MICROFINANCE INSTITUTIONS GROWTH ACTIVITY (MIGA) ACTIVITY DESIGN

FOR USAID/PERU

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ABBREVIATIONS

CAF	Corporación Andina de Fomento – Andean Development Corporation
COFIDE	Corporación de Desarrollo, S.A. - Financial Development Corporation
COPEME	Consorcio de Organizaciones privadas de Promoción de Desarrollo de la Pequeña y Micro Empresa - Private Consortium for the Promotion and Development of Microenterprises
COSUDE	Cooperación Suiza de Desarrollo – Swiss Development Cooperation
CU	Credit Union
DCA	Development Credit Authority
Edpyme	Small and Microenterprise Development Entity
FOGAPI	Guarantee Fund for Loans to Small Industry
FONDEMI	Microenterprise Development Fund
GOP	Government of Peru
GTZ	Agencia Alemana de Cooperación Técnica – Technical Cooperation German Agency
IDB	Inter American Development Bank
INEI	National Institute of Statistics and Information
LPG	Loan Portfolio Guarantee
MEDA	Mennonite Economic Development Association
MFI	Microfinance Institution
MIGA	Microfinance Institution Growth Activity
MOU	Memorandum of Understanding
MSED	Micro and Small Business Development
NGOs	Non Governmental Organizations
PEARLS	Protección, Estructura Financiera, Activos Improductivos, Rentabilidad, Liquidez, Señales Expansivas – Protection, Financial Structure, Unproductive Assets, Earnings, Liquidity, Indicators
PRISMA	Asociación Benéfica PRISMA
ROA	Return on Assets
ROI	Return on Investment
S&L	Savings and Loan
SBS	Superintendent of Banks and Insurance
SOW	Scope of Work
SO2	Strategic Objective Number 2
T.A.	Technical Assistance
USAID	United States Agency for International Development

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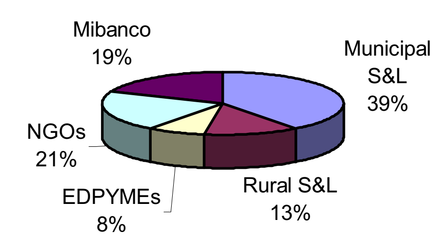
I. EXECUTIVE SUMMARY

Peru has more than 7.3 million microentrepreneurs and small farmers who are predominantly poor and largely excluded from access to formal sector services. Credit and other financial services have proved important in helping these people improve their standards of living. But after more than a decade of donor support to institutions providing microfinance services, there were still only approximately 240,000 micro credit clients in Peru at the end of September 2000. Micro credits are given primarily by Municipal Savings and Loans, Rural Savings and Loans, EDPYMEs (regulated institutions for micro financing), NGOs and Mibanco (Figure 1). The purpose of USAID/Peru's Microfinance Growth Activity (MIGA) is to significantly expand and diversify the provision of financial services by building sustainable institutions operating within a facilitative policy and regulatory environment.

The policy and institutional environment for growth of the micro finance sector is positive. First, numerous institutions are dedicated to delivering microfinance services through the application of best practices. Second, the legal and regulatory system has become increasingly conducive to growth of the sector, and the Government of Peru (GOP) has demonstrated a willingness to continue this trend. Finally, donors and other support institutions are expected to provide significant support to the sector over the coming years.

Figure 1. Share of microcredits, September 2000



The Microfinance Institutions Growth Activity (MIGA) will focus on strengthening high potential institutions, improving the policy and regulatory environment and providing capital support to microfinance institutions. Key to achieving the aggressive goals set for MIGA is leveraging USAID's limited resources for the microfinance sector by working with other donors and financial and support institutions inside and outside of Peru. Activity components include:

(1) Technical assistance and training to microfinance institutions. Based on assessments of the institutions' strengths and weaknesses (this Activity design is based on an analysis of 10 of Peru´s microfinance institutions), integrated programs of T.A. will help committed institutions to increase their scale, to expand geographically and to add important new services to their product mix, especially deposit services. While USAID will favor institutions providing loans under US$400 (currently mostly NGOs) to the poorest Peruvians, selected assistance will also be provided to other types of institutions, including EDPYMEs and municipal S&Ls. T.A. and training will be implemented under an expanded Cooperative Agreement with the local institution COPEME, supported by a long-term contract for high quality international assistance under the SEGIR IQC.

(2) Financial sector support, specifically to improve the policy and regulatory environment. This component will feature technical support to the SBS to develop norms, regulations and examination capabilities to effectively supervise microfinance programs. It will address key constraints to development of the sector, including the privatization of the Municipal S&Ls. USAID will actively promote coordination and dialogue among key elements of the GOP and among other donors in implementing this activity. The SEGIR IQC will provide most of the technical support under this component.

(3) Capital support to microfinance institutions. This component will utilize modest USAID resources to leverage private commercial and other donor financing for critical, timely equity and credit support to microfinance institutions. The equity bases of these institutions will be increased thereby enabling them to obtain licenses from the SBS and to attract increased formal financial market funding. The participation of new investors experienced in financial management will be encouraged to strengthen the institutions' governance structures. The program will involve both grants and loan guarantee facilities, and will also pursue the creation of a local second story credit facility that pools the resources of multiple donors.

Total planned USAID funding for MIGA is almost $10 million. Of this amount, more than half will be provided for the Technical Assistance and Training component. Approximately $US 1.8 million will be budgeted for the Capital Support component, and another $US 1.2 million for Financial Sector Support.

The five year MIGA Activity comprises part of USAID/Peru's Strategic Objective 2 "Increased Economic Opportunities for the Poor in Selected Economic Corridors," and will lead directly to Intermediate Result 2.2 "Increased Availability of Microfinance Services." The indicator targets for IR2.2 are:

- Number of microfinance clients served increased by 300 percent,
- Number of poverty loans (<$400) increased by 300 percent, and
- Number of micro savers increased by 100,000.

Each of the indicators listed above will be gender disaggregated as a function of percentages. USAID will strongly encourage microfinance institutions to apply best practices, and will emphasize strengthened operations and financial management. Institutions that can demonstrate improvements in lowering operating costs, increasing sustainability, diversifying services and in maintaining low delinquency rates will be the focus of USAID support. Where feasible, USAID will condition assistance on the incremental improvements of these indicators.

MIGA will be obligated under a bilateral agreement. Management of the Activity will be the responsibility of the SO2 Team Leader, the Microfinance Specialist and the Activity Manager. The Team will participate actively in policy and technical areas affecting the sector, and will assume a leadership role in coordinating with the GOP and other donors.

II. STATEMENT OF PROBLEM AND ACTIVITY RATIONALE

The SO2 strategy focuses on the large segment of the population classified as “poor,” as measured by such indicators as the lack of availability of sufficient resources to meet basic food and other living requirements. In 2000, it was estimated that more than one of every two Peruvians was classified poor. The current trend of low domestic and international investment is likely to continue over the next several years, resulting in dim prospects for substantial new formal sector job creation.

According to INEI (National Institute of Statistics and Information), in 1999 there were approximately 7.3 million economically active people engaged in microenterprises and small farming. (USAID/Peru defines microenterprises as those businesses with 10 or few employees. This is an important distinction, as other institutions, including commercial banks and even some Government entities, define microenterprise by a business´ assets or by the size of its loan.) These people and their family members comprise the majority of Peru’s poor. The poor generally do not have access to the benefits and services that can lead to improved standards of living. One of the most important of these is financial services. Without access to reasonably priced credit, most microenterprises are unable to acquire the working capital or investments required to expand and to increase sales. Without deposit services, the poor cannot properly manage their meager and uneven flow of earnings, neither can they be sure of the security of their savings. And without access to other financial services such as transfers, leasing and insurance, many people are excluded from important opportunities to increase their incomes and to reduce their risks.

Financial services have proven to facilitate the welfare development of the poor in Peru and throughout the world. For more than 10 years USAID and other institutions have supported the expansion of microfinance activities in Peru, although the most rapid expansion of the sector occurred during the past two or three years. As of December 2000 there were approximately 240,000 microcredit clients in Peru, excluding loans made by commercial banks to microenterprises, consumer credit by banks and pawn loans. Municipal Savings and Loans and Mibanco in urban areas and Rural Savings and Loans in rural and urban areas were serving most of these clients. The total loan portfolio stood at US$226 million, for an average outstanding loan balance of US$833 per client.

Table 1. Credit by microfinance institutions, Sept. 2000.

Institution	Number of loans	Loan Portfolio US$	Average Amount US$
Municipal S&L	107,583	102,368,421	952
Rural S&L	35,037	58,223,044	1,662
EDPYMEs	20,904	24,239,203	1,160
Mibanco	50,964	27,690,185	543
NGO (estimated)	56,559	13,338,812	236
Total	241,047	225,859,665	833
Bolivia with similar institutions, 2000	439,000	381,000,000	870

Only a small fraction of the poor, meanwhile, are being served in Peru’s rural areas and in particular the economic corridors emphasized in USAID’s Strategic Objective 2. USAID’s programs to support microfinance over the past five years were successful in providing initial support to institutions operating in some of these economic corridors, but weak management and limited capital have restricted the ability of these institutions to serve larger numbers of the poor. As of September 2000 all of the NGOs and EDPYMEs in Peru were serving about 72,000 clients.

In estimating Peru's potential microfinance market it is useful to study neighboring Bolivia, where nearly half a million poor clients now benefit from financial services. This represents about seven percent of the population. Although Peru's Per Capita Income is much higher than in Bolivia, the distribution of income is similar. In both countries the poorest 80 percent of the population earn approximately half of total income (World Bank, 1997). Assuming Peru's potential microfinance market also represents about seven percent of its population, the total potential number of clients is over 1.8 million.

Therefore, only about one sixth of Peru's potential market is currently being served. By strengthening Peru's microfinance institutions, including their ability to access increased capital, USAID can make significant progress towards providing this potential market with financial services.

Although Peru's economy is expected to grow at a reasonable pace (see Economic Analysis in Annex B) during the next five years, it will not be sufficient to provide jobs to the millions of its citizens who depend on self-employment and small farming. The causes of Peru's highly unequal income distribution (educational opportunities, access to infrastructure, lack of land titling, racism, to name some of the principal ones) cannot hope to be solved during this short period. Therefore, the number of Peruvians engaged in microenterprises will likely increase, and these people will require services to support the difficult, competitive environment in which they operate.

The potential for microfinance institutions to rapidly accelerate their ability to serve poor Peruvians is very promising. The economic and financial policy and regulatory structures are liberalized. The untapped market is large. There are a number of microfinance institutions with the potential to diversify and grow. And finally, the donor community is poised to provide additional support to this important sector.

The rationale for USAID's Microfinance Growth Activity (MIGA) is built primarily on the recognition that the sector's principal obstacle to growth is the lack of institutional capacity within the microfinance institutions. The most important obstacle is not loan portfolio financing, as there are numerous sources of funding available to capable institutions, including multi-lateral agency funds, Government of Peru funds, and commercial sources of funding. Although one should not diminish the importance of financing in the growth of the sector, institutional capacity is clearly a more fundamental pre-requisite.

USAID, with its strong field presence and deeper experience than other donors in the microfinance field, is ideally suited to accomplish the goal of institutional strengthening. From the perspective of resource leverage, USAID's greatest potential contribution is through increasing institutional capacity. By building strong institutions operating within a facilitative policy and regulatory environment, USAID will be able to optimize its contribution to the sector. By emphasizing well-placed technical assistance and training for microfinance institutions, we expect that USAID can contribute to a tripling of the number of microfinance clients over the next five years. Furthermore, by supporting the transition of microfinance institutions to full service financial intermediaries, we will have accomplished the significant mission of building a fully sustainable system. Once these microfinance institutions are able to capture public deposits and to access multiple financing sources, they will no longer require donor support. At that time, which may occur by the end of this Activity's five-year horizon, USAID will be able to claim success and our support will no longer be required for these institutions.

III. ACTIVITY GOAL AND PURPOSE

The Goal of the MIGA comprises part of the Mission's integrated strategy of Increased Economic Opportunities for the Poor in Selected Economic Corridors (SO2). The strategy is built on successes and experience gained during the second half of the 1990's, in which the Mission helped microfinance institutions extend credit to thousands of poor Peruvians. Through the Activity, USAID/Peru hopes to significantly reduce poverty by making vital financial services available to a wider population.

The purpose of the MIGA is to significantly expand and diversify the provision of microfinance services through a highly focused and intensified set of interventions. Fully sustainable and growing financial institutions operating within a facilitative policy and regulatory environment will provide these services. Services will be expanded in terms of the number of poor served, as well as geographically to serve many of the under-served and un-served areas of the country. Services will be diversified by making additional services available to help the poor manage their often-fragile financial lives, including the provision of savings, transfers, life insurance and other services.

IV. POLICY AND INSTITUTIONAL SETTING

A. Policy Environment

A variety of financial institutions, both regulated and non-regulated, are now serving small and microenterprise clients, including commercial banks, Municipal Savings and Loans, Rural Savings and Loans, Credit Unions, EDPYMEs and financial NGOs. A wide range of commercial enterprises, including small local stores, also provides financial services as part of other business activities.

The legal setting is microfinance-friendly. Microfinance institutions can be formed and make loans without license from the SBS. With about US$260,000 of equity an EDPYME can be formed, which is regulated by the SBS. An EDPYME can access funds from COFIDE, a government owned financing institution, and enjoys certain tax benefits as a regulated financial institution. With about $US1,400,000 of equity and a “B” rating from a recognized independent rating agency, an EDPYME is eligible to graduate to “Module 1” of the current Banking Law. This Module 1 status, which has yet to achieved by any EDPYME, allows the institution to mobilize public deposits. The existing legal system and currently required levels of equity are encouraging the formation of EDPYMEs. The SBS is supportive of development microfinance institutions, having licensed 12 EDPYMEs to date. Ten EDPYMES are actually operating.

COFIDE, which is majority owned by GOP, is a leader in financing for EDPYMEs, having financed seven of the 10. Given the newness and weaknesses of most of the EDPYMEs, financing seven of 10 is a relatively aggressive financing policy. COFIDE does express concerns about the performance of this portfolio.

In summary, Government policy has facilitated the development of formal microfinance institutions in Peru. Because of the current transition in government, past interventions by the government in delaying agricultural loan payments and the continuing economic recession, uncertainty exists within the industry. In particular there is concern that in the next few months government sponsored loan forgiveness programs may become a complicating issue for microfinance institutions, or that a government sponsored bank for the poor will be established. Even though these events could have major impacts on the industry, they do not now appear to be sufficiently imminent to be restricting development of the industry.

B. Institutions

B.1 Commercial Banks

Several commercial banks do a significant amount of lending to small and micro clients. Mibanco specializes in microfinance, while Solucion, a unit of Banco de Credito focusing on small enterprises, has added an impressive portfolio of microlending to its initial consumer-lending portfolio. Other banks make small loans, not as a directed policy, but as a byproduct of their many operations in the financial sector, such as Wiese Sudameris and Serbanco (Table 2). Commercial banks are expected to increase the number of small and micro loans over the coming years. Since commercial banks will not likely be the source of the microfinance sector's major expansion, they will probably not receive much USAID support under the MIGA. Nevertheless, those banks that focus on microfinance as part of their operations will be eligible for USAID support.

Table 2. Microloans in banks, May 2000.

Bank	Loan portfolio US$ million	No. of borrow -ers	Avg. loan US$
Wiese Sudameris	53.08	13,004	4,082
Mibanco	22.67	44,830	506
Solucion	18.24	22,101	825
Serbanco	5.33	3,701	1,441

From Owens and Tucker, Report on USAID/Peru Microfinance Strategy, August 2000, p.6. Data from SBS.

B.2 Municipal Savings and Loans

The system of fourteen Municipal Savings and Loans (Cajas Municipales) are owned by municipal governments. As a group they operate 79 offices in all regions of Peru. As of August 2000 their loan portfolio totaled US$151 million, and their deposits from clients totaled about US$88 million. Deposits during the year 2000 declined by 15 %, while the loan portfolio increased by 34 %. The two largest municipal S&Ls at Piura and Arequipa account for about half of deposits and loans of all 14.

These institutions often compete directly with EDPYMEs and NGOs for micro credit clients as well as for human resources. At the time of this writing, the SBS is reluctant to approve new applications for expansion of services by the municipal S&Ls until they are privatized. USAID shares this view, and strongly supports the privatization process. We believe that the stronger institutions with solid management, financial capabilities and good physical infrastructure, will become important contributors in microfinance markets as they achieve privatization. USAID will only work with privatized municipal S&Ls that commit to privatization and that show good prospects for financial sustainability.

B.3 Rural Savings and Loans

There are twelve Rural Savings and Loan (Cajas Rurales) institutions in Peru. Their equity is financed with private capital. These institutions are authorized to collect deposits from the public. About 100,000 people have deposits with the rural S&Ls, totaling about US$17 million as of August 2000. The loan portfolio in August 2000 was about US$56 million, with about 31,000 loans. The rural S&Ls operate 52 offices in Peru. Initially these institutions focused on serving agricultural production, but several now compete with microfinance institutions in the cities and towns. Because the rural S&L institutions are heavily influenced by political interests and funding, and because their owners are largely insolvent, this Activity will not likely provide support to these institutions. USAID will only work with these institutions should these limiting factors be corrected.

B.4 Credit Unions

Credit unions in Peru are closed in the sense that only members may borrow from and have savings accounts, and that they are associated with people at their work place or in their community. A recent USAID sponsored study reported the loans of the ten largest to be US$114 million in March 2000, and savings deposits of US$123. The Federation of Credit Unions, under the direction of the SBS, supervises these institutions. Few microfinance institutions mentioned Credit Unions as significant competitors. Credit Unions would require significant USAID resources in technical assistance and regulatory support. We believe the investment is not warranted because of their limited outreach, relatively weak administration and the lack of an active role by the SBS in supervising them. Furthermore, their lending tends to be for consumer credit, while the percentage of their loan portfolio to microenterprises and the poor is small.

B.5 EDPYMEs

The Government of Peru authorized EDPYMEs to be formed in 1996. Most were formed in 1997 and 1998 and most were formed from NGOs that previously were operating credit programs. By becoming an EDPYME the institution can access funds from COFIDE. Most of the EDPYMEs are small institutions, with less than US$2 million in loan portfolio. EYDIFICAR (which absorbed Confianza) is the largest with a loan portfolio of nearly $US10 million. Proempresa and Crear Tacna are the next largest. Both EDYFICAR and Proempresa hope to become authorized as a Module 1 EDPYMEs sometime in the year 2002 or 2003.

EDPYMEs will likely become the dominant type of organization providing micro loans, especially to residents of smaller towns and rural areas. As such, we expect them to receive considerable support from USAID under the MIGA Activity.

B.6 Non Governmental Organizations (NGO)

There are between 40 and 50 NGOs providing micro credits in Peru. SINFONED estimates that 28 of the principal NGOs provide micro loans to 57,000 borrowers, for a value of US$13 million. Many of these NGOs operate in the smaller towns and rural areas. Village banking is the dominant credit methodology among these institutions, though solidarity groups are also common. Few institutions administer individual loans.

Most of the NGOs are relatively weak organizations, still heavily depending on donor financing for their loan portfolio and to cover a portion of their operating costs. Only a few of the larger NGOs are expected to become EDPYMEs. The SBS does not view favorably the conversion of a large number of NGOs to EDPYMEs. Furthermore, if as an outcome of increased competition the microfinance market becomes saturated before these institutions reach a sustainable size, they will be under pressure to merge with other financial institutions or find other lines of business. In any case, USAID will focus its attention on the potentially sustainable NGOs.

B.7. COPEME – A Technical Assistance and Training Support Institution

COPEME, the Private Consortium for the Promotion and Development of Microenterprises, is Peru's principal source of non-financial assistance for microfinance institutions. COPEME´s microfinance support program is financed by USAID, while the IDB and the Ford Foundation provide assistance to COPEME in other areas. About 27 microfinance institutions, made up of NGOs and EDPYME´s, are members of the COPEME microfinance assistance program. Nonetheless, other financial institutions, including banks and S&Ls, are eligible to attend COPEME´s courses and even to receive other forms of assistance.

The microfinance training program implemented by COPEME has been particularly successful. Frequent well-attended courses are covering nearly all direct costs and attracting more and more participants. The technical assistance program is being implemented with several microfinance institutions. Nonetheless, this program is still modest in size and COPEME will require strengthening in order to more effectively implement its T.A. program. Finally, COPEME has developed an excellent body of financial data on each of its member institutions. This instrument, implemented under SINFONED, makes adjustments in financial data in order to objectively compare results from one institution to another. This information is valuable to microfinance institutions´ management, but is also a potentially powerful tool for donors and potential investors. COPEME is essence is developing a "rating" tool for participating institutions.

V. STRATEGIC APPROACH

The environment for microfinance expansion in Peru is positive. The MIGA Activity will build on existing components; focusing USAID resources on those components that most effectively employ the resources of USAID to encourage growth in the number of people served and improved financial strength of the service providers.

A. Principles Guiding the Activity

Implementation of the MIGA will be guided by six underlying principles:

1. Build on existing system of microfinance within a competitive context,
2. Require best practices by microfinance institutions serving poor microenterprises,
3. Focus USAID's limited resources on the activities that best achieve the measurement indicators,
4. Continue development of an effective and appropriate regulatory environment,
5. Support strengthened ownership/governance of microfinance institutions through privatization (of Municipal S&Ls) and by attracting new investors,
6. Leverage the impact of USAID resources by collaborating with other donors and Government of Peru.

A.1. Build on Existing System of Microfinance

The components for a successful microfinance industry are already in place, although in varying levels of development. Essential components are:

1. A legal system that allows formation of financial services companies and supports enforcement of loan contracts.
2. An economy of low inflation.
3. A regulatory and policy environment that permits institutions to receive varying levels of operating authority from the Superintendent of Banks and Insurance (SBS) as they improve their operations
4. More than three-dozen regulated institutions providing microfinance services to a wide variety of clients along with another three-dozen or more non-regulated financial institutions. These providers provide services in most regions of the country and have plans to provide services in all departments of Peru. There is no need for additional new institutions.
5. Donors and the Government of Peru provide funds for microfinance institutions, both for lending operations and for institutional development. Funds may be reimbursable or not reimbursable, with or without cost.

Currently there are more than 50 companies in Peru dedicated completely to microfinance, or that have major parts of their businesses dedicated to microfinance. There are a sufficient number of institutions that have several years of experience, want to expand the number of micro borrowers and savers, and show reasonably good performance that USAID can achieve the goals of this Activity without needing to encourage the development of new institutions.

Likewise, the policy and regulatory environment is capable of supporting the existing microfinance institutions. The efforts of this Activity will be to strengthen and improve the policy, regulatory and supervisory environment to enhance the number of micro entrepreneurs receiving financial services.

A partial system of funding is in place. Most institutions begin with donor funding. As they grow and improve their operations, they may apply to COFIDE, a government funding agency for regulated institutions. COFIDE can supply partial funding. Microfinance institutions still must find other sources of funds, usually the same donors that provided initial funding.

After demonstrating good performance over time, these institutions may accept public deposits to fund their finance activities. This activity will support a limited funding component that will help selected institutions speed the process to securing permanent funding sources.

A.2. Require Best Practices of Microfinance

USAID has been in the forefront of developing and applying best practices for microfinance around the world, and in Peru. Some of these best practices include: employment of proven credit methodologies, sound financial policies, effective management information systems and the utilization of employee performance incentives. Most of the important microfinance institutions receiving support from USAID through the Microfinance Initiative have accepted, in principle, the use of best practices, and are in varying stages of implementation. However, Activity managers must insist that future activity benefits are dependent on meeting these best practices as they can be applied in Peru.

A.3 Focus USAID's Limited Resources on Activities that Best Achieve Measurement Indicators

The needs are great; the resources few. Achieving the measurement indicators with the expected level of resources requires careful identification and selection of those activities that will most expand the number of microfinance customers, especially those receiving loans under $400 and those participating in micro savings.

Increased impact will occur through wise use of USAID resources to support technical assistance, training, regulatory and policy development and critical funds placements. Interaction with donors and those parts of the Peruvian Government with similar objectives is expected to provide multiple benefits, such as maintaining a beneficial policy environment, and helping other donors to provide funding for those areas receiving technical support.

USAID will focus its attention on supporting institutions to become self-sustaining. This will be accomplished only if microfinance institutions are serious about becoming full financial service intermediaries. It will be necessary to develop new products and services that will be mutually important to institutional sustainability as well as the financial well being of their clients. The most important of these services will be deposit mobilization. Other important services will include transfers or possibly leasing. Finally, microfinance institutions will have to review and revise their credit products in order to better meet the needs of their clients in a more competitive market.

USAID will also focus helping microfinance institutions to diversify their source of loan portfolio financing. In addition to savings, these institutions should look to other local and international sources, including commercial banks, new investors, bond emissions and other possible sources. This strategy has worked effectively in other countries. The Peruvian institutions must also take advantage of all possible financing resources. It will be for the benefit of their own institutions as well as the benefit of the country's development.

A.4. Continue Development of Effective Regulatory Environment

The Superintendent of Banks and Insurance (SBS) has developed regulations and procedures specific to the microfinance industry. But the implementation of these regulations is far from complete. The SBS still needs help in evaluating and addressing microfinance institutions. Among NGOs, EDPYMES, Municipal Savings and Loans, Rural Savings and Loans, Cooperatives and Banks all doing consumer and micro lending, the SBS has an enormous task to keep abreast of new developments in microfinance. This principle will support the good intentions of the SBS to encourage effective and sound institutions providing microfinance services in all regions of the country.

A.5. Support Strengthened Ownership/Governance of Microfinance Institutions through Privatization (of Municipal S&Ls) and by Attracting New Investors

Peru has experience in privatization of banks. But Peru's oldest and still largest providers of microfinance services, the Municipal Savings and Loans, are held in the hands of local government. A few of these are already considering privatization. If privatization is successful, significant additional equity capital will enter the industry, increasing the offer of micro loans, and especially savings products. This Activity will support those Municipal Savings and Loans that have decided to become privately owned, or owned by a mix of a majority of private investors and the municipalities.

Perhaps the most common model of EDPYME ownership is that the prior NGO owns a dominant proportion of the shares of the company, with the remainder held by a few individuals closely related to the NGO. Usually the NGO has limited additional resources to support expansion of the EDPYME. This Activity will support those well-managed EDPYMEs that want to benefit from wider ownership, and contribute best to the achievement of Activity indicators.

A.6. Collaborate with GOP and Other Donors

The sixth principle is to collaborate with the GOP, donors and other private institutions that support a sound approach to microfinance services. With its leadership around the world in establishing microfinance institutions and in supporting best practices that lead to solid and effective institutions offering services to the poor, USAID has an opportunity to influence how resources of the Government of Peru and other donors can be coordinated to enhance results above that which would occur without coordination. For example, the implementation of best practices in microfinance institutions within this Activity should encourage other donors to provide additional funding to reach more clients than would occur if donors function independently.

B. USAID's Capacity for Effective Implementation

Implementation of this Activity requires a strong mix of skills and activities within USAID. Microfinance is still a relatively new sector in Peru, and the country's experience and know-how in the area are limited. This is a highly integrated program, with USAID involvement ranging from the highest level of policy dialogue down to a strong technical understanding of financial management of microfinance institutions. It will be important that USAID staff participate actively at all these levels.

USAID will require the services of two full-time personnel closely involved in all areas of Activity implementation. To begin with, strong conceptual skills will be needed in understanding the policy, economic and social environment. In particular, the Government of Peru has in the past intervened in financial markets, forbidding financial institutions from collecting loans. Periodically there are statements by some desiring political office of the need to establish government owned financing mechanisms for the poor. These actions increase uncertainty and risk for the financial institutions, and often confusion for their clients. USAID staff will have to spend considerable time monitoring the political environment and providing timely and effective support for maintaining appropriate policies and regulations for the development of the microfinance industry.

USAID will also require its staff to evaluate the relative strength of Peru's microfinance institutions, and to determine the timely interventions that will be most useful to their continued development. The wide variety of potential institutions participating in the market, such as NGOs, Savings and Loans, EDPYME's and Banks will require advanced skills to assess the potential contributions of each and how each contributes to the measurement indicators.

In the technical area, skills are needed to observe in detail the activities and performance of specific institutions that are receiving support and determine if their development progress will meet program goals. Early detection of problems and decisions on adjustments keep the Activity on track, and assure compliance with the results indicators. It will require skill and experience to make these decisions in a timely manner before institutions sink too deeply into uncorrectable situations. USAID staff will work hand in hand with implementing institutions, particularly COPEME, in implementing the technical assistance component.

VI. ACTIVITY INTERVENTIONS

The Microfinance Growth Activity (MIGA) will consist of three integrated interventions: (1) technical assistance and training to microfinance institutions; (2) financial sector support to improve the policy and regulatory environment; and (3) capital support for microfinance institutions. Experience in the countries with more developed microfinance markets than Peru demonstrates that the most effective way of reaching increased clients is by building strong service delivery institutions operating in a facilitative policy and regulatory environment.

The main thrust of the MIGA will be directed at improving high potential microfinance institutions' capacity to expand and diversify the supply of financial services to microenterprises, with a particular emphasis on those institutions serving the poor with loans less than US$400. Limited activity resources will require that USAID focus its assistance on a relatively small number of institutions committed to growth and diversification.

Activity interventions will be demand driven. USAID will determine specific criteria by which institutions will be chosen to receive support and these institutions will compete openly for activity assistance. At the same time, USAID's staff and implementing institutions will be engaged in a continuous and substantive dialogue with the sector's microfinance service providers. In combination, these approaches will allow USAID to enter into support agreements with those institutions with the greatest potential to serve poor clients.

Throughout the discussion of activity interventions below, examples are given of the specific types of assistance planned. These examples are illustrative and not meant to be exhaustive.

