

The Microfinance Rating Outlook Report 2008

Prepared in collaboration with KPMG Luxembourg and edited by ADA

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LIST OF ACRONYMS

ACP	Africa, Caribbean, and Pacific States
CDO	Collateralized Debt Obligation
EECA	Eastern Europe and Central Asia
EU	European Union
IAR	Investment Advisory Report
IDB	Inter-American Development Bank
LAC	Latin America and the Caribbean
MENA	Middle East and North Africa
MFI	Microfinance Institution
MIX	Microfinance Information eXchange, Inc.
PKSF	Palli Karma-Sahayak Foundation
SSA	Sub-Saharan Africa
SIDBI	Small Industries Development Bank of India
SUFFICE	Support to Feasible Financial Institutions and Capacity-building Efforts
USAID	United States Agency for International Development
USD	United States Dollar

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This report aims at providing an overview of the state of the microfinance institutions rating market as at the end of 2007 and is based on data collected directly from the rating agencies. 2007 saw demand within the microfinance rating market grow by 19.5% and 539 ratings were performed bringing the global grand total to 2,280. With almost 1,000 MFIs having undergone a rating between 1997 and 2007, the microfinance rating market has developed from a negligible sector to a self-sufficient and mature market in certain countries.

However, this growth has not been harmonious across regions. LAC and Asia regions account for 78% of the global rating market and growth is still dynamic in 2007. Collectively, the EECA, SSA and MENA regions account for just 22 % of total ratings and remain to some extent underpenetrated or served markets.

The previous 2006 report¹ identified several market trends. These included the increasing levels of private investment in the microfinance industry and the need for MFIs to attract these resources in order to sustain their growth. Indeed, it can be safely assumed that these trends were confirmed in 2007 as highlighted by the 35% growth in international investments in MFIs. Aspects such as the Basel II Accords and the pressure from MFI stakeholders for more transparency and better governance within the microfinance sector have further contributed to the overall growth of the market.

It can be argued that these developments have had a knock on effect in terms of demand for microfinance ratings compared with demand for credit ratings. Be it for regulatory reasons or in order to raise additional funding, the most developed and mature MFIs have gradually shifted from using specialized rating products to using mainstream credit ratings. Most investors are familiar with these products as they offer a considerable advantage when meeting their own regulatory requirements. However, the demand for microfinance ratings is still real as they are considered as the best product for first time ratings by most of the MFIs and their donors.

Consequently, mainstream credit rating agencies are increasing their market share in the field year after year. This situation has remained constant despite the fact that specialized microfinance rating agencies have responded dynamically to the changing microfinance market by expanding geographically, consolidating their activities, and diversifying their products.

One such product diversification includes the development of the social performance evaluation, also called a social rating which are reported for the first time. This growing interest of private investors (both socially-oriented and for-profit commercial) is certainly financially profitable for the microfinance field and its sustainability. However, the microfinance players should not lose sight of their social mission and the poorer should not be excluded from the borrowing facilities because of a higher risk of default and social ratings help MFIs to maintain their social mission.

A further challenge to the rating market that was identified in the 2006 Outlook report was the closing of the Rating Fund and whether demand would decrease as a result. Seen as the Fund was still running in certain regions in 2007, it is still too early to analyse the effect on demand but what has become apparent is the fact that the Rating Fund contributed to the growth of the rating market without creating an artificial market. As the microfinance rating market continues to develop, it will inevitably meet new challenges along the way but as observed last year, it has the advantage of facing these challenges in a growing market.

1 "The Microfinance Rating Market Outlook Report 2006" Gail Buyske on behalf of the Rating Fund 2006: <http://www.ratingfund.org/documents.aspx>

In 2007, microfinance experienced yet another year of growth. Private investors and new participants entered the market and new specialized investment funds were set up. The ensuing growth in microfinance investments resulted in an increased demand and supply of MFI ratings.

Last year's Microfinance Rating Market Outlook reported that international investments in MFIs increased from USD 1.7 billion in 2004 to at least USD 4.2 billion in 2006. In 2007, this number amounted to USD 5.7 billion². This continuing increase highlights not only the sector's impressive performance but also the imminent growth opportunities for rating agencies.

MFIs reporting to the MIX - Microfinance eXchange, Inc. - have increased their loan portfolios from USD 7.5 billion in 2004 to USD 9.8 billion in 2005 and up to USD 13.5 billion in 2006³. These 2004-2006 figures are based on the MIX's analysis of 340 MFIs in all regions.

In 2007, the number of ratings amounted to 536 and almost 450 MFIs obtained at least one rating.

Some key questions raised in last year's report are still *considered* this year:

- Will regulatory requirements significantly influence the demand?
- Do mandatory ratings lead to voluntary ratings?
- Will the greater involvement of investors lead to a greater demand for mainstream credit ratings and what is their share?
- Did the announcement of the closure of the Rating Fund at the end of 2007 result in an artificial growth in demand for (co financed) ratings?
- Do microfinance investors make use of microfinance ratings in their investment processes?

Demand for credit ratings significantly increased in 2007 while demand for microfinance ratings slightly decreased. It will be interesting to monitor the evolution of this trend in the near future. Social ratings are new products and still in development but have already experienced a strong growth in 2007.

A growing number of MFIs request updates of their rating, which may demonstrate the increasing maturity of the market. This report will address the self-sufficiency of the microfinance rating market, taking into account the proportion of mandatory ratings as well as co-funded ratings.

The Microfinance Rating Outlook Report 2008 is based on data collected from more rating agencies than last year (17 in total). Some figures are therefore higher than they were compared to last year's report.

The report starts with an overview of the current market, including a presentation of the different rating products, stakeholders and regions. This is followed by a section on global trends of the market as a whole and a section dedicated to regional developments.

² The Consultative Group to Assist the Poor. <http://www.cgap.org/p/site/c/template.rc/1.26.1909>

³ Microfinance Information eXchange, Inc.-Microbanking Bulletin, Issue 16, Spring 2008. Part of these results differ from previous MIX Trend Lines report because of adjustments in the data sets.

Methodology

This report is based on MFI data collected from 17 rating agencies and is designed to offer a general overview of the microfinance rating market. Due to the fact that not all active microfinance rating agencies participated in the study and that the data used was provided by the rating agencies themselves, this report cannot be deemed exhaustive. Nonetheless, it offers an insightful analysis of the development of the industry and its present status.

Some differences occurred in the elaboration of the report with respect to last year. Firstly, as previously mentioned, the data collected and analyzed in 2008 originated from more agencies than in 2007. Therefore, more data were available for the 1997 – 2007 period and for this reason, the figures are higher than they were last year.

Secondly, the names of the rating products have changed slightly in order to reflect the product names as specified by the rating agencies. Furthermore, social ratings were included this year in the analysis, from the date that the agency launched this product.

Thirdly, the reference date used for this report is the date of the rating mission rather than the date of the most recent financial statements. This is because some mainstream raters generally perform mandatory quarterly MFI updates. However, most of these updates are desk-assessments and do not necessarily entail an on-site visit. As counting every quarterly update vastly inflates the numbers of rating conducted in the favor of mainstream raters, this year the mission date was used as a date of reference in order to try to avoid this issue. Moreover, the exact number of updates an MFI has obtained has been taken into consideration.

For credit and microfinance ratings, the updates of ratings have been tracked as follows:

- F = First rating
- U1 = First update
- U2 = Second update
- U3 = Third update etc...

Example: if an MFI has had a microfinance rating as a first rating and then a credit rating as a second rating, the credit rating should then be considered as U1.

Credit ratings and microfinance ratings are not mutually exclusive. This is the same if an MFI has had a mini-rating/diagnostic/IAR etc. as a first rating and continues to have a full rating – the full rating has to be considered as a U1.

On the other hand, social ratings are separate products all together and their updates have been identified as follows:

- S1= First social rating
- S2= Second social rating
- S3= Third social rating etc...

Example: social ratings and financial ratings are mutually exclusive so if an MFI has already had a microfinance rating followed by a social rating, the social rating would be identified as S1.

Description of the products

Microfinance rating

These correspond to the product that is commonly called a “Performance rating”.

These ratings are conducted under a methodology developed to provide a broad range of diagnostic information about the MFI's management, social mission, products, risk management, growth capacity, etc. These ratings not only measure the MFI's creditworthiness, but also its trustworthiness and excellence in microfinance. These are an indication of how good an MFI is compared to its peers, i.e. does the MFI reach micro-entrepreneurs efficiently and with high quality loans.

These ratings can be used by investors, especially socially-oriented, donors, technical assistance partners and the MFI's management and administrators.

Sub-categories of microfinance ratings: Diagnostics, Mini-ratings and IAR (Investment Advisory Report). These are rating products specific to the microfinance field and can be applied to young and/or small institutions. They emphasize the analysis of institutional features considered necessary to grow and to eventually prepare MFIs for a microfinance specialized rating.

Please note that in the report's graphs and tables, these figures are identified between brackets and by a note.

Credit rating

Credit ratings are the product of conventional rating agencies and have a narrower focus than the aforementioned microfinance ratings. Credit ratings predict the likelihood that an MFI will not be able to meet its obligations. These ratings are not concerned with how effective or efficient a MFI is at extending loans to micro-entrepreneurs.

These are conducted under a standard methodology applied to any kind of financial institution, be it a commercial bank or an MFI whose target customers are the poor. Its purpose is to make an opinion about the MFI's default risk during a given period of time. It focuses on credit risk rating and is used by investors, particularly commercial ones, and supervisory authorities as part of the compulsory requirements to comply with the regulation.

Social rating

The social rating is an independent assessment of an organization's social performance using a standardized rating scale. The social rating assesses both social risk (the risk of not achieving its social mission) and social performance. Achievement of social impact is the ultimate goal of social performance, but proving that a given intervention has caused a certain social outcome is a complex econometric exercise not possible within the quicker process envisaged for social rating. However, what a social rating can achieve is an analysis of the processes undertaken by an MFI toward its desired goals, and the results to the extent of analyzing outreach and quality of services provided.⁴

In addition to the above-mentioned products, a distinction should be made between mandatory and voluntary ratings. In some LAC and Asia regions, regulatory authorities require MFIs to conduct a rating to operate. Within the LAC region, ratings are mandatory in Bolivia, Peru and Ecuador. In Asia, Pakistan requires mandatory ratings for MFIs meeting specific criteria. It should be noted that the demand driven by regulation cannot explain the growth of the overall market. For instance, India is accountable for 98 ratings in 2007 although rating is not compulsory in this country. The proportion of mandatory ratings versus voluntary ratings has slightly decreased from 30% in 2000 to 15% in 2007.

⁴ The SEEP Network Social Performance Working Group's "Social Performance Map", <http://www.seepnetwork.org/content/library/detail/6040>, April 2008

The global rating market in figures

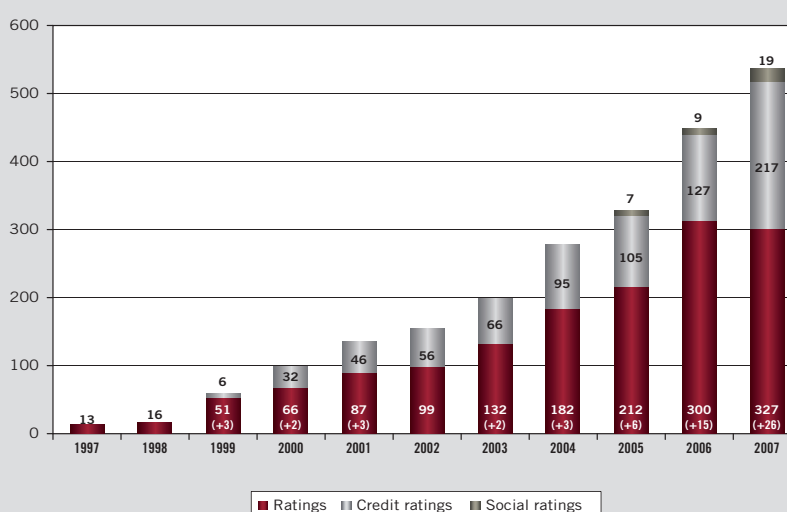
The global microfinance rating market amounts to 2.280 ratings, including (microfinance) ratings, credit ratings and social ratings. Out of a total of 984 MFIs rated since 1997, 441 MFIs have undergone a rating in 2007. The global growth for the three aforementioned products amounts to 19.5% in 2007. On the one hand, the number of microfinance ratings decreased from 315 in 2006 to 303 in 2007. On the other hand, the number of credit ratings increased from 127 in 2006 to 217 in 2007. Finally, the number of social ratings doubled, with 19 ratings reported in 2007 compared to 9 in 2006.

539 ratings in total

**Global increase
of 19.5%**

2007 figures

Number of ratings by categories between 1997 - 2007



Figures between () are microfinance ratings sub-categories products: Diagnostics, Mini-ratings and IAR

The table below shows the number of 2007 ratings split by categories, according to region. In total, 539 ratings occurred mainly in two regions, the majority of which were microfinance ratings.

However, although the microfinance ratings are still widely used in all regions, it is interesting to see the increase in credit ratings. While in 2006, LAC was the only region with a significant number of credit ratings, in 2007, there were 71 credit ratings in Asia and 8 in EECA.

Number of ratings by categories, by regions in 2007

	Microfinance rating	Credit rating	Social rating	Total
LAC	85 (+3)	138	8	230
Asia	109	71	3	183
SSA	34 (+20)	-	6	60
EECA	43 (+2)	8	2	55
MENA	10 (+1)	-	-	11
TOTAL	277 (+26)	217	19	513 (+26)

Figures between () are microfinance ratings sub-categories products: Diagnostics, Mini-ratings and IAR

Description of rating agencies

As previously mentioned, this report is based on the analysis of data collected from seventeen rating agencies. They can be classified into two main categories:

- Specialized MFI rating agencies
- Mainstream credit rating agencies

	Credit rating	Microfinance rating	Social rating	Agency type
Apoyoy Asociados	✓			Mainstream
BRC	✓			Mainstream
Class y Asociados	✓			Mainstream
Crisil	✓	✓		Specialized
Ecuability	✓			Mainstream
Equilibrium	✓			Mainstream
Feller	✓			Mainstream
Fitch Rating	✓			Mainstream
JCR –VIS	✓			Mainstream
M-CRIL	✓	✓	✓	Specialized
Microfinanza Rating	✓	✓	✓	Specialized
Microrate	✓	✓	✓	Specialized
Moody's	✓			Mainstream
PCR	✓			Mainstream
PlanetRating		✓	✓	Specialized
PRIME		✓		Specialized
Standard&Poor's	✓			Mainstream

Both having regional or global coverage, the specialized MFI rating agencies have historically produced only global risk assessments, while the mainstream ones have produced credit risk ratings.

