ქრისტალი CRYSTAL
მიკროსაფინანსო ორგანიზაცია MICROFINANCE ORGANIZATION

Microfinance Between State and Market

Impact of public policies
on development of microfinance in Georgia

April 2013
Paris, France

Content

JSC MFO CRYSTAL

‘Integrity is what we do, what we say and what we say we do’

Don Galer

JSC MFO CRYSTAL

2011
First equity investment from international MIV

2007
Transformed into commercial company - JSC MFO Crystal

2004
Spin off and transformed into independent MFI - Crystal Fund

1998
Began income generation and micro-lending project

1995
Established as local non-profit organisation - CHCA

- The **Mission** of Crystal is to offer wide range of high quality financial services to micro and small entrepreneurs throughout Georgia

- Our **Vision** is to become a leading microfinance institution renowned for quality of service, an innovative business model, a cohesive corporate philosophy, a focus on regional development and a commitment to social responsibility.

- **Background in brief:**

  Established in 1995 as IDP-focused local NGO, Crystal started pilot micro-lending project in 1998 with loan capital of just $10,000. By the end of 2012 Crystal:

  - *Serves more than 17,000 active borrowers;*
  - *Manages $16.4 million loan portfolio by holding $6.5 million equity capital;*
  - *Operates a network of 16 branch offices across 5 regions of Georgia;*
  - *14 strong and reputable international financial partner organizations (MIVs, DFIs);*
  - *By holding market share of 6.3%, Crystal is among top-3 largest Georgian Non-Bank MFIs*

Crystal's Core Corporate Values

Responsibility	***Fostering responsible business behaviour in all aspects of our work including Financial, Social and Environmental objectives***
Accessibility	***Being close and accessible for our clients everywhere, focusing on regional development, sound communication and cohesive corporate culture***
Partnership	***Promoting long-term, equal and mutually beneficial co-operation with clients, staff and all stakeholders***
Transparency	***Acting transparently with all stakeholders, making Crystal a predictable and reliable partner***
Professionalism	***Adhering to the highest professionalism level, maintaining rigorous ethical standards and aspiring to continual improvement in our service delivery***

Important Achievements and Awards

"From 15 local Microfinance organizations actively operating in the market, Crystal offers the best loan conditions to its borrowers"

Independent market survey
by "ilia-uni Business Review"
Tbilisi, Georgia. March 2012.

"Crystal is socially responsible organization towards its staff, community and environment; this is based on solid foundation of respective internal policies, implemented in practice by staff"

2011 Social Audit Report
By MFC using Quality Audit Tools.
Kutaisi, Georgia. December 2011.

2003

FIRST MFI in Georgia to obtain **International Credit Rating**

FIRST MFI in Georgia to receive **International Commercial Lending**

2006

Financial Transparency Award from CGAP

2010

FIRST MFI in Georgia to obtain **International Social Rating**

2011

Winner of international Smart Campaign: Plain Language Loan Contract for clients

FIRST Non-bank MFI in Georgia to receive **International Equity Investment**

2012

Platinum Prize From **Mix-Market** for Social Performance reporting

Organizational Structure

Shareholders

Crystal Fund (founder NGO), DWM (investor), Individual shareholders

Supervisory Board

ALCO	Risk Management Committee	Social Performance Committee	Internal Audit Committee

Executive Board of Management

Credit & Operations	Finance & Accounting	Risk Management	IT & MIS	Legal Counsel	HR	Marketing & PR	Administration & Logistics

Regional Branches/Service Centers

Credit Staff	Administrative Staff	Financial Staff

Financial Services

Multi currency Loans

Start-up financing

Non-credit products

Full financial service (Cash-desk operations)

Fast disbursement and simple procedures

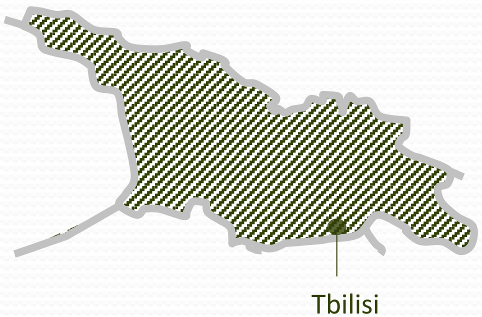
Strong commitment to International Client Protection Principles

Provision of financial services to individuals who, despite having the necessary skills, have difficulties to access traditional finances.

