mechanism in place to ensure the data/information submitted by MFIs to Tijara are valid? Is there documented evidence of the validity of any primary or secondary data reported? If so, what?

Data reliability: (stability/consistency of data collection process): Do you have a mechanism in place to ensure the data/information submitted by MFIs to Tijara are reliable? Is there documented evidence of the reliability of any primary or secondary data reported? If so, what?

Ask about the “consistency of data sources/process/reporting” over time.

Timeliness (currency and frequency): Is there evidence of management/operational planning in the form of a time schedule for data collection, data analysis and data reporting?

Q3: Do Tijara MFIs follow management best practices (MBP) in microfinance? How? What are the main challenges?

Methodology:

- Desk review of the methodology and questionnaire used by Tijara to conduct the MFI assessments
- Desk review of the seven MFI assessments carried out by Tijara (*Tijara MFI MBP will be drawn mainly from the questionnaire and the assessments*)
- Interview with Tijara Microfinance Team Leader on Tijara MBP.
- Compare Tijara management best practices with literature; determine best practices followed; assess challenges/weaknesses.
- **Interview with MFIs staff in Erbil on MBP.**

PHASE II

Phase II has been refocused on the verification of loan figures (number of loans and amount) from the physical files of loan recipients stored at the MFIs.

The main objective of Phase II is to see whether the loan figures as reflected in the loan physical files at the MFI match to the figures reported by Tijara to USAID/EGA USAID in the “Monthly Outreach and Performance” reports.

Methodology:

- Two MFIs were subject to this data verification: Al Bashaer and Al Mosaned: Al Bashaer for August 2009 and Al Mosaned for September 2009.
- Figures obtain from the field verification are compared to the figures reported by Tijara to USAID in the “Monthly Outreach and Performance” reports.

ANNEX B (cont.) Methodology

Methodology used for the MFI Interviews on Management Best Practices

The following methodology was used during the Interviews of the four MFIs on management best practices in Erbil at Tijara Office (Ainkawa) on November 3-5, 2009.

1. The use of a rapid self-assessment worksheet on the presence of key documents (policies, rules, systems and/or procedures, and MFI reporting) in key areas of management best practices and, on their current key challenges.
2. Interview of the MFIs staff that included mainly Executive Managers or Operations manager and Loan officers. For BFF, it included the Chief Accountant.

The main objective of the interviews is to valid our initial findings from the desk review on MFI management best practices, and, to identify other MFIs' weaknesses/strengths in management best practices.

GENERAL QUESTIONS:

How familiar are you with the "MFI management Best Practices" document produced by Izdihar/Tijara? How useful is it in your governance/management of your MFI?

For the two MFIs assessed (Al Aman, TEDC): In what ways the operational assessments have helped you to improve your management practices? Please explain how you have implemented the recommendations.

SPECIFIC QUESTIONS:

A- Board/Management

What are your main challenges in managing your MFIs?

- How do you communicate/interact with the Board to address those challenges?
- What oversight and accountability does the Board provide? Is it adequate? If not, why?
- How often the Board meets? Does the Board review and approve all major strategic and operational decisions and policies? How are they implemented?

B- Interaction/Dynamism of MFI with its stakeholders

- Describe your recent interaction with **government/local government**: frequency, purpose, accomplishments, and problems.
- Describe your recent interaction with **other stakeholders (banks, religious leaders, etc)**: frequency, purpose, accomplishments, and problems.
- Describe your recent interaction with other **MFIS, national & international networks**: accomplishments, issues.

C- Strategy: Who was/is engaged in strategic and annual operational planning, and how?

D- HR/Staff capacity: Are the roles and responsibilities of each staff clear? (clear job description/

Benefits/Attribution of incentives: In what ways does management support staff in their work?

To what degree is staff expertise valued versus their ability to be a team player?

Staff Capacity: Is staff training part of your business plan? Who initiates staff training and based on what criteria?

Loan Officers: What are your principal duties? What are your major challenges?

E. Products Marketing

Do you have a strategy for marketing? If not why, if yes please describe briefly.

-Describe how your MFI educates and promotes its products and services to (potential) clients.

