

Rating

D Insufficient

Procedures are in place, but with failings and certain problems are only partially addressed. There are medium-term risks for operations.



Performance indicators

| | Dec. 2003 | Dec. 2004 | Dec. 2005 |
|------------------------------|-----------|-----------|-----------|
| ACTIVITY | | | |
| Total number of staff | 43 | 48 | 52 |
| Total assets (M UGS) | 1,300 | 1,417 | 1,231 |
| (K USD) | 654 | 821 | 702 |
| Loan portfolio (M UGS) | 1,100 | 1,120 | 997 |
| Deposits (M UGS) | 98 | 115 | 64 |
| Nb. of active borrowers | 9,311 | 10,928 | 12,051 |
| Nb. of savers | 13,924 | 11,558 | 12,051 |
| Effective interest rate (%) | NA | NA | >55% |
| PAR 31 estimates (%) | 11.0 | 4.8 | 4.7 |
| Write-off ratio (%) | N/A | 15.2 | ~3 |
| Risk coverage ratio (%) | 160 | 109 | 141 |
| PERFORMANCE | | | |
| ROE (%) | (45.7) | (30.0) | (36.0) |
| Liabilities / Equity (%) | 42.1 | 65.0 | 50.9 |
| ROA (%) | (34.9) | (19.6) | (22.8) |
| OSS (%) | 44.2 | 54.8 | 48.9 |
| FSS (%) | 44.2 | 51.6 | 45.1 |
| Portfolio Yield (%) | 39.2 | 31.2 | 26.2 |
| Operat. expense ratio (%) | 66.7 | 55.2 | 50.2 |
| Staff productivity | 217 | 228 | 232 |
| Funding expense ratio | 2.7 | 4.3 | 4.6 |
| GROWTH | | | |
| Loan portfolio (%) | 24.0 | 1.8 | (10.9) |
| Savings portfolio (%) | 64.0 | 17.6 | (44.3) |
| Assets (%) | 0.6 | 9.0 | (13.1) |
| Exchange rate 1 USD = xx UGS | 1,987 | 1,726 | 1,754 |

Note: Reliability of 2005 data is not guaranteed (see section "I").

Planet Rating

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TERUDET, Soroti

May, 2006

Description of the institution

TERUDET started its operations in 1996 as the credit scheme of an integrated program designed to assist local farmers and traders and funded by the Royal Netherlands Government. This program was implemented through the District Local Government under the Soroti District Development Program (SDDP). In 2000, the credit scheme broke away from SDDP and started operating under the name of Kaso Rural Development Trust. The institution changed names to become the Teso Rural Development Trust (TERUDET) in 2002 and was incorporated in 2003 as a Non-Governmental Microfinance Institution. TERUDET is headquartered in Soroti, and conducts operations in Soroti, Katakwi, Kaberamaido and Amuria districts. As of March, 2006, TERUDET served more than 10,000 active borrowers, 80% through group lending and 20% through individual lending. The institution currently runs a loan portfolio of 997 M UGS (0.556 MUS\$).

Evaluation summary

TERUDET is adequately positioned on an underserved market and reaches out to the farthest rural areas that are not tapped by any other MFI. The portfolio performance has been strongly affected by the LRA insurgency that struck the region in 2003 but the portfolio is adequately managed and the PAR seems to have recovered healthy levels. The institution is however handicapped by the fact that it never reached sustainability, mainly due to a relatively low portfolio yield when compared to the effective interest rates and to high operating expenses related to a wide geographic coverage. This implies that TERUDET is in constant need for subsidies to cover its operating losses which makes it difficult to efficiently plan the activities. In 2005, an MIS crash revealed important weaknesses in the information system and greatly disorganized the data production process. The procedures used to reenter the data cannot guarantee the accuracy of the data for that year.

Improvements needed to reach minimum requirements on specific evaluation areas

- Revise business plan to adapt it to the institution's current situation
- Enhance staff skills in MIS management, accounting and financial management
- Secure MIS and data production process in order to guarantee data reliability at all times
- Implement an audit of main HQ procedures and functions including regular audits of the information system
- Secure sufficient funding to carry out the institution's strategy or adapt the institution's strategy to the level of funding currently available
- Ensure that the portfolio yield gets closer to the effective interest rate in order to reach profitability

Strategic goals

TERUDET wants to increase its outreach and serve up to 30,000 clients in the Soroti and Kumi area, and to enhance its product offering by the addition of an agriculture product and business development services.

TERUDET, M. Henry Okiria Okia (General Manager)

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■ Institutional presentation

Political and economic context

The LRA (Lord Resistance Army) insurgency that has been going on since 1987 in the Northern parts of Uganda, and that reached the region in 2003 has affected TERUDET's operations. Civilians in Soroti and the surrounding districts were forced to flee from their homes and some of them are still living in refugee camps. As a result, a number of loans granted in 2001 and 2002 have been written off in 2003 and 2004. Repayments on these loans are however still being slowly recovered.

Networks

TERUDET is a member of AMFIU, the association of Microfinance Institutions of Uganda and of MAIN, the Microfinance African Institutions Network.

Legal form, supervision and audit

TERUDET started its operations in 1996 as the credit scheme of an integrated program designed to assist local farmers and traders re-establish themselves following years of civil strife funded by the Royal Netherlands Government. This program was implemented through the District Local Government under the Soroti District Development Program (SDDP). In 2000, the credit scheme broke away from SDDP with the goal of becoming a self-sustaining microfinance institution. It started operating under the name of Kaso Rural Development Trust and changed names in October 2002 to become the Teso Rural Development Trust (TERUDET). It was incorporated in 2003 as a Non-Governmental Microfinance Institution.

