Micro-Finance Rating - Risk Assessment

# Crystal Fund (Crystal)

Kutaisi, Georgia

| <Risk Assessment> Rating grade | β beta | **Assessment:** Acceptable, needs improvement to handle large volumes Moderate safety, moderate systems |
|---|---|---|

**Visit dates**: 11-15 April, 2007 **Operational head**: Mr Malkhaz Dzadzua

**Maximum validity of rating***: till April 2008

**Rating**

Crystal shows moderate performance on governance and management aspects and reasonable performance on financial aspects. It has a professional leadership that plays an active role and has enabled the organisation to mobilise significant amount of borrowings from different lenders. On account of relatively high yield on its loan products, Crystal shows good performance on profitability and sustainability. As such, the overall outlook for Crystal is positive. However the weak second line of leadership, together with control systems that are only just developing, is a cause for concern. During 2006, Crystal had faced a major case of fraud that had unsettled its operations in one branch and Crystal had to write off a significant amount of loans. The organisation has recovered from the fraud and the quality of its loan portfolio is now reasonable. Crystal is now taking steps to strengthen its second line of management and internal control systems.

**In M-CRIL's view**, Crystal can absorb – from all sources – loan funds of GEL2.0 million (US$1.2 million) over the next one year for on-lending to its borrowers. However, given the organisation's plans to transform into a joint stock company by the end of the year, lenders are advised to conduct a due diligence prior to lending to the new entity.

A rating update after one year is suggested to ascertain changes in the creditworthiness and absorptive potential of the institution. **This rating is valid, subject to no other substantial inflows of loan funds into the organisation beyond the limits specified here** and to no other significant changes in the organisational structure and external operating environment.

**for Micro-Credit Ratings International Ltd**

**Sanjay Sinha, Managing Director**

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***Validity** This rating is valid till the next loan proposal made by the MFI to any financial institution or till any other significant change in the structure of the loan programme or in its external environment. A **rating update** (comprehensive repeat rating) is recommended whenever such changes take place or at the end of **one year** from the date of the initial assessment, whichever is earlier. Any substantial additional information that becomes available could also result in a rating update or a rating review (revision of rating grade based on a desk analysis).

**Liability** The rating assigned is a professional opinion of the assessors and M-CRIL does not guarantee the information and cannot accept any legal responsibility for actions arising out of the recommendations made.

## Category wise rating

| Category | Rating grade[1] |
|---|---|
| A *Governance aspects* | β |
| B *Managerial factors* | β |
| C *Financial performance* | β+ |
| **Overall** | β |

## Key Risk Factors

1 **Weak second line of leadership:** The second line of leadership in Crystal is presently weak and most of regular operational responsibilities are handled by the Executive Director (with the support of Branch Managers). The organisation does not have a dedicated head of credit operations to regularly monitor branch operations and follow-up on cases of overdues. On account of this weakness, coupled with the fact that Crystal did not have a strong Internal Audit function, a major case of fraud (through "ghost loans") in one of the branches of Crystal could not be discovered and checked in time, leading to significant losses.

Only recently (about five months before the rating visit) has Crystal recruited a qualified professional as Credit Risk Manager, who has been assigned the main responsibility of verifying loan applications. Although Crystal also has an Internal Auditor now, the organisation is yet to develop a comprehensive system of Internal Audit; the present system being simplistic and rudimentary.

## Key Programme Strengths

| Governance, experience and strategy | Management and operations | Financial |
|---|---|---|
| 1 Clear focus on microfinance<br>2 Good performance on fund mobilisation | 1 Qualified and experienced staff<br>2 Good MIS | 1 High capital adequacy<br>2 High Yield-to-APR ratio |

[1] M-CRIL's grading sheet is attached at the end of the report.

## Organisational Profile

| Legal form | Years of m-f Operation* | *Active clients* | *Staff* | *Loan Officers* | *Branches* | *Active loans/ Staff member* |
|---|---|---|---|---|---|---|
| Foundation (not-for-profit) | 9 years | 5,031 | 35 | 17 | 3 | 143 |

**Note:** Although Crystal was registered only in 2004, the microfinance programme of CHCA had begun in 1998

## Microfinance programme: Operational highlights

| Total net worth of MFI (GEL, US$) | Outstanding borrowings of MFI (GEL, US$) | Loan portfolio of MFI (GEL, US$) | Cumulative loans disbursed by MFI++ (GEL, US$) | Average loan size from MFI to borrowers (GEL, US$) |
|---|---|---|---|---|
| 1.2 million | 2.9 million | 3.0 million | 15.6 million | ~800 |
| 0.7 million | 1.7 million | 1.8 million | 9.2 million | ~470 |

**Note:** 1 USD = 1.7 GEL (Georgian Lari)
++ The cumulative amount of loan disbursed includes loans disbursed by the credit programme of CHCA

## Key financial ratios

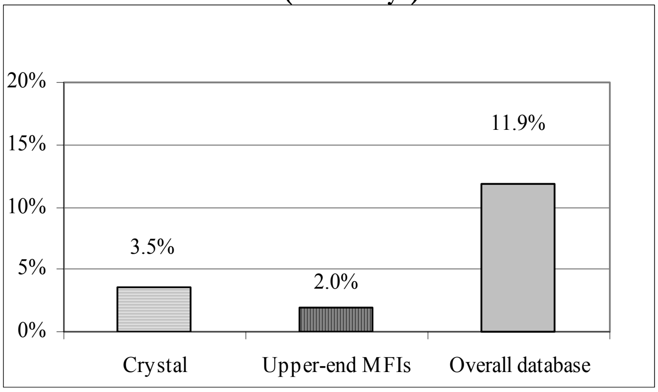
| Portfolio at risk (>=60 days) | Current repayment rate | Risk weighted capital adequacy ratio | Weighted average cost of funds | Loan portfolio to total assets |
|---|---|---|---|---|
| 3.5% | 98.0% | 36.2% | 9.9% | 69.1% |
| **Yield on portfolio** | **Other income to average portfolio** | **Financial cost ratio** | **Loan loss provisioning ratio** | **Operating expense ratio** |
| 43.2% | 12.5% | 14.0% | 0.6% | 23.7% |
| **Total income to average total assets** | **Total expenses to average total assets** | **Return on average total assets** | **Operational self sufficiency** | **Financial self sufficiency** |
| 43.8% | 42.8% | 1.0% | 103.5% | 97.3% |

**Notes**

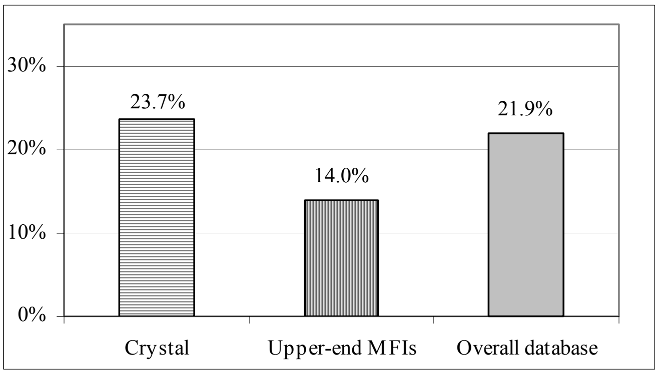
1. All figures are for the organisation's operations as on 31 December 2006
2. Other income includes income that the organisation receives from commission and penalties and bad debts recovered.
3. Adequate loan loss provisioning has been made for the current year on the basis of the quality of loan portfolio, as per the policies of the organisation. Loan loss provisioning at 0.6% of the average portfolio for the year is in addition to bad debts written off at 15.5% of the average portfolio. The unusually high loan write-off ratio is on account of significant losses incurred by the organisation due to a major case of fraud in one of the branches. The loan loss reserve is 4.1% of the gross loan portfolio outstanding at the end of the year.
4. For the calculation of FSS, market rate of interest has been taken at six-month LIBOR+6%. The six-month LIBOR as on 31 December 2006 was 5.365%.
5. The ratio of repayment rate and $PAR_{60}$ has been calculated from the MIS reports generated by Crystal. Accuracy of data generated by the MIS has been verified by the rating team through an audit of the systems at Crystal.