-Are new products and services currently in the process of being developed? If so, please describe.

-In what ways are office, equip and other facilities, adequate or inadequate for service delivery?

F. Management Information Systems (MIS)

Describe your monitoring and evaluation system. What are the main issues?

For the MIS, do you have policies, procedures to collect, store, and report on portfolio data and financial ratios/indicators? Please describe.

-Is information from the MIS systems regularly backed-up? Timely? User-friendly? And useful?

-What happens when the MIS software breaks down? Is this happening in practice?

-Is your financial/portfolio information available by branch, product and loan officer? How do you ensure of their accurateness? Up-to-date?

-Is this information used for timely assessments of loans, loan officers and branches? When and How?

G- Operational Risks

What are your MFI's major operational risks? How are you managing these?

-Are your Financial/ accounting system with standard procedures and controls?

- What cash management and portfolio quality controls are in place?

-What types of systems/processes do you have in place to prevent organizational abuses?

-Do you have specific procedures exist to detect and prevent fraud?

Who is responsible for determining, monitoring, and revising budget allocations?

-How is budget control being carried out?

Who is your internal auditor/ controller? And to whom does this person report?

-How often is internal audit of branch offices conducted? Is this announced in advance?

-What are the typical procedures conducted during a branch audit?

ANNEX C: Literature Reviewed

Publication Year: 2009

- Tijara 2009 Annual Workplan, Year 2.
- Outreach and Collection Performance Report, August and September 2009, Tijara/USAID-Iraq.
- Reports from Iraqi MFI Quarterly meeting: March 2009 & July 2009.
- Grant Agreement with Iraqi Al Aman Center (March 15, 2009); Amendment (October 6, 2009).
- The Iraq Microfinance Industry Performance Report: Performance Classification & Monitoring System (PCMS), Tijara/USAID-Iraq.
- Al-Aman Microfinance Institution Operational Assessment, Tijara/USAID-Iraq.
- Al-Basher Assessment, Tijara/USAID-Iraq.
- Al Takadum Assessment, Tijara/USAID-Iraq.

Publication Year: 2008

- Al-Aman Assessment, Tijara/USAID-Iraq.
- TEDC Assessment Report, Tijara/USAID-Iraq.
- Performance Monitoring Plan: April 2008-March 2011, Tijara/USAID-Iraq.

Publication Year: 2007

The Iraq Microfinance Strategy, IZDIHAR/USAID.

MFIs Manuals, Policies Procedures

- Credit Policies and Procedures Manual (Standard manual) –undated.
- Organization Policies and Procedures Manual for Iraqi Microfinance Institutions, --undated.
- Al-Bashaer Accounting Manual, August 2008.

ANNEX D: Illustrative M&E Field Evaluation Mission Schedule

8 – 10 Aug. 2009

Conducted a site visit to CHF branches in Najaf in order to introduce topics related to group lending, supervisor interviews, loan officer monitoring, and field visits to borrowers. This visit also served to introduce the MFI to the local SBDC to build linkages between business training programs and access to finance.

12 Aug. 2009

Conducted a site visit to the Al Mosaned MFI in Tikrit to track progress made toward implementing the recommendations of a previous assessment. This monitoring exercise was based on loan officer and client interviews and a review of the borrower filing and reporting system.

16 – 19 Aug. 2009

Conducted a site visit to the Al Thiqa MFI branch in Kirkuk to track the new group lending product, in its implementation and reporting. Reviewed client files and reporting systems for accuracy, conducted loans officer and supervisor interviews, and site visits to the fledgling groups in the field. Coordinated a meeting between the directors of Al Thiqa and the Kirkuk SBDC executive director to develop a training-to-lending pipeline.

5 – 9 Sep. 2009

Site visit to Relief International in Karbala and Najaf to track the ongoing group lending activities. The monitoring activities consisted of a review of client files and reporting systems for accuracy, loan officer and supervisor interviews, and site visits to the new and established groups of clients in the field.

13 – 14 Oct. 2009

Site visit to CHF and RI branches in Najaf to further develop new linkages between the MFIs and the Najaf SBDC.

