
Al-Ahlia Microfinance Company

Case Study

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Introduction

AlAhlia Microfinance Company Ltd (AMC) provides credit for individuals who own small projects or enterprises. ALAHLA customers are distributed in three main regions in Jordan: Amman (the capital), Irbid and Zarqa. The size of transactions may be small relative to fixed costs. The primary clientele of AMC consists almost by definition those who face several barriers to access credit from conventional financial institutions. These barriers comprise mainly high operational costs and risk factors. These risk factors are pronounced because: small borrowers' income stream can be intrinsically risky and heavily exposed to exogenous shocks (political and economic environment) and the borrowers often cannot provide collaterals because they possess few negotiable assets, whether they are physical or financial.

AMC believes that innovation is the most critical factor to overcome these barriers. It concentrates on professional and qualified borrowers only, quality of credit officer, motivation system, minimum default percentage, productive projects, borrowers' training, and technical assistance. Moreover, it provides the net loan directly to the borrower after discounting interest rate on the loan, commission, official stamps, and administrative expenses. However, many financial institutions around the world use dynamic incentives for repaying loans, where a borrower initially receive small sum, but as a satisfactory repayment history, the borrower may obtain progressively larger loans. The threat is to cut off any further lending when loans are not repaid.

AMC credit policy

First: Target sectors

Industry

Trade

Services

Professions.

Second: Loan Delivery Terms

Established project.

The maximum number of employees is ten.

The borrower's income is associated with monthly repayment installment.

The borrowers' age is 21 to 65.

The borrower has Jordanian nationality.

Third: Loan uses

Delivered loans used to finance working capital, purchasing raw material, supporting operating expenses, and the purchase of equipments.

Fourth: Repayment periods

The period for loan maturity is lasting from 6 months to about 24 months.

Fifth: Interest and Commissions

Loan interest is charged as a monthly flat rate based on the loan amount and repayment period. The range of interest is 1.00%- 1.25% due deducted from the delivered loan. For commissions the range is 1.5 % - 3.00% and is calculated in a similar way of interest.

Sixth: Loans types

1. Outstanding projects loans

The interest is calculated as monthly flat rate (1.25%) and deducted due. The deducted commission is 2%.

2. Home loan

This loan will be offered to the borrower at a monthly fixed interest rate and commission of 1.25% and 2%, respectively. The loan limit is from 700JD to 10.000 JD and the repayment period is lasting from 10 month to 12 months.

3. New projects loans

For this type of loans, AMC applies the same procedures. However, these projects are given a permission period lasting from 4 month to 12 month. For compensations of risk, the borrower will be charged a commission equals %1 multiplied by the number of permission months.

4. Automobile loans

AMC finances purchasing public transportation cars. The loan limit is from 2000JD to 15.000JD. The interest rate charged equals 9% annually. The repayment periods are lasting from 12-48 months with a one month permission period.

Seventh: Lending procedures

1. Contact the customer

- Loan officer visits the customer.
- Loan officer starts collecting information related to the borrower and guarantors to check their credit position.
- Contact the customer to provider AMC the required official documents in order to complete loan request products.

2. Filling the loan application

The borrower fills the loan request form and the credit officer checks the availability of the following documents: registration certificates, ID document, bank accounts for borrower and guarantors for the last six-month.

3. Preparing project's cash flow

AMC follows the cash flow lending policy, which is client-focused. It is based on the client's expected repayment capacity. This capacity is discounted by seminar claims and also by the risk that things many not work as planned. To stay in the business, AMC usually takes a less optimistic view of the borrower's repayment capacity than the borrower takes. This reflects several factors: one is that AMC's perspective gains and losses are different from the borrowers'. If the loan is repaid as promised, the AMC's gains are limited to the fees and interest collected. The borrower's position is different, if the investment funded by the loan works out, where he borrower's income many increase greatly through the leverage provided by the credit. On the other hand, if the cash flow loan goes sour, the AMC may lose the principal amount plus fees and interest that have not been collected. The borrower's situation may be ambiguous or subject to range of outcomes. This asymmetrical distribution of probable gains and losses make the AMC more cautions.

The following example explains the estimation of project cash flow by the AMC.

Client:

Proposed
Loan:

Breakeven Sales:

Loan Officer: _____ **Term:** _____ **Fixed Costs (Average):** _____
Interest: _____ **Percentage:** _____ **Amount:** _____ **JD Contribution Margin:** _____
Commission: _____ **Percentage:** _____ **Amount:** _____ **JD**

