

## EKI, Bosnia and Herzegovina

In early 1996, EKI began as a project of World Vision International (WVI), based in Zenica, Bosnia and Herzegovina (BiH). In 2008; EKI became a Microcredit Foundation (MCF), and now awaits its license as a Microcredit Company (MCC). EKI's vision is to reduce the economic causes of poverty in BiH. Their mission is to provide financial services and technical support to those who have no access to banking services, focusing on businesses that create or maintain jobs in BiH. As of December 2008 EKI serves 53,033 active borrowers with a total loan portfolio of 204 million BAM (104 M EUR).

### Social Performance Rating

#### Rating

**In progress**



#### Date of the Rating

**February 2009**

#### Country Profile

Indicator	BiH	ECA
<b>Demography</b>		
Urban population	46%	63%
Life expectancy at birth	75	69
<b>Health</b>		
Access to safe water	99%	94%
Mortality rate (<5) per 1,000 births	15	26
<b>Education</b>		
Adult literacy rate	97%	99%
Primary school enrolment ratio (%)	91%	91%
<b>Gender</b>		
% of parliament seats held by women	14%	15%
<b>Poverty lines</b>		
National	18.6%	
<b>Gini index</b>		
	26	
<b>HDI</b>		
	0.803	0.808
Rank out of 177 countries	75	

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REF: OW/160409

#### Rating highlights

- EKI has taken assertive steps to implement Social Performance Management; its social vision and mission, emanating from World Vision, are shared by all main stakeholders.
- Based on a thorough background study EKI has developed a core social objective to reach 40% low income households and has set additional social objectives. EKI could however better harmonize its social mission and different social objectives.
- EKI has developed indicators to monitor its social objectives that are integrated in the MIS and easily tracked by all staff. The relevance and reliability of these indicators requires further strengthening.
- There is high awareness and good commitment of staff to the social objectives as a result of the strong organizational culture and adapted HR processes.
- EKI serves a large percentage of its target clientele with a 7.5% overall penetration rate and a 9.8% penetration rate of households below the national poverty line. This is the result of a geographic targeting approach based on a nation wide survey.
- Given regulatory constraints services are limited to credit only. A wide range of credit products is offered that are attractively designed and packaged for clients.
- There is a clear focus on reducing interest rates to clients through increased operating efficiencies and EKI is among the most affordable MFIs in BiH.
- Client protection is well ensured with transparent loan conditions, (mandatory) disclosure of effective interest rates and systems in place to ensure fair treatment of clients.
- Fair treatment of staff is well ensured due to standardized performance evaluation and promotion, good capacity building and equal representation of women.

#### Social Performance Indicators

'000 EUR	Dec. 2003	Dec. 2004	Dec. 2005	Dec. 2006	Dec. 2007	Dec. 2008
<b>Social Performance Indicators</b>						
% of women borrowers	35.4%	35.6%	36.8%	39.4%	41.1%	42.0%
% of rural borrowers	n/a	n/a	n/a	62.8%	63.4%	63.7%
% group loan borrowers	n/a	0.8%	0.9%	1.2%	0.7%	0.0%
Retention rate	53.1%	50.6%	48.4%	57.7%	70.2%	67.1%
PAR 31-365	0.3%	0.4%	0.3%	0.3%	0.4%	1.7%
Portfolio Yield	23.1%	22.6%	21.0%	23.6%	21.6%	19.6%
Number of training days per staff	2.0	6.1	5.3	2.5	2.1	1.5
<b>Institutional Performance Indicators</b>						
Loan portfolio	15,239	19,368	26,610	44,227	79,781	104,187
Active borrowers	13,305	18,789	22,559	28,019	41,215	53,033
Staff	102	119	153	211	281	320

Refer to the GIRAFE rating for an analysis of the institutional performance indicators

## Microfinance sector

The microfinance sector in Bosnia and Herzegovina (BiH) was launched in 1996 with support from the World Bank (WB) and international NGOs. The largest MFIs, having adopted most industry best practices, are among the strongest MFIs in Eastern Europe, totaling 1.1 billion BAM (555 M EUR) of portfolio and 392,703 active clients as of December 2008, not including commercial banks (the biggest share being attributed to ProCredit with 163 M EUR and 68,752 loans as of December 2007).

MFI As of Dec. 2008	MFI Type	Portfolio in M EUR	%	Active loans	%
Mikrofin	MCC	116.3	21.0%	58,774	15.0%
<b>EKI</b>	<b>MCF</b>	<b>104.0</b>	<b>18.7%</b>	<b>57,318</b>	<b>14.6%</b>
Partner	MCF	93.2	16.8%	65,866	16.8%
LOK	MCF	67.6	12.2%	44,713	11.4%
Sunrise	MCF	48.5	8.7%	30,702	7.8%
Mi-Bospo	MCF	37.7	6.8%	36,248	9.2%
Prizma	MCF	37.4	6.7%	61,602	15.7%
Sinergija	MCC	26.5	4.8%	10,200	2.6%
Mikra	MCF	11.0	2.0%	13,320	3.4%
Žene za žene	MCF	8.5	1.5%	10,817	2.8%
Mikro Aldi	MCF	3.7	0.7%	3,143	0.8%
<b>Total</b>		<b>554.6</b>	<b>100%</b>	<b>392,703</b>	<b>100%</b>

According to the new microfinance law, adopted by both BiH entities' parliaments (June 2006 for Republika Srpska - RS- and October 2006 for the Federation of BiH -FBH-), MCOs have to transform into either Microfinance Foundations (MCF) or Microfinance Companies (MCC). RS-based MFIs are licensed and supervised by the Banking Agency of RS while FBH-based MFIs are licensed and supervised by the Banking Agency of FBH. Most FBH-based MCOs have received their license to operate as MCFs and most are registered as such.

Relevant bylaws have been issued in both entities, defining the minimum requirements for MCFs or MCCs, the scope of supervision, the reporting requirements, the way of forming reserves for the coverage of loan losses and the way to calculate the effective interest rate of loans, which MFIs are now required to disclose on the client's contract. Regulation does not include prudential norms given the absence of deposit taking risks. To date the supervisory capacity of the Banking Agencies remains limited and supervisory visits are still to commence in full.

