



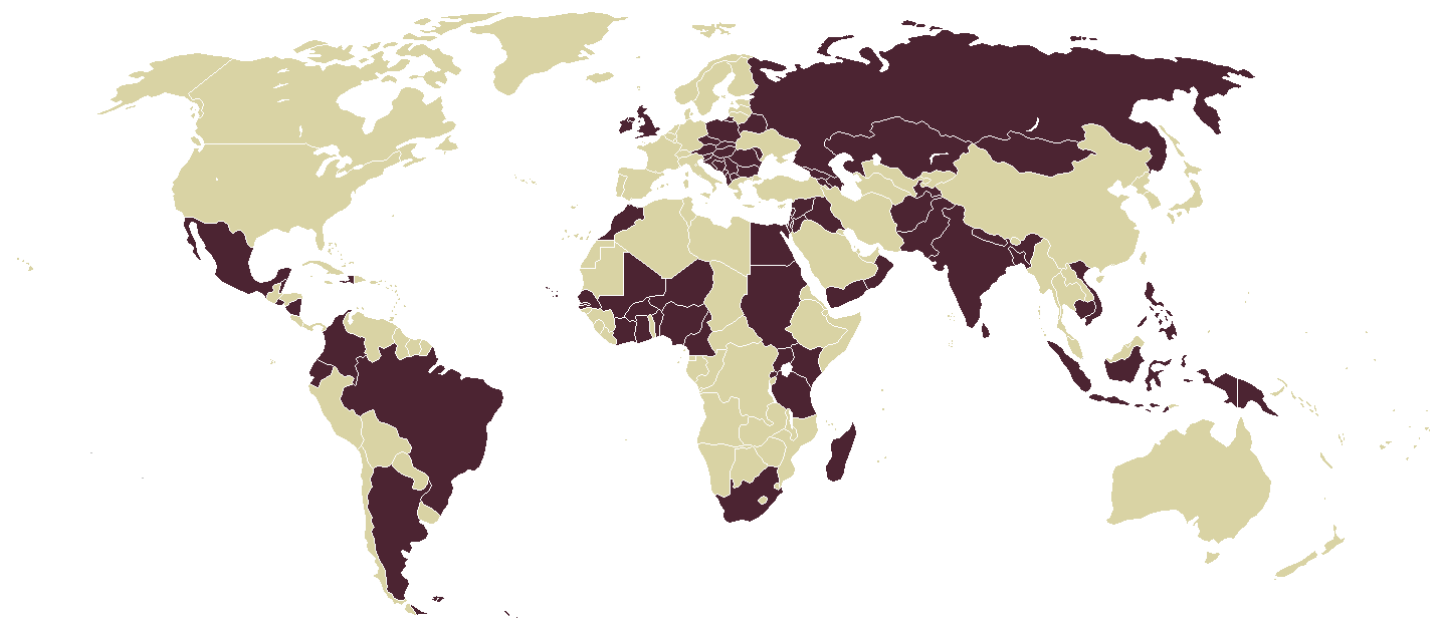
SHOREBANK INTERNATIONAL

**Institutional Assessment of the
Sindh Rural Support Organization's
Microfinance Program**

Submitted to

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30 July 2012





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**ABBREVIATIONS**

BOD	Board of directors
CIF	Community investment fund
CO	Community organization (group)
CRA	Credit assistant
CRO	Credit officer
EOBI	Employee Old Age Benefit Institution
FIS	Financial information system
FSS	Financial self-sufficiency
HR	Human resources
HRD	Human resource development
IA	Internal audit
IAD	Internal audit department
IGG	Income generating grants
IT	Information technology
LSO	Local support organizer
MER	Monitoring, evaluation, research
MF	Microfinance
MFB	Microfinance bank
MIS	Management information system
NGO	Nongovernmental organization
NRSP	National rural support program
OSS	Operational self-sufficiency
PIU	Project implementation unit (CIF)
PKR	Pakistani rupee
PSC	Poverty score card
RCED	Rural Credit Enterprise Development
SBI	ShoreBank International
SBI-P	ShoreBank International - Pakistan
SRSO	Sindh Rural Support Organization
TNA	Training needs assessment
UC	Union council (smallest form of government office)
VO	Village organization



EXECUTIVE SUMMARY

In preparation for the next phase of SRSO's microfinance (MF) program's development, ShoreBank International Ltd Pakistan (SBI-P) was engaged to perform a broad assessment of the credit operations – rural credit enterprise development (RCED). RCED is a separate MF program within SRSO. The following are the main strengths, weaknesses, and areas which will need strengthening in order to support expansion of RCED's activities and the organization:

STRENGTHS

A strong governance structure is in place, with active and committed board members. The management team is equally capable and committed. All senior staff is well qualified to perform their functions as the organization now exists.

The MF program, rural credit enterprise development (RCED), is positioned well within SRSO as a segregated program run independently of the grant-based activities, with separate financial information. This helps position SRSO to seek external commercial funding for the MF activities.

RCED's activities are based on operations of field offices previously held by NRSP. Products and methodology were inherited from NRSP, and were proven successful for delivering credit to rural farmers. Using this tested methodology RCED was able to greatly expand the portfolio across all districts of upper Sindh.

The weak management information system (MIS) is in the process of being replaced with new online software, integrated fully with accounting, human resources, and payroll. A data center has been established at the head office (HO) and staffed by qualified professionals. However, until the new MIS is fully operational in all districts, the quality of it and the data center operations will not be fully known.

WEAKNESSES

RCED's enterprise loan product is mostly urban based and using a monthly repayment process. Unlike the experience of most MFIs, the enterprise loan product at RCED has not performed as well as the traditional agricultural lending. Its methodology needs to be reviewed to identify where it diverges from best-practice enterprise lending and make the corrections that will allow an improvement in its PAR.

The organizational structure for managing field operations is inefficient and ineffective. Over the last two years, the operations manager has led SRSO's efforts to develop and install the new information technology (IT) – an online network – and replace the old MIS. Normally, this would be a fulltime job for an IT/MIS manager. At RCED, the operations manager is responsible for the management of all field operations as well. Resolution of this truly untenable situation is being attempted by the hiring of four middle level managers who will still report to the operations manager. The result will be four more employees for him to supervise and the continued responsibility for field operations. This report details an alternative structure to correct this weakness, by replacing the four middle managers with one senior



manager at the HO and moving field operations out of the control of an already fully engaged operations manager.

The structure within field offices is also of concern. The original staff structure has stretched into new forms as the organization has grown, resulting in a variety of combinations of the different positions used at the field unit (FU) and branch level. No standard staffing structure seems to exist, and work flows fluently between the various field positions.

It is recommended that RCED: merge the urban and rural offices into one line of reporting; identify characteristics of a typical small, medium, and large FU – client levels & staffing needs; assign existing offices to one of these categories; and harmonize current staffing with the appropriate office category. These standardized structures can then be used for future business projections and staff planning.

While a superficial review of the new MIS did not reveal any serious flaws, its installation at RCED could present a significant risk to operations. The software was developed locally, by an inexperienced team of microfinance software developers, and has never been in full production at another institution. The RCED team is also inexperienced managing a software installation and data migration process. In addition, this is an online system, which depends on stable, high speed communications technology that does not always exist in rural Pakistan. The IT staff reported feeling comfortable with the impending switch to the new MIS, but given the high risks it presents, caution is advised.

PREPARING FOR GROWTH

As the MF program grows in size and complexity, in products and staff structures, it will need to be brought to a new level of professionalism. Some areas that are working well now will be strained by the growth, so should be strengthened in preparation.

The governance of the MF program activities, which focus on sustainability, would be stronger with the addition of one or two board members with experience in private business and audit. Also, the BOD might benefit from a MF sub-committee comprised of members that are experienced in MF who can provide recommendations and guidance to the greater board on MF policies.

The SBI-P assessment team recommends building a human resource development (HRD) function at RCED HO. A number of growth challenges will require RCED to focus on staff development. This includes training staff to provide more complex products and methodology; navigate the automated MIS; and supervise greater numbers and levels of employees. In preparation, it is recommended that RCED create an HRD position responsible for planning and implementing staff development programs.

New credit policies and procedures have been approved for offering larger sized agricultural loans and some limited consumer loans. Both will require specific procedures separate from the current methodology for loan analysis and loan structuring. None is yet in place. RCED staff is strongly recommended to seek out information about best-practice loan analysis techniques for larger agricultural loans.



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An opportunity for strengthening both RCED's operations and offering better services to its clients exists, by partnering with one of Pakistan's branchless banking networks. If designed well, field staff could be relieved of much of the loan recovery work, through the use of an existing agent network. Also, deposit and other banking services could be linked to SRSO COs through the same network of agents, bringing valuable financial services to SRSO's clients.

In the future RCED a marketing expertise will be needed for better understanding its market (market mapping); developing products that respond to client needs; creating effective advertising materials; and understanding the full value of branding. It will be some time before RCED is of a size that requires a fulltime marketing professional, but in the interim developing some of that expertise in existing staff is recommended.

Internal controls at RCED are good, but will become very costly as the organization grows. Supervision of the credit process is robust, but at the expense of overstaffing the function. Currently, every new loan application is reviewed by at least five levels of the organization. At the other extreme, the internal audit department (IAD) does not have a single auditor specialized in MF methodology, or criteria for client visits as part of its audits. The two extremes need to be brought toward the middle, where fewer staff is used to supervise each credit and a more thorough audit of MF operations and the loan portfolio is performed.



SRSO BACKGROUND

SRSO was registered as a non-profit NGO on May 29, 2003. Its operating area is the nine districts of upper Sindh, where its main objectives are to support the government's poverty alleviation policies in all of the Union Councils (UCs) through rural committees that plan, implement, and manage development activities¹. "The vision of SRSO is to foster a framework of grassroots institutions in villages located in 253 Union Councils of 9 districts in Sindh, to harness the potential lying within the communities to help themselves²." It fulfills these by providing the following services:

- Social mobilization;
- Human resource development;
- Natural resources management;
- Social sector services;
- Physical infrastructure & technology development;
- Enterprise development;
- Gender & development;
- Rural credit & enterprise development (RCED)

The RCED operations were formed out of the NRSP's upper Sindh offices, staff, portfolio, and operating policies and procedures. Until the recent approval of revisions to RCED's credit policies (June 2012), RCED's credit program was a copy of NRSP's.

