



# **LA-CIF**

## **INSTITUTIONAL PROFILE**

**A CREDIT ENHANCEMENT FUND FOR SMALL BUSINESS BANKS AND MICROFINANCE  
INSTITUTIONS IN LATIN AMERICA**

**NOVEMBER 2001**

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## SUMMARY

Legal Name:	Latin American Challenge Investment Fund, S.A.
Country of Incorporation:	Panama
Legal Status:	Sociedad Anonima (S.A.)
Date of Inscription:	January 1999
Date of Initial Operations:	September 1999
Duration:	Nine Years (2008), unless extended by majority of the General Assembly

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Authorized Capital:	\$ 5M
Capital Issued / Outstanding:	\$ 1.9M
Estimated ROE:	10% after second year of operations

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Principal Shareholders:	<ul style="list-style-type: none"> <li>• Inter-American Development Bank / Multilateral Investment Fund (IDB/MIF) - USA</li> <li>• NORFUND - Norway</li> <li>• Développement International Desjardins - Canada</li> <li>• CARE – USA</li> <li>• Argidius Foundation – Switzerland</li> <li>• Swedfund and Swedish Cooperative Centre - Sweden</li> </ul>
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President of the Board:	Mr. Mehrnaz Rafat, NORFUND
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Fund Manager: Managing Director:	Cyrano Management S.A., office located in Lima, Peru Mr. Fernando Lucano Urioste
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Subordinated Debt:	IDB/MIF \$ 3M, 7 years Swedfund \$ 500K, 7 years Swedish Cooperative Centre \$ 500K, 7 years
Senior Debt:	Agencia Española de Cooperación Internacional \$ 1M, 5 Calvert World Values Fund \$ 200K, 3 years ASN NOVIB \$ 1M, 2 years

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Type of Portfolio:	Credit Risk, Short term loans and guarantees (< 3 years)
Client Target:	Microfinance Institutions (MFIs) and Small Business Banks (SBBs)
Geographic Focus:	Latin America and the Caribbean

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External Auditor:	Deloitte & Touche, Lima
Accountants:	Bureau, S.A., Lima
Accounting Norms:	U.S. GAAP
Banker:	Chase Manhattan Bank, New York
US Counsel:	Greenberg Traurig, Washington DC
Panamanian Counsel:	Tapia, Linares y Alfaro, Panama
Peruvian Counsel:	Estudio Alfredo Solf , Mr. Francisco Belaunde
Human Resources Counsel:	M&M Soluciones Integrales

## **1. MISSION AND OBJECTIVES**

- The Latin American Challenge Investment Fund S.A. ("LA-CIF") is a fund designed to promote the expansion of Micro-finance Institutions (MFIs) and Small Business Banks (SBBs) by providing them with access to financing from the private markets.
- MFIs and SBBs are currently facing an enormous unmet demand for the financial services they provide, highlighting the need to access commercial funds in order to finance their portfolio's growth.
- To this end, LA-CIF offers its clients with sound credit profiles a wide gamut of financial instruments: guarantees, direct and syndicated loans and the purchase of certificates of deposit, bonds and other commercial papers.

LA-CIF's mission is to maximize shareholder's returns and to familiarize commercial banks and private investors with the credit risk of MFI's and SBB's and encourage them to increase their direct exposure to these new generation of financial institutions. LA-CIF offers all products at commercial rates reflecting domestic and international financial market conditions.

## **2. POTENTIAL MARKET**

An estimated number of 50 million micro-enterprises exist in Latin America, of which only 5% have access to formal credit. Due to this high level of unmet demand a variety of institutions have entered this market. These can be categorized into 3 types of micro-finance institutions:

### **2.1 BANKS AND FINANCIAL COMPANIES**

Although micro-enterprises are not their main target market. Few banks and financial companies have entered the micro-finance market in order to expand their client base and achieve higher spreads in a relatively uncompetitive market. Examples include: Banco Santander (Chile); Banco República (Uruguay); Banco del Nor-este (Brazil), Sudameris (Peru).

### **2.2 BANKS AND FINANCIAL COMPANIES SPECIALIZED IN MICRO FINANCE**

This set of banks and financial companies are also formal institutions regulated by banking authorities. However they concentrate their assets in micro-enterprise loans. Most are the result of successful non-profit organizations that had the vision to create a commercial structure that has enabled them to expand their operations. In a few cases, they are branches of financial institutions that intentionally externalize these operations due to the specialized nature of this business. Examples of these institutions include: Fie, Prodem and Los Andes (Bolivia); Cajas Municipales, Mibanco, Financiera Solucion (Perú), Financiera Vision (Paraguay), the micro-credit affiliate of Banco de Desarrollo (Chile), Financiera Calpia (El Salvador).

