Throwing in the Towel:

Lessons from MFI liquidations

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For the FOCCAS case, in collaboration with
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The MFI liquidation cases rely almost exclusively on interviews of individuals who had first-hand knowledge of the situations. This record would not exist were it not for each person's willingness to share their experiences. To each of them – a special note of thanks!

Thanks also to the helpful souls at CGAP, without whom the author would have never found half the cases here.

Contents

INTRODUCTION **3**

ANALYSIS **4**

Microcredit as an "asset" 4
Servicing Transfers *4*
Repayment incentive *6*
Whither the MFI, Thither its Portfolio *7*
Risk to MF investors 8
Microfinance credit risk → MFI default risk *8*
Investing in Microcredit Portfolios *8*
Risk of Different Investment Types *9*
Servicer Risk *10*

RECOMMENDATIONS **11**

Pre-default *11*
Post-default *11*

CONCLUSION **13**

APPENDIX **14**

SOMED, Uganda 14
WEEC, Kenya 16
Bank Dagang Bali, Indonesia 18
FOCCAS, Uganda 20
ICICI Bank, India (Andhra Pradesh Crisis) 25

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Introduction

In June 2006, FOCCAS, a once promising Ugandan MFI with an unusually committed client base, became insolvent and was closed. Its socially responsible (SR) creditors recovered nothing from its liquidation.

In April 2007, WEEC, an up-and-coming Kenyan MFI lost its founder/director to an untimely death, and defaulted on its debt soon after. Its SR creditors recovered nothing.

In September 2008, Washington Mutual, one of the largest US banks and also one of the top subprime lenders, was shut down by regulators following extensive losses in its mortgage portfolio and a $17 billion run on its deposits.[1] However, its depositors and secured creditors suffered no losses.[2] Unsecured creditor losses were expected to reach $12 billion[3] or about 4% of its total assets.[4]

On its face, the comparison may seem a bit facetious – a $300 billion bank is hardly similar to institutions that may not even break $1 million. However, the comparison is important for one reason: in the microfinance world, recoveries by creditors following an MFI's collapse are rare. When MFIs fail, pursuing liquidations, even in the presence of relatively strong portfolios, is often deemed too costly and too difficult for SR investors to attempt. This may be unsurprising, given the often weak legal (judicial and enforcement) systems in the countries where many MFIs operate. As it turns out, these are not the only, nor even the primary obstacles to carrying out successful liquidations, so even when liquidations are attempted, results can be woefully inadequate. In fact, more often than not, SR investors walk away empty-handed.

Why should liquidations matter? In the course of my research, it has been noted by several prominent individuals in the microfinance community that since MFI failures are so rare, issues such as liquidations are really academic. To a degree, this is true. However, as I can attest directly from having worked in the mortgage market since 2001, periods of good financial performance are exactly the time to be developing strategies for coping with crisis, and not after-the-fact. Simply put, there is no reason to believe that microfinance is immune from business cycles. To the contrary – there is enough recent evidence (dot.com, housing) to suggest that industries that espouse this belief are treading down a path that leads to a particularly expensive lesson.

Drawing on interviews of MFI directors, executives and creditors who have directly experienced an MFI liquidation, this paper analyzes what makes these liquidations so different from those of traditional financial institutions, and provides suggestions for making them more effective. Five detailed MFI liquidation case studies are provided in the appendix.

[1] Office of Thrift Supervision, OTS Fact Sheet on Washington Mutual Bank, 25 September 2008
[2] FDIC website (http://www.fdic.gov/bank/individual/failed/wamu.html#possible_claims), retrieved 25 August 2009
[3] FDIC website (http://www.fdic.gov/bank/individual/failed/wamubalsheet.html), retrieved 25 August 2009
[4] JPMorgan Chase, WaMu's buyer, was a beneficiary of the US Treasury's Troubled Asset Relief Program (TARP), and it could be reasonably suggested that the US government was thus responsible for indirectly repaying WaMu's creditors. However, JPM was among the first to repay the TARP funds, and its executives have been adamant that they were forced to take them to provide cover for weaker banks who actually needed the help.

Analysis

Microcredit as an "asset"

For property to be considered an asset, it must generally retain value irrespective of its owner. However, in rare cases, assets have value only when associated with a given entity. Like David Beckham's foot, such assets can generate cashflow to their owners, but they cannot be independently transferred or sold. In accounting parlance, certain types of "goodwill" share this distinction – for example, the institutional knowledge of an organization can be very valuable, but it only retains its value so long as sufficient number of long-term staff is retained. Consequently, in the course of liquidation, such assets can be converted to cash only if the entire organization or large parts of it are sold in whole.

Microcredit appears to be just this type of asset. A microcredit portfolio is so closely associated with the MFI which created it, that it is in fact very difficult to realize its value without the MFI's organization. The natural consequence of this relationship is that to an outside party, the value of a microcredit portfolio becomes largely dependent on the default risk of the MFI itself. In effect, though creditors may have direct or indirect recourse to the portfolio, realizing its value via liquidation can prove quite challenging, often causing creditors to suffer far greater losses than even a conservative balance sheet would indicate.

Servicing Transfers

A servicing transfer is the move of the loan payment collections, reporting and related processes from one organization to another, regardless of who owns the loans. The ability to transfer servicing is a critical requirement for establishing true economic ownership of a loan, since without it, the ownership becomes effectively dependant on the servicer. In microfinance, executing a servicing transfer appears to be particularly challenging. To understand why, it's helpful to compare the collections processes between microfinance and traditional banking.

Microfinance, more than almost any other financial business model, is highly relationship-driven, with borrowers staying in direct and regular contact with their loan officer. In group-lending models, which dominate microfinance activities in many countries, the loan officer or designated MFI agent is responsible for group formation, client evaluation, and other activities long before the first loans are disbursed. Often, that same officer is responsible for then disbursing the loans and collecting payments. Although this might be reminiscent of the traditional banking mantra to "know thy client," and many successful traditional bankers do in fact establish long-term relationships with their clients, the servicing activities in banking are almost never conducted by the same individual, and instead are handled by a separate and fairly anonymous processing center. It is in fact common for traditional banks to outsource loan servicing to separate organizations, or at a minimum, to maintain separate payment processing centers independent of its neighborhood branches. Thus, when a loan has a servicing transfer, the sole indication to the borrower is a short letter from the new payment processing center, along with the newly addressed payment stubs. This is an important contrast to the close and continuous contact MFIs

maintain with their borrowers. Unsurprisingly, transferring the servicing of microloans to a different institution entails a far more complex process.

