

Document of the Inter-American Development Bank
MULTILATERAL INVESTMENT FUND

HAITI

EXPANDING THE PSYCHOMETRIC CREDIT-SCORING TOOL TO HAITI

(HA-M1047)

DONORS MEMORANDUM

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ABBREVIATIONS

| | |
|---------|--------------------------------------|
| CID | Center for International Development |
| EFL | Entrepreneurial Finance Lab |
| ESR | Environmental and Social Review |
| IFC | International Finance Corporation |
| LAC | Latin America and the Caribbean |
| MIF | Multilateral Investment Fund |
| PSR | Project Status Report |
| MSE | Micro and Small Enterprise |
| SME | Small and Medium Enterprise |
| SOGESOL | Société Générale de Solidarité |

EXECUTIVE SUMMARY

| | | | |
|--|--|-------------|-----------------------|
| Country: | Haiti | | |
| Executing Agency: | Société Générale de Solidarité (Sogesol) | | |
| | MIF will execute Component III. | | |
| Beneficiaries: | 2,000 Haitian Micro and Small Enterprises (MSEs) | | |
| Objectives: | <p>The general objective of the project is to increase access to finance for micro and small enterprises in Haiti. The specific objective is to implement an innovative credit-scoring tool based on psychometrics to unlock financing for micro and small enterprises in Haiti, which are primarily managed by or hire poor people.</p> <p>The Entrepreneurial Financial Lab (EFL) has developed a unique approach that uses psychometric assessments as a viable, low-cost, automated screening tool to identify growth-oriented SMEs, and to evaluate their risks. The use of psychometric tools to determine entrepreneurial ability and honesty offers huge potential in terms of increasing access to significant levels of bank finance for MSEs.</p> <p>This project will complement the regional project “<i>Rolling out a Psychometric Tool for Expanding Small Business Finance</i>” (RG-M1203) by the incorporation of Haiti as an additional beneficiary country.</p> | | |
| Financing: | MIF Non-reimbursable ¹ : | US\$ | 340,750 (72%) |
| | Local: | US\$ | 133,000 (28%) |
| | Grand total: | US\$ | 473,750 (100%) |
| Periods: | Execution period: | 30 | months |
| | Disbursement period: | 36 | months |
| Exceptions to the Bank policies: | None | | |
| Coordination with other development agencies: | IFC, as administrator of the G-20 Innovation Fund, co-finance the Regional MIF project RG-M1203 that will support this project. | | |
| Special Contractual Conditions: | SOGESOL has to sign a letter of understanding with EFL, detailing the commitments and responsibilities during the implementation of the psychometric tool, as an especial condition to the project. | | |
| Environmental and Social Review: | The Bank’s environmental review process cleared the project on May 14, 2012. Classified as a category “C” operation. | | |

¹ Out of the MIF contribution, US\$10,000 will be assigned to the corresponding MIF Agenda Account, and US\$15,750 to the MIF Impact Evaluation Account.

