Final Project: Microfinance Consulting Report

Analysis of

KRABAN SUPPORT FOUNDATION

Madrid/ Accra, April-July 2012




Financieros sin Fronteras

Master in Finance - Class of 2012

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Limitations of this report

With regards to the following report, it is important to keep in mind the following limitations:

Time

The authors were fortunate enough to be able to visit Ghana and the microfinance institution Kraban Support Foundation (KSF). During the trip we twice met with the CEO Nana Opare Djana and one of his Officers in Charge (OIC), Emmanuel Aboagye. We also had the opportunity to meet some of the Board members. Additionally, we visited two of the rural communities where KSF operates and were able to interview clients. Although these opportunities provided a good insight into the MFI, we found the time too restricted to make as thorough an analysis of the KSF and the Ghanaian microfinance environment as we would have wished to do.

Client Access

While we did have the opportunity to interview some clients from two distinct villages, we often had to interview them through a KSF employee that acted as translator. This inherently prevents a more open discussion between the client and the interviewer as the clients may not want to offend the KSF employee nearby. Also, KSF staff typically dictated who the students interviewed, and the sample pool can therefore not be seen as random or unbiased.

Access to Data

Gathering data was difficult at times. We did not have access KSF's actual computers and data mining accordingly came from limited sources. We therefore depended on KSF's cooperation for sources of information.

Lack of Data

Some data was simply non-existent. For example, actual write-offs were not made available and the group is not sure how and if they are recorded.

It is, however, important to note that while the author's realize these limitations as significant, we feel that our time in Ghana and the data we received through collaboration with the staff of KSF was significant enough to present the following report. It is the hope of the authors that this report serves as a building block for both KSF and potential investors.

Table of Contents

Limitations of this report I
Table of Contents III
1 Overview 1
1.1 Summary of Institutional Data 1
1.2 Mission and Vision 1
1.3 Organizational Strengths, Weaknesses and Competition 1
1.4 Macroeconomic and Political Environment 3
1.5 Other Environmental Factors 6
2 Institutional Set Up 7
2.1 Ownership and Governance 7
2.2 Management 8
2.3 Organizational Structure 9
2.4 Human Resources Management 9
2.5 Information Technology 10
2.6 Internal Controls 10
2.7 Internal Audit 11
2.8 External Audit 11
2.9 Regulation and Supervision 11
2.10 Ratings 12
2.11 External Relationships 12
2.12 Chapter Conclusion 12
3 Financial Viability and Risk Management 13
3.1 General Information 14
3.2 Financial Statement Analysis 16
3.3 Financial Performance Ratios Analysis 23
3.4 Interest Rate Analysis 24
3.5 Risk Management 24
3.6 Chapter Conclusion 24
4 Products 25
4.1 General 25

4.2 Voluntary Savings 26
4.3 Loans 27
4.4 Other Financial Products 32
4.5 Nonfinancial Products 33
4.6 Chapter Conclusion 34
5 Loan Portfolio Quality 35
5.1 Loan Portfolio Breakdown 35
5.2 Monitoring and management 36
5.3 Chapter Conclusion 37
6 Business Planning 38
6.1 General Information 38
6.2 Financial Projections 38
6.3 Funding 39
7 Social Performance 40
7.1 General Information 40
7.2 Intent and Design 41
7.3 Depth and Breadth of Outreach 42
7.4 Changes in the Social and Economic Lives of Clients and their Households 43
7.5 Demonstration Effect 43
7.6 Durability and Impact 44
7.7 Formalization of Otherwise Informal Activities 45
7.8 Chapter Conclusion 45
8 Findings and Recommendations 46
9 Information for Donors and Investors 47
9.1 Camel Rating Summary 47
9.2 Other Information for Donors and Investors 47
Appendix 48
Bibliography & Further Reading 65

1. OVERVIEW




1 Overview

In the overview section, we are introducing KRABAN Support Foundation (“KSF”, “KRABAN”) to give a summary of the strengths and weaknesses of the institution. Furthermore, we are taking a look at the competition and the market environment, as well as macroeconomic data of Ghana.

1.1 Summary of Institutional Data

The institution is accredited as a private voluntary organization in development and limited by guarantee under Act 179 of the Companies Code of 1963. Kraban Support Foundation’s core business is the delivery of financial services to rural informal agricultural operators in Ghana. The Head Office is in Accra, but the operational aspects center around the two Branch Offices at Somanya in the Yilo Krobo District of the Eastern Region and Takoradi in the Western Region. The organization is owned by 3 subscribers and managed by a 7-member Board of Directors. The main products offered by the organization are micro loans and skills training. Other services offered are individual saving deposits and educational programs covering social issues.

Currently there are 8017 active borrowers being financed with KRABAN’s credit assistance. A breakdown of the loans indicates that about 89.7% loans granted in 2010 went to small-scale women entrepreneurs while 10.3% of loans went to male clients. The bulk of the loans went into the agriculture produce marketing, fish and agro-processing, provision of agricultural and artisanal inputs. The loans were also used to finance poultry, beekeeping and bakery projects, and small business and communication services.

1.2 Mission and Vision

In its business plan, KRABAN states its vision as follows:

> “ Kraban believes in a sound transitional pro-poor strategy towards a path between market responses and social demands with an imperative gender focus. With this perspective, Kraban hopes to be the leading financial non-governmental institution in Ghana by 2025.”

The vision behind the financial and educational services provided by Kraban is thus in its essence humanitarian. Kraban’s mission as follows: “To develop innovative strategies that enhance the capacity of vulnerable groups to operate independently and effectively in the informal sectors of the Ghanaian economy”[1].

Kraban Support Foundation’s core business is the delivery of financial services and education to informal sector operators in Ghana, especially to female entrepreneurs. Financial loans are combined with supporting women’s groups, potential expansion in credit program, staff capacity building training workshop, credit monitoring and credit evaluation, all in order to secure that the resources granted to the local community will be deployed in an efficient manner.

1.3 Organizational Strengths, Weaknesses and Competition

In order to evaluate the strengths and weaknesses of KSF, we provide a SWOT and Porter´s Five Forces analyses.

[1] Kraban Support Fundation Strategic Business Plan, *Microficnance Operational Document*, October 2011.

S	▪ Large Client Network ▪ High demand for microfinance products ▪ Knowledgeable board and management	▪ Overall transparency of the organization ▪ Diversity of Funding sources ▪ Pre-determined products from current funding partners	W
O	▪ Untapped potential (50 Farmer-based organizations (FBOs) ▪ Potential to customize products, increase revenue and reduce Portfolio at Risk.	▪ Changes in regulation ▪ Upcoming elections in Ghana ▪ Macroeconomic Factors (e.g. Inflation, FX) ▪ Lack of diversifying funds	T

Figure 1: Swot Analysis

The data from mixmarket.org shows 64 registered MFIs that operate in Ghana, although the exact number is much bigger. The total loans thereby amount to USD146.5m with 247,279 active borrowers. The following graph shows Porter´s Five Forces to illustrate the environment KSF acts in.

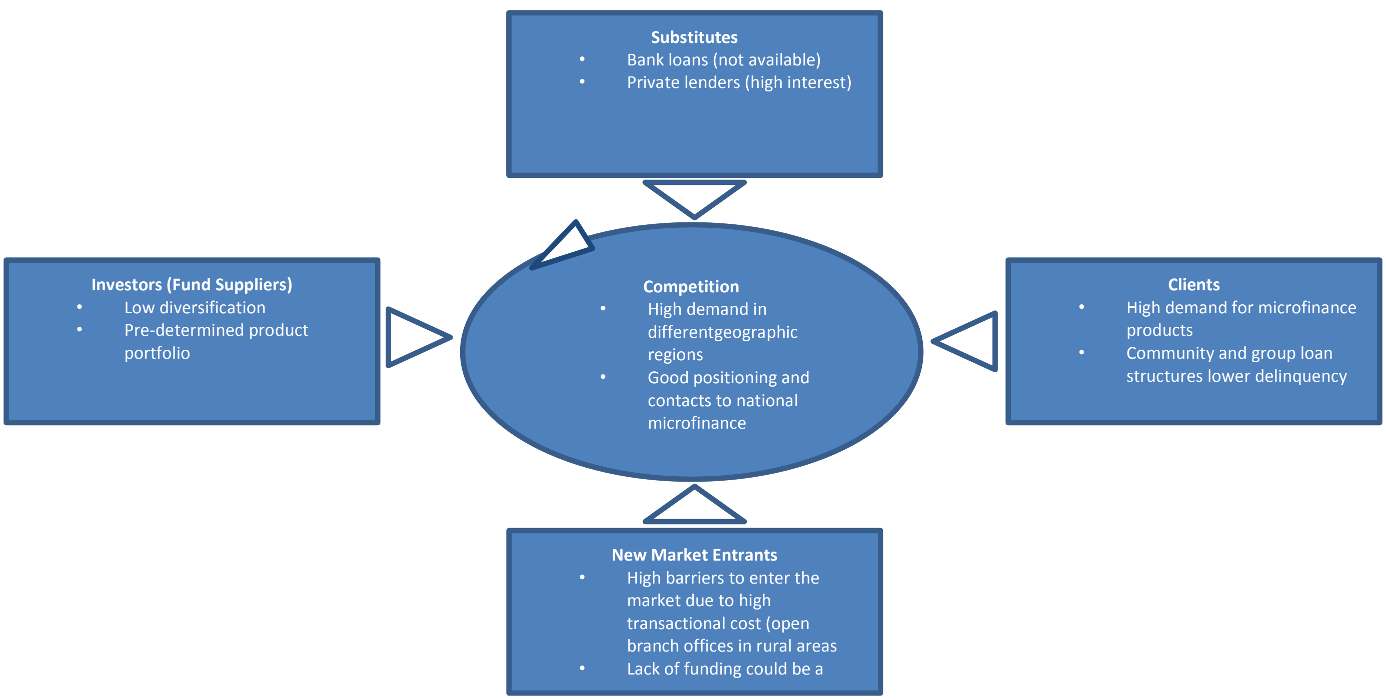


Figure 2: Porter´s Five Forces

1.4 Macroeconomic and Political Environment

1.4.1 General Statistics

POPULATION STATISTICS	
Population Size (2012)	25,241,998
Population growth (2010)	2.4%
Religion (2000)	Christian 68.8%, Muslim 15.9%, traditional 8.5%, none 6.1%
% urban population (2010)	51%
Rate of urbanization (2010-15 est.)	3.4% annual rate of change
Human Development Index	
HDI ranking (2012)	135
GDP PPP (2011 est.)	$3,100
Literacy rate (2000)	57.90%
life expectancy (2012)	64.2 years
Government and Economy	
Government type	constitutional democracy
Business environment rank	63rd
Anti-Corruption rank	69th
Growth (2011 est.)	13.50%
Inflation	8.8% (2011 est.) versus 10.7% (2010 est.)
Poverty Indicators	
1 dollar a day	30.10%
% share of GDP of 4th quintile	5.70%
Gini coefficient - out of 100	39.40

Table 1: Population statistics

1.4.2 Political environment:

Ghana gained independence in 1957, but democracy failed to manifest and Ghana became a single party state in 1964. Several decades followed with shifting ruling systems as democratically elected governments were quickly overturned by a series of military coups. Since the re-formation of political parties in 1992, Ghana has, however, experienced political stability and post 1992 the country has seen 2 peaceful transfers of power between parties solidifying Ghana's status as a functioning democracy.

1.4.3 Macroeconomic environment

1.4.3.1 Growth

Over the last 3 decades, the state of the Ghanaian economy has shifted dramatically. 28 consecutive years of growth averaging above 5 % annually has seen Ghana rise from a low income country to a middle income country. Recent growth rates have been especially encouraging with a 2011 initial growth rate estimates of 13.5%, making Ghana the fastest growing country in the world in 2011. While future growth rates are not expected to reach the levels of 2011, growth rates above 5% are still predicted in the foreseeable future.

While economic growth has been impressive, the growth has largely been driven by primary goods, oriented towards the global markets. In 2011 agriculture made up around 30 % of GDP and occupied 50 % of the labor force. Other major exports are gold, cocoa, timber, aluminum, manganese ore and diamonds[2]. Recent developments have solidified Ghana's economic situation, but also reinforced Ghana's reliance on commodities for economic growth. Firstly a newly discovered oil field contains 660 million barrels of oil, with oil revenues projected to commence in 2013. This discovery could add up to 7% annual to the Ghanaian´s GDP. Furthermore, Ghana is the 10th biggest producer of gold worldwide producing 92,380 Kg per annum.[3] The Ghanaian economy should thus benefit from the 17.5% annual increase in the gold price we have seen between 2007 and 2012.

1.4.3.2 Inflation

One of the main dangers facing credit issuers in Ghana is the inflation volatility. Since 2009 inflation has fallen by more than 10 %, decreasing from 19.30% in 2009 to 8.8% in 2011. While this in itself is a positive development, investors should be cautious of a longer term trends of high inflation volatility with a yearly volatility of >5%. The historic interest rate volatility suggests that there is a substantial risk of microfinance loan portfolios being eroded by inflationary pressures. In an extreme situation a 2 standard deviation upward movement of inflation would decrease the real value of a loan with a 5 year maturity by 25-35%. The risk is especially acute as 2012 is an election year, which historically has resulted in large fiscal and monetary expansions, leading to significant boosts in inflation. This was the case in the period around the 2008 (albeit with a different party in government), resulting in a jump in inflation in the period of 2007-2009 of 8.60 %.

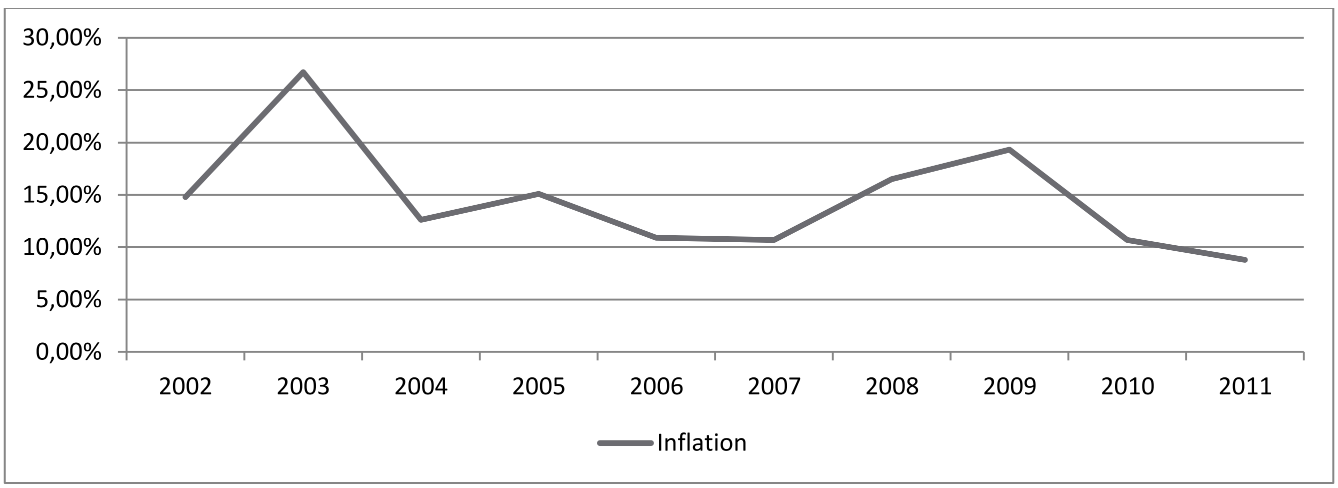


Figure 3: Inflation over time (Source: International Monetary Fund – 2011 World Economic Outlook)

1.4.3.3 Fiscal deficit

Another economic indicator that tends to be affected negatively in election years is the fiscal deficit. During the 2008 campaign the fiscal deficit increased from 5.8 to 8.3 % and it was still 4.7% by 2011. Whether a similar spike will be seen in this election cycle is hard to predict, but the possibility should certainly not be excluded. An increase in the budget deficit would add to an already growing fiscal deficit, and while the present debt to GDP

[2] https://www.cia.gov/library/publications/the-world-factbook/geos/gh.html
[3] http://www.bgs.ac.uk/mineralsuk/statistics/worldArchive.html

ratio stands at an acceptable 41.4%, another half a decade with high fiscal deficits could lead to significant increases in the demanded yield by foreign investors.

1.4.3.4 Current account

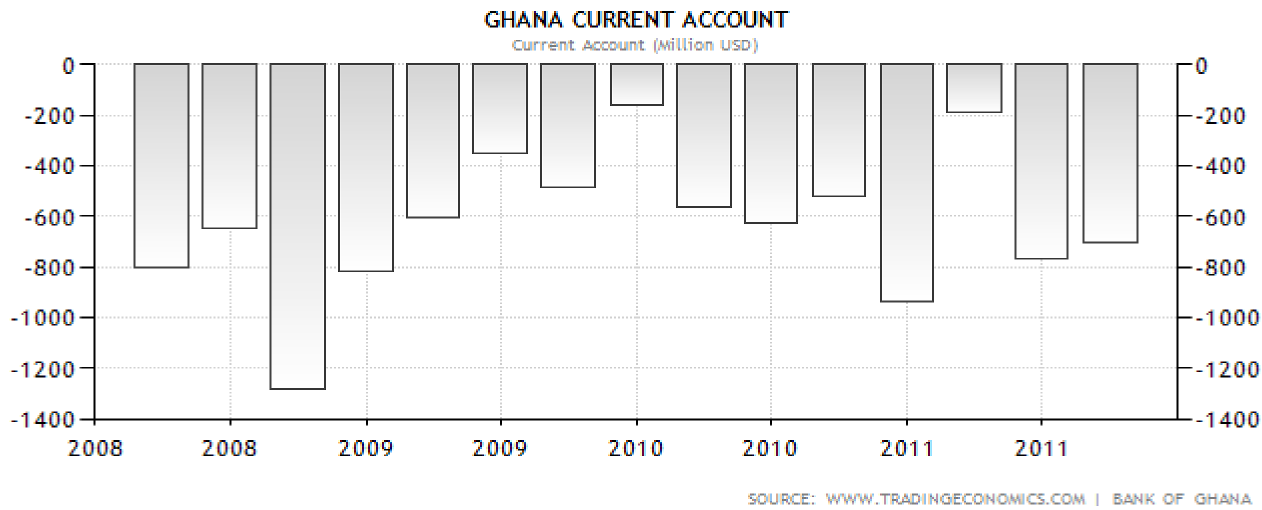


Figure 4: Current Accout of Ghana over time

In the last 5 years Ghana has consistently had a current account deficit, which peaked at around 1300 million dollars in the third quarter of 2008. We do not, however, believe that the current account deficit should be seen as an outright negative indicator of the Ghanaian economy. Instead the CA deficit seems to be an indication of international investors seeing the upside potential of the Ghanaian economy. While this could result in a crowding out effect of good investment possibilities in some sectors, we do not see capital demand in the microfinance sector as being anywhere near saturated.

1.4.3.5 Distribution of economic resources

The economic growth in Ghana has coincided with a large part of the Ghanaian population leaving absolute poverty. In the years 1992-2006 the fraction of the population living on below 1 dollar a day decreased from 51.1% to 30.0%[4]. The decrease in poverty, however, masks an increase in regional inequality. The South has prospered, whereas large parts of the more rural Northern population have been left largely untouched by the economy growth. In the period 1992-2006 the poorest quintile of the population (a large part of which can be found inland) experienced a decrease in its share of national income from 6.7% in 1992 to 5.1 % in 2006, leaving their GDP per capita largely unchanged.

1.4.3.6 Migration

The divergence in economic fortunes of the different regions has resulted in significant migration patterns. Much of the young population are leaving rural areas and migrating towards the cities (especially Accra). At present 51% of the population live in urban areas, but if trends continue, around 65% of the population will live in cities by the end of 2015. The extreme migration patterns could lead to serious negative consequences both in rural and urban

[4] http://www.indexmundi.com/ghana/income-inequality.html

areas. Rural areas will lose much of their working population, and urban areas will see an 35-45% increase in population over the next 4-5 years, which could put serious pressure on an already overburdened infrastructure.