In such a process, new collections officers must be sent to visit clients whom they have never met. In the unmapped/unmarked address system common in areas served by MFIs, simply the task of finding clients is hardly straightforward, and once found, convincing them that the person seeking the payment is authorized to do so can be another challenge. For group loans, assuming at least some number of group meetings were already missed in the intervening period between the original MFI's failure and the arrival of the new collections officer, it will take additional effort to restart group meetings. Finally, not to be underestimated, a still significant percent of MFIs do not have up-to-date, centralized loan reporting,[1] and it is likely that gathering the required repayment information would take additional effort & time, especially if the MFI's staff is uncooperative. Thus, the time and cost of setting up new collections on a large portion of the portfolio is itself significant, and this is exacerbated further by the small size of the loans.

Given the difficulty of executing a servicing transfer for a microfinance portfolio, perhaps it's not surprising that they have either never happened, or have been incredibly rare. One process that some may consider similar to a servicing transfer is an MFI merger, but the comparison is a very distant one – a merger involves keeping loan officers from both organizations in place (at least initially), and requires extensive planning and collaboration from both parties to ensure success. To compare this to a servicing transfer involving an entirely new set of loan officers, especially without the cooperation of the original MFI, is another matter altogether. Apparently, even planning for such a transfer is too much of a challenge – in the groundbreaking BRAC securitization of 2006, the final deal did not name a backup servicer, despite the fact that the need for one had been identified.[2] Similarly, ICICI Bank specifically cited servicer risk as something to be addressed in its MFI Partnership program,[3] though as of February 2008 had not done so.[4]

Perhaps discussing servicing transfers in the microfinance context is a moot point altogether. To use the example of BRAC above, in the unlikely case of its collapse, independently replacing its enormous loan servicing organization within any reasonable timeframe would be a near-impossibility. Even bringing in another organization with loan officers already on the ground would be a very serious challenge, since, in addition to the obstacles outlined above, the new organization would face an enormous increase in its workload.

The candidates that may potentially avoid some of these pitfalls are microfinance operations that utilize alternative payment systems – such as local merchants, mobile payments, commercial bank branches,

[1] CGAP, 2008 Microfinance Technology Survey, March 2009
[2] Ray Rahman and Saif Shah Mohammed, BRAC Micro Credit Securitization Series I: Lessons from the World's First Micro-Credit Backed Security (MCBS), published by MFAnalytics, Boston, 20 March 2007
[3] Bindu Ananth, Financing Microfinance: the ICICI Bank partnership model. Small Enterprise Development, Vol. 16, No. 1. (January 2005), pp. 57-65.
[4] Tanushree Chatterjee, Commercial Team – Microfinance and Agriculture, ICICI Bank, email interview, 25 February 2008

and so on – for which it would arguably be easier to transfer servicing. In such cases the contact with the individual borrowers is already intermediated, so technically investors would only have to work with the intermediaries, instead of the borrowers themselves, which, at least in theory, would make significant recoveries without the MFI somewhat more plausible. That said, forgetting the borrowers would be a mistake, because before collecting payments, one must first insure that borrowers continue to be interested in making them.

Repayment incentive

In traditional microfinance, whether group- or individual-based, one of the key repayment incentives for MFI borrowers is their expectation of future loans. This is further magnified by the widespread practice of growing loan sizes at each repayment cycle for clients who demonstrate good "repayment culture." The incentive is so strong that when MFIs continue to lend to defaulted customers (as part of an adjusted repayment plan, for example), they run the risk of eroding repayment culture across the portfolio, as other borrowers learn that the sanction of not issuing new loans to late- or non-repaid customers is not being enforced.[1] Naturally, it follows that in the absence of additional incentives, if loans are transferred to a collections company that does not originate new loans, borrowers would lose their primary repayment incentive and repayments would drop, and drop dramatically.

There are of course alternative repayment incentives, chief among them using the borrower's property as collateral. However, a large number of MFIs do not ask for collateral on their loans, and requiring it would in any case exclude a large number of current microfinance borrowers.[2] Indeed, microfinance is largely defined by its ability to make non-collateralized loans to the borrowers without a formal credit history. Nevertheless, in this study, effective collateral has proved to be the most reliable predictor of client repayment after their MFI ceased making new loans. Perhaps the most direct example is the case of two Croatian MFIs (NOA and DEMOS) forced by government regulation to suspend all lending on 1 Jan 2008 until they converted to a new status. Although that conversion was a drawn-out process that one of the lenders does not expect to complete until 2010, both saw only a relatively minor bump of 1-2% in delinquencies. As it happens, these institutions issue mostly individual loans that are well collateralized (DEMOS requires 110% collateralization in the form of signed checks, or liens on salary or pension[3]). Moreover, the Croatian legal system provides strong and relatively efficient enforcement, and individuals are well aware that default will result in eventual seizure of their collateral.[4] As it happens, the most successful liquidation case in this study – Bank Dagang Bali, with a recovery rate of over 73% on its microfinance portfolio – featured borrowers who either pledged physical collateral to their loans or held significant savings at the bank, which, even if these were not pledged as collateral, created the mental perception similar to that of actual collateral.

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[1] Ulrike Vogelgesang, Microfinance in Times of Crisis: the Effects of Competition, Rising Indebtedness, and Economic Crisis on Repayment Behaviour, University of Mannheim, November 2001

[2] ibid

[3] DEMOS SLC website (http://www.demos-skz.hr/products.htm), retrieved 25 August 2009

[4] Daniel Gies, Chairman of the Supervisory Board, DEMOS SLC, email and phone interviews, 17-22 June 2009

Besides collateral, another potential repayment incentive is reporting of repayment histories to credit bureaus. In such a situation, borrowers of a failing institution would still need to repay in order to avoid a negative mark on their credit history and thus retain the ability to borrow from other lenders in the future. In fact, in parts of Latin America where credit bureau reporting for MFIs is relatively common, portfolios of commercial MFIs that focus mostly on individual lending are seen as similar to traditional non-collateralized consumer credit, that is, as relatively liquid instruments transferrable to other institutions.[1] However, credit reporting for MFIs in most developing countries, especially outside Latin America, is at best in its infancy. Moreover, it is not clear that other banks/MFIs would necessarily treat a client default to a failed institution (as opposed to a "regular" default) as a disqualifier, especially for a client who otherwise demonstrates a good repayment history. By extension, we don't really know how such clients would actually behave following their MFI's failure. The situation, as far as I know, has yet to be tested in a microfinance context.

