Kosovo 2009

MICROFINANCE ANALYSIS AND BENCHMARKING REPORT

A report from Microfinance Information Exchange (MIX)
and Association of Microfinance Institutions in Kosovo (AMIK)

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OVERVIEW

The microfinance sector in Kosovo has been operating since 1999, and most microfinance institutions (MFIs) there started as economic development programs of international humanitarian organizations. Currently there are 14 MFIs operating mainly in rural areas, representing 18 percent of the financial sector in terms of number of loans and 7 percent in total loan amount. These figures indicate a large number of loans provided in small amounts (**see Table 1**).

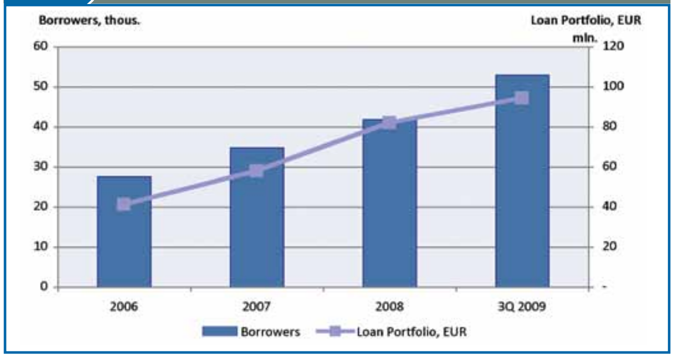
TABLE 1 STATISTICS ON MICROFINANCE PROVIDERS AND COMMERCIAL BANKS AS OF SEPTEMBER 2009

Institution	Founding Organization	Number of Branches	Active Borrowers	Loan Portfolio (euro)	Average Loan balance (euro)	Penetration rate
KEP Trust	Intl.Catholic Migration Committee	33	19,287	43,717,000	2,267	1.9%
FINCA	FINCA	7	12,218	17,694,000	1,448	1.2%
KRK	ADIE International	6	6,823	14,055,307	2,060	0.7%
KGMAMF	Grameen Trust	4	5,980	4,904,000	820	0.6%
AFK	Mercy Corps	6	3,609	6,766,000	1,875	0.4%
KosInvest	World Vision	3	2,271	2,289,000	1,008	0.2%
BZMF	World Relief	6	2,056	4,234,000	2,059	0.2%
START	Islamic Relief	2	1,434	877,000	612	0.1%
MESHTEKNA		2	380	383,000	1,008	0.0%
Qelim Kosovë	CELIM Italy	1	192	293,000	1,526	0.0%
Perspektiva "4"		1	100	94,000	940	0.0%
Atlantic Capital Partners		1	62	402,000	6,484	0.0%
CORDAID	CORDAID	1	15	116,000	7,733	0.0%
Kosova Aid and Development		1	13	18,000	1,385	0.0%
Total		74	54,440	95,842,307	1,761	5.5%
Pro Credit Bank - Kosovo	ProCredit Holding	60	96,172	465,647,490	4,842	9.7%
All other commercial banks in Kosovo (7 total)		*235*	*160,602*	*789,126,915*	*4,914*	*N/A*

Source: AMIK, 2009. AMIK members include: Agency for Finance in Kosovo (AFK), Besëlidhja/Zavet Microfinance (BZMF) , FINCA-Kosovo, Kosovo Enterprise Program (KEP Trust), Kosovo Grameen Missione Arcobaleno Micro Credit Fund (KGMAMF), KosInvest , Kreditimi Rural i Kosovës (KRK), QELIM Kosova, START

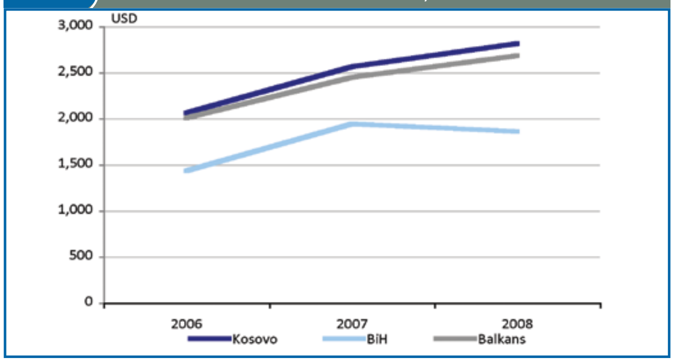
Kosovo Microfinance: Key Indicators 2008

