

GIRAFE

AgroInvest, Serbia & Montenegro March 2006

Rating

A+	
A	Excellent
A-	The institution excels in all evaluation areas and is a model for the sector. There is a long-term vision for continual improvement. There are no risks in the short and medium term for operations. Long-term risks are well managed and monitored.
B+	
B	
B-	
C+	
C	
C-	
D	
E	

Trend

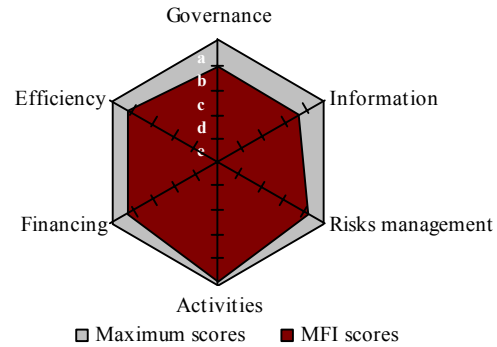
Positive	This trend is underpinned by the instability of AI's environment, all the more given the complexity of AI's legal structure. Nevertheless, AI has proved its ability to deal with regulation challenges and to define and implement pertinent solutions.
Stable	
Uncertain	
Negative	

Performance indicators

(K EUR, unless otherwise indicated)

	Sept. 2002	Sept. 2003	Dec. 2004*	Dec. 2005**
ACTIVITY				
Total number of staff	53	61	77	95
Assets	5,616	9,748	13,150	17,794
Loan portfolio	4,774	8,362	11,358	15,517
Active borrowers	5,208	9,629	12,967	14,679
PAR 31-365	0.2%	0.2%	0.2%	0.1%
PAR > 365	0.0%	0.0%	0.0%	0.0%
Write-off ratio	0.1%	0.1%	0.4%	0.2%
Risk coverage ratio	76.6%	51.3%	97.0%	94.0%
PERFORMANCE				
ROE	8.7%	11.1%	14.7%	12.5%
Liabilities / Equity	20.6%	50.3%	46.4%	52.0%
ROA	7.3%	8.1%	10.0%	8.4%
OSS	138.8%	138.5%	158.7%	152.8%
FSS	62.1%	87.5%	109.9%	102.4%
Portfolio Yield	30.8%	31.3%	33.6%	33.6%
Op. expense ratio	24.2%	22.0%	18.4%	18.9%
Staff productivity	98	158	168	155
Fund. expense ratio	0.3%	1.0%	2.9%	3.1%
GROWTH				
Portfolio growth	138.3%	75.2%	35.8%	36.6%
Asset growth	130.0%	73.6%	34.9%	35.3%

* Data For 2004 have been annualized for ease of comparison as the change in fiscal year resulted in a 15-month period for 2004 (Sept->Dec.)



Description of the institution

AgroInvest started as a microfinance program of World Vision International (WVI), disbursing its first loan in September 1999. Given the different legal requirements in the two Republics, two distinct entities had been created. In order to strengthen the legal structure and to comply with WV strategy, a holding company (based in Montenegro) and two limited liability companies (one in Serbia and one in Montenegro) have been created. As of Dec 2005, AgroInvest Group (AI) had a gross outstanding portfolio of 15.5 M EUR (23% in Serbia, 77% in Montenegro), for close to 15,000 active borrowers.

Rating summary

The MFI has been assigned a global rating of A-

This rating is underpinned by AI's key strengths, such as a pertinent credit methodology that perfectly suits the targeted rural clientele and results in strong portfolio quality; a solid financial performance despite high investments in HR and IT; a core position within WVI network and the ability to diversify funding sources on competitive terms. Governance remains an area where improvements could be implemented, noticeably regarding the integration of local members to the Board of Directors. Other areas for improvement include product development and innovation or information systems since eMerge has not yet been implemented in Serbia and still requires some adaptations to respond efficiently to all of AI's information needs.

This grade has been assigned with an **uncertain** trend, given the difficulty to predict potential evolutions of AI's political and legal environment.

Financing needs

AI anticipates funding needs of more than 12 M EUR over the 2006-2008 period. Planet Rating believes that AI has the capacity to manage this amount of additional funding given its current low leverage, strong risk profile and good earning quality.

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■ Microfinance sector

Serbian and Montenegrin legal environments are very different, with the obligation for MFIs in Serbia to operate through a partner bank, while a more favorable regulation is found in Montenegro. In both entities, commercial banks are providing consumer loans that serve as a substitute for microfinance loans, but are asking for stronger collaterals, such as salary domiciliation or salaried co-guarantors.

Montenegro: With 0.6 M inhabitants, Montenegro microfinance market is structurally limited. AgroInvest (AI) faces indirect competition from Alter Modus, an NGO that operates in urban areas but does not target rural villages yet. Opportunity Bank, a former NGO transformed into a full-service bank has a special agriculture line sponsored by KfW and charges interest rates that are significantly lower than those of AgroInvest¹, thus representing a strong competitor. Urban areas, where banks are operating are not a target market for AI that however suffers from banks' competition in peri-urban villages, noticeably Podgorica.

Serbia: Banks have been growing fast and downscaling trends are expanding, while ProCredit Bank is specifically targeting the SME market. With dozens of banks² present in main cities, competition has become very strong, driving down interest rates. Some banks have identified rural villages as potential target areas and began to send LOs to the field. The NGOs MDF and Mikrofin work with partner banks to provide funding to refugees and are not direct competitors of AI. They are both smaller in scale and operate predominantly in different geographic regions. Even though the bank market seems to be saturated in cities, large areas remain untapped.

■ Political & economic environment

The highly complex political and economic history of Serbia and Montenegro results in very different operating environments for microfinance in each republic. Although being one country, the Union of Serbia and Montenegro is composed of two republics and two semi-autonomous provinces (Kosovo and Vojvodina). During the Milosovic period, Montenegro's economy was separated from the rest of the country and was not under control of the federal Republic of Yugoslavia. Some structures are inherited from that period, including different central banks, currencies (Euro vs. Yugoslav Dinar), taxation systems, customs tariffs, and fiscal policy. A referendum regarding

¹ Nevertheless, accessibility to loans is hard for villagers working in agriculture, and collateral policies of banks are very conservative.

² 55 in Nis, of which 7 can be considered as potential competitors

the independence of Montenegro was held in May 2006 and Montenegrins expressed their willingness to go further in the separation from Serbia. Potential effects on AI's activities are difficult to assess but shall be limited thanks to the newly adopted legal structure (*see G domain for enhanced details*).

COFACE Country Risk Rating: C – (A very unsteady political and economic environment could deteriorate an already bad payment record).

After a decade of disinvestment and conflict, the political normalization process and the reforms undertaken since October 2000 have allowed the country to win international financial community support and consolidate its economic and financial situation. Foreign debt restructuring has improved the country's solvency, and Serbia and Montenegro benefits from skilled and low-cost workforce. Although economic growth has slowed due to the tightening of fiscal and monetary policy and moderation of farm production after an exceptional harvest in 2004, it has remained relatively robust. In 2006, it should be buoyed by investments made by newly privatized companies, the development of services, consumption, and a slight improvement in foreign demand. Sovereign risk has eased thanks to improved fiscal performance and the ongoing foreign-debt restructuring process.

USD millions	2003	2004	2005(e)	2006(f)
Economic growth (%)	2.1	8.0	5.0	5.0
Inflation (%)	11.2	9.8	15.9	13.6
Public sector balance (%GDP)	-3.3	-0.3	1.2	1.9
Exports	3,054	4,219	5,485	6,472
Imports	7,941	11,653	11,245	12,257
Trade balance	-4,887	-7,434	-5,760	-5,785
Current account balance (%GDP)	-9.7	-13.1	-7.8	-7.5
Foreign debt (%GDP)	69.2	62.0	59.3	58.4
Debt service (%Exports)	6.1	9.1	13.9	12.7

(e) estimate (f) forecast **Sources:** COFACE's Country Risk Ratings Guidebook 2006. Data is provided with authorization from COFACE - a shareholder of Planet Rating.

Major imbalances have nonetheless persisted. Inflation has reappeared and external accounts are still in a deteriorated state despite a reduced trade deficit, attributable mainly to a slowdown of imports. Those weaknesses largely derive from the still excessive share in the economy of state-owned companies lacking financial discipline, productivity, and competitiveness. The business environment has improved, however, and foreign investors have been demonstrating renewed interest in the country. The political situation has been shaky even if the government has strengthened its position by engaging in negotiations with the European Union on a stabilization and association agreement. Challenges to the country's territorial integrity have persisted as has the risk of early elections and coming into power of populist and ultra nationalist parties.

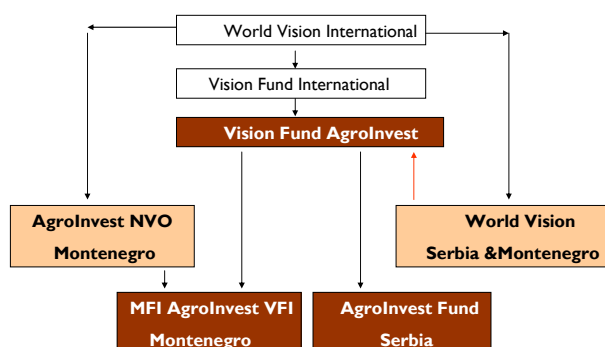
▪ Institutional presentation

Networks

AgroInvest (AI) is a member of World Vision International (WVI) and Warsaw-based MFC (the Microfinance Center for Central and Eastern Europe and NIS).

Ownership

The institutional transformation has been the MFI's main priority for the last two years and AI legal structure is nearly finalized, despite some expected evolutions³. AI Group is now comprised of five entities (one holding company based in Montenegro, one LLC and one NGO in each of the territories). The holding company is 100% owned by Vision Fund International (VFI)⁴. Both NGOs have been transferring their assets to the LLCs and are now used as fundraising entities (since LLC cannot receive subsidies). The two LLCs are the lending entities. The Board of Directors (BoD) of the holding oversees the operations for the whole group (*see complete legal and ownership chart in appendices*).



LLC

NGO

To ease the reader's comprehension, simplified names are used in the report to refer to the different entities created by AI. The actual names and the ones used in the report are provided in the table below. Each territory's NGO and LLC are jointly referred to as the Serbian or Montenegrin MFI. The whole group is referred to as AgroInvest (AI).

Name	Status	Referred to as
AgroInvest NVO	NGO	AI Montenegro NGO
MFI AgroInvest VFI	LLC	AI Montenegro LLC
AgroInvest Fund	LLC	AI Serbia LLC
World Vision S&M	NGO	AI Serbia NGO
Vision Fund AgroInvest	LLC	AI Holding

³ Next steps to be validated are the possibility of transferring funds from Serbian LLC to Montenegrin LLC and from the LLCs back to the holding.