Having looked at the alternative repayment incentives, let us get back to the base case – expectation of future loans. Interestingly, there is anecdotal evidence suggesting that borrowers view the closing of their MFI as a forgiveness of the loan. When rumors began to spread among borrowers of an NGO-MFI in Bolivia that it was closing, clients assumed their debts had been cancelled and stopped paying. In reality, it was only merging with other NGOs to form Eco Futuro, and to convince borrowers to continue repayments, the staff not only had to explain that the branch & loan officers would remain in place, but also had to display signage of both the NGO and Eco Futuro for some time.[2] Furthermore, there is evidence that such defaults become self-propagating, that is, once some borrowers stop paying, others may follow suit.[3] This outcome is even more prevalent in group lending, where there is a tipping point of defaults, after which the group guaranty becomes untenable, and the group falls apart.

Whither the MFI, Thither its Portfolio

While the discussion above may highlight the problems of recovering value from a portfolio after its MFI fails, what does the actual evidence show? Among the failures studied here, SOMED (Uganda) displayed largely the worst-case scenario, after allegations of embezzlement, with its CEO on the run, the staff unpaid for months, it's unsurprising that the outstanding portfolio basically melted away. Disappearances of loan portfolios have also been the rule among failing SACCOs (Savings And Credit Cooperative Organizations) in Africa, Latin America and the Caribbean – even after disposition of a failed organization's physical assets, a 20-30% recovery rate has been considered good.[4]

A particularly interesting example of losses as a result of eliminating the expectation of future loans is the current case of Fundación San Miguel Arcángel (FSMF), a Grameen replicator in the Dominican Republic. Following extensive fraud by members of executive management and subsequent scaling back of new

[1] Alex Silva, President and Founder, Omtrix, phone interview 1 June 2009
[2] McCarter, Elissa. Mergers in Microfinance: Twelve Case Studies. CRS Microfinance, 2002, p. 94.
[3] Philip Bond and Ashok Rai, Borrower Runs, December 2004
[4] Jesus Chavez, World Council of Credit Unions (WOCCU), phone interview 8 September 2009

disbursements due to losses, it found itself dealing with delinquencies of over 50% and rising. Lack of borrower confidence in the institution was directly cited as the reason for the delinquencies.[1]

The case of FOCCAS (Uganda) also shows a decline in portfolio value following the MFI's slide into insolvency. However, in this case some recoveries were made, though the amount was much lower than the portfolio value outstanding at the time of the failure. What's interesting is that another MFI (FINCA Uganda) effectively recreated the repayment incentive by offering borrowers who fully repaid their FOCCAS loans to continue borrowing from FINCA at a similar place in their loan cycle. It is likely that PostBank Uganda, one of FOCCAS creditors, may have done something similar. Ironically, though in both cases other creditors were unhappy with this client poaching, some of them may in fact have benefitted from these actions by enjoying a larger number of loans being repaid than would otherwise have been the case.

Risk to MF investors

Microfinance credit risk → MFI default risk

Given this context, it is apparent that the traditional valuation of credit risk, that is the risk of default multiplied by the expected loss in the event of default, becomes superfluous. First, measuring the latter is exceedingly difficult, as it requires evaluating the portfolio not for performance, but for collectability – an exercise with no realistic basis for calculation, given the multiplicity of scenarios, each with widely differing results, and little history to go upon. Second, unlike traditional loans, under certain scenarios microloans have the propensity to default *en masse*, rather than individually. Since one such scenario is the failure of an MFI, I suggest that one ought to explicitly plan for near-total portfolio loss following default, at which point the credit risk of an investment begins to approach the default risk of the MFI.

Investing in Microcredit Portfolios

The problem of portfolio recoveries after an MFI failure raises another question – purchasing and recently even securitizing microcredit portfolios has become a growing practice among commercial banks and other finance companies in India,[2] yet there is no evidence that any of them have put in place a credible backup servicer or another post-default collections framework. Thus, if the MFI from which the microcredits were purchased were to collapse, the owners of these assets would likely find themselves holding effectively worthless paper – a direct consequence of the credit risk of the portfolio being supplanted by the default risk of the MFI.

In this regard, the experience of India's ICICI Bank with its Andhra Pradesh portfolio in 2006 is instructive – when government action kept MFIs from collecting repayments on their loans, loans that ICICI had purchased from those same MFIs also went uncollected. An attempt to shift the portfolio to an

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[1] Kiva website (http://www.kiva.org/about/aboutPartner?id=66), retrieved 8 September 2009

[2] India Microfinance blog (http://www.indiamicrofinance.com/microfinanceindia/microfinance/microfinance-loan-securitization), retrieved 14 September 2009

alternative servicing channel proved fruitless, and recoveries (albeit small) were made only when servicing was finally moved back to the original MFIs. It's also noteworthy that the performance of MFI Partnership loans that had been issued under ICICI's name, with an MFI as facilitator and servicer, performed exactly the same as loans that the MFIs had issued themselves and that ICICI had purchased from their portfolio. As for the alternative servicing channel, while it was selected largely in response to political pressures, it isn't clear that another alternative even existed for ICICI.

Another compelling case is Kiva's experience with the failure of WEEC in Kenya. Kiva's innovative person-to-person (P2P) platform allows thousands of retail lenders to make loans to individual MFI clients. Kiva then transfers the funds to the MFI, which lends to the specified clients and in turn reports client-level repayments, delinquencies and defaults via the P2P platform. Each month Kiva and its MFI partners net out the total cashflows – the sum of all new funds raised via the Kiva platform against the sum of all incoming client repayments. However, the presence of such apparent P2P transactions belies the nature of the credit risk – when WEEC stopped repaying its obligations to Kiva, the latter had no choice but to change the status of all outstanding WEEC loans to defaulted, even if many of WEEC's clients may have continued on-time repayments. In fact, 93% of Kiva's loan defaults were generated by three failed or failing MFIs (WEEC, MIFEX in Ecuador, and FSMA in Dominican Republic), all brought down by organizational issues rather portfolio underperformance.[1] As for the legal underpinnings of the P2P transactions, I don't know whether Kiva's lending contracts dictate direct ownership, collateralization, or some other mechanism linking its funds to specified microloans, but it is very likely that these are effectively irrelevant. As Kiva's CEO, Matt Flannery had so clearly stated when discussing WEEC, without the MFI management's cooperation – whether granted willingly or obtained through threat of reputational, legal or other credible sanctions – there was simply nothing they could do to recoup their lenders' funds, and I would suggest that the same applies to all its MFI partners.

