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AFRICAP GOVERNANCE

REPORT AUTHORS
PAUL DI LEO AND AMIT BRAR

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This report was prepared by Paul Di Leo and Amit Brar of Grassroots Capital Management.

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Acronyms

AI: AfriCap Investment
AIM: ACCION Investments in Microfinance
AMIC: AfriCap Microfinance Investment Company
AMV: AfriCap MicroVentures
CMEF: Council of Microfinance Equity Funds
EBL/EBS: Equity Bank Limited/ Equity Building Society
FASL: First Allied Savings and Loans
FIEC: Financial Inclusion Equity Council
FTE: Full-Time Equivalent
FMV: Fair Market Value
GAC: Governance and Audit Committee
GCM: Grassroots Capital Management
ICOM: Investment Committee
LAC: Latin America and Caribbean
LP: Limited Partner
MFI: Microfinance Institution
MIV: Microfinance Investment Vehicle
OC: Operations Committee
PE: Private Equity
SSA: Sub-Saharan Africa
TA: Technical Assistance
TSF: Technical Services Facility

ASSESSMENT OF AFRICAP GOVERNANCE

"Those who are bold enough to go into uncharted waters are the ones that allow humanity to progress."[1]

There are two AfriCap narratives. One is of a pathbreaking fund that set out to demonstrate the relevance of the commercial microfinance model to Africa. It registered some early successes in its portfolio, attracted additional capital to more than triple in size, and nurtured African leadership at both the investment management and Board levels. As the African environments rapidly developed, the manager and the investors struggled to coalesce around a strategy for the Fund and diverged in their views of which, and how many, of the emerging opportunities to pursue. As the Board carefully considered the options, value was lost as the portfolio languished.

Nevertheless, we believe that AfriCap's contribution to the microfinance sector in Africa is unquestionable. In 13 years the Fund invested both equity and debt in 21 microfinance institutions (MFIs), more than any other equity fund investing in microfinance during that era, and managed $11 million in technical assistance (TA) support to its investee companies and the regional industry. With the benefit of this AfriCap capital and technical assistance, the African microfinance sector generated solid examples of investable MFIs that laid the basis for the subsequent growing interest in investment in African microfinance investment vehicles (MIVs) evidenced in recent years by a spate of Africa-focused funds.

From 2001, when AfriCap started, to 2013, the African microfinance portfolio grew more than 10 times to more than $6 billion. Prominent MFIs like Equity Bank (EBS) in Kenya and Socremo in Mozambique challenged early skepticism over the prospects for African microfinance. A few of AfriCap's key features and accomplishments were critical in its ability to realize these positive influences and results.

1 This and all subsequent italicized quotes are from interviews and comments by investors, board members, staff and observers of AfriCap. In keeping with the terms under which interviews were conducted, none of the quotes are for attribution. All those interviewed spoke in their personal capacities and not on behalf of AfriCap or any other entity.

01

Africa-based team

The Fund maintained an on-the-ground presence from the day it opened its doors for business. The fund manager started operations with an office in Dakar, Senegal, and later moved to Johannesburg, South Africa. **This strong local presence gave the Fund an edge in market knowledge over other investors –** seen in the high number of investments AfriCap closed as compared to its contemporaneous peers who did not have on-the-ground presence.

02

African management

In equity investing, it is crucial to know the company and establish a strong rapport with management. AfriCap started with a Canadian fund manager who handed over management, as planned, to an African manager within a few years. Having an African management team enabled AfriCap to develop better market intelligence and more rapidly gain the confidence and trust of the local MFIs. This was important, since many such institutions had little experience of sharing in ownership and governance. This approach bore fruit in the number and variety of deals. **Where contemporaneous funds invested in four to five African companies, AfriCap was able to make 21 investments in an eighyear span, encompassing NGO transformations, bank downscaling, mobile payments, and greenfields.**

03

Investment process

The Board members, representing investors, were highly engaged in the investment and TA processes, with high participation in committee meetings to support the investment team. In addition to the voting members attending AfriCap's investment committee (ICOM), other observers were also allowed to sit in during discussions. Investment decisions were made after due diligence and analysis that progressively improved as the investment team gained experience and benefited from the deeper experience of ICOM participants. The fund managers demonstrated the discipline to walk away from some promising investments when the terms were not right, and were successful in achieving exits in very difficult markets. **Through its investment process, the Fund set a standard for investing in African MFIs without making compromises or sacrificing ethics and transparency.**

04

Demonstration effects

The Fund's mandate was to seek out investable MFIs and to turn NGOs into promising shareholder-based companies. The Fund fulfilled this mandate by making most of its investments in startups and NGOs and by not restricting itself to the "low-hanging fruit" – like South Africa, Kenya, and Nigeria – but making investments all across the continent, from Burkina Faso in the west to Egypt in the north and Mozambique in the south.

AfriCap went on to make million-dollar-plus private equity deals in countries like Sierra Leone, Malawi, and Cameroon, where few had done so previously. Today, many of AfriCap's investees are well-recognized MFIs in their respective countries, including Equity Bank, Socremo, and Asusu.

By investing throughout the continent, AfriCap maximized its demonstration and development impact, a major accomplishment that continues to bear fruit today.

Furthermore, early investments like Equity Bank (Kenya) and First Allied (Ghana) generated strong positive returns comparable to the best performers in other parts of the world. **This validated the belief that Africa is investable and drew many "fence-sitters" to invest in the continent.**

05

Board and ICOM

AfriCap's ICOM and professional Board grappled with the difficulty of preserving focus even as they attempted to adapt and adjust strategies and structures to reflect new information and a deepening sense of how challenges and opportunities in Africa differed from those facing funds in other regions. **The Board worked hard to incorporate new views and insights and managed multiple transitions in key personnel while striving to preserve focus and discipline.**

06

Technical assistance

AfriCap's founders correctly diagnosed the generally less mature state of the African industry and institutions and implemented a companion TA component designed to support both portfolio companies and the industry overall. The technical services (TSF) and FinTech facilities funded the installation of technically sound managementinformationsystem (MIS) in five MFIs and placed professional managers in another nine. The annual CEO conferences originated by TSF and continued by FinTech were widely cited as unique and valuable occasions for MFI CEOs to exchange ideas. **Overall, the TSF and FinTech interventions identified and took steps to address key gaps in expertise and capacity.**

07

Investors/stakeholders

AfriCap strove to balance the interests of diverse stakeholders, which came to include development finance institution (DFIs) and foundations alongside investors with more traditional private equity intentions. **Companies in which AfriCap invested also attracted direct investment from some AfriCap shareholders and new entrants into the sector, confirming that AfriCap could play the leading role the fund's stakeholders had envisioned.**

This is AfriCap's success story. But there is an alternative narrative, one of a Fund that was star-crossed from the start: it had insufficient assets under management to field resources adequate to fully achieve its core objective, but was overloaded with additional objectives and challenges by a group of investors who, with the best of intentions, could not say no. Those objectives included developing local talent, nurturing immature institutions, and promoting innovation, all on top of managing a profitable portfolio of investments to be placed and liquidated within ten years.

From this perspective, after a five-year effort to launch the Fund, sponsors' commitment to providing continued focus and direction flagged, overwhelmed by distance and an overambitious agenda. What should have been carefully maintained as the core objectives –managing a successful closed-end private equity fund and generating positive demonstration effects, as Profund was doing – were set aside. Investors' impatience with the pace of investment early on, despite clear indications that Africa was a much more challenging environment than other regions, signaled the incoming management team that the goal was to build the portfolio quickly. But the new team received conflicting signals, investors praised them for growing the portfolio rapidly but chafing at what they saw as overly intrusive oversight and supervision.

The challenges to maintaining investment discipline, interestingly, included the success of exits early on, unstable internal processes, and the premature diversion of the management team's attention and effort to raising more capital. In stark contrast to other equity MIVs of its vintage, at AfriCap a dynamic developed in which constant innovation and growth were encouraged but not consolidated or capitalized on. In the absence of strong leadership from original sponsors and growing influence from new shareholders with different perspectives and agendas, focus and discipline broke down and the governance function collapsed. This resulted in the Board's inability to serve its essential functions of safeguarding a coherent strategy and structure, ensuring adequate capacity, and ensuring that risks were effectively managed.

01

Investment decisions

Impatience with the pace of investment in the early years sent an implicit, if perhaps unintended, message that deal-making should be prioritized over portfolio management and value creation. The two early successes in the portfolio reinforced this bias and **undermined a culture of disciplined and systematic portfolio management.** It was further exacerbated by the large number of investments in a span of seven or eight years, encompassing a wide variety of legal structures, regulatory schemes, levels of maturity, business models, and investment instruments across a vast landscape – geographically and otherwise. Whether more active postinvestment management could have preserved value is difficult to determine from today's vantage point, but whatever the root cause, AfriCap experienced a very high failure rate in its portfolio, with more than half its investments failing in financial terms.

02

Africa-based team

While the advantages of an Africa-based team were clear, there were disadvantages as well. With nearly all Board and committee members based outside the region, **the new and less experienced leaders put in place at the Board and investment management levels received inadequate support and guidance. Investors failed to recruit Africa-based Board members, including independent members, in part due to unrealistic limitations on compensation.**

03

African management

Similarly, while the advantages of building an African management team were clear, **the disruption attendant on nearly simultaneous transitions of Board, investment leaders, and TA leaders was underestimated by the Board, and the level of support the new leaders needed to function independently was not forthcoming,** again due in part to the lack (with one exception) of Africa-based and African Board members. The challenge was exacerbated by the small size of the team and turnover among its members.

04

Technical assistance

Although it clearly responded to capacity-building needs in the portfolio companies and the industry, **the technical-services function also served to dilute the focus and accountability of the investment management team.** Investments that required well-designed TA support foundered due to lack of follow-through and coordination between TA and investment management as well as diffuse and insufficient capacity and focus on the part of management.

05

Board and ICOM

The Board failed to address a difficult working relationship between the chair and the manager during the crucial period between 2005 and 2008. Given the difficulty in this important relationship, the Board and shareholders counterintuitively raised the stakes by proceeding with a recapitalization and restructuring of the Fund. The ICOM, which could have served as another tool of governance to cultivate and maintain a clear focus, suffered from an excessively open process and inconsistent follow-up. Thus, the two key governance **relationships intended to support, guide, and evaluate the fund manager were not fully functional.** This dysfunction was both a cause and an effect of the instability that characterized the Fund. Other equity MIVs have recapitalized and/or changed management, but none faced multiple changes in management and strategy and structure, coupled with four changes in the chair of the Board and churn at the ICOM.

06

Investors/stakeholders

AfriCap struggled and ultimately failed to reconcile the expectations and ambitions of the shareholder group even prior to the recapitalization, with some investors pushing for more rapid deployment while others struggled to enhance investment discipline. With the recap, significant new shareholders with their own views and expectations joined the Board. The tripling of capital encouraged consideration of new initiatives and strategies; coherence was further eroded. As multiple strategies jostled for preeminence – the original demonstration portfolio concept, a holding company, a multi-fund African manager – no clear focus or direction was endorsed by the Board.

Although these two narratives could not be more different, in both cases AfriCap's legacy is largely the same:

07

Creating a legacy

Overall, AfriCap succeeded in helping to demonstrate that microfinance in Africa is a dynamic and investable business and that investors can expect a return on their investment. Unfortunately for AfriCap's own investors, it showed both how this could be done and how it could fail. But future investors and managers can take confidence from AfriCap's investment and exit track record of and build on the lessons learned, both good and bad.

This assessment has focused on the role governance played in AfriCap's successes and failures; indeed, while we see validity in both narratives, overall we have found that governance left its fingerprints everywhere on AfriCap's successes and failures.

In 2005, the Council of Microfinance Equity Funds (CMEF), now the Financial Inclusion Equity Council (FIEC), issued "The Practice of Corporate Governance in Shareholder-Owned Microfinance Institutions," which was updated and reissued in 2012 as "The Practice of Governance in Microfinance Institutions." While written with MFIs in mind, these CMEF "Governance Guidelines" (as it will be referred to hereafter) is for the most part relevant and transferable to the governance of funds as well. As the AfriCap experience demonstrates, key principles, such as the "pivotal" role of the Board in governance and the Board's lead responsibility for such critical matters as strategy, management selection, succession, and risk control are equally relevant to funds themselves and to their investees.

Some of the key areas where the AfriCap Board and its committees featured prominently include:

- **Providing strategic direction:** The Board failed to maintain a clear focus for the Fund and to restrain shareholders' and managers' ambitions as the challenges of investing in Africa became apparent. While other contemporaneous funds proceeded cautiously in building their African portfolios and adjusted their original targets for amounts and timing, AfriCap pushed ahead ever more aggressively and repeatedly shifted strategies and priorities.

- **Fiduciary responsibility:** The ICOM – appropriately – empowered the managers to lead the investment process. Indeed, the character of the Fund very much reflected the different managers' approaches: a tendency toward caution in the early years, giving way to a more exuberant temperament, which in turn was succeeded by a careful, deliberate windup.

But while some degree of deference to the manager was appropriate, an extraordinarily open ICOM process undermined the ability of a very experienced core ICOM group to provide clear guidance and effective oversight and to nurture investment discipline in an inexperienced team. Following the recapitalization, when a relatively large pool of capital became available, the Board found it particularly difficult to maintain a focus on financial performance. A lack of investment discipline emerged even prior to the recap, however, with a very rapid pace of investments in 2006 – most of which did not go on to perform well. While the early divestment from Equity Bank was stunningly successful in several respects, motivating high interest in AfriCap's own recap and in African microfinance in general, the Board allowed this to cloud its vision of the challenges that still lay ahead.

- **Management performance:** The Board was inconsistent in monitoring and guiding management, chastising the first manager for an excess of caution while at times applauding the second manager for the rapid pace of investment even as it sought to nurture the team's capabilities to the necessary level. Furthermore, two generally acknowledged prerequisites for a successful fund were ignored at various times: full alignment between the Board and management and a chair with the full and consistent backing of the Board.