Service parameters:

- Loans, Remittances, Currency Exchange, Utility payment services
- Multi-currency loans for micro-entrepreneurs and agro-farmers
- Loans for existing businesses as well as start-ups
- No formal and artificial barriers/limits on purpose of the loan
- Loan size: $100 - $30,000 (focus on small loans up to $10,000)
- Pricing strategy: Market-Average
- Loan Maturity: 4-48 month; average: 12-15 month
- Loans for business, consumption, housing, education and other purpose
- Monthly repayments; grace periods are available, especially for agriculture
- No collateral requirement for loans up to $5,000
- 47% - rural clients; 50% - female
- Transparent prices, processes and procedures

Geographic Coverage



16 Service Centres throughout Georgia.

Main focus to regional micro-entrepreneurs.

95% of loan portfolio is outside Tbilisi.

60% of loan portfolio in rural and semi-urban areas

Target Market:

- Low income households
- Micro entrepreneurs, agro-farmers, start-ups and physical persons
- Remote regions and rural areas

Economic Overview

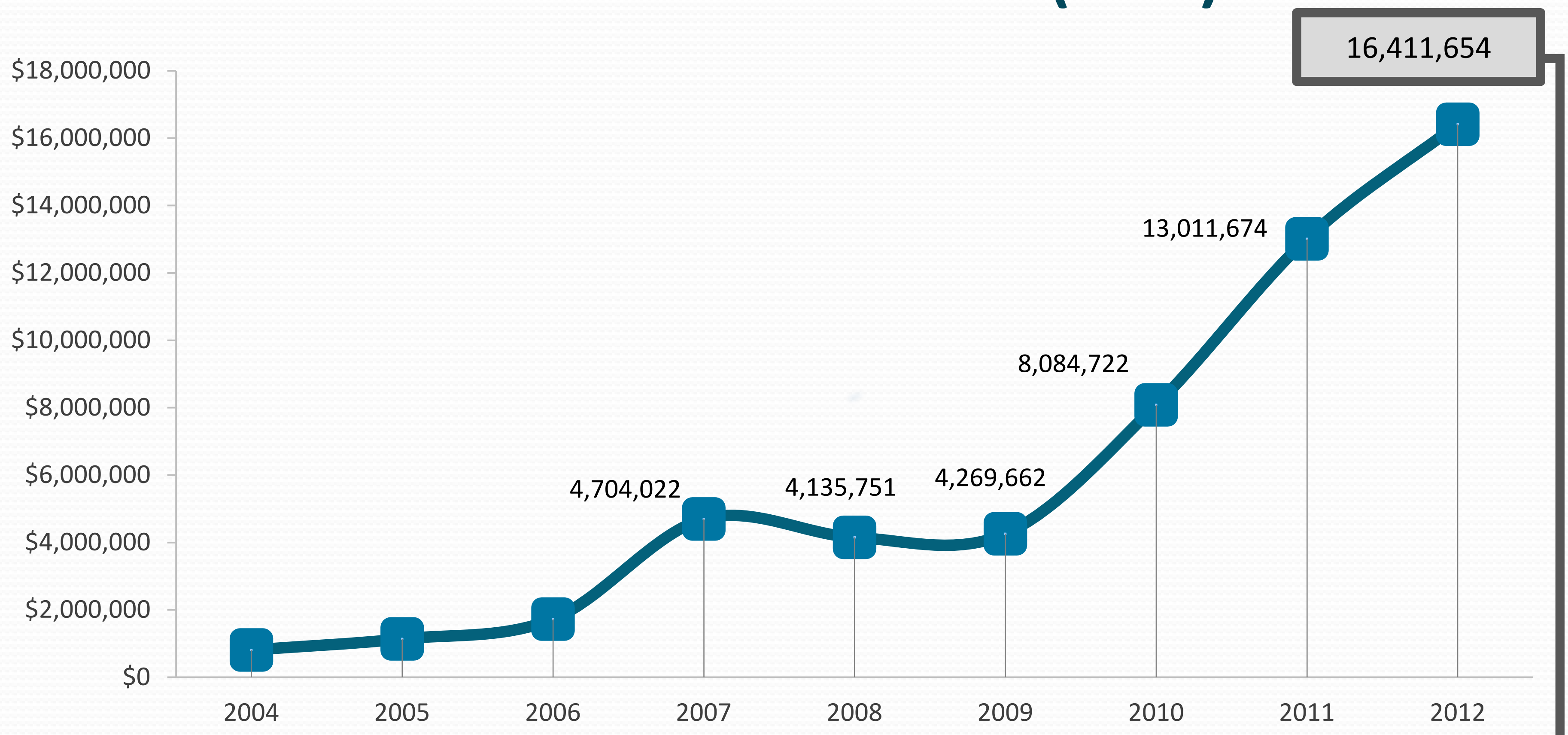
Crystal is one of the leading market players in Georgia since 2004. Recent high growth has shown competitiveness of Crystal on the market, especially in West Georgia.