I. BACKGROUND

A. Haiti's Socioeconomic Situation

- 1.1 Nowadays, Haiti is gearing up to rebound, facing new opportunities. In order to ensure that these efforts materialize, it is important to support the sustainable growth of micro and small enterprises (MSEs) as those firms are expected to play a key role in creating new jobs and helping the country to achieve sustainable economic growth.
- 1.2 As described in the Inter-American Development Bank's Country Strategy with Haiti, the country faces poverty and inequality challenges. Extreme inequalities among Haitians - income disparity and regional imbalances, lack of access by most to quality education, electricity and water and sanitation, and under-investment in agriculture and basic infrastructure - together with an inadequate business climate inhibiting private sector development have combined to weaken the stability required for sustainable growth and social progress.²
- 1.3 Despite these challenges, in 2009 the country registered the highest growth rate in the region (2.9%) after averaging 1 percent during the 1960-2005 period. The January 2010 earthquake interrupted this positive trajectory when the country experienced the greatest humanitarian emergency on record in the region.³
- 1.4 Both the government of Haiti and the international community agree the transition from emergency relief to sustainable recovery and growth will reveal additional challenges and that the years ahead are clearly the opening "to turn the earthquake into a window of opportunity". There is a shared recognition that long-term, substantial targeted support is required to move Haiti onto a path of sustained development that delivers economic growth as well as solutions to enduring social and environmental problems. It is equally recognized that strong Haitian ownership is sine qua non for this long-term support to be effective.⁴
- 1.5 The World Bank Group's *Doing Business 2011* ranks Haiti 31 out of 32 economies in LAC, and 162 out of 183 in the economies in the world. The lack of access to finance for Haitian MSEs in the formal and informal sectors have limited the MSEs sector contribution to economic development and job creation in different industries such as textile, agribusiness, and others. One of the main barriers that affect MSEs access to finance is the difficulty in providing real collateral. For example, 82% of Haitians do not hold clear title to their land or home⁵. Additionally, there is no functioning credit bureau in the country, and MSEs often operate without employing generally accepted accounting standards, which make credit assessments by financial institutions very complicated.

B. MIF Regional Project

- 1.6 The MIF has partnered with Entrepreneurial Finance Lab (EFL), launched by researchers at Harvard University, who have developed an innovative approach for assessing small enterprises' creditworthiness. Academic research has recently uncovered systematic

² Country Strategy with Haiti (2011-2015). GN-2646.

³ *Idem*

⁴ *Idem*

⁵ The Woodrow Wilson School's Graduate Policy Workshop: Growing the Middle: January, 2011

associations between entrepreneurial success and personal attributes measured with a scientific and statistics-based tool: psychometrics. Successful entrepreneurs consistently score higher on certain aptitude tests and have particular personality traits and cognitive styles. This type of screening has already been used extensively for pre-employment screening. The psychometric tool evaluates people rather than business. Specifically, it measures personality, intelligence, and character as direct indicators of a borrower's ability and integrity. The main advantage of this approach is that it does not rely on well-prepared financial statements, business plans, or borrowing history, and at a transaction cost that would allow for massive scale-up.

- 1.7 The MIF regional Project: “*Rolling out a psychometric tool for expanding small business finance*” (RG-M1203) is currently implementing the methodology in two financial institutions in Latin America (more precisely in Mexico and Peru) and two additional financial institutions will be selected in the following months, in addition to Haiti. The project will also further improve the power of the tool for identifying growth-oriented MSEs and evaluating their risk. Once further implemented, this tool could represent a breakthrough in scalable, replicable, and profitable lending to the missing middle, and may correct distortions that restrict productive SME growth, thus contributing to creating productive jobs and dynamic long-term economic growth.

C. Implementing the Psychometric Tool in Haiti:

- 1.8 The psychometric approach gets back to the basics of financial risk assessment related to the person rather than the business. The premise is that in order to invest effectively, one ultimately cares about identifying an entrepreneur's future cash flows. Screening tools should then measure two characteristics of entrepreneurs: their “ability” and “honesty,” which are critical in determining their creditworthiness (i.e., “willingness to pay” and “ability to pay”). While ability means whether a person can invest profitably, honesty determines whether a person would pay back if he/she is able to do so.
- 1.9 The testing process involves a 30-40 minutes automated assessment, analyzing key dimensions related to intelligence, business skills, and psychological parameters including ethics. It is important to note that the test is structured to evaluate the person objectively, avoiding potential biases often caused by human-based assessments. It is also meant to resolve the issues of high transaction costs.
- 1.10 In order to implement the tool in Haiti, this project will add the EFL questionnaire as a mandatory part of the application process for all Sogesol loan applicants seeking an amount equivalent to USD1,000 or more. This tool will be applied to new-to-bank clients as well as existing clients who apply for loan renewal. This “testing phase” will take place over a period of 12 months, giving an approximate sample size of 3,000 individuals. Their loan repayment data will be provided by Sogesol and processed by EFL to adjust the predictive model to the Haitian culture and context, as well as Sogesol's specific market segments.