A. Technical Assistance and Training

The provision of microfinance services in Peru is distributed among numerous institutions. Not counting the Municipal S&L's, the Rural S&L's and Mibanco, there are 28 EDPYME's and NGO's providing microfinance services that are registered under the COPEME-USAID Microfinance Initiative program. Of these 28 institutions, only four had greater than three thousand clients as of September 2000. None of the 28 institutions has been authorized by the SBS to mobilize deposits. Even the strongest of these institutions requires major improvements in a wide range of operational areas in order to become a fully sustainable entity.

The most important component of the MIGA activity will be the provision of intensive, integrated programs of customized technical assistance and training to the microfinance institutions. It is apparent that even some of the most advanced EDPYME's are still in the early stages of institutional development. As of the writing of this paper, some of these institutions are undergoing strategic planning exercises in which institutional strengths and weaknesses are being identified. The technical assistance and training needs of these institutions is comprehensive. The illustrative list below reflects needs expressed by leaders of the institutions themselves. Even the most advanced institutions will require support in most of the areas listed.

<u>For directors</u>:

- Strategic business planning and evaluation,
- Understanding financial and operating reports of financial institutions,
- Fiduciary and legal responsibilities in directing regulated financial institutions,
- Expected levels of revenues and costs for microfinance companies,
- How to access funding.

<u>For management</u>:

- Strategic planning, evaluation and follow-up,
- Market analysis,
    a. Data gathering and analysis methodologies.
    b. The economic and social environment,
    c. Strengths, Weaknesses, Opportunities, Threats,
    d. Competitor analysis,
    e. Product differentiation.
- Management skills and time management,
- Human resources management,
- Risk analysis and management,
- Financial and liquidity management,
- Preparing financial projections,
- New product development and implementation.

<u>For accountants, auditors and MIS workers</u>:

- Understanding financial reports,
- Chart of accounts and accounting standards of the SBS,
- Documentation standards for accounting records and for loans,
- Reporting requirements for management and for supervisory and regulatory agencies,
- Audit standards and techniques,
- Cost accounting,
- Pricing inter-office and inter-region internal transfers,
- Communications technology,
- Information systems administration,
- Information systems development, including needs assessment, specification writing, acquisition, installation and data transfer.

<u>For credit officers and supervisors</u>:

- Credit analysis,
- Loan administration and collections,

- Legal environment for loan administration,
- Financial calculations and mathematics for financial institutions,
- Human relations and loan portfolio management (group dynamics, recognizing and selecting compatible solidarity groups, motivating borrowers, recognizing willingness to pay, persuading borrowers to pay),
- Product marketing,
- Record keeping and documentation,
- Computer skills,
- Reporting requirements for financial system auditors and regulators,
- Management skills and time management,
- New product development and implementation.

For all employees:

- Operations of financial institutions (overview),
- Hazards of poor loan decisions and poor loan collections and their impact on the financial health of an institution,
- Service standards to customers,
- Regulation and supervision of financial institutions (overview).

USAID will place particular emphasis on providing technical assistance and training to those institutions committed to growth, to those committed to implementing best practices, and to those institutions receiving significant PL 480 Title II resources. Earnings by institutions receiving Title II resources will probably not be sufficient to purchase all the needed support including infrastructure improvements. External assistance will still be needed. None of the EDPYME's or NGOs will be able to grow in a healthy manner without significantly strengthening their operational capabilities.

USAID will strongly encourage institutions to position themselves as rapidly as possible into mobilizing public deposits, backing this encouragement with adequate doses of the highest quality technical assistance.

The incorporation of a cost-sharing program is planned for this component. This is important for several reasons, the most important being the value institutions will place on assistance that is paid for, at least in part. As a possible cost sharing approach, it may be proposed that institutions with initial average loan size of US$400 or less will be required to cover 25 % of the cost of the technical assistance. Institutions with initial average loan size of more than US$400 will be required to cover 50 % of the cost of the technical assistance.

No limits are set as to the amount of technical assistance that may be received by any one, or any one group, of institutions. The principal qualifying factor is to what extent does the technical assistance contribute to the accomplishment of the goals and indicators of the Activity.

There are several goals, however, that institutions must commit to in order to be eligible for subsidized technical assistance. Specifically they must meet the criteria set forth in Intermediate Result 2.2. These are:

1. Portfolio at risk for payments late by 30 days or more is below 5%,
2. Operating costs/gross loan portfolio reduced by 25%,
3. Financial sustainability increased by 25%,
4. For those institutions for which it applies, an effective micro savings program implemented.

All of the four criteria must be achieved within a reasonable time, approximately two years, after the technical assistance begins. Interim standards will be set which will govern future access to subsidized technical assistance via USAID funding. These standards will be fixed by semester and will be agreed upon by the benefiting institution, the institution supervising the technical assistance and USAID. The institution supervising the technical assistance will verify compliance.

B. Policy, Regulatory and Supervisory Support

B.1. Technical Support to the SBS

Over the past decade, Peru's SBS has proven to be a competent and effective regulatory and supervisory agency. It has forced the consolidation of the commercial banking sector and helped to prevent a crisis in the sector during the severe economic shocks of El Nino and the Asian crisis suffered in 1997 and 1998. The SBS has also been open to the growth of the microfinance sector and has recognized its own role in ensuring the health and stable growth of the sector. This institution's work will be crucial in strengthening and maintaining discipline and strong financial management in microfinance institutions. The SBS is an insurance policy that is well worth the price, and USAID should actively seek a strong, ongoing formal relationship with this institution.

The creation of the EDPYME regulatory module was an important action to recognize the role of microfinance institutions and to provide a framework under which these institutions could formalize their operations. To date, eight institutions have transformed into EDPYME's from NGO status and are making efforts to comply with SBS regulations and reporting requirements.

Unfortunately, the SBS does not have the technical or financial resources to adequately supervise the newly formed EDPYME's as it should. Until now it has had to sub-contract auditing firms to carry out examinations of EDPYME's, and this has not proved very effective. Although there is nothing inherently wrong with subcontracting this work, the SBS must first develop and strengthen its internal capacity to regulate and supervise microfinance institutions. It will require further technical assistance, especially at the international level, to accomplish this.

The EDPYME regulatory structure is in effect a training ground for microfinance institutions. Those EDPYME's wanting to expand and diversify services will have to graduate to Module 1 of the SBS's Modular Scheme of Operations outlined in Article 290 of the Banking Law. Most importantly, this will allow them to mobilize deposits from the public.

To date, no EDPYME has graduated to Module 1 status. The SBS will require technical assistance in assessing an institution's capacity to make this graduation and, more importantly, it will require assistance in supervising the new institutions' operations. Possible types of assistance to the SBS under the MIGA activity include:

- The development of norms that take into consideration the operational realities of microfinance institutions (e.g., lack of real guarantees, remote rural operations, high operating expenses),
- The development of methodologies to more effectively examine microfinance institutions and, in particular, to assess portfolio risk,
- Training of SBS and sub-contracted staff in carrying out effective examinations,
- Understanding internal control needs and methods in microfinance institutions,
- Technical assistance to evaluate the use of new technologies, and
- Technical assistance and training to reduce costs of supervising microfinance institutions.

B.2. Privatization of the Municipal Savings and Loans

The growth of Peru's Municipal S&L's has been uneven. Only two of these institutions, from Arequipa and Piura, have developed into strong institutions with solid management and significant assets. The municipal ownership structure of the S&L´s poses subjects the S&L's to political influence at a minimum, and outright corruption in worst cases. It is very difficult for S&Ls to increase their equity except through reinvesting profits. Finally, the SBS has made clear its position that the Municipal S&L's will not be permitted to expand geographically as long as they remain in the hands of the municipal governments. In conclusion, the benefit of these institutions has not and likely will not be maximized until they are privatized.

Fortunately, the recognition that Municipal S&Ls should be privatized is growing, even among some municipal governments. Top management from some of these institutions has been especially instrumental in pursuing privatization. Recently there have been diverse proposals with regard to the best strategy for S&L privatization. These include: (1) the privatization of individual S&Ls; (2) the merging of groups of S&Ls; and (3) the creation of one nationwide S&L by merging all of the S&Ls. Still, there are a number of political and legal hurdles that need to be overcome. Under the MIGA activity, USAID will support the privatization process with timely assistance. This assistance may take the form of consensus building among key players in the process, including with the Ministry of Economy, the SBS and the municipalities. Varied assistance instruments could be employed, including open and inclusive conferences and workshops, or direct assistance to critical institutions such as the Federation of Municipal S&Ls in developing a privatization strategy. It could also assist in identifying potential private investors, in performing due diligence and in developing the legal framework for privatization.

B.3. Support in other Policy Areas

Peru is in a period of significant political activity and uncertainty. Policies affecting the health of the microfinance institutions may be subject to change. During the coming electoral campaign it is almost certain that proposals will be made to establish government owned financial institutions to support the poor. Whether these proposals will prosper with the new government is unknown.

In addition, Peru has recently established policies that have important impacts on the health of financial institutions, as evidenced by the declaration that repayment schedules for agricultural loans must be renegotiated.

Therefore, this Activity will also address the development of appropriate policies and regulations for microfinance institutions. To reach the goals of this Activity, it will be critical to obtain the technical expertise needed to help the Government of Peru establish the best policies possible. USAID personnel will be substantively involved in coordinating with other donors to support policies and regulations that support microfinance best practices.

B.4. USAID-led Donor Coordination in Microfinance

Despite accelerated progress over the past several years, Peru's microfinance continues to mature slowly. There are a number of reasons for this, but the principal reason is because of institutional weaknesses of the service providers. There is certainly no lack of institutions – in fact, the proliferation of institutions is holding back the growth of the sector. Too many institutions pose the following disadvantages:

- Valuable technical assistance resources are used inefficiently on both high potential and low potential institutions,
- Financing for loan portfolio also spread inefficiently over both high potential and low potential institutions,
- The SBS and other GOP entities are burdened with supervising and overseeing too many institutions, and
- Donors spread their resources too thinly and inopportunely.

During the early stages of microfinance sector development, donors are the primary source of technical and financial resources. Peru is no exception, and this country's microfinance sector is still far from emerging from donor dependence. Currently, there is insufficient coordination among donors in the microfinance area. Such coordination will have significant benefits to the healthy development of the sector. More effective coordination among donors will lead to:

- Agreement on criteria for supporting microfinance institutions related to geographical focus, financial policies, and others,
- Pooling of financial resources to achieve leverage and efficiencies,
- Complementary use of technical assistance and other non-financial resources,
- Collaboration on specific initiatives, and

- Unified and strong positions before the GOP on important regulations, policies and other issues.

Effective, sustained coordination among donors is hard work. Normally, it requires the initiative and perseverance of two or three key individuals. Representation in effective donor coordination groups comes from individuals, not institutions. USAID, with its strong field presence and major participation in the microfinance area, will provide the early initiative of a donor coordination effort. The effort will begin by coordinating with a small group of most interested donor representatives. This group will identify one or two shared issues around which the group will organize further donor participation.

In addition to sharing information about their programs and to discussing and solving critical issues, the donor coordination group will serve as a forum for learning and research. It will meet regularly on relevant technical issues, with the special participation of guests from microfinance institutions, the SBS or other institutions. It may undertake research in important areas of concern. The donor coordination group will become a dynamic and influential think tank for the sector.

Over recent years and accompanying budget reductions, USAID leaders have been wont to say that the Agency has to "do more with less." One way of achieving this is utilizing every dollar more efficiently, including where possible leveraging other financial resources. Another way is not by funds themselves, but rather with the technical field personnel who are locally active. Effective donor coordination and collaboration will lead to significant, tangible results with little or no additional financial expenditures from USAID.

C. Capital Support

The total financial resources required to serve Peru's microenterprises and poor farmers are daunting. Using the rough estimate of the unserved market from Section II (Problem Statement and Activity Rationale) of 1.5 million people, assuming an average outstanding loan balance of $500, the market will require nearly US$750 million to serve all the potential clients. This amount is far beyond the reach of all the donors combined. USAID's budget for the MIGA is less than two percent of this sum.

Fortunately, significant financial capital can become available to Peru's microfinance institutions from other sources, including COFIDE, commercial banks, guarantee facilities, bond issuances, client deposits and from new investors. Currently, most microfinance institutions' long-term growth is restricted much less by lack of financing than it is by operational weaknesses. Relatively easily procured donor funding solves the short-term problem of taking care of the clients waiting at the door for low cost credit (lower cost than the moneylender), but may not contribute to removing the impediments to accessing commercial sources of funds.

This is why the technical assistance and training component described in the previous section is so vitally important. As the institutions become operationally stronger, they will increase their ability to access available financing. USAID's most effective means of supporting the capital requirements of microfinance institutions will be by assisting these institutions in identifying and attracting private commercial and semi-commercial funds.

Nevertheless, there will be opportunities for USAID to speed the development of the capacity of microfinance institutions to serve more micro clients by supporting their efforts to secure additional funds to on-lend. This will be accomplished by providing guarantees for access by microfinance institutions to private sector funds by executing timely, critical capital infusions in well-chosen microfinance institutions and by coordinating with other donors to establish a local funding mechanism.

The budget includes approximately US$1.35 million to provide support to up to five institutions. Below are four options for utilizing these funds. Should any combination of these options prove particularly effective, the Mission may explore expanding this component by procuring additional funding from USAID/Washington or other sources.

C.1. Funding Guarantee Mechanisms

USAID has two tools, a program tool and a financing tool, both of which are designed to promote microenterprise development by overcoming market imperfections that inhibit the flow of credit from commercial financial institutions to microenterprises. The program, called MSED for Micro and Small Enterprise Development, is a risk-sharing mechanism to encourage local financial institutions to loan to microfinance institutions previously unable to obtain funds from the commercial market. The financing tool, called DCA for Development Credit Authority, is used to guarantee funds provided by private sector financial institutions to microcredit suppliers. Both MSED and DCA may be used in addition to or in lieu of grant funding by Missions.

The MIGA Activity will utilize MSED and DCA as appropriate.

MSED Program

The MSED program offers several products including loan portfolio guarantee (LPG), bond guarantee, direct loan, wholesale guarantee and portable guarantee. Most interesting to microfinance institutions in Peru will be the LPG and the portable guarantee.

The LPG guarantees up to 50 % of the net loss on the principal amount of loans made by a financial institution to micro borrowers. Guarantees or loans are available for periods from three to 10 years. Loan sizes are limited to US$5,000 for microenterprises, and up to US$150,000 for small enterprises.

For some lenders, this guarantee can make a difference in persuading the lender to make the effort to learn how to loan to micro enterprises. Once successful, the lender often elects to continue the service without the guarantee, at least in that market. The lender may still request a guarantee to enter new markets or introduce new products.

The portable guarantee is also appropriate for institutions in Peru, and is currently proposed for Mibanco. In this case the guarantee is obtained by the microfinance institution, which uses the guarantee to shop for commercial bank funding, often on more favorable terms.

Resources of the Office of Development Credit, which selects the institutions to be provided guarantees, fund the MSED program.

DCA Tool

The Development Credit Authority will also be utilized as a funding mechanism for microfinance institutions. DCA is demand driven; its activities are designed and managed by Missions and supported by the Office of Development Credit. Funded projects must demonstrate the following characteristics:

- USAID development goals and Strategic Objectives can be achieved with credit assistance.
- The subsidy cost of each proposed activity can be reasonably estimated and put on budget.
- The borrowers, sovereign or non-sovereign, are deemed reasonably creditworthy.

Missions identify, design, authorize and implement DCA projects. While the Missions are responsible for developing the credit soundness of their activities, the Mission Chief Financial Officer after consultation with the Agency's Credit Review Board and with the assistance of G/GAD/DC, determines the subsidy cost. The Mission via DCA transfer authority uses its own operating year budget to fund the credit guarantee. The Global Bureau is able and willing to assist Missions in project design and other aspects of using DCA.

C.2. Grants to Microfinance Institutions

The most capable microfinance NGOs will eventually seek EDPYME licenses from the SBS. In addition to numerous other requirements, approximately US$260,000 is required to obtain this license. Some NGOs do not and will not have the equity base to meet this requirement. And because most if not all this amount must be deposited in cash in order to obtain the EDPYME license, this transaction would likely have a significant negative impact on the institution's ability to serve its clients during the months after making the deposit. Furthermore, although the minimal capital required to convert to an EDPYME is US$260,000, this level of equity is clearly inadequate for an institution planning on expanding significantly in a sound manner. Most respected authorities in the field would agree that the figure should be closer to US$1 million. The current Peruvian requirement for authorization to accept deposits (Module 1 of the Banking Law) is about US$1.4 million.

An institution's transition to the first level EDPYME status has the following important advantages:

- The prudent supervision of the SBS instills internal discipline and credibility to the institution.

- It gives the institution the ability to leverage its equity by accessing the formal financial markets. The institution may access external debt financing from diverse sources, including COFIDE, other second tier lending institutions (which are often supported by donors), commercial bank loans, multilateral finance institutions, socially responsible investment funds, bilateral donors and even through bond issuances. Potentially, an institution can leverage up to five or six times its equity, whereas it can only leverage on average one times its equity as an unlicensed institution. Several of the EDPYME have achieved leverage of two to three times equity. By diversifying its liabilities, the institution also protects itself from shocks in its liability structure.

This component will normally take the form of direct grants to microfinance institutions. USAID may consider operating such grants through trust funds or other mechanisms that would allow it to condition the grants on certain accomplishments. Regardless of the mechanism, these grants will be made by USAID if the funding will make a critical impact in improving an NGOs ability to deliver financial services in the short- to medium-term to its targeted clients. They will also be employed by USAID as an incentive to encourage NGOs to demonstrate improvement in key areas and indicators, including:

- Reduced loan delinquency rates, preferably below 5% after 30 days,
- Increased efficiency demonstrated by reduced operating costs as a percent of loan portfolio, and
- Increased financial sustainability over time, expressed by a ratio of total income as a percent of total costs (including real financial costs, less donor income).

C.3. Strategic Investment Promotion to Leverage Resources and to Strengthen Microfinance Institutions' Governance Structure

NGOs have demonstrated both willingness and the ability to develop and implement effective credit services for the poor. They initiate these services as a means to foster social and economic development of targeted disadvantaged groups. But in general, NGOs possess neither the strategic nor the technical skills to manage financial institutions. Many of these skills can be learned through intensive technical assistance and training, as well as by simply hiring technically qualified personnel with financial institution experience.

An important obstacle to transforming an NGO into a legitimate financial institution is often the lack of competent governance. NGOs are usually governed by well-intentioned, socially minded individuals with little or no financial management experience. Even in the cases where NGOs may have people from private industry and banking as their founders or on their boards, more often than not these people draw a clear line between their business lives and their NGO lives. They usually do not apply the same principles and rigor to the NGO that they applied in attaining success as private business people or bankers.

NGO ownership structures generally have a very limiting effect on microfinance expansion. In almost all cases they are fully owned by one institution, namely the non-profit NGO. Furthermore, in many cases their credit services program is only one of a range of social services for the poor (Caritas, Prisma and ADRA, for example). These institutions lack the diversity and experience of multiple owners. Even some of the EDPYME's are still fully or almost fully owned by the NGOs from which they were transformed.

The NGO ownership structure is a problem for at least three reasons. First, it will be difficult for institutions fully owned or controlled by NGOs to earn the blessing of the SBS to expand and diversify services and operations, especially deposit mobilization. Second, it will be difficult for the governance bodies of these institutions to analyze the financial environment and to navigate their institutions through the competitive and volatile financial setting. Third, and most importantly, NGOs lack the financial resources (solvency) to add capital when their microfinance institution requires it.

Few of Peru's microfinance institutions will be attractive to commercial investors during the next five years - unless USAID or other donors can add incentives to the investment packages.

This component is designed to leverage funding and to strengthen the governance structure of selected high potential microfinance NGOs by attracting experienced, solvent investors. International non-profit institutions such as Accion International, MEDA, and Seed Capital Development Foundation have proven to be participatory, competent investors in successful microfinance institutions throughout the world. They bring microfinance experience, technical expertise and sound judgment to microfinance institutions, as well as a strong interest in seeing their investments grow.

USAID will also explore the possibility of attracting wholly private business interests, local or international, as investors in microfinance institutions. Peru's microfinance market is relatively large and untapped, and probably will become in time a profitable investment option. Under this program, reputable individuals with a record of successful experience in the finance sector could be identified and provided with incentives to invest in the microfinance sector.

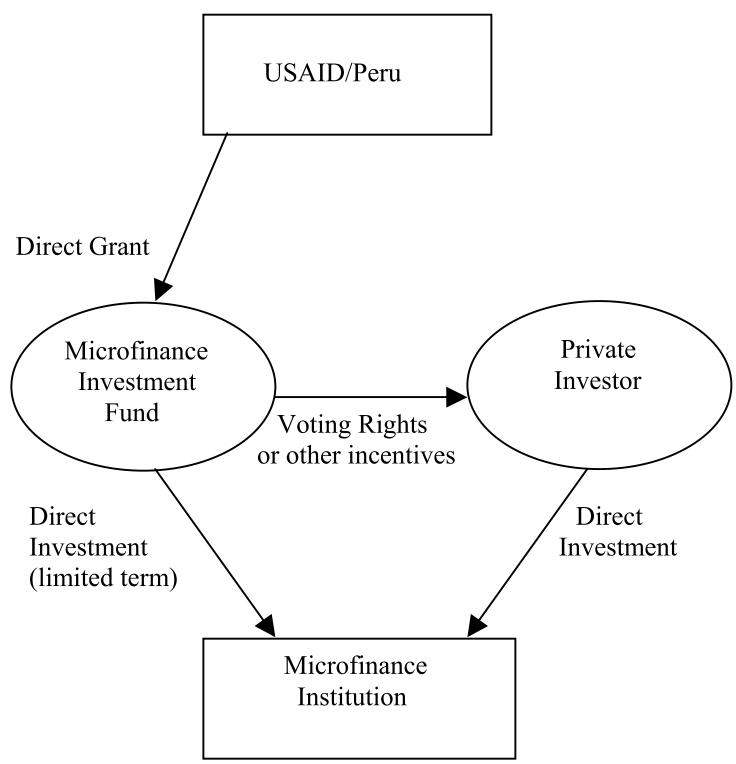
Under this component, USAID will utilize two types of incentives, alone or in combination. The first type of incentive will involve non-financial assistance or information, which might lead to the decision for a private investor to invest. USAID could support the preparation of objective, reliable rating information on microfinance institutions. It could also conduct feasibility studies, due diligence or other up-front studies required to entice potential investors.

The second type of incentive will involve direct grants by USAID to be used as investments of equity in microfinance institutions. As USAID is prohibited from taking equity in private institutions, these funds will be granted to a third party institution, which, in turn, will execute an equity investment in a microfinance institution. Numerous implementation options will be possible under this component. USAID will decide on the most appropriate one early in the Activity. One option is to augment an institution's (preferably an international non-profit institution) investment by matching it. This provides an institution with an up-front incentive that lowers the investor´s risk and increases its equity.

A second option involves the creation of a non-profit private investment fund (which could be the same fund created in Section B.3. below) designed exclusively to provide critical financing to

Peru´s microfinance institutions. USAID funding could be granted to this institution, which, in turn, would make equity investments in microfinance institutions. These equity investments using USAID funding would be tied as an incentive package to a private investor´s investment interests. For example, the fund could negotiate with a private investor to match that investor´s equity position in an agreed upon microfinance institution. As an incentive for the private investor to assume his risk, the investment fund could cede some of its shareholder rights to the private investor, such as voting rights. The investment fund´s investment would be for a limited period, for example three years, after which time it could give the private investor the first option to purchase its shares. This option involves indirect financial and/or non-financial incentives to the private investor, and would probably be a preferred option to USAID management. This option is illustrated in Figure 2 below.

Figure 2



A particularly timely opportunity to execute such a grant would be during the process of an NGO's transformation to EDPYME status. In such cases, USAID funds would serve the dual purpose of providing critical new equity and of adding improved governance. It would also result in a rapid leveraging of financial resources for the microfinance institution. Peru's banking law follows the international regulatory guidelines set by Basle, which allows for regulated institutions to leverage their equity up to a ratio of 11 to one. This ratio is too high for microfinance institutions because of their relatively unproven track record and because of the potential volatility resulting from the short-term nature of their loan placements. A ratio of between six and eight to one is more prudent for microfinance institutions. As an example, if a combined private investor/investment fund invested US$500,000 in a microfinance institution, within a period of a year or two this investment would leverage total financing of about US$4 million. By any standards this is an excellent return on USAID's investment.

C.4. Creation of a Microfinance Trust Fund or Second Story Bank

COPEME has made a preliminary estimate that during the next three years (2001-2003) the financing requirements for eight EDPYME's and the five largest NGOs will be nearly US$60 million. Of this amount, it estimates, about half will be provided by COFIDE and donor sources. Although COFIDE has been effective and relatively agile in its operations, it has the following disadvantages:

- COFIDE has a monopoly on microfinance lending,
- As a government institution, its mandate could change due to political decisions,
- Its lending is restricted to institutions subject to SBS regulation and supervision, and
- Its lending to any one institution is restricted to 30 percent of the institution's equity.

COFIDE's relative advantages and disadvantages aside, there will still be a shortfall of approximately US$30 million, according to COPEME. A viable option for covering this shortfall is the creation of a private microfinance trust fund or second story bank. Such an institution will require approximately US$5 million in equity and another US$15 million in debt financing in order to justify the time, effort and legal costs in creating such an entity, and also to cover the operating costs associated with managing a second tier portfolio.

Although USAID cannot possibly finance the entire US$20 million, it will seek to organize the cooperation of multiple donors around the activity. Donors such as the Inter-American Development Bank (IDB), the Andean Corporation for Development (CAF), the European Union, Spain, Holland, Belgium and Canada have already provided financing for this sector through different mechanisms. Approximately US$10 million in European Union funds is currently frozen in the Ministry of Industry's FONDEMI program because agreement cannot be reached on the future mechanism for executing the fund. Many of these donors, particularly the European bi-laterals, share USAID's focus on supporting those microfinance institutions that provide small loans to the very poor.

Once an EDPYME achieves Module 1 status and can accept public deposits, the funding need through institutions is diminished, but not eliminated. For the first few years deposit maturities will be shorter term than the loan requests. A second story funding mechanism usually provides intermediate term funds.

The primary benefit of a second story bank is to reduce costs for donors. Individual donors rely on donor country consultants to conduct the finding and evaluation of potential institutions to which they provide funds. The process requires extensive use of expensive consultants. Having a local institution that accepts part or all of the risk of loan collection also conduct loan analyses usually results in better credit decisions and is less costly.

A secondary benefit is reduced costs for the microfinance institution in finding financing opportunities and in loan application processing.

A second story bank can increase funds for the sector if its financial strength permits it to sell securities in the local market to obtain funding which it on-lends to microfinance institutions. This can occur only after several years when the second story bank has gained experience in the market. In some cases, donor funding is contingent on matching funding by the host country government, which may serve to increase funding to the sector. Donor funding pledged to a second story bank will most likely replace funds already intended to be utilized in the sector. Hence, a second story bank may or may not increase funding for the sector.

Given its strong field presence and long experience in the microfinance field, USAID is in an excellent position to generate dialogue with other donors regarding the creation of a private fund for microfinance support. USAID will begin by demonstrating a willingness to contribute an important part of its budget, for instance up to US$2.5 million, which would represent half of the new institution's equity. USAID will need to increase the MIGA budget and procure additional funding to implement this component. USAID could also provide technical and legal resources to support the process of creating such an institution. By doing so, USAID could leverage an additional US$15 million or more in other donor funding to support the trust fund or second story microfinance lending bank.

Whereas the concept of a second story bank would involve the creation of a new institution, another option is to create a trust fund, which is a simpler mechanism. The fund's statutes and directives could be established and managed by a group of participating donors and possibly other reputable individuals. The responsibility of executing loans from the fund could be given to an existing financial institution, such as COFIDE, FOGAPI or in a private commercial bank. The advantages and disadvantages of the second story bank and trust fund are listed in Table 3. Both options have clear advantages and disadvantages. Neither is the obvious preferred option; rather both options will have to be analyzed carefully by USAID and its partners.

Table 3: Advantages and disadvantages of trust funds and second story banks.

	Trust Fund	Second Story Bank
ADVANTAGES:		
Leverages USAID Resources	Yes	Yes
Provides Loans to NGOs	Yes	Yes
Managed Privately	In part	Yes
Potentially Sustainable over time	Yes	Yes
DISADVANTAGES:		
Creation could be Protracted Process	Somewhat	Yes
USAID loses Control over Resources	Somewhat	Yes
Subject to GOP Political Influence	Somewhat	No
Postpones microfinance institutions' Sourcing of true commercial financing	Yes	Yes

VII. PLAN OF ACTION

The MIGA Activity will have a five-year duration, assuming USAID planned funding levels will become available on a timely basis. Because of USAID's current involvement in the sector, it is expected that implementation of the new Activity will begin quickly after it is authorized. From a management perspective, USAID already has internal technical capacity in place with Microfinance Specialist Jaime Giesecke and Program Manager Eduardo Albareda. Furthermore, the technical assistance and training program will involve a continuation and expansion of the current program being implemented under the Microfinance Initiative by COPEME. This program should suffer no interruption at all. Following is a summary of the timelines for implementation of the MIGA Activity:

A. Year 1

- Amend Cooperative Agreement with COPEME to extend through 2005 and to add funding.
- Initiate TA and Training through COPEME.
- Execute SEGIR contract for TA under all three Activity components.
- Initiate TA under SEGIR.
- Initiate and sustain donor coordination; identify key commonly held issues; organize roundtables and technical seminars.
- Initiate assessments of NGOs for potential capital support.
- Identify key regulatory and policy constraints and issues.
- Develop and sign MOU with the SBS.

B. Year 2

- Implement TA and training through COPEME and SEGIR.
- Actively pursue the licensing of at least one EDPYME as Module 1 deposit taking institution.
- Address key regulatory and policy constraints.
- Continue strong donor coordination and seek collaboration on specific issues.
- Support process of privatization of municipal S&Ls.
- Aggressive strategic investment promotion results in at least one equity investment from a private investor.
- Pursue agreement on and begin design of a trust fund or second story bank.