MCFs and MCCs can essentially only provide credit as they are not allowed to offer other financial services. Both MCFs and MCCs are non-deposit taking, an activity reserved to banks. Some MFIs have investigated the possibility to offer insurance products to their clients (as a sales agent for an insurance company) but as of now this has remained limited in BiH.

The main difference in the offering of credit services between an MCF and MCC is that the maximum loan size is limited to 10,000 BAM or 5,000 EUR for an MCF and 50,000 BAM or 25,000 EUR for an MCC. As those wanting to transform into an MCC also have to temporarily operate as MCFs, they will need to reduce their maximum loan size down to 10,000 BAM while waiting for the MCC license.

The majority of MFIs offers individual loan products for different terms and loan sizes up to the maximum allowed loan size by law. Variations exist in terms of grace periods, repayment frequency and collateral requirements. Essentially, the majority of MFIs offer a similar range of loan products with the main competitive advantage relying on marketing and packaging of products and customer service.

### A changed environment

In recent years MFIs in Bosnia have shown strong growth rates with the vast majority achieving annual growth rates between 50-100% and some even above 100%. Given this strong emphasis on growth, and with the microfinance market reaching saturation, this has led to a situation of strong cross-indebtedness – it is estimated that 30 to 40% of the MFI clientele has at least two loans. Even if quite a number of MFIs made prudent use of the National Credit Register (CRK) to avoid over-indebtedness, other MFIs, mostly those with the aim to increase their market shares, continued to provide loans without a thorough check on the indebtedness of their clients. Some MFIs only started providing data to the CRK in 2009. Furthermore, many MFIs made a strong push to disburse loans over 10,000 BAM prior to their transformation into an MCF to avoid losing market share. These factors combined have led to a situation of over-indebtedness of many MFI clients.

The global financial crisis has had a twofold impact on this situation. On the one hand MSMEs were no longer able to borrow ever larger loan amounts to repay current debt given reduced liquidity in the financial sector in BiH. On the other hand it caused an economic slowdown in Bosnia as well as a reduction in inflow of remittances, which created increased difficulties for many of the MSMEs to meet their debt obligations. This has resulted in increasing levels of credit risk within the microfinance industry. The industry average PAR 30 has increased from 1.0% as of December 2007 to 2.5% as of December 2008. This upward trend is likely to continue in the coming year, especially as the government has been late in paying salaries and pensions in 2009. However, it should be noted that the majority of the MFIs are taking considerable steps to mitigate this situation as well as exploring joint initiatives.

## Socio-economic Environment

For the last four years, BiH has achieved strong annual GDP growth, in line with the MDG of 5.5%. Exports have surpassed the rest of the region, growing over 15% each year for the last two years. This year, BiH joined the more developed countries above 0.800 on the Human Development Index with a score of 0.803. Yet despite these postwar recovery efforts, the country still suffers from widespread poverty with 18.6% of the population living below the national poverty line of 238 BAM/month (122 EUR) in 2007. This is a slight increase as compared to 18.1% in 2004. Between regions, 17.3% of the Federation of BiH, 20.2% of the RS and 25.0% in Brcko live below the poverty line in 2007. There are succinct differences in poverty trends between regions as in 2004 these figures were 18.3%, 18.3% and 7.8% respectively.

Furthermore, there is a distinct difference between rural/semi-urban and urban regions with only 10.8% of the population below the poverty line in urban areas as compared to 23.7% in rural and semi-urban areas. Out of all these groups, it is households with children that run the highest risk of falling below the poverty line. Families with more than two children are the poorest of the BiH population.

The Extreme Social Exclusion Index counted more than a fifth of the BiH population without any monetary income, telephone access, health insurance, or primary education. Nearly 25% of the FBiH population lacked at least one of the above categories, compared to 20% in RS. Although RS has a larger proportion of poor people, it appears they are not as “extremely excluded” as in FBiH. In both areas, the Roma remain some of the most excluded from society. Only 3% of Roma hold permanent jobs and two-thirds have never attended primary school.

One of the leading causes of poverty and social exclusion in BiH is the exclusive labor market. In 2006, the Labor Force Survey acknowledged an aggregate unemployment rate of 30%. Even more telling is that nearly 57% of the able-bodied population has opted out of the workforce, neither employed nor actively seeking work. Among the unemployed, more than 75% have been searching for work longer than two years. Those that are employed in the localized labor market suffer from job and wage insecurity, with 47% having no opportunities for self-improvement and at risk of remaining socially excluded. The informal economy is a major reason for such extreme labor statistics, with 43% of total employment in 2004 coming from this side economy. Monthly earnings are up to 30% lower and job instability is much higher in the informal sector. Over 65% of the population that climbed out of poverty from

2000-2004 either moved into or remained in the formal sector. Enabling informal sector employees to start their own formal micro-enterprises will increase their income, job stability and contribution to the general health of the BiH economy.

The Gender Equality Act was adopted in 2003, but inequalities are still very present. This is captured in the Gender Development Index (2004), where BiH, FBiH and RS received 0.801, 0.806, and 0.779 respectively. This index combines economic and educational inequality indicators. Although more than half of the population is female, women in BiH have one of the lowest workforce participation rates in South-Eastern Europe at 40%. Women are also half as likely to gain employment as their male counterparts, and only earn 75% the salary of their male colleagues. Postwar government representation is also lower than before. Female parliamentary representation is 16%, with the MDG hoping to raise it to 25%. The state-level Gender Agency has been established to improve gender equality by implementing the new laws, with regional authorities in both FBiH and RS.

Overall educational achievements still lag the MDGs, with adult literacy at 96% (MDG is 99%) and primary school enrollment 1.2% lower than the MDG of 100%. Female rates lag behind, with twice as many women without any education as men. This explains the lower female wage ratio, as income for employees without a diploma is half that of those who have graduated. As of 2003, there was still no Ministry of Education. The BiH government organized the school system with the help of international agencies and the Ministry of Civil Affairs. Educational levels have a distinct impact on poverty with a poverty incidence of 38.6% for people without formal education, reducing to 26.5% for those having completed elementary school and 12.5% for those having finished secondary school.