D. Justification

- 1.11 Haiti has a significant need for innovative tools to better assess and identify the MSEs risk through the scarce information available. In that sense the psychometric tool could become a powerful means for unlocking financing to the unattended business segment.

- 1.12 The psychometric tool has been successfully implemented in Africa by Standard Bank. This case provides clear evidence of the effectiveness of the tool and its particular benefit for female clients. Standard Bank, the largest commercial bank in Africa, is placing loans to new or previously rejected SME clients in 9 countries in Africa and they have a goal to extend the use of the tool to 4 additional countries by the end of the year, for a total of 13 countries. For example, within only a few months of launching the tool in Kenya, Standard Bank was providing over \$1 million per month in unsecured working capital loans to small businesses (average loan size of \$7,000) that were previously not bankable because of lack of information, and that segment went from 0% to 20% of the bank's new lending country-wide.
- 1.13 The Kenyan example highlights the usefulness of this tool for women borrowers. It has been found to work better for women than other credit scoring tools, as fewer women are rejected for credit. Importantly, the African pilots have uncovered no differences between men and women in key personality traits associated with entrepreneurial success, and the same psychometric variables predict risk for males and females. As a result, both women and men in the African pilots have increased access to finance with the psychometric tool than through traditional credit scoring; however, given women's traditionally lower rates of borrowing as compared to men, this tool has brought comparatively more benefit to women. In Kenya, just over half of the applicants were female (51%), and proportionately more women were selected in the pilot approved clients (53% were women). In comparison, most Kenyan commercial banks average 42% women in their client base.
- 1.14 However, through piloting, the test has been found to more consistently predict entrepreneurial aptitude in males vs. females, signifying a higher predictive power for men. That is, on average, women do not answer the questions as consistently as their male counterparts. Therefore, as a predictive tool, the test plots men's expected behavior more accurately (how much more accurately is still being studied), but as a credit screening tool, the test consistently works better for both women and men than other options available and has brought undeniable benefit to previously rejected (male and female) clients. A traditional credit history-based screening tool has a model degradation of 36% from males to females. The psychometric tool still has model degradation, but it drops to 15% from males to females, more than halving the disparity between lending to men vs. women. The reduction in model degradation is due to the psychometric test's use of variables for honesty, calmness/steadiness, and dependability/dutifulness, which have proven to be stronger differentiators of risk for women than traditional credit screening models, which are often based on credit history, collateral, and fixed assets that women traditionally do not have.
- 1.15 Given the clear benefit this tool has brought Kenyan women borrowers; the tool is now being tested in Mexico (Bancomer) and Peru (BanBif) to see if results are similar. While the average loan size with Standard Bank is notably higher than Sogesol's (\$7,000 vs. \$800), the versatility and consistency of the tool are expected to serve Haitian female micro and small enterprises with similar levels of success as Kenyan female small business owners. The initial focus of the project will be the upper micro and small business segment with financing need over \$1,000.