- **Succession planning:** Transitions were premature, not to mention extraordinarily frequent. Furthermore, in several key cases they constituted transitions from more experienced and authoritative incumbents to those less experienced. In light of this, Board support and guidance for the new leaders as they grew into their new roles was insufficient.

- **Conflicts of interest:** While not necessarily more common than in other funds, the lack of clear procedures, consistently understood and applied, led to tensions and delays when the Board was faced with difficult decisions and could least afford distractions and disputes.

Overall, it is the conclusion of this assessment that the Fund took a very challenging and ambitious path, in part deliberately and in part out of an understandable ignorance of the African environment. Once on this path, the Board repeatedly failed to maintain focus and implement an adequate approach to mitigating and managing the attendant risks.

The challenges AfriCap faced were undoubtedly greater than those facing its contemporaries or most of the funds that have followed, and the extraordinary efforts many Board members made to support the Fund's success and address its challenges must be acknowledged. AfriCap's experience does suggest several areas in which the CMEF's Guidelines might be sharpened so as to supplement these individual efforts with structural support:

- **The Guidelines highlight** the contribution that independent directors can make in bringing a fresh and disinterested perspective to issues to which shareholder nominees may bring multiple agendas. Particularly in cases where Board members find themselves at odds with respect to strategy, management performance, or other critical issues, independents can take on a lead role in devising solutions.

- **More generally,** the Board's responsibility to evaluate its own capabilities and performance periodically warrants stronger emphasis. While AfriCap's original Board was a solid one, it arguably failed to supplement its deep expertise in international microfinance and private equity with the Africa-specific experience and networks it needed, particularly as the particular risks and challenges of the African environment became more obvious.

- **ICOM discipline** is paramount in setting the tone and maintaining the focus of a Fund. Policies with respect to membership, attendance, and reporting and follow-up procedures should be clearly specified, understood, and rigorously applied.

- **While the role of a fund's "sponsors" or "lead investors"** is not a formal or clearly defined one, at times of stress or challenge, some such entity has a critical and even indispensable role to play in supporting the chair and crafting and implementing responses.

Refinements such as these might help prevent some problems from worsening, or at least might help to sketch out a generally agreed-upon path to dealing with problems once they arise. As noted, however, the combination of solid structures and practices with engaged, dedicated individuals and solid working relationships is essential.

1. Introduction and Scope of the Assessment

The AfriCap story is an important one: as one of the first microfinance equity funds, tasked with concurrently developing the industry in an entire continent and developing local capacity at the investment management level, the Fund inevitably faced difficult challenges. But the progress of the African microfinance industry over the past 12 years is likewise indisputable, marked most graphically by the fact that Africa is now a leading target for microfinance investment and innovation[2]; AfriCap has participated in that process from the start.

▪ How exactly did AfriCap participate in this transformation of the African microfinance sector?

▪ Was it a bystander, a central protagonist, or a hindrance?

▪ What aspects of its structure, strategy, management, and governance were most influential?

The role of AfriCap's governance in the story is particularly salient and requires special attention because of the particular set of challenges and objectives the Fund's creators set for it. AfriCap's original core goal was to manage a successful private equity portfolio of investments in African MFIs that would demonstrate the "investability" of African commercial microfinance, similar to what ProFund was on its way to accomplishing in Latin America. At the same time AfriCap faced, or set for itself, two other challenges:

▪ First, while all funds of this vintage were breaking new ground, AfriCap faced perhaps the greatest challenges in designing and implementing an effective strategy: it was limited to one region where few other investors were active, experienced human resources were scarce, institutional development was less advanced, and microfinance industry regulation was generally not well defined.

▪ Second, it was planned from the outset that the initial Board chair[3], investment manager, and TA manager drawn from the Fund's sponsors would recruit and develop their own replacements and then step aside within a few years. No other such fund underwent this scale of senior-level transition so rapidly.

These two extraordinary features necessarily placed a premium on an effective and engaged Board and shareholder group to guide and oversee the evolving strategy and transitions.

As the AfriCap Fund winds down, there exists a unique opportunity to document and evaluate different views on the central performance issues through direct dialogue with the key participants while memories are somewhat fresh. Recognizing this ephemeral opportunity, in mid-2014 a number of AfriCap's shareholders engaged Grassroots Capital Management ("Grassroots") to undertake an evaluation of the Fund's governance[4], specifically assessing:

i) whether AfriCap and the TSF contributed to the overall strengthening of the MFIs in which the Fund invested;

ii) whether governance was conducted appropriately and whether the Board and its committees, as well as the investors/shareholders, conducted themselves according to AfriCap's mandate; and

iii) the major factors influencing the achievement or nonachievement of AfriCap's objectives.

This is an assessment of how well the governance of the Fund evaluated and supervised these critical dimensions of performance, rather than, in the first instance, trying to develop a judgment of the quality of AfriCap's portfolio companies or the value creation of specific TA initiatives.

2 Per the May 2014 "Spotlight on the Market" report, the region to which the highest number of investors plan to increase their allocations is sub-Saharan Africa (SSA).
3 In the case of the Board chair position, there were actually two chairs drawn from the sponsors before an independent African chair was elected.
4 Grassroots Capital Management, founded in 2007, is a U.S.-based impact investment manager and advisor. For more background in the firm, please consult www.grassrootscap.com.

For example, how did the governance of the Fund monitor and assess the Fund's performance with respect to "overall strengthening of MFIs in which the Fund invested" or ensure the "expertise of the investment officers employed"? In forming a view of the efficacy of governance in these regard, Grassroots necessarily needed to form a view of whether performance was successful or fell short, but the vantage point for this assessment was the Fund's own governance functions.

After this introduction, this report begins with a review of AfriCap's inspiration, concept, and strategy at the outset and a timeline summarizing key events. A third section examines the major areas where AfriCap's governance would be expected to exercise particular responsibility. A fourth and final section then provides a review of AfriCap's governance in the context of guidelines developed by the Council of Microfinance Equity Funds, to shed light both on where AfriCap governance did and did not reflect best practice and where the recommended best practice itself might warrant revisiting or strengthening.

The evaluation team undertook the following methods to collect information and perspectives: (1) interviews with AfriCap managers, staff, Board members, and shareholder representatives (a list of interviews can be found in Appendix A); (2) interviews with institutions in which AfriCap and FinTech invested and/or to which they provided technical assistance; (3) interviews with observers and participants in the microfinance industry in the region and globally; and (4) a review of publically available reports and assessments (see Appendix E for a selected bibliography). In addition, a number of shareholders have shared their own contemporaneous analyses of AfriCap at various points in its history.

Readers should bear in mind that this evaluation was primarily conducted via interviews. As interlocutors were assured that their comments would be treated as anonymous, ideas and observations are not attributed. While Grassroots has made efforts to resolve discrepancies and provide a balanced view where information is inconsistent, it is inevitable that in reconstructing decisions and contexts stretching back over 15 years, drawing on a fragmentary record and individual recollections, errors of fact and interpretation will be made. Grassroots regrets and apologizes in advance for these errors, but believes that the main lessons and conclusions of the assessment are nevertheless robust.

Finally, for purposes of disclosure, Grassroots wishes to note that it was engaged with AfriCap for several years.

The Gray Ghost Microfinance Fund, managed by Grassroots, warehoused an investment of $2 million as part of the 2007 AfriCap recap on behalf of the Global Microfinance Equity Fund, initially managed by Grassroots, which held an initial closing in 2008. Various investment officers and a Grassroots partner led the Gray Ghost commitment and sat at various times on the AfriCap Board and Board committees. None of these individuals have been involved in any Grassroots activities since 2010 and none had any involvement in this assessment. Grassroots' management of GMEF ended in early 2011. Grassroots continues to hold a de minimis (0.31 percent) Limited Partner (LP) interest in GMEF, which remains an investor in AfriCap.

2. AfriCap Ambition and Reality

a. A "ProFund for Africa"

The origins of AfriCap lie in the experience of ProFund in what was then the initial phase of efforts by the microfinance industry to "crack the capital markets" and broaden its investor base by institutionalizing NGO MFIs and demonstrating a track record of investment performance and liquidity for commercially oriented shareholder MFIs.

ProFund's objective had been to invest in financial institutions "so that they profitably and effectively can serve the microenterprise and small business markets [in Latin America and the Caribbean], and provide a reasonable return to investors" [5] or, alternatively, "to achieve superior financial returns for its investors by supporting the growth of regulated, efficient financial intermediaries that serve primarily microenterprises (MFIs) in Latin America and the Caribbean." [6] ProFund was itself inspired by the successful creation of BancoSol from a founding NGO.

When AfriCap was first conceptualized, ProFund, which had launched in 1995, was at its halfway mark. It had made nine investments in MFIs in eight countries (out of an eventual total of eleven investments in ten countries) and had a Latin American management team based in Costa Rica.

The 1999 feasibility study for AfriCap explicitly cited ProFund's approach and achievements and highlighted ProFund's role in addressing the lack of "patient risk capital . . . to support the expansion of commercial microfinance." The study identified a number of key elements of ProFund that it believed should be adapted and incorporated into the structure of AfriCap.

5 Report to the MIF Donor Committee, 1995.
6 Silva, Small Enterprise Development, March 2005.

In addition to drawing on the experience of ProFund, AfriCap also directly engaged many of the institutions and, indeed, individuals who had been directly involved in ProFund as its creators, managers, and advocates: Accion, Calmeadow, and IFC most prominent among them. The stage was set for microfinance to replicate a successful model that was critical to expanding its scale, scope, and impact to a critical region. AfriCap seemed designed and supported well enough to achieve in Africa the key goals set for ProFund in Latin America: institutionalizing MFIs, building a track record of successful investment, and nurturing indigenous management capacity. It was conceived with a similar objective: to support the commercialization of the microfinance industry by bridging the transition from a sector traditionally funded by donors to a scenario where the leading MFIs were raising most of their funds from commercial sources.

Table 1: ProFund and Africap Overlap

Investors	ProFund	AfriCap
Calmeadow (USAIS/DFID)	$499,829	$3,203,000
Omtrix	$250,000	
Accion International	$280,500	$200,000
Argidius Foundation	$500,000	$200,000
IFC	$3,000,000	$2,000,000
Calvert Foundation	$1,000,000	$100,000
Subtotal	$5,530,329	$5,703,000
Total	$22,326,803	$13,303,000
Percent of total	25%	43%
Institutional Leadership		
Calmeadow	Sponsor	Sponsor
Accion International	Sponsor	Sponsor
Omtrix	Manager	Back Office
Individual Engagement		
Alex Silva	Manager	Chair ICOM / OC
Martin Connel	Chair Project Assessment (MIF)	Chair Board (Accion), ICOM,
Lauren Burnhill	Board(MIF)	GAC
Maria Otero	Board (Accion)	Chair
Hany Assaad	Board (IFC)	Board (IFC)
Stefan Harpe	ICOM Member	Manager

From this initial inspiration, the process of conceptualizing and designing AfriCap was extended and careful. The founding phase took three years, beginning in earnest in early 1999 with a formal feasibility study. It was marked by the engagement of a wide range of stakeholders and a consultation process designed to devise a strategy and approach appropriate to the African environment. A steering committee was formed to systematically develop the concept; meetings of founding investors served to nurture and preserve consensus on key elements. Accion International, which was in the process of building its African engagement, joined Calmeadow as a sponsor. As the group of anchor investors coalesced, discussions of strategy and structure generated consensus and growing momentum around key features such as domicile, management, and budgets.

While the shared ProFund experience of many of the key participants informed these deliberations, the promoters of AfriCap ultimately set aside or overlooked some of the key lessons emerging from ProFund even at that relatively early date. An outside assessment of ProFund completed in early 2002[7] articulated some of these initial "learnings." In many cases, like the importance of the long-term commitment of a competent investment manager backed up by a high-quality Board, these conclusions echo those drawn in the AfriCap feasibility study.[8]

While some of the divergences only emerged over time, several were baked into AfriCap's structure from the start. Most noteworthy among these were the critical role of the manager and the importance of sharp focus. It is not necessary to assess the specific qualities and capabilities of AfriCap's mangers relative to ProFund's to recognize that the plan to switch managers after three years was a very high-risk strategy. In setting this as an explicit and significant design element of AfriCap, this was a risk its sponsors deliberately assumed.

A second key departure from the ProFund model and experience was the lack of focus built into AfriCap from the start. In addition to the human-resource development task that AfriCap was assigned, as noted above, the feasibility study noted that "the African microfinance industry overall is less developed than its Latin American counterpart was five years ago"; AfriCap was therefore tasked with "the careful nurturing of the many operators just now starting out or improving their business management capacities," including direct supervision of TA.[9]

While the reasons for this are clear, given the less mature state of the African industry at the time, the lessons of ProFund were also clear: first, in imposing a single-minded focus on building a high-quality portfolio, and second, in divorcing the TA process from the fund manager to enable the fund manager to focus foremost on delivering a successful private equity fund, rather than nurturing the future pipeline or building the industry.

There were also other areas where AfriCap's founders clearly identified the key challenges they faced. The feasibility study echoed ProFund's emphasis on the importance of the manager: "Recruiting the right Fund Manager will be critical. . . . And yet equally important will be the institutional support put in place to back up the chosen individual."[10] Similarly, the issue of cost was recognized early on: "AfriCap will need to manage its costs carefully. Given the geographic distances and need for constant monitoring of investments travel expenses could be significant."[11]

In both cases it is not clear that AfriCap, having identified key issues, was able to follow through consistently and coherently in addressing them. The issues surrounding fund management will be addressed at greater length below. On the budget, AfriCap's designers used ProFund as a benchmark, notwithstanding the fact that ProFund was recognized for running a very lean operation and dispensing with any functions that were not essential to creating value in its own portfolio. It is arguable whether this was ever the appropriate benchmark for AfriCap, which was significantly smaller than ProFund. But in the event, resource pressures were further exacerbated by two factors. First, operating expenses and compensation costs for qualified staff in Africa were simply higher than in Latin America. Second, the initial intention had been to "invest in a relatively small number of institutions. . . AfriCap will make capital commitments to a manageable number of institutions, about five to begin with."[12]

However, this gave way to a more ambitious effort: within its first five years (through 2006), AfriCap invested in eleven institutions.

