EVALUATION OF HONDURAS COVELO FOUNDATION DCA GUARANTEES

FINAL REPORT

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MAY 2009

This publication was produced for review by the United States Agency for International Development. It was prepared by SEGURA/IP3 Partners LLC under SEGIR Global Business, Trade and Investment II – IQC Indefinite Quantity Contract, Number EEM-I-00-07-00001-00 Task Order # 04, Development Credit Authority Evaluation.

On the Cover: Water purification was among the sectors that benefited from loans under the DCA Guarantees. Photo USAID/Honduras

TABLE OF CONTENTS

TABLE OF TABLES

TABLE OF FIGURES

LIST OF ACRONYMS & ABBREVIATIONS

AAP	Savings & Loan Association
ACA	Access to Credit for Farmers
ADICH	Association for Integrated Community Development
BANADESA	National Bank of Agricultural Credit
CAFTA	Central America Free Trade Agreement
CMS	Credit Management System
CNBS	National Commission for Banks and Securities
DCA	Development Credit Authority
DR-CAFTA	Dominican Republic-Central America Free Trade Agreement
EDA	Training and Development for Farmers
EGAT	Economic Growth, Agriculture, and Trade
EGAT/DC	Office of Development Credit
FACACH	Federation of Savings & Loan Cooperatives of Honduras
FINSOL	Solidarity Financier
FJMC	José María Covelo Foundation of Honduras
FUNDAHMICRO	Honduran Foundation for Support to Microenterprise
FUNED	Foundation for the Development of the Honduras Vision Fund
GDP	Gross Domestic Product
GMC	*Grupo Microfinanciero Covelo*
HDH	Brotherhood of Honduras
IFPRI	International Food Policy Research Institute
L.	Honduran Lempira
MCC	Millennium Challenge Corporation
MFI	Microfinance institution
MSE	Micro- and small-sized enterprise
MSME	Micro-, small-, and medium-sized enterprise
ODEF	Organization for Women Entrepreneurs
OPD	Private Development Organization
OPDF	Financial Private Development Organization
PILARH	Projects & Local Initiatives for the Regional Self-Development of Honduras
RED	Rural Economic Diversification
REDCAMIF	Microfinance Network of Central America
REDMICROH	Microfinance Network of Honduras
SME	Small- and medium-sized enterprise
TA	Technical Assistance
USAID	United States Agency for International Development
USD	United States Dollar

EXECUTIVE SUMMARY

The Office of Development Credit in the Bureau for Economic Growth, Agriculture, and Trade (EGAT/DC) of the United States Agency for International Development (USAID) contracted SEGURA/IP3 to carry out a series of evaluations of partial credit guarantees made under the auspices of its Development Credit Authority (DCA). This report presents findings and conclusions from an evaluation, carried out in March and April of 2009, of DCA guarantees used by the José Maria Covelo Foundation (FJMC) in Honduras. The evaluation sought to answer seven evaluation questions concerning the outputs, outcomes, and impact of the guarantees.

The evaluation team used a mixture of quantitative and qualitative methods to answer the evaluation questions, including a desk review of background documents and the DCA database, semi-structured interviews with FJMC officials and other stakeholders in Honduras, and an email-based survey of members of the Microfinance Network of Honduras (REDMICROH). The team developed an evaluation framework with indicators and interview questions to guide the investigation.

USAID and FJMC signed guarantee agreements on 9 September 2003 and 28 September 2005. Both are for loan portfolio guarantees that utilize the DCA. Both seek to increase access to credit by qualifying borrowers, defined as micro- and small-sized enterprises engaged in any of four sectors: (1) non-traditional agriculture or agro-industry, (2) wood products, (3) specialty coffee, and (4) light manufacturing.

FJMC was established as a private development organization (OPD) in 1991, and began to offer direct credit as a microfinance institution (MFI) in 1995. In January 2008, the organization established a commercial, licensed bank called Banco Popular Covelo (Bancovelo). At present, while FJMC still owns the portfolio that carries the DCA guarantee, Bancovelo administers it.

FINDINGS AND CONCLUSIONS

OUTPUT LEVEL

Evaluation Question 1: Loans Disbursed
Did the Covelo Foundation use the guarantee facility? How much local private capital was mobilized or leveraged? What potential market(s) did the DCA guarantee help open for the Covelo Foundation?

Conclusions: The Covelo Foundation has achieved additionality by using the DCA guarantee facilities to enter a new market: agricultural credit. The 2005 DCA agreement was instrumental in building Covelo's portfolio of agriculture loans. Most guaranteed loans conformed to the objective of supporting non-traditional agriculture, wood, and light manufacturing. The Covelo Foundation has highly leveraged guarantee resources obligated by the U.S. Government, at a ratio of 20 to 1.

Findings

- As of 30 September 2008, the Foundation had utilized 99.99 percent of its 2003 DCA loan limit, and 91.23 percent of its 2005 maximum.
- In 2003, prior to the signing of the first guarantee agreement, the Covelo Foundation's lending for agricultural uses was virtually zero.
- Two-thirds of the 279 loans that carried the DCA guarantee under the 2003 agreement financed non-traditional agriculture or agro-industry.
- Under the 2005 agreement, while most loans financed non-traditional agriculture, 65 of the loans were for traditional crops.
- The DCA guarantee has also supported a substantial number of guaranteed loans for light manufacturing, as well as a small number of loans for coffee and wood products.
- As of 31 March 2009, agriculture represented 92.7 percent of the Covelo Foundation's outstanding portfolio of loans bearing the DCA guarantee.
- As of 30 September 2008, the total DCA obligation of USD 140,800 had leveraged the equivalent of USD 2.83 million in loans, for a leveraging ratio of 20 to 1.

Evaluation Questions 2.a and 2.b
Did the Covelo Foundation's use of the DCA guarantee improve access to credit for the target sectors? Did characteristics of guaranteed loans differ from other loans in ways that improved access?

Conclusions: Through targeting farmers with little collateral, increasing the average size and tenor of microloans, and decreasing microcredit interest rates, the Covelo Foundation expanded access to credit for its customers in the nontraditional agriculture sector and increased lending to entrepreneurs.

Findings

- A Covelo official said the Foundation used the DCA facility to guarantee loans where the farmer is not able to offer real estate as collateral, but can only offer other assets (e.g., a vehicle), or has a co-signer to the loan. Guaranteed loans are therefore smaller and of shorter duration.
- Compared to nonguaranteed loans, the microloans that carry the DCA guarantee are larger, have a longer tenor, and carry a lower interest rate. In keeping with the intent of the guarantee agreement, the FJMC said it used the DCA facilities to make larger and longer-term loans, not to guarantee small working capital loans.

Evaluation Question 2.c
How did the DCA guarantees fit into the Covelo Foundation's ongoing strategy?

Conclusions: The Covelo Foundation had a clear strategy on how to use the DCA facility: to reduce risk while it entered a new market - agricultural production.

Findings

- The MFI's General Manager explained that the Covelo Foundation traditionally had played a leadership role in the microfinance sector in urban areas. Several years ago, however, he concluded that microfinance lending in urbanized areas was relatively well advanced, while rural lending was lagging; hence the guarantee agreements with USAID in support of this new strategic focus for the foundation. Loan officers then used the facility to mitigate the risk of lending to the then-unfamiliar agricultural sector.

Evaluation Question 2.d
Did guaranteed loans correspond to other objectives and parameters?

Conclusions: The guarantees helped the Covelo Foundation to move up market in the microcredit sector. Covelo loans helped at least some of the borrowers to increase their incomes and assets.

Findings

- The average DCA guaranteed microloan has exceeded the average value of nonguaranteed loans by at least 20 percent every year since the first DCA guaranteed loan was issued.
- The average tenor of guaranteed loans has also exceeded the tenor of average nonguaranteed loans every year. By March 2009, the average DCA guaranteed loan was twice as long as the average nonguaranteed loan.
- A sample of 17 percent of the 53 individuals who had received at least three loans with the DCA guarantee showed that, on average, they had increased their annual income by 46.4 percent.
- These borrowers also reported, on average, increases (between first and last loan applications) in total assets of 58.4 percent.

Evaluation Question 3
How did the Covelo Foundation implement its loan guarantee program? And why?

Conclusions: The Covelo Foundation's initial implementation of the guarantee program reflected the objective of lending to nontraditional agriculture sectors. Over time, as it gained more experience in agriculture lending, the Foundation focused on building its own client base without USAID assistance, as well as expanding access to credit for borrowers with less collateral to offer. This evolution suggests that the Foundation is sustainably building an agricultural lending business while increasing access to credit for its customers.

Findings

- The Covelo Foundation's initial close collaboration with the USAID Rural Economic Diversification (RED) Program led to a high level of loans for non-traditional agriculture. Later, as the FJMC began to form independent alliances with rural producers' associations, some loans went to traditional agricultural uses.

- During 2005 and 2006, the Covelo Foundation applied the guarantee to virtually all credits made to the agricultural sector, because it had the largest unutilized portion of the DCA guarantee to draw from and was just gaining experience in agricultural lending.
- During 2007, a USAID representative advised FJMC to use its remaining guarantee facility more strategically. Loan officers now use the facility to guarantee credits to borrowers that have relatively less collateral to offer.

OUTCOME LEVEL

Question 4: Partner behavior change
Did the Covelo Foundation/Bancovelo improve access to credit to the target sectors outside the DCA guarantees? Did they move into any new sectors/industries, types of borrowers, types of loans, or loan terms? If so, how and why and to what extent were the DCA guarantees responsible for improving the access of their customers to credit outside the guarantees?