1.5 Other Environmental Factors

1.5.1 Investment climate for microfinance

In the IMF yearly report on country specific business environments Ghana scores highly compared to its regional competitors. Across 10 categories Ghana gets an overall rank of 63rd globally, but with significantly better scores for investor protection and contract enforcement. In comparison, Nigeria is its closest regional rival with an overall ranking of 133rd, reflecting a markedly poorer performance across most indicators[5].

The relatively high ranking has happened through significant improvements in the investing climate over the last decade: When looking at the graph in appendix 1, Ghana has in the last 7 years clearly shown willingness to improve governance through progressive reforms. Most indicators have improved and international organisations generally agree that the Ghanaian government has been progressive in its attempt to implement recommended reforms. Unfortunately much of Ghana governance reforms came under the previous administration (2005-2008). The outcome of the 2012 election accordingly seems pivotal in determining future governing reforms.

Similar findings can be found in levels of corruption, where Ghana is also vastly outscoring its geographic neighbours in terms of creating efficient governance for business. Ghana is globally the 69th best country having corruption levels comparable to those of Macedonia, Turkey, and Latvia, but markedly lower levels of corruption than their neighbours in West Africa[6].

Fundamentally the Ghanaian economic climate is positive. It has continued high growth potential in a world economy that see limited short term growth potential elsewhere. From a fiscal perspective the government has a steady income stream in the foreseeable future through the exploitation of its oil reserves. Furthermore Ghana is a democratic country with a good business environment compared to its regional rivals. All in all we project that the above factors will result in a steady wealth transfer to the poorer electorate over the coming decade, which suggest an ideal investment climate for microfinance institutions.

[5] http://www.doingbusiness.org/~/media/fpdkm/doing%20business/documents/profiles/country/GHA.pdf
[6] http://www.transparency.org/country#MLI

2. INSTITUTIONAL SET-UP




2 Institutional Set Up

In the following section we analyze the institution's governance and management structure. Furthermore, we look at the human resources management and information technology in use. Finally, we evaluate the auditing practices and internal controls of the company.

2.1 Ownership and Governance

The KRABAN Support Foundation is a Financial-NGO with the legal status of an NGO. The company is owned by three "subscribers" or shareholders, namely Nana Opare Djan (CEO & Board Member) with 50% of the capital, Kofi Boakye Yiadom (Guinness Ghana Breweries Distributor, Kumasi) with 35% of the capital and Hilary Grace Wobil (Company Matron, Akosombo Textiles Limited) with 15% of the capital. Hilary Grace Wobil is also a member of the company's board. In the last financial year, there have been no changes in the composition of the ownership.

The board is the main body of the company, planning future activities and coordinating operations. It meets quarterly. The CEO, who is a member of the board without voting rights, will take action according to the board's decisions. The company changed its board in the last financial period and added 2 new members. Another member was replaced. The seven board members are introduced in detail in appendix 2. The changes were made to diversify the board and to add members with different backgrounds. Some of the board members have experiences in the financial sector. Board members can serve for two consecutive periods of 4 years.
Alongside the board, there is a "Committee of Trustees on Credit" ("COTC") that comes together every two weeks or "when needed". The committee is responsible for monitoring any decisions concerning the credit business and is a sub-committee of the board, consisting of four members. Again there is a mixture of members from the management team and the board, creating a nontransparent governing structure. The COTC approves the loans according to a Credit Policy Manual (which we have not seen yet). After the client groups submit their application to the branch offices for review and appraisal. After the COTC approves the loans, funds are given out.

The Addition of new members to the Board tells us that KSF was responsive to last year's group report, who recommended this move. Furthermore, the fact that one of the clients was added to the board is very positive.
Despite not having a right to vote, the CEO, however, seems to have strong influence on the board discussions and decisions. Keeping in mind that he is the major shareholder of the company, the independence of the board is consequently partly put into question. Furthermore, we were not able to confirm the existence of the COTC, since we could not look into meeting minutes. During meetings with various board members, we had the impression that the institution's vision is clearly shared by all members, which we find very positive.

Recommendations

- While we see a very positive development of the company in terms of governance issues, we believe board meetings have to be more effective, meaning the board has to evaluate the progress of the institution by setting measurable objectives and documenting of whether they are achieved or not.
- The separation of board and management is still not rigid enough. The CEO still has too much influence, creating key person risk and conflicts of interest due to the ownership in the company. Further diversification in the composition of the board members is desirable, especially with respect to investor acquisition.
- In order to verify board minutes, they should be signed by the board members on every page.

- The Committee of Trustees on Credit remains a black box to us. A transparent governance structure requires a clear mission of the committee, criteria for the member selection, fixed periods for meetings – in short: clear structures.
- The procedures for the board of directors should further be formulized in order to create more transparency for investors and to insure against the loss of key persons in the organization. Record keeping of all meetings is of the utmost importance. We recommend a manual that KSF can adapt to their unique needs but which we believe will make the board more effective.[7]
- The board must set targets for the institution that outside interested parties can understand and see whether they have been accomplished or not. This adds to the value of good governance by holding the board accountable and thereby helps to attract funding.

2.2 Management

KSF's management is headed by its founder Nana Opare Djan, who is also on the board of the institution. The table in appendix 3 gives an overview of the management structure.

During our visit to the institution we had the chance to meet with some members of the management team. Nana Opare Djan, the company's CEO has close to 15 years of experience in the (micro-) finance industry. He has an extensive network in Ghana's microfinance industry, being the general secretary of ASSFIN. This is of major importance, since ASSFIN interacts directly with the Bank of Ghana. Nana Opare Djan is hence playing a key role in the accreditation process that is currently in progress. A process which aims to make FNGOs regulated. Furthermore, Nana Opare Djan helps less developed FNGOs in building up capacities for their future endeavors.

Another key actor in KSF is Emmanuel Aboagye who plays a major role in managing the institution. The 36 year old employee has completed studies in Ghana and has taken part in conferences abroad. The administrative and financial management seems to be largely covered by him. Mr. Aboagye is also involved in the preparation of the strategic business plans, making him a key addressee for board members.

Other management team members are listed in the appendix 3. During our visit we were not able to verify their positions. The management and human resources plan going forward can be found in the business plan chapter later in the report.

In general, we see a very high capacity of the key management staff to develop the organization in the future. KSF's management is very well connected to governmental bodies and the national FNGO organization. While we see a positive development management setup, e.g. the additional training of Mr. Aboagye abroad, the issue of key person risk has not been resolved so far. Considering the importance of the CEOs network and contacts, we see a key person risk in Nana Opare Djan. Without the CEO, it is our opinion, that the organization would not be able to perform its core business. Mr. Aboagye is clearly also a key person in the organization and therefore bears a key person risk.

[7] http://www.mfi-upgrading-initiative.org/downloads/sampleboardmanual.pdf

Recommendations

- Formulize clear operational procedures on all organizational levels that enable the organization to react to changes in its management/ leadership structure, thereby reducing key person risk. This is especially important for the CEO/ OIC levels.
- Increase transparency for investors by clearly formulating the respective responsibilities of each management team member as well as board members.
- Further strengthen key managements' capabilities with regards to reporting and transparency. We believe Financeros sin Fronteras (FsF) could provide training on this matter.

2.3 Organizational Structure

Appendix 4 shows the organizational chart of the company. The headquarters of the organization are in Accra, hosting the company's management and administrational staff. KSF operates two branch offices, one in Somanya and another one in Takoradi. Both branch offices are led by a branch operations officer who is in steady contact with the headquarters. The branch offices are treated as cost centers. The management team regularly visits the branch offices and the communities they lend to. Due to conditions placed on KSF by current investors, the company is required to use its funds for specific regions and communities. The branches were chosen according to the requirements set by the investors.

During our field visits it became clear that the people in the communities knew the management as well as the field staff – showing that the management staff, as well as the field staff, interacts with their clients in the villages.

Due to the location of the communities, there is no other way than to have offices in the same area. We therefore see the efficiency requirement as satisfied. The lack of a proper IT system makes the information transfer rather difficult, increasing costs in the long-term. However, introducing an IT-system in communities and branch offices that rarely have access to electricity is quite difficult. Overall, we think that the organizational structure is sufficient and ensures accountability of the staff.

The current staff level meets the client demand. Future expansion plans can, however, only be realized by adding new staff. The business plan section covers this topic in more detail. While we were able to meet some credit officers during our trip to Ghana, it remains unclear to us, how often the management team meets with the staff of the branch offices. The bi-weekly meetings of credit officers with the communities were independently confirmed by credit officers and clients. We think that the organizational structure meets the requirements. Improvements are needed in the management of the organization.

Recommendations

- See "2.2 Management"

2.4 Human Resources Management

HR management is delegated to a separate officer (Millicent Asantewaa Donkor). She is in charge of a somewhat extensive HR policy. Job descriptions are updated, documented, and known to personnel. KSF also has established personnel policies, and procedures are in place and known to personnel. We had the impression during our visit that the salaries of the staff are rather low. Its policies and procedures outline a slim organisational structure in order to cut costs. Furthermore, we do not know the extent of communication of the CEO (management) with all staff members.

We have, however, not seen documentation concerning start-up training. Neither have we found evidence for continual job performance evaluation systems, such as evaluating the monitors absenteeism, client retention and general morale of individual employees.

Recommendations

- HR policy is significantly important because the way an institution treats its employees reflects how it treats its clients. This is something potential investors will notice. KSF should implement confidential employee surveys which will be handled by a third party, e.g. FsF, to give feedback to the board.

2.5 Information Technology

KSF has a standard level of computer services. The institution has a responsible IT officer that reports directly to a CEO. KSF uses Microsoft Office to store and handle most data. We saw no evidence of a direct interface between branch data (which is often handwritten) and central data. From our experience the level of data updates are rather infrequent, which makes it more complicated to quickly identify regional irregularities in payment schedules. We do, however, believe that data gathered has adequate back up and is mostly existent online. The overall assessment of the IT level is that KSF has a basic but somewhat adequate level given its needs.

Recommendations

- Free online systems of data-sharing such as dropbox should be implemented as this creates a timelier and more efficient dataflow between headquarters and the local branches. Furthermore, better organization of data is desirable as it would increase financial transparency and thereby increase attractiveness of the institution to outside investors.
- There is free software, tailored to the needs of MFIs. One example therefore is MIFOS, which provides software solutions for reporting and is open source. Since reporting is one of the main issues we identified at KSF, we highly recommend the introduction of this software.[8]

2.6 Internal Controls

Many of the institution's key policies and procedures are documented in manuals and have been updated. Personnel are, as far as we could verify, aware of these manuals and use them in their day-to-day operations. The incentive system has some deficiencies, as do the institution's accounting system and control policies and procedures, which could all be made more efficient. Generally we believe the internal controls system has improved from the last report, but the high rate of delays in the loan portfolio suggests that KSF should introduce better operational credit controls. Furthermore, KSF due to its reliance on foreign donors have liquidity gaps that require a postponement of credit to existing borrowers.

[8] http://mifos.org/product/download-mifos/business-intelligence-suite

Recommendations

- We still recommend formulizing internal manuals for job descriptions, payment management, planning and budgeting, accounting principles and the acquisition of fixed assets
- We recommend that a stricter cash on hand policy is introduced by the treasury to prevent future liquidity crises

2.7 Internal Audit

The small size of KSF means that an autonomous body of internal audit is not in existence.

Recommendations

- An external auditor could help develop an internal auditing structure, thereby improving the accounting processes in the Accra headquarter

2.8 External Audit

The MFI has an annual external audit. The Auditor issued an unqualified letter supporting the financial statements, stating that the financial statements reliable and publicly available and the MFI adhere to generally accepted accounting standards.

The financial statements are audited by K. Kye & Associates, a chartered accounting firm to the best of our knowledge. On May 16, 2012, the head of this firm was considered a “member in good standing” by the Institute of Chartered Accountants (Ghana). [9]

Recommendations

- We recommend that an official policy of auditor rotation on a three-year basis is introduced and that investors are clearly made aware of this policy, as this would minimize outsiders perception of risk associated with doing business with KSF.
- The external auditor must sign all pages of the audited report in order to assure the correctness of the statements to potential investors. We recommend the external auditor be made available to next years’ FsF group for communication.

2.9 Regulation and Supervision

Historically microfinance institutions have had very limited government oversight. Especially FNGOs have had free hands with little consumer protection. Currently, however, a new framework is being put in place that allows for FNGOs to be regulated and achieve the status as a regulated MFI. KSF would qualify as a Tier 3 institution. From the information that we have seen, KSF is in the later stage of this process, having engaged in a positive and sustained discourse with the Bank of Ghana. The new legislation will require KSF to have 10% capital adequacy ratio, which we believe is a) achievable and b) desirable for KSF, as we believe it would improve their business model.

[9] The Institute of Chartered Accountants (Ghana), Members in Good Standing, www.icagh.com, May 16, 2012

During our visit, the management showed us the application documents and correspondence with the regulatory body. Due to the CEO's position in ASSFIN, he showed great knowledge about the process.

2.10 Ratings

The 2011 report from IE business school was the first external rating report carried out specifically to rate KSF. We see this report as a very thorough investigation into workings of KSF. From 2011 to the present report we can also see a marked improvement, which suggests that KSF is making a genuine push to improve its performance and transparency to investors. The financial part of KSF, however, still weighs down its ratings and should be addressed quickly. Furthermore, the overall transparency in the organization still has to be improved.

Recommendations

- We recommend that KSF continues its current policy of a) transparency to outsiders and b) dialogue and implementation of recommendations as this has clearly moved KSF in a positive direction.
- In Ghana, we met with management to discuss their previous year's CAMEL score and touched upon areas of improvement. They should continue to focus on areas for improvement as the CAMEL analysis is a widely recognized rating system for MFIs. With that said, FsF is currently developing their own rating system for FNGOs, as the CAMEL analysis is more suited to mature MFIs.

2.11 External Relationships

As a FNGO, KSF has limited availability to raise capital at a sustainable price. KSF has therefore historically been reliant on foreign donors for capital. This hurts KSF's CAMEL rating as many of these donors have policies for granting capital that are institutionally specific and none-transparent, and which include subsidies if certain criteria are met. This means that KSF can lower its interest rate below what would otherwise be financially viable, which is positive for the local community, but means that KSF struggles in the financial aspects of the CAMEL. The reliance on donors for capital also means that KSF is exposed to withdrawal/expiry of these funds, which often leads KSF with a shortage of cash to hand in periods between grants.
Gaining access to market rates on loans would help reduce KSF's reliance on foreign donors and would therefore help in increasing KSFs financial independence. Becoming a regulated entity from the Bank of Ghana will mean that KSF will find it easier to access capital markets, leading to a more financially sound and sustainable institution. As described above, the organization has also good relationships to regulatory bodies through the position of its CEO at ASSFIN.

Recommendations

- Achieve a level of financial transparency that will allow the company to gain access to long term stable loans, so as to minimize the risk of exposure to foreign investors discontinuing their capital investments.

2.12 Chapter Conclusion

While we see improvements in the governance and management structure of KSF, overall transparency could be improved, leading to increased chances of acquiring new funds. The recommendations we made therefore mainly target the lack of transparency in the organization as well as the key person risk that results from non-existing operational guides.

3. FINANCIAL VIABILITY & RISK MANAGEMENT

3 Financial Viability and Risk Management

Notice: The financial analysis built upon the work of the previous group. This was done on purpose as it is our hope subsequent groups can use our work to update and continue FsF's ability to serve MFIs. We adjusted, corrected and expanded the excel spreadsheet where needed and updated the current figures.

While KSF has audited statements completed by an accountant in good standing with the Ghana's *Institute of Chartered Accountants* there are significant discrepancies within the audited financial statements. Below are some of the more striking examples:

- For 2011, Assets do not equal Liabilities & Equity (a USD 12,544 difference).
- In the Balance Sheet, the *Cash* account in the 2010 and 2009 statements does not match the footnote figures.
- In the Balance Sheet, the *Accruals* figures are missing for 2010 and 2009 in the statements, but appear in the footnotes.
- In the Income Statement, *Financial Revenue from Loan Portfolio* is broken down into two categories, interest received on loans and *Fees-Clients Registration/Membership*. The 2011 revenue is overstated 6%.
- In the Income Statement, *Personal Expenses* are severely understated in 2011 compared to the footnote figure ($7,815 instead of $36,833).
- In the Income Statement, *Other Administration Expenses* is severely understated in 2011 and 2010 compared to footnote figures.

In addition to the above mentioned examples, other accounting peculiarities exist. For example, Business Development (BDS) Fees are non-cash yet appear on the Income Statement. These figures represent the money KSF would have had to pay for facilities they used (classrooms, church halls, town halls, etc.) but they negotiated with the owner to use them for free. The CEO did say they received invoices for these. If this is the case, the accounting treatment would mean they have to recognize the invoice and create a liability for it, and until the owner or supplier also recognizes KSF does not have to pay, only then can KSF write off the liability (no effect to P&L). Additionally, *Director's Contribution* is another account in the Income Statement that is non-cash. This account entails services given by members of the Board, services including training staff, preparing manuals, etc., without any fees charged. The bottom line is that these non-paid fees should not be recognized as income.

Furthermore, the Cash Flow Statement in the 2011 Audit Report contained figures that did not make completely sense and we were not able to decipher where they came from. This is mainly due to the discrepancies noted above and the lack of footnotes for items in the CFS. Furthermore, much information that was needed for building a correct CFS was not available to us, yet, in the future we would like to expand on this by collaborating with KSF to create and understand together a working cash flow statement.

Analyzing the statements involved looking at their actual statements in the Audit Report, adjusting them using the figures in the footnotes, utilizing the conservative principal (we take the higher figure for expenses and lower for revenues. In addition to this, we also completed the ACCION CAMEL analysis. Below is a summary of the bottom-line impact of the Income Statement viewed from the 3 distinct perspectives.

USD	2011	2010	2009
As Reported in Audit			
Net Operating Income	6,953	22,730	(76,825)
Net Income	118,934	104,239	(4,880)
*Net Income	51,890	68,216	(34,965)
% of Donations for *Net Income	87%	67%	
Conservative			
Net Operating Income	(56,976)	14,952	(45,569)
Net Income	55,005	96,462	26,375
*Net Income	(12,039)	60,438	(3,709)
% of Donations for *Net Income		75%	
CAMEL Adjusted			
Net Operating Income	(195,278)	(115,428)	(212,354)
Net Income	(111,979)	(69,942)	(170,494)
*Net Income less BDS Fees, Director's Contribution (non-cash items)			

Table 2: Differences in versions of the financial statements

3.1 General Information

The analysis here within considers the *conservative* actual statements. According to our analysis, in terms of profitability and efficiency, KSF as an institution is not profitable on an operating income level, posting an operating income loss of 56.9 thousand USD in 2011. After taking into account ACCION CAMEL adjustments, net operating income loss for 2011 is 195.2 thousand USD. The difference is primarily caused by adjustments made to the financial expenses (capitalizing subsidized debt) and the negative effects of inflation, especially upon equity. From the meetings we held with management, we believe they are committed to becoming a profitable company but that is a secondary priority behind fulfilling their social mission of empowering individuals and communities to better their lives and alleviate themselves from poverty.

KSF historically has utilized the following funding sources:

	Funding Sources	Interest Charged
1	Social Investment Fund (S.I.F)	12.5-18.5%
2	MiDA – ACPC	15%
3	Microfinance Small Loans Centre (MASLOC)/ASSFIN	10%
4	Ghana Commercial Bank (GCB)/ASSFIN	30%
5	EB ACCION Savings & Loans Ltd	30-38%
6	RHEMA Consulting Ltd	25-27%
7	KIVA Micro funds	none
8	Energy-in-Common	none
9	International Alliance for Women (TIAW)	none
10	People Helping People International (PHP)	none

Table 3: Historical funding sources

The MFI has grown its total loan portfolio by 30% from 2009 to 2011, although it slightly decreased (1%) in 2011 from its 2010 value. The chart below provides a snapshot of the overall evolution of its loan book, which makes up more than 90% of KSF's asset base.