# Crystal – financial overview

**Portfolio at risk (>=60 days)**: 31 Dec 2006

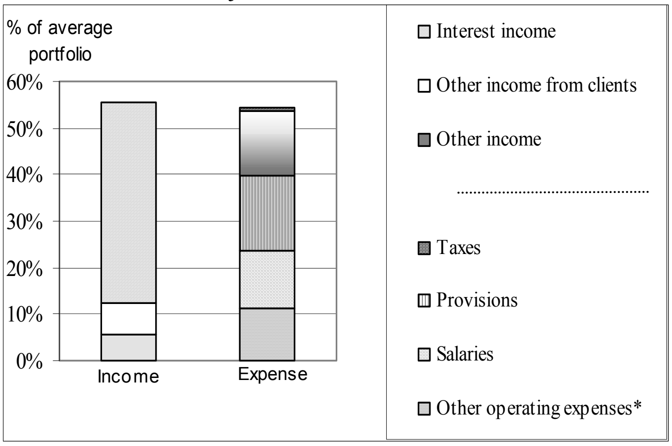



**Operating expense ratio**: 1 Jan 2006-31 Dec 2006



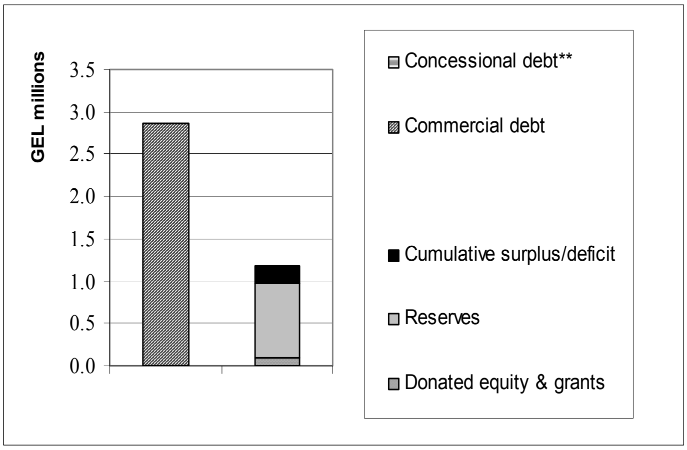

**Note**: 1. $n_{upper\text{-}end} = 10$ $n_{database} = 120$; Database figures as on 31 December 2005
2. Outliers and rated MFIs with no direct lending have been removed for analysis. Upper-end figures reflect top 10 MFIs.
3. The upper-end MFIs and overall database ratios represent simple averages for their respective samples.
4. The performance of either the Upper-end MFIs or all MFIs (overall database), do not necessarily reflect M-CRIL's rating standards.

**Income and expense distribution**:
1 Jan 2006-31 Dec 2006



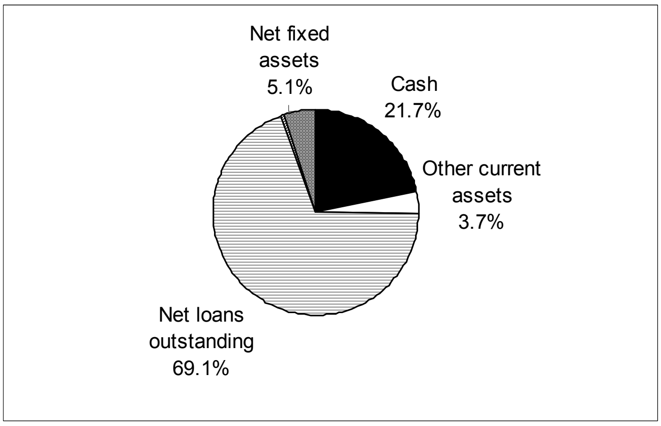

* Other operating expenses include travel, depreciation and administrative expenses

**Debt and equity composition**:
31 Dec 2006

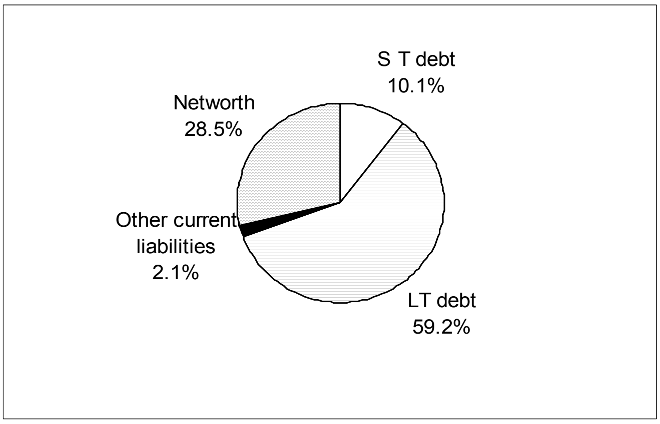



** Concessional debt is borrowing+comp.savings taken at < Bank PLR, voluntary savings taken at < bank deposit rates

**Asset composition**: 31 Dec 2006




**Liability & net worth composition**: 31 Dec 2006



**Country Profile: Georgia**

Georgia is located in southwest Asia, bordering the Black Sea, between Turkey and Russia. The region of present-day Georgia contained the ancient kingdoms of Colchis and Kartli-Iberia. The area came under Roman influence in the first century AD and Christianity became the state religion in the 4th century. Georgia has had a history of conflicts and occupations by the Persians, Arabs, Turks and Russians. It was independent for three years (1918-1921) following the Russian Revolution, but was forcibly incorporated into the USSR later. Georgia remained a part of USSR until the Soviet Union dissolved in 1991. Despite myriad problems, some progress on market reforms and democratisation has been made since then. An attempt by the government to manipulate legislative elections in November 2003 touched off widespread protests that led to the resignation of Eduard Shevardnadze, President since 1995. New elections in early 2004 swept Mikheil Saakashvili into power.

Some regions of Georgia continue to be tense. The region of Abkhazia in the West has been declared a conflict zone and is presently under a UN mission. Christians who earlier lived in this region have been forced to seek refuge in other parts of Georgia as internally displaced persons (IDPs). The regions around Abkhazia (including Zugdidi) have seen incidents of crime and social unrest in the past, but the situation is more or less stable at present.

Georgia's main economic activities include agriculture (products such as citrus fruits, tea, hazelnuts, and grapes); mining of manganese and copper; and output of a small industrial sector producing alcoholic and non-alcoholic beverages, metals, machinery, and chemicals. The country imports the bulk of its energy needs, including natural gas and oil products. Despite the severe damage the economy has suffered due to civil strife, Georgia, with the help of the IMF and World Bank, has made substantial economic gains since 1995, achieving positive GDP growth and curtailing inflation. Growth since 2002 has been positive, with GDP growth of 5.3% in 2002, and 8.3% in 2003, 9.5% in 2004 and 9.3% in 2005. Georgia had suffered from a chronic failure to collect tax revenues, but the new government is making progress in reforming the tax code, enforcing taxes, and cracking down on corruption. In addition, the privatisation process has taken off, permitting the government to boost expenditures on infrastructure, defence and poverty reduction. The country is pinning its hopes for long-term growth on its role as a transit state for pipelines and trade. The construction on two major regional gas pipelines has brought much-needed investment and job opportunities. Nevertheless, restructuring the sector and finding energy supply alternatives to Russia remains a major challenge.

The 2.1 million labour force out of 5.1million total population of Georgia is divided as 40% in agriculture, 20% in industry and 40% in services, while the contribution to GDP is 16.0% from agriculture, 26.8% from industry and 57.2% from services. The inflation rate during 2006 was 8.8% and during that during 2005 was 6.2%.

In the financial sector, banks are the major players, offering a wide range of deposit as well as credit products for all sections of the population. There are about 23 banks registered with the National Bank of Georgia. Most banks have also started entering the microfinance market, with the prominent ones in this market presently being Pro Credit Bank and Bank of Georgia. People's Bank, which has widespread presence across Georgia, could also be an important player in the future.

Apart from banks, credit unions and NGO-MFIs (including microcredit programmes run by international donor agencies) are the significant players in the microfinance market. Some of the prominent ones in this sector include Constanta, FINCA, SBDF, Crystal and Credo (World Vision).

As for the microfinance sector, in 2005, the Georgian Parliament recognised microfinance (as loans below GEL10,000) and allowed microfinance providers to be registered as Microfinance Organisations (MFOs). An association of MFOs called AGMO was formed and new legislation facilitated by AGMO has made it mandatory for microfinance providers to transform into for-profit Companies by December 2007, which will be under the direct supervision of the National Bank of Georgia. The larger MFOs – Constanta, SBDF, Credo and Crystal - are presently engaged in this process of transformation. However, the future of smaller NGO-MFIs in Georgia appears to be uncertain, with the new legislation.