Conclusions: The DCA guarantees to the Covelo Foundation achieved their goals of increasing lending to agriculture-focused SMEs and helping Covelo to expand and move up market in the agriculture sector. The DCA guarantee helped both the Covelo Foundation and Bancovelo jumpstart their lending to the agricultural sector. They have expanded access to credit in this sector for their customers by increasing the number of loans available, the average size and tenor of those loans, while keeping interest rates low. The FJMC became increasingly confident in risking its own capital in the sector without a guarantee. Rapid increases in agricultural lending have helped them become a significant actor in the agricultural microcredit sector.

Findings

- Between December 2003 and December 2006, the Covelo Foundation's agricultural lending increased more than 3,000 percent through loans with the DCA guarantee.
- Beginning in 2007, while the Covelo Foundation continued to expand its agricultural portfolio, a progressively smaller proportion of the loans carried the USAID guarantee.
- As of the end of March 2009, only 13.2 percent of the combined agricultural portfolio of the Covelo Foundation and Bancovelo carried the DCA guarantee.
- The March 2009 average nonguaranteed agriculture loan from the Covelo Foundation more than twice the size of a DCA guaranteed loan.
- The Covelo Foundation's average nonguaranteed agriculture loan tenor increased 50 percent between December 2006 and March 2009.
- Average nonguaranteed agriculture loan interest rates, while steady, remained below those for microcredit and mostly below those for SME loans.
- Eight people who initially received a DCA-guaranteed loan from the Covelo Foundation subsequently obtained housing loans from Bancovelo.
- At least one farmer who initially borrowed under the DCA guarantee subsequently obtained a non-guaranteed agricultural loan from Bancovelo.

- Officers of these two organizations confirmed that a successful credit history with the FJMC and/or Bancovelo could lead to further loan approvals.
- Several individual entrepreneurs have progressively worked up to larger loans and/or loans with a longer tenor under the DCA guarantee.
- The Covelo Foundation shares credit histories with the public credit bureau and at least one private bureau.
- Available data did not permit a determination as to which borrowers who had first obtained DCA-backed loans from FJMC then went on to obtain loans from other financial institutions.
- As of 30 June 2008, the Covelo Foundation and Bancovelo's combined agricultural portfolio represented 13 percent of the agricultural/forestry lending reported by members of REDMICROH, placing it in fourth place among members of the Network.

Question 5
What factors at the Covelo Foundation/Bancovelo were responsible for achieving the desired outcomes (e.g., TA, bank staff training, revised bank strategy, new procedures, changed structure, new management, etc.)?

Conclusions: The Covelo Foundation's initial success in lending to the agricultural sector with the DCA guarantee, along with development of new procedures, products, and related know-how, were primary causes of their increased lending to the agriculture sector without the guarantee. However, it is unlikely that these positive outcomes of the DCA guarantees will be sustained because Covelo put ceilings on its agricultural lending and is considering selling its agriculture portfolio, indicating it has neither the intent nor the scope to pursue agricultural lending any further.

Findings

- According to Covelo officials, by 2007 the Covelo Foundation had developed financial products and procedures suited to the sector and established financial relations with farmers, which helped it expand its non-guaranteed portfolio.
- Covelo has set ceilings on agricultural lending for both the Covelo Foundation (L. 30 million) and Bancovelo (L. 10 million).
- Both entities are already close to those limits. The Millennium Challenge Corporation (MCC) has provided funding specifically for agricultural lending, but outside of these resources, Bancovelo will not have room to extend agricultural lending
- As of April 2009, the Covelo Foundation was trying to decide between retaining its agricultural portfolio and seeking to sell it to a third party.

IMPACT LEVEL

Question 6: Market demonstration effect
Did other, non-partner banks initiate or increase lending to the target sector(s)? If so, to what extent was the DCA guarantee to Bancovelo responsible? How and why?

Question 7
Did access to credit (or the terms of credit) improve for loans to the target sectors? If so, how and why? What role if any did the DCA guarantee play as a demonstration model?

Conclusions: The Covelo Foundation's DCA-supported agricultural sector lending helped facilitate the entrance of one MFI into the agricultural sector: Association for Integrated Community Development (ADICH). We did not find evidence of any broader impact on agricultural sector lending. However, since the DCA guarantees have not even ended yet, it is too early to ascertain impact, which by definition is a long-term phenomenon.

Findings

- Lending by MFIs (outside of the Covelo Foundation) to the agricultural sector has increased substantially during the period in which the Covelo DCA agreements have been in effect. This increase is due almost exclusively to increased credit from existing providers of agricultural credit, rather than new entrants.
- Survey respondents and interviews with members of REDMICROH provided reasons unrelated to Covelo's experience for their organizations' expansion of agricultural lending: social motivation, desire to expand their portfolio, increase in competition in urban areas, cumulative organizational experience in the sector, and increased collateral that farmers are able to offer.
- ADICH only began to report agricultural lending in 2005, after the DCA guarantee program had begun. A representative of ADICH indicated that a packet of operational information on providing agricultural credit that had been developed by the Covelo Foundation, based largely on their experience with DCA-supported agricultural lending, was an "important factor" in their entrance into the agricultural credit market.

EXTERNAL FACTORS

What are the exogenous factors that have affected the financial sector? How have they done so? Have these factors affected the performance of the DCA guarantees?

Conclusions: Factors that *increased* the supply of and demand for agricultural credit include USAID and MCC technical assistance programs for small-scale farmers, increased competition among MFIs in urban areas, and demand by rural customers. Factors that *decreased* the supply of and demand for agricultural credit include the Government's agricultural debt forgiveness programs and subsidized lending programs, as well as fluctuations in world prices for agricultural goods.

Findings

A number of MFI representatives interviewed noted that TA provided by the USAID RED program and predecessor projects, as well as the MCC's Training and Development for Farmers (EDA) and Access to Credit for Farmers (ACA) programs, allowed participating farmers to access credit.

- Representatives of the Covelo Foundation and USAID said that in recent years the rural market had a higher level of unmet demand than the urban market.
- Virtually all MFI representatives interviewed cited past Governmental debt forgiveness schemes as a major deterrent to providing credit to the agricultural sector.

1. BACKGROUND

1.1 DEVELOPMENT PROBLEM

In 2003, more than 60 percent of the Honduran population was living in rural areas. Seventy-five percent of rural households fell below the poverty line, encompassing more than 2 million citizens.[1] GDP growth per capita hovered between 0.15 percent and 3.13 percent during 2000-2003.[2]

Agricultural activities represented 23 percent of the country's Gross Domestic Product (GDP) and employed more than 35 percent of the workforce. However, many micro- and small-sized farmers lacked access to affordable credit. Poor financial management and external market forces, including Hurricane Mitch in 1998, led to a serious banking crisis and high interest rates. High collateral requirements effectively barred most micro, small, and medium enterprises (MSMEs) from available loan facilities.[3]

The U.S. Agency for International Development's (USAID) experience in the Honduran MSME sector demonstrated the enormous potential these enterprises have for increasing economic growth and employment. For example, USAID estimated in 2003 that the Honduran forestry sector contributed 25 percent to the Honduran economy. The sector employed over 60,000 people and contributed 5 percent to the economy.[4]

For several years, with support from USAID and others, the José Maria Covelo Foundation (FJMC) had played a leadership role in Honduras in providing credit to micro- and small entrepreneurs (MSEs), primarily in urban areas. FJMC officers had been instrumental in forming the Microfinance Network of Honduras (REDMICROH), and otherwise promoting growth of the sector. The FJMC decided that improving access to credit for farmers was an urgent priority for development. However, the organization lacked hands-on knowledge about agricultural credit products and risks.

1.2 USAID'S RESPONSE

To help the Covelo Foundation realize its full potential to generate economic growth and reduce rural poverty, in 2003 and again in 2005 USAID signed partial credit guarantee agreements with the FJMC, under the auspices of the Agency's Development Credit Authority (DCA). The DCA offers an innovative financing mechanism to stimulate lending from the private sector, instead of providing traditional donor assistance through grant-funded programs. It is a partial credit guarantee (up to 50

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[1] USAID Honduras Action Memo regarding Development Credit Authority (DCA) Loan Portfolio Guarantee (LPG), December 20, 2003.
[2] The MIX Market, http://www.mixmarket.org/en/environment/environment.show.profile.asp?token=&CountryID=hn.
[3] USAID Honduras Action Memo regarding Development Credit Authority (DCA) Loan Portfolio Guarantee (LPG), December 20, 2003.
[4] *Ibid.*

percent) offered to private financial institutions in countries and sectors where local access to credit is limited.

1.3 THE EVALUATION ASSIGNMENT

In 2009, the Office of Development Credit (EGAT/DC) contracted SEGURA/IP3 to carry out a series of impact evaluations of partial credit guarantees to determine whether and how targeted development results were being achieved.

The series of evaluations being undertaken will help EGAT to test a series of development hypotheses related to the guarantees. Illustrative questions include:

- Under what circumstances does a DCA partner continue to lend to a targeted sector without a DCA guarantee?

- Were new borrowers under the DCA guarantee able to secure financing later without a guarantee because they established a credit history with the lending institution?