LOAN PORTOFLIO BREAKDOWN	2011	% Growth YoY	2010	% Growth YoY	2009
Current Loans (< 30 Days)	767,052	-14%	889,967	33%	667,307
% of Gross Loan Portfolio	65%		74%		73%
Rescheduled Loans (Current)	113,662	1%	112,216	-4%	117,138
Loans Past Due (1-30Days)	108,046	56%	69,280	-4%	72,095
Loans Past Due (31-90Days)	155,781	63%	95,843	145%	39,042
Loans Past Due (91-180Days)	36,177	82%	19,916	99%	9,997
Loans Past Due (>181Days)	7,232	-27%	9,866	8%	9,108
Loans in Legal Recovery (<180Days)	0		0		0
All Non-Current Loans as % of Gross Portfolio	35%		26%		27%
Total (Gross) Loan Portfolio	**1,187,951**	-1%	**1,197,087**	31%	**914,687**
Allowance for Loan Loss	(100,508)	22%	(82,688)	1%	(81,527)
Allowance for Loan Loss % of Gross Portfolio	8%		7%		9%
Net Loan Portfolio	**1,087,443**	-8%	**1,175,708**	36%	**861,901**

Table 4: Loan Portfolio Breakdown

A worrying trend has been the growth in percentage of all non-current loans (includes rescheduled) against the *Gross Loan Portfolio.* In KSF's most current Strategic Business Plan (October 2011), they cite a study conducted by the Bank of Ghana and Ghana Microfinance Institutions Network (GHAMFIN) in 2004 and re-assessed in 2010 by Support Programme for Enterprise Empowerment and Development (SPEED) Ghana in 2010 indicated that Kraban Support Foundation has been placed in the peer group of "Medium FNGOs" in Ghana. KSF cited conclusions of the study:

> *"Kraban (KSF) demonstrates a level of profitability that is lower than the average of its peers and the average of all RMFI participants: its adjusted return on assets (AROA) is -22%, compared with -19.1% for its peers and -0.07% for all RMFIs on average. Its adjusted return on equity (-23%) is similar to its AROA, lower than both its peer average (-26.88%) and the average of all RMFI participants (14%). It is 100.7% operationally self-sufficient (OSS) and 49.9% financially self-sufficient (FSS), compared to 88.2% OSS and 54.7% FSS for its peers and 123% OSS and 100.29% FSS for all RMFIs on average. The nominal yield on Kraban's gross loan portfolio (22%) is less than that of its peers (35.5%) and for all RMFI on average (40%)."*

More information on that study can be found in their Strategic Business Plan. In addition to that study and this report, KSF also works with Mix Market, one of the preeminent international microfinance monitors of MFI's, conducting analysis on financials as well as social performance.[10]

Recommendations

- Improve the efficiency of KSF financial bookkeeping and ability to generate key reports for the benefit of interested outside parties such as potential investors. We suggest a basic course on Microsoft Excel, many of which are free and available via the Internet. We suggest this because the financial statements contain

[10] www.mixmarket.org/mfi/ksf

more inputted figures than formulas. For example, the total amount from the footnote for administrative expenses should connect directly to the Income Statement. The summations in the statements should actual be the SUM formula and not just a figure type into the cell. By using formulas instead of just numbers, this will make it easier to understand how the sections (statement and footnotes) are connected and to make what should balance does in fact balance.

- It is essential that KSF begin to use financial ratio analysis, defined as the "Computation of analytical ratios from financial statements and interpretation of these ratios to determine their trends as a basis for management decisions. There is a great source from the Consultative Group to Assist the Poor (CGAP), which provides all the essential ratios for MFIs and how to calculate them. It can be found on the CGAP website.[11] By tracking the ratios commonly used to judge the efficiency and sustainability of MFIs, KSF will know benefit from knowing its strengths and figure out how to improve its weaknesses.

3.2 Financial Statement Analysis

Notice: The USD figures were translated from Ghanaian New Cedi FX rate of 0.64746:1 USD (2011 average, source: oanda.com)

While KSF produces financial statements following the accrual accounting method, as mentioned before, the quality and clarity of the financial statements are lacking. Given this lack of clarity, we have had to use our professional judgment in considering some aspects of the financials. All financial statements can be seen in the appendix 5; thereby we show three different versions of each statement (Actual Audited Statements, Actual Audited Statement with Conservative bias and CAMEL adjusted financial statements).

3.2.1 Income Statement Analysis

As mentioned above, we took a conservative approach and inputted the larger figures for any expense discrepancies. This report will cover in detail the actual statements, and briefly touch upon certain sections of the CAMEL analysis.

Total (gross) income has declined since 2009, primarily due to fallen interest revenue on the loan portfolio. While it's understandable that 2011 was a worse year than 2010 considering the *Net Loan Portfolio* was smaller, a 60% decline in revenue is severe. Furthermore, 2009 was such a better year than 2011 even though the *Net Loan Portfolio* was 21% smaller in 2009. The CEO, Nana Opare-Djan explained the lower revenues:

> *"Net Income was generally low in 2011 due mainly to the increase in macroeconomic indices in Ghana especially high cost of fuel and the attendant high cost of operational expenditure. The organisation's field operations increased due to the MiDA agricultural value chain program. Also because the MiDa program was a long-term interest yielding facility, we did not receive income from farmers immediately in year 2011. "*

From the chart below, we can see that unadjusted, key indicators while positive have not been stable (no trend) and shown no signs of steady improvement. This highlights the fact that one must consider the macroeconomic environment in which the MFI operates.

[11] http://www.cgap.org/gm/document-1.9.9603/FA%20summary%2008.pdf

Year	2011	Column1	2010	2009
Indicator	CAMEL Adjusted	Unadjusted	Unadjusted	Unadjusted
ROE	-22.4%	6.5%	13.2%	4.0%
ROA	-16.8%	4.6%	9.2%	2.8%
Operational Efficiency	6.4%	6.9%	1.4%	11.0%

Table 5: Key Financial Indicators

Unadjusted, *Total Expenses* have average 135% of *Gross Operational Income* since 2008. This highlights KSF's need for outside grants and donations to maintain its operations. Appendix 6 shows a chart with a breakdown of selected expense items. It should be noted that the *Provision for Loan Losses* makes up 23% of the *Total Expenses*, and as non-cash item it makes *Operating Net Income* look worse than it actually is, assuming of course actual write-offs do not exceed the provision.

Overall, issues exist on both sides of the P&L. The volatility in income, operational and financial expenses are too erratic (see appendix 7), suggesting either KSF's lack of efficiency in controlling all 3 aspects, or macroeconomic factors contributing to this volatility.

Additionally, while the overall loan portfolio has grown consistently over the years, the interest revenue derived from it has not. In fact, it should be noted that the implied interest rate by taking revenues from the loan portfolio divided by the *Gross Loan Portfolio* amount to a very low percentage, suggesting either large amount of late payments/defaults or something else.

	2011	2010	2009
Implied Interest Rate on Gross Loan Portfolio	4,4%	10,9%	10,2%
Implied Interest Paid to Funding Sources	2%	6%	6%

Table 6: Implied Interest Rates

Recommendations

- We recommend KSF create a document summarizing the major factors related to interest revenue and expense, what causes the fluctuations and how to address them. We believe operational expenses are an issue to the extent that low revenues from the loan portfolio are. If KSF can fix the revenue side of its Income Statement, this is likely to be effective tool to improve expense ratios.

3.2.1.1 Earnings

Turning to the *EARNINGS* portion of the CAMEL, this section of the analysis considers 3 quantitative items (ROE, ROA, and Operational Efficiency) and 1 qualitative item (Interest Rate Policy).

- **Return on Equity (ROE):** Measures the ability of the institution to maintain and increase wealth through income from operations. Primarily due to adjustments made in the CAMEL provisions of the loan portfolio and the effect of inflation upon equity, ROE in 2011 for KSF was -22.4%.

- **Operational Efficiency:** Measures and monitors progress toward achieving a cost structure that is closer to the level reached by formal financial institutions. The total operating costs on the portfolio incurred by the institution are only 6.4% of the loan portfolio.

- **Return on Assets (ROA):** Measures KSF's assets ability to generate revenue. Again, the CAMEL adjustments to the loan portfolio and equity negatively, ROA was -16.8% in 2011 for KSF.

- **Interest Rate Policy:** Measures the extent to which the entity's management analyzes and adjusts the interest rate, taking into account the institution's loan portfolio, and the cost of funds, the goal of profitability, and the macroeconomic environment. A key indicator of sustainability for any MFI is the annual percentage rate (APR). This figure takes into account the costs incurred by the institution, its growth prospects and economic environment variables of the country where the activity occurs. The result gives a guide to the MFI about the average interest should be set to its products in order to become self-sustaining and less dependent on donations.

The APR result for KSF obtained by our analysis is 43.68%. Compared to their 30% average interest rate policy, we can see why a strong structural dependence of its operations on grants and donations. While KSF does have an interest rate determination tool, it does not cover important factors such as operational costs and nor a profitability target. More detail on this is found in the *Interest Rate Policy* section.

3.2.2 Balance Sheet Analysis

3.2.2.1 Assets

Net Loan Portfolio makes up +90% of *Total Assets* in every year. The portfolio has increased 26% since 2009, but was slightly below its 2010 peak in 2011. Other relatively significant assets are *Fixed Assets* (4% of total). The large increase from 2010 to 2011 ($6,697 to $53,137) is due to large additions in equipment, primarily office and vehicle equipment.

Short-term Investments account for 2% of all assets in 2011. In the chart below, we can see they produced $1,204 in revenue in 2011, a return of 6.2% from $19,424 invested. Not a bad return in many places, but due to the high inflation (roughly 9% in 2011) in Ghana the short-term investments are producing losses. *Net Loan Portfolio* accounts for 98% of the revenues in 2011, yet as stated before, the implied interest rate/ return of this is 4.9%, a very low return. *Cash, Fixed Assets* and *Other Assets* (detailed in the chart above) are not directly tied to producing revenue but add-value to the overall operations of KSF.

Total Assets grew 26% from 2009 to 2010, but only 2% from 2010 to 2011. This slow-down was due to a lack of additional funding. This helps explain why the *Net Loan Portfolio* did not experience high growth in 2011 like it did from 2009 to 2010. Assets historically have been funded by 28% debt and 75% equity.

In our opinion, KSF could improve the management of its assets. *Short-term Investments* are currently losing money; they should consider other alternatives to where they invest now. Finally, the underlying issue with the management of KSF's assets is its loan portfolio, which is not producing enough revenue to cover the company's overall expenses.

3.2.2.2 Liabilities

Funding sources make up 91% of the *Total Liabilities*. Some of the sources of funding due charge interest while others repayment is simply the principal amount. A breakdown:

FUNDING SOURCES	Outstanding Amount 2011	Interest p.a.
SIF/ARB Apex Bank	123.017	12,5%
KIVA Micro Funds	-	0,0%
ASSFIN/GCB Ltd	-	30,0%
ASSFIN/MASLOC	-	10,0%
MiDA /Bank of Ghana	99.495	12,5%
RHEMA	23.324	27,0%
Energy-In-Common	9.518	0,0%
EB-ACCION	11.006	38,0%
Bank of Ghana Official rates (short-term)		29,9%
Average local lending 12 months rate		30,5%
*Those not in bold charge no interest only return of principal		

Table 7: Funding Sources (please note that the interest rates are averages provided by KSF)

KSF does access commercial loans through MiDA/Bank of Ghana, ASSFIN/GCB Ltdd, RHEMA, and EB-ACCION. Since 2009, the weighted average cost of these funds has average 15.7%, and was 14.4% in 2011.

3.2.2.2.1 Liquidity Management

Turning to the *LIQUIDITY MANAGEMENT* portion of the CAMEL analysis, it assesses KSF's ability to respond to 1) decreased funding sources and increases in assets, and 2) payment of expenses at a reasonable cost.

- **Productivity of Other Current Assets:** This indicator focuses on management of current assets that do not belong to the loan portfolio, especially investments in short-term cash. KSF utilizes the use of its cash, bank accounts, and short-term investments by investing in accounts that provide the highest possible return while balancing the need to liquidate quickly if necessary. ACCION states that treasury management should be consistent with the liquidity needs of the institution for its operations. This indicator penalizes whether an entity's investments are very conservative or very aggressive. KSF's result was 49% for 2011, highlighting a very aggressive investment policy with respect to its liquidity needs.

- **Debt Structure:** This indicator analyses the composition of the liabilities of the institution, including the amount, interest rate, payment terms, and sensitivity to changes in the macroeconomic environment. The institution has a funding strategy that neither minimizes funding costs nor leads to an optimal structure. However, KSF can and does access commercial loans via the Ghanaian financial system.

- **Availability of Funds to Meet Loan Demand:** During our visit in May 2012 we learned that KSF had not received new funds for that year and therefore was currently unable to meet its client's loan demand or expand to new areas. During our field visits many clients were eager for another round of financing, but seemed to still be waiting for the new round of financing. The ability for KSF to diversify their funding sources will depend on their ability to become more transparent and organize data more efficiently.

- **Cash Flow Projections:** This indicator measures the extent to which KSF is successful in projecting their cash flows needs. The analysis seeks to determine if they have prepared with sufficient detail and analytical rigor, and whether past projections have been adjusted accurately to the inflow and outflow of money. KSF's cash flow management is based on past experience rather than cash flow projections. Due to its operation size, this probably sufficient but we high recommend they begin to input a process that analytical tracks cash flow movements and allows them to project them on a forward basis.

Recommendations

- KSF needs to implement a system that tracks cash flows and one where it is easy to understand by outside parties. The ability of potential investors to view cash receipts from repayment of loans and others sources, as well as expense receipts, is key in their ability to make a knowledgeable decision about whether to lend to KSF.
- Investments in other current assets must take into account the liquidity needs of the company. The methodology behind this must also be available to potential investors.

3.2.2.3 Equity

Sources of Equity	2011	*% of RE*	2010	*% of RE2*	2009	*% of RE3*
Total Equity	908,492		789,557		676,275	
Share Capital (Original Investors)	378,302		378,302		378,302	
Reserves	475,185		314,794		271,598	
Retained Earnings	55,005		96,462		26,375	
Directors' Contribution	38,361	70%	14,341	15%	15,775	60%
Grants & Donations	44,938	82%	45,486	47%	41,860	159%
BDS Fees	28,682	52%	21,683	22%	14,309	54%
Operating Income	(56,976)	-104%	14,952	16%	(45,569)	-173%

Table 8: Breakdown of Equity Sources

The sources of equity are varied, but come mainly from accumulated Director's contributions, Grants & Donations, and Retained Earnings. *Director's Contribution* was explained by the CEO as "Income that subscribers who are the Board inject into the business as part of their Corporate Social responsibility to support marginalized societies ... Directors contributing such monies don't expect any returns from organization." Yet as mentioned before, this account is also free consultancy work given by the Directors. KSF did not provide a breakdown of the account and how much, if any, is actual cash donations. Documentation or how the amount of *Directors' Contribution* is determined was not provided. *Retained Earnings* therefore, are primarily positive because of grants and donations.

Taking into consideration only operating revenues, grants and donations, (excluding BDS fees & Director's contribution) KSF has been able to only post positive Net Income in 2010 ($60,438) compared to losses in 2011 (-12,039) and 2009 ($-3,709). *Retained Earnings* have fluctuated year over year since 2008 and no clear trend is present, suggesting sensitivity to variable costs and ability to generate significant revenue from the loan portfolio.

As stated before, KSF's main goal is to be independent; to find funding partners that give them freedom to operate how they see most efficient. Their ability to achieve this goal rests upon their ability to generate revenues above expenses without reliance on donations and subsidized debt.

3.2.2.3.1 Capital Adequacy

Turning to the CAPITAL ADEQUACY portion of the CAMEL analysis, the objective is to measure KSF ́s financial solvency in order to determine whether the risks are adequately compensated with capital and reserves, so that they can absorb losses.

- **Leverage:** it is the relationship between weighted assets by risk level and its own equity. The observed KSF ́s ratio is 1.57 times for 2011. It is positive that the leverage is low because these entities are normally more exposed to bad debt, operating expenses are higher compared to other financial institutions and finally because the possibility for NGOs to attract new funds is more limited than of a commercial bank.

- **Reserves' Sufficiency:** Measures the extent to which the institution is able to absorb hypothetical future losses by loan portfolio impairments. The level of provisions made by KSF is 70.1% of those required by the model, taking into account the level of delinquency that KSF has for different periods.

- **Ability to obtain Capital:** Assesses KSF ́s ability to respond to a need to increase the equity in a given time. The institution is able to maintain its capital in real terms, but relies on donations from individuals, corporations and development institutions, which, in case of shortage, would adversely affect the entity.

Recommendations:

- KSF has improved its record keeping of loan disbursements, most notable using the aging schedule suggest by ACCION. We encourage KSF to become even more rigorous in its record, primarily through a breakdown of the total loan portfolio by the type of loans it consists of. For example, it would be interesting to know in detail the % breakdown of urban versus rural loans, the duration of the different loan types and the average duration of total loan portfolio. We suggest KSF to incorporate this level of detail in its already existing excel record keeping database.
- Regarding KSF's ability to mobilize a significant amount of private sector capital and obtain commitments of future capitalizations, we believe it would be useful for KSF to create an investment proposal that specifically covers a how KSF would use a hypothetical amount of money, for example, $20-50 thousand USD. Explaining to investors exactly how the funds would be disbursed and the overall timeframe for collection interest and principal repayments. Describing the life of a hypothetical loan would enlighten investors to how KSF plans to use the funds, gather repayment and principal, and finally repay back investors. In addition, we also realize this report itself also lends to providing potential investors with an idea of investing in KSF.

3.2.3 Asset-Liability Management

KSF does not incorporate a rigorous asset-liability management program. Therefore, we will only cover the section of the CAMEL analysis that deals with this.

3.2.3.1 Liquidity Management

Assesses KSF's ability to respond to 1) decreased funding sources and increases in assets, and 2) payment of expenses at a reasonable cost.

- **Productivity of Other Current Assets:** This indicator focuses on management of current assets that do not belong to the loan portfolio, especially investments in short-term cash. KSF utilizes the use of its cash, bank accounts, and short-term investments by investing in accounts that provide the highest possible return while balancing the need to liquidate quickly if necessary.

  ACCION states that treasury management should be consistent with the liquidity needs of the institution for its operations. This indicator penalizes whether an entity's investments are very conservative or very aggressive. KSF's result was 287% for 2011, highlighting a very aggressive investment policy with respect to its liquidity needs.

- **Debt Structure:** This indicator analyzes the composition of the liabilities of the institution, including the amount, interest rate, payment terms, and sensitivity to changes in the macroeconomic environment. The institution has a funding strategy that neither minimizes funding costs nor leads to an optimal structure. However, KSF can access commercial loans via the Ghanaian financial system.

- **Availability of Funds to Meet Loan Demand:** Although KSF currently has the necessary funds to meet its clients' credit demands, during our field visits many clients were eager for another round of financing, but seemed to still be waiting for the new round of financing. Additionally, KSF has made clear their own desire for more funding because they know there are additional areas that could grow their business, in-addition to re-investing in clients more quickly.

- **Cash Flow Projections:** This indicator measures the extent to which KSF is successful in projecting their cash flows needs. The analysis seeks to determine if they have prepared with sufficient detail and analytical rigor, and whether past projections have been adjusted accurately to the inflow and outflow of money. KSF's cash flow management is based on past experience rather than cash flow projections. Due to its operation size, this probably sufficient but we high recommend they begin to input a process that analytical tracks cash flow movements and allows them to project them on a forward basis.