Risk of Different Investment Types

Given the experiences of investors outlined above, it is apparent that the various models of funding MFI lending – non-collateralized loans, loans with portfolio as collateral, portfolio purchases, and securitizations – have in fact little difference in terms of financial exposure, since they are all equally exposed to the risk of MFI default. In the event of the MFI's collapse, the net losses to creditors of all stripes would at least theoretically be dictated by claim priority rather than collateralization or direct ownership of portions of the portfolio. Ironically, if collection of outstanding loans proved impossible, it is quite likely that senior bondholders would suffer lower losses than holders of microcredit-backed securities, despite the fact that the latter have been marketed as safer assets to hold. After all, the former would be first in line for recoveries from the sale of physical assets, such as real estate and the like, whereas the latter would have nothing but the uncollectable portfolio to rely on. One might argue that securitizations might provide for some cushion, as all the MF securitizations to-date have included liquid collateral,[2] but I believe that is the extent of the protection. The other main risk protection offered

[1] Kiva website (http://www.kiva.org/about/partners), retrieved 25 August 2009

[2] Credit Rating Agency of Bangladesh (CRAB Ratings), BRAC MICRO CREDIT SECURITIZATION SERIES I, 28 February 2006

by asset-backed securities, risk subordination or tranching, offers little comfort when losses start to reach 70-80% or more.

Servicer Risk

The problem of the high impact of servicer risk on a microcredit-backed security has already been identified by Fitch, in its Rating Methodology for Bolivian microfinance. Since the servicer risk can never be completely mitigated, Fitch explicitly states that any microfinance securitization rating would be normally limited to between one and five notches above the rating of the MFI whose portfolio is being securitized.[1] As it happens, the Bolivian microfinance market is one of the oldest and most developed, and following an over-indebtedness crisis in the late 90s, has seen substantial expansion of credit bureaus to cover microfinance clients.[2] This, as has been previously mentioned, may help reduce the impact of an MFI default on the performance of its microcredit assets. However, the absence of such credit reporting makes other countries' environments substantially less conducive to even this relatively modest reduction in the impact of servicer risk.

This is a world apart from the relatively liquid asset model of traditional financial institutions. Take as an example the worst of the worst – the subprime MBS. To this day they are still very much passing aggregate loan payments (much reduced, of course) through to investors, despite the fact that nearly all of the original subprime lenders have long ago been marched off to their infamous grave. As bad as a loss of 20% or even 50% might be, it is still considerably better than losing 100%, which unfortunately, has been more common than not in the world if microfinance investment.

[1] FitchRatings, Rating Methodology for Bolivian Microfinance Credits, 19 April 2007
[2] Remy N. Kormos, Credit Information Reporting in Bolivia, 8 December 2003

Recommendations

Much like microfinance had to invent new lending methodologies for their clients, so must microfinance investors develop new liquidation methodologies. The studies of liquidations in this paper contain elements demonstrating that relatively successful liquidations may indeed be possible, but, unless the portfolios feature alternative borrower repayment incentives (i.e. collateral or credit bureau reporting), liquidations will require special and concerted efforts to be reasonably successful. With that mind, I propose some possible steps to consider:

Pre-default

At this level, a creditor needs to consider inexpensive options that would maximize its ability to recover its loan should the MFI fall into default.

1. Maximize the MFI's incentive to repay. Much like MFIs do with their borrowers, microfinance creditors should insure that the MFI's management's incentives are at least somewhat aligned with the creditors'. A teachable example is the case of WEEC, where creditors with physical collateral backing their loans were repaid, while others were left dangling in the wind, even if they had the portfolio itself as collateral. Having experienced this first-hand, Paul Mayanja of the Stromme Foundation shared a helpful suggestion – consider adding some physical property of the MFI directors as collateral for the loan, even if it's a symbolic amount relative to the loan size. It might not cover losses, but it would create an incentive for the MFI to cooperate.
2. Insure that agreements are drawn in a way that maximizes creditors' ability to gain significant control of the MFI in the event of default, such as through a receiver. The exact form of control or whether it's even possible depends largely on the nature and reliability of the judicial and enforcement systems of the country.
3. Build in debt covenants tied to specified capital or cash-flow thresholds, the violation of which would accelerate the loan, and thus create an opportunity for the creditor to gain control at an earlier time, or at least gain additional leverage with the MFI's management.
4. Negotiate that a small percentage of the investment be placed in a contingency fund that would be beyond MFI management's reach, but could be tapped under specified circumstances, such as default or insolvency. The fund need not be particularly large – it is probable that even a struggling MFI will be able to generate cashflow to pay for at least some portion of operations. The contingency fund would be used to cover the shortfall.

Post-default

Once an MFI is in default or close to it, the two primary objectives are to maintain its payment collections organization and borrower incentives to repay. Thus, there should be as little as possible immediate impact on borrowers. If new loan disbursements have to be halted, it's critical that the suspension be as brief as possible, and borrowers are given clear and believable signals that they will be getting new loans upon repayment of their existing ones. For this reason, it is best that the MFI be taken over at the earliest, before it runs out of funds. Beyond that, here are additional steps to consider:

1. As early as possible, confer with the other main creditors, both local and foreign, SRI and commercial, and try to come up with a consensus liquidation plan. As the FOCCAS case demonstrates, creditors working in opposing directions can make a bad situation much worse.
2. In nearly all circumstances, MFI directors/management will have to be replaced. The sooner this is done, the better.
3. Realize that it is probably best to repay local creditors first. Especially in countries were relationships can trump legal agreements, the local creditors will likely have advantages that they will use to undermine any scheme that has them suffering losses they could otherwise avoid, such as sharing recoveries with other creditors. In the case of FOCCAS, PostBank Uganda benefitted from being the channel for collecting borrower repayments, and during liquidation applied incoming payments to its own loan first, before passing the remainder on to the receiver.
4. Consider the incentives of MFI staff. Ideally, they would like to keep their jobs, but if that opportunity is unavailable, they will do the next best thing. If the next best thing happens to be keeping borrower repayments for themselves, as was alleged at SOMED, that is what they will do. Thus, it may make sense to pay bonuses for early recoveries, or even a portion of recovery proceeds to staff responsible for collections. Long-term staff morale and similar considerations are irrelevant in such situations, and it is important to keep as much critical staff around as possible until the liquidation is completed.
5. Before attempting to sell the MFI, its portfolio, or components thereof, try to stabilize its performance first, and then get a reliable audit. In most cases, whatever caused the MFI to get to this point is also likely to raise plenty of suspicions of both its unaudited financials and the organization as a whole.
6. If a buyer for loans cannot be found, but an MFI is found that is willing to take on borrowers, even if for free, it's probably worth taking the deal. In effect, the new MFI is stepping in to provide the repayment incentive for borrowers, which allows the portfolio to run-off, and outstanding capital to be recovered over a reasonably short time. Ideally, borrowers must be informed – preferably by the other MFI's staff – of what loans they can expect if they continue on-time payments.
7. Consider adding additional incentives for borrowers, such as waiving interest in return for early repayment.
8. If a receiver is hired, make sure the fee is well-aligned with investor interests. When fees are based strictly on time spent, the liquidation is likely to be extended unnecessarily and yield significantly reduced returns to investors. At a minimum, the receiver's payment should include a significant contingency fee component.

