EVALUATION OF AFRICAP MICROFINANCE FUND

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ABBREVIATIONS AND ACRONYMS

AVCA: African Venture Capital Association
DFID: Department for International Development
EBL: Equity Bank Limited
FINCA: Foundation for International Community Assistance
FASAL: First Allied Savings and Loans (Ghana)
FMO: Netherlands Development Finance Company
GLP: Gross Loan Portfolio
GNI: Gross National Income
IFC: International Finance Corporation
IFI: International Financial Institution
IPC: Internationale Projekt Consult
LFS: LFS Financial Systems
MBB: MicroBanking Bulletin
MFI: Microfinance Institutions
MIF: Microfinance Investment Fund
NGO: Non-governmental Organization
ROA: Return on Assets
ROE: Return on Equity
TA: Technical Assistance
TSF: Technical Service Fund
USAID: United States Agency for International Development
VC: Venture Capital

GLOSSARY

DATA IS NOT ADJUSTED FOR SUBSIDIES IN THIS EVALUATION WHEREAS BENCHMARKS DERIVED FROM THE MICROBANKING BULLETIN (MBB) ARE (SEE FOOTNOTE 4 FOR DETAILS ON MBB BENCHMARKS).

Debt/ Equity Ratio:	Total Liabilities/ Total Equity
Operational Self-Sufficiency:	Financial Revenue/ (Financial Expense + Net Loan Loss Provision Expense + Operating Expense)
Operating Expense/ Loan Portfolio:	Operating Expense/ Average Gross Loan Portfolio
Portfolio at Risk > 30 Days:	Outstanding balance, loans overdue> 30 Days/ Gross Loan Portfolio
Return on Assets:	Net Operating Income, net of taxes/ Average Total Assets
Return on Equity:	Net Operating Income, net of taxes/ Average Total Equity

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INTRODUCTION

AfriCap was first proposed in the late 1990s to be an equity investment fund for microfinance institutions (MFIs) in Africa. It was modeled on ProFund, a similar initiative founded in Latin America in 1995. The primary goal of AfriCap remains the same today as at inception: to demonstrate the commercial viability of microfinance in Africa. There are two parts to this goal. The first is to show MFIs can serve clients in a sustainable fashion. The second is that in doing so, MFIs can attract the capital required to remain viable businesses. This implies MFIs can attract sufficient portfolio debt and equity capital to maintain growth and adequate reserves while providing investors with a competitive return. These goals put AfriCap on the front lines of development finance where, in essence, the Fund is expected to help facilitate the sector's "transition to private capital."

When AfriCap was conceived, there were very few MFIs in Africa that were either commercially viable or on the path to becoming so. Challenges to becoming commercially successful were myriad and included lack of management talent, harsh operating environments, and poor regulatory regimes that both complicated and increased costs to growth and profitability aspirations. Additionally, microfinance in most countries had become highly dependent on foreign and national subsidies both for funding and operating support, which distorted both microfinance supply and demand.

It was thought that AfriCap, armed with an equity investment fund and a discretionary technical assistance facility, could invest in model MFIs that would provide both evidence of and catalytic influence on the commercial potential of microfinance in Africa.

THE FUND

With this environment and these objectives in mind, the AfriCap Microfinance Fund (AfriCap or the Fund) was established in 2000 with a $14.6 million equity investment fund and a companion $3.8 million technical service fund (TSF). Originally based in Dakar, Senegal, the Fund moved in 2006 to Johannesburg, South Africa. The Fund is managed by AfriCap MicroVentures Ltd. and invests in commercially oriented microfinance institutions (MFIs) in Africa. The Fund has made 11 investments for a total commitment of $10.5 million.

The Fund offers investees an "investment package" of equity and quasi-equity investment, active governance, and management/technical assistance funded through the TSF. The Fund has a ten year life after which investments will be sold with the capital and profits returned to investors. The Fund's capital must be fully invested in five years and all investment exited by the end of the Fund's life. To date, the Fund has made 12 investments and has divested from two, one fully and half of another for 1.24 and 2.3 times return on investment respectively (or internal rates of return of 132 and 24.5).

The TSF fund is used at the discretion of AfriCap fund managers and has two objectives. The first is to enhance investees' institutional development. The second is to communicate AfriCap's activities to audiences beyond their shareholder group in ways that have sector-wide impacts across Africa.[1] The TSF also provides funds for its own administrative management.

THE EVALUATION

After six years of activity, USAID and DFID jointly commissioned this evaluation of AfriCap to assess its mid term achievements and draw lessons that will benefit management, funders and other stakeholders in their design of and contribution to AfriCap II. The evaluation examines whether AfriCap achieved its goal of demonstrating the commercial viability of microfinance in Africa and whether the equity and TSF model has positive impacts on investee MFI performance, specifically:

- Was there greater concern regarding profitability and enhanced performance?
- Were investees able to leverage more debt as a result of AfriCap's involvement?; and
- Did MFIs experience mission drift as a result of increased commercialization?

The evaluation was also asked to discuss the TSF–equity fund model as a tool for developing microfinance in Africa and to assess AfriCap's role in future MFI equity demand in Africa.

The report has four parts focused on: 1) Investee Performance Impact; 2) Technical Service Fund; 3) Context: Transition to Private Capital and

[1] This evaluation was not mandated to evaluate AfriCap from a fiduciary perspective (e.g., if all TSF funding was put to use as reported) and as a result we did not verify TSF funding expenses, rather only the results or impacts of programmatic choices. Nor did it assess procedural or management quality questions, though investee performance evaluations can be seen as proxy measures of such. The evaluation did not investigate in any detail AfriCap's income, expense, grant disbursement and fund financial performance.

Equity Finance in African Microfinance; 4) Conclusions and Recommendations.[2]

METHODOLOGY

Secondary research, as well as stakeholder, investee, and management interviews formed the basis of our enquiry. A short survey provided investees an opportunity to express thoughts on AfriCap's impacts. Six of ten current MFI investees responded for a 60 percent response rate.

AfriCap's impact on investee performance indicators was measured for four of ten investments. These companies represent the universe of *mature investees* or those with AfriCap investments for over 15 months, and hence sufficient history to allow for impact to be observable. Performance is compared before, at the time of and after AfriCap investment and to benchmarks drawn from three different industry sources.

[2] This report is a condensed version of a longer report for USAID and DFID. Some details have been withheld for reasons of confidentiality or due to the proprietary nature of information.

