MULTILATERAL INVESTMENT FUND
PROJECT ABSTRACT

REGIONAL

TC Numbers: RG-M1030, RG-M1031, RG-M1032, RG-M1033

I. BASIC PROJECT DATA

Country/Region: Regional

Program Name/Number: Micro and small enterprise financing through formal financial institutions in Latin American.

Team: MIF (Tomas Miller, project leader, Carla Bueso (MIF-DEU), Marlene Zoraida Argüello, COF, Nicaragua; Guillermo Villacorta, COF, El Salvador; Fernando Catalano, COF Bolivia, and Edgar Carvajal, COF Ecuador.)
IIC (Jorge Ciurlizza, project leader, Melissa Thiglman, Alejandro Prada, Leg-IIC,)

Date of Request: February 10, 2004

Beneficiary: Micro and small entrepreneurs, small farmers as well as senders and recipients of remittances.

Executing Agencies: The following regulated microfinance institutions (MFI): Banco Precrédito, (ex Financiera Calpía) in El Salvador, Caja de Ahorro y Préstamos los Andes FFP in Bolivia, Financiera Procredit (ex Financiera Confia) in Nicaragua and Sociedad Financiera Ecuatorial in Ecuador (Banco Procrédit).

Financing Plan:

Line of credit	MIF:	US$	7,500,000
	IIC:	US$	7,500,000

This represents approximately 3% of the portfolio growth of these institutions for the next 4 years.

Technical Cooperation :

Executing agencies:	US $	972,000
MIF*:	US $	616,000

* 154,000 Per institution

Tentative Dates: EVP: July 2004

II. BACKGROUND AND PROBLEM STATEMENT

A. Background

2.01 The evolution of microfinance in Latin America has led to the surge of some successful institutions, which operate under the supervision of the banking authorities of their respective countries. The Multilateral Investment Fund has supported their emergence and consolidation by temporarily participating as shareholder in their equity and by providing technical assistance to strengthen their performance and outreach as well as the diversification of their products.

2.02 Expanding the provision of credit and microfinance institutions in the region has been the focus of the IDB group for thirty years. Over the last ten years, the MIF with its central mandate to finance the sector, and its range of investment instruments, has played a significant role in supporting the transition to commercially viable, regulated microfinance institutions. Through direct loans, investments and specialized investment vehicles, MIF has supported the top 40 leading, sustainable microlenders. On a cumulative basis, MIF has approved financing of US $ 57.6 MM in 21 operations.

2.03 Within the last few years, various bilateral, multilateral and socially responsible private investors and funds have also entered this market. MIF has worked cooperatively and actively with these other financiers, taking a lead role in financing the region's microfinance sector and working in partnership with over 30 co-investors.

2.04 The participating executing institutions have similar ownership, lending practices, corporate governance principles and management policies. These institutions had, as of December 31st, 2003, an outstanding loan portfolio of over 149,000 loans amounting to US $ 195.6 million. Their strong growth reflects in the fact, that they were able to increase their loan portfolio during 2003 by US $ 64.5 million, i.e. about 49%. These institutions have been able to substantially improve their financial services to their target group by recently adding remittances and investment loans to their palette and by introducing an ABC cost-accounting system with support of the MIF.

B. The Problem

2.05 In order to sustain their growth, these microfinance institutions have to gain access to additional funding, as they cannot, at this point, obtain the funds to grow solely from deposits of the public. The projections for year 2004 and 2005 call for a growth of the overall portfolio in the range of US $ 87 million and US $ 107 million respectively. Mobilization of deposits in local financial markets are estimated to cover about 60% of the required funding to meet the growing demand for credit.

C. Program Rationale and Additionality

2.05 The rational to structure these transactions together with IIC can be summarized as follows:

MIF has a successful track record in supporting the growth of microfinance institutions at an early stage of their lifecycle, at that time the risk perceived by private and commercial lenders was too high to assume a credit exposure.

2.06 MIF has supported a larger number of similar microfinance institutions as evidence by more than 75 initiatives supported throughout the region. As these institutions grow, their funding needs and the characteristics of the financial instruments demanded increases very rapidly. That is why MIF is increasingly partnering with private social investors and other commercial financiers which have similar mandates and investment objectives as the IIC.