David Ddamulira & Co. has been the external auditor firm for the past four years. The auditor only performed annual checks on the accounts and provided unqualified opinions. TERUDET's fiscal year begins on January 1st and ends on December 31st.

Ownership

TERUDET is owned by the local councils of the four districts in which it operates. The local councils appoint the Board of Directors for four years, according to their background and professional experience and ensure that each of the 10 counties of the operating area are represented on the Board. All of the current 10 directors have been reelected in 2005. TERUDET's General Manager is also the Board's Secretary.

Management team

The General Manager, who has been in position since 1998, is a member of the Chartered Institute of Bankers (ACIB), London, and of the Chartered Secretaries and Administrators (ICSA), London. All department managers (Accounting and finance, Information system, Operations,

Administration and Internal audit) are located at the head office in Soroti and have been in position for at least 3 years.

Donations

Since inception, the institution has received a total of approx. 1,000 M UGS in donations, mostly provided by the Dutch government through the districts, and by ICCO.

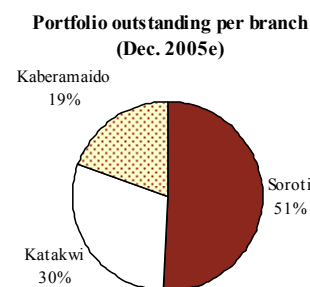
| Donor | Amount | Period | Purpose |
|---------------|-----------|-------------|----------------------------|
| Dutch Embassy | 455 M UGS | 2002-2004 | Operating expenses |
| ICCO | 330 M UGS | 2005-2007 | Equipment, training and TA |
| SUFFICE | 42 M UGS | 2003 – 2005 | Capacity Building |
| SPEED | 34 M UGS | 2002 | Software |
| Stromme | 13 M UGS | 2003 | Equipment |
| MCAP | 3.8 M UGS | 2005 | Furniture |

Funding sources (as of Dec. 2005)

| Loan provider | Interest rate | Duration | Initial amount | Initial amount (USD) |
|--------------------|---------------|-----------|----------------|----------------------|
| SUFFICE | 14% | 24 months | 60 M UGS | 340 K USD |
| MSCL | 14% | 24 months | 150 M UGS | 950 K USD |
| Stromme Foundation | 14% | 24 months | 75 M UGS | 570 K USD |

Organization

Headquarters centralize all strategic functions as well as loan decision, data processing, and liquidity management. Branch staff is composed of one branch manager, senior and junior microfinance officers (LO), who are in charge of the day-to-day loan management (client selection and training of groups, disbursement, repayment collection). Disbursements are made by check for individual loans, and in cash carried to the villages by the LO and the branch manager for groups. Repayments are made at the cashier desk¹. Once a week, money in excess is cashed at the bank.



Market penetration

TERUDET conducts its operations in both rural and urban areas through three offices in Soroti, Katakwi (north-east of Soroti) and Kaberamaido (west of Soroti). The 28 LO are assigned one or two sub-counties each in order to cover all sub-counties of the districts served. LOs in charge of Village Bank loans travel on motorbikes from Monday to Thursday and are able to serve even the farthest rural clients.

¹ Exceptions tolerated, see section "R".

Products and services

TERUDET currently offers three loan products: individual (for small businesses), employee loans (for salaried individuals) and group loans (for groups of approx. 30 persons through a village banking methodology). Amounts range from 50,000 UGS to 10,000,000 UGS with terms from four to twelve months, and a possible grace period of one week for group loans. Individual and employee loans bear a 3% flat interest rate per month calculated on the initial balance. Group loans bear a 4% flat interest rate per month. Individuals are charged a 1% application fee (commitment fee), and all borrowers have to cover the cost of stationery used for loan application. The annual effective rates vary between 53% and 90% depending on the loan product.

Repayment is made on a monthly basis for both individual and employee loans. Group loans repayments are scheduled on a weekly or bi-weekly basis and include compulsory savings that are fully reimbursed once the loan is cleared, but might also be used, upon decision of the group, to repay past due loans.

In 2005, TERUDET launched a pilot agriculture loan product with a specific repayment schedule that includes a more important grace period. Other products are currently under study (loans for smaller groups; 5-10 persons).

New premises

In March 2006, TERUDET moved into new premises located on Soroti's Main Street: it had bought the building two years ago through a sale by auction and with a specific district subsidy. TERUDET had not been able to move earlier due to litigation between the former owner and the bank selling the building as loan collateral.

MIS crash

The intrusion of a virus in the information system led to the loss of all electronic data from July to December, 2005. Both server databases and DLT back-ups were affected. Data is currently being re-entered in the system from printed documents. The process has been made longer due to the recent move.

■ Governance

Governance and Decision Making is rated « c »

Decision-making

- + Locally influent and strongly committed Board members give their full support to the General Manager: they are all easily available and located in Soroti, except for the Chairman who is based in Kampala, which allows easier contact with donors.
- + Wide delegation of powers to the General Manager allows a fast decision process.

- + The General Manager has a good understanding of the microfinance industry and of his market.
- Board members have relevant backgrounds (Central Bank, accounting, civil servants) but would need trainings to develop microfinance skills: they are ready for it, but funds have so far been mainly allocated to operational activities.
- Board members receive financial statements and PMT reports before their meetings. The delay in data production for 2005 (see section "I") however did not allow Board members to fully exercise their control power, monitor the institution and provide efficient help in meeting the strategic goals.