Recommendations

- KSF needs to implement a system that tracks cash flows and is easy to understand by outside parties. The ability of potential investors to view cash receipts from repayment of loans and others sources, as well as expense receipts, is key in their ability to make a knowledgeable decision about whether to lend to KSF.
- Investments in other current assets must take into account the liquidity needs of the company. The methodology behind this must also be available to potential investors.

3.3 Financial Performance Ratios Analysis

Below is summary of key indicators reflecting KSF's 2011 performance.

2011 Ratio Analysis *(some data gather from MixMarket.org)*	Column1	Column2	Column3
Profitability & Sustainability		***Portfolio Quality***	
Operational Self Sufficiency (OSS)	47%	Portfolio-at-Risk (PAR) Ratio 30	17%
Financial Self-Sufficiency (FSS)	29%	Adjusted PAR Ratio	22%
Returns on Assets (ROA)	(3%)	Write-off Ratio	N/A
Adjusted Return on Assets (AROA)	(17%)	Adjusted Write-off Ratio	1%
Return on Equity (ROE)	6%	Risk Coverage Ratio	50%
Adjusted Return on Equity (AROE)	(22%)	Adjusted Risk Coverage Ratio	75%
Asset/Liability Management		***Efficiency & Productivity***	
Yield on Gross Portfolio	4%	Operating Expense Ratio	9%
Portfolio to Assets	99%	Adjusted Operatin Expense Ratio	23%
Cost of Funds Ratio	7%	Cost per Active Client	13.46
Adjusted Cost of Funds	27%	Adjusted Cost per Active Client	34.29
Debt to Equity	32%	Borrowers per Loan Officer	668
Adjusted Debt to Equity	33%	Active Clien`ts Per Staff Member	9,606
Liquidity Ratio	67%	Client Turnover	
		Average Outstanding Loan Size	
		Adjusted Outstanding Loan Size	
		Average Loan Disbursed	148

Table 9: Ratio Analysis for 2011

3.3.1 Profitability and Sustainability

From the ratios, we can see that while ROE is positive at 6%, but adjusting for subsidies and donations, the figure comes to -22%. This again reemphasizes the institutions reliance on subsidized funding, grants and donations. Two other data points drive this point, financial self-sufficiency, only at 29% and operational self-sufficiency at 47%.

Trends in the portfolio quality suggest that lending requirements are not strict enough, as KSF has an adjusted PAR >30 days of 21.6%. Combined with a this high PAR is the fact that revenue from the portfolio is very low, suggests that KSF must raise interest rates it charges to clients and adhere to stricter lending requirements. From the 2011 Strategic Business Plan report they state, "The loan recovery rate…increased from 95% in 2007 to 96.5% in 2011." KSF has not provided the average time it takes to recover these loans.

3.3.2 Efficiency and Productivity

Operating Expense ratio (total expenses / average gross portfolio loan) is 9%[12], 4% higher than the *Yield on Gross Portfolio*, again highlighting the fact that loan portfolio is not producing enough revenue to cover costs. KSF *must* raise its interest rate, or minimize loan past due dates, or finally cut expenses by becoming more efficient.

- We recommend further analysis on possibly higher interest rates charged to clients because a 4% yield seems very low for any normal lending operation.

Utilizing data from mixmarket.org, we analysed KSF against 24 of its peers in Ghana. KSF in terms of portfolio size is smaller than the average (+$4 million). In terms of financial revenue from assets, KSF at 5% is well below the average of 38%, suggesting accounting errors or high default rate. In terms of operating expense to loan portfolio,

[12] Note most of the data had to be obtained from Mix Market.

KSF at 5% is well below the industry average of 42%. It is not clear why this discrepancies on the revenue and expense sides are so large, but keep in mind that data from mixmarket.org is not 100% vetted (MFIs send their data to Mix Market), meaning it should be taken with a grain of salt. For a more detailed view on peer analysis, please see appendix 10.

3.4 Interest Rate Analysis

Please refer to section 4.3.5 Interest Rate Determination for analysis and recommendations.

3.5 Risk Management

KSF does not currently have a formal risk management program in place. We believe they understand the concept of risk management but how they handle their risks is based more upon experience than analytical rigour. We are not aware of any sensitivity analysis KSF conducts.

Regarding financial risk management, prior to this year, KSF was not using the portfolio breakdown recommended by ACCION. Furthermore, how the institution finally declares and records write-offs is not clear. How these actual write-offs affect the loan portfolio amount, the loan loss reserve, and the loan provision amount is also not clear.

Recommendations

- KSF needs to have more transparency with regards to the quality of its loan portfolio. There needs to be a system in place that captures the delinquency of loans. We recommend KSF utilize the handbook *Microfinance Risk Management Handbook*, by Craig Churchill and Dan Coster, published 2001. It is very comprehensive and available online: http://kb.trilincanalytics.com/upload/f5/f546502afcea3e5.pdf
- We also recommend a more basic course on basic financial management, available on MicroSave.org at http://www.microsave.org/toolkit/basic-financial-management-and-ratio-analysis-for-microfinance-institutions-toolkit
- A scorecard with specific performance indicators for MFIs should be introduced. There are many available on the internet.

3.6 Chapter Conclusion

KSF must put its financial statements in order. The discrepancies in the 2011 Audit statement between the figures in the actual statements and those in the footnotes would not be acceptable to potential investors. This should be KSF’s number one priority before all other actions. Transparency and clarity of financial figures is key for KSF to obtain outside funds to utilize as they see fit. In addition, more information regarding the loan portfolio, specifically breakdowns of interest rates charged per communities, loan loss reserve and provision records, and write-offs must be made available.

4. PRODUCTS




4 Products

4.1 General

As a Financial NGO, KSF offers a moderate range of products and services to their clientele. The most important component, financial loans are complemented with a variety of educational services to further achieve KSF's goal of poverty reduction. Financially, nothing extends beyond saving products so insurance and transaction accounts are not being offered. KSF typically finds funding partners for each of their products. The funding partners then decide how these products will be implemented (i.e. 50 loans in village XYZ for agriculture). A drawback of this is that KSF is sometimes unable to adequately address the needs of some clients. Also, the dependence on finding funding partners places limitations on how much KSF can expand since they are not yet independent in the sense that they fund their own products like a bank. This limitation can be seen by the fact that their total client base has fallen from 9,606 in 2008 to 8,017 in 2011. This decline in clients has occurred due to the lack of new funding which has made some loan renewals impossible. This also shows that KSF is unable to enter new communities in need with their current funding structure.

A key-driving characteristic of KSF's lending is achieving community solidarity through a group lending practice. For KSF, this offers significant cost-savings and increases their ability to lend to a large number of people. This also allows the targeted communities to pool together both their resources and manpower to achieve favorable outcomes. Individual delinquencies become the responsibility of the group, which creates an additional pressure element of not wanting to disappoint your peers. Such a growth structure is also highly appropriate for future growth opportunities as the marginal cost of adding large numbers of people is much lower than dealing solely with individuals.

KSF has a 'Community Animation Manual' used by staff when dealing with clients. This is distributed to community leaders and summarizes all the products, loan terms, and regulations. It clearly outlines how groups should be composed and what the various positions of responsibility are. The 12 rules are covered in detail during the training period to ensure that all clients are aware of what the conditions are.

Given the small size of KSF, partnerships have been established with international organizations and other Ghanaian organizations to effectively market their products and provide appropriate training services. Within KSF, the loan and credit officers located in branch offices are responsible for initial marketing and outreach to communities. This includes handling the application process to find appropriate communities

KSF reaches their targeted communities through loan and credit officer staff in their two main branches. Each group must then appoint a Community Credit Animator (CCA) to be the main point of communication with KSF staff. Site visits revealed effective visual learning aids employed by KSF to explain aspects of the microfinance process. KSF products have a training period before any loan is actually issued to make sure the whole group understands the loan terms and how credit works. Additional info about the group selection process can be found in section 4.3. Due to the small size of KSF and constraints posed by funding, they are not able to serve the total loan demand in their target areas and marketing efforts are mostly by word of mouth.

Currently, KSF organizes groups into 4 categories. Each group should consist of a relatively socially homogenous group of people with all engaging in similar activities.

1. Production Groups

2. Marketing/Commerce Groups
3. Processing Groups
4. Storage/Inventory Groups

To match its mission, KSF targets the poorest who would otherwise not have access to any credit due to their geographic location and lack of formal collateral. As of 2011, 99% of their clients are in the *bottom half of population below the poverty line*, which is in line with their target demographic according to the 2011 Annual Report. As well, 89.73% of their total client base is female. However, it should be noted that during our two field visits clearly more than one in ten clients were male.

The structure of KSF's funding poses significant constraints on their operations. KSF receives large sums from few providers. Each of these providers has a specific goal (ie. geographic or social) and instructs KSF to act accordingly. This limits the ability of KSF to lend to areas where they feel they could make the most impact. Going forward it would be best for KSF to obtain unrestricted funding to ensure microcredit goes to where it is most needed and most effective. These partnerships also sometimes have resulted in duration mismatches for KSF. For example, Funding obtained from MiDA had to be repaid before the clients were able to cultivate their crops. This places significant pressure on funds as KSF is obligated to repay MiDA.

A big risk from the small number of funding suppliers is the liquidity crisis than can be emerged when one suddenly leaves. This occurred recently when the American organization KIVA terminated its partnership with KSF. Discussions with KSF staff revealed that KiVA believed there was a violation of the terms agreed to in their contract, which resulted in a sudden termination to the program. This highlights the vulnerability KSF´s current operations have due to their funding structure.

Recommendations

- **Develop a clear marketing policy** – This will allow for effective and fast implementation of new products once funding is obtained. Increasing awareness of KSF and its products outside of the current communities of operation would ensure faster client acquisition when new funds are received.
- **Develop a code of ethics for employees** – This could be a part of the community animation manual for example. Any additional training procedures or staff regulations that can be enforced in writing reinforce the social impact of KSF.
- **Extend business training beyond the initial pre-loan period** – By following up on training to ensure clients are operating their businesses effectively and capable of reaching the market will further highlight KSF's commitment to improving the quality of life in communities it targets. In the long-run this may also further reduce loan delinquency rates as client productivities increase.

4.2 Voluntary Savings

Alongside its lending, KSF offers saving products to their clients. Although these are not mandatory, their usage is heavily encouraged and benefits are clearly explained during the training process. Formulated as *susu* accounts, collectors are available on a weekly basis to collect any deposits. The money is available to the individual at all times, however the user is educated on the benefits of increasing their savings. An incentive of 20% extra interest is rewarded to funds held in account for 12 months. Saving deposits are tracked within each client's unique passbook. Its balance is updated and recorded at each meeting. By taking such low level deposits, KSF is reinforcing its mission of helping the poorest segments of Ghanaian society who normally do not have access to banking services. These saving accounts are held separately and KSF does not use them to fund its own loans. Current regulatory changes are taking place in Ghana, and KSF has made it a priority to become regulated as a tier 3 financial NGO. Regulations for these institutions state they are not allowed to take customer deposits. The reason being is to protect the clients against the institution tapping into the deposit base. It has not exactly been made clear if the *susu* money takers are KSF staff or if they are in fact working with rural banks that are legally allowed to take the deposits. If it is KSF taking it, then these operations will have to cease, if it is rural banks then more transparency will be needed with clear disclosure of the partnerships.

Since these loans are at a very low level, an aggregate breakdown cannot be provided. However the 2011 annual report indicates that there total savings of GHS 38,152 in 2010, up from GHS 17,586 in 2009. This sharp rise is a very positive indicator for the usage of this service by KSF clients. KSF claims that all 8017 of their active loan clients use their savings services; however without further documentation it is hard to verify this claim.

A financial incentive is also offered of 20% interest if the funds are held in the account for 12 months. KSF holds these loans separately and as a result these do not feed back into the loan issuing process. Once again, this is unacceptable going forward if it is KSF employees taking the deposits, so further clarification is needed on how the money is being held.

Recommendations

- **If KSF is taking as deposits more than the 10% allowed as guarantee, they must stop** – otherwise they will be in violation of regulations regarding Tier 3 FNGO's which creates significant legal risk that will scare away investors. *Otherwise….*
- **Clearer documentation** on how the savings are stored and with what institutions is mandatory. To comply with regulations KSF, must make clear who is in charge of the handling the deposits and where (ie. rural banks) they end up. This transparent disclosure would also alleviate investor concerns over the safety of these deposits for KSF clients.
- **Strategic goals** for the savings products should be established with targeted deposit sizes and amount of clients who actively use it. This would tie with KSF´s social mission and allow for an evaluation over time on the success of these products.

4.3 Loans

Kraban currently offers 2 group loans and 2 individual loans. Although historically their product range has been more diverse, they have been discontinued as they were meant to be single operations. The current gross loan portfolio stands at GHS 1,834,786 as of year-end 2011 with 8017 total active borrowers divided into 99 groups. With 99% of clients living in the *bottom half of the population below the poverty line*, KSF has been able to achieve its overall strategic goal of targeting the very poor that would otherwise not have access to financial credit. As well, 89.73% of their clients are women, which fulfill the other strategic goal of helping women who often have a significant economic impact. KSF states that all of their loans start off at GHS 100, however after successful completion of one loan cycle the group can apply for much larger loans. A registration fee is required to start the loan cycle (GHS 4895 in 2011) and training procedures. Although no formal collateral requirements are required, the pooling of all individuals into a group acts as informal collateral as each community becomes responsible for the defaults of their own members. Since each product is funded from different sources at different rates, there are different effects on profitability. However, KSF strives to focus on the social impact so when funding is received at lower rates it attempts to pass this down to the client. Until recently KSF appears to have been very successful in reaching communities to issue their loans, however a recent lack of new funding has prevented them from expanding their client base.

Gross Loans (GHS)	1.834.785,90
Communities	99
Avg Principal (GHS)	18.533,19
Clients	8.017
Avg principal (GHS)	228,86

Table 10: Loan Overview

4.3.1 Group Loans

- **SIKA ROSE:** This is the main loan product offered by KSF. Originating in November 2004, the Social Investment Fund of Ghana uses a Revolving Loan Fund to finance it and is managed by the ARB Apex Bank (Association of Regional Banks). Some additional funding is provided by Rhema Consulting. These loans are meant to finance the working capital needs of small-scale farmers and entrepreneurs. This product actively encourages savings by the client and this is tied into the passbook that all users get. As a core product, SIKA ROSE users undergo a long education process which makes the waiting period for the loan 6 weeks. According to KSF, this product has a 100% repayment rate from 2005-2008.
    - **Loan term:** 6 months with 1 month grace period at the start
    - **Loan size**: starts at GHS 100, increases after successful repayment cycles
    - **Interest rate**: determined by interest rate determination model (covered in other section)
    - **Charges:** 2% membership fee + 2% commitment fee on the loan
    - Target Communities: Ga East, Ga West, Ga South and Dangbe West Districts of the Greater Accra region
    - Currently reaching 2,098 small-scale enterprises
    - Training handled by Freedom from Hunger Ghana as well as the Ministry of Finance and Economic Planning

- **AGAPE**: These are loans given specifically to refugees/internally-displaced people within Ghana. It began in May 2005 and is funded directly by the International Alliance of Women (TIAW) from Canada through revolving capital loans. These loans are meant to support their income generating activities, often in the informal sector, inside the refugee camps. This loan requires a mandatory of 10% savings of the loan principal. Since this is a very specific loan to help people in refugee camps, the training is minimal and as a result waiting time for the loan is only 1 week.
    - **Loan term:** 6 months with 1 month grace period
    - **Loan size:** GHS 100 flat
    - **Interest rate:** determined by interest rate determination model (see below)
    - **Charges:** 2% membership fee + 2% commitment fee on the loan
    - 125 migrant workers have received USD 20,000 to date
    - Target region is the Refugee Camp in Gomoa Budumburm

4.3.2 Individual Loans

- **Extra Mile:** This was a microcredit program funded by KIVA designed to issue individual loans. Originating in November 2006 it issued USD$502,200 to 600 KSF clients. In 2007 Kiva determined that KSF was applying its policies inconsistently which resulted in a termination of the KSF-KIVA partnership and as a result, this program. The product was discontinued but a repayment plan had to be established which lasted several years.

- **Higher Heights:** This individual loan program is specifically meant to fund agriculture development projects through 4 farmer-based organizations. The target communities are Agormanya, Akinhwa and Akpamu. It is directly funded by the Millennium Development Authority (MiDA).
    - **Loan term**: 8 months + 4 month grace period
    - **Loan size:** not specified
    - **Interest rate**: 30% with monthly installment payments
    - Funds for these loans are obtained from MiDA at an interest rate of 15% with 18 months for KSF to repay
    - 188 farmers currently utilize this service for maize and chili pepper production

- **Green Energy Loans:** This product is meant to provide credit to entrepreneurs to set up energy facilities in rural areas. It is funded through the American NGO "Energy in Common". By providing solar lanterns it strives to promote clean energy use in the home and by small-scale entrepreneurs. As a simple way of obtaining energy in rural areas, KSF is able to make a lasting impact on communities by introducing these lanterns.
    - **Loan term:** Not specified, but KSF has 18 months to repay funding partner
    - **Loan size:**
    - **Interest rate:** 20% with quarterly payments
    - Target regions: Brong Ahafo, Western and Eastern Regions.
    - Interest rate charged is 20%

4.3.3 Discontinued Programs

- PCIP, BEAM, ORACLE, READY, SANKOFA, TEACH 1, 2, 3

4.3.4 Group Selection Procedure

The group selection process is modeled on KSF's *TEACH* lending strategy. Community outreach is done via the branch offices in their respective geographies to find villages which would benefit from access to micro finance. According to their 2011 Annual Report, KSF uses targeting tools (ie. Participatory Wealth Ranking, Housing Index) in order to find communities where they can make an impact. An important consideration is the economic viability of the villages themselves and how easily they can be linked to existing markets so that products can be sold. Once a village is selected a thorough training process is initiated to ensure the villagers fully understand all aspects of the loan. KSF's target market is strictly rural and they place an emphasis on female clients. Each client is provided with a passbook that is updated at weekly meetings. The passbook contains all principal and interest paid and still owed as well as savings info.

The loan training process explains all the guidelines of the loan and obligations they have to follow. Communities are organized into groups of five cells and each community appoints a representative to deal with KSF loan and credit officers. This grouping process also allows for a pooling of collateral for the whole community. However the collateral established is very informal and can take the form of small personal possessions such as jewelry. Initial loans are set at 100 Ghanaian Cedis but clients are able to borrow in larger amounts in subsequent periods.

4.3.5 Interest Rate Determination

According the KSF's 2011 Strategic Business Plan, "commercial bank interest rates range between 25 - 35%. The service sector generally attracts the highest rates while the rate for the agriculture and manufacturing sectors are lower. Micro-finance institutions in Ghana lend between 30 to 40%. Though usurious, micro-enterprises and groups prefer the services of the FNGOs due to their flexible nature of operations and their door-to-door service delivery." We also reviewed historical base rates for different commercial banks in Ghana and found the rate to be between 25-35% as a comparison to illustrate cost of funds to institutions such as KSF.[13]

KSF has a unique interest rate determination model. According to KSF, "The TEACH programme had provided the opportunities for Kraban Support Foundation to access various credits to on-lend to its society members. These credit facilities were sourced at different interest rates with varying amounts." Factors the Directors of KSF consider are summarized below:

- Donor funds obtained during a fiscal year
- Credit assistance obtained in a fiscal year
- Prevailing base rate of the Central Bank
- The Lending rate of the particular financial institution
- Insurance premium on the weighted average interest
- Inflationary trends in the country
- The value of the cedi

KSF adopted the factors based on the following conditions:

- Identifying all credit-sourcing institutions
- Determining the interest rate on each credit sourced
- Calculating the weight of each credit source (by multiplying the respective/corresponding interest rate of the various sourcing institutions and dividing the weight by the total number of credit sourced in a fiscal year)

Once weighted-average rate is calculated, KSF "implements the interest rate policy considering the Bank of Ghana's prevailing prime rate vis a vis the base rates of other commercial banks. In comparison with the Central Bank's rate and that of the commercial banks, the organisation adopts the lower rate of the three institutions." KSF summarises its interest rate policy as such:

> "KSF's interest (r) is summarized as follows as constituting the following elements {DF, Csy, PBRb, IR, IP, I, DVC} where **DF** is Donor Funds obtained in a fiscal year; **Csy** is Actual Credit assistance obtained in a fiscal year; **PBRb** is the Participating Bank's base Rate; **IR** is Rate of Inflation during a fiscal year; **IP** is Insurance

[13] http://www.businessghana.com/portal/finance/index.php?op=getBankRates

Premium monies insured; **I** is Rates of Interest during a fiscal year; **DVC** is the Cedi Value vis a vis Depreciation."