2.07 As the leading successful microfinance institutions become banks and increase their market share in their respective financial and capital markets, the IIC can become an important partner by offering additional services such as B-loans, loan participations and other financial instruments that are closer in nature to the demands of commercial banks and for which IIC has relevant experience.

2.08 The high quality of MIF´s outstanding investment portfolio for microfinance institutions is a reflections of IDB's pioneering role in terms of institutional building, policy dialogue and dissemination of best practices, which has allowed the emergence of a pool of qualifying microfinance institutions in which MIF has been able to invest on a selective basis.

2.09 Microfinance institutions have been able to develop lending methodologies based on cash flow analysis techniques that predict the repayment capacity of microenterprise. MIF has heavily supported the dissemination of these techniques, training of credit officers, and application of technology based systems in order to make credit available to those economic units that do not have collateral to secure loans. A closer look at the credit portfolio of these microfinance institutions shows that the same techniques can be applied to analyze credit of small and medium enterprises, particularly those that are not served by traditional commercial banks because of the high evaluation, structuring, and supervision costs.

2.10 A closer look at the structure of the loan portfolio of these four institutions shows the growth rates in terms of amounts of loans and volume of outstanding credits. As of April 2004, the segment of loans that are smaller than US $ 10,000 comprises a credit portfolio of US $ 131 millions and 128,000 loans with an average loan size of US $ 1,026. These are microcredit loans and this is the segment that will be supported with MIF resources, which will reach out to at least 7,000 clients. It is expected that within the next 4 years this credit portfolio will grow at an annual rate of 25%.

2.11 The other loan category that is growing at a faster rate is the one that reaches out to larger enterprises, with loans in the range of US $ 10,000 to US $ 150,000. The expected growth rate at this category is 38%, it is in this sector where resources from IIC will be allocated. The financial technologies applied to this segment is similar to the ones utilized for microcredit with the only major differences being a longer tenor, a deeper financial analysis and in some cases the requirement of a collateral. The fact that this sector is not being served by traditional commercial banks is reflected by the higher growth rate of these loan category.

MIF and IIC resource allocation
Evolution of aggregated loan portfolio

		Baseline 04/04	Annual Growth	Projected 2008
Loans < US $ 10,000	US $	131,432,153	25%	291,898,593
Number of Loans	#	128,063	17%	213,225
Average loan in US $	US $	1,026		1,369
MIF financing	7,500,000			
Number of Loans	7,310			
Projected Loan Portfolio < than US $ 10,000 in the next 4 years				160,466,440
		Baseline 04/04	Annual Growth	Projected 2008
Loans > 10,000 and < 150,000		76,763,077	38%	279,186,680
Number of Loans		2,778	31%	8,294
Average loan in US $		17,764		33,661
IIC financing	7,500,000			
Number of loans	422			
Projected Loan Portfolio > 10,000 and < 150,000 in the next 4 years				202,423,604

2.12 When dealing with microfinance institutions MIF's focus continues to be the supply of financial products to the microenterprise sector. Emphasis has been given to the design of new products to marginal clientele, such as rural lending, transfer of remittaces, and savings facilities. The IIC's mandate calls for the support of small and medium enterprises, to the extent that these targeted clientele are reached through the same institution, joint projects like the one here proposed are justified.

2.13 A joint team project with IIC and MIF staff members is evaluating the four participating execution institutions. The evaluation, due diligence and structuring of the transactions has benefited from MIF's participation because of its past dealings with these institutions, knowledge of the industry, and institutions (direct and indirect), understanding of the market terms and conditions (pricing, tenor and monitoring benchmarks), and the design of legal documentation to support, disbursed, collect and supervise these credit facilities. IIC is providing its experience in risk assessment, analyzing these institutions not only as outlets to reach out to microenteprises and small enterprises but rather as banks that are creditworthy and committed to SME financing.

2.14 Together, the skills and experience of the IADB group members will analyze and resolve the financial and developmental aspects of these investments. The project will be submitted individually by MIF and IIC to each of its authorities for ultimate approval.