Description of rating agencies

M-CRIL, Microfinanza Rating and Microrate currently perform the three types of rating products with regional or global coverage. The majority of agencies are specialized only in one single product, however, some agencies are able to offer at least two rating products. This is the case for Planet Rating that carries out both microfinance and social ratings.

With respect to mainstream agencies, S&P and Moody's have low market shares within the MFI credit rating market. These agencies are mainly active in the LAC area, where S&P covers both Mexico and Paraguay while Moody's covers Bolivia only.

S&P and Moody's have positioned themselves on the microfinance market with one single product, credit rating, which was already well established and being performed by agencies with either more market experience and a much stronger market presence or with attractive pricing and fees.

Rating agencies market share

	2007 Market share	1997 – 2007 Market share
Apoyoy Asociados	1% (0.9%)	% (1%)
BRC	0.4% (0.4%)	0.1% (0.1%)
Class y Asociados	10% (9.3%)	12.6% (12.2%)
Crisil	7.6% (7.1%)	6.6% (6.3%)
Ecuability	3.4% (3.2%)	3.2% (3.1%)
Equilibrium	2.2% (2.1%)	2.8% (2.7%)
Feller	0.2% (0.2%)	0.05% (0.04%)
Fitch Rating	10.4% (9.7%)	9.4% (9%)
JCR –VIS	1.4% (1.3%)	0.3% (0.3%)
M-CRIL	15.5% (14.4%)	21.8% (21%)
Microfinanza Rating	15.1% (16%)	9.2% (9.4%)
MicroRate	9.0% (8.6%)	15.7% (15.2%)
Moody's	0.4% (0.4%)	0.3% (0.3%)
PCR	-	0.3% (0.3%)
PlanetRating	11.6% (15.7%)	10.9% (13.5%)
PRIME	11.4% (10.6%)	5.2% (5.1%)
S&P	0.2% (0.2%)	0.5% (0.4%)

Figures between () takes into account microfinance ratings sub-categories products

Regions

This section offers a brief insight to the current rating market of each region: LAC, Asia, SSA, EECA and MENA. For an indepth analysis, refer to the chapter Regional Dynamics.

LAC – Latin America and the Caribbean

With 228 ratings, the LAC region remained the largest MFI rating market in 2007.

In this region, Peru continues to dominate the market. The Peruvian market has the largest representation of rating agencies, with six agencies in total. Class y Asociados, though only present in Peru, dominates the Peruvian market with 50 ratings in 2007 and a regional market share of 23%.

Despite the good performance of the rating market in the LAC region, some countries, such as Haiti, experienced a decrease from 12 ratings in 2005 down to one rating in 2007. On the other hand, countries such as Colombia, Mexico and Honduras support the overall growth of the LAC region market. The number of ratings in these countries has doubled between 2006 and 2007.

LAC is a region with a high proportion (38%) of mandatory ratings.

LAC is also a region with a high number of rating agencies (14) in a total of fourteen countries: Apoyo y Asociados, BRC, Class y Asociados, CRISIL, Ecuability, Equilibrium, Feller, Fitch Rating, Microfinanza Rating, MicroRate, Moody's, PCR, Planet Rating and S&P.

Asia

The Asian market is steadily growing and has increased by 17% in 2007. However, this development is mainly due to rating updates as the proportion of first ratings has decreased by 13%.

This market is still dominated by India and Indonesia with 98 ratings and 58 ratings respectively. Asia is the leading region in terms of first rating being performed in 2007.

Pakistan is the only country in the region requiring mandatory ratings but only 8 ratings have been registered in 2007 so far. In the future, it will be interesting to track the progression of the rating market in Pakistan in order to measure the impact of mandatory ratings on the rating demand.

The region is covered by seven rating agencies: CRISIL, Fitch Rating, JCR-VIS, M-CRIL, Microfinanza Rating, MicroRate, Planet Rating and PRIME. The market is dominated by M-CRIL and PRIME with 39% and 32% market shares respectively.

SSA – Sub-Saharan Africa

The SSA market is growing and is dominated by Planet Rating with 73% market shares. SSA MFIs, like those in the MENA region, are currently only interested in microfinance ratings.

Uganda's MFIs remained the major issuers of ratings since 1999, with twelve ratings in 2007 ahead of Ethiopia which registered six ratings. Despite having performed 9 ratings in 2006, Mali registered a significant decrease with only one rating in 2007.

Ratings are not mandatory in the SSA region.

The SSA region is covered by four rating agencies: M-CRIL, Microfinanza Rating, MicroRate and Planet Rating.

EECA – Eastern Europe and Central Asia

This market has been growing since 2005. In 2007, 45 out of the 53 ratings registered are updates.

The market is largely dominated by Microfinanza Rating with a 67% market share and Russia is the leading country with 14 ratings in 2007.

EECA is a region where ratings are not mandatory.

The EECA region is covered by five rating agencies: Fitch Rating, M-CRIL, Microfinanza Rating, MicroRate, and Planet Rating.

MENA - Middle East and North Africa

10 ratings have been obtained in MENA in 2007. It is the region with the smallest number of rating agencies, three in total: Microfinanza Rating, MicroRate, and Planet Rating.

One specific aspect in the MENA region is that the demand of MFIs in terms of ratings concerns only micro-finance ratings.

Although Morocco seems to be the most mature country within the region thanks to the fact that Moroccan MFIs have performed ratings each year since 2001, in 2007 the trend in terms of the number of ratings decreased. Contrary to Egypt, which remained stable with four ratings in 2004 and 2007, Morocco has declined from seven in 2006 to three ratings in 2007.

MENA is a region where ratings are not mandatory.

In 2007, MicroRate and Planet Rating were the only active rating agencies in the market, with two and eight ratings respectively.

**Overall growth
in 2007 reached
+18.8%**

Credit rating market is growing fast

After nine years of fast growth, the global microfinance rating market, encompassing all products together, increased by 18.8% in 2007. However, the number of MFIs having obtained a microfinance rating has decreased by 4% in 2007, following a 45% growth in 2006. In the meantime, the number of MFIs that achieved a credit rating within the year increased from 85 to 159, representing a growth of 87%.

Regarding the type of products used between 1997 and 2007, MFIs (984 in total) can be broken down as follows:

- Microfinance ratings only: 800 MFIs or 81%
- Credit ratings only: 108 MFIs or 11%
- Both products: 76 MFIs or 8%

Among the 76 MFIs having achieved both microfinance and credit ratings, two sub-categories of first ratings can be identified:

- Microfinance first rating: 72 MFIs or 95%
- Credit first rating: 4 MFIs or 5%

These figures clearly show that the vast majority of the MFIs in the rating market consider the microfinance rating as the best product for a first rating. Some of them shift from a microfinance rating to a credit rating because it is a milestone in their development, for example, a credit rating is the mainstream product when it comes to seeking external investments in capital markets.

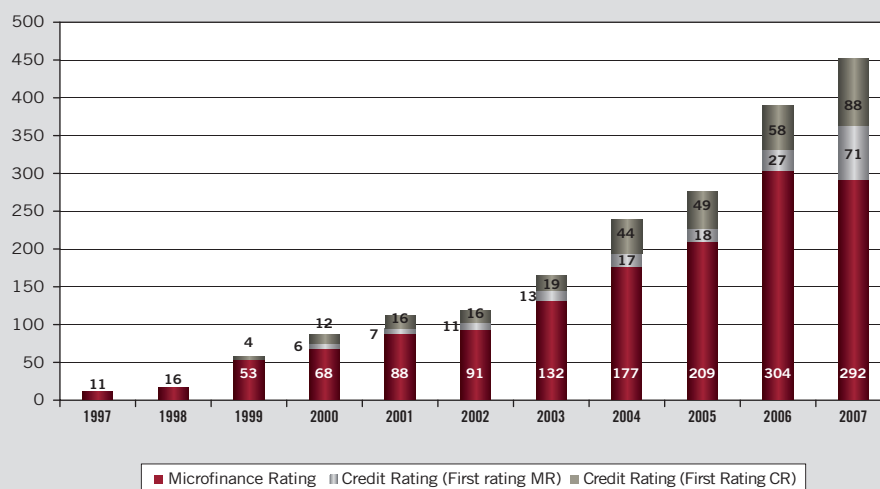
Only 11% of the MFIs in the sample have never requested a microfinance rating. This is mainly due to their location in countries within the LAC region where credit ratings are mandatory.

**Nbr MFIs with credit
ratings +87%**

**Nbr MFIs with mi-
crofinance ratings
-4%**

2007 figures

Number of MFIs by category of 1st rating from 1997 to 2007



The graph above shows the number of MFIs rated by type of product and only considers their first rating. This is a clear demonstration that more MFIs shift to the credit rating field as they reach a sufficient level of maturity in order to require that kind of product. The rating market of microfinance institutions seems to have entered a new stage and next year's report will probably confirm this trend, at least for some regional markets.

Social rating - a new product since 2005

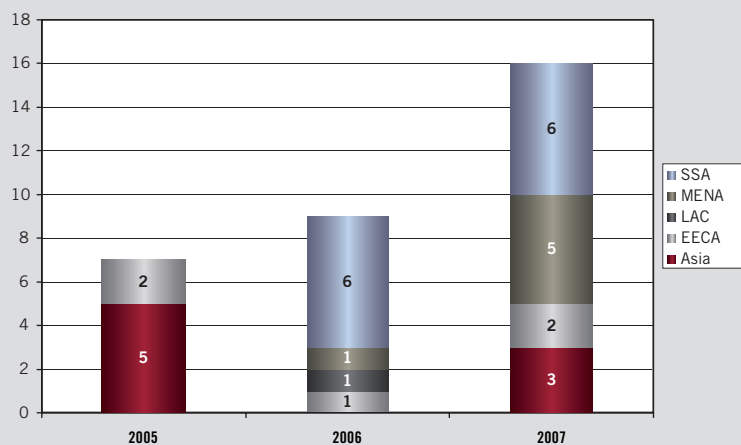
In 2007, 19 social ratings were obtained out of a total of 539 ratings and therefore represent 3.5% of the rating market. Four specialized agencies (Microfinanza Rating, PlanetRating, M-CRIL and MicroRate) have been offering this type of product since 2005. It had a good start with 6 missions in Asia (India) in 2005 but did not continue this trend in 2006. However, the market grew by 29% in 2006 and 111% in 2007. SSA accounts for a large part of the growth, with 6 ratings in 2006 and 2007. These results have been achieved by 2 countries in the region: Mali with 6 ratings in 2006 and Ethiopia with 4 ratings in 2007. These results in 2007 are largely due to donor initiatives which have supported the use of social ratings in these countries.

As a leading region for the microfinance rating market, LAC is also proportionally very active in this new area with 8 ratings in 2007. Three ratings have been performed in Nicaragua, two others in Peru, one in Mexico, Bolivia and Ecuador.

At the moment, this extremely new product only represents a small portion of the rating agencies' activity (5% of the total ratings for Microfinanza Rating, 4% for PlanetRating, 2% for M-CRIL and less than 1% for MicroRate) and has not yet been updated by any of the MFIs concerned. This is a promising product, though too recent to have sufficient historical background in order to identify significant trends. Social ratings have been included in the report as demand for product is likely to grow in the future.

19 social ratings in 2007 performed by 4 specialized agencies

Number of social ratings by region between 2005 and 2007



Breakdown between first and update rating as an indicator of market maturity

In the early days of the microfinance rating market (1997 to 1999), almost all of the rating missions were first-time ratings. After several years of growth, the proportion of updated ratings in 2007 shifted from being negligible to reaching 54% of the 441 MFIs having performed at least one rating. The decision of an MFI to invest in an update of its rating is very important since it means that it considers its first rating as an added value to the institution. This value may take the form of a tool to improve its governance or an incentive to reach more investors and investments.

The following chart shows the number of first ratings and updates between 1997 and 2007:

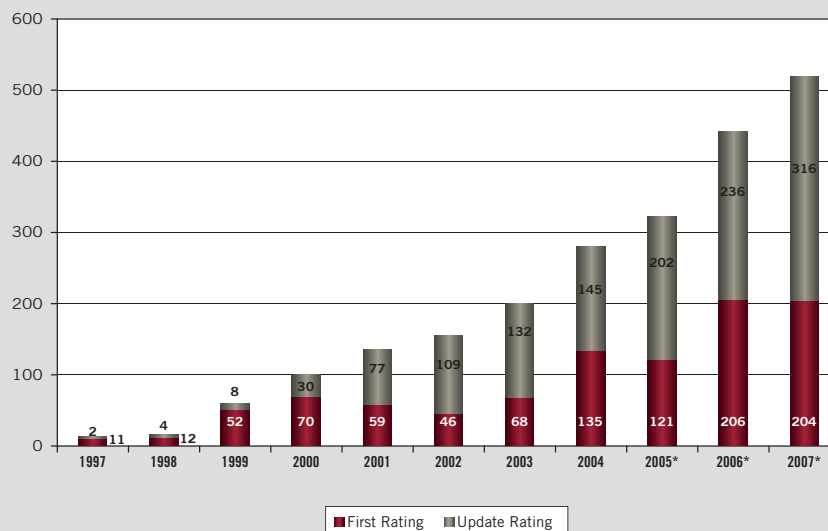
- The evolution of first ratings remained stable between 2006 and 2007 (-1%)
- The number of update ratings increased by 34% from 236 in 2006 to 316 in 2007.