The point of juxtaposing the ProFund lessons with AfriCap's design is not to suggest that the AfriCap promoters were somehow careless or negligent; on the contrary, the design process was careful and thorough. Rather, it is to highlight the fact that deliberate decisions were taken – calculated risks assumed – in an ambitious effort to try to adapt the ProFund model to a much more challenging environment in nearly every respect: institutional development, human-resource pool, regulatory framework. To some extent those challenges were identified at the outset and motivated the modifications of the ProFund model: for example, with respect to the companion TA facility. In other cases, the nature of the challenges was recognized, if not their severity, but the operational implications were not fully compensated for: for example, with respect to the maturity and capabilities of existing MFIs and asset markets. In still other cases, the investors set themselves an ambitious goal – transferring leadership at both the management and Board levels – which significantly heightened risks to the Fund without crafting a succession process that provided adequate support and guidance as the new leaders grew into their roles.

7 DiLeo and Cuadra, 2002

8 Because the ProFund experience was cited repeatedly as providing the inspiration and model for AfriCap, it is instructive to review in detail some of the findings most relevant to AfriCap; this is included in Appendix D.

9 Feasibility study, pp. 27–28.

10 Ibid., p. 28.

11 Feasibility Study, p 38.

12 Ibid., p. 40.

In all cases, these divergences placed a premium on the capabilities of a cohesive, capable, and engaged Board to provide ongoing oversight and guidance to the Fund to compensate, for example, for the discontinuity inherent in the planned management and governance transitions and to maintain a clear, sharp focus and adequate resources given the project's multifaceted objectives and its geographical and linguistic scope. The fact that the sponsors and investors deliberately embarked on a more challenging, higher-risk strategy in the case of AfriCap was on one level admirable; this is the type of risk and initiative that philanthropic and official capital are designed to take. But the consequent demands and expectations placed upon the Fund and its management team necessitated a very strong, coherent and focused Board with a strong local presence and Africa-specific experience. To deliberately embark on this riskier path was a perfectly reasonable and appropriate course of action under the circumstances, but it is the conclusion of this assessment that once the ambitious path was chosen, the Board subsequently failed to build its own capabilities and expertise to implement an adequate approach to mitigating and managing the risks. It was thus unable to clear the high bar that the shareholders and Board set.

b. Summary of AfriCap History: "A pioneer fund navigating uncharted waters"

The AfriCap Microfinance Fund was launched in October 2001 as a closed-end fund, the first equity investment fund focused on MFIs in Africa. With a target capitalization of US$15 million, it was ultimately capitalized at US$13.3 million. AfriCap was designed to provide patient venture capital and active governance to emerging commercial microfinance institutions (MFIs) in Africa. In addition, the AfriCap Technical Services Facility (TSF), grant-funded with US$3 million over the first five years, was intended to support capacity-building of the MFIs in the portfolio and broader industry development.

AfriCap was supported by institutional investors – mostly international development finance institutions – and invested with a double-bottom-line objective, focusing on social and financial returns. These aims were to be achieved by targeting and investing in institutions committed to serving low-income communities without access to conventional banking services.

The Fund was incorporated in Mauritius and its investment operations were initially based in Dakar, Senegal. Back-office and accounting support were provided first by Calmeadow in Toronto and then by Omtrix in Costa Rica. The Board delegated investment decisions and TSF allocations to an investment committee (ICOM), which worked closely with the fund manager. The initial aim was to invest in about ten MFIs over five years, and divest and liquidate over the following five years, for a total fund life of ten years.

The initial fund manager was AfriCap MicroVentures (AMV), established for this purpose by Calmeadow, the Fund's promoter and one of its sponsors. AMV established a small management team and operating base in Dakar. The initial investment manager was Stefan Harpe, a Canadian out of Calmeadow; Harpe, as planned from the outset, was replaced in 2005 by an African national, Wagane Diouf of Senegal, who took over as manager and moved the base of operations to South Africa.

In 2007, a second round of funding raised AfriCap's capital to US$42 million; AfriCap transformed into a permanent microfinance investment company which it was hoped would be publicly listed within six to seven years. As part of the recapitalization, the TSF was hived off into an independently governed technical support entity called FinTech, with grant funding totaling $8.4 million. The management team subsequently spun off into an independent management company owned by the AfriCap management team and intended to create a family of funds. In 2011 Anne Marie Chidzero became the third fund manager, with a mandate to wind the Fund down.

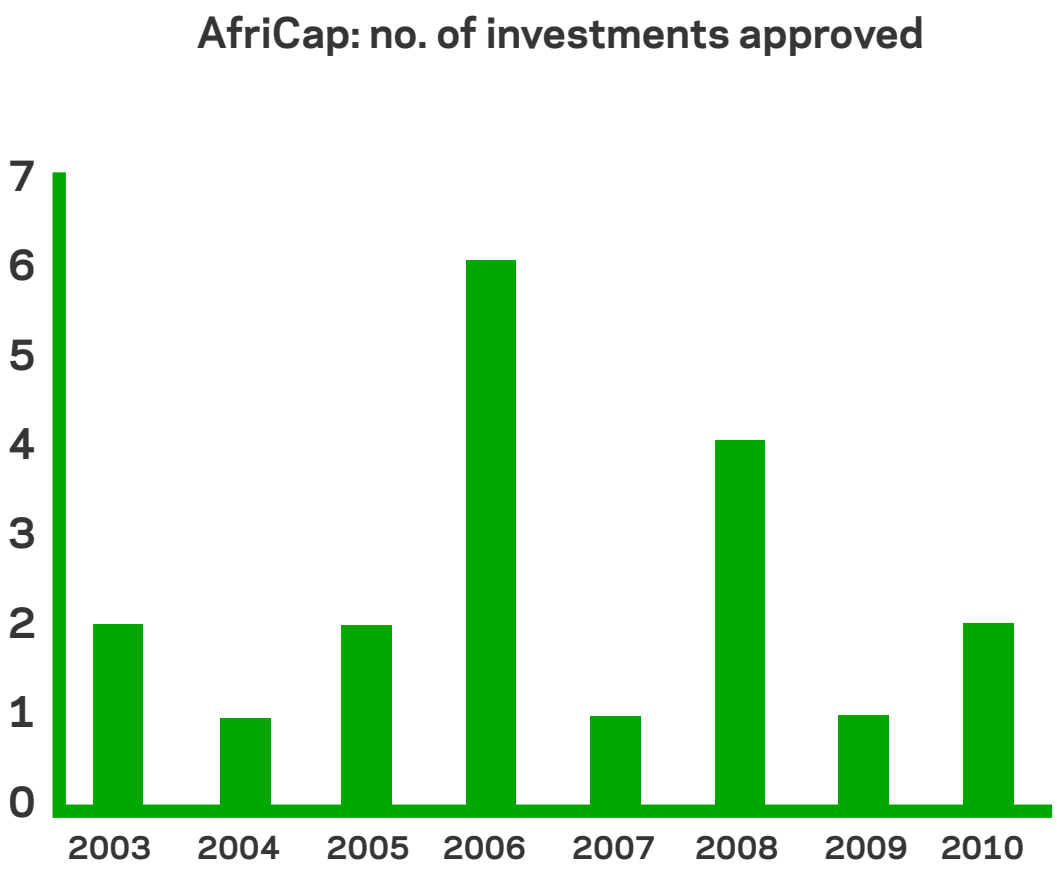
AfriCap made a total of 21 investments through equity, quasi-equity, and debt instruments across 16 countries in sub-Saharan African markets. Most of the investments (12 out of 21) did not, or are not expected to, recover their direct cost, and IRR to investors who entered at inception is estimated at 1 percent per annum. For those who exited at the time of the recap, IRR is estimated at 15 percent per annum. For those who entered at the time of the recap, IRR is estimated as –10 percent per annum.

c. Portfolio Performance

In all, the Fund made 21 investments in 16 countries, totaling $35.5 million, over a 7-year period. In comparison to other microfinance PE funds, AfriCap succeeded in closing a much larger number of investments, an indication of its determination to originate investments and demonstrate the "investability" of commercial microfinance over a broad swath of the continent. By way of comparison, two funds of the same vintage, Accion Investments and ShoreCap, closed four to five African investments each during the same period.

AfriCap's investments were not made consistently year after year. In 2006 and 2008 there were spikes in the number of investments. In 2006 alone the Fund closed six investments, with four more in 2008. Considering that these were mostly equity positions in early-stage companies, the number of deals in these two years is staggering. But the rapid pace was not an accident. In its early years, under the original manager, there had been clear concern over what some Board members took to be the slow pace of investment. So this acceleration under the new manager was welcomed. As one Board member reflected, "pace of investment, rather than quality, seemed more important to the management and the investment committee. The team thought it more important to invest."

Table 2: Investments by Year



While AfriCap clearly diverged from its peers in terms of the number of investments, investing in at least four times as many African companies as any other microfinance equity investor between 2002 and 2010, equally important were the types of companies in which AfriCap invested. While ProFund was judged to have invested mainly in relatively mature MFIs or alongside strong partners in Latin America and the Caribbean[13], AfriCap invested in a large number of startups or early-stage companies, typically held a minority stake, and typically was the only institutional investor.

Despite the signs that AfriCap was building a portfolio with substantial embedded risks and that would require intensive engagement by the investment team, third-party assessments consistently found the Fund to be performing well and building a solid portfolio.

An evaluation of AfriCap in 2007 found that performance assessments clearly show a ***positive association*** between AfriCap investments and enhanced investee performance. Though this observation is based on limited empirical evidence and does not establish attribution, the fact that performance has improved on all measures, both within the portfolio over time and compared to African MFI peer benchmarks, suggests the relationship is not a coincidence. At the very least, AfriCap has chosen its investments well. [14]

A 2007 AfriCap in-house review in anticipation of the conversion and recap reported that, on an fair market value (FMV) basis, the Fund had generated a 13 percent gross IRR as of 2007, with a portfolio of 12 investments: one full exit, one partial exit, two loans repaid, and eight investments held.

These sanguine views appear to have been encouraged by several phenomena. First came the relatively early and successful exits from Equity Bank and First Allied. Second, the resources and responsibilities of the TSF may have obscured accountability for following up post-investment and given a false sense that weaknesses within the portfolio could be addressed by resources drawn from outside the investment team.

Lastly, faced with the challenge of valuing illiquid investments in private companies, the Fund relied on its own valuations, which often turned out to be overly optimistic.

As of today, it is clear that the performance of AfriCap's portfolio was relatively poor. While several investments performed quite well, notably including two of its earlier investments, over half show realized or FMV cash multiples of less than one.

There also appears to be a clear difference in investment portfolio performance after 2005, with the pace of investment increasing markedly and the ultimate performance of the investments deteriorating: of the five investment closed between 2003 and 2005, four – including the outstanding performer Equity Bank – recovered cost and the fifth, with a money multiple of 0.9, nearly did. In 2006 alone six investments were closed, of which two are expected to realize positive cash multiples, three were written off entirely, and one recovered ten cents on the dollar.

13 "While the initial [ProFund] clients (1st to 3rd years) were predominantly NGO conversions (BancoSol, Mibanco, Finamérica, Los Andes), investees incorporated to the portfolio after the 4th year were mostly new commercial MFIs created specifically to serve micro-small entrepreneurs (Solidario, Bangente) and/or downscaling traditional financial intermediaries (Sogesol, Vision). Closing on the NGOs was somewhat easier as they tended to be simpler organizations. However, precisely because of the higher level of sophistication of the parties involved in the latter operations, the transactions with traditional licensed intermediaries were far more complex deals that consumed quite a bit more time, required ingenuity and frequently involved some form of financial engineering. On the other hand, and again because of the higher sophistication and experience of the newly found partners, once closed, those deals required less ongoing involvement than those involving NGOs. In most cases the deals involving NGOs entailed a radical transformation of the original institution from a NGO into a formal financial intermediary." (Silva 2005, p. 4)

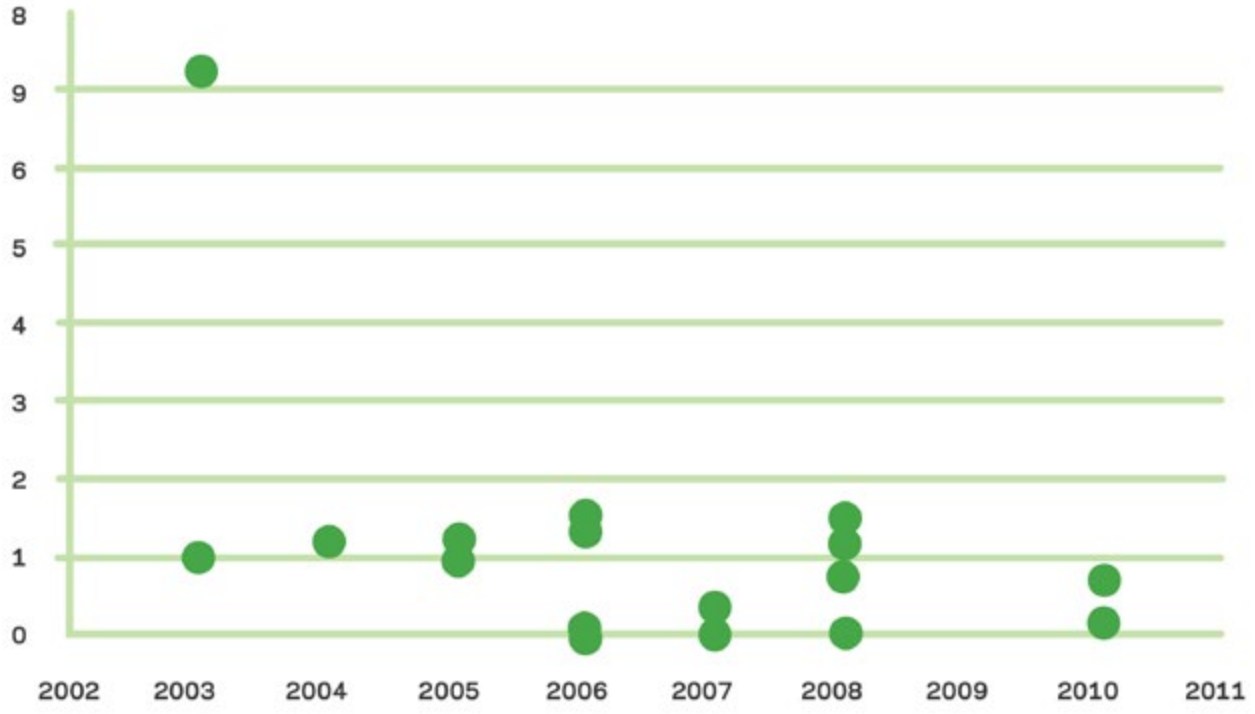
14 USAID, August 2007, p. 11.