Source: The CIA World Factbook: https://www.cia.gov/cia/publications/factbook/geos/gg.html
Microfinance Gateway:http://microfinancegateway.com/resource_centers/reg_sup/country_info/georgia
The Ministry of Foreign Affairs of Georgia: http://www.mfa.gov.ge/index.php?lang_id=ENG&sec_id=54

# 1 Organisational background

Crystal Fund was established as a not-for-profit Foundation in 2004. Crystal has its origins in the micro-credit programme of a Georgian NGO called Charity Humanitarian Center Abkhazeti (CHCA). CHCA was established by a group of internally displaced persons (IDPs) from the region of Abkhazia in Georgia, with the main objective of improving the social and economic conditions of Georgians from Abkhazia who have been forced to move out of the region due to civil strife (see Country Profile). CHCA started its micro-credit programme in 1998. Both CHCA and Crystal now have their target population as low-income families and small and medium entrepreneurs in different parts of Georgia, apart from IDPs from Abkhazia.

The microfinance programme of CHCA was initially started with grants provided as revolving loan fund by the UN High Commission for Refugees, USAID and the Dutch Refugee Council. This revolving loan fund of about US$353,000 became the initial (donated) equity of Crystal.

Crystal has its Head Office in Kutaisi, which is the north-western part of the country, and is the second-largest city of Georgia after the capital city of Tbilisi. The organisation operates from three branches each in Kutaisi, Zugdidi and Poti. Zugdidi is located near the politically troubled region of Abkhazia.

Crystal has a three-member Board. Mr Archil Bakuradze is the Founder and Chairman of Crystal and is also one of the Directors of CHCA. He is presently the Special Advisor to the Secretary General of the International Association of Business and Parliament based in the United Kingdom. The second member is the Credit Manager of the Kutaisi branch of TBC Bank (one of the leading banks in Georgia), who was also earlier the Coordinator of the credit programme of CHCA (for one year) and Coordinator of the Income Generating Programme of the Danish Refugee Council in Georgia for about three years. The third member is an engineer-economist who has over two decades of experience in various industrial units in Georgia and is presently involved in social work.

The senior management of Crystal is organised into a Management Committee consisting of the Executive Director who was Coordinator of the CHCA's credit programme for five years and has been leading the operations of Crystal since it was established; the Finance Manager of Crystal, who is a qualified Accountant and was looking after the finance function of CHCA for about eight years; and the Credit Managers of the Kutaisi and Zugdidi branches of Crystal.

# 2 Microfinance operations

## 2.1 Background of microfinance operations

At the time of the rating visit in April 2007, Crystal had operations around its three branch offices in Kutaisi (with two service centres, one in Kutaisi and the other in Samtredia), Zugdidi (with a service centre in Chkhorotsku) and Poti (with two service centres, one in Ozurgeti and the other in Senaki). The organisation had 5,024 active clients and an outstanding loan portfolio of GEL2.9 million (US$1.7 million) as on 31 March 2007. Crystal had a total staff strength of 41 (including 18 Loan Officers) as on the above date.

The organisation is led by the Executive Director, who is assisted by the Finance Manager. Crystal also has a Lawyer, who assists the organisation in recovery of overdue loans. There is also an IT Manager who is responsible for maintenance of the hardware and software used by Crystal. Apart from these senior staff, one qualified lawyer, having experience in various government organisations for about three years, has been appointed as Internal Auditor in March 2006. Crystal has also recently (about three months prior to the rating visit) appointed a Credit Risk Manager, who is a qualified professional having worked with several government departments for over a decade. The Credit Risk Manager would be primarily responsible for loan appraisal at the Head Office.

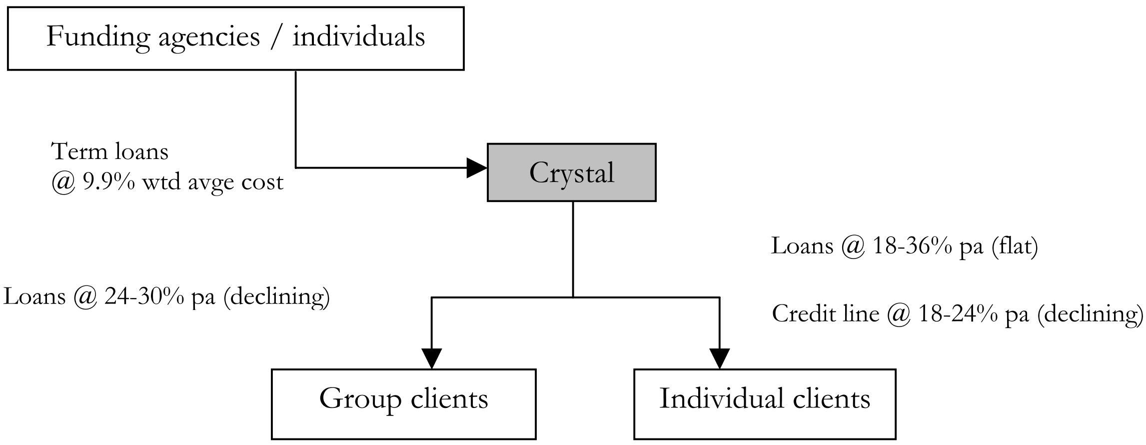
At the branches, the operations are managed by a Credit Manager, with the support of an Accountant and four-five Loan Officers. Branches also have a Lawyer-cum-Administrator, drivers and an administrative assistant.

Crystal has been successful in mobilising loan funds from several lenders. The following table presents details of the loans facilities availed by the organisation.

Amounts in USD, unless mentioned otherwise

| Name of institution | Date of receipt (first tranche) & amount received | | Amount outstanding (USD) (as on 31 Dec 06) | Interest rate (%) |
|---|---|---|---|---|
| Cordaid | Jul 2004 | 420,000 | 338,626 | 6% |
| Deutsche Bank | Jun 2006 | 700,000 | 705,559 | LIBOR+5% |
| Oikocredit | Jun 2006 | 300,000 | 302,382 | 12% |
| Oxfam/Novib (Euros) | Jul 2006 | 200,000 | 265,435 | 10% |
| CHCA | May 2004 | 60,000 | 60,676 | 12% |
| Keith Young | Dec 2005 | 10,000 | 10,079 | 0% |
| | | **Total** | **1,682,757** | |

Crystal has also borrowed from TBC Bank and Blue Orchard Finance in the past. The amounts borrowed are GEL 280,000 (US$ 155,555) and USD 50,000 respectively.




## 2.2 Microfinance policies

Crystal has a wide range of credit products offered for business purposes as well as for purchase of consumer goods. In addition, the organisation also provides credit to agricultural farmers. Potential clients are identified by the Loan Officers and then interviewed in detail by Loan Officers and also Credit Managers, if the proposed loan size is large. Information about the client's business, house type and condition, assets owned and family details is collected during the interview, and the client is also informed about the policies of the organisation and the different products offered.

Loan appraisal is the purview of the Loan Officer and Credit Manager in the branches and the Credit Committee in the Head Office. Loan applications together with the recommendation of the Loan Officer and business cashflows (in case of business loans) are sent to the Credit Manager through e-mail. The Credit Manager may ask for clarifications/queries, which are noted in the loan application sheet itself. Loan applications approved at branch level are sent to the HO Credit Committee through e-mail, together with the queries of the Credit Manager and the responses of the Loan Officer. The information is then checked by the HO Credit Committee, consisting of the Executive Director, the Internal Auditor and the Lawyer, who independently look at the application, the queries raised and the responses, and then take a decision on the loan. The Credit Committee may also ask for clarifications or more information before making a decision.

Loan Officers visit all clients prior to approval of the loan and visits for checking the utilisation of loan are made for a randomly selected sample of clients.

For consumer loans, Crystal has tied up with various shopkeepers and store managers, who direct customers needing loan for the purchase of any product to Crystal. Typical products that are financed are home appliances and goods such as televisions, washing machines, refrigerators, furniture etc as well as less expensive items such as mobile phones. The loan amount is transferred directly to the shopkeeper/store as soon as the client agrees to purchase the item and applies to Crystal for loan.

Loan disbursements are made through the client's bank account or through the shopkeeper (in case of consumer loans) within 3-5 days of receipt of the application.

**<u>Loan products</u>**

Crystal has five different loan products, which are explained briefly in the table below:

| Product category | Loan term | Loan size range | Interest rate |
|---|---|---|---|
| Individual (business) loans | 10-12 months | USD 300-5,000 | 18-36% pa (flat) |
| Group loans | 6-8 months | USD 100-300 | 24-30% pa (declining) |
| Consumer loans | 8-10 months | USD 100-1,000 | 18-30% pa (flat) |
| Credit lines | 21-24 months | USD 5,000-10,000 | 18-24% pa (declining) |
| Agri-business loans | 15-18 months | USD 300-5,000 | 18-36% pa (flat) |

In addition to interest, 1% of the loan amount is charged upfront as processing charges. From the amount collected as processing charges, Crystal pays a part to its bankers (through which the transactions with clients are routed) as commission. Prepayment penalty is collected at the rate of 25% of the interest lost due to prepayment (even in the case of flat rate of interest). In case of any default, a penalty is also collected.