Figure 1 Trends in Outreach and Scale for Kosovo Non Bank MFIs, 2006-2009



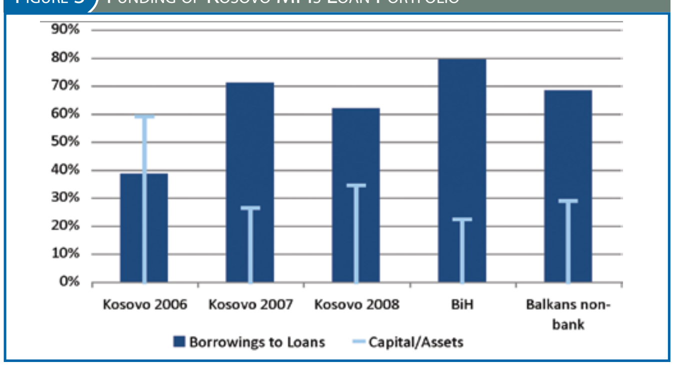
Sources: MIX Market, 2006-2008. AMIK Quarterly Statistics. Results are peer group totals.

Figure 2 Average Loan Balance Per Borrower, 2006-2008



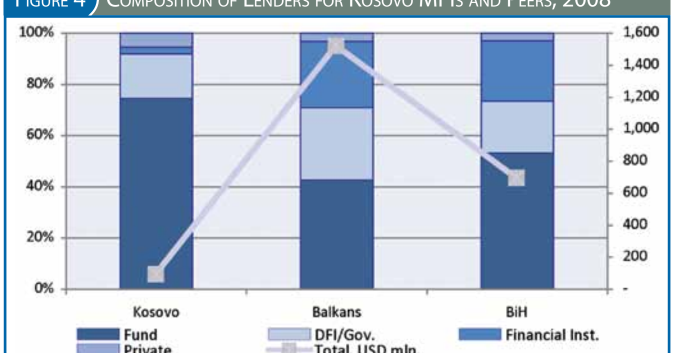
Source: MIX Market, 2006-2008. Results are peer group medians.

Figure 3 Funding of Kosovo MFIs Loan Portfolio



Source: MIX Market, 2006-2008. Results are peer group medians.

Figure 4 Composition of Lenders for Kosovo MFIs and Peers, 2008



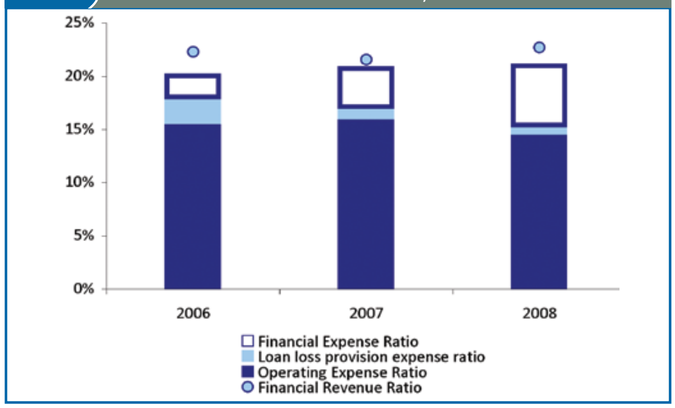
Source: MIX Funding Structure Database, 2008. Results are peer group totals. DFI=development financial institution, Private=NGO/Foundation

Table 2 Cost and Term of Debt in Kosovo, the Balkans, and BiH, 2008

	Kosovo	Balkans	BiH
Weighted Avg. Interest Rate	7.7%	6.8%	6.9%
Weighed Avg. Maturity in Months	58	65	56