In the RSP model, the delivery of social services (i.e. health, education, enterprise grants) to poor communities enhances community members' ability to successfully utilize credit services. At SRSO, credit clients access loans through groups independently formed for that purpose, and minimally linked to social services available through separate groups.

¹ SRSO website

² SRSO website, vision statement



ASSESSMENT OBJECTIVES

ShoreBank International Ltd Pakistan (SBI-P) team performed a moderately deep institutional assessment of SRSO's micro-credit operations using a combination of interviews, documents review, field and client visits. Six branches were selected for visits, based on a sampling criterion of strong, average, and weak PAR. The areas of review included:

1. Governance & management: BOD qualifications and functioning of the board & its committees; organizational structure & management qualifications;
2. Risk management & internal controls: Risk management policies, practices, & procedures; IA organization, audit plan, audit reporting, branch rating system, & management;
3. Products: Both features and pricing in context to the competition from the local market & methodology compared to best practice;
4. Branch/field operations: Portfolio management & field supervision, PAR, provisioning, effective yield on portfolio, operational efficiencies, and profitability leading towards OSS and FSS;
5. MIS & IT: General assessment of adequacy of IT infrastructure & MIS to support the business
6. HR performance management & HRD: Staffing levels, staff turn-over, management of performance against business targets, and staff development;
7. Financial management & performance: Growth, portfolio & geographic concentrations, & performance benchmarked against local & regional standards; and
8. Market positioning and areas of opportunity: Demand, competition, levels of saturation, regulatory and external factors, and areas of emerging opportunity and innovation.



INSTITUTIONAL ASSESSMENT

GOVERNANCE AND MANAGEMENT

The SBI-P team evaluated SRSO's governance structure and practices through interviews and a review of written governance policies. Based on the information that was available, SRSO's governance was assessed as strong, but could benefit from some improvements.

GOVERNANCE

The general governing body is comprised of 18 members from the government and private sectors, all with a social development interest. The board of directors (BOD) is elected from and by the general body, and is comprised of 14 members plus the Chief Executive – nearly the entire governing body. This is a particularly large BOD, which given the dynamics of the usual decision process leads to long protracted quarterly meetings. Given the relatively high attendance rate, a smaller more focused BOD would bring agility to the decision process, and more efficiency to the meetings.

The governance policy of SRSO outlines responsibilities for members of the general body and BOD, but does not establish minimum BOD member qualifications expected for accomplishing these responsibilities. In addition, BOD sub-committees for audit, risk management, and finance are suggested, but no requirements are given. Actual sub-committees in operation are executive and audit / risk management.

TABLE 1: SRSO'S BOARD OF DIRECTOR MEMBERS

BOD Member Name	Board / Sub-Committee Membership	Education	Key Positions Held / Qualifications
Mr. Shoaib Sultan Khan	Chairman	MA in English from Lucknow University, BA Law, Peshawar University, & completed Public Administration Course at University of Cambridge, UK	As Senior Advisor, South Asia Poverty Alleviation Programme (SAPAP) of the UNDP, Mr. Khan has set up demonstration pilots in the six countries of the SAARC region, on the pattern of the AKRSP. He has also received the Global 500 award in 1989, the Sitara-e-Imtiaz in 1990, the Ramon Magsaysay Award in 1992 and the WWF Conservation Medal in 1994.
Mr. Fazalullah Qureshi	Vice Chairman BOD / Chairman Executive Committee	MA Economics, Sindh University; Certificate in Development Economics, Glasgow University, UK; completed Fellowship in Development Economics from World Bank's Economic Development Institute (EDI) Washington D.C.	Serving as Chairman of the Board of Pakistan Steel; appointed Vice-Chairman/Member National Electric Power Regulatory Authority (NEPRA) in 2001 & served the Federal Secretary Planning & Development twice; Chairman of National Tariff Commission in 1999.



Dr. Rashid Bajwa	Member BOD & Executive Committee;	MPH degree from the UK and an MBBS from Pakistan	Extensive experience in the fields of management, social mobilization, community development, microfinance and policy; implementing one of the largest microfinance programs in Pakistan & chairman of BOD for NRSP Microfinance Bank
Mr. Muhammad NazarMemon	Member BOD, Executive & Audit Committees	MA Economics, University of Karachi; MA Regional Planning, Clark University, USA; Diploma in Comprehensive Regional Planning, United Nations Center for Regional Development, Japan; & Certificate in District Health Planning, Institute of Child Health, London, UK	Former CEO SRSO; Consultant Capacity Building National Reconstruction Bureau (NRB); served in development of area based programs for UNICEF, with special focus on women and children, in Tanzania and Uganda
Ms. Naheed Shah Durrani	Member BOD & Executive Committee		Civil Servant; Currently Secretary / Director General – Sindh Board of Investment; Previously 14 years in foreign ministry, district management group, & finance ministry. Also provincial secretary for education & Special Finance Secretary – Government of Sindh.
Mr. Tasneem Ahmed Siddiqui	Member	Political science, Islamia College, Sukkur; MA political science, Sindh University, Hyderabad; BA Law Sindh Muslim Law College	Former director general KatchiAbadis Authority; Deputy Secretary of the Labor Department based in Karachi; founder of SAIBAN, working for the poor communities for establishing low cost housing.
Mr. Suleman G. Abro	Member	Master Degree in Sindhi literature & Sociology; and LLB Degree	Ten years welfare activities with Sindh Graduates Association (SGA) an NGO; Founder and CEO of “Sindh Agriculture and Forestry Workers Coordinating Organisation” (SAFWCO).
Mr. AazarAyaz	Member BOD & Executive Committee	Master Degree in Economics	Executive Director of “The Researchers,” a research based development organization in Islamabad; over 30 Years in Corporate and Social Development sectors; Research areas are women's political empowerment and decentralization in Pakistan.
Mr. Ghulam Mustafa Abro	Member		Executive Director at Socio- Economic Research & Development Organization; area of expertise- Development Economics; Publications and Working Papers at National & International Level.
Dr. Muh’dSulem	Member BOD & Executive	MS from Karachi University in	Founded Hala Graduates Association; Founded Sindh Graduates Association;



anShaikh	Committee	Anesthesiology	Dr. Shaikh has been actively participating in the development management, poverty alleviation, social mobilization, networking and allied activities; Currently also Secretary Board of Trustees SZABIST & Chairperson Advisory Committee Centre for Information & Research.
Dr. Shereen Mustafa	Member BOD & Executive Committee	MS - Social Sciences from SZABIST (2006); MBA - Pakistan Institute of Management (PIM) Karachi (2003); MBBS - Peoples Medical College, Nawabshah (1990)	19 years Civil Servant – Govt. of Sindh Served in various capacities, in the provincial line departments and donor-assisted public sector programs.
Mr. Nazar Hussain Mahar	Member BOD & Executive Committee		Retired Civil Servant Ex-Additional Chief Secretary (Planning & Development Dept., Govt. of Sindh)
Dr. Sono Khangharani	SRSO CEO & Member Executive Committee	D.V.M. (Sindh Agriculture University Tandojam, Pakistan)	Extensive experience in Rural Development and association with Rural Support Programs (NRSP, TRDP & SRSO); Major contribution in rural microcredit, and poverty reduction programs; Presidential Award of Honor “Tamgha-e-Imtiaz” on 23rd March 2010.

BOARD MEMBER QUALIFICATIONS

SRSO’s board members all serve on a volunteer basis (as required by NGO regulations), but actively attend scheduled board meetings. Many are retired from senior public sector positions or have worked in the development sector at the executive level. All are well qualified, and are reported to engage with management appropriately on essential governance topics, especially in the areas of policy.

The board is not well represented from the business community. With a mandate for establishing financially sustainable micro-credit operations, the microfinance program could benefit from the addition of board members with business experience and their commercial perspective.

Also, the board fairly represents the gender imbalance in Pakistan’s management levels at public and private institutions – primarily male. Given that SRSO’s microfinance program primarily targets women, the board would also benefit from more female members to give it a stronger women’s perspective.

BOARD COMMITTEES

The following board committees and functions were outlined, but a TORs only exists for the executive committee. It is recommended that clear operating guidelines are developed for the committee meetings to ensure board members are kept sufficiently informed and involved in the oversight of these key areas of operations. It may also be useful to have a separate microfinance sub-committee comprised of board members with deeper experience with micro-credit, to advise and make recommendations about RCED policies to the greater board.



Also, the executive committee is particularly large, resembling a mini-BOD. If the greater board were reduced in size, this committee would also need to be down-sized.