Except the Group loans and consumer loans, all loans require physical collateral, which can be either Gold for 10-25% of the loan amount and/or other movable or immovable property. The document pledging the collateral to Crystal is officially notarised only in some cases, when the collateral is immovable property.

All loans are repayable on a monthly basis, except the credit line loans. A grace period of upto three months is allowed for Agri-business loans and loans for production/manufacturing.

In addition to the loan products described above, Crystal has also given one loan of 25,000 Pounds (UK) (US$59,372 as on 31 March 2007) in March 2007 to the International Association of Business and Parliament (IABP), head-quartered at London, UK. Mr Archil Bakuradze, who is Chairman of Crystal, is employed at a senior level with IABP. The loan to IABP is not collateralised and the loan agreement has not been notarised. However, IABP is a well-reputed international organisation and Crystal has reasonable assurance of repayment of the loan. The loan is also personally guaranteed by Mr Archil Bakuradze. The loan has been given as a bullet-repayment loan repayable in six months, with an option to repay parts of the principal earlier. The interest rate is 12% pa (on reducing balances), which is the market rate for loans to such institutions.

**Equity investments**

Apart from loans, as an experiment, Crystal has invested in two mid-sized enterprises – one tea estate and another agricultural trading company to an extent of 25% of the total equity of these enterprises. The value of these investments stood at GEL39,690 (US$23,347) as on 31 March 2007. The two organisations do not get their financial statements audited and the investments by Crystal were based on the financial statements prepared by the two organisations to present to tax authorities.

At the end of 2006, Crystal had invested in only one of these entities and the value of the investments was GEL18,290 (US$10,759) as on 31 December 2006. This investment was made using a loan at 0% interest received specifically for such investments from a private investor known to the Board of Crystal.

The investments were made after February 2006 and Crystal expects annual returns (matching the annual yield of Crystal) from these enterprises as per a pre-decided business plan. These returns are expected after a 'gestation period' of three years.

# 3 Observations

## 3.1 Governance & strategy

Crystal shows moderate performance on governance and strategy with a grade of $\beta$. Crystal has a professional governing body, which is actively involved in the strategic management of the organisation. A major strength of Crystal is that it has been able to mobilise a significant amount of loan funds from different lenders. The organisation also has well-defined plans for future growth and transformation. However, the weak second line of leadership is a cause for concern.

- Governance

  Crystal has professional members on the Board, who have knowledge and experience of banking/microfinance. Crystal has been successful in mobilising a significant amount of loan funds from diverse sources. Crystal's linkages with its lenders is a significant strength that many other MFIs of similar scale in Georgia have not been able to match.

  Crystal's promoters and top management are committed to full transparency of operations. Crystal was the first MFI in Georgia to get itself rated by an independent international rating agency (Microfinanza, Italy). Crystal has also received a score of 'five diamonds' from the Microfinance Information Exchange (MIX), for uploading its financial and other data on the MIX website.

- Strategy for microfinance operations

  Crystal has a clear focus on microfinance and offers a wide range of credit products, in order to cater to different needs of its market. With its consumer loans for low and middle-income households, Crystal operates in a niche market. Although the interest rates charged by Crystal are higher than those of banks and other MFIs operating in the region, Crystal offers the advantages of easier procedures, quicker appraisal and availability of loan in just 3-5 days after application as compared to the one week to ten days time taken by banks.

  Most of Crystal's clients come from urban and semi-urban areas and its loans in these areas constituted 86% of the organisation's loan portfolio, while loans in rural areas constituted the remaining 14%.

  Crystal has been steadily reducing its portfolio under Group loans. While these loans constituted about 77% of the organisation's portfolio as on 31 December 2002, they contribute to only 0.7% of the total portfolio as on 31 December 2006.

  Crystal has been focusing on the consumer loans to low and middle-income families, which is a niche segment product that it offers. A significant 77% of the active clients of Crystal have availed of these loans as on 31 December 2006. Consumer loans constituted 48% of the portfolio of the organisation as on the above date.

  At the same time, Crystal has not diluted its focus on supporting small and medium enterprises. The individual business loans offered by Crystal constituted 50.4% of the loan portfolio of the organisation at the end of 2006 and 22% of the active clients of Crystal had availed of these loans.

  With regard to the equity investments as a product, there is no definitive plan to extend these services and the two equity investments that have been made are experimental, with a view to assess if it is a financially sustainable product that can be offered in the future. Crystal does not expect any return from these investments for the next three years, after which Crystal expects to receive annual dividends matching Crystal's annual yield from its micro-credit products.

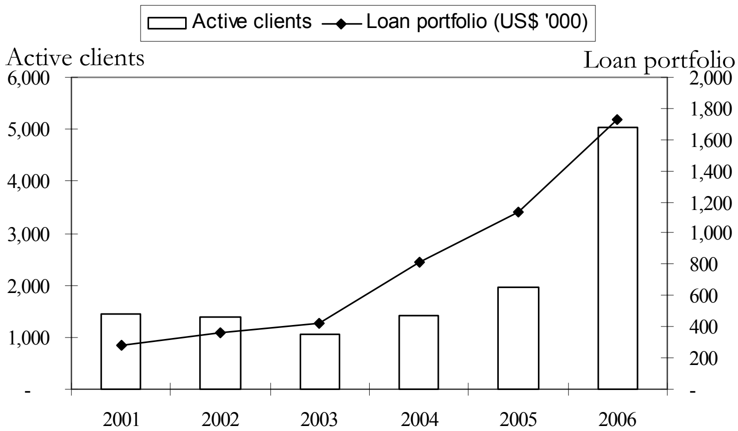
In M-CRIL's view, the equity investment products do not appear to be a prudent business proposition. This is because due to their inherent nature (as equity investment and not loan), the products carry more risk and Crystal may not be able to earn sufficient returns on these investments. As such, loan products are safer avenues than equity investment and in the case of loans, higher returns are also assured.

In the future, Crystal plans to have a presence in several market segments, with a mix of microfinance products – consumer loans and business loans to individuals as well as micro-insurance and money transfer services. Crystal also plans to deepen its operations in rural areas in the future, through a network of service centres apart from branches.

- Growth, expansion and fund mobilisation

During 2006, Crystal has shown significant growth, particularly in terms of the number of active clients (158%). The loan portfolio has grown by 53% during the year.

The organisation expects to have an outreach of around 6,500 active clients and a loan portfolio of US$3.3 million by the end of 2007.




In the next two years, Crystal plans to open one branch each in Batumi (Adjara region) and one in the capital city of Tbilisi. In addition, it also plans to start several sub-offices (service centres) across the country, to help the organisation build a client-base for the future.

Crystal has been successful in mobilising loan funds from several lenders. Particularly during 2006, the organisation has mobilised a significant amount of funds. Crystal has received a sanction of US$2.0 million from the Deutsche Bank. It has already received US$700,000 from the Bank till the time of the rating visit.

- Competition

Crystal operates in a competitive market, with several MFIs and banks being significant players. While the competition is not high at present, the organisation is likely to face high competition from MFIs such as Constanta, SBDF and Credo and also to a lesser degree from FINCA in the future. High competition is also expected from Pro Credit Bank and from Bank of Georgia, particularly in the consumer loans and individual business loans segment.

Most of the MFIs in Georgia presently operate in the low-income and middle-income market segment. However, Constanta, which is one of the largest MFIs in the country and has most of its portfolio in group loans, has been expanding aggressively and is trying to make an entry in the middle-income and high-income market segment.

Most of the banks presently operate in the high-income and middle-income segment. However, Pro Credit Bank, which has the highest market share in micro-credit loans in Georgia (as per a market study carried out for by ACT Reasearch, Georgia), has been expanding aggressively and is expected to be a significant competitor to all Georgian MFIs in the future.

With Constanta and Pro Credit Bank expected to be significant players in the middle-income market segment, <u>the competition for Crystal and other MFIs is likely to intensify in the future</u>. Crystal believes that its main competitive advantage is the easier procedures and quicker appraisal (compared to banks). Crystal also expects to have a wider reach, particularly in rural areas, through a network of branches and service centres across the country.

Crystal monitors its competitors regularly and is a member of the Georgian association of MFIs – Association of Georgian Microfinance Organisations (AGMO). The members of AGMO (Constanta, FINCA, SBDF, Crystal and Credo) meet regularly and share operational data. They have also made a beginning towards forming a Credit Bureau by sharing information on defaulters. However, some of the MFIs have not been cooperating in terms of providing regular information.