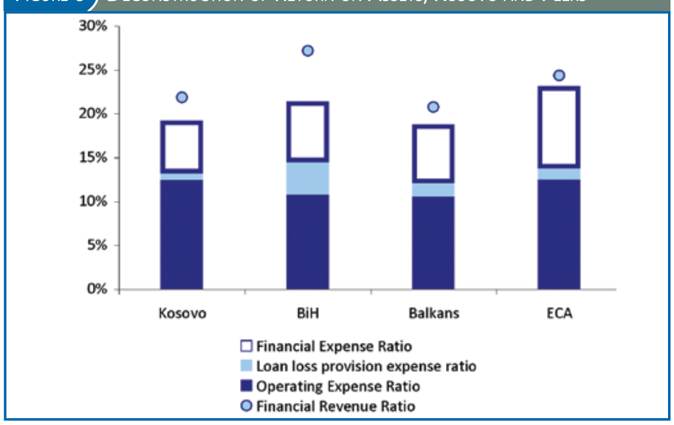
Source: MIX Funding Structure Database, 2008. Results are peer group weighted averages.

Figure 5 Deconstruction of Return on Assets, Kosovo 2006-2008



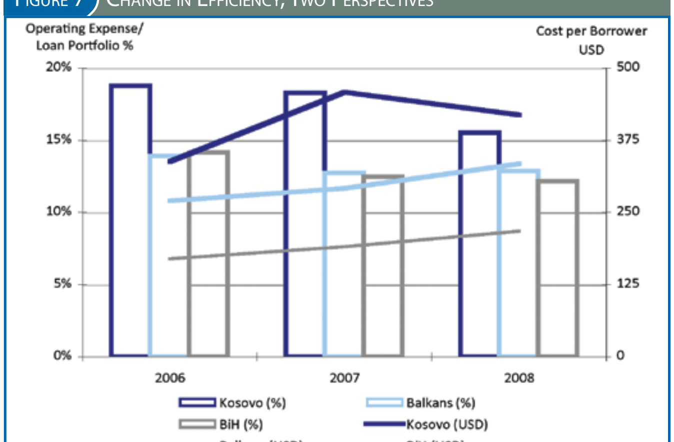
Source: MIX Market, 2006-2008. Results are peer group medians.

Figure 6 Deconstruction of Return on Assets, Kosovo and Peers



Source: MIX Market, 2008. Results are peer group medians.

Figure 7 Change in Efficiency, Two Perspectives



Source: MIX Market, 2006-2008. Results are peer group medians.

Kosovo has the highest number of poor people in the Balkans with a national poverty rate of 45 percent (990,000 people). The non-bank microfinance sector has a penetration rate[1] of 5.5 percent versus 9.7 percent for ProCredit Bank, which is the biggest bank in Kosovo. Thus, the total penetration rate is about 15 percent, signifying that there is room for the sector to grow in the next few years. In comparison, other microfinance sectors in the Balkans have higher penetration rates: 84 percent in Bosnia and Herzegovina (BiH), 35 percent in Serbia and Montenegro, and 23 percent in Albania.

DEVELOPMENTS IN THE LEGAL AND REGULATORY ENVIRONMENT

In the initial phase of their operations, MFIs registered as NGOs and were regulated by the United Nations Mission in Kosovo (UNMIK). MFIs registered at the Ministry of Public Services and their profits were tax exempt. In March 2008, UNMIK approved the Regulation 2008/28 on the Registration, Licensing, Supervision and Regulation of Micro-Finance Institutions, thus enabling MFIs to transform into "licensed" deposit-taking entities. Deposit-taking MFIs would need to be registered at the Ministry of Trade and Industry as a Joint Stock Company (JSC) or Limited Liability Company (LLC). The Regulation also provides a clause for MFIs not capable of meeting the capital requirements for deposit-taking institutions to become "registered" institutions instead. Registered MFIs can continue operating as NGOs providing microfinance loans as the only product, whereas licensed MFIs may operate as commercial entities and are allowed to mobilize deposits from the public.