Only 80% of the population is covered with adequate healthcare, despite claims of universal coverage. The under 5 mortality rate of 9.3/1000 is still higher than the MDG of 7, although the life expectancy MDG has been met at 74. Access to sanitary water is not a large problem in BiH, ranking first on the BDI-1 scale (99%).

The protection of the environment has not been a priority of the BiH government, but will be taking more of their attention as they strive to meet the EU agenda. Municipal and industrial waste is discharged directly into rivers, and only 50% of urban and 10% of rural areas have sewage connections. Poor air quality is also an environmental problem in BiH, with Tuzla having the worst carbon emissions in the region. Toxic air levels are sometimes as much as three times worse than the maximum allowed.

Currently 52% of the country has forest cover, with an MDG of reaching 60%.

**Sources:** UNDP (2003), Human Development Report: Millennium Development Goals in B&H; UNDP (2006), The Human Development Index – going beyond income; EBRD (2007), “Beyond Transition” by Peter Sanfrey and Gorana Krstić.

## Evolution of Socio-Economic Indicators

Social Economic Indicators	BiH	MDG	ECA
HDI	0.803		0.808
Rank out of 177 countries	75		-
<b>Demography</b>			
Total population (millions)	3.9		461
Urban population (% pop.)	46%		63%
Total fertility rate (birth per women)	1.2	1.7	1.5
Life expectancy at birth	75	74	69
<b>Health &amp; Nutrition</b>			
Mortality rate (<5) per 1,000 births	15	7	26
Underweight of children < 5 (%)	20		
Population undernourished (% pop.)	9%	0%	6%
Access to safe water (% pop.)	99%		94%
<b>Education</b>			
Adult literacy rate (% of people ages 15 and above)		99%	99%
Primary school enrolment ratio (%)	91%	100%	91%
<b>Gender</b>			
Women literacy rate	95%		
% of parliament seats held by women	14%	25%	15%
<b>Poverty and inequality</b>			
Below 1\$ a day	< 2%		< 2%
Below national poverty line	18.6%		
GNI per capita (current USD)	2,980		
Gini index	26		
<b>Environment</b>			
Forest area (% of land area)	43%	60%	38%
<b>Economy</b>			
Economic growth	6.8%		
Foreign debt (% GDP)	13%		
Internet users (%)	24%	15%	19%
Inflation (%)	10%		
Unemployment	29%	12%	
Agriculture (% GDP)	10		
Service (% GDP)	64		

**Sources:** UNDP (2007-08), World Bank (2007), PRSP (2007). Most data as of 2005, 2006 or 2007. MDG: Millennium Development Goals for 2015.

## Institutional Presentation

### Social Mission

EKI has established its core social vision and mission in formalized statements. Its **vision** is to “reduce economic causes of poverty in Bosnia and Herzegovina” and

acknowledges that two of the main transitional problems in BiH are high unemployment and widespread poverty. This vision is put in practice through their **mission**, which is to provide financial services and technical support to those who have no access to banking services and to businesses that create new or maintain the existing jobs in the entire Bosnia and Herzegovina where needed and where possible. In 2006 EKI reviewed their vision and mission, and set its core social objective<sup>1</sup>: EKI will sustain 100% financial self sufficiency and have at least 40% of its clients from low income households with the aim to achieve significant improvements for 5% of clients in that very group. EKI defines low-income households as those with a monthly income of less than 270 KM (138 EUR) per household member.

EKI defines itself as a non-profit organization that listens to its clients, makes flexible decisions and takes acceptable risks. It values their decentralized organization consisting of motivated, committed, and professional staff and board members.

### Characteristics of Outreach

No nationally or internationally benchmarked data is available on the poverty or level of financial exclusion of EKI’s clientele. The best possible approximation to provide an overview of the level of poverty of EKI’s clientele is the level of income per household member. The number of clients with an income level (as measured by EKI) below the national poverty line<sup>2</sup> has seen in increase between 2006 and 2007 from 31.3% to 38.2%, before slightly declining in 2008 to 35.9%. The table below provides a more detailed overview per branch of the percentage of clients below the national poverty line, percentage of clients with less than 270 KM in income per household member per month, percentage of rural and percentage of female clients as of December 2008.

Branch	< 258 KM	< 270 KM	% rural	% women
Banja Luka	33.3%	31.0%	62.6%	37.2%
Bihać	40.5%	50.7%	54.4%	45.6%
Bijeljina	38.5%	46.6%	72.5%	39.7%
Brčko	34.7%	37.9%	53.2%	37.7%
Bugojno	39.4%	49.5%	60.1%	35.5%
Doboj	40.8%	51.8%	72.2%	35.6%
Gradačac	31.8%	30.9%	84.4%	37.9%
Mostar	36.1%	39.2%	49.3%	40.7%
Sarajevo	35.3%	45.3%	55.2%	47.2%
Tuzla	34.3%	37.1%	70.0%	49.6%
Visegrad	32.8%	39.0%	50.9%	42.8%
Zenica	35.0%	40.6%	53.8%	43.6%
Živinice	36.8%	41.4%	76.8%	50.1%
Zvornik	34.4%	43.8%	72.1%	44.9%
EKI total	35.9%	41.4%	63.7%	42.0%

<sup>1</sup> EKI internally uses the term ‘end-statement’.

<sup>2</sup> The poverty line for 2008 has been adjusted from the 2007 survey by the Consumer Price Index and is 258 KM in 2008.

EKI also tracks the number of children benefiting indirectly from its services, which in 2008 were 30,612 children. Furthermore, EKI reports that as of December 2008 14% of their loans were for disabled persons, refugees, displaced persons and returnees.

