The Government of the Republic of Sierra Leone
United Nations Development Programme
United Nations Capital Development Fund

KfW Bankengruppe
CORDAID

SIERRA LEONE MICROFINANCE SECTOR DEVELOPMENT

MITAF II

JOINT PROJECT DOCUMENT

Country : Sierra Leone

Name of the Project : Sierra Leone Microfinance Sector Development – MITAF II

Joint Vision Sierra Leone 2 : Increased access by the rural poor to markets and social services, and to justice and information, in an effort to widen their economic and social opportunities

Expected effect : To have contributed to the development of 1) an inclusive financial sector that provides access to financial services to micro, small and medium enterprises (MSMEs), particularly in rural areas and 2) a greater access to market opportunities and information for MSMEs in rural areas.

Expected outputs : **At the micro level**: improved capacity and outreach of financial services providers in semi-urban and rural areas and improved availability of additional capital to partner Financial Service Providers (FSPs) in semi-urban and rural areas through appropriate instruments and linkages

At the meso and the macro levels: strengthened support infrastructure for the sector and improved regulatory environment.

National partners : The Ministry of Finance and Economic Development, the Bank of Sierra Leone, the National Microfinance Association, the Association of Commercial Banks and financial services providers.

Programme duration: 2010 - 2014

Anticipated start/end dates:
Fund management options: Parallel

Type of execution
Direct Implementation for UNCDF Resources
Direct Implementation for UNDP Resources

Total estimated budget for five years: US$ 14,770,000,000

Out of which:

1. **Funded budget** :	US$ 14 022 000
2. **Unfunded budget**:	US$ 748,000

Total estimated budget includes both programme costs and indirect support costs

Programme Financing

UNCDF:	US$	2,325,000
UNDP:	US$	1 325000
KfW:	US$	8,500,000
CORDAID:	US$	1,872,000
Funding gap:	US$	748 000
Total	**US$**	**14,770,000**

Approved by:

Government of Sierra Leone Dr. Samura W. KAMARA Minister of Finance & Economic Development	
Bank of Sierra Leone Mr. Sheku Sambadeen Sesay Governor	
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UNITED NATIONS CAPITAL DEVELOPMENT FUND
UNCDF
UNITED NATIONS DEVELOPMENT PROGRAMME

Content

ABREVIATIONS AND ACRONYMS

AC	: Advisory Committee
ACB	: Association of Commercial Banks
ARD	: Association for Rural Development
BoD	: Board of Directors
BoSL	: Bank of Sierra Leone
CEDA	: Community Empowerment Development Agency
CB	: Community Bank
EU	: European Union
FIB	: First International Bank
FSDP	: Financial Sector Development Plan
FSP	: Financial Service Provider
GDC	: German Development Cooperation
GDP	: Gross Domestic Product
CLG	: Company Limited by Guarantee
GNI	: Gross National Income
GoSL	: Government of Sierra Leone
GTB	: Guarantee Trust Bank
IC	: Investment Committee
KfW	: KfW Bankengruppe
LAPO	: Lift Above Poverty
MDG	: Millennium Development Goals
MITAF	: Microfinance Investment and Technical Assistance Facility
MFI	: Microfinance Institution
MoFED	: Ministry of Finance and Economic Development
MSME	: Micro, Small and Medium Enterprise
NASSIT	: National Social Security and Insurance Trust.
NGO	: Non-Governmental Organization
PAGE	: Promoting Agriculture, Governance and the Environment
PAR	: Portfolio at Risk
PRSP	: Poverty Reduction Strategy Paper
SLAMFI	: Sierra Leone Association of Microfinance Institutions
SLL	: Sierra Leone Leone (lawful currency of Sierra Leone)
SME	: Small and Medium Enterprise
SMT	: Salone Microfinance Trust
TA	: Technical Assistance
TSP	: Technical Service Provider
UNCDF	: United Nations Capital Development Fund
UNDP	: United Nations Development Programme
USD	: United Stated Dollar

Executive Summary

Sierra Leone, a land of 71,740 sq.km, is home to a population of 6.3 million, which grows at a rate of 3.6% per year. The population density is 76 inhabitants/sq.km. The Gross National Income (GNI) per capita (2007) is among the lowest in the world at USD 260, compared to the average of USD 952 in Sub-Saharan Africa. After three democratic elections held in the country (presidential, legislative & local), Sierra Leone has now exited from a post-conflict situation and is moving from a peace consolidation one to face development challenges.
UNDP, UNCDF, CORDAID, KfW have supported the Government of Sierra Leone to implement the Phase I of the Sector Development Program-MITAF I. Based on the evaluation of Phase I that shows important achievements: (i) Build partnership and mobilize resources (ii) Create an enabling environment; (ii) Create a supportive infrastructure and (iv) A microfinance sector with number of clients increased from 13,000 in 2004 to 123,000 in 2009 (v) Attract market leaders and (vi) Investors.

The current Phase II will include some lessons learnt through the final evaluation:

a. Financing of the microfinance sector should be more market-driven;
b. Better understand, promote and monitor overall institutional capacity within the providers of microfinance services;
c. A long time is required to build institutional capacity; this process is about people, not numbers and is often a question of changing hearts and minds.

The overarching goal of the program is to contribute to the achievement of the Millennium Development Goals, in specific the goal of cutting absolute poverty by half by 2015 (MDG 1) and promote gender equality and empower women (MDG 3).

The program will contribute to this goal within the context of the FSDP by supporting the development of a competitive and sustainable inclusive microfinance sector that provides access to financial services to poor and low-income people in general and micro and small businesses in particular with a special focus on rural areas. The project will:

- promote synergy and mainstreaming of the informal microfinance into the financial system;
- make financial services accessible to a large segment of the potentially productive Sierra Leoneans;
- promote linkages between various types of microfinance actors and the commercial banks;
- support inclusiveness of the microfinance sector (reach the excluded, quality, adapted products, affordability, consumer protection, financial literacy, social performance);
- help MFIs upgrade to deposit taking financial institutions;
- support institutional sustainability in the microfinance sector;
- assist in improving the legal and regulatory environment, with special emphasis on regulation pertaining to financial service providers (FSPs) in rural areas;
- assist in building up an appropriate support infrastructure that could take over the non financial services component of the programme that promotes innovations and training facilities.

With a total budget of 14,770,000 USD funded for 13,822,000 USD by UNCDF (2,325,000 USD); UNDP (1,325,000 USD); KfW (8,500,000 USD); CORDAID: (1,872,000 USD); (with a funding gap of 748,000 USD); and in partnership with Financial Sector Development program, the Phase II aims at its end at providing access to financial services to around 390,000 active clients from the achievement of 123,000 of Phase I.

I. Situation analysis

1.1. Background and contextual analysis

Sierra Leone, a land of 71,740 km2, is home to a population of 6.3 million, which grows at a rate of 3.6% per year and a population density of 76 inhabitants/sq.km. The Gross National Income (GNI) per capita (2007) is among the lowest in the world at USD 260, compared to the average of USD 952 in Sub-Saharan Africa. After three democratic elections held in the country (presidential, legislative & local), Sierra Leone has now exited from a post-conflict situation and is moving from a peace consolidation one to face development challenges.

Sierra Leone remains at the bottom of UNDP's Human Development Index, with 70% of the population living below the national poverty line of $ 1.25 per day, a life expectancy of 42 years of age and literacy levels of 35%. It ranks 153 out of 156 on the Gender Development Index, with women's literacy rates at just over half that of men. Under the Global Hunger Index, Sierra Leone is classified as "extremely alarming".

On May 2009, the UN Family in Sierra Leone drafted and adopted a Joint Vision for the country which had been elaborated to supersede the UNDAF. This Joint Vision defines the UN contribution to implementing the Government's Agenda for Change, to accomplishing the mandate given by the Security Council and to supporting the goals and work of the UN Peacebuilding Commission. The Joint Vision document therefore establishes the general framework for cooperation between the Government of Sierra Leone and the UN Family. The Joint Vision targets five priority areas:

- consolidation of peace and stability
- integrating rural areas into the national economy
- economic and social integration of the youth
- equitable and affordable access to health
- accessible and credible public services.

Furthermore, additional substantive synergies of activities will be achieved through six underlying programmatic issues and special considerations, one of them being the MDGs. The Government is determined to move the country away from the bottom of the Human Development Index. The UN support in the five priority areas will contribute to the achievement of the MDGs and respective programmes and projects will be assessed in light of their contribution to reaching the MDGs.

In order to achieve this goal, the GoSL and the UN Family have recognized the need for integrating rural areas into the national economy, through greater access to information, agricultural and vocational training, market opportunities, financial services, security, justice and land.

Rural development is critical to the nation's growth. The rural areas, however, face particular challenges. Poor roads and limited infrastructure result in lack of transportation, lack of information and, thus, limited market access. Moreover, the costs of financial services (fees, various extra payments) are often not transparent or excessively high.

The continuing gap between the urban and rural society of Sierra Leone remains worrying. However, with its abundant water and land resources and with about 70% of the population living in rural areas, Sierra Leone has all the preconditions not only to become self-sufficient in food production but also to become a regional food exporter.

1.2. The Financial Sector

The number of institutions providing financial services has grown significantly, with almost 40 banks, microfinance institutions (MFIs) and other programs providing some form of financial services.

The number of commercial banks has increased to 14 with the entry of a number of new banks in the last two years, particularly Nigerian banks. Several of the commercial banks have piloted microfinance schemes in the past year (Ecobank, First International Bank, Union Trust Bank) in direct competition with microfinance institutions. There are now at least 9 independent MFIs in the country: ARD, BRAC, CEDA, Finance Salone, GGEM, Hope Micro, LAPO SL, Luma, and SMT. The 23 banks and MFIs have concentrated their lending in urban areas.

In addition to the commercial banks, there are 6 community banks created by the Bank of Sierra Leone primarily serving rural populations. The number of international NGOs and donor projects providing financial services has also continued to grow.

1.3. Diagnostic of the microfinance sub-sector

The microfinance sector has several strengths as well as areas of weakness. The Table below presents a summary.