C. Year 3

- Implement TA and training through COPEME and SEGIR.
- Actively pursue the licensing of at least one EDPYME as a Module 1 deposit taking institution.

- Address key regulatory and policy constraints.
- Support process of privatization of municipal S&Ls.
- Continue strong donor coordination and collaboration on specific issues.
- Active promotion for private strategic investments results in a second equity investment from private investor.
- Dialogue with the GOP and other donors' results in the successful creation of trust fund or second story bank with the financial participation of several other donors.
- Evaluate Activity and adjust program as appropriate.

D. Year 4

- Implement TA and training through COPEME and SEGIR.
- Actively pursue the licensing of at least one EDPYME as a Module 1 deposit taking institution.
- Address key regulatory and policy constraints.
- Continue strong donor coordination and collaboration on specific issues.
- Active promotion for private strategic investments results in a second equity investment from private investor.

E. Year 5

- Implement TA and training through COPEME and SEGIR.
- Evaluate MIGA Activity and options for follow-on program.

VIII. DEFINITION OF SUCCESS

STRATEGIC OBJECTIVE NUMBER 2
ACTIVITY FRAMEWORK

INCREASED ECONOMIC OPPORTUNITIES FOR THE POOR IN SELECTED ECONOMIC CORRIDORS

INTERMEDIATE RESULT 2.2
Increased Availability of Microfinance Services

Indicators:
1. Number of microfinance clients served increased by 300 percent.
2. Number of poverty loans (<$400) increased by 300 percent.
3. Number of micro savers increased by 100,000.

IR2.2.1: Strengthened Institutional Capacity to deliver Microfinance Services

Indicators:

1. Portfolio at risk in 30 days below 5%.
2. Operating Costs/Gross Loan Portfolio reduced by 25%.
3. Financial Sustainability (Level 2) increased by 25%.
4. Effective micro savings program implemented in four institutions.

IR2.2.2: Improved Regulatory Environment

Indicators:

1. Improvements in the regulations governing the provision of microfinance services.
2. Improved SBS supervisory practices for micro financial services providers.
3. Credit reference system expanded geographically.

IR2.2.3: Microfinance funding availability expanded.

Indicators:

1. Strengthened equity position of selected microfinance institutions.
2. Strengthened and diversified governance structure of selected microfinance institutions.
3. Permanent local funding mechanism for microfinance NGOs established and functioning.

IX. FEASIBILITY ANALYSIS, KEY ASSUMPTIONS, RISKS

A. Feasibility Analysis

USAID personnel have the general skills to carry out this Activity. Highly specialized skills can be acquired through Activity mechanisms, such as by bringing specialists under the SEGIR agreement.

Elaborating the vision for development of the microfinance industry in Peru and maintaining that agreement will require continued consultation and discussion with opinion leaders for the industry, be those from the Government of Peru, donors, microfinance institutions, and regulatory and support institutions. The USAID/Peru Mission will ensure that sufficient time is allocated among the team members to continue the necessary contacts with other institutions to maintain abreast of their program and to provide a continuing leadership role for the industry development.

B. Key Assumptions and Risk Control

Several key assumptions underlie this Activity design. They are:

1. Continued economic stability,
2. Appropriate microfinance policies and regulations are maintained by the Government of Peru,
3. The criteria for forming microfinance institutions and progressing through the regulatory requirements until microfinance institutions can capture deposits from the public continues relatively unchanged,
4. Donors continue to make funds available for non-regulated microfinance institutions, and
5. USAID funding levels for the Activity are not reduced.

B.1 Continued Economic Stability

The normal development of microfinance institutions requires the avoidance of a major recession or significant jump in the rate of inflation. At present the economy is not expected to decline into a major recession, nor is it expected to grow especially rapidly. A greater than normal uncertainty exists because of the pending political campaign.

Control of Economic Risks

The success of financial institutions is threatened by instability, such as with a major recession. A recession reduces loan demand, creating a situation where microfinance institutions cannot grow, and may decline in the number and amount of borrowers. Often a recession also creates excess supply of funds, causing interest rates to decline. Both of these reduce the earnings ability of microfinance institutions.

In the initial stages of a recession, default rates rise. Because micro loans are usually short term, the effect on default rates should be a temporary condition. Institutions need to be ready to adjust their lending policies in accordance with the economic conditions.

High inflation creates another set of problems. If interest rates are allowed to increase, many investments are no longer viable, and loan demand declines. If interest rates are constrained, then loan portfolio earnings may not cover operational costs. If inflation generates increased costs of funds, the microfinance institution can quickly adjust earnings on the loan portfolio. If a recession increases loan defaults, the microfinance institution usually purges these loans from their loan portfolio within a year.

Micro loans seldom have real guarantees, which can be sold for loan repayment. As a consequence, the microfinance institution must be especially vigilant to adjust its lending policies quickly in response to the changing economic situation. Technical assistance provided by the MIGA Activity will assist institutions in responding to changing economic conditions in a timely manner.

B.2 Appropriate Microfinance Policies are Maintained

No pending change in microfinance regulations are expected. But the Government of Peru has created risks for finance institutions in the recent past especially by meddling with the agricultural finance sector. The upcoming electoral campaign could bring more suggestions for actions prejudicial to the developing microfinance institutions.

Control the Risk of Inappropriate Microfinance Policy Changes

The ongoing coordination with other donors that is a part of this Activity will enhance the ability of USAID to detect adverse economic policies and to generate a response in support a well functioning microfinance industry. Donor coordination meetings will be held periodically, and more often if necessary to support appropriate policy initiatives. Especially difficult issues can be brought to the attention of the Embassy personnel for their support.

B.3 Criteria for Forming Microfinance Institutions do not Change

Currently developing microfinance institutions can plan their development in acquiring increasing levels of supervision and in accessing funding until they are authorized to take deposits from the public. An NGO can become licensed as an EDPYME with a minimum of capital, about US$260,000, and a relatively low level of technical capabilities. With this license, they are eligible to seek funds from COFIDE for a portion of their loan portfolio needs. Other doors may also be opened, for example the formation of a corporation facilitates adding investors or joining with another finance institution. Some donors look more favorably on those institutions that have achieved regulated status.

As an EDPYME progresses and acquires more capital it may apply to be licensed under Module1, which requires about US$1.5 million of equity and also carries more stringent operating requirements. With the license for module 1 the EDPYME may accept deposits from the public, increasing its financing options and enhancing its possibilities for continued self-sustainability.

Control of Risks of Microfinance Licensing

If the requirements to become an EDPYME are significantly increased, fewer NGOs will become registered and therefore have reduced access to funds. They will also be subject to higher taxes as NGOs. For some NGOs, not becoming an EDPYME will postpone some additional costs, such as for an internal auditor. Until interest rates begin to decline because of increased competition, these NGOs can probably remain in the market.

A more difficult problem to resolve may be access to funds for lending. In this case the option to establish an additional funding mechanism for non-regulated institutions can be elevated in importance and a timetable for implementation accelerated.

B.4 Donors continue to make funds available for non-regulated microfinance institutions.

It is expected donors will continue to support microfinance initiatives in Peru, both for non-regulated and well as for regulated institutions. Funds are expected to continue both for technical assistance and for lending to microfinance institutions for on lending to borrowers.

Control of Risks of Non-Funding

Growth in the number of microfinance borrowers and in the total microfinance loan portfolio depends mostly on donors making available additional funds. Many of the larger NGOs and EDPYMES are nearing financial sustainability, and they could continue even if the total amount of loan funds remains constant. If donors require repayment of existing loans and refuse to give new loans, some microfinance institutions will need to significantly reduce their costs or look for merger partners.

Many NGOs and EDPYMES have substantial equity capital; they would be less affected by a cutoff of new funding. Those that have progressed to become financially sustainable can continue indefinitely without additional donor support.

B.5 No Significant Funding Reduction by USAID during Implementation

The Activity design contemplates a funding level of US$10 million. If funding is significantly reduced during Activity implementation, it is recommended that the capital support component be reduced first. If funding inadequacies persist, Mission personnel will decide between reducing technical assistance and training to microfinance institutions or reducing sector support.

Control of Risks of Reduced Funding from USAID

Funding reductions, unless drastic, should not terminate implementation of this Activity. If reductions are minor the expected impact is that the development of some microfinance institutions will be delayed. No institution should go out of business because of minor funding reductions that require elimination of the capital support component.

Funding reductions that also require reduction in the amount of technical assistance and training for sectoral support will likely delay development of the industry and reduce the achievements contemplated for the activity. If USAID and its partner organizations select technical assistance recipients well, no institution should go out of business solely because of funding reductions.

X. FINANCIAL PLAN AND BUDGET

MIGA implementation will require total expenditures of US$13,838,130 over 5 years. Of this USAID provides US$9,383,130 or 74 % and counterpart expenditures account for US$3,450,000 or 26 %.

Spending by USAID of US$9,383,130 is allocated as follows:

- USAID Activity administration, US$1,093,682 (11 %) of USAID expenditures,
- Technical assistance and training, US$5,734,448 (58 %),
- Capital support, US$1,210,000 (12 %), and
- Strategic investment promotion, US$1,800,000 (18 %).

The Activity requires agreement with COPEME to carry out technical assistance and training in the amount of US$4.47 million and with a SEGIR IQC contractor in the amount of US$2.47 million. These funding agreements will be structured as multiyear agreements with periodic performance assessments and subject to funding availability.

Counterpart funding will come from fees COPEME charges for technical assistance and training and the strategic investments. COPEME will charge 50 % or 25 % of the cost of technical assistance to the microfinance institutions, depending on the type of clients served. Thus counterpart contributions for technical assistance and training will be US$2.1 million.

The strategic investment promotion expenditures are estimated to attract counterpart investments from private investors and socially responsible investment funds of at least US$1.35 million.

Table 4. MIGA budget

Components	FY2002	FY2003	FY2004	FY2005	FY2006	Total	%
USAID Activity administration costs	**206,000**	**212,180**	**218,545**	**225,102**	**231,855**	**1,093,682**	**11%**
1 Technical Assistance, Training	**963,200**	**1,261,446**	**1,264,789**	**1,268,233**	**976,780**	**5,734,448**	**58%**
Technical Asst. COPEME, all lenders	250,000	300,000	300,000	300,000	250,000	1,400,000	
Avg. total cost per TA package	50,000	50,000	50,000	50,000	50,000		
Cost to Activity @ 50 % *	25,000	25,000	25,000	25,000	25,000		
Number of instances	10	12	12	12	10	56	
Tech Assist, COPEME, poverty lenders	375,000	450,000	450,000	450,000	375,000	2,100,000	
Avg. total cost per TA package	50,000	50,000	50,000	50,000	50,000		
Cost to Activity @ 75 % **	37,500	37,500	37,500	37,500	37,500		
Number of instances	10	12	12	12	10	56	
Technical Asst. & Training, SEGIR	180,000	300,000	300,000	300,000	180,000	1,260,000	
Avg. cost per instance	30,000	30,000	30,000	30,000	30,000		
Number of instances	6	10	10	10	6	42	
Training, primarily local, COPEME	50,000	100,000	100,000	100,000	50,000	400,000	
Avg. cost per instance	2,500	2,500	2,500	2,500	2,500		
Number of instances	20	40	40	40	20	160	
COPEME operational support	108,200	111,446	114,789	118,233	121,780	574,448	
2 Financial sector support, SEGIR	**250,000**	**250,000**	**250,000**	**250,000**	**210,000**	**1,210,000**	**12%**
Support for SBS	80,000	80,000	80,000	80,000	60,000	380,000	
Policy development	80,000	80,000	80,000	80,000	60,000	380,000	
Others	90,000	90,000	90,000	90,000	90,000	450,000	
3 Capital support for microfinance institut	**325,000**	**550,000**	**550,000**	**325,000**	**50,000**	**1,800,000**	**18%**
Strategic investments promotion	225,000	450,000	450,000	225,000	-	1,350,000	
Fees for guarantees	100,000	100,000	100,000	100,000	50,000	450,000	
TOTAL	**1,744,200**	**2,273,626**	**2,283,335**	**2,068,335**	**1,468,635**	**9,838,130**	**100%**
Total SEGIR	430,000	550,000	550,000	550,000	390,000	2,470,000	25%
Total COPEME	783,200	961,446	964,789	968,233	796,780	4,474,448	45%

* Represents half the cost of a technical assistance intervention.

** Represents 75 % of the cost of a technical assistance intervention

Table 5. MIGA Administrative costs.									
				FY2002	**FY2003**	**FY2004**	**FY2005**	**FY2006**	**Total**
Personnel costs	**Per day**	**Days**	**Incr/yr**						
Microfinance Spec.	290	221	3%	64,090	66,013	67,993	70,033	72,134	340,263
Activity Specialist	300	221	3%	66,300	68,289	70,338	72,448	74,621	351,996
Administrative costs	**Per person /month**	**No.**							
Travel International	4,500	2	3%	9,000	9,270	9,548	9,835	10,130	47,782
Travel local	10,980	2	3%	21,960	22,619	23,297	23,996	24,716	116,589
Communications	1,000	2	3%	2,000	2,060	2,122	2,185	2,251	10,618
Office space	8,500	2	3%	17,000	17,510	18,035	18,576	19,134	90,255
Training	12,500	2	3%	25,000	25,750	26,523	27,318	28,138	132,728
Audit and evaluation				25,000	25,000	25,000	75,000	25,000	175,000
Other	1,000	2	0%	2,000	2,000	2,000	2,000	2,000	10,000
Total				**232,350**	**238,511**	**244,856**	**301,391**	**258,123**	**1,275,231**

Table 6. COPEME operational support.									
	Cost/mo	**Incr./yr.**	**FY2002**	**FY2003**	**FY2004**	**FY2005**	**FY2006**	**Total**	**%**
Personnel	1,100	3%	77,000	79,310	81,689	84,140	86,664	408,803	71%
Number of persons			5	5	5	5	5		
Travel	2,000	3%	24,000	24,720	25,462	26,225	27,012	127,419	22%
Communications	400	3%	4,800	4,944	5,092	5,245	5,402	25,484	4%
Office materials	200	3%	2,400	2,472	2,546	2,623	2,701	12,742	2%
TOTAL, US dollars			**108,200**	**111,446**	**114,789**	**118,233**	**121,780**	**574,448**	**100%**

XI. MANAGEMENT PROCEDURES

USAID's SO2 Team will manage the MIGA activity. Supervised by the Team Leader, a full-time project funded Microfinance Specialist and the Activity Manager will manage all components. As this activity will require USAID's leadership among the donor community and much substantive policy dialogue with key members of the GOP, the MIGA implementation team will continue to develop its understanding of policy issues and an ability to negotiate at high levels. Strong support and occasional involvement of the Mission Director will also be critical to the success of this activity.

USAID's SO2 Team, led by the Legal Advisor, will develop a bilateral agreement for the MIGA Activity. The agreement document will encompass all the components of MIGA and will serve as a means to authorize and obligate all Activity Funds. USAID's GOP counterpart for the agreement will be the Ministry of Economy and Finance (MEF). There are advantages of working with the MEF as opposed to other ministries. First, the one of the MEF's principal mandates is maintaining sound policy for a stable economy. Since the MIGA Activity is based on sound economic and financial principles (and requires them, as well), the MEF will likely view the Activity as supportive of its own goals for Peru's development. Second, it is less likely the MEF will be interested in diverting funds for political reasons (e.g., agricultural loans, export development) than other government entities whose mandates may involve supporting specific sectors and in executing Government-financed projects.

A. Technical Assistance and Training

The Technical Assistance and Training component of MIGA will be implemented by COPEME. This institution has demonstrated the technical capabilities to assess the needs of microfinance institutions and to develop appropriate technical assistance and training programs to address these needs. Its training programs have been extremely successful, and have attracted the participation of COPEME members as well as other institutions such as Municipal Savings and Loans. COPEME has also developed a strong working relationship with the SBS, and SBS personnel have conducted some of COPEME's training courses. Because of the quality of its courses, COPEME has covered its direct expenses through fees charged.

COPEME staff has worked closely with several NGOs and EDPYME's to evaluate the institutions' needs and to design technical assistance packages. Its record to date shows that COPEME must improve its ability to draft effective scopes of work and to select quality contractors. A part of the operational budget of COPEME will be used to improve its own staff's ability to improve its performance in the sub-contracting area. Finally, USAID should continue to support and build on COPEME´s capacity to collect and report on institutional financial data. Good quality, objective financial data will complement other components of this Activity by providing donors and potential investors with timely information about microfinance institutions.

USAID is not concerned with the sustainability of COPEME per se. USAID's focus will remain on the target group, which are the microfinance institutions. Nevertheless, it is important that COPEME charge a nominal fee for its services in order to assure that its services will be fully valued. COPEME will continue its policy to charge 50 percent of the direct costs of technical services, but this policy should be limited to all non-NGO institutions, including EDPYMEs, municipal S&Ls and banks. The Mission, together with COPEME, will consider the possibility of a separate policy for institutions serving the poorer client segments. Because of their their focus on the poor, microfinance institutions providing average loans under US$400 may be charged 25 percent of the direct costs of technical assistance. This would ensure the selective participation of those institutions most interested in expansion and institutional strengthening.

This Activity will be executed by amending the current Cooperative Agreement with COPEME, extending it through year 2006 and by increasing the total budget by US$4,475,448. Implementation of the current agreement with US$800,000 in USAID funds should be accelerated to expend funds at a rate consistent with the new, increased budget.

COPEME has compiled a solid database of local consultants in the area of microfinance. Nevertheless, there are some technical assistance needs, which cannot be addressed by local consultants, or only partially addressed. These include rural credit, savings instruments design, information systems design, and others.

Therefore, an additional technical assistance mechanism will be required to implement this component. The recommended mechanism is USAID's Financial Services (FS) component of the Support for Economic Growth and Institutional Reform (SEGIR) indefinite quantity contract (IQC). This mechanism is fully appropriate for the technical assistance and training component, as SEGIR covers technical areas such as:

- Financial research and information dissemination,
- Developing and applying innovative financial instruments to improve the efficiency and competitiveness of financial services,
- Programs to strengthen and implement financial supervisory and regulatory structures and institutions,
- Support to strengthen and expand microfinance and rural finance, and
- Support to bank as well as non-bank financial institutions.

Many of the firms listed as prime and sub-contractors under SEGIR possess strong backgrounds and capabilities in development finance. If the total amount for this component will be under $2 million, USAID may either choose from the list of contractors without competition or it may elect to compete the contract among all approved SEGIR contractors. If the contract amount exceeds $2 million, the Mission is obligated to compete the SEGIR contract.

A long-term contract of four years will be signed with a qualifying SEGIR consortium that will essentially buy access to continued short-term consultants throughout the duration of the project.

All SEGIR assistance under this component will be channeled through COPEME, although USAID will approve all short-term technical assistance consultants. Under the arrangement, COPEME will still charge a fee of 25 or 50 percent to institutions receiving the assistance (should this fee policy be agreed upon), but it will not incur any direct costs (because USAID will pay all SEGIR costs). The income earned by COPEME with SEGIR consultants will be deposited by COPEME in a special microfinance development fund that will be jointly programmed by USAID and COPEME.

B. Sector Level Support

This component requires strong engagement at the regulatory and policy levels. Today, no other donor or institution has assumed this important role. USAID will place a high priority on playing this leadership role under the MIGA Activity. Most of the time spent by the SO2 Team Leader on microfinance should be devoted to this component. The Microfinance Specialist and the Activity Manager should also devote significant time and effort on this component in order to be effective. There may be policies or other issues arising that require and merit the force of the USG's political will. In these cases the involvement of USAID's Mission Director, or even the Ambassador, may be appropriate. Possible issues could include support for a new law or opposition to a political decision, which could distort the market.

Under this component, USAID and the SBS will sign a Memorandum of Understanding that commits the two institutions to working together in developing and implementing sound systems for microfinance regulations and supervision. The MOU will include an annex outlining a program strategy and implementation plan. This relationship will encourage the active support of the SBS throughout Activity implementation. Direct funding to the SBS is not planned for under the Activity, rather assistance will be channeled to the SBS through the SEGIR contracting mechanism.

Support for the privatization of the Municipal Savings and Loans will also require services rendered under the SEGIR contract. This technical assistance will be utilized on a short-term, as needed basis. Therefore, the SEGIR contract should be drafted to include elements from each of the three components of the MIGA Activity: technical assistance and training to microfinance institutions, policy and regulatory support, and capital support. USAID will be substantively involved with the drafting of scopes of work and oversight of all SEGIR assistance.

C. Capital Support

The capital grants and strategic investment promotion efforts will be managed within the USAID Mission with strong participation from diverse members of the SO2 Team. Potential grant recipients will be identified and negotiated by technical staff, including the Team Leader, the Microfinance Specialist and the Activity Manager. The technical staff will also be involved in active ongoing efforts to identify and attract private local and international investors.

The involvement of the Mission's Controller will be important for each of these instruments. In particular, the Controller must be involved with any agreement involving the disbursement of funds in increments over time based on the recipient's compliance with mutually agreed upon requirements. The Legal Advisor and Contracting Officer must also be involved in the design, negotiation and contracting of these agreements.

Experts hired under the SEGIR contract described in the Sector Level Support Component may also be used to assist in the planning and execution of the Capital Support component. An example of possible assistance would be to execute due diligence on microfinance institutions and/or on potential international investors.

The component to create a trust fund or second story institution will be managed by the Team Leader, the Microfinance Specialist and the Activity Manager. Because of the potentially complex legal and financial implications of such a program, this component will also require close involvement by the Team's Legal Advisor and Controller.

This component, in particular, will require strong consensus building among different institutional groups. First, in order to achieve the goal of resource leverage, it will require close, ongoing coordination with other bi-lateral and multi-lateral donors in order to gain their financial participation in the program. Secondly, different entities within the GOP will also have a stake in such a program. COFIDE, as the country's dominant second story lender, will have to be consulted and it will be important to have this institution's backing. Preliminary indications are that COFIDE will support the creation of such a Fund or institution. The Ministry of Economy and the SBS will also need to be consulted and possibly substantively involved for policy and regulatory reasons.

XII. PERFORMANCE MONITORING PLAN

The MIGA Activity contributes to Strategic Objective No. 2, "Increased Economic Opportunities for the Poor in Selected Economic Corridors." The Intermediate Result 2.2 is "Increased Availability of Microfinance Services." The measurement indicators are:

1. Number of microfinance clients served increased by 300 percent.
2. Number of poverty loans (<$400 for the initial disbursement) increased by 300 percent.
3. Number of micro savers increased by 100,000.

All activities conducted under MIGA should contribute to accomplishment of these goals as measured by these indicators.

Microfinance clients are those natural or legal persons who receive micro loans, or participate in savings programs by microfinance providers. Microenteprises, as defined by USAID/Peru, are businesses with 10 or few persons. The persons or companies must receive their products from any one of the microfinance providers supported by USAID at the beginning of the Activity, or from providers added to the list because they are receiving support during the Activity period. A natural or legal person may count only once, even though he/she may have multiple loans, or they may have both loans and deposit accounts. In the case of Village Banking and solidarity loan groups, care will be taken to count people receiving loans, not loans to the groups.

A microfinance institution is considered to have received assistance through this Activity if it meets one or more of the following criteria:

- Received technical assistance funded through this project,
- Received specialized training funded through this Activity, or
- Received capital support (grant, investment or guarantee) under the Activity.

The fact that one or more employees of the institution have attended a training meeting or course is not sufficient to classify that institution as having received assistance through this Activity.

Poverty loans are those loans to clients that had initial loan disbursements with the reporting institution of up to US$400 (or whatever is the current USAID poverty loan definition) equivalent in the month of disbursement. As an option to reduce data storage requirements, the institution may report the amount of the initial loan disbursement as the amount disbursed for the last loan disbursed more than two years ago. For example, if a microfinance institution disbursed the first loan to a client five years ago and does not have ready access to those records, it may report the last loan that was disbursed to that same client before January of 1998.

If the institution cannot determine the amount of the initial loan disbursement, nor the amount of the disbursement two years ago, then it should report the amount of the last loan disbursement.

Institutions with village banking programs should only use the amount disbursed for the external loan, that is the loan from the NGO, and not the internal loan, that is the loan from internal savings in the group.

A Micro Saver is any natural or legal person who puts a deposit for any amount in an institution specializing in microfinance products and receiving assistance from USAID at the beginning of this Activity or having received assistance from USAID through this Activity. The deposit may be in the form of a demand (checking), saving or time deposit, regardless of the currency. Deposits in guarantee do not qualify. No minimum or maximum amount is required. Institutions reporting should report persons with accounts, not the number of accounts. This is especially true for time deposits where many different deposit accounts may be active with different amounts or maturities.

Clients with only forced savings should not be counted as a saver for purposes of this Activity. Village banking programs should not report deposits for the internal account.

A. Measurement Indicators

A.1 Increased Availability of Microfinance Services

Measurement indicators for Intermediate Result 2.2 are:

1. The number of microfinance clients served increased by 300 percent,
2. The number of poverty loans, that is loans with initial disbursement amount up to US$400, increased by 300 percent, and
3. The number of micro savers increased by 100,000.

SINFONED will be tasked with determining the institutions classified as receiving assistance through this Activity and with reporting the number of clients served by each institution, including number of clients, number of poverty loans, and increased number of savers. The numbers should be reported quarterly to USAID. Each of the numbers above will be gender disaggregated by percentages to demonstrate the Activity´s strong focus on poor women.

A.2 Strengthened Institutional Capacity to Deliver Microfinance Services

Measurement indicators for Sub-Intermediate Result 2.2.1 are:

1. Portfolio classified at risk for loan (principal or interest) payments 30 or more days past due is below 5 percent of the gross loan portfolio,
2. Operating costs / Gross Loan Portfolio is reduced by 25 percent,
3. Financial sustainability (level 2) in increased by 25 percent, and
4. The institution has implemented an effective micro savings program.

Portfolio at Risk is the sum of the outstanding principal balance on those loans with a payment of principal or interest more than 30 days past due, divided by the gross outstanding loan portfolio.

Operating Costs include all costs for personnel, directors, general administrative costs, depreciation of fixed assets, fees for banking services, taxes of fixed assets and operations, and other costs. They do not include set asides for bad debt, income taxes, or financial costs.

The Gross Loan Portfolio is the total amount of principal due on loans outstanding, without subtracting set aside for bad debts nor principal due on loans with past due payments.

Financial Sustainability is the financial plus other operating income for the period divided by financial costs plus all operating costs, including set aside for bad debts. An imputed cost of below market rates on liabilities is not applied, nor is a market rate of interest applied to equity.

An Effective Micro Savings program means that an institution has available products suitable for micro savers, and that there are a substantial number of micro savers participating.

A.3 Improved Regulatory Environment

Sub-Intermediate Result 2.2.2 is an "Improved Regulatory Environment." This includes the supervisory environment. The measurement indicators are:

1. Improved regulations governing the delivery of microfinance services,
2. Improved SBS supervisory practices for micro financial services providers,
3. Credit reference system expanded geographically and serving all regions of the country.

Each assessment will consist of identification of the accomplishments followed by a brief description to include quantitative and/or qualitative data showing the results.

For an illustration, results cited in an assessment could be:

- Issuance of improved norms for supervision of micro credits, micro deposit products or other aspects of microfinance institution operations,
- Reduced time and expense by microfinance institutions that result from changes in reporting requirements by the SBS
- Reduced number of loans classified as deficient (and which require increased bad debt set asides) because of bad credit histories in other financial institutions,
- Reduced costs or reduced time delay for requests for credit repayment histories,
- The introduction of new products as a result of laws and or regulations and/or the utilization of these products. An example could be warehouse receipt backed loans,
- Number of users of stored value card based financial transactions in rural areas as a result of standardization of operating systems and procedures,
- Increased number of money transfers from or to rural areas because of the development of a standardized interface and operating procedures among participating financial institutions.

It is expected the Activity will cite no less that four significant accomplishments per year.

B. Baseline Data

Prior to Activity startup, the Team will determine the initial baseline data from which to measure results of the Activity. Table 7 presents an example format to record the baseline data for NGOs and EDPYMEs. It contains data as of September 2000. Other types of institutions that receive T.A. or capital support from USAID, such as banks or municipal and rural S&Ls will also need to be included in the baseline data. Institutions that begin to receive T.A. or capital support after the Activity begins will need to establish their baseline data, which will come from the period immediately prior to when they begin receiving support from USAID.

Table 7 includes NGOs and EDPYMEs that have participated in programs supported by USAID and which have provided information to SINFONED. Not all of the institutions listed in Table 7 will receive technical assistance or capital support through MIGA, and hence may not be included in determining the results of the measurement indicators. Nevertheless, Activity managers will develop additional and more detailed measurement indicators to be used in Activity supervision and control, and in estimating the impact on institutions receiving indirect assistance from USIAD. Activity managers will also want such information to monitor development of the Peruvian microfinance industry.

Prior to Activity startup the data will be updated to the latest available information. Plus, sample data in Table 7 presented here for illustrative purposes will need adjustments. For example, in column 1 some institutions may be reporting the number of group loans, not number of clients.

In column 2 the definition of poverty loan is changing. Previously a poverty loan was determined to be up to US$300 or equivalent in local currency. Beginning in 2000 poverty loans are defined as the amount in local currency equivalent to US$400. Even that amount could change pending decisions on whether to apply an inflation factor to the US$400.