- <u>Transformation</u>

Under the new legislation applicable to microfinance institutions in Georgia (which was facilitated by AGMO), all MFIs presently registered as Foundations are required to transform into an Open Joint Stock Company (OJSC) by December 2007. After the transformation, they will be supervised and controlled directly by the National Bank of Georgia and not the Ministry of Social Justice, as is presently the case.

There is lack of clarity regarding several issues associated with the transformation of Crystal and other MFIs in Georgia. The main issues are: 1) whether the assets owned by a not-for-profit Foundation can be transferred to a for-profit entity owned by private individuals; 2) the tax implications of such transfer of assets and equity in the proposed for-profit entity; and 3) how exactly the transformation would be carried out – through a reorganisation of the existing Foundation or through "sale" of assets and liabilities to the new OJSC or by creating a company as a subsidiary of the existing Foundation.

Crystal has consulted a Georgian consultancy firm – DLA Piper Gvinadze and Partners LP, based in Tbilisi, for advice on the process of transformation, taxation and other related issues arising out of the proposed transformation. The consultancy firm has suggested various options for the transformation process, discussing the pros and cons of each option and also mentioning the possible tax implications. Crystal has also contacted Price Waterhouse Coopers for advice regarding the taxation implications of the proposed transformation. However, a clear picture on the process of transformation and the tax implications is yet to emerge.

- Second line of leadership

  A major issue of concern for Crystal is the weak second line of leadership. Most of the operational responsibilities are presently handled by the Executive Director (with the support of Branch Managers), since Crystal does not have any dedicated head of credit operations or a Manager/Officer for MIS (data consolidation and reporting). This is a significant cause for concern since Crystal plans to grow at a significant pace in the future.

  Crystal had faced a major case of fraud during 2006 and had to write off loans amounting to nearly US$100,000 on account of the fraud, and this amount was 59% of the total amount written off during the year. The Credit Manager of Poti branch of Crystal had defrauded the organisation of around US$140,000 through "ghost loans". The $PAR_{60}$ in the Poti branch as on 31 December 2006 was US$38,528, which was 64% of the total $PAR_{60}$ of the organisation. All the staff of the branch have been fired and a criminal case has been filed against the Credit Manager.

  One of the major reasons for the fraud was the fact that the organisation does not have any head of credit operations to regularly follow-up all cases of overdues and for regular monitoring of branch staff and operations. Another significant reason is that Crystal did not have a strong Internal Audit function.

  Crystal has recently recruited a qualified and experienced person as Credit Risk Manager, who is expected to take up the responsibility of credit appraisal and verification of loan applications. Crystal also has an Internal Auditor who is presently a part of the Credit Committee at the Head Office and has also been visiting branches for checking of accounts and loan applications. However, in spite of these additions, the second line of leadership continues to be weak.

### 3.2 Managerial factors

Crystal displays moderate performance on managerial factors with a grade of $\beta$. The grade reflects the organisation's qualified and experienced human resource and good MIS. However, the grade is low on account of the relatively weak systems for tracking overdues and internal control.

- Human resource quality and management

  Crystal has qualified and experienced staff at all levels. However, as mentioned before, the second line of leadership is weak, with the Executive Director having to look after overall credit operations as well as regular data consolidation and reporting.

  The organisation has reasonable systems for induction and training of staff, which is done mainly through on-the-job training by attaching new recruits to existing staff as assistants. The probation period is three-six months.

  Commitment and motivation at all staff levels is high and staff attrition rate in Crystal has been low. Crystal has developed a grade-based incentive system for staff, which rewards staff for growth in portfolio but also has in-built disincentives (which reduce the grade of the staff and therefore his pay) for portfolio-at-risk beyond pre-decided levels.

- Accounting and MIS

Accounting

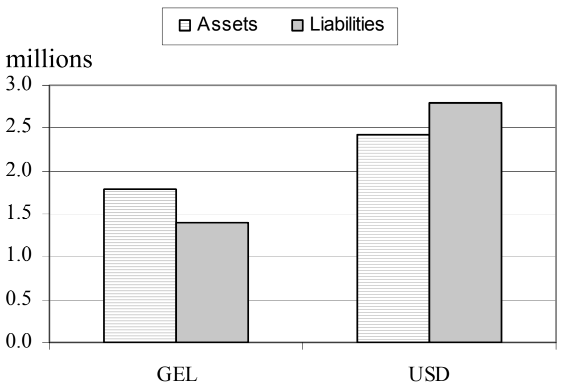
Crystal has a computerised accounting system and uses Oris for accounting. The software is used in the branches and the Head Office and monthly Trial Balance and Income and Expenditure statements are prepared in the Head Office.

The organisation accounts for all expenses and incomes (including grant income) on accrual basis. There are clear policies for de-recognition of interest and penalty incomes in the case of overdue accounts.

Crystal has prudent policies for loan loss provisioning based on the ageing of the loans. 100% loan loss reserve is created on all loans that are more than 180 days old. These loans are written off if they are considered to be irrecoverable or if the Court has ruled against Crystal's case for recovery of loan or in case of death of the client.

Crystal continues to face the risk of losses due to foreign exchange fluctuations, since its assets and liabilities are not perfectly matched in all currencies. Crystal disburses loans both in Georgian Lari and US Dollars and at the end of each month, the Finance Manager and Executive Director decide how much is to be disbursed in which currency during the next month, based on the asset-liability position at the end of the month and the availability of funds. Thus, the foreign exchange risk is borne partly by Crystal and partly by the client.

The figure alongside shows the position of Crystal's assets and liabilities in GEL and US Dollars as on 31 December 2006. As shown in the figure, there is a positive gap of about GEL 0.5 million and negative gap of about the same amount in US Dollars. However, the gaps are not very high at present, in relation to the total assets.




Although the Georgian Lari has been very volatile in the past in relation to the US Dollar, the Lari has been more or less stable (with slight appreciation) over the last one year, on account of the falling Dollar.

The rating team noted that the audited statements of Crystal (which are presented in English) are of poor quality, with inadequate explanatory notes and very poor grammar. Crystal plans to get its financial statements audited by an internationally reputed firm from 2007 onwards.

MIS

The MIS of the organisation is fully computerised. Crystal uses the latest version of Loan Keeper software at its Head Office and branches. The software has been developed by a local vendor and is customised to meet Crystal's requirements.

The software has well-defined user rights and back-up arrangements are made for data security. All data relating to credit such as client details, disbursement and collection is entered in the database by the Loan Officers and Accountants on a daily basis. Once the data has been entered, the software is capable of generating all the required reports.

The software can generate portfolio reports across Branch, Products and also staff. It can provide overdue amounts with ageing and status of portfolio through generation of critical ratios like portfolio at risk. The software has also been upgraded to handle multiple currencies, which helps Crystal handle indexed loans. The conversion rate between Georgian Lari and US Dollars, as provided by the National Bank of Georgia, is entered in Loan Keeper on a daily basis, to facilitate conversion of assets and liabilities in US Dollars to the local currency.

The MIS of Crystal is good and is adequate to meet its present as well as future requirements.

- <u>Tracking system for overdues</u>

Although Crystal has reasonable systems for tracking overdues, the organisation is not very strict about following up on cases of overdues. Although each branch has a Lawyer, he/she is mainly involved in preparing the loan contract and explaining the terms and conditions of the loan to the clients.

The MIS software is used for tracking of clients with overdues. In case of any default, a warning notice is sent to the client within one week after the date of missed instalment. The warning note mentions a date for paying the amount overdue, which is generally one month after the date of the notice.

If the overdue amount is not received by the mentioned date, the branch Lawyer visits the client together with another warning note asking the client to pay the amount overdue within one month. In case payment is not received by the mentioned date, Crystal may file a suit for recovery of pledged assets. However, the organisation tries to settle all cases out of Court, to avoid the delays involved in legal settlement.

Crystal's credit policies do not permit restructuring of loans in general. However, in exceptional cases, where the client is genuinely not able to make payment as per schedule, Crystal allows for the repayment instalment to be postponed.

- <u>Financial planning and control systems</u>

Crystal has reasonable systems for financial planning. Credit Managers send annual estimates of disbursements and collections based on the estimates provided by Loan Officers. Based on these, the Finance Department prepares annual physical and financial projections, which are presented to the Board and discussed in the presence of all Directors and the Executive Director. The annual plan is finalised by the Board by the first of November every year.

Based on the finalised plan, targets are assigned to branch staff and variance analysis is carried out on a monthly basis by the Finance Department. The plans may be revised in case of significant variations.

With all its financial transactions routed through banks (or through shopkeepers), Crystal's control systems would have been good if the organisation had a head of overall credit operations to monitor branch operations regularly. However, the absence of a head of operations makes the control systems weak and susceptible to frauds as in the case of Poti branch described earlier.