Strengths and Weaknesses of the Microfinance Sector		
	Strengths	**Weaknesses**
MACRO LEVEL Regulatory Environment	• There is no "over regulation", and NGOs are permitted to offer credit • New non-prudential guidelines for non-deposit taking institutions passed exempt these MFIs from many requirements. • New prudential reporting requirements for deposit-taking MFIs allowing BRAC and LAPO to seek such a license.	• Limited capacity – both quantitative and qualitative - of the BoSL to supervise community banks, to be further stretched with deposit-mobilizing MFIs. • Some banks interpret the banking law to state that there are limitations on non-collateralized lending • Regulations for community banks exist but there is no enforcement regarding their lack of compliance with the regulation, resulting in weak supervision • Non-deposit mobilizing MFIs must be audited if have over 100 clients – may be stringent for small institutions

Legal Environment	• Law is flexible in terms of institutional types able to offer microfinance
	• Law has no counter-productive restrictions such as interest rate caps or directed lending requirements
	• Laws are under review as part of Financial Sector Development Plan
		• Banking law
		  o prohibits exchange of information on clients, need for credit bureau
		  o Specific, appropriate regulations for community banks need be drafted.
		  o Need updates to accommodate new technology / distribution channels.
		  o Community banks fall under this law, and are treated as commercial banks
		• Land Title unclear impacting agricultural lending
		• Privatization Act does not restrict future government investments in financial institutions and banks

MESO LEVEL Infrastructure	• Audit firms trained in	• Weak MFI and commercial bank networks –

Strengths and Weaknesses of the Microfinance Sector		
	Strengths	**Weaknesses**
	microfinance • several MFIs report to the Mix Market to promote transparency	including SLAMFI and the Association of Commercial Banks (ACB) • Limited training resources available outside of MITAF
MICRO LEVEL Outreach	• Consistent growth in outreach over the past four years • Wide coverage	• Outreach to rural areas not deep • Almost no outreach to agriculture
Institutional Actors	• Range of institutional types including NGOs, NBFIs, community banks and commercial banks • New entrants with international expertise showing capacity to scale up quickly • Increasing interest among commercial banks	• Local NGO-MFIs starting to outgrow their legal structure and lack of ownership is likely to be an issue. • Traditional commercial banks showing interest, but lack capacity to offer microfinance either retail or wholesale • Most community banks struggle with basic operations and reporting, as well as sustainability
Institutional Capacity	• Capacity of new entrants to grow with adequate financing. These include Ecobank Microfinance, LAPO, and BRAC.	• Continued need for institutional strengthening in basic areas such as planning, governance, human resource management and delinquency management for MFIs and community banks. • limited capacity for innovation and new product development. • Limited exposure of commercial banks to best practice microfinance.
Financing	• Increasing willingness of MFIs and commercial banks to explore linkages • Some commercial banks expressing interest in investing in and controlling community banks	• Only one international MFI sufficiently funded to achieve its business plan. • Limited access to long-term financing from commercial banks for MFIs. This also limits funding for agriculture.
Products	• Products generally in line with microfinance methodologies, well adapted to informal traders	• Limited diversity of products • No agricultural products, and risk aversion to offering them (MFIs would like a partial guarantee)
Delivery Channels	• Decentralized lending technologies among MFIs • Low-cost branch office structure among MFIs	• Commercial banks have heavy branch structures, making it expensive to reach rural areas. • Limited linkages with rural actors

1.4. Ongoing and expected initiatives to support the sector

There are a number of initiatives implemented – or in the pipeline - to support the microfinance sector.

FSDP

Since early 2008, the BoSL has been developing a plan to restructure and revitalize the financial sector. This Financial Sector Development Plan (FSDP) is an ambitious strategy seeking which was approved by cabinet in 2009 and is going to be implemented with assistance from the World Bank, KfW, GTZ, AfDB and others:

1) to build a strong, sound and effectively functioning banking system;

2) to increase access to finance by broadening its outreach, strengthening microfinance and rural credit governance and supervision, and addressing the community banks;

3) to improve mobilization and investment of long term funds, through strengthening the contractual savings institutions and the capital market;

4) to establish an enabling environment largely in line with best international practice as a precondition for implementing a financial sector reform program consistent with Sierra Leone's long term objectives and ensuring that the implemented program achieves these objectives.

Small Business Guarantee Facility

The Ministry of Trade and Industry charged with the development and implementation of the Private Sector Development Strategy has identified access to finance for small and medium enterprises (SMEs) as a key limiting factor. It has USD 500,000 to create a partial guarantee facility in order to encourage commercial banks lending to SMEs which have insufficient collateral.

Venture Capital Fund

DFID is looking at alternative ways to promote SMEs. It is supporting a Venture Capital fund for equity investments in SMEs. The fund has met with some challenges, as culturally SME owners do not like to take on partners, but it is still in the early stages.

USAID's Promoting Agriculture, Governance and the Environment (PAGE)

This multi-faceted rural development project has a specific focus key value chains in the agricultural sector including rice, cocoa, coffee, palm, sorghum, cassava and vegetables. It plans to build on existing farmer field schools to form marketing associations. Managed by ACDI/VOCA, an organization with a track record of success in developing farmer's cooperatives, there may be important synergies for MITAF II's agricultural focus.

Ministry of Agriculture/ IFAD

The Ministry of Agriculture (MOA) also has three plans to promote rural access to finance:

1) With IFAD Financing, it is supporting the strengthening of the existing six community banks and the opening of seven new ones

2) Also with IFAD funding, it is targeting the expansion of the Financial Service Association model in more rural areas

3) It has a consultant working on the design of an agricultural development bank, which it hopes to fund with private capital. The bank would specialize in agriculture.

Splash Cash

A private sector initiative, but with important impacts that it needs to be mentioned is the Splash Cash partnership with Guaranty Trust Bank (GTB) to offer mobile phone banking services. The pilot initiated in June in urban centers, and the first service available will be money transfers.

Kiva

Kiva provides MFIs with loans using the peer to peer lending model. Its loans are in USD, but are interest free. Costs incurred by the institutions include current loss as well as the cost of placing client on the Kiva site and maintaining their information up to date. Kiva is limited in terms of loan funding to no more than 30% of outstanding portfolio and approximately USD 300,000 maximum to a single institution.

MITAF

MITAF's implementation began in July 2004 when Enterprising Solutions Global Consulting was contracted as the TSP. The TSP set up the Microfinance Investment and Technical Assistance Facility (MITAF), which enables the project to function legally in Sierra Leone under the auspices of UNDP.

Its overarching goal was to contribute to the achievement of the Millennium Development Goals – specifically the goal of cutting absolute poverty by half by 2015 by developing a competitive, sustainable and inclusive financial sector that provides access to financial services to poor and low-income people in general, and to micro and small businesses in particular. To achieve this goal, the project looked broadly at the microfinance sector from the micro, meso and macro levels. In order to build a competitive, sustainable, inclusive financial sector, the project addressed two major constraints: the absence of professional microfinance institutions to drive the development of a microfinance sector and the lack of an enabling environment shaped to optimally develop the growing sustainability and outreach of the young microfinance industry. The project addressed these issues by concentrating on four mutually reinforcing program outputs:

1) Potential leaders of the microfinance industry have reached sustainability and have considerably increased their outreach within a competitive environment.
2) Strategic partnerships are built with other donors, equity investors and commercial banks in joint support of a sustainable pro-poor financial sector.
3) A professional microfinance unit has been established in the Bank of Sierra Leone to ensure an optimal enabling environment for the development of the microfinance industry and its eventual integration into the financial system.
4) Sound microfinance principles have been disseminated and are widely accepted and adopted.

As of September 2009, the four donors had committed US$ 17.2 million in funding for the project, had approved US$ 13.4 million and disbursed US$ 11.7 million. Project funding was supporting 13 partner lending institutions as of September, 2009.

The project was slated to end on July 2, 2009. However, the donors agreed to extend the project for at least 6 months through December 31, 2009 with the possibility of extension through July 2010 if a follow-up project is not in place to ensure the continuation of services.

Potential for coordination with existing and planned efforts

MITAF II will have the advantage over its predecessor of working in an environment with various complementary efforts. This should enable it to focus very efficiently on its mandate to increase access to finance at the micro level (i.e. the financial institutions).

II. MITAF II Strategy

2.1. Background

According to both the final evaluation of MITAF and the Restructuring MITAF II report, the delivery of financial services is unevenly distributed throughout the country, as commercial banks and MFIs have concentrated their operations in and around urban centers. There seems to be market saturation in urban microcredit markets due to the large number of FSPs and the fast-paced growth in outreach. However, such saturation has to be taken prudently as it may have also resulted from the lack of product diversification. There are almost 40 commercial and community banks and MFIs providing services in a country with a population of about 6.3 million, 23 of which operate in the same urban centers. Of these, at least 16 provide microloans to poor entrepreneurs. Sector stakeholders consistently report that fierce competition for clients and increasing multiple lending is becoming their biggest challenge, contributing to problems of portfolio quality and potential client over-indebtedness.

Urban Credit Market Saturation

"The banking sector has changed drastically over the last two years. The number of commercial banks has doubled but the market hasn't grown because the economy has contracted. There has been a lowering of standards with so many banks, some who will do anything to get business. I see the potential for microfinance institutions but hope we do not end up with as many MFIs as banks." *Managing Director, commercial bank*

"We are having a harder time to get clients to repay. In the past, we could put some pressure because we were the only source of their loans. Now, we see that many clients have taken loans from other institutions and they can't manage the amount of money they have. One commercial bank actually sends people to collect their loan payments from our clients on the days they come to us for repayment." *Finance Manager, MFI*

The increasing saturation of urban microcredit markets calls for more room for financial institutions to extend services to under-served rural areas. However, the rural market faces severe constraints related to lack of adequate infrastructure, poorly diversified economic activities, which prevent financial institutions to address the financial needs of rural people. With already stretched institutional structures, most FSPs do not have the capacity to expand into such difficult rural market and there is a strong need for assistance to improve poor rural people access to financial services.

Microfinance services are more readily available in urban centers, but the rural outreach is increasing. As can be seen by the map of MITAF's outreach in December 2008, MFIs have a relatively wide reach in rural areas. The penetration, however is not that deep, in a large part because the financial products offered in rural areas are the same as urban, designed primarily for trade.

Increasingly MFIs are recognizing the limitations of their product range. As competition is starting to be felt in Freetown, and institutions start to reach deeper into rural markets, several institutions are looking for ways to serve agriculture in particular.

All local MFIs note that they do not have in-house capacity for research and development, and find this to be an area where investments will be needed in the future to build capacity. Only BRAC has the capacity to research and develop products.

As for rural (non-agriculture) microfinance, both community banks and MFIs are covering this market, and there is limited though rising interest by commercial banks (e.g. Ecobank) to offer retail products at the microfinance level. New entrants, such as BRAC and LAPO have deliberately prioritized the rural areas and expect to expand their outreach considerably over the next five years (combined target of 96,000 clients). MFIs need technical support to design and test new products and to manage a large branch expansion to reach these areas more effectively. Similarly to the urban areas, financial instruments are needed to facilitate financial linkages between commercial banks and MFIs as well as between productivity-oriented value-chain approaches and MFIs.