- 1.16 The results of these tests have been statistically analyzed by comparing the scores of the tested entrepreneurs to their actual business performance and loan repayment history. The evaluation methodology is a standard logit probability of default model.⁶ EFL's out of time and out of sample testing reveals that the results are very stable, and have stood the test of independent evaluations by risk departments at third party financial institutions. Simulated implementations suggest a 20-45% reduction in default and a 15-30% increase in profits, with less than 40% of the cost of traditional evaluation and due diligence. Overall the test exceeded the predictive power of traditional credit-scoring models in developing countries which use audited financial statements and credit history. Moreover, the model contains certain dimensions that are consistent across cultures; although average levels are different, the key dimensions of ability and risk attributes for a microenterprise owner or an SME owner do not change across countries.
- 1.17 The situation faced by some African countries is similar to the Haiti context; therefore, there is enough information available that will help the psychometric approaches to become a powerful tool to unlock financing to underserved male and female Haitian small enterprises. Furthermore, given the particularities of Haiti and having a language other than Spanish-English, which is not available within the staff hired by the regional project, it is essential to have a full time professional, French and/or Creole speaker, completely dedicated to the implementation of the tool in Haiti. In that sense, the regional project does not count with extra resources to implement the tool in Haiti and the tools also has to be translated to French and Creole.
- 1.18 Furthermore, after the successful launch of the Sogesol testing process, ideally the testing will be extended to other financial institutions such as Sogebank and/or Fonkoze. The methodology that would be used to incorporate these two financial institutions to the project will be determined by the EFL during implementation of the Sogesol testing.
- 1.19 **The MIF and Bank Strategy.** This project is consistent with MIF's private sector development and poverty-alleviation goals, and supports the goals of the SMEs Finance Agenda, "Innovative Models for Small Business Lending," which seeks to expand financial services specifically targeting the small business segment by developing upscaling models for microfinance institutions and downscaling models for commercial banks. Additionally, the project is aligned with the objectives of the "Haiti Social Investment Fund" funded by The Spanish Government and managed by the Inter-American Investment Corporation. The Haiti Social Investment Fund was designed to increase the availability of loans for Haitian SMEs while reducing borrowing costs.
- 1.20 Furthermore, once EFL's tool is well adopted in Haiti, this project aims to scale up and complement the IDB's initiative "Business Development and Training Services Program for Investment in Haiti." -HA-L1057- (IDB's BDS Program). This program would support the provision of Business Development services to facilitate the access of productive units to credit or to enhance the productivity and profitability of new entrepreneurial investment projects to be financed through new loans.

⁶ The results show that the EFL assessment can predict default with an AUC (a common summary metric to evaluate credit scoring models) of 0.752 (equivalent to a Gini of 0.5), with all individual relationships significant at the 95% level. To translate this into default rates, in one sample with overall default rate of 12%, the top 5th of scorers on the EFL assessment have a default rate of just under 3.4%, while the bottom 5th have a default rate in excess of 26%.

II. OBJECTIVES AND BASIC COMPONENTS OF THE PROGRAM

A. Objectives

- 2.1 The general objective of the project is to increase access to finance for micro and small enterprises in Haiti. The specific objective is to implement an innovative credit-scoring tool based on psychometrics to unlock financing for micro and small enterprises in Haiti, which are primarily managed by or hire poor people.

B. Components and Activities

1. Component I: Pilot Implementation to Adjust the Psychometric Tool to the Local Market (MIF: \$170,000, SOGESOL: \$64,500)

- 2.2 The objective of this component is to implement the psychometric analysis tool in Sogesol by adjusting it to the local market context and gathering information on how make it robust. The test will be applied at time of loan disbursement. Normally, the application of EFL tool is conducted during loan officers' field visit to potential clients, rather than at the branch offices at the time of loan disbursement, but testing with computers in the field during these earlier stages of the process is not feasible because of the large number of loan officers, and concerns about security. During this phase Sogesol might use the EFL score as part of the credit granting decision, but the main purpose is to increase the robustness of the tool to the local conditions. It is expected that this phase will take between 12 and 18 months.
- 2.3 The specific activities include the followings: (i) development of pilot implementation plan; (ii) customization and programming of the tool; (iii) translation of the tool into Creole and French; (iv) IT infrastructure for pilot implementation of the pilot; (v) training Sogesol's staff involved in the pilot implementation;⁷ (vi) perform the test on loan renewals and new loans; and (vii) tool re-calibration based on the results. This last activity is important, as it deals with an analysis of the ability of the model to separate risk among potential loan recipients. During the adjusting phase of the tool, it is important to align client incentives. Replying to the EFL application needs to be a high-stakes situation, otherwise response patterns are biased. If clients know they have already been approved for their loan when they come into the branch for loan disbursement, they have little incentive to put effort into the test. There are two possibilities to create a high-stakes situation that are planned to be used in this project:
- (i) Clients will not be informed that their application has been approved until after taking the test. Both clients and loan officers have to be under the impression that their performance on the test is relevant for the loan decision.
 - (ii) If clients have to be told that the application has been approved in order to get them to come into the branch for disbursement, they need an extra incentive based on their performance on the test. One example is to add a \$25 application fee that is then waived based on performance on the test.