As most MFIs were established through donations, the issues of asset transfer from the NGO to the new business entity (JSC or LLC) and retroactive taxation of transforming MFIs in relation to their Public Benefit Status are still debated, which is why the transformation process has been blocked for over a year. However, stakeholders recognize that transformation would be beneficial for the microfinance sector, regulatory bodies, and Kosovo's population, as MFIs would have a clearly defined ownership structure, would become tax payers, and would be able to offer deposit products to people with limited access to financial services.[2]

FINANCIAL PERFORMANCE

At the end of 2008 and in 2009, many MFIs in the ECA region experienced decrease in outreach (in some cases because of over-indebtedness in the sector), increase in delinquency and high foreign exchange losses due to the effects of the global financial crisis and economic slowdown. The Kosovo microfinance sector was shielded from many of these risks, as demonstrated by continuous strong growth in outreach, profitability and efficiency gains in 2008. The market in Kosovo is still young and unsaturated, thereby allowing MFIs to grow. Additionally, MFIs are not exposed to foreign exchange risk, as the local currency is the euro and most MFI debt is denominated in euros. However, Kosovo's economy is heavily dependent on remittances, which make up 14 percent of the GDP, and these are expected to decrease as Kosovo workers in Western Europe start feeling the effects of the crisis. As many microfinance clients are not formally employed and rely on funds from relatives working abroad to smooth out their cash flows, credit risk for Kosovo MFIs is expected to increase in 2009.

1 Penetration rate is defined as the number of microfinance borrowers divided by the number of people living below the national poverty line. World Bank statistics on poverty rate levels were used.

2 AMIK organized a workshop in November 2009 on Transformation of MFIs in Kosovo with 84 participants (international investors, regulators and state authorities) to address these issues. A Task Force was established to put forth solutions. The Terms of Reference for the Task Force were signed by three governmental institutions: the Ministry of Economy and Finance, Ministry of Public Administration and the Central Bank of Kosovo and will be composed of representatives of these three institutions including AMIK.

Trends for Kosovo MFIs show that strong growth in outreach continued in 2008 and into 2009 (**see Figure 1**). MFIs increased their borrower base by 20 percent in 2008 and by 27 percent as of 31 October 2009. However, the growth in portfolio was slower, compared to the increase of 41 percent in 2008 versus only 15 percent in the third quarter of 2009. The decrease in remittances in Kosovo reduced the purchasing power of clients, and as a result MFIs became more conservative in their lending by disbursing smaller loans - the median indicator for average loan balance per borrower has decreased from 2,023 euros (USD 2,810) in 2008 to 1,904 euros (USD 2,644) in 2009, while in prior years it had been continuously rising (**see Figure 2**).

Strong growth of Kosovo MFIs was enabled by an influx of foreign debt investments. Total borrowings outstanding increased by 234 percent since 2005, going from 23 to 77 million USD. MFI borrowings funded over 60 percent of loan portfolio in 2008 versus 39 percent in 2006 (**see Figure 3**). As MFIs funded a greater portion of their portfolio through commercial debt, financial expense ratio shot up from 2 percent in 2006 to 5.5 percent in 2008. The composition of active lenders in Kosovo is similar to that of the typical MFI in ECA, but other Balkan peers, especially BiH, receive a quarter of their debt from local banks (**see Figure 4**). MFIs in Kosovo borrow mostly from international investors - 70 percent of all borrowings come from microfinance investment vehicles (a.k.a. funds) - as they offer more favorable conditions than local banks. However, as commercial investors moved in later in this market, interest rates and terms of loans are still higher than for the rest of the sub-region (**see Table 2**).

In terms of profitability, Kosovo MFIs are on par with peers from the Balkans with adjusted ROA at 1.3 percent, which was higher than the median for the ECA region at 0.3 percent. High profitability was driven by decreased expenses while revenues have not fluctuated much - yields were at 24 - 25 percent in the past three years on par with levels in the Balkans and lower than in BiH (**see Figure 5**). Total expense ratio was down from 21 percent in 2006 to 19 percent in 2008, largely driven by decrease in operating and provisioning expenses (**see Figure 6**). Moreover, compared to peers (especially in BiH) the provisioning expenses from Kosovo MFIs are much lower, denoting the lower risk levels they face.