One of the best and stable portfolio quality and credit risk management indicators in Georgia/Caucasus region

Providing investment access throughout the regions/rural areas means that Crystal holds the key to unlocking a largely closed portion of Georgia's economic potential.

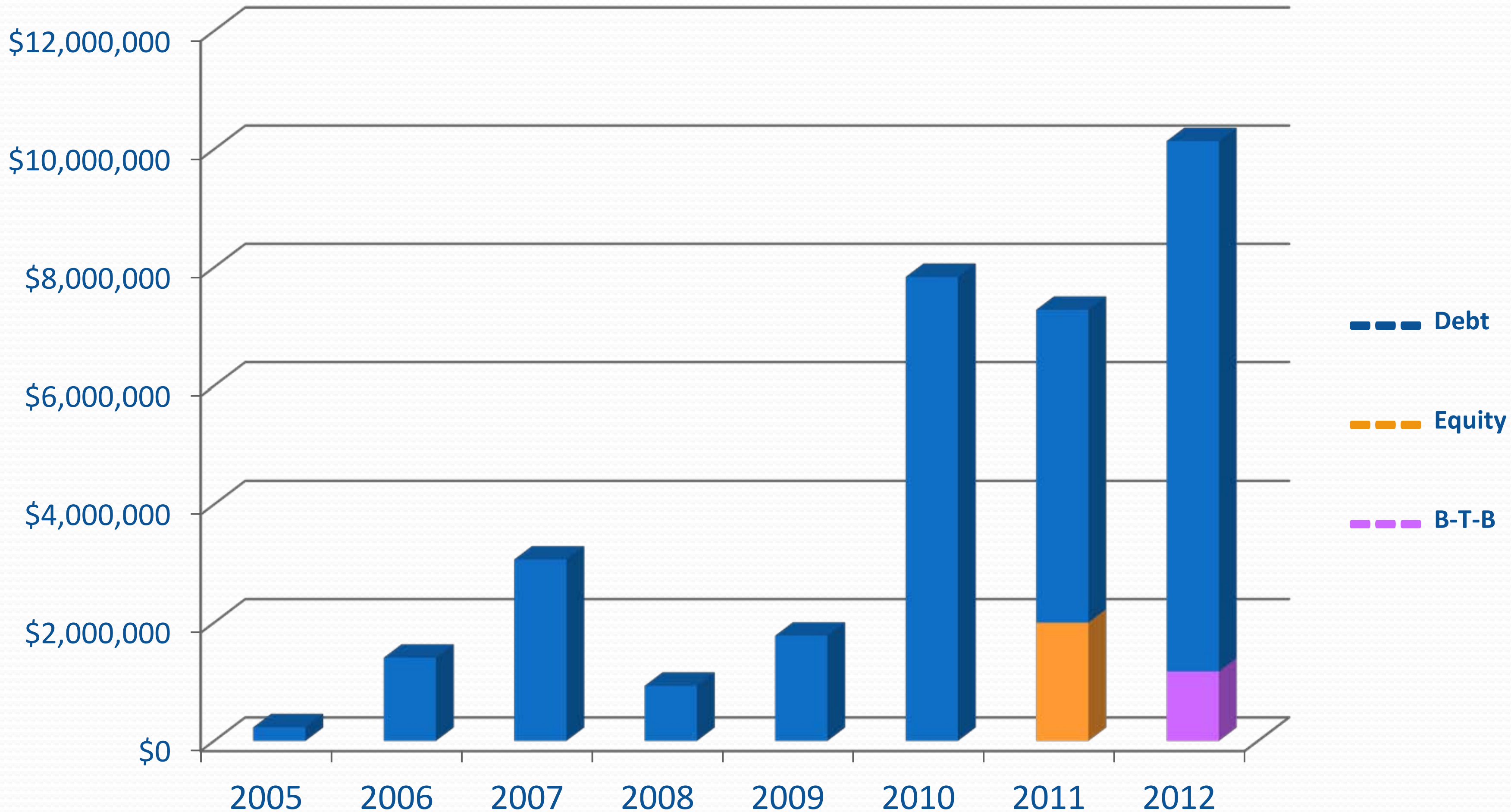
	2008	2009	2010	2011	2012
Loan Portfolio ($)	**4,135,751**	**4,269,662**	**8,084,772**	**13,011,674**	**16,411,654**
Total Assets ($)	4,701,912	5,592,366	9,172,050	15,507,284	20,455,408
Average Loan Size ($)	1,230	1,441	1,461	1,457	1,300
Rural Clients	26%	37%	42%	45%	47%
PAR>30	**1.79%**	**2.59%**	**0.34%**	**0.23%**	**0.52%**
Write-offs	0.2%	4.6%	1.8%	0.34%	0.56%
Operational Self-Sustainability	129%	118%	134%	137%	138%
ROA	8.12%	4.07%	8.10%	7.65%	7.94%
# of active Loans	**4,104**	**4,534**	**7,511**	**12,317**	**17,101**
# of Personnel	70	85	100	124	162
# of branch offices	13	14	15	16	16