Table 7. Illustrative baseline data for MIGA.							
September 2000 Institution	Col. 1 Number of loan clients	Col. 2 Number of poverty loan clients	Col. 3 Number of micro savers	Col. 4 Portfolio at risk > 30 days	Col. 5 Operating costs/Loan portfolio	Col. 6 Financial sustain-ability	Col. 7 Loans to women
NGOs				%	%	%	%
Camara de la Libertad	1,411	212	0	12.9%	21.7%	150.1%	53.0%
Caritas Peru	10,969	9,872	0	3.9%	64.2%	70.5%	80.0%
Cence BBCC							
Cence Prog. Viv.							
Detec	344	310	0	3.8%	17.7%	202.7%	70.7%
Edaprospo - PAF	1,194	1,075	0	5.7%	45.8%	93.8%	64.8%
Edaprospo - BBCC	1,880	1,692	0	5.5%	62.1%	67.1%	81.0%
Finca	6,023	5,421	0	1.4%	48.0%	102.5%	97.0%
Fondesurco	1,260	1,134	0	15.0%	10.6%	71.8%	45.1%
Fovida	683	615	0	12.8%	20.6%	120.9%	66.2%
GCOD	1,408	1,267	0	97.0%	5.3%	102.8%	78.3%
Habitat Cusco	263						
Habitat Trujillo	2,328	2,095	0	7.3%	20.8%	69.1%	53.0%
IDESI Huancayo							
IDESI La Libertad	311	280	0	20.4%	38.4%	74.5%	41.9%
IFOCC							
IPR	114	103	0	0.0%	8.2%	66.5%	50.0%
Manuela Ramos	733	660	0	7.4%	20.7%	96.9%	80.8%
MIDE							
Ppoder							
Prisma	25,189	22,670	0	5.3%	22.7%	107.6%	50.9%
Promujer*	1,662	1,496	0	0.0%	99.4%	11.3%	100.0%
Project Hope							
Rasuhillca	2,667	2,400	0	13.4%	23.2%	116.5%	78.5%
Yanapay							
Total NGOs	**58,439**	**51,300**	**0**				
EDPYMEs							
Confianza	1,835	1,652	0	3.6%	23.2%	118.1%	n.d.
Crear Arequipa	2,276	2,048	0	8.0%	15.9%	140.4%	53.5%
Crear Cusco*	411	370	0	0.0%	17.3%	63.7%	45.9%
Crear Tacna	2,285	2,057	0	5.4%	13.6%	132.6%	45.8%
Credivision*	441	397	0	0.0%	47.9%	7.6%	68.7%
Edyfica	8,717	7,845	0	9.7%	21.2%	105.3%	53.5%
Nueva Vision	618	556	0	16.6%	23.6%	55.4%	30.2%
Proempresa	2,928	2,635	0	6.7%	24.2%	122.4%	49.0%
Raiz	377	339	0	6.9%	44.2%	63.6%	n.d.
Solidaridad*	1,016	914	0	0.7%	51.6%	16.0%	64.0%
Total EDPYMEs	**20,904**	**18,814**	**0**				

* Began operations in 2000.
Column 1, 2. Number of people receiving loans, not number of groups.
Column 3. Number of people with saving or time deposit accounts, not number of accounts.
Column 4. Outstanding balance of loan portfolio with payment > 30 overdue divided by gross loan portfolio.
Column 5. Total operating costs, excluding loan loss provisions, including depreciation, divided by gross loan portfolio
Column 6. Total income less donor contributions divided by total financial and operating costs including set aside for bad debts. An imputed cost of below market rates on liabilities is not applied, nor is a market rate of interest applied to equity.

C. Special Situations

NGOs may convert to EDPYMEs or banks and EDPYMEs may convert to banks during the lifetime of this Activity. Likewise, it is expected some institutions will merge. If a merger occurs, the data reporting arrangements may also change. The cooperating institution and USAID will need to maintain the benchmark data set in sufficient detail to allow the appropriate adjustments to be made in the reported data.

ANNEXES

ANNEX A. MICROFINANCE INSTITUTIONAL ANALYSES

A brief evaluation of 10 microfinance institutions was completed to guide Activity design. Follows is a brief description of those institutions, which are:

1. Caritas del Peru
2. Crear Arequipa
3. Caja Sur, Rural Savings and Loan of Arequipa
4. Municipal Savings and Loan of Arequipa
5. Edificar
6. FINCA Peru
7. Habitat Trujillo EDPYME
8. Prisma
9. Proempresa
10. Solidaridad

ANNEX A.1 CARITAS DEL PERU

Cáritas del Peru was created as a civil association in 1955 by the Peru Episcopal Conference. The Assembly of Associated Bishops is the controlling body and selects the Board of Directors of Bishops. About 80 % of the Bishops from the 49 Dioceses of Peru have joined the Assembly. The General Secretary directs the operations.

The objective of Cáritas del Peru is to support the pastoral activities of the Church through promotion, coordination and Christian communication in all forms to assist the integral development of the community.

In January 1999 Cáritas joined with Catholic Relief Services and USAID to launch their microfinance program, called PROMESA. Seven offices are participating: Cusco, Sicuani, Ayaviri, Juli, Tarma, San Ramón and Huánuco. PROMESA is located within UGIM, the Unit for Generation of Income and Microcredits. An abbreviated organization of Cáritas of Peru and the UGIM unit is shown in Figure 1.

UGIM has applied for a license to operate as an EDPYME, and has received approval from the SBS to organize the company. Nine months remain for them to complete the organization and receive approval for operations. The EDPYME will be called OMICROM. Cáritas was specifically not chosen as a name to avoid the impression that loans may not need to be repaid.

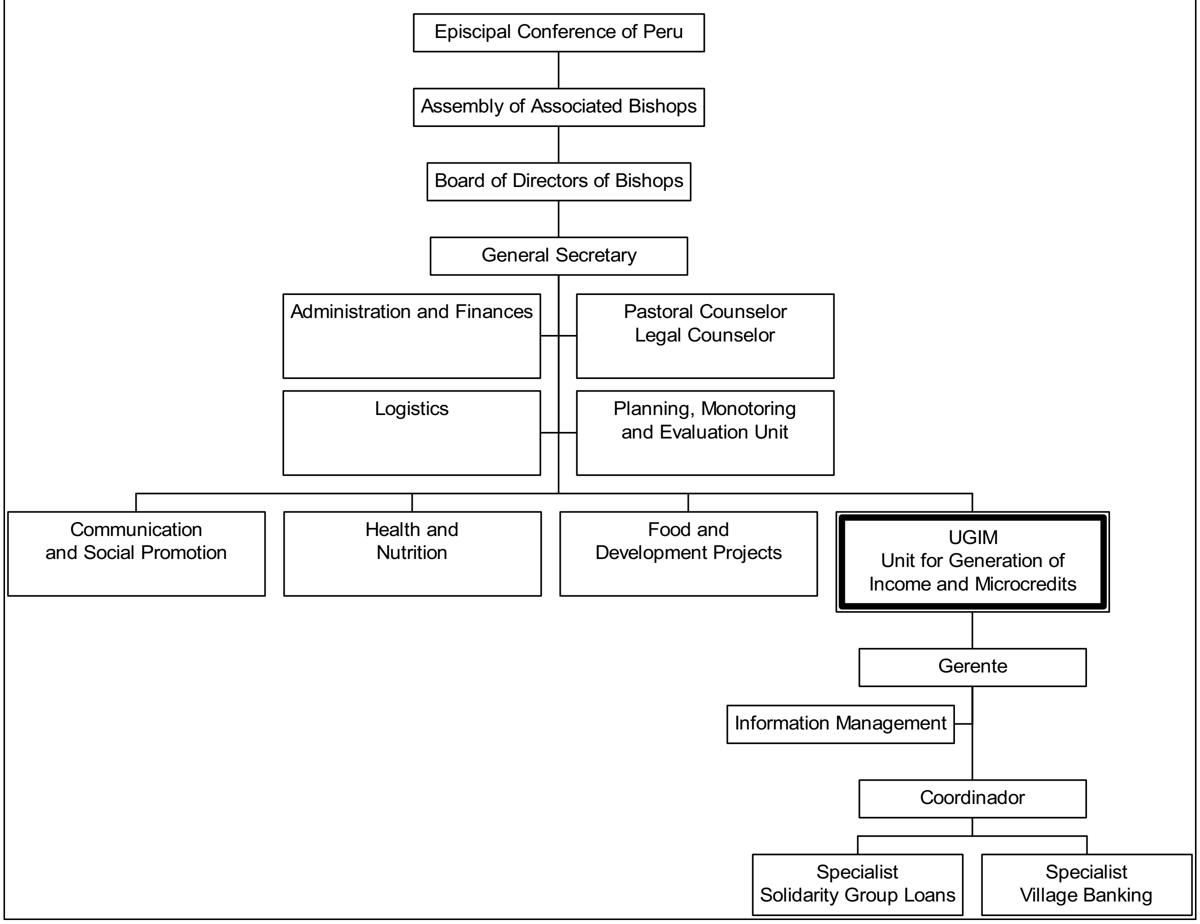
The Bishop of Tacna and Moquegua and First Vice President of Cáritas of Peru, Hugo Garaycoa Hawkins, the moving force behind establishing the micro credit program has also been quite clear that the institution is to be sustainable and its services to be "permanent, recoverable and adjusted to the demands of the clients."

The remainder of this discussion applies primarily to the components and results of the microcredit program PROMESA. Cáritas de Peru hopes to formalize the program of PROMESA into the EDPYME OMICRON and then incorporate the various other microcredit programs operating in Peru into OMICROM.

Credit products: Village Bank, Solidarity Group

Two credit products are offered, village banking and solidarity group loans. The village-banking product is a typical product of village banks, with loans by PROMESA to village bank members and obligated savings, generating an additional internal loan portfolio. Loan cycles may be either 4 or 6 months, and principal payment may be monthly or at the end of the period. Interest must be paid monthly. The interest rate in all cases is 4 % per month. The commission varies between 1 and 3 % depending on the time period and whether principal payments are monthly or balloon payment. Annual effective interest rates range from 75 to 78 %.

Annex A Figure 1. CARITAS OF PERU



The solidarity group product is a small group loan, and like the village bank may be for a period of 4 to 6 months with monthly principal repayments or a balloon principal repayment at the end of the loan. Interest payments are due monthly. Nominal interest rate is 4 % per month. Fees range between 1 and 3 % depending on the type of principal repayment and loan period. Effective annual interest rates range from 68 to 72 %. Maximum amounts that can be borrowed increase as prior loans are successfully repaid.

Loan Portfolio

As of September 2000 the loan portfolio was $1.5 million, with 10, 969 loans, for an average outstanding loan balance per borrower of $ 140. During the year PROMESA disbursed 10,601 loans for a value of $3.72 million, for an average loan size of $ 206. In September there were 58 employees, of which 36 are credit analysts. Thus the average number of credits per analyst were 305, pretty good for so young an institution, and the total loan portfolio per credit analyst was $42,493, relatively low.

Despite the Bishop's pronouncements about the importance of loan collections, there is a problem in this area. In September the portfolio at risk is 14 .7 % of the portfolio with payments late one day or more, and 4.9 % of the portfolio with payments 30 days or more. This repayment rate is poor for village banking. The three offices with the largest portfolios, San Ramon, Tarma and Huanuco have the poorest performing portfolios. Unless collections are improved quickly these offices may not be sustainable.

Management has taken some actions to improve collections, restricting in two offices the ability to make new loans until late payment rates decline. They also report sending special teams to help with collections. Yet there is not in place a system of standards for collections, nor incentive payments for good credit analysts with good collections performance. Nor has management dismissed any credit analysts for poor collections.

Overview of Financial Results

For the fiscal year ended September 2000, PROMESA had net earnings of $364,307, after receiving donations of more than $570,000. Net operating losses were $ 213,317. Financial income was 32.0 % of total loan portfolio, as was gross financial margin, because there were no financial costs.

Operating costs represented 42.7 % of total loan portfolio. Personnel costs were 18.6 % of loan portfolio. Thus, operating losses were 13.9 % of total loan portfolio, offset by donations for operating costs of 37.3 % of the loan portfolio.

Set asides for losses for non-payment of loans represents only 53.6 % of the portfolio at risk. Set aside for loan losses are said to follow the SBS recommendations, but are probably insufficient.

The total loan portfolio of just over $1.5 million appears insufficient to cover operational costs for Caritas. In part this may be due to cost of maintaining operations in too many locations for the size of the portfolio.

Needed Technical Assistance and Training

Caritas needs support at all levels of the institution, perhaps most importantly for directors of the program. The vision elaborated by Bishop Hugo Garaycoa Hawkins appears to be moving Caritas in the proper direction. Technical managers at UGIM also speak the correct concepts of making proper credit decisions, (based more on repayment ability and less on family funding needs), a high level of collections and control of costs to achieve sustainability.

Nevertheless, the institution is in transition and needs considerable support establishing a market oriented business plan and installing sound financial and operational management techniques. Transformation from a charity organization to a financial organization serving a targeted market segment is just beginning, and needs to be communicated forcefully throughout the entire organization, from Assembly of Associated Bishops who function as owners, to directors to administrators to operations staff. Some themes of training might be fiduciary responsibilities of owners and directors, banking operations, managing risks, loan decision making and collections, conducting credit audits, market analysis, strategic and financial planning and others. In short, training is needed in all areas of financial company management.

The institution expresses their appreciation for the support for the process of formalization of the institution and securing the license to operate as an EPDYME, and of course hopes that will continue. This support includes funds for lending, improved infrastructure, improved information systems, training of personnel and support to improve the image of the company.

Until the license to operate as an EDPYME is secured, the institution supports COPEME in their desires to become the institution for self-regulation of microfinance institutions.

A written request for support presented by Caritas is included here:

1. Encuentro de instituciones especialistas en micro finanzas
2. Desarrollo de nuevos productos financieros en el mercado de las micro finanzas
3. Capacitación especializada al personal de la institución de las IMF
4. Pasantías en instituciones especialistas en micro finanzas con éxitos
5. Incluir componentes de capacitación dirigida a clientes de los proyectos de micro créditos
6. Buscar el nexo entre el sistema financiero y las IMFs para palanqueo de recursos monetarios
7. Presentar a las IMFs como organismos lideres en la lucha contra la pobreza
8. Apoyo constante a las actividades de crédito que realiza las IMFs.

Annex A Table 1. Selected Loan Portfolio and Financial Data	
PROMESA (CARITAS NGO)	
Item	**Sep. 00**
Loan Portfolio Data	
Total loan portfolio (US$)	1,529,753
Net loan portfolio (US$)	1,489,879
Loan portfolio a risk > 30 Days (US$)	74,428
Loan Loss reserves (US$)	39,874
Number of loans disbursed in the period	18,022
Amount of loans disubrsed in the period(US$)	3,719,361
Average size of loan disbursed (US$)	206
Number of current loans	10,969
Number of employees	57
Number of credit analysts	36
Financial Data	
Fixed assets (US$)	184,086
Total assets (US$)	2,241,706
Total liabilities (US$)	1,657,560
Total Equity (US$)	584,147
Financial Income (US$)	489,650
Financial Costs (US$)	0
Other Income (US$)	577,624
Total operating costs (US$) *	702,967
Personnel costs (US$)	363,281
Profits (US$)	364,307
Indicators and Ratios	
Total loan portfolio / Total assets	68.2%
Net loan portfolio / Total loan portfolio	97.4%
Loan portfolio at rist / Total loan portfolio	4.9%
Loan loss reserve / Loan portfolio at risk	2.6%
Financial Income / Total loan portfolio	32.0%
Financial costs / Total loan portfolio	0.0%
Gross financial margin	32.0%
Personal costs / Total loan porfolio	23.7%
Total operating costs / Total loan portfolio	46.0%
Profits / Total loan portfolio	23.8%
Profits / Total assets	16.3%
Profits / Equity	62.4%
Total liabilities / Total assets	3.3%
Total loan portfolio / Equity	261.9%
Total loan portfolio / Credit analyst (miles US$)	42,493
Number of current credits / Credit analyst	305
Exchange Rate	**3.515**
* Includys loan loss setaside, depreciation, personnel costs, general admin costs	

ANNEX A.2 CREAR AREQUIPA EDPYME

Crear Arequipa was created in November 1997 and authorized by the SBS and began operations in April 1998. The EDPYME is not yet authorized to capture deposits from the public. Crear Arequipa EDPYME earned its credit experience with 6 years of operations as an NGO. The NGO HABITAT AREQUIPA SIGLO XXI began its credit operations with a support from the Inter-American Development Bank (IDB) of $200,000 for loans and S/490,000 from FONCODES.

From it's beginning the NGO offered credit to micro and small enterprises in the Departments of Arequipa and Puno. Unusual in this early period of microcredits in Peru, the NGO took the position that credits were to be repaid. Consequently they insisted in a reliable evaluation of the client's ability to pay, formal contracts that were enforceable in the courts, real guarantees that were registered and promissory notes by the borrower. With this policy the NGO was able to show high collection rates, which continue to the present in the EDPYME.

Today Crear Arequipa has more than 2,300 customers with a total loan portfolio of just over $ 2 million. Average loan size is about $1,000.

Ownership

Crear Arequipa EDPYME is a stock corporation owned by the NGO Habitat Arequipa Siglo XXI and by 7 other private persons. The NGO Habitat owns 26 percent of the shares; two private persons associated with the NGO own 26 and 23 percent respectively; a private socially oriented foreign person owns 23 percent, and the remaining 3 percent is owned by four private persons.

A board of seven Directors represents the shareholders. Key executives come from the NGO and from local banks. Both the General Manager, and Credit Manager have bank and well as NGO experience. The administrative organization is shown in Annex A Figure 2.

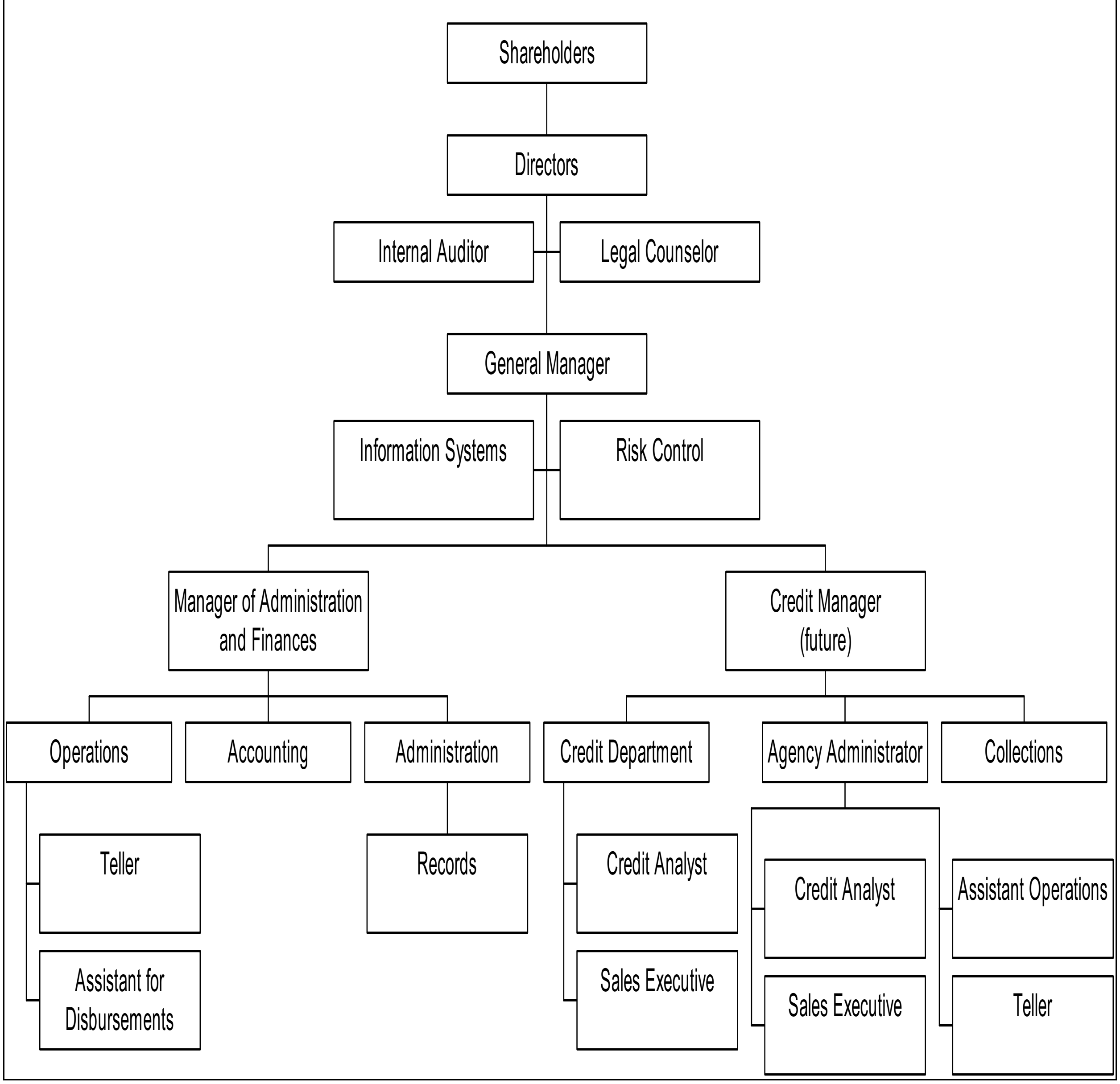
The company operates from modest but adequate central office in Arequipa's central business district, and one satellite office in Arequipa.

Credit products

Crear has only one credit product that of individual credits, but with a variety of options for destination of the credit, and with varying conditions for interest rate, loan period and other conditions. For credits in Soles the most common interest rates are 4.0 % and 4.2 % per month. There are also a significant number of credits priced at 5.0 % per month. For credits in dollars the most frequent number of credits are priced at 2.5 % per month. For October 2000 the average interest rate for all loans was equivalent to 3.9 % in Soles.

Loans are available for consumers, micro business and individuals.

Annex A Figure 2. CREAR AREQUIPA EDPYME



The Market

Crear Arequipa is concerned about saturation of the micro credit market in Arequipa, as well as in cities and towns in the region. In the last two years many additional institutions have entered the market served by Crear. They consider it will be difficult to gain market share where they now offer services. Solucion and the Municipal S&L can better serve the market for larger credits, because their greater access to funds. Crear does not yet have an effective product to arrive at those clients who want loans less than $400. Their tendency is toward smaller loan amounts, but not yet so small.

The solution for management of Crear is to look toward Lima for additional market. Consultation to the SBS has indicated such a request would be approved, of course with the proper administration and evaluation of the market there. Opening an office in Lime would require at least $1 million of additional funds for lending. To secure that amount of funds will likely require an increase in equity by investors. The NGO Habitat does not have available funds to invest, so other institutions or private persons would need to be approached for investment. Management felt current owners or others in the community would match any investment in equity provided by donors; but potential investors seemed less motivated to invest now without greater incentives.

Loan Portfolio

The total loan portfolio to September 2000 is just over $2 million, an increase of 26 percent from December 1999, which then was an increase of 29 % over December 1998. This rate of growth is often seen in microfinance institutions with sufficient funding. This rapid growth also helps keep late payment rates lower.

Net loan portfolio is 87 % of total loan portfolio in September, the same in December 1999 and 79 % in December 1998. This is relatively high and consistent across the three observations here, compared to most microfinance institutions that have a highly variable percent of funds in the loan portfolio depending on when lendable funds are received.

Average size of loan disbursed is about $1,000 and has remained constant over the last three years. Loans are utilized for commerce (44 %), production (32 %), and for services (24 %). From earlier years there are now fewer commerce loans and more services loans.

During 1999 Crear Arequipa disbursed 2,720 loans, 96 % in local currency. The number disbursed in 2000 will be slightly higher, still with almost all in local currency.

Portfolio at risk is 8 % in September, up from 5.9 % the previous December and up from 1.6 % from December 1998. Loan loss reserve as a share of portfolio at risk is 91 % and appears to be adequate. No loans were written off in 1998 and 1999; in 2000 loan write-offs represented 6.4 % of the total loan portfolio. This amount of write-off is high, unless it comes from delayed write-offs that should have been done in prior years.

The loan portfolio per credit agent is $145,958, about midrange for many micro credit programs. That amount is, however, down 42 % from December 1998 when it was $251,614 per credit analyst. Likewise the number of current loans per credit analyst is 163, down 36 % in the same period. Between December 1999 and September 2000 the number of credit agents has increased from 18 to 24. While credit analysts increased by 6 during this period, total employment increased by only 5. As a result, in December 1999 the credit analysts represented 42 % of company employees, in September 2000 credit analysts represented 58 % of company employees.

Overview of Financial Results

Financial income for Crear Arequipa was$636,571 in 1999, 39.3 % of the total loan portfolio. Financial costs were low, $119,926 or 7.4 % of the loan portfolio. Thus the gross financial margin is 31.9 % of loans.

Operating costs were $359,554 in 1999, 24.4 % of the loan portfolio, perhaps a bit high for an institution at the level of development and providing the mix of loans as does Crear Arequipa. Costs in 1998 were reported at only 14.4 % of the loan portfolio; the level of costs for the year 2000 appear to be more in line with those of 1999. Profits were $72,329 and represented a return on assets of 3.9 % and a return on investment of 18.4 %, respectable compared to other microfinance institutions visited in Peru. Profits to September 2000 are considerably higher than in 1999.

Leverage, that is total loan portfolio divided by equity, is 3.95 in September. This is a level not generally reached until nearly a decade of experience in micro credit.

Debts total US$1.9 million. All debts are with donors and other institutions that provide funds for development institutions. Forty five percent of liabilities are denominated in U.S. dollars, the rest in Soles. The currency of the loan portfolio appears not to be in line with the currency of the liabilities. One loan representing 37 % of the liabilities returns the interest earned to Crear Arequipa to help cover costs and maintain the value of the fund.

Needed Technical Assistance and Training

Crear Arequipa has a capable management team in place. They are lending in a crowded market, competing with the Municipal S&L, Solución, the CajaSur (Rural S&L) and some banks. In fact, they see the market in Arequipa as saturated, as well as the markets in the surrounding towns. They are looking to Lima as a market less saturated. However, they do not have sufficient funds to open an office there.

The management requested support from donors in three ways, an equity investment, a source of funds and technical assistance especially for information systems.

Until now it does appear that the lack of additional funds has severely restraining the portfolio growth of Crear Arequipa. According to management, however, future growth will be restricted. Unless their use is restricted, new funds would most likely be directed towards opening a Lima office.

The company is working on improving their operations and skills, to be able to secure a B+ or better rating that would allow them to capture deposits from the public. They consider that review to be two years or more in the future.

The information system is written in Visual Fox Pro, is adequate for now, but will need an upgrade as the institution becomes more sophisticated.

Crear Arequipa may benefit also from a better understanding of their market, and how to adjust their products to generate additional demand in the region they now serve.

Potential of Working with Donors

Crear Arequipa provides loans of about $1,000. They consider it difficult to reach the market of loans for $400. They would need to develop new products. They also consider they cannot go upscale, because Solucion and the Municipal S&L of Arequipa has greater resources (funds) to address this market. They claim the market is forcing them to go more to smaller loans.

There is little to recommend for use by USAID for poverty lending, unless they develop new product for smaller loans. They would be a medium level interest as a sustainable microfinance company. But they may not be able to reach so many clients as some other lenders. However, they would rank above some other EDPYMEs in terms of credit risk. Crear Arequipa does not necessarily require infusion of new funds, either for credit or investment. But their growth will be relatively slow until they qualify to capture deposits or they secure additional funding sources. Qualifying for deposit taking could take up to 3 or 4 years without technical assistance. Or if they had additional low-cost funds, they could purchase part of their own technical assistance. By then the market may have changed substantially.

They could benefit from technical assistance for strategic planning, market analysis and for new product development, in addition to the support for improved information system mentioned above. As they prepare for the application to capture deposits, they will need a wide range of support, such as review of and adjustment of operations, preparation of manuals, additional investment in security of offices and others.

Annex A Table 2. Selected Loan Portfolio and Financial Data			
CREAR AREQUIPA EDPYME			
Item	**Sep. 00**	**Dec-99**	**Dec-98**
Loan Portfolio Data			
Total loan portfolio (US$)	2,043,418	1,621,333	1,258,072
Net loan portfolio (US$)	1,894,608	1,510,086	1,243,375
Loan portfolio a risk > 30 Days (US$)	162,809	95,818	20,234
Loan Loss reserves (US$)	148,809	111,247	14,696
Number of loans disbursed in the period	2,353	2,631	1,553
Amount of loans disubrsed in the period(US$)	2,344,005	2,533,638	1,742,399
Average size of loan disbursed (US$)	996	963	1,122
Number of current loans	2,276	1,767	1,280
Number of employees	24	19	14
Number of credit analysts	14	8	5
Financial Data			
Fixed assets (US$)	59,245	43,311	35,463
Total assets (US$)	2,354,979	1,861,797	1,587,859
Total liabilities (US$)	1,837,706	1,468,219	1,249,201
Total Equity (US$)	517,273	393,578	338,658
Financial Income (US$)	631,667	636,571	249,840
Financial Costs (US$)	112,437	119,926	44,409
Other Income (US$)	16,988	1,574	5,751
Total operating costs (US$) *	371,314	395,554	181,789
Personnel costs (US$)	143,380	161,651	99,361
Profits (US$)	108,133	72,329	14,377
Indicators and Ratios			
Total loan portfolio / Total assets	86.8%	87.1%	79.2%
Net loan portfolio / Total loan portfolio	92.7%	93.1%	98.8%
Loan portfolio at risk / Total loan portfolio	8.0%	5.9%	1.6%
Loan loss reserve / Loan portfolio at risk	91.4%	116.1%	72.6%
Financial Income / Total loan portfolio	30.9%	39.3%	19.9%
Financial costs / Total loan portfolio	5.5%	7.4%	3.5%
Gross financial margin	25.4%	31.9%	16.3%
Personnel costs / Total loan portfolio	7.0%	10.0%	7.9%
Total operating costs / Total loan portfolio	18.2%	24.4%	14.4%
Profits / Total loan portfolio	5.3%	4.5%	1.1%
Profits / Total assets	4.6%	3.9%	0.9%
Profits / Equity	20.9%	18.4%	4.2%
Total liabilities / Total assets	78.0%	78.9%	78.7%
Total loan portfolio / Equity	395.0%	411.9%	371.5%
Total loan portfolio / Credit analyst	145,958	202,666	251,614
Number of current loans / Credit analyst	163	221	256
Exchange rate	**3.515**	**3.48**	**3.13**

* Includes loan loss reserves, depreciation, personnel costs and general administrative costs

ANNEX A.3 RURAL S & L OF AREQUIPA - CajaSur

Rural Savings and Loan of the South - Arequipa (trade name CajaSur) began operations in December 1993 with the purpose to capture public deposits and provide financing directed to medium, small and micro businesses in rural areas. Headquartered in Arequipa, the company provides services from its central office and from offices in the towns of Camaná, Mollendo, Corire and Pedregal.