In terms of efficiency as measured by operating expenses to loan portfolio, Kosovo MFIs are still below the norm for the Balkans. However, the indicator has been going down since 2006, demonstrating efficiency improvements (**see Figure 7**). This was due not only to gains from economies of scale as loan portfolio grew while fixed costs remained the same, but also improved staff efficiency as evidenced by the decrease in cost per borrower in 2008 (this indicator increased for peers in 2008). Finally, in 2008 risk levels for Kosovo MFIs were some of the lowest among peers, with portfolio at risk (PAR) over 30 days at 1.2 percent versus 2.2 percent in the Balkans and 2.5 percent in BiH.

2009 will be a more challenging year for Kosovo MFIs as the effects of the economic slowdown reach more microfinance clients. Risk levels have gone up; as of November 2009, PAR over 30 days stood at 4.6 percent but was still lower than for Bosnian peers, where it reached 7 percent. Provisioning expenses are expected to increase as a result. At the same time, efficiency gains may be lower in 2009 due to the slowdown in portfolio growth. However, unlike many peers in the ECA region and the Balkans, Kosovo MFIs have maintained a steady growth in outreach, continue to be profitable, and will soon have the option to attract deposits, which should ease some of their funding risks.

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Kosovo 2009 Benchmarks

	Benchmarks				Trend Indicators (unadjusted)		
	ECA	Kosovo	Balkans	BiH	Kosovo 2008	Kosovo 2007	Kosovo 2006
INSTITUTIONAL CHARACTERISTICS							
Number of MFIs	218	7	35	12	6	6	6
Age	9	8	9	11	8	7	6
Total Assets	4,766,477	9,368,387	50,434,230	56,655,094	13,348,744	10,977,744	8,063,569
Offices	6	8	18	34	9	7	8
Personnel	34	36	148	165	39	43	30
FINANCING STRUCTURE							
Capital/ Asset Ratio	22.8%	36.1%	24.9%	22.2%	34.4%	26.2%	58.9%
Debt to Equity	2.9	1.8	3.0	3.5	1.9	3.4	0.7
Deposits to Loans	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Deposits to Total Assets	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Portfolio to Assets	88.0%	94.3%	91.7%	92.3%	94.9%	84.8%	89.8%
OUTREACH INDICATORS							
Number of Active Borrowers	2,163	5,704	12,863	29,786	4,484	3,752	3,809
Percent of Women Borrowers	43.0%	34.3%	41.6%	42.1%	29.3%	23.3%	22.2%
Number of Loans Outstanding	2,266	5,704	13,320	33,475	4,484	3,752	3,809
Gross Loan Portfolio	3,951,943	8,830,199	41,314,440	52,126,390	12,682,392	9,378,592	7,079,227
Average Loan Balance per Borrower	2,177	2,747	2,679	1,858	2,811	2,559	2,059
Average Loan Balance per Borrower/ GNI per Capita	68%	186%	77%	49%	191%	174%	140%
Average Outstanding Balance	2,120	2,747	2,521	1,800	2,811	2,559	2,059
Average Outstanding Balance / GNI per Capita	66%	186%	76%	48%	191%	174%	140%