As mentioned before, the implied interest rate in 2011 from the Gross Loan portfolio 4.4%, compared to the supposed average interest rate of 30%, the yield on the portfolio is far below that.

Recommendations

- While KSF does have an interest-rate determination model in place that covers many important factors, it fails to consider the specific operating costs for KSF as well as profitability considerations. If the goal is to become sustainable, the key questions in setting interest rate policy should be as follows
    - At what percentage can we cover costs (operational and financial)?
    - Above and beyond that, what percentage of profit due we want to obtain (considering default rates, etc.…).
- We believe the APR model does not capture the necessary interest rate for KSF. Due to the volatility of their income inflows and expense outflows (operational and financial) the APR could change year to year quite significantly. Below are calculations for APR 2009-2010:

Year	APR
2009	49,23%
2010	41,81%
2011	43.68%

- We recommend that KSF take a course provided by CGAP, *Delinquency Management and Interest Rate Setting for Microfinance Institutions*.[14] This course can provide a solid foundation for creating an interest rate policy that can lead to sustainability and independence from reliance on donor funds.

4.3.6 Sources of Funding

Historically, KSF obtained funding from a variety of sources. The largest of which was the Social Investment Fund within Ghana that provided revolving credit loan facilities, however the nature of KSF's operations which strives to create partnerships with other organizations results in a large number of funding partners. No new funding has been received in 2011; however the structure of existing liabilities indicates something about how current products have been funded.

(GHS)	2011	2010	2009
SIF/ARB Apex Bank	190.000,00	200.000,00	200.000,00
MiDA /Bank of Ghana	153.669,00	280.148,00	-
LSI -RHEMA Consulting Ltd	35.424,00	45.000,00	-
LSI (Individual)-LAA	600,00	-	-
Energy-in-Common	14.700,00	5.510,00	-
EB-ACCION	16.999,00	24.999,03	94.085,09
ASSFIN/GCB Ltd	-	2.600,08	28.464,00
ASSFIN/MASLOC	-	-	46.669,00

Table 11: Funding Sources

[14] http://www.cgap.org/gm/document-1.9.34366/CGAP%20Delinquency%20Management%20and%20Interest%20Rate%20Setting%20Course.pdf

Below is a chart of total historical sources of funding and the rate at which they were obtained from. The wide range of interest rates highlights KSF's vulnerability to its funding partners. This may also create uncertainty regarding future expense patterns. High interest rates that then have to be passed on to the end user may also place KSF at risk of losing clients to competitors.

Institution/Program	Principal	Charged to KSF
Social Investment Fund	642.800,00	12.5%-18.5%
MiDA	280.148,00	15%
ASSFIN	50.000,00	10%
Ghana commercial Bank	50.000,00	30%
EB ACCION Savings & Loans	220.000,00	30%-38%
RHEMA Consulting	140.000,00	25-27%
KIVA Micro Funds	529.701,20	0%
Energy-in-Common	14.700,00	0%
TIAW	37.500,00	0%
People Helping People intl	15.675,00	0%

Table 12: Historical Fuding Sources

Recommendations

- **Obtain additional sources of funding, preferably unrestricted** – the main challenge KSF is facing right now is marketing themselves to gain new funding. Despite an abundance of microfinance funding sources, KSF has been unable to attract new funds in recent years. This low success rate may also influence the fact that KSF has to choose funds from sources that place restrictions on how they are used. Obtaining unrestricted funding sources would allow KSF to better carry out lending practices where they feel the impact will be more significant. The methods for doing this are of course elaborated in other sections and our final recommendation.
- **Break down loan portfolio by product** – This allows for a better understanding of what products are being used and how much each contributes to profitability.

4.4 Other Financial Products

KSF does not offer any financial products aside from microloans and savings deposits. The product portfolio is currently in line with the operating capacity of KSF and unless structural changes occur, we do not expect this to change in the near future. Other products such as insurance products and checking accounts would further allow for the empowerment of KSF clients. Expanding into other products is severely limited by the technological constraints of KSF when operating in rural areas. The dependence on donor funds also limits the ability of KSF to create new products. However, given the partnership structure KSF operates on, perhaps in the future they can enter into new agreements to market a more diverse range of financial services to their clients.

Recommendations

- **Consider offering other products such as checking, insurance, or microleasing** – these simple products can have large impacts when used for the first time by KSF clients and improve the social performance. Microleasing of equipment to clients for example is a relatively simple way to allow the client to generate cash flows the following day. This equipment can be used to enhance their own production or can allow them to rent out services to the village. Clients also have an incentive not to damage or destroy the equipment because they are still liable to the lender (KSF).

- Although a diversification of products may be limited by capacity and man hours, we believe some of the technological improvements recommended in this report can help facilitate them.

4.5 Nonfinancial Products

As part of its TEACH philosophy, Kraban offers extensive training to its clients. Microcredit training is a mandatory requirement in order to become a client of KSF. A series of meetings is held before the first loans are issued to ensure the community is aware of all requirements and obligations. Additional training is also provided for social aspects as well as business development. To accomplish this, KSF has entered into partnerships with other NGOs, such as MiDA, which have the knowledge and capacity to run effective training programs. Many of these secondary training programs continue after the loan has been issued, which is very helpful in developing the economic potential of clients. Weekly meetings with community coordinators are mandatory and training is incorporated into these meetings to ensure everyone is receiving the training that is needed.

These training programs include business specific learning for

1. Book Keeping
2. Credit Management
3. Records Keeping
4. Business/Marketing Plans

Not much supporting documentation is provided to validate the extent and effectiveness of these training practices however. Some evidence of their success was seen during site visits when KSF clients showed us machinery that they purchased with their microcredit loans and learnt how to use with help from training. KSF staff is also very helpful in helping clients find markets for their products.

In addition, and to match the social aspect of KSF’s mission, additional health and social training is provided in the following areas. These are a critical component of KSF´s overall strategy and have a tremendous impact on the ground. Since KSF specifically targets the very poor in rural areas, opportunities to access education are very sparse. The impacts these programs have are one of the reasons why KSF is so successful on the ground with its clients.

- Health and Education
- Environmental, family planning, immunization, breast feeding, diarrhea management
- Civic/Population Education
- HIV/AIDs, land title registration, electoral procedures
- Family/Property Law & Legal Education
- Marriage and divorce registration, head of family accountability, domestic violence, testate/interstate succession

Interviews with KSF clients showed a general understanding of how microfinance works and the conditions of their loans. This shows that the training process has been very helpful in successfully educating clients. Although it is hard to link the two directly, the high repayment rate may also be slightly attributed to the various business skills given to all clients. The extent of training, which includes social aspects, certainly causes larger expenditures which may decrease long run profitability. However, KSF´s tendency of finding partners and NGO to engage in these activities helps minimize expenses.

Recommendations

- The ability of KSF to find partners to engage in both business and social training has tremendous social impact on lives of their clients.
- A big risk to the sustainability of these training programs is the dependence on other NGO partners to undertake many of these programs when the community engagement process begins. Entering into clearly defined long-term partnership (with supporting documentation) or further developing in house training methods could alleviate investor concern about ongoing social performance.

4.6 Chapter Conclusion

The strength of Kraban in terms of offered products derives from creating long – lasting relationships with its clients. In our view the company has a good understanding of both market competition and borrowing needs of its clients. The product quality and design is appropriate given the range of Kraban's operations and market focus. The terms of the loans and training programs are generally well understood by borrowers and add significant value to their economic activities. The interest rate determination model is well defined but, in our opinion contains major flaws.

We do find that there are several key aspects that the company has to further improve upon. The sole ability to obtain funds from more diversified sources can determine the company's future survival. KSF already cannot fully satisfy the needs of its current clients, and in case of capital shortage from currently available sources the company's financials will be additionally pressured. Kraban has to continually diversify in terms companies that provide funds and training services. The reliance of MFI on current contractors is too significant from the business point of view. The company has to continue improving its services by expanding on its current products portfolio. Adding insurance products will have a tremendous impact on client's economic security, given heavy focus on agricultural business, largely determined by weather conditions. KSF has to further develop its internal policies – the formalization in the areas of product marketing and employees' code of conduct, will improve the company's rankings and allow for easier monitoring of MFI's activities.

The deficiencies in data provided by Kraban are of concern. We highly recommend that the MFI provides investors with detailed breakdown of its loan portfolio by product and savings products breakdown by community. This would allow for better clarity in terms of sources of cash flows by each product and for clear evaluation of the demand for products by given communities. Finally, the transparency in savings storing and entities responsible for their safekeeping is of key importance.

5. LOAN PORTFOLIO QUALITY




5 Loan Portfolio Quality

5.1 Loan Portfolio Breakdown

5.1.1 Asset Quality

- **Portfolio at Risk:** measures past due loans over 30 days. Typically, loan terms in microfinance institutions are between 120 to 180 days with weekly repayments, and therefore any delay in payments of more than 4 weeks is considered at risk of default. Using the calculation methodology of CAMEL, the PAR for KSF is 21.6%. This fairly high number comes from a significant portion of the portfolio being 31-90 Days past due, in addition to a significant amount of rescheduled loans. The amount of loans past due over 90 days is only 8.4% which indicates that delinquencies do not last very long and current repayment issues may simply be tied to agricultural cycles or market trends.

- **Non-performing Loans:** Reflects the portfolio impairment according to the risk weight assigned by the model for delinquencies of more than 180 days. KSF Identifies 0.6% of its portfolio as uncollectible. KSF is able to actively keep track of its non-performing loans. All KSF clients have their records kept in their individual passbooks. In addition, KSF has portfolio at risk calculations for each community and group, which allows them to spot problems as they develop.

- **Loan Loss Provisions –** Based on our Camel analysis, KSF has not had sufficient loan loss reserves to cover the at risk components of their loan portfolio.

KSF (in USD)	2011	2010	2009
Loan Loss Allowance	100,508	82,688	52,785
Camel Calculation	143.309	113.604	92.598

Table 13: Loan Loss Provisions

- **Portfolio Classification System:** This is the qualitative review of the terms of the portfolio impairment and the assessment of the institution´s policies associated with the portfolio at risk. Last year KSF did not have a portfolio classification as promoted by ACCION. However, this year, as evidenced in the 2011 Audit report, KSF has moved to the Rescheduled Aging Status recommended by ACCION.

- **Productivity and Long-Term Assets:** The institution manages its assets over time without a thorough analysis of its impact on the entity. However, at this time, this lack of analytical rigor does not represent a risk to the institution. Fixed assets primarily consist of leasehold, equipment, motor vehicles, and furniture. Vehicles contain the most risk as they are used for the long-trips to rural areas. KSF takes care to maintain the quality of its vehicle so that can utilize them for a long time.

- **Infrastructure**: The institution has an infrastructure that may not guarantee maximum productivity, but is adequate in almost all respects. They have field offices in their rural locations, and their headquarters in Accra provide room for 8-12 person meetings. In addition, they utilize their own vehicles to make weekly trips to clients.

Recommendations

- KSF must describe why a significant amount of loans are >30 Days past due, whether this is a one-off item or a long-term structural problem. A more rigorous classification of loans, including duration of the loan and when interest payments take place. These records are kept at an individual level within the passbooks; however a timely conversion to an electronic format may be limited by access to technology outside of the main Accra office.
- Rescheduled loans must also be broken down on 1-30 Days, 31-90 Days, and so on. In addition, a clear written policy regarding loan restructuring would reduce investor uncertainty over the long term quality of loans
- Although classification is provided by geography, further classification by product would also be helpful. Different products fund different economic activities and are funded at different rates. Such additional information could help identify future repayment problems as well as to categorize loans by risk level to KSF. Loan recovery documentation is essential for investors to understand how long it takes for KSF to recover loans.

5.2 Monitoring and management

KSF loans can be considered monitored at two levels, at the individual level between the client and KSF ground staff, and electronically within the Accra headquarters. A requirement of becoming a KSF client is to maintain an individual passbook that is updated at weekly meetings. This allows for the community officers to keep track of all payments and obligations. Although there is a large amount of PAR between 30-90 days, this could be acceptable given the informal nature of the activities undertaken by KSF clients. The low amount of PAR after 90 days shows that the collections policy of KSF appears to be working. The policy of aggregating clients into groups places a great deal of societal/peer pressure on individuals to ensure that they follow through on their economic activities so that they can repay their loans. Failure to do so means that your group is required to provide funds which causes unwanted frictions.

On a less regular basis, all of this information is compiled and stored at the Accra headquarters. Operational loans are categorized by the group they are in. A summary of this info can be seen below which is current as of December 31, 2011. Although loans are summarized by client group, additional breakdowns are not provided by product or loan officer. Info provided shows that there have been no significant delinquency crises in the past five years. There is no indication that loans are provided to KSF staff or board members at preferential rates. This is a responsible policy and prevents many conflicts of interest that could be financially detrimental. For a breakdown of the *Gross Loan Portfolio*, please refer to appendix 11.

There is no indication that KSF has had independent testing of its portfolio done to assess portfolio quality as well as its policy regarding loan write-offs and renegotiations. Auditing has only been performed on final financial statements before distribution. Had more time been available in Ghana, an ideal situation would have been to analyze the paperwork for some of KSF´s biggest loans.

Recommendations

- **Breakdown of PAR by product type and credit officer** – this will build on the current community based breakdown and will allow for better detection of problems as they occur.
- **Independent auditing of the loan portfolio and practices** – This will increase investor confidence in the quality of KSF operations and ability to effectively handle loan delinquencies.

- **Have documents in writing explaining the renegotiation and write off policies** – again, clarification of these matters will provide investors with confidence about the sustainability of KSF operations to ensure preferential or ad-hoc treatment is not being given.

5.3 Chapter Conclusion

In order to attract investors, Kraban has to further develop its policies and provide additional information on the performance of its loan portfolio. The average recovery rate on the loan has to be delivered to the investors as they are interested in evaluating loss given default, which is a crucial parameter in any financial risk model. Moreover, we recommend that KSF provides the public with clear and detailed policies for write – offs and loan negotiations. Also, details on potential loan payback period extensions would be highly appreciated. The independent auditing practices on loan portfolio numbers and practices are absolutely necessary in case of companies such as Kraban that is, operating in a very volatile economic and political environment. We urge the company's management to provide additional breakdowns of its portfolio at risk by product type and by credit officers to improve the tracking process of potential loss occurrences and staff inefficiencies. Finally, we recommend breaking the rescheduled loan portfolio by 1-30 days and 31 – 90 days maturities going forward and to provide the investors with detailed classification of each product given its use and rates that they are charged at.

6. BUSINESS PLANNING




6 Business Planning

6.1 General Information

In our meetings, KSF's management pointed out that they are not satisfied with the current requirements the investors want them to meet. At the moment, KSF acts as an intermediary between funds and loan recipients. The investors thereby require KSF to use the money in a specific area for a specific part of the population (e.g. farmers in the Eastern region). Those requirements limit the possibilities of KSF tremendously. The institution's management showed us in independent meetings that there is a very high demand for microfinance in various areas of the country. In particular they mentioned 50 so-called FBOs (Farmer Based Organizations) and 100 CSCS (Cooperative Savings and Credit Societies) that demand microloans. While we were not able to verify these numbers, the field visits showed clearly an over-demand for the products KSF offers. Therefore, KSF formulated the goal to access funding that is independent from a certain location or population sector in order to utilize the funds most efficiently. Furthermore, funds that could be decided over independently would enable the institution to better meet their goals stated in their vision.

While in Ghana, KSF provided us with a three-year business plan, stating clear objectives for the following periods. Three objectives are pointed out for the coming three years:

1) Access capital of GHC 600,000
2) Promote, sensitize and develop 20 Farmer Based Organizations (with 20 members each) as well as 25 Cooperative Savings and Credit Societies (with 40 members each), adding up to 1400 new customers
3) Recruitment of six permanent team members for field work

Meeting these goals means an increase in the number of customers by 1400 borrowers. The plan is backed up by macroeconomic research and an analysis of the competitive environment, KSF acts in.

While the business plan states clear objectives, it does not give a clear outline how to achieve the goals. While the operational part of the plan seems to be very much thought through, the funding and financing part is much less distinctive. In our opinion, the biggest concern is acquiring the additional funding that is the basis for new loans to communities (and the resulting staff increase). Furthermore, the question arises, why KSF did not manage yet to secure further funding, when the demand for their products is so high. Answers to this question are given in this report: The organization must increase its transparency for foreign investors in order to acquire new, independent funds.

Recommendations

- Refine the strategic plan with clear and realistic milestones on a monthly basis, especially covering funding plans
- Include matching financial projections (please see "6.2 Financial Projections" for details)

6.2 Financial Projections

The current business plan only contains financial projections for the cost-side of the business, which are based on the experience of the management team. These projections are based on the objectives KSF wants to reach in the next three years. From an investor point-of-view, the projections are not sufficient.

Recommendations

- Forecast profit & loss statement, balance sheet and cash flows for the business plan period
- Clearly state the assumptions made for the forecasts, e.g. default rates, expected inflation, number of customers, available funding, administrative expenses, number of staff and personal expenses etc.
- Include a sensitivity analysis with base case, bad case and best case scenarios
- Include matching financial projections (please see "6.2 Financial Projections" for details)

6.3 Funding

The current sources of funding are explained in detail in "4.3 Loans – Sources of Funding".

For the future development of the KRABAN Support Foundation, funding is the central and most important issue. During our research it became clear that the organization currently acts as an intermediary for international microfinance investors. KSF thereby only distributes pre-defined products to their network of farmers, women and small-size entrepreneurs. Thereby, KSF is not able to utilize its large network of communities that show much more demand for similar microfinance products. In order to overcome this problem, the main goal of KSF is and must be independent funding. This would, in our opinion lead to a much more efficient usage of KSFs capabilities.

While the loan operations seem to work very well, funding is hard for KSF to acquire. We think that this is mainly due to the lack of transparency that the organization currently displays. Therefore, it is even more important to work on and with the recommendations made in the previous chapters, in order to make KSF more attractive to international and local investors. Additional funding would, in our opinion surely add value to the MFI.

The business plan only very briefly covers the funding issues faced by the organization. During our meetings with the management, a list of possible investors was presented to us. Management was not able, however, to gives us reasons why some of the investors declined collaboration.

Recommendations

- Setup a clear strategy for funding acquisition, including list of possible investors and milestones. Thereby focus on a more diversified base of investors on order to decrease dependencies on single investors.
- Track and record reasons for decline of potential investors in a separate document
- Put together an investment proposal document for investors (including strategic business plan, projected financials)
- Work on the transparency issues that were discovered in the last and this current analysis

7. SOCIAL PERFORMANCE




7 Social Performance

7.1 General Information

Kraban Foundation defines its mission statement as follows: "To develop innovative strategies that enhance the capacity of vulnerable groups to operate independently and effectively in the informal sectors of the Ghanaian economy"[15]. The company's main focus is to reach poor individuals living in the rural areas of the country and to provide them with the means of financing that are otherwise unavailable. In 2010 99% if the company's total number of clients were people living below the poverty line. Kraban utilizes the models of community education and group lending which purpose is to increase the efficiency of clients in managing their businesses and funds and to motivate the borrowers to pay back their loans in time. In our view the company has clearly identified its target groups and goals in terms of social impact and quality change in the lives of their clients. We believe however that some of the goals highlighted in the Strategic Business Plan lack concrete measures for their achievement. For example, Kraban aims at identifying the "marginalised groups" with viable projects for credit assistance; it does not however describe what is considered a marginalised group, neither indicates the means for doing so. Based on our assessment and data at hand, we find that Kraban lacks the measurable indicators highlighting their social achievements.