Table 3: AfriCap Investments

Name	Country	Date of Investment	Cash In	Realized	Unrealized	Multiple
1 Equity Bank	Kenya	2003	1,600,000	11,600,000	NA	7.3
2 Pride Uganda	Uganda	2003	1,114,000	1,151,423	NA	1
3 First Allied S&L	Ghana	2004	600,000	727,000	NA	1.2
4 Socremo	Mozambique	2005	6,722,792	1,816,379	5,976,278	1.2
5 Pride Tanzania	Tanzania	2005	1,500,000	1,3326,106	NA	0.9
6 UTB	Sierra Leone	2006	1,231,393	72,907	1,552,989	1.3
7 WWB	Ghana	2006	2,7871,109	300,000	NA	0.1
8 ACCESS	Madagascar	2006	657,501	918,960	NA	1.4
9 Opportunity	Malawi	2006	950,697	11,307	NA	0
10 CAP	Senegal	2006	168,816	1	NA	0
11 QFI	Egypt	2006	716,109	1	NA	0
12 Susu	Nigeria	2007	3,807,088	182,991	NA	0
13 Wizzit & Rcubed	South Africa	2007	1,857,284	NA	600,000	0.3
14 Ferlo	Senegal	2008	1,105,284	NA	40,000	0
15 Asusu	Niger	2008	3,464,860	235,151	4,180, 623	1.3
16 La Regionale	Cameroon	2008	2,199,601	2,478,105	76, 203	1.2
17 BACB SOFIPE	Burkina Faso	2008	1,250,318	NA	1,834,634	1.5
18 Tujijenge	Tanzania	2008	863,400	475,599	221, 682	0.8
19 AF&I	Cote d'Ivoire	2008	882, 601	24,500		0
20 Birima	Senegal	2010	1,599,601	148,006	143, 855	0.2
21 Finance Salone	Sierra Leone	2010	449,601	NA	300,675	0.7
Total			35,528,055	21,474,436	14,926,939	1.02

Some data estimated.

Table 4: Money Multiples by Year of Initial Investment



Note: Realized proceeds plus most recent FMV divided by cost of investment. Gross basis; no adjustment for fees and expenses.

Altogether, 12 of AfriCap's 21 investments have failed to recoup their initial cost or are most recently valued below cost, including 11 of the 16 investments closed in 2006 and thereafter.

To be fair, it must be acknowledged that the African operating environment was generally more hostile than in other regions. Contemporaneous microfinance investors that operated in multiple regions confirm that Africa was a more challenging environment than they faced elsewhere, and their African portfolios underperformed compared to other regions. However, in light of this context, the question arises whether AfriCap's decision to undertake a relatively aggressive investment program was ill advised. It is not clear that the Board or ICOM fully and frankly considered the likely ramifications of this approach.

Incorporating the technical assistance efforts into the picture further reinforces the conclusion of underperformance. Particular aspects of the TA efforts, for example the CEO conferences AfriCap organized, are almost universally recognized as having strengthened the coherence and visibility of the African microfinance industry overall. Similarly, some of its secondment and training initiatives are credited with strengthening particular institutions and helping them to overcome challengets.

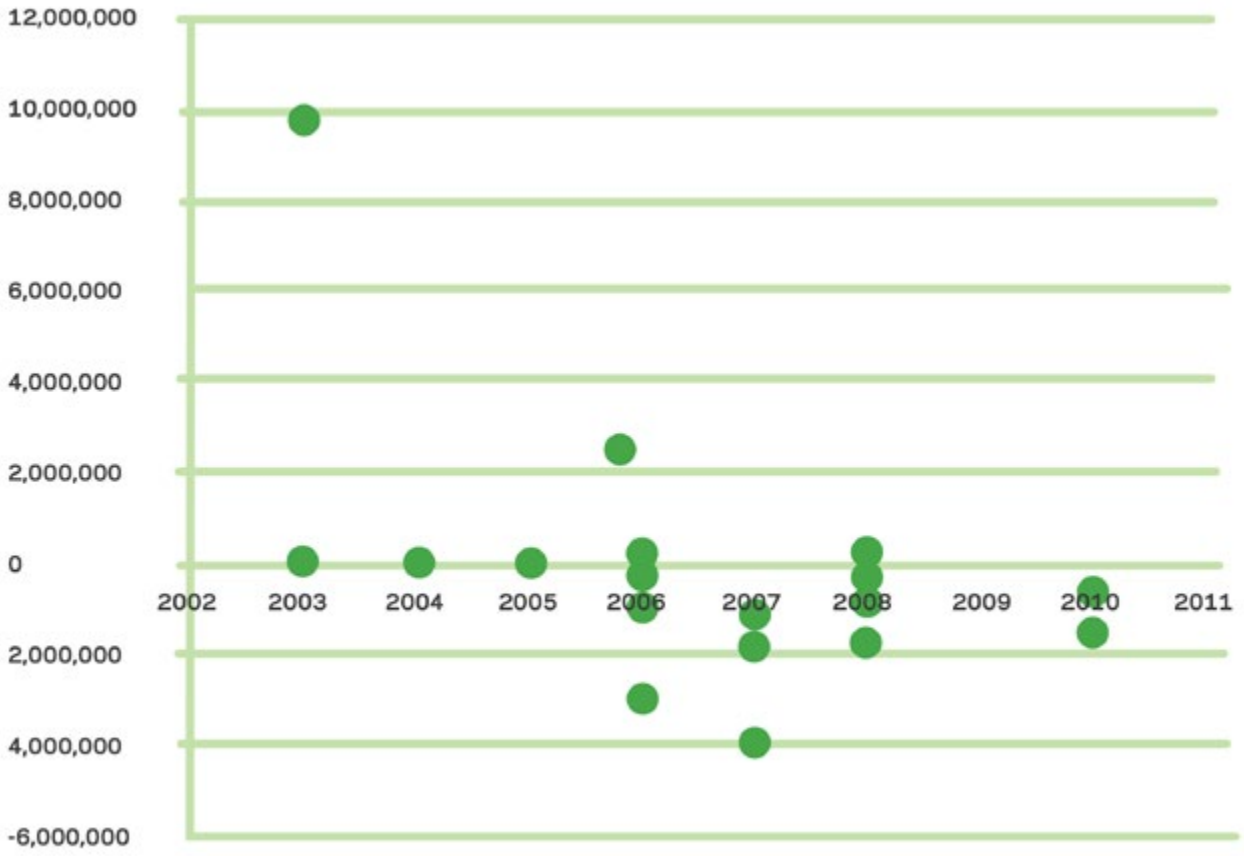
Table 5: AfriCap Technical Assistance to Portfolio Companies[15]

Name	Value Accretion	Fintech TA	TSF TA	Net Value Accretion
1 Equity Bank	10,000,000	NA	228,020	9,771,980
2 Pride Uganda	37,423	NA	225,138	-187,715
3 First Allied S&L	127,000	NA	122,014	4,986
4 Socremo	1,069,865	944,244	238,049	-112,428
5 Pride Tanzania	-167,894	NA	0	-167,894
6 UTB	394,503	NA	86,452	308,051
7 WWB	-2,487,109	419,260	16,018	-2,922,387
8 ACCESS	261,459	NA	252,681	8,778
9 Opportunity	-939,390	11,118	NA	-950,508
10 CAP	-168,815	NA	30,626	-199,441
11 QFI	-716,108	NA	30,000	-746,108
12 Susu	-3,624,097	337,362	NA	-3,961,459
13 Wizzit & Rcubed	-1,257,284	499,230	NA	-1,756,514
14 Ferlo	-1,065,284	99,734	NA	-1,165,018
15 Asusu	950,914	1,281,604	NA	-330,690
16 La Regionale	354,707	1,094,055	NA	-739,348
17 BACB SOFIPE	584,316	361,554	NA	222,762
18 Tujijenge	-166,119	546,627	NA	-712,746
19 AE&I	-858,101	857,280	NA	-1,715,381
20 Birima	-1,307,740	183,505	NA	-1,491,245
21 Finance Salone	-148,926	514,602	NA	-663,528
Total	873,320	7,150,175	1,228,998	-7,505,853

15 Sources: Appendix 5, Evaluation of AfriCap Microfinance Fund, USAID, June 2007; Table 5, of FinTech Africa Final Report, prepared for Bill & Melinda Gates Foundation, May 2014, p. 13.

In a very fundamental way, however, AfriCap's TA failed to translate into economic value in the specific recipient companies. For nearly all of AfriCap's investments, the total cost of TA provided by the TSF and FinTech combined was greater than the financial value created in the company during AfriCap's hold, based on realized proceeds or the most recent FMV. The benefits of TA can be evaluated in different ways; however, the TA function failed to achieve AfriCap's overarching objective of demonstrating the viability of commercial microfinance.

Table 6: Value Accretion Net of Cost of Technical Assistance

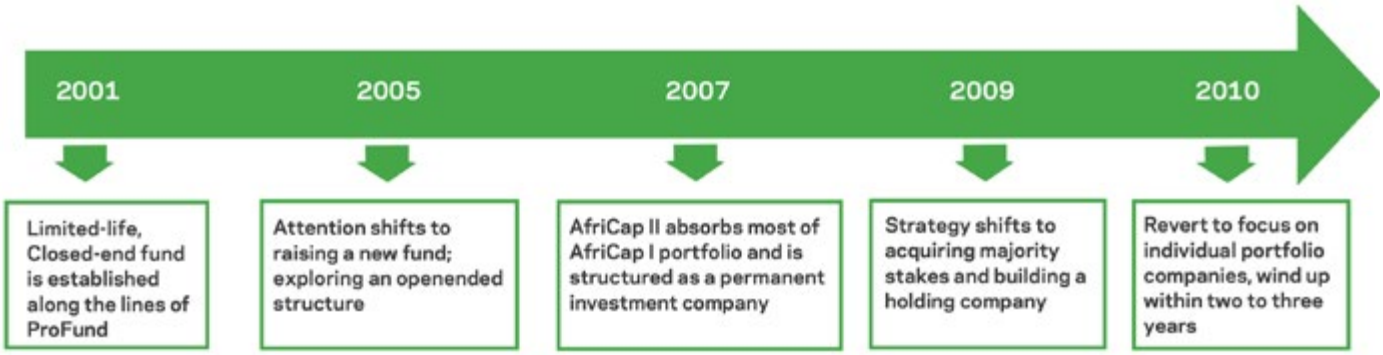


3. Key Governance Issues

a. AfriCap Strategy and Structure

Much more than most funds, AfriCap's strategy and structure changed significantly and repeatedly during its life. Launched with the intention of replicating ProFund's narrow but profound and influential success as a closed-end private equity fund, which conclusively demonstrated the existence of an investable commercial microfinance industry, AfriCap, emboldened by its early success with several investments and an apparently robust pipeline, shifted its emphasis barely four years into its life to become a follow-on fund with an open-ended structure. AfriCap II was created as a permanent investment company with no obligation to liquidate individual investments but, instead, the goal of providing liquidity to investors after six to seven years, either through an initial public offering (IPO) or the strategic sale of the entire company. With this foundation, the Fund began to explore consolidation and holding company initiatives for its portfolio companies. But stresses on the Fund led to retrenchment, reversion to a portfolio-management emphasis, and ultimately the decision to liquidate the portfolio by the end of 2013.

Table 7: Timeline of Fund Structure



Similarly, the management function underwent several changes in structure and strategy. At the outset, AfriCap Micro Ventures (AMV), an Ontario corporation wholly owned by Calmeadow, was engaged as manager to provide investment management and administrative support to the Fund, including management of the technical support facility:

- An investment committee appointed by the Board approved all investments and, with the participation of an appointee of TSF funders, all TSF commitments.
- Management fees and expenses were to be submitted to the investment committee or its designee for approval.
- Management was to devote its exclusive time and attention until the substantial liquidation of the Fund and the approval of two-thirds of the shareholders.