CajaSur is a stock corporation organized under the law No. 25612 and directed primarily by two principal family groups of investors, and also by a group of about 3,000 small amount shareholders. The owners select five people to serve on the Board of Directors, plus four outside directors are invited to participate. Currently these outside directors are a banking specialist, a manager of an insurance company, a medical doctor who also is active in economic development in the region; and a local businessman. Two of the director positions are vacant, because of observations by the SBS.

Overall administration of the company is provided through the General Manager, with other key positions being the Chief Administrator and Accountant; the Chief of Supervision of Credits and Collections, Chief of Operations, and the Chief of Information Systems. Annex A Figure 3 shows the organizational structure for CAJA SUR.

CajaSur selects two people who are responsible leaders in each community where there is an office to serve as Delegated Directors. These people help by providing local information to Agency officials to improve decisions about credits. They do not participate in the Board of Director meetings.

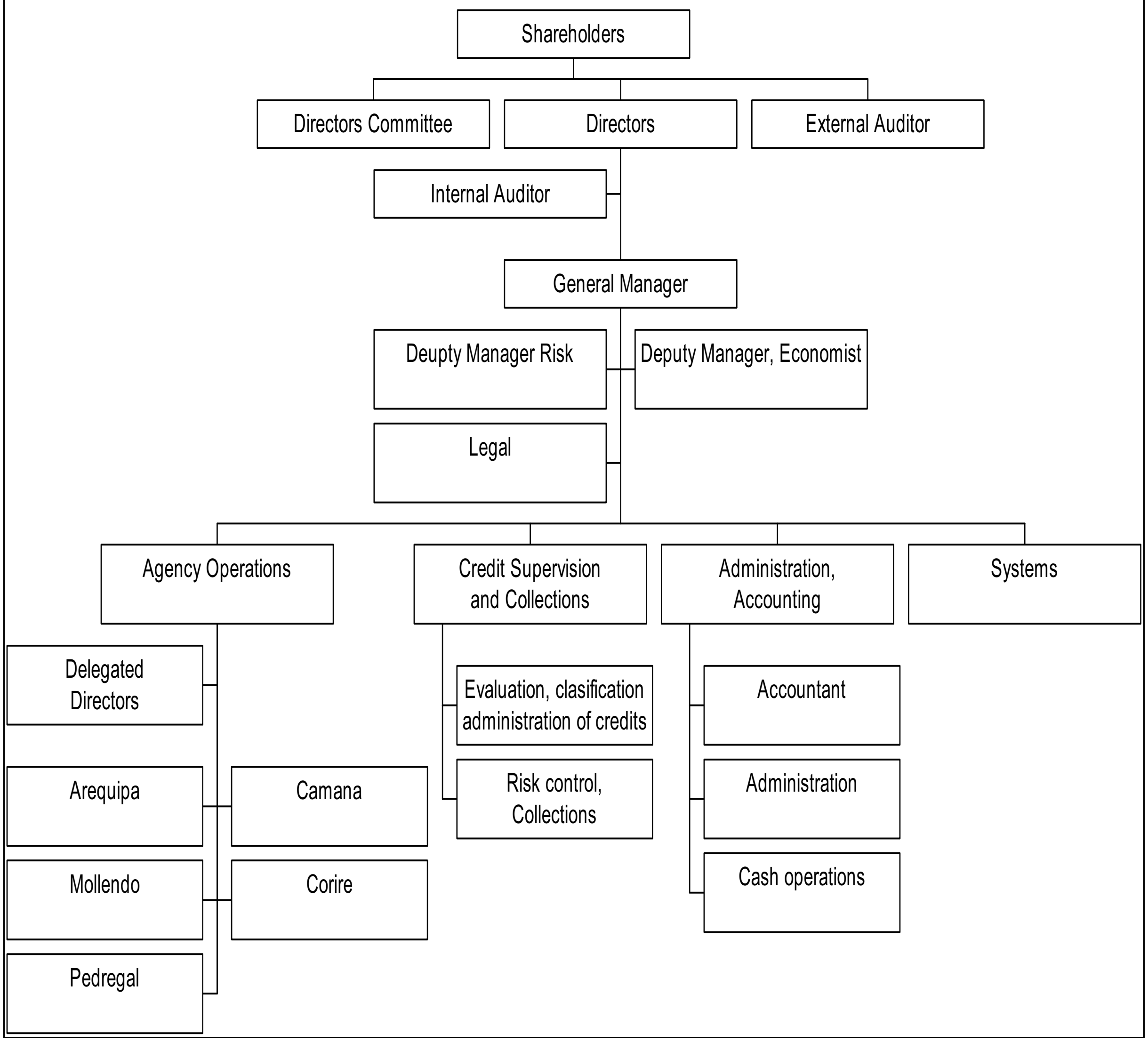
Credit products

Credits are all individual. Dollar denominated loans account for 92 percent of credits disbursed in 2000, soles for 8 %. Loans are given for:

- Agriculture, 78 %
- Micro enterprises, 10 %
- Consumer, 8 %
- Multisector, 2 %
- Mortgage, 2 %.

The company is trying to reduce the share of credits for agriculture, which in prior years was about 90 % of disbursements. The reduction is progressing slower than planned. Average amount disbursed per loan is about $1,000.

Annex A Figure 3. CAJA SUR, AREQUIPA



Financial income as a percent of the total loan portfolio was 28.2 % in 1999. This is low for a microfinance institution at this stage of development of the company and the market.

Lending to organized groups is a relatively new product. An example would be a loan to a community to purchase a tractor, or to invest in irrigation infrastructure. These loans are usually in the $30,000 to $80,000 range. The loan is secured with real guarantees, and all members of the group must sign the loan, including their spouses.

Operations

CAJA SUR considers its strength on lending in rural areas. Management notices the commercial banks are closing their offices in the towns served by CAJA SUR, and the company expects more Banks to leave. So far only a few microfinance institutions have entered the small towns and rural areas where CAJA SUR provides financial services. The company expects to increase operations in urban areas such as Arequipa, but does not expect their growth in urban markets to match the growth of competitor microfinance institutions, which have more funds, more experience in that market, and more physical facilities to serve customers. They do expect to become an important provider of financial services in rural areas and small towns.

The administration of CajaSur demonstrated much greater understanding of rural markets, with knowledge of which are profitable and which are not, and expressed a much greater optimism about being able to successfully serve these areas than did administrators of most other institutions visited.

New promotion for savings products has focused on what they call products to serve the family. For example, a savings account oriented to children called "New Savings" has a special passbook and pays one percent more than standard savings. Another product encourages savings for home improvements, and another trying to promote certificates of deposits.

Negative Political Actions

The management expressed great concern about the impact of the actions by the GOP, hindering CajaSur's ability to collect its loans. The GOP policy is to allow certain borrowers the option of renegotiation the repayment of their loans, an action which results in most borrowers stopping payments. Because most of these loans were financed through COFIDE, CajaSur has requested relief from its repayment obligations. No information is available on when a decision may be available. Meanwhile, default rates on these loans continue to rise.

Not only has the renegotiation policy affected collection of specific loans, it has also had the affect of causing greater uncertainty in the region, both for the borrowers and for CajaSur. In addition, suggestions by some that a development bank will be started, and promises by those running for political offices that loans will be forgiven, or interest rates reduced, or repayment periods increased further increases incentives for default. Talk of a rural bank causes some to become confused, thinking that the Rural S&L's are those banks, and some borrowers now expect favorable treatment.

As a further example, last April Caja Rural de Ahorro and Credito de Arequipa established the trade name CajaSur, which it uses on its buildings, on all advertising materials and all of its correspondence. A major motivating factor was an effort to communicate to customers that the company was not part of the government. As a result, they claim, savings mobilization has improved significantly.

To improve future prospects, CAJA SUR is cultivating relationships with two other regional rural S&L's. Initially relationships would be informal such as cooperating in training, purchase of supplies or services as auditing or software, and others. If successful, more formal arrangements could be developed such as information sharing, money transfers, interchange of payments or others. Ultimately mergers could result.

Loan Portfolio

The loan portfolio stands at $6.8 million in August 2000, and was about the same as in December 1998.

Loan collections have been a continuing problem for CajaSur. Portfolio at risk in August 2000 stood at 22.9 %, was 13.0 % at the end of 1999 and 17.9 % at the end of 1998. October and November has seen small reductions in portfolio at risk. The company hopes to end the year 2000 with portfolio at risk less than 15 %.

Of late the company is suffering from the Peruvian Government program to require renegotiation of loans taken by selected borrowers. To date 135 borrowers with a total outstanding loan balance of about $700,000 have entered into this program and are not currently paying their loans pending a renegotiation with CajaSur. Renegotiation efforts by administrators of CajaSur and the borrowers have been unsuccessful. Currently CajaSur is requesting the GOP through COFIDE, who provided the funds involved in this program, to restructure the repayment plan for CAJA SUR to match what the borrowers are requesting. No near-term resolution of this issue is expected. Meanwhile the loans continue to account for about half of the portfolio at risk of CajaSur.

Loan loss reserves in August were $0.9 million, and represent 58 % of past due portfolio. Most of the portfolio is partially protected by loan guarantees issued by FOGAPI, which probably reduces the need for provisions. Even so, reserves appear to be low, unless somehow CajaSur achieves forgiveness of repayment of its loan obligations to COFIDE that are associated with the defaulting agricultural borrowers entering the repayment program.

CajaSur has a total of 50 employees, but only 10 assigned as credit analysts. This represents an average of 268 clients per credit analyst, and a loan portfolio of $762,000, extremely high compared to most microfinance institutions. It may be that the 10 reported credit analysts do not include those supervisors or others directly supporting the credit analysts, and that more than 10 employees are directly involved in credit operations. Typically about one third of employees are directly involved in credit operations.

Overview of Financial Results

In August total assets were $10.7 million, liabilities of $8.9 million and equity of $1.9 million. Liabilities are 4.8 times equity.

Earnings are positive, $278,000 in 1999 and $116,000 to August 2000. For 1999 financial income is 28.2 % of loan portfolio and financial costs are 7.2 %, for a gross financial margin 21.0 %, relatively low compared to most microfinance institutions in Peru. Fortunately, total operating costs are also lower than most microfinance institutions, 13.7% of loan portfolio.

Profits represent 2.8 % of total assets, a respectable achievement, and 16.0 % of equity, better than most microfinance institutions in Peru. CajaSur has achieved a leverage of its equity to loan portfolio of 4.37 times.

Needed Technical Assistance and Training

CAJA SUR suggested several areas of support from donors that would enhance their ability to serve their customers.

1. Ability to source lower-cost funds to enhance its ability to expand loans to customers in rural areas.
2. Training. A series of help is needed, including most of the skills to run a modern financial institution, such as financial institution mathematics, internal controls, control of risks, financial management, technical skills of operations, credit analysis and many others.
3. Technical assistance in specific operations, such as marketing, product development, software, financial management. others.
4. Support for political leaders to develop and sustain appropriate policies and regulations for development of the financial sector and the economy in rural areas and small towns.
5. Support for group of rural S&Ls to secure services of internationally recognized external auditor.

The reviewing microfinance specialist concurs with items 2 to 4 above. Support for item 4 would be directly by USAID and not through the CajaSur.

If one views the supply of savings services as a useful product for rural residents, support for item 1 would likely decrease, rather than increase, economic utility for rural residents. Better CajaSur accelerate its development of savings products. In particular it will need more emphasis in products that increase the length of time savings are left in the institution, so the company can more nearly match savings with the time period most rural customers ask for loans.

Support for item 5 should be dependent on a decision by the owners of CajaSur and the GOP that the institution will be privatized and become an institution independent of the government and not subject to government control through its ownership. If such is the case, USAID support for an internationally recognized auditor may be warranted to support the process of privatization, not as an ongoing support.

Capabilities of Working with Donors

CajaSur is interested in working with donors to improve the institution's ability to reach additional customers. For donors that wish to serve agricultural producers, they may want to consider CajaSur. Also the company is more focused on serving the smaller or mid sized towns where commercial banks are reducing their presence. Even most of the EDPYMEs are not comfortable enough in their understanding of rural markets to try to begin operations there.

Of the companies interviewed, CAJA SUR was most knowledgeable about the various agricultural crops or products by region that were sufficiently profitable to justify lending. For a donor that wishes to reach agricultural markets, at least this rural S&L could be a useful companion institution.

Some difficult elements to overcome would be the high level of late payments. While higher default rates for temporary periods are understandable in agricultural lending, the levels shown by CajaSur seem excessive. Even eliminating the recent late payers caused by action of the GOP, default rates are too high.

The actions by the GOP may also be a limitation. Until that situation is resolved, and some understanding is achieved about future such acts, lending through the rural S&Ls carries extremely high risks.

Annex A Table 3. Selected Loan Portfolio and Financial Data			
Rural Savings and Loan of Arequipa (CajaSur)			
Item	**Aug-00**	**Dec-99**	**Dec-98**
Loan Portfolio Data			
Total loan portfolio (US$)	6,791	7,616	6,751
Net loan portfolio (US$)	5,869	6,879	6,309
Loan portfolio a risk > 30 Days (US$)	1,552	989	1,208
Loan Loss reserves (US$)	-922	-737	-442
Number of loans disbursed in the period	3,489	3,452	3,727
Amount of loans disubrsed in the period(US$)	2,845	3,064	3,200
Average size of loan disbursed (US$)	815	888	859
Number of current loans	2,829	2,679	2,861
Number of employees	52	50	53
Number of credit analysts	13	10	12
Financial Data			
Fixed assets (US$)	729	709	669
Total assets (US$)	10,711	9,845	9,294
Total liabilities (US$)	8,859	8,307	7,467
Total Equity (US$)	1,853	1,741	1,410
Financial Income (US$)	1,232	2,147	1,936
Financial Costs (US$)	-410	-549	-587
Other Income (US$)	176	38	81
Total operating costs (US$) *	-672	-1,045	-934
Personnel costs (US$)	-301	-437	-422
Profits (US$)	116	278	203
Indicators and Ratios			
Total loan portfolio / Total assets	63.4%	77.4%	72.6%
Net loan portfolio / Total loan portfolio	86.4%	90.3%	93.4%
Loan portfolio at rist / Total loan portfolio	22.9%	13.0%	17.9%
Loan loss reserve / Loan portfolio at risk	-59.4%	-74.5%	-36.6%
Financial Income / Total loan portfolio	18.1%	28.2%	28.7%
Financial costs / Total loan portfolio	-6.0%	-7.2%	-8.7%
Gross financial margin	12.1%	21.0%	20.0%
Personal costs / Total loan porfolio	-4.4%	-5.7%	-6.2%
Total operating costs / Total loan portfolio	-9.9%	-13.7%	-13.8%
Profits / Total loan portfolio	1.7%	3.7%	3.0%
Profits / Total assets	1.1%	2.8%	2.2%
Profits / Equity	6.2%	16.0%	14.4%
Total liabilities / Total assets	82.7%	84.4%	80.3%
Total loan portfolio / Equity	366.6%	437.4%	478.9%
Total loan portfolio / Credit analyst (miles US$)	522	762	563
Number of current credits / Credit analyst	218	268	238
Tipo de Cambio	**3.515**	**3.48**	**3.13**
* Includes loan loss reserve, depreciation, personnel costs and general costs.			

ANNEX A.4 MUNICIPAL S & L OF AREQUIPA

The Municipal Savings and Loan of (CMAC Arequipa) began operations in 1986, under the Supreme Degree 157-90 EF, which authorized the creation of the Cajas Municipales. CMAC Arequipa is 100 % owned by the Municipality of Arequipa. The company captures deposits from the public, makes loans and offers other financial services.

A Board of seven Directors governs the company. Three Directors are appointed by the Municipality of Arequipa, two serve with the group of majority shareholders and one serves with the minority group of shareholders. One director is a representative of the Chamber of Commerce and Industry, one is a representative of the Clergy, one is a representative of micro and small businesses and is suggested by the Chamber of Commerce and Industry, and one is appointed by COFIDE or the Banco de la Nación.

Three persons share the top level of administration of CMAC, one with primary responsibility for credits, one with primary responsibility for administration and one with primary responsibility for savings. Three other key executives provide support for the area of operations (Sub Manager of Operations), Chief of the Risks Unit, and Chief of Accounting.

Credit Products

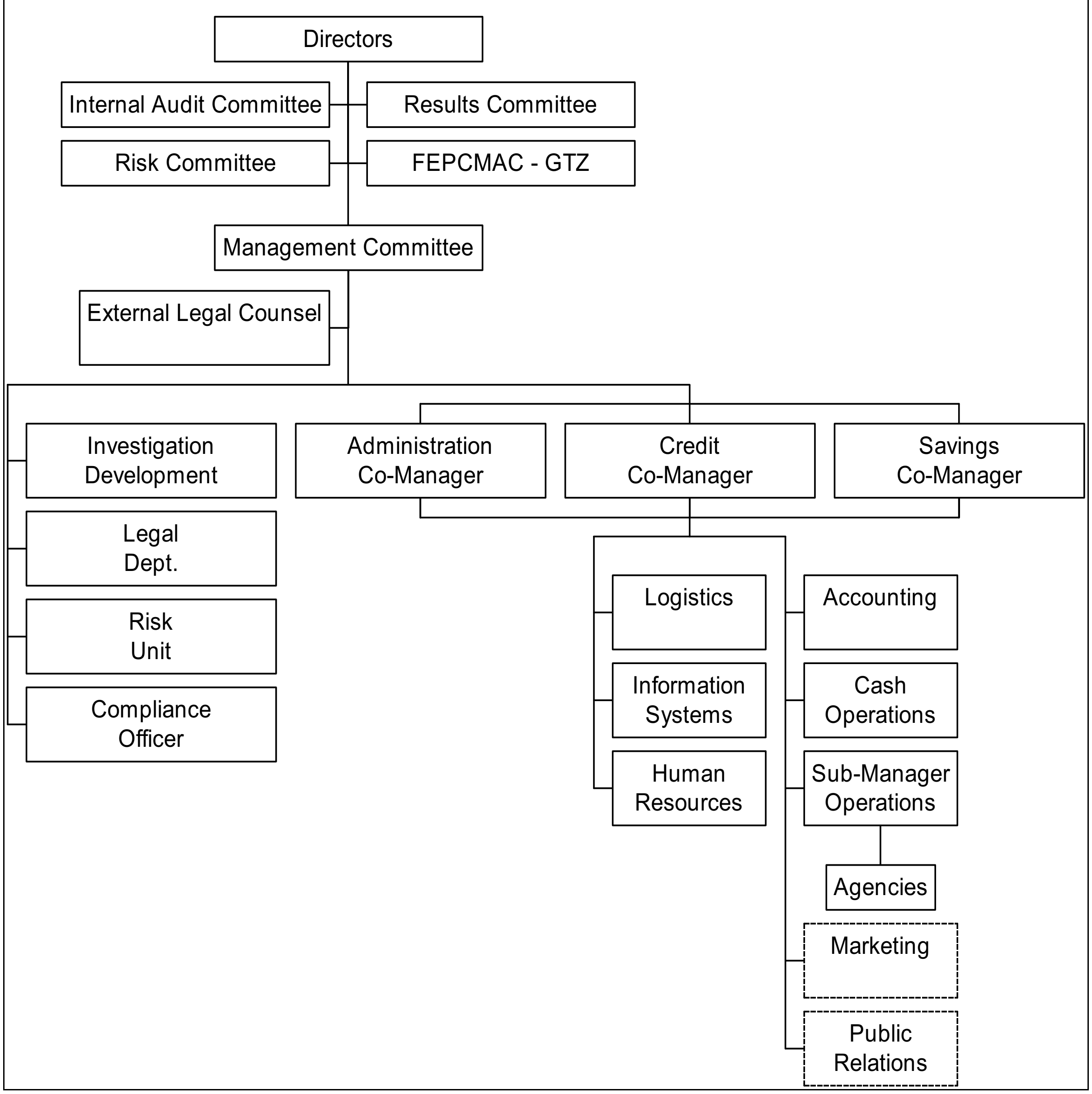
CMAC of Arequipa has 4 credit products, as follows:

1. Small and medium sized enterprise credit for working capital or for acquisition of fixed assets. The applicant must be in business for at least 6 months.
2. Personal credit for whatever purpose, with various operating modes and types of guarantees. Guarantees may be personal, existing deposit in the institution, or real assets. Repayments may be discounted from a wages for workers in certain companies. Credit for purchase of an automobile is included here.
3. Credit for agricultural production and fixed assets for agricultural producers. Requires at least 3 years of experience.
4. Gold backed loans are based on the value of the gold, usually jewelry, offered as security. Disbursements are immediate and funds may be used for whatever purpose.

Loans are offered in Soles and in US dollars.

Interest rates for loans are variable depending on the currency, amount borrowed, in some cases the loan term, when the interest is paid and type of guarantees offered. The average interest rate for loans as of October was 3.4 % per month in national currency. The highest average rate was for gold backed loans of 5.37 % per month. The lowest rate was for agricultural production loans at 3.24 % per month.

Annex A Figure 4. CAJA MUNICIPAL DE AHORRO Y CREDITO AREQUIPA



The average size of loans disbursed ranged from US$247 for gold backed loans, to US$us7,617 for agricultural production loans.

Small enterprise loans accounted for 75 % of the outstanding balance of loan portfolio, followed by personal loans for 18 %, agricultural production loans for 4 % and gold backed loans for 3 %.

The default rate was highest for agricultural production loans, nearly half the outstanding balance is late paying. CMAC Arequipa is reducing the amount of agricultural loans. The best paying loans are personal loans in Soles. Overall the default rate is 13.7 percent for payments 30 or more days late, not a good number compared to most microfinance institutions.

Annex A Table 4A. Types of loans, outstanding balances, number, average amount disbursed and interest rates, October 2000.						
Loan type	**Cur-rency**	**Outstanding balance (thousands)**	**Number active clients**	**Default rate 30 days**	**Average amount disbursed**	**Weighted average monthly interest rate**
Small enterprise	Soles	50,964	18,933	10.25 %	3,676	4.31 %
	$us	12,558	3,172	16.79 %	6,061	2.14 %
Personal	Soles	19,038	8,691	5.25 %	2,643	3.78 %
	$us	1,059	552	13.02 %	2,913	1.89 %
Agriculture production	Soles	2,710	425	12.06 %	7,255	4.34 %
	$us	721	134	48.42 %	7.617	2.05 %
Gold backed	Soles	3,292	14,771	26.25 %	247	5.37 %
Total/average		126,184	46,678	13.07	175,783	3.40 %

Loan Portfolio

The loan portfolio totaled US$36 million in October 2000, up 22 % from December 1999, and December 1999 was up 16 % over December 1998. As of October 2000, the percent of loans for each product were as follows:

- Small enterprise 75.2 %
- Personal 18.7 %
- Agricultural production 3.9 %
- Gold backed 2.5 %.

Disbursements in the year 2000 have been 48 % in U.S. dollars and 52 % in Soles. Earlier periods saw most disbursements in U.S. dollars.

For the year 1999 CMAC disbursed 78,922 loans, 34 % more than the year before. The number of loans disbursed in 2000 will likely be slightly more than in 1999.

The number of loans outstanding is also increasing, from 38,685 in December 1998, to 40,637 in 1999 (up 5.1 %), and to 46,678 in October 2000 (up14.9 %).

At the end of October, CMAC Arequipa reports a 6.0 % share of the loan placements in the financial system of Arequipa, up from a 3.4 % share of loan placements in December 1998.

The portfolio at risk for payments in arrears more than 30 days is 5.2 % in October 2000, up from 4.7 % in December 1999 but about the same as December 1998 (5.1 %). Loan loss provisions were 116 % of portfolio at risk in October 2000. Reserves are higher then most institutions, but are down from previous periods.

Loan write-offs have been relatively high for 1998 and 1999, 4.8 and 4.9 % of the total loan portfolio respectively. Through October 200 the loan write-off has been lower, 1.4 % of the outstanding loan portfolio.

Deposits From the Public

As of October 2000 CMAC Arequipa had 36,313 savings accounts, 941 CTS (compensation for time in service) accounts, and 4,426 time deposit accounts. Deposits from the public totaled US$4.14 million, of which 38 % were in the form of savings accounts, and 62 percent were time deposits. Deposits from the public are increasing, causing excess liquidity. CMAC Arequipa responded recently by reducing the rates paid for savings. The company reports is has 8.2 % of the deposits in the financial system of Arequipa, up from 4.4 % in December 1998.

Overview of Financial Results

CMAC Arequipa is the most profitable of the ten financial institutions reviewed, with a 21.3 % return on equity in 1999, and the return in 2000 will probably be similar. Return on assets was 2.1 % in 1999, lower than most microfinance institutions because of the greater leverage of equity. In October 2000 the loan portfolio represented 6.6 times equity, and total assets were 9.6 times equity. Few microfinance institutions reach this level of leverage.

Financial income for 1999 was 35.5 % of the loan portfolio, while financial costs were 14.9 %, for a gross financial margin of 20.6 %. Operating costs were 17.8 % of the loan portfolio, low for microfinance institutions, and especially so considering the average size of loan made of US$591. Profits were 3.1 % of total loan portfolio.

The loan portfolio per credit analyst stood at US$444,144 as of October 2000, an outstanding result. Most microfinance institutions reviewed had loan portfolios per credit analyst much lower. Each credit officer administered on the average 579 active credits, also much higher than other microfinance institutions. Much of this is accounted by the extremely efficient administration of the gold backed loans, where two officials administer 14,771 credits. For the small and medium size loan product, there were 22,105 loans outstanding administered by 68 credit analysts, for an average of 325 each, still one of the best observed in Peru.

Total assets of CMAC Arequipa are US$52 million. The loan portfolio is US$46 million and represents 69 % of total assets. Liquid assets represent 26.8 % of total assets, up two percentage points from December 1998. Equity stands at $ 4.5 million as of October 2000. Earnings for the period were just over $ 1 million, already an increase of about 20 % over last year’s earnings.

Deposits from the public are increasing as a percent of liabilities. In December 1998 savings accounts and certificates of deposit from the public represented 58 % of total liabilities, while in October 2000 savings accounts and certificates of deposits from the public represented 77 % of total liabilities.

Capabilities of Working with Donors

CMAC Arequipa has long experience of working with donors, receiving support from GTZ during more than a decade when that donor was supporting the Municipal S&Ls. Accounting and management information systems appear adequate, operational procedures are in place for relatively efficient operations. The CMAC has the best risk identification and evaluation system of all the institutions observed in Peru for this activity.

The administrative team appears capable and has a focus on leading the institution to acquire private sector investors, which will permit expansion of the company. That expansion could be within or without the region of Arequipa.

The process of adding private investors may be subject to manipulation as different economic interests attempt to acquire interests in the company (not only CMAC Arequipa) on favorable terms. Political support in this area could be helpful.

Support Needs

It appears that CMAC Arequipa has been able to take advantage of the technical support of GTZ over many years. The company is largely self-sufficient for its own operations, with sufficient income to acquire additional capital if the ownership structure is changed. Mostly CMAC Arequipa can pay for technical assistance and training. Donors could be attentive to specific needs during the process of privatization and acquiring additional investors, especially in the areas of public policy as it applies to the process of privatization.

Annex A Table 4B. Selected Loan Portfolio and Financial Data			
MUNICIPAL SAVINGS AND LOAN AREQUIPA			
Item	**Oct-00**	**Dec-99**	**Dec-98**
Loan Portfolio Data			
Total loan portfolio (US$)	35,975,630	29,045,136	24,964,705
Net loan portfolio (US$)	33,774,235	27,345,671	22,967,253
Loan portfolio a risk > 30 Days (US$)	1,862,276	1,374,026	1,261,804
Loan loss reserves (US$)	-2,167,032	-1,667,163	-1,950,845
Number of loans disbursed in the period	67,263	78,922	58,722
Amount of loans disubrsed in the period(US$)	47,835	46,638	43,442
Average size of loan disbursed (US$)	711	591	740
Number of current loans	46,678	40,637	38,685
Number of employees	201	193	164
Number of credit analysts	81	74	63
Financial Data			
Liquid assets (US$)	13,912,546	11,025,772	8,575,002
Fixed assets (US$)	1,882,286	1,951,657	1,985,765
Total assets (US$)	51,956,066	43,397,741	34,737,311
Total liabilities (US$)	46,526,666	39,154,780	31,221,681
Total Equity (US$)	5,429,400	4,242,960	3,515,630
Financial Income (US$)	10,738,677	10,301,311	9,617,382
Financial Costs (US$)	-4,443,116	-4,314,354	-3,473,983
Other Income (US$)	6,295,561	5,986,957	6,143,399
Total operating costs (US$) *	-4,525,433	-5,183,906	-4,467,945
Set aside for bad loans (US$)	(770,306)	(556,930)	(857,339)
Personnel costs (US$)	-1,926,013	-2,155,890	-1,653,258
Profits (US$)	1,076,964	902,431	824,259
Indicators and Ratios			
Total loan portfolio / Total assets	69.2%	66.9%	71.9%
Net loan portfolio / Total loan portfolio	93.9%	94.1%	92.0%
Loan portfolio at risk / Total loan portfolio	5.2%	4.7%	5.1%
Loan loss reserve / Loan portfolio at risk	116.4%	121.3%	154.6%
Liquid assets / Total assets	26.8%	25.4%	24.7%
Financial Income / Total loan portfolio	29.8%	35.5%	38.5%
Financial costs / Total loan portfolio	12.4%	14.9%	13.9%
Gross financial margin	17.5%	20.6%	24.6%
Personal costs / Total loan porfolio	5.4%	7.4%	6.6%
Total operating costs / Total loan portfolio	12.6%	17.8%	17.9%
Profits / Total loan portfolio	3.0%	3.1%	3.3%
Profits / Total assets	2.1%	2.1%	2.4%
Profits / Equity	19.8%	21.3%	23.4%
Total liabilities / Total assets	89.6%	90.2%	89.9%
Total loan portfolio / Equity	662.6%	684.5%	710.1%
Total assets / Equity	956.9%	1022.8%	988.1%
Total loan portfolio / Credit analyst (US$)	444,144	392,502	396,265
Number of current credits / Credit analyst	576	549	614
Tipo de Cambio	**3.515**	**3.48**	**3.13**

* Includes depreciation, personnel costs and general costs.