Planning

- + The four-year strategic plans (2003-2006 and 2006-2009) are well documented and prepared. They have been written by the Board and the Management team, and include a good diagnosis of the institution's situation and environment.
- Nonetheless, the first plan was based on the strong assumption of political stability, which was quickly proven wrong. It has not been updated to take into account the effects of LRA insurgency and was thus of little use for several years. The subsequent plan sets roughly the same goals than the previous one (become profitable by 2006 and expand to Kumi) and does not include several scenarios.
- The plans focus on reaching ambitious growth targets through mobilization of additional funding resources and do not sufficiently focus on solving the internal weaknesses (essentially MIS).
- Owners have set for TERUDET the social mission of serving all of the sub-counties in the four districts, which implies higher operating costs (low productivity of LO in some very remote areas) and spreads thinner the MFI's current limited financial means.

Management team

- + The General Manager is experienced and dedicated to the institution.
- + The management team is fairly dimensioned, comprising all the necessary positions for an institution of that size, and would be able to handle a significant growth.
- Some key skills (accounting, IT, and internal audit to a minor extent) need to be strengthened in order to ensure the institution's sustainability.
- Management team supervision needs to be reinforced.

Human resource management

- + The institution managed to keep most of the staff despite low salaries by providing regular trainings, most of which were fully paid by donors.

- + HR procedures, such as recruitment contracts, salary grids, trainings, appraisals and vacations rules, are all clearly set and monitored both by the HR Manager and the General Manager.
- + Appraisals are done on an annual basis (or more frequently for new hires) and are used for promotion and/or contract renewal purposes. An assessment form is filled by the employee, his direct supervisor and the HR Manager: according to performance, a grade is given along with actions for improvement.
- Staff turnover has been relatively low so far, but some resignations already occurred due to low salaries. It could grow into a serious issue, especially if the lack of funds is believed to endanger the institution's future.

Improvements needed to reach minimum requirements

- △ A business plan for the three to five years to come that takes into account the evolution of the environment and that describes different scenarios.
 - △ A management team with enhanced skills in MIS management, accounting and financial management.
-

Information

Information and equipment is rated « e »

Description of the MIS

| | |
|-----------------------------------|---|
| Equipment | <ul style="list-style-type: none"> ▪ All computers are linked by an internal LAN network. ▪ Monthly data back-up on DLT tapes (provided by a donor). |
| Accounting | <ul style="list-style-type: none"> ▪ Solomon's Microsoft software. ▪ PMT used for reporting purposes and reports sent to donors and AMFIU. |
| Portfolio and savings information | <ul style="list-style-type: none"> ▪ Loan Performer software since 2002. ▪ The two software are not interfaced and loan data is manually entered into the accounting system on a daily basis in HQ. ▪ Client data is only available in paper format. ▪ Cash operations are immediately recorded by the cashier in the system through a teller module. |

Management Information System (MIS) and equipment

- + Most computers run under Windows XP.
- + Data entering processes are well designed and performed accordingly under normal circumstances.
- However, procedures are currently disorganized due to the move (the network was still not fully stable at the time of the rating mission) and the data loss.
- The 2005 data had been printed out and is currently being re-entered in the system: the lack of appropriate checks makes it impossible to ensure it will be accurate.
- Loan Performer literacy is enough for routine basic operations, but not enough to handle potential problems and special requirements.

- Average level of Solomon's literacy is not sufficient to avoid system misuses and ensure the extracted data is accurate.
- Data security procedures are not yet efficient. Following the 2005 virus attack, a firewall was installed. Future data loss can however only be avoided through an improvement of the institution's IT skills and equipment (anti-virus system put in place and frequently updated, staff trained to basic security measure, thorough back up performed on a regular basis, network administration improved).
- The current DLT back-up system is not sustainable given the high price of tapes, and is to be replaced by CD-Rom back-ups.
- Some paper documents are not sufficiently protected against fire or theft.
- Some key documents, such as bank statements original copies, have been taken by the external auditors to their offices in Kampala.
- Despite a will of change and the inclusion of budgets for new software in funding requests, the IT improvement plan has not been sufficiently studied so far.

Information on activities

- + Loan Performer reports are regularly printed out and provide all the information needed for Branch managers and loan officers to manage their portfolio.
- However, the data crash disorganized the data production process which currently does not ensure that data is fully reliable (insufficient reconciliation between portfolio and accounting data).
- Data could be used for a deeper analysis of the portfolio performance.

Financial and accounting information

- + PMT reports are produced every quarter, which ensures that adequate ratios are calculated.
- + Basic information such as trial balance and inventory is available once a month.
- + Accounting and cash are reconciled every evening. Accounting and bank accounts are reconciled on a monthly basis.
- Reconciliation between Loan Performer and the accounting books was only performed until December, 2004, and reliable financial information could not be provided for 2005 or for Q1 2006.
- Movements of the loan loss reserve could not be reconciled.
- Discrepancies are observed between PMT and audited financial statements or from one PMT to another (ex: big differences in reported interest income), one of the identified reasons being that end of quarters operations

are not duly performed before the production of quarterly PMT reports.

- A better analysis of the institution could be performed if the data was more reliable.
- No analysis is done at branch level.

