



# Microfinance Briefing Paper: Institutional Development of Lao MFIs during 2008-2010

## Introduction

This paper presents an overview of the institutional development performance of Lao MFIs during the period 2008 to 2010. Baseline assessments were conducted during September 2008 and April 2009 with 18 MFIs/SCUs that partnered with the BoL-ADB Catalyzing Microfinance for the Poor Project, and follow-up assessments were conducted with the same MFIs in November 2010<sup>1</sup>. The assessments utilized a comprehensive assessment tool<sup>2</sup> covering approximately 60 areas of institutional capacity across 7 categories as outlined in Table 1.

The results presented in the following sections average out the scores for all MFIs within each of the 3 institutional type groupings: Deposit-Taking MFIs (DTMFI), Non Deposit-Taking MFIs (NDTMFI), and Savings and Credit Unions (SCU). Naturally some MFIs scored well above the average in their grouping and others below. The groupings do however serve to illustrate differences in performance across the 3 institutional types.

### 1. Governance

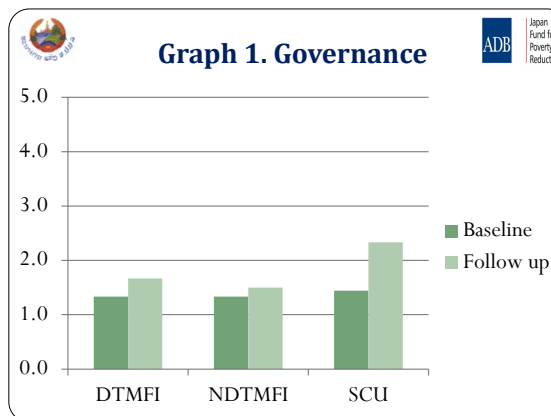
Assessment of governance systems focused on the composition and quality of the board and the extent to which it functions in providing effective oversight of the MFI. All MFIs started from a very low base, with either no boards in place or very ineffective ones that were not aware of, let alone fulfilling, their responsibilities. Following the delivery of governance training (most board members who attended said this was the first time they had received any training) and follow-up support, boards began to function better across all institutional types, as shown in Graph 1. Interestingly, member-owned SCUs demonstrated the best overall quality of governance of the 3 institutional types. Despite the improvements, overall governance quality is still considered weak.

**Table 1: Institutional Assessments**

1. Governance
2. Strategic Management
3. Clients, Products & Marketing
4. Social Performance & External Relations
5. Human Resources
6. Portfolio Management
7. Financial Management

Scoring system:

| 1    | 2    | 3            | 4    | 5      |
|------|------|--------------|------|--------|
| WEAK | FAIR | SATISFACTORY | GOOD | STRONG |



| Key areas of progress   | Main challenges remaining  |
|---|--|
| <input checked="" type="checkbox"/> Most Boards meet monthly, have agenda, keep | <input type="checkbox"/> Many Boards do not meet separately from staff and |

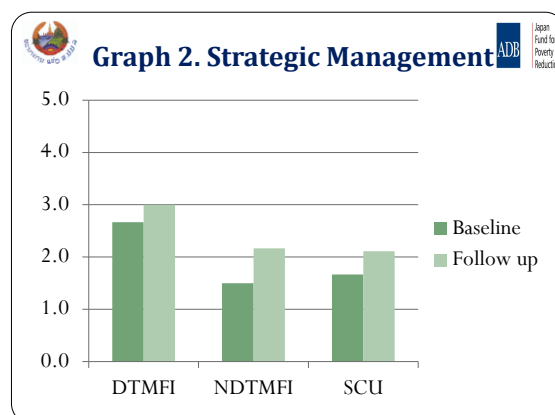
<sup>1</sup> These 18 MFIs represented almost all of the MFIs registered with the Central Bank at the time

<sup>2</sup> The Microfinance Institutional Assessment Tool was developed and provided by World Education Australia / Good Return

|   |   |
|---|---|
| signed minutes  | sub-committees  |
| ✓ Most MFIs have a clear organisational chart / structure   | <input type="checkbox"/> Most boards still lack financial skills  |
| ✓ Most Boards have 1 or 2 members with some training        | <input type="checkbox"/> Boards need better understanding of their responsibilities and how to fulfill them |
| ✓ Most Boards are generally aware of their responsibilities | <input type="checkbox"/> MFIs lack clear objectives and Key Performance Indicators                          |
| ✓ Most MFIs have functioning credit & audit sub-committees  |   |