Loan Portfolio Growth (USD)



A small dip experienced during times of civil unrest in 2008 has been effectively overcome, with a significant rise in the Loan Portfolio value after 2009

Funding dynamic (USD)



Funders and Partners

Strong Reputation:

Crystal is well-known in international finance market, with 14 years of successful experience in responsible microfinance and active co-operation with Financial Institutions, MIVs and Development Agencies.

Excellent Credit Record:

There was no any single fact of delays on debt repayments on Crystal's whole credit record.

Successful Fundraising:

Totally over $30 million commercial funding has been attracted in 2004-2012.

COMMERZBANK · kfw BANKENGRUPPE · Developing World Markets – Investing for Impact · responsAbility – leading social investments · incofin investment management · Oikocredit – investing in people · symbiotics – Reaching out through investments · European Bank for Reconstruction and Development · IFAD – Enabling poor rural people to overcome poverty · MicroVest – Investing in one world · BlueOrchard – Microfinance Investment Managers · Deutsche Bank · თიბისი ბანკი TBC BANK · micro CREDIT ENTERPRISES

Donors and TA providers:

- USAID; UNHCR; SV; IRC; Save the Children; Chemonics
- UNDP; IOM; PUM; CGAP; MFC; FMO; BFC; FSFM

Networks:

- Smart Campaign; MIX Market; UN Global Compact; AmCham-Georgia ; Microfinance Centre;
- Association of Georgian Microfinance Organizations; Credit-Info Georgia

Main drivers of Growth

*In 2012 Crystal obtained "**BBB**" Microfinance Institutional Rating Grade with "Stable" outlook. [Microfinanza Rating. Dec 2012]*

Extract from Crystal's 2012 Institutional Rating Report:

Crystal's profitability and sustainability is good all along the period of analysis. The company has been performing well since the crisis, showing a positive and constant growth trend.

Company has a fair responsible growth thanks to the prudent approach of the management.

- One of the best experience in regional and rural micro-lending in Georgia
- Effective business model tailored to micro and small business funding
- Active, motivated, loyal and experienced front staff
- Strong reputation both on local and international level
- Wide range of financial services, good geographic spread and distribution
- Local currency lending, start-up financing, focus on non-collateralized loans
- Well-developed infrastructure, cash-desk services, strong MIS
- Commitment to social responsibility, client oriented philosophy
- Transparent, simple and straightforward loan procedures
- Well diversified funding sources (14 international lenders and fund managers)
- Strong portfolio quality, internal control and risk management systems

Social Responsibility

<u>Some implemented Projects:</u>

Medical Assistance program to People in Need from Abkhazia and South Ossetia.

"House of Charity" for elderly people at Humanitarian Association "Catharsis".

Trust-building program among conflict-affected people, providing medical assistance to economically deprived.

Ecological project entailed cleaning of well-known botanical garden in Zugdidi

Various Social programs for disabled children in Imereti Region (Kutaisi, Tskaltubo, Samtredia).

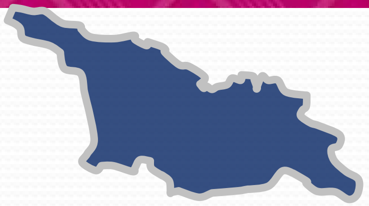
- Crystal is actively involve in implementation of various humanitarian and charity projects. Company accomplishes social activities directly itself or through partner NGOs. Budget of social fund is defined as 2%-3% of company's annual income

- Crystal identified the following target groups and priorities for its social fund:
  - *IDPs and people in need living in/around conflict zones;*
  - *Medical assistance programs;*
  - *Projects for disabled children and elderly people*
  - *Poverty elevation programs (loan guarantee fund)*

MFI Regulation in Georgia

Georgian MFI sector stimulates income generation to make clients sustainable, rather than direct poverty alleviation

Microfinance in Georgia



<u>GEORGIA</u>

Capital: Tbilisi

Currency: Lari (GEL)