Improvements needed to reach the minimum required

- △ Efficient back-up procedures and protection of data against loss, manipulation or deterioration
 - △ Increased software literacy for key MIS/accounting staff
 - △ Systematic reconciliation of accounting and portfolio data.
 - △ Clarified loan loss reserve movements that abide by the generally accepted accounting standards.
-

■ Risk

Risk Management is rated « d »

Procedures and internal controls

- + Internal procedures manuals are well written and procedures are known by all staff.
- + Control procedures for field operations include a healthy separation of task as well as numerous control points, notably in the disbursement process. Internal group operations are closely monitored and verified by field staff during their weekly/bi-weekly visits to groups.
- + Cash management procedures ensure a reasonable level of cash security for transactions performed at the branches (secured and separate teller window, safe). Disbursements to rural groups imply cash management risk that however could not be reduced further (cash transfers performed by car with two staff) without transferring the risk to the end client.
- Despite a sufficient number of controls, some non-compliance to the rules is tolerated which implies risks that are not adequately monitored (repayments that should be made by group leaders directly at the branch are sometimes carried by LOs²).
- Weaknesses in the IT processes and organization create a significant risk of data manipulation: IT Department officers perform the incompatible tasks of entering data and managing the systems (unrestricted access to portfolio and accounting electronic and paper data) and the lack of proper data does not allow to swiftly identify all errors.

Internal audit

- + Internal auditors conduct sufficient appropriate field checks with a methodology that allows to control most loan transaction related risks.

² In 2004, random audit controls helped identifying the case of a LO cashing group loan repayments with delays. The LO has been asked to gradually repay the amount that reported to be missing through deductions on his monthly salary.

- The internal audit department however does not provide a comprehensive control of all risks (no audit of HQ; lack of well-designed audit plan, internal audit reports provided to all relevant parties but not systematically followed by corrective actions).
- The internal audit department does not provide a general plan of how and why these audits need to be performed.
- External auditors review classic accounting procedures (procurement, depreciation) and check on a few loan files for procedure compliance but do not examine with sufficient care portfolio related accounts. For instance, Planet Rating identified movements that do not comply with usual accounting norms in the 2004 audited loan loss reserve (loans write-offs are not clearly identified nor balanced with the appropriate accounts).

Improvements needed to reach the minimum required

- △ Implementation of an audit of main HQ procedures and functions including regular audits of the information system.
 - △ Deeper investigation by external auditors to support internal audit team.
 - △ Stiffer reaction when procedures are violated or only partially applied.
-

■ Activities

Activities: products and services is rated « c »

Marketing and competition

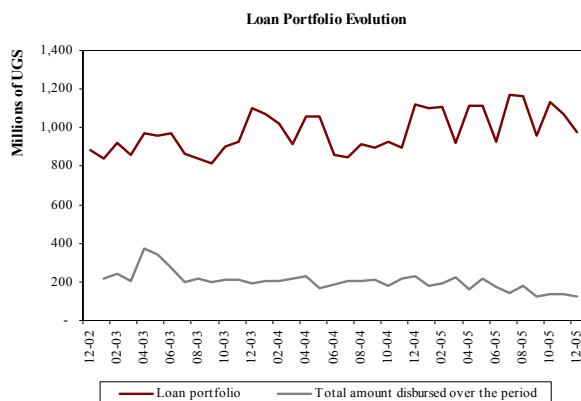
With its Village Bank loans, TERUDET reaches out to the farthest rural areas where it serves a clientele that is not being tapped by any other microfinance institution. However, several microfinance institutions are active in the region: Centenary Bank, Pride, Uganda Finance Trust (branches in Kumi, Soroti and Kaberamaido, also serving Lira, Busia, and Katakwi), and UWESO (branches in Soroti and Kumi). Competition is thus increasing steadily on the individual loans for which TERUDET has competitive disadvantages (low cash availability, higher interest rates, and lower loan amounts).

Credit methodology

- + Loan processing procedures are clear and include all necessary steps, such as basic business evaluation by loan officers, repayment capacity assessment, written approval and acceptance, identification and registration of guarantees.
- + Village Banks designated representatives are well trained on loan procedures and book keeping.
- + Loan officers are well trained to internal procedures and have the appropriate skills to deal with the borrowers.
- Business evaluation is however not sufficiently detailed or documented to allow a sound decision for big loans.

Portfolio evolution

The total portfolio has more or less stagnated for the past three years and has even decreased by 10% between 2004/2005: this is due to the fact that negative results and important write-offs have absorbed a big share of the additional funding secured during that period, which did not allow TERUDET to increase its loan portfolio. The institution has made the choice to reduce the average loan size and spread these scarce resources on an increasing number of clients.



Quality of the portfolio

| | Dec. 2003 | Dec. 2004 | Dec. 2005 |
|-------------------------------------|-----------|-----------|-------------|
| Loan portfolio (USD) | 553,467 | 649,004 | 568,655 |
| Loan portfolio (K UGS) | 1,099,821 | 1,119,864 | 997,495,015 |
| Change (%) | 24.0 | 1.8 | (10.9) |
| Average outstanding loan | 458,862 | 565,615 | 603,535 |
| Number of active borrowers* | 9,311 | 10,928 | 12,051 |
| Change (%) | N/A | 17.4 | 10.3 |
| Average outstanding loan per client | 59 | 59 | 47 |
| PAR 31 estimates (%) | 11 | 4.8 | 4.7 |
| Write-off ratio (%) | N/A | 15.2 | 2.9 |

Note: 2005 data has not been fully reconciled with accounting data. Data accuracy not guaranteed.

- + PAR ratio has been maintained at a reasonable level for the past two years. The sharp decrease, from more than 11% in 2003 to less than 5% in 2004 is mainly due to the write-off of bad debts accumulated during the insurgency (150 M UGS; 15% of the loan portfolio). These written-off loans are followed up and are currently being slowly recovered (approx. 5 M UGS recovered to date).
- Recording of recovery from loans written off is not well secured (vouchers are not numbered, thus preventing the tracing of the total amount that has been recovered by Branch managers or loan officers in the field).