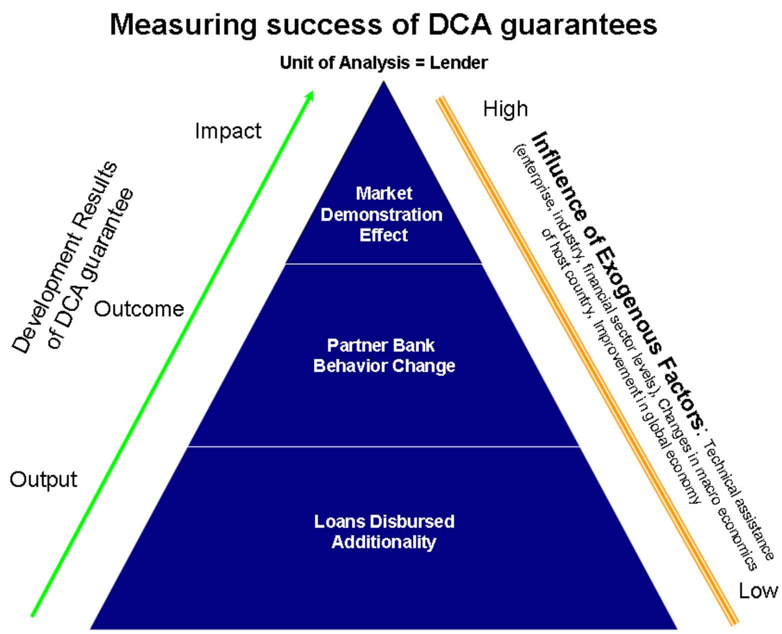
The evaluation in Honduras was carried out in accordance with an Evaluation Framework, developed for the series of investigations noted above. This framework sets forth a series of evaluation questions that investigate development results. These results occur at three levels, as follows (also see Figure 1):

Outputs – the disbursement of loans that have additionality. Additionality is defined as loans that are in new sectors/industries or geographic areas and/or loans that have terms which differ from non-guaranteed loans. In other words at the output level, USAID is interested to know how disbursed loans differ from business-as-usual for the partner lender.

Outcomes – behavior change of the partner financial institution that resulted from using the guarantee. While frequently, this is measured post-expiration of the guarantee, there are instances when lenders are learning as they use the guarantee.

Impacts – changes in the behavior of <u>other</u> financial institutions that can be at least partly attributed to the DCA guarantee, through a market demonstration effect.

FIGURE 1. DCA EVALUATION PYRAMID



This report presents findings and conclusions from an evaluation, carried out in March and April of 2009, of DCA guarantees used by FJMC. Its objective is to determine the impact of the guarantees on FJMC's lending practices.

1.4 EVALUATION METHODOLOGY

The team began in March 2009 by tailoring the evaluation framework mentioned above to fit the Honduran context (see Appendix D). The resulting document, "Evaluation of Honduras Bancovelo DCA Guarantees: Evaluation Framework with Indicators & Interview Questions" (3 April 2009), contains a systematic presentation of evaluation questions with corresponding data sources, data collection methods, a description of the use of evaluation findings and conclusions, interview questions, and corresponding indicators and analysis.

The team used a mix of quantitative and qualitative methods to collect and analyze data from both primary and secondary sources. In March 2009 the team first carried out a desktop analysis. Literature reviewed included:

- Legal agreements for both the 2003 and 2005 guarantees
- Action packages for both guarantees
- Biennial reviews for both guarantees
- Credit review board meeting notes
- Faxes, memos and email exchanges related to DCA guarantee coverage of individual loans
- A credit rating report for the *Fundación Microfinanciera Covelo*

- Final report for the USAID Honduras Microfinance and Banking Support Program (2005).

We also reviewed and began to analyze data relevant to the Covelo Foundation's DCA guarantees from USAID's Credit Monitoring System, an information management system that houses data on utilization of guarantees. The resulting desktop analysis helped the team to identify additional evaluation questions.

The team leader, accompanied by a representative from EGAT/DC during the first week of the mission, visited Honduras from April 13 to 24, 2009. Upon arrival in Honduras the team conducted semi-structured interviews with key stakeholders and others who could provide evidence to support the evaluation. These interviewees included 6 representatives of USAID/Honduras, 4 representatives of U.S. Government-funded programs in Honduras, 7 Honduran Government officials, 3 staff of the Covelo Foundation, 4 representatives of Bancovelo, 11 representatives of Honduran financial and development organizations, and 1 World Bank official. (See Appendix A for a list of persons met.) In addition to working closely with representatives of the Covelo Foundation to obtain relevant data from the institution's information system, the team also collected literature and additional secondary data to support the evaluation.

In addition to the interviews and other field activities, in April-May 2009 the team also conducted an email-based survey of members of the Microfinance Network of Honduras (REDMICROH). This survey allowed us to reach a broader set of the members of the Network than was possible through in-person interviews. For a copy of the survey form please see Appendix B. Results of the field visit, interviews, data collection, and survey are discussed in the body of the report below.

1.5 DATA LIMITATIONS

At USAID's request, the evaluation team did not speak with Covelo's borrowers. Therefore, the evaluation does not address the borrower's perspective, nor does it assess the impact of Covelo loans on the borrowers.

The evaluation took place before the completion of the guarantee periods, which means that it is a little early to evaluate impact of the guarantees on the microfinance sector in Honduras. Impacts resulting from demonstration effects, increased competitiveness of the Covelo Foundation, and others will not likely be fully realized until market forces catch up to the guarantees' outcomes.

On a related note, the survey we conducted of REDMICROH members drew a low response rate (only five organizations responded). Therefore, while interesting as individual responses, the survey data are not representative of REDMICROH members as a whole.

The present document proceeds as follows: following the present Background, we summarize key aspects of the DCA agreements with the Covelo Foundation and discuss findings and conclusions regarding the outputs, outcomes, and impacts of the credit guarantee activity.

2. USAID'S DCA AGREEMENTS WITH COVELO FOUNDATION

As noted above, USAID's partner in the DCA agreements under study is the José María Covelo Foundation of Honduras. This entity (FJMC or "the Covelo Foundation") was established as a private development organization (OPD) in 1991; it began to offer direct credit as a microfinance institution (MFI) in 1995. Since then the Covelo Foundation and its spin-off entities have gone through a complicated institutional evolution, as the size of its portfolio has grown and in response to changes in the enabling environment.[5] A major change was the establishment of Banco Popular Covelo (Bancovelo), a commercial bank licensed in January 2008.[6] Later that year the FJMC sold most of its loan portfolio to Bancovelo; however it retained ownership of that part of its portfolio that carried the DCA guarantees, as well as loans in default. At present (May 2009) the loans that carry the DCA guarantee are still owned by the Covelo Foundation, but they are administered by Bancovelo. Because these organizations are closely related, for evaluation purposes we generally treat them as one entity.

USAID and the Covelo Foundation signed legal agreements on 9 September 2003 and 28 September 2005.[7] The 2005 agreement generally followed the objectives and parameters of the 2003 agreement (see Table 1). Both are for loan portfolio guarantees that utilize the DCA. Both agreements sought (and seek) to increase access to credit by qualifying borrowers. Both define "qualifying borrowers" as micro- and small-sized enterprises (MSEs), with micro-enterprises defined as having between one and ten full-time employees and small-enterprises employing between 11 and 25 persons.[8] Likewise both agreements target the same qualifying projects or sectors:

- non-traditional agriculture or agro-industry,
- wood products,
- specialty coffee, and
- light manufacturing.[9]

The agreements do not specify the emphasis that was to be given to any of these sectors; this was left up to the Covelo Foundation and to the market. At the same time both agreements seek to help the Covelo Foundation "expand and move up-SEGmarket" (see discussion below).

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5 For a timeline of major institutional developments, see Appendix C.

6 The Covelo Foundation is one of the bank's major shareholders. The FJMC's General Manager indicated that this organizational development was not a result of the DCA guarantee facility.

7 Guarantee agreements are accompanied (generally preceded) by action memoranda that provide additional insights as to the objectives of the guarantee programs. However the guarantee agreement represents the sole legal agreement between USAID and the partner bank. These agreements do not incorporate by reference the action memoranda; in fact a representative (2005) agreement states that "the [present] Agreement constitutes the entire agreement between the Parties concerning the subject matter of the Agreement and supersedes any prior understanding or written or oral agreement" (Section 12.10).

8 In 2003, this represented a change from the original action memorandum, which targeted "micro, small *and medium* enterprises" (italics added). In 2005 both the action memorandum and the guarantee agreement focused on MSEs.

9 Likewise in 2003 the action memorandum listed somewhat different qualifying projects than were reflected in the final guarantee agreements. In 2005 the qualifying projects were the same in both documents.