Crystal has appointed an Internal Auditor, who, till the time of the rating visit, was involved mainly in credit appraisal and verification of loan applications in branches. He had also made visits to the branches to check if the policies and procedures prescribed are being followed. However, the Internal Audit system as it is presently designed, is inadequate and may not be able to check all risks such as the risk of loss of business to competitors or loss due to poor follow-up on cases of overdues.

Under the present system, each branch is visited at least once a month and each visit is generally for one day only, but may be extended to three days if required. The Internal Auditor submits a written report only if serious problems are noted and no written reports had been prepared since October 2006 till the time of the rating visit. In general, the observations of the Internal Auditor are discussed in monthly management meetings attended by some of the Directors, the Executive Director and Finance Manager and the Credit Managers of the branches.

Strong systems for internal control in general and internal audit in particular are more important for Crystal, since it plans to have several operational locations through a network of service centres in addition to regular branches. Even at the time of the rating visit, Crystal had three branches and as many as five service centres.

- Quality of clients/member groups

Visited group clients as well as individual clients showed good awareness about the organisation's products, policies and norms. Crystal has a wide-client base with small shop-keepers trading in clothes and other merchandise in the local markets as well as medium-large entrepreneurs such as those having a nursery of vegetables or those involved in processing tea.

- Infrastructure

Crystal has a reasonable infrastructure base of about GEL229,000 (US$135,000) as on 31 December 2006. This includes buildings (the Kutaisi Head Office and Zugdidi branch office), computer hardware and software, vehicles, furniture and fixtures at branches and the Head Office. The current level of infrastructure is adequate and is being employed effectively in the overall management of the microfinance programme.

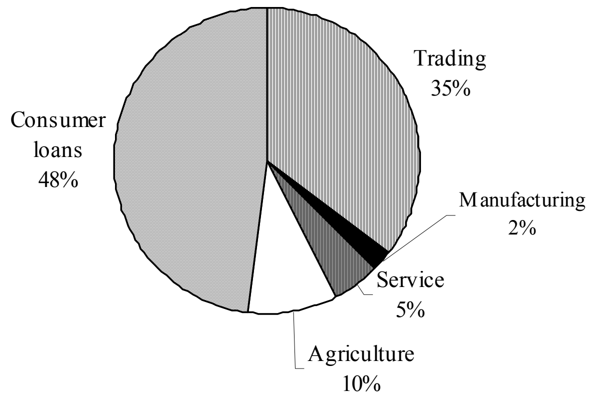
### 3.3 Financial performance

The financial performance grade of Crystal is reasonable at β+. The grade is mainly on account of high capital adequacy, high Yield-to-APR ratio and reasonable performance on profitability and sustainability. But for the loss due to the fraud in Poti branch, the quality of Crystal's loan portfolio is also reasonable.

➢ Credit performance and asset quality

Crystal has reasonable credit performance. Its current repayment rate is 98.0% and the $PAR_{60}$ is 3.5% as on 31 December 2006. However, excluding the PAR in Poti branch, the $PAR_{60}$ as on the above date is only 1.2%. Moreover, the total $PAR_{60}$ as on 31 March 2007 is only 1.9% (including the PAR in Poti branch, but excluding an amount of US$ 50,104; 3% of the outstanding loan portfolio as on 31 March 2007, which was written off during January-March 2007).

During the year 2006, the organisation had written off loans of US$169,168 or 9.8% of the gross portfolio outstanding as on 31 December 2006. 5.7% of the gross portfolio was written off on account of the fraud in Poti branch and the remaining was written of on account of bad loans mainly in Zugdidi branch.




As on 31 December 2006, the restructured loans formed 0.2% of the loan portfolio.

In terms of diversification, Crystal's portfolio is reasonably well diversified, with consumer loans and loans for trading being the major constituents. The figure above shows the purpose-wise composition of Crystal's loan portfolio as on 31 December 2006.

➢ Mobilisation of funds

Crystal has been successful in mobilising commercial loan funds from several institutional lenders, particularly during 2006. The organisation mobilised loan funds of US$1.2 million during 2006 from Deutsche Bank, Oxfam/Novib and Oikocredit. Crystal has been sanctioned loan funds of US$2.0 million from Deutsche Bank, of which it had received US$700,000 till the time of the rating visit.

With its reasonably high capital adequacy and reasonable performance on profitability and sustainability, Crystal should not face much difficulty in mobilising loan funds in the near future. However, the weak second line of leadership may restrict the growth of the organisation.

➢ Asset, liability and equity composition

Crystal has utilised its assets reasonably with about 70% deployed in loans. Cash in bank is high at 22%, on account of lower disbursements in Poti than what was planned due to the case of fraud and also because the organisation had received USD 200,000 from Deutsche Bank and Euros 100,000 from Oxfam/Novib towards the end of the year. On the liability side, the long-term debts constitute 67% and the net worth contributes to 28.5% of the total assets. Short-term debt and other liabilities make up the remaining 4.5%.

Crystal has reasonably high capital adequacy at 36.2% and the organisation should not have difficulty in borrowing funds from commercial lenders in the near future.

As per the organisation's Business Plan, Crystal expects equity investment of about US$55,000 over the next two years.

➢ Profitability and Sustainability

Crystal shows reasonable performance on profitability and sustainability, with its OSS at 103.5% and FSS at 97.3% as on 31 December 2006. This is mainly on account of the high yield that Crystal earns on its portfolio. The organisation's operating expense ratio is relatively high at 23.7% (compared to the OER of other Georgian MFIs rated by M-CRIL – 18-22%). In terms of profitability, the organisation has a positive RoA of 1.0% as on 31 December 2006.

Crystal is likely to maintain the same level of profitability in the future, unless it is forced by its competitors to reduce the interest rates on its loans.

## 4 Conclusions

| Strengths | Weaknesses |
|---|---|
| Organisational<br>✓ Clear focus on microfinance<br>✓ Good performance on fund mobilisation | Organisational<br>✗ Weak second line of leadership |
| Managerial<br>✓ Qualified and experienced staff<br>✓ Good MIS | Managerial<br>✗ Relatively weak internal control systems<br>✗ Moderate systems for tracking overdues |
| Financial<br>✓ High capital adequacy<br>✓ High Yield-to-APR ratio<br>✓ Reasonable quality of loan portfolio | Financial<br>✗ Relatively high operating expense ratio |

# 5 Creditworthiness

Crystal has achieved a rating grade of ***beta ($\beta$)***.[2] In terms of creditworthiness this implies **moderate safety**. Crystal shows moderate performance on governance aspects. The organisation has a professional Board that is actively involved and has also enabled Crystal to avail of commercial borrowings from several lenders. However, the weak second line of leadership is a significant cause for concern.

Crystal's systems for internal control are also nascent and untested. The organisation had faced a major case of fraud during 2006, on account of which it had to write off nearly US$100,000 (almost 6% of its loan portfolio as on 31 December 2006) and its operations in one branch were almost brought to a standstill. However, in spite of the fraud, has shown significant growth during the year. Crystal's performance on financial sustainability indicators is reasonable, mainly on account of the high yield on its portfolio.

**In M-CRIL's view**, Crystal can absorb – from all sources – loan funds of GEL2.0 million (US$1.2 million) over the next one year for on-lending to its borrowers. However, given the organisation's plans to transform into a joint stock company by the end of the year, lenders are advised to conduct a due diligence prior to lending to the new entity.

A rating update after one year is suggested to ascertain changes in the creditworthiness and absorptive potential of the institution. **This rating is valid, subject to no other substantial inflows of loan funds into the organisation beyond the limits specified here** and to no other significant changes in the organisational structure and external operating environment.

[2] The Rating Grade given measures performance on the rigorous standards established by M-CRIL. The assessment uses an instrument designed specifically for the conditions and nature of MFIs operating in Asia and is comparable with other ratings done by M-CRIL in this region.