Portfolio diversification

The loan portfolio is by essence concentrated in the Soroti area and there is no specific policy regarding loan portfolio diversification by sector. Loans however accommodate

clients with diverse activities: salaried workers, civil servants, petty traders, micro-entrepreneurs of all kinds as well as rural clients deriving some of their income from agriculture activities. The latter represents 5% of the loan portfolio.

Credit risk coverage

| ESTIMATES | Dec. 2003 | Dec. 2004 | Dec. 2005 |
|-------------------------|-----------|-----------|-----------|
| Risk coverage ratio (%) | 160.4 | 109.4 | 140.5 |
| PAR 31 net of loan loss | (8.0) | (0.6) | (2.3) |
| provision / Equity (%) | | | |

- + The provisioning method is clear and provides a sufficient level of risk coverage.
- + Solidarity group guarantee along with compulsory savings in Village Banks ensure a reasonable level of protection against credit risk.
- Most of the guarantees required for individuals loans (movable – fridges, bikes, cars, etc. – or immovable properties, personal guarantees) are either difficult or impossible to mobilize in case of default.

Savings Activities

| | Dec. 2003 | Dec. 2004 | Dec. 2005 |
|----------------------------|-----------|-----------|-----------|
| Outstanding deposits (USD) | 49,192 | 66,618 | 36,500 |
| Outst. deposits (K UGS) | 97,751 | 114,949 | 64,025 |
| Change (%) | 64.0 | 17.6 | (44.3) |
| Number of depositors | 13,924 | 11,558 | 12,051 |

Note: 2005 data has not been fully reconciled with accounting data. Data accuracy not guaranteed.

- The drop in the amount of saving is due to the fact that TERUDET used to collect voluntary savings and had to stop due to the introduction of the MDI act that restrict savings collection.
- No interest is served on savings.

Improvements needed to reach minimum requirements

- △ Increase competitive advantages on individual loan products through faster disbursements and more predictable disbursement dates.
- △ Improve business evaluation skills of staff working in urban areas

Financing and liquidity

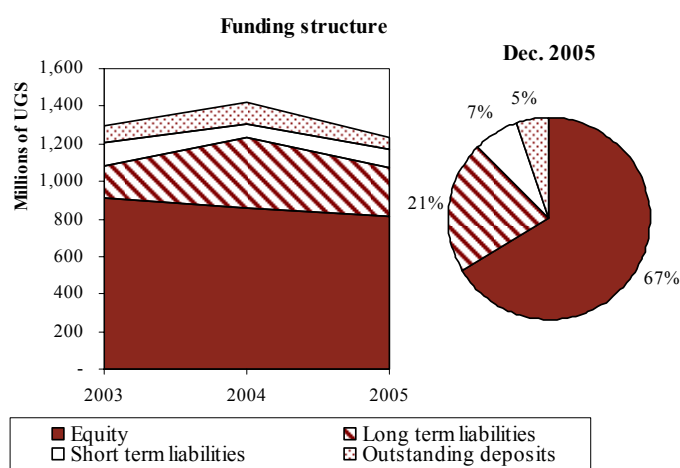
Financing and liquidity is rated « d »

Financing strategy

- TERUDET funds the biggest part of its activities through donations, and a smaller part through long term liabilities provided by local wholesale lenders specialized in microfinance (SUFFICE, MSCL, Stromme).
- + Thanks to its special positioning in an underserved market, TERUDET has managed to keep the support of several important partners and to acquire new ones in

the recent years (in 2005, ICCO approved a grant of 150,000 EUR; approx. 325 M UGS).

- The very high level of operating losses before donations (TERUDET accumulated over 1 B UGS in operating losses over the past three years; see section “E”) is however very difficult to sustain: the institution has not been able to mobilize sufficient amounts of donations and is slowly eroding its equity base by approx. 100 M UGS per year.



| | Dec. 2003 | Dec. 2004 | Dec. 2005 |
|--------------------------|-----------|-----------|-----------|
| Liabilities / Equity (%) | 42.1 | 65.0 | 50.9 |

Asset and liability management

Asset and liability management (ALM) risks are currently limited:

- + Very low interest rate risk: although loan providers’ interest rates are reviewed every semester, TERUDET’s theoretical margin is sufficient to cover potential interest rate increase.
- + No maturity risk: equity and long term liabilities fund short term loans to clients.
- + No FX risk: TERUDET has not contracted any loan in foreign currency.

Liquidity management

- There are some basic liquidity procedures to manage cash shortages: this however comes at the cost of clients having to wait for long weeks, or even months, before their loan is disbursed.
- Procedures defining which loans are disbursed first in case of liquidity shortage are not clear.