⁷ The process is simple, but it is important that the entire staff of the branch knows how to administrate the test, since the ideal is that a client walking into the branch applying for a MSE loan could be guided by anyone to the testing device or terminal and do the test on their own.

- 2.4 The expected results are: (i) 17 branches have acquired the psychometric risk-assessment tool and received training; (ii) the tool has been administered to 3,000 clients; (iii) data on repayment rates for each accepted client collected 6 month after the test with comparative analysis of the test scores; and (iv) statistically validated results in terms of the tool's predictive power as well as the financial viability of lending to these previously ignored market segments.

2. Component II: Mainstream Implementation of the Psychometric Tool (MIF: \$105,000, SOGESOL: \$38,500)

- 2.5 Once the psychometric tool is adapted to the local environment and its predictive power assessed, a proposal for mainstreaming the use of the tool within Sogesol will be developed. In this stage, Sogesol will provide the financing needed for the new loans at its own risk, or potentially using guarantee programs if available. The idea is to revisit Sogesol's internal approval process and procedures that have excluded most of the potential clients, and use a modified application process with some traditional credit scoring evaluation in conjunction with the psychometric application.⁸
- 2.6 Additionally, a broader strategy to scale up the project in Haiti will be developed by EFL. The BDS Program will be a main piece of this initiative by partially or totally (to be defined) converting the cost associated to the deployment of the tool in other financial institutions.
- 2.7 The specific activities include steps to: (i) analyze pilot results and develop a proposal for mainstreaming implementation of the tool; (ii) mainstream implementation; (iii) integrate to the IDB BDS Program; and (iv) conduct psychometric tool maintenance and customization based on increasing results.
- 2.8 The expected results are: (i) a mainstreaming proposal for the psychometric tool integration in Sogesol decision making has been developed and is being implemented; (ii) the tool unlocking financing to at least 1,000 small enterprises; (iii) a scaled-up model using the BDS program under execution; and (iv) a system in place in order to continuously adjust the tool for increasing predictive power based on fresh information gathered from new loans.

3. Component III: Dissemination of Project Results (MIF:\$30,000, Sogesol: \$0)

- 2.9 The objective of this component is to share the results of the projects with other local financial institutions in Haiti, to extend the impact of the project. Information such as the predicting defaults, improved financial performance of Sogesol, and the expanded access to finance will be constantly collected by EFL and documented. Lessons learned would be identified by rigorously analyzing the data from the implementation in Sogesol, systematizing the best practices in the approach of using psychometric principles for evaluating credit risk, and disseminating them to a broader set of stakeholders engaged in small business finance in Haiti. The main goal of this component is to promote effective communication to enhance the impact of the project and to provide those who need it

⁸ For example, instead of requiring a fixed amount of years of business history and a big amount of collateral, the FI may allow applicants to apply with less history and no collateral as long as they reach a certain level of the psychometric application.

with knowledge of what works, in order to catalyze behavioral changes among a broader number of financial institutions in Haiti.

- 2.10 The dissemination will be achieved by developing case studies summarizing the experience, and a specialized workshop with Haitian financial institutions and other related institutions. During the project execution the possibility of conducting an impact evaluation will be assessed; however, it is not foreseen as a viable option at the current stage.
- 2.11 The activities contemplated include: (i) development of case studies; (ii) development of a workshop to share the results with Haitian financial institutions and other interested local institutions. The outcome of this component will be: (i) case studies with the results of the project and lesson learned published and disseminated; (ii) at least 80% of Haitian financial institutions participate in a workshop to share the project results.
- 2.12 Even though the executing agency is Sogesol, this particular component will be executed by MIF in order to assure a proper documentation and dissemination of the project results. MIF/KSC will be in charge of this component.

