

UNRWA MD WEST BANK and GAZA – occupied Palestinian territories

Comprehensive Social Rating

^sBBB-

The UNRWA Microcredit Department in the occupied Palestinian territories (MD-oPt) commenced credit operations in 1991, aimed at supporting small income-generating activities through SME loans. From 1994, the MD-oPt changed its focus to microfinance lending in the formal and informal sectors through group and individual credit products. The MD-oPt targets a broad clientele, with a focus on Palestinian refugees.

The MD-oPt operates in the major urban centers in the West Bank and Gaza, achieving a wide geographic outreach among the target population, although outreach to rural areas is still limited. Financed activities mainly include consumption, trade, production and services. Housing loans and training are available to clients in Gaza only. The MD-oPt is the largest microfinance provider within the oPt and plans to further extend its outreach and services through the introduction of pilot savings products in 2009.

Organization	Sep-08
Active borrowers	8,777
Gross outstanding portfolio	10,246,894
Branches	10
Total staff	165

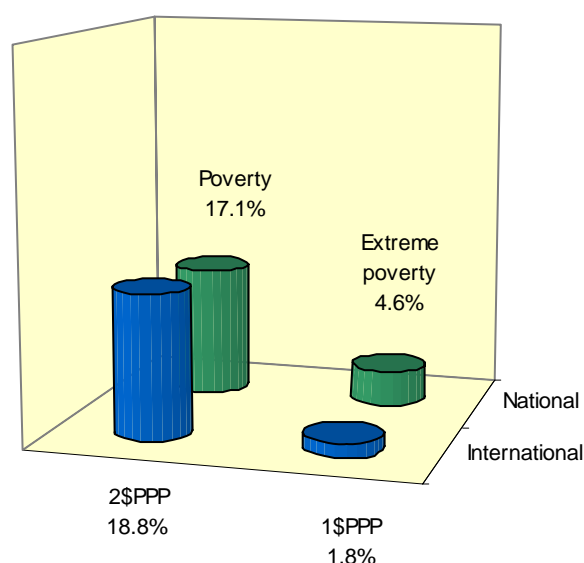


Legal Form	Autonomous department of UNRWA, a UN relief agency
Year of inception	1991
Area of intervention	Urban, semi-urban
Credit methodology	Individual, solidarity group
Financial service	Credit
Non-financial service	BDS activities (Gaza only)

Social indicators	Sep-08
Female staff	32%
Staff turn-over ratio	16%
Real portfolio yield	18%
Financial awareness of clients: Interest rate	60%
Individual methodology, clients	94%
Female clients	17%
Refugee clients	48%
Clients without completed primary education	1%
Financed business in informal sector	70%
Employed in financed activity	2.88
Households owning dwelling	76%
Clients without improved water source	12%
Clients without improved sanitation	46%
Clients without previous access to credit	62%
Average disbursed loan amount, US\$	1,524
Median annualized loan disbursed (\$PPP)	2,563
Client drop-out ratio	32%
PAR30	6%

See annex 2 for more details.

Clients below poverty lines, survey on clients



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AREA	Main results of the social rating
<p>Social performance management system</p>	<p>↑</p> <p>Clear commitment of the governance and top management to the social mission of the UNRWA-Microcredit Department in the oPt (MD-oPt), reflecting the general UNRWA mandate and including the continuity of operations during crisis.</p>
	<p>Strategic vision to transform the MD-oPt into an independent entity, separated from UNRWA, to ensure the long-term sustainability of operations.</p>
	<p>The Medium Term Plan (2005-2009) identifies SMART social objectives even if they are not yet translated into a complete set of targets.</p>
	<p>A specific unit dedicated to the social performance management will be created soon; a workbook organizing objectives and information needs according to the social goals of the mission is in place.</p>
	<p>Social focus prevailing in the strategy for product design and expansion.</p>
	<p>Adequate monitoring of the social performance based on relevant client level data available in the MIS and on external studies investigating the client satisfaction and the achieved impact.</p>
	<p>Adequate alignment of the product design to the target clientele.</p>
	<p>↓</p> <p>The extensive mission statement, including various target groups, partly hinders the clarity of the social goals and the ability of the staff to prioritize the target clientele, resulting in a non-uniform identification of the target group by the personnel.</p>
	<p>An Advisory Board for the department is in place; nevertheless, the Board's limited involvement and decision-making power still restrict the overall effectiveness of the governance.</p>
	<p>Certain risk of mission-drift is involved in the process of management turn-over and entry of new shareholders involved in the medium/long-term institutional transformation.</p>
<p>Social responsibility</p>	<p>↑</p> <p>The labor climate and the participation of staff in decision-making is overall adequate, even if no formal monitoring tools are in place.</p>
	<p>Good and increasing training opportunities for the staff, including external as well as internal activities, coordinated by a specialized officer. However, a formal link between the staff appraisal and training opportunities is lacking.</p>
	<p>Improvable gender balance among MD-oPt staff.</p>
	<p>The level of remuneration does not always meet the staff expectations, especially at management level. No incentive scheme is currently in place.</p>
	<p>The specific measures in place to address gender issues have been limited to date. However, the management is committed to reinforce the overall strategic approach to the topic.</p>
	<p>↓</p> <p>Room for improvement in the measures to mitigate the clients' over-indebtedness risk related to the lack of a credit bureau, some shortcomings in the financial analysis of the repayment capacity. However, the MD-oPt is committed to joint the credit bureau that should be operating in 2009.</p>
	<p>The scarce promotional activities (e.g. written material), the flat interest rate and the absence of a detailed repayment schedule may limit the overall clarity of the conditions and costs of products. No formal mechanisms to address clients' complaints are currently in place</p>
	<p>No specific activities are carried out to benefit the community and the environment, also due to the specific role played by other UNRWA departments.</p>

Some of the outreach results refer to recent clients (see annex 1). ↑ positive elements of analysis ↓ negative elements of analysis

AREA	Main results of the social rating
<p style="text-align: center;">DESCRIPTION</p> <p><i>Outreach</i></p>	Geographical outreach quite deep, in line with the national benchmark: 26% of clients in the Gaza strip, 55% of the clients in governorates with higher poverty than the national average.
	Quite deep outreach in absolute terms, substantially in line with the national average in terms of social profile (e.g. refugee status), monetary poverty and access to basic services.
	Demographic profile: on average clients are 38.43 years old, 80.7% are married, live in households of 6.68 members, with high dependency ratio (1.44 income earning and 5.41 dependents).
	17% of clients are female and 27% of households are female headed. Limited bargaining power in household: 45% of female clients exert a full control over the loan use and 48% a partial control.
	48% of clients are refugee (higher than average for Palestine 41%), and 18% are living in refugee camps. Refugee clients are concentrated in Gaza (85% of the total)
	Good education: 64.6% and 27.6% of clients have secondary or university degree; 7% have completed elementary cycle and 0.84% have not. 94% - 86% of children go to school.
	70% of enterprises are informal, 55% are in place for more than three years, 60% of clients own the business place. The median business capital is US\$ 4,987 and monthly clients' income is US\$ 793.
	Main sectors financed: consumption (34% of clients), service (26%) and trade (23%). Main loan use: fixed / working capital (15% and 31% of recent clients), repayment of debts (27%), housing (18%).
	Quite good effect on supporting jobs: on average, 2.88 persons work in businesses -1.25 family members and 1.66 non-family members. 2.4 are regular and 0.4 are sporadic workers.
	Considerable economic poverty, in line with national average: 17.1% and 4.6% of recent clients are poor and very poor (national), 18.8% and 1.8% of them live on less than PPP\$2/day and PPP\$1/day.
	46% of the recent clients report shortage of income, insufficient to cover medical and food expenses (33% - 37%). Coping strategy: borrow from financial institutions (46%), reduce expenditures (44%).
	76% of clients own the housing unit they dwell in (national average 82%) and 29% own land.
	Access to basic services quite limited and in line with the national benchmark: 12% and 46% of the clients do not have improved water sources and improved sanitation.
	Significant financial inclusion effect: 62% of the recent clients without previous access to formal credit, 24% and 67% without a current/saving account and credit/debit card. High heterogeneity of the client base indicated by the presence of 27% of the clients with previous access to banks.
	<p style="text-align: center;">↑</p> <p><i>Quality of the services</i></p> <p style="text-align: center;">↓</p>
Quite broad outreach, with 8,777 active clients and US\$ 10,246,894 outstanding portfolio. MD-oPt is the largest MFI operating in Palestine, even if its outreach is lower than the MENA benchmark.	
After some years of unstable trend, the growth rates present positive values in the period Oct07–Sept08: 20% increases in the no of borrowers and 45% in the outstanding portfolio.	
Considering the various characterizations of the target in the mission, the outreach is in line with the stated objectives, even if there is some room for improvement in reaching women.	
Product diversification plan including saving services as well as the introduction of a specific product for women and the replication of the housing product in the West Bank.	
The system of service delivery is good. Clients attach a large value to the ease of procedures, including collateral requirements, and perceive the time to receive a loan as adequate.	
The customer service provided by the field staff is overall adequate.	
The overall variety of credit products is intermediate (including business, consumption and housing); however not all of the products are available in all areas yet.	
Some rigidities in the loan products related to the lack of grace periods, parallel loans and formal rescheduling policy.	
The interest rate is perceived as high by the clients. It is above than that charged by banks and it is not differentiated by cycle, loan amount or clients' repayment performance.	
Loan access for women clients in Gaza is restricted to group lending methodology for the first cycles and to the individual methodology starting from the fourth cycle.	
The client drop-out ratio is rather high, equal to 34% in the period Oct07-Sept08. The corresponding reasons are not systematically tracked.	

Some of the outreach results refer to recent clients (see annex 1). ↑ positive elements of analysis ↓ negative elements of analysis

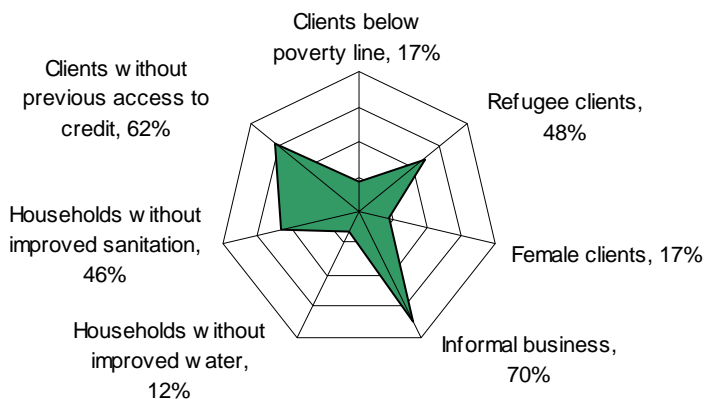
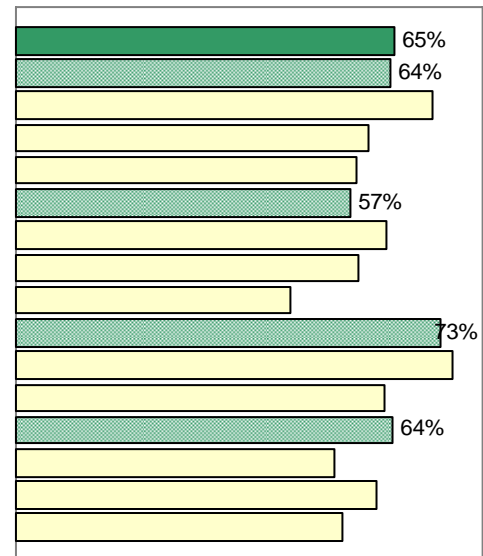
Final opinion

MD-oPt demonstrates a strong commitment to the social mission in the extremely complex context of the oPt. A stronger governance will be crucial to preserve the original mission as MD-oPt enters a delicate phase of top management turn-over and the possible institutional transformation. Even if there is some room for improvement in the identification of priorities in the mission statement, an overall adequate strategy to achieve the social goals is formalized, and will be supported by a dedicated unit for social performance management. The system in place to monitor the achievement of the mission is adequate overall, even if the strong information potential is not fully exploited for decision making. The alignment of human resource systems to the mission presents room for improvement in terms of hiring, staff performance assessment and incentive system (not available).

The labor climate is good overall, also thanks to the participatory approach adopted and the increasing number of training opportunities provided. The gender-related performance, both towards staff and clients, presents room for improvement and the management is committed to implement specific strategies to address the issue. The market presence of several providers of financial services coupled with the inherent vulnerability of the clients' businesses due to the external context brings about a considerable risk of client over-indebtedness, which could be better mitigated in certain cases. As far as the social responsibility towards the community and the environment are concerned, no specific policies or activities are yet in place. With a good coverage of the oPt and a large scale of operations compared to the national benchmark, the MD-oPt breadth of outreach is adequate. Given the broad mission statement and the quite deep results achieved, the depth of outreach can be considered well aligned to the intents of the mission, even if room for improvement is observed in the gender outreach.

The currently variety of services offered is currently limited, yet it is likely to be enhanced in the future. The quality of the services is adequate overall, especially thanks to the delivery system, the ease of procedures and the customer service. Some room for improvement is related to the limited flexibility in the repayment schedule and in the differentiation of the cost charged to clients with different risk profiles.

