

FMO

Finance for Development



BRAC BANGLADESH

Tackling the Barriers I – Through Securitisation and Structured Finance?

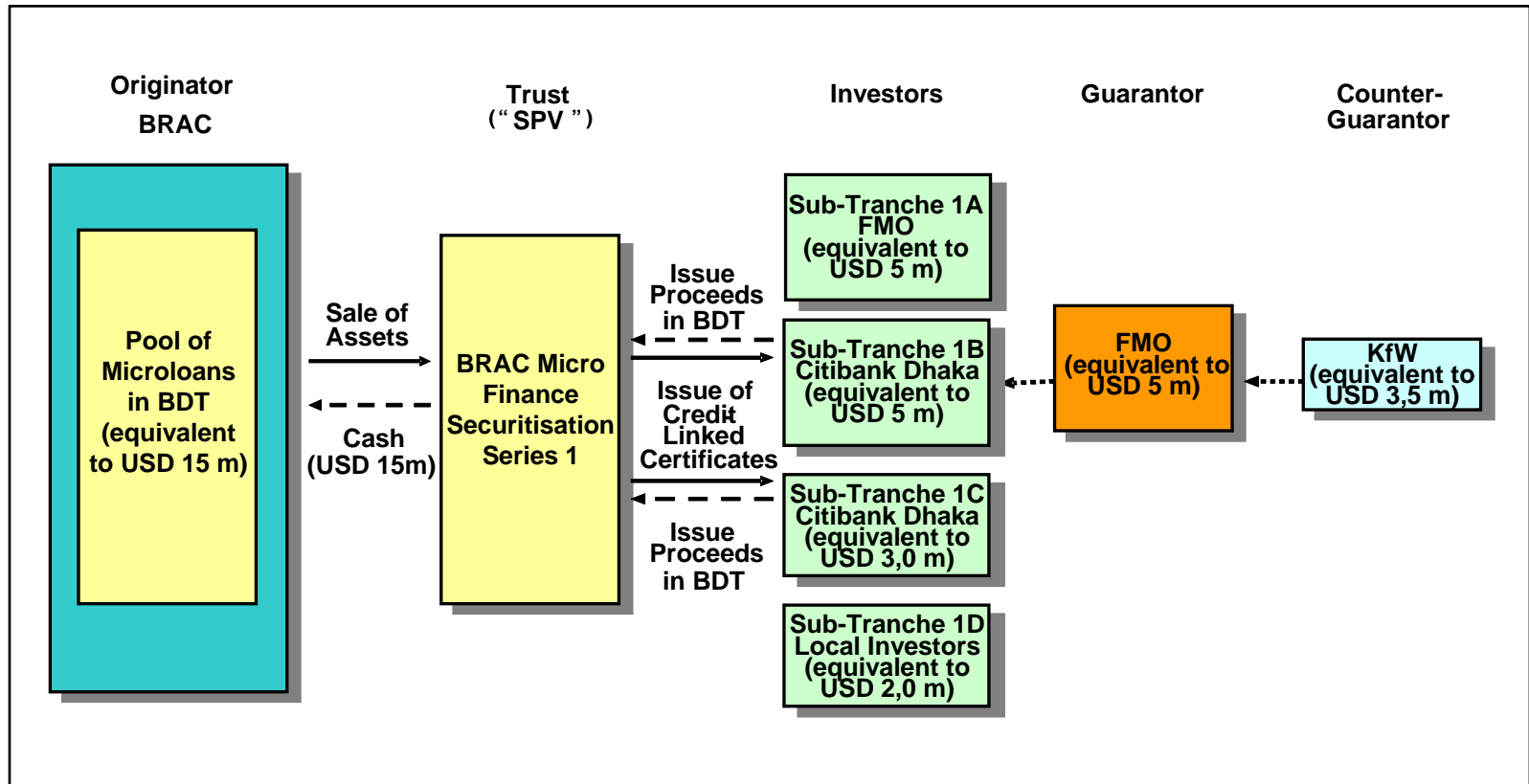
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Deal Characteristics

Asset Class:	Micro Financing, mainly group lending, in Bangladesh
Originator:	BRAC Bangladesh
Volume:	USD 180 Mio. (BDT equivalent), USD 30 mln max exposure at any one time
Issuance:	Volume is divided into 12 tranches issued over 6,5 years
Maturity:	Each bond amortizes over 1 year
Structure:	True Sale, no subordination of investments
Lead Arranger:	RSA Capital
Investors:	FMO, Citibank (Dhaka), Local Investors
(Counter-)Guarantor:	FMO/KfW

Structure



Risks and Mitigants

- BRAC as Servicer:
- BRAC is a profitable and efficiently managed organisation (4 million loans; \$100-1000 each @ 25-30% yield)
 - Equity ratio with 32% = comfortable
 - Good portfolio quality
 - Sound credit technology
- Structure:
- Several credit enhancement measures such as FMO guarantee (with KfW counter-guarantee), 50% overcollateralisation, substitution of delinquent loans and debt service reserve account
 - The transaction was significantly structured by FMO and KfW, which have broad experience with less developed countries and similar financings

Benefits

Short Run Benefits of BRAC

- Lower cost of funds
- More efficient balance sheet
- Increase of ROE and ROA
- Retains competitive advantage

Long Run Benefits for BRAC

- Even lower cost of funds
- Better access to capital markets
- No longer fund constrained
- Spend less time in “fund-raising”
- Increase transparency and professionalism leads to lower risk of error and fraud
- Quantify uncertainties- risk; and then hedge risk if possible

Benefits of Micro Entrepreneurs

- More borrowers have access to start up and growth capital
- New efficiencies can translate to lower borrowing cost
- Pride of Ownership

Benefit of Investors

- Superior return
- Liquidity
- Diversification
- Event risk reduction
- Overcome constraints

Lessons Learned

- Innovation of this kind takes a very long lead time and has high closure risks. In the BRAC case, the local authority approvals process was very difficult. Transactions of this kind can only be undertaken with resolved and dedicated sponsors and financiers.
- The concept of “true sale” needs careful explanation to all parties involved. Local legal systems must provide sufficient basis and comfort that bankruptcy remoteness is achieved.
- The IT systems of the originator must be state-of-the art to support the reporting requirements of a securitisation structure.
- Matching cash flows is complex and requires careful attention.
- The number of parties involved in the transaction and their diversity of locations (Bangladesh, Germany, Hong Kong, New York, the Netherlands) complicates matters. Prior experience in securitisation structures by the key persons is a must.
- Conclusion: securitisation is an interesting option if the MFI has a high volume, has a top IT system in place and is operating in the right legal framework. Long lead times are nevertheless to be expected.