III. COST AND FINANCING OF THE PROGRAM

- 3.1 The total estimated budget amount is US\$473,750. The MIF will contribute US\$340,750 on a non-reimbursable basis. The Executing Agency will provide local counterpart of US\$133,000.
- 3.2 As part of the cash counterpart, Sogesol will be asked to finance with their own resources acquisition of the testing devices and installing them in their branches.⁹
- 3.3 The estimated period of execution is 30 months and the estimated period of disbursement is 36 months.

| BUDGET CATEGORIES | MIF | SOGESOL | TOTAL | % |
|----------------------------|----------------|----------------|----------------|--------|
| Coordination and Logistics | 0 | 20,000 | 20,000 | 4.46% |
| Component I | 170,000 | 64,500 | 234,500 | 52.34% |
| Component II | 105,000 | 38,500 | 143,500 | 32.03% |
| Component III | 30,000 | 0 | 30000 | 6.70% |
| Evaluation | 10,000 | 0 | 10000 | 2.23% |
| Contingencies | 0 | 10,000 | 10,000 | 2.23% |
| SUBTOTAL | 315,000 | 133,000 | 448,000 | |
| <i>Percentage</i> | <i>70%</i> | <i>30%</i> | <i>100%</i> | |
| Impact Evaluation Fund | 15,750 | - | - | |
| Agenda Account | 10,000 | - | - | |
| TOTAL | 340,750 | 133,000 | 473,750 | |

⁹ Based on the experience, the EFL uses touch screen netbooks, which make the taking of the test easy for any level of computer knowledge. The test results will be transferred via internet, therefore every device will be equipped with an internet access, so that at the end of each day the tests can be transferred to EFL's servers and be analyzed, and within 24 hours the result is sent back to financial institution's central risk control.

- 3.4 **Sustainability.** The sustainability of the project will come from the good implementation of the model and proof of the power of predictability of the tool. If the psychometric tool proves to have sufficient predictive power for profitable lending as it has been shown in Africa, the financial sustainability of the initiative will come from the financial institutions that will be willing to pay for the service. Additionally, the IDB's BDS program could support some local financial institutions (those that are members of the BDS program) by financing the "per test" cost fee associated to the use of the technology. At the end of the project, the psychometric credit-scoring tool will be available to all the Haitian financial institutions. Finally, the tool could be used in the country for other non-financial activities such as the selection of the best candidates for a specific project with limited resources.

IV. KNOWLEDGE CAPTURING AND SHARING

- 4.1 This project will have an entirety connection with the regional project which is under execution by EFL, in order to support the comprehensive strategy to maximize knowledge capturing and sharing to catalyze potential systemic changes. Giving MIF's support and commitment to Haiti, the knowledge generated and captured by the project will be used for best practices and lessons learnt outside and within the institution, for that reason the project would have a component III dedicated to dissemination of project results by a case study and a workshop to share the results of the project with other local financial institutions.

V. EXECUTING AGENCY AND EXECUTION MECHANISM

- 5.1 In 1999, a Senior Manager at Générale Haïtienne de Banque S.A. Sogebank, Haiti's largest commercial bank, became interested in microfinance after observing successful experiences in other regions. He was convinced that microfinance offered Sogebank an opportunity to achieve both social and business objectives and he persuaded the decision makers at the bank to explore new possibilities. In August 2, 2000, Sogebank as parent company created the **Société Générale de Solidarité (Sogesol)**, an independent commercial micro-lending institution using a "service company" model. The Company has its headquarters in Port-au-Prince. Sogesol is committed to the mission of promoting Haitian entrepreneurship through adapting traditional banking methods to respond to the needs of micro and small entrepreneurs.
- 5.2 Sogesol expressed interest in implementing the psychometric tool after the MIF-EFL joint mission to Haiti during which the EFL's psychometric tool methodology was presented to local financial institutions. In terms of the size, terms and conditions: (i) Sogesol provides US\$450-500 loans to 10,000 clients (ii) Sogesol has an increasing base of clients; and (iii) final rate applied to Sogesol's clients (including disbursement fee, commissions, etc) is 28%. Furthermore, Sogesol plans to strength SME segment, and has already invested US\$5 million in SMEs.
- 5.3 Sogesol was created in 2000 by its parent company, Sogebank, in order to reach a broader client base, and currently has a gross loan portfolio of US\$17.1 million and 21,642 clients (58.9% are woman). The assets of the company are US\$22 million. The institution's Return on Assets is 2.12% and its Return on Equity is 18.31%. The