## 2. Strategic Management

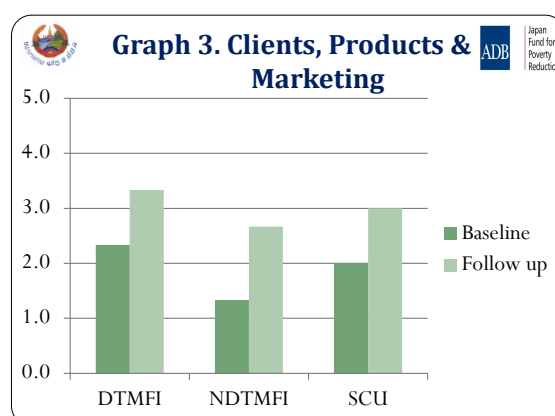
The area of Strategic Management includes the effectiveness of senior management in setting and implementing a clear strategy for the institution, being aware of internal strengths and weaknesses as well as external competition and threats, and responding appropriately. The project delivered Business Planning training to assist MFIs to identify clear objectives, set targets, put plans in place to achieve these, and monitor progress. On-site individual support was also provided to managers to help them implement these plans. Graph 2 shows small increases in management capacity across all 3 institutional types. Deposit-Taking MFIs tend to be larger and more professionally managed than the smaller NDTMFIs and SCUs. Overall performance in strategic management improved from weak to fair.



| Key areas of progress                              | Main challenges remaining  |
|--|--|
| ✓ Most managers have had some training             | <input type="checkbox"/> In general management skills are still weak         |
| ✓ Some MFIs have a business plan in place          | <input type="checkbox"/> Most MFIs lack competent second-level manager(s)    |
| ✓ Most MFIs have a range of policies in place      | <input type="checkbox"/> Many MFIs lack a clear plan for growth              |
| ✓ Some MFIs track progress against targets monthly | <input type="checkbox"/> Some MFIs stuck in a rut, no innovation or progress |
| ✓ Efficiency is generally improving                | <input type="checkbox"/> Efficiency levels still generally low               |

## 3. Clients, Products & Marketing

The area of clients, products and marketing assesses how well MFIs know their clients, design appropriate products to meet stated client needs with transparent pricing, and attract new clients with effective marketing services. The range of products available is generally appropriate to client needs, some level of client assessment takes place, and products are modified based on client needs and preferences. Marketing is typically weak. Graph 3 shows consistent improvements across all institutional types, with DTMFIs scoring highest. Overall performance improved from weak to fair. Outreach of the 18 reporting MFIs increased by 17% during the year to September 2010, from 9,982 to 11,685 active borrowers.

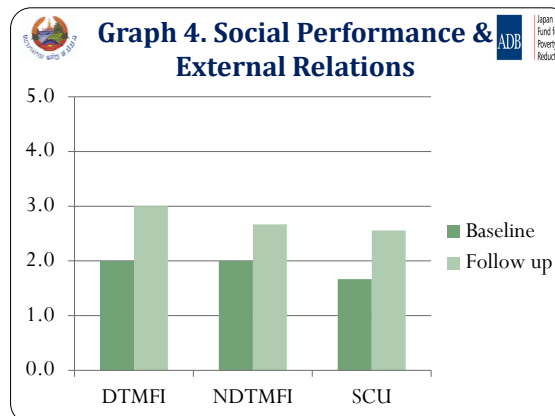


| Key areas of progress | Main challenges remaining |
|-----------------------|---------------------------|
|-----------------------|---------------------------|

|   |  |
|---|--|
| ✓ Good range of savings and credit products available | ☐ Interest rates highly variable across MFIs. High interest rates typically used to cover low efficiency |
| ✓ Some conducting formal marketing activities         | ☐ Little or no assessment of client demand and preferences   |
| ✓ Loans typically approved within one week            | ☐ Most lack a clear, consistent brand or marketing   |