Improvements needed to reach minimum requirements

- △ Secure sufficient funding to carry out the institution’s strategy or adapt the institution’s strategy to the level of funding currently available

Efficiency and Profitability

Efficiency and Profitability is rated « e »

| Profitability analysis | Dec. 2003 | Dec. 2004 | Dec. 2005 |
|---|-----------|-----------|-----------|
| ROE (%) | (45.7) | (30.0) | (36.0) |
| Liabilities / Equity (%) | 42.1 | 65.0 | 50.9 |
| ROA (%) | (34.9) | (19.6) | (22.8) |
| Profit generation | | | |
| OSS (%) | 44.2 | 54.8 | 48.9 |
| Portfolio Yield (%) | 39.2 | 31.2 | 26.2 |
| Operating expense ratio (%) | 66.7 | 55.2 | 50.2 |
| Staff productivity | 217 | 228 | 232 |
| Loan officer productivity | 443 | 455 | 482 |
| Average outstanding loan per client (UGS) | 118,121 | 102,477 | 82,773 |
| Funding expense ratio (%) | 2.7 | 4.3 | 4.6 |
| Cost of savings (%) | 0.0 | 0.0 | 0.0 |
| Cost of liabilities (%) | 13.3 | 12.5 | 10.6 |
| Loan Loss Provision expense ratio (%) | 19.7 | 0.9 | 0.5 |
| PAR 31-365 (%) | 11.0 | 4.8 | 4.7 |
| Write-off ratio (%) | N/A | 15.2 | 2.8 |
| Asset management | | | |
| Outstanding Loan Portfolio / Assets (%) | 69.7 | 74.9 | 75.8 |
| Non-portfolio income as a % of financial revenues (%) | 0.0 | 0.0 | 0.0 |

Note: 2005 data has not been fully reconciled with portfolio data. Data accuracy not guaranteed.

Overview of the profitability

- TERUDET has not yet been able to reach profitability with ROAs fluctuating below the -20% bar. The difficult operating environment (LRA insurgency in 2003, deep outreach to rural areas) partially explains this performance that is however mainly due to internal challenges (see explanations below).

Portfolio yield and effective interest rate

- The portfolio yield has been decreasing during the past two years (from approx. 40% in 2003 to approx. 26% in 2005), and is particularly low when compared to the effective interest rate charged on its loans (between 53% and 90% depending on the loan products). This very important yield gap could be explained by a combination of (a) a quality of the institution’s portfolio that would be significantly worse than that currently reported, (b) fraud, (c) data inaccuracy leading to an overestimation of the total portfolio amount, (d) important discount on interest rates granted, voluntarily or not, to some clients.

Operating expense ratio

- Despite its decrease, the operating expense ratio is still high at more than 50%. This poor performance is largely due to the strategic choice made by the Board to set up

upfront a large and scattered geographical network before getting sufficient funding to not fully utilize it.

- This led TERUDET to try and minimize its expenses by keeping staff salary at a very low level (most LOs earn less than 200,000 UGS per month) which puts challenges on staff motivation and retention (see “G”).
- It is to be noted that the low average of loan size is also a key driver of the high operating expense ratio.

Funding expense ratio

- The funding expense ratio is on a slightly upward trend and is likely to keep increasing in the years to come, given that TERUDET has few options but debt financing to fund the desired growth of its loan portfolio.

Loan loss provision expense ratio

- Bad loans accumulated during the insurgency have been provisioned in 2003 and were largely written-off in 2004, which explains the evolution of the ratio (approx. 20% in 2003, close to 0% in 2004). Given the current level of provision and based on the available data for portfolio quality, TERUDET might not incur additional provisioning expenses for 2005.

Asset management

- The current level of asset investments in the loan portfolio is reasonable at 75% of total assets, given the fact that the new premises granted by the local districts represent another 20%.

▪ Client friendliness

Transparency

- ✚ A repayment schedule indicating the amount of capital and interest of each installment is provided to the borrower upon disbursement of the loan.
- ✚ All transactions are recorded in passbooks for group loans and individual borrowers receive clear vouchers for each of their transactions.
- Loan contracts have recently been revised and slightly improved but they do not yet provide all the loans’ characteristics and conditions in a clear and easily understandable way.
- Interest on loan is computed on the initial balance and the effective interest rate (total cost of the loan on average loan balance) is not provided.

Total cost of the loan

| | |
|--------------------------|--|
| Interest rate | 3% to 4% per month on the initial loan balance |
| Application form | 5,000 UGS |
| Commitment fee | 1% of the loan amount |
| Effective interest rate* | 53% to 90% per annum |

* Based on loan amounts of 1 M and 2.5 M UGS, and loan terms of 4 and 12 months

Adaptation of services to client’s needs

- TERUDET has conducted several market studies over the past year in order to identify client’s needs. This has resulted in the identification of potential improvement or new products, most of which have however not been fully implemented yet.
- Based on these studies TERUDET has reduced the minimum number of members required to form a Village Bank and has started piloting an agricultural loan product.

Efficiency

- The loan application and evaluation process is well designed and efficient. Clients nevertheless usually have to wait for a significant amount of time (from one week to one or two months) before they can get their loan due to the current cash shortage situation.
- ✚ Repayment transactions are swiftly managed by the cashier for individual loans.
- Group meetings convened on a (bi-)weekly basis for Village Banks repayments can last up to two or three hours. The length of these meetings essentially depends on the group leaders’ efficiency.

Accountability

- There is no formal mechanism by which clients can get information on TERUDET’s financial situation, which is not crucial given the fact that TERUDET does not collect savings from its clients.
- There is no formal channel for clients to file their complaints.