INVESTEE PERFORMANCE IMPACT

AfriCap has committed to and made 12 investments for a total investment commitment of $10.5 million. The portfolio demonstrates a diversity of institutional types as well as investment instruments, and is invested in 12 different countries across the continent. The average investment to date is $740K and the average commitment is $880K. This average is slightly higher than the $600K AfriCap thought it would on average need to pay for its target of 25 to 35 percent minority share of each MFI it took a position in. At the same time, this average is lower than the average estimated aggregate investment AfriCap thought it would make when debt investments were included, which was projected to be between $1.5 million to $2.0 million per investee. All investments are in MFIs, save one that is in a microfinance "infrastructure" company that works with MFIs.

GROWTH, PROFITABILITY AND EFFICIENCY

Growth, profitability and efficiency performance were measured for four mature investments (i.e., all investments over 15 months old) at a time before investment, at the time of investment, and over 15 months after investment.[3] We found investee portfolio and number of loan clients had stronger growth rates after AfriCap's investments and rates far in excess of the benchmark performance by all African and large African MFIs found in the MicroBanking Bulletin (MBB) (see Table One). [4] Depositor growth rates were similarly higher though by a lesser margin, particularly compared to the all African average.

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[3] Due to lack of data availability and the different timing of the investments, we were not able to use the same data points within the three-year period for all institutions in the sample. For the purpose of analysis, however, the dates used were not so substantially different as to prevent trend analysis (see Appendix Four).

[4] See: Benchmarking African Microfinance 2005, (2005) The MixMarket, Washington, DC; Overview of the Outreach and Financial Performance of Microfinance Institutions in Africa, (2005); and MicroBanking Bulletin and Performance Benchmarks at: http://www.mixmbb.org/en/assets/Trend_Lines_2003-05_MFI_Benchmarks.xls. The MicroBanking Bulletin (MBB) is the premier benchmarking source for the microfinance industry, reaching back as far as 1997. The MicroBanking Bulletin's industry commentary, analysis and benchmarks are widely used by investors, donors and other service providers to facilitate greater standardization and a better understanding of developments in the microfinance sector. The publication features financial and portfolio data provided voluntarily by microfinance institutions (MFIs). This data supports benchmarks which allow MFIs to compare performance on a range of

TABLE ONE INVESTEE GROWTH TRENDS *			
	Before Investment	Time of Investment	After Investment
Gross Loan Portfolio (GLP)	41,810,690	69,308,700	233,598,896
GLP Growth		65.8%	237.0%
Benchmark: Africa		98.4%	9.2%
Benchmark: Africa Large		32.6%	20.4%
No. Borrowers	139,334	136,998	488,380
Growth No. Borrowers		-1.7%	256.5%
Benchmark Growth Rate: Africa		15.8%	-0.3%
Benchmark Growth Rate: Africa Large		4.0%	34.8%
No. Depositors	155,883	559,172	1,108,546
Growth No. Depositors		258.7%	98.2%
Benchmark Growth Rate: Africa		111.8%	94.8%
Benchmark Growth Rate: Africa Large		-22.8%	70.8%
*Sample size for this table is four MFIs. Due to different investment dates, data for each MFI does not come from specific years. Benchmark indicators are used from the most representative years. Trends are therefore indicative rather than statistically precise.			

Table Two shows investee efficiency and profitability to have generally improved after AfriCap investments. While operating cost measures suggest mixed performance, it must be recalled that AfriCap investments were made in MFIs requiring capacity investments and/or experiencing rapid periods of growth, either of which can have negative impacts on costs, profitability, and portfolio performance.

Nonetheless, Table Two shows AfriCap investees' performance was better on most counts after AfriCap investments. Return on assets (ROA) and Return on equity (ROE) profitability measures remained stable over time and outpaced both benchmarks by a large margin. Portfolio at risk (less than 30 days) improved after investment and bettered benchmarks by a significant margin. Most noticeably, and importantly, AfriCap investees had far superior returns on equity, a critical measure of commercial viability.

performance indicators (e.g., growth, efficiency, profitability, etc.) to its peer group (e.g., size, region, profitability etc.). It also allows for establishing industry performance standards. See http://www.mixmbb.org/en/company/about_the_mbb.aspx.

CAPITAL STRUCTURE

AfriCap investees showed marked improvement on both capital indicators collected (see Table Three). The capital to asset ratio shows capital adequacy held against future, unexpected losses due to credit, market, and operational risks inherent in lending activities. Commercial banks tend to maintain coverage of around 10 percent. Microfinance institutions tend to maintain a higher ratio of around 20 percent or more. This level provides risk insurance of a form, but is expensive. Many MFIs rely on equity to fund portfolio growth as opposed to debt. This practice and higher reserves negatively affects ROE and is indicative of prudent but not particularly sophisticated financial management. The lower level of reserves exhibited by AfriCap investees suggests commitment to an increasingly refined focus on profitability and confidence in financial risk calculations, asset management, and institutional ability to raise additional capital if required.

TABLE TWO
INVESTEE EFFICIENCY & PROFITABILITY TRENDS

	Before Investment	Time of Investment	After Investment
Operating Self Sufficiency	125%	113%	125%
Benchmark: Africa	107%	111%	107%
Benchmark: Africa Large	129%	128%	117%
Return on Assets	4%	2%	4%
Benchmark: Africa	-1.4%	-1.0%	-1.9%
Benchmark: Africa Large	2.3%	2.4%	0.9%
Return on Equity	22%	11%	27%
Benchmark: Africa	-3.6%	-2.8%	-4.9%
Benchmark: Africa Large	6.4%	11.5%	4.8%
Portfolio at Risk 30 days	5%	8%	4%
Benchmark: Africa	4.7%	3.8%	4.7%
Benchmark: Africa Large	3.7%	4.5%	5.2%

Sample size for this table is four MFIs. Due to different investment dates, data for each MFI does not come from specific years. Benchmark indicators are used from the most representative years. Trends are therefore indicative rather than statistically precise.

The debt to equity ratio shows AfriCap investees' overall leverage. We expected this ratio to rise with increased asset growth and improved access to portfolio refinance. As seen in Table Three, the ratio rose faster than benchmark averages. A large part of the difference can be explained by the common use of retained earnings by most African MFIs for portfolio growth – an expensive and not particularly effective strategy for achieving commercial viability or institutional expansion. Leverage ratios are low often because MFIs cannot access debt capital for portfolio finance.

Our data set did not allow for a direct empirical assessment of investees' improved access to capital resulting from AfriCap investments. Stakeholder interviews and the investee survey suggest, however, that AfriCap has had a modest impact on investees' ability to raise capital. Support has been both indirect through improved market credibility and direct through loan negotiation advice and contact making. This finding must be qualified by the observation that it was not AfriCap *per se* that provided credibility, rather investees interviewed unanimously stated it was the presence of the International Finance

Corporation (IFC) as an investor in AfriCap that provided this credibility.