### Client change

To measure improvements in the lives of clients EKI has conducted a baseline survey in early 2007 among 900 clients from low income households (below 270 KM) with a follow-up study in January 2008. The survey showed a result that at least 23% have increased their income levels beyond 270 KM per month. Most notably, this increase originates from clients with an income above 180 KM. The percentage of clients with an income below 180 KM remained more or less stable between the base-line and follow-up survey.

### Market penetration

As one of the top microcredit organizations in BiH, EKI has 14 branch offices and 58 sub-branches. Half of the branch offices are located in the Federation of BiH, while there are six in RS and one in Brčko. EKI has identified a total target clientele of households and SMEs of 714,000 throughout all of BiH. As of December 2008 EKI has a market penetration of 7.43%. The table below shows the penetration rate per branch.

Branch	# households	# registered businesses	# active borrowers	Penetration rate
Banja Luka	98,905	11,110	4,114	3.7%
Bihać	48,421	4,503	2,630	5.0%
Bijeljina	26,791	2,758	4,530	15.3%
Brčko	22,002	4,238	3,225	12.3%
Bugojno	32,491	4,624	2,677	7.2%
Doboj	51,770	4,784	4,920	8.7%
Gradačac	27,296	2,634	4,227	14.1%
Mostar	65,070	8,132	4,382	6.0%
Sarajevo	61,111	10,810	4,497	6.3%
Tuzla	50,319	4,796	5,771	10.5%
Visegrad	26,110	2,457	2,323	8.1%
Zenica	64,076	7,465	5,215	7.3%
Živinice	42,006	928	2,473	5.8%
Zvornik	28,771	1,960	2,049	6.7%
EKI total	645,139	71,199	53,033	7.4%

### Products and services

EKI's product offering includes five categories of loans. In December 2008, there were over 57,318 active loans with an outstanding loan portfolio of 204 M BAM (104 M EUR). The compounded effective interest rate for the total portfolio is estimated at 19.7%.

- Microloans are designed for small registered and non-registered businesses and amounts to 36% of the total outstanding loan portfolio. Loan amounts range from 300-5,000 KM – with an average of 2,300 KM and with a period of 1-36 months. The average effective interest rate for this product is around 20%.
- Agricultural loans for registered and unregistered businesses amount to nearly 29% of the total outstanding loan portfolio. Loan amounts range from KM 5,001-10,000 – with an average of 9,400 KM in 2008 and with a period of 1 – 60 months. The average effective interest rate for this product is 18%.
- SME loans for registered businesses to purchase working capital or fixed assets. They amount to 15% of the total outstanding loan portfolio. Loan amounts and period are the same as SME loans, with an average loan size of 12,300 KM in 2008. The average effective interest rate for this product is 19%.
- Housing reconstruction loans and loans for households account for 15% and 5% of the total outstanding loan portfolio. Housing loans range from 1,000-10,000 KM and have an average size of 6,700 KM, while household loans have an average of 1,800 and must be below 5,000 KM. Housing reconstruction loans are for 36 months if they are below 5,000 and up to 60 months otherwise. Household loans are for a period of 1-36 months. Both of these loans have received portfolio restrictions for 2009. Housing loans should not exceed 15% of the portfolio and household loans should not exceed 5%. The effective interest rates are 19% and 25%, respectively.



- Short-term loans are designed for clients who need an additional (second) loan. Clients are eligible for this product if they are in the higher cycles of crediting and have no history of delinquency. They account for less than 1% of the portfolio. Loan amounts range from 300-3,000 KM for a period of 6 months and have an average of around 700 KM. The effective interest rate is 32%

EKI discontinued disbursements of its revolving loan product in 2008, although there were still 126,000 BAM outstanding at the end of 2008. Considering the difficult economic circumstances, EKI does reschedule loans for clients with solid credit histories. Rescheduling takes place on an individual basis and must be approved by OMs.

There are no product launches planned for 2009, given the economic climate and decreased client demand. There are some test projects underway with the EBRD, to examine whether very poor families in the region would benefit from access to credit.

## Social Performance Rating

### ▪ Institutionalization of the mission

#### Social mission and strategy

EKI has a clear intent to achieve social impact which emanates from the vision and mission. During a review in 2006 EKI decided to not change the mission but to formulate a core social objective. However, the mission statement could become more specific to indicate the specific target group with which EKI aims to work (low-income households) as it currently only mentions people excluded from banking services.

The core social objective itself is based on extensive research of the socio-economic environment in BiH as well as a thorough market research to identify the potential target market for EKI. There have been no revisions or updates to the objective, which could mean a loss of meaning as the poverty line is subject to change as a result of inflation. For example the poverty line has increased from 185 BAM in 2004 to 258 BAM in 2008.

Besides the core social objective EKI has also set other internal goals, including i) to have at least 10% of clients from disadvantaged groups (disabled, displaced, returnees, etc.), ii) to ensure that at least 8,000 jobs are created and/or sustained, iii) to have at least 40% female clients.<sup>3</sup> EKI

<sup>3</sup> The first two originate from the covenants in the loan from Vision Fund and the third objective is taken up in the incentive system for LOs.

could benefit from streamlining the status of the different social objectives to ensure that their relative importance in achieving the different objectives is clear to all staff.

EKI's vision and mission is well shared by its main stakeholders. Even if the social focus mostly emanates from WVI they are well shared by the local BOD members. Both the BOD and management are strongly committed to achieve the social objectives. The BOD of EKI MCF has sufficient capabilities to monitor the social objectives as it contains members with strong local and community development experience. There is limited risk of mission-drift in the short term as the ownership is not expected to be opened up beyond WVI before the end of 2010. A good transition is planned for the new BOD members of EKI MCC which already join current BOD meetings in preparation of their new function. The three selected members all have a strong financial background, but a limited background in development. The related risk of mission-drift is mitigated by the continued supervision of the EKI MCC BOD by the EKI MCF BOD.