ANNEX A.5 EDYFICAR EDPYME

EDYFICAR EDPYME is a corporation (Sociedad Anónima) created from the microcredit operations of CARE Perú. It is licensed by the SBS (Superintendent de Bancos y Seguros) to operate as an EDPYME (Entidad de Desarrollo a la Pequeña y Micro Empresa). EDYFICAR has three years operating as an EDPYME, and more than ten years experience in micro credit as an NGO before the changeover. USAID was an original donor supporting CARE Perú at startup in 1986.

CARE Peru owns 97 % of the shares, with three private persons associated with the institution owning 3 %. The Board of Directors includes 7 private persons and includes management staff. Recently EDYFICAR named a private sector businessman to the board with the idea to promote the incorporation of private sector investors. Still, for the foreseeable future, CARE Perú expects to retain at least 51 % ownership.

EDYFICAR provides credits through 11 agencies in Lima and interior cities and towns. The agencies (with share of loan placements in 2000 shown in parenthesis) are Norte (13%) and Sur (10%) in Lima, Puno (11%), Arequipa (10%), Trujillo (13%), Zarate (7%), Piura (4%), Chimbote (5%), Ayacucho (6%), Huaraz (8%) and Cajamarca (11%). Accepting deposits is not yet authorized; the company expects such authorization in 2003.

Credit products: Individual, Solidarity Group, Rotating Fund

EDYFICAR has three credit products. Individual credits, the most important, are for persons working with micro enterprises, and whose principal income is from their business. Solidarity Group credits are oriented for groups of 4 to 5 persons located in a specific area or have other affiliation and require a group credit to obtain a loan. Finally, Rotating Fund credits are directed to women groups that want especially small credits, generally less than $400.

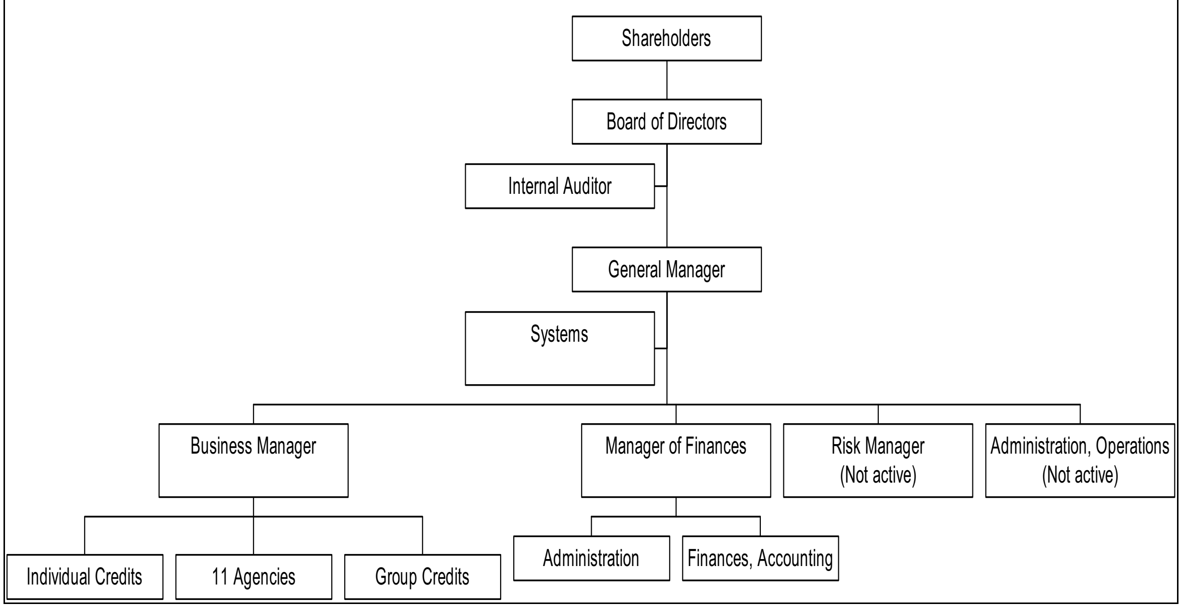
All credits are granted for a period of 4 to 24 months, the most common time period being 11 to 12 months. Interest rate is 4.5 % per month in Soles and 2.25 % per month in US dollars. There is a commission of 2 % for loans in either currency.

Loans disbursed in 2000 are for agriculture (less than 1 percent), commerce (61 %), production (28 %), services (7 %) and others (3 %).

Operations

EFIFICAR's organizational chart is shown in Annex A Figure 5. All loan processing is done in Lima.

Annex A Figure 5. EDYFICAR EDPYME



Systems

The management information system for EDYFICAR is from a Bolivian company that supplies software to financial institutions. It utilizes an Informix database management system running on a Unix operating system. It is a tested and reliable system, though EDYFICAR has to make modifications for to use it with some of its credit products. The company is implementing systems to connect remote offices with the central office data processing, through a mix of leased telephone lines and private sourced wide area networks.

EDYFICAR is testing using hand held computers by credit analysts that would provide credit analysts access to most of their client information in a small convenient package. Daily updates are anticipated. Also the credit analyst is expected to enter client data on the spot as he/she receives it from the client or potential client. By using a relatively simple method of credit scoring incorporated into the programs, the credit analyst may be able to inform most clients immediately of their approval or rejection of a credit request. The company hopes to expand to company wide use in 2001.

Four people operate and program the management information system.

Loan Portfolio

Loan portfolio is increasing rapidly, increasing by 38 % from January to September 2000, and increasing by a factor of 2.4 times the portfolio at the end of 1998 (Annex A Table 5). Loan size remains relatively constant, at about US$1,500 per loan. Consequently the number of clients has increased in line with the increases in portfolio amount; serving 8,717 clients at the end of September 2000.

Loan portfolio at risk was 9.7 % in September, somewhat higher than recommended for microfinance institutions, but still below that of many other Peruvian financial institutions. Portfolio at risk was also high in 1999 (8.9 %) and in 1997 (7.6 %).

Set asides for non collectible loans are according to the SBS requirements, and represent 87.5 % of the portfolio at risk, about in line with observed set asides in many microfinance institutions. In September 81 % of the loan portfolio was rated as normal, perhaps a little low but in line with Peruvian experience.

Each credit analyst on average has a loan portfolio of US$186,875 in September 2000, up from US$156,634 at the end of 1999. Each credit analyst administers 171 clients, an increase from 138 clients in 1999. This is lower than most microfinance institutions.

Overview of Financial Results

Earnings are positive for 1999 and 2000. Losses in 1997 probably reflect high costs and reduced income during startup. Projecting earnings to grow at current rates, profits should total about US$275,000, or about 2.4 % of total assets slightly less than last year. Return on equity should be about 8 % by the end of 2000, considerably less than the 11.3 % of 1999.

Financial income was 31.6 % of the total loan portfolio through September 2000. Projected for the year financial income should exceed $4.016 million or 39 % of projected loan portfolio, an important increase from the 34.2 % of 1999. Gross financial income as a percent of total loan portfolio in the mid 30's is relatively low for microfinance institutions, until competition begins to force loan rates lower.

Operating costs as a percent of total loan portfolio are in the mid 20's, about normal for microfinance institutions at the stage of development of EDYFICAR.

Gross financial margin (financial income less financial costs) declined from December 1999 (27.9%) to September 2000 (24.1%). It is not clear if the margin at year-end will reach that of last year.

Fortunately for EDYFICAR, cost of funds is relatively low, 6.3 % in 1999 and 7.6 % through 3 quarters of 2000.

Possibilities of working with donor agencies as USAID

Strengths

- The largest of the EDPYMEPs, and one of the earliest. It is profitable and has significant respect in the market,
- Delivery of services in 9 regional cities and towns,
- Long experience of working with donors and modern information system can generate wide variety of reports,
- Focus on middle strata of poor clients,
- Funding not required. EDYFICAR has access to adequate funds. Technical assistance would speed cost reduction activities and entry into new markets, especially savings,
- EDYFICAR has the potential to add many microenterprise clients with relatively low donor expenditures for support,
- The risk of funds being lost or inappropriately used is relatively low.

Weaknesses

- Limited presence in rural and agricultural areas,
- Average loan size is about $us1,500.

Needed Technical Assistance and Training

Some areas where technical assistance is needed are:

1. Development of new products, especially deposit mobilization,
2. Improve risk assessment and control,
3. Development of market information, and incorporating that information into the development of products,
4. Training for staff about the norms and work standards for regulated financial institutions, including several specific skills as Agency Managers, auditing, financial controls, liquidity management, credit evaluations and others;

EDYFICAR requested support for the development of an Association of EDPYMEs. This may be useful for the EDPYMEs, but there appears to be little benefit for USAID programs. Associations often provide an access point for donors both to receive information and to present information, data describing the industry, and lobby activities. USAID already has or can do all of these activities as needed.

Annex Table A.5. Selected Loan Portfolio and Financial Data			
EDYFICAR EDPYME			
Item	**Sep. 00**	**Dec-99**	**Dec-98**
Loan Portfolio Data			
Total loan portfolio (US$)	9,530,609	6,891,888	3,954,952
Net loan portfolio (US$)	8,718,102	6,391,388	3,756,549
Loan at risk > 30 Days (US$)	927,516	615,415	300,048
Loan loss set aside (US$)	812,507	500,500	198,403
Number of loans disbursed	7,406	6,575	4,212
Amount of loans disbursed (US$)	11,109,404	9,941,998	6,574,808
Average size of loan disbursed	1,500	1,512	1,561
Number of current loans	8,717	6,060	3,323
Number of employees	110	95	35
Number of Credit Officials	51	44	16
Financial Data			
Fixed assets (US$)	452,694	205,177	82,748
Total assets (US$)	11,675,621	9,507,105	4,114,058
Total liabilities (US$)	8,334,264	7,237,344	3,123,323
Total equity (US$)	3,341,358	2,269,761	990,735
Financial income (US$)	3,012,644	2,357,471	872,204
Financial costs (US$)	720,259	435,057	189,776
Other income (US$)	106,028	344,828	319
Total operating costs (US$) *	2,049,297	1,714,943	698,722
Personnel costs (US$)	814,843	775,575	271,565
Profits (US$)	206,245	313,506	-21,086
Indicators and Ratios			
Total loan portfolio / Total assets	81.6%	72.5%	96.1%
Net loan portfolio / Total loan portfolio	91.5%	92.7%	95.0%
Loans at risk / Total loan portfolio	9.7%	8.9%	7.6%
Loan loss set aside / Portfolio at risk	87.6%	81.3%	66.1%
Financial income / Total loan portfolio	31.6%	34.2%	22.1%
Financial costs / Total loan portfolio	7.6%	6.3%	4.8%
Gross financial margin	24.1%	27.9%	17.3%
Personnel costs / Total loan portfolio	8.5%	11.3%	6.9%
Operating costs / Total loan portfolio	21.5%	24.9%	17.7%
Profits / Total loan portfolio	2.2%	4.5%	-0.5%
Profits / Total assets	1.8%	3.3%	-0.5%
Profts / Equity	6.2%	13.8%	-2.1%
Total liabilities / Total assets	71.4%	76.1%	75.9%
Total loan portfolio / Equity	285.2%	303.6%	399.2%
Total loan portfolio / Credit officer (US$)	186,875	156,634	247,185
Number of current credits / Credit officer	171	138	208

ANNEX A.6 FINCA PERU

FINCA Peru was founded in 1984, and immediately began offering credits to low income people. In 1993 the company secured a grant for $300,000, beginning a process of credit management following improved practices and collections technology. The company serves primarily women with a mix of rural (majority) and urban customers. Currently FINCA provides services from its offices in Ayacucho, Lima and Huancavelica.

Since 1993 FINCA Peru has obtained several other donations to bring their current loan portfolio to nearly $650,000 and their equity to more than $975,000. There is little debt; $18,000 as of September 2000.

Products

FINCA Peru uses the village banking methodology, with the exception of a few Special Loans. The FINCA loan, "external loan" in the village banking terminology, is granted for a period of 4 months, at an interest rate of 4 % per month. There is no commission. A commitment to save on a regular basis is a condition of the loan. Loan payments for most groups are monthly. Only the group guarantee is required.

Because FINCA Perú is an NGO, it is required to pay the IVG tax. This makes the credit cost to its clients about 65 to 75 % per year.

Savings mobilization is within the village bank group, and totaled about $1.3 million ending the third quarter of 2000. This savings is used to finance the internal loan portfolio. FINCA reports that for many groups there is now excess liquidity, more savings than internal loans. For now FINCA keeps the interest earned on these excess deposits.

Loan Portfolio

The loan portfolio reached a peak in 1997 at more than US$900.000, and has declined since then and has remained relatively steady since the end of 1998, between US$650,000 and US$700,000. Loans represented 59 % of total assets in September 2000, rather low, and a verification of management's assertion that there is less loan demand, at least in the urban areas.

Loan collections are good. The Portfolio at risk is low, 1.4 % in September 2000 and 1.7 % in December 1999. This level is typical for village banks. As a consequence, loan loss reserve is high, 190 % of the portfolio at risk in September 2000. This is up significantly from 1998 when loan loss reserve was 88 % of the total loan portfolio.

FINCA Perú now has 17 credit promoters, down from 20 last year. In addition there are 3 credit supervisors. The total loan portfolio per credit promoter is very low, $30,209 in September. The number of clients per promoter is 274, in line with many microfinance institutions, but not sufficient to generate much profits with the size of credits granted. The average size of a credit disbursed in 2000 is US$123.

FINCA Perú has been successful in mobilizing savings, with a balance of nearly US$1.3 million in savings in September. Most of these funds are used for the "internal loan" of the village bank. Excess savings are placed in a bank and FINCA keeps the interest paid to cover defray their costs of administration.

As of September 2000, FINCA Peru had 6,023 active loans.

Overview of Financial Results

Despite its small size, FINCA Peru is profitable, but just barely. In 2000 earnings before direct donations should be about $75,000. Because of the large equity, profits as a percent of equity is small; 9.1 % through three quarters in 2000, but higher than the entire year of 1999 (2.8 %) and 1998 (6.0 %). Profits as a percent of assets is reasonable for microfinance institutions, 7.9 % through September of 2000, but a rather low 2.0 % in 1999 and 4.0 % in 1998.

Financial income as a percent of the loan portfolio would appear adequate, at 62.7 % for three quarters of 2000, 71.0 % for 1999 and 83.0 % in 1998. But out of this FINCA pays the IVG tax. This can be seen in operating costs, which were 50.1 % to September 2000 and 71 % for the year 1999. In this case personnel costs may be a better indicator of operating costs. For 2000 to September, personnel costs represented 29.9 % of loan portfolio, and 36 % of loan portfolio in 1999, to December. Operating costs are still relatively high. Reducing operating costs will most likely depend most on increasing loan volume without significantly increasing the number of employees.

Like most MFIs, financial costs are low because of donated or low cost funds, or the NGO lending its equity. To September date in 2000 financial costs are 8 % of the loan portfolio.

Possibilities of Working with Donor Agencies and USAID

Strengths
- Profitable, with little subsidy, low operational and finance costs,
- Has nearly $1 million in equity,
- High repayment rates.

Weaknesses
- Attitude of NGO lingers,
- Internal savings limits growth of external loan portfolio,
- Competitors have grown faster in their market with similar products, suggests some product defects or weaknesses,
- Information systems inadequate (in process of improvement),
- Lack some key skills for financial intermediation.

FINCA Peru has a small and successful microfinance operation. The company focuses on a specific product it believes best serves the intended customers. There appears little formal effort to learn the true needs of customers concerning their products and to adjust their products accordingly. As a consequence, there is a good possibility that competitors are gaining market share.

The lack of growth of the loan portfolio could also be caused by the success of the savings program. Savings of bank members are lent within the same bank, and the earnings distributed among the members. Thus, an internal loan costs less than a FINCA loan. The FINCA loan portfolio may be a victim of FINCA's success in promoting savings.

Needed Technical Assistance and Training

FINCA Peru needs assistance in nearly every aspect of financial company operations. Specifically some needs are:

1. Strategic Business Planning,
2. Market positioning,
3. Product development,
4. Funding alternatives,
5. Support for preparing for supervision of the SBS,
6. Village Banking and Regulatory Environment, how to incorporate savings of village banks into FINCA administration,
7. New product development for larger credits,
8. Review operational procedures and corresponding manuals,
9. Evaluate risk for specific products and market opportunities,
10. Training for staff in the operations of financial institutions,
11. Preparation of operating manuals,
12. Establishing an internal audit system.

Perhaps the most important support for FINCA Peru is to help management and staff adopt a market oriented approach. The company believes its products are very useful for its clients. But growth in the amount of the loan portfolio of FINCA Peru is probably smaller than the growth of the loan portfolio of competitors.

Annex A Table 6. Selected Loan Portfolio and Financial Data			
FINCA - PERU			
Item	**Sep. 00**	**Dec-99**	**Dec-98**
Loan Portfolio Data			
Total loan portfolio (US$)	664,590	695,756	723,680
Net loan portfolio (US$)	647,140	685,261	686,806
Loan portfolio at risk > 30 Days (US$)	9,179	11,927	44,761
Loan loss reserve (US$)	17,450	10,495	36,874
Number of loans disbursed in the period	13,369	17,137	8,193
Amount of loans disbursed (US$)	2,070,529	2,729,271	1,157,108
Number of current loans	6,023	5,984	5,166
Number of employees	32	53	44
Number of credit analystsNúmero de Analist	22	19	21
Financial Data			
Total assets (US$)	1,118,446	1,214,748	1,313,154
Total liabilities (US$)	142,437	316,904	441,094
Total equity (US$)	976,009	897,843	872,060
Financial income (US$)	416,512	494,100	600,461
Financial Costs (US$)	52,855	29,447	84,824
Other income (US$)	57,935	26,788	74,479
Total operating costs (US$) *	333,087	464,725	537,616
Personnel costs (US$)	198,959	250,186	213,864
Profits (US$)	88,505	24,715	52,500
Indicators and Ratios			
Total loan portfolio / Total assets	59.4%	57.3%	55.1%
Net loan portfolio / Total loan portfolio	97.4%	98.5%	94.9%
Loans at risk / Total loan portfolio	1.4%	1.7%	6.2%
Loan loss reserve / Loan portfolio at risk	190.1%	88.0%	82.4%
Financial income / Total loan portfolio	62.7%	71.0%	83.0%
Financial costs / Total loan portfolio	8.0%	4.2%	11.7%
Gross financial margin	54.7%	66.8%	71.3%
Personnel costs / Total loan portfolio	29.9%	36.0%	29.6%
Total operating costs / Total loan portfolio	50.1%	66.8%	74.3%
Profits / Total loan portfolio	13.3%	3.6%	7.3%
Profits / total assets	7.9%	2.0%	4.0%
Profits / Equity	9.1%	2.8%	6.0%
Total liabilities / Total assets	12.7%	26.1%	33.6%
Total loan portfolio / Equity	68.1%	77.5%	83.0%
Total loan portfolio / Credit analyst (US$)	30,209	36,619	34,461
Number of current loans / Credit analyst	274	315	246

ANNEX A.7 HABITAT TRUJILLO

The NGO Habitat Trujillo was organized in 1987 as a not-for-profit institution to support the less favored economic sectors in the Region La Libertad. The next year the NGO began its credit operations with us$80,000 in funds from the Interamerican Foundation. Today the company serves nearly 2,400 borrowers with a loan portfolio of us$1.8 million (average outstanding balance of us$771 per loan).

Seven directors, all from the local community, govern Habitat Trujillo. The Director of the Microenterprise Project directs credit operations, supported by key executives Coordinator of Credit and Recuperations, Administrative Manager, Systems Chief and Accountant.

The company has received its authorization to organize as an EDPYME, and notified the SBS it intends to start in January of 2001. Arrival of additional funds and potential tax issues may influence the start up date. More likely the company will start by March 2000.

Credit products: Individual, Solidarity Group, Special Credits

Habitat Trujillo has three principal credit products: Individual, Group Solidarity and Special. Loans are predominately for commerce (80 %), production (14 %) and services (6 %).

Individual Credits

Individual credits are now about half of the loan portfolio and are increasing their share. Individual credits can be given up to us$3,000. In 2000 disbursements averaged us$1,069. These loans are granted up to 24 months, but most are taken for 10 months. The interest rate is 4.2 or 4.5 % per month, depending on funds source, and paid on a declining balance. There is no commission.

Solidarity Group Credits

Solidarity groups were the original credit product, and are now declining in the share of portfolio. Originally groups were large, but now are usually 2 to 4 persons grouped together to strengthen their guarantees (cross personal guarantees) to receive a loan. Loans are most frequently for commerce. Average loan disbursement amounts are slightly smaller than for individual loans. Loan periods and interest rates are the same as for individual credits.

Special Loans

Special loans are of two types. One type is replenishment loans, which can be approved for borrowers to provide temporary funds within their prior-approved credit amount. For example, if a borrower had an initial loan for us$1,000 and had paid the loan balance down to us$700, that same borrower could receive a special loan for us$300, up to a limit of his prior approved credit limit or S/5,000, which ever is less.

Parallel loans are the second type and were provided as additional funds to existing borrowers with an outstanding repayment history, and who provide additional real guarantees. Again the limit is S/5,000. Parallel loans are being phased out.

Loan Portfolio

The amount of loans disbursed has declined in the last three years by about 30 %. As a consequence the outstanding loan portfolio has also declined. As of September 2000 the total loan portfolio is US$1,771,067. Portfolio at risk for payments over 30 days is 7.3 %, a bit high but within acceptable limits for microfinance institutions. Loan loss reserve as a percent of past due portfolio is 86 %, a bit low but within acceptable levels.

Operations

Habitat Trujillo conducts its operations from its central office in the city of Trujillo, and from offices in five towns in the region, Ascope, Chepén, Pacasmayo, Virú and Otuzco. Credit is the principal activity, accounting for 89 % of its gross revenues. There are 23 persons working full time in credit and 8 others giving the equivalent of 5 full-time persons, for a total of 28 persons. About 20 more people work in non-credit activities. Annex A Figure 6 shows an organization chart. The Administrative Manager, Accountant and Computing Chief coordinate closely with the Microenterprise Director.

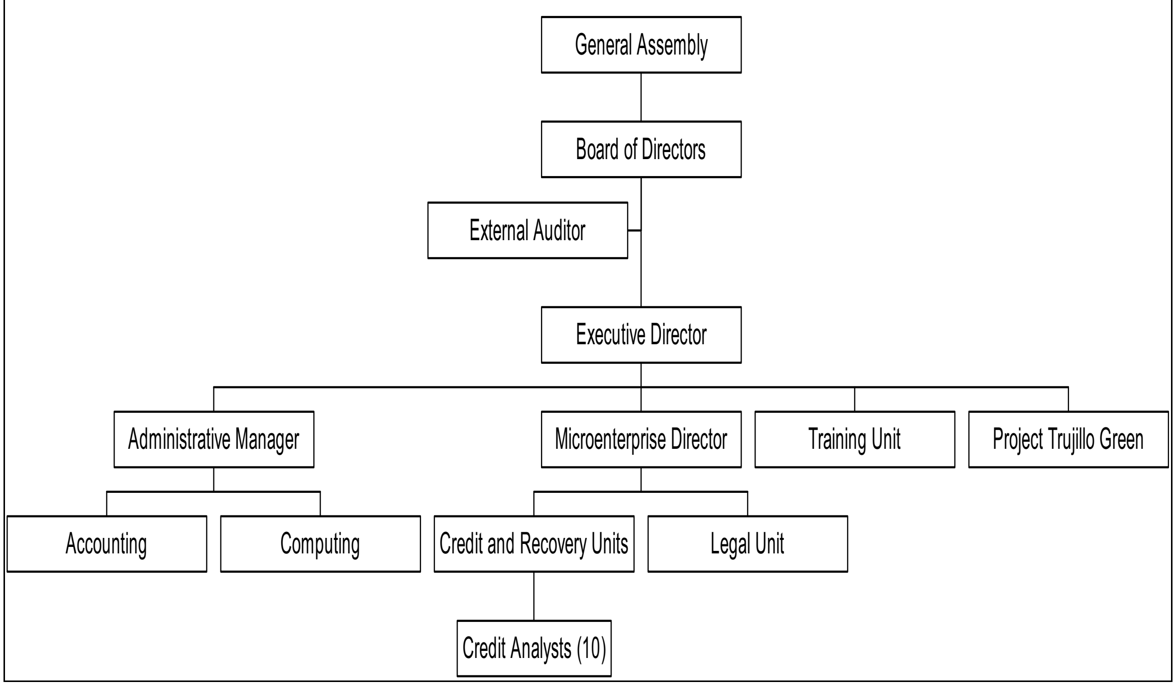
Ten credit analysts find customers in their assigned region, process loans, approve some, and collect. New borrowers, larger loans and loans to borrowers with some previous late payments are approved by a loan committee. Habitat Trujillo does not lend directly for agricultural production, though agriculture is the dominant or important economic activity in all the towns it serves.

Currently the NGO sources outside funds from Foncodes, BID and Fondemi, which total about US$1.6 million and represent 88 % of the loan portfolio. The remaining 12 % and operations funds are from the NGO's own resources. Habitat Trujillo's management says their loan portfolio is limited by availability of funds.

Habitat Trujillo participates in the credit reference system INFOCORP, and also provides financial and operations data to USAID/COPEME's Microenterprise Initiative.

The NGO has developed relationships with several banks to support disbursements and payments of loans. All loans are disbursed by check prepared in the central office. Usually credit analysts are visiting the central office once or twice per week and bring loan request documentation and retrieve and deliver disbursement checks.

Annex A Figure 7. Habitat Trujillo



Loan payments are mostly made in the central office in Trujillo, costly and time consuming for some clients. Loan payment programs have been negotiated with Banco Continental and Banco de la Nación. This will permit loan payments in town nearer the borrowers. Only a few payments are done this way now.

The amount of loans disbursed each year is declining, mostly because of longer payment periods. Average size of loan disbursed in 2000 is $1,068, down slightly but probably because of the economic slowdown. The heavy focus on commercial loans remains, though it is declining. The loan portfolio at risk is relatively high, at 7.47 %. This number includes three mortgage-backed credits, which have been renegotiated and the debtors are making payments. If these were classified as on time, the portfolio at risk would be 5.96 %.

The average loan portfolio per credit analyst is US$177,107, in line with many microfinance institutions. The number of loans per credit analyst at 233 is a little low, but not so different from many microfinance institutions.

Systems

The management information system has been built internally. Two persons full-time administer the system and write programs. Programs are grouped into 4 modules: Credit, Accounting, Finances/Budget and Internal Controls. The first two are written in Clipper, the last two using PowerBuilder and SQL. As resources permit, the intention is to rewrite the system using Oracle as the database manager and Visual Basic to write the front end. The internal network is Novel version 4.11. Terminals run Windows operating system.

Most payments and all disbursements and expenditures are entered from the central office. Each day Habitat downloads reports from Banco Continental of payments received and updates their system. Banco de la Nación is updated manually. Each day credit analysts receive needed reports by email, through direct dial-up connection.

The systems group cites a lack of support in Trujillo for higher level languages such as PowerBuilder, Oracle and Unix. There are few users and no support groups in the city. It is difficult to obtain programming tools to make their work more efficient.

Overview of Financial Results

As of September 2000 Habitat Trujillo had total assets of US$3,462.970, liabilities of US$2,883,970 and equity of US$579,214. This results in a leverage of assets to equity of 6.0 and a leverage of loan portfolio to equity of 3.1. To significantly expand its liabilities and assets will require an increase in equity. This is not available from the principal owner, and will require new investors, donor support or significant growth in retained earnings.

Profits for the last two years are barely positive, following profits of US$120,916 in 1998. As a consequence profits as a share of assets and equity are nearly 0 for the last two years.

Financial income is 41 % of loan portfolio, financial costs are 21.8 %, for a gross financial margin of 19.4 %. Total operating costs represent 25.4 % of total loan portfolio. Non-financial income saves the company from showing loses.

Needed Technical Assistance and Training

The NGO demonstrates some strengths and weaknesses. Beginning with the strengths, which are:

- The company is profitable, and probably can continue to be profitable, though it may be difficult to meet the increased costs associated with becoming an EDPYME with out a larger loan portfolio,
- High level of leverage of equity for a NGO, permitting sufficient earnings to be profitable with a small equity,
- Knowledge of lending in towns in the region

Weaknesses are:

- Limited equity, the company needs to find other investors, or the NGO will grow slowly as equity is increased by retained earnings,
- Lack of funds means many of their larger borrowers are attracted to competitors to get larger loans,
- Management information system will require significant increase in resources to keep up with operations changes.

Growth of the NGO has been constrained since 1997 because of the lack of additional funds for lending. During this period the market in Trujillo is becoming congested with many lenders, making markets in towns in the region of increasing interest.