⁴ Holding created by WVI that owns all WVI NGOs that has been transformed into LLCs

AI is governed by a five-member Board of Directors (BoD), the holding being the only entity to have a BoD. New Board members are elected by the existing Board. The current BoD is headed by Mr. Max Buskens (*see composition of BoD in appendices*)

AI's founder, WVI, remains the key decision-maker and has a *de facto* veto right on key issues:

- WVI representatives sit on AI BoD (the Chairman of the Board is a member of WVI's BoD)
- WVI loan contract with AI outlines very strict rules on operations, among which are maximum PAR and write-off ratio levels.
- WV controls 100% of AI's total equity and owns the eMerge loan tracking system.
- AI benefits from WVI's network through trainings, IT licensing, and technical assistance plus some funding obtained through WVI.

Shall the legal environment evolution complicate the fund transfers between entities; AI will keep receiving strong support from its founder organization.

Management team

See organizational chart in appendices

AI management team is headed by an expatriate Executive Director (ED), Kyhl Amoson, who has held that position since 1999 and is expected to stay at least until the end of the institutional transformation. The team is comprised of a Financial Manager, a Human Resource (HR) Manager, a Business Development Manager, a Montenegrin MFIs Director and an Internal Auditor (not formally part of the Senior Management Team but invited to their meetings) who reports directly to the Audit Committee of the Board. The local team has been recently reinforced with the hiring of a Director for Serbian activities (*see Organizational chart in appendices*).

The Executive Director has been on leave during two 6-month periods (in 2005 and 2006). In 2005, the Business Development Manager stood in for his position and the Montenegro MFIs Director is currently the acting Executive Director. These absences did not disrupt the institution's activities and help prepare the organization for a potential succession.

Donations

Since inception until end of 2005, AI has received donations amounting to more than 4 M EUR, coming from international donors such as SIDA Sweden (2,285 K EUR), CIDA Canada (1,235 K EUR), BPRM (226 K EUR), WV US (154 K EUR), WV Canada (133 K EUR) and WV Australia (83 K EUR).

Legal form, supervision and audit

AI is under the supervision and regulation of the Ministry of Finance in Serbia and of the Central Bank in Montenegro.

- In Montenegro, AI is subject to monthly reporting and periodic inspections. Effective interest rates have to be computed for each loan disbursed and have to be included in the loan contract. Prudential norms only include a maximum leverage of 300% (debt/equity) and a ban on savings collection. MFIs are authorized to provide loans⁵, leasing product, and consulting.
- In Serbia, the law expressly prohibits non-banking structures from providing loans and therefore all microfinance operations must be channeled through a registered bank⁶ and follow banking norms⁷. By law, non-banking structures cannot borrow funds in foreign currency. This problematic legal environment has greatly limited funding opportunities for AI during previous years, but the transformation into a Limited Liability Company (LLC) owned by a Montenegro-based holding shall allow for easier money transfers between AI entities in Montenegro and Serbia, thus preventing lack of funds.

AI initially operated independently of any banking structure when it launched services in Serbia in 2001 and despite successive attempts to get the Serbian government to approve its lending activities, AI did not get any favorable response. As a result, a bank partnership was eventually signed in 2003. The government is currently inquiring about the 2001-2003 lending activities and interviewed several staff members (as citizens). Risks to see AI sanctioned (through AI Serbian NGO) are estimated low by management.

PriceWaterhouseCoopers was the external auditor for FY 2000 (end of FY was September 30th) and, after the merger, KPMG was hired for FY 2001 and FY 2002. Ernst and Young has been the auditor since FY 2003. The auditors produced consolidated reports in EUR as well as separate financial statements by republic in EUR. In 2004, the auditors have approved these financial statements without reserve. In 2005, each firm was audited, as well as several consolidations (“Holding+LLCs”, all Montenegrin firms, all Serbia-based firms) but the auditors did not produce consolidated data for AgroInvest Group. They expressed reserves regarding the accounting of interests⁸.

⁵ Authorized maximum loan sizes are 8,000 EUR for individuals and 20,000 EUR for businesses.

⁶ The bank is party to the loan contract but bears no credit risk.

⁷ One of the obligations is the constitution of an 18% reserve. With the old partner bank it was the responsibility of AI, but the new partnership with Commercial Bank specifies that the reserve is constituted by the bank. Other rule is a 20% revenue tax.

⁸ The organization recognizes the originated interest and fee as income on a cash basis. Under the Montenegrin accounting standards these should be

AI frequently receives additional audits by organizations such as CIDA, World Vision MEER, KfW and Central Bank of Montenegro. None of these additional audits identified major weaknesses or inaccuracies, apart from non compliance with the requirement from Central Bank of Montenegro regarding the integration of the Effective Interest Rate in the loan contracts.



Organization

- AI is progressively moving its headquarters (HQ) from Belgrade to Nis in Serbia (for all operational matters) and Podgorica in Montenegro. The Belgrade office only hosts the Executive Director, Finance Manager, Internal Auditor and Business Development Manager⁹, the HR Manager having moved back to Montenegro.
- Eleven lending offices are operating: five in Montenegro (Podgorica, Berane, Bijelo Polje, Njivice and Pljevlja) and six in Serbia (Cacak, Kraljevo, Uzice and the newly opened Nis, Leskovac, and Vranje). All credit decisions and loan tracking data entry are decentralized to the branches. Accounting data is first processed at the branch level and then centralized.
- In addition to the branch level staff, the 254 Village Associations¹⁰ play an integral role in the service delivery. Each village typically groups around 150 households that share solidarity links and are interrelated in terms of communications, road systems, businesses, family, education, and history.
- AgroInvest works with partner banks in both republics for disbursements and in Serbia for all loan operations. In Montenegro, the partner bank is only used to disburse the loans in order to limit cash risk and because of Central Bank’s regulation. Clients receive a document upon loan signature and must present this document with identification to the bank to receive the loan. In Serbia,

recognized on an accrual basis. The external auditors were unable to estimate the effects of this matter on the net result of the organization.

⁹ On maternity leave at the time of the mission.

¹⁰ 115 in Serbia and 139 in Montenegro. See A section for enhanced details on their role;

the bank is a legal party to the contract, which is signed by the client, AI, and the bank. The bank therefore maintains a separate account for each client and tracks repayments by client, although it is AgroInvest staff and not the client that physically brings the cash to the bank for repayments.

Products and services

A detailed description of products is provided in appendix
AgroInvest's range of products is minimalist, as the institution offers only one loan product in all its branches, the Village Association (VA) Agroloan. The loans range from 250 EUR to 5,000 EUR (maximum of 1,500 EUR for a new client) with terms from 3 to 36 months (maximum of 18 months for new clients) and a maximum grace period of 6 months. The nominal interest rate is of 18% per year¹¹ and AI charges also fees of 2 to 2.5% (with an additional 1% commission for the partner bank in Serbia). Repeated clients can benefit from better rates thanks to a grade system (clients graduate silver or gold according to their number of cycles, and are then offered monthly rates of 1.4% and 1.3%). The effective interest rate thus varies from 32.1% to 36.2% in Montenegro and from 33.3% to 37.4% in Serbia.

AgroInvest developed the Village Associations' (VA) system to combine the village banking and individual loan models. Clients form the VA and nominate respected members of the village to serve as community representatives, known as the Village Council (VC). These village groupings are informal and serve only to facilitate the work of loan officers (LOs), particularly in remote and less populated areas. The VC members provide assistance with marketing, client selection, loan monitoring, repayment collection and delinquency management.

A new product named "fast loan" is being tested in two branches in Montenegro, for both repeated and new clients, who can benefit from simpler processes (less collaterals, shorter terms), and therefore quicker disbursements (one day). This loan is not tracked separately in the system but seems to show good results. It shall be extended to all Montenegrin branches in 2006.

¹¹ Serbian clients now benefit from lower rates than they previously did. Nominal monthly interest rate dropped from 1.7% to 1.5% thanks to the bank new partnership

■ Governance

Governance and Decision Making is rated « **b** »

Decision-making

The new legal structure gives both entities a common BoD, which was particularly needed for Serbian activities where ownership was not clear¹². The current BoD serves an appropriate role of mission setting supervision, notable through the Audit Committee. The clear mission to support rural families while being financially sustainable is shared by the BoD and management team and guides the institution's strategy. Plans and budgets are submitted to the Board for discussion and approval, with the initiative being in the operational team's hands. The BoD remains the final decision-maker, discusses relevant subjects and asks for deeper analysis when needed. The Board (essentially its President) has been particularly involved during the ED absences and closely followed all critical files.

AgroInvest BoD however still lacks local qualified professionals involved in running the MFI, as well as key competences in banking and finance, which are even more necessary given the new for-profit statute (*see list of Board Members in the appendices*). These weaknesses have been clearly identified and efforts have been made to strengthen the BoD¹³ but must be pursued. This will have to be dealt with soon given that some members are to be replaced in the coming months and that the Board could be running for a while with only three members, all of which are living outside S&M. The new Chairman of the BoD has an extensive experience in Board membership and is really willing to find local individuals to join the BoD, even if it has so far proven difficult to find such people locally without paying them.

The BoD receives all necessary information and the quality of reports is improving over time. Board minutes are well-documented.

Planning

The Strategic Plan process for 2006-2008 involved the right actors (BoD for mission and vision and operational senior staff for financial projections and detailed action plan). The Management Team collectively gained experience over the course of previous business planning processes and has been able to update the plan while the ED's was on leave.

The plan addresses relevant subjects and strategies, although it could provide more details on competition and

¹² As a branch of an international NGO, the institution had no statutory BoD.

¹³ Definition and formalization of their tasks and responsibilities in a BOD policies

products diversification matters. Now that the main legal challenges have been addressed, AI will be able to focus on its market, and fully use its financial and human resources to face competition.

The main lines of the 2006-2008 Strategic Plan are:

- Finalization of the legal and ownership structure (validation of free capital flows between AI MFIs; completion of asset transfers between NGOs and LLCs) as well as organizational structure (staff satisfaction assessment; social performance management system).
- Performance improvement and expansion for Montenegro: opening of a new office in 2007 in South Montenegro, generalization of the fast loan and improvement of the competitiveness of existing VA product (price, quality of services).
- Potential establishment of a structure allowing AI to lend directly to its clients in Serbia. Though this would clearly be optimal, the current structure already solved many of the existing issues and should allow for an enhanced growth in Serbia.