The social objectives are well integrated in the decision making processes of EKI. The BOD receives an overview of the achievement of the core social objective for every meeting as well as for the other social objectives set by WVI. Furthermore, management monitors progress on a monthly basis. The vision, mission and social objectives are clearly communicated to staff and they are aware of the objectives to be achieved as well as the rationale behind the objectives. To date the Social Performance Management has been championed by the Marketing Department which has been responsible for conducting the initial research, and continues to research client satisfaction, client retention and impact studies.

The social mission is integrated in the strategy and planning process although there are areas for improvement. The research leading up to the formulation of the core social objective has greatly influenced the geographical targeting within the country. However, the business plan does not actively focus on the implementation of the social objectives, nor does it analyze challenges and/or constraints for the implementation. Furthermore, EKI could benefit from a stronger financial analysis on the costs and benefits of its social mission and objectives to better understand the influence of its social mission on its financial bottom line.

#### Social performance monitoring

EKI has established a good performance monitoring systems for its social objectives, although indicators used require further refinement and the quality of surveys can be enhanced.

Social indicators relevant to the core social objective and additional social objectives have been defined. However, EKI does not monitor to which extent its clients do not have access to banking services as mentioned in its mission statement. The indicators are all integrated in MIS and readily available to employees via the intranet. Knowledge of these indicators is widespread among employees, although monitoring of the indicators at branch level could be improved beyond the incentive system. Institutional targets and results are regularly presented and discussed amongst management and Board and include monitoring of the following indicators on a monthly basis:

- % of clients in low-income households, % of women clients, % of rural clients, and number of jobs created and sustained.

The client-level indicators could be further refined:

- The income level per household member is directly taken from the income level of the loan application divided by the household members. International best practice uses consumption levels to determine poverty levels as income levels might be understated.<sup>4</sup>
- There is no specific definition of what is rural and urban, nor for how to measure if a job is created and/or sustained. This is left to the interpretation of the LO.

In addition to these standard indicators, there is a monthly monitoring of client retention and exit interviews are conducted by the LOs to determine reasons for drop-out. Furthermore, EKI also monitors client satisfaction of new clients one month after the loan is disbursed, which is also reported on through monthly reports. The monthly reports are monitored by the management team and the statistics on client satisfaction and drop-outs are made available to staff through the intranet. Additionally, EKI also carries out client satisfaction surveys for specific loan products. In 2008 this was done for the Micro and Agro loan products.

To measure improvements in the lives of clients EKI has conducted a baseline survey in early 2007 among 900 clients from low income households with a follow-up study in January 2008<sup>5</sup>. The survey was supported by focus group discussions. The accuracy of the survey could be improved as it was conducted by the LO responsible for the client and it cannot be seen as an impact measurement as no control group was used. EKI can explore further possibilities to use existing data in the MIS for more structural tracking of changes in the lives of clients.

There is basic control on the social performance indicators by the Internal Audit department through their audits of the

<sup>4</sup> Income could either be not identified (e.g. home grown food) or not revealed (e.g. income from remittances, illegal activities, etc.)

<sup>5</sup> A new baseline study was conducted in January 2009.

branches and marketing department. This control is mostly focused on the establishment of the income level, which is also checked by the credit committee as it is part of the standard loan appraisal. There are limited other controls on other indicators such as number of jobs created and/or sustained.

### **Staff mobilization**

Staff commitment to the social mission and objectives is well ensured through EKI's HR systems and internal communication.

During recruitment EKI does not screen for prior social involvement or familiarity with the EKI mission. However, the orientation training reviews the values and missions of EKI and elaborates on the client outreach targets. As the percentage of low-income households within the EKI client base has been on a declining trend (c.f. Characteristics of Outreach), it will likely become necessary for EKI to provide more formalized training on skills to enhance targeted outreach to underrepresented social groups.

The key social objectives have been included in the incentive system. LOs are very familiar with these goals and how to monitor their own results on the intranet platform. The social objectives and social responsibility to clients are however not formally included in the semi-annual evaluation of staff. In general, there is an uneven performance per LO and branch, and the present incentive level may not be sufficient motivation to push staff that continually are below the target. Partially this can be attributed to the fact that as the objectives are all achieved on average for EKI there is limited focus by management to review individual branch and/or LO performance.

During the formulation of the core social objective there was very limited formal staff input. However, the staff is overall very supportive of the social mission of EKI. This is supported by clear communication of the vision and mission of EKI, which is clearly posted in all branches, as well as social outreach targets.

### **Targeting and service offering**

#### **Breadth of outreach**

EKI serves a significant portion of its target clientele. With a nation wide presence it currently has a 7.43% penetration rate based on an estimated total number of 714,000 potential clients. Looking more specifically at poor households EKI has a penetration rate of 9.8% based on the fact that it serves 19,407 clients in households that are

below the national poverty line out of a total of 193,692 households below the national poverty line in BiH.<sup>6</sup>

These penetration rates should be seen in the light of a nearly saturated market. All MFIs in BiH combined serve a total of 392,703 clients as of December 2008. Off-setting for cross-lending between MFIs, this results in an overall estimated market penetration in BiH of 40%. Further growth is expected to be limited as the market is more or less saturated, with few remaining growth areas in rural areas and lower income households.

### Client targeting

EKI has clearly identified its target clientele based on a nation wide survey conducted in 2006. A focus was chosen for low income households as formulated in the core social objective. After this initial definition there has not been an update to the definition of the target groups. The targeting approach to reach these goals has been mostly through a geographic targeting through opening of branches and sub-branches in underserved areas, as well as through setting targets for specific products. As there is limited data available on the economic profile of the population in specific regions the targeting is supported by market surveys conducted prior to opening a sub-branch.

Specific individual targeting by LOs has remained limited to date. Even if social objectives are integrated in the incentive system for LOs, the amount of the monthly bonus represented by this part does not seem sufficient to increase motivation fro LOs to meet their social objectives. Especially in the current context, giving rising levels of client delinquency and low demand, LOs are more concerned with finding clients with good repayment potential. The social indicators of each client are discussed during the credit committee, but as EKI has not been in a position that it had to choose between clients this is not actively used to prioritize clients from preferred social groups.