Population: 4,497,600

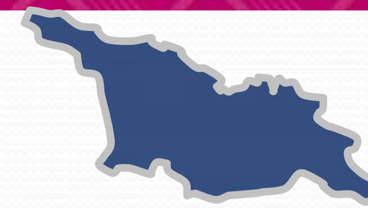
GDP per capita: $3,520

GDP real growth: 6.1%

Unemployment: 15.1%

- Development of microfinance sector in Georgia initiated in the mid-nineties by a number of local NGOs and foundations supported by international donor agencies
- ‘Light touch supervision’ regulated by the Law on Microfinance Organisations has led to a significant rise in the number of non-bank MFIs from 2007.
- MFI sector in 2012:
  - 62 registered non-bank MFIs, but only 6-7 institutions have a MIX Market profile, conducting “classical” micro-lending with some commitment to social responsibility. Crystal being one of these, having won the highest **<u>Platinum</u>** prize from MIX Market for Social Performance in 2012.
  - With market share of 5.6% of total financial sector, in 2012 Georgian Non-Bank MFIs manage: $313 million Loan Portfolio, $409 million Total Assets and around 200 thousand active borrowers
  - Competition primarily with those commercial banks providing micro and consumer loans of up to $ 10,000.

MFI Regulation



Georgian MFI Sector:

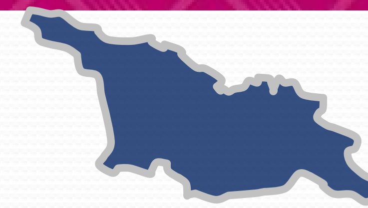
The industry demonstrated significant and stable growth in the last few years: around 60% annual growth in Loan Portfolio.

Despite global financial crisis and political instability in the country (Russian-Georgian military conflict in August 2008), MFIs total portfolio increased almost 4 times in 2007-2012.

Industry stakeholders estimate that total potential market for microfinance loans is around $500-$600 Million. This would be 2 times more than the consolidated portfolio of Georgian MFIs in 2012

- The legal status of all non-bank MFIs in Georgia is regulated by the Law on Microfinance Organizations adopted on the 18 July 2006
- The Law defines a microfinance organization as a legal entity in the form of limited liability company or joint stock company, registered on the basis of its application to the National Bank of Georgia
- The Law defines the notion and amount of micro credit: the maximum loan amount per borrower should not exceed 50,000 Georgian Lari (about $30,000)
- Clause 4/3 explicitly prohibits microfinance organizations from taking deposits from physical or legal persons
- MFIs are required to have an initial paid-in capital of GEL 250,000 ($150,000)
- The Law regulates the audit, record-keeping and reporting obligations of microfinance organizations

Permitted Activities for MFIs



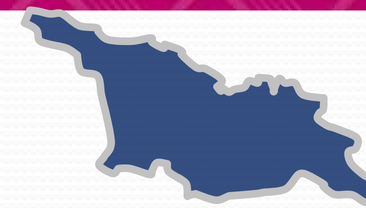
MFI Supervision:

The National Bank of Georgia (NBG) is the key regulator of the finance industry: Commercial Banks, MFIs, Insurance companies & Credit Unions.

Microfinance organizations are obliged to report to the Financial Monitoring Service of Georgia, which is the state agency responsible for ensuring Georgia's compliance with FATF recommendations concerning anti-money laundering, counter terrorism financing and other types of financial crime

- Providing micro loans to legal and physical persons, including consumer, pawn shop, mortgage, non-collateralized, group and other loans (credits);
- Investment into government and public financial papers;
- Money transfers;
- Acting as an agent for an insurance company;
- Consulting work related to micro lending activities;
- Receiving loans (credits) from resident and non-resident legal or physical entities;
- Hold shares in other legal entities which should not exceed 15% of microfinance organization's statutory capital;
- Other financial services contemplated by the legislation of Georgia, including micro-leasing, factoring, currency exchange transactions, issuance, sale and other transactions related to notes and bonds.

Main Obstacles of the Sector



Other challenges:

2008 August conflict and global financial crisis has had a negative impact on Georgia's finance sector, including microfinance.

Problems faced by sector are very similar to those experienced by the majority of countries featured in the "Banana Skins" report.

The main Banana Skins: a surge in bad loans, shortages of liquidity and funding and declining profitability

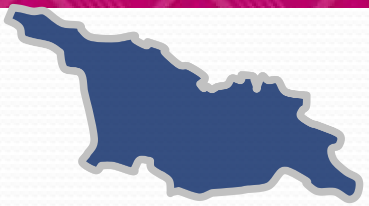
- Reputational Risk – there is no formal difference between classical MFIs and other purely commercial financial institutions (e.g. Pawnshops and private money-lenders)
- Increased risk of over indebtedness (caused by limited market size and aggressive competition from banking sector)
- Restriction on taking deposits (Banks have preference)
- Limited maximum loan size (Banks have preference)
- Loan loss reserve is not recognized as expense item (Banks have preference)
- Limited funding sources in Local Currency
- Political risks, Conflict zones, local currency fluctuations
- Lack of business experience and financial literacy in micro and small entrepreneurs

Industry Analysis

'The ability to learn faster than your competitors may be the only sustainable competitive advantage'

Arie de Geu

Key Statistics



Georgia

Budget Revenues
$3.57 bln.