TABLE 2: BOD COMMITTEES

Committee	Function	Membership
Executive	On behalf of full BOD supervise the implementation of board policies; make recommendations to full board on changes to policies and funding plans; supervise the CEO; and lead strategic planning efforts.	Mr. Fazalullah Qureshi, Chair Dr. Muh'dSuleman Sheikh Mr. AazarAyaz Dr. Rashid Bajwa Mr. Muh'dNazarMemon Ms. Naheed Shah Durrani Dr. Sheeren Mustafa Mr. Nazar Hussain Mahar Dr. Sono Khangharani
Audit & Risk Management	Oversight of SRSO's audit & control functions; supervision of the Manager of Internal Audit; assess and monitor risks; and monitor financials and bank accounts	Mr. Muh'dNazarMemon, acting chair Mr. Ghulam Mustafa Khero Manager of Internal Audit, Secr
Human Resources	TOR not yet developed	New committee, not yet approved by BOD

RECOMMENDATIONS:

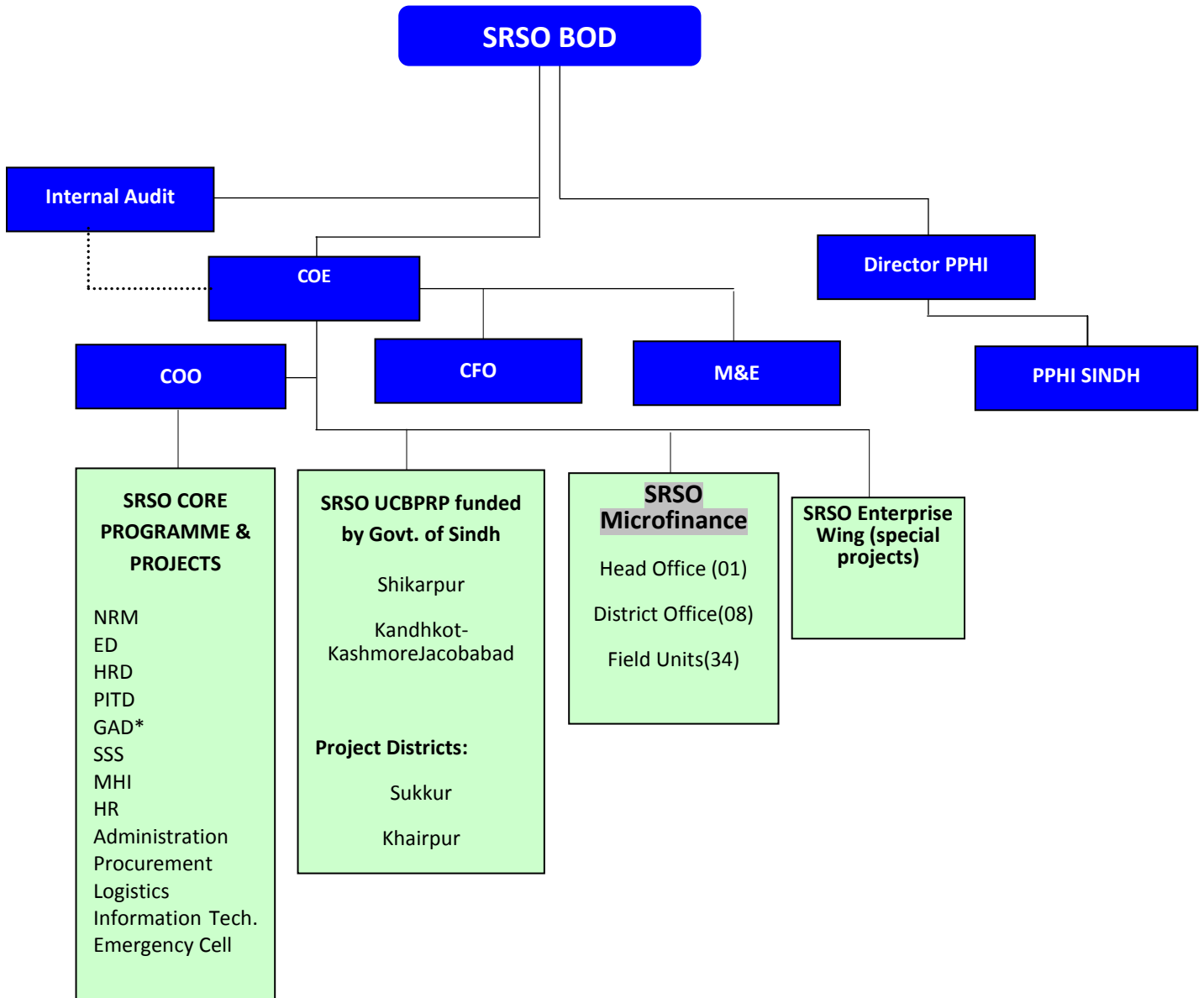
1. Evaluate to benefits of a smaller BOD membership (and executive committee);
2. Change the mix of BOD member expertise to include more business and audit experience;
3. Create audit procedures specific to MF operations; and
4. Investigate the value of adding a microfinance sub-committee.

ORGANIZATIONALSTRUCTURE

In July 2011, SRSO officially separated RCED, its micro-credit operations, into a separate program within the NGO. While still legally part of the NGO, micro-credit staff is confined to those activities, and are not shared with the other programs. Financial reports for the micro-credit program are also segregated. This was done in order to more efficiently manage the larger specialized micro-credit staff, and segregate the income generating operations from the grant-based services. RCED's goal of full operational and financial self-sustainability is close to achievement. The following is an organogram of the entire SRSO:

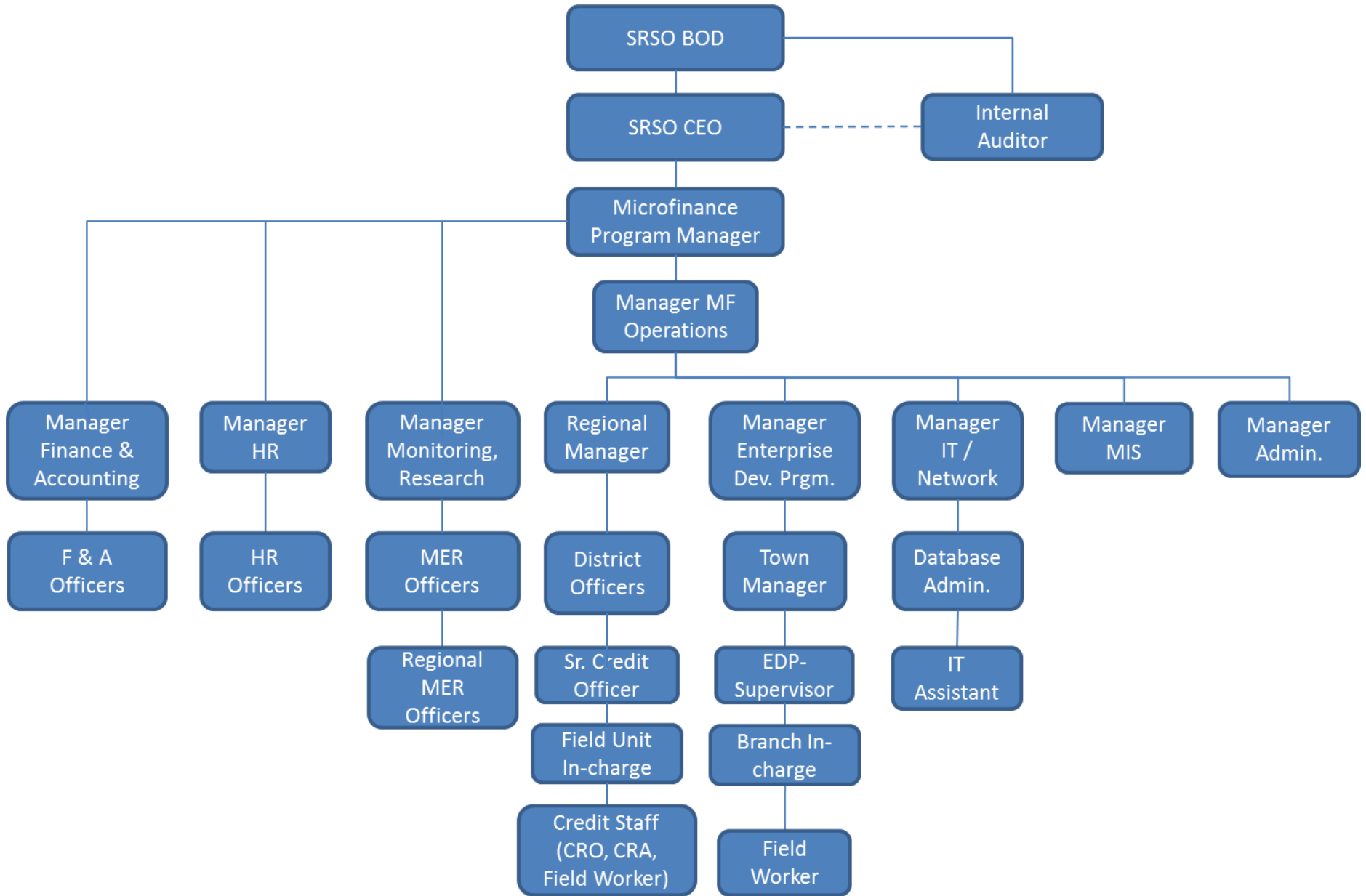


FIGURE 1: SRSO ORGANOGRAM



The microfinance (RCED) structure follows:

FIGURE 2: RCED ORGANOGRAM



RCED STRUCTURE

The organizational structure of RCED is not ideal. Management of RCED head office departments is split between the microfinance head and operations manager, while some decisions can only be made by the head. This has led to some confusion among the staff about who to approach for which decisions.

The largest staff, in the field, report to the operations manager, who is also responsible for IT, MIS, and administration, while also leading the development and implementation of a new data center and integrated MIS. In an effort to support him in the management of field operations, four regional manager positions have been authorized. It is unclear that enough authority and decisions could be delegated to these new managers to sufficiently alleviate the burden on the operations manager.

The dual structure for managing urban and rural offices is inefficient and should be reviewed. Urban offices are reporting to a separate manager at the head office, presumably because most of the urban loans are for enterprises. However, the lending methodology is not significantly different for the enterprise loans, making it unclear why a separate management structure is needed. Also, rural offices should have some enterprise loans as part of their portfolios, so the product expertise cannot be confined to just the urban offices. Should the number of field units for a district warrant splitting the district into two offices, for a better span of control, it would become very difficult to maintain the two structures.

Field structures are inconsistent and confusing, especially at the field unit level. No two offices seem to have the same positions doing the same work. Some of the FUs visited used several credit assistants and field workers, and no credit officer, and others operated with a combination of credit officer, credit assistants, field workers, field assistants, and junior social organizers. The SBI-P assessment team was unable to identify a standard structure among the FUs or across the various positions.