First ratings -1%

Updates +34%

2007 figures

Breakdown first and update ratings between 1997 and 2007



*Excluding the social ratings, hence the difference with total ratings

The chart above shows that the number of first ratings is still high. This means that the market is not saturated because a significant number of MFIs have just entered the market and should regularly need to update their ratings. The maturity of the market is reflected, at least partially, by this balance between first ratings and update ratings.

Of the MFIs that have had a microfinance rating, 42% of them went on to update that rating (see next page). This share reaches 90% for credit ratings, which may be explained by regulatory reasons, or additional fund raising requirements. It is important to note that these percentages do not take into consideration MFIs having obtained their first rating in 2007 since these will not perform a first update before 2008.

The second table shows the average frequency of updates for both microfinance and credit ratings as well as for all ratings, whatever the product. As assumed in the introduction of the report, credit ratings are more frequently updated (less than one year) than microfinance ratings (almost every second year). It is also interesting to note that 303 MFIs have updated a microfinance rating, i.e. made at least 2 microfinance ratings and 90 MFIs have updated a credit rating, i.e. made at least 2 credit ratings.

GLOBAL TRENDS

Market characteristics – Maturity

90% of credit ratings and 42% of microfinance ratings have been updated

Proportion and average frequency of updates (product breakdown)

	At least 1 rating (Nbr of MFIs)	At least 2 ratings (Nbr of MFIs)	% of update
Microfinance ratings	716	303	42 %
Credit ratings	100	90	90 %

	Frequency of update (year)	Sample (Nbr of MFIs)
Microfinance ratings	1.9	303
Credit ratings	0.8	90

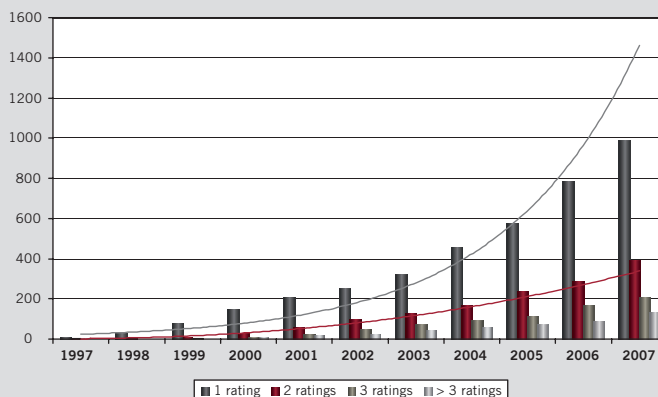
The chart below represents the number of MFIs having achieved their first rating, at least 1 update, at least 2 updates and strictly more than 3 updates between 1997 and 2007. The chart shows the trends for the first two categories. It also shows that the number of first rated MFIs grew exponentially since 1997 with a small decrease in 2007, meaning that the market for first ratings is less booming. On the other hand, the first-update trend is more linear, but the results for 2007 are above the line and the updates market tends to take the lead at the expense of the first rating market.

The analysis of the data related to first and updated ratings provides useful information concerning the two main products that are microfinance and credit ratings. Depending on the year, at least 80% of the first ratings are microfinance ratings and around 50% of the update ratings are credit ones. This means that microfinance ratings are the preferred product for a first rating. Some MFIs shift to credit ratings after a few updates.

It should be kept in mind that the trends identified in this section relate to the overall market and when looking at specific regions, the findings could be slightly different. The LAC region accounts for a large part of the overall market and update ratings as it is probably the most mature region. However, different maturity levels can be observed in the different regions (see the regional sections for more details).

Average frequency of updates: 1.9 yr for microfinance ratings and 0.8 yr for credit ratings

Evolution of the Nbr of MFIs by rating rounds between 1997 and 2007



What are the market drivers?

The strong growth of the global microfinance industry, as well as the significant increase in foreign investments (+35% in 2007) and MFIs' motivation to attract more investors have all certainly encouraged a demand for more transparency and more ratings in 2007.

This section examines whether or not mandatory ratings and subsidized ratings are key drivers in the establishment of a self-sufficient rating market.

In this report, the focus is put only on ratings co-funded by the Rating Fund as data from other co-funding initiatives were not collected/recorded.

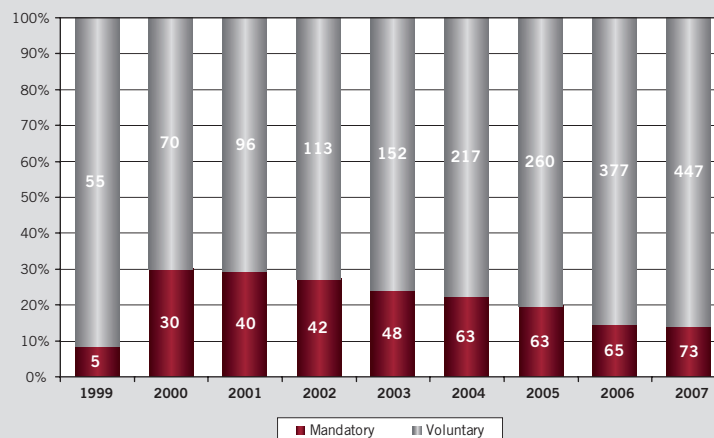
Mandatory ratings account for less than 15% of the ratings in 2007

Mandatory ratings

MFIs are required by the regulation authorities to obtain a rating in some countries within the LAC region and Asia regions. In the LAC region, this is the case for Bolivia, Peru and Ecuador, and in Asia, only Pakistan requires mandatory ratings for MFIs meeting certain criteria. As a result, demand driven by regulation cannot explain the growth of the overall market. For instance, India alone is responsible for 98 ratings in 2007 and does not require ratings.

The following chart shows the proportion of mandatory ratings between 1997 and 2007. This percentage slightly decreases from one year to the other (30% in 2000 – 15% in 2007). Mandatory ratings account for a small part of the rating market. More details will be explained on this aspect in the regional section as it is mainly an LAC issue.

Proportion of mandatory and voluntary ratings between 1997 and 2007



Mandatory rating figures (284 MFIs in the sample) in LAC region show that:

- 43 MFIs achieved only mandatory ratings (15%)
- 224 MFIs achieved only voluntary ratings (79%)
- 7 MFIs achieved both kind of ratings (6%)

The regulated MFIs represent 21% of the sample and account for 39% of the ratings in the region. These MFIs actually undergo more updates than non-regulated MFIs. However, when looking more closely at the data, regulated MFIs which are the most active in the rating field (large number of updates) alternate between mandatory and voluntary ratings and undergo a rating even though they are not required to do so. There is no clear correlation between mandatory ratings and the type of product chosen. *Within the region, another interesting figure is the largest number of ratings for a non-regulated MFI amounting to 17 (i.e. 16 updates).*

GLOBAL TRENDS

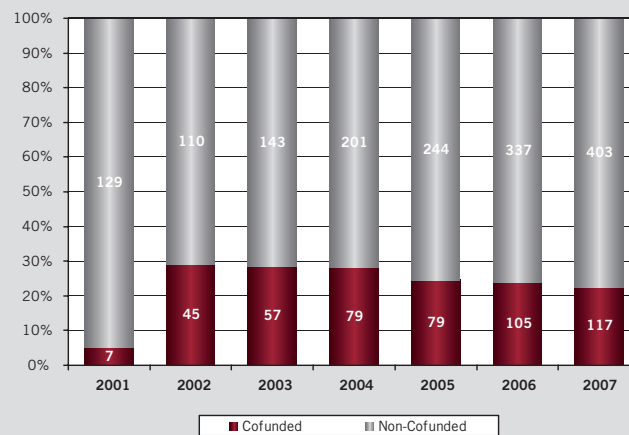
Market characteristics – Self-sufficiency

The share of ratings co-funded by the Rating Fund is slightly decreasing

Ratings co-funded by the Rating Fund

The second indicator of the microfinance rating market's self-sufficiency is the proportion of co-funded ratings. The underlying question is: does the co-funding of ratings trigger the demand in the market or does it sustain it artificially? To answer this question, only information of the Rating Fund co-funding initiative is taken into consideration.

Evolution of the share of co-funded* ratings between 2001 and 2007



**by the Rating Fund*

The co funding by the Rating Fund started in 2001, and applications were closed in mid 2007 for MFIs in the LAC region and by the end of 2007 for all other regions with last reimbursements being made in 2008. It has contributed to convincing reluctant MFIs to join the rating market and find an interest in being rated.

The chart above shows the evolution of the proportion of co-funded / non co-funded ratings between 2001 and 2007. Although the number of co-funded ratings steadily grows, the proportion compared to the total number of ratings is slightly decreasing with 29% in 2002 and 22% in 2007. It represents “only” 25% of the market on average. The situation is very different from one region to another and the most dependent on co-funding are the EECA region (50% of the ratings), the MENA region (47%) and the SSA region (43%) while the LAC region (21%) and Asia (10%) seem to be less dependent on co-funding.

Taking into account different products, the proportion of co-funded credit ratings represents between 3% and 6%, depending on the year considered. The proportion for microfinance ratings is between 30% and 45%. Microfinance ratings are more co-funded than credit ratings as MFIs demanding credit ratings are usually more mature. Moreover, a lot of credit ratings are mandatory ratings, i.e not eligible for co financing, which explains the related small proportion of co funding. However, the growth of credit ratings is greater than the growth of co-funded microfinance ratings. This clearly means that the increasing market is only moderately driven by the Rating Fund initiative.

Globally, out of the 984 MFIs in the sample, 356 MFIs (36%) have benefited at least once from the Rating Fund:

- Only 1 co-funding round: 255 MFIs
- 2 co-funding rounds: 78 MFIs
- 3 co-funding rounds: 23 MFIs (including 8 joint ratings)

GLOBAL TRENDS

Market characteristics – Self-sufficiency

Among the 356 MFIs:

- 271 (76%) benefited from co funding for their first rating
- 85 (24%) for one of their updates

Among the 271 MFIs having benefited from co-funding for their first rating:

- 71 (26%) went on to achieve non co-funded updates
- 40 (15%) obtained only co-funded updates
- 160 (59%) did not achieve any update

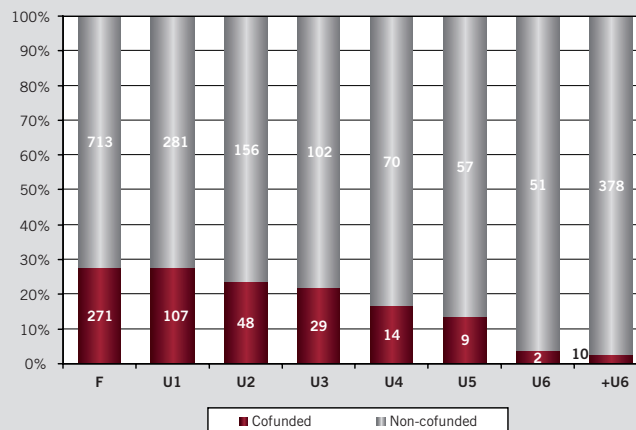
41% (26%+15%) of the first ratings co-funded led to at least one update. Only 26% led to a non co-funded update, to be compared to the other 628 MFIs, independent of the Rating Fund, and their 31% of updates (192 MFIs).

The end of the Rating Fund does not seem to have created an artificial growth of the market

The graph below shows the proportion of ratings co-funded for each rating round. The immediate result is that the proportion of co-funded ratings decreases with each rating round. This is quite normal considering the mission of this co-funding initiative was to trigger the demand among MFIs that were reluctant to pay for a rating. Less understandable was the initiative's willingness to co fund MFIs who were already engaged in the rating process and who frequently updated their ratings. Some MFIs received co funding for its sixth update and beyond and indeed, after such a number of updates, a MFI is not expected to require a co funding.

Finally, the closing of the Rating Fund in 2008 does not seem to have created the artificial growth in the number of ratings in 2007 that some may have expected. Indeed, MFIs could have benefited from the last co-funding in order to obtain a first rating or an update.

Evolution of the share of co-funded* ratings with the update round



*by the Rating Fund

In conclusion to the self-sufficiency of the rating market, the Rating Fund's subsidies and mandatory ratings are not the most significant market drivers. The strong growth of the microfinance industry in the world (with loan portfolios amounting to USD 13.5 billion in 2006), as well as the significant increase in foreign investments (+35% in 2007) and the MFIs' willingness to attract more investments has certainly encouraged foreign investors to demand more transparency and therefore require more ratings in 2007.

Growing competition in a more mature market

Agencies performing ratings for MFIs can be divided into “Specialized” and “Mainstream” categories. Mainstream agencies carry out credit ratings not only for MFIs but also for other companies. Specialized agencies’ products are specifically designed for the microfinance market and better fit MFIs needs. However, they are not as common to investors as mainstream credit ratings are.

The table below shows the regional coverage of agencies, whatever their type. Some cover several regions, others only one region or a single-country (ex: PRIME in Indonesia).

Specialized agencies start to propose credit ratings to MFIs

Regional coverage by rating agency

	Asia	EECA	LAC	MENA	SSA	regions covered
M-CRIL	✓(98 %)	✓(2 %)			✓(0 %)	3
MicroRate		✓(1 %)	✓(76 %)	✓(2 %)	✓(21 %)	4
PlanetRating	✓(5 %)	✓(12 %)	✓(31 %)	✓(13 %)	✓(39 %)	5
Class y asociados			✓			1
Microfinanza Rating	✓(3 %)	✓(44 %)	✓(48 %)	✓(1 %)	✓(4 %)	5
Fitch Rating	✓(1 %)	✓(16 %)	✓(83 %)			3
Crisil	✓(99 %)		✓(1 %)			2
PRIME	✓					1
Ecuability			✓			1
Equilibrium			✓			1
Apoyoy Asociados			✓			1
S&P			✓			1
JCR-VIS	✓					1
PCR			✓			1
Moody's			✓			1
BRC			✓			1
Feller			✓			1
Nbr of agencies	7	5	14	3	4	

* M-CRIL effectively performed ratings in SSA in conjunction with MicroRate through their alliance. The data was recorded under MicroRate.