Through provision of investment banking advice (an AfriCap investment officer is an ex-investment banker), AfriCap was also involved in the public offering of one of its investees. This said, investees did not generally report a great deal of new capital acquisition since AfriCap's investments, though that which was sourced did tend to have longer tenors and slightly lower prices. Modest amounts of new debt from local sources indicated some diversification of sources, particularly through modestly improved deposit business. It should be noted that several investees stated that they did not need great quantities of new capital given their strategic plans and present ability to absorb or put capital to use productively.

TABLE THREE
CAPITAL STRUCTURE AND TRENDS

	Before Investment	Time of Investment	After Investment
Capital to Assets	20%	25%	15% **
Benchmark – Africa	43	34	27
Benchmark - Africa Large	28.2	27.7	24.6
Debt to Equity	3.9	3.2	4.6
Benchmark – Africa	1.3	2.0	2.6
Benchmark - Africa Large	2.7	2.6	3.1

* Sample size for this table is four MFIs. Due to different investment dates, data for each MFI does not come from specific years. Benchmark indicators are used from the most representative years. Trends are therefore indicative rather than statistically precise.

** Does not include Socremo which is a relatively small institution with 47% equity to assets ratio and its inclusion would distort average as they are not weighted.

POVERTY ALLEVIATION

AfriCap's investees did not demonstrate any significant mission drift. Over the three time periods, AfriCap investees maintained relatively consistent percentages of women loan clients, levels that reflected MBB benchmarks. Average loan size over the three time periods did rise but was significantly lower than the MBB benchmark for large African MFIs. AfriCap investees' loan size was significantly larger than all Africa benchmark primarily because NGO MFIs have significantly lower averages (but are also typically highly subsidized without which they could not make small loans). Average loan size by Gross National Income data was not available to this study in a methodologically consistent fashion. Data for three investments prior to and at the time of investment was available and showed AfriCap investees offering loans below the all African average for the GNI benchmark (AfriCap average 104 in 2005 while the GNI average was 100 for all MFIs and 144 for large African MFIs.). These data suggest that while AfriCap investees did not exhibit mission drift, they do not exclusively serve the poorest of the poor or those living on less than US$1 per day, though certainly a significant number of the poorest of the poor were being served. These findings are also consistent with the two previously mentioned surveys.

TABLE FOUR
INVESTEE SOCIAL IMPACT

	Before Investment	Time of Investment	After Investment
Women as a % of Loan Clients	52%	41%	56%
Benchmark: Africa	65.3	52.7	54.5
Benchmark: Africa Large	54.9	40.4	52.1
Average Loan Size	329	566	428
Benchmark: Africa	96	130	164

INVESTEE PERFORMANCE DISCUSSION

Our analysis shows a *positive association* between AfriCap investment in an investee and enhanced investee performance (though it is not empirically possible to directly attribute the relationship to AfriCap specifically - see TSF discussion below). That performance has improved on all measures and investees have outperformed their African peers on most indicators, suggests AfriCap's investment and investee performance is not coincidence. At

the very least, we can say AfriCap chose its investments well. Some caution is required as the data sample is small and the performance was measured when AfriCap had a very small number of active investments to manage. The Fund's ability to manage a greater number of investments at the same time will test their capacity in an entirely new way.

AfriCap's participation has also modestly enhanced investees' ability to raise new capital. While investees did not report specific examples of how AfriCap helped to raise capital, most felt that the credibility brought by AfriCap has or will help in capital acquisition (albeit relying heavily on IFC reputation).

On the issue of increased attention to profitability, data suggests that investees are employing more precise and coordinated capital and risk management strategies which seek at once to control costs and put capital to more profitable use through leverage. Finally, AfriCap investees are serving a variety of clients including the poorest of the poor, indicating that they have not succumbed to mission drift. The percentage of women served is also consistent with African benchmarks.

KEY FINDINGS

- Investees saw growth, efficiency and profitability performance increase after AfriCap investments;
- Investees report better access to capital after AfriCap investments; and
- Investees show no significant mission drift away from low income markets.

TECHNICAL SERVICE FUND

AfriCap offers investees an "investment package" of equity and quasi-equity investment, active governance, and management/technical assistance provided through its $3.8 million Technical Service Fund. The TSF can be used at the discretion of AfriCap fund managers and has two objectives. The first is to enhance investees' institutional development. The second is to communicate AfriCap's activities to audiences beyond their shareholder group in ways that have sector-wide impacts across Africa.[5] The TSF also provides funds for its own administrative management.

CATEGORY ONE - SUPPORTING INVESTEES

Category I funding has the objective of defraying development and operational costs of "early stage" companies through technical assistance (TA) grant funding. This is justified, at least in part, by

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[5] This evaluation did not include an evaluatation of AfriCap's fiduciary standing (e.g., was all TSF funding put to use as reported?) and as a result we did not verify TSF funding expenses, rather only the results or impacts of programmatic choices. Nor did it assess procedural or management quality questions, though investee performance evaluations can be seen as proxy measures of such. The evaluation did not investigate in any detail AfriCap's income, expense, grant disbursement and fund financial performance. Findings and future discussions are thus necessarily conditioned by limitations of scope and resources.

potential high social returns on such investments (i.e., poverty alleviation). These expenditures are intended to confront classic private equity challenges related to enhancing growth and resolving specific business problems (e.g., improve management information systems, better human resource policies etc.). TA also has the objective of encouraging a more "commercial" business culture.

AfriCap's demand-driven TA funding focuses on investee priorities and has, as anticipated in the prospectus, supported a range of TA projects from systems upgrades and management support, to human resources training. AfriCap has spent just over $1.3 million by Q1, 2007 (estimated) on technical assistance to investees. AfriCap's TA funding to MFIs over 15 months old averaged $75k annually, or 25 percent less than the amount anticipated.[6] The majority of TSF Category I funding has been used to enhance management capacity either through subsidizing management services or through "baskets" of TA services. These latter services include management, process, product and service support. Modest amounts were spent on business planning exercises (including business planning and investment preparations) and incurred the least costs.

BOX ONE

AFRICAP TSF CATEGORY II EXPENSE ON HEALTH AND RISK MANAGEMENT – HIV/AIDS

The HIV/AIDS risk management initiative, supports rigorous risk management practices by the microfinance industry and financial services industry to meet and manage the risks created by HIV/AIDS. A guide "Partners and Action: Financial Institutions and Health and HIV/AIDS Risk Management," was produced and the organization and hosting of a workshop with more than 60 participants from 30 countries in Africa.