TABLE 1. DCA GUARANTEE AGREEMENTS WITH THE COVELO FOUNDATION: OBJECTIVES

Parameters	2003 DCA	2005 DCA
Action Memoranda*		
USAID Strategic Objectives (SOs)	SO1 Competitive market-led growth improved in target areas.	SO 522-022 Economic freedom: open diversified expanding economies.
Other objectives *"The DCA guarantee will…"*	(1) "…significantly increase the abilities of [qualifying borrowers] in the targeted sectors to expand their revenues in a variety of markets." (2) "facilitate microfinance institutions' (MFIs') ability to **expand and move up-market**." (3) "[contribute to] increased levels… of investment." (4) "[contribute to] promotion and participation of the Honduran economy in world trade."	(1) "… facilitate the increased provision of loans to [qualifying borrowers] in productive sectors in rural areas… and other traditionally under-served areas… and thus contribute significantly to income generation, poverty reduction, and national economic performance." (2) "… facilitate Covelo's ability to expand and move up-market."
Guarantee Agreements*		
Qualifying borrowers	Micro- and small-sized enterprises (MSEs)** that: - are established under law - are creditworthy - have the potential for competitiveness in Honduras or international markets	*[Same as 2003]*
Qualifying projects (sectors) ***	- **Non-traditional agriculture** or agro-industry - Wood products - Specialty coffee - light manufacturing	*[Same as 2003]*

*Notes: * See footnote 3 for relation of action memoranda to guarantee agreements.*
***The Guarantee Agreement defines micro-enterprises as having 1-10 employees, and small-sized enterprises as having 11-25 employees.*
**** The Agreement further lists certain sectors as excluded (e.g., military-related), and several as requiring prior written approval from USAID (e.g., pesticides).*
*Sources: Action Memos & Guarantee Agreements for corresponding years. For terms in **bold**, see Table 3.*

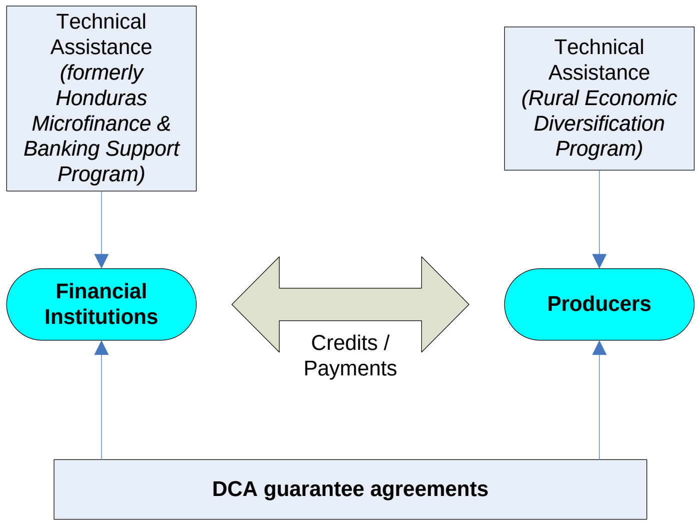
We looked to the background action memoranda to clarify two of these terms (those shown in bold in Table 1), starting with "non-traditional agriculture." Interviews with stakeholders indicated that various definitions of this term are possible. However, as shown in Table 2, the action memoranda clarified that the DCA guarantee was intended to be used in close conjunction with a complementary USAID program, i.e., Rural Economic Diversification (RED). The idea was that the RED program would provide technical assistance to help farmers produce non-traditional cash crops, while the DCA guarantee would help those beneficiaries obtain financing. The current director of the USAID-supervised RED Program defines non-traditional agriculture as "everything except rice, beans, corn, coffee, and sugar cane" – a definition that has the virtue of operational clarity.

TABLE 2. COVELO FOUNDATION DCA GUARANTEES: INTERPRETATION OF KEY TERMS

Key Terms Used in DCA Guarantees with Covelo	Clarifying Language in Action Package	Therefore…
Non-traditional agriculture – one of several "qualifying projects" or sectors. Both Guarantee Agreements use the phrase.	"Intended beneficiaries [i.e., borrowers from the Covelo Foundation] will receive USAID technical assistance through the Mission's contractors in the agricultural sector working with growers of non-traditional crops…." (p. 2 of 2005 Action Memorandum.)	USAID's definition of "non-traditional agriculture" should be reflected in the working definition used by FINTRAC, the contractor for USAID's RED Program. Per the Director of that program, "non-traditional agriculture" is "everything except rice, beans, corn, coffee, and sugar cane."
Expand and move up-market – one of several objectives for the partner financial institution to achieve via the DCA. Both Action Memoranda use the phrase.	DCA credit assistance will help "the Covelo Foundation, [which] has a limited capital base, … extend its portfolio of loans to allow for larger loan sizes with longer maturities to its increasing small business clientele…." At the same time, "the DCA guarantees will significantly increase the abilities of MSMEs… to expand their revenues…" (pp. 1-2, and p. 2 of Attach. 1, of 2003 Action Memorandum).	The present report assumes that two definitions of "expanding and moving up-market" are valid: (1) To allow Covelo to offer larger loans with longer maturities to the qualifying borrowers. (2) To help borrowers expand their revenues.

To provide further background: when the initial agreement was signed in 2003, most of the sectors noted as qualifying for DCA coverage also had a counterpart technical assistance component for producers (see Figure 2). At the same time that the RED Program supported non-traditional agriculture, other USAID activities promoted the development of a specialty coffee market, and the sustainable production of wood products on lands in or adjacent to national forests and parks. Likewise as shown USAID also assisted financial institutions (primarily MFIs), via the Honduras Microfinance and Banking Support Program, which ended in 2005. The Mission's goal was to maximize benefit by promoting synergy between the DCA agreements and these various programs. While mid-decade budget cuts curtailed this scheme, the RED Program has continued to provide technical assistance to farmers (albeit on a more modest scale than originally intended). Recently as well programs funded by the U.S. Millennium Challenge Corporation (MCC) have effectively picked up where earlier USAID activities left off. MCC programs assist financial institutions (via the Farmer Access to Credit [ACA] program), and producers (via the Training and Development for Farmers [EDA] program).

FIGURE 2. CONCEPTUAL SCHEME OF USAID/HONDURAS ASSISTANCE TO MICROCREDIT & AGRICULTURAL SECTORS



Source: USAID/Honduras, "Modelo de Transición", April 2009.

The 2003 action memorandum also clarified the phrase "expand and move up-market." As shown in Table 2, this involves both: (i) allowing the Covelo Foundation to offer larger loans with longer maturities to the qualifying borrowers, and (ii) helping borrowers expand their revenues. We generally follow these definitions below.

While the 2003 and 2005 guarantee agreements embody generally similar objectives, they also reveal relatively minor differences. The 2003 action memorandum emphasized helping importers and exporters, while the 2005 memorandum focused on assisting rural entrepreneurs and reducing poverty. This change reflected the somewhat different emphases of a new USAID strategic framework in Honduras.[10] A further difference was that, in 2003, USAID not only sought to help the Covelo Foundation move up-market – it also tried to assist two banks reach further *down*-market, i.e., expand their lending to SMEs.[11] In 2005 USAID only worked with the Covelo Foundation on a new DCA agreement; the Mission did not negotiate with other MFIs at that time. In other words, the 2003 scheme articulated a broader vision of market development than was explicitly reflected in the 2005 documents.

With regard to other parameters, the 2005 guarantee agreement has a higher total guarantee ceiling than the 2003 DCA agreement. The maximum loan portfolio amount is for USD 3 million, with 50 percent covered by the guarantee. General parameters of the two guarantees are as follows:

[10] As noted in the Evaluation Framework, evaluation of the DCA guarantees vis-à-vis the Mission's objectives lies outside the scope of the present study.
[11] The Action Memorandum of 20 December 2003 included two other potential partners in Honduras besides the Covelo Foundation: Banco Atlántida and Banco Grupo El Ahorro Hondureño. Review of experiences with those banks lies outside the scope of the present assignment.

TABLE 3. DCA AGREEMENTS WITH COVELO FOUNDATION: GENERAL PARAMETERS*

Item	2003 DCA	2005 DCA
Max. portfolio amount / Max. cumulative disbursements	USD 1,000,000	USD 2,000,000
Guarantee ceiling (max. USAID liability)	USD 500,000	USD 1,000,000
USAID guarantee percentage	50 %	50 %
Period for placing loans under coverage	9 Sept 2003 - 8 Sept 2009	28 Sept 2005 - 31 Mar 2012
Coverage expiration date	8 Sept 2010	27 Sept 2012

** Values are the equivalent in Lempiras of U.S. dollars (USD) shown.*

Fees are proportionately the same for both guarantees:

TABLE 4. DCA GUARANTEE AGREEMENTS WITH COVELO FOUNDATION

Fee Type	2003 DCA	2005 DCA
Origination (% of guarantee ceiling)	1.0 %	1.0 %
Utilization (% per annum of avg. outstanding principle guaranteed)	0.5 %	0.5 %

The two DCA agreements contain only one restriction as to the terms and conditions of the guaranteed loans offered to the qualifying borrowers: they limit the "maximum loan amount to any one borrower" to USD 100,000 (see Table 5). While this condition might seem to run contrary to the objective of helping Bancovelo "move up-market," in reality in no way did it constrain lending patterns (see below). The agreements are silent (i.e., they permit flexibility) as to other loan terms and conditions, including tenor, purpose (e.g., short-term working capital, long-term investment), interest rate, and so on. The policy here is, in the words of the 2003 agreement, "for loans [to] be made at interest rates and on terms consistent with those generally prevailing among private commercial lenders in the borrower's country" (Section 2.02(c)).

TABLE 5. DCA GUARANTEE AGREEMENTS WITH COVELO FOUNDATION: LOAN TERMS

Loan Terms	2003 DCA	2005 DCA
Max. loan amount to any one borrower*	USD 100,000	USD 100,000
Tenor	n.a.**	n.a.**

** Represents cumulative loan amount. Values are the equivalent in Lempiras of U.S. dollars (USD) shown.*

*** Except as constrained by period of coverage; see Table 1.*

3. FINDINGS & CONCLUSIONS

As noted above, findings and conclusions are organized into seven questions, marshaled into three levels: (1) outputs, (2) outcomes, and (3) impacts.