#### 4. Social Performance & External Relations

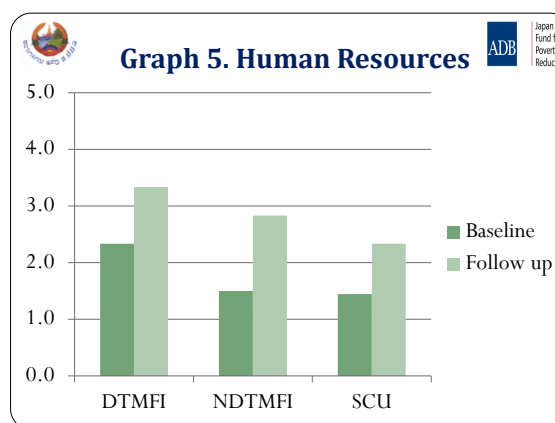
The area of social performance & external relations includes social objectives and measuring progress, poverty targeting and tracking, approaches to gender, client satisfaction, networking and government relations. Improvements seen in this area relate mainly to increased levels of pro-poor lending, improved networking and stronger relations with the central bank. Graph 4 shows modest improvements and fairly consistent levels across all institutional types. Overall performance is fair. Pro-poor loans (loan size <3.2 million kip) comprised 66% of the total loan portfolio of reporting MFIs. The proportions of rural and female clients remained consistent at 34% and 60% respectively.



| Key areas of progress                             | Main challenges remaining                                 |
|---|---|
| ✓ Most are serving more poor clients              | ☐ Lack clear social performance objectives or measurement |
| ✓ Improved relationships with Bank of Lao         | ☐ Lack assessment of poverty levels or impacts            |
| ✓ Increased participation in MF sector activities | ☐ Lack structured assessment of client satisfaction       |
|   | ☐ Few operate in remote villages, most serve towns        |

#### 5. Human Resources

The area of human resources refers to the ability of the organization to recruit, train, support, manage and incentivize staff to achieve their potential. It includes staff policies, procedures and staff efficiency. Baseline assessments revealed that many MFIs did not have clear job descriptions or staff contracts, staff policies or incentive systems. Efficiency was thus low. These issues were addressed in a variety of training sessions and in on-site support visits. Graph 5 shows improvements across the board, with most improving from weak to fair. Participating MFIs/SCUs increased their staff efficiency levels from a baseline of 133 accounts per credit officer to 167 accounts per credit officer in September 2010. However, this is still low by international standards and can be accounted for by a range of factors, including: the industry still being in its infancy and not yet reaching scale or strong efficiency, high incidence of individual lending as opposed to group lending, and low population density. As the sector matures it is expected that more trained and qualified staff will be available to MFIs, and performance and efficiency levels will continue to improve.

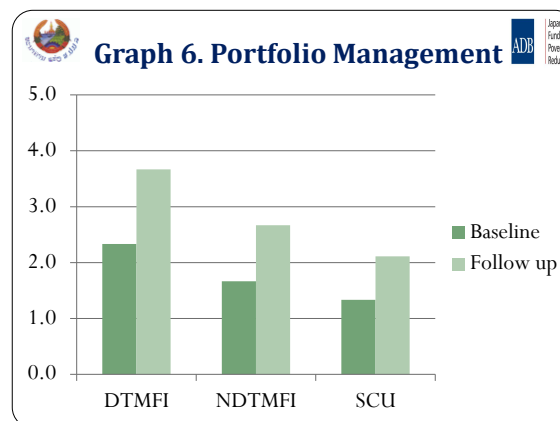


| Key areas of progress | Main challenges remaining |
|-----------------------|---------------------------|
|-----------------------|---------------------------|

|   |  |
|---|--|
| ✓ Many staff trained over past two years            | <input type="checkbox"/> Many staff lack adequate training to perform roles well |
| ✓ Most have contracts and job descriptions in place | <input type="checkbox"/> Incentive schemes still rare, or not well designed      |
| ✓ Most MFIs have personnel policies                 | <input type="checkbox"/> Difficult to retain competent, skilled staff            |
| ✓ Some starting to introduce incentive schemes      | <input type="checkbox"/> Most lack a staff training plan or budget               |
| ✓ Productivity levels improving (but still low)     | <input type="checkbox"/> Lack of performance appraisals                          |

## 6. Portfolio Management

Portfolio management is central to microfinance operations and includes portfolio quality, growth, planning, credit assessment and delinquency management policies and procedures, and MIS systems. At the outset most MFIs were weak in this critical area, most had no awareness of standard portfolio quality measures such as PAR, loan loss provisioning or other standard practices. Considerable training effort has been dedicated to such topics as credit management, delinquency management, policies and procedures, and MIS systems. Significant gains were made by almost all institutions, as reflected in Graph 6. The aggregated loan portfolio of the 18 reporting MFIs nearly doubled from a baseline level of 14.8 billion Kip to 27.5 billion Kip. Much remains to be done to achieve satisfactory levels of portfolio management. Average weighted PAR(30) levels for the sector have been between 7% and 11% during 2009 and 2010. At September 2010 only 28% of 18 reporting MFIs complied with the industry standard of PAR(30)<5%. Main reasons identified for the underperformance are lack of enforcement of delinquency management policies and procedures, irregular monitoring of loans, inappropriate loan appraisal and collection methods, and lack of staff incentives for timely collection.

