

**Macedonia: Macedonia Microcredit Bank (MMB) – ProCredit Bank**

**Ex post evaluation report**

<b>OECD sector</b>	24030 – Financial intermediaries of the formal sector	
<b>BMZ project ID</b>	2002 66 098	
<b>Project executing agency</b>	ProCredit Bank (PCB) – formerly Macedonia Microcredit Bank	
<b>Consultant</b>	-	
<b>Year of ex post evaluation</b>	<b>2006</b>	
	<b>Project appraisal (planned)</b>	<b>Ex post evaluation (actual)</b>
<b>Start of implementation</b>	3/2003	1/2004
<b>Period of implementation</b>	36 months	35 months
<b>Investment costs</b>	No information available	No information available
<b>Counterpart contribution</b>	No information available	No information available
<b>Financing, of which Financial Cooperation (FC) funds</b>	EUR 1.5 million	EUR 1.5 million
<b>Other institutions/donors involved</b>	IFC, IMI, EBRD	IFC, EBRD, PCH, FMO
<b>Performance rating</b>	1	
• <b>Significance/relevance</b>	1	
• <b>Effectiveness</b>	1	
• <b>Efficiency</b>	1	

**Brief description, overall objective and project objectives with indicators**

The project comprised the foundation and buildup of a fully licensed commercial bank specialized in micro and small lending, the Macedonia Microcredit Bank, which was later renamed into ProCredit Bank Macedonia (PCB). Since its foundation the balance-sheet total and the loan portfolio of ProCredit Bank have developed very positively. In the period from the start of business activities in October 2003 until 2006 the balance sheet total rose to almost EUR 89 million (as of mid-2006) and the loan portfolio to EUR 67 million (as of October 2006). Thus, ProCredit Bank plays an important role in the financial sector in Macedonia. Against the background of the high excess demand for micro and small loans that existed at the time of the project appraisal the establishment of the new bank was to be implemented complementary to the existing micro-finance offers in order to ensure the demand-oriented supply of micro and small enterprises. In order to endow the bank with sufficient capital FC trust funds of EUR 1.5 million were provided to MMB in the form of an equity capital contribution.

The project objective was to provide sustainable loan offers and other financial services at market conditions to micro and small enterprises. In this way a contribution was to be made to the sustainable promotion of the private economy in Macedonia and to the development of the financial sector (overall objective).

The project objective was considered achieved if the following indicators were fulfilled at the end of the third business year:

- The share of loans in the gross loan portfolio with interest and/or principal arrears of over 30 days ("portfolio at risk") is not more than 4%;
- The net loan portfolio has reached EUR 18 million;
- The average loan amount of the total portfolio is EUR 5,000.

The overall objective was considered achieved if at the end of the third business year 20% of the borrowers had received follow-up loans (according to the figures reported by PCB).

### **Programme design / major deviations from the original programme planning and their main causes**

The framework conditions in the Macedonian financial sector have substantially improved in the last few years. In July 2004 Standard & Poors, one of the three large rating agencies, granted a BB rating with stable outlook to the Republic of Macedonia and in August 2005 the rating was even raised to BB+. This means that the country has come closer to the much sought-after investment grade (BB- and higher), which allows large institutional investors to invest in a country. Macedonia has a two-tier banking system. The Macedonian National Bank (NBRM) supervises the banks and operates as an independent legal entity pursuant to the National Bank of the Republic of Macedonia Act. The principles applied by the supervisory authority of the national bank are based on the principles of the Bank für International Settlement (BIS) for effective banking supervision. Currently 20 banks are active in Macedonia (at project appraisal the number was 25), which have either a full or a limited banking license. In addition, there are 14 so-called savings houses (21 at project appraisal), which are non-bank financial intermediaries. While the banks account for a share of 98.7 % of the total assets of the banking system in Macedonia, the savings houses account for only 1.3%. 52% of total assets of the banking system belong to foreign banks (e.g. Greek and Slovenian bank, but also foreign development banks such as the EBRD). 16 of the 20 banks have their headquarters in Skopje. Most of the banks have a dense branch network with branches in almost every large town in Macedonia. Nevertheless, measured by the size of the national economy, the banking sector is still relatively small with total assets accounting for around 39% of GDP. As in the past the banking sector is concentrated on few banks. The three largest banks account for almost three quarters of total assets and three quarters of savings deposits. Though the banking system was improved in the last few years there is still a high need for consolidation.