2.15 Although presented as one project because of the common denominators, common management practices, ownership, corporate governance, and lending technologies, the evaluation and risk assessment is being performed separately for each participating institutions. Because of the similar ownership, it has been possible to introduce a cross default clause will linked the four institutions, so that if one executing institutions defaults the remaining three will automatically also be on default. This feature allows that the weaker institutions and the ones operating in riskier macroeconomic environments received, relative to their equity, more funds from MIF/IIC.

III. PROGRAM OBJECTIVES AND DESCRIPTION

Objectives

3.01 The objectives of the program are: a) to provide funds at commercial terms in order to support the growth objectives of these financial institutions so that they can increase their loan portfolio in at least 13,200loans over the next 2 years and b) to support the introduction of measures to better serve senders and receivers of remittances with adequate financial products.

Description

	Credit Line	Technical Cooperation
MIF Funding	**7,500,000	*616,000
IIC Funding	7,500,000	
Locally Mobilized funds	15,000,000	
Microfinance Institutions		972,000
TOTAL	22,500,000	1,588,000

*evenly distributed among the four executing agencies.

** see table 1 for distribution

3.02 MIF and IIC will earmark a combined exposure of US $ 15,000,000 distributed among the participating microfinance institutions as follows:

Table 1 Lines of Credit

MFI	MIF	IIC	Local Funds	Total MIF-IIC
Caja de Ahorro y Préstamo Los Andes-Bolivia	$ 2,000,000	$ 2,000,000	$ 4,000,000	$ 4,000,000
Banco Procredit (ex Financiera Calpia -El Salvador	$ 2,000,000	$ 2,000,000	$ 4,000,000	$ 4,000,000
Financiera Procredit (Financiera Confia)-Nicaragua	$ 1,250,000.00	$ 1,250,000	$ 2,500,000	$ 2,500,000
Banco Procrédito- (Ex - Sociedad Financiera	$ 2,250,000	$ 2,250,000	$ 4,500,000	$ 4,500,000

Ecuatorial)Ecuador				
Total	$ 7,500,000	$ 7,500,000	$ 15,000,000	$ 15,000,000

3.03 Interest rates: The interest rate of the credit lines will reflect the inherent risk of each institution and the market in which the institution operates. The following are the interest rate levels expected to be charged: Caja de Ahorro y Préstamo Los Andes S.A. Libor six months plus 375 to 400 basis points (L + 375 to 400 Bps), Banco Procredit S.A. in El Salvador (ex-Financiera Calpia) (L+ 375 to 400), Financiera Procredit S.A. in Nicaragua (ex Financiera Confia) (L+400 to 500), Banco Procredit S.A. in Ecuador (ex Sociedad Financiera Ecuatorial) (L + 375 to 525).

3.04 Tenor: The lines of credit will have a 6 year maturity. Draw-down will have a two year horizon, with quarterly amortizations. Renewal draw-downs will be subject to satisfactory financial and outreach (developmental) results.

3.05 Expected results: Financial results will be monitored based upon the pre-agreed levels in the following areas: quality of assets, solvency, leverage, and liquidity measures. Developmental results (outreach) will be monitor based on the results reached in terms of number of clients served, composition and structure of the loan portfolio, and the flow of remittances.

3.06 Non reimbursable technical assistance: MIF will contribute US $ 154,000 for each one of the participating microfinance institution to continue innovating, monitoring the evolution of remittances and other products and to refine products to adjust them accordingly. The participating institutions will introduce a card to card transfer technology to facilitate sending money to Nicaragua, Ecuador, El Salvador and Bolivia. In order to facilitate the distribution of remittances especially in remote rural areas, an internet platform for payments using the sender´s debit/credit cards will be installed. A network of 5 ATM per institution will be installed in remote areas to facilitate the distribution of remittances among the clientele.

3.07 The four banks have currently 14,000 clients that receive remittances on a monthly basis. With this project debit cards will be issued to existing clients so that new financial products can be designed to better serve senders and receivers of remittances.