In January 2006 Calmeadow proposed creating a new management entity, AfriCap Investment (AI), which would be majority, and eventually entirely, owned by senior members of the management team and to which the AfriCap management contract would be transferred. In proposing the change, Calmeadow noted:

One of the legacies of AfriCap Fund is the creation of a Fund Management Company with private equity and management competence that will hopefully continue to raise funds and contribute to the development of the African private sector. This proposal is one more in a series of steps that have supported the successive transformation of the Management Company into one which is managed and owned by local professionals who have demonstrated full commitment to AMV and to support development of commercial microfinance in Africa through equity investment. Reconstituting the Fund Management Company as an entity incorporated in Africa and majority owned by employees fully focused on microfinance in Africa is a logical next step in this direction.[16]

As part of the creation of AfriCap II in 2007, AI subcontracted with a new company formed by the fund manager for advisory services. However, substantial oversight and authority remained vested in the AMIC Board and, in particular, the AMIC chair, including over such matters as the advisor's budget, reporting, providing leadership and support in AMIC strategy development and implementation, overseeing and ensuring the advisor's performance, and undertaking advisor performance reviews.

Within months of the launch of AfriCap II, this arrangement was challenged, as AMIC Chair's oversight was perceived by management to be excessively intrusive. Not without dissent, the shareholders ultimately agreed to sell AI to a management company created and controlled by the fund manager and began to explore new strategic directions for AfriCap, as well as to develop new initiatives of AfriCap's own. Initially this arrangement engendered significant confidence and support, but by the end of 2010, the management company and AfriCap had agreed to part ways.

After careful consideration of alternative management arrangements, at the end of 2010 the shareholders selected the AfriCap Board chair, who had been serving as interim manager for several months, to hire a staff and oversee the wind-down of the Fund over a two- to three-year period.

While, in retrospect, the extent and frequency of shifts in strategy and structure at both the Fund and advisor levels is stunning, at the time these shifts were generally based on a thoughtful and considered reassessment of the environment and opportunities AfriCap faced and the challenge of forging a common vision among and between shareholders and management, particularly as people with new perspectives joined senior management, the Board, and the investor group.

16 Calmeadow, memo to shareholders, January 23, 2006.

Valid as these changes may have been in and of themselves and taken individually, taken together they created a fundamental lack of stability, accountability, and coherence. Additionally, the process of considering, adopting, and implementing the changes absorbed substantial amounts of management and governance attention and energy, which was diverted from managing the investment portfolio itself.

b. Budget and Human Resources: "Too much money, too few people on the ground in Africa"

The question of the adequacy of AfriCap's human resources played out on two levels: was the budget sufficient for the task, and did staff and Board members have the necessary skill and experience? With respect to the budget, the answer early on was that the budget was almost certainly inadequate. Intentionally or not, AfriCap's budget seemed to have taken the ProFund management fee of 3 percent as a benchmark, ignoring the fact that Omtrix had already been recognized as extraordinarily frugal; that ProFund's capital commitments, and thus its base for calculating fees, were two-thirds higher than AfriCap's ($22.3 million versus $13.3 million), and that Africa was likely to be a more costly operating environment than Latin America.

AfriCap made some efforts to cushion itself against these pressures. ProFund's management-expense ceiling of 3 percent for was relaxed slightly to allow for annual expenses of up to 3.5 percent, calculated as a two-year rolling average but including advisory fees to Omtrix.

More important was the TSF. As the 2007 USAID assessment noted, "AfriCap has benefited from significant TSF Category III funding, which in addition to paying for TSF management, has helped the Fund to develop capacity, pipeline, and marketing efforts (suggesting Fund management fees may be too low)."[17]

The investment team was authorized to recoup direct salary and travel expenses associated with managing the TSF plus a reasonable overhead allocation, thus effectively supplementing its budget: a potentially significant offset. According to the 2007 USAID evaluation, of the four FTE on the management team, 1.63 were devoted to the TSF; thus these costs were recouped. However, nearly one FTE of this time and effort was sourced from the three-person investment team, meaning that only two FTE were available for managing what was then a portfolio of ten companies (one having been exited) at a time when the team was also actively engaged in planning for AfriCap II.

Overall, while the TSF and then FinTech activities and funding undoubtedly supplemented the resources of AfriCap's investment team, they may ultimately have done more damage by obscuring the true resources effectively devoted to creating value for the Fund in the portfolio companies and obscuring accountability for creating that value. While a high degree of coordination between the TA and investment functions was originally envisioned, this appears to have in fact been the case only in the early years; thereafter, the TA envisioned for portfolio companies was largely unspecified at the time of investment and little monitored thereafter. Eventually, FinTech operated largely independently of the AfriCap investment function. In contrast, procedures in place at other contemporaneous funds required a detailed TA program to be submitted and approved as a precondition for the ICOM to approve an investment.

17 Evaluation of AfriCap Microfinance Fund, USAID, June 2007, p. 12.

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The FTE resources available also have to be viewed in the context of travel and language requirements. Travel was undoubtedly taxing in all regions, but perhaps somewhat more so in Africa. With respect to language, both ProFund and AfriCap faced regions with three main working languages (four for ProFund, counting English), but as a practical matter, nearly all ProFund's investments, with the exception of SogeSol, were effected in Spanish-speaking countries. By contrast, eight of AfriCap's investments were in French-speaking countries and a ninth, the Fund's largest, was in Portuguese-speaking Mozambique.[18]

The goal of nurturing an African management team added another challenging dimension to the human-resource picture. This objective had always been prominent in the thinking of at least some of AfriCap's investors and promoters and, as of 2007, remained a key feature in the thinking about AfriCap II. Indeed, the USAID/DFID evaluation highlighted this as a key finding: "AfriCap, as an African based and managed investment fund provides a counterbalance to the internationalization of microfinance in Africa: a made in Africa solution."[19]

Indeed, there were compelling business reasons to put an African national in place as manager. Another equity manager contemporaneously active in the region recalled that he felt seriously handicapped without an African national on his team who could more effectively navigate local networks and operating environments; he ultimately did bring an African national on board.

However, despite its clear advantages, this goal posed significant challenges. The pool of qualified candidates was small and highly sought after by conventional financial-services companies. At the first meeting of the AfriCap steering committee in 2000, it was noted that the search for the initial manager would likely take four to five months and that salary requirements would be competitive. Presumably on the basis of this input, the steering committee decided less than three weeks later to offer the manager position to Stefan Harpe, a Canadian who had midwifed AfriCap as the Calmeadow investment director, and to seek to recruit African nationals initially for junior positions, to be primed to take over as fund manager within three years.

While AfriCap adhered to the decision to recruit a new manager after three years, it was not done carelessly. The Board did carefully consider its options in selecting a replacement, including the possibility of conducting a search. In the end, it was decided that a search process would be destabilizing and that there were clear advantages to promoting from within, especially given the presence an inside candidate who had shown energy and initiative. Once again, it was not a case of the Board making a decision hastily or without carefully considering the options but rather, having done so, finding itself unable to provide the oversight and support to compensate for the challenges and risks its choice entailed.

While staffing levels and time allocation fluctuated at various points during the Fund's life (see "Staffing History," included in the Appendix), a snapshot was prepared as part of the USAID evaluation in 2007. Given that, at the time this evaluation was prepared, the Fund held 10 active investments, it appears the investment team was stretched. Among other things, resources devoted to "Board participation" were quite constrained, notwithstanding the importance attributed to AfriCap's governance role elsewhere in the evaluation. Overall, of the three team members with direct investment responsibilities, less than two FTE were estimated to be devoted to developing and managing the investment portfolio.

18 One example of such language challenges was the Fund's experience with Bankers Realm, an English-language MIS with support in Kenya. The system, which at one point was seen as the backbone of a common back office to support MFIs and potential consolidations or shared services, became an encumbrance for French-speaking West African MFIs, which struggled with language and substantive differences with MFIs in the English-speaking countries.

19 Evaluation of AfriCap Microfinance Fund, USAID, June 2007, pp. 36, 38.

Table 8: Estimated Workload Distribution (Percentage of Time Worked)[20]

	Equity Fund Administration	Pipeline Development	Deal Preparation	Board Participation	Other Fund Activities	Technical Support Administration	Technical Support Management	Technical Support Other
Managing Director	15%	30%	20%	10%	5%	5%	10%	5%
Investment Officer	1%	15%	30%	1%		18%	35%	
Investment Officer	2%	30%	38%	5%	5%	5%	10%	5%
Administration	30%					70%		

This impression gets some confirmation from a summary of staff responsibilities included in a review of AfriCap performance to date prepared by AfriCap and published in 2007, in which individual management company staff members are reported as sitting on the boards of as many as eight companies.[21] Furthermore, these crude estimates of the quantity of human resources available for investment activities ignores turnover, which appears to have been high.

Although the workload on the investment team was high, there were multiple indications that the time involved to source and manage investments would be longer than initially anticipated. Discussions of the investment pipeline noted that AfriCap had encountered institutional weaknesses and obstacles that made transformation and investment very complex and slow. The development of new commercial opportunities showed more promise, although those prospects took more time to research and cultivate. AfriCap management and Investment Committee acknowledged that these features of the landscape meant that AfriCap needed to revise its expectations regarding the time it would take to develop relationships, negotiate a partnership, and begin to exert some influence in investee institutions at the Board or senior management level.

The human-resource challenge was particularly daunting because AfriCap simultaneously set itself the goals of building a solid and influential portfolio and developing locally sourced staff. While skilled and capable individuals were recruited, they required more support in the area of microfinance; in dealing with startup, early-stage, and high-growth companies; and in other aspects of portfolio management than was at first appreciated.

Aside from the budget and the adequacy of the quantity of human resources committed to achieving AfriCap's objectives, there is also the question of instability in the key positions – i.e., three managers, four chairs – and the distance separating key players from each other and, in some cases, from the region.

Personal characteristics played a role as well. Several of the key people, including all three investment managers and the third Board chair, had never held comparable positions previously and inevitably needed to "learn on the job" and, more importantly, win the confidence of their counterparts (which, given the challenging circumstances, was difficult to do). While such transition issues are inevitable in cases where, as with AfriCap, a deliberate decision has been made to develop new talent, in this case African nationals, the Board was clearly overambitious in combining so many transitions and so much on-the-job training at key junctures in AfriCap's evolution. During one such phase, over a three-month period, both the manager and Board chair were replaced with people who were clearly capable but lacked experience in executing the responsibilities they were being handed.

c. Investment Management Team Structure and Supervision

Separate from budget matters, as well as from the question of how completely specific individuals filled the ideal set of qualifications and skills, is the question of how a board can strike the appropriate balance between providing support and oversight on the one hand and micromanaging on the other. Both structures and personalities play critical roles in determining whether this balance is successfully struck or whether there will be constant, debilitating tension and suboptimal performance. The AfriCap experience seems to illustrate the limitations of structure in achieving a good outcome in the absence of engaged and constructive relationships between key protagonists.

As noted above, the structure of the AfriCap management function evolved significantly during the life of the Fund. Initially wholly owned by the fund promoter, Calmeadow, the manager became partly and then wholly owned by the investment team, with the expectation that it would use AfriCap's success to evolve into a permanent feature of the African impact investing landscape as a manager with multiple funds and initiatives. Such an evolution would have mirrored the experience of similar managers in other regions, including Omtrix in Latin America and Caspian in India.

20 Ibid., p. 28.

21 Africap Review, 2007

But while AfriCap's management structure seemed to follow a solid and progressive path, the key relationships necessary to make the evolution and transitions successful do not seem to have been consistently in place. One such relationship was that between the Board chairs and the managers. Others were the relationships within the management team itself; whether team members were being appropriately and fairly incentivized was also in question.

AfriCap suffered from unresolved differences regarding the roles of the Board, its committees, and the manager and the appropriate degree of oversight and distribution of authority. These are common challenges; nearly every fund struggles to set its own workable balance. However, it is important to recognize that achieving this balance depends on a combination of structure and personal relationships: when new relationships are forged, the balance has to be struck anew. AfriCap's frequent changes in key personnel meant that it was perpetually facing this issue.

The ineffectiveness and instability of these key relationships had two consequences in particular. First, for much of the Fund's life, the Board chair struggled to reconcile divergent views and articulate stable and clear guidance for the manager. A case in point was the pace of investment. Notwithstanding the resource challenges and constraints on the investment team, there are indications that the Board expressed dissatisfaction with the pace of investment in the early years of the Fund.

In the 2003 annual report published in 2004, for example, the Board chair commented: "Our earlier frustration in making initial investments is behind us and it is clear that this current year will see several new investments and an increasingly positive environment for expanding our portfolio." Initial projections that the portfolio would reach $4.8 million by the end of Year 2 were not realized, with actual outstanding of $2.6 million. At the time four additional investments were predicted to close in 2004, but none of them ultimately did; indeed, no additional investments were closed in 2004.

It is not farfetched to suspect that the investment team noted such sentiments and pressures and interpreted them as encouragement to prioritize building the portfolio, even though there were Board and committee members who supported the deliberate pace of investment and counseled caution. By the end of 2006, the new team had indeed accelerated the pace, making eight more investments, including four startups. Of these, four were ultimately written off.

A second area where confidence, mutual respect, and a certain degree of good chemistry are required to make any structure work is in striking the balance between providing an appropriate degree of oversight and enforcing accountability, with the need to empower the manager and avoid micromanagement. Here again, the key relationship is between the chairs of the Board and of key committees, in particular the investment committee, and the fund manager.

At AfriCap, the lack of stable and constructive relationships between these key positions created prolonged distractions and diverted energy from core functions.

AfriCap's instability also helped make other issues that bedevil nearly all funds more difficult to resolve. One is the question of successor funds. The manager is necessarily, and to some extent appropriately, preoccupied with its future viability, which almost always requires planning for a successor fund to begin well before the initial fund is anywhere near successful completion. This inevitably creates some tension with investors: while they have a clear interest in ensuring that the manager can support adequate staff and resources to successfully manage its portfolio, which in most cases requires successor initiatives, they do not want too much time and attention diverted prematurely.

d. Investment Committee

As in most investment funds, the ICOM was tasked with a direct and engaged role in overseeing and guiding the management team and safeguarding the Fund's focus and the coherence of its strategy.