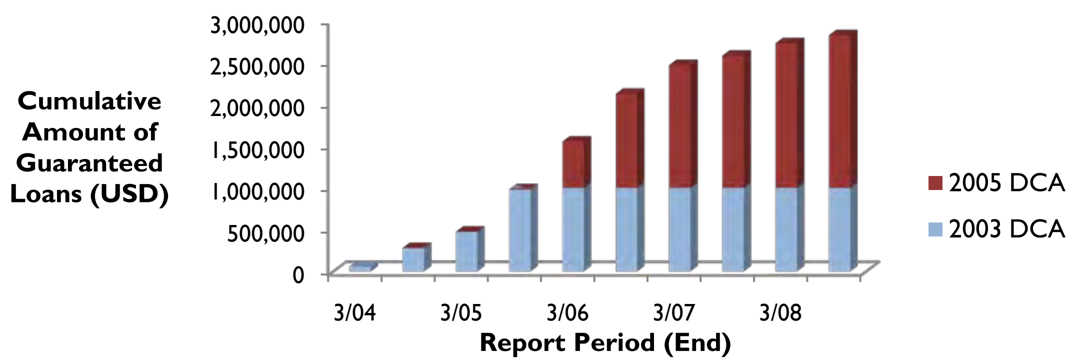
3.1 OUTPUT LEVEL

Question 1: Loans disbursed
Did the Covelo Foundation use the guarantee facility? How much local private capital was mobilized? What potential market(s) did the DCA guarantee help open for the Covelo Foundation?

FINDINGS

The Covelo Foundation has made extensive use of both DCA guarantees. As shown in Figure 3, the Foundation quickly began to use the DCA guarantee authority after it was established in September 2003, and by September 2005 it was reporting 98 percent cumulative utilization of its USD 1,000,000 maximum loan amount.[12] That same month the MFI signed its second DCA guarantee, which allowed for up to USD 2,000,000 in covered loans. Two years later (in September 2007) it was reporting near-total cumulative utilization of the first facility, and 79 percent cumulative utilization of its second facility. Since then utilization of the second facility has increased more slowly. As of 30 September 2008, the Foundation had utilized 99.99 percent of its first (2003) DCA maximum authorized amount, and 91.23 percent of its second (2005) maximum. The Lempira (L) 6.2 million in guaranteed loans outstanding at that date represented 10.9 percent of the Covelo Foundation's entire remaining portfolio (L. 57.4 million).[13]

FIGURE 3. CUMULATIVE VOLUME OF LOANS WITH DCA GUARANTEE

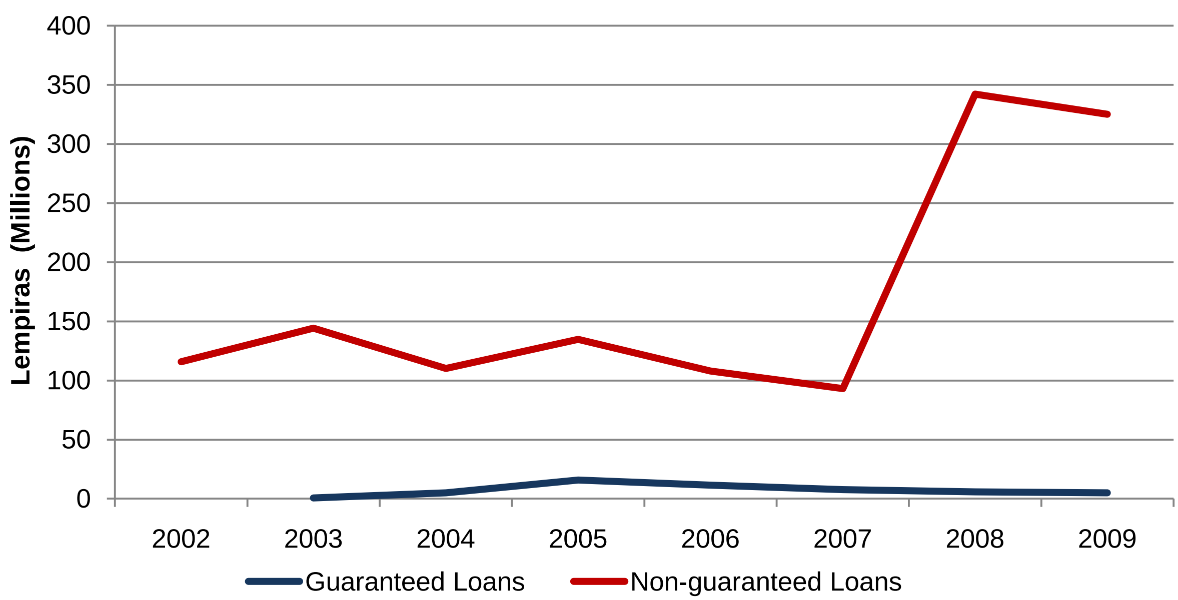


[12] Loan limits or maximums stand at twice the ceiling level of the (50 percent) coverage provided by the DCA guarantee. Note that the DCA guarantee facility does not revolve. In this and the following discussion, we generally use the word "loan" interchangeably with "credit."
[13] For comparison purposes, at that date Bancovelo had an active portfolio of L. 953.9 million.

The DCA guarantee facilities have mobilized local resources. The 2003 DCA involved an obligation of USD 25,600, while the second obligated USD 115,200 in U.S. Government resources, for a total obligation of USD 140,800. As of 30 September 2008 those resources had leveraged the equivalent of USD 2,824,669 in loans, for a leveraging of 20 to 1. Further, as of September 2008 USAID had only received USD 16,737 in claims net of recoveries for the two DCA facilities. When the two facilities close, remaining obligated resources will revert to the U.S. Government.

Guaranteed loans targeted two general sectors: agriculture/agroindustry and microcredit generally. As shown in Figure 4 below[14], the value of guaranteed loans to these two sectors represented between 0.5 and 10.4 percent of the total value of Covelo (Foundation and Bancovelo) loans to these sectors.

FIGURE 4. VALUE OF COVELO GUARANTEED AND NON-GUARANTEED LOANS TO MICROCREDIT AND AGRICULTURE, DECEMBER 2002 TO MARCH 2009



Source: Covelo Foundation, May 14, 2009. Includes both Covelo Foundation and Bancovelo lending.

Table 6 shows the cumulative number of guaranteed loans that the Covelo Foundation has made as of 30 September 2008 under both facilities – 844. These figures do not represent loans to unique borrowers. In fact 53 persons received three or more guaranteed loans, and three borrowers even received ten or more such guaranteed credits.[15] Guaranteed loans varied in size from $158 to $21,345. In 2008 the average size of a guaranteed loan was $ 2,675.[16]

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[14] In June 2008, the Covelo Foundation sold its portfolio to Bancovelo, but retained the DCA guaranteed loans. The non-guaranteed loan figures for December 2008 and March 2009 in Figure 4 include the Bancovelo portfolio.

[15] A small number of these credits may have been renewed. USAID allows renewals of guaranteed loans as long as it does not exceed the maximum loan amount of USD 100,000 for each borrower.

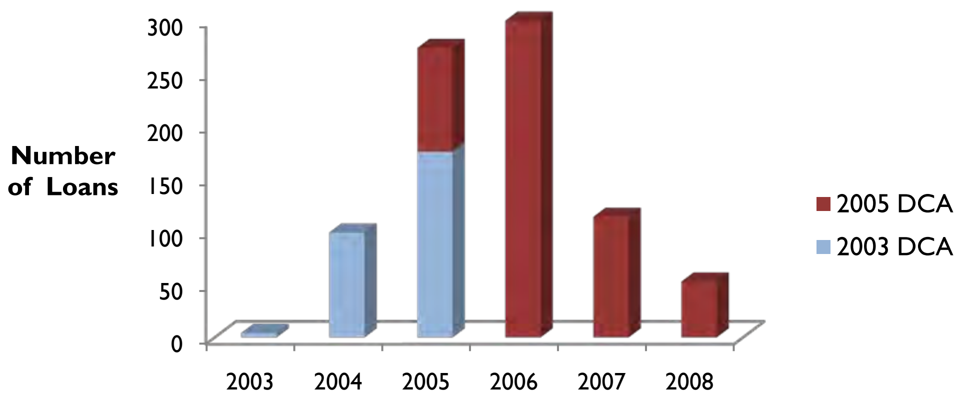
[16] For a comparative discussion of trends over time in loan sizes with and without the guarantee facility, see below.

TABLE 6. CUMULATIVE NUMBER OF LOANS WITH DCA GUARANTEE

DCA Agreement	3/04	9/04	3/05	9/05	3/06	9/06	3/07	9/07	3/08	9/08
2003	8	61	132	269	279	279	279	279	279	279
2005	--	--	--	--	166	347	430	475	534	565
Total	**8**	**61**	**132**	**269**	**445**	**626**	**709**	**754**	**813**	**844**

The annual number of *new* loans made covered by the guarantee peaked in 2005 and 2006 (see Figure 5). In those years the Covelo Foundation signed (respectively) 274 and 300 new loans that carried the partial credit guarantees. The number of new loans guaranteed dropped off in 2007 and 2008. (For discussion of the operational reasons for this trend, see Question 3, below.)