Recommendations

- First and foremost, the company has to define its social objectives using SMART criteria. Kraban needs to specify the indicators that would measure the achievement of such social goals. The company has to develop social benchmark that they aim at achieving on annual basis and in the longer term. We recommend the usage of CIMS method, but only with clearly specified social targets.
- Evaluate the social impact that the company has on its clients using publicly available tools and set measurable and achievable goals in this area. Develop the step by step strategy that highlights the process of realising such social checkpoints in short, medium and long term. As such, SMART[16] goals and strategy of their achievement is essential for most investors in the MFI business.
- We recommend measuring the social goals also in terms of social responsibility towards clients and stakeholders. For example, a good indicator of such measurement would be the retention of old clients or the % of client complaints actually attended over a period of time.
- KSF needs to separate social goals from activities. The activities are steps that have to be undertaken in order to achieve goals. In order to evaluate the social impact, the company has to adopt top – down approach. If the company is planning on increasing the HIV/AIDS awareness of its clients, it should list this under its social objectives, and identify steps (activities) necessary for the achievement of such goal. As mentioned, this goal has to be SMART. The following questions should be answered in analysed HIV/AIDS awareness goal: What institutions Kraban will cooperate with on this matter? What communities will be considered? In what geographical regions? What specific programmes the company will target? How will the training be delivered? How will it be financed? What will be the time horizon? Specifically, how will the results of these activities be measured over time? Such an approach has to be adopted for all social goals and aligned with the company's mission.

[15] Kraban Support Fundation Strategic Business Plan, *Microficnance Operational Document*, October 2011.
[16] SMART = Specific, Measurable, Attainable, Relevant, Time – bound.

7.2 Intent and Design

As previously stated, Kraban is, at the moment, an intermediary between fund providers and individuals who obtain such funds. As such, the company is highly dependent on external sources of capital, and has almost no flexibility in terms of both selecting the clients and shaping their product portfolio. Kraban supplies microloans to four different groups: production[17], marketing[18], processing and storage. This source allocation is perfectly in line with the goal of supporting the poorest communities, providing them with training and allowing for financial independence after the business becomes profitable. The main channel through which Kraban reaches new clients are the Cooperative Savings and Credit Societies (CSCS). The CCAs as the community representatives are the main link between the community and Kraban. CCAs reside within the community and therefore are an excellent source of information to loan officers in terms of clients' financial needs and potential new entrepreneurial activities within the community. Kraban has three branches – the Accra's headquarters, branches in Takordi and Somanya districts. The whole system is based on the filed visits and controls within the communities with CSCS as main link between the clients and the institution. In our view, the structure of joint lending is efficient in the environment with little or no collateral held by the borrowers. We also think that given the company's focus on poor communities located in rural areas, the financial products offered by KSF are well aligned with its clients' needs. At the same time the product design and client group breakdown, serve the company's mission of alleviating poverty. The loans are mostly designed for agricultural activities and small-sized urban entrepreneurial businesses which are in fact the main source of income for many of the KSFs clients.

The close relationships between group members, and responsibilities held by community members imply that the borrowers are pressured to repay their loans outstanding in order to receive a next round of financing for their respective group. The existence of CCAs within CSCS allows for some form of control and monitoring over borrowers. During our field visits we found that Kraban's representatives have developed excellent relationships with their clients. At the same time, the training[19] programs offered by Kraban in cooperation with third party companies add significant value to borrowers. What we found however, is that the training programs' quantity and their length are often not sufficient, that is, clients would enjoy further training in their respective areas of economic activities. Furthermore, since the communities are located in rural and often remote areas, the costs associated with timely visits of loan and credit officers are substantial and amounted to around $11,703[20] in 2011, which was around 20.5% of total administrative costs. The current structure with no or limited credit and lack of clients/communities selection flexibility disfavours Kraban's operations as it does not allow for optimal funds allocation.

Recommendations

- Obtaining new sources of financing with the possibility of developing tailor – made products in the communities in closer proximity of company's branches, and subsequent, consistent expansion to more remote areas and the increase in the market penetration and outreach.
- We recommend that the company's staff engage in the gathering of as much information as possible on KSFs potential clients. This would allow for more accurate client targeting and more effective product design process in the future, when the company hopefully diversifies its sources of funds and would be

[17] Loans for farmers for food crops purchases.
[18] Buying and selling of agricultural products.
[19] Simple accounting, farming techniques, managing loans repayment and other entrepreneurial skills.
[20] Gasoline, travel, car repair and maintenance, accommodation and meals

able to select projects and clients independently of its donors. The example of a detailed data checklist is provided in the appendix 12.

7.3 Depth and Breadth of Outreach

The number of active clients in 2010 was 8,017. The data for 2011 is unknown at this point. Kraban reports that 93% of borrowers were women in 2010 and 91% as of today. Based on our field visits and some conflicting numbers in the sources coming directly from Kraban, we have reasons to believe that women ratio as a total of borrowers may be overstated. We are highly sceptical in terms of Kraban's ability to increase its outreach due to limited means of obtaining external funds. We believe at the same time that CEO and his team have an excellent understanding of the lending business in Ghana, and therefore are able to expand their product offer and select their clients more carefully, decreasing at the same time the non-performing loans in their gross portfolio. Kraban states that it is using the targeting tool including means tests, participatory and/or wealth ranking or housing indices to target communities. We however, cannot verify this information as we have seen no documentation. As for measuring poverty, the company does not provide any indicators such as Poverty Assessment Tool or Progress out of Poverty Index (PPI). Given the importance of such measurements from the investors' and donors' perspective, we believe it is absolutely necessary that the company delivers such rankings on regular basis.

Recommendations

- We recommend that Kraban evaluates the social impact of its operations using one or several of the following, publicly available indices and tools:
  - Cerise Social Performance Indicators[21]. This highly interactive and informative tool has been developed in order to evaluate the impact of MFIs on the communities they operate in. Cerise provides the interested parties with an excel file that can be used to measure financial performance, intent and social strategy, governance, targeting and outreach, quality of services and more.
  - PPI index. The use of this index is of crucial importance for any MFI. It allows for evaluation of the change in the clients economic situation over the time of loan financing.
  - Progress Out Of Poverty. The PPI is an objective client poverty assessment tool. It measures the participation of the clients living on income below National Food Line, National Poverty Line[22], USAID "Extreme" Poverty line, $1,25/Day etc. in the total clients' community. PPI is an easy to use and publicly available to assess the social change in the lives of clients.
  - INCOFIN ECHOS – a comprehensive tool for evaluation the extent to which an MFI realizes its social objectives in practice. It also helps measuring the outreach of the company and its contribution to the society and the quality of services provided. The company is scored in five dimensions: mission/vision, scale and outreach, environment & community Support, human resources and customer service quality.
  - Social Performance Task Force (SPTF) – Poverty Assessment Tools. The organization is one of the best recognized for providing MFIs with means of measuring its social performance over time. The evaluation can be conducted from the perspective of an NGO, Investor or an association. SPTF provides MFIs with guides on strategic management, social audit, market research or client protection. s

[21] Most recent version 3.3.1 for 2011.
[22] Also 150% or 200% of NPL.

7.4 Changes in the Social and Economic Lives of Clients and their Households

We evaluate the impact of Kraban Foundation on the economic and social lives of its clients by means of direct communities' visits and face to face interviews. The institution does not measure a change in their clients welfare. Regardless of geographic location, groups or community size, loan amount its terms, its maturity or ultimate allocation, we have identified the following recurring themes in clients' responses:

- Funds provided by Kraban are necessary from the clients' perspective. Acquisition of these loans is essentially the only way both for achieving breakeven point and future financial independence.
- Interest rates paid on loans are not considered excessive by the clients. For many borrowers however, increasing the cost of funds would effectively hinder their ability to pay back the loans. From clients' perspective, the optimal rate ranges between 15 and 20%. Rates from 30% to 40% are still considered "manageable".
- Training programmes provided by Kraban are almost universally viewed positively by clients. Similarly, demand for such initiatives exceeds their supply.
- Many borrowers cannot obtain next round of financing due to inability of other group members to meet their obligations. Such liquidity standstill severely hurts the existing businesses' operations.
- Most of our responders were able to make profit on their operations thanks to micro loans. Also, in almost every case, the whole portion of the loan was allocated.

Limitations of the study:

- The responses obtained, were delivered to us by the translator that was a Kraban representative.
- We were not allowed to select the communities by ourselves. The locations we have visited were selected by Kraban's staff beforehand.
- Clients responses might have been biased due to Kraban's staff presence at the sites. We assume that providing an unfavourable response might influence the future obtainment of the loan.
- Some concerns:
    - Clients did not always understand all details concerning the products.
    - Some conflicting responses in terms of the loan grace period granted within a single community and the actual interest paid.

Recommendations

- In order to retain clients, more funds and training programmes are necessary. We advise Kraban collects more feedback from its clients and offers more reliable ways of evaluating client's responses. Copiling more information about their clients or conducting surveys among its clientele on regular basis in order to evaluate their needs and opinions (products, support), would definitely add value to Kraban's services. We emphasize the necessity of delivering objectivity in field visits' environment, arranged for third party entities or research teams.

7.5 Demonstration Effect

Kraban Foundation is following the Asian MFI model similar to the one adopted by Grameen bank founded in 1983 in Bangladesh. We define the following key aspects:

- Lending to the poor individuals with zero or low collateral.
- Most loan takers are women[23].

[23] For Grameeen bank the ratio of female loan takers is around 91%. Based on our field visits and client interviews we have reasons to believe that the numbers may be overstated.

- Group – based credit approach is the basis of the lending model.
- Saving products are offered and their use is highly recommended by the bank.

In 2011, there were 250 credit unions, 125 rural banks, 45 FNGOs and 12 licensed Savings and Loans companies[24] all of which are considered microfinance institutions. The microfinance NGOs utilize a similar model to that of Kraban, meaning they obtain funding from external sources[25], individual and group loans offerings, which often include credit with Education methodology and lending among others. By utilizing its unique TEACH[26] methodology Kraban is effectively implementing the strategy of increasing the effectiveness of its clients in terms loan repayments, managing their business activities and strengthening responsibilities for other members within credit group. We did not identify clear trends in terms of following or replicating specific models within Ghanaian microfinance businesses.

Kraban grants most of its loans within specific communities. The word of mouth advertising between clients is limited due to poor infrastructure and low mobility of community members. The propagation effect within clientele is therefore severely limited in case of Kraban. This implies that higher degree of market penetration is still required from the company. This could be achieved through accessing different clientele, especially in the metropolitan areas such as Accra where Kraban's head branch is located. During our visit in Accra we have found that there are large opportunities in the city, due to substantial number of small enterprises, shops and boutiques. The turnover for such businesses is naturally larger than in the rural areas. At the same time, large demand for MFI funds exists.

Recommendations

- Creating tailor – made products along with broadening the range of services offered, in order to expand the client network in metropolitan areas. This should strengthen the propagation effect between existing and potential groups of clients. We would like to emphasize however that given the higher MFI competition in the urban areas, Kraban should assess threats and opportunities prior to potential expansion.

7.6 Durability and Impact

As long as the clients have consistent access to the funds, they are generally able to expand their businesses by subsequently developing various skills and contacts, also in terms of finding new markets and contractors. We have found that clients are usually efficient in the ways they utilize the funds. However, as mentioned before, the potential lack of additional financing sources does not allow for further expansion of operations by current clients. Also, even though the group lending structure has many benefits, it can discriminate the economically efficient clients in the case that less efficient group members do not settle their liabilities. Finally, after several rounds of financing, clients might not need additional loans. The fact that the company cannot select its clients independently of their sponsors has however a negative impact on the company's loan portfolio quality. If Kraban could freely select both the communities and target individuals in a strategic manner, it would not only boost its profitability but also reward its well performing clients. As mentioned in the point 4, regarding products, no insurance services are being offered by Kraban as of June 2011.

[24] Licensed Non – Bank financial institutions.
[25] Subsidized credit.
[26] Training Education And Credit Health.

Recommendations

- If Kraban is not be able to extend its financing, the current clients will not be able to continue their operations if reliant on subsequent loans. Kraban has to provide consistent sources of funds to their borrowers. Again, this highlights the importance of Kraban receiving funding independent of requirements hindering their ability to target the best communities/clients.

7.7 Formalization of Otherwise Informal Activities

We are uncertain at this point whether KSF has eradicated usurious moneylenders from its geographic areas. However, during our field visits we interviewed some of the clients and they informed us that the loan that KSF gave them was the first they had ever received. We believe this highlights that at least some of the areas KSF reaches out to do not have any other lending options. We cannot say with complete confidence whether usurious moneylenders have been eradicated or have become themselves micro lenders. Clients also did state that the community members tend to help those that run into trouble, whether it be financial or other types of problems.

7.8 Chapter Conclusion

We have no doubt that Kraban´s main purpose is to help those in need. The company's employees have developed close relationships with the communities it engages with and are highly motivated to help clients develop their businesses to achieve financial independence. Kraban clearly highlighted the importance of social impact within its operations; however we believe it has not developed a quantifiable strategy for achieving these goals. The only way of convincing investors and donors that the company is actually improving its client's economic lives is to provide them with scores and rankings coming from comprehensive and broadly recognised tools designed for such assessment. We recommend using several of these tools simultaneously over the long term horizon. The significance of this point cannot be overstated, as many investors do not even consider lending their funds to the companies that do not publish such data on regular basis.

8. FINDINGS & RECOMMENDATIONS




8 Findings and Recommendations

Findings: Through our research and the time spent in Ghana with the institution Kraban Support Foundation, we have concluded they demonstrate both strengths and weaknesses. They are strong in achieving social community-level economic development where they operate. Moreover, the management of the organization shows strong capabilities and commitment for developing the institution in the future.

A critical operating weakness that prevents KSF from fully achieving their mission is the fact that they act as an intermediary between organizations and end-clients with no-say on the type of products or where they distribute them. In this way, the products they deliver are predetermined by the donor, who may not have the most complete knowledge of how funding should be allocated. This is further accentuated by an inability to attract new funding in the last two years which stems from weak transparency in their financials and corporate governance.

Immediate Goal: Kraban is an MFI with the goal of diversifying its funding sources, with the intent to gain funds and implement them as they see fit. Kraban has the expertise and experience to better allocate funds than serving just as middle man. The freedom to allocate funds would in-turn could produce a stronger loan portfolio while simultaneously enhancing their mission of poverty alleviation among the poorest of the poor.

Recommendations: We focus on 3 actions Kraban can put into place to achieve their goal.

- **Enhance Transparency** – Financial and Governance
    - **Governance**:
        - Clearer separation of management and board members
        - Formalize procedures of board and management (CEO, OIC) in order to reduce key person risk and make operational procedures more transparent
        - Formalize clear responsibilities for each management level
        - Better record keeping of meetings and documentation of key decisions
    - **Financial**: Documentation is a must for potential investors. Although proper steps have been taken since the last report to better address some factors such as Portfolio-at-Risk, further steps must be taken. We recommend the following:
        - Accounting Policies must confirm to CGAP guidelines. As mentioned prior, issues within the 2011 Audit Report were significant.
        - Portfolio breakdown by product (total amounts with PAR divisions, average recovery rate, etc.) is a must to understand on a deeper level the health of the loan portfolio.
        - Implement IT systems that help with documentation of all products offered by geography and client.
        - Information about how the loan recovery/renegotiation process occurs. What are the criteria for renegotiation? If, how and when is loan considered written-off?

9. INFORMATION FOR DONORS & INVESTORS




9 Information for Donors and Investors

The application of conventional analysis of a financial institution does not fully identify the strengths and weaknesses of microfinance institutions. The reasons for this are given in the CAMEL analysis report in appendix 12. It is also worth noting that the CAMEL Analysis itself has limitations, which are also touched upon in the appendix. At this point, we want to briefly summarize the CAMEL scoring for KSF.

9.1 Camel Rating Summary

KSF improved its score by 4.9 points compared to 2011. This means that KSF still gets a C grade, but their utilization of last year's group's report signals commitment on their behalf to improve the institution overall. We believe sincerely that a B score is possible within the next year.

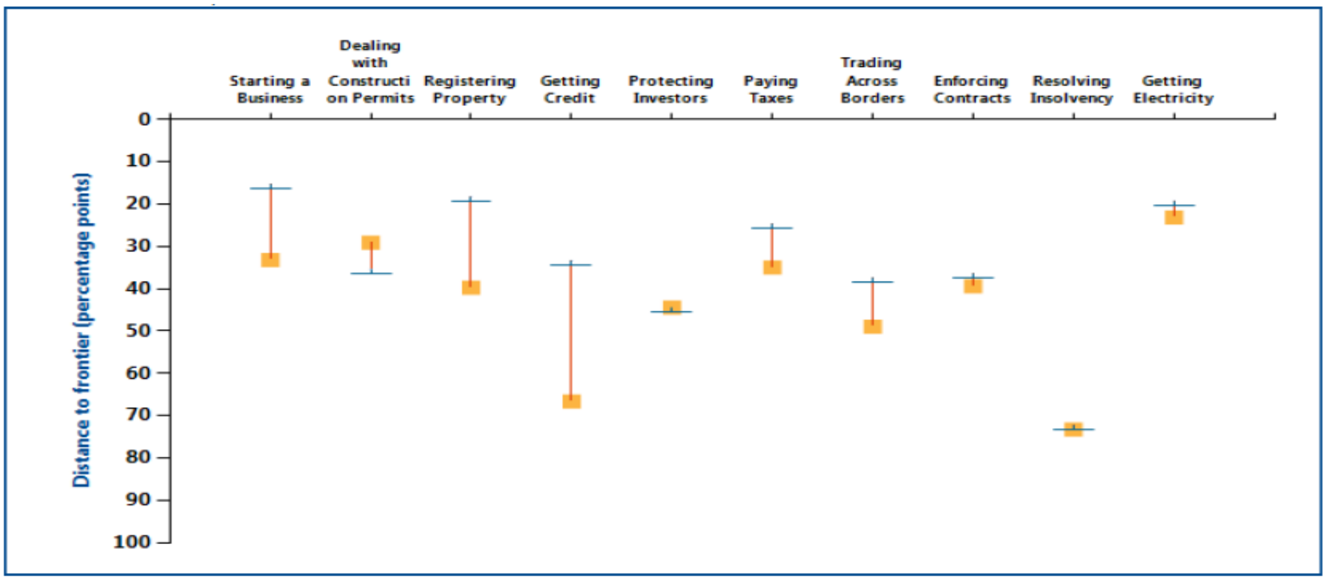
QUANTITATIVE INDICATORS			QUALITITATIVE INDICATORS		
	OBRONI	**MAX. PUNT.**		**OBRONI**	**MAX. PUNT**
CAPITAL ADEQUACY Weighting (Max. 15%)					
1. Leverage	5.0	5	9. Ability to Raise Equity	2.0	5
2. Adequacy of Reserves	4.0	5			
ASSET QUALITY (Max. 21%)					
3. Portfolio at Risk	0.0	8	10. Portfolio Classification System	1.8	3
4. Write-offs/Write-off Policy	7.0	7	11. Productivity of Long-term Assets	1.2	1.5
			12. Infrastructure	1.2	1.5
MANAGEMENT (Max. 23%)					
			13. Governance/Management	4.8	6
			14. Human Resources	2.4	4
			15. Processes, Controls, and Audit	1.6	4
			16. Information Technology System	2.0	5
			17. Strategic Planning & Budgeting	1.6	4
EARNINGS (Max. 24%)					
5. ROE	0.0	5	18. Interest Rate Policy	2.4	4
6. Operational Efficiency	8.0	8			
7. ROA	0.0	7			
LIQUIDITY MANAGEMENT (Max. 17%)					
8. Productivity of Other Current Assets	0.4	2	19. Liability Structure	6.4	8
			20. Availablilty of Funds to meet Credit demand	2.4	4
			21. Cash Flow Projections	1.2	3
TOTAL	24.4	**47**		31.0	**53**
OBRONI	55.4				

9.2 Other Information for Donors and Investors

It is our belief that additional funding would add-value to KSF. Specifically, it would be interesting to see how a minimal investment ($25-50 thousand USD) for which KSF could customize the loans and target the clients they desired would result in terms of returns for investors and efficiency on the part of KSF. We recommend an initial investment of this size, over a period of 6-12 months. If the investment shows satisfying results, we believe KSF has the capabilities and demand to execute larger investments.