Table 9: Roles and Responsibilities

AfriCap was poised to benefit from a very strong and experienced committee from the start. It was originally stipulated, for example, that Calmeadow and Accion, as sponsors, would hold permanent seats on the ICOM in an effort to provide consistency and continuity. In addition, experienced ICOM members were nominated by most of the institutional investors. For a variety of reasons, however, the ICOM was challenged in fulfilling its core responsibilities.

Perhaps most significant, the concept of formal membership in the committee did not seem to be observed from the inception of the Fund until sometime in 2009. While the ample participation of Board members, alternates, and others in committee meetings showed their admirable readiness to lend their experience and insights to support the manager's efforts, it also likely contributed to an erosion of accountability, lack of follow-up, and overall lack of investment discipline.

Following a Board meeting in April 2005, the manager delicately noted to the Board chair that "I think that the days when we wanted to appear open and transparent to everyone are over, and we need to tip the balance back towards an efficient meeting process and limit attendance." But even with the problem identified, meetings continued to be open.

This open-door approach had disconcerting results. From 2004 to 2006, 22 different people were identified at various times as ICOM members.

Table 10: Participation in ICOM Meeting

While the Calmeadow nominee attended all meetings during this period and acted as chair, the second sponsor representative seat, from Accion, was filled by three different people, who together attended 9 of 17 meetings. During 2008 and 2009, even the continuity of the chair was interrupted when he stepped down for 18 months. Other than the chair, only three members attended at least two-thirds or more of the 19 meetings; one of these also stepped down – in this case permanently – in 2008. In part because the ICOM was responsible for both the investments and the TSF, meetings were often lengthy. One former ICOM member described the ICOM's message to shareholders as "If you want to be a part of what's happening, we'll make room."

It may not be surprising, given this lack of continuity and consistency, that the committee inadvertently gave the manager mixed messages. While some members recall the completeness of information and timeliness of reporting as their primary focus, others complimented the manager for the pace of investment and the robust pipeline, particularly from mid-2005 and thereafter.

In some respects, the situation improved in later years. By 2009, membership of the operations committee (OC), which replaced the ICOM, stabilized. But issues of continuity continued, attendance was spotty, and potential conflicts intensified.

The ICOM based its investment decisions on reviews of investment proposals prepared and presented by the fund manager. The ICOM met once every two months, or sometimes more frequently if required, over the phone or in person.

A review of one-third of the companies in which AfriCap invested finds several themes:

- The majority of the investee companies were at an early stage, based in large, underpenetrated markets, and led by dedicated promoter-managers. It was expected that AfriCap capital would spur these companies on to a high-growth trajectory, which would be the main source of investment returns, with forecast cumulative annual growth rate (CAGR) in assets ranging from 20 to 120 percent. It is not clear that the challenges and risks of managing such high growth were emphasized.

- In most of the investments, AfriCap was the first institutional investor. While as the first mover it gained some advantage with respect to pricing, the responsibility inherent in its unique position was not highlighted.

- As noted earlier, the role of TA was supporting the companies; building values was generally unspecified.

- AfriCap took a significant minority stake (20 to 30 percent) in all the companies, but it was not necessarily clear how it would ensure the desired improvements in governance from this minority position.

- The investment instrument most often used was common equity which generally meant it was locked into companies where its influence was limited.

At the time of investment, all of the companies were arguably "investable" and offered the potential of creating social value by expanding microfinance services in low-income communities. However, by making investments in a large number of such companies under these terms, AfriCap took on a herculean task. Was the investment team ready to take on an active role in supporting so many high-growth businesses? Was there a solid plan to monitor these businesses as they entered a high-growth phase? How much time would be required to exert the desired influence, in light of AfriCap's minority and often isolated position?

Although a TA budget was usually part of the investment plan, it often did not reflect a specific assessment of the company's TA needs. Was there a solid plan to meet the TA needs of the company through the entire tenure of the AfriCap investment? Was the TA support team (TSF/FinTech) part of the investment decision process to ensure that the needs and ownership of the TA would be properly assessed up front? In the case of the Equity Building Society investment, the TSF manager was closely involved in investment due diligence and developed a detailed TA plan, but there is no evidence that such close coordination between the TSF manager and the investment management team was characteristic of other, later investments.

AfriCap's position as the pathbreaking investor in the region meant that its investment analyses of the companies were generally not supported by an independent view of other investors, lenders, or raters – leaving a big responsibility on the investment team to get it right each time without the benefit of an "extra pair of eyes" from other stakeholders or independent observers (lenders/regulators/raters) to validate or challenge their investment thesis.

Overall, post investment support to companies was expected to be the investment manager's primary focus, according to the original concept and strategy, but it appears that the investment team did not or could not preserve this focus. While a portfolio review process was in place to monitor companies' performance, it did not seem able to generate actionable plans and accountability for addressing the identified issues in each case.

In some cases, it appears that TA was planned to assist companies in strategic planning, effectively outsourcing to external consultants an opportunity to influence the investee company's business strategy when it was needed most. It was often not clear what the investment team saw as its own role in supporting the investees. Nor is it clear how the ICOM understood and monitored the investment team's plan to create value.

Ironically, the Fund's early success may have contributed to an atmosphere in which investment discipline was allowed to deteriorate. As one Board member noted: "The Equity Bank success led Board members to refrain from asking questions. Nobody wanted to be the black sheep, asking questions in the face of success."

e. Board Engagement and Capacity

As early as the initial steering committee meetings in 2000, the importance of providing for continuity on the Board and ICOM was recognized and permanent seats on these two bodies were allocated to Calmeadow and Accion to "reinforce the commitment they have to a long-term engagement and continuing responsibility for governance oversight." Despite this intent, the ICOM chair was the only member of the original sponsor group who remained engaged through most of the life of the Fund; only one other Board member remained engaged throughout the life of the Fund.[22]

Reflecting the challenges it faced in translating its ambitions and the ProFund model into the challenging and very different reality it faced in Africa, AfriCap has been characterized by a very high degree of instability: in leadership, management, structure, and strategy. Other equity MIVs have recapitalized (AIM, 2006), changed management (ShoreCap, 2009), and changed strategy (Catalyst, 2008). None, as far as we are aware, have changed management three times, chairs four times, strategy at least four times, and structure three times. Certainly none have undergone simultaneous changes in all four dimensions even once.

While some or all of these changes can be questioned in hindsight, at the time there were good reasons for them, and all were pursued after careful and reasoned consideration. But cumulatively, such a dramatic scope and scale of change illustrated instability in the views of shareholders and directors and also placed an enormous responsibility on directors to manage the changes constructively. As one investor noted, "what we earlier considered positives [about AfriCap] turned into negatives. We were attracted to the fund seeing a variety of shareholders, microfinance experts, but in fact participation of so many shareholders turned out to be negative. If shareholders were limited maybe the fund's strategy would have been more focused."

The challenge of managing transitions and preserving the initial cohesion painstakingly built during the launch process was overwhelming. The centrifugal forces that emerged created problems repeatedly during the Fund's life, but were particularly evident during the search for a replacement for the second manager. The selection process dragged out for a year.

Candidates and indeed approaches – engaging an established third-party manager or recruiting an individual – were solicited and rejected. In the views of a number of observers and participants, this prolonged interregnum, when active, accountable management of the portfolio was absent, bears significant responsibility for the loss in value that many portfolio companies realized.

The capabilities of the Board itself also warrant scrutiny. Investors seemed comfortable with a Board composed almost entirely of members who were not African and, with few exceptions, were based outside the region and had limited direct experience there. While this was somewhat understandable in the early years of the Fund, when it was a novel and pathbreaking initiative, it becomes harder to understand by the time of the recap, when the Fund had tripled in size and new strategies, like a holding company, were under serious consideration. Given such circumstances, continued efforts to recruit more African and independent Board members with regional experience would probably have been advisable.

f. Technical Assistance

Early on, a decision was taken to combine AfriCap's investment with technical assistance. While this was contrary to the approach ProFund had taken, which was deliberately not directly involved in TA funding or provision, it reflected the assessment of AfriCap's creators that the more challenging African environment and the generally less developed state of the region's MFIs and industry warranted a companion TA capability.

This was consistent with the view taken by a contemporaneous fund, ShoreCap, which was launched together with a companion TA facility, ShoreCap Xchange. However, the functioning of AfriCap's TA function, in both its iterations, mostly functioned quite differently from that of ShoreCap.

AfriCap's TA function took two forms. During AfriCap I, the TSF was a $3.8 million fund used at the discretion of AfriCap fund managers. The TSF had two objectives: to enhance investees' institutional development (Category I expenditures) and to communicate AfriCap's activities to audiences beyond its shareholder group in ways that would have sector-wide impacts across Africa (Category II expenditures). The TSF also provided funds for its own management (Category III expenditures).[23]

For AfriCap II, a different structure was implemented (in response to a Gates Foundation requirement that its funds go to a nonprofit recipient), but the concept was the same: TA would be designed and delivered primarily in support of AfriCap's portfolio companies, with some more general industry-building efforts also contemplated.

22 Steering committee, December 4, 2000.
23 Evaluation of AfriCap Microfinance Fund, USAID, June 2007. Pages 9-10.

The TSF was run by a manager who reported to the fund manager; TA commitments were approved by the AfriCap ICOM. The TSF was considered a key value creator for AfriCap companies and, by all accounts, the relationship seemed to work well in the Fund's early investments, when the TSF function of supporting the investment program was well coordinated and implemented. In the case of Equity Building Society, TA focused on its planned transformation into a bank, recruiting key staff, and enhancing information technology (IT). In the case of First Allied Savings and Loan, TA efforts focused on human-resource issues, IT, and addressing portfolio at risk (PAR).

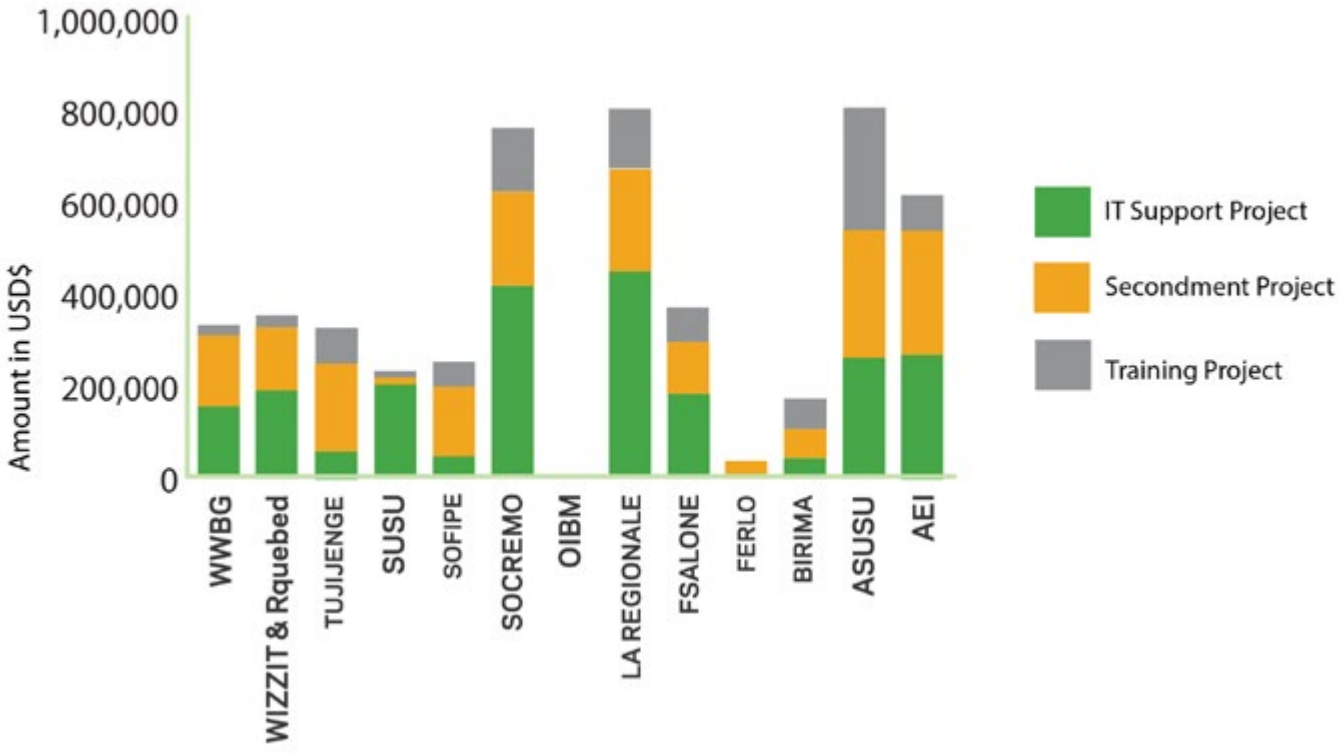
In these cases, there was close coordination between TSF and fund managers. For example, in the Equity Bank investment, the TSF manager and investment officer conducted joint due diligence. The TSF manager later presented a TA plan funded jointly by AfriCap, DFID, and Equity Bank .

This was similar to ShoreCap's approach. ShoreCap's investments were supported by TA from ShoreCap Xchange. The investment team was led by a manager who reported to the Board. The Shorebank TA team had its own manager and Board whose decision-making was independent. However, coordination between investment and TA teams was achieved through joint due diligence. Investment manager looked at the deal during the due diligence mission while TA manager prepared a detailed TA plan. The TA plan showed how XChange would support the company through the life of the investment. This plan was approved by the XChange TA Board and was an integral part of the investment proposal – the ShoreCap ICOM could not approve any proposals which did not have a detailed TA plan attached.

After AfriCap's initial investments, for which TA was designed, the planned close coordination appeared to diminish. This corresponded to a change in TSF management, with the departure of the initial manager seconded by DFID and the appointment of a new fund manager.