Social performance	Adequate
Social Performance Management system	Adequate
Mission and strategy	Good
Tracking and monitoring systems	Adequate
Systems consistency to the mission	Adequate
Social Responsibility	Adequate
Social responsibility towards personnel	Adequate
Social responsibility towards clients	Adequate
Social responsibility towards community and environment	Improvable
Outreach	Good
Alignment of outreach depth to the mission	Good
Breadth of outreach	Adequate
Quality of the services	Adequate
Variety of services	Adequate
Appropriateness to clients' needs	Adequate
Non financial services	Adequate



Outreach	Depth	Breadth
IMF	Poverty index 17%	No. clients 8,777
Benchmark*	18%	13,796
	medium-high	medium-small

*Depth: national poverty index. Breadth: median no borrowers of MFIs in MENA (MIX 2006)

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1. Institutional presentation

Institutional profile

The UNRWA Microfinance Department¹ in the occupied Palestinian territories (MD-oPt) is **an autonomous department of UNRWA that commenced credit operations in 1991** as a response to the first Intifada. The Department initially aimed to serve formal small and medium enterprises. However, a limited market for SME lending spurred the MD-oPt to change its vision in 1994 to focus on microfinance intermediation through both group and individual lending.

As of September 2008, the MD-oPt presents a **loan portfolio worth over US\$ 10.2 million** with **8,777 active borrowers** served through a network of 10 branches covering the major cities in the West Bank and Gaza Strip (WBGs) and managed through the headquarters in Jerusalem.

Throughout its history, the MD-oPt has realized **volatile growth due to the ongoing political and economic setbacks** linked to the Israeli occupation². Most recently, the 2006 election of Hamas and the ensuing blockades have negatively affected

UNRWA-MD oPt	Dec-05	Dec-06	Dec-07	Sep-08
Gross outstanding portfolio US\$	7,543,883	5,534,740	7,335,674	10,246,894
Growth in outstanding portfolio	28%	-27%	33%	45%
Active borrowers	11,965	8,239	7,105	8,777
Growth in active borrowers	20%	-31%	-14%	20%
Branches	8	9	9	10
Total staff	185	173	165	165

operations through early 2007. By late 2007 and into 2008, the WB has experienced increased stability, although the crisis remains ongoing in Gaza where Hamas retains control and access is extremely limited. Throughout the Intifada periods, and in spite of the political and economic unrest, the MD-oPt has maintained operations (with existing clients) in select sectors, with the exception of areas under curfew. Risk mitigation measures adopted during the Intifada periods include limiting loan size, lowering minimum loan size and restricting disbursement to select sectors and existing clients. Disbursements in Gaza are currently available to both existing and new clients, even if a more conservative collateral policy is applied (see Chapter 6).

The MD-oPt offers a variety of **credit products** utilizing both the group (Solidarity Group Loan –SGL-, Gaza) and individual Small Scale Enterprise (SSE) loan, Microenterprise Credit (MEC) and MEC+ methodologies. A Consumer Lending Product (CLP) was launched in 2002 and in 2006 a Housing Loan Product (HLP) was introduced in Gaza. The HLP will roll out in the West Bank in late 2008. **Limited non-financial services are offered to clients in Gaza only** through a self-sufficient training programme. **Savings** mobilization is also foreseen and will be piloted in 2009.

¹United Nations Relief Works Agency for the Palestinian Refugees in the Near East.

²Following the outbreak of the 2nd intifada in 2000, the MD-oPt programme outreach was severely affected: in 2002, outreach fell to a five-year low, with fewer than 7,500 loan disbursements worth barely over US\$ 5 million.

Financial performance

The operational and financial performance of the MD-oPt is influenced by the unstable political and economic situation and characterized by:

- Portfolio quality improvement since the 2006 crisis, although the recent low PAR in Gaza is primarily due to a large portion of the portfolio concentrated in the fully collateralized HLP.
- Operational sustainability achieved in the WB, though not yet in Gaza.
- Negative profitability and lower than average productivity compared to MENA regional MBB benchmark.
- Cash management includes a large amount of liquidity (42% for WBGS as of Sept08) kept in monthly term deposits (2.5% interest) also due to the slowdown in Gaza disbursements since 2006.
- The repayment rate is in some cases affected by UNRWA's reputation as a humanitarian relief agency, even if MD-oPt branches are located in separate locations than UNRWA relief activities.
- Management time spent on UNRWA general and administrative activities somewhat hinders efficiency and productivity, yet the benefits of operating under the UNRWA umbrella in terms of ease of movement, donors' network and institutional reputation is not to be under-estimated.

Financial performance	Dec-05	Dec-06	Dec-07	Sep-08
PAR 30	22.8%	39.5%	7.1%	5.5%
PAR 30 West Bank	21%	29.7%	7.6%	6.8%
PAR 30 Gaza	27%	47.3%	3.5%	3.2%
Write-off ratio	10.2%	16.0%	19.9%	2.5%
Restructured loans	0%	0%	0%	0%
ROE^a	-4.5%	-14.9%	-0.48%	n.a.
ROA^a	-3.7%	-11.8%	-0.38%	n.a.
Oper. Self-sufficiency (OSS)	81%	77%	101%	123%
OSS West Bank	72%	82%	120%	143%
OSS Gaza	86%	38%	85%	96%
Staff productivity (borrow.)	65	48	43	53
L0 productivity (borrow.)	110	99	88	115
Operating expense ratio	48.0%	55.0%	40%	32%
Portfolio yield	28.4%	26.3%	23.9%	30.3%
Risk coverage ratio	55%	54%	75%	65%

Source: MD oPt internal calculations based on audited ('05,'06) and internal ('07,'08); income from training program is not included. ^aIncludes Jordan and Syria. n.a. not available.

2. Context

Socio-economic context

With a human development index worth 0.731, the occupied Palestinian territories are classified among the medium human development countries. In terms of growth in per capita Gross Domestic Product (GDP), the oPt economy has continued to be the worst performing in the Middle East and North Africa sub-region (MENA). Nevertheless, the oPt shows a stronger position than the Arab States within the life expectancy and education indexes of the HDI.

The macroeconomic performance of the oPt is rather poor and continues to suffer from the military and administrative measures imposed by the Israeli occupation, particularly since the outbreak of the Al-Aqsa Intifada in 2000. Restrictions on the movement of people and commercial goods, coupled with the closure of the Israeli labour market to Palestinians and the repeated destruction of physical assets during regular military incursions are key elements in the economic downturn in the territories. Indeed, during the period 1999-2007, and reflecting the devastating economic effects of the intifada, the GDP per capita in the oPt declined by about one third.

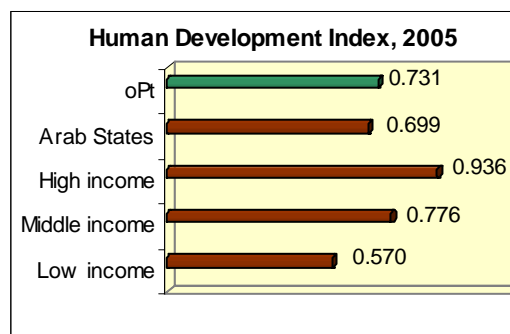
The Government of Israel and donor boycott of the Hamas government following the Palestinian elections of 2006 further aggravated the protracted economic decline as the Palestinian Authority (PA) was unable to meet most obligations or deliver services. The creation of the Fayyad-led caretaker government in Ramallah led to a lifting of the embargo for the West Bank in June 2007. Meanwhile, continued control by Hamas of the Gaza Strip has led to diverse political realities and economic performance of the separate territories in recent periods. In the West Bank, the flow of international assistance recommenced and the fiscal situation of the PA gradually improved. On the other hand, the situation in Gaza has intensified as the Government of Israel has brought the closure to unprecedented levels. Thus, the Gaza economy, highly dependent on outside inputs and markets, currently suffers from extensive and possibly irreversible damage to the productive capacity in all sectors (construction, furniture, clothing, agriculture, fishing, etc.).

Population under poverty line	West Bank	Gaza	oPt
National poverty line	19%	52%	30%
National extreme poverty line	10%	35%	18%
\$2 a day (PPP)¹	16%	29%	21%
\$1 a day (PPP)¹	2%	4%	3%
USAID extreme poverty line²	7%	13%	9%

2007 PECS conducted by the Palestinian Central Bureau of Statistics (PCBS);

¹2005. ²Median expenditure of households below the national line

living **under the national poverty line**, while **18%** is **below the national extreme poverty line**³. By international standards, **21%** of the population are **poor** (less than 2\$PPP/day) and **3%** are **very poor** (1\$PPP/day), respectively. The poverty incidence is significantly higher in Gaza than in the West Bank, with a diverging trend: as the poverty headcount rate fell in the West Bank from 24 percent in 2006 to 19.1% in 2007, the rate increased in Gaza from 47.9% to 51.8%, respectively. The PECS data also indicates that the external assistance reduced overall official household poverty from 34.1% to 30.3% of all households in the oPt.



Human development	oPt	Arab States ^a
Population (millions)	3.9	313.4
Urban population (%)	72%	55%
GNI per capita (US\$)	1,374	2,794
HDI	0.731	0.699
life expectancy index	0.799	0.708
education index	0.891	0.687
GDP index	0.505	0.702

Sources: Human Development Report 2007 and GNI data referring to the Middle East & N Africa.

Based on the Palestinian Expenditure and Consumption Survey (PECS) for 2007, about **30%** of the population is

living under the national poverty line, while 18% is below the national extreme poverty line³. By international standards, 21% of the population are poor (less than 2\$PPP/day) and 3% are very poor (1\$PPP/day), respectively. The poverty incidence is significantly higher in Gaza than in the West Bank, with a diverging trend: as the poverty headcount rate fell in the West Bank from 24 percent in 2006 to 19.1% in 2007, the rate increased in Gaza from 47.9% to 51.8%, respectively. The PECS data also indicates that the external assistance reduced overall official household poverty from 34.1% to 30.3% of all households in the oPt.

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³In 2007, the national poverty line and the extreme national poverty line (subsistence) used by the Palestinian Central Bureau of Statistics (PCBS) are equal to New Israeli Shekel (NIS) 2,362 (US\$ 572) and NIS 1,886 (US\$ 457), respectively. The poverty incidence refers to the level of household consumption.

In general, poverty more severely affects the **refugee** population (about 41% of the population in 2007) than the non-refugees. In particular, the poverty incidence of the population living in refugee camps (15% of the households in 2006 PECS) was found to be about 6 percentage points above the average poverty in Palestine⁴. On the other hand, the **rural** population, which accounts for only 28% of the total, does not show significant differences in terms of poverty incidence compared to the urban population⁵. According to the 2007 PECS, the average monthly per capita expenditure ranged from US\$ 144 in urban areas, to US\$ 132 in rural localities, though it dropped to US\$ 97 in the refugee camps.

The **Gini index is high**, equal to 0.64 for the income distribution in 2006, reflecting the large inequality in the distribution of wealth among the population.

The **unemployment rate**⁶ in the oPt for the second half of 2007 remained amongst the highest in the world at 28.9% –around double the MENA average. Divided by area, the broad unemployment rate in the West Bank was about 25.5 percent, compared to 36.4 percent in Gaza (45.3% if adjusted for the unpaid absentee workers). Overall, the unemployment rate is higher for the refugee population (32.3%) than for the non-refugee population (27.03%). The already high degree of informality in the oPt labour market has been increasing since 2000, resulting in a lower share of wage labour positions alongside a higher share of self-employed persons and unpaid family members, as well as a decline in the number of employers.

The oPt progress towards achieving the Millennium Development Goals surpasses that of the Arab States. Nevertheless, the territories achievement of the poverty and environmental goals within the target timeframe seems unlikely.

MILLENNIUM DEVELOPMENT GOALS		Arab States ^a	oPt	2015 target oPt
1: Eradicate extreme poverty and hunger	% of Population Below \$1 (PPP) per Day*	na	3%	Unlikely
	% of Poorest Quintile in National Income or Consumption	na	7%	
	% of Underweight Children Under Five Years of Age	na	2%	
2: Achieve universal primary education	Net Enrolment Ratio in Primary Education	83%	92%	Highly likely
	% of Pupils Starting Grade 1 who Reach Grade 5	na	99%	
	Literacy Rate of 15-24 year-olds	75%	99%	
3: Promote gender equality	Ratio of Literate Women to Men 15-24 years old	80%	99%	Likely
	% of Seats Held by Women in National Parliaments	na	6%	
4: Reduce child mortality	Under-Five Mortality Rate	58	22	Likely
	% of 1 year-old Children Immunised Against Measles	86	95	
7: Ensure environmental sustainability	Forested land as % of land area	7%	2%	Unlikely
	% of the Population with Sustainable Access to and Improved Water Source (i.e. public water networks)	na	98%	
	% Population with Improved Sanitation (i. E. public sewage network)	71%	52%	

MDG, OPT, 2005 Progress report. Data refer to the most recent year available during 2000-2005. *2005 PECS, household expenditures

Microfinance sector

The microfinance sector in the occupied Palestinian territories is one of the most long-established in the MENA region. The advancement and **growth of the sector has been notably hindered since the advent of the second Intifada in 2000** and the economic recession and political turmoil that followed, however.

According to a market survey conducted by the Palestinian Network for Small and Microfinance (“Sharakeh”)⁷ in 2006, **potential microfinance clientele in the territory is equal to 190,000 borrowers** of which only 10 – 15% were being reached at the time of the study. Potential demand for small deposit savings services was even higher, with over 300,000 potential clients in the WBGS. As of early 2008, the Network estimated that around 30,000 clients were being served in the oPt microfinance market with a combined outstanding portfolio of US\$20 million.

⁴PECS 2004: household consumption poverty for Palestine and for refugee camps is worth 25.5% and 31.6%, respectively.

⁵PECS 2004: household consumption poverty for urban and for rural population is worth 24.4% and 24.6% respectively.

⁶PCBS, includes discouraged workers.

⁷Sharakeh was registered as a local NGO in 2004, with headquarters in Ramallah and currently 10 MFI members.