The planned quantitative goals are adapted to each entity's market conditions and more realistic than previous ones (slow growth in number of clients but product diversification for MNG where the market is limited and AI's coverage already high vs. quick increase in number of clients in Serbia where wide areas remain untapped). In 2004 the legal burden had been underestimated and non-disbursement periods (related to the change in bank partnership) had not been anticipated. The Serbian MFI was thus not able to reach its targets (in 2004 AI forecasted to reach 25,000 active clients by the end of 2006 for a portfolio of 29 MEUR). The funds needed to finance this growth (6.2 MEUR¹⁴) have now been secured and the growth in Serbia should not suffer from lack of funds anymore with the new structures in place.

The new financial projections are of high quality and updated regularly (using Microfin). Objectives are defined at the institutional level and declined per branch and per LO. The budget planning process is of high quality with improvements noted in tools and involvement of branch staff. The budget tracking and monitoring is efficient and adopts best practices.

Management team

The management team has been reinforced over the years with operational management for Serbia and Montenegro now being separated to better address these two territories particular needs. A Senior Management Team (SMT) has

been formed (with formalized meetings, minutes and follow-up on decisions) and consists of the ED, the Serbia MFI Director, the Montenegro MFI Director, the Business Development Manager, the Finance Manager and the Human Resource Manager. The IT Division has not been created as an independent department yet but a new staff has been joining the existing one and the system administrator fills in for the IT Manager and is in charge of supervising the MIS transition together with the SMT (cf. I). The Internal Auditor, based in headquarters, reports to the Audit Committee of the Board.

The management team provides an effective leadership and has a good understanding of key challenges, communicates well and succeeded in creating the right and confident mindset among staff. The team has relevant professional experience for their respective positions, with the exception of the newly hired Serbia Director who has no previous experience in microfinance but does have strong management skills.

Though quite young, this team has proved its capacity to manage the institution during the periods when the ED was on-leave. Trainings and on-the-job experience allowed them to acquire the required operational skills which considerably lowered the key-person risk, all the more given that the ED has been spending most of his time on legal and institutional structure matters that are now resolved. The Board has sufficiently anticipated the potential departure of the ED. Even though no formalized succession plan has been set up, the necessary measures have been taken to ensure a smooth transition if the ED was to resign in the medium term. The BoD Chairman's implication, availability and experience also support SMT's work and shall ease this possible transition.

Nevertheless, the challenges ahead (adaptation to the new for-profit statute, growing competition, long-term expansion plans including significant growth) leave room for improvements in Internal Audit (*see R for enhanced details*), product development (noticeably for possible new fee-based products as insurance) and institutional strategic planning (in case of expansion in other countries, or merging with other institutions).

Human Resource Management

AI has always given a great importance to HRM, with the early creation of an HR Manager position, discussions on HR role in the Strategic Plan and a comfortable budget dedicated to HR during the last years. The HR department is responsible for all strategic aspects of HR (recruitments, training planning, performance reviews, salary grid, and incentive systems definition), while the administrative tasks are outsourced. The creation of new entities has been highly time-consuming for the HR Manager since it implied

¹⁴ 4 M for Serbia and 2,2 M for Montenegro, with contracts already signed or close to be signed with Incofin, Deutsche Bank, KfW, Blue Orchard, Vision Fund

the transfer of all staff contracts¹⁵ from NGOs to LLCs¹⁶ and the application of for-profit entities rules (such as pro-format payrolls...). The process is now over and the HRM can now dedicate herself exclusively to more HR specific aspects.

- The recruitment and induction process is clear and pertinent and allows AI to benefit from skilled staff. Investments have been made at the Senior Management level to attract new and relevant competencies.
- Performance reviews are conducted each year to evaluate each employee's achievements, update the objectives and identify training needs.
- The salary grid has been recently redefined (June 2004) and seems to be effective to prevent staff from leaving for other institutions or banks¹⁷, as shown by low turnover (average of 2% on the last 3 years).
- The incentive schemes for LOs and branches have been defined to be coherent with both social¹⁸ and financial objectives and can be hard to reach. The lack of funds experienced in Serbia have also made incentives quite difficult to get (no LOs in Serbia got a bonus last year), which could have negative effects if the situation was to last longer. Bonus policies are very demanding for all staff (regional and corporate staff as well) and represent an award for exceptional performance rather than a variable part of salary, as typically seen in microfinance.
- Being the main asset of AI, human resources are constantly being trained, both externally and internally, with courses adapted to specific needs of all staff (from field staff to senior management). Trainings expenses account for close to 15% of all expenses in 2005, and the standard is to dedicate at least 3% of financial revenues to trainings. In 2006, the priority will be given to middle-management with ambitious professional training program for all branch managers, using highly elaborated tools and expertise of external consultants (PWC).
- AI also uses "acting" positions as an opportunity for LOs and senior management to gain field or management experiences. In case of vacancies of Branch Managers (BM) (linked to the opening of new branches, maternity leaves or departures of staff), the positions are filled for a few months with LOs or newly hired Senior management staff (such as the new Serbia MFI Director) which promotes internal learning exchange and is also a tool to identify fraud cases or to lower the cost of new branches set up.

¹⁵ ED is the only employee of the holding structure. Until all portfolio of the Serbian NGO is transferred to the Serbian LLC, some staff has to be maintained in the NGO for signature purposes, as the NGO works with Meridian Bank for remaining loans. See "F" and "R" for enhanced details

¹⁶ Cf. Organizational chart in appendices for staff distribution

¹⁷ Opportunity bank has tried to hire staff from AI but hasn't succeeded whereas others Montenegrin MFIs have seen staff leaving

¹⁸ Targets such as percentage of women are part of the incentives computation.

	Sept. 2002	Sept. 2003	Dec. 2004	Dec. 2005
Total number of staff	53	61	77	95
% Credit officers	53%	49%	43%	37%
Turnover	5%	2%	1%	3%

Information

Information and equipment is rated «b»

Description of the MIS

- | | |
|-----------------------|--|
| Equipment | <ul style="list-style-type: none"> ▪ Computers, ADSL/ISDN and access to Virtual Private Network in all branches. ▪ Servers dedicated to eMerge/ Sun Systems/ LTS/ mail ▪ Intranet portal for information sharing. |
| Accounting | <ul style="list-style-type: none"> ▪ Sun Systems: internally designed software to produce all analytic data needed ▪ Data entry by Regional Finance Manager. Bookkeepers send branch journal vouchers (Excel) on a weekly basis ▪ Data tracked at the Village Association level ▪ Daily reconciliation with bank statements at the branch level, checked weekly by the RFM. ▪ Comprehensive monthly reconciliations ▪ Monthly financial statements per entity, region and consolidated including depreciation and provisions |
| Portfolio information | <ul style="list-style-type: none"> ▪ eMerge (Temenos) used in MNG with additional in-house application to generate reports and administrative documents (Crystal based) ▪ Loan Tracking System (Access, C++) used in SER. Implementation of eMerge to be done after resolution of bugs. ▪ Client data entered at the branches; sent for consolidation by email on daily basis |

Management Information System (MIS) and Equipment

AgroInvest began the implementation of eMerge in 2004 in Montenegro and had planned to set it up Serbia in 2005 but paused the implementation given the numerous difficulties encountered during the migration process in MNG. As a result, Serbia and Montenegro currently use different software. eMerge was however installed as part of a global WVI initiative¹⁹ and AI, despite IT staff preference for a locally-developed software, decided to continue with the implementation of eMerge and to stabilize it. At the time of the rating mission, the team was to attend an eMerge

¹⁹ All WVI-founded MFIs have implemented eMerge. AgroInvest has paid for the eMerge licence, at a lower rate negotiated by WVI, and has also signed an annual maintenance contract.

Administration Training session²⁰ for the very first time. This should allow AI to internalize the necessary skills and not to rely anymore on the maintenance firms that have been difficult to mobilize and have not proven to be efficient.

In Montenegro all branches are currently using eMerge²¹ along with an application that was internally developed to compensate for eMerge shortcomings. The changes in legal status brought new regulatory obligations for AI that cannot be performed automatically by eMerge, which added up to other bugs previously found in the system. Most of eMerge weaknesses are however now being handled:

- The computation of the Effective Interest Rate is now handled with an internally developed additional module, and therefore EIR is included in all contracts.
- Partial and early repayments are now correctly accounted for.
- The slow performance of database has been mainly addressed²²,
- Lower staff productivity²³.

In Serbia, the locally developed LTS is still used to manage the information on activities, and despite its high vulnerability (Access database) provides AI with all needed information. The experienced and recently reinforced IT team of three succeeded in developing complementary modules and applications to generate all needed reports, as well as adequate policies to insure data security²⁴.

Information on activities

Despite its inconvenient information production process, AI generates all the information it needs to manage its operations efficiently. Relevant reports are issued and used by field staff for portfolio monitoring. Comprehensive data (outstanding loan portfolio, PAR, number of active/repeated clients) are available per branch, LO and VA and consolidated monthly. AI also performs studies on its markets (market size, market penetration), its competitors (conditions offered, SWOT analysis) and its clients (satisfaction, drop-out explanation). An ambitious social impact measurement tool is to be implemented in 2006 and should provide AI with interesting qualitative information.²⁵

²⁰ Held by experts of DBS

²¹ Some information has to be checked in the old system as clients' history cannot be found in eMerge (used for example to determine the interest rate to apply).

²² Reports are still extremely long to be produced and bugs remain in generation of information

²³ Client administrators are handling more or less half of the number of files they were able to manage with the LTS system

²⁴ Data manipulation risk is limited due to good authorization levels. Data loss risk is managed via frequent back-up and storage procedures.

²⁵ A team of 5 staff (the Executive Officer, head of project which allows 50% of her time on this project, one technical staff (IT manager), one

Financial and accounting information

Accounting has been highly complicated by the creation of new companies which implied new charts of accounts (AI is currently using 4 charts of accounts) and required numerous adaptations in Sun Systems. Regional Finance Departments in each region have been created to ease the accounting processes. Thanks to the Finance team's skills, AI financial and accounting information is available on demand, timely and of high quality.

Financial statements are available monthly (consolidated, per region and per company) and comprehensive financial analysis is generated for internal and external use, following the industry best practices, with prior period data available for ease of comparison. Useful operational and financial analysis includes results by founder, by VA, by branch and is used to estimate start-up costs and break-even levels. With new products being launched, ABC analysis would be interesting to add.

The legal requirement in Serbia to operate through a partner bank brings specific challenges, as the MFI is dependant on the bank's quality and frequency of information. AI was previously working with Meridian Bank with which it encountered big issues related to information reconciliation that are all not resolved yet²⁶. AI recently signed a new partnership with Kommercial Bank²⁷ which is greatly easing reconciliation, transparency of transactions, and staff work.