It is difficult to empirically attribute investee performance improvements to AfriCap TSF support, though some attribution was possible in cases where TSF funding was the sole and largest supplier of TA funding. Interviews and surveys clearly suggest, however, that TA funding was important. Investees tell of being highly satisfied with TSF support. A confidential survey asking investees to rate their AfriCap TSF experiences showed excellent average ratings (all ratings were above four except in one instance a three was given for knowledge of local context - see Table Five).

While most investees believed TA funding was valuable, they noted that funding *coupled* with AfriCap's board participation was key to maximizing the Fund's overall performance enhancement impact. Investees reported that this combination contributed to a more disciplined profit-oriented business culture, and led to stronger strategic decisions and improved management execution. Like TSF funding, AfriCap's governance involvement is favorably viewed by all stakeholders interviewed (management, board members, investors, etc.). Investees did voice

TABLE FIVE
INVESTEE TSF EXPERIENCE

Rating system: 1 poor and 5 excellent	
Experience of service provider	4.8
Knowledge of local context	4.4
Timing of services	4.4
Duration of services	4.6
Price of services	4.6
Confidential investee survey of 10 MFI investees with 6 responses or a 60% response rate.	

[6] Base figures are drawn from the USAID – AfriCap agreement. The average is about 30 percent less than AfriCap's prospectus.

minor issues common to situations where a well-informed, motivated minority shareholder actively pushes for change. By and large, however, interviews suggest AfriCap's governance role is valued as much -- or possibly more -- than TSF funding, though investees did voice a unanimous preference for both together.

CATEGORY TWO – "SECTOR" SUPPORT

Category II expenses have the specific objectives of a) supporting communications and industry promotion activities to legitimize the microfinance industry and b) accompanying the development of AfriCap's investment portfolio to generate "public good" outcomes. These goals have the intention of ensuring AfriCap and AfriCap's TSF investors would see benefits to the sector beyond the commercial demonstration of Fund profitability.

AfriCap has spent just over $1 million, or one third of TSF funding, on Category II activities. Communications expenses have been split equally between AfriCap's annual report and other forms of communications. The AfriCap Microfinance Network provides funding for investees to work together on specific shared business problems ($42K), creating a common strategy network platform or providing solutions to specific shared problems ($45K), and CEOs Roundtable ($50k). A further $23K has been spent on investee network development to encourage investees to share knowledge and best practices. The focus of the network to date has been on the use of technology (e.g., electronic banking cards, cell phone technology etc).

AfriCap has also consciously pursued financial innovation as a part of its "social good" investments. It has invested $169K in a company seeking to provide an electronic card based banking platform which through a pilot program hopes to reach 10,000 cards holders throughout Africa. A second investment will support an Innovation Centre to be hosted by an investee. The Centre will pilot the use of technology to support customer solutions and more efficient business practices to the benefit of AfriCap Fund investees and the industry in general.

In other Category II expenses, the TSF also sponsored a Bank Downscaling event ($96K) and sponsorship and participation in other industry events that simultaneously helped to promote AfriCap, explore pipeline potentials, and generally support the industry. Finally, AfriCap has engaged in a significant project to provide risk management guidance to the industry related to HIV/AIDS and microfinance (see Box One). This initiative represents the single largest TSF expense ($240,000) and brought together many industry stakeholders to produce and promote a health and HIV/AIDS risk management guide for MFIs.

BOX TWO

SOCIAL INVESTMENT FUND PERFORMANCE

Many hundreds of successful commercial social investment CII funds suggest that dual objectives can be managed simultaneously. Most of these funds, however, are much larger and most have passive social impact goals (i.e. avoiding negative, as opposed to seeking out positive impacts). Enterprising Solutions has evaluated several development funds with dual objectives (e.g., environmental, social, microfinance, labor rights funds, etc.) and has found that "dilution" effect concerns are legitimate and that there is a *strong negative association* between multiple development objectives and financial success.[1] We suspect too, though we have not empirically confirmed, that fund size is a critical element to managing social good objectives: the smaller the fund the greater the risks associated with multiple business objectives.

CATEGORY THREE – TSF ADMINISTRATION

Category III expenses relate to the management of the TSF. AfriCap billed a total of $1.3 million to manage TSF funds, or 36 percent of total funding from 2001 to 2007. Of this, 40 percent went to salaries

and benefits, 15 percent to travel, and 41 percent to overhead. While this is not a fiduciary evaluation of AfriCap, it is notable that since inception (including Q1 2007 estimates) AfriCap will have received an estimated $4.0 million in fund administration fees compared to a total of $1.3 million in TSF administration and overhead funding. This means of its total income, roughly 25 percent of the Fund's *guaranteed* income was derived from Category III expenses. The TSF, in short, provides a significant contribution to the maintenance of AfriCap in the form of shared office space, personnel and related overhead expenses.[7]

This level of Category III expense is not surprising. AfriCap's three percent fund management fees is a figure borrowed from the venture capital sector and is not derived from significant past experience of other funds. AfriCap is not like most venture capital (VC) funds from which this percentage fee is derived since most funds are national or regional in focus. Most VC funds also work in economies that are stable, have a large pool of trained managers to draw from, and fund and transaction sizes are dramatically larger. Small business funds without TA funds, by contrast, regularly charge 6.5 percent fees with the extra 3.5 percent being considered a development fee.

TSF DISCUSSION

This evaluation was tasked with addressing whether the combination of a discretionary technical assistance fund and an equity fund was an appropriate model for supporting the commercialization of microfinance in Africa. To answer this, we start with two commonly asserted premises for having an investment fund with discretionary technical assistance funding, both of which figured in the creation of AfriCap and the TSF.

UNDERWRITING COSTS AND OFFSETTING RISK

The first premise asserts that because equity investments in African MFIs are difficult to make, a TSF fund is required to offset risks and underwrite costs associated with uncharted financial waters. Funding is necessary to bolster investee performance and subsidize management costs that are inevitably high as a proportion of invested funds (i.e., small average investments and fixed investment management costs).

Many MFI investors interviewed for this evaluation and similar work undertaken by USAID generally accept this premise to be true, though not exclusively.[8] There are those who believe if an MFI is "investable", then any technical assistance required can successfully be capitalized.

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[7] According to AfriCap and readings of its prospectus and donor agreements, there were no set limits to the amount of Category III expenses as a percentage of the fund. By comparison, ShoreCap has a 15 percent limit.

[8] In this instance, one must remember the moral hazard associated with asking such a question to an investment agent who undoubtedly would take (and rightly so) any free money that came their way without much difficulty. This conclusion is drawn from interviews with stakeholders for this evaluation and other investment related publications. See Appendix 1 for relevant references.