Some areas of needed assistance are:

1. Development of new credit products,
2. Training for NGO staff about the norms and work standards for regulated financial institutions,
3. Technical assistance in marketing of credit products, and eventually savings products,
4. Modern tools for software development,
5. Institutional strengthening in all aspects of finance company operations
   a. Standards for financial institutions,
   b. Software standards for financial institutions,
   c. Help with modern communications equipment to communicate with remote offices.
   d. Strategic planning,
   e. Market analysis,

Capabilities of Working with Donors

Positive elements some donor may find attractive for working with Habitat Trujillo are:

- The NGO can work in smaller towns in the regions surrounding Trujillo,
- Can target funds to specific areas and market segments. Some targeted groups or areas will require the donor to subsidize operations costs. Most donor operations to target groups will require loan funds as well.
- Relatively low cost operations compared to most Peruvian microfinance NGOs.

Donors may find some difficult elements to overcome when working with Habitat Trujillo:

- The NGO has a higher risk than many other micro credit operations. This is because of limited equity to cover difficult periods of operations,
- Better financed microfinance institutions are entering their markets, especially in Trujillo. These will likely reach more clients, at least in urban areas.

Annex A Table 7. Selected Loan Portfolio and Financial Data			
HABITAT TRUJILLO NGO			
Item	**Sep. 00**	**Dec-99**	**Dec-98**
Loan Portfolio Data			
Total loan portfolio (US$)	1,771,067	1,972,087	2,074,721
Net loan portfolio (US$)	1,659,193	1,843,078	1,950,539
Loan portfolio a risk > 30 Days (US$)	130,135	147,616	146,143
Loan Loss reserves (US$)	111,874	129,009	124,182
Number of loans disbursed in the period	2,940	4,354	4,495
Amount of loans disubrsed in the period(US$)	3,120,866	4,736,928	5,413,346
Average size of loan disbursed (US$)	2,328	2,375	2,273
Number of current loans			
Number of employees	30	30	30
Number of credit analysts	10	10	10
Financial Data			
Fixed assets (US$)	395,509	117,053	155,409
Total assets (US$)	3,462,970	3,908,895	3,342,129
Total liabilities (US$)	2,883,756	3,465,079	2,874,739
Total Equity (US$)	579,214	443,816	467,390
Financial Income (US$)	729,328	1,138,841	1,113,767
Financial Costs (US$)	385,407	414,888	284,697
Other Income (US$)	107,004	25,927	51,476
Total operating costs (US$) *	450,715	737,589	748,276
Personnel costs (US$)	183,511	284,416	299,656
Profits (US$)	1,704	313	120,916
Indicators and Ratios			
Total loan portfolio / Total assets	51.1%	50.5%	62.1%
Net loan portfolio / Total loan portfolio	93.7%	93.5%	94.0%
Loan portfolio at rist / Total loan portfolio	7.3%	7.5%	7.0%
Loan loss reserve / Loan portfolio at risk	86.0%	87.4%	85.0%
Financial Income / Total loan portfolio	41.2%	57.7%	53.7%
Financial costs / Total loan portfolio	21.8%	21.0%	13.7%
Gross financial margin	19.4%	36.7%	40.0%
Personal costs / Total loan porfolio	10.4%	14.4%	14.4%
Total operating costs / Total loan portfolio	25.4%	37.4%	36.1%
Profits / Total loan portfolio	0.1%	0.0%	5.8%
Profits / Total assets	0.0%	0.0%	3.6%
Profits / Equity	0.3%	0.1%	25.9%
Total liabilities / Total assets	83.3%	88.6%	86.0%
Total loan portfolio / Equity	305.8%	444.3%	443.9%
Total loan portfolio / Credit analyst (miles US$)	177,107	197,209	207,472
Number of current credits / Credit analyst	233	238	227
Tipo de Cambio	**3.515**	**3.48**	**3.13**

* Includes loan loss setaside, depreciation, personnel costs, and general administrative expenses

ANNEX A.8. PRISMA

PRISMA began its micro credit program, called PASA (Programa de Apoyo a la Seguridad Alimentaria), in 1995. The program's objective is to improve the social-economic situation of the most vulnerable population by providing credits.

At first the program provided individual credits for productive activities of microenterprises. Loan collections from this era were not good.

In 1997 the strategy transformed to give more emphasis to self-sustainability and to adhere to the micro credit best practices policies of USAID. The NGO continued its focus on the poor, but now based on the concept of group guarantees. Adding to Title II funding, PRISMA has opened areas in the north of Peru with funds from Fondo Contravlor Peru Canada, and in the areas of coca production with funds from Alternative Development by USAID/CONTRADROGAS. In additional some mining companies have financed PRISMA credit programs in the areas near their facilities.

From its beginning, PRISMA's micro credit program has grown every year. Services are now provided in 11 Departments of Peru, 7 in the mountains, 2 in the tropics and 2 along the coast.

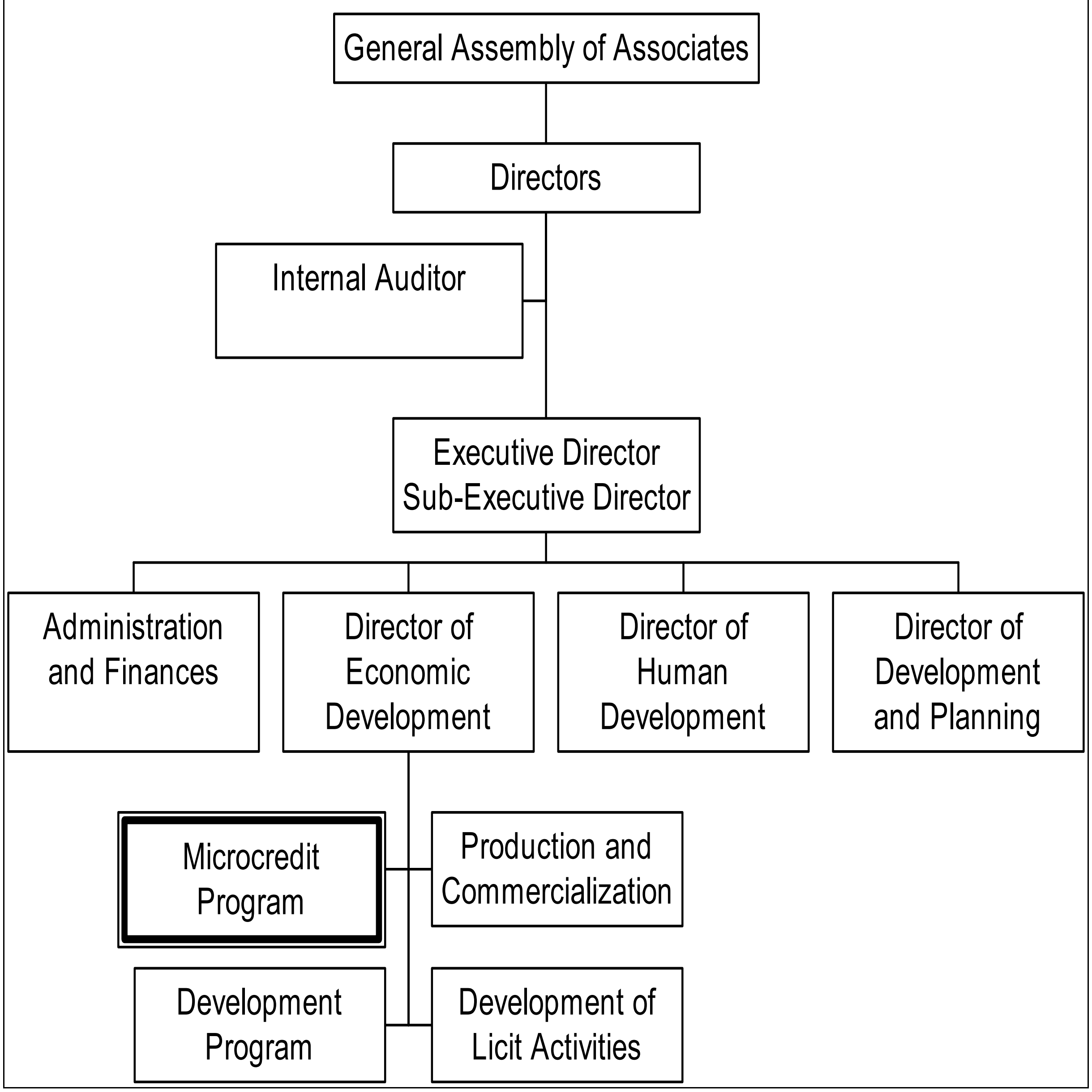
Two types of credit are offered. First is the ACPD (Asociaciones Comunales ProDesarrollo). This is a typical village bank product, eliminating the work bank for political purposes. This product is aimed at the poorest segments of the population capable of handling credits. The second product is solidarity group lending, provided for all but specifically intended to help those borrowers with more advanced financing needs.

Because of the credit demand, in 1998 PRISMA established a separate Microcredit Manager within their organization. This has helped to accelerate the development of policies and operating systems to achieve an efficient and sustainable program with high quality services for customers. The Microcredit group has adopted many of the policies and parameters suggested by USAID and by the SBS for the administration of its programs. Implementing them will take some time.

The administrative organization of all of PRISMA is shown in Annex A Figure 8A, with some detail not shown to conserve space. Annex A Figure 8B shows the administrative organization of the Microcredit Operations within PRISMA.

The Credit Committee includes key executives of PRISMA and for one part operates as a traditional credit committee approving credits. It also functions more globally, approving policies and methodologies of implementation to achieve the objectives of the credit program.

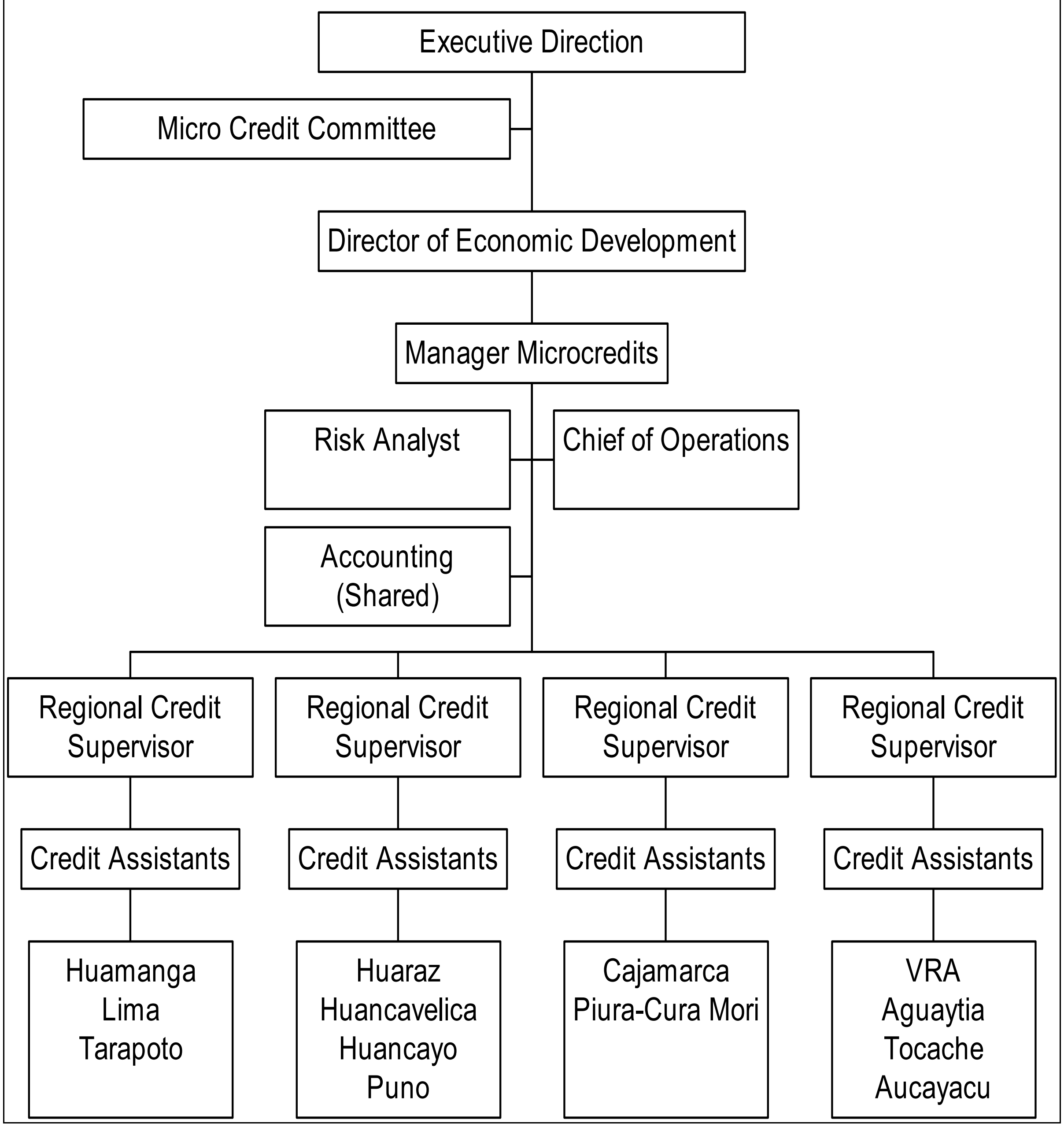
ANNEX A FIGURE 8A. ASOCIACION BENEFICA PRISMA



The Microcredit Program operates semi autonyms from other programs of PRISMA. Recently, accounting for the credit program was separated from other activities of PRISMA, including efforts to identify separately costs for the credit program, though some cross subsidy may still be present.

PRISMA offers credits through 13 local agencies located around Peru.

ANNEX A FIGURE 8B. MICROCREDIT GROUP



Credit products

The ACPD is a traditional village back product. A promoter from PRISMA helps a community to form a group of people who want credits and are willing to participate in a savings program. A ACPD group is composed of about 20 people, in 4 groups of 4 to 6 members in each. Attendance at a periodic meeting is required. Initially the loans come from the resources of PRISMA. As group funds are generated from the required savings, an internal loan portfolio is also generated. The promoter of PRISMA provides training to members of the group on the operations of savings and credit decisions.

ACPD groups may be rural or urban. Urban groups have uniform monthly payments of principal and interest over 4 months. Rural groups receive 6 or 7 month loans, and most borrowers elect to have a grace period for capital repayments. The grace period is normally the same as the loan period. Interest must be paid monthly. Any missed payment of capital or interest causes the loan to be classified as in default. ACPD's account for 89 % of the loan portfolio.

The ACPD group loan is generally directed to those people who are the poorest. Loan amount per borrower for the first cycle is a maximum of about US$143 for urban loans and about US$171 for rural loans. The maximum loan size after 3 years is about US$600. Loan term is 4 months for urban loans, 6 months for rural loans.

The solidarity group loan is expected to benefit those with a slightly higher level of economic development. The initial loan size is between $143 and $ 286.

The solidarity group loan is a traditional group guaranteed loan practiced in many microfinance companies. Groups are 3 to 5 persons. Loans are small at first, from about US$145, and increases as the repayment history of the borrower remains favorable. Solidarity loans are 11 % of the loan portfolio.

For both products the interest rate is 4 % per month for urban loans and 4.5 % per month for rural loans. There is no commission. The interest to be paid is calculated using the entire amount of the loan disbursement over the entire loan period. The resulting annual percentage rate for urban loans with monthly payments exceeds 90 %. The annual percentage rate for most rural loans with a balloon capital payment is about 54 %.

Loans policies say credit is available for any purpose, though currently requests for consumer loans may not be approved.

The grace period for agricultural loans holds the possibility of masking potentially high default rates, even though interest payments are due monthly.

Loan Portfolio

As of the end of September there were 25,189 loan clients, with a loan portfolio of US$4,424,435, an average outstanding loan balance of US$176 per client. ACPD groups account for 89 % of the loans, the Solidarity Groups 11 %. Loans are nearly evenly split between men and women. Clients in rural areas receive 69 % of loans, urban areas 31 %.

Late payments have been a problem with PRISMA. At the end of October the portfolio at risk was 10.0 % for 30 days late. The company reports that for November the rate had fallen to 5.5 % for 30 days late. This is considerably better than earlier results; for December 1999 the rate was 16.7 %. The company is making a concerted effort to collect past due loans. Also, for the first time in 1999 and continuing in 2000 the company has written off old past due loans, mostly those coming from the 1996 and 1997 period when individual loans were granted. Write offs in 1999 were US$103,698, and in 2000 were US$147,805, 4.6 % and 3.3 % of the loan portfolio respectively. These write offs are a bit on this high side, unless they represent delayed write offs from earlier periods.

The total loan portfolio represents 81.4 % of total assets, reasonable for an NGO dependent on donors for funds to lend. Loan loss reserves appear to be relatively low as of September 2000, just 55.5 % of the portfolio at risk.

Average per loan disbursement in 2000 has been $234, not much different from 1998 average of $213. The amount of loans disbursed per year in increasing rapidly, up 95 % from December 1998 to December 1999, and up 86 % from December 1999 to September 2000.

Each credit promoter handles an average of 254 clients as of September 2000, with a loan portfolio of $45,000. This is lower that it needs to be for PRISIM to be a self-sustainable microfinance institution. PRISM hopes to achieve 400 clients per promoter in 2001. Even this may not be sufficient to meet competitive pressures that may come as more institutions enter the microfinance market.

PRISM reports one promoter has a loan portfolio with 3,500 clients. Removing this promoter from the calculation yields an average of 221 clients per promoter.

Overview of Financial Results

For the first time in 2000, PRISMA will likely show profits that exceed income from donations. Profits in 1999 were US$237,828 while other income, which is mostly donations, was US$438,326. Profits to September 2000 were US$289,422 while other income is US$202,281.

Most of the funds that are provided to PRISMA are shown on the financial statements as equity, which was US$5,437,384 in September 2000. Equity exceeds the total loan portfolio of US$4,424,435.

Financial income represents 32.6 % of gross loan portfolio. Financial costs are only 0.4 %, leaving a gross financial margin of 32.2 %. But total operating costs in 1999 were 41.1 % of gross loan portfolio. The difference is made up of donations and other income.

There are no long-term debt, and only minimal short-term debt in the form of accounts payable.

Loan loss reserves were low, only 55.7 % of the outstanding portfolio at risk. In December 1999 profits were 5.3 % of the total loan portfolio and 5.4 % of total assets.

Capabilities of Working with Donors

PRISMA NGO has extensive experience working with donors in implementation of development and assistance projects. Since 1995 it has implemented micro credit programs with donor support. From 1997 the NGO decided to reorient the focus of micro credit programs toward self-sustainability, and to comply with USAID micro credit policies.

Needed Technical Assistance and Training

PRISMA is still young in credit administration, and needs improvement at all aspects of financial institution administration. Some specific needs are:

1. Support for to install operational procedures matching the SBS norms for microfinance institutions,
2. Support for the process of transformation to a regulated institution,
3. Institutional Strengthening:

- Training employees in operations of financial institutions,
- Evaluation and improvement of operations, including preparation of operating manuals,
- Credit decision making and collections,
- Loan documentation,
- Internal controls,
- Accounting and auditing standards and procedures,
- Product development for credit products and later for deposit products,

4. Improve information systems and communications with remote offices.

Prisma supports the proposal of COPEME to establish self-regulation of NGOs and other finance institutions not regulated by the SBS or other entity. This is already mostly being done through USAID program support to the industry.

Annex A Table 8. PRISMA			
Item	**Sep. 00**	**Dec-99**	**Dec-98**
Loan Portfolio Data			
Total loan portfolio (US$)	4,424,435	2,274,325	1,328,014
Net loan portfolio (US$)	4,177,578	2,140,067	1,289,026
Loan portfolio a risk > 30 Days (US$)	443,328	378,903	46,466
Loan Loss reserves (US$)	246,857	134,258	38,988
Number of loans disbursed in the period	33,088	25,470	10,005
Amount of loans disubrsed in the period(US$)	7,757,117	4,175,405	2,132,473
Average size of loan disbursed (US$)	234	164	213
Number of current loans	25,189	16,745	10,471
Number of employees	119	73	43
Number of credit analysts	99	55	32
Financial Data			
Fixed assets (US$)	166,678	103,289	15,626
Total assets (US$)	5,437,384	3,610,116	2,183,932
Total liabilities (US$)	84,535	50,283	101,038
Total Equity (US$)	5,352,849	3,559,833	2,082,894
Financial Income (US$)	1,134,597	742,461	274,595
Financial Costs (US$)	29,246	9,186	15,071
Other Income (US$)	202,281	438,326	407,014
Total operating costs (US$) *	1,018,211	933,773	472,119
Personnel costs (US$)	488,015	382,565	226,902
Profits (US$)	289,422	237,828	194,419
Indicators and Ratios			
Total loan portfolio / Total assets	81.4%	63.0%	60.8%
Net loan portfolio / Total loan portfolio	94.4%	94.1%	97.1%
Portfolio at risk / Total loan portfolio	10.0%	16.7%	3.5%
Loan loss setaside / Portfolio at risk	55.7%	35.4%	83.9%
Financial income / Total loan portfolio	25.6%	32.6%	20.7%
Financial costs / Total loan portfolio	0.7%	0.4%	1.1%
Gross financial margin	25.0%	32.2%	19.5%
Personnel costs / Total loan portfolio	11.0%	16.8%	17.1%
Total operating costs / total loan portfolio	23.0%	41.1%	35.6%
Profits / Total loan portfolio	6.5%	10.5%	14.6%
Profits / Total assets	5.3%	6.6%	8.9%
Profits / Equity	5.4%	6.7%	9.3%
Total liabilities / Total assets	1.6%	1.4%	4.6%
Total loan portfolio / Equity	82.7%	63.9%	63.8%
Total loan portfolio / Credit analyst (miles US$)	44,691	41,351	41,500
Number of current credits / Credit analyst	254	304	327
Exchange rate	3.515	3.48	3.13

* Includes loan loss reserve, depreciation, personnel costs and general costs.

ANNEX A.9. PROEMPRESA

PROEMPRESA has 15 years of credit experience, 12 as IDESI Nacional, an NGO, and 3 as an EDPYME. PROEMPRESA wants to be a leading financial entity at the national level in serving micro and small enterprises, both in its geographic reach as well as with efficiency and profitability.

PROEMPRESA is a stock corporation owned 99 % IDESI, and the other 1 % owned by two private people related to the NGO. The owners select a board of directors of 6 people. Key management positions include the General Manager; Credit Manager; Accounting, Administration, Logistics and Operations; and Information Systems. The administrative organization is shown in Annex A Figure 9.

Credit products

PROEMPRESA only gives individual loans, which are given different names, but are essentially differentiated by the amount or purpose of the loan.

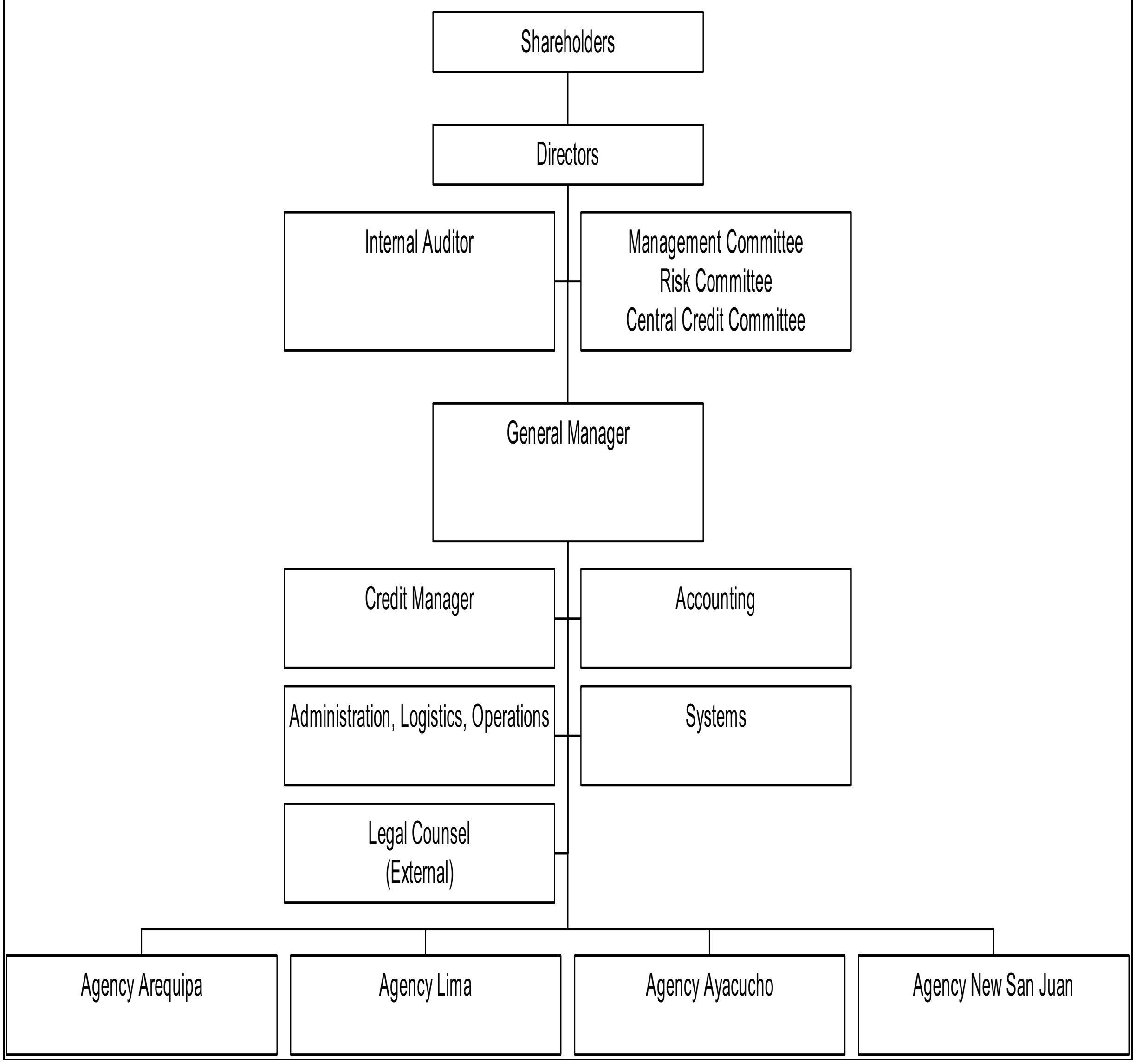
- **ProCrecer** is for amounts from US$50 to US$990, from 1 to 6 months,
- **ProMercado** from US$1,000 to US$5,000, from 1 to 24 months,
- **ProDesarrollo** from US$3,000 to US$10,000, from 8 to 24 months
- **ProInversion** up to US$3,000 and up to 3 years to purchase store locations.

Interest rates range between 3.49 % and 4.49 % in Soles, and between 2.25 % and 2.75 % in dollars depending on the amounts. Interest is calculated on a declining balance method. For the first credit with PROEMPRESA there is a 3 % commission for life insurance. With a good repayment history the second credit has a 1.5 % commission, and for third and following credits with a good repayment history there is no commission. PROMESA considers a borrower a prompt payer if the total days of late payments are less than 3 times the number of monthly payments completed. The count of late days restarts for each loan. A credit committee approves all loans. Depending on the amount of the loan the credit committee may be at local offices or at the central offices in Lima. The larger the amount, additional people participate in the credit decision.

Operations

The company serves its clients from the central office in Lima and from offices in Ayacucho and Arequipa. Since becoming an EDPYME, the company has exhibited good growth in its loan portfolio, good collections and profitability. As of September there are a total 44 employees, 18 of which are credit agents.

Annex A Figure 9. PROEMPRESA S.A., EDPYME



Loan Portfolio

Loans outstanding as of September 2000 are US$3.8 million, an increase of 28 % from December of 1999, but an increase of only 24 % from December 1998. The loan portfolio grew rapidly during the year 1998, because of transfer of clients from the prior NGO to the books of Proempresa. For the year 1999 the loan portfolio remained nearly constant, but resumed its growth in the first quarter of 2000.

The loan portfolio represents 66.1 % of total assets. The portfolio at risk is 6.7 % for 30 days past due. Loan loss reserves are 121 % of portfolio at risk. These past due amounts are common for Peru, not so good for well managed microfinance institutions in other countries.

Lima accounts for about half of loan disbursements, Arequipa a little more than one fourth, and Ayacucho a little less than one fourth. Sixty percent of loans are for commerce, 24 % for services and 16 % for production. Women receive a little less than half of the loans, men a little more than half. Two thirds of disbursements are in Soles, the remainder in dollars.

The loan most utilized is ProDesarrollo, with 71 percent of disbursements in 2000. This is the product with the largest loan amounts. ProMercado with loans from US$1,000 to US$5,000 is the second most common loan size. The smallest loan, from US$50 to US$990, only accounts for 1 % of disbursements in 2000. The average size of loans disbursed in 2000 is US$1,306. Forty percent of loans are for periods of 1 to 6 months, another 43 % for periods of 7 to 12 months. Seventeen percent are for periods longer than 1 year.

Product	Share of disbursements
ProDesarrollo	71 %
ProMercado	20 %
ProCrece	1 %
ProInversion	8 %

Eighteen credit analysts serve 2,928 credits, or 163 credit per analyst, a relatively low number. The company's goal is to reach an average of 330 clients per credit analyst, and expects the maximum number of clients per analyst to be 400. Because the loan amount is relatively high, US$1,308 average outstanding balance per credit, the total loan portfolio per credit analyst is a respectable US$212,558.

The loan portfolio is 2.92 times equity, a good leverage for a microfinance company this young.

Overview of Financial Results

PROEMPRESA is profitable, earning US$173,282 in 1999, representing a 16.1 % return on equity, a 4.06 % return of assets, both good for a microfinance institution. Financial income represented 64.5 % of total portfolio, financial costs of 19.1 % of portfolio, for a gross financial margin of 45.4 %. Operating costs are still relatively high, at 36.6 % of the loan portfolio, but include provisions for non-collectible loans. However, personnel costs are relatively low, at 14.4 % of loan portfolio.