Appendix

1) Doing Business in Ghana



Note: For economies added to the *Doing Business* sample after 2005, the starting point is the year in which they were added: 2006 for Montenegro; 2007 for Brunei Darussalam, Liberia and Luxembourg; 2008 for The Bahamas, Bahrain and Qatar; and 2009 for Cyprus and Kosovo. See the data notes for more details on the distance to frontier measure.
Source: Doing Business database.

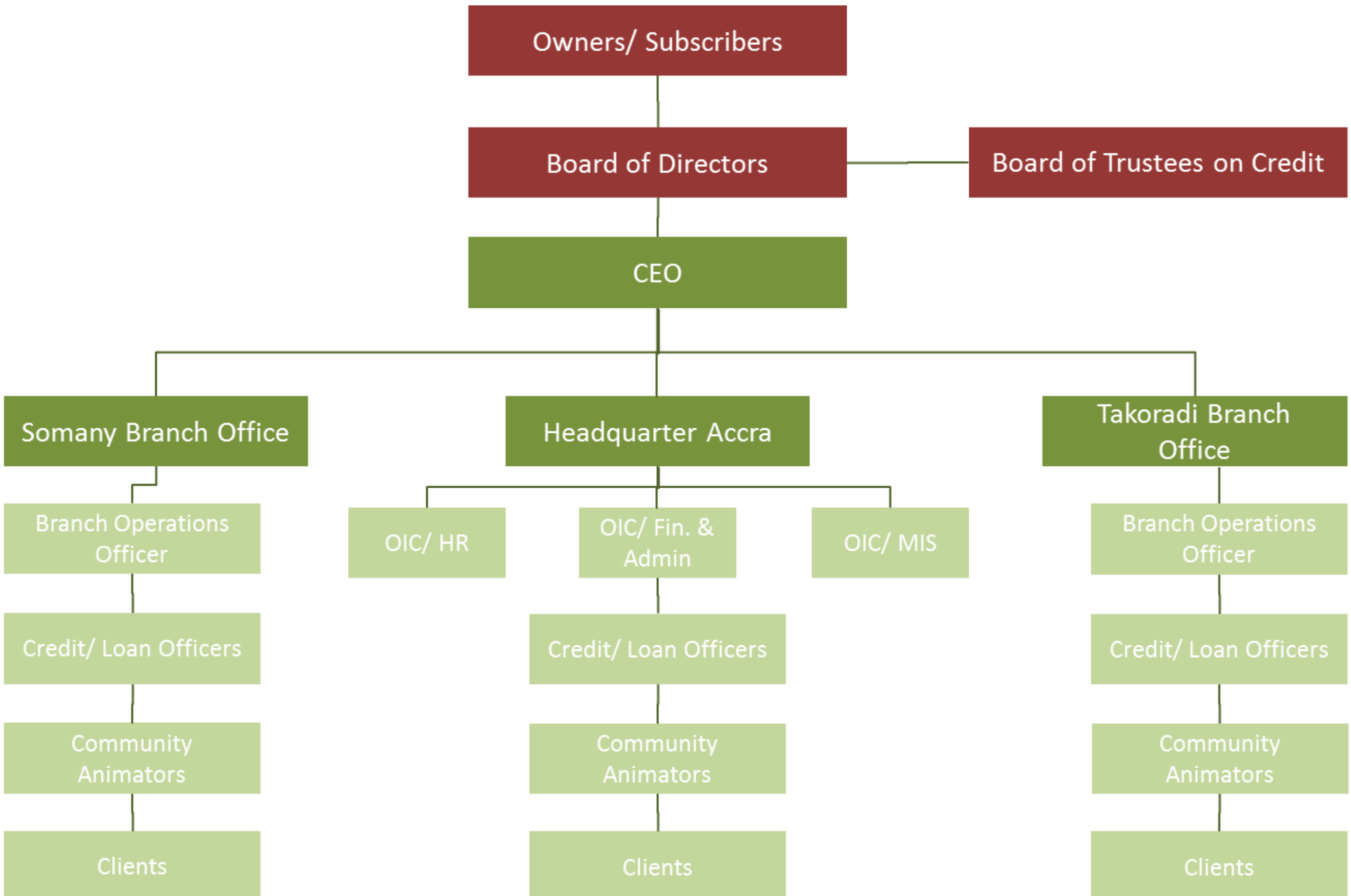
2) Board members in detail

Name	Position	Occupation & Experience
Dr. Matthew Kwadjo Etrebi*	Chairman	Pharmacist & Businessman
Nana Opare Djan*	Board Secretary	CEO of KSF, 15 years of experience in (Micro-) Finance
Ezekiel Anim Oboubisah*	Member of the Board	Chief Accountant of KSF
Hilary Grace Wobil	Member of the Board	Nutritionist
Eunice Ohenewaa Ameyaw	Member of the Board	Entrepreneur
Jerry Thompson Owusu-Amo	Member of the Board	Environment Health & Safety Practitioner
Augustine Annora Amankwah	Member of the Board	Reverend Minister
*also member of COTC		

3) Management in detail

Name	Position
Nana Opare Djan	CEO
Emmanuel Aboagye	OIC, Finance/ Administration
Millicent Asantewaa Donkor*	OIC, Human Resources
Margaret Nkrumah	OIC, Management Information Systems
Comfort Ofori Asante	Senior Operations Manager
* also member of COTC	

4) Organizational Structure of KSF



5) Financial Statements

a) Profit&Loss Actual Audited Statements w/o conservative bias

P&L		2011	2010	2009
Financial revenue from loan portfolio		52,854	130,646	93,332
Financial Revenue from Investment	II	1,268	1,554	2,017
TOTAL INCOME		**54,122**	**132,200**	**95,349**
Personnel expenses		7,815	18,838	88,659
Other adminstrative expenses		7,064	25,654	36,626
Administrative Expenses		**14,880**	**44,492**	**125,285**
Interest and fee expenses on funding liabilities		4,058	23,306	14,292
Interest on deposits		3,937	11,769	5,294
Provision for Loan Losses		24,294	29,903	27,303
Financial Expenses		**32,289**	**64,978**	**46,889**
Total Financial, Loan Loss and Operating expenses		**47,169**	**109,470**	**172,174**
NET OPERATING INCOME (LOSS) BEFORE TAXES		**6,953**	**22,730**	**(76,825)**
Income tax expenses, continuing operations		0	0	0
NET OPERATING INCOME (LOSS) AFTER TAXES		**6,953**	**22,730**	**(76,825)**
Grant and Donations	IV	**44,938**	**45,486**	**41,860**
Other non-operating income	V	**67,044**	**36,023**	**30,084**
Total Non-Operating Revenue and Expenses		**111,981**	**81,509**	**71,945**
NET INCOME (LOSS)		**118,934**	**104,239**	**(4,880)**

b) Profit&Loss Actual Audited Statements with conservative bias

P&L		2011	2010	2009
Financial revenue from loan portfolio		**49,685**	**130,646**	**93,332**
Financial Revenue from Investment	II	**1,268**	**3,571**	**2,017**
TOTAL INCOME		**50,953**	**134,217**	**95,349**
Personnel expenses		**36,833**	**18,838**	**57,403**
Other adminstrative expenses		**38,807**	**35,448**	**36,626**
Administrative Expenses		**75,640**	**54,287**	**94,029**
Interest and fee expenses on funding liabilities		4,058	23,306	14,292
Interest on deposits		3,937	11,769	5,294
Provision for Loan Losses		24,294	29,903	27,303
Financial Expenses		**32,289**	**64,978**	**46,890**
Total Financial, Loan Loss and Operating expenses		**107,929**	**119,265**	**140,918**
NET OPERATING INCOME (LOSS) BEFORE TAXES		**(56,976)**	**14,952**	**(45,569)**
Income tax expenses, continuing operations		0	0	0
NET OPERATING INCOME (LOSS) AFTER TAXES		**(56,976)**	**14,952**	**(45,569)**
Grant and Donations	IV	**44,938**	**45,486**	**41,860**
Other non-operating income	V	**67,044**	**36,023**	**30,084**
Total Non-Operating Revenue and Expenses		**111,981**	**81,509**	**71,945**
NET INCOME (LOSS)		**55,005**	**96,462**	**26,375**

c) Profit&Loss CAMEL adjusted statements

P&L	2011	2010	2009
Financial revenue from loan portfolio	49,685	130,646	93,332
BDS Fees (Business Developement Services)		28,682	21,683
Financial Revenue from Investment	1,268	3,571	2,017
TOTAL INCOME	**79,635**	**155,900**	**125,433**
Personnel expenses	18,168	14,226	17,150
Other adminstrative expenses	57,472	40,061	76,879
Administrative Expenses	**75,640**	**54,287**	**94,029**
Interest and fee expenses on funding liabilities	83,410	73,245	47,912
Interest on deposits	3,937	11,769	5,294
Provision for Loan Losses	36,180	21,006	67,116
Other CAMEL financial adjustments	75,747	111,021	123,436
Financial Expenses	**199,274**	**217,041**	**243,759**
Total Financial, Loan Loss and Operating expenses		**274,913**	**271,328**
NET OPERATING INCOME (LOSS) BEFORE TAXES		**(195,278)**	**(115,428)**
Income tax expenses, continuing operations	0	0	0
NET OPERATING INCOME (LOSS) AFTER TAXES		**(195,278)**	**(115,428)**
Grant and Donations / Directors Contributions	83,299	45,486	41,860
Total Non-Operating Revenue and Expenses		**83,299**	**45,486**
NET INCOME (LOSS)	**(111,979)**	**(69,942)**	**(170,494)**

d) Balance Sheet Actual Audited Statements w/o conservative bias

BALANCE SHEET		2011	2010	2009
Liabilities with Others		266,360	361,449	239,054
Accounts Payable (Sundry Creditors)		22,293	24,702	13,488
Other Liabilities		0	0	4,140
Accruals	5	3,299	0	0
Total Liabilities		**291,952**	**386,151**	**256,682**
Share Capital		378,302	378,302	378,302
Reserves		530,190	411,256	297,973
Total Equity	6	**908,492**	**789,557**	**676,275**
TOTAL LIABILITIES & EQUITY		**1,200,444**	**1,175,708**	**932,956**
Cash	3	2,986	6,555	1,514
Short Term Investments		19,424	19,424	6,808
Net Loan Portfolio		1,087,443	1,114,398	861,901
Fixed Assets	2	40,593	6,697	10,245
Other Assets	4	37,455	45,450	51,028
TOTAL ASSETS		**1,187,900**	**1,192,524**	**931,497**

e) Balance Sheet Actual Audited Statements with conservative bias

BALANCE SHEET		2011	2010	2009
Liabilities with Others		266,360	361,449	239,054
Accounts Payable (Sundry Creditors)		22,293	24,702	13,488
Other Liabilities		0	0	0
Accruals	5	3,301	2,696	2,680
Total Liabilities		**291,955**	**388,847**	**255,222**
Share Capital		378,302	378,302	378,302
Reserves		530,190	411,256	297,973
Total Equity	6	**908,492**	**789,557**	**676,275**
TOTAL LIABILITIES & EQUITY		**1,200,447**	**1,178,405**	**931,497**
Cash	3	2,986	6,555	1,514
Short Term Investments		19,424	19,424	6,808
Net Loan Portfolio		1,087,443	1,114,398	861,901
Fixed Assets	2	53,137	6,697	10,245
Other Assets	4	37,455	28,634	51,028
TOTAL ASSETS		**1,200,445**	**1,175,708**	**931,497**

f) Balance Sheet CAMEL adjusted statements

BALANCE SHEET - ADJUSTED	2011	2010	2009
Liabilities with Others	266,360	361,449	239,054
Accounts Payable (Sundry Creditors)	22,293	24,702	13,488
Other Liabilities	0	0	0
Accruals	3,301	2,696	2,680
Total Liabilities	**291,955**	**388,847**	**255,222**
Share Capital	378,302	378,302	378,302
Reserves	493,861	384,045	260,567
Total Equity	**872,162**	**762,347**	**638,869**
TOTAL LIABILITIES & EQUITY	**1,164,117**	**1,151,194**	**894,091**
Cash	2,986	6,555	1,514
Short Term Investments	19,424	19,424	6,808
Net Loan Portfolio	1,044,642	1,083,483	822,089
Fixed Assets	59,608	10,402	12,652
Other Assets	37,455	28,634	51,028
TOTAL ASSETS	**1,164,115**	**1,148,497**	**894,091**

6) Breakdown of expenses

	USD	%
Total Expenses	107,929	100%
Operational	75,640	70%
Financial	32,289	30%
fuel	*3,454*	3%
vehicle repairs	*723*	1%
sponsorship	*7,582*	7%
salaries & allowances	*10,601*	10%
training	*6,337*	6%
foreign exchange loss	*4,909*	5%
*Provision for Loan Losses**	24,294	23%

*Non-cash expense

7) Volatility of key indicators

	% Change YoY			
	2011	**2010**	**2009**	**Volatility**
Income	-62%	41%	-20%	52%
Operatinal Expenses	39.3%	-42.3%	13.2%	42%
Financial Expenses	-50.3%	38.6%	75.0%	64%

8) Breakdown of Assets

ASSET BREAKDOWN	2011	% of Assets	% change Yoy	2010	% of Assets	% change Yoy	2009	% of Assets
Cash	2,986	0%	(54%)	6,555	1%	333%	1,514	0%
Short Term Investments	19,424	2%	0%	19,424	2%	185%	6,808	1%
Current Loans	767,052	64%	(14%)	889,967	74%	33%	667,307	56%
Rescheduled Loans (Current)	113,662	9%	1%	112,216	9%	(4%)	117,138	10%
Loans Past Due (1-30Days)	108,046	9%	56%	69,280	6%	(4%)	72,095	6%
Loans Past Due (31-90Days)	155,781	13%	63%	95,843	8%	145%	39,042	3%
Loans Overdue 91 to 180 days	36,177	3%	82%	19,916	2%	99%	9,997	1%
Loans Past Due (>181Days)	7,232	1%	(27%)	9,866	1%	8%	9,108	1%
Loans in Legal Recovery (<180Days)	0			0			0	
Total (Gross) Loan Portfolio	1,187,951		(1%)	1,197,087		31%	914,687	
Loan Loss Reserve	(100,508)		22%	(82,688)		57%	(52,785)	
Net Loan Portfolio	1,087,443	91%	(2%)	1,114,398	93%	29%	861,901	72%
Fixed Assets	53,137	4%	693%	6,697	1%	(35%)	10,245	1%
Prepayment (Electricity+Rent)	7,285	1%	(22%)	9,383	1%	(80%)	46,835	4%
Stocks (JHU-CCP+Solar Lanterns)	28,037	2%	83%	15,324	1%	663%	2,008	0%
Staff Debtors	2,133	0%	(46%)	3,927	0%	80%	2,186	0%
Other Assets	37,455	3%	31%	28,634	2%	(44%)	51,028	4%
TOTAL ASSETS	1,200,445		2%	1,175,708		26%	931,497	

9) Breakdown of Liabilities and Equity

Liabilties & Equity	2011			2010			2009	
SIF/ARB Apex Bank	123,017	42%	(5%)	129,492	33%	0%	129,492	51%
KIVA Micro Funds	0	N/A	N/A	0	N/A	N/A	0	N/A
ASSFIN/GCB Ltd	0	N/A	(100%)	1,683	0%	(91%)	18,429	7%
ASSFIN/MASLOC	0	N/A	N/A	0	N/A	(100%)	30,216	12%
MiDA /Bank of Ghana	99,495	34%	(45%)	181,385	47%	N/A	0	N/A
RHEMA	23,324	8%	(20%)	29,136	7%	N/A	0	N/A
Energy-In-Common	9,518	3%	167%	3,568	1%	N/A	0	N/A
EB-ACCION	11,006	4%	(32%)	16,186	4%	(73%)	60,916	24%
Liabilities with Others	266,360	91%	(26%)	361,449	93%	51%	239,054	94%
Accounts Payable (Sundry Creditors)	22,293	8%	(10%)	24,702	6%	83%	13,488	5%
Other Liabilities	0	N/A	N/A	0	N/A	N/A	0	N/A
Subscription (ASSFIN/GHAMFIN)	388	0%	50%	259	0%	N/A	0	N/A
TAX – PAYE	786	0%	183%	278	0%	N/A	0	N/A
Utilities – (Telephone: Takoradi)	0	N/A	(100%)	228	0%	(22%)	291	0%
Legal Fees	726	0%	80%	403	0%	0%	403	0%
Auditors	324	0%	0%	324	0%	67%	194	0%
Provident Fund	1,077	0%	(11%)	1,206	0%	(33%)	1,793	1%
Accruals	3,301	1%	22%	2,696	1%	1%	2,680	1%
Total Liabilities	291,955	24%	(25%)	388,847	33%	52%	255,222	27%
Share Capital	378,302	42%	0%	378,302	48%	0%	378,302	56%
Reserves	530,190	58%	29%	411,256	52%	38%	297,973	44%
Total Equity	908,492	76%	15%	789,557	67%	17%	676,275	73%
TOTAL LIABILITIES & EQUITY	1,200,447			1,178,405			931,497	

10) Overview of key indicators

	Gross Loan Portfolio		Financial Revenue/Assets		Financial expense/ assets	
	Average	**KSF**	**Average**	**KSF**	**Average**	**KSF**
2011	19,214,749	1,127,376	38%	4%	3%	3%
2010	4,909,349	1,240,870	38%	13.29%	6%	3.39%
2009	4,118,588	994,881	38%	8.87%	6%	1.98%
2008	4,445,172	1,057,102	36%	13.83%	6%	1.74%
	Return on equity		**Operating expense/ loan portfolio**		**Portfolio at risk > 30 days**	
	Average	**KSF**	**Average**	**KSF**	**Average**	**KSF**
2011	26%	6%	42%	7%	3%	17%
2010	4%	3.24%	51%	4.74%	6%	11.14%
2009	-4%	-6.48%	56%	9.10%	7%	5.77%
2008	-4%	0.92%	46%	12.36%	7%	7.91%

11) Loan Portfolio Breakdown

Kraban FNGO						
		2011		2010		2009
Loan Portfolio : Portfolio Aging Report	No. of Clients	Gross Loan Portfolio	No. of Clients	Gross Loan Portfolio	No. of Clients	Gross Loan Portfolio
Current Portfolio (PAR < 30 days)	7,265	1,506,820	7,265	1,675,580	8,801	1,331,923
Growth (%)						
PAR 31 -90 days	464	240,603	464	107,002	561	60,300
PAR 91 - 180 days	133	55,876	133	30,761	165	15,440
PAR 181 - 365 days	44	6,091	44	10,158	53	9,018
PAR > 365 days	22	5,079	22	5,079	26	5,050
Renegotiated loans	89	20,317	89	20,317		-
Total	8,017	1,834,786	8,017	1,848,897	9,606	1,412,731
Write-offs, during the period	215	33,777	215	31,491	195	19,458

12) Data checklist for social performance section

CUSTOMER PROFILE	STATUS OF CLIENTS	INTERACTION WITH THE MFI
Name	Poverty status of the client	Credit Officer Name
Age	**Social status indicators**	Number of clients per loan officer
marital status	State of health	MFI services accessed:
Sex	Dwelling	Type and purpose of credit
Number of people under guardianship	Access to food	Other services offered
Level of customer education	Value of the assets	Transactions made:
Occupation or sources of income	Level of education	Collateral
Previous business experience	Business value	Credit cycle
Location (urban / rural)	Savings:	Amount awarded
Quality of local infrastructure:	Quantity	Liquid accounts
Electricity, water, transport access	Regularity	Savings deposits (SUSU)
Market Conditions	Located within the community	Payment in arrears
Previous experience with other MFIs	Assistance:	
In MFI since (date)	Group Meetings	
	Training	
	Self-help services	

13) CAMEL Analysis (Please see section 9 for a score overview)

The application of the conventional analysis of a financial institution does not identify the strengths and weaknesses of microfinance institutions for three reasons:

1. They develop their activity in unstable macroeconomic scenarios, with high inflation, which can significantly impact their financial statements. The main assets of MFIs are of monetary nature and the real value of equity decreases with time, representing an unrealized loss for the entity that is not always registered for accountancy purposes.