GLOBAL TRENDS

Market competition – Rating agencies

Among the most active agencies, a few perform both microfinance and credit ratings, though the largest part of their business is the microfinance rating: M-CRIL with 13% of credit ratings, Microfinanza Rating with 3%, Crisil with 8% and MicroRate with only one credit rating (in 2007). This product diversification of rating agencies is recent and reflects the trend identified in the “Products” section.

Types of rating agencies and products range

	Credit Rating	Microfinance Rating	Social Rating	Type
M-CRIL	✓(13 %)	✓(85 %)	✓(2 %)	Specialized
MicroRate	✓	✓		Specialized
PlanetRating		✓(96 %)	✓(4 %)	Specialized
Class y asociados	✓			Mainstream
Microfinanza Rating	✓(3 %)	✓(92 %)	✓(5 %)	Specialized
Fitch Rating	✓			Mainstream
Crisil	✓(8 %)	✓(92 %)		Specialized
PRIME		✓		Specialized
Ecuability	✓			Mainstream
Equilibrium	✓			Mainstream
Apoyoy Asociados	✓			Mainstream
S&P	✓			Mainstream
JCR-VIS	✓			Mainstream
PCR	✓			Mainstream
Moody's	✓			Mainstream
BRC	✓			Mainstream
Feller	✓			Mainstream

GLOBAL TRENDS

Market competition – MFIs' loyalty

MFIs' loyalty to rating agencies is still high

An interesting indicator of the market's competitiveness is the MFIs' loyalty to the rating agencies. The vast majority of the MFIs have been customers of only one rating agency and half of them have achieved only one rating. However, among those 388 MFIs having updated their rating at least once, 99 MFIs (26%) changed to another agency once, 16 MFIs (4%) changed twice, 2 MFIs switched four times and 2 others changed five times.

When looking at the regional breakdown, the more competitive markets are the LAC region and Asia, but the customer loyalty is not absolute in other markets either.

Number of MFIs rated by one or several agencies for each region

	ALL		Asia		EECA		LAC		MENA		SSA	
	#	%	#	%	#	%	#	%	#	%	#	%
1 agency	865	88 %	385	88 %	97	98 %	232	81 %	24	83 %	127	96 %
2 agencies	99	10 %	52	12 %	2	2 %	35	12 %	5	17 %	5	4 %
3 agencies	16	2 %	2	0 %			14	5 %				
4 agencies	2	0 %					2	1 %				
5 agencies	2	0 %					2	1 %				
TOTAL	984		439		99		285		29		132	

Some agencies appear to be focused on specific types of ratings. These should be understood as first, update, co-funded and mandatory types of ratings. For instance, first ratings account for more than 70% of PlanetRating and PRIME missions. Regarding update ratings, the "specialized" agencies are Class y Asociados (94%) and Fitch Rating (88%). Another aspect is the co-funded ratings representing 56% and 49% of the missions achieved by Microfinanza Rating and PlanetRating respectively, whereas the overall percentage of ratings co-funded by the Rating Fund is around 25%. Finally, Ecuability (97%) and Class y Asociados (74%) are the most active agencies in the regulated field.

All this information is summarized in the table below:

First ratings	Update ratings	Cofunded ratings	Mandatory ratings
PRIME (84 %)	Class y Asociados (94 %)	Microfinanza Rating (56 %)	Ecuability (97 %)
PlanetRating (74 %)	Fitch Rating (88 %)	PlanetRating (49 %)	Class y Asociados (74 %)

REGIONAL DYNAMICS

Regional discrepancies

Indepth overview of the regional rating markets

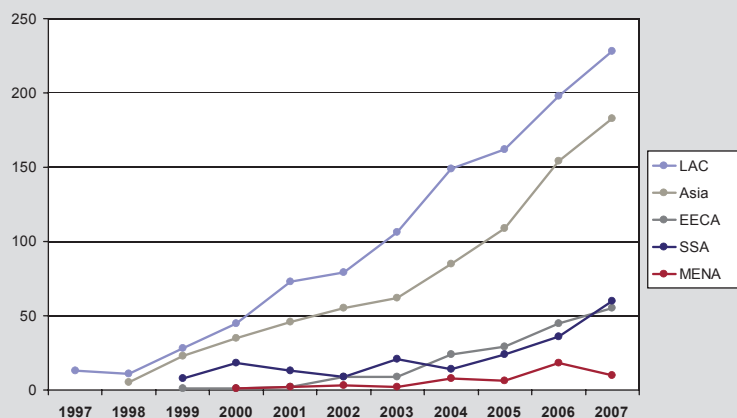
After having presented the global microfinance rating market in the first part of our report, it is now particularly interesting to look at specific regional aspects. The different regions considered in the introduction of the report were:

As all regional markets are growing, MENA is lagging

- LAC** – Latin America and the Caribbean
- Asia** – East Asia Pacific and South Asia
- SSA** – Sub-Saharan Africa
- EECA** – Eastern Europe and Central Asia
- MENA** – Middle East and North Africa

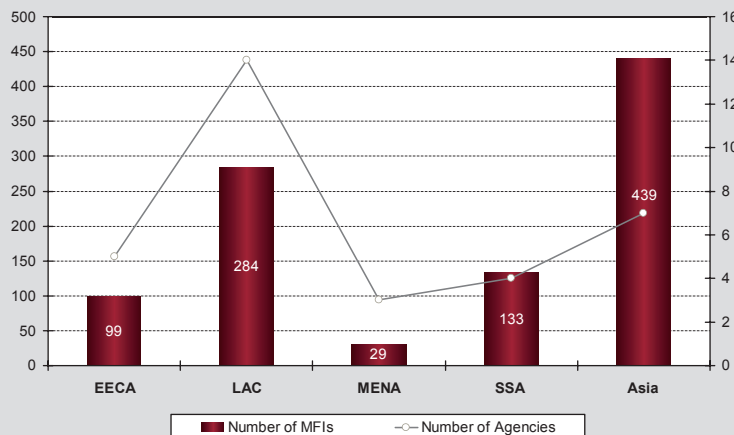
The graph below shows the evolution of the number of ratings by regions between 1997 and 2007. The LAC region is still the leading region followed by Asia. A relevant aspect of the 2007 data is the significant growth of the Sub-Saharan Africa region which is now the third in terms of number of ratings.

Global number of ratings (social and financial) by regions



In the following sections we will try to highlight specific aspects of each region such as the maturity of their respective market, and assess the dependence or independence of that rating market on the Rating Fund and the regulatory requirements to conduct ratings.

Number of MFIs and rating agencies by regions

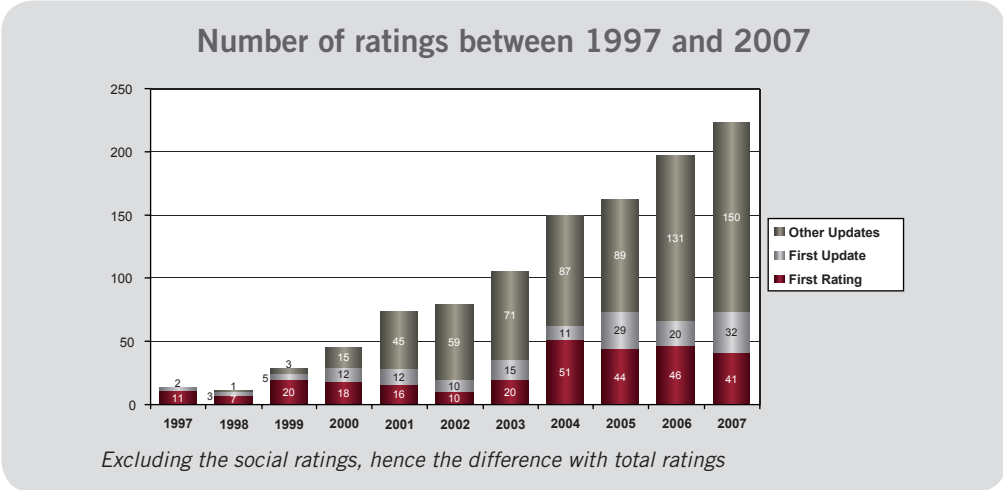




The leading region

Latin America and the Caribbean has always been the leading region in the microfinance rating field and this has been again confirmed by the 2007 data. The number of ratings was expected to grow at a slower rate or to stabilize as the market was becoming more mature. Contrary to this belief, the 2007 data showed a growth of 13% in the total number of ratings in the region (see the graph below).

The market of update ratings is booming, the market of first ratings is stabilizing

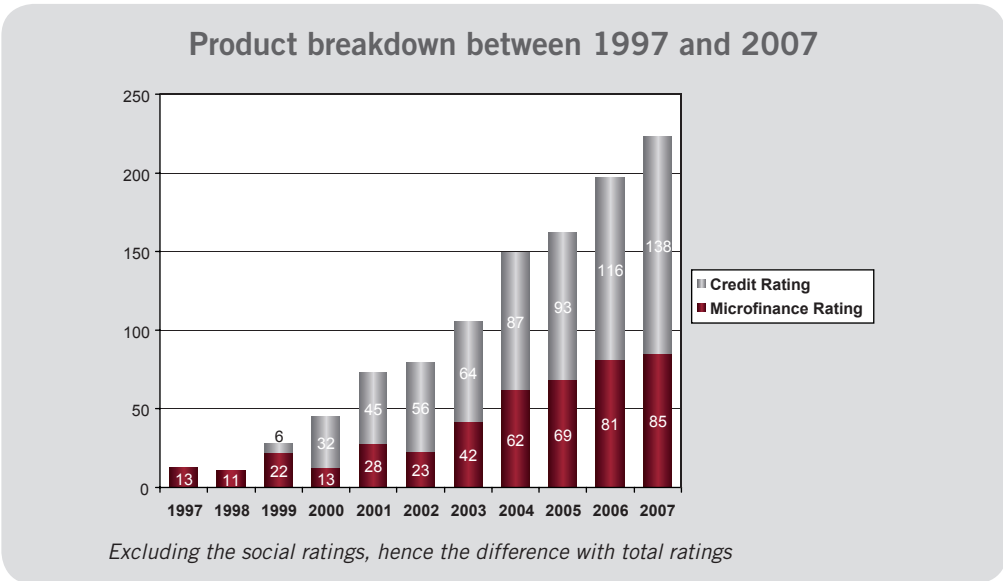


This trend is not only explained by the increasing number of update ratings in this particularly advanced region. Indeed, the large number of first ratings in 2007 (41) means that the market is still growing. The number of first updates is also a good indicator to measure the maturity of a local rating market. It shows that 32 MFIs have made an update of their first rating in 2007 (11% of the regional sample), as such indicating that the potentiality of the update market is still large (47% of the MFIs in the region have been rated only once).

The average frequency observed for updates, among MFIs having updated their rating at least once, is the following:

- Every 2.2 years for a microfinance rating (33% of MFIs have updated a microfinance rating)
- Every 0.7 years for a credit rating (27% of MFIs have updated a credit rating)
- Every 1.5 years for both products (53% of MFIs have updated a rating whatever the product)

Both products, microfinance rating and credit rating, are growing



REGION LAC

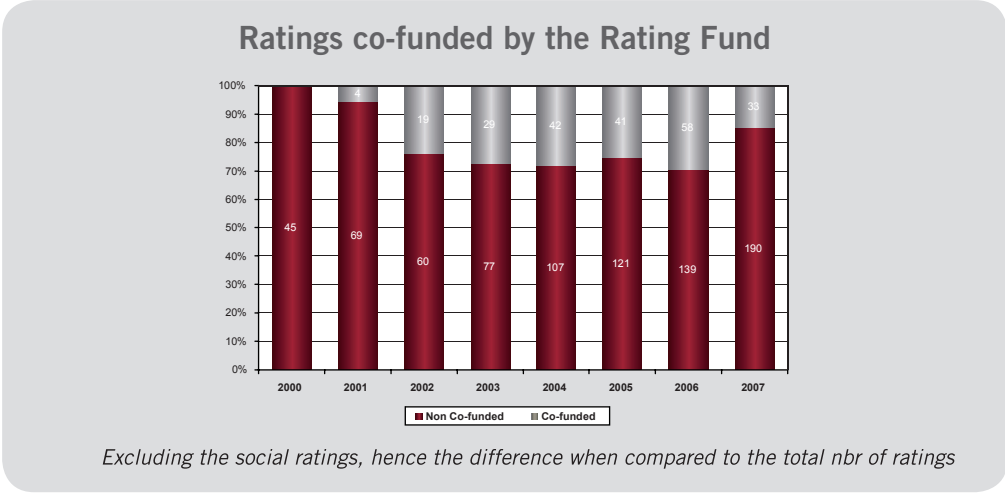
Market self-sufficiency



In this section, we will try to identify whether or not the local rating market is supported by external factors such as regulation bodies in different countries and the Rating Fund.