Despite the described improvements in the banking system the sector is still restricted in its function as an intermediary. The share of the cash in circulation in GDP was 5.1% in 2005, while the ratio of the M3 supply to the M1 money supply was 350%. The overall volume of loans made by the banks to enterprises and households at the end of 2004 was approx. EUR 765 million. This was an increase of 27% compared to the 2003 figures. Nevertheless, this corresponds to only about 18% of 2004 GDP.

Lending by the commercial banks to the private sector was insufficient at the time of the project appraisal. Some of the reasons for this were inefficient administrative structures of the banks and deficiencies in the area of corporate governance. In addition, there was a lack of confidence of the private sector in the commercial banks which was due to the fact that the bank's shareholder structures are often unclear and to the suspicion of insider loans and money laundering. Due to the fact that at the time of the project appraisal interest rates were high in comparison to other countries in the region (approx. 13%) the demand for loans on the part of enterprises was limited. On the other hand, the commercial banks preferred to lend only to very profitable enterprises. In particular in the lower credit segment (loans of less than EUR 20,000) the banks hardly offered any loans because they considered MSMEs not as part of their customers.

The private sector in Macedonia is dominated by micro, small and medium-sized enterprises, which play a central role for the country's economic development and the creation of jobs. Of a total of 49,687 registered active enterprises (2004) 99% are classified as micro and small enterprises. The large majority of these enterprises employ only up to ten persons. Not even 1% of enterprises have a staff of more than 50. Almost half of the enterprises is active in the retail and wholesale sectors, followed by the producing sector and the service sector. Of the registered staff (approx. 250,000 persons) 56% are working in small enterprises, 25% in medium-sized enterprises and 19% in large enterprises.

In July 2003 ProCredit Bank Macedonia was founded on the basis of the law on microfinance banks in the form of a closed joint-stock company under Macedonian law, with a capital of EUR 5 million and started business in October 2003. Besides KfW, the European Bank for Reconstruction and Development (EBRD), the International Finance Corporation (IFC) and the Internationale Micro Investitionen (IMI) – which was later renamed into ProCredit Holding AG – participated in the establishment of the bank. In 2004, in the context of the increase of the bank's capital to EUR 9 million, the Nederlandse Financierings-Maatschappij voor Ontwikkelingslanden NV (FMO) was admitted as a further shareholder.

Against the background of the expected developmental importance of ProCredit Bank Macedonia for a sustainable target-group oriented promotion of SMEs and the positive signal for the expansion and deepening of the financial sector, Financial Cooperation (FC) funds of EUR 1.5 million were made available through KfW as trust funds to acquire a stake in the share capital of the bank. Originally KfW acquired 25% of the capital worth EUR 1.25 million. Another 25% of the share capital was acquired by three other shareholders. With the acceptance of FMO as a shareholder the KfW trust share in the share capital fell to 20.83%. As a result of the capital increase in December 2004, in which KfW as the trustee of the German government participated only partially by subscribing shares worth EUR 220,000, the trust share held by KfW was reduced further to 14.7%. With the 2004 capital increase ProCredit Bank Macedonia reached the required equity capital to be allowed to work as a commercial bank with a full central bank licence. Thus, a number of restrictions to its business activities do no longer apply. The licence was granted at the end of 2004. According to schedule the trust share held by KfW is to be sold to ProCredit Holding in 2007. The trust funds will then be repaid to the German government<sup>1</sup>.

The business activities of ProCredit Bank Macedonia are monitored by a supervisory board. Further organs of ProCredit Bank are the shareholders' meeting and the Audit Committee, which reports to the Supervisory Board. With a staff of approx. 330 persons at the end of 2005 the number of employees has almost doubled compared with the staff of 170 at the end of 2004. According to the planned figures roughly 180 more employees will have joined the payroll by the end of 2006. The staff appreciate ProCredit Bank Macedonia very much as an employer. Thus far it has not been difficult to recruit sufficiently qualified staff on the local labour market. The employees are given intensive training to prepare them for their jobs. In the last few years the productivity of the loan officers have developed positively. On average every one of the 120 loan officers extends 16.5 loans per months and handles a portfolio of 165 loans with an average volume of approximately USD 565,000 (as of October 2006). By comparison: In 2003 on average every one of the roughly 30 loan officers extended 10 loans per months and handled a portfolio of 45 loans with an average volume of approximately USD 225,000.