ANNEX E: Deficiencies or Weaknesses in Management Best Practices

Deficiencies or Weaknesses	MFIs	Comments/Conclusions
Loan officers:		
Unclear responsibility, recovery practices, lack of incentives	Al Bashaer	Policies procedures are lacking or not followed. There are also issues of capacity of loan officers to know well and carry out their duties and/or the management capacity to track loan officers' duties and responsibilities. They should be addressed clearly through a clear plan. The quality of the loan officer's interventions is essential. They should have both professional competence and be familiar with local context.
Absence of Tracking repayments	Al Bashaer	
Loan filing flaws	TEDC	
Some loans provided w/ no fees or interests	TEDC	
Client site visits not done for loans less than \$1500	Al Aman	
Long loan processing time	TEDC	
Loan officer/Accountant workloads	TEDC	
Issues on Loan repayments through banks	Al Aman	
Lack of procedures in delinquency	Al Aman	
Loan officer not familiar w/ key ratio/indicators	Al Aman	
Governance and Management:		
Irregular board meetings	Al Bashaer	There is evidence of critical governance issues. Good governance includes a sound governing structure; free from political interference, adapted to local context, competent and stable staff. Board and management do not function effectively because they are not familiar or unclear on their respective Roles and Responsibilities (R&Rs), or Board meets on irregular basis. By-laws, R&Rs, policies and procedures should be clarified and documented and followed appropriately. Weaknesses of experience or know-how in such key areas as credit operations and financial management should be addressed.
Organizational issues related to HR, FM and staff responsibilities	Al Bashaer	
Absence of Board and Staff knowledge and familiarity of manuals and their application	Al Bashaer	
Board composition and Transparency issues	TEDC	
Procedures in credit approval not followed (circulation of loan documents for signing instead of consensus meeting)	Al Aman	
Management lack of capacity to track loan officers' performance	Al Takadum	
Lack of familiarity w/ MFI vision, plan, mission by staff	Al Aman	
Mayors as Board members, COI?	Al Takadum	
Tijara Deputy as Board member	Al Takadum	
Filing/Back up		
HR filing flaws/ Unlicensed Software & Un update antivirus	TEDC	Who is in charge of filing and back-up is held to a high degree of responsibility and requires timely actions to secure MFIs' critical data and information, and to accommodate audit and controls. Policies and procedures on filing and back up, and software should be applied or created if lacking.
Absence of back-up files (electronic or physical)	TEDC, AL Aman,	
Inconsistent and often incomplete trail of auditable docs for loan repayments	TEDC	

Deficiencies or Weaknesses in Management Best Practices (cont.)

Deficiencies or Weaknesses	MFIs	Comments/Conclusions
Internal Control/Audit		Internal audit, internal control, and managing risks are essential functions in the MFIs assessed, but this is a key area of weakness. Internal controls are often insufficient, with a lack of procedures and systems. In best practice, internal auditing should be independent and objective. Tijara should proactively help MFIs to strengthen internal control systems and create an internal audit function with a clear TOR to ensure and monitor the appropriateness and effectiveness of internal control systems.
Audit function to be created	Al Aman	
Branch manager=internal auditor in Fallujah Internal auditor: no capacity in the two other branches: Tijara deputy does it	Al Takadum	
Remoteness: less verification	Al Takadum	