3.08

	El Salvador	Ecuador	Nicaragua	Bolivia	Total
Potential Share of the current # of remittance Transactions	6%	4%	6%	7%	5.80%
Current volume of operation *	1.86	0	0.24	0.14	2.24
Expected volume of operation in 36 months*	5.04	3.04	3.57	1.42	13.07

* monthly flow of remittances in US $

It is expected that these institutions will be able to capture approximately 5% of the remittances market in their respective countries. The table above shows the current monthly flow of remittances of these banks and the level that is expected to be reached through this project.

3.09 MIF´s technical assistance will partially cofinance : a) client information, marketing and training (US $ 200,000), b) research and product development (US $ 100,000), Procesing Center (US $ 36,000), development of internet platform (US $ 180,000), training of staff (US $ 100,000).

IV. COST AND FINANCING

4.01 MIF's total exposure will be US $ 7,500,000. The same will be true for the IIC. Table 1. shows the breakdown of the resources among the four microfinance institutions.

Table 2.

MFI (December 2003)	Assets	Equity	MIF Exp./Equity	IIC Exp./Equity
Caja de Ahorro y Prestamo Los Andes-Bolivia	$98,688,000	$11,734,000	17.0%	17.0%
Financiera Calpia (Banco Procredito)-El Salvador	$86,577,000	$14,967,000	13.4%	13.4%
Financiera Confia (Financiera Procredito)-Nicaragua	$31,198,000	$5,500,000	22.7%	22.7%
Sociedad Financiera Ecuatorial (Banco Procredito)-Ecuador	$26,117,000	$9,376,000	24.0%	24.0%
Total	$242,580,000	$41,577,000	18.0%	18.0%

4.02 Compared to the accumulated capital base of these MFIs, the relative aggregated exposure of MIF and IIC will be 18% with a higher percentage in the institutions operating in Nicaragua and Ecuador.

V. EXECUTING AGENCIES

5.01 MIF has had a satisfactory business relationships with the executing agencies through previous direct transactions or through some of MIF's investment funds. In some cases a long standing relationship was initiated through the IDB's support to NGO's that originated these MFIs.

5.02 The following table shows the date at which MIF, as investor, donor, or lender first engaged in business relationships with these institutions.

	First established business relationships with MIF/IDB			CURRENT (Dec. 2003)	
	Date	Number of clients	Credit Portfolio	# Clients	Current Portfolio
MFI					
Caja de Ahorro y Prestamo Los Andes-Bolivia	1995	15,954	6,000,000	53,213	82,179,000
Financiera Calpia (Banco Procredit S.A.)-El Salvador	1994	3,468	1,988,000	64,346	75,672,000

Financiera Confia (Financiera Procredit S.A.)-Nicaragua	2000	9,041	14,006,000	32,800	27,000,000
Sociedad Financiera Ecuatorial (Banco Procredit S.A.)-Ecuador	2001	386	539,000	12,752	26,000,000
Total		28,849	22,533,000	163,111	210,851,000

VI. MAJOR ISSUES

5.03 A thorough financial evaluation to assess credit methodology, quality of assets, solvency, gapping analysis, liquidity situation is being carried out for each of the these institutions. IIC has been leading the financial analysis and coordinating with MIF the structure of the transaction and the terms and conditions.

VII. ACTION PLAN

6.01 A joint presentation (MIF, IIC) will be made to the extended credit committee during the month of June, 2004.
Submission to EVP is expected to be done by July 2004
Approval by MIF donors committee will be seeked during the month of August.
The IIC board of directors is expected to approve the project by August.

VIII. SOCIAL AND ENVIRONMENTAL IMPACT AND PROPOSED MEASURES

7.01 Both the IIC and MIF policies on social and environmental policies will be taken into consideration for project execution. The four microfinance institutions are not directly engaged in activities that have potentially deleterious environmental effects. The clients of these institutions seek on average loans that are less than US $ 2,000, work in the majority of case in the trade and service sector which generally do not have adverse impacts on the environment. Nevertheless, in order to mitigate any potential risk, MIF will take the following precautionary steps: a) Each MFI will be provided a list of highly polluting industrial sectors and those enterprises operating in these sectors will not be eligible to receive financing with MIF funds unless a cost-effective mitigation plan is presented, b) the MFIs will be obliged to be in compliance with local environmental norms and regulations, as well as to not be in violation of any child labor and forced labor laws, rules and regulations.