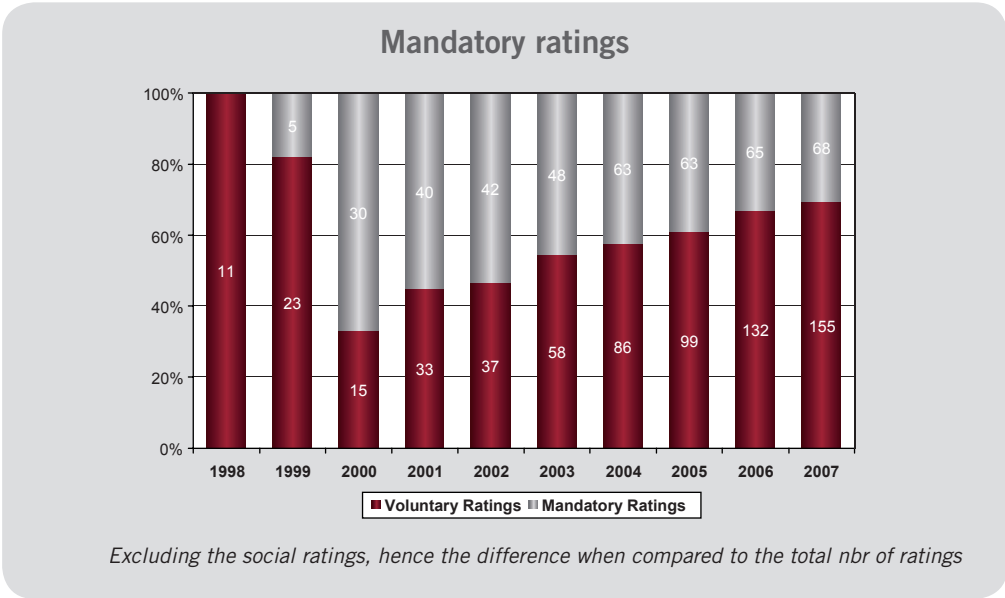
The chart below represents the number and the percentage of ratings co-financed by the Rating Fund between 2001 and 2006. The ratio seems to be stabilized with around 25% of the ratings co-funded between 2002 and 2006. In 2007, this ratio dropped to 15%. This is a normal result as the Rating Fund closed for the Latin America region in 2006/07. Among the ratings co-funded in 2007, 76% were microfinance ratings and only 24% were credit ratings.

The percentage of ratings co-funded by the Rating Fund has dropped to 15% in 2007



LAC is the only region apart from Asia to require ratings for MFIs meeting certain criteria. However, the demand for ratings is only partially regulation driven as 80% of the ratings in the region in 2007 were voluntary. This percentage has increased slightly over the years. Thanks to the regulation, the market boomed in 2001 (with a growth of 62%) but the importance of this factor is not as evident as in 2007, and increasingly more MFIs ask for a rating on a voluntary basis.

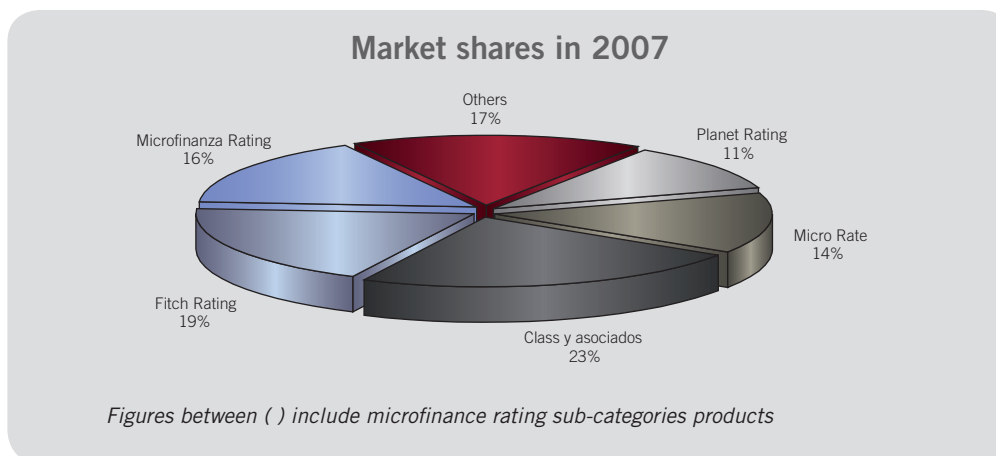
The percentage of mandatory ratings is slightly decreasing whilst voluntary ratings are still increasing



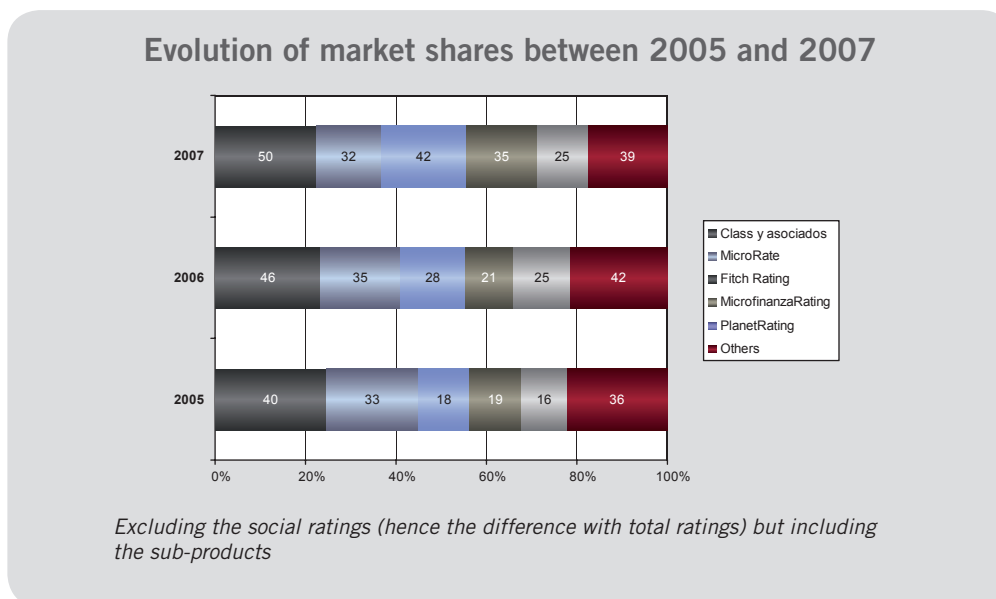


In 2006, 10 agencies were active in the region. This number amounted to 12 in 2007 with 3 additional agencies (BRC, Moody's, Feller) and one leaving the market (PCB). The most active agencies and their respective market shares are shown in the chart below.

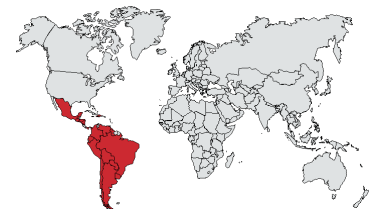
Class y Asociados accounts for 23% of the market although it is only active in Peru. All of the ratings performed by the agency in 2007 were updates and 58% were mandatory ones. Microfinanza Rating and PlanetRating are more dependent on the Rating Fund than other agencies (respectively 40% and 32% of their ratings in the region are co-funded). PlanetRating is mainly active in the field of first ratings.



Market share rankings have significantly shifted each year, with Fitch Ratings jumping from the third position in 2005 to second in 2007. This trend could be explained by rise of voluntary ratings. Conversely, 88% of the ratings performed by Ecuability are within the regulated market.

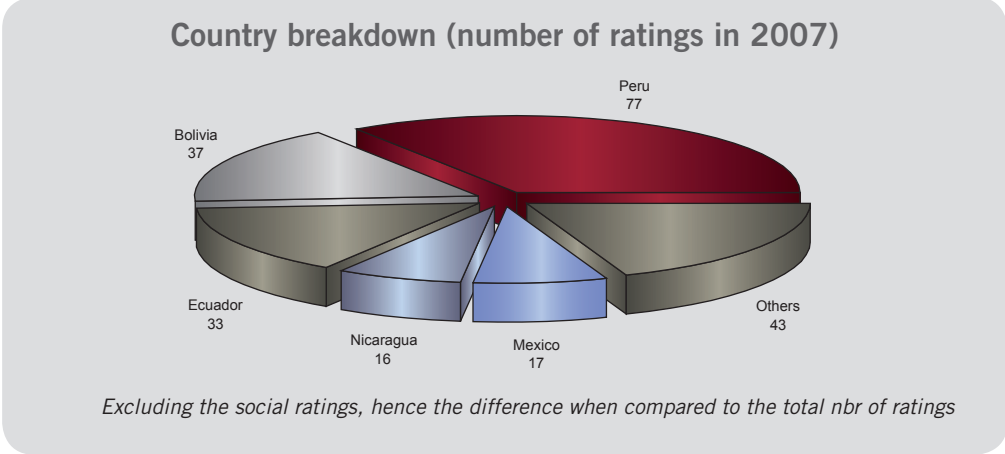


Most of the agencies active in the region provide only credit ratings, PlanetRating and MicroRate are specialized agencies providing only microfinance ratings while Microfinanza Rating provides both products (80% microfinance – 20% credit in 2007).



The most active and mature countries within the LAC region are Peru, Bolivia and Ecuador. Other countries are following the trend drawn by these leaders; Mexico, Columbia and Honduras have for instance doubled their number of ratings between 2006 and 2007. On the other hand, the rating market in Haiti reached a peak in 2005 (12) before falling down in 2006 (1) and 2007 (1). The Haitian National Network of Microfinance Institutions had actually encouraged all of its members (18) to undergo institutional diagnostics (funded by USAID) in 2005. The institutional strengthening programs that resulted are currently being implemented, with follow-up ratings or assessments planned by the end of the process.

Number of ratings in Mexico, Columbia and Honduras has doubled between 2006 and 2007

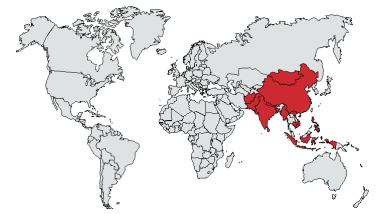


When looking at first ratings and update ratings as a maturity indicator of the market, it can be observed that 92% of the MFIs rated in Peru in 2007 were undergoing an update. This situation is similar in Bolivia (95%) and Ecuador (80%). Based on the rating market, the region is actually divided into 3 sub-regions: mature countries, emerging countries and underdeveloped countries. Nicaragua could be seen as a hyphen between the two first sub-categories as most of the MFIs rated in 2007 were update missions (92%) but only counted two credit rating missions.

In the 3 leading countries, the emergence of the market has been stimulated by the regulated credit ratings imposed to MFIs meeting certain criteria. We can, however, observe that the proportion of mandatory ratings is decreasing as the market is becoming more and more autonomous. In the emerging countries, MFIs are not forced by regulation authorities to be rated.

Regarding the ratings co-funded by the Rating Fund, the dependence of the 3 first countries is around 15% while the emerging countries benefit from it for about 30% of their ratings. The country dynamics within the region can be summarized in the table below (2007 figures):

Mature countries	Emerging countries
Peru, Bolivia, Ecuador	Nicaragua, Mexico, Columbia, Honduras
Regulated MFIs	Non-regulated MFIs
Mainly Credit ratings (82%)	Mainly Microfinance ratings (87%)
Small proportion of first ratings (11%)	Large proportion of first ratings (38%)
Around 7% of ratings co-funded by the Rating Fund	Around 23 % of ratings co-funded by the Rating Fund



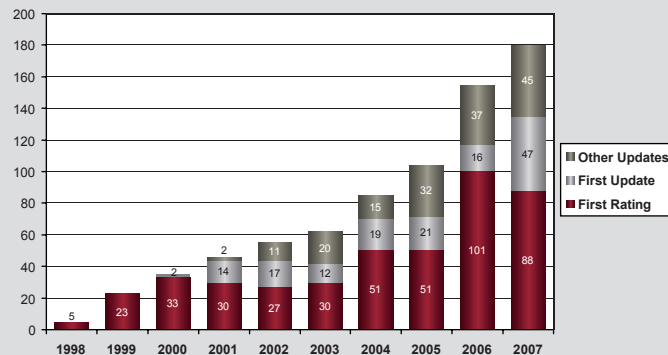
Two leading countries: India and Indonesia

Since 1997, 439 MFIs have been rated in Asia, and 148 have obtained an update. The growth in the number of ratings is almost exponential. In recent years, the most active category used to be first-time ratings, however, in 2007, this trend shifted with a 13% decrease of the first ratings and a 194% increase of the first updates. Update ratings in 2007 account for more than half of the total ratings.

Regular growth since 1998:

+22% in 2005
+48% in 2006
+17% in 2007

Number of ratings between 1997 and 2007



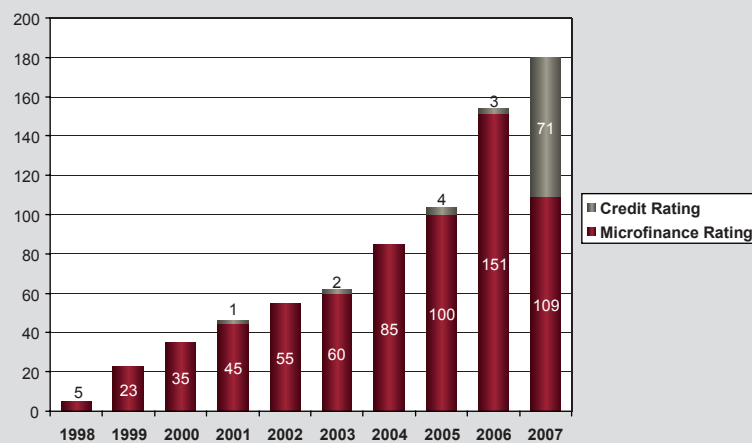
Excluding the social ratings, hence the difference when compared to the total nbr of ratings

The average frequency of updates amounts to 1.8 years for microfinance ratings and 1.0 year for credit ratings in the region.

In 2007, not only was there a shift between first and update ratings, but a significant change from microfinance ratings to credit ratings also occurred. While the first type of ratings decreased by 28% in comparison with the 2006 figures, the second type has been multiplied by more than 23 over the same period. Therefore, the proportion of microfinance ratings decreased from 98% in 2006 to 61% in 2007.

This trend is largely due the Indian rating market which appears to be independent in itself and not reflective of the overall situation in the region. India left aside, the microfinance rating is still the main product in Asia and, as shown in the graph below, the region does not appear to be as mature as originally thought.