With the creation of FinTech, the concept of targeting TA in support of portfolio companies remained the same. The FinTech manager a member of the AfriCap investment team, although as a formal matter TA funding was approved by the FinTech Board rather than the AfriCap ICOM as previously. In 2009, however, the FinTech manager moved out of AfriCap and became independent. This progressive separation of the TA and investment functions meant that the initial focus of TA on portfolio capacity-building and performance was further weakened.

Table 11: TA and the Role of FinTech [24]



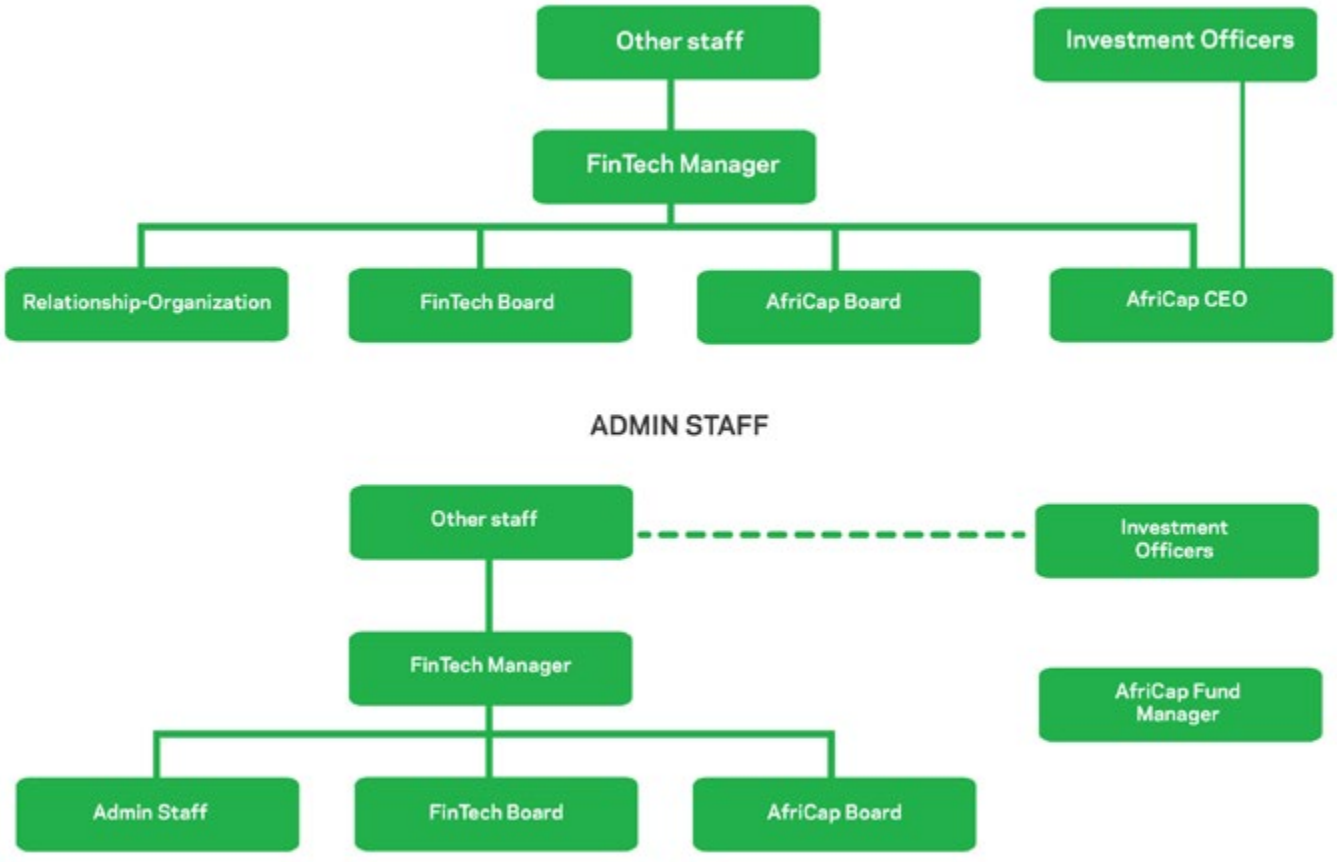
24 Source: Brice, James, Felicia van Staden, Stephane Mabiala, and Janine Elske in partnership with Fintech. "Exit Report: Investments, Impacts and Lessons Learned in the Microfinance Industry across Africa, November 2013," p. 15,

In many respects, the TA management change appeared to improve matters. FinTech, for example, arranged the replacement of five CEOs, showing both the formidable size of the task facing AfriCap and how TA could add value. In such cases, AfriCap's TA was important in building capacity in investee MFIs as well as in raising the stature and legitimacy of the African commercial microfinance industry.

In some respects, TA generated positive results – a Gates Foundation assessment in May 2014 found that between 2009 and 2013, portfolio growth and financial parameters improved in nine of eleven companies. From the perspective of value creation, however, AfriCap's TA, as an instrument of support for portfolio companies, was severely handicapped by inadequate coordination and oversight with the investment process and suffered from loss of focus and accountability.

g. Infrastructure

Figure 1: AfriCap and FinTech's Relationship – Organization Chart (before 2010)[25]



25 Source: Cordier, Charles and Gregory Thys. "External Evaluation of FinTech Africa Technical Assistance Facility," p. 13.

AfriCap's initial design appeared to reflect the recognition that Africa posed special logistical challenges and that the team would be stretched to undertake its core responsibilities of building a portfolio and investment staff. Thus the reasonable decision was taken to try to relieve the team of some important but secondary responsibilities such as financial administration, which were contracted out to Calmeadow in Toronto and later, temporarily, to Omtrix in Costa Rica.

While well intentioned, understandable, and perhaps correct, this decision had negative consequences not fully appreciated and therefore not managed by the Board. Most importantly, it undermined clear responsibility and accountability for reporting, which became a chronic source of tension between management and the Board.

h. Conflicts of Interest

Throughout the initial years of AfriCap, when some of the investors in the Fund were also actively investing directly into African MFIs, the Fund operated in the absence of a formal conflicts-of-interest policy and procedures. Some AfriCap investors were also investing directly into the same companies where AfriCap was an investor, as in WWB Ghana and Socremo. The management company formed in 2008 that assumed management of AfriCap was partly owned by one Fund investor that was also actively investing in African MFIs independently of AfriCap.

While such conflicts were not unique to AfriCap, and in fact historically have more often been the rule than the exception in the small world of microfinance, the effective absence in AfriCap of a formal policy/process to disclose and agree in advance upon policies and procedures in each case led to subsequent differences in views, unnecessary contention, and distraction from core issues.

Following the 2007 recap, the governance and audit committee (GAC) was left to manage any conflicts, but at times the committee found itself preoccupied with other issues. When the GAC did turn its attention to conflicts, it found that shareholders' conflict reports were incomplete and out of date. As late as 2011, GAC members stated that "AfriCap needs to tighten its conflict of interest practice." However, by 2011 all of AfriCap's investments were made and most of the conflicts already in place.

A related issue with indirect relevance to the question of conflicts was the relative absence of independent directors on the Board and its committees. Efforts were made at various times to recruit independents to the Board, but only one, Anne Marie Chidzero, remained for any significant length of time. Similarly, with the ICOM members drawn exclusively from the Board, Ms. Chidzero was also effectively the only independent member of that committee. As tensions and questions arose about conflicts, the absence of more independent directors with experience and stature eliminated one possible means of alleviating concerns.

4. Summary of Governance Functions (CMEF Framework)

In 2012, the Council of Microfinance Equity Funds (now the Financial Inclusion Equity Council (FIEC)) updated its 2005 report "The Practice of Corporate Governance in Microfinance Institutions" (the Governance Guidelines). The Governance Guidelines are primarily aimed at shareholder MFIs but remain relevant to other corporate forms, such as credit unions and NGOs. The Governance Guidelines were not intended to cover governance of investment funds. However, in undertaking this governance review of AfriCap, Grassroots concluded that the Governance Guidelines offer a comprehensive framework largely applicable to the governance of funds[26] as well.

In using the CMEF Governance Guidelines as a framework for the assessment of how AfriCap's governance supported or undermined its performance, Grassroots posed three high-level questions:

- Were the "best practices" recommended by the Governance Guidelines appropriate and sufficient, and did AfriCap largely follow them?

- Did the best practices contain gaps or misguidance that contributed to any performance shortfall that AfriCap realized?

- Did AfriCap, despite complying with best practices, suffer due to developments beyond its control?

In other words, did AfriCap not follow best practices, were the best practices not really best practices, or do things sometimes just go wrong even if you follow solid best practices?

According to the CMEF Governance Guidelines, governance, broadly defined, is the system of people and processes that keep an organization on track and through which it makes major decisions.

Although many external and internal actors play a role in governance, including senior management and internal and external auditors, the CMEF Governance Guidelines makes clear that "although governance takes place in this broad context, the board of directors is the pivotal point through which all these players connect."[27]

According to the Governance Guidelines, the following major responsibilities of the Board of Directors reflect the broad purposes of governance:

26 In the excerpts from the CMEF Governance Guidelines that follows, references to "MFIs" have been replaced with references to "Funds."

27 CMEF, "The Practice of Corporate Governance in Microfinance Institutions," 2nd ed., 2012, pp. 4–5.

1. Define and uphold the social mission and purpose of the Fund

CMEF Commentary

The board has a major responsibility to set the strategic direction of the organization. This direction is carried out through strategic planning and oversight of performance vis-à-vis the strategic plan (p. 27).

When board representation is determined by shareholding percentages, little room is left for independent directors (defined as directors who are neither direct shareholder representatives nor members of management) who can take an institution-wide perspective, or who bring the perspective of other stakeholders. The use of independent directors should be a priority for improving governance among MFIs (p. 8).

AfriCap Experience

By not recognizing the demands posed by the multiple goals set for AfriCap, the Board failed to set a realistic mission that could be translated into a coherent strategy. Instead, its determination to push ahead on all goals simultaneously placed enormous pressure on management and led to what one observer described as AfriCap's "see-saw existence," with shareholders' moods fluctuating. There was always something to be happy about, but something to be unhappy about as well.

- If management took the time to carefully develop deals and walk away when warranted, as a PE manager should do and indeed as AfriCap's MIV contemporaries did, it was faulted for not showing results.

- If the manager engaged with less mature companies throughout the continent in an effort to build models for the sector, it could be faulted for poor investment discipline.

- If African management were put in place, they could be faulted for lack of experience or gaps in their capabilities or expertise.

While some efforts were made to bring independent members onto the Board, only one independent member served for any length of time; this member was initially not well experienced in governance.

Elaboration

Sponsors, shareholders, and the Board should clearly articulate priorities at the outset.

At least annually, the Board should explicitly review progress toward objectives, reasons for any shortfalls, and remedial measures.

Confidence in and support of the Fund's leadership is essential. If the Board cannot coalesce around the incumbent leadership, it should either replace or supplement the team or explicitly adjust expectations and objectives to better fit the team's capabilities.

Objectives and strategy should not be maintained if the Board does not have full confidence in the team's ability to execute them.

One or more independent members with experience and stature should be recruited and explicitly tasked with the role of challenging assumptions and group thinking.

2. Develop and approve strategic direction (with management); monitor achievement of strategic goals

CMEF Commentary

Achieving balance between the board's role in governance and management's role in managing is a fine line that may take time and significant effort. Organizations need to make their own assessments on how best to change their governance culture; add board members for skills, independence, or both; and define clearly the role of the board chair vis-à-vis the managing director or CEO. Maintaining the delicate equilibrium between management versus board capture is at the heart of good governance (p. 12).

At each meeting, the board should track a carefully chosen set of indicators aligned with financial goals and social mission – a 'scorecard' or 'dashboard.' These indicators should give a complete and focused picture of the institution, and the presentation should show trends over time. Such a scorecard is an essential tool for the board in fulfilling its mandate to guide strategy (p. 26).
Understand the organization's strengths and weaknesses (strategic role is to address these strengths and weaknesses) (p. 6).

AfriCap Experience

From early on, the Board appeared to lack full confidence in management; this continued through all three managers. As a result there was constant tension, particularly with the first two managers and the Board, and for most of the Fund's life. There was never a stable and agreed-upon allocation of authority, or indeed a working relationship between management and the Board. Particularly between the crucial years of 2005 and 2010, the critical relationship between the Board chair and the fund manager was dysfunctional.

Elaboration

Boards should move quickly and decisively to address any indication of misalignment between the strategic goals of investors, the Board, and management. Board members should assert their responsibility and authority to resolve such misalignments as soon as they are revealed.

Hindsight is easy! But when boards face tensions in trying to balance objectives, for example a commitment to nurturing a management team and accommodating its perspective while maintaining a focus on achieving stated priority objectives, outside advisors or a committee of independent Board members might be engaged to help the Board commit to a coherent course of action.

3. Foster effective organizational planning, including succession planning

CMEF Commentary

Succession planning becomes a particularly sensitive issue for emerging [funds]. It is important to ensure that the [Fund] is grooming future management and that there is a plan of succession. Management succession is a clear and important responsibility of the board (p. 12).

Succession planning is another key responsibility of the board. This is an important aspect of evolution from founder-based beginnings, but can be sensitive. The board should develop a pool of prospective replacements (p. 30).

AfriCap Experience

At the fund-manager level, AfriCap shareholders and the Board committed themselves to succession because of an arbitrary and preordained schedule and a mixed assessment of the initial manager's performance.

Similarly, at the Board-chair level, the 2005 succession seemed driven by preset plans rather than the new chair's readiness for the role.

While in both cases the successions may have been unavoidable and even desirable, given the inexperience of the successors in both cases, a much more careful and deliberate process of support and guidance should have been implemented.

Elaboration

Given the critical importance of the roles of chair and fund manager, Boards should take pains to validate their choices and ensure that proper support for a successful transition is in place. Given the pressure they often face to fill these positions, Boards should have their choices for these roles independently confirmed and agree with the new appointees on a fully articulated plan to remediate any deficiencies.