portfolio at risk over 30 days is 10.21% and over 90 days is 7.99%.¹⁰ The main promoter of this project is Sogesol's General Manager Daphne Loussaint Héraux.

- 5.4 ProFund, the first-ever microfinance equity fund in which MIF invested, provided to Sogesol an equity investment of US\$205,000, and to Sogebank a subordinated loan of US\$400,000. The latter was used for the loan portfolio growth of Sogesol. ProFund was liquidated in 2005. ProFund presence on the Sogesol board reassured other investors, and the outside world, that the MFI remained viable despite its complicated circumstances. During the period the ProFund was shareholder of Sogesol, the institutions grew from 517 to 7,086 clients and from a portfolio of US\$1.4 million to a portfolio of US\$4.9 million.
- 5.5 **Execution Mechanism.** Sogesol will be responsible for the execution of the project and the required reporting. MIF will execute the Component III and will hire the main consultancy of Component I and II by request of Sogesol.
- 5.6 **Disbursement by Results.** The MIF resources allocated in Component I and II will be dedicate to hire the Entrepreneurial Financial Global Ltd of Bermuda (EFL) as it is the only provider of a psychometric scoring tool available in the market. The contract and payments to EFL will be done directly from the IDB Country Office in Haiti based on results. The Component III will be executed by MIF/KSC in collaboration with the IDB Country Office in Haiti. No disbursement to the executing agency is required in this project.
- 5.7 **Procurement and Contracting.** For the procurement of goods and contracting of consulting Services, the IDB policies (GN-2349-9 and GN-2350-9 or revised versions) and MIF guidelines that are consistent with IDB policies will be applied.
- 5.8 **Sole Source Selection.** A sole sourcing hiring to the Entrepreneurial Financial Global Ltd of Bermuda (EFL for US\$275,000 is necessary for this project implementation because EFL is the only available provider in the market that offer a psychometric scoring tool. No competition process is possible. As described by the GN-2350-9 Paragraph 3.10 (d) "Single-source selection may be appropriate only if it presents a clear advantage over competition when only one firm is qualified or has experience of exceptional worth for the assignment."
- 5.9 As part of this contract, EFL commits to hiring a full time employee to manage the implementation of the psychometric tool in Haiti. This employee will be available to the project from the beginning of the project to the end.
- 5.10 EFL is a corporation registered under Bermuda's law. The EFL has an affiliate company based in Cambridge, Massachusetts, EFL LLC and other affiliate based on Peru, EFL SAC. EFL was spun out of Harvard University's Enterprise Finance Lab Research Initiative (EFLRI) which is a not-for-profit organization currently housed at Harvard. EFL is the pioneer in applying psychometric tests to evaluate credit risk of business clients of commercial banks. It developed and validated the tool to unlock large-scale bank finance for SMEs in LAC and other developing countries. It was incubated by Harvard University, but the University has no ownership stake in EFL.

¹⁰ Information from MIX Market. <http://www.mixmarket.org>

- 5.11 Based on Annex 10 of OP 619-1, Sogesol requested the Bank at Haiti's Country Office to proceed with a single source selection contract with EFL on their behalf.