ANNEX F : Schedule of Meetings and Field Visits

Date	Events
October 8	Meeting between USAID MEPP A/COTR Howard Johnson and USAID/EGA COTR for Tijara, Anar Khalilov and IBTCI staff (Harvey Herr, Fidele Rabemananjara, Mary Harvey and John Roscoe to discuss the objective of the assessment.
October 12	SOW finalized and approved by USAID/EGA and works began.
October 15	Start-up meeting with Tijara staff to present the assessment objectives with the presence of Mark Wease, Deputy COP; Tim Shumaker, M&E Director; all microfinance staff: Muhammad Junaid, Microfinance Team leader; Ala'a Frangoul, Sr. Program Manager & Deputy Microfinance Director; C. Ross Roulet, Senior Microfinance Advisor; Muhammad Ali Yazdani, Capacity Building Expert; Shoghair Yerchanig, Senior Finance Specialist; and Qaisar Nadeem, Senior Grant Manager;
October 19 & 22	Key Informant Interviews with Tijara Microfinance staff and M&E staff (Fidele Rabemananjara and Mary Hayden).
November 3-5	Field visits by Fidele Rabemananjara and Mary Hayden in Erbil at Tijara Office in Ainkawa: Interview with four MFIs on Management Best Practices: <ul style="list-style-type: none"> - Al Aman: Mr. Hussien A.Ibrahim, Executive Manager, Mr. Mohamd Othamn Hasan, Operations Manager, and Mr. Mohamd Taha Hasan, Senior Loan Officer. - TEDC: Mr. Bashar Ali Ridha, Executive Manager; Mr. Jihad Ali, Loan Officer Supervisor - Al Tathamun: Mr. Luay Muhyee Al-deen, Executive Manager; Mr. Fanner Maher Mahmoud, Loan Officer. - BFF: Mr. Nawzad Omar Mawlod, Assistant Manager; Mr. Salam Mohammed Abdul, Loan Officer Supervisor; Mr. Rahman Alla Dhia Sha'alan, Chief Accountant. <p>We also met: Mr. Bakhtiar Shwany, Regional Manager, Tijara USAID Provincial Economic Growth Program (PEG).</p>
November 9	Debriefing of Phase I to Anar Khalilov, USAID/EGA COTR, and Lee Briggs, USAID/PROG/MEPP-II COTR.
November 25	Follow-up meeting with Tijara staff for Phase II on data flow process and field verification with two MFIs: Al Bashair and Al Mosaned.
December 3	Meeting with Al Bashair (and Tijara) for the data verification to walk through the process of gathering the loan files and identifying the loan value.
December 5- 11	Field work by IBTCI through the accounting firm to conduct the data verification at Al Bashair in al Mansour/Baghdad and Al Mosaned, Kirkuk.
December 13	Final report submitted to USAID

ANNEX G : Loan data verification reports

Al Bashaer Audit report

Baghdad on 7/12/2009

No. 554

Messrs International Business & Technical consultants Inc (IBTCI)

Baghdad Iraq

Mr. M. Zubaidy

Subject :Al Bashair Iraqi Organization

Dear sirs

Re your email of 3/12/2009 , we have visited "Al Bashair – Iraqi Organization " , Located in Baghdad and conducted the required audit by you , concerning their disbursed of loans during the month of Aug.2009.

AS per your request we give here below the result of our audit which was limited to the under mentioned information :-

- No. of loans disbursed during the month of Aug.2009 was 452 (only four hundred & fifty two loans) .
- Total value of the 452 loans which was given during Aug.2009: \$ 753500.00 (USD\$ only seven hundred ,fifty three thousands and five hundred).

We enclose herewith a list of 12 pages showing all the details of the loans given by Al Bashiar Iraqi organization during the month of Aug.2009 signed & stamped by both our company & al Bashair Org for your reference .

We assure you our best attention and co- operation

Yours faithfully

Saad Sulaiman

Certified Public Accountant

Al Mosaned Audit Report

Baghdad on 10/12/2009

No. 559

**Messrs International Business & Technical consultants Inc (IBTCI)
Baghdad Iraq
Mr. M. Zubaidy**

Subject: Al Mosnad Organization at Salah Al Deen/ Tikreet,

Dear sirs

Re your email of 3/12/2009 , we have visited "Al Masanad – Organization " , Located at Salah Al Deen Tikreet and conducted the required audit by you , concerning their disbursed of loans during the month of Sept.2009.

AS per your request we give here below the result of our audit which was limited to the under mentioned information :-

- **No. of loans disbursed during the month of Sept.2009 was 67 (only sixty seven loans) .**
- **Total value of the 67 loans which was given during Sept.2009: \$114300 (USD\$ only one hundred ,fourteen thousands and three hundred).**

We enclose herewith a list of 2 pages showing all the details of the loans given by Al Mosnad Organization during the month of Sept.2009 stamped by them and signed & stamp by us for your reference .

We assure you our best attention and co- operation

Yours faithfully

**Saad Sulaiman
Certified Public Accountant**