The **supply of financial services** in the oPt is currently provided by a range of actors including commercial banks (21 operating in the WB alone) and microfinance institutions (MFIs) of various legal status (UN, NGOs, limited companies, cooperatives), of which ten are registered member of the Network. Before 2006, the majority (around 60%) of microfinance clients was concentrated in the Gaza Strip; however, following the election of Hamas in 2006 and the political and economic crisis of mid-year, the trend inverted, resulting in the current prevalence of microfinance operations in the West Bank. Overall, the industry has a **wide outreach on the national territory** through large branch networks in the WBGS. The **variety of services** offered industry-wide remains limited and is primarily focused on credit products. This is also due in part to government regulation which currently prohibits the provision of savings or insurance services by MFIs, which to date remain unregulated.

The major microfinance providers seem to target similar **market niches concentrated in urban areas** where the demand is larger and restrictions on movement have less of an impact on service delivery. Resultantly, **competition is growing**, particularly in the urban centers, and **client over-indebtedness** is becoming increasingly common. Nevertheless, the **MD-oPt retains a strong presence on the market** as the historically dominant actor (serving over 40% of total active clients according to the 2006 Network study).

There is currently **no credit bureau**; although some informal information sharing is undertaken among loan officers and the Palestinian Monetary Authority is considering the implementation of a credit bureau in 2009 (the MD-oPt has already committed itself to report to the credit bureau, should it be established).

Palestinian MFIs are members of the **local Sharakeh network** and the **regional Sanabel network**. Both networks contribute to research on the market and offer training to MFI staff as well as perform advocacy roles at the industry and policy levels.

The **regulatory and supervisory environment** for microfinance in the oPt **has been limited** to date, also due to the gaps and contradictions in legislation between the West Bank and Gaza. The majority of MFIs which function as Non Governmental Organizations (NGOs) currently operate outside of the regulated financial system. Nevertheless, the Palestinian Monetary Authority (PMA) as well as the Capital Markets Authority (CMA) is seeking to better integrate microfinance operations into the regulatory structure. The PMA has drafted a microfinance law with the support of the European Union, while the CMA has drafted a set of MFI licensing guidelines. According to the CMA guidelines, every MFI must be registered as a private shareholding company and must obtain a license in order to continue microfinance operations, thus potentially signaling an upcoming transition for the sector. Given the separate draft legislation being prepared by both the PMA and CMA, the final jurisdiction of MFIs is not yet clear, even if its longer history and greater political power suggests the PMA will remain in control.

MFIs are subject to a **governmentally mandated interest rate ceiling** which indicates a maximum of 9% annual interest rate applicable; however, financial institutions are allowed to charge fees which bring the effective interest rate above this threshold. The MD-oPt is aligned with the practice of the other financial institutions and charges a 9% annual interest rate plus other fees which result in the monthly cost included in the loan contract (e.g. 2%). The current **legal system for realizing collateral in case of delinquency is weak**, as the policing and court enforcement of contract law is highly dysfunctional and barely operational, particularly in Gaza.

Neither the current regulatory framework nor the Microfinance Law drafted by the PMA currently **foresees the collection of savings by non-banking MFIs**. However, once MFIs in the sector realize a more consolidated financial performance, the mobilization of client savings may be allowed to a certain degree by the PMA. The MD-oPt is currently attempting to negotiate a Memorandum of Understanding with the PMA whereby an exception would be made to the existing legal framework and the Department would be allowed to begin pilot savings products in 2009, although not allowed to intermediate such savings.

3. Social performance management system

Mission, social objectives and strategy

MISSION STATEMENT:

“The Microfinance Department endeavours to improve the quality of life small business owners, microentrepreneurs and poor households through the provision of credit and other financial services that sustain jobs, decrease unemployment, reduce poverty, economically empower women and youth and provide income-generating and asset-building opportunities to Palestine refugees and other proximate poor and marginal groups. The department will also provide safe-saving services to poor clients to help them save for the future and provide a financial safety net to help them cope with personal and family emergencies and crises. The department strives to provide scalable interventions with measurable macroeconomic impact by concentrating its financial services in poorer urban areas where there is a high density of Palestine refugees.”

VISION:

“The Department is committed to realizing the United Nations vision of building inclusive financial services for the poor through expanding its credit services and introducing savings and deposit instruments for the poor. By developing financial services that serve the poor, the department will advance beyond its present position as the foremost microfinance institution in the occupied Palestinian territories (oPt) to that of a leading institution in the region, where it will be one of the first to pioneer voluntary savings to poor clients.”

SOCIAL VALUES (UN):

- Independence
- Loyalty
- Impartiality
- Integrity
- Honesty
- Accountability
- Respect for diversity
- Prevention of conflict of interest
- Non-acceptance of gifts

Mission, ownership and governance

The current mission statement is the result of an update undertaken in 2006 when the MD-oPt extended its product offer from solely enterprise credit to also include consumer and housing products. The statement includes reference to the social goals (SG) and reflects the Departments’ historic focus on Palestinians. This focus is reiterated by the governance and top management identification of the priority target as the **Palestinian population** and **Palestinian refugees** in particular. Nonetheless, the mission statement also makes explicit reference to **various groups**, namely: small business owners, poor, Palestinian refugees and other proximate poor and marginal groups, women and youth⁸. The extensive mission statement and the inclusion of various target groups in the mission are partly due to the nature of the MD-oPt as a UNRWA Department, and not as an independent institution. Yet while the current formulation helps the Department to better segment the target population, on the other hand, it also **hinders the clarity of SG1**. The **SG2 makes explicit reference to the provision of credit, savings and other financial services**, even if currently credit is the only financial service available. Although not mentioned in the mission statement, the management places a strong emphasis on the provision of products tailored to clients’ specific needs gauged by client feedback. The **SG3 includes an extensive list of desired impacts** from the mission statement, making the set of goals very ambitious, as is further demonstrated through the expressed desire to reach macroeconomic impact.

Social Goals (SG)	Key words in mission statement
SG1: Reaching target clients	<ul style="list-style-type: none"> ▪small business, poor, Palestine refugees, proximate poor and marginal groups, women, youth ▪poorer urban areas where there is a high density of Palestine refugees
SG2: Meeting client needs	<ul style="list-style-type: none"> ▪provision of credit and other financial services ▪provision of income-generating and asset-building opportunities ▪provision of safe-saving services and a financial safety net
SG3: Creating change	<ul style="list-style-type: none"> ▪improve the quality of life ▪sustain jobs, decrease unemployment, reduce poverty, economically empower women, youth ▪help clients cope with personal and family emergencies and crises ▪provide scalable interventions with measurable macroeconomic impact

⁸Defined by UN standards as the 15 to 24 years old population.

Key terms utilized in the mission statement to describe the target clients **do not rely on a formalized definition**, such as a classification of “marginalized” and “poor”.

The **awareness** of the UNRWA general mandate among the personnel is sometimes stronger than that of the specific mission of the MD-oPt. This, coupled with the highly detailed **segmentation of the intended target** in the mission, may contribute to the non-uniform understanding of the target group by the personnel, both at the management and field level. Moreover, the mission is not visible in all branch offices or regularly reviewed in staff meetings.

MD-oPt is an **autonomous department of the UNRWA**, a UN relief agency, which maintains full ownership of the Department⁹. The MD-oPt mission follows the general strategic mission of the UN including a central commitment to human development, to building inclusive financial services for marginalized populations and to helping achieve the Millennium Development Goals (MDGs).

As a department of UNRWA, the **MD Advisory Board (AB)**, which meets once yearly, is not entitled to execute decisions but rather only to formulate recommendations¹⁰. Apart from the CEO, whose active participation is crucial, the members of the AB are not systematically involved in all of the strategic decisions, representing major **weaknesses in the governance**. All the same, the existence of an AB represents a good step towards building independent governance while within the UNRWA structure.

The **social commitment** among the management is good, especially at the top level. Concurrently, the **balance between social and financial concerns** as demonstrated at the governance and management level is good and relies on a strong social focus coupled with an emphasis on the importance of financial performance (portfolio quality, efficiency, productivity) to delivering sustainable and self-sufficient microfinance services. The Board also supports the development of social performance management and measurement, with a **specific focus on impact**, as exemplified through the commitment to measuring performance through external studies (including impact assessments, social ratings and market research).

The MD-oPt **governance and management remain committed during the ongoing crisis and occupation**. The social commitment of the Board is further demonstrated by the maintenance of operations despite often adverse operating conditions, as well as by issues addressed in AB meetings (e.g. linking the housing product to improving the conditions in refugee camps, promoting savings products to reduce clients' vulnerability, etc.). This commitment is also linked to UNRWA's specialization in operating in conflict areas and dedication to maintain financial support for the microfinance sector as long as the current humanitarian emergency persists. Indeed, UNRWA views the MD as an instrument that encompasses dimensions of both humanitarian and development assistance and thus also asks for a wide inclusion among MD-oPt clients of marginal groups including women, youth and the disabled.

The MD-oPt is in the process of defining an UNRWA **exit strategy**, whereby the Department would exit from the UNRWA structure. The exit aims to ensure the sustainability and flexibility of management and operations while also boosting the Department's productivity and efficiency in order to ensure a long-lasting service to the target clients. One of the central pillars of the MD-oPt strategy is that an upcoming transformation would **spin-off the microfinance operations** from the UNRWA structure **as independent legal entities** in each of the three countries of operations. The management envisages the possibility of creating a regional **holding company** that would unify the national entities and to which UNRWA would transfer the assets in return of capital. Each independent entity would have the initial capital fully subscribed by UNRWA.

The West Bank and Gaza operations would be registered as a private shareholding company¹¹ with all or the majority of shares held by the holding company. Depending on the capital requirements and potential saving mobilization, the establishment of a regional bank may also be considered as the final step of the transformation process. Within this process, UNRWA would maintain a direct governance role during the initial years, while structuring an exit process through the gradual sale of the holding company shares to public and private investors.

The medium term will bring about a **delicate management transition process**: while some members of the management team would remain, the historic leader of the institution would retire and new management members will be brought in. However, it is worth mentioning that the current management team remains very committed to the social orientation of the future team including the selection of members for the new leadership, requiring a balance between the financial expertise and the commitment to serving marginal groups and refugees in conflict areas. In addition to the management transition, the final exit of UNRWA and

⁹The MD-oPt also administers the OPEC Fund for International Development (OFID) trust fund through an Administrative Agreement. During 2007 the fund increased by a further US\$ 4.5 million. There is not yet an exit strategy for the fund.

¹⁰The Advisory Board presents recommendations that must then be approved by the UNRWA Commissioner General. In practice the CG has always followed the AB recommendations.

¹¹Non deposit-taking.

the capital requirements for deposit mobilization will translate into the need for further capitalization in the medium term. Even if the current management team is committed to continuing serving the same target segment of the market, the management turn-over and the choice of the **new shareholders** may entail some risk of mission drift in the medium term to the extent that the main strategic guidelines will be oriented towards the financial performance.

The various transformation options will be fully considered in the upcoming **business plan and feasibility study for transformation** which will be realized in 2009, with plans to begin the transformation process by 2010 and expectations to reach completion in 2011. Current regulations do not seem to oblige the MD-oPt to change the operations model, though the situation also depends on the content of any forthcoming microfinance law.

The **MD-oPt strategy** shows a strong overall focus on the achievement of the social goals of the mission. The **Medium Term Plan (MTP)** covering the period 2005-2009 was last updated in 2006 and does not include all of the current strategic guidelines of the MD-oPt. Nevertheless, an external consultant has been tasked with formulating a new business plan by the end of 2009. The MTP identifies **SMART social objectives** in terms of: extending the supply of housing loans to Palestinian refugees, increasing the outreach to women entrepreneurs, reducing clients' household poverty, creating household assets, generating new investment opportunities for small businesses and microenterprise with no access to bank loans, contributing to household consumption smoothing, improving the lives and habitat of poor Palestinian refugees and safeguarding the poorest clients through saving services. Explicit reference is further made to the objective to improve the reporting on the impact of microfinance intermediation at the business and household level.

The SMART objectives are not yet translated into **targets**. For instance, no specific targets on gender related outreach, average loan size or % of refugee clients have been formalized or utilized by the management. While the MTP includes a target in terms of number of branches and a breakdown of the portfolio growth projections by product¹², no formal target is clearly identified and used in terms of portfolio structure.

The current Business Research Unit is in the process of being transformed into a **Social Performance Management (SPM) Unit** that will be charged to support the setting of social objectives and targets, measuring social performance and integrating social information into the strategic decision making processes in order to improve the targeting, adequacy of the services and change/impact of MD-oPt. The activities planned for the short term include: workshops with the staff to raise awareness of the SPM framework, the review of policies, procedures and product design, the assessment and use of current information available and the identification of specific SP indicators. In particular, the internal creation of a **SPM workbook** for the Department is worth mentioning. The SPM workbook represents a good basis for the introduction of SP management as it includes: a formalized analysis of the mission, social goals and objectives, the identification of information needed by diverse stakeholders to be integrated into decision making and aligning systems and operations to the social mission. Furthermore, the workbook organizes the SMART objectives included in the MTP by the categories of social goals identified in the mission (targeting the intended population, adequacy to their needs and change realized in their lives).

The MD-oPt **product development strategy** aims to diversify the services options available to clients in order to better respond to their specific needs and meet the social goals. The current MD-oPt product line meets a range of social and economic objectives, including business development, poverty alleviation, job creation, household asset formation and women's incorporation. Consumer and housing lending represent important facets of the current MD-oPt strategy. The Department aims to increase its portfolio of consumer loans, products intended for low-paid waged workers in the private and public sectors without direct access to formal consumer credit services, to help the clients' families restore assets that were sold-off or lost during periods of unemployment and poverty. Meanwhile, the HLP, aimed at both refugees and non-refugees, is set to be introduced in the West Bank before the end of 2008.