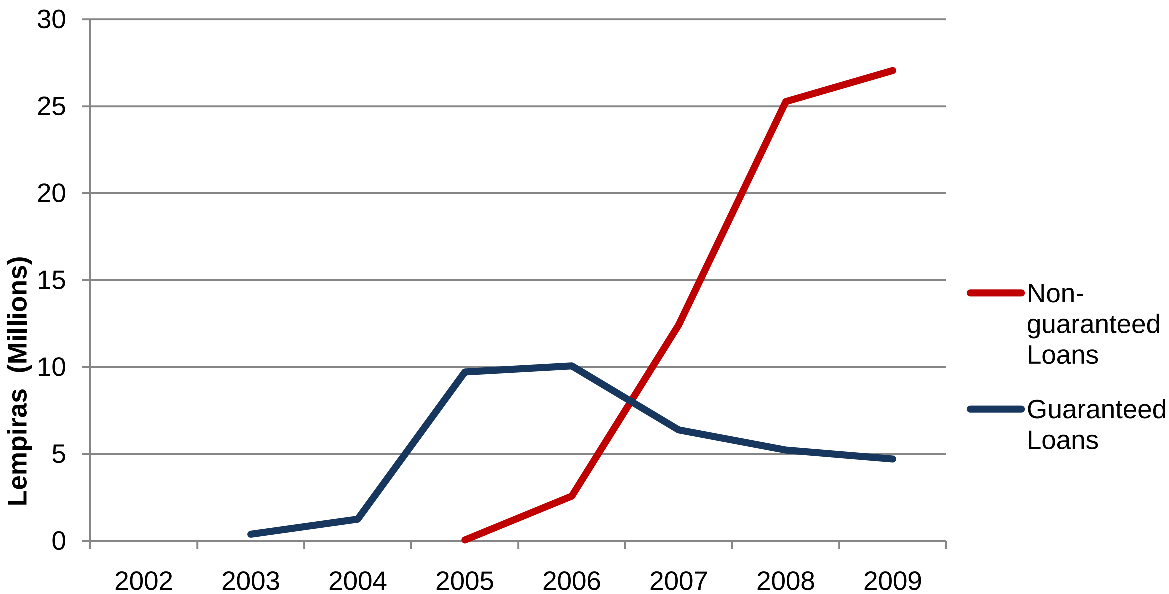
FIGURE 5. NUMBER OF NEW LOANS WITH DCA GUARANTEE: BY YEAR



Lending by the Covelo Foundation to the agricultural and agro-industry sector has grown under the DCA.[17] In 2003, prior to the signing of the first guarantee agreement, the Foundation's lending in this area was virtually zero. By 31 December 2006, the Foundation had an outstanding balance of L. 12,646,000 in guaranteed loans to micro- and small-scale agricultural and agro-industry producers. As of 31 March 2009, outstanding guaranteed loans to this sector represented L. 4,198,271, approximately USD 222,248.[18] This represented about 8.5 percent of the FJMC's entire portfolio of L. 49.6 million at that time. In addition, while the value of guaranteed loans decreased over time as Covelo reached its utilization limit, the value of *non*-guaranteed agricultural loans grew sharply (see Figure 6).

[17] Throughout the present document, unless indicated otherwise we translate both *agricultura* and *agropecuario* as "agriculture" or "agricultural."
[18] As of 30 April 2009, one U.S. dollar (USD) is worth about L. 18.89.

FIGURE 6. VALUE OF COVELO AGRICULTURE PORTFOLIO, DECEMBER 2002 TO MARCH 2009



Source: Covelo Foundation, May 14, 2009. Data for each year are for December, except for 2009, for which data were available through March.

Looking at these loans more closely: most – but not all – of the DCA guarantees supported loans to non-traditional agriculture and agro-industry.[19] As shown in Figure 7, two-thirds (66.7 percent) of the 279 loans that carried the DCA guarantee under the 2003 agreement financed agriculture (non-traditional) or agro-industry.[20] Of these 186 loans, most (107) were in agriculture, 28 for livestock, eight for pigs and four for poultry – all defined according to our earlier definition as non-traditional. Another 39 were for agro-industrial uses. Such financing continued under the 2005 agreement (see Figure 8. Non-traditional crops such as eggplant, sweet potatoes, cabbage, African palm, and other horticultural products, along with agro-industry, represented 71.2 percent of total loans made under the 2005 facility. However 65 of the loans guaranteed under the 2005 agreement (11.5 percent of the total) were for *traditional* crops – nearly all for rice planting and production. (For discussion of the operational reasons for this development, see Question 3, below.)

[19] As noted above, "non-traditional" is here defined as everything except rice, beans, corn and sugar cane. (A fifth crop, coffee, defined as "traditional" per above, is discussed separately below.)

[20] Data available in the CMS and the Foundation's electronic data system did not always provide sufficient information as to whether a particular agricultural use was traditional or non-traditional. When in doubt we assumed "non-traditional." Further investigation (e.g., contacting individual borrowers) lay outside the scope of the present investigation.

FIGURE 7. NUMBER OF LOANS WITH DCA GUARANTEE, BY USE IN 2003

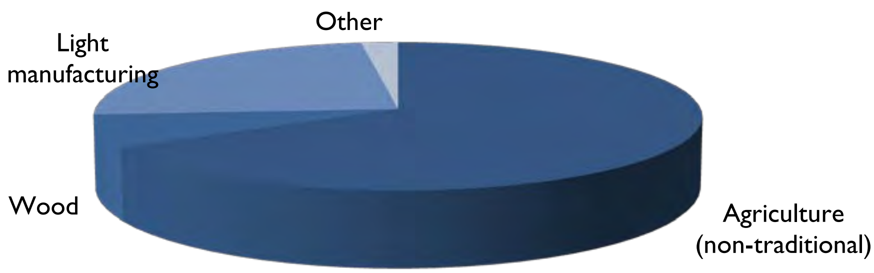
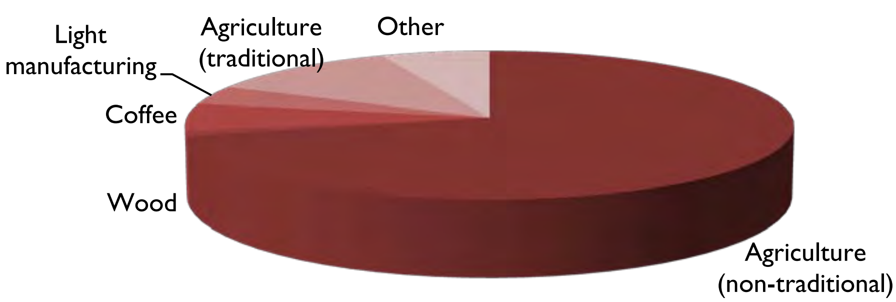


FIGURE 8. NUMBER OF LOANS WITH DCA GUARANTEE, BY USE IN 2005



As of 30 September 2008. Source: CMS and author's calculations.

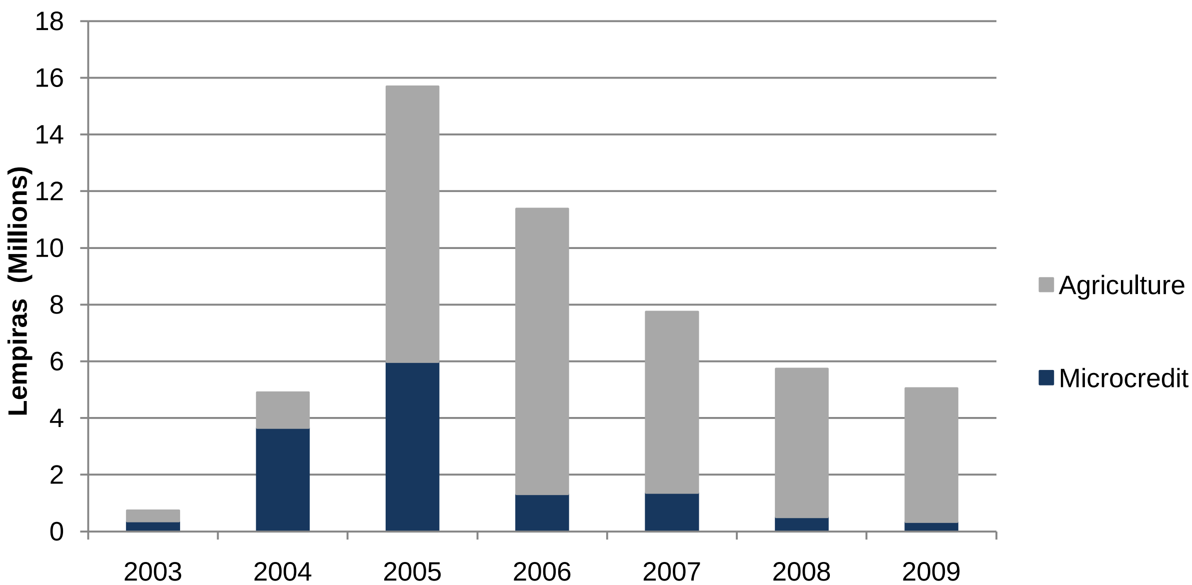
To a modest degree, the DCA guarantees also helped the Covelo Foundation provide credit to the coffee sector. As noted above, while in general coffee is considered a "traditional" market in Honduras, USAID specifically targeted "specialty coffee" under its DCA guarantees. While the Foundation did not make any loans to the coffee sector under the 2003 guarantee, the 2005 DCA facility has guaranteed some 33 credits to this sector (5.8 percent of the total number of credits; see Figure 8. We could not determine from available data whether these credits supported the production of "specialty" or traditional coffee.

The Covelo Foundation has also used the DCA guarantees to support the financing of light industry: 67 credits under the 2003 guarantee (24.0 percent of the total; see 7.a), and 23 loans under the 2005 agreement (4.1 percent of the total). This, however, was not a new sector for the

Foundation. Finally a small number of guaranteed credits financed wood products – another targeted sector.

Reflecting the shift in lending pattern between the two DCA guarantee periods, noted above, agriculture absorbed most of the Covelo Foundation's loans guaranteed under the 2005 agreement (see Figure 9 below). As of March 31, 2009, agriculture represented 93 percent of the Covelo Foundation's outstanding portfolio of loans that bore the DCA guarantee. Given this overwhelming sectoral focus, the following discussion focuses primarily on the targeted sectors of (mostly non-traditional) agricultural and agro-industrial production.

FIGURE 9. VALUE OF GUARANTEED LOANS, BY CLASSIFICATION



Source: Covelo Foundation, May 2009. Data for each year are for December, except for 2009, for which data were available through March.