All financial reports are widely disseminated to relevant people and closely reviewed by management and BoD. Information sharing is eased by AI Intranet.

▪ Risk

Risk Management is rated « a »

Procedures and internal controls

Policies, rules and procedures have been formalized in comprehensive manuals. Credit and finance manuals still need to be updated with the latest changes, which has been included in the relevant department's objectives. The application of procedures is constantly checked and the segregation of duties is adequate²⁸. Hierarchic controls are regularly performed and the portfolio management is

finance analyst, and two operational staff) is dedicated to this project for a budget of approximately 80,000 USD, funded at 99% by MFC. It aims at assessing life conditions and welfare improvements made possible through the provision of financial services by the institution.

²⁶ The case might finish in court. Amounts still due by the bank are evaluated at approximately 130,000 EUR.

²⁷ Conditions are much better as fees are lower and the 18% legal reserve is the responsibility of the bank.

²⁸ At least two staff members see the clients. Data entered by separate staff, several levels of Credit Committee, VC.

closely monitored for compliance to defined procedures, which is eased by the availability of timely information. Disbursements are channeled through banks which thus limit the cash handling risk. Repayments are collected in the villages without insurance, but several staff travel together (at least two) in order to mitigate the risk and no robbery has been reported so far.

AI credit methodology gives a key role to VCs who support LOs in several tasks (from clients' selection to delinquency management). Such implication of non-staff in the credit processes could be risky²⁹ but is closely monitored by LOs, BM, RM and internal audit, and was recently formalized by the signature of contracts with the VCs³⁰. Fraud is effectively controlled at the branch level by daily reporting and monitoring of the loan portfolio by BM and Finance staff. Another level of internal control lies in staff rotation thanks to the "Acting BM" system (see HR § in the Governance section).

Internal audit

AgroInvest has a good risk management culture with great implication of the Senior Management Team on key risks. The Internal Audit had been implemented as a key position years ago, but the development of audit procedures and policies has suffered from repeated changes in the IA position³¹ and from the new legal structures which brought new regulations and challenges. The new IA though relatively new (started at the end of 2004) has a deep knowledge of AI's rules and procedures (she had been a bookkeeper, cashier and Senior Accountant) and benefits from her prior experience as a Finance Inspector in a mobile phone company. Specific trainings on IA in microfinance and MIS challenges would help her to better organize her work and prioritize her controls.

The IA performs deep controls on legal issues, finance and credit operations as well as other HQ departments (notably HR given the new legal obligations brought by LLC statute) and competition. Based on a very detailed and adequate annual plan, approved by the Audit Committee of the Board, the IA inspects each branch at least once a year and meets with randomly selected clients (approximately 2% of clients). Regular direct reporting to this Audit Committee ensures good information flow, feedback, validation of findings and follow-ups of recommendations. No new

hiring has been planned for 2006, but new staff will be needed if targets are to be met in Serbia.

KPMG performs very comprehensive³² annual external audits using international accounting standards and has certified accounts without reserve.

■ Activities

Activities: products and services is rated « a »

Marketing and competition

The microfinance sector has become far more competitive in both territories over the years, with banks downscaling and targeting low-income clients. Even if the competition remains very low in rural and remote areas, AI has to pay increasing attention to its competitors' strategy and develop its marketing tools.

AI's range of products is still minimalist though adaptations have been made through time to better suit clients' needs (amounts, duration) and give them better conditions (lower interest rates for repeated clients). The loan methodology includes a couple of competitive edges, notably the collection of repayments in the village and easier guarantees requirements than banks. Interest rates are less competitive than banks but are following a downward trend (for all clients in Serbia and repeated ones in Montenegro), and are similar to other MFIs. AI allocates 3% of profit to "happy child" projects, which consist in funding children-linked infrastructures in the villages, such as schools or playgrounds. This is very appreciated by AI's clients and VA.

Whereas large untapped rural areas remain in Serbia, the Montenegrin market is close to saturation with aggressive actors having entered the sector and offering several types of products with attractive conditions. Despite having a new product under way (a fast loan is being tested and shall be offered in all branches in the coming months), AI product development has been slow and has to become a priority to guarantee AI's growth and market shares. AI's core competitive advantage resides in its proximity to clients which tends to become less true in villages close to cities (particularly true in the Podgorica area) where banks have begun to attract AI's clients.

Competition has been identified as one of the main risks to be faced and the Internal Auditor and other dedicated staff are conducting market researches with improved tools and techniques. A marketing based on word-to-mouth has been sufficient in remote rural areas so far, but now needs to be

²⁹ Since inception, only one case of fraud has been discovered in Krajlevo which resulted in a change in the VC and net loss for AI of 1,300 EUR.

³⁰ As a LLC, AgroInvest could not pay the VCs by cash anymore. Contracts have been signed to respect legislation. Amounts paid are the same than before (1.1 EUR per client, and 1.2 EUR if the association is older than 2 years).

³¹ Three different persons in two years. The current IA has previously worked with AgroInvest, but left for a 2-year period to another company.

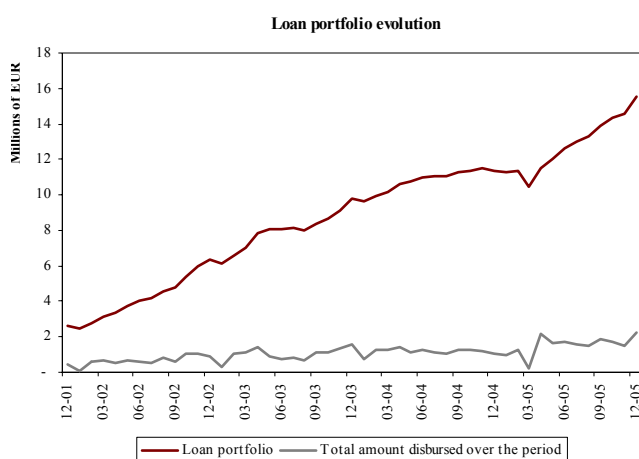
³² In 2004, 49 loans had been audited, (balance, as well as internal controls relating to approval, disbursement, collection, booking and all other procedures relevant to the loan).

more sophisticated to retain clients especially if offices were opened in more saturated areas in the Southern part of MNG.

Credit methodology

AI's excellent portfolio quality and high staff productivity is attributable mainly to the rigorous application of pertinent credit methodology and policies, and to the recruitment and training of good operational staff:

- Client selection is mainly based on reputation and on cash-flow assessment, and is eased by VCs who review all clients' files, perform home visits together with LOs and assess the clients' debt capacity. VCs also play a key role in loan monitoring as they are in charge of collecting all repayments prior to the LO's visit.
- Credit Committees (branch manager and one or two other LOs in addition to the presenting LO) approve loans and decide on the loan amount. Given the pre-selection by LOs, the Credit Committee does not typically reject applications, but represents another level of internal control.
- Thanks to the availability of up-to-date information and to the VA methodology, delinquency can be addressed immediately by LOs.
- LOs are typically born in the community, committed, well-trained and motivated with good knowledge of their region and market. Branch managers are experienced and have a clear vision of their role of both supervision and support.
- All lending staff is aware of client over-indebtedness risk and tries to mitigate it through their own investigation and consultation of Credit Bureau database (only available in Serbia for now).

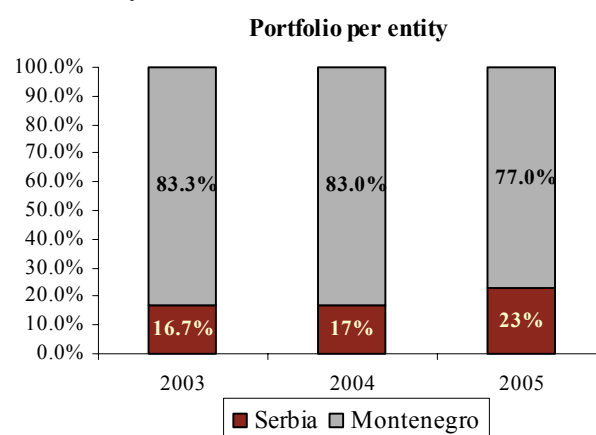


Evolution of the portfolio

Fast growth of loan portfolio over the past three years is driven by the increase of both number of clients and average outstanding loan by client (larger amounts are lent to repeated clients). Growth has been slowing down in 2004 and 2005 though remaining high (above 35%) and is forecasted to be maintained at such levels in the coming

years. Seasonality is low, even if the Orthodox holidays season (January) is traditionally a peak of activity.

The change in bank partnership and legal transformation explain the dip in disbursements in March 2005, which should not happen anymore now that both issues have been addressed. The new legal set up is expected to solve all funding problems of the Serbian MFI and it is planned that the loan portfolio in Serbia will reach the Montenegrin size within two years.



K EUR, unless otherwise stated	Sep. 02	Sep. 03	Dec. 04	Dec. 05
Loan portfolio	4,774	8,362	11,358	15,517
Evolution	138%	75.2%	35.8%	36.6%
Average outst. Loan	3,251	6,977	10,351	12,710
Number of active borrowers	5,208	9,629	12,967	14,679
Evolution	149%	84.9%	34.7%	13.2%
Average outst. loan per client	917	868	876	1,057
% of GDP per capita	68.6%	38.8%	36.5%	40.7%
Av. amount disbursed	1,386	1,409	1,847	1,583
% of GDP per capita	104%	63.0%	77.0%	60.9%
PAR 31-365	0.2%	0.2%	0.2%	0.1%
PAR > 365	0.0%	0.0%	0.0%	0.0%
Write-off ratio	0.1%	0.1%	0.4%	0.2%

Quality of the portfolio

Despite fast growth (over 35% in the last two years) and competition increase, AI portfolio remained of very high quality with a PAR>31 below 0.2% over the period. Quality is similar in Serbia and Montenegro despite higher short-term PAR in MNG (PAR1-31 of 0.8% vs. 0.4% in SER) and quite homogenous in all branches, thanks to high reliance on VA-based methodology, good training of staff, high supervision and support of middle-management. AI has a policy of writing off each month loans that are late by more than 180 days. Its write-off ratio remains more than reasonable and is even decreasing (around 0.2% in 2005 vs. 0.4% as of end of 2004). Loan rescheduling is not allowed.

Portfolio diversification

AI portfolio is highly concentrated in agriculture (89% of the portfolio as of end 2005; mainly animal breeding and greenhouses). AI does not have specific rules to monitor the diversification of its portfolio but branch managers are responsible for not investing more than 50% of the branch resources in the same type of business as defined by their categories (animal husbandry, greenhouse, etc.) and the geographic dispersion of branches brings some form of natural diversification with loans to various types of activities.