EKI regularly monitors the achievement of its social objectives (c.f. Social Performance Monitoring) and based on this EKI can take corrective action if needed. However, to date the targets set have been more or less automatically met on average by EKI, even if differences exist between branches and between LOs (c.f. Characteristics of Outreach). Therefore, to date no corrective action has been needed and there has been no need to enhance targeting methods. This could change in the near future as EKI has seen a decrease in the percentage of low-income households from over 50% at FYE07 to 41.4% as at FYE08, which is just above its target of 40%. This

reduction can mostly be contributed to the increase of the national poverty line, although the percentage of clients below the poverty line also slightly reduced from 38.2% at FYE07 to 35.9% at FYE08.

### Service Design and Client Satisfaction

EKI has a broad product range that matches the needs of low income households and small businesses in BiH. Products are evaluated through market research, analysis of loan performance from the MIS system and feedback from employees, and show an understanding of client needs.

EKI's core products are its Microloans, Agroloans and SME loans. These loans cover the full range from 300 to 10,000 BAM, with different terms, collateral requirements and grace periods. They are repackaged into various concepts to become more attractive to customers. In addition housing loans have been added for home-improvement purposes and household loans for consumption purposes. Short-term loans exist for emergency funding needs. Transforming into an MCC, EKI will soon be able to offer loans up to 50,000 BAM. To date EKI has not yet diversified its financial services beyond credit as it is restricted by local law, but is exploring opportunities to engage in partnerships with banks or becoming a bank in the medium term.

Client satisfaction surveys are carried out for specific products by the marketing department – for Micro and Agro loan in 2008 – to better understand client needs and potentially adapt or modify products and procedures. No new products are currently planned for 2009, although EKI does participate in a study with EBRD to determine the potential and impact for loans for very low income households.

Client satisfaction is well monitored by the marketing department. Calls are made to 10% of new client within a month of loan disbursement. Exit surveys are conducted by LOs for every departing client 60 days after the loan was repaid. On average, clients score EKI with a 9.5 one month after disbursement, and with 8.7 when they leave (on a scale of 1 to 10). The exit interviews show that the main reasons for exiting are that clients are not in need of a loan 56% or have a loan in another MFI 20%. Clients appreciate the fast service by EKI 42% and client friendliness 26%. The two main factors that they do not like are high interest rates 47% and the guarantees 15%. The customer satisfaction surveys on the Micro and Agro loan products had similar findings.

In terms of retention EKI has a moderate retention rate. For those clients who have the opportunity to choose whether to renew a loan or not only 48% chooses to renew the loan

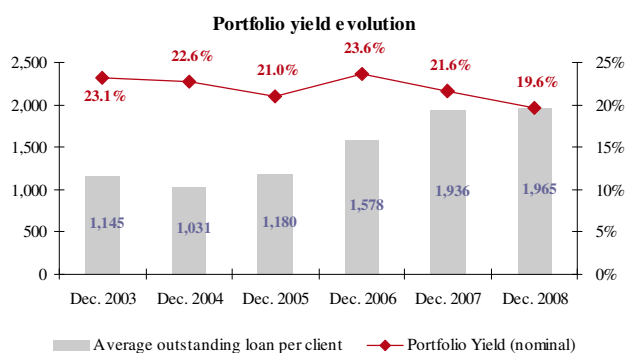
<sup>6</sup> The BiH Household Budget Survey 2007.

within the same year; however, this percentage goes up to 67% if the period for rejoining is extended to 2 years. This latter ratio is also confirmed by the CGAP retention formula looking at rejoining borrowers as a percentage of clients who repaid their loan.<sup>7</sup>

### Cost of the Services

With a portfolio yield dropping below 20% in 2008, EKI has one of the lowest effective interest rates among the MFIs in BiH, being one of only three MFIs with a portfolio yield below 20%. The EIR per product ranges from 18.5% to 23.5% for the majority of the portfolio, consisting of Agro, Micro, SME, and Housing loans. The EIR for household and short-term loans is higher, with household loans costing 25.1% and short-term at 31.5%, although they only represent 4.8% and 0.2% of the loan portfolio respectively.

There has been a downward trend in the portfolio yield over the years. There has been a strong focus by EKI to become more efficient, and the operating expense ratio reduced from 12.7% in 2005 to a low 7.7% in 2008. Even with increasing financial costs, this has made it possible for EKI to reduce interest rates over the years. Additionally, in 2008 EKI also consciously decided to lower its ROA from a previous level of around 7% to around 4% to be able to further reduce its interest rates. For 2009, interest rates have been increased slightly to remain at the same level of profitability (ROA of 3-4%). Even with this increase EKI will remain with one of the lowest interest rates in the sector.



Transaction costs are relatively low for clients, although as a result of the choice for EKI to reduce operational risk and not handle cash; clients do have to go to a commercial bank for loan disbursement and repayments. EKI is conscious of this and does make a concerted effort to work with banks that charge no or a low deposit fees. EKI is efficient in its speed of disbursement of loans and this is positively viewed by clients. Similarly, EKI has flexible rules in place for

<sup>7</sup> See the back page of this report for a definition of the retention rate formulas.

collateral and adjusts this to the access to collateral of each client (assets, guarantors).

## Social responsibility

### Client protection

The institution is transparent in its communication with clients. Loan conditions are clearly explained to clients who receive a copy of the loan contract and a clear repayment schedule. The new law in BiH has also contributed to transparency as the effective interest rate is now clearly communicated on as mandatory under the law.

EKI has good systems in place to ensure clients are treated well with respect and dignity. Being part of WVI it has adopted its code of conduct for staff which includes fair treatment of clients and abstinence from improper behavior. Furthermore, a formal client complaint system is in place to monitor the treatment of clients by LOs since mid 2008. The phone number that clients can call – answered by the Internal Audit department – is posted clearly in all branches. EKI has significantly reduced the use of intermediaries used for the housing loan in some communities. Part of the reason<sup>8</sup> was that EKI felt it could not sufficiently guarantee the fair treatment of clients.