# Financial statements of Crystal Fund

## Balance Sheet - as on

| 31 Dec 2005 | | | | | 31 Dec 2006 |
|---|---|---|---|---|---|
| **US$** | **Assets** | **GEL** | **GEL** | **US$** | **US$** |
| | | | | | US$1=GEL1.7 |
| | **Current assets** | | | | |
| 28,901 | Cash in hand and bank | | 894,383 | | 526,108 |
| | Equity investments | | 18,290 | | 10,759 |
| 6,545 | Deferred tax assets | | 81,922 | | 48,189 |
| 10,981 | Tax receivables | | 13,516 | | 7,951 |
| 15,492 | Other current assets | | 38,235 | | 22,491 |
| | Loans outstanding | | | | |
| | Current | 2,784,904 | | 1,638,179 | |
| | Past due | 178,704 | | 105,120 | |
| | Restructured | 4,753 | | 2,796 | |
| 1,193,243 | Gross loans outstanding | 2,968,361 | | 1,746,095 | |
| (61,541) | (Loan loss reserve) | (120,432) | | (70,842) | |
| 1,131,702 | Net loans outstanding | | 2,847,929 | | 1,675,253 |
| **1,193,622** | **Total current assets** | | **3,894,275** | | **2,290,750** |
| | **Long term assets** | | | | |
| 12,550 | Intangible assets | 18,017 | | 10,598 | |
| 102,138 | Net property and equipment | 210,718 | | 123,952 | |
| **114,688** | **Total long term assets** | | **228,735** | | **134,550** |
| **1,308,309** | **Total Assets** | | **4,123,010** | | **2,425,300** |
| | **Liabilities and Networth** | | | | |
| | **Current liabilities** | | | | |
| 18,540 | Tax liabilities | | 26,400 | | 15,529 |
| 14,895 | Accounts payable | | 27,457 | | 16,151 |
| 11,684 | Interest payable | | 34,048 | | 20,028 |
| | Short term debt | | | | |
| 61,271 | CHCA | 103,150 | | 60,676 | |
| 85,558 | TBC Bank | | | | |
| 88,571 | Current part of LT debts | | | | |
| 235,399 | Total short term debt | | 103,150 | | 60,676 |
| **280,518** | **Total current liabilities** | | **191,055** | | **112,385** |
| | **Long term liabilities** | | | | |
| | Long term debt | | | | |
| 356,295 | Cordaid | 575,665 | | 338,626 | |
| 8,467 | Loan from individual – Keith Young | 17,135 | | 10,079 | |
| | Deutsche Bank | 1,199,450 | | 705,559 | |
| | Oikocredit | 514,050 | | 302,382 | |
| | Oxfam/Novib | 451,240 | | 265,435 | |
| 364,762 | Total long term debt | | 2,757,540 | | 1,622,082 |
| **364,762** | **Total long term liabilities** | | **2,757,540** | | **1,622,082** |
| | **Net worth** | | | | |
| 515,389 | Registered equity | 876,161 | | 515,389 | |
| 48,016 | Grants | 95,573 | | 56,219 | |
| 40,459 | Retained net surplus/(deficit) | 169,362 | | 99,625 | |
| 59,165 | Current net surplus/(deficit) | 33,319 | | 19,600 | |
| **663,029** | **Total net worth** | | **1,174,415** | | **690,833** |
| **1,308,309** | **Total Liabilities and Net Worth** | | **4,123,010** | | **2,425,300** |

## Income Statement – for the year ending

| 31 Dec 2005 | | | | | 31 Dec 2006 |
|---|---|---|---|---|---|
| US$ | Income | GEL | GEL | US$ | US$ |
| 389,761 | Interest on loans | 1,078,560 | | 634,447 | |
| 21,897 | Financial service fee | 86,329 | | 50,782 | |
| 32,350 | Penalties | 86,346 | | 50,792 | |
| 9,109 | Foreign exchange gain | 90,278 | | 53,105 | |
| 6,721 | Other income | 48,608 | | 28,593 | |
| **459,838** | **Total income** | | **1,390,121** | | **817,718** |
| | **Financial costs** | | | | |
| 40,844 | Interest on borrowings | 210,297 | | 123,704 | |
| 23,226 | Foreign exchange loss | 138,491 | | 81,465 | |
| **395,769** | **Gross financial margin** | | **1,041,333** | | **612,549** |
| 28,190 | Provision for loan losses | 15,812 | | 9,301 | |
| 6,368 | Bad debts written off | 387,253 | | 227,796 | |
| **361,211** | **Net financial margin** | | **638,268** | | **375,452** |
| | **Operating expenses** | | | | |
| 123,701 | Salaries | 308,595 | | 181,526 | |
| 17,709 | Travel | 44,456 | | 26,151 | |
| 10,394 | Depreciation | 34,789 | | 20,464 | |
| 118,493 | Administrative/office expenses | 203,152 | | 119,501 | |
| **270,296** | **Total operating expenses** | | **590,992** | | **347,642** |
| **90,914** | **Net Surplus/Deficit** | | **47,276** | | **27,810** |
| 90,914 | Profit before tax (PBT) | | 47,276 | | 27,810 |
| 31,749 | Tax | | 13,957 | | 8,210 |
| **59,165** | **Profit after tax (PAT)** | | **33,319** | | **19,600** |

## Notes to the financial statements

1. Income includes interest income, fees and earnings from other microfinance related services offered by the MFI rated. All loan portfolio related income is recognised only when it is actually received (**cash basis**). Grants allocated to the organisation's microfinance programme are treated as donated equity in the balance sheet (and not regarded as operational income).
2. Financial costs (interest on borrowings and savings, if any) and operating costs are calculated on an **accrual basis**. Loan loss provisioning expense and the corresponding balance sheet entry (loan loss reserve) is as computed by Crystal, based on the quality of the loan portfolio.

## Glossary

1. Current repayment rate
   Ratio of principal recovered (net of pre-payments) to the principal due during the current year.
2. Portfolio at risk ($PAR_{60}$)
   Ratio of the principal balance outstanding on all loans with overdues greater than or equal to 60 days to the total loans outstanding on a given date.
3. Yield on portfolio
   The interest income on loans divided by the average loan portfolio for the year.
4. Other income to average portfolio
   Total income other than from the interest on loans divided by average portfolio.
5. Financial cost ratio
   Total interest expense for the year divided by the average portfolio.
6. Loan loss provisioning ratio
   Total loan loss provisioning expense for the year divided by the average portfolio.
7. Operating expense ratio
   Ratio of salaries, travel, administrative costs and depreciation expenses to the average loan portfolio.
8. Average loan portfolio
   This represents the average loan outstanding for the year computed on a monthly basis.
9. Average total assets
   This represents the average total assets for the year calculated on an annual basis.
10. Operational Self-Sufficiency
    Ratio of total income to total costs for the year.
11. Financial Self-Sufficiency
    Ratio of total income to total adjusted expenses for the year. Adjustments have been made for subsidised cost of funds (w.r.t. market interest rate), equity (w.r.t. inflation) and in-kind donations.
12. Risk weighted capital adequacy ratio
    Ratio of networth to risk weighted assets (Risk weights: 100% for all assets except the following: fixed assets & interest bearing deposits: 50%; cash 0%).

# Projected Cash Flows and Financial Statements for five years

- The following assumptions and projections - derived from the limited information available from the organisation on its future financial projections – are tentative in nature. These **should not be viewed in isolation nor be regarded as a basis for investing in the future** - only the main risk rating report provides an opinion on investments.
- All assumptions are based on the data gathered during the rating exercise and the savings and credit methodology used by the organisation.

## 1 Basic Assumptions

(see also Notes to Cash Flow Projections below)

| For the year ending: | 31-Dec-06 | Dec-07 | Dec-08 | Dec-09 | Dec-10 | Dec-11 |
|---|---|---|---|---|---|---|
| Clients | 6,500 | 7,529 | 9,886 | 12,841 | 15,341 | 17,045 |
| Yield on average portfolio | 43.2% | 41.0% | 39.0% | 37.0% | 36.0% | 35.0% |
| Cost of external funds | 9.7% | 9.8% | 10.0% | 9.6% | 9.6% | 10.0% |
| Repayment rate from groups | 96.0% | 97.0% | 98.0% | 98.0% | 98.0% | 98.0% |
| Loan loss reserve ratio | 4.1% | 4.0% | 3.5% | 3.0% | 2.5% | 2.5% |
| Loan loss rate | 13.0% | 4.0% | 2.0% | 2.0% | 2.0% | 2.0% |
| Number of active borrowers at year end | 5,031 | 6,400 | 8,700 | 11,300 | 13,500 | 15,000 |
| Number of loans disbursed | 6,796 | 8,000 | 10,875 | 14,125 | 16,875 | 18,750 |
| Average loan size (USD) | 471 | 529 | 647 | 706 | 765 | 824 |