The **gender empowerment** concern is present at the institutional level as demonstrated by the awareness of the management on the limitations of the current gender-related social performance in terms of share of women in client base to date, design of products tailored to women's needs and empowerment. The management currently presents a willingness to adopt a strategic approach to gender issues, as demonstrated by the recent formalization of a "gender action plan", including the goals of gender sensitive human resource management, increased female client share and gender based product design. In particular,

¹²By the end of 2008, the objective for share of outstanding portfolio by product is distributed as follows: Microenterprise Credit product 27%, Solidarity Group Loan product 5%, Consumer Lending Product 13%, the Small-Scale Enterprise Product 28%, the Housing Finance product 27%.

the management is considering the replication in the West Bank of an individual loan product targeting women with **income generating activities carried out inside the households**. This product is associated with a specific marketing strategy based on household visits that has proven effective at targeting female clients in the UNRWA-MD Syria operations. The participation of two staff members in the general UNRWA gender committee aimed at improving the gender-related performance agency wide both at the staff and client level is also worth mentioning.

The MD-oPt **expansion strategy** considers the density of micro and small businesses in the area and the presence of Palestinian refugees, even if the second criterion is not supported by a specific investigation tool and, once opened, branches do not exclude non-refugee Palestinians from the services. Overall, the expansion strategy is in line with the broad intended target population.

As a strategy to provide clients with a safety net to face crisis and emergency situations, MD-oPt plans to launch **pilot savings services**. In order to design services adequate to the clients' needs, by the end of 2008, the Business Research Unit will conduct a survey on potential clients that will complement the external savings market survey carried out in 2007. In spite of the **current legal restrictions** (see Chapter 2), MD-oPt plans to start offering saving services in early 2009, with a clear service vision coupled with the non-intermediation of the savings mobilized. Until the medium term, the saving collection does not seem to represent a funding strategy. The strategy adopted to cope with the risk of sanctions related to the non-compliance with the legal framework includes, as a best case scenario, an arrangement with the PMA that would exceptionally allow the Department to collect savings from the clients. Indeed, even if the MD-oPt is not a properly licensed institution, it seems that the PMA will allow it to be regulated. As a worst case scenario, the management is considering an appeal to the president of Palestine through the general UNRWA Memorandum of Understanding which entitles UNRWA to carry out activities beneficial to the Palestinian population. Moreover, the collection of savings is intended not only from the MD-oPt credit clients but also from the public, which will be defended on the basis of the broad "client base" of the UNRWA body. Nonetheless, a certain degree of risk of sanctions and tensions in system relationships exist related to the partial compliance to the legal framework.

Tracking and monitoring system

The current MD-oPt system has a **limited capacity** for realizing adequate tracking and monitoring due to the projected operations growth and also linked to the fact that branches are not online and there is a dual system for the West Bank and Gaza. It is worth mentioning however, that in the short to medium term the institution plans to adopt a **new loan tracking system** that will be better able to support the projected growth. The management also presents a strong **willingness to enhance the monitoring system** in order to make the information better available for decision making and social performance improvement (targeting, service quality, impact). Moreover, the SPM workbook includes a map of existing information and identifies information gaps and potential sources to fill the gaps.

- SG1 The MIS includes **relevant information** on the socio-economic profile of clients, such as: gender, age, marital status, citizenship, number of dependents, refugee status, business sector, list of assets, income, number of family members and non-family members employed in the client business, formal/informal, disability status, business ownership and business place ownership. In addition, breakdowns are available for gender, product, area, and client cycle. While the data is updated at every loans cycle, it is not yet systematically utilized to inform the decision-making.
- SG2 The adequacy of the products to clients needs is not based on an internal system; however, it is monitored through punctual **external studies** (impact assessment and savings feasibility study) as well as through the **informal information flow** at the branch level which is facilitated by monthly branch meetings. There is **no systematic calculation of drop-out ratio** or formal tracking of reasons for client dropout, even if an impact study in 2006 included the investigation of reasons for client drop out. In addition, the auditor investigates client willingness to renew the loan and reasons of anticipated drop-out during field visits while branch managers have easy access the list of clients who have left the institution. It is worth mentioning that the institution plans to conduct a second savings survey to investigate the needs of the clientele.
- SG3 In 2006 an **external impact assessment** was conducted in MD-oPt operational areas (Jordan in 2007, Syria in 2008). The constant staff concern on measuring client impact is also demonstrated by the inclusion of client loan use and life change in the auditors' investigation during planned client visits. Nevertheless, currently there is no systematic internal mechanism to track the impact of MD-oPt operations.

The system potential for reporting is remarkable: the majority of the **socio-economic information** and gender-specific breakdowns (see SG1) are available through **automatically generated reports** and to date

have mainly been used for integration into donor reporting. The socio-economic indicators of the client profile are not systematically monitored and used at branch and operations level for the ordinary decision-making process (the management mainly monitors the client poverty through loan size). Yet, there is willingness to make a more effective use of the data currently available and to adapt the products characteristics to the clients' needs based on the increased use of client level information. The information available on the **service adequacy** to clients needs seems to be integrated in the process of decision taking on the **introduction of new products and modifications to existing products**. For instance, the MEC+ product, with a higher loan amount and term than the MEC product, was introduced with the main objective of retaining graduating clients by meeting their specific needs.

Systems consistency to the mission

- Product design

The overall consistency of MD-oPt product design to the mission is adequate. The **minimum loan size** is quite high in absolute terms: US\$ 200 for SGL in Gaza and US\$ 400 for MEC in Gaza (US\$ 280 in the West Bank). However, considering that the target clientele is not intended as the poorest of the poor, the loan size seems in line with the mission. The MD-oPt requires **collateral of post-dated checks** from all clients in order to facilitate raising cause in court when needed. Should the potential client not have a bank account, the MD-oPt provides a letter to the Bank of Jordan assisting the client to open an account and receive the checks. Considering the broad target population and reduced cost for opening an account (US\$15 thanks to a special agreement with the Bank of Jordan), the collateral requirement does not seem to represent a barrier to the target client service access. In general, the collateral requirements are accessible to the target clients within the limits imposed by the unstable economic and political situation. For example, due to the deteriorating conditions in Gaza, the HLP is subject to the personal guarantee of an UNRWA employee. However, when introduced in the WB the HLP will only require a notary deed and guarantor.

The **delivery system** is adequate to the mission, considering the restrictions on movement in the oPt and the Departments' efforts to locate operations in areas highly concentrated with the Palestinian population (i.e. urban centers).

- Human resource management

As already mentioned, the future **Social Performance Management Unit** will be responsible for the overall management of social performance and improving the strategy and systems in coordination with other members of the staff.

Nevertheless, the overall HR alignment to the mission is currently limited.

Staff recruitment is based upon the UN system and considers the general social concerns of human development; particularly, the recruitment system emphasizes the relief and development value for the Palestinian refugees of working in UNRWA. However, there is no specific criterion adopted during the selection process to assure the **alignment** of the **candidates' personal aims** to the MD-oPt **mission**. Moreover, staff induction and training **does not seem to include formalized methods to disseminate the mission** among the staff. While the **operations manuals** include a description of the broad contents of the mission, they **do not include the formal mission statement** and do not formalize a specific definition of the key terms used to describe the target clients (e.g.: "small business"). Finally, the staff appraisal process **does not include formal criteria** to link the performance evaluation to the progress towards achieving the social goals identified in the mission. No incentive system is currently in place.

LIMITED RISK OF VOLUNTARY MISSION DRIFT

- *Even if a strong commitment exists, the management turn-over in the medium term and the potential entry of new shareholders through a transformation process involves the main strategic guidelines to be oriented towards financial performance.*

CERTAIN RISK OF INVOLUNTARY MISSION DRIFT

- *The extensive mission statement includes a long list of intended target clients and outcomes which hinder the clarity and focus of the mission as well as the accurate dissemination.*
- *Reporting for strategic decision making is focused on financial and productivity information and does not yet include specific social indicators to measure the achievement of the social goals.*
- *There are no specific criteria adopted during the staff selection process to assure the alignment of the candidates' personal aims with the mission. Moreover, staff induction does not include formalized methods to disseminate the mission among the staff.*

4. Social responsibility

Social responsibility towards personnel

As of September 2008, the total number of MD-oPt staff is equal to 165, lower than the numbers as of December 2005 and 2006. The **drop in total number of staff** registered in 2006 and 2007 was due to the political and economic crisis that led to the dismissal or transfer to other departments of about half of the Gaza staff (mainly LOs).

The **gender balance** of the MD-oPt staff is not fully adequate, with 32% of female staff and 19% of female staff in management positions. This is partially reflecting the larger constraints faced by women in workforce participation. No specific activities have been carried out to

Staff	Dec-05	Dec-06	Dec-07	Sep-08
Total staff	185	173	165	165
Female staff	16%	24%	32%	32%
Female staff in management	39%	91%	19%	19%
Staff turn-over ratio^a	10%	9%	13%	16%
Staff transfer	0%	2%	21%	0%
Male	11%	5%	11%	16%
Female	13%	28%	17%	15%
Management	33%	5%	5%	10%
Loan officers	22%	9%	21%	22%
Administrative staff	6%	13%	7%	9%
Support staff	0%	0%	0%	0%

^aDoes not include staff transfers

promote the staff sensitivity on gender issues so far. However, it is worth mentioning that the gender balance among staff represents a concern of the top management and that two MD-oPt staff participate in the UNRWA gender committee, established to improve the agency's gender performance. The "gender action plan" developed by the MD-oPt also includes some activities to enhance a gender sensitive human resource management.

The **staff turn-over rate** is to be monitored and it is equal to 16% for the period Oct07-Sept08, showing an increasing trend. Even if the reasons of staff turn-over are not currently tracked, some of them seem to relate to the **level of remuneration** compared to the qualifications of the staff. Staff turn-over is concentrated in the category of LO and is overall quite balanced among male and female members of the staff.

The **labor climate** is overall adequate, even if no formal tool is in place to monitor staff satisfaction and salary adequacy.

The overall **participation** of staff in decision making is quite good, although limited in some respects by the hierarchical organizational structure and the UN operating environment. The frequent staff meetings, both at the branch and institutional level, coupled with the open door management style, provide some opportunities for staff to contribute input and share concerns. It is worth mentioning that despite the difficult logistical situation for the staff based in Gaza, strong efforts are made at the HQ level to promote their maximal inclusion and involvement. The increase in the last two years of the training activities has also represented an opportunity for the staff operating in different areas to build **team spirit** and share concerns with the management.

The MD-oPt relies on the UNRWA **code of conduct** for the staff, including ethical norms related to sexual harassment and the acceptance of favors and gifts. However, some weaknesses are observed in terms of formalization and completeness of **human resource policies** specifically tailored to the Department, as well as **dedicated human resource management**.

- On the one hand, the **salary** level of the field staff is **in line or slightly above** that of other MFIs. On the other hand, the remuneration at management level does not seem to be in line with the microfinance sector. Moreover, the workload of the MD-oPt staff is generally higher than other equally rewarded UNRWA positions in other departments. **No proper incentive scheme** is currently available also due to the rigidities in the salary policy of UNRWA; however, a system rewarding the best performing staff is in place under the form of mobile and transport allowances and the management is considering the introduction of non-monetary incentives.
- The **contractual conditions** are **quite adequate**, including basic salary, provident fund¹³, family allowance, 24 days leave, 14 sick days, and 7 days emergency leave. The duration of the contract is one year (renewable) for the majority of staff, after a six months probationary period. Nevertheless, a limited share of the staff is **paid on a daily basis** before the probationary period. The introduction of a specific insurance for the staff covering accidents and injury may significantly improve the social responsibility towards the personnel.
- The benefit package is quite good and includes health insurance and access to a consumer loan that includes the same conditions offered to the clients; however, scholarships are not available.

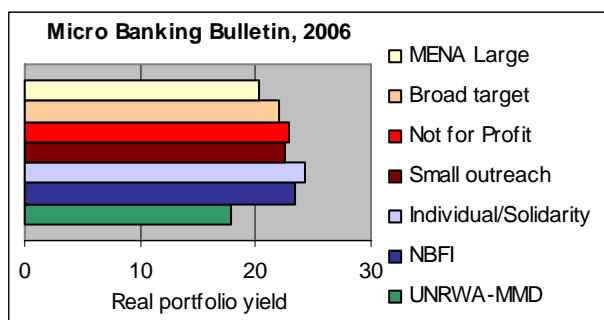
¹³Staff contributes 7.5% and UNRWA contributes 15%.

- In the last two years, internal and external **training opportunities have been adequate overall**, largely due to the financial support received from USAID. However, due to the logistic complexity of operations, the activities carried out in the Gaza Strip have been limited compared to the West Bank. The training activities are coordinated by a **dedicated training officer** and are based on an annual plan and budget¹⁴. Moreover, participants' feedback is systematically collected to monitor the effectiveness. Internal trainings are delivered by a select group of staff members specifically chosen and trained for this purpose. However, the links between the staff performance appraisal and the training opportunities provided are not formalized. Internal career opportunities are available, also due to the preference given to the internal staff with equal level of competency.

Social responsibility towards clients

The operation manuals include some **ethical guidelines** for the relationship between LOs and clients, including honesty, respect and professionalism. No specific activities to benefit the clients apart from credit operations have been directly carried out so far by the MD-oPt, even if the other UNRWA departments are active in various activities including food assistance, education and health.

In spite of the **concern on gender issues**, the overall strategic approach and the specific measures in place to address the topic have been limited to date. The MD-oPt has only offered a women specific product in Gaza (SGL) due to the specific market characteristics¹⁵. Moreover, women clients in Gaza do not have access to the MEC product and can avail individual credit only after the third cycle of the SGL. However, the "gender action plan" includes as an objective the increase of the female client base as well as the design of gender-tailored products. In the short term, a product specific to women will be introduced in the WB (Women Household Credit). Two MD-oPt staff participate in the UNRWA gender committee to reinforce the gender related performance in terms of the adequacy of female clients reached, adequacy to female client needs and other gender issues.