4. Ensure that the MFI manages risks effectively; assume fiduciary responsibility

CMEF Commentary

Ensure financial survival and solvency; protect shareholders' rights; set key financial targets; evaluate CEO on financial objectives (p. 22).

The board must be continually alert to potential risks and should expect to devote much of its time to identifying and man- aging risks, and determining the risk appetite of the [Fund] (p. 27).

Committees are the workhorses of the board. Committees should meet before formal board meetings and report their progress and findings to the board in an oral report at board meetings, supported by minutes of the committee meetings (p. 24).

[Board members should] avoid making an uninformed judgment/policy decision (if information is inadequate, work with management to get the information needed) (p. 6).

Some warning signs that boards should watch for include . . . Incomplete, incorrect, or nonexistent board reports or financial information; management reluctance to provide information (p. 29).

AfriCap Experience

The primary vehicle for the Board to safeguard the financial integrity of the Fund was the ICOM/OC, which had full authority over all investments and, for most of the Fund's life, TA.

The ICOM's effectiveness was undermined by its open-door policy and very inconsistent participation.

The ICOM did not appear to have the resources or the information to effectively monitor the manager's postinvestment activity.

The available information does not indicate how well the full Board was briefed on ICOM deliberations, although given the expansive ICOM participation by Board members, maybe it was not considered necessary.

Elaboration

Consistent and committed participation in the ICOM by qualified members is critical. Efforts should be made for discussions to be focused and substantive.

The routine participation of nonmembers in ICOM meetings should be avoided, to encourage the accountability of members. The purpose of meetings (as between updates and decision items) should be clearly distinguished.

All meetings should carefully document any follow-up required.

A systematic process for monitoring follow-up on risks or deficiencies identified in the due diligence and analysis should be in place.

5. Oversee management performance, including selection, support, evaluation, and compensation of the chief executive officer (CEO)

CMEF Commentary
The chair is expected to play a more active role than other board members.The board chair should interact regularly with the CEO, have an active role in recruiting board members, be responsible for succession oversight, and be an ex-officio member of all committees (p. 20).

Boards should regularly meet in executive session without management present to discuss matters that may be particularly sensitive regarding management. The standard board agenda should designate a time for an executive session in order to create consistency around this practice. Executive sessions are an important part of preventing management capture (p. 23).

AfriCap Experience
Oversight of the fund managers during the first eight years was inconsistent and counterproductive.

There was recognition of a difficult working relationship between the chair and the manager during the 2005 to 2010 period, which the Board failed to address and arguably exacerbated.

There appear to have been ample misgivings over performance and alignment, but there is no evidence that there were full and focused airings of these issues.

Elaboration
While Fund "sponsors" or lead investors typically have no special formal role, they do bear an ultimate responsibility to keep the Fund on course when the formal governance structure, for example, the authority of the chair, is proving insufficient to the task.

6. Ensure adequate resources to achieve the mission including assistance in raising equity and debt

CMEF Commentary
No commentary provided

AfriCap Experience
While the Board appeared informed and satisfied with the qualifications of the management team, it did not appear to focus on the sufficiency of resources given the simultaneous demands of portfolio management, origination, and developing new initiatives on a small team.

The existence of the TSF and FinTech may have played a role in obscuring how inadequate investment team resources were to the task of managing and creating value in the portfolio.

Public documents at various times noted that the fund manager was sitting on eight to ten company boards.

Elaboration
It is not clear how the Board satisfied itself that resources were adequate to the task; in hindsight it appears that such an analysis was either poorly done or not done.

Boards should periodically review the allocation of roles and responsibilities among team members and explicitly confirm that resources are adequate or direct that supplementary resources be engaged.

7. Ensure that the organization changes to meet emerging conditions; particularly in times of distress, temporarily assume management responsibilities

CMEF Commentary
The board must be continually alert to potential risks and should expect to devote much of its time to identifying and managing risks, and determining the risk appetite of the MFI. Boards should conduct regular risk assessments and ensure that risk management plans are in place (e.g., scenario, contingency, and/or continuity of business plans) (p. 27).

AfriCap Experience
The board and shareholders were receptive and engaged in considering how to adapt Fund strategy to reflect conditions and take advantage of opportunities as they were recognized. However, the focus on changes in strategy and structure was allowed to distract attention from the performance of the core business of the private equity portfolio.

The Board and shareholders as a group were reluctant to accept that misalignment between key actors in the Fund existed; when they finally accepted this, they were slow in implementing a solution.

Elaboration
Independent Board members or advisors with little or no responsibility for previous decisions and no conflicts might be engaged in circumstances where disagreements arise among Board members over fundamental issues of strategy and management. Disagreements of such a fundamental nature should not be resolved through compromise.

8. Uphold the ethical standards of the organization with transparency and avoid conflicts of interest

CMEF Commentary
When joining the board, each new director should sign a code of conduct agreeing to a primary commitment to the MFI in all board dealings. New directors should also complete a conflict of interest form, which lists all potential conflicts and over- lapping affiliations. Members with an acknowledged conflict of interest on a given issue should excuse themselves from voting on that issue (p. 18).

AfriCap Experience
Conflict policies and reporting requirements appear to have been poorly understood and erratically complied with, adding to tensions and further impeding a smooth and effective process for dealing with mounting challenges. Valuable time was lost both in resolving conflict situations that should have been fully aired early on and in agreeing on processes that should have been put in place at the outset.

Summary and Conclusion

The challenges AfriCap faced were undoubtedly greater than those facing its contemporaries or most of the funds that have followed. The extraordinary efforts many Board members made to support the Fund's success and address its challenges must be acknowledged. Overall, however, it is the conclusion of this assessment that with the Fund launched on a very challenging and ambitious path, the Board repeatedly failed to maintain focus and implement an adequate approach to mitigating and managing the attendant risks. That said, AfriCap succeeded in helping to demonstrate that microfinance in Africa is a dynamic and investable business and that investors can expect a return on their investments.

The CMEF Governance Guidelines provide a basis for identifying how AfriCap's governance could have more effectively supported its performance. In some respects, the Governance Guidelines could be more prescriptive: for example, in suggesting actionable steps that boards might take along the lines above. While a variety of other tools and frameworks exist to help guide and evaluate governance, as a practical matter, simpler is probably better.

Board members should not compromise on matters of fundamental disagreement or misalignment with respect to strategy or key personnel. Boards should be critical of their own performance as well as that of management. Boards should accept their ultimate responsibility for financial performance unless it is explicitly determined that financial loss or underperformance is acceptable.

In all these fundamental areas of Board responsibility, AfriCap's governance fell short. While the Board deserves credit for pushing ahead into uncharted waters and for charting a course that many others are now following, to the benefit of African MFIs and their partners, it also deserves the blame for AfriCap's underperformance and for its unfulfilled promise.

Appendix A: Interviews

Ira Lieberman, Lipam International, FinTech
Stefan Harpe, Oikocredit, formerly AfriCap
Anne Marie Chidzero, AfriCap
Emile Groot, FMO
Lauren Burnhill, formerly Accion
Hany Assaad, formerly IFC
Martin Connell, Calmeadow
Alex Silva, Omtrix, Calmeadow
Wagane Diouf, formerly AfriCap
Edvardas Bumsteinas, EIB
Carole Maman, BIO
Peter Gachuba, formerly AfriCap
Lars-Olof Hellgren, Nordic Microcap, AfriCap Sweden
John Fischer, Accion, formerly AIM
Deepak Malik, NorFund
Ben Botha, Socremo
Paul Christensen, formerly ShoreCap
Brian Richardson and John Da Silva, Wizzit
Fahan Bamba, Afrique Emergence & Investissements
Xavier Pierluca, Bamboo Finance

Appendix B: AfriCap I Key Features, 2001–2006

	AC-I (a)	AC-I (b)
Year	2001 - 2005	2006
Fund Size	$13 mil	$13 mil
Structure/life	Standard LP - PG strcuture/ limited life	Standard LP - PG strcuture/ limited life
Manager - Promoter/Shareholders Manager office location	Calmeadow (40%) Employees (6%) Senegal	Calmeadow (40%) Employees (6%) South Africa
Investors	Calmeadow: 24% IFC:15% Africap-Sweeden: 15% EIB: 13.5% FMO:11% BIO:7.5% 7 others incl UNCDF, Cordaid, Accion, Calvert, Triodos: 13.6%	
Board - Chair	Maria Otero (2002-2003) Martin Connell (2003-2005)	Anne-Marie Chidzero
Board - Members	Martin Connell (Calmeadow) Alex Silva Lars - Olof Hellgren (Sweden) Hany Assaad (IFC) Emile Groot (FMO) Cyrille Arnould (EIB)	Alex Silva Lars-Olof Hellgren (Sweden) Hany Assaad Emile Groot (FMO) Edvardas Bumsteinas (EIB)
Investment Committee	Alex Silva Hany Assaaad Carole Maman	Alex Silva Hany Assaad Carole Maman
Capacity Building Chair Budget Key investments	TSF $3.15 mil Equity Bank Pride Tanzania (C/L) First All S&L, Ghana (EQ) Socremo (EQ) Pride Uganda (C/L)	TSF CAP, Senegal (EQ) QFI, Egypt WWBG, Ghana (EQ) Access Fin, Madagascar (EQ) Union Trust Bank, Sierra Leone Opp. Int'l Bank, Malawi (EQ)
Key exits		Equity Bank (50%) First All S&L (100%)

Appendix C: Africap II Key Features, 2007–14

	AC-I (a)	AC-I (b)	AC-II (c)
Year	2007	2008-2010	2011-2014
Fund Size	$49 mil	$49 mil	$49 mil
Structure/life	Company w. strong Board Permanent structure		Company w. strong Permanent structure
Manager office location	South Africa	South Africa	South Africa
Investors	Calmeadow: 6% IFC: 4% EIB: 17% FMO: 11% Swedfund: 7% Finnfund: 7% Nordic Microcrap: 10% BlueOrchard: 12% Gray Ghost / GMEF: 5% Norfund: 7% Others: 14%		
Board - Chair	Anne-Marie Chidzero (Exec Chair)	Anne-Marie Chidzero	Deepak Malik
Board - Members	Alex Silva Lars - Olof Hellgren (Sweden) Emile Groot (FMO) Emile Groot (FMO) JP Schrevel/X Pierluca Deepak Malik (Norfund)	Alex Silva Lars-Olof Hellgren (Sweden) Emile Groot (FMO) Edvardas Bumsteinas (EIB) JP Schrevel/X Pierluca Deepak Malik (Norfund) Andrej Machacek Richard Arlove Jacco Minnaar* Nothando Ndebele Yaasiin Kannoo - Abax* Rajesh Shibdeen - Abax*	Alex Silva Lars-Olof Hellgren (Nordic) Emile Groot (FMO) Edvardas Bumsteinas (EIB) JP Schrevel/X Pierluca Deepak Malik (Norfund) Oscar Carlsson (Swedfund) Richard Arlove(?) Clarel Benoit(?)
Board - Committetees *Observer to the meeting **on the Advisory Team	Investment Comm	Operations Comm. Alex Silva (Chair)	Operations Comm. Alex Silva (Chair) Xavier Pierluca Andrej Machacek Emile Groot Anne-Marie Chidzero** Nothando Ndebele** Lilian Oyando**
	Gobernance Committee Anne-Marie Chidzero (Exec Chair)	Governance Committee Lauren Burnhill	Governance Committee Edvardas Bumsteinas (EIB) Lars - Olof Hellgren Deepak Malik
Capacity Building Chair Budget Key investments	TSF/Fintech Ira Lieberman $8.5 mil Wizzit, S. Africa (EQ)	Fintech Ira Lieberman La Regionale Sofipe BACB WWBG Asusu Access Madagas Birima Finance Salone Tujijenge	
Key exits		Equity Bank (50%)	

Appendix D: Lessons from ProFund

Because the ProFund experience was cited repeatedly as providing the inspiration and model for AfriCap, it is instructive to quote some of the findings of the 2002 DiLeo–Cuadra assessment of ProFund that are most relevant to AfriCap at some length (emphasis added):

▪ As a general matter, ProFund has selected the larger, more mature Latin American institutions for its investments (p. 5).

▪ ProFund's very success in operating so effectively at such low cost has established a standard for investment operations that other MFI funds, operating perhaps in more challenging environments, should be held to but will be hard pressed to replicate(p. 8).

▪ A fund's objectives must be narrowly defined and assiduously adhered to, especially in the case of a pioneering initiative where translating a concept to implementation will inevitably be more complicated than anticipated (p. 12).

▪ A fund's ability to lead investments is likely to diminish if it is identified with the interests of any sponsor or investor with other agendas in the target sector. This independence was largely a function of the substantive capabilities, communications skills, and integrity of ProFund's management and of the broad vision of the key sponsors and investors. . . . However, the importance of specific structural elements should also be noted, in particular, the division of labor between the Investment Committee, which operated with complete authority over individual transactions, and the Board, which restricted itself to broad strategic and performance guidelines and oversight (p. 12).

▪ Substantial and ongoing TA is essential in nearly all investments, and it is critical that adequate funding and an array of providers be available, but the financing and provision of TA should be entirely independent of the investment fund. . . . ProFund has benefited from the clarity of agenda and identity provided by the lack of any significant TA function, either funding or delivery (p. 12).

▪ There is little to be gained and significant downside risk to the fund and the industry in undertaking a fund without capable and independent management (p. 12).

▪ The qualities of the fund manager are the single most important ingredient for success (p. 12). Among the critical attributes that ProFund's manager brought to the table were:

▪ Strong and demonstrable commitment to and linkages with the region;

▪ The credibility and stature with respect to finance and business (not necessarily microfinance) to assert own judgments;

▪ Communications and diplomatic skills necessary to manage a diverse board and implement an independent course of action; and

▪ Ability to maintain a sharp focus and respond well to a concrete performance based structure.

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