Access to finance appears to be one of the challenges faced by MFIs. The MFIs on average have invested 80% of their assets in loan portfolio, and only 13% available in cash and short-term investments. Growth, therefore, will require additional financing.

The financial infrastructure to support microfinance institutions is relatively weak. There is no credit bureau, though over the past six months growing competition in the cities is increasing the need for one. The Sierra Leone Association of Microfinance Institutions (SLAMFI) remains an informal body, which has yet to become active in defining its mandate or offering support to its members. Audit firms, trained in CGAP standards, are improving, but continue to leave some important gaps in their analysis. Local training services are not strong enough to offer value added to the larger MFIs.

The capacity of the Central Bank to conduct effective off- and on-site supervision is still weak. The Financial Sector Development Plan (FSDP) seeks to address this by i) recruiting one or two long-term technical advisors for at least a two year period; and ii) drafting and implementing a training program for departmental staff in risk-based on-site and off-site supervision. Staffing capacity will also be strengthened. In order to ensure that the capacity of the banking supervision is not too stretched, it will focus on deposit-taking institutions and NASSIT.

2.2. Lessons learned from the final evaluation of MITAF[1]

Overall MITAF is considered a success by following criteria: (i) it moved financial services out of the government to independent financial institutions; (ii) it provided a joint platform for a coordinated donor approach; (iii) it introduced microfinance best practice to Sierra Leone based on the CGAP principles; (iv) it turned around the microfinance concept from charity to sustainable services; and (v) it attracted the interest of commercial banks to venture into rural and microfinance services and hence contributed to facilitating an inclusive access to finance. For this purpose BoSL and the sponsoring donor organizations expressed mutual consent to consider a second phase of MITAF (MITAF II) in order to continue promoting the microfinance industry of Sierra Leone respectively its ultimate target group of low income

[1] See Annex 1: Key results, findings and lessons learned from the final evaluation report of MITAF

population as well as micro and small enterprises. Some of the key lessons that emerge from the MITAF project are:

It is important for donors to set a clear focus and emphasis of the project and expected results. In other words, donors should clarify the type of financial services to be promoted, where the services are to be promoted (Urban? Rural? Both?), and in light of this, whether the existing service providers are likely to be able to deliver on donor expectations.

It is important that financing of a microfinance sector is market-driven. Project objectives and targets need to be based on valid and realistic assessments of the absorptive capacity of the market, both at the customer and the service provider level. As markets develop, it should be incumbent on project funders and managers to continue to monitor the effect of funding on growth in outreach, to ensure that market over-saturation does not occur and that service provider capacity is not surpassed.

It is imperative to understand, promote and monitor overall institutional capacity within the providers of microfinance services. When project incentives promote increasing outreach while expecting growing levels of cost-recovery, but the project provides little operational subsidy and does not set clear and measurable expectations about institutional capacity, long-term institutional sustainability is likely to be compromised.

It takes a long time to build institutional capacity; this process is about people, not numbers and is often a question of changing hearts and minds. It is a process that works most effectively when it is demand-driven. Assistance provided "for" rather than "with" is much less likely to be adapted by the recipient institutions. Further, it cannot be expected that all institutions will be able to take advantage of capacity-building assistance regardless of its quality; such institutions should not be able to access continued funding that would help expand their portfolios.

2.3.The joint project

Project Goal

The overarching goal of the program is to contribute to the achievement of the Millennium Development Goals, in specific the goal of cutting absolute poverty by half by 2015 (MDG 1) and promote gender equality and empower women (MDG 3).

Project Objective

The program will contribute to this goal within the context of the FSDP by supporting the development of a competitive and sustainable inclusive microfinance sector that provides access to financial services to poor and low-income people in general and micro and small businesses in particular with a special focus on rural areas. The project will:

- promote synergy and mainstreaming of the informal microfinance into the financial system;
- make financial services accessible to a large segment of the potentially productive Sierra Leoneans;
- promote linkages between various types of microfinance actors and the commercial banks;
- support inclusiveness of the microfinance sector (reach the excluded, quality, adapted products, affordability, consumer protection, financial literacy, social performance);

- help MFIs upgrade to deposit taking financial institutions;
- support institutional sustainability in the microfinance sector;
- assist in improving the legal and regulatory environment, with special emphasis to regulation pertaining to financial service providers (FSPs) in rural areas;
- assist in building up an appropriate support infrastructure that could take over the non financial services component of the program, which promotes innovations and training facilities.

Project Strategy

Implementing MITAF II, the Technical Service Provider, hired by the funders (CORDAID, KfW, UNCDF and UNDP) through a tender process will establish and manage a company limited by guarantee pursuant to the Companies Act 2009 of Sierra Leone ("MITAF II CLG"). Its services, operations and licensing requirements will fall within the purview of the Other Financial Institutions Act 2001 of Sierra Leone. The donors and UN agencies (i.e. UNDP and UNCDF) will not be part of the CLG. However, they will be members of the Investment Committee which will take decisions on the funding proposals prepared and presented by the TSP. The IC decisions will be binding for the CGL and the TSP.

The Funders will pool their funds earmarked for the MITAF II program ("MITAF II") to an account opened by the TSP in their joint name at a commercial bank in Sierra Leone acceptable to the Donors and subject to the terms and conditions to be set by the Donors. The use of the funds will be governed by the decisions taken by the Investment Committee.

MITAF II will expand its focus from primarily MFIs to cover the full range of eligible banks, non-bank financial institutions, cooperatives and specialized finance institutions which reach out to the target group. Simultaneously MITAF II shall expand the semi-urban and rural outreach of the financial intermediaries by supporting small business finance, agricultural finance and encouraging microfinance innovations. MITAF II will also collaborate with existing and upcoming programs and initiatives for promoting access to finance.

MITAF II will structure itself into a "Refinance Facility" with financial instruments (which expect a return and can eventually become a sustainable funding source) and a "Non-refinance Facility" offering subsidies in the form of grants and technical assistance on a cost-sharing basis. Financial instruments - such as loans – will be clearly divided from non-financial instruments - such as grants for the purchase of basic equipment and for technical assistance.

Sector Wide Approach

MITAF II will maintain the sector wide approach but mainly focus its activities on the micro- and meso-level in order to ensure maximum efficiency, as the macro level is being substantially addressed by the FSDP. It will address the macro level to the extent that such intervention is considered crucial for the micro level and is not adequately addressed by other donor programs or government strategy, mainly FSDP[2]. The Financial Sector Development Programme has four major pillars:

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[2] Sierra Leone: Financial Sector Development Programme, June 2009.

a) Banking: "The FSDP addresses banking objectives in five major areas, i.e. a) building banking sector capacity; b) strengthening banking supervision and regulation; c) strengthening payments systems; d) strengthening short-term financial markets, monetary policy and financial system stability; and e) strengthening central bank infrastructure.

b) Access to finance: by strengthening microfinance and rural credit governance and supervision, broadening its outreach, and addressing the community bank dilemma. It is our view that conducting a significantly large successful outreach program depends heavily on launching it from a sound legislative, regulatory and governance foundation and utilizing sound, robust, reasonably well managed institutions.

c) Strengthening contractual savings and capital markets.

d) Strengthening the enabling environment and capacity building: by focusing on establishing an appropriate legal framework, including those aspects relating to the debt recovery and land-related issues. We will also address other enabling environment issues including education, training and communications capability, and establish a high profile, focused FSDP structure and process to ensure that all key stakeholders have a voice and that the FSDP strategy and its actions are implemented largely as envisaged and scheduled.

The FSDP-MITAF II programme is in line and in synergy with the FSDP, by largely covering the pillar "Access to finance" while contributing based on the gaps to be filled to the implementation of the other pillars mainly through the improvement of the enabling environment, the strengthening of the financial infrastructure and the promotion of savings.

Use of Resources:

UNDP resources will be used exclusively for capacity building and UNCDF resources mostly will be used for capacity building but also for refinancing. CORDAID resources will be used mainly for refinancing according to the distribution (p. 24) whereas KfW money will be utilized for both capacity building and refinancing.

Demand

The partners agree that pushing credit delivery and pumping too much funds into the microfinance market must be avoided under MITAF II. Therefore, a proper demand analysis, a sound incentive system for the TSP and well-defined indicators are critical. In that respect, a conflict between outreach targets and capacity building targets should be avoided in the TSP activity.

This issue of demand will clearly and in priority be addressed by the TSP mainly in designing its 5-year Plan. In addition, ratings will be carried out on promising FSPs of phase I and be a criteria for any support in Phase II. This rating will constitute a way of grounding a tailored support based on clear identified needs and will be a baseline against which progress induced by our support will be measured. Moreover, savings promotion as well as focus on rural areas will help also dealing with urban credit led market saturation identified by the evaluation as an important issue.

Rural areas: The support to underserved clientele mainly in rural will support i) innovations in reach out in rural areas; "ii) linking rural lending with specific market opportunities like out grower schemes; ii) linking banks and MFIs thru equity participation, guarantees & improved credit risk assessment; iii) designing and funding a program to increase savings by small savers such as V S &L; iv) putting major emphasis on the introduction, promotion and implementation of mobile telephone banking; and v) supporting mobile payment systems" (FSDP).

Current other initiatives and Coordination:

The programme will coordinate with the Financial Sector Development and its results are included in achieving the objectives of the FSDP as explained in the strategy. In addition, synergies will be developed with other important initiatives that will have or could have impact on the programme are:

- Remittance: Sierra Leone is a pilot country;
- TECHMIFA: Sierra Leone is included as one of the potential next country to be supported by this important capacity building set up mainly with Spanish funds with the participation of AfDB managing the coordinating unit and UNCDF contribution.
- MicroLead: Through this global initiative supported also by Gates Foundation, UNCDF has supported BRAC. The reporting of BRAC will be done through the programme, ensuring thus coordination and accountability regarding results to be achieved.
- Remittances Pilot programme.

Exit Strategy (see below also).

In order to have a long-lasting impact, the programme will seek to transfer its non refinance function to strengthened national facilities. However, the transfer of the resources regarding the not used resources or the outstanding portfolio for the refinance component will be decided in due course by each participant investing in it, based on a thorough evaluation and the perspectives designed by the TSP after three years.

Component 1: Promotion of sustainable access to appropriate financial services by a large segment of the productive Sierra Leoneans, with special focus on semi-urban and rural population and women.