Conclusion

Much good effort has been focused on making MFIs more professional, more transparent, better risk managers, and generally less likely to fail. These efforts must surely continue. However, despite the best of intentions, failures will still happen, and as time progresses, we are likely to witness failures of even a couple of the large MFIs. This is an unavoidable aspect of business.

Continuing growth of microfinance should include some improvement in dealing with MFI failures. The few case studies here and the handful of recommendations should be only a starting point. As I embarked on this research, it became immediately apparent that there is a great dearth of any sort of documentation pertaining to MFI failures – most of the cases described here were found through word-of-mouth. The few documents that do deal with failures have mainly covered successful turnarounds – simply put, no one wants to write about their failures. This is obviously understandable, but in the long run, it harms those same organizations that keep their failures out of the public eye. I have heard from a number of individuals involved in a liquidation how much they could have benefitted from having some past examples to go by, yet all were left to devise their own solutions without such benefit.

I would like to propose that the microfinance community reconsider this approach and make at least a minimal write-up of each liquidation process, including its financial outcomes, public. Naturally, the MFIs involved aren't around to do this, but in all but the smallest cases, there are invariably investors, MF networks or other parties involved who could produce a brief case study. Not only would this help the microfinance community, it would contribute to a public record from which the case writers themselves stand to benefit.

After all, planning for failure is like writing a will – if you wait until you need it, it'll be too late.

Appendix

SOMED, Uganda

SOMED (Support Organization for Micro Enterprises Development) was based in the Kibaale District of Uganda. Until 2006, it was viewed as a successful microfinance provider, making the short-list of the 2003 Rural Pro-Poor Innovation Challenge (RPPIC), a competition co-sponsored by International Fund for Agricultural Development (IFAD) and CGAP. Since SOMED never reported its data to the MIX, it is not possible to provide portfolio statistics, but at the time of its closure in 2007, its portfolio was about UGX 1.7 billion (USD 1 mln[1]).

In 2006, SOMED began to have repayment problems to at least one of its creditors. Initially, the organization's management blamed the shortfall to a slowdown in borrower repayments, and asked for additional time.

In fact, during this time, the company was collapsing, with salaries not having been paid for months. As staff began to leave in large numbers, loan collections effectively ceased. The vast majority of the UGX 1.7 billion portfolio was never recovered, though there were indications that branch managers and staff may have been using loan repayments they did collect to cover their own salaries, so the real repayment rate could not be determined. In Dec 2007, the Ugandan authorities closed down the institution, citing allegations of embezzlement, extortion, and fraud.

In an effort to recover its loan, one of the creditors – the Stromme foundation – sued SOMED and its CEO, and was awarded damages. However, by then the CEO had gone into hiding. It was alleged (though never proven) that he had purchased a number of properties, and there were other indications that embezzlement may have been involved. However, since Stromme's credit had been secured only by the CEO's personal guarantee and a lien on the portfolio, there was nothing that could be recovered – with staff gone, there was no way to collect on the portfolio, and with the CEO in hiding, there was no way to recover damages from him personally.

After the judicial ruling, the former Operations Manager of SOMED proposed to the creditors a restructuring plan, to bring back the staff to collect on the existing portfolio and restart operations. However, the balance sheet by this time showed an institution grossly insolvent, and restarting operations would have required infusion of new capital that no organization was willing to invest. In the words of one creditor, it would have been equivalent to "throwing good money after bad." There was also a significant level of mistrust of the numbers being shown, given the creditor's belief that the balance sheet had been misrepresented for quite some time prior to SOMED's closure in 2007.

Sources:

[1] USD 1 = UGX 1,696 on Dec 31 2007, source: http://finance.yahoo.com/currency-converter

1. Paul Mayanja, CEO of Stromme Microfinance East Africa Ltd., phone interview 28 July 2009
2. Abdallah Byabasaija, former Operations Manager at SOMED, phone interview 6 July 2009
3. MicroCapital, Another Microfinance Institution (MFI) Closes in Uganda as Chaos Continues in the Sector, 9 January 2008.
4. IFAD website (http://www.ifad.org/ruralfinance/poverty/rppic.htm#finalists), retrieved 28 August 2009

WEEC, Kenya

WEEC (Women Economic Empowerment Consort) was founded in 1996 in the Kiserian area in Kenya to empower disadvantaged but economically active rural women. As of 2003 (the latest reported numbers available on MIX), it had a portfolio of USD 362,391 and 2,895 active borrowers. In April 2007, the institution's founder and Executive Director, Jedidah Waigwa, passed away unexpectedly, and her spouse took over the management of the organization.

Although WEEC had some organizational challenges prior to Ms. Waigwa's death, including a weak MIS, several creditors – including Kiva, Stromme, and others – believed that it had promise as an MFI and saw it as a good credit risk.

Unfortunately, the new director had little interest in the organization's future, and within 6 months of the founder's death, WEEC became insolvent and began to fall delinquent on its repayments to Kiva (Kiva's loan terms dictate monthly repayments). Following the founder's death, Kiva had sent its staff and volunteers to WEEC, however its efforts to work with the organization proved fruitless, as the relationship with the new director had become poisonous. Moreover, it should be noted that (according to Kiva) portfolio performance was not the primary reason for the organization's insolvency.

When reviewing their options for loan recovery, both Kiva and Stromme eventually came to the same conclusion – pursuing legal processes was likely to cost more than the expected benefit. There was some discussion between the two of collaborating in pressing their claims, but Kiva pulled out after initial meetings, having determined that this too had little chance of success. Both decided that the protections within the Kenyan legal system were insufficient, and neither party had any physical collateral backing their claim, only the organization's portfolio. Stromme also had a personal guaranty from Ms. Waigwa, put this was of course unenforceable given that the guarantor was deceased.

At the same time, pursuing the alternative recovery option – calling on their portfolio liens – was deemed impracticable, since without the organization's staff and support, collecting on outstanding loans would have been exceedingly difficult. Note that this was the case despite the fact that Kiva, as a P2P lending platform, has far more data on individual microfinance borrowers than most other microfinance investors.