2. Due to its social character, most of them are subsidized entities; therefore, in order to determine the financial sustainability of the microfinance activity *per se*, the analysis must distinguish between the subsidized part and that which is not. Thus, we can get an idea of the institution's financial performance and the quality of its loan portfolio, and we can also compare it with other entities.

3. The poor quality of available information, both in the absence of third parties contrasting reports (audits, rating agency reports, reports from industry analysts, reports from the supervisory body, etc..), and the lack of technical and human resources regarding the accounting and financial reporting system.

These characteristics have created a need to make an accurate adaptation of the tools of conventional financial institutions´ analysis and evaluation to microfinance. One of the best-known methodologies for the analysis of

MFIs is the ACCIÓN International's CAMEL. The issues discussed in this methodology is available on line at http://www.mixmarket.org/sites/default/files/medialibrary/10011.150/CAMEL.pdf

The CAMEL standards used to rate ACCION affiliate institutions are no less rigorous than those applied to traditional financial institutions. These high standards apply to asset quality, profitability, and other key indicators, and in some areas, such as provisioning requirements and leverage limits; the ACCION CAMEL standards are even more rigorous. ACCION's development and use of the CAMEL is one of several efforts contributing to the establishment of a set of worldwide microfinance performance standards

Perspective

While the ACCION CAMEL plays a critical role in the development and management of healthy and sustainable microfinance institutions (MFIs), it is not an all-purpose tool. It is important to know the CAMEL instrument measures and what it does not. According to Rhyne and Otero (1994), the two pillars of success for microfinance are scale and sustainability. Scale refers to the degree to which an MFI reaches its target market, in other words, the extent of client coverage. Sustainability refers to the extent to which, in reaching its target market, an institution covers the costs of providing financial services after adjustments to its profit and loss statement. The ACCION CAMEL assessment instrument measures the level of sustainability of an MFI. However, it does not rate the institution in terms of client coverage per se, but rather, for example, it measures the financial implications of client coverage for the institution in terms of efficiency and profitability. Also, the CAMEL does not rate the institution in terms of *social* or *economic impact* at the **client level**. It is important to remember this fact when analyzing the MFI as whole.

Financial Statement's Adjustments

For better analysis of the nature of an MFI, ACCION´s CAMEL proposes six previous adjustments to the financial statements. Below, we will assess their impact on KSF, based on the financial statements (USD denominated)

Adjustment 1: Non-Microfinance Activities

This adjustment is intended to exclude from analysis any activity not related to microfinance. It does not apply in KSF's case because all its income is derived from microcredit activity.

Adjustment 2: Portfolio Impairment

CAMEL proposes an adjustment to the loan loss provision percentage rates according to defaulted loans aging. The provisioning rates are based on the experience of ACCIÓN International.

According to KSF's 2011 Audit Report, the institution' annual provision (Loan Loss Reserve as a % of Gross Loan Portfolio) has increased from 6% in 2009 up to 8% in 2011. Their policy is based upon intuition gained from experience, but the increasing provision suggests an increasing impairment issue.

By applying the CAMEL's 2009-2011 accumulated loan loss provision adjustment, a 42.8 thousand USD shortage in the reserve is found. This represents 3.6% of the total portfolio, and would increase the provision from 100.5 thousand USD to 143.3 thousand USD: In terms of the total portfolio this represents an increase from 8.5% to 12%. The following chart shows the development and detail of the adjustment:

Last year's report strongly penalized KSF for not having a complete breakdown of their loan portfolio, meaning they did not follow exactly the ACCION recommended structure:

Rescheduled Aging Status
Current Loans
Rescheduled Loans (Current)
Loans Past Due 1-30 Days
Loans Past Due 31-90 Days
Loans Past Due 91-180 Days
Loans Past Due >180 Days
Loans in Legal Recovery <180 Days

It should be noted KSF has improved on this issue and is now following the above structure almost perfectly. Yet, they could still be further rigorous in their approach. For example, while they did provide a figure for Rescheduled Loans, they were not broken down into time frames, for example, 1-30 days, 31-90 days, and so on. For this matter, we assumed the amount for Rescheduled Loans to be 1-30 days, possible risk under-estimation.

Given that the risk of loan loss is the one of, if not the most important determinant in the decision making of potential investors, we also recommend KSF to adopt a more concrete policy for the calculation of the reserve portfolio impairment (such as the system proposed by the CAMEL method).

Adjustment 3: Non-performing Loans

Typically, unregulated microfinance institutions do not cancel their bad loans on their balance sheets, since they are not legally compelled to do so. Consequently, their assets get increased artificially. The adjustment proposed by CAMEL considers any 180+ days non-performance credit as bad loans or litigious. At December 31st, 2011, KSF must canceled 7.2 thousand USD from its balance sheet with the following details:

Write-off Adjustment (% over portfolio, growth %)

	2011			2010			2009	
Adjustment	**(2,633)**	**-1%**	**-448%**	**757**	**0%**	**-92%**	**9,108**	**7%**
>180	7,232	2%	-27%	9,866	5%	8%	9,108	7%

KSF cancel from the total loan portfolio all the Non-performing loans (>180 days) as defined by ACCION. They should charge it to reserves, so that portfolio accurately reflects the total amount of recoverable credits. If the loans have been rescheduled, this should accurately be noted in the total loan portfolio breakdown.

Given that the loan loss reserve has been previously adjusted to absorb the write off, there is no net effect neither on the balance sheet nor the income statement. Although there is no impact on the financial statements, this adjustment provides more reliability and credibility to the management or financial reporting and accounting that KSF develops.

Adjustment 4: Explicit & Implicit Subsidies

To determine the viability of an MFI and to determine the entity's ability to cover the cost of financing at commercial rates, the financial statements must be adjusted for subsidies.

In this sense, we distinguish between the effect of donations (which are generally accounted as current income) and debt at below-market rates. The adjustment considers the former as equity investments, while for the latter, the difference between the subsidized price and the commercial rate is considered a higher financial expense. Note, CAMEL regards subsidized debt to all those liabilities at a cost of less than 75% of the market price which the entity has normally access to.

When applying this adjustment in KSF, although grants and donations are clearly identified in the financial statements, it has not been possible for us to determine the cost of debt of KSF, since we did not have access to precise information on the maturity structure of liabilities.

We've been forced to approximate using the weighted average cost of debt at the end of the period. As shown in the chart below, the cumulative adjustment at December 31, 2011, is 63.2 thousand USD.

End of Period Debt USD (% and weighted average rate)

	2011			2010			2009		
	Amount	%	tipo	Amount	%	tipo	Amount	%	tipo
Subsidized Debt	232,030	87%	11.99%	314,444	87%	12.36%	159,708	67%	12.03%
Commercial Debt	34,330	13%	30.53%	47,005	13%	30.90%	79,346	33%	30.00%
	266,360		14.38%	**361,449**		14.77%	**239,054**		17.99%
Adjustment of Subsidized Debt USD (% increase over original financial expenses)									
Financial Expenses	4,058			23,306			14,292		
Adjustment	79,352			49,939			33,620		
Adjusted Financial Expenses	**83,410**	**1956%**		**73,245**	**214%**		**47,912**	**235%**	
Accumulated Adjustment	162,911			83,559			33,620		

We estimate that KSF would have to support financial expenses of 1956% higher if it had no access to subsidized debt. Given the limited room for maneuver on the rest of their operating costs, we believe that the only way to bear this financial burden would be to apply its clients an average rate of interest as close as possible to the APR (Annual Percentage Rate) set by the CAMEL Method for sustainability. For 2011, we calculated an APR rate of 43.68%, however it fluctuated year to year. In 2010 it was 41.81% and in 49.23% in 2009.

Within this section it would also be necessary to adjust the services provided at below- market price and other gratuities. Even if according to the information provided by KSF there are no items of this nature, We recommend KSF to adopt measures in order to clearly identify in its accounting records, all the services (personnel cost, supplies, outsourcing etc.) provided at a price below market, indicating the amount subsidized in each one (obtained by the difference between actual price and market price), in order to better monitor the sustainability of the activity.

Adjustment 5: Inflation

This specific adjustment devalues equity and revalues fixed assets by inflation data (year to year, end of period) and compares it to the provision recorded to the effect, if it exists. KSF does not make any adjustment in accounting, showing an undervaluation in real terms of equity, since they are funding primary monetary assets (loan portfolio represented +90% of assets in 2011). In this case, KSF has to take into account the effect of inflation because their own funds have suffered a loss of value of 22% using 2009 as a starting point.

As shown in the chart below, the loss is barely compensated for the revaluation of fixed assets, and is a cumulative 21% of the total equity in 2010. This would be the percentage in which KSF should increase its capital in nominal terms in its aim to maintain the value of the portfolio in real terms and thus to ensure sustainability and solvency (ratio: active on equity). In this sense, the entity should affect inflation to their customers as an additional financing cost.

Inflation Adjustment (USD, % of Equity)

	2011		2010	
Inflation	9%		15%	
Equity	908,492		789,557	
Fixed Assets Revaluation	2,767	0%	1,298	0%
Equity Devaluation	(78,514)		(112,319)	
Annual Adjustment	(75,747)		(111,021)	
Accumulated Adjustment	(186,768)	21%	(111,021)	14%

By the effect of inflation, KSF should increase the average size of its portfolio: first, to remain being competitive for their clients, who will require higher amounts in nominal terms, and second, to be efficient from an operational standpoint, offsetting the effect of inflation on operating costs (assuming it does not affect the gross margin). If KSF does not take account of this fact, its operational efficiency and competitive market advantage are greatly reduced overtime.
The improvement in inflationary expectations in Ghana for the next few years allows estimating a lower impact in this respect in the coming years.

Adjustment 6: Accrued Interest
This adjustment reduces revenues in the amount of accrued interest on non-performing loans (>30 Days). Given the high portfolio turnover and frequency of payment typical of the microfinance industry, the recording of accrued interest is rare and typical a negligible amount.
Following the CAMEL methodology, if the institution does not accrue interest, no adjustment is necessary. As KSF does not have an accrued interest account, we have decided not to make this adjustment.

Camel Indicators
CAMEL methodology analyzes 21 indicators. Eight of them are quantitative and have an overall weight of 47% in the final scoring, while the remaining thirteen are qualitative and overall weight of 53% of the final score. The score at the end is a number on a scale of zero to five, five being the measure of excellence. Like rating agencies, this numerical score also corresponds to an alphabetic rating (AAA, AA, A, BBB, BB, B, C, D, and unclassified).

The result of our analysis for KSF is a **C** rating.

Below covers all of the quantitative scoring sections, as well as some of the qualitative. Management & Governance were qualitative decisions based on our research and the different scoring criteria.

Capital Adequacy

The objective is to measure KSF´s financial solvency in order to determine whether the risks are adequately compensated with capital and reserves, so that they can absorb losses.

- **Leverage:** it is the relationship between weighted assets by risk level and its own equity. The observed KSF´s ratio is 1.57 times for 2011. It is positive that the leverage is low because these entities are normally more exposed to bad debt, operating expenses are higher compared to other financial institutions and finally because the possibility for NGOs to attract new funds is more limited than of a commercial bank.
- **Reserves´ Sufficiency:** Measures the extent to which the institution is able to absorb hypothetical future losses by loan portfolio impairments. The level of provisions made by KSF is 70.1% above those required by the model, taking into account the level of delinquency that KSF has for different periods.

Ability to obtain Capital: Assesses KSF´s ability to respond to a need to increase the equity in a given time. The institution is able to maintain its capital in real terms, but relies on donations from individuals, corporations and development institutions, which, in case of shortage, would adversely affect the entity.

Aspects for improvement and recommendations:

- KSF has improved its record keeping of loan disbursements, most notable using the aging schedule suggest by ACCION. We encourage KSF to become even more rigorous in its record, primarily through a breakdown of the total loan portfolio by the type of loans it consists of. For example, it would be interesting to know in detail the % breakdown of urban versus rural loans, the duration of the different loan types and the average duration of total loan portfolio. We suggest KSF to incorporate this level of detail in its already existing excel record keeping database.
- Regarding KSF's ability to mobilize a significant amount of private sector capital and obtain commitments of future capitalizations, we believe it would be useful for KSF to create an investment proposal that specifically covers a how KSF would use a hypothetical amount of money, for example, $20-50 thousand USD. Explaining to investors exactly how the funds would be disbursed and the overall timeframe for collection interest and principal repayments. Describing the life of a hypothetical loan would enlighten investors to how KSF plans to use the funds, gather repayment and principal, and finally repay back investors. In addition, we also realize this report itself also lends to providing potential investors with an idea of investing in KSF.

Asset Quality

- **Portfolio at Risk:** measures past due loans over 30 days. Typically, loan terms in microfinance institutions are between 120 to 180 days with weekly repayments, and therefore any delay in payments of more than 4 weeks is considered at risk of default. Using the calculation methodology of CAMEL, the PaR for KSF is 21.60%. This fairly high number comes from a significant portion of the portfolio being 31-90 Days past due, in addition to a significant amount of rescheduled loans.
- **Non-performing Loans:** Reflects the portfolio impairment according to the risk weight assigned by the model for delinquencies of more than 180 days. Identifies 0.6% of its portfolio as uncollectible KSF.
- **Portfolio Classification System:** This is the qualitative review of the terms of the portfolio impairment and the assessment of the institution´s policies associated with the portfolio at risk. Last year KSF did not have a portfolio classification as promoted by ACCION. However, this year, they did provide us excel documentation and they appear to have moved to the Rescheduled Aging Status recommended by ACCION.
- **Productivity and Long-Term Assets:** The institution manages its assets over time without a thorough analysis of its impact on the entity. However, at this time, this lack of analytical rigor does not represent a risk to the institution. Fixed assets primarily consist of leasehold, equipment, motor vehicles, and furniture. Vehicles contain the most risk as they are used for the long-trips to rural areas. KSF takes care to maintain the quality of its vehicle so that can utilize them for a long time.
- **Infrastructure:** The institution has an infrastructure that may not guarantee maximum productivity, but is adequate in almost all respects. They have field offices in their rural locations, and their headquarters in

Accra provide room for 8-12 person meetings. In addition, they utilize their own vehicles to make weekly trips to clients.

Aspects for improvement and recommendations

- KSF must describe why a significant amount of loans are >30 Days past due, whether this is a one-off item or a long-term structural problem. A more rigorous classification of loans, including duration of the loan and when interest payments take place.
- Rescheduled loans must be broken down on 1-30 Days, 31-90 Days, and so on.

Earnings

- **Return on Equity (ROE):** Measures the ability of the institution to maintain and increase wealth through income from operations. Primarily due to adjustments made in the CAMEL provisions of the loan portfolio and the effect of inflation upon equity, ROE in 2011 for KSF was -22.4%.
- **Operational Efficiency:** Measures and monitors progress toward achieving a cost structure that is closer to the level reached by formal financial institutions. The total operating costs on the portfolio incurred by the institution are only 6.4% of the loan portfolio.
- **Return on Assets (ROA):** Measures KSF's assets ability to generate revenue. Again, the CAMEL adjustments to the loan portfolio and equity negatively, ROA was -17% in 2011 for KSF.
- **Interest Rate Policy:** Measures the extent to which the entity's management analyzes and adjusts the interest rate, taking into account the institution's loan portfolio, and the cost of funds, the goal of profitability, and the macroeconomic environment. A key indicator of sustainability for any MFI is the annual percentage rate (APR). This figure takes into account the costs incurred by the institution, its growth prospects and economic environment variables of the country where the activity occurs. The result gives a guide to the MFI about the average interest should be set to its products in order to become self-sustaining and less dependent on donations.

The APR result for KSF obtained by our analysis is 43.68%, in Ghanaian New Cedi monetary terms. Compared to their 30% average interest rate policy, we can see why a strong structural dependence of its operations on grants and donations. KSF appears to set its interest rates based solely on the market for loans charged by formal and informal lenders, and does not include a cost analysis in the equation of setting interest rate policy. However, it should be noted that the ability of KSF's client to pay a higher interest rate is not clear, and further research is necessary. Finally, it is important to remember the social mission KSF is serving, one of empowering individuals and communities to better their lives and alleviation from poverty. This fact must be taken into consideration when considering the appropriate interest rate. This does not mean KSF does not have the ability to pay back a loan and handsome return to investors, but the issue being what kind of return investors desire, taking inflation, social and other factors into account.

Aspects for improvement and recommendations

- Overall profitability is affected in the CAMEL model by inflation effects, adjustments to the loan portfolio, and adjustments made for grants and donations. The ability of KSF to combat these effects to charge an appropriate interest rate to compensate these events.. The appropriate interest rate range and appropriateness depends on a number of factors. We suggest KSF provide an overview of the types rates it could charge, the returns it could provide to outside investors, the timeframe necessary to deliver those returns, and the risk factors that could affect KSF's ability to meet those returns.

Liquidity Management

Assesses KSF's ability to respond to 1) decreased funding sources and increases in assets, and 2) payment of expenses at a reasonable cost.

- **Productivity of Other Current Assets:** This indicator focuses on management of current assets that do not belong to the loan portfolio, especially investments in short-term cash. KSF utilizes the use of its cash, bank accounts, and short-term investments by investing in accounts that provide the highest possible return while balancing the need to liquidate quickly if necessary. ACCION states that treasury management should be consistent with the liquidity needs of the institution for its operations. This indicator penalizes whether an entity's investments are very conservative or very aggressive. KSF's result was 49% for 2011, most notable because loan disbursement in 2011 were much lower than in 2010, thus lowering the liquidy.

- **Debt Structure:** This indicator analyzes the composition of the liabilities of the institution, including the amount, interest rate, payment terms, and sensitivity to changes in the macroeconomic environment. The institution has a funding strategy that neither minimizes funding costs nor leads to an optimal structure. However, KSF can access commercial loans via the Ghanaian financial system.
- **Availability of Funds to Meet Loan Demand:** Although KSF currently has the necessary funds to meet its clients' credit demands, during our field visits many clients were eager for another round of financing, but seemed to still be waiting for the new round of financing. Additionally, KSF has made clear their own desire for more funding because they know there are additional areas that could grow their business, in-addition to re-investing in clients more quickly.
- **Cash Flow Projections:** This indicator measures the extent to which KSF is successful in projecting their cash flows needs. The analysis seeks to determine if they have prepared with sufficient detail and analytical rigor, and whether past projections have been adjusted accurately to the inflow and outflow of money. KSF's cash flow management is based on past experience rather than cash flow projections. Due to its operation size, this probably sufficient but we high recommend they begin to input a process that analytical tracks cash flow movements and allows them to project them on a forward basis.

Aspects for improvement and recommendations

- KSF needs to implement a system that tracks cash flows, and one where it is easy to understand by outside parties. The ability of potential investors to view cash receipts from repayment of loans and others sources, as well as expense receipts, is key in their ability to make a knowledgeable decision about whether to lend to KSF.
- Investments in other current assets must take into account the liquidity needs of the company. The methodology behind this must also be available to potential investors.

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