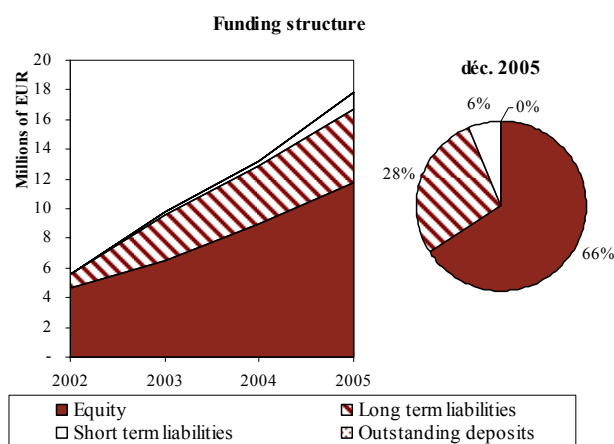
Credit risk coverage

AI changed its conservative provision policy in 2002 (a provision of 2% of the healthy portfolio was then constituted) and adopted one that adapts to provision to the level of risk (see notes to financial statements for further details). Guarantees are required as an additional measure of risk coverage (two co-signors who have to be salaried, administrative ban on salaries, promissory note, bill of exchange, pledge of land/houses) according to the amount lent and the level of risk. Such guarantees are mainly used to pressure clients and contribute to mitigate credit risks, even though they are rarely used in court and if court decisions are difficult to execute. Settlement by mutual consent, eased by the implication of VC and the community, seems to work as shown by the amount recovered on write-off loans (23.1% of write-off amount in 2004 were recovered in 2005).

EUR	Dec. 2002	Dec. 2003	Dec. 2004	Oct. 2005
Risk coverage ratio	76.6%	51.3%	97.0%	94.0%
PAR 31 net of loan loss provision / Equity	0.0%	0.1%	0.0%	0.0%

Financing and liquidity

Financing and liquidity is rated « a »



	Sept. 02	Sept. 03	Dec. 04	Dec. 05
Liabilities / Equity ratio	20,6%	50,3%	46,4%	52,0%

Details of the funding structure are provided in appendix.

Being a non-deposit taking MFI, AI funds its activities with equity (66%) and debts (34%). Equity is made of donations, retained earnings and paid-in capital of LLCs (coming from transfers from the NGOs and WVI, see appendices for further details). AI has accumulated positive retained earnings since 2001 that account for more than 39% of equity in 2005. As of end 2005, the international donors supporting AI are the World Vision network (WV Canada, WV US, WV Australia), CIDA Canada, SIDA Sweden, and BPRM. Concessional lenders are KfW (Austria and Germany) and Cordaid.

The accumulation of positive retained earnings explains the low leverage level (0.52 consolidated) which together with the good risk profile and excellent credit track record of the institution leaves room for more the addition of new debts (the maximum leverage is of three in Montenegro and are not set in Serbia).

Asset liability management procedures

Asset and liability management (ALM) risks are identified and efficiently limited.

- **No maturity risk:** as of end of 2005, more than 94% of the loan portfolio was short-term (less than one year) while close to 95% of funds being either equity or long-term loans.
- **Limited FX risk:** Even though AI has to deal with two currencies (EUR in Montenegro, Yugoslav Dinar in Serbia) this is more of an administrative burden than a source of foreign exchange risk. The Yugoslav Dinar was previously linked to the Deutsche Mark, and has not fluctuated considerably against the EUR, thus preventing major exchange variations since most liabilities are denominated in Euros. Furthermore, AI has protected itself against devaluation by indexing loan contracts with borrowers in EUR in Serbia. 77% of portfolio is invested in Montenegro and therefore in EUR. Previous loans contracted in USD have all been reimbursed.
- **Low interest rate risk:** Some of AI’s borrowings are based on variable benchmarks (EURIBOR) but expected fluctuations represent a minor risk as they are mitigated by AI’s high portfolio yield and low blended funding cost resulting from both low overall leverage (0.52 in 2005) and concessional funding.

Financing strategy

The Senior Management Team has shown its ability to negotiate good conditions for its debt funding (mostly made of long terms subsidized loans) and allowed AI to benefit from competitive though increasing rates and from long

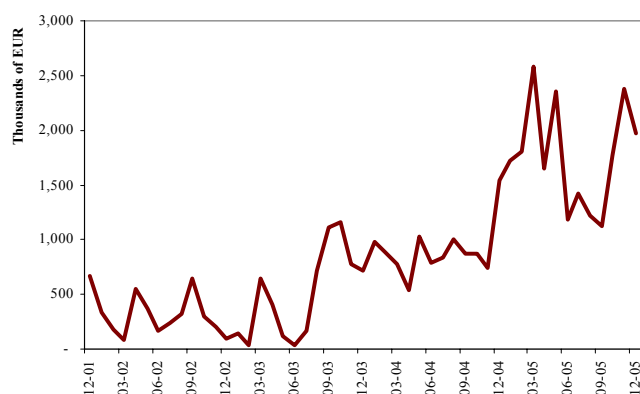
term resources (83% of the liabilities). Nevertheless, current conditions might not be available anymore, and the share of commercially-priced debts is likely to increase in the coming years in continuation of the current trend (several loans at commercial rates have already been contracted in 2005 and 2006 notably with Blue Orchard and Incofin). Local funding at good prices is not yet available, as interest rates range from 12 to 15%. In order to keep the possibility to access subsidies, AI chose to maintain its historical NGOs structures³³.

Over 100% of the funds needed to finance 2006's growth are secured for Montenegro (2 M EUR needed), and over 50% for Serbia (4.2 MEUR), the rest currently being negotiated. The objectives set in the previous Strategic Plan were not reached because of the ban on foreign currency borrowing in Serbia. The legal transformation which opens to possibility to channel funds through the Montenegrin Holding should make various funding opportunities available for the following years and make it possible to reach the ambitious goals defined in the strategic plan.

Liquidity Management

Annual liquidity forecasts are defined based on lending activity projections and are updated on a monthly basis according to disbursements plans sent by the branches. The system has proven efficient even in lack of funds period, as LOs were asked to stop disbursements before the liquidity crisis occurred, which limited potential perverse effects of such crisis. Branches can take the initiative to contact other branches and borrow funds from each other to meet short-term needs during the month.

Evolution of cash balance



Efficiency and profitability

Efficiency and profitability is rated « a »

Overview of the profitability

AI has been profitable for many years (ROE and ROA of 12.5% and 8.4% in 2005, respectively) and its profitability

³³ LLCs are not allowed to finance their activities on grants.

follows a slight upward trend with increasing portfolio yield and decreasing operating expense ratio which compensate for higher funding costs. As of December 2005, the operational self-sufficiency ratio reached a comfortable level of 152.8%.

Profitability analysis	Sept. 2002	Sept. 2003	Dec. 2004*	Dec. 2005
ROE	8.7%	11.1%	14.7%	12.5%
Liabilities / Equity	20.6%	50.3%	46.4%	52.0%
ROA	7.3%	8.1%	10.0%	8.4%
Profit generation				
OSS	139%	139%	159%	152.8%
Portfolio Yield	30.8%	31%	33.6%	33.6%
Operating expense ratio	24.2%	22.0%	18.4%	18.9%
Staff productivity	98	158	168	155
Loan officer productivity	186	321	393	419
Average outst. loan per client (EUR)	917	868	876	1 057
Funding expense ratio	0.3%	1.0%	2.9%	3.1%
Cost of liabilities	1.9%	3.9%	3.9%	3.4%
LLP expense ratio	(1.1%)	0.1%	0.3%	0.2%
PAR 31-365	0.2%	0.2%	0.2%	0.1%
Write-off ratio	0.1%	0.1%	0.4%	0.2%

Asset

management

Outstanding Loan Portfolio / Assets	84.9%	85.7%	86.2%	87.1%
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*Data for 2004 have been annualized as the change in fiscal year results in a 15-month period

Portfolio yield and Effective Interest Rate (EIR)

The portfolio yield slightly increased over the period (from 30.8% in 2002 to 33.6% in 2005) due to a higher weight of Serbian activities in the portfolio where EIR was higher prior to the change in bank partnership which occurred at the end of 2005. Thanks to a very high portfolio quality, the portfolio yield is close to theoretical EIR. Declining interest rates as clients go from cycle to cycle³⁴, lower rates offered in Serbia (from 1.7% to 1.5%) combined with increasing competition putting high pressure on interest rates shall result in declining portfolio revenues in the coming years. Nevertheless, the predictable drop in portfolio yield could be partially compensated by a further improvement in asset utilization (portfolio/total assets ratio already increased from 84.9% in 2002 to 87.1% in 2005).

Operating expense ratio

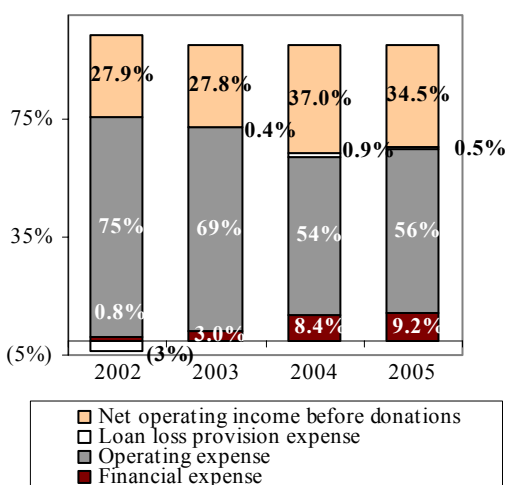
Thanks to improvements in productivity and economies of scale, the operating expense ratio dropped from 24.2% in 2002 to 18.9% in December 2005, despite hiring of new

³⁴ Cf. details of products in the appendices.

managers, large IT investments and important legal costs. The ratio should keep decreasing thanks to further economies of scale brought by the planned portfolio growth and productivity gains allowed by expected improvements of eMerge.

- LO productivity has been trending upward over the period and reached 419 in 2005 (experienced LOs have higher productivity, the highest productivity is above 600 loans per LO). Global staff productivity has decreased because of hiring of new staff dedicated to the MIS.
- The bonus scheme, though difficult to reach, are quite motivating for LOs and all branches staff. The fact that the compensation scheme is based on clear and ambitious objectives allows AI to have part of its operational costs indexed to future profitability levels.

Cost structure in % of financial income



Funding expense ratio

The funding expense ratio increased over the period with fewer subsidies and borrowing at concessional rates available and increasing funding at commercial conditions. This ratio is expected to increase in the coming years as the institution accesses more commercial funding, but could be contained if AI decides to raise equity funding, thanks to its new institutional statute.