Budget Expenditures
$4.42 bln.

Budget Deficit
$855.74 mln.

Average Inflation
6%

External Debt
$3.59 bln.

GDP
$12.62 bln.

Source: NBG

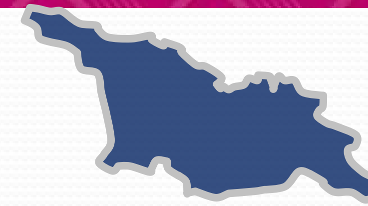
The Georgian economy is currently experiencing GDP growth higher than that of pre-crisis years, with predicted sustained growth, higher than that of most peer countries.

Georgia is one of the most promising financial markets in CEE and the CIS, with a comparatively low presence of financial institutions, signaling room for growth.

While liberal policies promote MFI development, the banking sector dominates the Georgian microfinance sector, controlling about 75% of the market.

MFIs have demonstrated resilience during times of crisis, showing stable portfolio growth and maintaining portfolio quality (at a level four times better than that of the banks).

Macro Economic Context



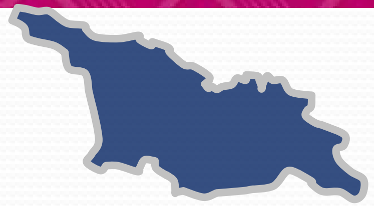
In December 2011 Fitch Ratings upgraded Georgia‘s Foreign- and Local-Currency IDRs to “**BB–**” with a Stable Outlook (from “B+” Positive in 2008).

The economy is estimated to have grown by 6% in 2013.

Source:
Fitch Ratings,
2011 Georgia Rating Report

- Georgia has become known for its pro-liberal reforms, minimal level of corruption and light regulatory environment.
- Economy is growing strongly, real GDP is set to grow by an average of 7%-8% in next 3 years. Country has a long track record of acceptable inflation level: last 3 years average inflation was around 6%.
- Georgia was placed 16th in the World Bank‘s Ease of Doing Business rankings for 2012, up from 137th as recently as 2005. Country has strong growth prospects, and its favorable business climate has attracted FDI.
- Georgia received strong multilateral and bilateral donor support following its war with Russia (in 2008) and can count on a pipeline of concessional lending until 2015

Microfinance Environment



Global Microscope on the Microfinance business Environment 2012:

Georgia suffered a significant decline in score and rank in 2012 Global Microscope study.

Dropping 12 places from 26th to 38th, Georgia's microfinance environment has deteriorated with minimal access to dispute resolution mechanisms and poor price transparency.

Source: Economist Intelligence Unit Limited 2012

Key characteristics of the microfinance business environment in Georgia:

- Funding for small MFIs remains an issue owing to a volatile macroeconomic environment and fierce competition with banks.
- The environment is conducive for organic growth with efficient (liberal) legislation and healthy demand within the micro-lending segment.
- Disclosure of interest rates is still poor, with little regulatory pressure for lenders to display hidden costs.

Key changes and impacts in last years:

- MFIs, which have many local investors/lenders, are increasingly viewed as deposit-takers. The regulator has begun investigating MFIs with more than 400 individual, local investors on the grounds that this amounts to deposit-taking.
- A broader definition of collateral has helped micro-entrepreneurs to access credit. However, strict provisioning laws on unsecured lending restrict credit flow to microfinance.
- Credit bureau coverage has reached almost one third of the adult population. However, private credit bureaus have little incentive to invest in expanding data coverage beyond commercial banking clients.

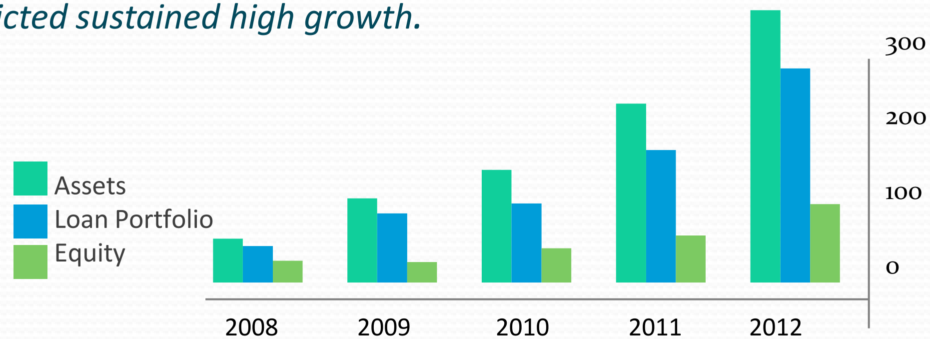
Georgian Financial Market

Institutions	2007	2008	2009	2010	2011	2012
Commercial Banks	18	20	19	19	19	19
Non-Bank MFIs	**15**	**27**	**38**	**49**	**62**	**62**
Credit Unions	24	18	18	18	18	18