VI. MONITORING AND EVALUATION

- 6.1 The IDB Country Office in Haiti in collaboration with the Headquarters in Washington D.C. will be responsible for supervising and monitoring the project. Additionally, the IDB Country Office in Peru in charge of EFL's regional MIF project will be also supporting this project and proper coordination will be assured from MIF Headquarters.
- 6.2 **Project Status Reports.** Sogesol will be responsible for presenting Project Status Reports (PSRs) to the MIF within 30 days after the end of each semester. These reports will follow a format previously agreed upon with MIF and will provide information on project execution, milestones, and project objectives as stated in the logical framework (Annex I) and other planning instruments. The PSR will also describe project issues encountered during execution and outline possible solutions. Within 90 days after the end of the execution term, Sogesol will submit a final Project Status Report (final PSR) to the MIF, which will highlight results achieved, prospects for project sustainability and lessons learned.
- 6.3 **Financial Supervision.** As no MIF resources will be managed by Sogesol, a financial audit will not be required.
- 6.4 **Evaluation.** The evaluation of this project will be carried out as part of the evaluation of the regional MIF project to implement the psychometric tool in Latin America. Extra resources are reserved for that purpose. This evaluation is going to be hired by the IDB Country Office in Peru in collaboration with the IDB Country Office in Haiti and MIF headquarters. The evaluation will assess project outcomes, and use indicators in the logical framework to determine the degree to which these have been achieved, including the expected sustainability of the project. This evaluation will also assess the success of the psychometric tool to increase MSEs' access to finance in Haiti. At least three months prior to project completion, a Closing Workshop will be held with representatives from the Bank, as well as other relevant participants to evaluate results achieved and lessons learned.
- 6.5 As part of the project, Sogesol will monitor the financials of the families of the owners of the micro and small enterprises that request financing. Sogesol will do it by gathering this information at the time of analyzing the client's profile for its first loan and then at the time of each renewal. All the data gathered by the project will be gender desegregated.

VII. BENEFITS AND RISKS

A. Benefits

- 7.1 At the end of the execution of the project, Sogesol will have adjusted a new tool to assess small enterprises creditworthiness in Haiti, and will be incorporated as part of the Sogesol decision process. It is expected that this tool will be also incorporated by other Haitian financial institutions once proven to successfully measure credit risk. It is expected that about 2,000 MSE clients will have been tested by the psychometric tool by the end of the

project, of which at least 1,000 will have been granted access to finance. Sogesol will increase its portfolio in US\$2 million. More importantly, the project will generate hard evidence on the impact as well as sufficiently detailed proposals for how the tool could be implemented on a full scale by the Sogesol for new lending on a continuous basis and how could be replicated in other Haitian financial institutions.

B. Risks

- 7.2 The following risks are involved in the project; (i) Loan officer acceptance: Sogesol has recently implemented a scorecard for evaluating risk, giving the institution recent experience, obtaining loan officers' participation and acceptance of the initiative could be challengeable. Mitigation: an incentive will be placed in order to promote adequate loan officer involvement in the pilot project; (ii) Client acceptance: Sogesol recently encouraged all loan clients to open savings accounts, managing client relationships could be a risk. Mitigation: the application of the psychometric tool will be associated to a new loan or renewal, therefore, it will be perceived as necessary step in order to get the financing; (iii) Literacy: while the majority of clients are literate, we do not know what percentage of clients will be able to complete the assessment without assistance, plus the appropriate language to be use. All Sogesol forms are in French, but conversations between officers and clients are in Creole. Mitigation: the test will be offered in Creole and French, and the client will have the opportunity of determining the language at the beginning of the test. Support from the loan officer will be offered if necessary; and (iv) Computer literacy is low, and therefore it is not clear what hardware platform will be most appropriate for the case of Haiti: tablets, touch-screen computers, or traditional computers. Mitigation: To work through all of these issues, an initial study using focus groups with multiple translations and hardware platforms will be performed before rolling out the pilot testing across Sogesol's 17 branches.

VIII. ENVIRONMENTAL AND SOCIAL CONSIDERATIONS

- 8.1 The project's activities are not expected to have a direct negative impact on the environment as they involve technical cooperation for a scoring system, process reengineering and staff training. It was therefore classified as a category "C" operation. The Bank's environmental review process cleared the project on May 14, 2012.