



A COMPARATIVE ANALYSIS

Afghanistan's Microfinance Sector vs. Counterparts in Neighboring Countries

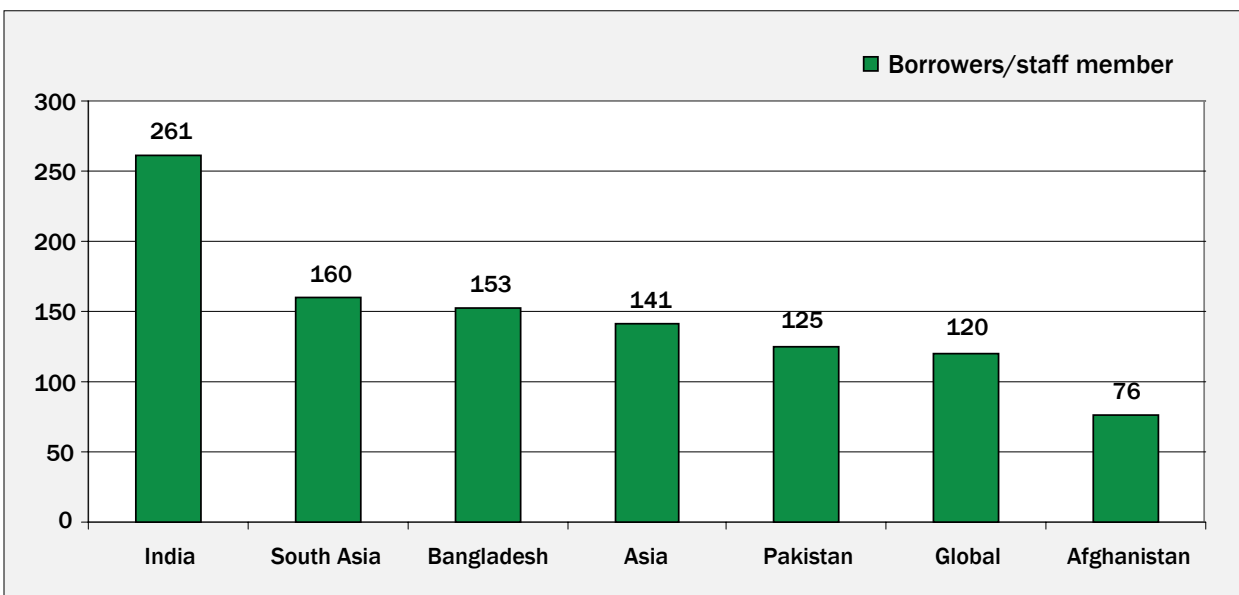
**Regional and Global Averages
September 2009**

Microfinance Investment Support Facility for Afghanistan (MISFA) is a Limited Liability Company (LLC) fully owned by the Afghan Government's Ministry of Finance (MoF). It was established in 2003 as a vehicle through which the Afghan Government and international donors could channel technical assistance and funding to build and strengthen Afghanistan's microfinance sector, as well as the lower ranges of Small and Medium Enterprise (SME) lending.

Following is a quick look at how Afghanistan's microfinance sector measures up with its counterparts in neighboring countries, as well as with regional and global averages, using some key indicators of efficiency and sustainability.

(The data for Afghanistan has been taken from the monthly progress reports submitted by MISFA partner MFIs, and the data for the rest of the countries/regions is from the MIX Market.)