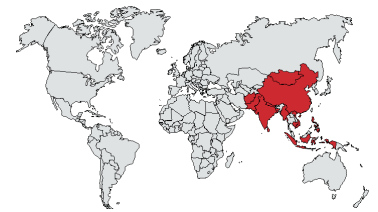
Product breakdown between 1997 and 2007



Excluding the social ratings, hence the difference when compared to the total nbr of ratings

REGION ASIA

Market self-sufficiency

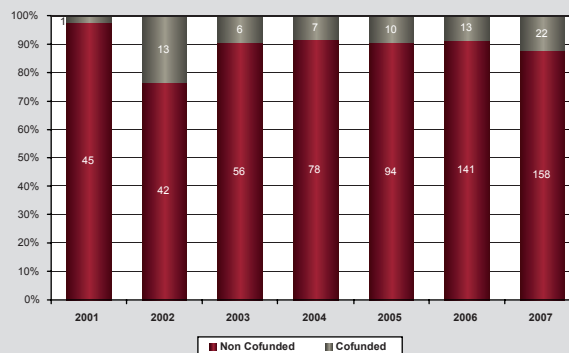


The Asian rating market like other regional markets (LAC excluded), is largely independent of regulatory bodies. However, the Indian Apex Bank, the Small Industries Development Bank of India (SIDBI), requires ratings from all of its MFI partners and accounts for 70 percent of the rating demand in India. Thus in this particular case, the requirements originate from investors and not from the supervisory authorities.

The only country within the region that requires mandatory ratings is Pakistan. All microfinance banks in Pakistan must be rated (only after three years of operations for banks that do not collect deposits). This regulation led to few voluntary ratings in 2007 as 3 ratings out of 8 were performed on a voluntary basis.

Around 10% of the ratings are co-funded by the Rating Fund

Ratings co-funded by the Rating Fund

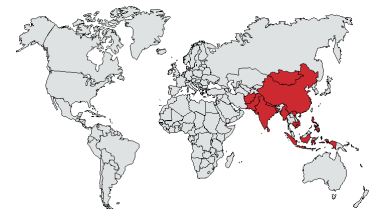


Excluding the social ratings, hence the difference when compared to the total nbr of ratings

Five mandatory ratings in Pakistan

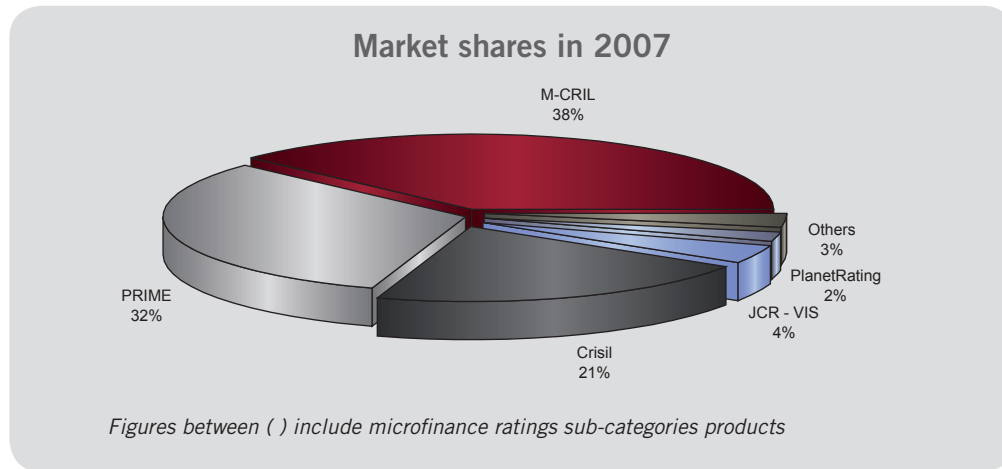
Considering the co-funded ratings, the region seems to be less dependent on the Rating Fund than the overall market. However, the situation varies from one country to another.

For instance, in 2006, PRIME in Indonesia performed ratings subsidized by its founders. However, in 2007, the agency shifted from performing co-funded ratings to becoming a profit-driven rating agency. This change did not lead to a reduction in the number of ratings being carried out. Some MFIs that had been rated for the first time in 2006 have carried out an update in 2007. It is important to notice that PRIME co-funded ratings are not included under co-funded ratings in the above graph since this initiative is independent of the Rating Fund.

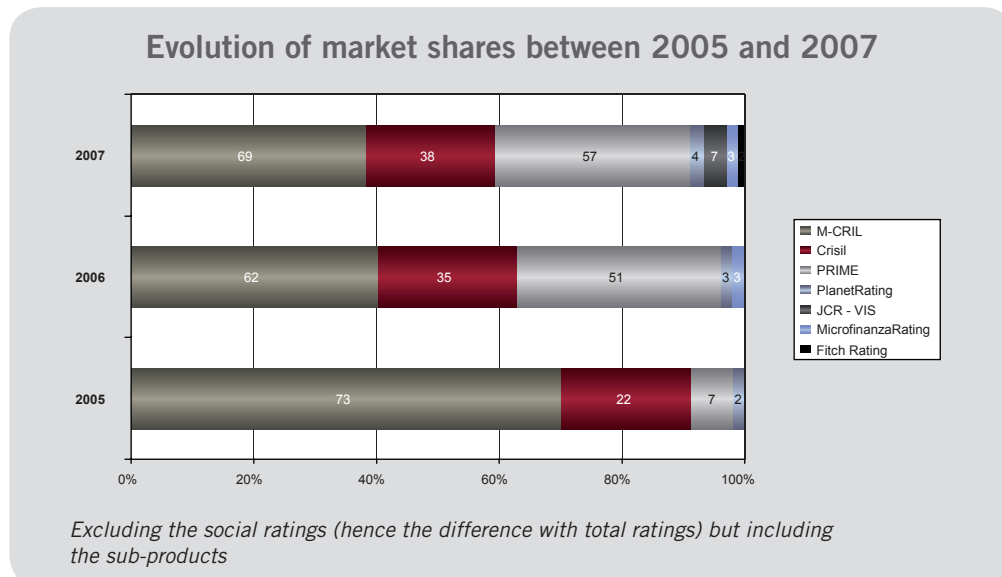


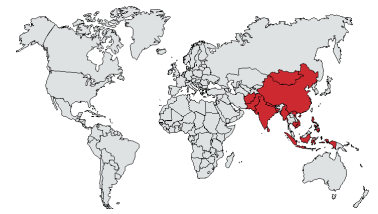
The three agencies dominating the Asian market are PRIME, active in Indonesia, M-CRIL and Crisil, that are both mostly active in India. Their respective market shares in 2007 are: 32%, 38% and 21%. The JCR-VIS agency is only active in Pakistan with 7 ratings in 2007. Most of these were mandatory ratings.

In India, the market is shared by two agencies M-CRIL and Crisil, which both carried out microfinance and credit ratings.



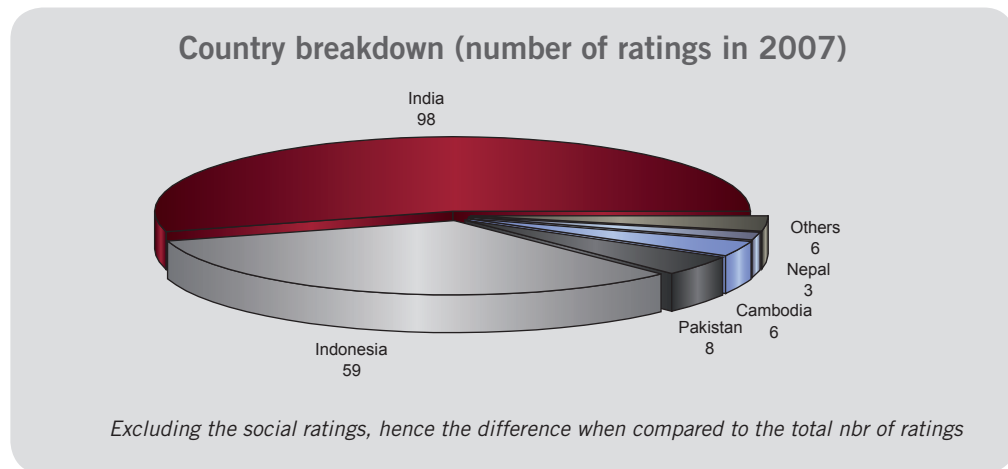
PRIME's emergence on the Indonesian market is significant and its market share increased from 7% in 2005 to 32% in 2007. In the meantime, M-CRIL's share dropped from 70% to 39%, although the actual number of ratings performed did not decrease much.





Cambodia could be considered as the most regular country with a few ratings each year since 1998. The demand in Pakistan is mainly but not exclusively driven by the regulation. Nepal made a strong appearance on the market with 7 ratings in 2005 that dropped to only one rating the year after.

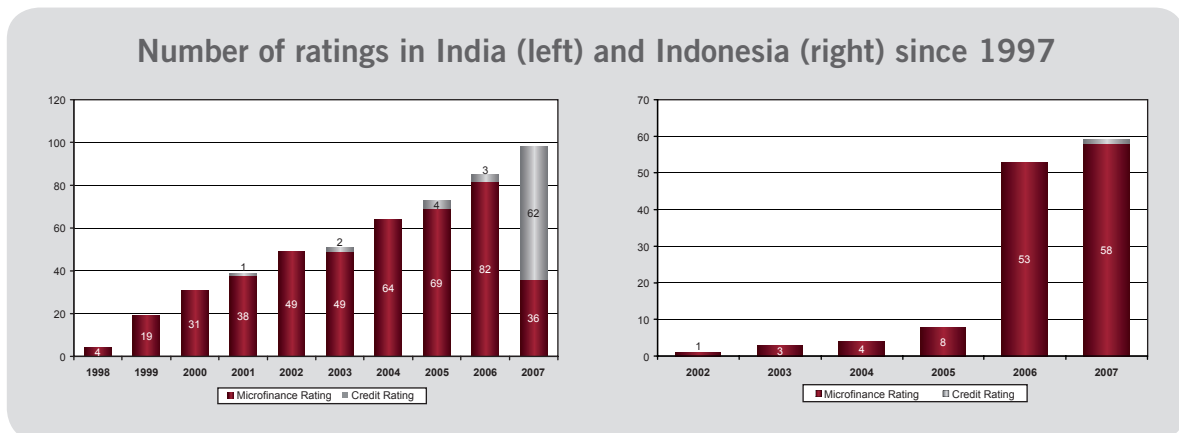
Bangladesh has a large MFI market but, unlike India, the apex organization Palli Karma-Sahayak Foundation (PKSF) performs its due diligence internally and does not require ratings. Although there were 9 assessments in Bangladesh in 2004 and 6 in 2005, none were conducted in 2006 and only one in 2007.

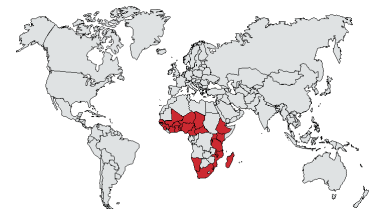


India and Indonesia

In 2007, India seems to have reached a second stage of maturity. The first stage could be reflected by the shift from first ratings to update ratings. These updates account for two thirds of the ratings in India in 2007. The second stage could be reflected by the shift from microfinance specialized products to mainstream products.

The market in Indonesia has grown very fast thanks to the emergence of PRIME, funded by the Bill & Melinda Gates Foundation, which demonstrates the under-penetrated nature of the Indonesian market. Some of the MFIs rated for the first time in 2006 have performed updates in 2007. In 2007, 30% of the ratings were updates. However, the local market is still too young to be able to make further assumptions on its evolution.





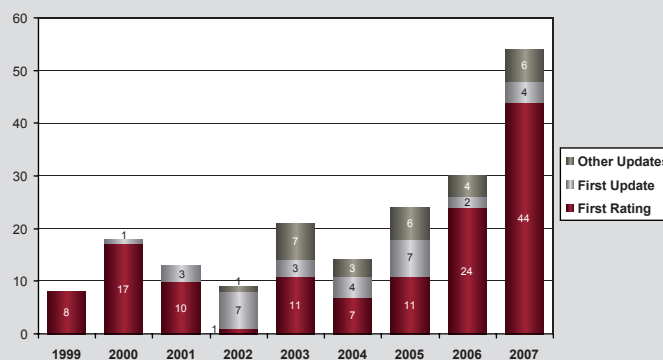
Impressive growth since 2004

Prior to 2004, the SSA rating market was stagnating. Since 2005, it has experienced a rapid growth of 386% in 3 years, from 14 ratings in 2004 to 54 in 2007:

- +71% in 2005
- +25% in 2006
- +80% in 2007

Four years of continuous growth (mainly first-time ratings)

Number of ratings between 1997 and 2007



Excluding the social ratings, hence the difference when compared to the total nbr of ratings

As previously seen in the “Regional discrepancies” section, the SSA region is now the third region out of 5 in terms of the number of ratings in 2007. The gap with the second region (Asia) is huge, but the SSA region seems to make up its delay and get a decent foothold in the microfinance rating market.

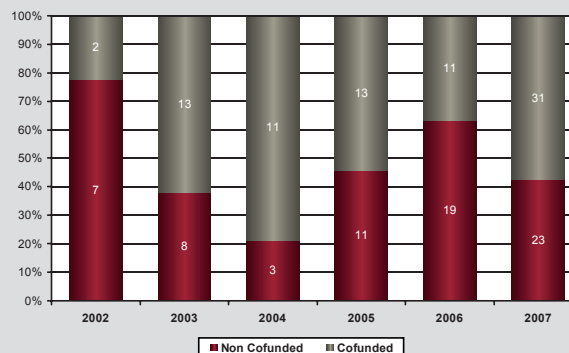
The SSA rating market now contains 133 MFIs and 31 (23%) of them have updated their rating at least once. At the moment, unlike some more mature regions, MFIs in the region have only an interest in microfinance ratings and not yet in credit ratings. The market is emerging and has not yet reached a mature level yet. Few MFIs have already updated their rating and no credit rating has been achieved in the region since 1999.

The average frequency of updates observed in the region is 2.5 years, which is six months more than the global market.

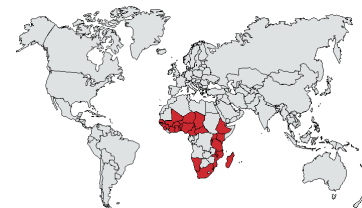
If the regional market has no dependency on regulation (only voluntary ratings), the proportion of ratings co-funded by the Rating Fund is higher than on the global market. It needs to be less dependent on external aspects to be considered as an autonomous market.