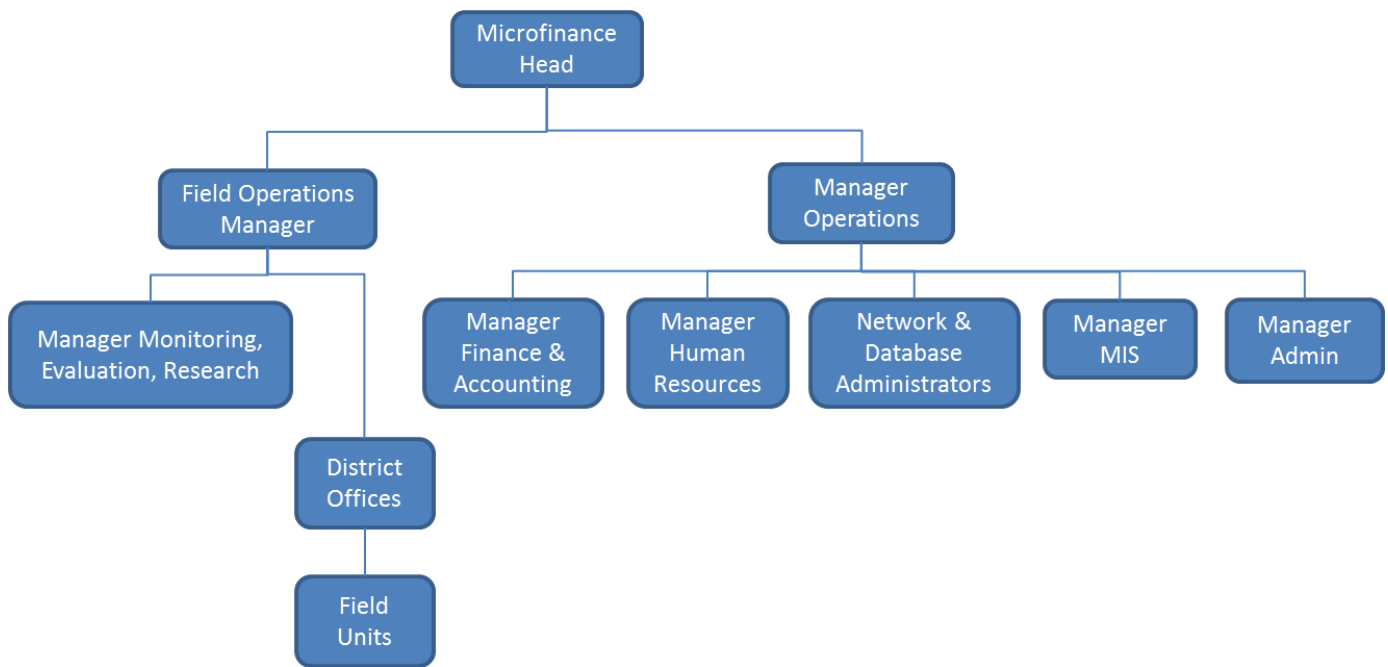
Part of the problem of bringing consistency across the various field positions is the design of those positions. Credit is delivered with a combination of at least two, but sometimes four different positions. As RCED's product mix continues to grow and loan sizes increase, the types of skills and level of education required by field staff will change. Now is a good time to reassess the number and types of positions being used to deliver credit, revise job descriptions, and adjust qualifications for hiring, where necessary.

New positions are being added to district and field offices for data entry into the new MIS. This may be the best use of human resources during peak transaction periods, but may also be unnecessary. Some thought should be given to the possibility of training existing FU staff to use the new MIS rather than adding a new position. For example, the finance staff can do the data entry for the accounting transactions, and credit officers could enter new loan applications, while accounting staff entered the financial transactions. Since the new MIS should bring efficiencies to the operations by eliminating some work, it would be unfortunate not to capture those savings because additional staff has been hired where it wasn't needed.

ORGANIZATIONAL STRUCTURE RECOMMENDATIONS:

1. Replace the RCED regional manager positions with a new Head of Field Operations at the head office and reassign direct supervision of field offices to this new position. Move monitoring under the new head of field operations.
2. Assign the Manager of Operations to oversight of all other head office departments.
3. Combine the management structure for rural and urban offices so all offices report to a district manager according to their location.
4. The new RCED head office and field management structure would look like the following:

FIGURE 3: PROPOSED RCED ORGANOGRAM



In this structure the operations manager is responsible for all HO departments that support the credit operations. His team’s goal would be efficiently serving the business generating side of operations. The field operations manager would then be free to focus on RCED’s ‘business’ – serving the MF clients and generating the income.

5. Standardize field structures to make planning for expansion easier and help field managers better control their operations by:
 - a. Creating standard job descriptions and titles for the traditional agricultural and livestock lending, which might include consolidating similar work into a single position;
 - b. Identifying a model to be used across the organization. This could be done by analyzing the existing FUs and designing the ideal structure for a small, medium, and large FU in terms of number of COs they can comfortably handle and with what staff. This would



- give managers a tool for calculating when more staff will be needed and in which positions;
- Reevaluating grade (pay) levels of supervisors and managers of the larger FUs identified above to recognize their greater responsibilities; and
 - Reviewing staffing needs (skills, qualifications, job descriptions) for delivering the new mix of loan products, that includes enterprise loans and larger agricultural loans (not just for sugar cane) in all districts and more FUs.

MANAGEMENT PROFILE

The following table summarizes the qualifications of SRSO's HO management team that have responsibilities associated with the microfinance program, and managers at RCED:

TABLE 3: MANAGEMENT TEAM

Area of Responsibility	Name	Areas of Responsibility	Education & Experience
At Head Office:			
Chief Operating Officer	Under recruitment	Core program operations; HO administration & IT	
Chief Financial Officer	Syed Mansoor Durbari	SRSO financial mgmt. & accounts	MBA, Finance; BS Institute of Chartered Accountants of Pakistan; Worked as Sr. Auditor at Ford, Rhodes, Sidat, Hyder & Co., Chartered Accountants (Ernst & Young); Deputy Manager at EFU General Insurance Limited; Financial controller in Elite Publishers Limited; Program Manager Finance in Indus Resource Centre (IRC); Accounts officer in Sindh Rural Development Project - SRDP; Coordinator - Finance and Administration in SPO, Turbat Office; Head of Internal Audit - SPO Head Office; Finance Manager in SRSO – Karachi Office
Internal Audit Head	Muhammed Hamza	Internal audit of all SRSO activities	C.A (Finalist); 5 years as Auditor at recognized audit firms
Head of Monitoring, Evaluation, & Research	Nazia Shah	MER of all social programs; policies for all SRSO	M.A Sociology & LLB; 6 years of experience in the MER sector
Staff Training Manager	Hafeeza Khatoon	Staff training for all of SRSO	M.A Sociology; 8 years' experience in HRD sector
At RCED:			
Microfinance Head	Shazia Zubair Gulshaikh	Mgmt. of all micro-credit activities; promotional	M.Com. in 2004; 8 years with SRSO in Microcredit program.



		materials; product design	
Operations Manager	Zubair Ahmed Soomro	Mgmt. of SRSO data center & MIS for credit, finance, support to MF Head for supervision of field operations	BCIT in 2004; 7 years with SRSO in IT & Microcredit.
HR & Admin Manager	ZubairSoomro	Hiring, payroll, & performance mgmt. of RCED staff	MPA; 9 years at various capacities at National level organizations.
Finance & Accounts Mgr.	SaffarBhanbhro	Financial reporting & accounting transactions for RCED	M.A (Economic) in 2010; 7 years' experience in finance & accounts (5 year with TRDP & 2 with SRSO)
Monitoring, Evaluation, & Research Mgr.	ArifaRoohi	Monitoring credit operations, client impact assessments, & market research	M.Sc. (Physical Chemistry) in 1996. 16 months with NCHD as District Officer; 1 year as Zonal Coordinator at UNDP; 3 years of working experience at SRSO in different capacities (MER, HRD)
Wholesale Lending Mgr.	To be recruited	Oversight of CIF	

QUALIFICATIONS & SKILLS

SRSO senior managers are all well qualified for their respective positions. The RCED managers are also qualified and have strong experience working in their fields. The MF head and operations manager both have good field experience as well. Overall, the RCED team is quite strong and capable for working at the level in which the organization currently operates.

However, as RCED deepens its product mix with larger or more complex loans, and as RCED grows into a larger organization, the management team will be challenged to adapt. With the larger loan products comes a need for better cashflow analysis, and stronger analysis skills of credit officers and their supervisors. This could potentially lead to a need to create some specialization among credit officers, and an increase in the skill levels of their supervisors. This in turn could lead to the need to adjust the hiring requirements of some of the field positions. The challenge will be for the management team to adapt and adjust to the growing organization, without having the previous experience in a larger organization.

ROLE OF SRSO EXECUTIVES WITH MICROFINANCE PROGRAM

The roles of SRSO executives with the MF program are well organized and efficient. Their intersection with the MF team is at the appropriate level and does not seem to unduly interfere with the MF decision process.

The SRSO CEO provides direct supervision of the MF program, while day-to-day running of RCED is handled by the MF Head. The SRSO department heads provide the central policies under which RCED staff operate (finance, accounting, HR), but much of the procedures are unique to the MF operations. HO department heads set SRSO policies (under the BOD's approval) and RCED staff has functional reporting to them, for compliance to the policies only. MF has its own HR, finance, and monitoring, evaluation, and research (MER) departments that process their own transactions.

INTERNAL CONTROLS

RISK MANAGEMENT

SRSO does not have a formal risk management policy or practice. Risk is minimally managed through the internal audit department(IAD), and at management meetings on an ad hoc basis.

GOVERNANCE AND MANAGEMENT OF IAD

The IAD is supervised by the BOD through the audit sub-committee. Current members of the committee are few and none have audit experience.

The IAD staff is also relatively new to audit, and none have field experience in MF. Given the difficulties controlling fraud in a financial institution, the current IAD function is insufficient.