Risks related to the offering of its financial services are covered relatively well. The risk of over indebtedness is well dealt with by EKI as it has been very proactive in using the national credit register in its loan application. On the other hand, EKI does not make any form of insurance available to its clients to protect them from financial shocks, for example credit life insurance is not offered. There is limited risk of clients being defrauded with secure financial operations as EKI staff does not handle cash.

Client privacy is well ensured as all client documentation is stored securely in branches. Also clients sign waivers to allow their personal credit history to be checked through the national credit register. Under the new law it is mandatory for EKI to file a court case against a client prior to writing off their loan which has resulted in a significant increase in the number of court cases filed from 90 and 78 in 2006 and 2007 respectively, to 223 in 2008. The amount of loan portfolio involved in these cases is 3 M BAM in 2008.

### Human resources policy

HR policies are formalized and hiring practices are fair and equal ensuring that all staff is treated equally and given the same development opportunities. Staff development is

<sup>8</sup> The other main reason being that most intermediaries were not sufficiently productive in bringing in new loans for EKI.

highly valued and intensive training and follow-up are provided to new staff. Also existing staff do receive yearly update training with an average of 1.5 days of training per person in 2008. In the past years there has been a declining trend, mostly as a result from less support from donors for training of staff. Overall management staff does receive the highest level of training (4.0 days), followed by LOs (1.8 days) and administrative staff (0.6 days). Promotion is transparent and based on bi-annual evaluations. Career paths exist within EKI, although possible advancement beyond LO is naturally limited given the limited number of management positions.

Staff remuneration is satisfactory and above average for the industry. Remuneration levels are not automatically updated with inflation. A significant increase was made in 2008 for both Branch and Senior Management (ranging from 15-30%) and the top-end of the salary scale for LOs was increased by 13%. The incentive system for LOs is transparent and LOs are well informed about the system. The scheme has been adjusted in January 2009 given the changing market conditions, as in 2008 the average bonus paid out was about half as compared to 2007.

Women are well represented within EKI comprising 57% of all staff. There is a noted difference between staff categories with only 33% of top management being female<sup>9</sup>, although this is 79% for branch management, 50% for LOs and 69% for administrative staff. With the exception of top management where only one third is female, all other staff categories have more than 50% women. There is representation from all regional, ethnic and religious groups, and tensions are not apparent between co-workers. However, there is no policy in place to actively monitor and/or guide this equal representation.

Risks related to the work of the staff are limited, also because Loan Officers do not carry or come in contact with cash. The only area of concern is the frequent use of cars, which has seen an increase in car accidents to 29 for a total of 187 LOs.

Employees at EKI are not formally organized and have no direct representative on board or management level. Staff feedback is possible through an open institutional culture. If not regularly planned, EKI does carry out staff satisfaction surveys. The conclusions of the last survey in the first half of 2007 was that staff in general was satisfied with their work in EKI but felt burdened by their work (mainly LOs) and felt there was not sufficient communication from the SMT explaining the strategy and changes in procedures. In the current situation, as employee responsibilities become more demanding with decreased client demand and difficult

economic conditions, management should take extra concern for employee satisfaction and maintaining a quality working atmosphere.

### **Social responsibility towards the community**

EKI, being associated to WVI, where possible links with their social programs. The most common link is to provide financial services to people that are supported by WVI. An experiment will also start with a guarantee fund to try to reach out to people supported by WVI that do not meet the guarantee requirements of EKI. Over the years, EKI has outgrown the social programs of WVI and as of December 2008 this only represents 1.7% of the loan portfolio.

EKI also provides additional support to its agricultural clients in the form of flyers to inform them on improved agricultural practices. There is also an employee charity fund, wherein almost all staff donates a small percentage of their salaries. Employees from each branch nominate community members to receive support. Donations-in-kind or monetary donations are given to recipients after approval by a centralized committee. The value donated was 12,155 BAM in 2007 and 17,505 BAM in 2008.

EKI plays an exemplary role in the BiH microfinance sector. EKI is often involved in activities to strengthen the sector and is currently active to bring all MFIs in BiH together to address the situation of over indebtedness of clients and cross-indebtedness between MFIs. EKI was one of the first MFIs to both use and provide data to the CRK in an effort to prevent systematic over indebtedness of clients in BiH.

Several procedures are in place to ensure respect of basic human rights. EKI has a system in place to ensure child protection. All EKI staff sign a child protection policy (inherited from WVI) stating the adequate behavior to adopt when working with children. EKI also performs a background check on staff with the police before hiring new staff since 2008.

### **Social Responsibility towards the Environment**

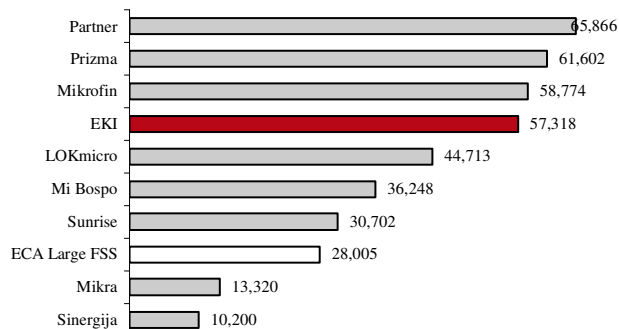
EKI has developed an environmental assessment as part of the loan appraisal leading to exclusion of environmentally hazardous activities. This assessment determines whether EKI can finance the business activity or not. This assessment is however only used for loans under the EBRD and IFC funds, but is not streamlined throughout the whole organization. Staff initially received training on this at the time of implementation, but no update training has been provided since the implementation of the EBRD in 2006. For its internal operations EKI does not have an eco-efficiency policy in place.

<sup>9</sup> Two of which are the General Manager and Finance Manager.