Cost of credit	2005	2006	2007	Oct07-Sept08
Portfolio yield (PY)	28.4%	26.3%	23.9%	30.3%
<i>PY West Bank</i>	30.2%	34.1%	33.7%	37.4%
<i>PY Gaza</i>	27.5%	24.9%	15.7%	20.4%
Inflation rate	2%	3%	7%	11%
Real portfolio yield	25.5%	22.3%	16.0%	17.9%
National lending rate	6.7%	7.2%	6.3%	5.6%

- The **portfolio yield** of the MD-oPt in the period Oct07-Sept08 is worth **30.3%**, which is an **intermediate** level, reflecting the **difficult environmental conditions** on the one hand and the **room for improvement in efficiency** on the other hand. Due to the high inflation affecting the NIS, the **real portfolio yield** is much less, worth **18%** in the last period of analysis; this is a relevant reason why the cost charged by the MD-oPt appears **lower** than all the **peer groups** considered. The evolution of the portfolio yield in the past three years is more the result of the portfolio quality (particularly weak in Gaza during 2006 and 2007) than the effect of deliberate pricing policies, as demonstrated by the substantially lower yield on the Gaza portfolio. As shown in Chapter 1, the MD-oPt is still in the process of reaching full sustainability; the interest rates applied are **based on the cost structure**¹⁶ of products and are periodically reviewed by the management.
- Due to the numerous MFIs active on the market, client over-indebtedness is on the rise. The MD-oPt clients are exposed to this risk: 27% of recent clients declare the purpose of the current loan to be the repayment of other loans, while 48% of them affirm they have used loans to repay debts in the past. **No credit bureau** is currently available in Palestine impeding a reliable verification of clients' total indebtedness, even though an informal exchange of information between MFIs seems to exist, especially in the Gaza Strip. The **basic assessment of clients' repayment capacity** is improvable in terms of detailed cash flow and financial analysis, as well as inclusion of all household incomes (for MEC product) and household expenditures (for all products)¹⁷. Even if the assessment capacity of loan officers has benefited from the training over the last year, the accuracy of the clients' repayment

¹⁴Training budget for the year 2009: Gaza US\$43,300; West Bank US\$89,800.

¹⁵While female-run microenterprises are common in Gaza, the involvement of women in informal businesses carried out in public places seems to be more restricted in the West Bank.

¹⁶Cost calculations include an assumption on the provision cost under normal conditions (3-5%).

¹⁷Normal, optimistic and pessimistic scenario may be considered to improve the assessment. The household expenses are taken into account through the no. of dependents and wives, but no specific quantification is included in the analysis.

evaluation presents some room for improvement.

As a mitigating measure, the MD-oPt policy establishes a ceiling of 30% on the repayment capacity¹⁸ of clients, even if there is no policy to limit client multiple borrowings. It is worth mentioning that in 2007 the MD-oPt limited the lending activities in Gaza due to the decline in the political-economic situation thus also limiting the risk of client over-indebtedness.

- The policy by which loans are disbursed in US\$ in Gaza or Jordanian Dinar (JD) in West Bank exposes some clients with income denominated in different currencies¹⁹ to a certain degree of exchange rate risk.
- Consumer protection

- Although the loan officers' oral explanation provided to the borrowers seems to be adequate, neither promotional material nor clear written loan conditions are distributed to the clients or clearly visible within the branch offices. The introduction of a specific marketing function charged with the coordination of promotional activities and tools should have a positive impact on clear communication about product features. On the one hand, the MD-oPt calculates the interest rate on the flat basis, while on the other hand the institution does not charge additional commissions or fees for the loan. Clients are provided with a copy of the loan agreement (showing the monthly flat interest rate and the penalty rate) and with receipts to back each transaction. Nevertheless, the absence of a detailed repayment schedule, including the breakdown of installments by principal, interest and outstanding balance for clients leaves room for improvement.

- No formal mechanisms for handling client complaints are currently in place, although clients sometimes report claims and suggestions to the loan officers.

- As of now, no specific activity is carried out to foster the consumer education and financial awareness of clients. However, possibly due to the good education level of the clients, the majority of them are aware of the interest rate charged (60%). At the same time, the knowledge of the interest amount paid, the range of products available and the procedures applicable in case of late payment is more limited. It is also interesting to note

Financial awareness of clients	Total	Male	Female	Urban	Rural
Interest rate	60.0%	56.6%	70.5%	61.0%	50.0%
Interest amount	36.1%	40.4%	22.7%	36.0%	37.5%
Range of products available	12.8%	13.3%	11.4%	11.0%	31.3%
Procedure in case of late payment	12.5%	13.3%	9.8%	11.9%	18.8%

Clients entered between May06-Apr07

that the interest rate awareness was observed to be higher among female rather than male, and among urban rather than rural clients.

- The current **internal audit function** is performed both at **UNRWA** general level (control) and at the **MD-oPt level** (verification), ensuring an overall adequate performance. However, the internal verification function presents some room for improvement in terms of scarcity of dedicated staff (one dedicated staff member for WB, Jordan and Syria and from July 2008 and one dedicated staff member in Gaza) which entails limited client visits. The direct reporting of the verification officer to the director of the department is not aligned with the best practices and is due to the centralization of the audit function at UNRWA level and to the emerging governance structure. It is worth mentioning that the management attaches importance to building an internal audit culture in the department²⁰. The MD-oPt department regularly audits its financial statements and is exposed to external assessments and verifications with a certain frequency.

- The main findings²¹ of the impact of the MD-oPt program on the economic activities (impact and market study, 2007, West Bank and Gaza) of clients show a mixed picture, with some positive and some unclear results in terms of impact of the operations on the clients. However, it is worth considering that the moment when the study was realized (mid 2006) may have biased the results due to the severe economic and political crisis that affected the oPt. The main findings of the study are presented below:
 - Positive impact of the Department on the clients' investments (the average current investment of drop-outs is lower than that of the active clients);
 - No clear impact of the program on employment;
 - 35.6% of the borrowers declare that their savings have increased since becoming MD-oPt members;

¹⁸The loan installment by the net business income must be less than 30%. Since August 2008, the loan tracking system has been programmed to automatically deny repayment amounts over the established income, without specific authorization.

¹⁹The Palestinian Authority's salary are denominated in NIS, as is the majority of NGOs; on the contrary, UNRWA pays salaries in US\$ in Gaza and in JD in West Bank. Some of the international companies (e.g. hotels) pay in US\$.

²⁰E.g.: the importance of the verification function was stressed during the 2008 annual staff meeting.

²¹The correlation between the participation in the program with the profits of the micro entrepreneurs, the contribution to the household expenses, the monthly expenditures and asset retention was not found to be statistically significant.

- The probability of a client to notice a positive change in his autonomy and his partner's respect is very high when he stays longer in the program.

Social responsibility towards community and environment

While **no formal MD-oPt policy** concerning social responsibility towards the community and the environment is in place, as an UNRWA Department, the MD-oPt operations are subject to the general environmental policy of the agency. However, compliance to such policy is not guaranteed by a specific list of prohibited activities to finance or by proper monitoring and enforcement systems.

Some elements of social responsibility towards the community can be identified in MD-oPt operations. Namely, the Departments **maintenance of operations** in both Gaza and the West Bank throughout the 2nd Intifada period, despite the economic difficulties and fact that some other MFIs were forced to close operations, represents the MD-oPt's strong commitment to the communities in which it operates. Moreover, the 2007 impact study²² found a positive correlation between participation in the MD-oPt and the hiring of employees, even if the overall employment creation is low. At the same time, the indirect effect on supporting existing jobs of MD-oPt is quite good, with **2.88 persons working** in the **activities financed**, out of which 1.25 are family members (including the client) and 1.66 are non-family members.

The MD-oPt status as an UNRWA Department means that it can often be associated with the various relief and humanitarian programmes (health, education, social services, etc.) of the UNRWA body in general. Nevertheless, there are currently no specific activities or projects undertaken by the MD-oPt in itself focused on community development or environmental responsibility.

²²Impact and Market Research Report for UNRWA's Microfinance and Microenterprise Program in the Palestinian Territories, PlaNet Finance, 2007.

5. Outreach

Operational areas

The geographical coverage of the MD-oPt is broad. The network of 10 branches covers the **main urban centers** of the WBGS. The **Gaza Strip**, which concentrates **26%** of the active clients and **36%** of the outstanding portfolio, presents a significantly higher incidence of poverty than the national average, imputable to the deteriorated political and economic situation (see Chapter 2 for more details). Even if operations were never suspended in the area, the political/economic situation led the management to sharply decrease the share of operations carried out in Gaza in the last years (64% at the end of 2006, 34% at the end of 2007 and 26% as of September 2008), in order to limit the credit risk to MD-oPt and the risk of client over-indebtedness.

Regions of operation	Poverty	Extreme poverty	UNRWA-MDoPt, Sept08		
			Active clients	Outstanding portfolio	
West Bank	Nablus	54%	23%	15%	12%
	Jenin	62%	26%	7%	5%
	Tulkarem	60%	31%	8%	6%
	Qalqilya	61%	31%	1%	1%
	Hebron	59%	28%	13%	12%
	Bethlehem	50%	26%	13%	12%
	Ramallah	47%	19%	16%	16%
Gaza	Gaza city	65%	37%	12%	19%
	Khan Younis	75%	46%	8%	9%
	Deir al-Balah	71%	44%	6%	8%
oPt	58%	30%	100%	100%	

UNDP Poverty in the occupied Palestinian territory, 2007, income based.

Looking at the geographical distribution of the operations and by comparing the poverty incidence in each of the governorates²³ where the MD-oPt is present with the national average, the geographical outreach appears to be quite deep and substantially in line with the national level.

The operations are almost uniquely carried out in urban centers, where the population and also several microfinance providers are concentrated. Rural clients²⁴ and the rural portfolio account for only 4% and 2% of the total, respectively, and the poverty incidence in rural and urban areas does not present significant differences.

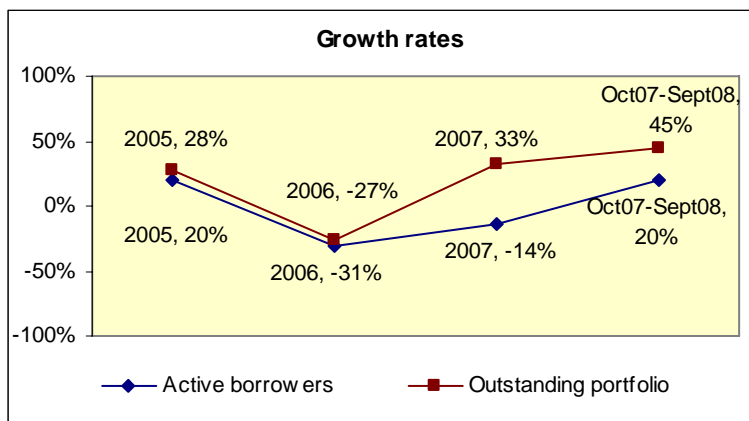
Clients reached²⁵

With **8,777 active clients** and an outstanding portfolio worth **US\$ 10,246,894**, the breadth of outreach of the MD-oPt is quite broad, even if it is lower than the MENA benchmark²⁶. It is worth considering however, that the Department is currently the largest MFI operating in the occupied Palestinian territories.

The **unstable growth rates** registered during the last years reflect the political and economic evolution of the context. The rate of growth in number of borrowers and outstanding portfolio fell from 20% and 28%, respectively, in 2005 to -31% and -27% in 2006, mainly due to the closure of the Gaza Strip (-39%, -36%).

The recovery of the portfolio growth in 2007 is attributable to the restart of the operations in the West Bank, while the continuous negative growth in the number of borrowers in 2007 was due to the writing-off of a very large portion of loans²⁷, especially in Gaza. The last period analyzed, October 2007 – September 2008, shows a positive trend, with **20%** increases in the **number of active borrowers** and **45%** in the **outstanding portfolio**.

Due to the political situation, the growth objectives fixed in the Medium Term Plan 2005-2009 were not met; a review of the growth plans is foreseen within the strategic planning process that will be realized in 2009.



²³It is worth mentioning that the figures may present some inaccuracies, given that the classification by governorates is realized on the basis of the branch location and not on the clients' actual residence.

²⁴Clients with agricultural activities financed.

²⁵The information is mainly based on a survey of recent clients and integrating, when relevant, data from the MIS. See Annex 2 for more details.

²⁶Median number of borrowers of the MFIs in MENA (MIX 2006) is equal to 13,796.

²⁷Write off ratio worth 20% in 2007, with an average loan outstanding written-off worth US\$392.

Overall, the **outreach** of the MD-oPt appears to be **quite deep** in absolute terms and substantially **in line with the national benchmarks** in terms of social profile (e.g. refugee status), monetary poverty and access to basic services. The overall profile of clients presents elements of vulnerability such as the dependency ratio within the households, limited bargaining power of female clients, food and health insecurity. A large share of the clients is financially excluded before joining the Department, even if a high heterogeneity of previous access to financial services is observed.

Considering the results and the various characterizations of the target clients included in the mission statement, the **actual outreach** can be considered overall **in line with the stated objectives**, even if some **room for improvement** can be identified in serving **women**.