Those who hold this position also assert that if it were not for market distorting interventions by numerous actors (including donors and microfinance investment funds (MIF) offering non-fully risk adjusted interest rates and return expectations), more purely commercial investment could be made. This counter proposition has more credence when funds invest exclusively in top-tier MFIs where capitalized TA can be put to use productively in short order. The experience of ProFund, a similar fund for Latin America recently wound up, and that of a growing number of other funds making equity investments, seems to support the notion that equity investments *can* be made in the absence of discretionary TA funds. Their success, however, is conditioned by making investments in more mature markets (as in the case of ProFund) or in top tier MFIs. There is also the issue of indirect TA support as well, as many MFIs have TA from a variety of non-investor related sources.

Once we picked our targets, now we must put on a beauty pageant for MFIs that weren't even on the map two years ago.

MIF Investment Fund Manager

Whether practitioners are correct is not for this evaluation to say. What we can say, however, is that in the case of AfriCap, equity investments coupled with TA and governance advice have had a positive empirical association with improved investee performance. Would such outcomes have been otherwise achieved? Possibly, but the question may be moot in the medium term as investment in the African microfinance sector is increasingly teamed with discretionary TA funding. Indeed, as the supply of MFI investment capital grows worldwide, competition for placing funds in "investable" institutions is becoming intense. In Africa, where the supply of investable MFIs remains relatively small, TA funding is becoming a critical element of a competitive "investment package". Reports from most corners of the MFI "capital supply" community indicate this trend is prevalent in Africa among the top tier MFIs. The need for TA funding, as a result, is not just a function of offsetting risk and underwriting costs, it is an element in simply being competitive as an investor. Moreover, AfriCap investees often face highly subsidized competitors in most markets from both international MFIs with investment and support from organizations like FINCA, ProCredit, LSF, Opportunity International, and state-sponsored programs or institutions.

BALANCING MULTIPLE GOALS WITH IMPACT

The second premise holds that TA funding in association with equity investments can create social goods beyond those generated by investing in MFIs. In the case of AfriCap, this means using TSF funds to demonstrate the benefits of commercialization to the African microfinance sector as a whole.

Opinions are mixed as to the validity and efficacy of such an approach. Many industry observers question, for example, whether a fund can successfully manage multiple financial and social objectives or "social

goods goals". They believe attention paid to "non-core" investment activities diverts attention from primary financial objectives (i.e., in the case of AfriCap, demonstrating the commercial viability of microfinance in Africa through profitable investments). Others posit that while the vehicle (i.e., the equity-TA fund model) may be the correct tool, distance between the two funds is required for both objectives to be concurrently served and impacts maximized. They would cite as an example company foundations pursuing social goals related to its founder's business interests. The social good question is complex given all the variables to consider. To simplify assessment, there are two levels at which to consider the impact of the TSF on social goods outputs.

At the level of AfriCap's own performance, the TSF has contributed to the Fund's goal of demonstrating the commercial viability of microfinance in Africa. The Fund has benefited from investee performance enhancements. AfriCap has also seen a good share of its overhead paid for by the TSF, through pipeline development, business plan and deal work, fund promotion and fund credibility building (e.g., event participation, sponsorships, annual reports, etc.).

Conversely, there is no evidence that Category II activities negatively impacted the Fund's performance. Some specific investments activities were not as successful as desired (e.g., aborted deals that received business planning support, losing TA investments in another MFI, etc.). These negative experiences are inevitable in the course of doing business and did not have significant negative impacts on AfriCap's overall performance, nor would they had the investments been capitalized.

SECTOR LEVEL IMPACT

At the sector impact level, the degree to which the TSF has allowed AfriCap to impact the commercialization of microfinance is more debatable. Our findings suggest the TSF has not had a significant impact on the market, but has had some influence at the international practitioners' level (including donors, MIF funds, consultants, etc.). Most African microfinance sector stakeholders outside international practitioners' and the immediate investee stakeholder universe, however, have little detailed knowledge of AfriCap other than it is a source of equity funding. The Fund is simply too small and its TSF Category II activities too modest compared to the many donors with multi-millions to spend in Africa on the same or similar goals.

This is not to say that specific TSF sector initiatives have not been successful. AfriCap's support for sector events and its HIV/AIDS Risk Management guide have received positive feedback. The demonstration and business impact of its innovation centre and electronic card investments may also yield good and broad impact. However valued these activities may be, when set against the influence and impact of larger donor activities begs the question: is an equity fund the most efficient and effective tool for sector building?

KEY FINDINGS

- Category I TA is associated with performance enhancement for all MFIs and all measures of TA (efficiency, profitability, and ability to raise capital);
- TA funding is likely required to ensure level playing investment field and ensure competitive investment sector;
- Category II TA has helped to enhance credibility and support Fund capacity and has achieved modest sector wide impacts;
- Experience suggests social funds with simple missions and scale as measured by asset size will have greater chance of success and influence on the sector.

CONTEXT: TRANSITION TO PRIVATE CAPITAL AND EQUITY FINANCE IN AFRICAN MICROFINANCE

The primary goal of AfriCap microfinance is to demonstrate the commercial viability of microfinance in Africa. There are two parts to this goal. The first is to show that microfinance institutions can serve clients in a sustainable fashion, i.e., make a profit. The second is that in doing so, MFIs can attract the capital required to remain viable businesses. This goal requires that MFIs attract sufficient portfolio debt and equity capital to maintain reserves and provide investors with an adequate return on capital. It also implies expansion of services to the unserved poor, which, in turn demands capital for institutional growth and development of new markets. These development goals put AfriCap on the front lines of finance development where in essence, the Fund is expected to help facilitate the sector's "transition to private capital."

Below we outline the challenges facing this mission by reviewing the market for microfinance in Africa, the resulting demand for capital among MFIs, and MFI financing trends within Africa.[9]

EQUITY INVESTING IN AFRICAN MFIS: CONTEXT

Banks in Africa, as in many developing regions, focus primarily on large commercial clients and higher net worth retail clients. Less than 15 percent of all bank assets are lent to business of any size and usually no more than five percent of any African nation is "banked."[10] Given the critical role of finance as an input to economic growth, the implications of limited financial infrastructure are significant. This is particularly so in light of several years of growing, low inflation economies enjoyed by most African nations. These conditions are generating significant new market opportunities – opportunities that many low income households, micro and small business are unable to take advantage of in the absence of financial services.