This component will have two sub-components:

Non-refinance window: This sub-component will emphasize financial services providers' capacity strengthening (both human and technical) mostly in semi-urban and rural areas, the development of innovative financial products for rural and agriculture needs, the promotion of rural extension of financial services providers operating in urban centers, the promotion of appropriate financial products and services for women and the promotion of synergy and mainstreaming of the informal microfinance into the financial system.

As in MITAF I, grant funding would be set up on a competitive basis – as a challenge fund to which institutions need to apply. Proposals can include the need for financing basic equipments and/or technical assistance. Some of the institutions with international networks are able to source their own technical advisors. Other institutions will likely rely on MITAF II to identify the advisors / consultants to support their work. Two non-financial approaches will be implemented on a cost-share basis and for the following purposes:

- *Purchase of basic equipment:* Grants will be used for, fixed assets or specific projects for innovations or introduction of social performance monitoring. Banks may also be considered if they wish to reach the poor in rural areas, not only for savings mobilization, but also for extending loans and other financial services.

  Innovation and special project grants will not be limited to fixed assets. The cost of introducing the innovation or expansion should be able to be presented as a specific project, which MITAF II will fund. This implies exceptional funding of operational, technical support and fixed asset costs for these specific projects.

- *Training*: Given the recognized impact of trainings, MITAF II plans to offer them on a cost-share basis. The trainings will focus on the sector requirements, which today appear to be primarily in the areas of governance, financial management and product development. It will work with larger MFIs to develop in-house training capacity on basic things such as loan officer training. If a training center is created, MITAF II will conduct trainings through this institute in order to build local capacity. Local FSPs will continue to be the major participants in trainings, though some banks may start to send staff. The training support will also aim at linking with academia and local trainers to develop local training capacity. The clients may benefit from other support for Business development services.

<u>Refinance window</u>: This sub-component will extend additional capital to partner FSPs through diverse instruments including loans, guarantees, quasi equity and promote linkages between various types of microfinance actors and commercial banks.

1. <u>Loans</u> will be provided to FSPs (qualified MFIs, community banks and other providers of financial services excluding commercial banks) in need of long-term funding to serve their rural and agricultural clientele. MITAF II will explore the possibility to cooperate with Kiva on microfinance loans to agriculture, as Kiva could take a senior loan position on riskier portfolio.

2. <u>Partial guarantee facilities for refinancing of MFIs</u> will be offered as "borrower" guarantee facility. This implies that the FSP seeking funding from a commercial bank will request a guarantee facility. MITAF II will perform due diligence on the MFI. Once approved, the MFI can use the guarantee facility as collateral in negotiations with the bank or banks of its choosing. The coverage of the risk will be partial and declining. The guarantee will seek the leverage effect.

3. <u>Quasi-equity in the form of subordinated debt</u> for those privately owned MFIs which require *additional capital in order to increase their equity, and demonstrate a sufficient return.* Many MFIs remain NGOs. This institutional type should not be eligible for this type of loan. Target group will be qualified privately owned FSPs

Component 2: Strengthening the support infrastructure: For meso level, the specific objective will be to strengthen the infrastructure to support microfinance institutions. Emphasis will be put on developing tools for improved information flow among MFIs, capacity building of audit firms, and developing local training institutions to provide appropriate services to MFIs on a sustainable basis.
This sub-component will assist the structuring and strengthening of suitable partners at the meso level (e.g. universities, training centers, associations…) through the provision of equipment, technical assistance, a procedures and policy manual, diffusion of best practices to its members, training of staff, field visits, etc.

The sub-component will also help implement a critical mass of local technical service providers in such areas as: business planning, MIS, accounting, financial analysis. The project will assist in preparing appropriate training material and diffusion to the staff of the partner local service providers and the strengthening of selected training and support institutions.

This sub-component will also continue the role performed by the preceding program in data collection and dissemination. The sub-component will assist in building such capacity into an eligible institution so that the collected information could be used effectively if it were to create a simple newsletter and send updates to investors, the microfinance gateway and other resource in order to expand the information about Sierra Leone and encourage investment.

To the extent possible – and provided that this is not addressed by the FSDP - the project will assist in the implementation of a credit bureau that will collect and disseminate credit information among the MFIs. Therefore, the partners will explore partnerships with institutions having expertise in the field of credit bureau; however, the decision will be taken in due course by all partners with a leading role played by BoSL. In that framework, the current discussions between UNCDF and IFC will be taken into account

Component 3: Improving the regulatory environment.

For the macro level, this component will limit its activities to supporting continued reforms of microfinance regulation, as the FSDP will take care of most of the supervision aspect. This approach will be implemented provided that the other measures required improving the legal and regulatory framework for the microfinance be supported by the FSDP. The sub-component will continue to assist in shaping of regulatory environment conducive for integrating the microfinance sector into the financial system and disseminate policies for microfinance institutions. This sub-component will also promote financial literacy and client protection. Many funders, including UNCDF, are engaged in the client protection campaign. The supported FSPs through MITAF II will also be informed of that campaign so that they can apply the principles.

Component 4: Program management.

MITAF II will be structured as a company limited by guarantee with a trust account approach set up and managed by a TSP. In other words, MITAF II will be incorporated as a guarantee company without shares in order to have a legal identity according to the laws of Sierra Leone. The sponsoring funders will contract a consulting company to act as a TSP for MITAF II including the authorization to manage their funds along MITAF II objectives and principles, based on the decision made by the Investment committee including all the funders and functioning outside the CLG. The donors as well as UN agencies (UNDP and UNDP) will not take part to the CLG. However, they will be the members of the Investment committee. The IC decisions will be binding for the CLG and the TSP.

This component will support the management of the program, i.e. the TSP to be selected through an international tender. The TSP will have the responsibility to manage all aspects of the project, through a signed performance-based contract between KfW representing all participating donors and BOSL respectively. The TSP will enjoy two particular entitlements: (i) to manage and administer the funds pooled by the sponsoring donors; and (ii) to contract on behalf of the sponsoring donors and BOSL respectively MITAF II services to MFIs. The component will fund the following activities:

- Establishment of MITAF, company limited by guarantee
- Establishment of systems and procedures, and drafting of respective manuals,
- Establishment and implementation of an adequate MIS and a transparent and efficient accounting system,
- Hiring, training and supervision of required professional and support staff,
- Production of an initial 5-year business plan for approval by the Advisory Committee,
- Submission of an Annual Work plan and budget for approval by the Advisory Committee,
- Management of the performance based agreements and monitoring of the investments,
- Reporting to the Advisory Committee and Investment Committee in regular intervals,
- Preparation of meetings of the Advisory Committee and the Investment Committee,
- Provision of the necessary equipment and logistic support to the staff of the PMU,
- Implementation of an appropriate M&E system,
- Efficient and transparent management of the funds.

2.4. Results

Overall, in addition to its support at macro and meso level, as it will be detailed in the Resources and Results Framework, the Project will help achieve the following quantitative results by 2014:

- 390,000 active clients including 150,000 savers and 240,000 borrowers; if we take the total budget of 14,770,000 $US, the cost to serve a client is: 38 $US; the total number of active clients represent three times the achievement in phase I of 123,000 (evaluation); 50% of the clients will be women.
- The projected outstanding savings balance is 14.8 M $US thus 1.6 times the 2010 baseline.
- The projected outstanding loan portfolio is 19 M $US thus around 2 times the 2010 baseline.
- The percentage of semi-urban/rural represents 53% of active clients compared to 33% in 2010; 65% of rural borrowers compared to 45% in 2010 and 54% of rural savers compared to 34% in 2010;
- 6 FSPs applying good principles (CGAP), 2 times the baseline in 2010;
- 6 FSPs applying financial self-sufficiency thus 3 times the baseline in 2010.
- The leverage of the funds will be as follows:

Funders	UNCDF	UNDP	KfW	CORDAID	Total funded budget
Resources in $US	2 325 000	1 325 000	8 500 000	1 872 000	14 022 000
Indirect leverage of UNCDF funds without funding gap	6	11	2	7	
Indirect leverage of UNCDF funds w/ funding gap	6	11	2	8	
Leverage of UNCDF funds without funding gap and with savings	12	22	3	15	
Leverage of UNCDF funds with funding gap and savings	13	23	4	16	

These results do not include the following expected achievements from BRAC as included in the agreement signed with UNCDF global Microlead programme 127 236 active borrowers including 72 563 active savers. The TSP workplan approved by the Investment Committee will determine the final results to be achieved against which the project will be evaluated.

2.5. Sustainability of results

The Refinance component

In case a decision is taken against a further extension, the Refinance component will be liquidated. Loans outstanding beyond the implementation period of MITAF II may be collected by the TSP subject to a contract addendum corresponding to the expected level of effort or a contract with a chartered accountant for such purpose. The net liquidation proceeds of the Refinance component shall be distributed on a pro rata basis as follows:

- The KfW share shall be returned to the BOSL. BOSL shall decide on the subsequent deployment of the funds in coordination with KfW;
- CORDAID shall retrieve its share and re-transfer it to its headquarters.

In case a decision is taken in favour of continuing the MITAF services, the Refinance-Component of MITAF II may be transformed into a for profit company thereby opening up also to commercial shareholders. Since the Refinance component shall be organized and governed along commercial business and efficiency principles, it may be fairly easily transformed into a formal financial institution and fully licensed for this purpose if so desired. The institutional transformation of MITAF II would take place through an asset transfer to a company newly established and licensed for this purpose. The asset transfer will be carried out in exchange for an equity participation of the sponsoring donors proportionate to their respective capital contributions, subject to the approval of each individual donor. The new company would also take over the relevant staff previously hired and trained by the Manager and also incorporate already established and market tested products as well as systems and procedures.
The sustainability of the results will be also guaranteed by the (i) improvement of the legal and regulatory framework and by the enhanced capacity of the central bank to perform its supervision roles; (ii) the

strengthening of the local facilities to provide long lasting support to the sector in capacity building and developing human capability of the FSPs (iii) by the sustainability of 6 FSPs and the application of international standards of 6 FSPs ensuring thus an increased and sustainable supply of financial services and (iv) developing linkages with the local financial markets.

The Non-Refinance component:

The success of MITAF II's Non-Refinance component will be measured by its impact on launching a broad based expansion and upgrading of the country's microfinance sector through MFIs' improving their technical capacity, expanding into rural areas and implementing innovative financial products. However, small MFIs - especially those operating small scale and in rural remote areas – will expectedly remain incapable of financing comparatively expensive technical assistance or expensive equipment. To the extent possible, MITAF will coordinate with other locally owned initiatives to encourage the sustainability of the technical resources. In this regard MITAF II will collaborate with existing relevant and suitable meso level institutions to transfer training capacities and to take on the information compilation and dissemination role.