In the past three years ProCredit Bank Macedonia has been undergoing a change from a micro finance bank specialized in granting loans into a universal bank, which in addition to loans offers its customers all different types of banking products (savings products, payment services etc.). This development is the result of a strategy aimed at ensuring sustainability and at making the refinancing of the lending business increasingly independent of donor support by establishing an own deposit-taking business. However, currently the extension of micro and small loans continues to be the core business. As of October 2006 the share of loans with a volume of less than EUR 10,000 ("micro loans") in the total portfolio was 90 %. In addition, new loan products were established (for example loans for housing improvement or special offers for agricultural loans). The deposit-taking business was expanded, for instance through hiring additional staff and the introduction of new savings products. Customer deposits rose from EUR 1.8 million at the end of 2003 to EUR 70.9 in October 2006. The conditions of ProCredit Bank Macedonia are market driven. In addition, money and credit cards (issued by the bank itself and by international institutions such as Visacard and Mastercard) were successfully introduced in the course of 2005. All branch offices were equipped with cashpoints.

Another key aspect of the business policy of ProCredit Bank Macedonia is regional expansion. The branch network, which comprised seven branches and offices in 2004, was expanded to 16 branches at the end of 2005. In October 2006 the number had already risen to 21. On the

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<sup>1</sup> Trust funds not yet disbursed in the amount of EUR 3,367.36 will be repaid together with the redemption of the funds after the shareholding of the German government has been sold.

one hand the expansion strategy of the bank aims at extending the network for the regular customer group of micro and small enterprises (MSEs). On the other hand, however, the existing branch offices are being shifted or rehabilitated in order to promote the further build-up of the deposit-taking business.

ProCredit Bank Macedonia has set itself the goal of becoming the country's most customer-friendly bank. The degree of service in terms of processing times is impressive. Nevertheless, credit assessments are performed with great care. On average, approx. one fifth of the loan applications are rejected, mostly because of poor creditworthiness and a poor credit history of the applicant. Based on the number of loans approved, around one third are granted for a lower amount than that originally applied for. The main reason for the reduction in the loan amount is that the business and financial data provided justify only a small loan amount. An assessment as high risk and insufficient security also lead to a reduction in the requested loan amount. Environmental aspects are taken into account in the loan decision. Overall, the credit enhancement policy of ProCredit Bank is conservative. In the event of loans exceeding EUR 10,000 houses, flats or plots of land have to be pledged. Additionally, all other assets of the applicant and the personally liable guarantors are included. Most of the loans are collateralised to approx. 200%. In the event of loans of up to EUR 10,000 and the newly introduced agricultural loans the collateral requirements are more moderate and flexible.

ProCredit Bank Macedonia carefully monitors its loan portfolio. Same-day information about arrears can be gathered from the management information system. Provisions for loan losses comply with international standard requirements. Debt consolidation and loan restructuring are taken care of by the respective credit committee. Non-performing loans (NPLs) are brought before a court. On average, however, such legal proceedings take between 2 and 3 years. To save time and court expenses, ProCredit Bank Macedonia usually strives to reach extrajudicial agreements with borrowers in cases involving non-performing loans.

Since its foundation ProCredit Bank Macedonia has shown above-average growth and was able to establish its position in the financial sector in Macedonia. The balance-sheet total of ProCredit Bank Macedonia increased continuously between December 2003 and the end of 2005 from EUR 10.6 million to EUR 76.4 million. At the end of the first half of 2006 it had reached EUR 88.6 million. The average annual growth rate of the balance-sheet total in the period from 2003 to 2005 was 172 %. In the year 2005 the bank's after tax earnings were EUR 0.9 million. Earnings were retained and used to strengthen the capital base, which now amounts to EUR 10.0 million. The portfolio of loans outstanding increased almost nine times in the period from December 2003 (EUR 7.3 million) to October 2006 (EUR 66.8 million) and currently represents around 70% of the bank's total assets. Between 2003 and September 2006 ProCredit Bank Macedonia extended altogether 19,046 loans with a volume of EUR 64.8 million. The share of commercial loans that have been overdue for more than 30 days ("portfolio at risk") remained almost continuously below 1%. The main sectors represented in the commercial loan portfolio outstanding are trade, which accounts for 39 %, followed by the service sector, accounting for 36%, followed by agriculture and food production, accounting for 14% each and the producing sector with 11%. Loans are granted in local currency (MKD), USD and EUR, with MKD loans accounting for most of the volume (around 83% MKD, around 17% EUR and 1% USD). Short-term loans of up to 12 months (almost 60%) continue to dominate the loan portfolio. This is an indication of the low development stage of the Macedonian credit sector. However, there is substantial demand for medium to long-term investment finance loans to which the bank intends to react by introducing corresponding products. Deposits from non-banks (customer deposits) rose from EUR 1.8 million at the end of 2003 to EUR 45.2 million at the end of 2005. This reflects the successful efforts of ProCredit Bank Macedonia to mobilise savings deposits. Today savings deposits represent the second largest financing source of ProCredit Bank Macedonia. The current capital base of the bank is EUR 10.0 million. This is a share of 13 % of the balance-sheet total and can be considered as acceptable. The average return on equity in 2005 was 9% and the average capital adequacy ratio was 24%.