TABLE 4: IAD STAFFING

Names	Position / Designation	Date of Appointment	Qualification	Total Experience
Mr. Muhammad Hamza	Manager IA	December 2011	CA finalist	8 months
Mr. Maqsood Ahmed	Auditor	April 2010	MA Economic	3 years and three months
Mr. Ali Raza	Auditor	January 2012	CMA	1 year and 7 months
Mr. Sandeep Kumar Bajaj	Auditor	January 2012	ACCA	1 year and 7 months

AUDIT PRACTICES

The IAD prepares quarterly audit work plans, which are approved by the board's audit committee. The plan is developed on the basis of financial data, portfolio at risk (PAR) of MF offices, and uses a random sampling process. The IAD conducts planned, surprise, follow-up and special investigation audits.

TABLE 5: AUDIT PLAN COMPLETED JULY – SEPT 2011

Area	Target	Actual	%
District Office	5	5	100%
Field Units	15	15	100%
Continuous Pre-payment audit			
Surprise audits:			



1. District office 2. Human Resource Development 3. Enterprise Development 4. Logistic Department		1
		All Sectors Head office Core Head office Core

TABLE 6: AUDIT PLAN FOR JULY - SEPTEMBER 2012

Location	Area	Target
Head Office	Finance Department	1
	UCBPRP	1
	VRP	1
	Other Sectors	1
District Office	RCED	1
	UCBPRP	1

An audit rating criteria is in the process of development, and is expected to be completed by the end of September 2012.

After a review of the IA policies and procedures, minutes of audit committee meetings, audit charter, audit reports, and discussions with the manager of IAD and other staff members, the SBI-Pteam observed the following strengths:

1. Internal Audit Manual approved by the Board exists and audit staff is familiar with it;
2. BOD's audit committee is active; quarterly meetings are conducted and audit observations are discussed and resolved with action plans;
3. Head of IAD reports to audit committee of board;
4. Audit plans are approved by the audit committee of the board;
5. Annual performance appraisal of the manager of IAD is done by the chairman of audit committee;
6. IAD employees' tenure in a particular area has been defined; and
7. Audit observations / findings are shared with the relevant staff and their comments are also obtained.

AUDIT & RISK MANAGEMENT RECOMMENDATIONS:

1. Form a risk management committee of RCED senior managers and the CEO.
2. Designate someone in RCED at a middle management level (such as the MER Manager) to coordinate risk management activities, including:
 - a. Lead regularly scheduled risk management meetings;
 - b. Prepare agenda for meetings;
 - c. Track identified risk areas and report to risk committee; and



- d. Record & circulate minutes of meetings among participants for action.
3. Strengthen the audit BOD committee with more audit expertise.
4. Hire or train one or two specialized MF auditors that can identify the specific risks of MF, and perform audits comparing actual operations against policies and procedures.
5. Develop an audit rating criteria to assign to field offices and departments which weight the various aspects of operations. This is an important tool for determining how often to perform audits, monitoring visits, and other forms of supervision.
6. Include visits to borrowers as part of field audits, choosing clients based on credit officer experience, risk of product, area, activity, and PAR.
7. Define the tenure of external auditors in the TOR or audit charter. Ernst & Young have been SRSO's external auditors since 2007, a longer period than is prudent.

FIELD OPERATIONS & SUPERVISION

A good process for establishing portfolio targets is in place, where field staff collaborates with head office managers to set realistic business goals. Some offices have been challenged by local law and order issues, and recent natural disasters, but overall the portfolio targets have been achievable.

Supervision of field staff is primarily performed by the field unit in-charge (field unit supervisor) who reviews every loan application and visits all COs on a rotating basis. District program officers (district managers) in turn supervise the field unit supervisors in their district. The nine districts have recently been divided into four regions with a regional manager in each reporting to the head office operations manager (RCED head of operations).

The SBI assessment team recommended eliminating this most recent layer of management until the organization is of a greater size. Keeping the organization as flat as possible, (fewest levels of supervision) helps ensure that information from the field can make its way up through all the levels and to the managers who can use it to make decisions. The more layers of management, the less likely all the important information will make it through.

In RCED's organization, most of the direct supervision of the credit operations happens at the district office, so these officers must be strong managers. Adding the regional manager position could be a strategy for adding stronger management skills to supervise the field operations. This works only if the right combination of expertise and skills can be found, so the regional manager position is more than just another layer.

Loans are approved (sanctioned) at the district level, where checks are issued off bank accounts held at the field unit level. Given the current supervision structure and level of responsibilities at the district versus the field unit, sanctioning at the district level seems appropriate. However, with the MIS upgrade it is hoped that issuing of disbursement checks could be automated or moved to the field unit to improve the efficiency of that process.

Large amounts of cash (averaging PKR 500,000 daily) are collected in field units and satellite branches during peak recovery periods. This high volume of cash can lead to theft, robbery, and snatching risks that may also cause injury to staff and losses for RCED. These risks can be mitigated by increasing security around the offices or through a change in the recovery system.

Several agent networks have been setup around Pakistan for performing financial transactions with banks and other financial institutions. SRSO is encouraged to investigate how one of the agent networks could be used to support loan recoveries, thus reducing the number of repayments coming through the RCED offices.

Savings being performed in the COs are not standardized, in terms of bookkeeping and transacting with a bank. In some cases, very poor records are being kept and savings are not being deposited with a bank. Credit staff is not supervising the COs' savings activities, and little is known about them. RCED managers have been discussing the possibility of making savings a mandatory condition for taking a loan, but Pakistan regulations place strong limits on how this might be accomplished.

The SBI-P team recommends that SRSO investigate a partnership with one of the banks to provide savings services, through one of the agent networks. The bank would then become responsible for selling its services to RCED clients. This arrangement would bring important deposit services to RCED clients, without adding to the MF staff's responsibilities for training and monitoring COs.

The assessment team also identified a few operational issues that have been added to the recommendations below:

FIELD OPERATIONS & SUPERVISION RECOMMENDATIONS:

1. Investigate a branchless banking relationship with one of Pakistan's agent networks for collecting loan recoveries, and providing deposit and other bank services to RCED clients;
2. Provide fireproof file cabinets for loan files, financing agreements (stamp papers), and other legal documents now kept in wooden cabinets. Alternatively, loan files could be scanned and moved to an online storage as part of the new MIS;
3. Make operations manuals available in Sindhi at all offices;
4. Make fire extinguishers available in district, town, and unit offices; and
5. Issue field staff identity cards, as evidence to clients that they are authorized to receive cash on behalf of SRSO, and as a deterrent to unauthorized individuals.

MARKET & PRODUCTS

MARKET POSITION

The microfinance market is dominated by a few microfinance banks (MFBs), mostly in urban centers, and a few small NGOs in rural locations. Only SRSO is fully present in nearly all of the UCs of upper Sindh. The main MFB competitors are FMFB, Khushhali, and Tameer. The main MFI competition comes from ASA, a strong Bangladesh organization.

Competitors offer nearly identical loan products, using similar procedures, but in different places. If RCED expands its urban operations they will compete directly with the MFBs, which may be possible initially since RCED loans are priced lower. A market map has not been drawn, but would be very helpful for planning expansion into new products or making pricing changes.

PRODUCTS & METHODOLOGY

RCED dominates the rural market, but has a limited product offering. Currently, three products are offered – crop, livestock, and enterprise – all using the same methodology. This has been an efficient and acceptable practice while loan amounts are small and loan terms short. Borrowers are assessed to verify that they have sufficient monthly cashflow to cover household expenses, so the loan amount is not diverted for consumption. And, the loan amount is small enough that repayment is not likely to be a burden, even if the financed activity fails to yield sufficient income.

The loan methodology compares well to best practice for the current lending scheme. However, it will prove insufficient for larger loans, which are more dependent on the success of the income generating activities; and longer terms which present more opportunity for those activities to fail or cash to be diverted.

After some difficulties offering credit out of existing SRSO COs, RCED began to separate the credit clients into separate credit COs independent of the social service COs. Field workers and junior social organizers (JSOs) are responsible for linking credit clients to services available in the social service COs. Unfortunately this linkage is not being consistently made. During the assessment team's field visits clients complained that now that the credit is separated, they no longer have access to social services.

Also, while SRSO's vocational training program has developed a large portfolio of trainings, there has been little focus on technical skills training, especially for RCED borrowers in agriculture, livestock and poultry. Increasing borrowers' technical skills should lead to better repayment rates and increased capacity to borrow larger amounts in the future.

CIF

Community Investment Funds (CIF) are grant funds given to UCs for a revolving loan fund they make available to community members that do not qualify for RCED loans. The CIF is currently being run by SRSO's Union Council Based Poverty Reduction Program (UCBPRP), not RCED. However, a plan exists to bring the management of the CIF into RCED during this year.

CIF is a community-managed fund from which micro-loans are provided to poor women through groups called village organizations (VOs). The management of the CIF is entirely in the hands of the VO, which decides who will borrow, how much, at what service-charge, and how repayments should be structured. Main conditions attached to the CIF are:

- the fund should be used by poor women (using the PSC);
- for only income-generating activities; and
- the fund should be revolving.

Around 80% of the CIF was used by recipients on the purchase of livestock - especially goats, 13% on establishing small village-level enterprises, and the remaining 7% on agriculture inputs. These mirror RCED's products.

Internationally, experience with community managed revolving loan funds has not been good. This is because the VO's rarely have the skills to properly select borrowers who have the capacity to repay; structure repayments so they are tied to existing cash flows; and follow-up with borrowers to encourage repayments.

In the case of the CIF, repayment discipline is eroded by the availability of income generating grants (IGG) through the same VOs. While the grants are targeted at the poorest group members, it still results in some group members being asked to repay and others not.

Perhaps the most significant problem with the CIF is the premise that women that are not considered credit-worthy enough to borrow from RCED are somehow able to repay a VO loan. An analysis of loan recovery rates was not available to learn more about how the individual CIFs are performing. It would be useful to know if a direct relationship exists between the PSC rating and repayment rates. If so, perhaps RCED should be adjusting the score for which it accepts clients. Where recovery rates are low, a new approach should be considered.