For both Refinance and Non-Refinance components, the TSP will in due course (e.g. after 3 years) be required to submit alternative proposals which address all relevant aspects of offering MITAF services on a sustainable basis beyond its implementation period including the treatment of the program assets.

III. Results Framework (2010 - 2014)

Result 1: Sustainable access to appropriate financial services is available to a large segment of the productive Sierra Leoneans, with special focus on rural population and women.

Expected output 1.1: Improved capacity and outreach of financial services providers in semi-urban and rural areas

1. assessment of the human and technical capacity needs for FSPs (MFIs, Community banks, commercial banks, other non-bank financial institutions) implemented – or willing to implement – in rural areas (conduct a diagnostic of their strengths and weaknesses to identify areas that need support);
2. have a rating report on each applicant prior to the discussion of the proposal within the IC;
3. provision of training sessions for target staff of FSPs through available training programs locally and abroad in governance, financial management, etc.;
4. provision of logistics and equipment support, including motorcycles, safes, computers, MIS software, generators, etc.;
5. provision of technical assistance – both short term and long term – to help FSPs in business planning, processes and procedures, internal control, delinquency management, governance issues, client protection principles, social performance monitoring etc.;
6. provision of assistance in market research and innovative product development to rural operating FSPs to better address the actual needs of the target beneficiaries (loans, savings, money transfers, micro insurance, agriculture financing, etc.); assistance will include needs assessment on the part of the target population (both women, farmers, other rural active population), identification of training institutions in market research for microfinance for staff of FSPs, hiring of consultants to help in new product design, testing and implementation;

7. study tours for FSPs staff in neighboring countries to have them better familiarize with best practices and experience in building sustainable institutions.

Expected output 1.2: Improved availability of additional capital to partner FSPs in semi-urban and rural areas through appropriate instruments and linkages

1. assessment of the financial gap in rural and semi urban areas and types of financial instruments needed;
2. completion of a study on how to promote linkages between commercial banks and MFIs and community banks working with the rural population;
3. promotion of savings mobilization among FSPs through the following actions: identification of the savings potential of rural population, assistance in implementation of appropriate channels and products for savings mobilization, monitoring system;
4. provision of long term loans to qualified FSPs to serve the financial needs of rural micro entrepreneurs, women and farmers;
5. implementation of a partial guarantee facility to serve as a collateral for eligible MFIs and community banks in order to promote commercial banks lending to microfinance sector;
6. implementation of partial guarantee facility for agricultural lending to promote increased lending to farmers by rural operating FSPs;
7. implementation of quasi-equity instruments for mature FSPs to help them increase their lending capacity in addressing the needs of the rural population.

Result 2: Strengthened support infrastructure

Expected output 2.1: Strengthened support infrastructure for the sector

1. assist in structuring and strengthening the institutions and networks at the meso level in policy dialogue, advocacy, credit and savings culture, etc.;
2. design a capacity building program and provide in- and off-country training courses to key personnel;
3. provide equipment support to eligible institutions / networks as well as technical assistance in setting the procedures; structuring its governance;
4. assist the institutions / networks in data collection from the FSPs and information dissemination among FSPs through bulletins, etc.;
5. design and provide training sessions to selected audit firms in inclusive finance and CGAP best practices to equip them with the capacity to serve the sector;
6. help design and implement a credit bureau to ease credit information flow among the FSPs;
7. assist in the implementation and training of a critical mass of local technical service providers: training centers, consulting firms, etc. in partnership with CGAP through workshops and seminars;
8. participate jointly with the FSDP in providing the training material and certified microfinance trainers for the eligible institutions / networks.
9. Link up with academia and local technical service providers to set up local training facilities and mechanism in support to capacity building development of the sector.

Result 3: Improved regulatory environment

Expected output 3.1: Improved regulatory environment

1. assist in structuring the microfinance supervision unit within the BoSL;

2. assist in structuring the microfinance promotion unit within the Ministry of Economic development;
3. disseminate information and assist FSPs to comply with the registration and licensing requirements of the BoSL;
4. design a strategy for the community banks in coordination with IFAD and improve their supervision;
5. disseminate new policy guidelines for FSPs;
6. assist in revitalizing the microfinance sector database implemented by the current program;
7. support the FSPs to comply with the legal and regulatory framework;
8. support the supervision capacity and ensure that the sector is properly supervised.

Result 4: The program is implemented and managed properly

Expected output 4.1: the TSP is recruited and the company limited by guarantee is registered, licensed and operational

1. identify and select the TSP through a tender process;
2. sign with the TSP a performance-based contract;
3. assist in the creation, registration and licensing of the company limited by guarantee;
4. assist in setting the IC, AC and the company the governing bodies;
5. TSP to design and implement procedures manual;
6. provide equipment and logistics
7. ensure the proper functioning of the IC, AC and the company governing body;
8. ensure a good quality of the investments to achieve the expected results in outreach and sustainability;
9. .Ensure a proper monitoring of the investments by taking the right measures against FSPs not achieving their contractual results.

Expected output 4.2: the M&E system is in place

1. finalize the M&E framework;
2. organize field missions to familiarize FSPs and other partners with the M&E system;
3. organize periodic monitoring sessions;
4. Set up clear mechanisms to collect, analyze and present data quarterly
5. Ensure FSPs reporting to Mix Market;
6. Ensure a proper reporting quarterly;
7. undertake the MTR and the final evaluation.

Please, refer to Annex 2 for The Results and Resources Framework Table.

IV. Management and Coordination arrangements

MITAF II's strategy, policy and operations will be harmonized with other donor interventions relevant to the FSDP and target group support in order to ensure maximum efficiency. MITAF II will operate as a company limited by guarantee duly registered and licensed in Sierra Leone set up and implemented by a TSP hired through a tender process. Regarding the UN agencies, this is similar to NGO modalities.

The coordination will be done mainly with other FSDP activities by a clear delineation of roles and responsibilities mainly at macro level including the support to BoSL, as explained in the programme strategy (see above).

MITAF II will build on the current governance structure of MITAF, which has been refined, market tested and mutually accepted over the past years. MITAF's current governance structure offers a platform for sector dialogue between relevant players of the GoSL, the donors and the MFIs and by the same token also exercised strategic guidance and control of the TSP. MITAF II's principle governance bodies will be (i) the Advisory Committee; (ii) the Investment Committee; and it will be managed by the TSP. The AC and the IC are additional bodies outside the formal legal structure of Company Limited by Guarantee.

General Principles: The members of the Advisory and Investment Committee will continue abiding to the following principles: transparency; independence and objectivity; responsibility; adherence to microfinance best practices[3] , consideration of the national priorities for microfinance[4]. None of the members of the Advisory Committee or the Investment Committee will receive remuneration in return for their services. The members of the AC and the IC should be trained in microfinance or finance and have the technical expertise to take decisions on the sector.

Advisory Committee

Composition: The Advisory Committee will reflect a proper representation of the country's microfinance industry at all macro, meso and micro levels. It will be chaired by the Governor of the BoSL and shall consist of one representative of each of the following organizations: BoSL, MoFED, the ACB, and SLAMFI, in addition to the members of the Investment Committee (see below). The TSP will serve as the Secretariat to the Advisory Committee.[5]

Meetings and Voting: The Advisory Committee will meet at least twice a year, either in person or by phone. Each member will have one vote. All decisions will require at least 66% of the votes of the attending members (supermajority principle).

Responsibilities: In order to support the development of a competitive, sustainable pro-poor financial sector, the Advisory Committee will provide a framework where stakeholders will:

1. Provide strategic guidance to the project and ensure that it is aligned with national priorities for the sector and coordinated with all applicable components of the FSPD.
2. Approve the 5 year business plan (to be established by the TSP (Manager) upon commencement of the management agreement) and amendments thereof;
3. Review the annual budget and amendments thereof;
4. Review the results work plan and budgets of the TSP (Manager);
5. Approve issues not related to services of MITAF II's Non-Refinance or Refinance Components;
6. Promote sound microfinance practice by advocating professionalism, transparency and good governance in the microfinance industry.

Investment Committee

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[3] Best-practices in microfinance are reflected in the "Donor Guidelines for Selecting Financial Intermediaries", and CGAP Focus Notes, Technical Papers and other publications.

[4] e.g. National Microfinance Strategy, PRSP, FSAP

[5] Note that so far the Bankers' Association and SLAMFI are no active members of the Advisory Committee.

Composition: The Investment Committee will continue being restricted to sponsors of funds for MITAF II operations. Assumingly such sponsors will be restricted to donor organizations and investors. Currently the IC comprises of a representative from each of the contributors: UNDP, UNCDF, CORDAID and KfW; In order to encourage fund contributions of meaningful size, sponsors should commit at least USD 1.0 million to qualify for a representation in the Investment Committee. The chairman of the Investment Committee will be appointed in rotating order. The TSP (Manager) will be the secretariat of the Investment Committee but would be prohibited from voting.

Meetings and Voting: The Investment Committee will meet at least twice a year, either in person or by phone. Each member will have one vote. Those members contributing more than USD 3 million will have an additional vote. All decisions will be taken by consensus and if not will require at least 66% of the votes of the attending members (supermajority principle). In case a sponsor earmarks his contribution exclusively for the Refinance Component (resp. the Non-Refinance Component); the member representing this sponsor will abstain from voting on investments of the Non-Refinance Component (resp. the Refinance Component).

Responsibilities: The function of the Investment Committee shall comprise the following:

1. Determine the business policy, including mainly investment guidelines and criteria for access to finance within the framework of the operating policy guidelines as outlined in this report and further refined by the TSP (Manager) upon taking office;
2. Review the results work plan and budgets of the TSP (Manager);
3. Approve investment proposals in respect of Refinance and Non-Refinance Components
4. Monitor the performance of the TSP (Manager) along the performance indicators defined in the management agreement and approve the performance based fee, if applicable;
5. Determine the signing and disbursement authorities of the TSP (Manager);
6. Decide on Management Agreement issues (e. g. appoint or dismiss the CEO and the other key members of the TSP; terminate the Management Agreement for cause; propose a new Agreement; adjust the performance indicators) and inform the Advisory Committee;
7. Approve any type of legal action within the context of risk and default management.
8. request short assessments and preparatory studies of financial sector development related questions
9. Take decisions on other issues as may deem relevant

The decision on MITAF II investments will be at the exclusive discretion of the Investment Committee. Decisions of the Investment Committee will not be conditional upon additional approval of the sponsoring donors or any other party. An investment approval of the Investment Committee gives immediate authorization to the TSP to proceed with the contracting process.