A point particularly emphasized by Kiva's founder Matt Flannery is that the new director had no incentive to repay – not having any plans to remain in the business, he had no reputation to protect, and was primarily motivated by securing his personal assets, regardless of the cost to the organization his wife had founded a decade earlier. At one point in his discussions with Stromme, the new director proposed to convert the creditor's claim to equity, but, given his lack of interest in the organization's future, Stromme understandably saw little value in such a deal. As if to underscore the point, it is noteworthy that WEEC did repay the debts to local creditors who had physical property of the director as collateral backing their claims.

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2. Matt Flannery, co-founder and CEO of Kiva, phone interview 27 July 2009
3. Kiva website, http://www.kiva.org/about/aboutPartner?id=6, retrieved 3 August 2009
4. Mix Market website, http://www.mixmarket.org/mfi/weec, retrieved 31 August 2009

Bank Dagang Bali, Indonesia

Bank Dagang Bali (BDB) was one of the first modern microfinance lenders, founded in Bali in 1970 by a family that had been lending informally in the local markets since the 1950's. From the very beginning, its focus was to provide financial services to the local Balinese community of tradespersons and merchants in the wholesale and retail business sectors. It provided a range of financial services, including deposits and individual loans (with and without collateral). Notably, BDB did not focus on solely the microenterprise sector – while 50% of its borrowers had loans below $550, this accounted for less than 5% of portfolio value. Conversely, loans above $50,000 made up over 56% of the portfolio, while representing only slightly over 3% of borrowers. It was thus one of the very few and earliest examples of commercial banks serving both microenterprises and well-off customers.

As of Dec 31, 2001, it was a well-capitalized institution, with USD 84 mln in deposits, and USD 24 mln in outstanding loans, representing roughly 400,000 savings and 12,500 loan accounts. The M-CRIL rating issued in April 2002 specifically cited the institution's ability to absorb USD 13 mln in loan funds over the next three years for on-lending.

However, in April 2004 – almost exactly 2 years after M-CRIL's rating – BDB's banking license was revoked by Bank Indonesia, Indonesia's central bank, "because of extreme liquidity problems allegedly triggered by fraudulent transactions."[1] During this time there were never allegations that the bank's microfinance, or for that matter commercial, portfolio was underperforming – the fraudulent transactions in this case referred to BDB's "funds of combined value of close to Rp 1 trillion [USD 120 mln[2]] being placed with [Bank] Asiatic … [that] were later used as loan collateral by the son of a BDB owner, who is married to a daughter of a Bank Asiatic owner."[3] This, combined with similar fraudulent transactions with three other banks, amounted to a staggering sum for the bank: they increased BDB's liabilities by IDR 1.26 trillion (USD 151 mln).

Upon revocation of BDB's license, Bank Indonesia formed a Liquidation Team, headed by the former Bali Chief of Police and comprised of two former BDB Directors, a former Higher Judge, and three other professionals. It also commissioned an independent final audit. Since BDB was a deposit-taking institution with a deposit guaranty provided by the Government of Indonesia, there were additional audits of deposits undertaken by the State Auditor.

The liquidation team proceeded to lay off staff while liquidating the institution's assets. Some of the portfolio was allowed to run off, other parts were sold to other commercial banks. A portion of the microfinance portfolio was sold to a village bank in Bali, while other MFIs and village banks purchased loans on an individual basis. As of the time of the publication of this paper, that is five years following

[1] Bill Guerin, "New Worries for Indonesian Bank Sector," Asia Times Online, 17 April 2004, retrieved from http://www.atimes.com/atimes/Southeast_Asia/FD17Ae02.html on 31 August 2009

[2] USD 1 = IDR 8333 on 8 April 2004, source: http://finance.yahoo.com/currency-converter

[3] Dadan Wijaksana, "BI to Fight Court Ruling on BDB Case," The Jakarta Post, 26 June 2004, retrieved from http://www.thejakartapost.com/news/2004/06/26/bi-fight-court-ruling-bdb-case.html on 31 August 2009

the bank's closure, the liquidation team is wrapping up its affairs and beginning to auction off BDB's physical assets.

During the early months of the liquidation period, borrowers were offered discounts on interest and penalties if they repaid early. The team judged the program successful, and is considering offering again a similar discount for the few months remaining before it turns all remaining assets over to the Ministry of Finance. It should be noted that many of BDB's loans were collateralized by physical assets (land or automobile registration certificates). Non-collateralized loans had been given to the bank's employees or wage-earning customers, in both cases repayments being deducted from their paychecks. The remaining cohort was non-wage-earning customers without collateral, but who had savings accounts with BDB. In most cases a customer's savings exceeded the amount of their loan, which, even if they did not explicitly collateralize the loan, created the mental perception similar to that of actual collateral, especially given that repayment of deposits by the Indonesian government guaranteeing them was a slow and drawn-out process.

To-date, recoveries have been at 73% of original loan value, with the microfinance portfolio generally exceeding the overall recovery rate (the numbers are not discounted for inflation). The liquidation team expects to see final recoveries hit 90% before the end of 2009, following implementation of their final incentive plan that waives all penalties and interest. Liquidation costs, including salaries, have been paid by the interest cash flow generated by recovered funds placed as time deposits at other banks. The monthly operational cost of the liquidation accounted for about 0.1% of total assets recovered.

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2. Femke Bos, Fund Manager, Triodos Investment Management B.V., phone interview 14 July 2009
3. BDB balance sheets, April 8 2004 and July 2009; provided by Indra Suryatmaja
4. M-CRIL microfinance rating, Bank Dagang Bali, issued 11 April 2002, retrieved from MixMarket.org

FOCCAS, Uganda

Co-authored with Godfrey Jjooga Ssebukulu[1]

FOCCAS (Foundation for Credit and Community Assistance) was founded in 1996 to provide microcredit product with education services to poor rural women in eastern Uganda, using a village banking model. Its last reported MIX data in 2004 shows a portfolio of USD 1.1 mln, serving nearly 17,000 active clients, organized into 487 credit associations. FOCCAS had been established by Freedom from Hunger (FFH), a US-based NGO, and was transformed to an independent institution in 1998, though with ongoing technical assistance from FFH. As of June 2006, FFH still had an outstanding loan originally issued to FOCCAS as a guaranty to support commercial lending, but later converted to a cash loan following significant underperformance of the commercial portfolio.

FOCCAS also had a number of both local and international lenders, including Ugandan commercial lenders Nile Bank Limited (later acquired by Barclays) and the state-owned PostBank Uganda Limited. Its list of international socially-responsible investors (SRIs), included the Stromme Foundation, SUFFICE (a project of the EU and the Government of Uganda), ECLOF Uganda, and Cordaid. Some of these creditors later claimed that FOCCAS management had misrepresented the company's financial state of affairs, including its outstanding debts, when soliciting credit. This later manifested in the disputes that arose among the creditors during the liquidation process.