### **2.3 UNREGULATED CREDIT INSTITUTIONS**

These are foundations or non-profit organizations that serve the micro-enterprise sector taking more of a social than a financial approach. However, many have been both successful and profitable and several are in the process of converting to regulated financial institutions. Often these organizations do not convert due to a lack of a commercial vision or because of legal obstacles. Examples include: Fundación Woman's World Banking Colombia (Cali, Colombia), Fundasol (Uruguay), Emprender (Argentina), Acodep (Nicaragua).

## 2.4 POTENTIAL MARKET IN 8 LATIN AMERICAN COUNTRIES

Country / Year	# MFIs	Total Assets (M \$)	Estimated anual Assets Growth (2001-2003) M \$	Average ROE of 5 top MFIs
Bolivia / 2000	27	497	473	9%
Brazil / 1999	15	16	15	17%
Colombia / 1999	28	107	102	22%
El Salvador / 1999	62	289	276	58%
Nicaragua / 1999	12	46	44	32%
Paraguay / 2000	33	308	294	25%
Peru / 2000	42	456	670	29%
Dom. Rep. / 1999	7	76	72	22%

## 3. CREDIT APPROACH

LA-CIF's assets consists exclusively of debt instruments with short term maturities (< 3 years) and preferably liquid or negotiable instruments. LA-CIF does not purchase shares or issue subordinated loans.

### 3.1 PRODUCTS

LA-CIF principally offers five types of credit products:

- **Direct Loans:** denominated in US Dollars, these loans are designed for institutions operating in highly dollarized economies.
- **Credit Line:** this instrument allows clients to make use of LA-CIF's maximum loan term of 3 years during which they can gradually increase their loan amount.
- **Syndicated Loans:** designed for MFI interested in lowering their transaction costs, LA-CIF can package the debts from various commercial banks or local investors into a single contract loan.
- **Purchase of Debt Instruments:** LA-CIF can purchase from MFIs short and medium term debt instruments such as bonds issues and CDs
- **Guarantees:** Stand-by Letters of Credit (SBLC) issued by an international bank with an investment-grade rating are used to fully or partially back local bank loans given to MFIs. The SBLC's are collateralized with deposits made by LA-CIF in the international banks issuing the SBLC.

### 3.2 TARGET CLIENTS

LA-CIF targets financial regulated institutions, this includes banks, financial companies and credit unions. Eventually LA-CIF will finance non-regulated institutions that are in the process of formalizing their financial activities. Specifically, LA-CIF targets MFIs and SBBs with strong financial performances that require credit lines and access to private capital sources.

### 3.3 PRICING STRATEGY

The yield of LA-CIF's credit operations reflect market conditions, which is consistent with LA-CIF's objective to maximize shareholders return and to promote the link between clients and private sources of capital. The yield is calculated based on the following three factors:

### **1. Market Rates**

- a. International reference rate: LIBOR
- b. Domestic reference rates: inter-bank market rate
- c. Country risk premium: the spread between US T-Bills and the country's sovereign debt.
- d. Client risk premium: calculated based on the client's financial performance.

**2. Competition:** LA-CIF will negotiate competitive rates whenever clients have access to financial markets.

**3. LA-CIF's financial structure:** LA-CIF's expected rate of return is based on a cost and risk projection, which takes into consideration a minimum base rate and a mixture of various rates of return.

## **3.4 RISK MANAGEMENT**

The Fund Manager mitigates client credit risk by (i) creating an appropriate protection structure for each operation (ii) using a USAID guarantee facility (iii) elaborating appraisal reports that monitor market risk, counterparty risk as well as the portfolio's overall risk.

The following risks are evaluated and monitored:

### **Market Risk**

1. Country risk
2. Market environment
3. Rate and investment policies
4. The policies set by regulatory or supervisory agencies
5. Performance of the financial sector and the micro-finance industry

### **Counterpart - Quantitative Risk**

1. Matching of currencies and maturities
2. Liquidity
3. Portfolio and assets quality
4. Profitability
5. Capital adequacy
6. Capital structure
7. Financial margins
8. Operating efficiency
9. Reimbursement capacity

### **Counterpart - Qualitative Risk**

1. Transparency and quality of information
2. Strategic plan
3. Market position
4. Shareholder's solvency
5. Institutional vision and management capacity of shareholders
6. The ability of the institution's human resources
7. Audit and internal control process

## **3.5 EXPOSURE LIMITS**

LA-CIF's portfolio is subject to the following exposure limits:

1. 50% of LA-CIF's equity can be invested in one transaction.
2. 25% of LA-CIF's equity can be invested in one country.
3. 20% of the client's liabilities.