Even if banks demonstrated greater willingness to serve the "un or underserved", weak financial systems, non-existent credit information, slow and expensive payment systems, weak contractual law and enforcement systems, inappropriate or non-existent regulatory regimes, shallow managerial talent pools, and poorly developed communication infrastructure combine to provide significant disincentives to outright barriers for financial sector expansion. Unlike many other regions around the world, most African nations are still emerging or frontier microfinance markets in terms of sophistication of MFIs and regulations to support the sector.

Despite these challenges, African MFIs have proven that they can profitably serve the poor. Still, MFIs reach only a fraction of the low income market– in most countries less than 2.5 percent.[11] While this affords good growth prospects, constraints to serving a larger market share clearly inhibit the expansion of the sector to investors. Returns on equity to the sector in most African nations do not make an immediately obvious case for investment given competing alternative uses of capital (the All African average ROE between 2003 -2005 was 3.7 and 7.5 percent for large African MFIs).[12] An informal survey of

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[9] A host of other relevant elements to a successful transition to private capital are not discussed, such as financial regulatory issues, business and tax laws, financial infrastructural weakness, competing investment opportunities, etc.

[10] See for example Bald, Joachim (2007), Regional MSME Investment Fund for Sub-Saharan Africa (REGMIFA), KfW and IFC; Basu, Anupam, Rodophe Blavy, and Murat Yulek (2004) Microfinance in Africa: Experience and Lessons from Selected African Countries, International Monetary Fund, Washington, DC.; Benchmarking African Microfinance 2005, (2005) The MixMarket, Washington, DC.

[11] Evaluation of International Fund for Agriculture Development's (IFAD) Rural Finance Policy undertaken by Enterprising Solutions in 2006, available upon request from IFAD

[12] *MicroBanking Bulletin* (MBB) Issue No.14, available at http://www.mixmbb.org/en/

BOX THREE
TROUBLE AHEAD? HIGH INTEREST RATES & FOREIGN OWNERSHIP

The potentially toxic public relations and political brew of high interest rates and foreign ownership may have been foreshadowed by the outcry by many in the microfinance community over the recent Compartamos initial public offering. Compartamos listed its shares on the Mexican Stock Exchange for over US$400 million. The listing provoked an extensive debate among MFI practitioners from around the world about the development validity of a few owners benefiting so largely from a microfinance serving the poor. The foreign ownership element was not central to the debate, but did draw some fire. The issues that flamed the debate most was the incorrect impression that Compartamos charged over 100 percent interest to it's largely female client base (the rate is much lower, in fact). Growing political sentiment in all regions of the world that microfinance interest rates are too high may have significant political implications for microfinance in Africa.

African Venture Capital Association (AVCA) members, for example, shows portfolio returns expectation of around 20 percent -- returns that some MFIs are capable of achieving but with much less certainty competing opportunities.[13] This and the generally small pool of private equity capital combine to ensure a scarcity of private equity capital for MFIs in Africa.

Tough Investing. "Investability" concerns compound scarcity and competing investment challenges. In microfinance, corporate governance bias towards mission-oriented capital and governance structures such as cooperatives, both reduce the demand for and complicate the injection of private equity in African MFIs. Cooperatives, for example, often do not want, or cannot easily take on new equity. NGO MFIs and newly transformed MFIs are often heavily influenced by mission and often fear or distrust private capital, particularly if it is strongly profit oriented. Conversely, private capital is often uncomfortable with sharing ownership with "socially-oriented" owners, particularly those not familiar with the discipline and orientation of risk capital.

These challenges are compounded by private capital owners' lack of knowledge about microfinance and a lack of regulatory predictability or protection (particularly in reference to interest rate caps). Investors must also consider the long term nature of any commitment due to few easy exit options available in any sector, let alone microfinance. Stock market capitalization, for example, is typically less than 25 percent of GDP (whereas in more developed countries it is a multiple of GDP) and markets have limited liquidity, offering all but a few MFIs a realistic source of capital and investors of exit.[14] Maintaining capital liquidity in traditionally volatile economies is a standard investment practice among investors, a consideration which further decreases the attractiveness of microfinance.

Finally, and more generally, the buying and selling of businesses (or parts of businesses) in Africa is still quite a new phenomenon and there is little institutional infrastructure or business culture in most countries to support this activity. These conditions discourage minority share ownership and limit an institution's ability to source important growth capital.

Development Capital Remains Important in the Transition to Private Capital. So even while exemplary and successful MFIs exist in Africa, as a sector, microfinance does not yet offer a broadly compelling investment option for private capital. The relative scarcity of capital and significant barriers to financial development will continue to constrain sector growth and the transition to private capital in Africa. As a result, "development

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[13] See www.avcanet.com.

[14] See de Sousa-Shields (2004) *et al* Sustainable and Responsible Investment in Emerging Markets, International Finance Corporation of the World Bank.

capital" from donor organizations, international financial institutions, and microfinance investment funds remain critically important to sector development. They are, by all measures, indispensable risk takers and, as such, catalysts for private capital despite the relatively modest funding they can make available. But very little such funding reaches Africa. For example, of funding invested by global international financial institutions only $155 million or eight percent has been invested in Africa (2005 figures). Of this, less than ten percent (estimated) has been equity investments.[15] This said, development capital equity tends to be placed in the largest and best known or least risky MFIs. Just three MFIs account for 31 percent of all development capital in Africa. Over 40 percent of all is invested in only six countries; by contrast, less than two percent of this total is invested in 20 least funded countries. The result is many high growth opportunities are likely being overlooked.[16]

The impact of development capital is also distinctly different than that of private capital. For example, development capital rarely enjoys the kind of oversight that direct ownership applies to risk capital. Development capital's social agenda can also send complex business signals whereas the restless and clear drive to maximize profitability of private capital does not. International financial institutions (IFI) and bilateral agencies are simply not built to make investments in the same way as a venture or equity fund like AfriCap (which is why they often use funds to invest their capital). Similarly, MIFs often have neither capacity nor the incentive (although this is becoming less true as they too move towards more private sector models) to push MFIs the way in which purely private capital can. So while overall sector impacts are positive, development capital can constrain the transition of MFIs from businesses with a predominantly social ethos to ones with disciplined profit and social missions. Such a transition is critical if private capital is to fully relieve donor agents from the task of meeting the financial needs of the hundreds of millions of poor in Africa.

The support of commercially oriented MFIs may also prove critical to a simultaneous but nascent trend of commercial bank interest in microfinance. Increasingly, commercial banks are considering the microfinance market. Most have little or no knowledge of the market. As a result, some have considered purchasing or working through established MFIs (e.g., informally, infrastructure sharing, wholesale finance arrangements, etc.). Some observers suspect that the future of microfinance in Africa will be dominated by commercial banks. If this is the case, then grooming MFIs to have a commercial outlook may prove critical to facilitating formal linkages or outright sales of MFI assets, and there remains a need for a fund such as Africap as discussed below.