Loan Loss Provision expense ratio

The change in provisioning method explains the 2002 negative loan loss provisioning ratio (-1.1%) which remains very low over the period thanks to the high and improving portfolio quality (0.2% in 2005). This ratio shall remain stable in the coming years, as AI credit methodology is efficiently applied by skilled staff but could be affected by the launching of new products.

Asset management

As of December 2005, more than 87% of assets are invested in the portfolio and the rest is either in fixed assets (1.5%) or in cash (11%) which shows a good level of asset utilization. It is to be noted that short-term investment

opportunities are not readily available in Serbia and Montenegro at attractive rates.

By the new bank partnership, the bank is responsible of the constitution of the 18% legal reserve, and idle resources remain minimal. Furthermore, AI has a high capacity to absorb and deploy funds thanks to the expansion of the network and ample HR in the field in Serbia.

Adjusted performance

Details concerning the specific adjustments are included in the appendices

AI is financially self-sufficient after GIRAFE adjustments although the FSS is now only slightly above 100%. The adjustment expense ratio of 10.9% in 2005 is attributable to the standard adjustments of the cost of funds (27% of all adjustments) and inflation (73%). The current loan loss provisioning policies did not require any adjustments.

	Sept. 02	Sept. 03	Dec. 04	Dec. 05
Adjustment expense ratio	28.9%	13.5%	9.6%	10.9%
AROE	(19%)	(5.7%)	(0.4%)	(2.6%)
AROA	(16%)	(4.2%)	1.3%	(0.5%)
Financial self-sufficiency	62.1%	87.5%	109.9%	102.4%

Profitability outlook

Profitability is expected to slightly increase as AI gains in size, generates more economies of scale and eventually benefits from its high IT investments. This positive outlook could however be negatively affected by continued competitive pressure on interest rates and loss of clients in rural areas close to big cities. The main challenges ahead include

- the finalization of the institutional transformation;
- the validation of the possibilities of transferring funds between legal structure that compose AI Group in both territories
- the resolution of issues encountered with the eMerge system,
- the development of new fee-based products for which AI has no experience (insurance)
- the increasing and aggressive competition which could bring along client cross/over-indebtedness.

The opinions expressed within this report are valid for one year after the rating mission. Beyond one year, or in case of a major change during this period affecting the institution's performance, that change due to the institution itself or its operating environment, Planet Rating does not guarantee the validity of the opinions contained herein, and recommends that a new rating evaluation be undertaken. Planet Rating cannot be held responsible for investments/financings that are made based on this report.

Benchmarking

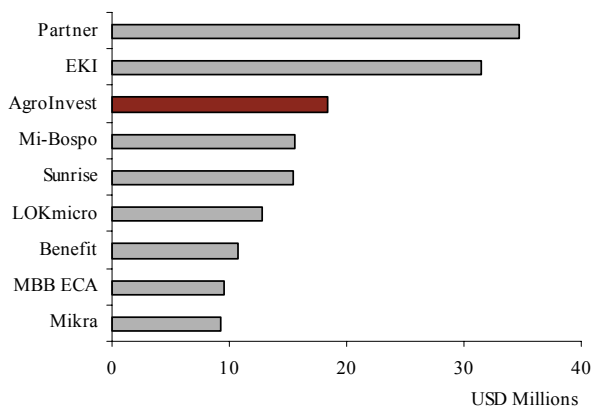
AI is being compared to its peer group as defined by the MicroBanking Bulletin (cf. table below) and to institutions based in Eastern Europe recently rated by Planet Rating.

Classification based on MBB criteria

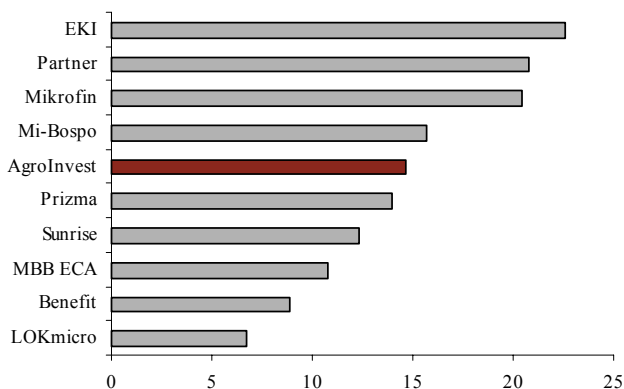
Area	Europe and Central Asia (ECA)
MBB peer group	ECA Large Broad: AgroInvest (Serbia and Montenegro), EKI (Bosnia and Herzegovina), Fundusz Mikro (Poland), FOR A (Russia), Opportunity Microfinance Bank, Inc (Philippines), Sunrise, Partner (Bosnia and Herzegovina), XacBank (Mongolia).
Maturity	Young (7 years of operations)
Scale of operations	Large
Target population	Broad

Source: MBB August 2005

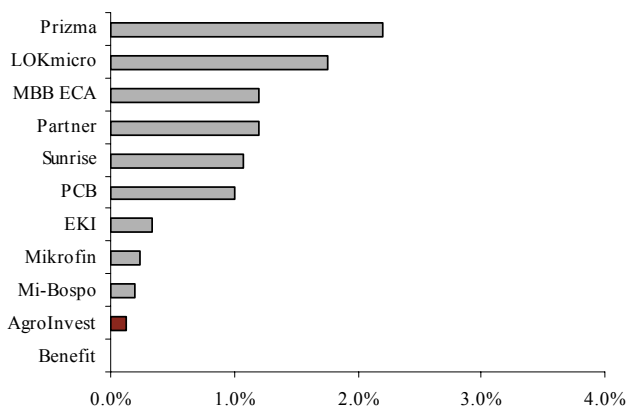
Gross Loan Portfolio - End 2005



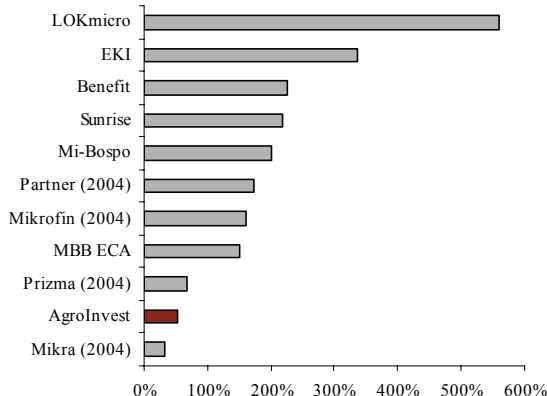
Number of Active Clients - End 2005



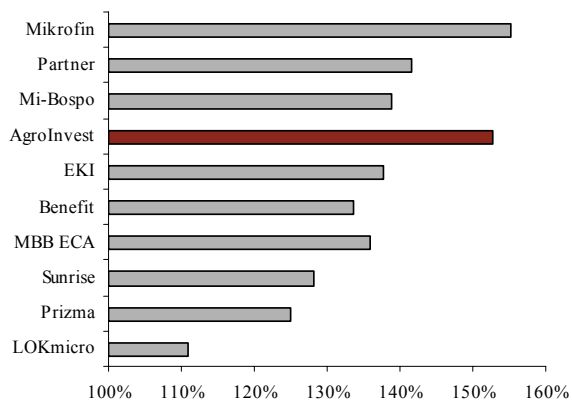
PAR > 30 days - End 2005



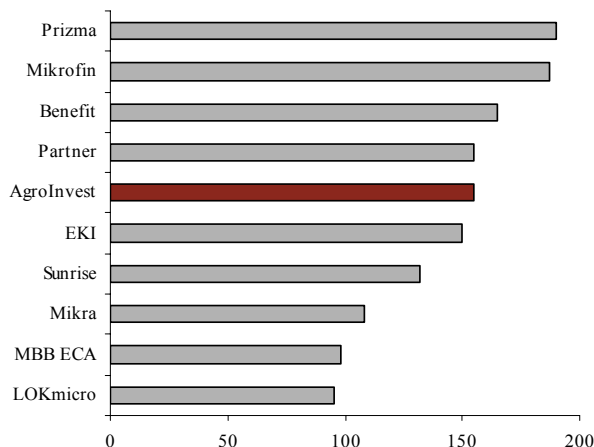
Debt/Equity Ratio - End 2005



Operational self-sufficiency - End 2005



Staff Productivity - End 2005



■ Appendices

Acronyms

AI	AgroInvest
ALM	Asset/Liability Management
BoD	Board of Directors
EU	European Union
EUR	Euro
EURIBOR	Euro Interbank Offered Rate
FY	Fiscal Year (October 1st to September 30th)
HQ	Headquarters
HR	Human Resources
GNP	Gross National Product
GDP	Gross Domestic Product
IT	Information technology
LO	Loan officer
MBB	MicroBanking Bulletin
MIS	Management Information System
MFI	Microfinance institution
MFC	Microfinance Center for Central and Eastern Europe and the Newly Independent States
NA	Not Applicable
NGO	Non Governmental Organization
PAR	Portfolio at risk
ROA	Return on assets
ROE	Return on equity
SME	Small and medium sized enterprise
USAID	United States Agency for International Development
UNDP	United Nations Development Program
USD	United States Dollar
VA	Village Association
VC	Village Council
YUN	Yugoslav Dinar
WVI	World Vision International

Formulas and ratios

- Personnel productivity: Active borrowers/Total personnel (end of period)
- Loan officer productivity: Active borrowers / Total Loan Officers (end of period)
- Return on assets (ROA): Net operating income before donations/ Average assets
- Adjusted return on assets: AROA: Adjusted net operating income before donations/ Average assets
- Return on equity (ROE): Net operating income before donations/ Average equity
- Adjusted return on equity: AROE: Adjusted net operating income before donations / Average equity
- Leverage: Debt (savings + debts) / equity (end of period)
- Portfolio yield: Portfolio revenue / 13-month average gross outstanding portfolio
- Operating expense ratio: Operating expense / 13-month average gross outstanding portfolio
- Funding expense ratio: Interest and fees paid on funding liabilities / 13-month average gross outstanding portfolio
- Cost of funds ratio: Interest and fees paid on funding liabilities / Average funding liabilities (deposits + borrowings)
- Loan loss expense ratio: Net loan loss expense / 13-month average gross outstanding portfolio
- Adjustment expense ratio: Total adjustments / 13-month average gross outstanding portfolio
- Net portfolio as a % of assets: Net outstanding portfolio / total assets (end of period)
- Operational self-sufficiency: Revenue from operations/ (Financial expense + Loan loss expense + Operating expense)
- Financial self-sufficiency: Revenue from operations/ (Financial expense + Loan loss expense + Operating expense + Adjustments)
- Risk coverage ratio: Loan loss reserves / Portfolio at risk (31-365 days)

- Write-off ratio: Loans written off/ 13-month average gross outstanding portfolio

Notes to the financial statements

General notes to financial statements per CGAP Disclosure Guidelines

- The MFI follows the CGAP disclosure guidelines.
- The Financial Statements presented include a balance sheet, income statement, and accompanying notes.
- The financial statements provided include 3 years of data.
- Segment Reporting for Multiservice Microfinance Institutions: AI only offers microfinance services.
- Portfolio reporting
 - Loan loss provision expense: expenses related to actual or anticipated loan losses are shown separately from other expenses in the income statement (“loan loss expense”).
 - The loan loss reserve is shown as a negative asset in the balance sheet. It is calculated each month according to the methodology described in the table.

