Microfinance
A new commercial investment opportunity?

UNEP Finance Initiative
Barcelona, 19 May 2005
The economically active poor – a huge need

- c. 2 billion people living under poverty threshold
- c. 500 million micro-enterprises
- c. USD 500 credit need per micro-enterprise per year
- need for credit, but also savings, insurance, pension, transfers
- demand is still largely unmet
Microfinance - a specific market segment

- informal rural & urban areas of emerging markets
- micro and small enterprises
- a very dynamic, grassroots economic sector
- a vast untapped potential – bottom of the pyramid linkage
Microfinance - a truly commercial approach

• No need for charity but flexible provision of adapted financial services
• No contradiction with social objectives
• Lasting social impact through profitability
• Greater outreach through commercialisation
• Acceleration of growth through K markets access
• Microfinance is a new segment of global finance
Microfinance - investment impacts

• strong link to family economics
• stimulating grassroots entrepreneurship
• growth of micro and small businesses, job creation
• raising family living standards
• reinforcing self-esteem
• community & financial infrastructures development
• dynamic inter-generational virtuous cycles

⇒ A very efficient way to alleviate poverty,
⇒ 2005, the UN year of Microfinance
Micro-banks / local financial services providers

- microfinance institutions as specialized financial intermediaries
- different legal formats (banks, NBFC, cooperatives, NGOs, etc.)
- increasingly regulated entities (65% of DMCF clients)
- know intimately the sector in which they operate
- created financial products adapted to target segment
- developed specific delivery channels (ensuring proximity)
- included sophisticated IT developments (ATMs, palm pilots, etc.)
Micro-banks / different segments

- thousands of microfinance programs worldwide
- c. 250 sustainable/commercial micro-banks
- efficient financial intermediation
Micro-banks / strong track record of leaders

- excellent track-record over past 10 to 15 years for leading MFI
  - solid profitability (ROE in the 20s is usual)
  - very fast growth (average DMCF clients = 40% per year over last 3 years)
  - low portfolio at risk (average default rates of 3%), excellent diversification
  - products and services range adapted to client needs
  - low D/E ratios, high solvency
  - very good MIS systems and reporting capabilities
  - solid governance and high professionalism of boards and management
  - access to many commercial sources, no subsidies at all
Micro-banks / examples

<table>
<thead>
<tr>
<th>December 2004</th>
<th>UMU Uganda</th>
<th>Share India</th>
<th>Compartamos Mexico</th>
<th>TSKI Philippines</th>
</tr>
</thead>
<tbody>
<tr>
<td>Assets</td>
<td>M$ 17.05</td>
<td>M$ 32.50</td>
<td>M$ 133.4</td>
<td>M$ 11.80</td>
</tr>
<tr>
<td>Loan Portfolio</td>
<td>M$ 10.08</td>
<td>M$ 28.70</td>
<td>M$ 101.2</td>
<td>M$ 7.40</td>
</tr>
<tr>
<td>Clients</td>
<td>36,864</td>
<td>328,846</td>
<td>309,637</td>
<td>122,832</td>
</tr>
<tr>
<td>Average loan size</td>
<td>$273</td>
<td>$87</td>
<td>$327</td>
<td>$60</td>
</tr>
<tr>
<td>PAR (30 days)</td>
<td>4.5%</td>
<td>0.00%</td>
<td>0.57%</td>
<td>1.65%</td>
</tr>
</tbody>
</table>
Microfinance - a nascent global financial segment

- Increased attention and specific legislation by regulators
- Audits by superintendents of banks
- External annual audits by recognized local auditors
- Ratings by top rating agencies and specialized rating agencies
- Creation of credit bureaus
- Formation of local intermediaries’ associations
- Development of international microfinance networks
- Clear commercialization trend of microfinance
- Multiplication of investment funds both in debt and equity
Microfinance debt - a new asset class?