## 4. SHAREHOLDERS AND ORGANIZATION

### 4.1 SHAREHOLDERS

LA-CIF was incorporated under the laws of the Republic of Panama; the shareholders are:

Shareholders	Common Shares	(%)	Incentive Common Shares	Total Common Shares	(%)	Preferred Shares	Total Shares
FOMIN/BID	600	31.4%	0	600	28.9%	599,400	600,000
NORFUND	500	26.2%	0	500	24.1%	499,500	500,000
DESJARDINS	250	13.1%	0	250	12.0%	249,750	250,000
CARE	125	6.5%	0	125	6.0%	124,875	125,000
ARGIDIUS	100	5.2%	0	100	4.8%	99,900	100,000
SWEDFUND	100	5.2%	0	100	4.8%	99,900	100,000
SCC	100	5.2%	0	100	4.8%	99,900	100,000
SCDF	46	2.4%	76	122	5.9%	45,954	46,076
SIDI	42	2.2%	12	54	2.6%	41,958	42,012
MEDA	15	0.8%	23	38	1.8%	14,985	15,023
FUNDA-PRO	11	0.6%	18	29	1.4%	10,989	11,018
ETIMOS	7	0.4%	12	19	0.9%	6,993	7,012
ENLACE FONDOS	7	0.4%	12	19	0.9%	6,993	7,012
FUNDES	7	0.4%	12	19	0.9%	6,993	7,012
<b>Capital</b>	<b>1910</b>	<b>100.0%</b>	<b>165</b>	<b>2075</b>	<b>100.0%</b>	<b>1,908,090</b>	<b>1,910,165</b>

### 4.2 BOARD OF DIRECTORS

The Board is responsible for the supervision and control of LA-CIF's management. The Board is composed of at least 3 but no more than 9 directors at most. The Board is currently comprised by:

NORFUND	Mehraz Rafat (Chairman) / Emile Lindoe
MIF/IDB	Tomas Miller / Sandra Darville
DESJARDINS	Ghislain Paradis / Pierre Emond
SWEDFUND/SCC	Viviana Vargas / Kurt Karlsson
CARE	Calvin Miller / Gordy Molitor
SIDI	Edmond de Capele / Alka Couet
SCDF	Damian von Stauffenberg

Each "main investor" is entitled to appoint a Board member. "Main investors" are defined as the top 9 shareholders with the largest share of the total capital.

### 4.3 EXECUTIVE AND CREDIT COMMITTEE

To improve the efficiency of the Board, several of their rights and duties have been delegated to an Executive Credit Committee that consists of 3 members. Decisions concerning LA-CIF's portfolio are taken by the Credit Committee comprised by 3 members of the Executive Committee and external experts with no voting rights. Members of the Executive and Credit Committee are nominated by the Managing Director and appointed by the Board.

<b>EXECUTIVE AND CREDIT COMMITTEE</b>	
Edmond de Capele (Paris)	Senior micro-finance investment analyst for SIDI (Paris). Former Finance Director of a leading French petroleum group.
Damian von Stauffenberg (Washington DC)	Chairman of Microrate (Washington DC), a company specialized in the evaluation and rating of micro finance institutions. Former high-level executive of the International Finance Corporation (IFC).
José Blanco (Lima)	Head of the Desjardins International project based in Lima. Former executive for the technical assistant provider for credit unions (Quebec).
Vincent Megard (Paris)	Investment Officer at AXA – Assets Management (Paris).
Carl Muñana (Lima)	Independent investor and financial consultant. Former high level executive of JP-Morgan (New York).

#### **4.4 FUND MANAGER**

LA-CIF has a management agreement with Cyrano Management S.A. (Panama) dated December 1, 2000. The Fund's Manager is remunerated by a management fee based on the size of assets and the income that generate by management's "off-balance" sheet activities. In addition to this, the Fund Manager receives an incentive based on LA-CIF's financial performance. The fund's management is the responsibility of Fernando Lucano and it is managed from its head office in Lima, Peru. The management's duties include:

1. Identify, analyze and create business opportunities.
2. Structure, appraise, negotiate and close client agreements.
3. Convene and manage the Credit Committee.
4. Analyze, monitor and supervise the creditworthiness and performance of LA-CIF's clients and LA-CIF's overall portfolio and manage all client related aspects on behalf of LA-CIF.
5. Fundraising.