In early 2006, a representative from FFH was at FOCCAS on a routine visit, and during his examination of the company's finances, it became apparent that the reporting to-date had been inaccurate and incomplete, and that the institution was in fact insolvent. Having never achieved operational self-sufficiency, and with no more funding coming in from FFH, it was kept afloat only by the back-to-back loans contracted over time. Moreover, with its near-term cashflow also looking bleak, FOCCAS was simply going to run out of funds very shortly if nothing were done.

These financial gaps were presented at the June 2006 FOCCAS board meeting, and as there was no clear source of additional capital, it was decided that the institution be closed. At the outset, FFH took the lead with developing a plan – collecting outstanding repayments and offering clients who had successfully repaid their FOCCAS debts the option of transferring to another MFI, without losing their place in the borrowing cycle; in other words they could receive a loan of similar amount as the one they had just repaid to FOCCAS. Concurrently, FOCCAS itself would suspend the issuance of new loans.

FFH had identified FINCA Uganda as the most suitable partner for this plan, both because of the relative similarity of its business model as well as its physical presence in FOCCAS' area of operation. Initially FINCA and FOCCAS, with the help of an outside HR firm worked jointly, with FINCA's management coming to address FOCCAS' staff regarding the transition plan. The DFID Financial Sector Deepening Uganda Project stepped in to provide a grant for handling the PR aspects of the transition, with

[1] Consultant/Managing Partner (Frontline Associates) and former Transformation Manager (DFID Financial Sector Deepening Uganda Project)

Communication for Development Foundation Uganda Limited (CDFU) hired to formulate and implement the communications strategy comprising of radio announcements with targeted messages, radio talk shows, and printed materials in local languages. The communication strategy had two main objectives: 1) to inform and sensitize clients of the transfer program to FINCA and, 2) to avert negative publicity arising from the closure of yet another MFI. As it turned out, the PR campaign and collaboration with FINCA would last only two weeks.

From the outset there were a number of issues with the FFH plan to transfer FOCCAS clients to FINCA. Though it initially received support from Cordaid and SUFFICE (the latter changed its mind soon after), the other creditors viewed it as a dishonest attempt on the part of FFH to protect itself and its directors on the FOCCAS board, whom this plan would have let off the hook for the personal guarantees they'd given to some of FOCCAS' creditors. In addition, the plan was seen as self-serving in another way: since FOCCAS had received a loan from PostBank only a few months before the crisis hit, when an FFH staff member had been already working with FOCCAS as a full-time technical officer, some creditors felt that FFH must have known that the institution had fundamental operating weaknesses, yet allowed the PostBank loan to go through nonetheless. Moreover, most felt that FFH had not acted in good time to avert the crisis at FOCCAS, and then when crisis hit, presented them with a *fait accompli* solution urging the creditors to be considerate and expect to lose money in the process. To make matters worse, the plan, which effectively allowed FINCA to cherry-pick FOCCAS' best clients without paying any consideration, was just too bitter a pill to swallow.

For its part, FFH felt that its decision-making power over FOCCAS was misunderstood – it had no institutional seat on the board, though it did have board representation through its president. Moreover, it felt that PostBank was scapegoating FFH, while absolving itself of responsibility – after all, its Managing Director was also a member of the FOCCAS board and in fact headed its finance committee a year prior to the loan being approved. Nevertheless, disagreements about blame aside, the liquidation plan put forth by FFH was by all accounts unusual for a financial firm, and the FFH employee on the ground at the time did later volunteer that it would perhaps have been better to involve creditors at the outset, as the plan was being developed. As things stood, from the perspective of the creditors, FFH already had questionable standing, and dictating the solution to a problem partly of its own making didn't sit well with them.

In addition to creditors, there was also significant disagreement with the FINCA transition plan among the FOCCAS staff, many of whom felt that there was no reason to close the MFI in the first place. Moreover, when the Managing Director of FINCA came to address the FOCCAS staff at the outset of the transition plan, he made clear that FINCA would not necessarily bring any of them on board. Thus, the staff had little incentive to work with borrowers to insure good repayment. Later during the transition, FINCA did hire some of them, but in, the words of one staff member, it was too little, too late. The staff was also beginning to cluster around the liquidator appointed by Nile Bank, who had started promoting a turnaround plan for FOCCAS.

It is worth noting FINCA's perspective on the situation – while it was willing to take good clients for free, it was not willing to pay for those clients, or purchase the portfolio or any part of the FOCCAS operation. For one, it felt that the FOCCAS portfolio data it was shown was suspect. It also felt that the new clients would require it to expend resources to be trained and sensitized to its lending methodology before they could be disbursed new loans. At the same time, FINCA had concerns about the credit quality of FOCCAS clients, given the state of affairs at the organization. In a way, the very fact that FOCCAS was being forced to sell its portfolio was reason enough to have doubts about purchasing it or any of its loans. Those same concerns applied to its staff as well. In hindsight, FINCA feels that the concerns had been justified – in fact, all the staff it had acquired from FOCCAS were later dismissed because of fraud. Meanwhile, FINCA has been dropping many former FOCCAS clients after they failed to demonstrate good repayment culture.

With no support from any angle, it is hardly a surprise that the plan was cancelled after just two weeks. The FFH representative was asked to leave the premises, and with that, FFH's involvement with FOCCAS came to an end. From there, the liquidation took a different turn.

The removal of FFH may also have removed the one point of agreement among the creditors. Driven partly by anger and confusion over "new" creditors (i.e. those FOCCAS did not bother to inform about when soliciting credit), there was no agreement over the priority of claims, and many of the parties jockeyed for advantage. Two separate receivers were appointed – one by SUFFICE and one by Nile Bank (the two later agreed to use the Nile Bank-appointed receiver, Superstar Auctioneers and Bailiffs). However, the real war was between the two local banks – Nile Bank and PostBank. For some time, FOCCAS had been using PostBank as a payment collections facility, and many of the loan repayments were still coming in via its branches. Once the liquidation process started, PostBank objected to sharing these incoming repayments with other creditors citing fraud in the issuance of the SUFFICE-guaranteed Nile Bank debenture. Amidst this confusion, PostBank called the 50% loan guarantee from Cordaid and applied repayments from FOCCAS clients to fully recover its loan, passing on only a small amount back to the liquidator.