Organization

The institutional organization of MITAF II will cater for two factors: (i) to enable an efficient operation of MITAF II's business; and (ii) to provide an organizational split between the Refinance and the Non-Refinance Components for the purpose of transparency and effective control.

Institutional Set Up: The two Components on Refinance and Non-Refinance Services will be administered by two separate departments, each governed by individual systems and procedures. However the two departments will be managed by the same TSP setting the CLG. The IC and the TSP will ensure a proper coordination and synergy between the two windows to support the development of the sector. The structure of the required staff and the respective policy guidelines on systems and procedures will be drafted by the TSP, taking stock of any relevant documents already designed in Phase I.

Accounting: The two separate departments shall be accounted as separate profit centres for the purpose of performance, impact and cost control. MITAF II's management information system will be structured in a way to separately monitor and control the development of the two Components.

Operations: The due diligence of a MITAF II investment of either Component will be subject to the respective policy guideline and eligibility criteria. The criteria should include a prior rating of the FSP seeking support from the funding mechanisms. On the other hand, if a FSP qualifies for both Components of MITAF II then the two Components will be fine tuned in order to ensure implementation efficiency and maximize the benefit on the institution building and the business development of the respective FSP.

Management

TSP (Manager): An independent consulting company will be selected through an international tender and contracted on the basis of a separate performance-based management agreement to act as a TSP for MITAF II. The management agreement will be concluded for 5 years equal to the scheduled lifetime of MITAF II, but reviewed annually based on the performance achieved.

Entitlements: The TSP will enjoy two particular entitlements: (i) to manage the funds pooled by the sponsoring donors; and (ii) to conclude contracts as MITAF II CLG with beneficiaries.

Tasks and Responsibilities: The TSP will exercise a hands-on and full time management of MITAF II including but not necessarily restricted to:

General:

- Manage MITAF II in conformity with its overall objective, operating policy and guidance provided by its governance bodies with the aim to efficiently achieve the results,
- Establish systems and procedures, and draft respective manuals, taking stock of any relevant document or experience from Phase I,
- Establish and implement an adequate MIS and a transparent and efficient accounting system,
- Hire, train and supervise required professional and support staff, whether full time employees or associated consultants,
- Communicate with relevant authorities as the case may be,
- Communicate with the donor community and introduce other donors to MITAF II,
- Produce an initial 5-year business plan for approval by the Advisory Committee to be adjusted from time to time,
- Submit an annual budget for approval by the Advisory Committee,

- Efficiently monitor MITAF II investment portfolio
- Report to the Advisory Committee and Investment Committee in regular intervals,
- Prepare meetings of the Advisory Committee and the Investment Committee and provide secretarial services,
- Other duties as may be determined by the Advisory Committee and the Investment Committee.

Refinance component:

- Develop and market products of the Refinance component,
- Screen the market and develop a project pipeline subject to the eligibility criteria, taking into account any relevant document or experience from Phase I,
- Carry out due diligence of MITAF investments (loans, quasi equities, guarantees),
- Produce self-explicatory, risk and problem based decision papers for approval by the Investment Committee,
- Negotiate and execute investment agreements in accordance with the operating policy,
- Disburse funds according to contracted conditions precedent and defined signing authority. Monitor proper use of funds,
- Control proper servicing of the investment agreements, in particular collection of receivables,
- Carry out prudent liquidity management,
- Establish and implement an appropriate risk management,
- Carry out timely and effective default management
- Ensure accurate quarterly reporting, its submission to the PB and its posting on MIX Market;
- Submit a proposal for self-sustaining continuation of the refinance component for approval by the Investment Committee
- Other duties as may be determined by the Advisory Committee and the Investment Committee.

Non-Refinance component:

- Screen the market and develop a project pipeline subject to the eligibility criteria,
- Carry out an appraisal of potentially eligible FSPs,
- Design tailor-made and inclusive institution building packages containing time frames, workable objectives and verifiable success indicators,
- Produce self-explicatory, risk and problem based decision papers for approval by the Investment Committee,
- Negotiate and execute the non-refinance agreements in accordance with the operating policy,
- Disburse funds according to contracted conditions precedent and defined signing authority and in particular subject to evidenced success criteria,

- Monitor proper use of funds on the basis of verified indicators and seek documentary evidence in respect of fixed asset grants,
- Control the execution of the non-refinance agreements, in particular the adherence of the FSPs to the contracted covenants including the cost sharing covenants
- Carry out prudent liquidity management,
- Collect, aggregate and disseminate information on the microfinance industry
- Other duties as may be determined by the Advisory Committee and the Investment Committee.

Contracting Authority: MITAF II CLG will be empowered to contract beneficiaries directly. Any commitments to FSPs will be exclusively contingent on the approval of the Investment Committee including the compliance to any conditions determined by the Investment Committee to such approval. Contracts will be executed between MITAF II CLG and the respective FSP.

Bank Account Authority: The TSP shall open a special account in an international bank satisfactory to the donors to which the donors shall disburse their funds in tranches. The donors and BOSL respectively shall entrust the TSP as management of MITAF II CLG with the management and administration of this account by power of attorney. The TSP will draw from the bank account (opened in the name of MITAF II as a multi-donor fund) amounts up to a ceiling to be determined by the procedures manual for financing the day to day operations of MITAF II.

Management Remuneration: As stated above any contracting executed by the TSP will be in the name of MITAF II CLG. In turn neither the pooled funds nor the FSP investment portfolio will appear on the balance sheet of the TSP. The TSP will also neither participate in the revenue derived from the Refinance Component nor will the TSP absorb or share the risk of a defaulting FSP.

In order to increase the performance motivation of the TSP it is recommended to build a success element into the TSP's remuneration scheme. Banking on other programs with similar objectives the fee structure could consist of following two components:

- a fixed annual fee based on level of effort (man days, running costs)
- a performance fee based on pre-defined milestones, which would top off the TSP's fixed annual fee by to 10%. In turn the TSP will lose his success fee in case of verified underperformance. The indicative projection of MITAF II's annual business development may serve as a benchmark for determining the TSP's entitlement for his annual success fee.

The ultimate fee payable to the TSP will be determined through the international tender process.

Partners roles and responsibilities:

National Stakeholders:

The Government represented by the Ministry of Finance and Economic Development (MoFED) has mandated BoSL to implement the Financial Sector Development Plan ("FSDP"). BoSL considers FSDP-MTTAF II as an integral and strategic component of the FSDP. A proper representation and ownership of the programme as well as mechanisms of coordination will be set up through the participation of the national stakeholders represented by: BoSL, MoFED, the ACB, and SLAMFI, to the AC. This Committee chaired by the Governor of the BoSL will provide overall guidance, approval of annual budget and workplan and promote sound principles.

The population will be benefit from services provided by the FSPs as well as from financial literacy initiatives dealing also with client protection.

The contractual partners (national supporting institutions, Financial Service Providers) commit themselves to achieve the objectives set up in the performance-base agreements and to ensure a proper on-time reporting.

Funders:

The funders accept a division of labour: (a) tender process according to KfW procedures with the full participation of the other funders (discussion of the TORs, the evaluation process, evaluation of the bids and final decision) (b) the TSP contract to be signed between the TSP and KfW (on behalf of BoSL) (b) Mandate letter between UNCDF, UNDP, CORDAID and KfW including the cost sharing of TSP remuneration (currently: 50% KfW, 30% UNDP/UNCDF and 20% CORDAID; these percentages will be reviewed with new funders joining the project); (d) project document governing the implementation to be designed by UNCDF with the full participation of the funders and approved document to be signed by the Government and UN agencies with the signed MOU between all the actors as an annex. The funders will take part to AC, IC meetings; will carry out joint monitoring mission that could be a multipartite review (including key national stakeholders) and joint evaluation. (For contributions of the funders, see V).

In addition, each donor will have the following additional role:

UNDP will not contribute to the Refinance component;

UNCDF will contribute to macro and meso level as well as to non-refinance (mainly) and refinance components. Regarding specifically UNCDF, this programme supports the achievement of objective 1 of the Corporate Management Plan and contributes to the achievement of the Building Inclusive Financial Sectors in Africa (BIFSA II). In addition, UNCDF is supporting other initiatives: MicroLead and Remittances pilot programme.

KfW resources: for Refinance and Non-Refinance of MITAF II, the costs of TSP and evaluation.

CORDAID mainly for the Refinance component of MITAF II but CORDAID will also contribute to the Non-refinance, the TSP costs and the evaluation.

The table below shows the contribution of 650,000 USD coming from Finance Salone sales.

V. Fund Management arrangements

Requirement: Funding will be required for four purposes: (i) the refinance services; (ii) the non-refinance services; (iii) the remuneration of the TSP and (iv) audit and evaluation. Subject to donor statutory regulations, some sponsoring donors may contribute just two of these purposes. Any of the MITAF II founding donors – UNCDF, UNDP, CORDAID and KfW – shall contribute to the remuneration of the

TSP. The ultimate amount of funds pledged for MITAF II will determine the appropriate size and investment requirement for MITAF II's own institution building.

Pooling: MITAF II CLG will contract directly with beneficiaries, in order to mitigate one of the biggest perceived weaknesses of the first program, namely the very slow processing of refinance facilities via the sponsoring donors. The funds will be put into a multi donor-fund through which the TSP can implement the approved decisions of IC. The sponsoring donors will transfer their funds to this multi-donor fund and a bank account will be opened in the name of the company based on tranches and according to their rules. The tranches will be disbursed subject to a clear analysis of the results achieved by the TSP. For UN agencies, this is a direct cash transfer.

Transfer Pattern: The sponsoring donors will transfer their funds in installments. The aggregate sum of the first installment will be sufficient to cover the estimated funding requirement of the first six months of the lifetime of MITAF II. Any subsequent transfer will be contingent on a number of conditions, in particular: (i) the TSP performs to the satisfaction of the Advisory and Investment Committee; (ii) the Investment Committee has authorized the call for funds; (iii) the non-refinance services are implemented and absorbed according to plan; (iv) at least 80% of the preceding aggregate installment has been committed or disbursed to MFIs.