Loan Portfolio ($)	2007	2008	2009	2010	2011	2012
Commercial Banks	2,883,475,682	3,595,008,900	3,076,604,656	3,531,535,082	4,633,333,404	5,258,524,480
Non-Bank MFIs	**35,719,055**	**67,598,198**	**77,179,625**	**129,473,299**	**208,745,497**	**313,006,039**
Credit Unions	605,496	824,764	910,397	884,629	1,733,335	2,945,066
Total:	**2,919,800,234**	**3,663,431,862**	**3,154,694,678**	**3,661,893,010**	**4,843,812,236**	**5,574,475,585**

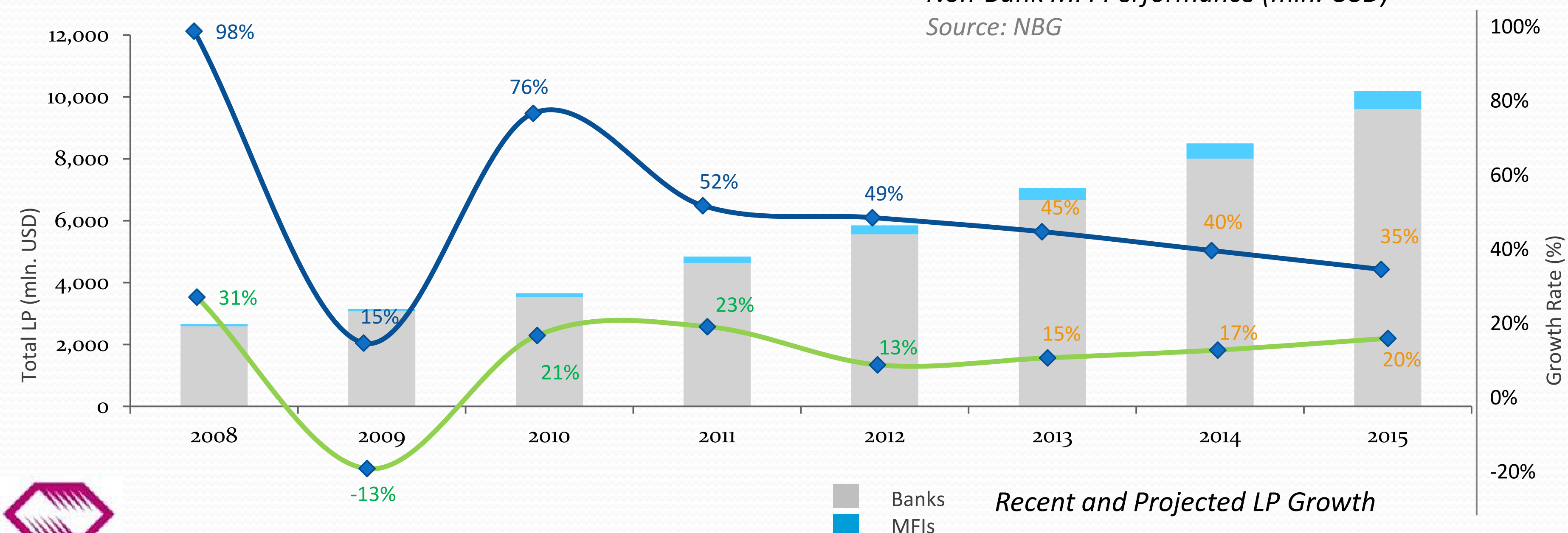
MFI's Impressive Performance

Despite the 2008 banking recession , MFIs continued to register growth in Loan Portfolio, assets and equity, followed by a rapid recovery in 2010, and predicted sustained high growth.