■ Appendices

| TERUDET Balance sheet | Notes | UGS | | | USD | | | Evolution | |
|---|-------|----------------------|----------------------|----------------------|----------------|----------------|----------------|----------------|----------------|
| | | Dec. 2003 | Dec. 2004 | Dec. 2005(e) | Dec. 2003 | Dec. 2004 | Dec. 2005(e) | 2004/2003 | 2005/2004 |
| ASSETS | | 1,300,188,833 | 1,416,940,105 | 1,231,382,104 | 654,298 | 821,172 | 701,990 | 9.0% | (13.1%) |
| Short Term Assets | | 1,011,782,518 | 1,167,233,660 | 983,926,735 | 509,163 | 676,457 | 560,920 | 15.4% | (15.7%) |
| Cash and Due from Banks | | 83,627,340 | 74,926,798 | 39,670,544 | 42,084 | 43,423 | 22,616 | (10.4%) | (47.1%) |
| Short Term Investments | | - | - | - | - | - | - | - | - |
| Short Term Net Loan Portfolio | | 905,793,380 | 1,061,094,862 | 933,121,391 | 455,825 | 614,946 | 531,957 | 17.1% | (12.1%) |
| Short Term Gross Loan Portfolio | | 1,099,820,956 | 1,119,863,486 | 997,495,015 | 553,467 | 649,004 | 568,655 | 1.8% | (10.9%) |
| (Loan Loss Reserve) | | 194,027,576 | 58,768,624 | 64,373,624 | 97,641 | 34,059 | 36,698 | (69.7%) | 9.5% |
| Interest Receivable | | - | - | - | - | - | - | - | - |
| On loan portfolio | | - | - | - | - | - | - | - | - |
| On investments | | - | - | - | - | - | - | - | - |
| Accounts receivable and other assets | | 22,361,798 | 31,212,000 | 11,134,800 | 11,253 | 18,089 | 6,348 | 39.6% | (64.3%) |
| Long term assets | | 288,406,315 | 249,706,445 | 247,455,369 | 145,136 | 144,715 | 141,070 | (13.4%) | (0.9%) |
| Long Term Net Investments | | - | - | - | - | - | - | - | - |
| Long Term Gross Loan Portfolio | | - | - | - | - | - | - | - | - |
| Net Fixed Assets | | 288,406,315 | 249,706,445 | 247,455,369 | 145,136 | 144,715 | 141,070 | (13.4%) | (0.9%) |
| Other Long Term Assets | | - | - | - | - | - | - | - | - |
| LIABILITIES AND EQUITY | | 1,300,188,833 | 1,416,940,105 | 1,231,382,104 | 654,298 | 821,172 | 701,990 | 9.0% | (13.1%) |
| Liabilities | | 385,500,526 | 558,194,900 | 415,145,067 | 193,997 | 323,496 | 236,667 | 44.8% | (25.6%) |
| Short term liabilities | | 214,667,193 | 183,194,900 | 155,145,067 | 108,028 | 106,169 | 88,446 | (14.7%) | (15.3%) |
| Demand Deposits | | - | - | - | - | - | - | - | - |
| Compulsory Deposits | | 97,751,450 | 114,949,400 | 64,025,351 | 49,192 | 66,618 | 36,500 | 17.6% | (44.3%) |
| Short Term Time Deposits | | - | - | - | - | - | - | - | - |
| Short Term Borrowings | | 60,000,000 | 60,000,000 | 60,000,000 | 30,194 | 34,772 | 34,205 | 0.0% | 0.0% |
| Interest payable | | 5,704,688 | - | - | 2,871 | - | - | (100.0%) | - |
| Accounts Payable and Other Short Term Liabilities | | 51,211,055 | 8,245,500 | 31,119,716 | 25,771 | 4,779 | 17,741 | (83.9%) | 277.4% |
| Long term liabilities | | 170,833,333 | 375,000,000 | 260,000,000 | 85,969 | 217,327 | 148,222 | 119.5% | (30.7%) |
| Long Term Time Deposits | | - | - | - | - | - | - | - | - |
| Long Term Borrowings | | 170,833,333 | 375,000,000 | 260,000,000 | 85,969 | 217,327 | 148,222 | 119.5% | (30.7%) |
| Other Long Term Liabilities | | - | - | - | - | - | - | - | - |
| Equity | | 914,688,307 | 858,745,205 | 816,237,037 | 460,302 | 497,676 | 465,323 | (6.1%) | (5.0%) |
| Paid-In Capital | | - | - | - | - | - | - | - | - |
| Donated equity | | 982,192,539 | 982,192,540 | 982,192,540 | 494,272 | 569,219 | 559,931 | 0.0% | 0.0% |
| Retained earnings without donations and reserves | | (67,504,232) | (123,447,335) | (165,955,503) | (33,970) | (71,543) | (94,608) | 82.9% | 34.4% |
| Current year | | (453,080,194) | (266,263,103) | (301,670,168) | (228,005) | (154,310) | (171,977) | (41.2%) | 13.3% |
| Other equity accounts | | - | - | - | - | - | - | - | - |

Note: 2005 data has not been fully reconciled with portfolio data. Its accuracy is not guaranteed.