Provisioning methodology

Provision	< 30 days 10%
	31 to 60 days 25%
	61 to 90 days 50%
	91 to 120 days 75%
	after 121 days 100%

Write-off Loans that are more than 180 days late are written off.

- Loans are written off when they are past due over 180 days upon decision by the Credit Committee.

- The following table reconciles these movements:

EUR	Sept. 2002	Sept. 2003	Dec. 2004	Dec. 2005
Loan loss reserve, January 1st	43,196	5,754	6,693	23,688
+ Loan loss provision expense	13,099	10,398	72,546	28,300
- Provision reversal	46,945	0	18,588	2,327
- Loans written off during the year	3,585	9,459	36,963	31,169
Loan loss reserve, year end	5,765	6,693	23,688	18,492

- Accrual vs. Cash accounting: Interest income and costs are calculated on an accrual basis. Calculation of interest for loans in arrears stops when the loan is written off.

5 Portfolio quality

- Indicators: Portfolio quality and the calculations of such are displayed in the tables in Section A and the calculations are based on standard portfolio at risk calculation of: (outstanding loan principal for loans in arrears over X days)/(total portfolio outstanding).

- Renegotiation of loans: the MFI does not refinance/reschedule loans

- Insider loans: the MFI does not allow employees to borrow funds.

6 Donations

- Revenue from donations is shown separately from income generated by operations in the income statement.

6.2 Current period donations:

Donor	Amount (EUR)
BPRM	226,455
CIDA Canada	1,235,201
SIDA Sweden	2,285,023
WV Canada	133,738
WV US	153,800
WV Australia	82,861

- Donations accounting methodology: are recorded in the income statement and income from donations are clearly identified in the balance sheet.

- In-kind donations: There were no in-kind donations identified.

6.5 Cumulative amount of all prior period donations: see table above. The total amount is over 4 MEUR.

7 Details of liabilities

7.1 Liabilities are listed in a table at the end of the report

7.2 Deposits: AI is not allowed to collect savings.

8 Other significant Accounting Policies

8.1 Accrual or deferral income/expense accounting: all expenses and revenues are accounted on an accrual basis, except for unexpected revenues.

8.2 Depreciation of fixed assets: The depreciation of fixed assets on a flat basis is done using the following table:

Type of assets	%
Vehicles	20%
Others	33.33%

8.3 Inflation accounting: none

8.4 Currency mismatch: please refer to the F area for more information on potential mismatch.

8.5 Accounting treatment of unrealized gains or losses due to foreign currency fluctuations: none.

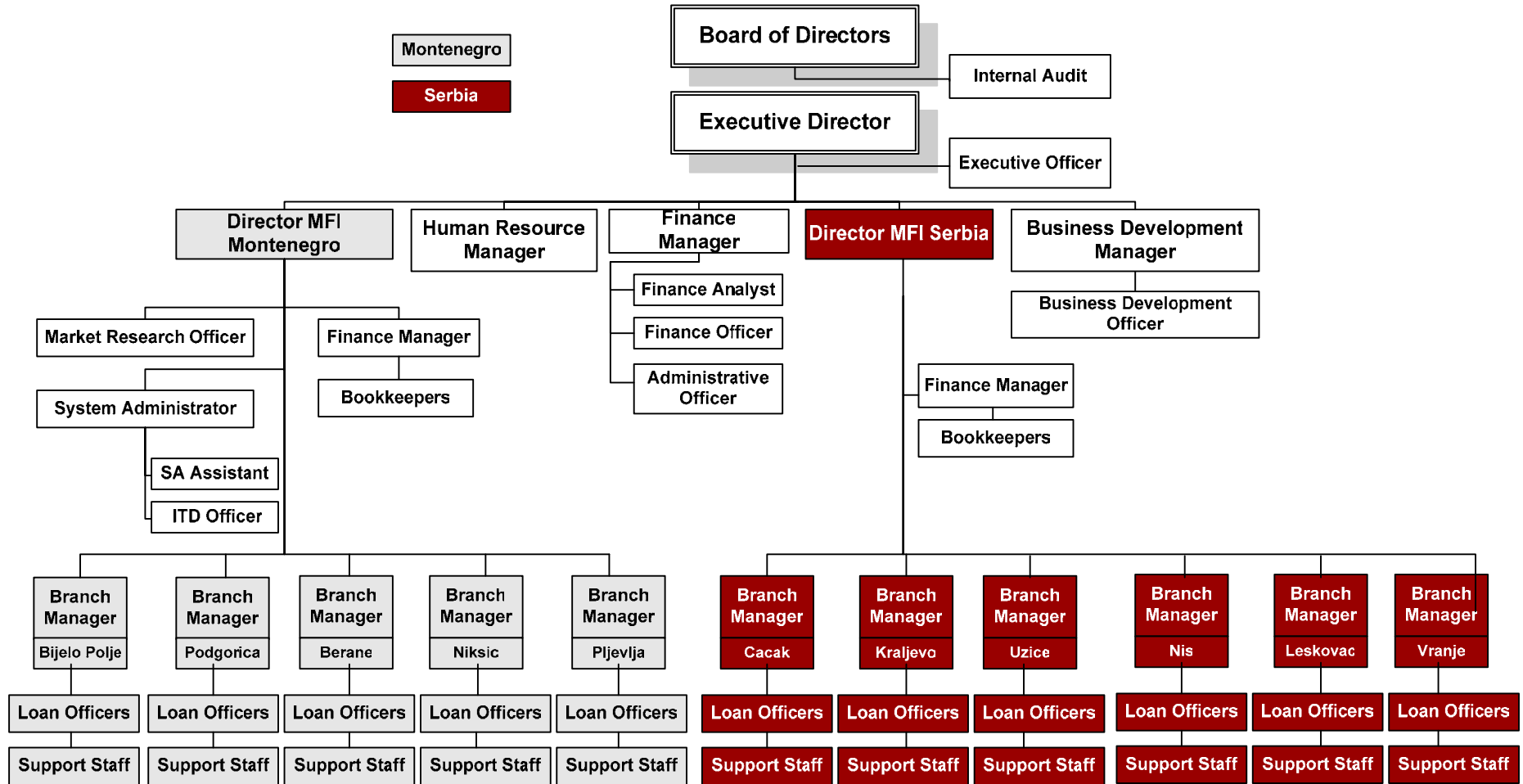
Adjustments

	Sep. 2002	Sep. 2003	Dec. 2004	Dec. 2005
Adjustment for the cost of funds = (a*b)-c	58,056	185,925	303,685	370,186
Average amount of borrowings (a)	442,287	1,682,101	3,014,179	4,328,424
Shadow price of borrowings (b)	15.0%	15.0%	12.0%	12.0%
Interest expense on borrowings (c)	8,287	66,390	148,442	149,225
Adjustment for inflation = (d-e)*f	880,627	753,858	939,917	1,011,056
Avg. Equity (d)	3,381,971	5,569,534	7,734,633	10,347,511
Average fixed assets (e)	120,389	184,836	215,295	236,950
Inflation rate (f)	27.0%	14.0%	10.0%	10.0%
Adjustment for in-kind donations	-	-	-	-
Staff and technical assistance	-	-	-	-
Other	-	-	-	-
Adjustments for provisions	-	-	-	-
Loan losses	-	-	-	-
Other risks	-	-	-	-
Other adjustments	-	-	-	-
Total adjustments	938,683	939,783	1,243,602	1,381,242

AgroInvest Balance sheet	EUR				Evolution		
	Sep. 2002	Sep. 2003	Dec. 2004	Dec. 2005	2003/2002	2004/2003	2005/2004
ASSETS	5,615,933	9,748,194	13,149,851	17,794,272	73.6%	34.9%	35.3%
Short Term Assets	5,461,634	9,532,821	12,934,049	17,535,004	74.5%	35.7%	35.6%
Cash and Due from Banks	667,389	1,157,588	1,555,875	1,974,516	73.5%	34.4%	26.9%
Short Term Investments	-	-	-	-	-	-	-
Short Term Net Loan Portfolio	4,768,269	8,355,218	11,334,092	15,498,294	75.2%	35.7%	36.7%
Short Term Gross Loan Portfolio	4,774,023	8,361,911	11,357,780	15,516,786	75.2%	35.8%	36.6%
(Loan Loss Reserve)	5,754	6,693	23,688	18,492	16.3%	253.9%	(21.9%)
Interest Receivable	-	-	-	-	-	-	-
On loan portfolio	-	-	-	-	-	-	-
On investments	-	-	-	-	-	-	-
Accounts receivable and other assets	-	20,015	44,082	62,194	(22.9%)	120.2%	41.1%
Long term assets	154,299	215,373	215,802	259,268	39.6%	0.2%	20.1%
Long Term Net Investments	-	-	585	585	-	-	0.0%
Long Term Gross Loan Portfolio	-	-	-	-	-	-	-
Net Fixed Assets	154,299	215,373	215,217	258,683	39.6%	(0.1%)	20.2%
Other Long Term Assets	-	-	-	-	-	-	-
LIABILITIES AND EQUITY	5,615,933	9,748,194	13,149,856	17,794,272	73.6%	34.9%	35.3%
Liabilities	961,032	3,264,027	4,164,757	6,084,349	239.6%	27.6%	46.1%
Short term liabilities	39,532	133,690	293,630	1,073,161	238.2%	119.6%	265.5%
Demand Deposits	-	-	330	2,739	-	-	730.0%
Compulsory Deposits	-	-	-	-	-	-	-
Short Term Time Deposits	-	-	-	-	-	-	-
Short Term Borrowings	-	87,161	-	834,800	-	(100.0%)	-
Interest payable	-	-	-	-	-	-	-
Accounts Payable and Other Short Term Liabilities	-	46,529	293,300	235,621	17.7%	530.4%	(19.7%)
Long term liabilities	921,500	3,130,337	3,871,127	5,011,188	239.7%	23.7%	29.5%
Long Term Time Deposits	-	-	-	-	-	-	-
Long Term Borrowings	676,838	2,600,203	3,340,993	4,481,055	284.2%	28.5%	34.1%
Other Long Term Liabilities	244,662	530,134	530,134	530,134	116.7%	(0.0%)	0.0%
Equity	4,654,901	6,484,167	8,985,098	11,709,924	39.3%	38.6%	30.3%
Paid-In Capital	-	-	-	2,873,000	-	-	-
Donated equity	4,008,126	4,956,407	5,722,077	4,117,077	23.7%	15.4%	(28.0%)
Retained earnings without donations and reserves	-	1,479,430	3,214,691	4,671,516	132.7%	117.3%	45.3%
Current year	294,658	1,031,276	394,702	1,298,391	250.0%	(61.7%)	229.0%
Other equity accounts	11,074	48,330	48,331	48,331	336.4%	0.0%	0.0%