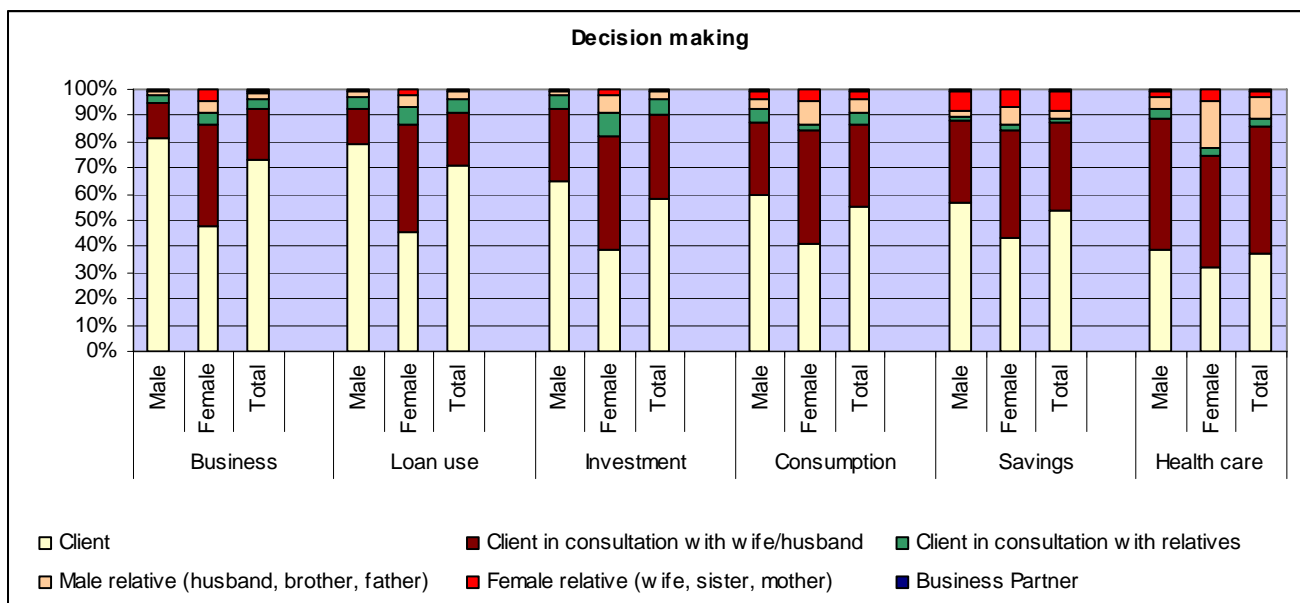
Social vulnerability and household profile

- On average, the MD-oPt clients are **38.43 years old** (median 37): **80.7%** of them are **married** and 17.9% are single, while 0.8% and 0.7% are widowed and divorced, respectively. A marginal share of married male clients live in polygamous households (2.2%); in 2004, the percentage of polygamous marriages registered in Palestine was 3.5%. The **average number of household members** is just above the national average (**6.68**, compared to 6.5); while the number of **members contributing** with income to the household (**1.44** on average), compared to the number of **dependents** (**5.41**) shows a high dependency ratio and a condition of considerable vulnerability. However, clients refer to the sources of income as **constant** in the large majority of cases. 0.1% of the clients present a disability (hearing, speaking or moving).

GENDER OVERVIEW:

Female borrowers represent 17% of the client base and 13% of the outstanding portfolio; 45% of female clients exert a full control over the loan use and 48% a particle control (consultation with husband/relative). 27% of households are headed by a female.

The share of **women** clients as of September 2008 is equal to **17%**, which is quite limited in absolute terms. However, it is worth considering that at national level the women's labor force participation remains low, accounting for only 15.7% of the formal labor force²⁸. The sharp drop observed in 2007 (from 27% in December 2006 to 17% in December 2007) is largely imputable to the slowdown of operations in **Gaza**, where the product offer is more women oriented than in the West Bank. In the West Bank and Gaza, the share of female clients is higher in the **CLP** product (14%) than in the MEC product (8%). On the one hand this is due to the lack of a specific individual product tailored to the women entrepreneurs' needs, while on the other hand it is due to the prevalence of male LO in charge of marketing. In Gaza, women are specifically targeted through the solidarity group product, while the MEC product is available only to male entrepreneurs. **27% of female clients are head of household**; this information, compared to the share of female headed Palestinian families (8.2% in PCBS, 2006), suggests a higher vulnerability than the national average. The few cases (6.8%) where a lack of control over loan use was observed are concentrated in rural areas. In all of the decision making process investigated, the women clients are found to have a **lower bargaining power** than other players



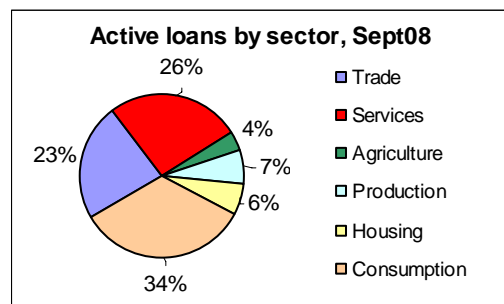
²⁸The main reason for the low participation is "housekeeping". (PCBS, Labor Force Survey, July-Sept. 2007).

(household members, relatives and business partners) than men clients, reflecting the gender issues and social condition of women in Palestine. In particular, the larger differences in independent decision making between male and female clients are observed in **loan use** (79% of male and 45% for female), **business** (82% and 48%) and **investment** (65% and 39%). On the other hand, decisions about children's education and healthcare seem to involve a larger number of household members, with a better gender balance.

The share of **refugees** in the client base of the MD-oPt, equal to **48%**, is higher than the share of refugees among the Palestinian population in 2007 (41%), confirming a certain vulnerability profile of the clients. Refugee clients are concentrated in Gaza, where they account for 85% of the total, compared to 35% in the West Bank. About 18% of the clients (37% of the refugee clients) are living in refugee camps. The **education** profile of clients is **good** and overall in line with the national average: 64.6% of them have secondary education, 27.6% a university degree; 7% of the clients only have an elementary degree and only 0.84% have not completed any education cycle. This is confirmed by the high percentage of young **household members going to school: 94%** in age 6-12 and **86%** in age 13-17.

Business activities and employment support

- The MD-oPt credit policy does **not allow start-up** activities due to the higher risk profile. The majority of clients have been working in their business more than three years (55%), 21% and 20% of the clients' businesses have been in place for 1-3 years and 6-12 months, respectively, and only 4% of the clients have been running a business for less than 6 months.
- The large majority of the enterprises financed belong to the **informal sector (70%²⁹)**, which is generally prevalent in Palestine. The **business place** is **owned** in the majority of cases (60%), while 13% of the clients rent it. The median business **capital** is worth US\$ 4,987 (data available for 72% of the clients). The median monthly **income** of clients³⁰ is worth US\$ 793.
- A large share of clients use the loan for **consumption purposes** (34%), while 26% and 23% of clients are engaged in **service** and **trade** activities, respectively. The rise in the share of consumption portfolio during the last years, from 13% as of December 2006 to 34% as of September 2008, is the result of the expansion of the CLP product. Production only accounts for 7% of the active loans; the decrease in the share of production portfolio (from 15% in 2006 to 7% as of now) is partially the reflection of the management decision to reduce the SSE portfolio due to the higher risk entailed in larger loan sizes³¹. The financing of agriculture, concentrated in Jenin and Hebron, is also marginal (4% of active clients) due to the risks related to the sector. The purpose of loans for recent clients is fixed (15%) and working (31%) capital, housing improvement for 18% of the clients and repayment of debts for 27% of them. Household expenses, education and health services account for only 3%, 4% and 2% of the loan purposes, respectively.



On average, **2.88 persons work** in the **activities financed**, out of which 1.25 are family members (including the client) and 1.66 are non-family members. The majority of them are regular workers (2.4), while on average 0.1 of the businesses' employees are seasonal and 0.4 are sporadic workers. 51% of the clients are self-employed, while 43% are employed. It is also worth mentioning that, due to the instability of the economic situation, 2% of the respondents declared to be unemployed. The major source of income for 66% of the clients is represented by businesses and wages from private sector, while public sector salaries are the main income for 34% of the clients.

²⁹ Results based on data available for 59% of the loans active as of September 2008.

³⁰ Source: MIS. Salary (for CLP and HLP clients) and the median monthly business income (for MEC, MEC+, SGL and SSE). Other incomes of the family are not included.

³¹ The management decided to significantly reduce the SSE portfolio in Gaza and has currently ceased all SSE lending in the West Bank.

Economic poverty

Considering the household consumption based definition of poverty, **17.1%** and **4.6%** of the MD-oPt recent clients are **poor** and **very poor** (national and national extreme poverty lines), respectively. Looking at the internationally applied standards, **18.8%** and **1.8%** of the clients fall below the **PPP\$2/day** and **PPP\$1/day** lines, while **42.7%** of them live on less than **PPP\$3 a day**. A certain incidence of poverty in the client based is also confirmed by the 7% of clients whose consumption is lower than the median consumption of households below the national poverty line (USAID definition of extreme poverty).

Considering the monetary poverty parameter, the outreach of the MD-oPt is quite deep and substantially in line with the national benchmark. **Rural clients** are found to be generally poorer than the urban ones, yet no dramatic differences emerge from the gender and West Bank / Gaza breakdown of poverty rates, even if slightly higher poverty rates are observed among **male clients** and those of the **West Bank**. This, coupled with the fact that poverty incidence among the Gaza population is higher than the national average, may indicate that the population served by the Department in Gaza is generally less poor than the average in the area.

In addition to the average consumption patterns, it is worth considering the high variability of income and expenses, which results in a high vulnerability for the MD-oPt clients and households. Particularly, **46%** of the recent clients have experienced periods of **shortage of income** to face household expenses in the last 6 months, while **33%** and **37%** of the clients reported that income was not sufficient to cover **medical** and **food expenses**, respectively. The prevailing **coping strategies** for households experiencing shortage of income are similar to the ones generally adopted by the lower-end population of Palestine³²: borrow from financial institutions (46% of cases), reduce expenditures (44%), selling jewelry (33%), and getting help from family and friends (28%). Borrowing from financial institutions as a coping strategy to compensate for the lack of income may constitute a serious risk of over-indebtedness in some cases. 14% of the clients receive food assistance (16% in Gaza) and 2% receive financial assistance from humanitarian organizations, figures that are lower than the corresponding average data for the Palestine population³³. Food aid and other safety nets have played a major role in preventing an even higher number of people falling into poverty and food insecurity.

Monetary poverty	UNRWA-MD oPt	Male	Female	Urban	Rural	West Bank	Gaza	oPt*
National poverty line	17.1%	17%	17%	16%	28%	18%	16%	18.4%
National extreme poverty line	4.6%	4%	5%	4%	11%	5%	4%	6.1%
\$3 a day (PPP)	42.7%	44%	40%	41%	57%	42%	43%	43.9%
\$2 a day (PPP)	18.8%	2%	2%	1%	5%	19%	18%	20.7%
\$1 a day (PPP)	1.8%	19%	19%	18%	30%	2%	1%	2.5%
USAID extreme poverty line	7.0%	7%	8%	6%	14%	7%	6%	9.1%

Households of recent clients. See annex 1 for more details. *PPI elaboration of PECS2005, based on consumption at household level.

Asset property

76% of clients **own** the **housing** unit they dwell in (less than the national average of 82%) and 29% own some land. It is worth mentioning that 99% of the HLP active loans as of September 2008 were disbursed to Palestinians registered as refugees by UNRWA. The ownership of the major available durable goods for the Palestinian households demonstrates that the condition of MD-oPt clients is in line or slightly above the national average: 99% of clients own a refrigerator (95.7% for Palestine), 60% have a telephone line (compared to 47.2%), 22% own a private care a car (18.2% in Palestine)³⁴.

Access to basic services

The share of clients without access to basic services is relevant in absolute terms and in line with the national benchmark: **12%** and **46%** of the clients **do not have improved water** sources and **improved sanitation**, respectively, while all of the households are connected to the public electricity network. This picture confirms the quite deep outreach of the MD-oPt. The main source of water for the clients in the West Bank is the West Bank Water Department (public, 54% of clients), while in Gaza it is the EISahel (93% of the clients).

³²PBCS 2003, coping strategies of the poorest 16% of the population: borrow from financial institutions (60% of cases), reduce expenditures (46%), selling jewelry (17%), and getting help from family and friends (34%).

³³76 percent of households in the GS have received some type of in-cash or in-kind assistance; 23 percent of households have been assisted in the WB. (FAO food security survey 2008).

³⁴PCBS, Housing and Housing, Conditions Statistics, 2006.

Access to basic services	UNRWA-MD oPt	Male	Female	Urban	Rural	West Bank	Gaza	oPt
Clients without improved water source ¹	12%	14%	5%	10%	31%	17%	2%	11%
Clients without improved sanitation ²	46%	46%	45%	42%	88%	63%	11%	55%
Clients without electricity ³	0.0%	0%	0%	0%	0%	0%	0%	0.3%
Access to financial services								
Clients without previous access to formal credit*	62%	63%	59%	63%	56%	66%	54%	na
Households without current / savings account	24%	21%	34%	25%	19%	33%	7%	na
Households without credit/debit card	67%	65%	72%	66%	75%	83%	32%	na
Previous access to credit:								
None	54%	56%	50%	55%	50%	58%	47%	na
Moneylenders, providers, family, friends	8%	7%	9%	8%	6%	8%	7%	na
NGOs, cooperatives, credit and saving associations	11%	9%	18%	9%	38%	15%	2%	na
Banks and regulated financial institutions	27%	28%	23%	29%	6%	19%	44%	na

Households of recent clients. See annex 1 for more details. oPt data are based on the PECS 2007. na: not available. ¹Not connected to the public water network. ²Cesspit, or no connection to sewage system. ³ Public electricity network

Access to financial services

The **financial inclusion effect** of the MD-oPt appears significant: **62%** of the recent clients declare not to have had access to formal and semi-formal credit before joining the department. **24%** of the clients do not have a **current/saving account**³⁵ and **67%** do not have a **credit or debit card**.