For example, a poverty alleviation scheme could be designed that combines grants with technical skills training and social services. This would be a structured program that steps targeted clients through training and grant process, from which they are expected to graduate to RCED loans after a set period of time. Examples of such schemes have been piloted in Africa.

MARKETS & PRODUCTS RECOMMENDATIONS:

1. Market mapping of each district to identify potential market and competitor products & pricing.
2. When designing for larger loans (i.e. sugar cane) add more analysis of the activity being financed. For example, require a calculation of estimated input costs, crop yields, and sales prices to determine an affordable loan amount and repayment capacity.
3. Repayment on larger loans should be tied to the sale of the crop, but a second source of repayment (ideally monthly) should be encouraged, so the entire loan repayment is not dependent on the one activity.
4. Add requirement to crop loans for monthly repayments when the household has the cashflow.
5. Create a stronger link between credit and social service COs, so all SRSO clients can benefit. This should be done by adding the responsibility to the SRSO social service staff. The RCED field worker can help with the coordination, but the bulk of the work (costs) belongs outside RCED.
6. Analyze the performance of CIF to capture any lessons learned, especially about high versus low recovery rates.
7. Restructure the CIF and IGG components to create a more effective and sustainable poverty alleviation intervention.

MARKETING AND PRODUCT DEVELOPMENT

SRSO is a strong brand in Sindh, which was enhanced by the goodwill created through its work distributing aid following recent floods. The name RCED, however, is not yet established as a brand. It would make sense to establish the MF operations under SRSO's brand, by simply referring to it as SRSO Microfinance or SRSO Credit.

Branding is also important for presenting an image of the organization to outside supporters and potential funders. Funding decisions are influenced by the appearance of an MFI as being professional and focused on good practice, and sustainable operations. Since mixed NGOs, which offer both social services and credit often make commercial funders nervous, it is important that the MF unit of SRSO look like an independent MFI, within its current legal structure.

This professional, MFI image will be enhanced by creating new office designations and job titles that are more consistent with the typical credit MFI. For example, a branch office would normally be larger than a field unit. And, district program officers would be called district managers.

RCED does not have a formal marketing function. Advertising and promotion is done by field staff, advertising materials are developed by HO managers, and the limited market research done is performed by the MER department. Given the size and type of operations, a formal marketing position is not yet required. However, as RCED grows and develops there could be benefit from identifying one or two managers for formal training in the marketing function, so important principles for good advertising and promotion can be utilized.

Product development is a new process at RCED and also not well understood by staff. While it is not appropriate to designate a product development position, RCED would benefit from better understanding the formal process for properly developing new products. Again, designating one or two employees to be trained to lead future product development would be beneficial.

MARKETING & PRODUCT DEVELOPMENT RECOMMENDATIONS:

1. Consider rebranding the MF operations with a name that includes SRSO, but is less complicated than RCED;
2. Standardize office designations and job titles to be more consistent with a credit MFI; and
3. Designate one or two employees to be trained in marketing, advertising, and product development, who can then lead RCED's work in these areas.

HUMAN RESOURCE FUNCTION

Overall the HR department is well staffed, organized, and operated.

PERFORMANCE MANAGEMENT

A good performance management system is in place for field staff and their supervisors, using annual appraisals tied to job descriptions. Management of the performance of middle and senior level managers might be strengthened by adding business goals (from the budget) to their appraisals, including loan portfolio targets, PAR and profitability (OSS and expense controls).

HIRING & RETENTION

The hiring process is reasonably efficient, with appropriate involvement of field supervisors to identify hiring needs, and make local support staff hires. The RCED HR office recruits, interviews, and selects professional and field staff to ensure a standard quality of staff is maintained.

Staff turnover is high – 27% over the last 12 months – of which turnover in field staff was the largest portion. The median staff turnover rate internationally is 17%. It was not clear what is driving the high turnover, other than the normal difficulties retaining people to do the uncomfortable and demanding work of traveling throughout rural Pakistan. However, since the costs of recruiting, training, and replacing staff are not small, it would be useful to further investigate the reasons for staff leaving.

Vacant positions are filled mostly through promotion of existing staff, which are identified by their managers, and based on annual performance appraisals. As RCED grows to a size that makes it more difficult to identify the best candidate for promotion, an internal job posting system should be considered. This gives more power over the employee's career to the individual employee, and helps managers better understand each employee's career goals.

Staffing levels are difficult to maintain at an ideal level, due to the seasonal nature of RCED's agricultural credit activities. The main credit unit at RCED is the field unit, where all of the staff works together as if a single credit officer. For this reason, the most important ratios are clients to FU and COs to FU. Below are statistics about RCED's client to staff ratios:

TABLE 7: FIELD STAFFING

Description	Data
Number of Field Units	52
Number Credit Supervisors & FU in-charge	27
Number Credit Officers	23
Number Credit Assistants	35
Number Field Workers	53
Number COs (groups)	4,155
Number Clients	43,871
Number COs per FU	80
Number Clients per FU	844

RCED management is satisfied with the client ratio the field staff is managing. As expected, field staff did not always agree. In the optimum organization a FU is comprised of a credit officer, credit assistant, and field worker (promoter) working together to do promotion, form the COs, identify potential borrowers, and submit loan applications. Each field unit delivers credit to 844 clients within 80 groups. This ratio might compare well with other MF programs using a similar methodology, but it is difficult to compare given RCED's FU structure.

Given the high turnover rate for field staff and the critical need for full staffing during peak disbursement and recovery periods, RCED managers must focus on hiring and training new recruits between peak volumes. Management is encouraged to create a pool of excess human resources (hired before they are needed) to avoid offices being caught short staffed especially during peak periods.

COMPENSATION SYSTEMS

A salary survey among similar types of organizations has not been done to determine how competitive RCED's salaries are among its competitors for human resources. During interviews, the assessment team received conflicting information from staff and managers about satisfaction with compensation levels, making it difficult to know whether it is a significant factor in staff turnover.

SUCCESSION PLANNING

No formal succession plan exists at RCED. However, managers have done a good job of recognizing which positions among the professional staff are key to safe and efficient operations. For example, only one network administrator function exists at SRSO, which is staffed by an IT professional with highly specialized and unique skills. Due to the critical need for these skills to keep RCED's systems running, and supporting its daily operations, a backup resource must always be in place to replace this individual should he suddenly leave. RCED's operations manager has ensured that such a backup is in training.

While, there is good evidence that succession planning is happening at RCED, it would be wise to formalize the process somewhat, to ensure no serious gaps exist. It would also help managers to regularly focus on their employees' career development and prepare for moving qualified individuals up through the organization.

TRAINING

During the last year RCED hired 120 new employees, who were trained in three batches over the year. The RCED HR manager provides a brief 2 to 3 hour orientation before employees are sent to their new posts. Recruits must then wait to join the next scheduled policy and procedure training, which is conducted by senior MF managers. In the interim they receive informal and unstructured instruction by local staff.

SRSO's training department provides additional training support for management training primarily. External trainers are hired for the provision of skills training, such as communications, leadership, and other professional skills.

With 120 new hires each year, most of which is field staff, RCED is now of a size where a dedicated MF trainer would be appropriate. This would allow more frequent new employee training, relieve MF managers from the burden of preparing and conducting training sessions, and bring more professional training methodology to the process.

A training manager should also be tasked with conducting regular training needs assessments (TNAs) of all of RCED's staff, from which an annual training plan is developed. The training plan should include information gathered during each employee's annual appraisal, about their career goals. It should also respond to RCED's succession plan for key professional and management positions. The training manager would design and conduct all training of new field staff, and coordinate professional training needs with SRSO's training manager.

HR & TRAINING RECOMMENDATIONS:

1. Create an employee handbook that summarizes policies and details important responsibilities of each employee, independent of the HR policies and procedures documents;
2. Include a staff development and succession planning component to the annual appraisal process that can be used for planning by senior management and the training manager;
3. Formalize succession planning into an annual process of identifying important (key) positions in the organization, individuals that could be developed to move into those positions in the future, and a plan for developing their capabilities;
4. Create a training position at RCED that:
 - a. Performs annual or bi-annual TNA;
 - b. Creates annual RCED training plan;
 - c. Prepares and conducts training of new field staff; and
 - d. Supports the HR manager with recommendations on staff development and career planning activities.
5. Research staff turnover with employee exit interviews, anonymous surveys, and staff interviews; and
6. Create a pool of entry-level human resources that are trained and ready to be assigned when employees in their district resign.

IT SYSTEMS AND MIS

RCED's credit operations are migrating from a fairly primitive MIS inherited from NRSP, which was inadequate for supporting the organization. Over the last 18 months new software was selected, customized, and installed, and data migration has been nearly completed.

IT SYSTEMS

The new software is web-based, operating in real-time on Oracle, a strong platform. This new operating environment requires that the MIS sits in a central data center, with field offices connected through stable phone, satellite, or radio communications. Due to the cost of outsourcing the data center to

another company, RCED setup its own. This required purchasing the necessary servers and other equipment; sourcing qualified IT (data center) staff; identifying and installing stable data communications that can reliably support expected transaction volumes; and develop data center facilities and operating procedures robust enough to provide essential security.

Data center staff is well qualified and have achieved the initial setup of the center, but some important questions about the ability of the network to support RCED's operations remain to be tested. The rural nature of RCED's operations makes it difficult to obtain band-width and line speeds that can support the high volume transactions that are expected during loan disbursement and recovery periods. Also, standard data center protocols are planned, but not yet in place, such as a fire retardant system, keypad entry, and an off-site disaster recovery process.

While a centralized online MIS gives RCED a tremendous advantage for bringing efficiencies to its operations and quick access to detailed and consolidated reporting, it also puts the organization at greater risk should the system fail. With the current distributed system, if one office has a failure the others can keep operating. In the new centralized form, a failure at the HO affects everyone.

MIS

The new MIS currently being installed was originally developed for NRSP Bank, but not implemented. It has since been customized for RCED and includes integrated modules for finance, HR and payroll. Plans have been made to add micro-insurance and staff health insurance to the MIS in the fall.