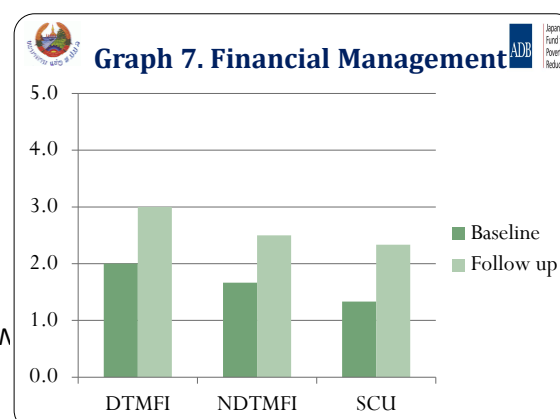


| Key areas of progress  | Main challenges remaining  |
|--|--|
| ✓ Most now familiar with PAR(30) and tracking this monthly             | <input type="checkbox"/> High levels of delinquency remain           |
| ✓ Most now have credit & delinquency management policies               | <input type="checkbox"/> Weak credit assessment                      |
| ✓ Good growth in most portfolios                                       | <input type="checkbox"/> Delinquency management practices still weak |
| ✓ Some improvement in delinquency management                           | <input type="checkbox"/> Some still lack a portfolio plan / targets  |
| ✓ Most have computerized MIS and are able to produce portfolio reports | <input type="checkbox"/> Some cases of high write-offs               |

## 7. Financial Management

Financial management encompasses the ability to produce accurate and timely financial statements and understand these, asset-liability management, liquidity and cash flows, accounting systems and internal controls, overall profitability and dividend arrangements. Almost all MFIs were weak in these areas at the commencement of the project, thus the project delivered accounting training as well as internal controls and MIS training. All 3

*Institutional Development of Lao MFIs during 2008-2010, Shane N*



MFI types showed improvements, moving from weak to fair. Average operational self-sufficiency has consistently been above 100% since baseline. The proportion of profitable MFIs increased from 33% at baseline to 56% in September 2010 (a further 17% were close to becoming profitable with OSS levels between 95% and 100%). Among the least profitable organizations are the Village Bank Associations (NDTMFIs) which are still heavily dependent on donor funding support - they operate in areas with high transaction costs (low population density and very remote clients) and very poor populations.

| Key areas of progress  | Main challenges remaining   |
|--|---|
| ✓ Most able to produce monthly financial reports                                     | <input type="checkbox"/> Cash flow and liquidity management typically weak                    |
| ✓ Most MFIs are profitable   | <input type="checkbox"/> Most 'accountants' lack basic accounting knowledge or qualifications |
| ✓ Computerised accounting / MIS systems (MBWin) widely used, most have trained staff | <input type="checkbox"/> Little or no Asset-Liability Management                              |
| ✓ Some MFIs have now conducted external audits                                       | <input type="checkbox"/> General financial management and accounting skills weak              |
|  | <input type="checkbox"/> Internal audit function weak, few external audits                    |

### What else is needed?

Overall, institutional capacity improved over the two-year period from 2008 to 2010, with ratings in most categories improving from 1-2 (Weak to Fair) to 2-3 (Fair to Satisfactory) on the 5-point scale. Deposit-Taking MFIs tend to be larger and have better overall capacity than other institutional types, but have lower rural and pro-poor penetration. Clearly, there is significant room for improvement and a strong need for ongoing training and support in order to achieve international standards in service provision. Key sector needs to facilitate further institutional development include:

1. Quality staff training that leads to qualifications - in particular in the areas of MFI Management, Credit Management, and MFI Accounting; and ongoing Board development and training support
2. Other meso-level infrastructure - Improved MIS support, specialised MFI audit services, benchmarking systems for comparing MFI performance, and greater information sharing and collaboration within the sector
3. Access to funding - Domestic & international debt and equity funding for successful MFIs
4. Attention to Social Performance - a simple poverty assessment tool, Introduction of Social Performance Management approaches, and client education programs such as financial literacy training

If the trend of strong growth evidenced in the sector in recent years continues then organizational capacity can be expected to increase accordingly in the years ahead.

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