Donors' financial contribution: The table below shows committed amounts of contribution from primary donors:

Donors		Amount (USD)
UNDP		**1 325 000**
UNCDF		**2 325 000**
KfW	Remaining funds of MITAF I	3,100,000
	New funds	5,400,000
	Total	**8,500,000**
CORDAID (Refinance: 1,440,000 and Non-refinance: 432,000)		**1,872,000**
TOTAL		**14 022 000**

Funding gap: The total budget is estimated at 14,770,000 USD whereas funds currently committed from participating donors is 14,022,000. The funding gap for an amount of 748,000 USD will be researched from potential partners such as Austria and Andorra who have expressed some interest in contributing to the pro

This gap will only show up towards the end of the program, in year 5. In the meantime, the company limited by guarantee will be able to secure additional funding with the assistance of existing or foreseen donors.

Regarding specifically the UN agencies, the programme is implemented through a Direct implementation modality (DIM). All the donors, including UN agencies will provide resources to the TSP that will be held in a common account based on the annual workplan approved by the Investment committee.

Communication: Each participating organization shall take appropriate measures to publicize the joint programme and to give due credit to the other participating organizations. Information given to the press, to the beneficiaries of the joint programme, all related publicity material, official notices, reports and publications, shall acknowledge the role of the host government, the donors, the participating UN organizations and any other relevant parties. In particular, this will include due recognition of the role of each participating organization and national partner in all external communications relating to the joint programme.

VI. Monitoring, Evaluation and Reporting

A Monitoring and Evaluation (M&E) system will be set up as an integral part of MITAF II, which primary function would be to assist management to implement and monitor the project by:

- designing and organizing regular flow of relevant data and information;
- analyzing the information to check whether pre-set, goals are being achieved and identifying the reasons for delays.

The M&E will be set up as a Unit within the company and will be managed by the TSP. Specific activities of the M&E Unit will include:

- Monitoring the overall implementation, including procurement, disbursement and financial management;
- Collecting and analyzing quarterly data from the MFIs, based on the performance-based agreements;
- Monitoring of performance indicators;
- Monitoring the extent to which MFIs are reaching out the target groups particularly women and the rural population;
- Monitoring and assessing the extent to which the project supported institution-building mechanisms are effective in strengthening the capacity of MFIs.

A set of minimum performance indicators will be developed and captured in the performance-based agreements signed between the project and each beneficiary. Failure to meet the performance indicators will result in suspension or curtailment of funding.

FSPs receiving assistance under the programme will submit quarterly progress reports to the project on performance against standard indicators and targets as set in the performance-based agreements. In addition, partner MFIs will be required to post their data on the MIX Market.

The TSP will have the responsibility to draft quarterly and annual reports to be submitted to the sponsoring donors, the Government of Sierra Leone, the Advisory committee and the Investment committee. The refinance and non refinance services, cordinated by the TSP, will be administered by two separate departements each governed by individual systems and procedures.The TSP will also set up a unit within the company for the M&E.

The funders will carry out joint monitoring at least once a year that could be extended to amultipartite annual review including all the key stakeholders.

A Mid-Term Review would be undertaken by the end of Year 3. It would draw from the M&E data compiled during the first three years of project implementation. In addition, a final evaluation will be undertaken by the Donors at the end of year 5. Both the mid-term review and the final evaluation will be jointly undertaken by the sponsoring donors and the national stakeholders. UNCDF evaluation unit will lead the process of the joint evaluation with the full participation of all the project stakeholders including, MoFED, BoSL, UNDP, KfW, CORDAID…

The evaluation will assess the programme's overall performance, the outputs and outcomes produced against its initial targets, the impact it has brought or would likely bring about, its relevance to assisting the partners to achieve the targets of its business plan and management efficiency. The evaluation will be forward looking, offering lessons learned and recommendations to improve programme performance. The results of this evaluation will feed into strategic, thematic and outcome evaluations carried out by the partners and stakeholders.

Success in carrying out development evaluation requires partnerships in evaluation with national and international actors. In the context of wider efforts to improve the efficiency and added value of the development operations, opportunities for collaboration on evaluations with development partners are now actively sought. Opportunities will be sought for collaboration with programme partners in conducting the evaluations, including but not limited to collaboration in developing the terms of reference for these evaluations.

The appropriate utilization of the funds will be subject to an annual review by an independent auditor. The auditor will be selected by the donors and funded by the project.

As in Phase I, UNCDF evaluation Unit will coordinate the joint evaluations.

Funding for the evaluation and annual audit is included in the programme's budget.

The following reports are included in the TSP contract:

Title of Report	Due Date	Responsible
▪ **Business Plan**	3 months after operation starts	TSP
▪ **Inception Report**	Beginning of year 1	TSP
▪ **Work Plan and budget**	Beginning of project and annually	TSP
▪ **Annual Progress Report**	Annually	TSP
▪ **Key Performance Indicators**	Quarterly	TSP
▪ **Audited Financial Statements**	Annually	MFIs
▪ **Annual TSP audit**	Annually	TSP/ Donors (lead: KfW)
▪ **Mid-Term Review**	End of year 3	Donors (lead: UNCDF)
▪ **Final evaluation**	End of Year 5	Donors (lead: UNCDF)

VII. Legal context

As in all agreements between the Government of Sierra Leone and UNDP, the project document referred to in the Standard Basic Agreement shall be the main instrument governing the conduct and performance of the contractors and agents.

The following type of revisions may be made to this project document with the signature of the UNDP Country Representative only, provided he or she is assured that the other parties involved in the project have no objection to the proposed changes:

- Revisions in, or addition of, any of the annexes of the project document;
- Revisions which do not involve significant changes in the immediate objectives, outputs or activities of the project, but are caused by the rearrangement of inputs already agreed to or by cost increases due to inflation;
- Mandatory annual revisions which rephrase the delivery of agreed project inputs, or reflected increased expert or other costs due to inflation, or take into account agency expenditure flexibility.

VIII. Risks and mitigations

Below table summarizes risks perceived to impede an efficient and effective implementation of MITAF II.

Risks & Mitigations	
Risks	**Mitigation**
Economic and political instability leading to social unrest	Conduct detailed environmental analysis before implementation
Macro environment unstable (high interest rates, inflation etc)	Planning should take into account trends and turbulences in the macro environment that could directly impact on the financial sector
Deterioration of enabling infrastructure (roads, bridges, communication etc.)	Develop innovative products and tools to increase outreach in the rural and remote areas
Funds offered for MITAF II are insufficient	At this point in time KfW, UNDP, UNCDF and CORDAID have expressed clear interest in funding MITAF II. Indicative amounts have already been earmarked. The risk of MITAF II not materializing because of insufficient funding seems low. Discussions will also commence with other potential sponsors, once the legal option most suitable for KfW, UNDP, UNCDF and CORDAID is selected. NASSIT, the domestic pension fund has indicated interest to support MITAF II. Finally MITAF II will also endeavour to establish bank linkages with MFIs, which in the case of success would multiply the MITAF II funds availed to MFIs.
Not all donors are willing to pool funds	The fall back position would be to maintain MITAF's s status quo. Yet sponsors unwilling to pool funds would now be committed to pay to MITAF II a facilitation fee in return for MITAF II's effort to identify, analyze and package a deal for that donor. Also such donors would be denied a membership in the Investment Committee. In conclusion, the unwillingness to pool funds will not be a killing factor for MITAF II, though this would have a significantly adverse impact on the efficiency of particularly the Refinance component.

FSPs default on the Refinance component	The default risk of FSPs will be contained through a conservative selection, a thorough analysis and a timely monitoring. MITAF II will enjoy a broader refinance product range allowing an effective tailoring of its services to FSP requirements. Furthermore, the contractual covenants of the FSPs will entitle MITAF to quickly enforce mitigating actions as it deems fit MITAF enjoys the particular advantage of having access to technical assistance capacities, which may be quickly mobilized if deemed advisable.
Insufficient demand side (FSPs willing and able to develop innovative products to tackle the market mainly in rural areas	Carry out and update a market analysis and strengthen capacity FSP capacity building.

IX. Work plans and budgets

The total budget is estimated at 14,770,000 USD.
A detailed work plan ("business plan") will be developed by the TSP within 3 months after project commencement.

Refer to Annex 4.

Annex 1: MITAF key results and evaluation findings

Key Project Results

MITAF has exceeded project outreach targets. At September, 2009, 13 the partner lending institutions financed by MITAF were serving close to 120,000 clients: 79,610 active loan clients served by 8 MFIs and 39,573 clients (savings and loans) served by 5 banks. Taken together, the FSPs have achieved very broad geographic coverage throughout the country, although only one covers a major part of the country itself. This is particularly impressive considering the difficulty of reaching rural areas of the country.

One of MITAF's key achievements was to help ensure that microfinance is seen as an integral part of the financial sector in Sierra Leone, both through discussions held with government at the Investment Committee level and by its work with the Bank of Sierra Leone (BoSL). Interviews with representatives of the BoSL and the Ministry of Finance and Economic Development (MOFED) during the evaluation showed that government understands the key role that microfinance can play as part of the financial sector. Indeed, strategies to continue to build the microfinance sector are an integral part of the recently approved Financial Sector Development Plan (FSDP).

Key Evaluation Findings

MITAF has been instrumental in building an inclusive financial sector in Sierra Leone.

When the project started in 2004, there were a handful of relief and development agencies providing credit but there was no real microfinance sector. At the end of 2009, there are about 30 microfinance institutions and commercial and community banks offering financial services to the poor and underserved. Many of these have benefited from MITAF's financial and non-financial assistance, without which they would not have been able to achieve the impressive results they have. Because it has adhered to and promoted internationally-recognized good practice, MITAF has served as a catalyst for developing not just quantity but quality throughout the sector as a whole.

The operating environment in Sierra Leone remains a challenge to the continued growth and sustainability of project results.

Financial institutions in Sierra Leone face significant challenges in providing services to microentrepreneurs. These include: continued pervasive poverty, further exacerbated by the recent economic downtrend, that severely constrains the effective market for clients' goods and services; limited infrastructure throughout the country, particularly the lack of adequate roads, electricity and communication systems, that further limits client market opportunities and the ability of institutions to offer sustainable, quality services, particularly in rural areas; a limited pool of qualified staff, particularly managers, available to fill key functions; lack of a credit culture that would foster client willingness to repay loans and a high degree of corruption resulting in lending fraud; a high incidence of client illness, accidents and death. When combined with a lack of sufficient institutional structures and systems, the result has been serious problems of portfolio quality that continue to plague the entire financial sector. In 2008, the percentage of non-performing loans in the commercial banking sector was 23%, and at June 2009, only two of MITAF's FSPs were meeting the criteria of Portfolio at Risk more than 30 days (PAR>30) of 5% or less, with the overall average of the 13 FSPs exceeding 10%.