Number of Voluntary Depositors	0	0	0	0	0	0	0
Number of Voluntary Deposit Accounts	0	0	0	0	0	0	0
Voluntary Deposits	0	0	0	0	0	0	0
Average Deposit Balance per Depositor	0	0	0	0	0	0	0
Average Deposit Balance per Depositor/ GNI per Capita	0%	0%	0%	0%	0%	0%	0%
Average Deposit Account Balance	0	0	0	0	0	0	0
Average Deposit Account Balance/ GNI per Capita	0%	0%	0%	0%	0%	0%	0%
MACROECONOMIC INDICATORS							
GNI per Capita	3,780	1,474	3,595	3,780	1,474	1,474	1,474
GDP Growth Rate	8%	11%	7%	7%	11%	11%	11%
Deposit Rate	5.4%	4.0%	4.0%	3.6%	4.0%	4.0%	3.1%
Inflation Rate	9.0%	4.4%	3.2%	1.3%	4.4%	4.4%	0.6%
Financial Depth	42.9%	0.0%	64.6%	65.9%	0.0%	0.0%	0.0%
OVERALL FINANCIAL PERFORMANCE							
Return on Assets	0.3%	1.3%	1.6%	4.2%	2.6%	2.0%	3.5%
Return on Equity	2.9%	3.9%	8.0%	15.5%	5.9%	4.2%	6.7%
Operational Self-Sufficiency	117.1%	113.3%	113.3%	121.5%	113.3%	111.0%	129.1%
Financial Self-Sufficiency	104.3%	106.5%	110.1%	123.2%	N/A	N/A	N/A
REVENUES							
Financial Revenue/ Assets	24.4%	21.9%	20.8%	27.2%	22.7%	21.6%	22.3%
Profit Margin	4.0%	6.1%	9.1%	18.8%	11.7%	9.9%	19.1%
Yield on Gross Portfolio (nominal)	29.4%	23.2%	23.0%	26.4%	24.8%	23.3%	24.9%
Yield on Gross Portfolio (real)	19.3%	18.0%	18.3%	24.6%	19.5%	18.1%	24.2%
EXPENSES							
Total Expense/ Assets	24.2%	20.5%	18.4%	20.5%	19.3%	19.4%	20.9%
Financial Expense/ Assets	8.9%	5.5%	6.2%	6.5%	5.5%	3.6%	2.0%
Provision for Loan Impairment/ Assets	1.3%	0.7%	1.5%	3.7%	0.7%	1.0%	2.3%
Operating Expense/ Assets	12.8%	12.7%	10.8%	11.0%	14.7%	16.2%	15.7%
Personnel Expense/ Assets	7.2%	7.2%	5.8%	6.5%	7.8%	7.7%	7.7%
Administrative Expense/ Assets	5.1%	5.6%	4.6%	4.0%	6.0%	7.5%	8.0%
Adjustment Expense/ Assets	2.0%	0.7%	0.5%	0.3%	N/A	N/A	N/A
EFFICIENCY							
Operating Expense/ Loan Portfolio	15.0%	13.7%	12.6%	12.1%	15.5%	18.3%	18.8%
Personnel Expense/ Loan Portfolio	8.2%	8.2%	7.2%	7.2%	8.9%	9.0%	9.2%
Average Salary/ GNI per Capita	3.9	10.1	5.5	5.5	10.8	11.6	8.7
Cost per Borrower	309	398	313	217	419	458	338
Cost per Loan	289	398	313	213	419	458	324
PRODUCTIVITY							
Borrowers per Staff Member	58	70	104	145	68	69	82
Loans per Staff Member	59	70	104	146	68	69	82
Borrowers per Loan Officer	167	189	209	228	161	143	176
Loans per Loan Officer	169	189	211	231	161	143	176
Voluntary Depositors per Staff Member	0	0	0	0	0	0	0
Deposit Accounts per Staff Member	0	0	0	0	0	0	0
Personnel Allocation Ratio	37.0%	42.4%	52.5%	64.8%	40.2%	48.0%	58.4%
RISK AND LIQUIDITY							
Portfolio at Risk> 30 Days	2.0%	1.2%	2.2%	2.5%	1.5%	1.5%	2.0%
Portfolio at Risk> 90 Days	1.0%	0.6%	1.2%	1.0%	0.6%	0.8%	1.0%
Write-off Ratio	0.4%	0.7%	1.2%	1.5%	0.7%	1.3%	1.9%
Loan Loss Rate	0.3%	0.6%	0.9%	1.2%	0.3%	1.1%	1.7%
Risk Coverage Ratio	78.0%	92.9%	89.0%	88.7%	92.9%	118.1%	99.9%
Non-earning Liquid Assets as a % of Total Assets	5.5%	3.4%	6.0%	4.5%	3.2%	11.9%	9.2%