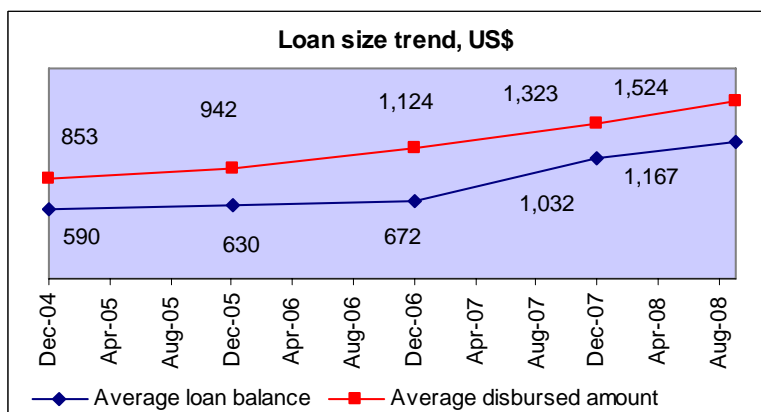
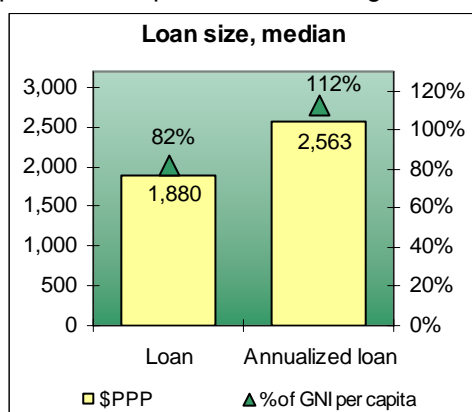
The presence of **27%** of the clients with **previous access to banks and regulated financial institutions**, coupled with the prevalence of clients without previous financial access indicates a large heterogeneity of the client base. 11% of the clients have previous experience in NGOs and other non-regulated financial institutions.

It is interesting to note that the clients in the **West Bank** present overall a **more limited access to both basic and financial services**: 63% of them live in households without improved sanitation, and 66% did not borrow from formal providers in the past. On the other hand, **44%** of the **Gaza** clients declare to have had previous access to **banks** and formal financial institutions; this may be partly due to the higher share of housing loans in Gaza compared to the West Bank. The more limited access to basic services in the West Bank is in line with the slightly higher incidence of monetary poverty compared to the Gaza clients.

Loan size analysis

With an average loan disbursed worth US\$ 1,425 in the period Oct07-Sept08, and an average outstanding balance representing 85% of the national GNI per capita, the loan size of the MD-oPt is intermediate. Considering the disbursed amount of all loans active as of September 2008, the **median** amount stays at US\$1,130, equivalent to **\$PPP 1,880** and to 82% of the per capita GNI. Given that the average loan duration is lower than one year, the loan size results larger when annualized, with a median value of \$PPP 2,563, worth 112% of the GNI per capita.

The trend over the past years shows a clear increase in the loan size, mainly due to the change in the structure of portfolio by product, including: the increase of the CLP (with higher loan amounts) relative to the MEC portfolio, and the introduction of the HLP product in 2006, which is currently worth 21% of the total portfolio and presents an average balance of US\$ 3,778³⁶.



³⁵In addition to the mandatory account necessary to open in order to produce the post-dated checks used as guarantee.
³⁶In the last 3 years, the yearly growth for HLP, CLP and MEC was respectively 61%, 40% and 4%.

6. Quality of the services

Variety

The current variety of MD-oPt **financial services is limited to credit**, with five separate loan products offered in Gaza and three loan products on offer in the West Bank. Nevertheless, the Department is studying the potential market interest and feasibility for offering **pilot saving products in 2009**. A savings study conducted by the Department in 2007 showed that clients possess a willingness to save and a high trust in UNRWA, even if the ability to save was found to be limited. The pilot savings products are planned to be introduced in Gaza and in two WB branches (Jenin and Tulkarem) in early 2009. In addition, the introduction of insurance services through a partnership may be considered in the medium term.

The **overall variety of credit products is intermediate** and not all products are available in both areas (WBGS). In the West Bank, the Microenterprise Credit (MEC) and MEC+ loans are offered alongside the Consumer loan (CLP), while in Gaza the Housing (HLP)³⁷ and Solidarity Group (SGL) products are also offered. The SSE capital investment/working capital loan, the Departments original loan product, is in the process of being phased out due to the declining market. Meanwhile, by late 2008 the HLP will be introduced in the West Bank and the MEC+ will be introduced in Gaza to replace the SSE.

To date, there is no specific product designed to meet the financial needs of the small agricultural producers, mainly due to the risk involved as well as restricted conditions on movement in the areas. Start-up businesses are not financed and parallel loans are not offered.

The MD-oPt utilizes both the **individual and solidarity group methodology**. Solidarity group lending is offered in Gaza only and is characterized by groups of three to ten female members. As of September 2008, the group methodology encompassed 7% of total borrowers and 5% of the outstanding portfolio, realizing a steady decline in recent years³⁸. Concurrently, MD-oPt registered a **decline in the overall portion of female borrowers**, down from 32% female clients in 2004 to 17% female clients as of September 2008.

In order to better meet the needs of female borrowers, the MD-oPt plans to introduce a **new product targeting female borrowers in the West Bank** modeled on a product previously developed in the UNRWA MD Syria operations, the Women Household Credit (WHC). The WHC is an individual loan product that can be utilized for both businesses carried out in the household or for consumption purposes. The product requires a personal guarantor for the borrower and adopts a personalized marketing strategy based on visits by female loan officers to potential women clients in their households.

Adequacy

Overall, the MD-oPt **product offering to clients is adequate** considering the service delivery which caters to clients' needs, the ease of credit procedures and the customer service presented by the MD-oPt staff, even if clients express some dissatisfaction related to loan terms and size as well as the cost of credit.

The MD-oPt **service delivery** and transactions can be somewhat limited by the restricted conditions on movement in the oPt (permits, checkpoints, etc.). However, the location of the MD-oPt branches in densely populated urban areas coupled with the possibility of field transactions, with the LOs collecting repayment at the clients' business, contribute to the overall adequate system of service delivery.

Loan disbursement is realized through checks that must be taken to a nearby bank to be cashed. Although this signifies an additional transaction cost to the client, the process is facilitated by the central and urban location of branches near the major banks and does not seem to represent a reason for client dissatisfaction. The **time to disburse the loan** is intermediate, ranging between one to seven days and is perceived as good by the clients. Overall, the clients appreciate the ease of the credit procedures³⁹ while the documents and procedures required to access the services seem adequate and are not overly cumbersome to the loan application process.

³⁷Aimed at housing renovation and improvement.

³⁸The SGL product stood at 20% of the total outstanding portfolio and 30% of active borrowers in 2004, declining to 10% of the portfolio and 23% of borrowers in 2006 and 3% of the portfolio and 9% of borrowers in 2007.

³⁹UNRWA MD-oPt Impact Assessment 2007, PlaNet Finance.

Credit products						
US\$	SGL-Gaza	MEC-Gaza & WB	MEC+ West Bank	CLP-Gaza & WB	HLP-Gaza	SSE-Gaza
<i>Methodology</i>	Solidarity Group	Individual	Individual	Individual	Individual	Individual
<i>Currency</i>	US\$	US\$ in Gaza JD in WB	JD	US\$ in Gaza JD in WB	US\$	US\$
<i>Type of interest</i>	Flat	Flat	Flat	Flat	Flat	Flat
<i>Min. interest rate</i>	2% monthly	2% monthly	1.65 % monthly (US\$ 8,553 - 12,619) 1.5 % monthly (US\$ 12,620 - 21033)	2% monthly	9% yearly	9% yearly
<i>Max. interest rate</i>	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
<i>Commissions</i>	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
<i>Min. amount</i>	200	400 in Gaza 280 in WB	8,553	3 x monthly salary	12 x monthly salary	3,000
<i>Max. amount</i>	4,000	8000 in Gaza 11217 in WB	21,033	3000 in Gaza 3x monthly salary in WB	15,000	working capital 30,000, investment capital 70,000
<i>Max amount (first loan)</i>	400	1000 in Gaza 1402 in WB	12,620	3000 in Gaza n.a. in WB	15,000	n.a.
<i>Min. maturity (months)</i>	4	4	4	4	18	12
<i>Max. maturity (months)</i>	11	11	18	11	36	36
<i>Average maturity (months)</i>	6	6 months in Gaza 8 months in WB	8	6 months in Gaza 8 months in WB	24	24
<i>Interests payments</i>	monthly	monthly	monthly	monthly	monthly	monthly
<i>Principal payments</i>	monthly	monthly	monthly	monthly	monthly	monthly
<i>Grace period (months)</i>	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
<i>Collateral</i>	Loan contract+ notarial deed	Loan contract+ post-dated cheques	Loan contract+ post-dated cheques and notarial deed (for new clients)	Loan contract+ post-dated cheques	Guarantor (UNRWA employee) Loan contract post-dated cheques	Guarantor (UNRWA employee) Loan contract post-dated cheques

JD: Jordanian Dinar

The MD-oPt clients appreciate the service access facilitated by the **guarantee requirements**, with the majority of clients satisfied with the guarantee conditions according to the 2007 impact study, as well as the client survey in which 74% of clients ranked the collateral requirements as good or very good. In particular, clients appreciate the fact that no physical collateral is required. The MD-oPt requires **post-dated checks** from all individual clients to ease the enforcement process of clients' obligations in case of default. In some cases, personal guarantors are also required, particularly in Gaza where the HLP product carries the additional guarantee requirement of personal **guarantor by UNRWA employee** in an effort to mitigate the risk of the declining economic situation in the area.

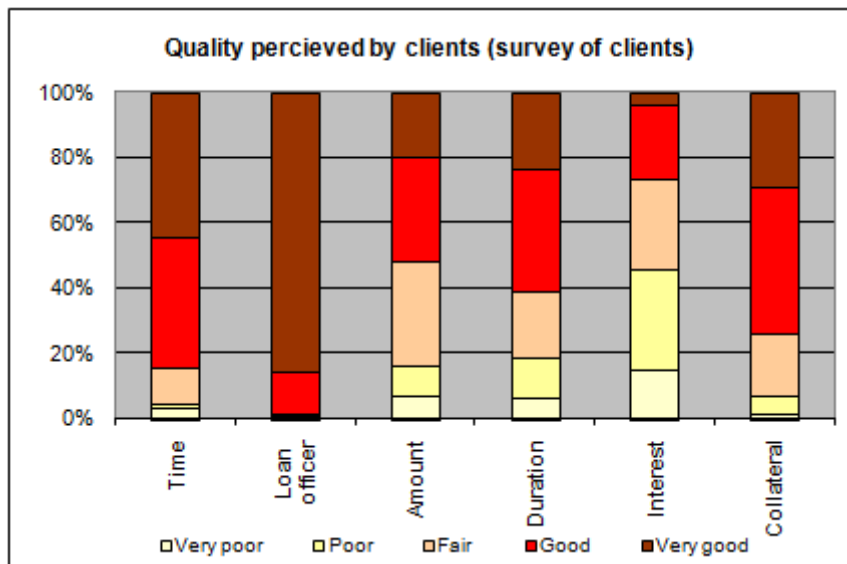
Access to business loans by **female clients in the Gaza Strip** is limited to the **solidarity group methodology** in the first three loan cycles, after which clients may continue to borrow only through the individual methodology, subject to the business analysis. According to the 2007 impact assessment, the majority of group clients (66%) expressed willingness to borrow individually versus 34% who preferred to remain in group lending, illustrating a rigidity to the methodology. The relevance of such rigidity is diminished, however, by the current blockade to the flow of persons and goods in the area and the consequent slowdown in economic activities and demand for loans.

Given the conditions of banks and MFIs in the market, the MD-oPt guarantee requirements seem to constitute a **competitive advantage**. Indeed, while the opening of a bank account brings about some

additional costs⁴⁰ to the client; the clients do not seem to perceive these costs a burden. However, it is worth mentioning that the savings strategy of MD-oPt does not seem to consider the use of such accounts to foster clients' savings, also due to the fact that banks do not generally show interest in targeting MD-oPt clientele.

The MD-oPt **loan terms** are slightly less flexible than those offered by the competition and perceived as short by a share of the clients (12% according to 2007 impact assessment). Loan **rescheduling** is not allowed according to MD-oPt policy and also due to the management orientation towards increasing the level of repayment discipline among the clients and field staff. Nevertheless, case by case rescheduling arrangements are made at the branch level though they are neither formalized nor tracked separately in the MIS. The **monthly repayment frequency** is perceived as adequate to the business and income cycles of the clients. Moreover, after the repayment of 2/3 of the loan, clients have the option to prepay the remainder of the loan in order to immediately apply for a subsequent loan, even if no reduction in the interest payable is allowed. No grace periods are available.

The MD-oPt maximum **loans size** for first loans as well as in general are lower than some of the competition. There is a general perception among the clients that the loan sizes are limited compared to their financial needs⁴¹, while in the client survey conducted the loan amount ranks



as the primary concern for the borrowers, with nearly 50% of survey respondents ranking the loan amount as fair, poor or very poor. It is worth mentioning, however, the somewhat unrealistic expectations of a portion of the clients that emerged during focus group discussions, whereby clients would like to receive a higher loan amount while making smaller installment repayments with a lower interest rate. These expectations may be linked in part to the humanitarian relief role played by the UNRWA as well as the difficult operating conditions stemming from the ongoing economic crisis. There are currently no formal systems in place to communicate the variation in loan size approved compared to the loan size requested by the client. This lack of communication constitutes a reason for client dissatisfaction and can lead to the eventual rejection of the loan offered to the client in some cases when the clients' financial needs are not adequately met.