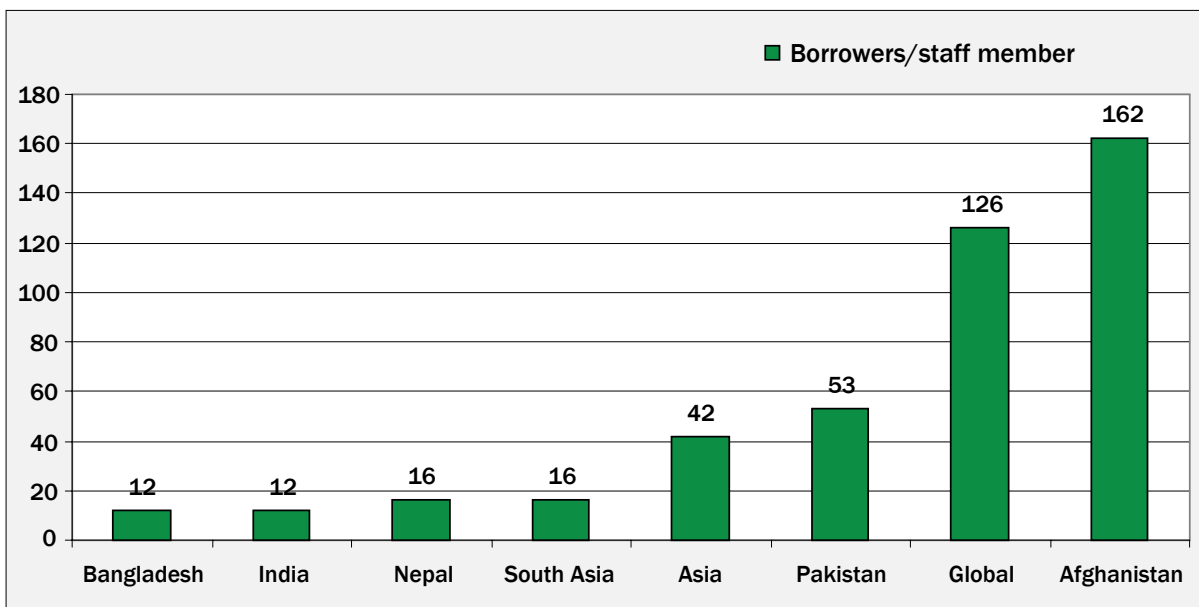
Indicator 1: Staff Productivity



While on the face of it, the average for Afghanistan appears to be lower than that of the other countries/regions, it has to be recognized that the operating environment in Afghanistan is very different from the countries in the rest of region, including in Pakistan and India, its two closest neighbors. This is mainly due to the fact that the ratio of the number of non-credit staff (mainly support staff involved in security, such as guards, drivers, etc.) to credit staff is higher in Afghanistan. This is understandable considering the insecurity of the environment. Among Microfinance Institutions (MFIs) in Afghanistan, the credit staff, essentially the loan officers, usually comprises less than **50 percent** of the overall staff. Whereas in other countries (India and Bangladesh), the credit staff would be in the range of **80-85 percent** of the total staff.

In addition, the **population density** in Afghanistan is much lower than in some of the other South Asian countries, such as India, Bangladesh and Pakistan. This reduces the capacity of loan officers to cover a large number of clients; they would have to travel much longer distances to cover the same number of borrowers.