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[15] See Xavier Reille, Hannah Siedek, Nicole Pasricha,: Public Investor Microfinance Porftfolio, CGAP 2005 Survey.

[16] Isern, Jennifer, CGAP Annual Conference in Benin, October 2006, cited in Bald.

ANOTHER EQUITY TREND TO CONSIDER

Another notable if nascent microfinance investment trend in Africa is the finance of internationally owned and controlled MFIs. There are two threads to follow.

The first relates to "greenfield" or starting up brand new MFIs. These efforts are predominantly led by international microfinance organizations following the IPC-ProCredit model, where greenfield operations are 100 percent owned and managed by international firms. Greenfield operations typically have significant start up subsidies ranging from $1.5 to $2.5 million and often enjoy minority share investments from development capital suppliers.[17] The second thread is spun by international organizations such as Opportunity International, FINCA, and ACCION among others, who also have access to significant technical assistance and grant funding (e.g., many have received multimillion dollar grants from foundation and development institutions). While it is debatable that these internationally owned MFIs dominate national microfinance markets, they conceivably have the technical and funding capacity to do so, and in some markets have already taken considerable market share. More importantly for this evaluation, they have the ability to attract – even monopolize – scarce development capital resources.

The scope of this evaluation was not to empirically assess the depth and implications of the internationalization of microfinance in Africa. It is worth articulating some of the arguments in this report for public debate as they reflect on the need for "made in Africa" solutions. Certainly, international efforts have resulted in some excellent microfinance institutions and have increased the number of poor served. In many markets, international MFIs have catalyzed competition and the adoption of best practice microfinance. For many, these impacts are both good and sufficient, believing that ends justify the means or, if the poor are served, so too is the mission of poverty alleviation.

There are others, however, who wonder about the implications of international ownership, particularly in those institutions where national managers do not easily rise beyond the branch level. Those with this position argue that internationalization does not necessarily maximize the full development impact of the sector the way national ownership might. There are some significant economic and political considerations to this argument such as the potential political backlash over supporting the internationalization of microfinance assets. There is increasing political concern over the perceived high interest rates being charged

[17] It should be noted that often greenfield MFIs are supported in countries or regions where no other MFI exists or is willing to go. In some cases, however, they are established in markets with viable MFIs. Even in some underdeveloped markets such as the Democratic Republic of Congo or Sierra Leone, ProCredit has entered with subsidies that are as large as the several local institutions striving to be viable. In Malawi, Opportunity International also supports its organization with significant subsidies.

the poor. Juxtaposed with increasing international ownership, high interest rates may raise concerns about commitment to local capacity development and sustainable development impact of microfinance.[18]

AfriCap, as an African based and managed investment fund, provides a counterbalance to the internationalization of microfinance in Africa: a made in Africa solution which supports through its investments a range of MFI development options including local ownership, greenfields, and international ownership. Given that some observers predict commercial banks will increasingly enter the market, a savvy investment fund developing MFIs to sell would be a boon to the sector goal of serving more poor faster. The impact of a commercial social investment fund selling MFI stakes to commercial players may have significance far beyond microfinance if it can provide quantitative proof of financial and social performance.[19]

THE END GAME: WHAT ARE THE OPPORTUNITIES?

By some estimates, MFIs in Africa will require approximately $400 million in portfolio finance and about $60 million in equity over the next seven to ten years just to maintain current rates of growth. Lack of sector informed and "risk friendly portfolio refinance capital has left many MFIs reliant on their own equity and retained earnings for a significant portion of their portfolio finance, which on average constitutes about 25 percent across the continent."[20] This, along with typically high reserve and capital adequacy requirements, leaves a considerable portion of funding unavailable for growth and development. Low leverage ratios may dampen demand for equity, but perhaps not for various types of growth oriented mezzanine capital (e.g., preferred shares, subordinated convertible debt, etc.) By one estimate, 63 smaller or Tier Two MFIs will require an estimated $160 million in portfolio finance and $20 million in mezzanine finance (equity and a variety of debt instruments) over the next five years.

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[18] It is not the purview of this paper to challenge or judge the value of the greenfield or foreign ownership model except as it relates to the context of investment in African MFI equity. True, the model has not been exposed to serious regional and or global economic downturns. The consequence of not anticipating the effects on African microfinance and the ultimate reaction of, for example, ProCredit a multinational microfinance corporation, to the simultaneous meltdown of sub-Saharan economies and troublesome assets in Eastern Europe (i.e., who gets supported and who doesn't) is neither clear nor tested. The systemic risk and systemic response of international microfinance corporations are unavoidably serious considerations for the long term development of microfinance in Africa.

[19] AfriCap's social impact work may be important in this regard, although a review of the scopes of work for developing social indicators suggests using and/or creating systems that are not current or known to commercial institutions. There may be some merit to the idea of considering established norms such as the International Standards Organizations or the Global Reporting Initiative systems – imperfect as they are -- which have good and established market credibility.

[20] Bald, Joachim (2007), Regional MSME Investment Fund for Sub-Saharan Africa (REGMIFA), KfW and IFC.

Another 50 Tier One MFIs will require $73 million in equity (inclusive of subordinated debt).[21]

Trends and challenges not withstanding, there appears to be a modest if somewhat difficult market for equity investments in African MFIs. Significant market information asymmetries seem to obscure the view of development capital for smaller opportunities and thus, finding the next "Equity Bank" deal will require investment savvy beyond what most international investors have developed. Managing and developing small investments, once made, afford even greater challenges for most funders, if not only for the relatively small transaction sizes, but for the technical challenges of growing small institutions (which are such that many organizations now prefer to start greenfields over investing in existing institutions). This is particularly true of second tier MFIs which demand higher risk capital and "early stage" governance guidance (e.g., distressed MFIs, transforming NGO MFIs, small commercial banks, or privatizing banks, etc.).

Finally, it is important to consider the potential impact AfriCap may have on the sector if commercial banks begin to enter the market in a significant way. AfriCap's buying and selling of MFI shares will have two potentially important commercializing impacts on the sector. Through its investments directly, it is likely AfriCap will consider selling shares to commercial banks, and by doing so, demonstrate the viability of the sector to the conventional financial system. Indirect impacts by example will also affect commercial bank and conventional investor attitude to the sector, likely encouraging greater investment and interest in the sector. Few commercial actors are in a position to concretely demonstrate the sector's commercial potential as AfriCap.