Importance ranking	
Survey of clients	
1	Amount
2	Duration
3	Interest
4	Loan officer
5	Time
6	Collateral

The **cost of credit** seems to be higher than some of the competition and especially compared to banks. Clients perceive the interest rate as high and frequently cite it as a central concern (nearly 46% of survey respondents perceived the interest rates as poor or very poor). This view may also be due to the expectations generated by the MD-oPt association with UNRWA as a relief agency as well as the negative economic situation in general. The interest rate charged is higher than that of the banks and is not differentiated by loan cycle, loan amount or clients' repayment performance.

Overall, the **customer service** provided by MD-oPt field staff is good. A loan officer hand-over policy which includes the early identification of incoming staff and a period of overall positively contributes to the client service and satisfaction. Over 85% of survey respondents perceived their relationship with the MD-oPt LO as very good and nearly 13% rated it as good⁴².

⁴⁰The minimum amount that clients are required to save in a bank account in order to receive the post dated checks is worth around US\$ 15 plus a minimal opening fee.

⁴¹According to the 2007 impact assessment, 18.8% of clients considered the loan amount insufficient.

⁴²According to the 2007 impact assessment, nearly 50% of respondents considered their relationship with UNRWA staff as excellent, 40% consider the relation as good and only 5% thought that their relation with the staff was bad.

The **client drop-out ratio** is rather high, equal to 35% and 32% in 2006 and in the period Oct07 to Sept08, respectively. The decrease in the rate registered in 2007 is mainly due to the exceptional volume of loans written-off in the period (write-off ratio worth 21%). Although the reasons for client drop-out are not systematically tracked, the 2007 impact assessment identified inadequate repayment periods (36%), loan interest rates too high (27%), inappropriate loan

Client drop-out	Dec-05	Dec-06	Dec-07	Sep-08
Client drop-out ratio	18.2%	35.1%	17.3%	32.3%
Client drop-out ratio West Bank	16.0%	26.9%	20.1%	39.1%
Client drop-out ratio Gaza	19.2%	38.4%	15.7%	19.1%
PAR30	22.8%	39.5%	7.1%	5.5%
Loans by cycle				
First cycle				42%
Second cycle				19%
Third cycle				10%
≥ fourth cycle				29%

*The last period corresponds to Oct07-Sept08, annualized

amounts (23%) and credit not renewed (9%) as the central reasons for drop out. Among the socioeconomic reasons cited for drop-out, 66% of the drop-out clients indicated the poor economic situation in the oPt as the primary reason for drop-out since clients' customers could not afford to buy their products or services⁴³.

Non-financial services

Limited non-financial services are offered to clients in Gaza only through the Small Microenterprise Training Programme, self-sufficient training courses (tracked separately than MD-oPt regular operations) open to both clients and non-clients. The courses include over 60 modules outsourced to external providers, including, among others: business development, accounting, bookkeeping, languages, and taxation. A dedicated MD-oPt staff position is in charge of coordinating the training activities from Gaza and an evaluation system is in place to assess the quality of the trainers, material and logistics. The participant fees (180-200 participants per year) almost entirely cover the cost of the training. The training courses are not likely to be expanded into other areas in the future.

⁴³Additional 2007 impact assessment findings include: 28% of former clients cite the military occupation as a handicap to their development. Most former clients consider their MD-oPt participation very positive (33%) or positive (37%) while nearly 11% of past clients consider their experience negative or very negative.

Annex 1 - Statistics

Poverty lines

The following table presents the value, in local currency, of the national and international poverty lines used to assess the profile of clients.

The national extreme poverty line reflects a budget for food, clothing and housing. The national poverty line adds other necessities including health care, education, transportation, personal care, and housekeeping supplies.

Poverty lines

Consumption per capita per day,	Base year	Value	Most recent	Value adjusted
National poverty line	2007	12.94	Oct-07 Sep-08	13.99
National extreme poverty line	2007	10.33	Oct-07 Sep-08	11.17
\$2 a day (PPP)	1993	5.49	Oct-07 Sep-08	12.74
\$1 a day (PPP)	1993	2.74	Oct-07 Sep-08	6.37

2005 PECS conducted by the Palestinian Central Bureau of Statistics (PCBS). National poverty line developed by the Palestine National Poverty Commission in 1998 for West Bank and Gaza Strip (World Bank, 2004)

The poverty rates among MD-oPt client base are obtained using the PPI tool for Palestine, which uses the PECS2005 data and bases the definition of poverty on the consumption level of households adjusted for price differences in Gaza and the West Bank and for the household size. Applying such definition of poverty on the PECS2005 data yields household poverty and extreme poverty rates of 18 and 6% respectively. These data differ from the PECS2007 poverty and extreme poverty rates, which are possibly based on the personal (rather than household) and expenses (rather than consumption) definition of poverty. It is important to clarify that PECS2007 data are used in the context section, while the poverty incidence among clients is based on and is compared to the PECS2005 data.

Loan size

To increase the relevance of the most commonly used proxy of outreach depth, the loan size analysis includes the following adjustments:

- Dividing the loan size by the GDP per capita
- Expressing the loan size in \$PPP
- Normalizing the loan size to one year term
- Considering not only the average loan size, but also the median and other moments of the distribution (1st and 3rd quartile)

The analysis is based on the complete list of loans active as of September 2008 (disbursed amount).

Loan size	US\$		\$PPP		% of GNI per capita	
	Loan	Annualized loan	Loan	Annualized loan	Loan	Annualized loan
Average	1,895	1,927	3,151	3,206	137.9%	140.3%
Mode	1,412	1,541	2,349	2,563	102.8%	112.1%
Minimum	200	308	333	513	14.6%	22.4%
1st quartile	847	1,130	1,410	1,880	61.7%	82.2%
Median	1,130	1,541	1,880	2,563	82.2%	112.1%
3rd quartile	2,000	2,260	3,327	3,759	145.5%	164.4%
Maximum	40,000	38,136	66,535	63,434	2910.6%	2774.9%
Standard deviation	2,134	1,583				

Active loans as of September 2008, amounts disbursed.

Survey on clients

In order to provide a complete description of the poverty outreach, a survey on recent clients has been realized. Recent clients are defined as those clients with an active status at the date of the evaluation, who took their first loan with the MFI in the 12 months preceding the social rating (October 2007-September 2008).

Sample characteristics:

- Design: multiple steps cluster
- Size: 180 clients
- Branches included: Gaza, Khan Yunis, Nablus, Jenin, Ramallah, Hebron

In addition to those included in the report, some other findings of the survey on clients are presented below.

BASIC SERVICES	Absolute frequency	Relative frequency
Water supply		
Not connected to the public water network	21	12%
Connected to the public water network	159	88%
Total	180	100%
Sewage system		
Cesspit, or no connection to sewage system	83	46%
Public sewage system	97	54%
Total	180	100%
Electricity		
Not connected to the public electricity network	0	0%
Connected to the public electricity network	180	100%
Total	180	100%
FINANCIAL SERVICES		
Previous access to credit		
None/only MMD	98	54%
Other bank or financial institution	48	27%
MFI	12	7%
Credit cooperative or credit and saving associations	8	4%
Employer	1	1%
Moneylender	1	1%
Friends/ relatives	11	6%
Other	1	1%
Total	180	100%

The lack of access to improved sources of water and to improved sanitation is considered in the following cases: Not connected to the public water network. The lack of access to improved sanitation is considered in the following cases: Cesspit, or no connection to sewage system

Annex 2 – Social indicators

UNRWA-MD oPt, Sept08

SOCIAL RESPONSIBILITY	
Female staff*	32%
Female staff in management*	19%
Staff turn-over ratio*	15.5%
Portfolio yield*	30.3%
Real portfolio yield*	17.9%
National lending rate*	5.6%
Financial awareness of clients: Interest rate	60%
Financial awareness of clients: Interest amount	36%
Financial awareness of clients: Range of products available	13%
Financial awareness of clients: Procedure in case of late payment	13%
OUTREACH	
Active borrowers*	8,777
Growth in active borrowers*	20%
Growth in outstanding portfolio*	45%
Individual methodology, clients*	94.2%
Solidarity group methodology, clients*	5.8%
Agriculture, clients*	3.5%
Female clients, portfolio*	12.8%
Female clients*	16.7%
Female clients head of household	27.3%
Refugee clients	48.3%
Clients without completed primary education	0.9%
Household members in age 6-12 attending school	94.0%
Household members in age 13-17 attending school	86.0%
No. of household members	6.68
No. of members contributing to household income	1.44
No. of members depending on household income	5.41
No. of constant sources of household income	1.47
Financed business in informal sector	70%
Employed in financed activity (avg, including client)	2.88
Employed in financed activity (avg, family, including client)	1.25
Employed in financed activity (avg, non-family)	1.66
Clients below the national poverty line	17.1%
Clients below the national extreme poverty line	4.6%
Clients below the 3\$PPP/day international poverty line	42.7%
Clients below the 2\$PPP/day international poverty line	1.8%
Clients below the 1\$PPP/day international poverty line	18.8%
Clients below the USAID extreme poverty line	7.0%
Households owning dwelling	76%
Households owning land	29%
Clients without improved water source	12%
Clients without improved sanitation	46%
Clients without electricity	0.0%
Clients without previous access to formal or semi-formal credit	62%
Households without current / savings account	24%
Households without credit/debit card	67%
Households without food security	37%
Average balance per borrower / GNI pc*	85.0%
Average disbursed loan amount, US\$*	1,524
Median loan disbursed (\$PPP)**	1,880
Median annualized loan disbursed (\$PPP)**	2,563
QUALITY OF THE SERVICES	
Client drop-out ratio*	32%
PAR30 *	6%
Clients at ≥ fourth loan cycle*	29%

Sources: survey on recent clients; *MIS; **Database of active loans. See annex 1 for more details

Annex 3 – Definition of acronyms and indicators

Acronym / indicator		Definition / formula
Financial Performance	Operational self-sufficiency (OSS)	$(\text{Financial revenue} + \text{Other operating revenue}) / (\text{Financial expenses} + \text{Loan loss provision expenses} + \text{Operating expenses})$.
	Financial self-sufficiency (FSS)	$(\text{Adjusted financial revenue} + \text{Other operating revenue}) / (\text{Adjusted financial expenses} + \text{Adjusted loan loss provision expenses} + \text{Adjusted operating expenses})$
	Return on equity (ROE)	Net income before donations / Average equity
	Return on assets (ROA)	Net income before donations / Average assets
	Portfolio at Risk (PAR30)	Portfolio at Risk > 30/ Gross outstanding portfolio
	Write-off ratio	Write-off of loans / Average gross portfolio
	Risk coverage ratio (>30 days)	Accumulated reserve / Portfolio at risk >30 days
	Loan loss reserve ratio	Accumulated reserve / Gross portfolio
	Funding expense ratio	Interests and fee expenses on funding liability / Average gross portfolio
	Operating expenses ratio	Operating expenses / Average gross portfolio
	Loan officer productivity – Borrowers	Number of active borrowers / Number of loan officer
	Staff productivity – Borrowers	Number of active borrowers/ Number of staff
Debt/Equity ratio	Total liability / Equity	
Context	HDI	Human Development Index
	GDP	Gross Domestic Product
	GNI	Gross National Income
	GDI	Gender-related Development Index
	WB	World Bank
	FMI	International Monetary Fund
	UNDP	United Nations Development Program
	MDG	Millennium Development Goals
	\$PPP	International dollar, based on Purchasing Power Parity
Social Performance Management system	SG	Social Goal. Social goal 1 = reaching target client; Social goal 2= meeting clients' needs; Social goal 3 = creating change
	SMART	Specific, Measurable, Achievable, Realistic, Time-bound
Social responsibility	Staff turn-over rate	Staff who left during the period / Average staff at in the period
	Portfolio yield	Interest income from portfolio / Average net portfolio
	Real portfolio yield	$(\text{portfolio yield} - \text{inflation}) / (1 + \text{inflation})$
Outreach	Average outstanding loan	Outstanding portfolio / number of active loans
	Average disbursed loan	Amount issued in the period / Number of loans issued
	Average outstanding loan on per capita GNI	$(\text{Outstanding portfolio} / \text{number of active loans}) / \text{GNI per capita}$
	Median loan disbursed on GDP pc	50 th percentile of loans issued in the period / GDP per capita
	Annualized disbursed loan	Amount disbursed * (12 / months of loan term)
	Disbursed loan, \$PPP	Amount disbursed in local currency * \$PPP conversion factor
Quality of the services	Client drop –out rate	$(\text{number of active clients at the beginning of the period} + \text{number of new (first time) clients entering during the period} - \text{clients written-off during the period} - \text{number of active clients at the end of the period}) / (\text{number of active clients at the beginning of the period})$

Annex 4 – Social rating scale

Rating grade	Definition
S^SAAA	Excellent capacity to effectively translate its mission into practice and to promote social values. Very high likelihood to achieve social goals.
S^SAA	Very good capacity to effectively translate its mission into practice and to promote social values. Very high likelihood to achieve social goals.
S^SA	Good capacity to effectively translate its mission into practice and to promote social values. Very high likelihood to achieve social goals.
S^SBBB	Completely adequate capacity to effectively translate its mission into practice and to promote social values. High likelihood to achieve social goals.
S^SBB	Adequate capacity to effectively translate its mission into practice and to promote social values. High likelihood to achieve social goals.
S^SB	Fairly adequate capacity to effectively translate its mission into practice and to promote social values. Reasonable likelihood to achieve social goals.
S^SC	Moderate capacity to effectively translate its mission into practice and to promote social values. Reasonable likelihood to achieve social goals.
S^SD	Inadequate capacity to effectively translate its mission into practice and to promote social values. Low likelihood to achieve social goals.

The rating grade can be corrected with a + or – sign, which implies a slight positive or negative variation respect to the main grade.