Non-Bank MFI Performance (mln. USD)

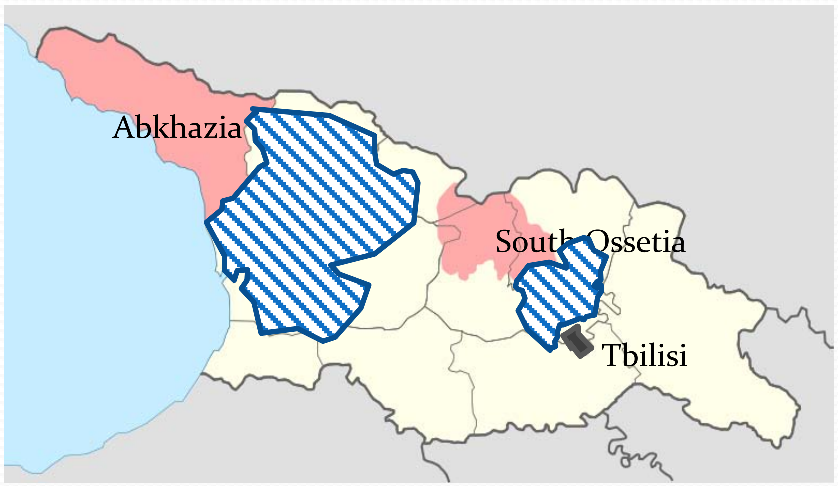
Source: NBG



Recent and Projected LP Growth

Obstacles for Growth

#1 – Conflict Zones

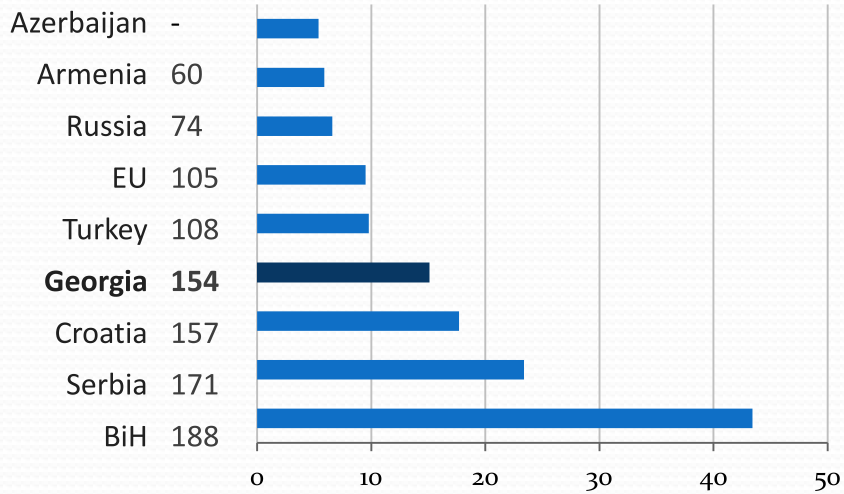


Crystal's main current target area

Conflict Zones

The presence of international organizations promote stability. In operation during the 2008 war and being predominantly located near the conflict zone, Crystal are experienced in working in a conflict environment.

#2 - Unemployment



Unemployment rates (%) and CIA world ranking

Source: CIA World Fact-book

2005	2006	2007	2008	2009	2010	2011
13.8	13.6	13.3	16.5	16.9	16.3	15.1

Georgian unemployment rate

Source: NBG, Geo-stat

Unemployment remains high, at a level of 15.1% in 2011, which is higher than in pre-crisis years. While lower than a number of Balkan states, this figure is significantly higher than neighbouring countries.

Summary

Georgia's economic development, especially in the agricultural sector, remains hindered by the 'limited access to credit and processing facilities' (FAO).

See FAO, 2011 available at: http://coin.fao.org/cms/world/georgia/en/CountryInformation.html

Potential Risks and Mitigation Tools

	High Losses	Medium Losses	Low Losses
High Probability	**Aggressive and unhealthy competition from banks** Further expansion in rural areas Stable organizational growth, offering new services	**Political risks, Stricter regulation and control** Improve MFI dialogue with NBG and policy makers Increase international presence in the sector	**Over-indebtedness, decrease in portfolio quality** Balanced growth, avoiding over-indebtedness, credit bureau Conducting regular credit rating assessments
Medium Probability	**Reputational Risk of the Microfinance sector** Improving the MFI association's capacity, Active PR in the society Commitment to responsible microfinance and social mission	**A lack of market penetration capabilities** Expansion into rural areas, focus on small size and local currency loans New regions, new products, new technologies	**Mission drift , too much commercialization** Balance in ownership structure, presence of international MIVs Commitment to responsible lending, defined social goals & objectives
Low Probability	**Macro-economic factors, High inflation** Portfolio diversification, focus on local market and agriculture Improve ALCO management and alternative financial instruments	**Frauds and daily operational risks** Improve staff motivation system, exchange of information Responsible lending, strong internal control, effective credit risk management	N/A

THANK YOU!

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