<u>Despite clear improvement in institutional capacity at the micro, meso and macro levels, internal weaknesses continue to jeopardize sustainability</u>

The significant resources devoted by the project to providing capacity-building services through training and technical assistance to the FSPs and to local institutions at the meso and macro levels have had a positive impact. Nevertheless, while project services have contributed to improved institutional strength in many FSPs, most continue to demonstrate significant internal weaknesses in governance, management, staffing, systems and internal controls (please refer to Section 8 for a detailed analysis of PLI capacity). Institutional weaknesses in meso and macro level institutions, such as the Sierra Leone Association of Microfinance Institutions (SLAMFI) and the Banking Supervision Department of the BoSL also raise questions about the ability of these institutions to continue to fulfill their key roles after the project ends. SLAMFI has not met since 2007 and was essentially non-functional as of September 2009, while the Banking Supervision Department is severely under-staffed.

<u>Project targets provided incentives for significant outreach but also had unintended negative impact on the FSPs and the sector as a whole.</u>

It is clear that the project outreach targets were set by the donors and the Government of Sierra Leone (GoSL) with the sincere desire to help to reduce poverty by building an inclusive financial sector. Nevertheless, the targets did not reflect an adequate analysis of the capacity of the microfinance sector at project inception nor realistic expectations about the speed with which sufficient capacity could be built. Further, some of these targets created an incentive system that was detrimental to sustainable results. In particular, the two key quantifiable project targets – increasing numbers of clients served and covering all operating and financial costs through income (financial self-sufficiency) – create conflicting incentives for FSPs. Indeed, in order to reach both targets, most FSPs grew without sufficient investment in internal structures needed to support their rapid growth. Operating costs in many FSPs are inflated by the high levels of PAR and write-offs, making it difficult to reach financial self-sufficiency expectations. Therefore, in addition to containing costs by not investing in sufficient staff and systems to manage their growth, many FSPs charge extremely high effective interest rates.

Another unintended result of project funding that promoted the development of a number of FSPs and a fast-paced growth in outreach has been a contribution to increasing saturation of urban microcredit markets. There are almost 30 commercial and community banks and MFIs providing services in a country with a population of about 5.5 million, 23 of which operate in the same urban centers. Of these, at least 16 provide microloans to poor entrepreneurs and MITAF has supported the development of 13 of these. Recent studies have indicated a level of demand that the evaluation team believes to be unrealistic (see Section 3.3.4). Nevertheless, these studies indicate an expressed demand for microloans from 120,000 households in urban areas throughout the country; the 13 FSPs supported by MITAF alone report 120,000 outstanding loans at June 2009, and most of these loans are in urban areas. Sector stakeholders consistently report that fierce competition for clients and increasing multiple lending is becoming their biggest challenge, contributing to problems of portfolio quality and potential client over-indebtedness.

Despite the saturation of urban microcredit markets, there is some room for financial institutions to extend services to under-served rural areas. However, the rural market for credit is much more limited than the urban market due to the severity of constraints faced by rural clients and financial institutions alike. With already stretched institutional structures, most FSPs do not have the capacity to expand into the difficult rural market; indeed, their poor performance with regard to portfolio quality indicates that they are struggling to manage their existing, largely urban, portfolios.

<u>The project implementation structure did not promote optimally efficient and effective delivery of funding and other services</u>

The chosen project structure has not proved optimal in practice, with an Investment Committee that retained the authority to approve each project investment and allowed donors to contract directly with the FSPs, but delegated all other roles to one consulting firm. Although the IC was intended to ensure coordination of donor funding, in practice it enabled each donor to finance the type of institutions it prefers without regard to the microfinance market as a whole (please see Section 5.1.2 for further discussion). One result has been the proliferation of fairly weak institutions providing financial services to the poor, in a market that likely cannot support most of them in the long term. Because donor funds were never pooled and as each donor contracted separately with each PLI, efficient disbursement and tracking of donor funds remained a challenge through the project.

The TSP performed very well, enabling the project to meet most of its targets, and donors and MFIs alike appreciate the services that the TSP has provided. However, there has always been a conflict of interest for the TSP on the ground between the roles of "financier" and "capacity-builder". This conflict of interest was exacerbated by the fact that the TSP's contract was performance-based and its compensation was contingent upon achieving project targets; an inherent tension was created between encouraging FSPs to expand and helping them to build capacity. Further, ambitious project goals dictated that the TSP also identify and ensure capacity-building for numerous other local recipient institutions at meso and macro levels as well as administer the project overall. Fulfilling these multiple roles exceeds the capacity of one consulting firm and contributed to limited results at the meso and macro levels.

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Annex 2: Results & Resources Framework

Agenda for Change: Raising the quantity and value-added productivity in agriculture through "enhancing rural financial access through microfinance institutions"

Joint vision Sierra Leone 2: Increased access by the rural poor to markets and social services, and to justice and information, in an effort to widen their economic and social opportunities

JOINT PROGRAM OUTCOME : To have contributed to a rural population that is less isolated and has greater access to information, market opportunities and financial services

Overarching Goal: To contribute to the MDGs, in specific the goal of cutting absolute poverty by half by 2015 (MDG 1) and promote gender equality and empower women (MDG 3) through employment creation and improvement of livelihood.

Project Goal: Development of a competitive and sustainable inclusive financial sector that provides access to financial services to poor and low-income people in general and micro and small businesses in particular with a special focus on rural areas

Indicators: (to be reviewed based on the TSP approved (5-Y plan)
Active clients: Baseline: 2010: 131 745; 2011: 150 000; 2012: 200 000; 2013: 270 000; 2014: 390 000;
Active savers: Baseline: 2010: 47 604; 2011: 50 000; 2012: 70 000; 2013: 100 000; 2014: 150 000
Active borrowers Baseline 2010: 95 165; 2011: 100 000; 2012: 130 000; 2013: 170 000; 2014: 240 000
Percentage of semi urban and rural active clients: Baseline 2010: 33%; 2011: 38%; 2012: 43%; 2013: 48%; 2014: 53%.
Percentage of semi urban and rural borrowers: Baseline 2010: 34%; 2011: 39%; 2012: 44%; 2013: 49%; 2014: 54%.
Percentage of women: at least 50%

Poverty orientation: At least 70% of the clients can be considered as poor

FSPs: FSPs applying best practices (CGAP) Baseline 2010: 3; 2011: 3; 2012: 4; 2013: 5; 2014:6;
Financially sustainable: Baseline 2010: 2; 2011: 3; 2012: 4; 2013: 5; 2014: 6

PAR 30 days: Average PAR 30 d reduced at least to 5%

Joint program outputs	Intermediary outputs	Implementing partner	Indicative activities for each output	Resource allocation and indicative timeframe					Total $US
				Y1	Y2	Y3	Y4	Y5	
At Micro level: Result 1: Sustainable access to appropriate financial services is available to a large segment of the productive Sierra Leoneans, with special	**1.1: Improved capacity and outreach of financial services providers in semi-**	**TSP/BoSL/FS** Ps/Trainers/ot her companies	Training sessions for target staff of FSPs through available training programs locally and abroad in governance, financial management						

focus on rural population and women.	**urban and rural areas**		Logistics and equipment support: motorcycles, safes, computers, MIS softwares, generators						
			Technical assistance – both short term and long term – to help FSPs in business planning, processes and procedures, internal control, delinquency management, governance issues						
			Assistance in market research and innovative product development to rural operating FSPs and study tours						
		TSP/FSPs/ Trainers/ Auditors...	Assessment of the financial gap in rural and semi urban areas and types of financial instruments needed						
			Study on how to promote linkages between commercial banks and MFIs and community banks in rural						
			Identification of the savings potential of rural population, assistance in implementation of appropriate channels for savings mobilization						
			Sub-total Non-refinance	**130 000**	**900 000**	**622 000**	**550 000**	**144 000**	**2 346 000**
	1.2: Improved availability of additional capital to partner FSPs in semi-urban and rural areas through appropriate instruments and linkages		Long term loans to qualified FSPs to serve the financial needs of rural micro entrepreneurs, women and farmers						
			Partial guarantee facility to serve as a collateral for eligible MFIs and community banks in order to promote commercial banks lending to microfinance						
			Partial guarantee facility for agricultural lending						
			Quasi-equity instruments for mature FSPs						
			Refinance	**1 480 000**	**2 140 000**	**2 154 000**	**0**	**0**	**5 774 000**

Sub Total Micro Level				**1 610 000**	**3 040 000**	**2 776 000**	**550 000**	**144 000**	**8 120 000**
R. 3 : At MESO level : **The framework conditions for FSPs improved through sustainable strengthening of meso-level institutions** Baseline 2010: no Business plan 2011: BP implemented 25% 2012: Business plan implemented 50% 2013: BP implemented 75% 2014: BP implemented 10%	**2.1: A functioning MFIs Network with increasing sustainability level**	**TSP**/other companies of meso level/SLAMFI /trainers…	Design a five year business plan for SLAMFI						
			Establish a performance-based agreement with the network on a cost-sharing basis						
			Assistance in structuring and strengthening the network in policy dialogue and sensitization						
			Capacity building and training to hired staff of the network and study tour to its President and Director						
			Equipment support to the network and TA in setting the procedures; structuring its governance						
	2.2 local capacity for meso support developed		Assistance to the network in data collection and information dissemination among FSPs						
			Training sessions to selected audit firms in inclusive finance						
			Training of a critical mass of local technical service providers: training centers, consulting firms, etc. in partnership with CGAP						
			Training material and certified microfinance trainers for the planned Training Center						
			Non refinance	**62 000**	**143 000**	**120 000**	**87 000**	**0**	**412 000**
Sub Total Meso level				**62 000**	**143 000**	**120 000**	**87 000**	**0**	**412 000**
R. 3 : At MACRO level : Framework conditions for FSPs are improved through a conducive legal and regulatory framework and a functioning Central Bank Baseline: 2011: Functioning microfinance supervision unit within the BoSL Credit Bureau	**3.1: regulatory functioning Microfinance supervision within the CB and a promotion unit set within MoFED**	**TSP**/BoSL/MoFED/FSPs/IFAD/CBs	Assistance in structuring the microfinance supervision unit within the BoSL						
			Assistance in structuring the microfinance promotion unit within the Ministry of Economic development						
			Dissemination of information and assistance to FSPs to comply with the registration and licensing requirements of the BoSL						
			Design and implementation of a credit bureau						
			Assistance in revitalizing the microfinance sector database						