KEY FINDINGS

- There is a large unmet retail level demand indicating significant potential for existing and new institutions;

- There is modest demand for equity and more for mezzanine finance among Tier One and Tier Two African MFIs;

- Demand for capital will require an experienced niche investor focused on high risk MFIs, this is particularly true of Tier Two MFIs where greatest gains can be made;

- A "made in Africa" fund provides local and regional credibility that provides both tangible and intangible value to the commercialization debate/trend in Africa particularly given significant and growing internationalization of MFI equity investments in Africa.

[21] ibid.

CONCLUSIONS AND RECOMMENDA-TIONS

Results from this evaluation show that AfriCap has proven to be a good high risk MFI investor in a challenging operating environment. Our data suggests that the relationship between investee performance improvements and AfriCap's participation are neither a coincidence nor simple luck. Rather, it appears to be a combination of making good investment decisions and/or the sound application of capital, governance, and TA investments. We would also posit that AfriCap's TA, in combination with solid, profit-oriented governance has yielded greater value than either element alone and that good governance was an unappreciated element of their investment package until some time after investment.[22]

While investee performance trends are clear, AfriCap's participation has not obviously enhanced investees' ability to raise new capital, though investees do feel that the Fund has raised their credibility in local capital markets (if only vicariously through IFC's reputation). Fund investees also seem as committed to the low income market and mission drift within the portfolio is not apparent.

As noted, although it is not possible to attribute performance enhancement with any given action taken by AfriCap, the TSF has certainly been an important tool for AfriCap. In addition to providing performance- enhancing TA, the TSF has helped support AfriCap's infrastructure and human resource capacity and development. It allowed AfriCap to participate in and support sector events that proved important venues for promoting the Fund, sourcing deals, and engaging sector professionals.

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[22] Enterprising Solutions has interviewed over 30 investees of different funds on a confidential basis over the course of the last three years and invariably 80 to 90 percent of investees in any given portfolio have recognized the value of governance input.

Modest Returns to Sector Development. The Fund's impact on supporting microfinance commercialization in Africa is debatable. At the level of the investee, performance enhancement provides a demonstration of commitment to and the results of commercialization. This undoubtedly affects competition and fosters improved MFI performance in local markets. It is our judgment, however, that overall trends towards commercial microfinance in Africa would not be weaker in the absence of AfriCap TSF Category II activities. TA subsidies with this objective have been and continue to be available from many quarters for both MFI and microfinance/finance sector infrastructure level investments. AfriCap's influence on the sector seems limited to a small circle of stakeholders in national markets and international practitioners and donors and, ultimately, the Fund must be viewed as one actor among many promoting commercialization of microfinance in Africa. It is by far neither the largest nor most influential.

This observation questions the efficacy and strategy employed by AfriCap donors as a means to promote commercialization of microfinance in Africa. It is not that AfriCap cannot pursue this objective without impact. Nor is it the case that this objective materially diverted AfriCap's attention from its primary investment objectives. There is just little compelling evidence that the same funding applied elsewhere by others could not achieve the same results, or that funding available to AfriCap added significantly to overall efforts. We also conclude that supporting the *growth and profitability* of AfriCap as a "social investment fund" is a better strategic route to sector wide influence and demonstration effects. Finally, there are considerable economic, political and sector influencing benefits available to an African fund that would only be enhanced by scale and profitability.

RECOMMENDATIONS[23]

AfriCap's role as a catalyst for the commercialization of microfinance in Africa should focus on its core business of investment. To this end, its main social good objective should be to act as a catalyst for the transition to private capital and the continued commercialization of microfinance in Africa. This role is absolutely critical to the sustainability of microfinance if private capital is to relieve development capital from the task of meeting the financial needs of the hundreds of millions of poor in Africa.

AfriCap has influenced the commercialization of microfinance in Africa but it can have a much more powerful and broader impact through greater investment scale and a continued demonstration of profitability (of both itself and of its investees). Clearly, the African microfinance context presents opportunities for a specialized investment fund like AfriCap, opportunities that other investors will find difficult to take advantage of. TA subsidies will remain a constant in the sector, and the ability of investors to put attractive investment packages on the table will define competitive advantage among investors seeking the best

[23] Recommendations found here are generalized and based upon more specific recommendations made to USAID and DFID.

MFI investments. Competition at the retail level will also increase, much coming from internationally owned greenfields and/or subsidiaries, underscoring the need for TA subsidy parity among investors.

To maximize its influence on the sector, we would recommend AfriCap be encouraged to grow as a "made in Africa" investment fund brand. It should continue to focus on its core business of being a high value added specialty investor in high growth potential African MFIs.

To achieve these goals, we recommend AfriCap increase its funding base considerably and maintain a TSF to investment ratio of 1:3 to maintain TA funding parity with competing investors and MFIs. We also recommend that AfriCap have access to its TA funding to ensure *its own growth and evolution*, including brand development and possibly expansion to new types of financial sector deals. Funding should also support dedicating more time to working with co-investors and potential buy out investors.

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APPENDIX 2: TERMS OF REFERENCE

This document presents a Scope of Work (SOW) for an assessment of the AfriCap fund to be conducted by Marc de Sousa-Shields, Research Director on the AMAP FS KG Transitions to Private Capital research topic.

The AfriCap Microfinance Fund (AfriCap) is a $15 million equity investment fund dedicated to the microfinance industry in Africa. It is incorporated in Mauritius, with an operational base in Johannesburg, South Africa, recently relocated from Dakar, Senegal. The fund makes investments in a select number of leading microfinance institutions (MFIs) in Africa committed to commercial viability. AfriCap has a dual mission – to generate both a commercial return to shareholders and a social return in the form of a viable microfinance industry.

It is the only specialized equity fund for microfinance institutions based in Africa, and invests in institutions committed to serving low-income communities without access to conventional banking services. AfriCap is a ten year fund and takes a long-term perspective to building value and developing an active governance role with each investee institution.

AfriCap operates using two separate but closely linked facilities. The Equity Investment Fund identifies, analyzes, and makes equity investments into qualified African MFIs. The Technical Services Facility or TSF provides those investees with specialist technical support, if needed, to enhance the equity investment.

In 2000, USAID provided a US$500,000 Implementation Grant Program grant to Calmeadow for investment in the AfriCap Microfinance Fund. This consisted of just over seven percent of donor investment in equity and technical services funds. Whereas DFID contributed about 30 percent of the total investment in both funds.[24] For both USAID and DFID, the funding was equally divided between the Equity Investment Fund and the Technical Services Facility.

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[24] DFID has committed £1.4m which represented ca. $2.7m out of $3.8m for the TSF and to refinance £1.6m of Calmeadow investment that should be equivalent to $2.5m. At the end, DFID should have contributed ca $5m for $17.2m