One observer also noted that PostBank was poaching the FOCCAS clients who used its facilities to repay their loans. However, the PostBank official in charge of the FOCCAS account denies this, expressly stating that, though it wanted to offer the FOCCAS clients its own services, it did not pursue this after objections from other creditors. As it turns out, such objections would have been in any case unenforceable, and it is probable that PostBank pursued this policy at least on some level. After all, doing so would have been effectively providing a repayment incentive to the clients, similar to what was attempted via the original FINCA transition plan, and would have helped it recover its own funds. As it happens, although FFH's transition plan had been shut down, FINCA also continued to pick off good clients who had fully repaid their FOCCAS loans, but had been frustrated by the non-disbursement policy. It did this with the help of some FOCCAS staff who were hoping to get thus hired by FINCA, and was further helped along by the continuing effect of the initial PR campaign. Ironically, the unintended side

effect of these actions by FINCA and probably by PostBank was to increase the client repayment rate to FOCCAS, thus increasing overall recoveries.

Back in the Nile Bank camp, its appointed liquidator, rather than doing the bidding of its client and looking to sell the organization or its assets, focused his energies on attempting to turn the organization around. At one point in its operations, the liquidator made the decision to rescind the suspension of new loan disbursements for clients who had fully repaid. The idea was to make the operation more saleable to potential bidders, though, interestingly, when the remaining assets of FOCCAS were sold, they were sold to a buyer working for the same company as the liquidator. The line between the liquidator and the buyer was very blurred, and given the circumstances, one cannot rule out the possibility that FOCCAS funds were utilized by the liquidator to prop up the business of the portfolio buyer, that is, his own company.

With all the disagreements between FFH, the creditors, the receivers, and most importantly, without any loans being disbursed by FOCCAS (other than the period when this suspension was rescinded by the liquidator), it should not be surprising that client performance was suffering. Yet not everything had been lost – the FOCCAS brand was highly valued by its clients and many were hoping that it would restart lending. That hope, the unavailability of other lenders in certain areas, and the incentives provided by FINCA and PostBank motivated some borrowers to continue repayments on their loans.

The liquidation process at FOCCAS went on for two years, at a very high cost to the SRIs. In the end, PostBank, by way of its control of the repayment channel, was able to fully recover its loan. Nile Bank was also able to recover its share, in part by calling on the SUFFICE guarantee, and the rest via the funds recovered by the liquidator. Stromme, Cordaid, U-ECLOF, SUFFICE and FFH did not receive any funds from the FOCCAS liquidation. However, Stromme did file suit against the FOCCAS directors through the Ugandan courts, and were awarded full damages in the value of their loan, which they now expect to recover in full in the next few months. It is unclear whether the other SRIs have any options left to recover their money.

As for the clients, some, as had been mentioned, went over to FINCA, others to PostBank and other MFIs. However, it has been noted by several of those involved that FOCCAS clients had been especially devoted to their lender, and the FOCCAS brand had been highly valued. At least in the low-coverage areas where it had been pretty much the only MFI, in the words of one former employee, some clients are probably still out there, waiting for FOCCAS to return.

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5. Marc Bavois, Freedom from Hunger, phone interview 1 July 2009
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ICICI Bank, India (Andhra Pradesh Crisis)

Before delving into the case, one should first note what this isn't – an MFI failure followed by liquidation, as in the prior cases covered here. However, it does serve as a useful lesson of what might happen when investors are faced with collecting on a portfolio without the original MFI.

In March 2006, the Collector (district officer) of Krishna district in Andhra Pradesh (AP) closed some 57 branches of Spandana and SHARE in the district, the two largest MFIs in India, as well those of a few smaller MFIs. Though many branches were reopened relatively soon, the MFIs' ability to conduct business continued to be hamstrung. Borrowers had been given the impression that they need not repay MFI loans since the MFIs had violated a number of laws, including criminal laws, and it was widely reported that borrowers had also been informally told by government staff that their loans would be taken over by the government or other banks at lower interest rates. To make matters worse, the local and national press had taken a clear partisan stance and continued to inflame the public and borrower sentiment against the MFIs.

In this hostile environment, India's largest microfinance investor – ICICI Bank – faced a substantial drop in repayments in its AP portfolio. To the best recollection of the regional manager, ICICI had about INR 1.4 billion (USD 31.6 mln[1]) in microfinance loans in the Krishna District, split roughly 50/50 between its Partnership loans and those it purchased directly from the MFI portfolios. Under the Partnership program, a participating MFI partner issued loans to borrowers on ICICI's behalf, thus originating loans directly on ICICI's balance sheet. The portfolio purchase loans, on the other hand, were originated by the MFI itself, aggregated in its portfolio, and then sold in bulk to ICICI. Though a Partnership loan constituted a direct contract between the borrower and ICICI, with the MFI only acting as an intermediary facilitating the agreement, this distinction proved of little relevance in the course of the crisis – in both cases the MFI was the sole realistic link with the borrower.

For ICICI and other microfinance players, the crisis had implications much broader than their exposure to the Krishna district, as it inevitably raised questions regarding the political risk of microfinance in India. Thus, ICICI held a number of meetings with high-level government officials both at the local level, and with the Reserve Bank of India (RBI), both in order to resolve the crisis as well as establish clearer legal and political boundaries for microfinance in general. In one of those discussions, local officials suggested that ICICI could use the government-backed Village Organizations (VOs) to collect on the outstanding loans.[2] Though it knew that these would probably not be effective at collecting payments on its portfolio, ICICI nevertheless agreed to the plan.

In fact, its reservations had proved correct – the VO collectors had no incentives to exert themselves on ICICI's behalf, especially as the borrowers were their own neighbors. To make matters worse, the VO

[1] USD 1 = INR 44.28 on 1 March 2006, source: http://finance.yahoo.com/currency-converter

[2] The Velugu system – a government subsidized SHG linkage program in AP, of which the VOs were a part – was in fact one of the underlying factors for the crisis, as it put the MFIs in direct competition with the government.

system was in direct competition with the MFIs, and many of its collectors were the very individuals involved in agitating borrowers against the MFIs. Still, ICICI worked to educate borrowers in credit culture, but perhaps unsurprisingly, its collections via the VOs proved negligible. After six months, ICICI reverted collections back to the original MFIs.

The MFIs proved better than the VOs, but in the end, some 1.5 years after the onset of the crisis, they were only able to collect on some 20-25% of ICICI's Krishna district portfolio that had been outstanding in March 2006.

As a postscript, and perhaps to underscore how difficult transferring microcredit servicing can be, as of February 2008, that is nearly two years after the AP crisis, ICICI Bank still had not developed a process for transferring servicing for its Partnership and non-partnership microcredit portfolios.

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