Indicator 2: Cost per Borrower (in US\$), per year

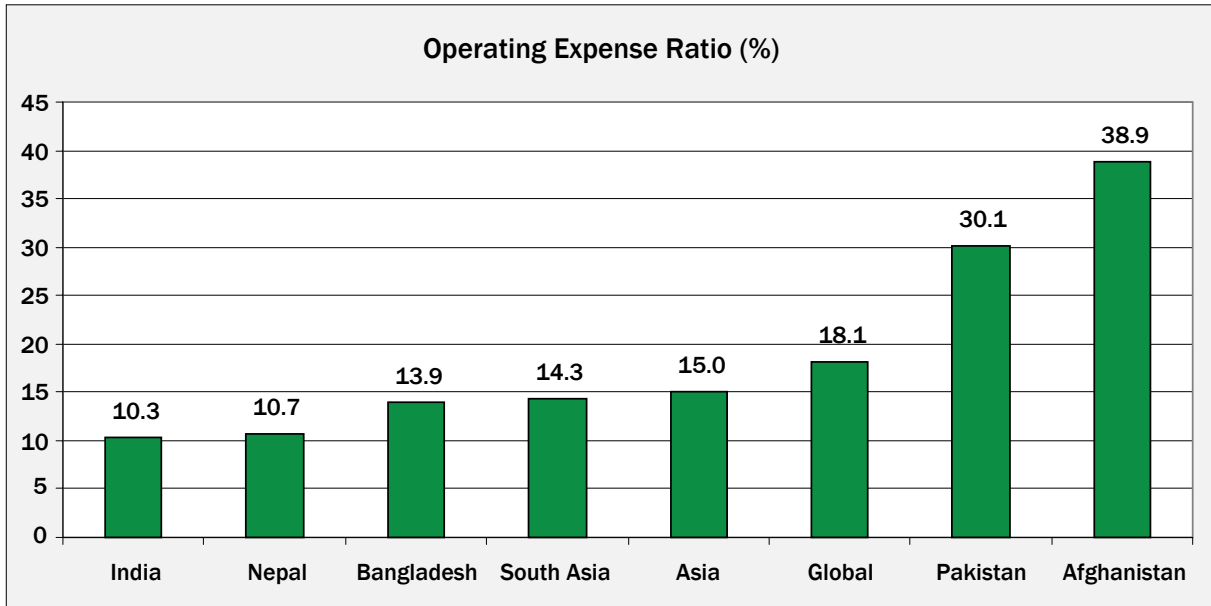


The annual cost per borrower for Afghanistan is about **\$162**, which is much higher compared to the averages in the region. It goes without saying that in a country characterized by instability and ongoing conflict, operating costs would be very high. Staff salaries and administrative costs are far higher in Afghanistan, compared to the other countries in the region. And due to the lower population density in a given area and larger distances that the loan officers have to cover, it makes it very difficult for them to be as productive as their counterparts in the region. But it has to be recognized that as the outreach of the sector increases, this ratio is likely to drop significantly, as the overhead and staff costs remain quite stable, or at least do not increase in direct proportion to the increase in outreach.

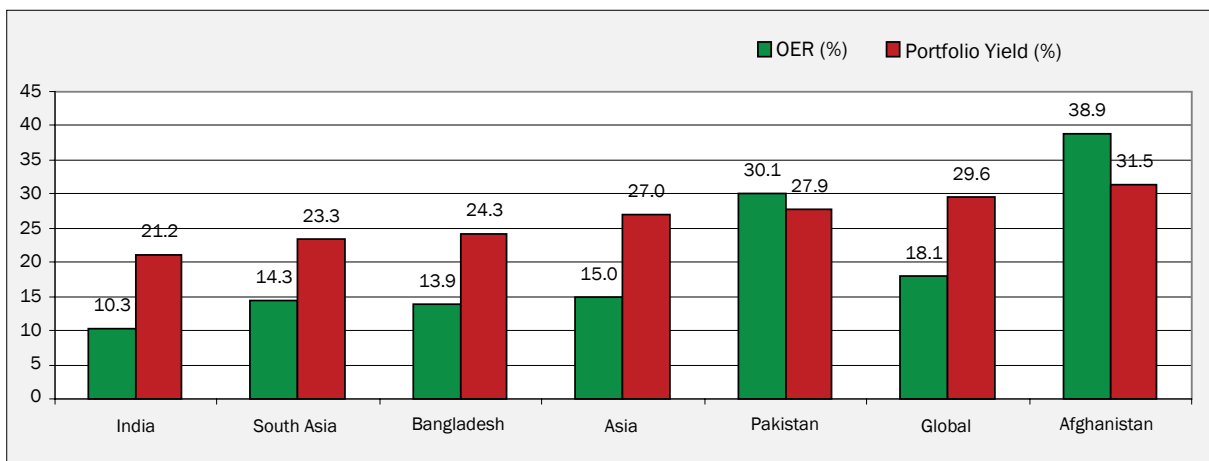
Indicator 3: Operating Expense Ratio (OER), %

The operating expense ratio measures the total of operating expenses (personnel, administrative and depreciation) as a proportion of the average outstanding portfolio. This is the most standard ratio for measuring operational efficiency. The Operating Expense Ratio (OER) in Afghanistan is much higher than that of the other countries in the region and also the global average. This is mainly due to the higher operating expenses in Afghanistan. For instance the average salary of a loan officer in Afghanistan is in the range of **\$200-400** (all expenses, e.g. transportation, lunch, performance bonus, etc. included), compared with India and Bangladesh, where the average is about **\$100**. In addition, hiring of extra support staff, mainly for security – an unavoidable expense in the volatile context of Afghanistan – increases personnel cost to a much higher level than in the other countries.