The new MIS includes most of the essential components for RCED's limited product offering, such as:

- Customer records to which loan files can be attached;
- Application processing for tracking processing time and performing online sanctions (approvals);
- Individual loan records associated with their COs (groups);
- Loan recovery processing that supports bullet, monthly, and irregular payments; and
- Online report generation for a comprehensive list of reports.

In a more comprehensive software design structure, product parameter files would be used to make it easier to add new products, make the data entry process more efficient, and add controls to the quality of information being entered. This of course results in much more complex and costly software that would allow:

- RCED to add new products without additional programming support from the software vendor (NRSP);
- Automatic population of product specific information into new loan setups, making it faster and more accurate (i.e. loan limits by cycle, repayment type & frequency per product, loan term);
- Automatic calculations of repayment dates & amounts;
- Verification and limits on transactions being entered based on its product, producing error messages or field limits based on product policies (i.e. limits on loan amounts depending on the

cycle, limit on loan term according to product, or type of repayment, as in monthly payments for enterprise, but not bullet).

Also, a more robust MIS would offer an online report writing feature that would allow RCED staff to create ad hoc reports without a programmer's support. This would give MF staff a faster and more flexible means for investigating portfolio trends or producing special request donor reports.

MIS IMPLEMENTATION

While the IT and MIS staff is highly qualified, especially for the size and complexity of RCED's operations, they are still not experienced running an MIS implementation. Software vendors experienced with installation and data migration can typically manage this process in half the time, but more importantly, understand where to look for and avoid the most critical and costly problems. RCED's team should be commended for the progress they have made, even with the longer timeframe. However, until RCED goes live with the new software, and successfully makes its way through peak processing periods (disbursement & recovery), the potential for serious work disruptions exists.

This is exacerbated by an MIS that has not been in production at any other institution before its installation at RCED. Being the alpha site would normally guarantee a greater number of problems than well-established software already tested in production at numerous MFIs. Potential software problems are compounded with the additional concern about communication line speeds, and inexperienced implementation staff.

Together, these concerns make this software installation very high risk.

IT & MIS Recommendations:

1. Create and test a disaster recovery site;
2. Pilot the new MIS through a peak transaction period at limited sites before going live across all offices;
3. Create a special help desk unit at HO for at least the first few weeks to answer phone calls with questions from the field as they get used to the new procedures;
4. Develop a fallback plan for operating without the new MIS should its installation fail within the first month;
5. Once the new MIS is stable, evaluate opportunities for additional automation (i.e. moving loan documents online);
6. Train current finance, accounting, & loan staff to use the new MIS rather than hiring new data entry (MIS) staff in the field;
7. Train all staff in basic computer skills, and give appropriate access to credit, accounting, & HR staff for making online inquiries on their MIS; and
8. Provide non-MIS field staff with a bi-lingual MIS operations manual.

FINANCIAL MANAGEMENT

The finance department has strong internal controls and procedures. An operating manual documents the institution's finance and accounting policies and procedures. Preparation of financial statements, budgeting and variance management are good. However, the annual budget is not supported by a strategic and business planning process where strategies are identified, business changes documented, and assumptions for financial projections detailed.

A fully developed three to five year strategic and business plan is also an important tool for describing RCED to potential investors in a professional manner. Most commercial funders will expect to see the more comprehensive business plan, and view it as evidence that the organization is professionally run.

The current financial information system (FIS) is only marginally adequate, but is in the process of being replaced with a new integrated FIS. This should bring added efficiency to the operations by reducing the manual work and number of transactions. However, instead of enjoying a reduction in staffing, management plans is to add new positions to the field units to do the accounting data entry. The SBI team recommends not making additions to staff, but rather adding the FIS data entry responsibility to the employees currently making the accounting entries.

Also, not all FUs are connected to a reliable source of electricity and internet, which will prevent them from accessing the new online FIS. This will slow the consolidation of information and reduce the benefits of an online system.

FINANCE & ACCOUNTING RECOMMENDATIONS:

1. Train current finance and accounting staff to use the new MIS rather than hiring new;
2. Purchase damage and loss insurance on more expensive assets, such as the new IT servers, and property insurance for the new offices being constructed in Sukkur;
3. Start revising the finance and accounting policies and procedures in advance of the new FIS' operations;
4. Identify and begin allocating SRSO costs associated with RCED, so the OSS and FSS are more accurate; and
5. Prepare a 3-5 year strategic and business plan, with supporting text.



OPERATIONAL PERFORMANCE

LOAN GROWTH & OUTREACH

TABLE 8: LOAN PORTFOLIO GROWTH

Year-end	Agriculture	% growth	Livestock	% growth	Enterprise	% growth	Total	% growth
2008	6,145,202		32,987,217		2,933,923		42,066,342	
2009	26,638,708	333%	78,353,878	138%	9,575,729	226%	114,568,320	172%
2010	265,448,807	896%	84,861,345	8%	28,298,600	196%	378,608,761	230%
2011	497,051,504	87%	77,719,013	-8%	31,874,220	13%	606,644,738	60%

The loan portfolio has seen very rapid growth over the last several years, with the majority of that growth in agriculture. This verifies MicroWatch's³ market demand analysis which reported that RCED had only tapped 3% of the available market.

PORTFOLIO AT RISK

The following table demonstrates RCED's PAR experience over the last four years:

TABLE 9: PORTFOLIO AT RISK PER PRODUCT

	Agriculture	Livestock	Enterprise	Total
2008	41%	31%	42%	33%
2009	13%	15%	20%	15%
2010	2%	14%	8%	5%
2011	1%	16%	9%	3%
PAR > 30 days	2%	16%	7%	4%

Overall, the portfolio has recovered well from the disastrous flooding of 2009 and 2010, and is now at a more acceptable performance. The livestock product is the primary exception, making management's decision to reduce that portion of the portfolio seem wise. The enterprise product PAR has steadily improved, but remains high. It is recommended that the enterprise loan analysis process be reviewed to identify changes in the methodology and loan structure that might improve its performance.

FINANCIAL & OTHER PERFORMANCE INDICATORS

The following key performance indicators show RCED's performance since being separated from SRSO's financial reports.

³ March 2012 issue



TABLE 10: KEY PERFORMANCE INDICATORS

Year-end (PKR)	2010		2011	
	Unaudited-RCED	Audited-RCED	Unaudited-RCED	Audited-RCED
Gross Portfolio	378,608,752	606,644,737		
PAR > 30 days	16,272,718	23,354,962		
PAR 1 to 29 days	3,392,276	2,196,069		
Profit	(11,071,754)	(20,304,276)		
Equity	144,480,135	144,287,625		
Borrowing	251,330,000	579,806,666		
Interest on Loans	23,639,755	75,596,084		
Interest Expense	(10,999,017)	(35,340,181)		
Operational Expenses	(26,667,352)	(44,600,406)		
Total Liabilities	261,127,469	598,169,119		
Total Assets	405,607,604	742,456,744		
Current Assets	394,983,701	711,907,118		
Current Liabilities	150,907,469	297,336,410		
Impairment loss on loan advance	(9,907,637)	(50,741,950)		
Write Offs	-	15,215,064		
Active groups	3,196	4,155		
Disbursal amount	512,262,800	765,476,951		
Nbr. loans disbursed	37,724	50,560		
Active clients	10,904	43,871		

TABLE 11: PERFORMANCE RATIOS

Year-end:	2009	2010	2011	Pakistan's Industry Benchmarks ⁴	International Industry Benchmarks
	Audited-SRSO	Un-audited-RCED	Audited-RCED		
Ratios					
Growth in gross portfolio	172%	230%	60%	NA	
PAR ≤ 30 days	15%	5%	3%	NA	
PAR > 30 days	2%	16%	7%	4.1%	4.1%
OSS		50%	58%	99.7%	112%
ROA	6.03%	-2.73%	-2.15%	-0.1%	2.4%

⁴ Pakistan's Microfinance Network 2010 report



ROE	9.04%	-7.66%	-9.38%	-0.2%	8.5%
Portfolio Yield	12.8%	11.9%	19.0%	32.9%	
Cost of Funds	NA	8.8%	8.5%	7.4%	
Operating Expense	NA	10.8%	9.1%	25.7%	21%
Portfolio to Assets	NA	93.3%	81.7%	56.7%	
Debt to Equity	NA	1.74	4.02	3.29	
Liquidity Ratio	NA	1.57	1.67	NA	
Write-off Ratio	-	-	30%	NA	
PKR					
Average disbursement	11,927	13,579	15,140	12,949	
Loans per employee	261	397	201	131	130
Loan per credit staff	915	1886	919	304	305
Cost per Client	NA	707	882	3,051	9,900
Op Expense / disbursements	90.7%	5.2%	5.8%	NA	

RCED's operations are highly efficient by any standards. The cost per client is one third the industry average in Pakistan and one tenth the international norm. This is driven primarily by the high number of clients per staff, which is three times the norm.

OSS, ROA, and ROE are trending well toward full sustainability. OSS was reported to have reached 107% as of quarter ending March 2012. However, not all HO SRSO costs are included in this calculation.

The operating expense ratio (operating expenses / average portfolio) is decreasing and is well below the average for MF in Pakistan and internationally. Portfolio to assets shows a high percentage of earning assets and also compares well to Pakistan industry benchmarks.

IMPLEMENTATION ROADMAP

The following summarizes the report's recommendations into the main areas identified by the assessment team for which SRSO and RCED may wish to take action:

Tasks	
Strengthen Governance	<ul style="list-style-type: none"> As BOD member terms expire, replace some with audit & private business experience; Add MF sub-committee; Write missing terms of reference for sub-committees; and Fully allocate SRSO costs associated with RCED, in order to better understand its financial position.