CONCLUSIONS

The Covelo Foundation has achieved additionality by using the DCA guarantee facilities to enter a new market: agricultural credit. The 2005 DCA agreement was instrumental in building Covelo's portfolio of agriculture loans. Most guaranteed loans conformed to the objective of supporting non-traditional agriculture, wood, and light manufacturing. The Covelo Foundation has highly leveraged guarantee resources obligated by the U.S. Government, at a ratio of 20 to 1.

Question 2
Did the Foundation's use of the DCA guarantee improve access to credit for the target sectors? How did the DCA guarantees fit into Bancovelo's ongoing strategy? Did characteristics of guaranteed loans differ from other loans in ways that improved access? Did guaranteed loans correspond to other initial objectives and parameters?

FINDINGS

Access to Credit

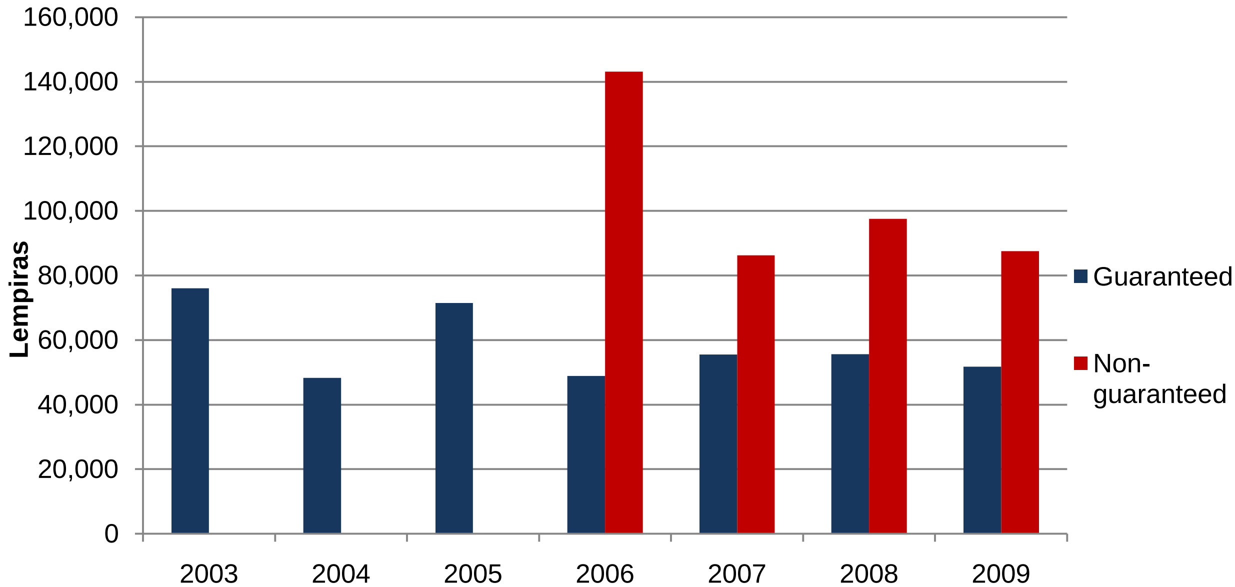
To determine whether and to what extent the DCA guarantees encouraged Bancovelo to increase access to credit, we examined a variety of measures of credit access: loan size, loan tenor, and interest rate. We compared guaranteed and non-guaranteed loan data by classification because Covelo's agricultural lending and microcredit have different properties that affect lending strategies and loan terms.

Agriculture

The figures below compare the characteristics of average loans in FJMC's agricultural portfolio, with and without the DCA guarantee. On average, loans that carry the DCA guarantee are smaller and of shorter duration than loans that do not carry this guarantee. An official with Bancovelo explains that the reason for this difference lies in FJMC's strategic use of the DCA facility to guarantee loans where the farmer is not able to offer real estate as collateral, but can only offer other assets (e.g., a vehicle), or has a co-signer to the loan.[21] Even with the partial guarantee the Covelo Foundation considers these loans as higher risk; therefore these loans are generally smaller and of shorter tenor. In addition, a farmer or an agro-industrial borrower with title to property is generally more likely to seek resources for longer-term investments (e.g., to improve a storage facility) than would a poorer farmer who does not own real estate that can be used as collateral, and who would be more interested in financing one crop cycle.

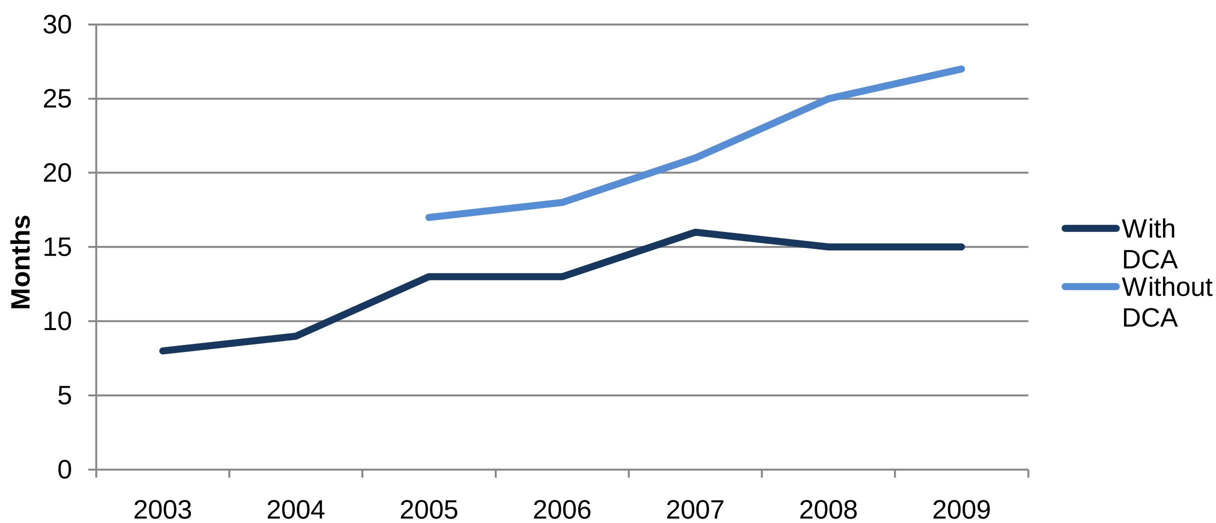
[21] For further background on this strategic choice, see Question 3, below.

FIGURE 10. AVERAGE SIZE OF GUARANTEED AND NONGUARANTEED AGRICULTURE LOANS



Source: Covelo Foundation, May 2009. Data for each year are for December, except for 2009, for which data were available through March.

FIGURE 11. AVERAGE TENOR OF GUARANTEED AND NONGUARANTEED AGRICULTURE LOANS



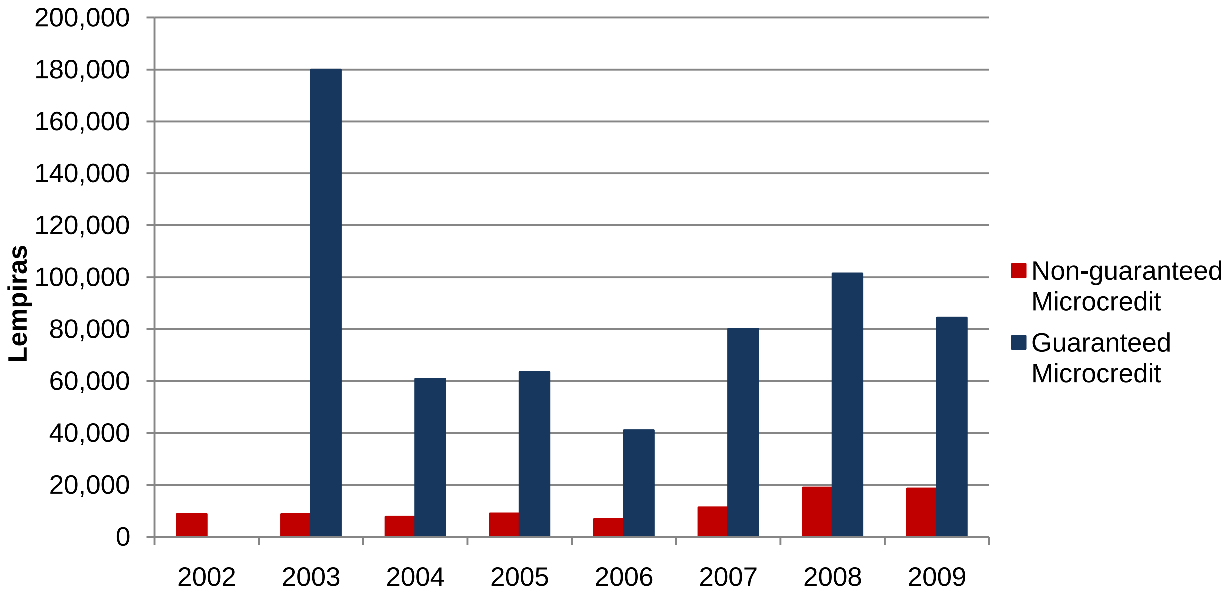
Source: Covelo Foundation, May 2009. Data for each year are for December, except for 2009, for which data were available through March.

Interest rates are roughly similar with and without the DCA guarantee, averaging 21 percent between 2003 and 2009. As of March 2009, the rate for guaranteed loans was 19 percent, while nonguaranteed loans carried an average 21 percent interest rate.