ProCredit Bank Macedonia is the only Macedonian bank that was granted an international rating up to now. The rating agency Fitch awarded a "BB+". Given the weak country rating of Macedonia, this is the best rating currently awarded to any company in Macedonia.

## Key results of the impact analysis and performance rating

The following indicators, which were to be reached at the end of the third business year of the bank (at the end of 2005), were defined to measure the achievement of the project objective, i.e. the sustainable use of loan offers and other financial services (provided at market-based conditions) by private micro and small enterprises from all sectors of the economy:

- The share of loans in the gross loan portfolio with interest and/or principal arrears of over 30 days (portfolio at risk) is at maximum 4 % (as of the end of 2005: 0.69%).
- Increase in the net loan portfolio to EUR 18 million (as of the end of 2005: EUR 47.9 million).
- The average loan amount of the total loan portfolio is EUR 5,000 (as of the end of 2005: EUR 3,750 million).

At the end of the third business year of the bank all three indicators for the achievement of the project objective were completely fulfilled or even exceeded. In the current business year the positive development of the indicators seems to be continuing. At the end of October 2006 the net loan portfolio already amounted to EUR 66.8 million. The average loan amount continued to fall to EUR 3.430. At the end of October 2006 the share of loans with interest and/or principal arrears had temporarily risen to just over 1% but then again fell to 0.97%. Thus figure reflects the excellent quality of the bank's loan portfolio. Especially in comparison with other Macedonian banks ProCredit Bank Macedonia is occupying a prominent place given its constantly good portfolio quality. In the expansion of its business activities ProCredit Bank Macedonia is making progress faster than planned and is doing so without any negative impacts on the portfolio quality.

The overall objective of the project was to contribute to the sustainable promotion of the private economy in Macedonia and to the development of the financial sector. The overall objective was considered achieved if at the end of the third business year 20% of the borrowers had received follow-up loans (according to the figures reported by PCB). Already at the end of 2005, 46% of the borrowers had been granted such follow up loans. Therefore, we consider the overall objective to have been fully achieved as well.

The establishment of ProCredit Bank Macedonia as a financial intermediary with external capital contribution has had noticeable positive structural impacts on the Macedonian financial sector. The high growth rates of the loan portfolio of ProCredit Bank Macedonia made a substantial contribution to improving the credit supply to MSEs and their access to the formal financial sector. Not only were new products (MSE loans) introduced and established in the market (broadening of the financial sector), but new customer groups (MSEs) could be reached as well (deepening of the financial sector). In addition, ProCredit Bank Macedonia had a positive demonstrative effect on local banks. The bank has shown that it can be a profitable business to grant loans in the lower segment (less than EUR 10,000). As a result other commercial banks are increasingly showing an interest in becoming active in the MSE lending segment. Altogether ProCredit Bank Macedonia is currently granting approx. 90 % of its commercial loans in the segment of loans with amounts of less than EUR 10,000. Additionally, the bank also extends loans of more than EUR 10,000 and, in this way, also serves the segment of small and medium-sized enterprises. Here it is directly competing with the established Macedonian banks. This competition is reflected in a continuous fall in interest rates, among other things. Customers benefit from this greater competition in the form of better conditions, offers of new products (e.g. loans with lower collateral requirements) and improved service.

Protecting the environment and natural resources did not play any role in the objectives of the project. Environmental aspects are routinely included in the loan appraisal, however, and ProCredit Bank Macedonia generally does not finance projects that have an adverse impact on the environment. The project had the general potential to contribute to gender equality. The high number of micro enterprises financed positively impacts employment, income and poverty reduction efforts. Participation and good governance did not constitute explicit programme objectives.

The audit of the records performed under the ex post evaluation revealed no misappropriation of funds.