Financial costs for the year 2000 appear to be lower, only 8.7 % of the loan portfolio through the first 9 months of the year. This is in part because of the method of financing provided by COFIDE has lowered the cost of funds. This year COFIDE is offering loans indexed to the US dollar, which results in lower rates because of lower inflation, rather than Soles based rates of 1999 and earlier.

Currently PROEMPRESA is preparing for its first rating experience. It hopes to achieve the "B" rating, which if repeated a year from now will permit the company to apply for the authority to capture deposits.

Needed Technical Assistance and Training

PROEMPRESA has and is benefiting from donor support to improve its operations. Currently, for example it is cooperating with COPEME to improve its strategic planning and to strengthen the institution. They praised donor support for their institution.

Additional support is needed. This includes training in operations of financial institutions, support for marketing programs, technical skills in credit decision-making and administration, new product development and others. Also human resource development is needed. A lack of adequately prepared people can restrict growth and performance of the company. Proempresa wants to be sure their customers receive the highest quality experience.

The support for microfinance institutions to participate in the Credit Bureau should be continued, especially for regions outside of Lima.

PROEMPRESA is growing and needs additional equity, and would appreciate donors willing to support their growth for the next few years until the company can better attract private investors. A more effective support would be to help them acquire private sector investors, and to progress as rapidly as possible to obtain licensing at Module 1 stage to take deposits.

Finally, the management of Proempresa supports the regulatory institutions gaining better understanding of the operations of microfinance institutions. Regulators visiting microfinance institutions often promote supervisory standards that can hamper operations without improving transparency, security or improve returns. Discussions directly between the microfinance institutions and the supervisory agency are often charged with suspicions on either side of the motives of the other. An intermediary to the process could contribute to better understanding on the part of each side.

Annex A Table 9. Selected Loan Portfolio and Financial Data			
PROEMPRESA EDPYME			
Item	**Sep. 00**	**Dec-99**	**Dec-98**
Loan Portfolio Data			
Total loan portfolio (US$)	3,826,050	2,995,174	3,082,170
Net loan portfolio (US$)	3,515,464	2,783,071	2,990,157
Portfolio at risk > 30 Days (US$)	256,474	144,557	92,465
Loan loss set aside (US$)	310,586	212,104	92,013
Number of loans disbursed in the period	1,857	5,299	3,908
Amount of loans disbursed in the period (US$)	2,426,091	6,707,692	5,917,973
Average size of loans disbursed (US$)	1,306	1,266	1,514
Number of current credits	2,928	2,622	2,598
Number of employees	44	42	41
Number of Analysts	18	14	14
Financial Data			
Fixed assets (US$)	226,785	187,683	212,460
Total assets (US$)	5,786,899	4,267,363	3,746,006
Total liabilities (US$)	4,478,439	3,189,223	2,807,668
Total equity (US$)	1,308,460	1,078,140	938,339
Financial income (US$)	1,535,430	1,930,394	904,792
Financial costs (US$)	332,127	571,573	237,380
Other income (US$)	66,537	38,115	195,847
Total operating costs (US$) *	962,735	1,095,655	805,112
Personal costs (US$)	336,335	432,214	368,690
Profits (US$)	180,518	173,282	2,875
Indicators and Ratios			
Total loan portfolio / Total assets	66.1%	70.2%	82.3%
Net loan portfolio / Total loan portfolio	91.9%	92.9%	97.0%
Portfolio at risk / Total loan portfolio	6.7%	4.8%	3.0%
Loan loss setaside / Portfolio at risk	121.1%	146.7%	99.5%
Financial income / Total loan portfolio	40.1%	64.5%	29.4%
Financial costs / Total loan portfolio	8.7%	19.1%	7.7%
Gross financial margin	31.5%	45.4%	21.7%
Personnel costs / Total loan portfolio	8.8%	14.4%	12.0%
Total operating costs / Total loan portfolio	25.2%	36.6%	26.1%
Profits / total loan portfolio	4.7%	5.8%	0.1%
Profits / Total assets	3.12%	4.06%	0.08%
Profits / Equity	13.8%	16.1%	0.3%
Total liabilities / Total assets	77.4%	74.7%	75.0%
Total loan portfolio / Equity	292.4%	277.8%	328.5%
Total loan portfolio / Analyst (thousands US$)	212,558	213,941	220,154
Number of current credits / Analyst	163	187	186
Exchange Rate	**3.515**	**3.48**	**3.13**
* Includes loan provisiones, depreciation, personnel costs and general operating costs.			

ANNEX A.10 SOLIDARIDAD

EDPYME SOLIDARIDAD began operations in February 2000, and by October of that year reached a loan portfolio of just more than us$600,000. The company was born from the credit operations of the NGO CES (Centro de Estudios Sociales Solidaridad) in and around the northern PerU city of Chiclayo. The NGO, begun in 1978, embarked on its credit operations in 1994. By the time the EDPYME was formed the NGO had developed and implemented four credit products.

SOLIDARAD is a stock corporation owned 98 % by the NGO CES, two natural persons owning the other two percent. The owners select a Board of five people to direct the company. Four key executives administer the company; General Manager, Credit Manager, Account-Administrator and Internal Auditor. The administrative organization is shown in Annex A Figure 10.

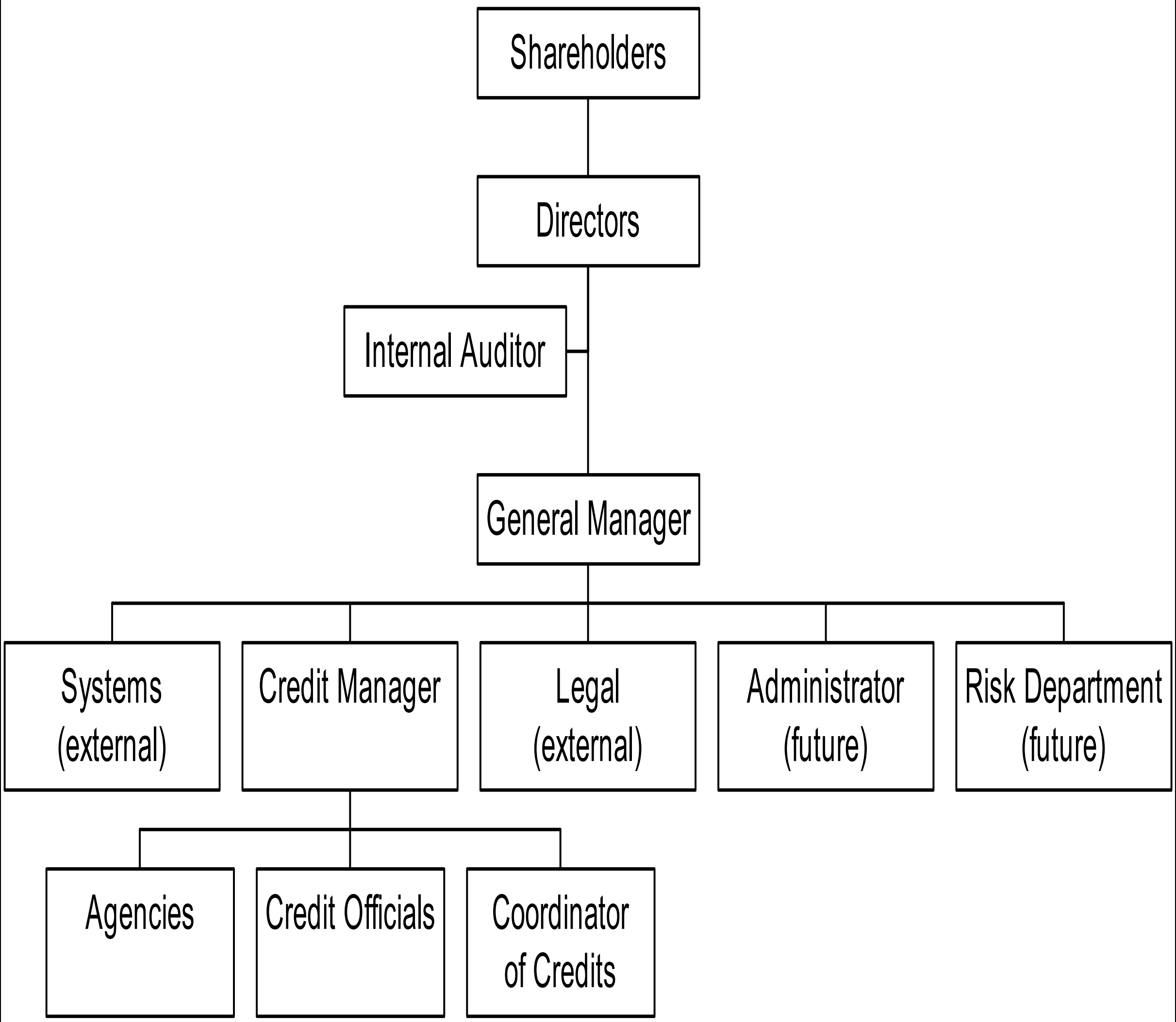
SOLIDARIDAD utilizes an unusual operational technique, that of Operators. Operators are NGOs that do the credit promotion and sales, and are also responsible for collections. They are paid by commission; currently set at 4 %. Of that 4 % commission, 2.5 % is paid upon disbursement, and the remaining 1.5 % is paid upon collection. In addition SOLIDARIDAD may support the Operators by training, some equipment and help with loan placements and collections.

To date the NGOs being utilized by SOLIDARIDAD are CES and another with a longstanding relationships with CES. Therefore, the training and control of the NGOs is not such a large problem. Further, this arrangement allows SOLIDARIDAD to reduce operating costs, by not having to pay salaries and establish offices in all the communities in which they make loans. It also allows SOLIDARIDAD to potentially grow more rapidly than possible by hiring and training their own employees. Continuation of this model to unknown NGOs will require more formalized selection, training and supervision procedures yet to be developed.

When the loan is granted through an Operator the customer pays an additional commission of 4 %, which is passed on to the Operator.

While this is the current model, SOLIDARIDAD recognizes the more traditional approach to establishing company owned and operated offices may also be more effective in some situations, especially when the size of the market justifies. So the company anticipates a mixed form of organizations to deliver services in the most efficient manner to communities both large and small.

Annex A Figure 10. SOLIDARIDAD



Credit products: Individual, Solidarity Group, Community Group

The credit products of SOLIDARIDAD apply to both urban (40 % of loans) and rural (60 % of loans) areas. Rural loans are principally in the area of Lambayeque and Chota (Cajamarca). The four loan products are:

Community banks

Micro loans directed principally to groups of women. Loan amounts range from US$175 to US$2,100, from 1 to 6 months, an interest rate of 56 % in Soles and 23 to 43 % in dollars depending on funds sources, and a commission of 2 to 5 %. Some other charges may apply, and some loans may be granted a grace period before first payment is due. Community banks account for 15 % of loans in 2000. Average loan size is US$137.

Solidarity Groups

Loans for agricultural production and processing. Loan amounts may vary by source of funds, but are generally between US$350 and US$10,000. Terms are from 1 to 6 months (4 months for some funds sources), with an interest rate of 56 % in Soles and 30 % in dollars, and a commission between 2 to 4 %. Some additional charges may apply. No grace period is available. Solidarity group loans account for 19 % of loans in 2000. Average loan size is US$278.

Individual Credits

Primarily directed to microenterprises in urban areas to support productive activities. Loan mount range from US$1,500 to US$100,000, terms from 1 to 36 months for most funds sources, an interest rate of 56 % in Soles and 27 % in dollars plus a commission of 2 to 4 % depending on who originates the loan. Other charges may apply. In 2000 individual loans account for 66 % of loan disbursements. Average loan size is US$2,040.

Shared Responsibility Groups

Directed to support small producers of rice and sugar cane, which have real guarantees. These loans are not reported separately.

Loans may be granted for productive activities (purposes, for commerce and services. Production loans are generally for 36 months; commercial loans are most often for 12 months.

Operations

The operational model of working through Operators and the management team at Solidaridad offers some advantages to micro credit delivery. They are:

Advantages
- Allows more rapid access to existing loan portfolio of non regulated financial institutions, operators may be less than full time
- Commercial focus by management, willing to test product needs of customers
- Communications, data information and payments system is more advanced than typical MFI with less than one year of experience. This should allow more efficient delivery of credit to remote areas and small towns, though efficiency results are not yet apparent. Payments system through Banco de Crédito should reduce costs of establishing local offices in small towns.
- Small headquarters staff, potential for lower cost administration. Loan officers paid nearly entirely by commission.
- Management speaks of their agricultural lending experience. Some time is needed to judge their results.
- Higher level of financial institution management skills than many microfinance sector competitors.

Some challenges confront SOLIDARIDAD, such as:

- Limited equity, the company needs to find other investors.
- Not yet profitable, needs to increase loan portfolio to about $1.8 million (about 3 times current loan portfolio). Acquiring needed funds will be challenging.
- Lack of control over performance of Operators.
- Current commission for Operators is likely to increase as new non-related NGOs are incorporated into system. Needs to carefully plan strategy for incorporation of non- related NGOs as Operators.

A principal need is funding. The company points to several market segments they could address, including increased penetration of existing markets with existing products if they had additional funds. To acquire more funds will likely require increased equity, either directly through selected NGOs or investment institutions.

Loan Portfolio

The loan portfolio has grown to US$451,730 in September, and represents 43 % of total assets. The portfolio at risk is 1.3 %, low, but not so unusual for newly established micro loan companies. As expected loan loss reserves are 118 % of portfolio at risk.

The company has 8 employees including 2 persons to supervise loans issued by the Operators. Because the Operators are institutions and may have several people that process loans, a measurement of loan portfolio per credit analyst and number of clients per credit analyst is not comparable with other institutions in this review.

SOLIDARIDAD uses the payments system of Banco de Creditos. That allows loans to be disbursed and payments collected. There is a monthly fee for this service and well as a per transaction fee, which is paid by the client. The information system queries daily or more often the back to receive data on loan transactions and updates it database accordingly. To facilitate customer utilization at the Banco of Creditos, SOLIDARIDAD issues each loan customer a plastic bankcard. This bankcard carries the logo of SOLIDARIDAD and has a customer name and account number. It does not yet have a magnetic strip to carry data.

Overview of Financial Results

As usual for a start up company, loses exist, US$181,158 though September 2000. As expected, financial income is low for this year, 14.5 % of portfolio, and is not representative of future years. Likewise, financial costs are low, 2.8 % to September. Operating costs are through September are 50.9 % of the loan portfolio.

Needed Technical Assistance and Training

Some needs for technical assistance are the continued development of the “Operator” model for loan marketing, administration and collections. Specifically they could use assistance in:

- Criteria for selection of NGOs,
- Technology for motivation and control of Operators that are non-related to Solidaridad,
- Documenting operational parameters for NGO Operators,
- Training of NGO personnel as loan officers.

Institutional strengthening is also needed, including:

- Communications and control of remote loan officers,
- Compensation system for Operators,
- Continued development of use of plastic “bank” card to assist product delivery and to acquire and retain customers.

Assistance in reviewing of performance for existing products and refining market segments and marketing plans for each product

Capabilities of Working with Donors

Positive elements for donors who may wish to work with Solidaridad are:

- Can work in agricultural production credit, and can reach relatively small towns and remote areas at relatively low cost.
- Can target funds to specific areas and market segments. Some targeted groups or areas will require the donor to subsidize operations as well as provide loan portfolio funding. Other segments will require provision of loan portfolio funds only.
- Company management open to innovative methodologies to reach desired target market.

- Without specific restrictions on the market to serve, the tendency is for Solidaridad to serve customers in the US$1,000 to US$3,000 size of loans.

Some difficult to resolve elements donors may find are:

- Higher risk than many other micro credit operations. This results primarily because of limited equity and existing loan portfolio to cover costs.
- Reliance on Operators increases difficulty of designing donor programs.

Annex A Table 10. Selected Loan Portfolio and Financial Data			
SOLIDARIDAD EDPYME			
Item	**Sep. 00**	**Dec-99**	**Dec-98**
Loan Portfolio Data			
Total loan portfolio (US$)	451,730	n.a.	n.a.
Net loan portfolio (US$)	444,856	n.a.	n.a.
Loan portfolio a risk > 30 Days (US$)	6,040	n.a.	n.a.
Loan Loss reserves (US$)	6,873	n.a.	n.a.
Number of loans disbursed in the period	1,016	n.a.	n.a.
Amount of loans disubrsed in the period(US$)	687,261	n.a.	n.a.
Average size of loan disbursed (US$)	676	n.a.	n.a.
Number of current loans	1,016	n.a.	n.a.
Number of employees	8	n.a.	n.a.
Number of credit analysts	2	n.a.	n.a.
Financial Data			
Fixed assets (US$)	137,047	n.a.	n.a.
Total assets (US$)	1,049,622	n.a.	n.a.
Total liabilities (US$)	574,282	n.a.	n.a.
Total Equity (US$)	475,340	n.a.	n.a.
Financial Income (US$)	65,610	n.a.	n.a.
Financial Costs (US$)	12,780	n.a.	n.a.
Other Income (US$)	19,650	n.a.	n.a.
Total operating costs (US$) *	230,068	n.a.	n.a.
Personnel costs (US$)	110,202	n.a.	n.a.
Profits (US$)	-181,158	n.a.	n.a.
Indicators and Ratios			
Total loan portfolio / Total assets	43.0%	n.a.	n.a.
Net loan portfolio / Total loan portfolio	98.5%	n.a.	n.a.
Loan portfolio at rist / Total loan portfolio	1.3%	n.a.	n.a.
Loan loss reserve / Loan portfolio at risk	113.8%	n.a.	n.a.
Financial Income / Total loan portfolio	14.5%	n.a.	n.a.
Financial costs / Total loan portfolio	2.8%	n.a.	n.a.
Gross financial margin	11.7%	n.a.	n.a.
Personal costs / Total loan porfolio	24.4%	n.a.	n.a.
Total operating costs / Total loan portfolio	50.9%	n.a.	n.a.
Profits / Total loan portfolio	-40.1%	n.a.	n.a.
Profits / Total assets	-17.3%	n.a.	n.a.
Profits / Equity	-38.1%	n.a.	n.a.
Total liabilities / Total assets	54.7%	n.a.	n.a.
Total loan portfolio / Equity	95.0%	n.a.	n.a.
Total loan portfolio / Credit analyst (miles US$)	226	n.a.	n.a.
Number of current credits / Credit analyst	508	n.a.	n.a.
Tipo de Cambio	**3.515**	**3.48**	**3.13**

n.a.: not applicable, SOLIDARIDAD began operations in 2000.

* Includes loan loss reserve, depreciation, personnel costs and general costs.

ANNEX B: ECONOMIC ANALYSIS

Beginning in 1990 the Fujimori administration eliminated nearly all trade, investment and foreign exchange controls, and reduced the size of government through layoffs and the privatization process. The administration's economic restructuring program restored fiscal discipline through tax reform and elimination of most subsidies.

At mid-year 2000, Peru's economy was in the midst of a fragile recovery, with expectations of real growth after two years of recession but continued uncertainty about the GOP's economic policies following President Fujimori's resignation, and in anticipation of the upcoming 2001 elections. Peru continues to suffer the effects of the series of external shocks that hit in 1997 and 1998. This century's severest El Nino, which struck in the second half of 1997, had a dramatic negative effect on Peru's fisheries, agriculture and mining production. The Asian economic crisis, which began in late 1997, compounded the effects of El Nino and resulted in a souring of Peru's terms of trade as metals prices dipped due to a reduction in demand from Asia.

After registering 6.7 percent growth rate in 1997, real output fell 0.4 percent in 1998, with a concurrent drop in exports and imports. The economy began to recover in the second half of 1999, but posted growth of only 1.4 percent for the year, less than population growth. Despite the slumping economy, the GOP has maintained strict fiscal discipline. Inflation is at its lowest level in a decade, dropping steadily from 7.3% per annum in 1995 to 3.5% in 1999. Fiscal discipline combined with the GOP's continuing commitment to allocate 40% of its budget to social sectors has been instrumental in cushioning the socio-economic impact of the financial crises.

During 1998, many companies could not service their high indebtedness, thereby triggering a major restructuring of the financial sector. After a stream of takeovers, mergers and liquidations, the banking system became highly concentrated, with 64 percent of loans and 76 percent of deposits held by the four largest banks by mid-2000. During 1999, commercial bank loan portfolios fell about 17 percent to about $11.0 billion. Equity decreased three percent to US $1.9 billion. At the end of 1999 the Superintendency of Banks and Insurance (SBS) reported that 9.1 percent of loan portfolios were non-performing.

In 1999, the rate of Gross Domestic Investment as a percentage of GDP decreased substantially after being steady since 1995 at an average level of 24%. During three of the last five years, Peru had a positive balance of payments as the current account deficit was financed by the inflow of investment. Exports and direct foreign investments have been crucial to strengthening Peru's BOP in the recent past. Peru's public and private external debt for the medium and long-term is equivalent to 45% of GDP and short-term debt is 10%. Hence, Peru's debt burden still represents a significant pressure on the economy.

If economic factors behave as they have recently, notwithstanding external shocks and barring any dramatic moves by the GOP in the economic front, Peru could anticipate an average growth rate of 4-4.5% per year during the next five years. Nevertheless, it is doubtful that overall economic policies or performance during this period will affect a percentage increase in formal sector employment with respect to the base of employable persons. It is likely the number of microenterprises will increase, thus spurring increased demand for services, including financial services, for this sector.

ANNEX C: GENDER ANALYSIS

The growth of microfinance worldwide is having important gender implications. Peru is no exception. As in many countries, the financial service sector in Peru has for many years been dominated by commercial banks. These institutions are highly formalized and cater primarily to well established, formalized businesses. Because most businesses, both at the ownership and management levels, have traditionally been dominated by men, women have largely been excluded from access to financial services, especially credit.

Microfinance programs are having a revolutionary impact on women´s access to financial services. Many if not most of the micro enterprises in Peru are owned and managed by women. This is true particularly in the area of commerce and trade, where women dominate in purchasing and reselling products of all types, from household goods to candy. Women are also active in small production, in areas such as textiles, food preparation and small farming. Furthermore, in many indigenous households women are the principal managers of money. Therefore, among the poor, women are prime candidates for credit. Financial institutions that provide microfinance services, including S&Ls, EDPYME´s and NGOs, all have a strong focus on women clients. None of these institutional groups has less than 40 percent women clients.

As a result of having access to micro credit, many Peruvian women have lifted themselves out of poverty. With hard work and strong innate business skills, these women used initial small loans for working capital. After increasing their income and re-investing part of this income back into their businesses, women continue to take out successively larger loans resulting in continued growth and income.

The focus of USAID/Peru's MIGA Activity will be on providing microfinance services to the very poor. This will be accomplished working through institutions giving loans under US$400. The predominant microfinance methodology employed at this level is the village banking methodology. This methodology involves a strong emphasis on women. COPEME´s July 2000 Microfinance Bulletin shows that approximately 60 percent of village banking clients were women. In addition to receiving loans, village banking programs provide auxiliary services that train and empower women. Women are taught simple finance and bookkeeping, and are given the responsibility of managing their internal loan portfolios, including both credit and savings services. As they meet regularly in groups, their meetings are often used to teach simple lessons in health or in other areas. These programs empower women both financially and socially. Women at the village banking level start many community level initiatives.

In conclusion, the MIGA Activity will have a strong focus on women, principally through the provision of financial services, and secondarily by training and empowering women with other skills. Activity data at the Intermediate Result level will be disaggregated by gender in order to track the program´s impact on women. The percentage of total loans and the percentage of loans under US$400 will be reported by gender.

ANNEX D: DEVELOPMENT CREDIT AUTHORITY GUIDELINES

Office of Development Credit
Development Credit Authority

Guiding Principles

1. DCA is principally intended for credit enhancement purposes and may be used where (a) the Agency's sustainable development objectives may best be achieved effectively using credit, and (b) the risks of default may be reasonably estimated and managed.

2. DCA is not a separate program but rather a financing tool to be used in addition to or in lieu of grant funding where appropriate. Accordingly, the principles and policies applicable to the use of Development Assistance (DA) grant funding are presumed to be equally applicable to DCA funding, unless otherwise indicated.

3. DCA loans and loan guarantee agreements will be utilized only when the partner is a non-sovereign entity. No sovereign loans or loan guarantees are permissible under DCA.

4. DCA shall be a demand-driven initiative, with Operating Units having primary responsibility for designing, authorizing, and implementing activities in support of approved Strategic Objectives and within Administration and Congressional priorities for assistance.

5. DCA operations require a clear separation of responsibility for assessing the developmental soundness and the financial soundness of each activity, with the later responsibilities entrusted to the CRB and the M/CFO.

6. DCA requires true risk sharing. For loan guaranty transactions, USAID shall not cover more than 50% of a lender's risk unless the CRB otherwise approves.

7. DCA financing shall not be used unless it is probable that the transaction would not go forward without it, taking into consideration whether such financing is available for the term needed and at a reasonable cost.

8. DCA assistance shall be made at or near market rates. Direct loans shall be made at or above the U.S. Treasury cost of borrowing for comparable maturities.

9. DCA fees shall be based on risk with higher risk activities being charged higher fees to the extent feasible, taking into consideration the costs of the development conditionality imposed on the activity.

10. Currency mismatches are discouraged. Currencies earned by DCA activities should match the borrowers' liabilities.

11. DCA is intended to produce greater development impact and increase Agency performance as reported under GPRA. DCA is not intended for budget support or to increase the nominal assistance levels to specific borrowers. Preference will be given to credit enhancement activities that are of a wholesale versus retail nature where USAID agrees to support a broad range of developmentally significant activities that meet defined eligibility requirements.

12. DCA is intended to be used in USAID presence countries in support of Agency Strategic Objectives and in support of Mission-financed policy and institutional reforms. DCA is also appropriate for use as part of an exit strategy in counties where USIAD assistance is being phased out.

13. DCA is intended to address market imperfections. Activities eligible for DCA financing shall have positive financial rates of return.

ANNEX E: PERSONS INTERVIEWED, INSTITUTIONS VISITED

USAID/Peru:
Thomas Geiger, Mission Director
Michael Kaiser, SO2 Team Leader
Jaime Giesecke, Microfinance Specialist
Eduardo Abareda, Program Manager
Samuel Chincaro, Project Management Specialist

USAID/Washington:
Kathleen J. Wu, Credit Risk Supervisory Officer
Paul Sabatine, Credit Risk Supervisory Officer

Consortium of Private Organizations for the Promotion and Development of Small and Micro Enterprises (COPEME):
Armando Pillado-Matheu, General Manager
Francisco Duler, General Manager of the Microfinance Initiative
Ana Jimenez, Deputy Manager, Microfinance Initiative
Carlos Rios, Ranking and Supervision Specialist
Jack Burga, Director

Ministry of Economy and Finance:
Carlos Giesecke, Chief of Investment Office
Milton von Hesse, Agriculture and Rural Development Specialist

Development Finance Corporation (COFIDE):
Jacinta Hamann, Risk Manager

Superintendent of Banks and Insurance (SBS):
Luis Cortavarria, Superintendent
Jose Zapata, Intendent of Financial Institutions
Eduardo Casavilca, Intendent of Financial System Evaluation
Roberto Olivares, Financial Institution Analyst

Small Industry Loan Guarantee Fund Foundation (FOGAPI):
Edgard Coquis Fernandez, General Manager
Lizardo L. Cruchaga, Business Manager

Inter-American Development Bank (IDB):
Odette Zamalloa, Sector Specialist

German Development Cooperation (GTZ):

Philipp Buxx, Assistant to the Director
Gustavo Mendez, Principal Program Advisor

European Union:
Stephane Muller, Deputy Director
Margarita Migallon, Cooperation Attache

Swisscontact:
Juan R. Hagnauer, Representative

Sarona Global Investment Fund:
Gerhard Pries
Alex Escobar

SISEM Systems Development:
Wiler R. Seminario, Director
Johnny F. Oblitas, Systems Director

Arequipa Municipal Savings and Loan:
Willy Escobedo, General Manager
Luis Alberto Gallegos, Manager
Guillermo Nevado, Deputy Operations Manager
Alejandro M. Guevara, Chief, Internal Auditing
Patricia Torres, Chief, Accounting
Jose Manuel Diaz, Chief, Risk Unit

Caritas/Catholic Relief Services:
William Farrand, Microfinance Program Director
Jesus Aguilar, General Coordinator
Carlos Venturo, Administration and Sales Director
Carolina Cueva Schaumann, Project Coordinador

EDPYME Solidaridad:
Moises de la Piedra, General Manager
Pedro Yesquen, Credit Manager

FINCA Peru:
Iris Lanao, Executive Director
Javier Vega, Microcredit Manager
Carlos Gutierrez, Economic Development Manager

PRISMA:
Thomas Fallon, Deputy Director
Javier Vega Diaz

Sullana Municipal Savings and Loan:

Luis A. Leon, General Manager

Solucion:
Guillermo Zarak, General Manager
Danilo Chavez, Manager of Operations and Finance
Carlos Pacheco, Deputy Manager of Planning and Control

Mibanco:
Manuel Montoya, General Manager

Pro Empresa:
Macario Veramendi, General Manager

Habitat Trujillo:
Carlos Diaz, Administrative Manager
Jose Luis Flores, Microenterprise Project Director
Luis Enrique Malpica, Chief of Computer Management
Pedro Mendoza, Credit and Collections Coordinator

Crear Arequipa:
Javier Ernesto Valencia, General Manager
J. Humberto Meneses, Director
Percy Simons, Director
Ralph M. Guerra, Deputy Manager of Administration and Finance

Caja Sur Rural Savings and Loan:
Carlos Collantes, General Manager

EDPYME Edyficar:
Ana Maria Zegarra, General Manager
Nancy Goyburo, Business Manager
Patricia Hurtado, Chief of Systems