<p>Improve RCED Structure</p>	<ul style="list-style-type: none"> • Eliminate regional manager positions • Add new Head of Field Operations at the head office • Assign supervision of district offices to new Head of Field Operations. • Move monitoring under the new Head of Field Operations. • Move all other HO departments under Manager of Operations. • Eliminate separate urban office structure & combine with rural according to their location. • Standardize field structures by: <ul style="list-style-type: none"> ○ Creating standard job descriptions and titles for the traditional lending; ○ Organizing FUs into small, medium, large, for rural & urban; ○ Reevaluating grade (pay) levels of supervisors and managers of the larger FUs identified above; and ○ Reviewing staffing needs (skills, qualifications, job descriptions) for delivering the new mix of loan products in all districts and more FUs.
<p>Strengthen internal controls & risk management</p>	<ul style="list-style-type: none"> • Form a risk management committee of RCED senior managers and the CEO; • Designate an RCED middle manager to coordinate risk management activities; • Add specialized MF auditors to IA; • Develop an audit rating system, especially for RCED; • Provide fireproof file cabinets in all offices for important files; • Purchase damage and loss insurance on more expensive assets, such as the new IT servers; • Make all operations manuals available in Sindhi at all offices; and • Make fire extinguishers available in district, town, and unit offices.
<p>Create Marketing Expertise</p>	<ul style="list-style-type: none"> • Designate employee(s) to be trained in marketing, advertising, and product development, who can then lead RCED's work in these areas; • Rename the MF operations to capitalize on SRSO brand; • Standardize office designations and job titles, using terminology more commonly used by MFIs; • Map current markets, looking for potential growth areas and identifying competitive positions.
<p>Improve credit performance</p>	<ul style="list-style-type: none"> • Research best practice ag lending methodology and add more crop analysis & cashflow projections to larger loan applications (i.e. sugar cane); • Require monthly repayment on agricultural & livestock loans when



	<p>household cashflow allows;</p> <ul style="list-style-type: none"> • Review methodology for analyzing & structuring enterprise loans to reduce the PAR; • Create a stronger link between credit and social service COs for currently available services; • Investigate providing technical training to ag & livestock borrowers; • Capture lessons learned from performance of CIF to use in its redesign; and • Restructure the CIF and IGG components to be more sustainable.
Strengthen HR management	<ul style="list-style-type: none"> • Formalize succession planning process by: <ul style="list-style-type: none"> ○ creating annual succession plan; ○ including a staff development and succession planning component to employees' annual appraisal; • Create a training position at RCED HO to plan staff development, coordinate training activities, & conduct standard policy & procedure training sessions; • Research staff turnover to resolve the current high rate; • Implement a permanent process for gathering the above information from employees; and • Create an employee handbook that details employees' rights and responsibilities.
IT, MIS, Technology	<ul style="list-style-type: none"> • Investigate a branchless banking relationship with one of Pakistan's agent networks for collecting loan recoveries, and providing deposit and other bank services to RCED clients; • Pilot the new MIS through a peak transaction period at limited sites before going live across all offices; • Staff a special help desk unit at HO during first few weeks going live in all offices; • Evaluate opportunities for additional automation once new MIS is stable (i.e. moving loan documents online) • Train current finance, accounting, & loan staff to use the new MIS rather than hiring new.

SRSO may want to seek outside advice and assistance to implement some of these recommendations, especially where a broader experience with microfinance outside of Pakistan could be of value or special expertise is needed. The areas where an external perspective may be of the most use are:



1. Restructuring field operations to be more efficient and consistent with best practice MF;
2. Creating a more formal risk management function;
3. Strengthening credit analysis and methodology for larger agricultural loans, and enterprise loans;
4. Redesigning CIF & IGG;
5. Setting up a MF training department;
6. Researching & negotiating a branchless banking solution; and
7. Preparing a three-year strategic & business plan.

ANNEX 1: Document List

LIST OF DOCUMENTS REVIEWED

Assessment Area	Documents
Governance & Management	Board Member Profiles
	BOD Executive Committee TOR
	Governance Policy
	RCED Business Plan Projections
HR & Training	Staff Categories
	Appraisal Form
	Post Training Report
	Manpower Request Form
	List of Trainings
	Personal Employee File
Field Operations	Social & Technical Appraisal Form
	Loan Sanction Form
	Household Survey Form
	Terms of Partnership (TOP)
	Case file of Borrower
Audit	Internal audit reports
	Internal audit policy manual
	TOR of internal audit
	Minutes of board audit committee
Supervision	Monitoring reports
	RCED annual program review
	PAR by Unit
	MER annual operational plan
Finance & Accounts	Unit wise income and expenditure
	Ratio analysis
	MER presentation
	Standard operating policies-Finance
Products & Methodology	Enterprise Development Policies
	RCED Financials March 2012
	RCED Credit Manual June 2012
IT & MIS	IT Policy
Other	SRSO Presentation
	Audit Report 2011

ANNEX 2: Interview List

INTERVIEW LIST

<u>Meeting with</u>	<u>Position</u>	<u>Head Office / RCED</u>	<u>Review Component</u>
Dr. Sono Khangharani	CEO	SRSO HO	Gov. & Mgmt; Risk Mgmt
Dr. Ghulam Rasool Samejo	PIU Team Leader	SRSO HO	Other credit programs
Hafeeza Khatoon	Manager Staff Training	SRSO HO	HR & Training
Masood ul Hassan	Company Secretary	SRSO HO	Governance & Management
Muhammed Hamza	Manager Internal Audit	SRSO HO	Internal Audit
Nazia Shah	Monitoring, Evaluation, Research	SRSO HO	Monitoring & Supervision
Ruksana Riaz Ali	Sr. Manager Gender Equality	SRSO HO	Governance & Management
Syed Mansoor	CFO	SRSO HO	Finance & Accounting
Zubair Soomro	Human Resource Manager	SRSO HO	HR & Training
Naveed Hussian	Unit In charge	RCED Naushera Feroz	Field Operations
Aftab Ahmed	Town Manager	RCED Larkana	Field Operations
Maqsood Ahmed	District Program Officer	RCED Larkana	Field Operations
Rustam Ali Somro	Regional Manager	RCED Larkana	Field Operations
Dur Muhammad Chachar	Unit In charge	RCED Ghotki	Field Operations
Arifa Roohi	MER Sr. Officer	RCED	Monitoring & Supervision
Arifa Roohi	MER Sr. Officer	RCED	Marketing & product dev.
Field visits	Larkana office	RCED	Field Operations
Field visits	Ghotki office	RCED	Field Operations
Field visits	Mirpur Mathelo office	RCED	Field Operations
Field visits	Thul office	RCED	Field Operations
Field visits	Sukkur district office	RCED	Field Operations
Field visits	Panjhatti office	RCED	Field Operations
Field visits	Kandiyaro office	RCED	Field Operations
Field visits	Naushera Feroz district office	RCED	Field Operations
Imran & Tarique	Network & Database officers	RCED	IT & MIS
Riaz Memon	MIS Manager	RCED	IT & MIS
Saffar Bhanbhro	Finance & Accounts Sr. Officer	RCED	Finance & Accounting
Shazia Larik	HR Sr. Officer	RCED	HR & Training

ANNEX 2: Interview List

ShaziaZubair	Head of RCED	RCED	Governance & Management
ShaziaZubair	RCED Head	RCED	Marketing & product dev.
Zubair Ahmed Soomro	Operations Manager & IT	RCED	IT & MIS
	CIF		Other credit programs

ANNEX 3: Financial Statements

COMPARATIVE BALANCE SHEETS

Balance Sheet	2009	2010	2011
	Audited-SRSO	Un-audited-RCED	Audited-RCED
ASSETS			
Cash and Bank	882,111,741	39,090,882	171,858,910
Loans and advances to customers	103,810,177	355,892,819	540,048,208
Other assets	102,593,949	2,669,759	17,357,804
Intangible assets	20,469	-	-
Long term investments	234,560,758	-	-
Short term assets	771,312,133	-	-
Property and equipment	129,593,364	7,954,144	13,191,822
Total assets	2,224,002,591	405,607,604	742,456,744
LIABILITIES AND CAPITAL FUND			
Liabilities			
Surplus on revaluation of assets	10,000,000	-	-
Deffered grant	685,791,626	-	6,399,376
Borrowings	244,810,273	110,220,000	294,433,333
Other Liabilities	13,996,007	150,907,469	297,336,410
Employee benefits	17,956,120	-	-
Total Liabilities	972,554,026	261,127,469	598,169,119
Capital fund			
HO A/c	-	197,573,622	217,685,388
Endowment Fund	1,000,000,000	-	-
Retained earnings	251,448,565	(53,093,487)	(73,397,763)
Total capital fund	1,251,448,565	144,480,135	144,287,625
Total liabilities and equity	2,224,002,591	405,607,604	742,456,744

ANNEX 3: Financial Statements

COMPARATIVE PROFIT AND LOSS STATEMENTS

Income Statement	2009	2010	2011
	Audited-SRSO	Un-audited-RCED	Audited-RCED
Interest Income	8,069,317	23,639,755	75,596,084
Interest expense	(6,453,388)	(10,999,017)	(35,340,181)
Net Interest income	1,615,929	12,640,738	40,255,903
Fee and commission income	1,957,844	5,676,445	17,941,905
Grant income	384,328,608	38,221,037	33,280,939
Other Income	43,079,890	8,120,600	4,936,104
Profit on bank deposits	139,675,925	5,533,845	12,971,040
Total operating income	570,658,196	70,192,665	109,385,891
Impairment losses on loans and advances to customers	(302,631)	(9,907,637)	(50,741,950)
Operating income after	570,355,565	60,285,028	58,643,941
Staff Costs	(70,314,468)	(10,392,805)	(30,238,113)
Other operating expenses	(48,533,778)	(16,274,547)	(14,362,293)
Program assistance expenditure	(325,478,516)	(41,788,463)	(30,554,023)
Depreciation	(12,941,992)	(2,900,967)	(3,793,788)
Profit before tax	113,086,811	(11,071,754)	(20,304,276)
Income tax expense	-	-	-
Net profit after tax	113,086,811	(11,071,754)	(20,304,276)
Other comprehensive income	-	-	-
Net Income	113,086,811	(11,071,754)	(20,304,276)