## 2 Projected Balance Sheets

*'000 USD*

| As on: | Dec-06 | Dec-07 | Dec-08 | Dec-09 | Dec-10 | Dec-11 |
|---|---|---|---|---|---|---|
| **Assets** | | | | | | |
| Cash balance | 526 | 149 | 246 | 354 | 509 | 542 |
| Loans outstanding | 1,746 | 3,028 | 5,185 | 7,358 | 9,428 | 11,394 |
| Loan loss reserve | -71 | -121 | -181 | -221 | -236 | -285 |
| Net loans outstanding | 1,675 | 2,907 | 5,003 | 7,137 | 9,192 | 11,109 |
| Other current assets | 79 | 121 | 207 | 294 | 377 | 456 |
| Long term investments | 11 | 15 | 26 | 37 | 47 | 57 |
| Net fixed assets | 135 | 227 | 363 | 441 | 471 | 513 |
| **Total Assets** | **2,425** | **3,419** | **5,846** | **8,264** | **10,597** | **12,677** |
| **Liabilities and Net Worth** | | | | | | |
| External borrowings | 1,683 | 2,468 | 4,468 | 6,254 | 7,861 | 9,101 |
| Other liabilities | 52 | 91 | 156 | 221 | 283 | 342 |
| Provision for forex losses | 0 | 30 | 82 | 156 | 250 | 364 |
| Donations and equity | 572 | 599 | 627 | 627 | 627 | 627 |
| Retained surplus/deficit | 100 | 119 | 231 | 514 | 1,007 | 1,577 |
| Current surplus/deficit | 20 | 112 | 283 | 493 | 570 | 667 |
| Net worth | 691 | 830 | 1,140 | 1,633 | 2,203 | 2,870 |
| **Total Liabilities and Net Worth** | **2,425** | **3,419** | **5,846** | **8,264** | **10,597** | **12,677** |

## 3 Projected Income Statements

*'000 USD*

| For the year ending: | Dec-06 | Dec-07 | Dec-08 | Dec-09 | Dec-10 | Dec-11 |
|---|---|---|---|---|---|---|
| **Income** | | | | | | |
| Interest | 634 | 979 | 1,602 | 2,320 | 3,021 | 3,644 |
| Other income | 130 | 151 | 207 | 258 | 283 | 342 |
| Foreign exchange gain | 53 | | | | | |
| **Total Income** | **818** | **1,130** | **1,809** | **2,578** | **3,304** | **3,986** |
| **Cost** | | | | | | |
| Financial | 124 | 217 | 381 | 542 | 706 | 867 |
| Foreign exchange loss | 81 | | | | | |
| Provision for forex losses | | 30 | 52 | 74 | 94 | 114 |
| Loan loss provision | 9 | 50 | 60 | 39 | 15 | 49 |
| Loan write off | 228 | 137 | 112 | 165 | 244 | 285 |
| Depreciation | 20 | 23 | 36 | 44 | 47 | 51 |
| Operating costs (excl.depr.) | 327 | 534 | 813 | 1,098 | 1,485 | 1,786 |
| **Total Cost** | **790** | **991** | **1,455** | **1,962** | **2,592** | **3,152** |
| **Surplus/Deficit** | **28** | **140** | **354** | **616** | **712** | **834** |
| Tax | 8 | 28 | 71 | 123 | 142 | 167 |
| **Profit to balance sheet** | **20** | **112** | **283** | **493** | **570** | **667** |

## 4 Projected Cash Flow Statements

*'000 USD*

| For the year ending: | Dec-07 | Dec-08 | Dec-09 | Dec-10 | Dec-11 |
|---|---|---|---|---|---|
| **Inflows** | | | | | |
| Opening cash | 526 | 149 | 246 | 354 | 509 |
| External borrowings | 1,176 | 2,765 | 3,000 | 3,412 | 3,882 |
| Repayments from members | 2,817 | 4,768 | 7,632 | 10,590 | 13,190 |
| Equity investments | 28 | 28 | | | |
| Increase in other liabilities | 39 | 65 | 65 | 62 | 59 |
| Interest income | 979 | 1,602 | 2,320 | 3,021 | 3,644 |
| Other income | 151 | 207 | 258 | 283 | 342 |
| **Total Inflow** | **5,716** | **9,583** | **13,522** | **17,723** | **21,627** |
| **Outflows** | | | | | |
| Disbursement | 4,235 | 7,037 | 9,971 | 12,904 | 15,441 |
| Repayments to lenders | 391 | 765 | 1,213 | 1,805 | 2,642 |
| Operating expenses (excl. depr.) | 534 | 813 | 1,098 | 1,485 | 1,786 |
| Interest paid on borrowings | 217 | 381 | 542 | 706 | 867 |
| Increase in other current assets | 43 | 86 | 87 | 83 | 79 |
| Increase in long term investments | 4 | 11 | 11 | 10 | 10 |
| Tax | 28 | 71 | 123 | 142 | 167 |
| Fixed assets purchase | 115 | 172 | 123 | 77 | 93 |
| **Total Outflow** | **5,567** | **9,337** | **13,168** | **17,214** | **21,085** |
| **Net cash balance** | **149** | **246** | **354** | **509** | **542** |

## 5 Key projected performance ratios

| For the year ending: | Dec-06 | Dec-07 | Dec-08 | Dec-09 | Dec-10 | Dec-11 |
|---|---|---|---|---|---|---|
| Operational self-sufficiency | 104% | 114.1% | 124.3% | 131.4% | 127.5% | 126.4% |
| Return on average assets | 1.0% | 4.8% | 7.6% | 8.7% | 7.6% | 7.2% |
| Operating expense ratio | 23.7% | 23.3% | 20.7% | 18.2% | 18.3% | 17.7% |
| Average outstanding/borrower (USD) | 347 | 473 | 596 | 651 | 698 | 760 |
| Portfolio growth rate | 46.3% | 73.4% | 71.2% | 41.9% | 28.1% | 20.9% |
| Risk weighted capital adequacy ratio | 36.2% | 26.4% | 21.2% | 21.3% | 22.5% | 24.3% |

# 6 Notes to the projections

1. The operating expense ratio is based on current levels and is projected based on changes in overall productivity and growth in staff, branches and portfolio.
2. Estimated external borrowings are subject strictly to performance based on the findings of this microfinance capacity assessment (credit rating).
3. Equity investments are projected as per the Business Plan of the organisation.
4. Average loan size to members is projected to increase steadily, matching with the organisation's plan to disburse more loans to individual entrepreneurs
5. Interest income is taken as [yield on portfolio*average portfolio for the year]. The yield is projected to decrease, as the organisation makes its products more competitive.
6. Other income is the income that the organisation earns on commissions, penalties and bad debts recovered
7. Estimates on growth in outreach and demand for loans from the organisation have been made based on current growth levels and future expansion potential and capacity.
8. Repayments to lenders is 20-33% per annum on the projected liability structure and the actual repayments due on the present outstanding debt.
9. Interest paid is taken as the [average cost of external funds * the average external borrowing liability figure].
10. Provision for foreign exchange losses has been created at 1% of the gross loan portfolio.
11. In the projections the net worth figure includes equity, retained surpluses and current surplus.
12. Taxes are taken at 20% of taxable income.

# 7 List of abbreviations

| | |
|---|---|
| AGMO | Association of Georgian Microfinance Organisations |
| APR | Annual Percentage Rate |
| CHCA | Charity Humanitarian Center Abkhazeti |
| DCB | Demand Collection Balance |
| FSS | Financial Self-Sufficiency |
| GEL | Georgian Lari |
| HO | Head Office |
| HR | Human Resource |
| IDP | Internally Displaced Persons |
| LIBOR | London Inter-Bank Offered Rate |
| LT debts | Long Term Debts |
| M-CRIL | Micro-Credit Ratings International Ltd |
| MFI | Micro Finance Institution |
| MIS | Management Information System |
| NGO | Non Government Organisation |
| OER | Operating Expenses Ratio |
| OJSC | Open Joint Stock Company |
| OSS | Operating Self-Sufficiency |
| $PAR_{60}$ | Portfolio At Risk (greater than 60 days) |
| PAT | Profit after tax |
| PBT | Profit before tax |
| RoA | Return on Assets |
| SBDF | Small Business Development Fund |

# M-CRIL's Microfinance Rating Symbols

| M-CRIL Grade | Description |
|---|---|
| α++<br>alpha double plus | Highest safety, very good systems<br>➢ most highly recommended |
| α+<br>alpha single plus | Very high safety, good systems<br>➢ highly recommended |
| α<br>alpha | High safety, good systems<br>➢ highly recommended |
| α–<br>alpha minus | Reasonable safety, good systems<br>➢ recommended |
| β+<br>beta plus | Reasonable safety, reasonable systems<br>➢ recommended, needs monitoring |
| β<br>beta | Moderate safety, moderate systems<br>➢ acceptable, needs improvement to handle large volumes |
| β–<br>beta minus | Significant risk, poor to moderate systems<br>➢ acceptable only after improvement |
| γ+<br>gamma plus | Substantial risk, poor systems<br>➢ needs considerable improvement |
| γ<br>gamma | Highest risk, poor systems<br>➢ not worth considering |