Only 23% of MFIs have updated their rating

Ratings co-funded by the Rating Fund



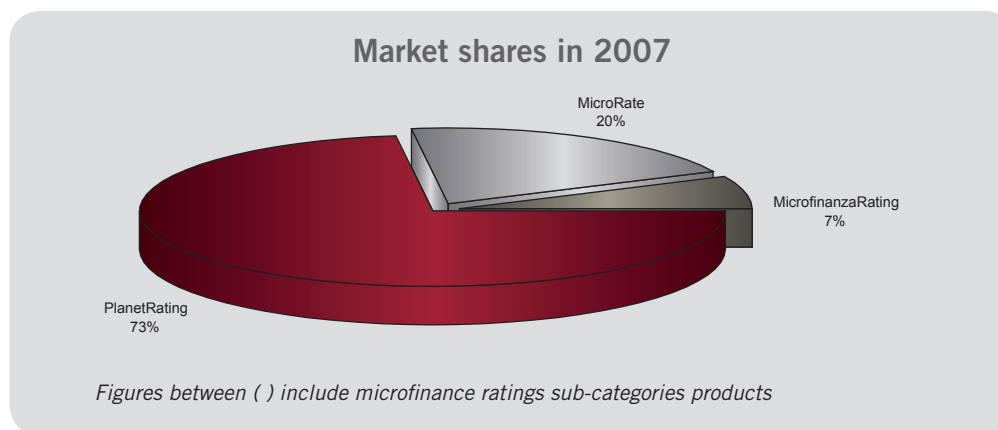
Excluding the social ratings, hence the difference when compared to the total nbr of ratings



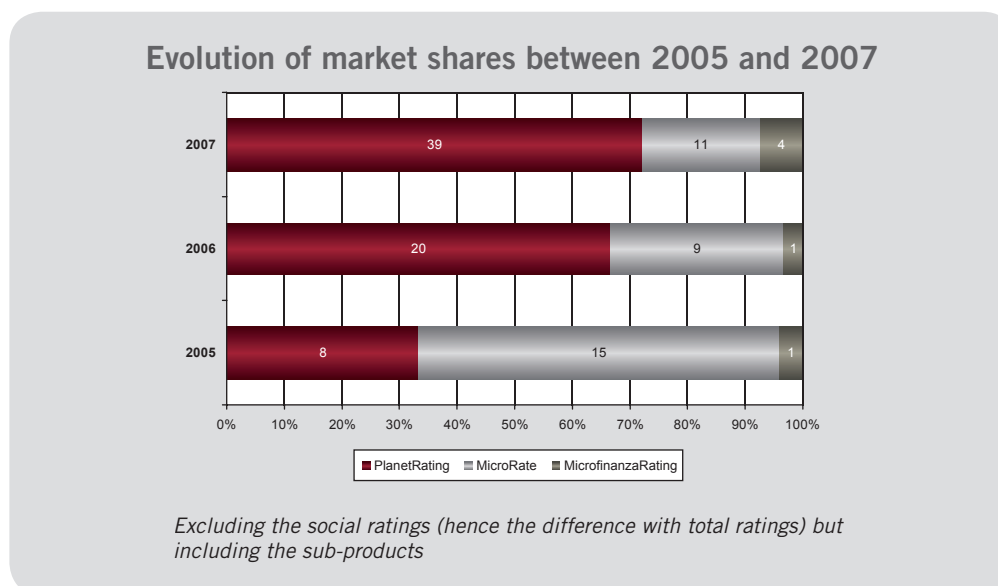
Three rating agencies operate in the region. All of them are specialized agencies with global coverage (PlanetRating, MicroRate and Microfinanza Rating) since there is no current market for mainstream agencies supplying only credit ratings.

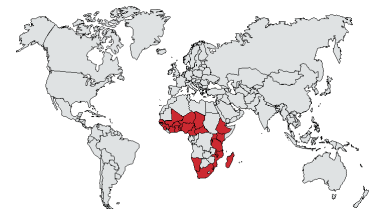
The chart below presents the respective market shares of these three agencies in 2007 and the graph at the bottom of the page shows the evolution of these market shares between 2005 and 2007. The market is dominated by PlanetRating with a 56% share (excluding microfinance ratings sub categories). This market share amounts to 73% if the microfinance ratings' sub categories are taken into account.

Furthermore, 95% of the ratings performed by PlanetRating are first-time ratings and 75% of Microfinanza Rating missions have been co-financed by the Rating Fund. This shows that the market is still emerging.



According to the chart below, market shares have significantly changed a lot between 2005 and 2007 if we take into account the rating sub categories. There is a large growth for Planet Rating compensated by a decrease of MicroRate shares from 60% in 2005 to 20% in 2007.

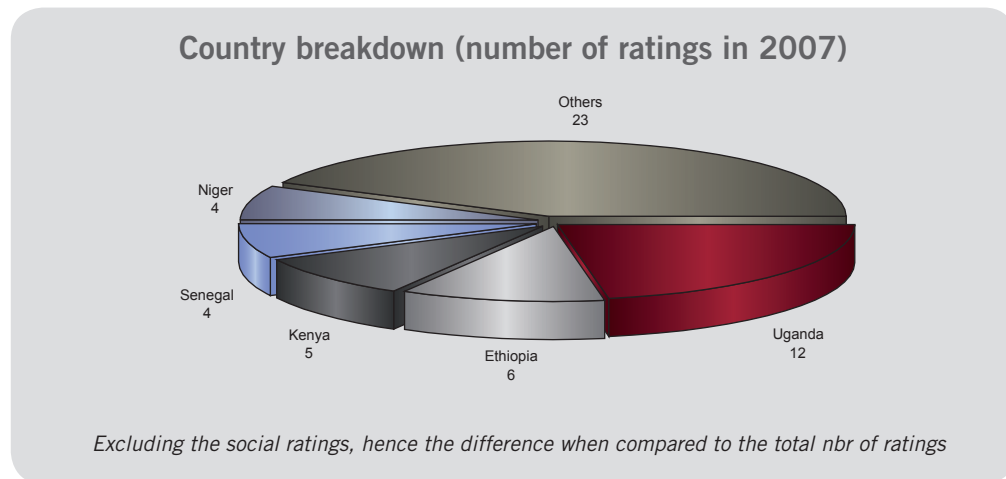




The SSA region is not led by one or two countries that account for most of the ratings as we saw in some other regions like in Asia. Indeed, the region is composed of 17 active countries having carried out 54 rating exercises in 2007. Twelve of them took place in Uganda (22%), followed by Ethiopia (6), Kenya (5), Senegal and Niger (4). The other twelve countries account for 23 other ratings.

The impressive growth of the region is hiding very different country dynamics.

Large discrepancies between the different countries



All rating peaks in Africa can be explained by rating programmes funded or largely co-funded by donors.

Uganda is actually the most active and mature country in the rating field as its number of ratings is growing and reached every year 12 in 2007. Among those, 92% are first ratings and 33% have been co-funded, which is less than the overall region.

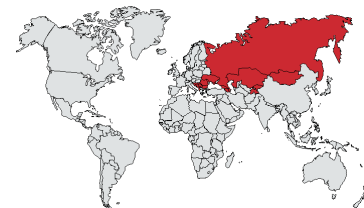
Senegal is very stable in terms of number of ratings with 3-4 each year, but more than half of these are co-funded.

Mali has experienced a peak in 2006 with 9 ratings, but it dropped in 2007 to one rating only.

Ethiopia, Kenya and Niger have all experienced a spectacular growth between 2006 and 2007 from almost no rating to respectively 6, 5 and 4 missions.

As mentioned above, the different dynamics between countries can be partially explained by co-financing initiatives other than the Rating Fund carried out in the recent years by local associations or programmes. For instance, in Uganda (as of 8 June 2007), 14 MFIs were rated using SUFFICE fund's services. SUFFICE is actually a European Union and Government of Uganda programme, which was closed in December 2007. Mali's peak in 2006 can be explained by the USAID/Worldbank donor initiative to encourage transparency and sound development of the sector.

The rating market within the region is still very dependent on such initiatives but is willing to develop on a sustainable basis.

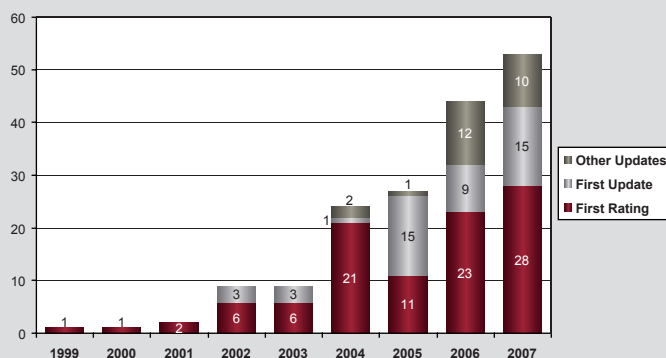


Continuous growth since 2005

In the EECA region, 99 MFIs located in 18 countries have been rated at least once. Among those MFIs, 46 (47%) have updated their rating. The average frequency considered for the update of the microfinance ratings is 1.7 years, which is less than the overall market.

*High proportion of updates but few credit ratings:
Still an emerging market*

Number of ratings between 1997 and 2007



Excluding the social ratings, hence the difference when compared to the total nbr of ratings

The below graph presents the breakdown between microfinance ratings and credit ratings between 1997 and 2007. It shows that 8 credit ratings have been carried out each year since 2004. 8 MFIs in 8 different countries are undertaking a credit rating every year. Thus, credit ratings in 2005, 2006 and 2007 are updates.

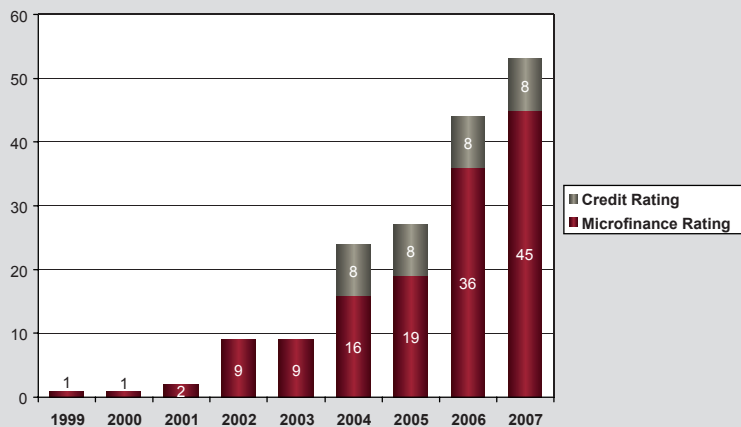
The number of microfinance ratings has been growing since 1999:

- 2005: 16 ratings i.e. +19%
- 2006: 36 ratings i.e. +84%
- 2007: 45 ratings i.e. +25%

Following the growth of microfinance ratings, the total number of ratings is also growing by 13% in 2005, by 63% in 2006 and by 20% in 2007.

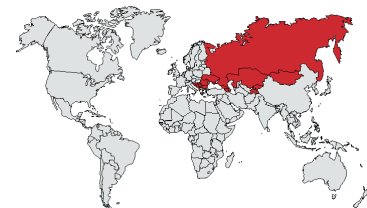
Continuous growth since 1999

Product breakdown between 1997 and 2007



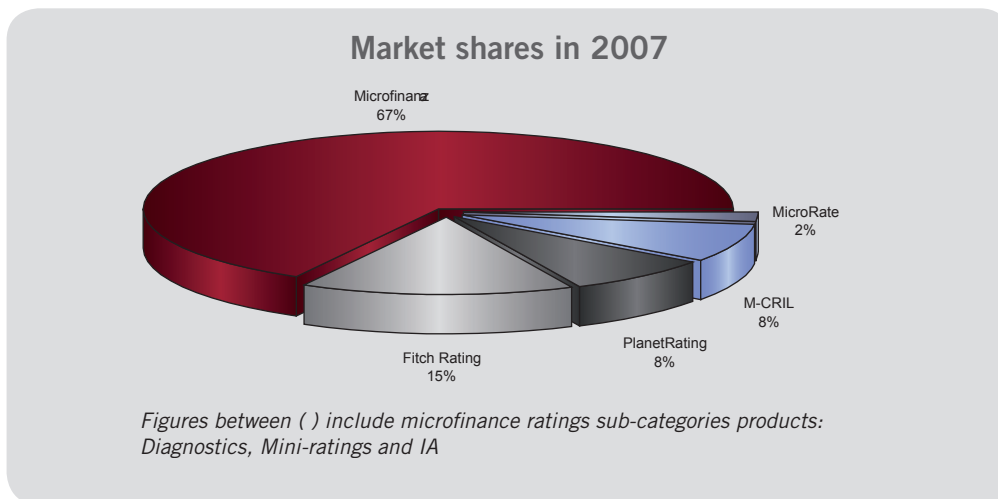
Excluding the social ratings, hence the difference when compared to the total nbr of ratings

If mandatory ratings are not required in this region, the local market seems to be highly dependent on the co-financing initiative of the Rating Fund. Around 50% of the ratings have been co-funded since 2004.



Rating agencies

The local market is shared by five rating agencies. Four of them are specialized in the microfinance area (Microfinanza Rating, PlanetRating, M-CRIL and MicroRate). Fitch Rating is the only mainstream agency and has performed all the credit ratings within the region. The market is dominated by Microfinanza Rating which accounts for 67% of the ratings carried out in 2007. The agency's market share has steadily grown every year. Most of its ratings are first ratings, representing 72% in 2007.