#### **4.5 SHARES CAPITAL**

LA-CIF was created with an initial authorized capital of USD 5M. At present the subscribed and paid-in capital is USD 1.91M. The capital was sold in Equity Units. Each Unit consisted of 999 preferred shares and 1 common share at a par value of 1 USD per share.

#### **4.6 VOTING RIGHTS**

Only common shares have voting rights. Common shares may only be obtained through the purchase of equity units. However, a limited number of non-voting common shares have been granted to initial investors (sponsors).

#### **4.7 DISTRIBUTION OF DIVIDENDS**

Preferred shares receive an annual cumulative dividend of 6% on paid in preferred capital at redemption. Preferred shares will be redeemed at par value over a two-year period during 2007 and 2008. The General Assembly will determine if any dividend payment is to be given to common shareholders, but only after the preferred shares have been fully redeemed.

## 5. FUNDING BASE

LA-CIF has entered into the following debt contracts (see appendices for contracts and information of investors):

### 5.1 SUBORDINATED DEBT

- ***Inter-American Development Bank / Multilateral Investment Fund*** : \$ 3M sub-debt with 2 year grace period loan. 25% of the principal to be repaid 6 years after the disbursement and the remaining 75% 7 years after the disbursement. The funds were disbursed on March 23, 2000.
- ***Swedish Cooperative Centre***: \$ 500K sub-debt, 2 year grace period loan. 25% of the principal to be repaid 6 years after the disbursement and the remaining 75% 7 years after the disbursement. The funds were disbursed on March 21, 2000.
- ***Swedfund***: \$ 500K, 2 year grace period loan. 25% of the principal to be repaid 6 years after the disbursement and the remaining 75% 7 years after the disbursement. The funds were disbursed on March 21, 2000.

### 5.2 SENIOR DEBT

- ***Agencia Española de Cooperación Internacional - AECI***: a \$ 1M loan, one third of the principal due after 3 years, one third after 4 years and one third after 5 years from the date of the disbursement.
- ***Calvert Foundation***: \$ 200K 3 year loan dated September 30, 1999.
- ***ASN NOVIB (Holland)***: \$ 1 M, 2 years (contract in process).

### 5.3 USAID GUARANTEE

USAID has provided LA-CIF with a \$ 6M, 5 year guarantee. This guarantee allows LA-CIF to protect its portfolio. The guarantee facility includes a \$ 300K cumulative deductible to be paid by LA-CIF in case of client default. Subsequent losses up to \$ 6M on transactions placed under the facility, would be shared on a pari passu basis between USAID and LA-CIF.

## 6. APPENDICES

### Appendix 1 - Directory of References

Auditors:	<b>Deloitte &amp; Touche</b> Eduardo Gris Percovich – Partner Paseo de la República 3074 San Isidro, Lima – Peru Telephone: (511) 442-3434 Fax: (511) 442-2861	
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## Appendix 2 – Legal Documents

LA-CIF has signed the following legal documents:

- Articles of Incorporation (Panama)
- Shareholders Agreement
- Management Company Contract
- USAID Guarantee
- Subordinated Debt Agreement with the IDB/MF
- Subordinated Debt Agreement with Swedfund AB
- Subordinated Debt Agreement with Swedish Cooperative Centre
- Senior Debt Agreement with Agencia Española de Cooperación Internacional
- Loan Agreement with Calvert World Values Fund

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## Appendix 3 – Management Company Staff

### Managing Director

Fernando Lucano Urioste      Owner of Cyrano Management, a company specialized in financing of micro finance institutions. Former project leader at IDB (Washington DC) and SIDI (France).

### Risk Analysts

Marco González Aguayo      Master´s Degree in Finance from Universidad del Pacífico in Lima.

Gustavo Santivañez Monge      Former university finance professor in Lima.  
B.A. in Business Administration from Universidad Católica (Peru)

### External Consultants

Socorro Acuña      Finance Director of Caja Municipal de Arequipa, former financial consultant for IPC in Nicaragua.

Carlos Muñana      Independent financial consultant in Lima. Former General Manager of JP-Morgan in New York and Mexico.