- attractive to both institutional and individual investors
- unique combination of social and financial returns within same product
- very high and effective social impact
- appealing financial risk – return profile
- limited credit risk
- High insulation of microfinance sector from macroeconomic shocks
- low correlation with other asset classes in portfolio
- low volatility of financial returns
- attractive fast growing industry
Microfinance - Importance of Global Microfinance Funds

• Provide diversification of funding sources to MFI
• Provide fast and flexible access to funding
• Complement the domestic capital offering
• Serve as catalyst and demonstration effect for local capital
• Maintain demanding reporting standards
• Introduce Microfinance practitioners to new investors’ segment
• Provide opportunity to investors of doing well by doing good
BlueOrchard Finance : a specialized asset manager

• **Microfinance** : not charity, but provision of financial services to specific unattended segment of entrepreneurs (the working poor of the world);

• **Our mission** : to promote social and economic development through Microfinance by facilitating access to capital markets

• **Our philosophy** : there is no contradiction between social impact and commercial investments; Profitability is key to sustainability of impact, flows of funds growth and greater outreach

• **Our company** : A for-profit asset manager created in 2001, based in Geneva; a 10-person team exclusively focused on Microfinance; about $135 million under management
BlueOrchard Finance – *Our adapted product offering*

**• Dexia Micro-Credit Fund (Manager)**
- Luxembourg SICAV part 2, launched in September 1998 by Dexia-BIL
- Targeting leading and transforming MFI with short term debt (max. 3 years);
- 6-year track record, over 230 loans made, no default, net USD return 34.3%
- Total assets: $60 millions, 51 MFI, 21 countries
- Fast and flexible delivery of loans

**• BlueOrchard Microfinance Securities I, LLC (Manager)**
- Delaware (USA) Special Purpose Vehicle
- Targeting the best MFI worldwide with 7-year debt at fixed rate
- First securitization of portfolio of international loans to MFI
- Total assets: $80 millions, 14 MFI, 7 countries
- In collaboration with OPIC and JPMorgan securities / Chase
BlueOrchard Finance – Our adapted product offering

- **ResponsAbility Global Microfinance Fund** (Main partner)
  - Luxembourg registered FCP
  - Different debt segments
  - Total assets: $12 millions, Debt: 22 MFI, 12 countries
  - Fund sponsor: Crédit Suisse Bank
Dexia Micro-Credit Fund : NAV (May 2005)

- Only private investors (individual and institutional)
- Very few historical redemptions (long average holding period)
- Increased interest from large institutional investors (pension funds)
Dexia Micro-Credit Fund: portfolio (May 2005)

Geographic diversification

- Africa: 3%
- Eastern Europe: 19%
- Central America: 21%
- South America: 26%
- South Asia: 2%
- East Asia: 5%
- Central Asia & Middle East: 3%
- Liquidities: 21%

USD Millions

- Nicaragua
- Ecuador
- Bosnia
- Hertzegovina
- Peru
- Russia
- Mexico
- India
- Cambodia
- Bolivia
- Colombia
- Serbia and Montenegro
- Philippines
- Uganda
- Kyrgyzstan
- Mongolia
- El Salvador
- Kazakhstan
- Tanzania
- Albania
- Kosovo
Dexia Micro-Credit Fund : the track record (May 2005)

- Net return of $Libor + 2% delivered each of the past 5 years
- Very low volatility of financial returns
- No correlation with other asset classes
- Good liquidity (monthly) at no cost

<table>
<thead>
<tr>
<th>USD Asset Class</th>
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<tbody>
<tr>
<td>Share price</td>
<td>13,434.5 USD</td>
</tr>
<tr>
<td>Creation date</td>
<td>09/1998</td>
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<tr>
<td>Cumulated return</td>
<td>34.3%</td>
</tr>
<tr>
<td>2000 ROI</td>
<td>7.77%</td>
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<tr>
<td>2001 ROI</td>
<td>6.78%</td>
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<tr>
<td>2002 ROI</td>
<td>4.10%</td>
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<tr>
<td>2003 ROI</td>
<td>3.21%</td>
</tr>
<tr>
<td>2004 ROI</td>
<td>3.95%</td>
</tr>
<tr>
<td>2005 ROI (YTD)</td>
<td>1.39%</td>
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<tr>
<td>Last month</td>
<td>0.45%</td>
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Dexia Micro-Credit Fund
Investment process

• Complete data collection
• Field visits and cross checks at industry level
• Independent external rating
• Credit committee
• Monitoring on a monthly basis (web enabled database)
• Field visit checks at least once per year for each MFI
Dexia Micro-Credit Fund
Investors’ profiles and available services

• both individual (private banking) and institutional
• mid to long-term investment horizon
• interested in unique combination of financial and social returns
• trust based on excellent > 6 year track record
• tickets range from $10,000 to $5,000,000
• monthly newsletter detailing performance of fund
• individual presentations possible
One key bottleneck to faster growth

• Foreign exchange risk
  – Prohibits major entry in entire regions
  – Lack of instruments on commercial markets
  – When hedging opportunities exist, very expensive
  – We need alliance with major financial player or alternative mechanism