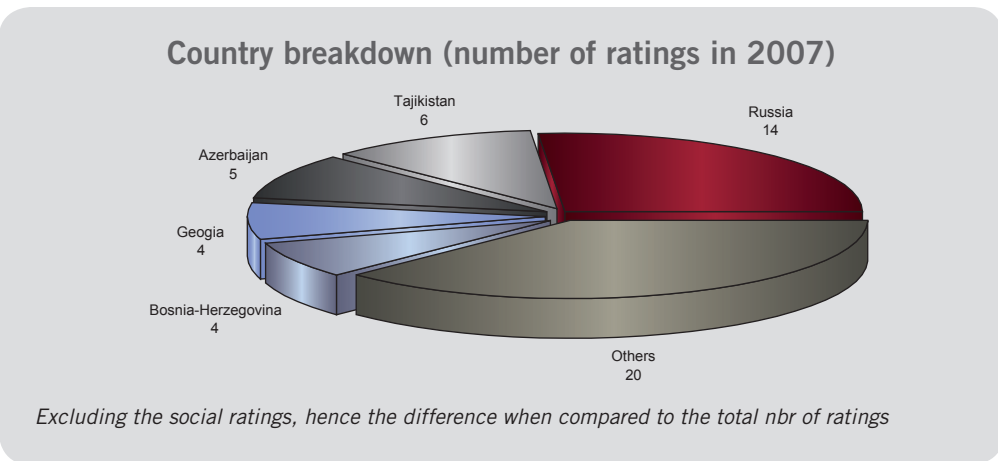
Country dynamics

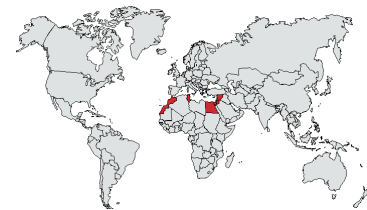
Russia is the leading country within the region with 14 ratings obtained in 2007. Russia aside, the demand is fragmented among many countries such as Tajikistan (6), Azerbaijan (5), Bosnia and Herzegovina, (4) and Georgia (4).

The recent growth of Tajikistan's market with 2 ratings in 2006 complemented by 6 ratings in 2007 (almost all first-time ratings) can be explained by co-funding initiatives that complement the Rating Fund (GTZ's Support for Small and Medium MFOs project).

The situation is similar in Azerbaijan with the Azerbaijan Rating Support Program launched in 2007 to help MFIs undertake their first rating by co-financing up to 60% of the related costs.

Several local co-funding initiatives, in addition to the Rating Fund





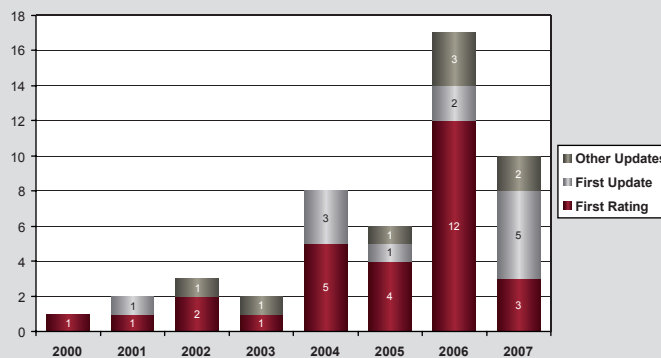
2007: Decrease in the number of first ratings

29 MFIs have been rated in the region and 12 of them (41%) have updated their rating at least once. The number of first-time ratings however dropped between 2006 and 2007 (-75%), and was partially compensated by the growth of update ratings (+40%).

Microfinance rating is mainly the only product being used in the region although one credit rating did take place in 2007. Its maturity level is not yet high enough yet to experience a shift from microfinance products to mainstream ones. Another indicator reflecting the lack of maturity is the frequency of updates of 2.1 years, which is slower than the overall market for this kind of product.

Drop in 2007 from 17 to 10 ratings

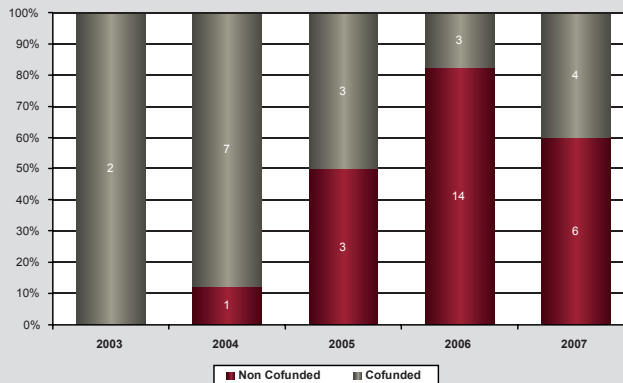
Number of ratings between 1997 and 2007



Excluding the social ratings, hence the difference with total ratings

Regarding the dependence of the rating market on the Rating Fund and the regulatory requirements to perform ratings, it can be noticed that none of the countries require mandatory ratings. This clearly shows that the rating market is not driven by regulation. Nevertheless, although less than 20% of the ratings were co-funded by the Rating Fund in 2006, this proportion reached 40% in 2007. This is much more than the overall market.

Ratings co-funded by the Rating Fund



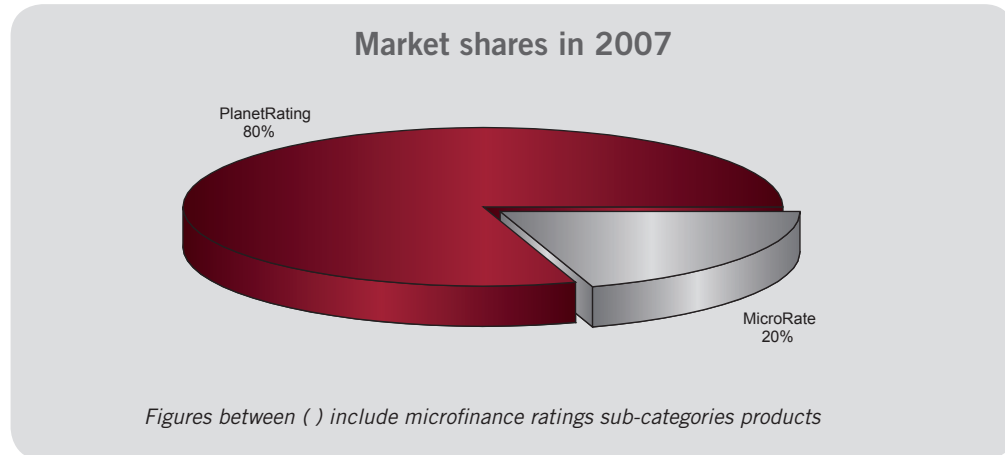
Excluding the social ratings, hence the difference with total ratings



Rating agencies

PlanetRating and MicroRate are the only two agencies that have carried-out rating missions in the region in 2007. Around 80% of them have been performed by PlanetRating. All MicroRate's ratings during the year were updates and took place in Morocco.

Microfinanza Rating performed a couple of ratings but disappeared from the sample in 2007. It was replaced by MicroRate which started its activity in the region in 2006.

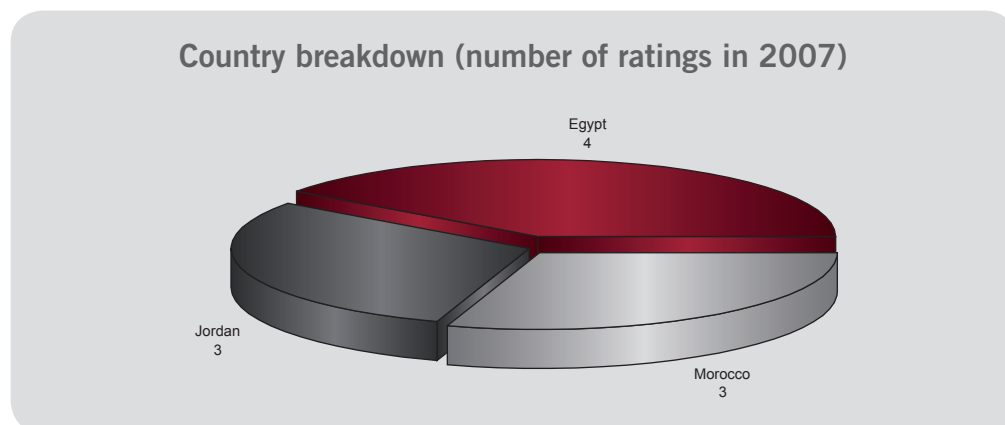


The rating market in Morocco is certainly the most stable one in the region

Country dynamics

Ratings in 2007 were equally shared among three countries: Egypt (4), Morocco (3) and Jordan (3).

Morocco seems to be the most mature country within the region with Moroccan MFIs undergoing ratings each year since 2001. However, ratings dropped from 7 to 3 in 2007.



Egypt and Jordan experienced a leap in their respective number of ratings as no ratings were carried out in either country in 2006.

Increased professionalization of the microfinance rating sector

The microfinance rating field has experienced a regular and impressive growth since 1997. The rating agencies and the emergence of specialized microfinance rating agencies with global coverage played a central role in this development. Over the past few years, the emergence of initiatives like PRIME in Indonesia have rapidly been developed to serve an under-penetrated market and mainstream agencies have quickly responded to the growing demand for credit rating products.

The ongoing geographical development of most agencies and their willingness to open offices in new regions or to affiliate with one of their peers, MicroRate and M-CRIL – now called MicroRating International for instance, is supporting this market growth. Agencies are also active in the product development field with specialized agencies starting to compete with mainstream ones for credit ratings. However, microfinance rating remains the first external evaluation product typically used by an MFI. Several MFIs that use credit ratings undergo microfinance ratings as well, which proves the importance of such products in the development of this market.

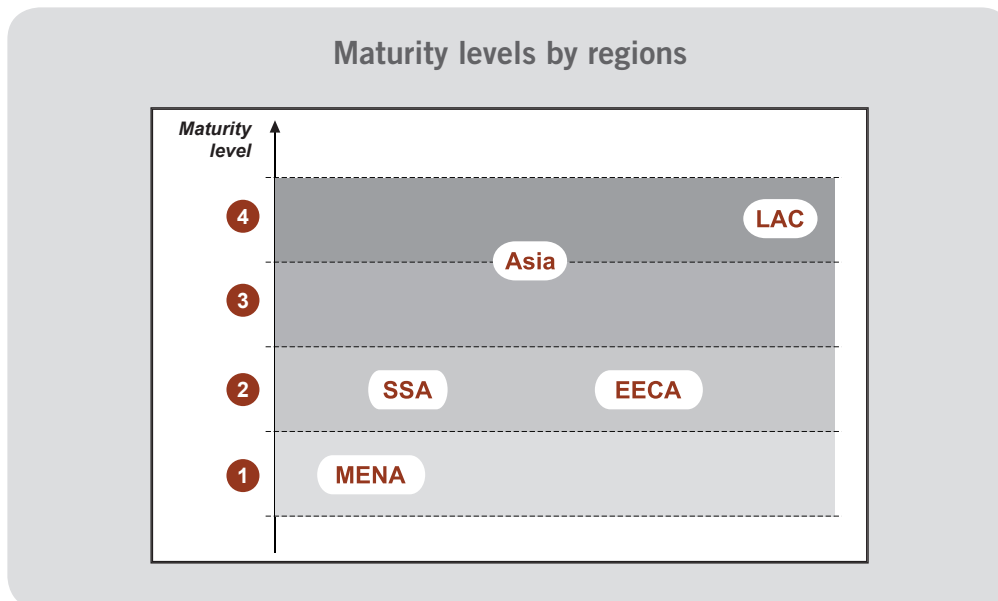
Further discussions among specialized agencies could lead to the standardization of microfinance credit rating recognized by most private investors and especially designed to meet the needs and expectations of MFIs. As stated in the dedicated section of the report, MFIs' loyalty to their rating agency is still high but a few of them have switched several times from one agency to another. This rather new attitude might mean that the market is becoming more competitive and could provide better conditions for MFIs in terms of product adequacy, quality and rating costs.

As a conclusion to the regional sections, several maturity levels can be identified (the following numbers refer to the diagram below):

1. Very few ratings, only microfinance ones
2. Fast growing number of ratings, mainly first microfinance ratings
3. The proportion of updates becomes greater than the proportion of first ratings
4. Credit rating becomes the major product at the expense of microfinance rating

A mature market can be identified according to two main considerations:

- A large proportion of update ratings compared to first time ratings
- A large proportion of credit ratings compared to microfinance ratings



In 2007, the growing demand for ratings was driven by the following considerations:

1. The necessity for MFIs to attract more investments to support their own growth and the needs of their borrowers. In order to achieve that goal, they have to undergo a rating so that their investors can work in an environment they are familiar with and meet their own regulatory requirements.
2. Mandatory ratings are required in three Latin America countries by regulatory bodies: Bolivia, Ecuador and Peru.
3. The willingness of MFIs' management, administrators and donors to have a fair view of the MFI financial performance and its institutional risks and leverages to improve these aspects.

The first point is certainly the main explanation for the spectacular growth of credit ratings between 2006 and 2007. The increased activity of private investors in the field led to more demand for credit ratings. The use of modern financial structures such as CDOs (Collateralized Debt Obligations) by MFIs to attract more funding and reduce cost, is likely to accelerate this trend.

The maturity of the LAC rating market is certainly due in part to mandatory ratings at the first stage. However, regulated MFIs undergo voluntary ratings in addition to the mandatory assessments. This means that regulation is only a trigger for the market and does not support all the demand. The Basel II rules regulating commercial banks will certainly put pressure on MFIs funded by such banks to obtain a rating. This would actually reduce the capital charge for banks and reduce the cost of funding for MFIs.

This trend towards better practices in terms of financial transparency and performance is positive news and has to be encouraged. This could be supported by regular audits as well as ratings. The growing interest of private investors (both socially-oriented and for-profit commercial) is certainly financially profitable for the microfinance field and its sustainability.

However, the microfinance stakeholders should not lose sight of their social mission and the poorer should not be excluded from the borrowing facilities because of a higher risk of default. The social performance evaluation, also called social rating, appears to be the best product to monitor this risk and is expected to represent a future area for the growth of specialized agencies.

Appui au Développement Autonome (ADA), Luxembourg, is an NGO specialised in microfinance and collaborates with microfinance institutions all over the world through financial and non-financial support and exchange.
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