Planet Rating – TERUDET, Uganda – May 2006

| Income Statement | Notes | Dec. 2003 | Dec. 2004 | Dec. 2005 | Dec. 2003 | Dec. 2004 | Dec. 2005 | 2004/2003 | 2005/2004 |
|--|--------------|----------------------|----------------------|----------------------|------------------|------------------|------------------|------------------|------------------|
| Financial Revenue (a) | | 359,603,796 | 323,255,418 | 288,249,021 | 180,965 | 187,339 | 164,326 | (10.1%) | (10.8%) |
| Financial Revenue from Loan Portfolio | | 357,432,796 | 304,604,672 | 279,341,821 | 179,872 | 176,530 | 159,248 | (14.8%) | (8.3%) |
| Interest on Loan Portfolio | | 331,949,965 | 239,014,874 | 238,384,394 | 167,048 | 138,518 | 135,899 | (28.0%) | (0.3%) |
| Fees and Commissions on Loan Portfolio | | 9,372,250 | 26,554,593 | 4,846,123 | 4,716 | 15,389 | 2,763 | 183.3% | (81.8%) |
| Penalty Revenue on Loan Portfolio | | 16,110,581 | 39,035,205 | 36,111,304 | 8,107 | 22,622 | 20,586 | 142.3% | (7.5%) |
| Financial Revenue from Investments | | - | - | - | - | - | - | - | - |
| Other Operating Revenue | | 2,171,000 | 18,650,746 | 8,907,200 | 1,093 | 10,809 | 5,078 | 759.1% | (52.2%) |
| Financial Expense (b) | | 24,920,833 | 41,636,492 | 49,095,091 | 12,541 | 24,130 | 27,988 | 67.1% | 17.9% |
| Interest paid on borrowings | | 24,920,833 | 41,636,492 | 40,083,591 | 12,541 | 24,130 | 22,851 | 67.1% | (3.7%) |
| Interest paid on deposits | | - | - | - | - | - | - | - | - |
| Net Inflation Adjustment Expense | | - | - | - | - | - | - | - | - |
| Other Financial Expenses | | - | - | 9,011,500 | - | - | 5,137 | - | - |
| Financial income [c=a-b] | | 334,682,963 | 281,618,926 | 239,153,930 | 168,424 | 163,209 | 136,338 | (15.9%) | (15.1%) |
| Net Loan Loss provision expense (d) | | 179,997,724 | 8,960,000 | 5,455,000 | 90,581 | 5,193 | 3,110 | (95.0%) | (39.1%) |
| Loan loss provision expense and write-off | | 179,997,724 | 13,560,000 | 5,605,000 | 90,581 | 7,859 | 3,195 | (92.5%) | (58.7%) |
| Recovery from Loans written off | | - | 4,600,000 | 150,000 | - | 2,666 | 86 | - | (96.7%) |
| Operating expense (e) | | 607,765,433 | 538,922,029 | 535,369,098 | 305,848 | 312,326 | 305,205 | (11.3%) | (0.7%) |
| Personnel Expense (includes fringe) | | 223,844,033 | 231,415,350 | 232,236,650 | 112,646 | 134,114 | 132,394 | 3.4% | 0.4% |
| Administrative Expense (non-staff operating expenses) | | 383,921,400 | 307,506,679 | 303,132,448 | 193,202 | 178,212 | 172,811 | (19.9%) | (1.4%) |
| Depreciation and amortization | | 49,981,373 | 57,444,220 | 55,775,350 | 25,152 | 33,291 | 31,797 | 14.9% | (2.9%) |
| Consulting fees | | - | - | 10,825,000 | - | - | 6,171 | - | - |
| Rent and utilities | | 29,688,814 | 20,370,045 | 21,067,295 | 14,940 | 11,805 | 12,010 | (31.4%) | 3.4% |
| Travel and transport | | 124,840,420 | 93,010,732 | 98,954,231 | 62,824 | 53,903 | 56,412 | (25.5%) | 6.4% |
| Stationery and office supplies | | 80,688,538 | 26,563,904 | 15,334,138 | 40,605 | 15,395 | 8,742 | (67.1%) | (42.3%) |
| | | | | | | | | - | - |
| | | | | | | | | - | - |
| | | | | | | | | - | - |
| Others | | 98,722,255 | 110,117,778 | 101,176,434 | 49,680 | 63,818 | 57,679 | 11.5% | (8.1%) |
| Net Operating Income Before Taxes and Donations [f=c-d-e] | | (453,080,194) | (266,263,103) | (301,670,168) | (228,005) | (154,310) | (171,977) | (41.2%) | 13.3% |
| Income Taxes (g) | | - | - | - | - | - | - | - | - |
| Net Operating Income Before Donations [h=f-g] | | (453,080,194) | (266,263,103) | (301,670,168) | (228,005) | (154,310) | (171,977) | (41.2%) | 13.3% |
| Non Operating Revenue (i) | | - | - | - | - | - | - | - | - |
| Non Operating Expense (including related taxes) (j) | | - | - | - | - | - | - | - | - |
| Net Income Before Donations [k=h+i-j] | | (453,080,194) | (266,263,103) | (301,670,168) | (228,005) | (154,310) | (171,977) | (41.2%) | 13.3% |
| Donations (l) | | 348,887,700 | 210,320,000 | 259,162,000 | 175,572 | 121,889 | 147,744 | (39.7%) | 23.2% |
| Net Income (after Taxes and Donations) [m=k+l] | | (104,192,494) | (55,943,103) | (42,508,168) | (52,433) | (32,421) | (24,233) | (46.3%) | (24.0%) |

Note: 2005 data has not been fully reconciled with portfolio data. Its accuracy is not guaranteed.

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

Rating Scale

| Factors | Area Rating | Global Rating | Explanation |
|---------|-------------|---------------|---|
| 4 to 5 | a | A+ A A- | Excellent The institution excels in the evaluation area 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. |
| 3 to 4 | b | B+ B B- | Good Procedures are well developed, effective, and incorporate a long-term perspective. Some improvements could be made. Long-term risks are identified in the strategic plan. |
| 2 to 3 | c | C+ C C- | Minimum required Procedures are functional but with certain failings. There are minor risks in the medium term for operations, but these risks are being managed and monitored. |
| 1 to 2 | d | D+ D D- | Insufficient Procedures are in place, but with failings, and certain problems are only partially addressed. There are medium-term risks for operations. |
| 0 to 1 | e | E | Immediate risk of default or very insufficient There are immediate or underlying risks for operations or an unacceptable under performance. |