Signature: _____ **Date:** _____ **Loan Supervisor Signature:** _____

Item	2002					2003							
	Pre-Loan	9	10	11	12	1	2	3	4	5	6	7	8
Beginning Balance	200	200	337	417	547	887	1277	1717	2207	2747	3177	3657	4187
Cash Inflow													
Sales from Current Products	2400	2400	2400	2400	2400	2400	2400	2400	2400	2400	2400	2400	2400
Sales from New Products		1000	1050	1100	1150	1200	1250	1300	1350	1400	1450	1500	1550
Net Loan		2676											
Other Cash Revenues		0	0	0	0	0	0	0	0	0	0	0	0
Total Revenues	2400	6076	3450	3500	3550	3600	3650	3700	3750	3800	3850	3900	3950
Cash Outflow													
Raw Material	2000	2720	2720	2720	2560	2560	2560	2560	2560	2720	2720	2720	2720
Owner's Salary	250	250	250	250	250	250	250	250	250	250	250	250	250
Employee's Salaries		0	0	0	0	0	0	0	0	0	0	0	0
Rent	100	100	100	100	100	100	100	100	100	100	100	100	100
Utilities	50	50	50	50	50	50	50	50	50	50	50	50	50
Transportation			0	0	0	0	0	0	0	0	0	0	0
Capital expenditure		2560		0	0	0	0	0	0	0	0	0	0
Total Expenses	2400	5689	3120	3120	2960	2960	2960	2960	2960	3120	3120	3120	3120
Net Cash before Loan	200	587	667	797	1137	1527	1967	2457	2997	3427	3907	4437	5017
Loan payments		250	250	250	250	250	250	250	250	250	250	250	250
Ending Balance	200	337	417	547	887	1227	1717	2207	2747	3177	3657	4187	4767
Debt Service Ratio		2	3	3	5	6	8	10	12	14	16	18	20

4. Client's sign and application fees

The client signs the loan request application and pays in cash the application fees.

5. Financial statements

AMC requests the financial statement, of the project for the last three years in order to analyze these statements by the credit officer and to check the borrower creditworthiness.

6. Loan officer's recommendations

After completing all previous procedures, loan officer put his notes and recommendation on the loan application.

7. Reviews and recommendations of loans supervisor

Loan officer sends the clients' application to loans supervisor to analyze the application and to check the safety of the client's situation. In addition, he will visit the client to check the accuracy of information in order to write his report.

8. Branch Manager Recommendations

Branch manager put his opinion clearly based on the documents and information available to him.

9. Credit Department

When credit department in AMC headquarter receives the loan application, it will check the safety of client position, and the relevancy of the loan with AMC policy. Then it will put its recommendations on the application.

10. Credit Committee and Decisions.

AMC has two credit committees

- **First Credit Committee:** examines application loans up to 5000JD.

- **Second Credit Committee:** examines application loans higher than 5000JD.

Each committee studies the application loan and make the appropriate decision. After that it informs the branch manager about different details of that loan in accurate way in order to pay the demanded loan.

11. Times of providing the loan

The loan will be provided to the client over all days during the month after completing all contracts and documents. The maturity date will be determined based on the following table:

Days of Loan Payment	Maturity Date
24,25,26,27,28,29,30,1,2,3,	3
4,5,6,7,8,9,10,11,12,13,	13
14,15,16,17,18,19,20,21,22,23	23

12. Loan Repayment Methods

The client or any of his guarantors are required to pay the monthly installment of the loan on maturity date.

Required Documents

ID document

Recent contract or registration document of the project location

Registration certification at the ministry of industry and trade.

Bank account document for the last three or six months.

AMC Difficulties

Non availability of accurate financial data that can help the AMC to make accurate decisions.

Most customers do not know the financial issues that many help them when they request the loan, especially the estimation of project future cash flow. Therefore, this responsibility will be transferred to the credit officer.

The spread of the micro-projects in different locations around the country.

Non availability of the correct number of women who work in their houses.

Outreach

The outreach of the AMC is to some 1178 active borrowers overwhelmingly men (around 70%). They can borrow through head-office and branches. The main concentration of the AMC is individual lending with an average loan size of 3000JD. AMC does not offer its loans to illiterate, rural or clients below poverty line, because they are looking mainly for profitable customers who face a reasonable level of risk exposure. As result, the percentage of clients who starting the micro enterprise for the first time does not represent more than 0.1% of the AMC clients.

Financial sustainability

Staff productivity

AMC employs 47 persons to provide microfinance loans. Staff productivity is 25 which is low comparing with other microfinance institutions in other developing countries. This is because the AMC works on commercial rather than social welfare and looks for selective clients who can satisfy the borrowing requirements. And as month before, the AMC does not look for illiterate clients or clients below poverty line.

Portfolio Quality

AMC concentrates an efficient, effective, and prudential management of its loan portfolio. This can reconfirm by the full risk coverage, which exceeds 100%, portfolio at risk (PAR) which equals 7.5%, loan loss rate which is less than 1% and the arrears rate of 7.10%.

Financing

AMC depends on two main financing sources: its capital and grants. The major three founders are Jordan National Bank, USAID grants, and AMIR program. It is worth noting that the internal source financing to loan ratio for the AMC equals 89.70%.

Operating performance

The costs of carrying out microfinance business are usually high relative to the value of loans. On one hand, financial transactions often bear significant overhead and fixed costs, independent of the size of transactions. These costs include the administrative costs of making payments, keeping open offices, loan monitoring, etc. Therefore, the AMC considers from the beginning these factors, by achieving sufficient revenue to cover these costs. As result, the operational and financial self-sufficiency in AMC exceeds 124% and 114%, respectively. In addition, the real (effective) interest rate charged on the loans reaches 25% which is sufficient to cover commercial funding ratio, which equals 14.15% only.