In terms of administrative expenses, office rent and transportation are also much higher in Afghanistan than in the neighboring countries. While most loan officers typically use bicycles or motorcycles in Bangladesh, India and Pakistan for field work; their Afghan counterparts are forced to use cars, which are more costly, due to the tougher terrain, weather and security conditions.



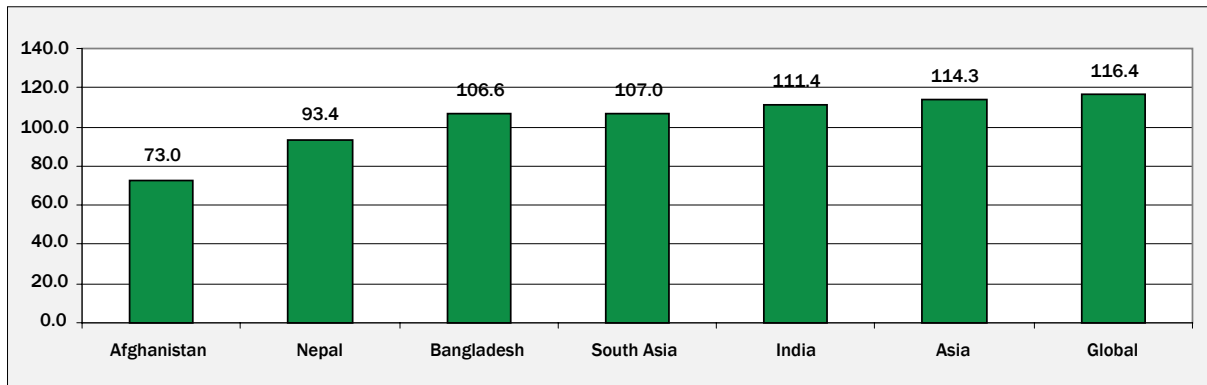
Indicator 4: OER vs. Portfolio Yield



The chart above illustrates the relationship between the Operating Expense Ratio (OER) and Portfolio Yield (interest income earned from the portfolio outstanding). But for Afghanistan and Pakistan, the portfolio yield in all the other countries/regions is higher than the operating expense ratio, suggesting that the MFIs in the other regions are making a margin, before accounting for the cost of funds and for loan losses. This also suggests that the Afghan MFIs on the whole are not able to meet their operating expenses from the interest they charge clients.

The yield on portfolio for Afghan MFIs is not much higher than those of other MFIs operating in the region, in spite of their much higher operating costs; suggesting that the interest rates in Afghanistan are lower than the actual operating costs.

Indicator 5: Operational Self Sufficiency (OSS)



Operational Self Sufficiency (OSS) measures the ability of an MFI to meet all its operational and financial costs out of its income from operations. As the above table shows, although the Afghan microfinance sector has yet to achieve break-even (or 100% OSS), it is well on its way. It should be noted that the Afghan microfinance sector is still quite young, with the first microcredit loans issued in 2003, only about six years ago.

Still, the distance that the sector has covered in terms of operational sustainability is quite significant considering the odds – insecure environment, low staff capacities, high operating costs, and a collapsed financial system, among others. The achievements of the other countries in the region have to be viewed against the fact that they have a significantly longer history with microfinance (about 25 years, in the case of Bangladesh), and also that they didn't have to encounter the kind of circumstances/challenges that the Afghan MFIs face on a daily basis.