AgroInvest Income Statement	Notes	EUR				Evolution		
		Sep. 2002	Sep. 2003	Dec. 2004	Dec. 2005	2003/2002	2004/2003	2005/2004
Financial Revenue (a)		1,054,399	2,230,089	4,450,641	4,295,258	111.5%	99.6%	(3.5%)
Financial Revenue from Loan Portfolio		1,000,116	2,181,963	4,342,389	4,267,157	118.2%	99.0%	(1.7%)
Interest on Loan Portfolio		844,104	1,903,401	3,858,285	3,741,064	125.5%	102.7%	(3.0%)
Fees and Commissions on Loan Portfolio		156,012	278,562	484,104	526,093	78.6%	73.8%	8.7%
Penalty Revenue on Loan Portfolio						-	-	-
Financial Revenue from Investments						-	-	-
Other Operating Revenue		54,283	48,126	108,252	28,101	(11.3%)	124.9%	(74.0%)
Financial Expense (b)		8,287	66,390	375,892	395,005	701.1%	466.2%	5.1%
Interest paid on borrowings		8,287	66,390	148,442	149,225	701.1%	123.6%	0.5%
Interest paid on deposits						-	-	-
Net Inflation Adjustment Expense								
Other Financial Expenses				227,450	245,780	-	-	8.1%
Financial income [c=a-b]		1,046,112	2,163,699	4,074,749	3,900,253	106.8%	88.3%	(4.3%)
Net Loan Loss provision expense (d)		(35,272)	8,028	41,968	19,747	(122.8%)	422.8%	(52.9%)
Loan loss provision expense and write-off		(33,846)	10,398	53,958	28,300	(130.7%)	418.9%	(47.6%)
Recovery from Loans written off		1,426	2,370		8,553	66.2%	(100.0%)	-
Operating expense (e)		786,726	1,535,696	2,386,836	2,397,098	95.2%	55.4%	0.4%
Personnel Expense (includes fringe)		483,189	910,931	1,130,465	1,220,800	88.5%	24.1%	8.0%
Administrative Expense (non-staff operating expenses)		303,537	624,765	1,256,371	1,176,298	105.8%	101.1%	(6.4%)
Depreciation and amortization		38,272	71,435	108,191	106,710	86.7%	51.5%	(1.4%)
Consulting fees		5,269	6,366	18,452	11,108	20.8%	189.9%	(39.8%)
Village Council			84,264	189,049		-	124.4%	(100.0%)
Communication expenses / Office supplies / Travel expenses		64,376	116,961	229,464	464,365	81.7%	96.2%	102.4%
Occupancy expenses		31,347	68,565	98,716	136,542	118.7%	44.0%	38.3%
Vehicles expenses		69,123	103,619	174,208		49.9%	68.1%	(100.0%)
Training expenses		47,550	76,360	138,028	335,896	60.6%	80.8%	143.4%
Advertising		12,317	14,821	19,206	22,615	20.3%	29.6%	17.7%
Bank fee / Audit fee		30,048	47,444	244,527	48,859	57.9%	415.4%	(80.0%)
Others		5,235	34,930	36,530	50,203	567.2%	4.6%	37.4%
Net Operating Income Before Taxes and Donations [f=c-d-e]		294,658	619,975	1,645,945	1,483,408	110.4%	165.5%	(9.9%)
Income Taxes (g)				219,967	185,017	-	-	(15.9%)
Net Operating Income Before Donations [h=f-g]		294,658	619,975	1,425,978	1,298,391	110.4%	130.0%	(8.9%)
Non Operating Revenue (i)						-	-	-
Non Operating Expense (including related taxes) (j)						-	-	-
Net Income Before Donations [k=h+i-j]		294,658	619,975	1,425,978	1,298,391	110.4%	130.0%	(8.9%)
Donations (l)		233,464	229,729	79,555	158,434	(1.6%)	(65.4%)	99.1%
Net Income (after Taxes and Donations) [m=k+l]		528,122	849,704	1,505,533	1,456,825	60.9%	77.2%	(3.2%)

Organizational chart



Financing sources

Loan Providers	Currency	Initial Amount	Capital outstanding on the last audited statements	Interest rate	Maturity date and repayment schedule (grace period, etc.)
KfW Germany	EUR	4,850,000	3,735,855	3.00%	2007, Balloon
		1,550,000			2008, Balloon
		400,000			2008, Balloon
		500,000			2009, Semi-An
		500,000			2010, Semi-An
		1,000,000			2010, Semi-An
KfW Austria	EUR	500,000	500,000	Euribor + 3.00%	2007, Balloon repayment
		900,000		3.00%	2007, Balloon repayment
Cordaid	EUR	600,000	330,000	6.00%	2007, Semi-annual, 2 years grace
Blue Orchard	EUR	750,000	750,000	Euribor + 6.25%	2008, Semi-annual, 20 month grace
Vision Fund	EUR	1,250,000	1,250,000	6.25%	2007, Balloon repayment

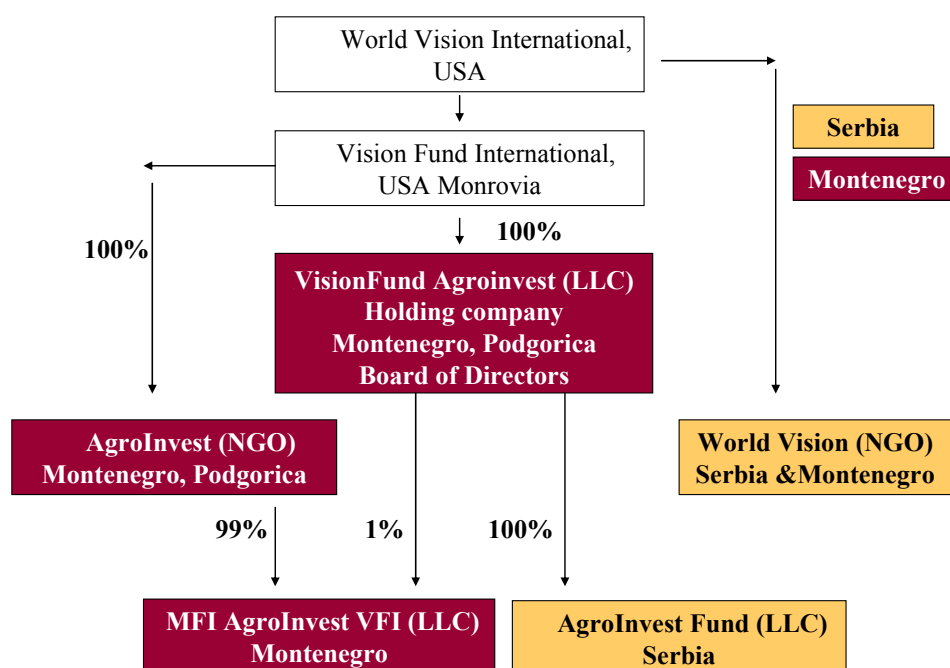
Board of Directors

Name	Position on Board	Education	Current position	Date of election
Max Buskens	Chairman	Corporate Law	Advisor	February 2005
Ros Piper	Member	Social development	Advisor	August 2001
Jadranka Zec	Member	Economist	Project manager	February 2005
Vasilije Boskovic	Member	Lawyer	Lawyer	March 2003
Vladimir Cizmanzki	Member	Priest	Advisor	March 2003

Products

Name of the product	Loan for business activities
Creation Date	1999
Client type	Rural
Authorized loan size (minimum and maximum)	250 – 5,000 EUR
Average disbursed loan size	1,476
Authorized loan length (minimum and maximum)	3 - 36 months
Average loan length	18
Grace period	0 – 6 months
Collateral requirements and other conditions	Guarantors
Repayment Schedule (ex. weekly, monthly)	Monthly
Nominal annualized interest rate	18.0% (average)
Effective Interest Rate	Serbia: 33.3% to 37.4% Montenegro 32.1% to 36.2%
Flat or declining?	Flat
Fees and penalties	2-2.5%
Major changes since creation (rate, size, term)	Changes made to loan size, interest rate and application fee. Benefit made for repeated clients (rates of 1.4% or 1.3% per month).

Legal structure



- **World Vision International** is a Christian humanitarian organization. Its HQ is in the USA.
- **Vision Fund International** was founded by World Vision International in 2004 as the holding company for all WVI micro finance institutions around the world. HQ is in the USA.
- **Vision Fund AgroInvest** was founded by Vision Fund International in 2004 as a holding company for all AI MFIs. HQ is in Montenegro, Podgorica. Transferring ownership over MNG MFI is in process.
- **AgroInvest NVO** founded by World Vision International (WV Montenegro) in 1999, legal form of local non government organization established in 2003. Licenced by central bank of Montenegro in 2003. HQ is in Montenegro (Podgorica). Transferring assets from AI NVO to MFI AI VFI is in process.
- **MFI AgroInvest VFI** was founded in 2005 from Vision Found International and AgroInvest NVO as LLC. Licensed by central bank of Montenegro in 2005. HQ is in Montenegro (Podgorica).
- **World Vision Serbia and Montenegro** was founded by World Vision International in 2001 as a non-resident humanitarian organization. HQ is in Serbia, Belgrade. Transferring capital from WVSCG to Serbia MFI in process.
- **AgroInvest Fund** was founded by Vision Fund AgroInvest in 2005 as a LLC with HQ in Nis, Serbia.

Name	Legal status	Territory	Role
AgroInvest NVO	NGO	Montenegro	Fundraising (donations)
MFI AgroInvest VFI	LLC	Montenegro	Lending entity MNG
AgroInvest Fund	LLC	Serbia	Lending entity SER
World Vision S&M	NGO	Serbia	Fundraising (donations)
Vision Fund AgroInvest	LLC	Montenegro	Holding