In summary, we have arrived at the following rating of the project's developmental effectiveness:

In our opinion the project objective to enable private micro and small enterprises from all sectors to use loans and other financial services at market conditions in a sustainable manner was well achieved. In the segment of loans of less than EUR 10,000 ProCredit Bank Macedonia is the most important source of financing in the entire formal financial sector. The loan portfolio grew rapidly to EUR 47.9 million, which is 2.5 times the figure planned for the end of 2005. This is a clear indication of the strong demand for the bank's financing offers. The same statement can be made for the average amount of the loans granted, which is only EUR 3.750. Almost 100 % of its commercial loans were granted to enterprises with up to 10 employees. Overall, we classify the project's **effectiveness as good (sub-rating 1)**.

The overall objective of the project was to contribute to the sustainable promotion of the private economy in Macedonia and to the development of the financial sector. Already today almost one out of every two customers take out a new loan after having repaid their first loan. These follow-up loans usually have a higher loan amount than the first loan. What is more, the loan term tends to be longer. The project has exemplary, positive structural effects on the financial sector and on the development of MSEs in Macedonia. The country's financial sector was deepened (by reaching new customer segments) and broadened (by offering new financial products). Most of the bank's customers obtained their first bank loan from ProCredit Bank Macedonia, thus gaining access to formal financial services. The interest margin for short and medium-term loans has clearly fallen in the last three years due to the growing competition in the Macedonian banking sector, which was also substantially fuelled by ProCredit Bank Macedonia. By offering tailor-made loans to MSEs ProCredit Bank makes a significant contribution to supporting the private-sector economy and to creating and safeguarding income and employment in Macedonia. Overall, we rate the **significance/relevance** of the project as **good (sub-rating 1)**.

We rate the allocation efficiency of the project as good. The credit interest rates are positive in real terms and are in line with market rates. ProCredit Bank monitors its credit portfolio efficiently. Its portfolio-at-risk ratio is at an extraordinarily low level, and any cases of default are usually settled extra judicially, thus avoiding lengthy legal proceedings. We also rate the production efficiency as good. The productivity of the staff is good and continues to increase. Since the 2005 business year ProCredit Bank has operated profitably. The financial situation of ProCredit Bank is sound, too. Interest income continues to be the most important source of income of the bank, even though interest margins have continuously fallen in the last few years due to high competitive pressure. We consider the **efficiency** of the project to be **good (sub-rating 1)**.

In a summarised assessment of all impacts and risks described above, we **rate the project's developmental effectiveness as good (rating 1)**.

### **General conclusions and recommendations**

Selected promotional measures implemented under FC - for instance the introduction of new credit technologies at a single bank – may within a few years serve as an example and generate broad-scale effects. In order to achieve such effects the return produced has to be clearly documented (among others for potential imitators).

Access to medium and long-term investment finance is a decisive criterion for financing the assets of MSEs, particularly in the producing sector. Therefore, from a national economic viewpoint it would be desirable to provide medium and long-term financing to build up the asset base of MSEs. This should be part of the promotional strategy pursued.

## Legend

Developmentally successful: Ratings 1 to 3	
Rating 1	Very high or high degree of developmental effectiveness
Rating 2	Satisfactory developmental effectiveness
Rating 3	Overall sufficient degree of developmental effectiveness
Developmental failures: Ratings 4 to 6	
Rating 4	Overall slightly insufficient degree of developmental effectiveness
Rating 5	Clearly insufficient degree of developmental effectiveness
Rating 6	The project is a total failure

### Criteria for the Evaluation of Project Success

The evaluation of the "developmental effectiveness" of a project and its classification during the ex-post evaluation into one of the various levels of success described in more detail below concentrate on the following fundamental questions:

- Are the **project objectives** reached to a sufficient degree (aspect of project **effectiveness**)?
- Does the project generate sufficient significant **developmental effects** (project **relevance** and **significance** measured by the achievement of the overall development-policy objective defined beforehand and its effects in political, institutional, socio-economic and socio-cultural as well as ecological terms)?
- Are the **funds/expenses** that were and are being **employed/incurred** to reach the objectives appropriate and how can the project's microeconomic and macroeconomic impact be measured (aspect of **efficiency** of the project conception)?
- To the extent that undesired (**side**) **effects** occur, are these tolerable?

We do not treat **sustainability**, a key aspect to consider for project evaluation, as a separate category of evaluation but instead as a cross-cutting element of all four fundamental questions on project success. A project is sustainable if the project-executing agency and/or the target group are able to continue to use the project facilities that have been built for a period of time that is, overall, adequate in economic terms, or to carry on with the project activities on their own and generate positive results after the financial, organizational and/or technical support has come to an end.