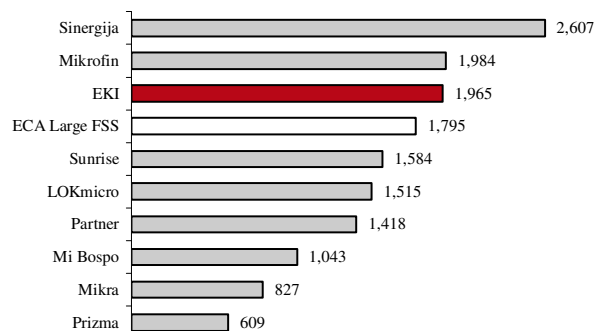
*The opinions expressed within this report are valid for one year after the rating mission. Beyond one year, or in case of a major change during this period affecting the institution's performance, that change due to the institution itself or its operating environment, Planet Rating does not guarantee 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

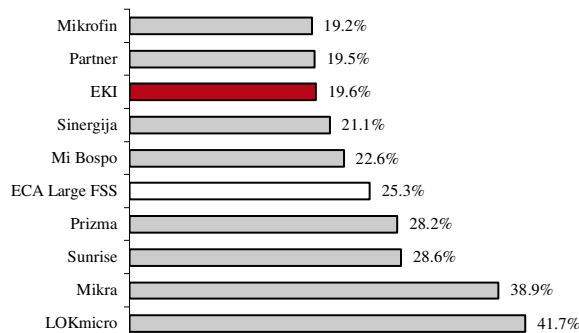
Number of loans outstanding



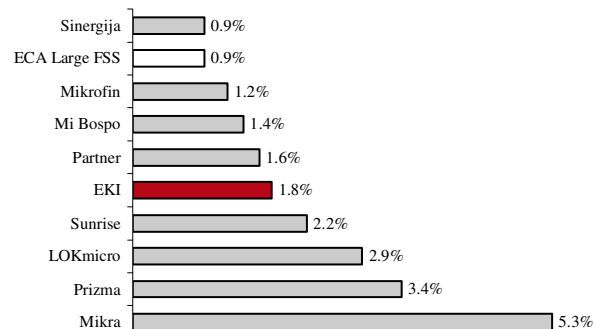
Average outstanding loan per client (EUR)



Portfolio Yield



PAR 31-365



Sources: EKI, Mi-Bospo - Planet Rating data as of Dec. 2008; other MFIs - Dec. 2008 reporting to AMFI; ECA Large FSS peer group - Mix Market 2007 Benchmarks, median.

## ■ Performance Indicators

	Dec. 2006	Dec. 2007	Dec. 2008
<b>Composition of the clientele</b>			
% of women clients	39.4%	41.1%	42.0%
% of rural clients	62.8%	63.4%	63.7%
% of clients in socially marginalized groups*	17.6%	16.9%	14.0%
<b>Appropriateness of services</b>			
PAR 31-360 days	0.3%	0.4%	1.7%
PAR > 360 days	0.0%	0.0%	0.0%
Retention Rate (CGAP Formula)	58%	70%	67%
Retention Rate (enhanced)	45%	48%	48%
Retention Rate (enhanced, including rejoining borrowers year n+1)	67%	67%	n/a
Share of consumer lending	0.3%	2.7%	4.7%
Average amount disbursed per loan	1,938	2,165	2,168
% of GDP per capita	78.3%	77.9%	69.0%
Portfolio Yield (nominal)	23.6%	21.6%	19.6%
<b>Human Resources policy</b>			
% of women among professional staff	57.3%	53.4%	57.2%
% of women among management	37.5%	33.3%	33.3%
% of employees who received at least two days of training	58.8%	48.0%	34.1%
Number of training days per staff	2.5	2.1	1.5
Min/Max LOs salary ratio	280%	300%	300%
Min/Max professional staff salary ratio	175%	183%	183%
Traffic accidents per loan officers	2.3%	8.0%	15.5%
Instances of assault per loan officer	0.0%	0.0%	0.0%
<b>Entering clients**</b>			
% below national poverty line	31.9%	40.7%	33.2%
% below 50% of national poverty line	2.0%	2.8%	1.7%
% below 1 USD / day PPP	0.0%	0.1%	0.0%
% below 2 USD / day PPP	0.8%	1.4%	0.7%
<b>Active borrowers**</b>			
% below national poverty line	31.3%	38.2%	35.9%
% below 50% of national poverty line	2.1%	2.6%	2.3%
% below 1 USD / day PPP	0.1%	0.1%	0.1%
% below 2 USD / day PPP	0.8%	1.3%	0.9%
<b>Achievement of change (3-year or 5-year clients)</b>			
% of clients that have experienced a positive change in their social status	n/a	n/a	n/a
% who have moved above the relevant poverty line	n/a	n/a	n/a
% still below the relevant poverty line	n/a	n/a	n/a
Number of jobs created (client level)	7,424	9,968	10,371
Number of jobs sustained (client level)	44,530	60,177	70,148

\*Includes invalids, minority groups, refugees, displaced persons and returnees. \*\*Based on household income data collected during loan appraisal; indicator not fully reliable, see Social Performance Monitoring.

## ■ Formulas

- Portfolio yield: Portfolio revenue / 13-month average gross outstanding portfolio
- Cost of savings ratio: Interest and fees paid on deposits/Average deposits
- Cost of borrowings ratio: Interest and fees paid on borrowings/Average borrowing
- Retention Rate (CGAP): Repeat borrowers / Borrowers who ended their loan during the period
- Retention Rate (enhanced): (Active borrowers end of period – constant borrowers) / (Active borrowers beginning of period + new borrowers – constant borrowers)
- Penetration rate: active clients / number of households

## ■ Rating scale

Rating	Definition
5+ 5	<b>Advanced:</b> Long-lasting commitment to social goals; efficient management of social performance and social responsibility risks; institution very likely to achieve a positive social impact
4+ 4	<b>Convincing:</b> Clear commitment to social goals; reasonable management of social performance and social responsibility risks; institution likely to achieve a positive social impact;
3+ 3	<b>In progress:</b> Clear intent to reach social goals; social performance management systems being implemented
2+ 2	<b>Incipient:</b> Clear intent to reach social goals; low capacity to manage social performance
1+ 1	<b>Intangible:</b> Intention to reach social goals is non tangible; low level of management of social performance