Microcredit[22]

The figures below compare the average size, interest rates and tenor for microloans, with and without the partial credit guarantee. In general, the microloans that carry the DCA guarantee are larger, have a longer tenor, and carry a lower interest rate. An official with Bancovelo explained that the Covelo Foundation does not use the credit guarantee for its smallest microloans for working capital. He said that the FJMC had (and still has) a large number of microloans for as little as $50, with a tenor of only four to six months. Due to relatively high transaction costs, the FJMC may offer such microloans at annualized interest rates of 40 percent or more. In keeping with the intent of the guarantee agreement, the FJMC uses the DCA facilities to make larger and longer-term loans, not to guarantee small working capital loans.

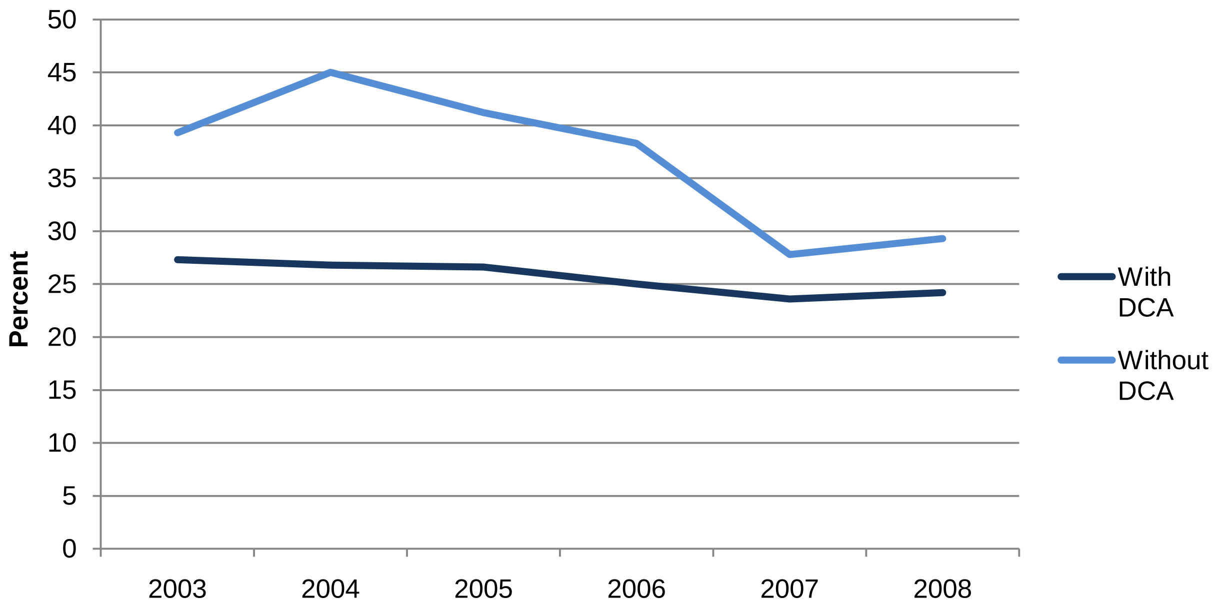
FIGURE 11. AVERAGE SIZE OF GUARANTEED AND NONGUARANTEED MICROLOANS



*Note: *For December of year indicated except 2009, for which data were available through March. Does not include agricultural lending.*
Source: Covelo Foundation/Bancovelo, May 2009.

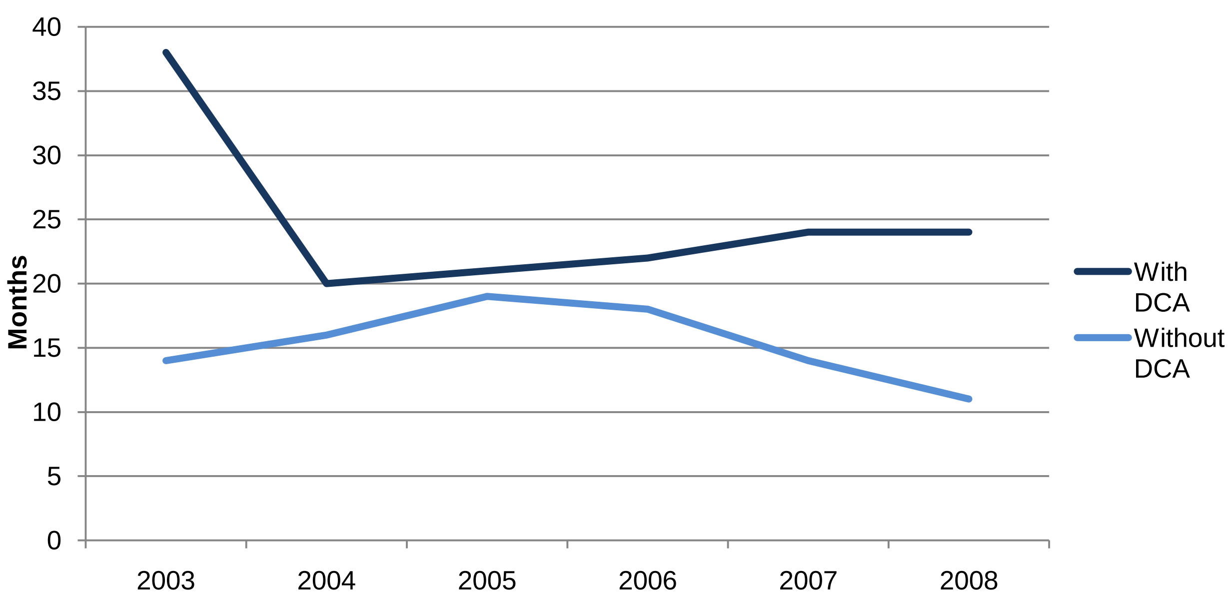
[22] Covelo defines a microloan as a loan under L. 150,000 (approx. $8,100).

FIGURE 12. AVERAGE INTEREST RATES OF GUARANTEED AND NONGUARANTEED MICROLOANS



*Note: *For December of year indicated. Does not include agricultural lending.*
Source: Covelo Foundation/Bancovelo, May 2009.

FIGURE 13. AVERAGE TENOR OF GUARANTEED AND NONGUARANTEED MICROLOANS (MONTHS)



*Note: *For December of year indicated. Does not include agricultural lending.*
Source: Covelo Foundation/Bancovelo, May 2009.

When we consolidate agricultural and microcredit lending together, we see that, on average, the interest rates at which the Covelo Foundation offers both guaranteed and non-guaranteed loans have generally declined during the period of the DCA guarantee. As shown in the table below, the average interest rate on guaranteed loans offered by the Covelo Foundation dropped steadily from 2004 to 2007, then rose slightly in 2008. This movement parallels changes in average lending interest rates in Honduras. More significantly, however, the *spread* between the FJMC's guaranteed lending, and the average rates for all domestic lending, *fell* sharply during the period: from 690 basis points in 2004 to only 230 basis points in 2008.[23] Stakeholders surmise that this decline, a positive development, is due primarily to increased competition among MFIs that make loans to micro- and small entrepreneurs. However this benefit has only accrued to some of those who borrowed from the Covelo Foundation. In fact nearly three fourths (74.5 percent) of the entrepreneurs who borrowed under the 2005 guarantee agreed to pay a 22 percent interest rate—the same median interest rate as under the 2003 DCA agreement. The Covelo Foundation does not generally lower interest rates for repeat borrowers who have established successful credit histories.[24]

TABLE 7. LENDING INTEREST RATES: COVELO FOUNDATION LOANS WITH DCA GUARANTEE VS. HONDURAS (2004-2008)

Item	2004	2005	2006	2007	2008
Covelo Foundation w/ Guarantee	26.8 %	23.6 %	22.4 %	18.5 %	19.3 %
Honduras*	19.9 %	18.8 %	17.4 %	16.6 %	17.0 %
Spread (Basis Points)	*690*	*480*	*500*	*190*	*230*

Sources: Covelo Foundation: CMS. Honduras: Economist Intelligence Unit (EIU), Honduras Country Report, February 2009, p. 12. 2004-2007, actual; 2008, estimate. Figures represent average "lending interest rate."

The Covelo Foundation's Strategy

The Covelo Foundation's strong sectoral focus as shown in loan data, along with interviews with Foundation executives, reveal that the microfinance institution had a clear strategy for using the DCA facility: to reduce risk while it entered the agricultural lending market. The MFI's General Manager explained that the Foundation traditionally had played a leadership role in the microfinance sector in urban areas.[25] Several years ago, however, he concluded that microfinance lending in urbanized areas was relatively well advanced, while rural (and particularly agricultural) lending was lagging; hence the guarantee agreements with USAID in support of this new strategic focus for the Foundation. Loan officers then used the facility to mitigate the risk of lending to the (then-unfamiliar) agricultural sector.

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[23] Financial institutions almost always charge a higher interest rate for MSEs than they do for regular borrowers, due to greater perceived risk, relatively higher transaction costs due to unfamiliarity and smaller loan sizes, and so on. For additional discussion of broad trends that may have affected interest rates charged by the financial and banking sectors in Honduras in recent years, see Section 3.4, below.

[24] Sometimes, however, the Foundation will slightly reduce interest rates after borrowers have paid off a portion of their debt.

[25] In fact the sector's membership organization, the Microfinance Network of Honduras [REDMICROH] originally was known as "REDCOVELO."

The strategic use of the DCA as articulated by the FJMC's officers and described above is consistent with the Covelo Foundation's Strategic Plan 2006-2010. This document includes a general objective of developing new "products and services that are competitive, innovative, specialized and diversified, and that satisfy market demand" (p. 20). While the document does not go to the level of mentioning specific target markets such as agriculture-sector lending, the Covelo Foundation's use of the credit facility has worked towards this general objective.[26]

Other Objectives and Parameters

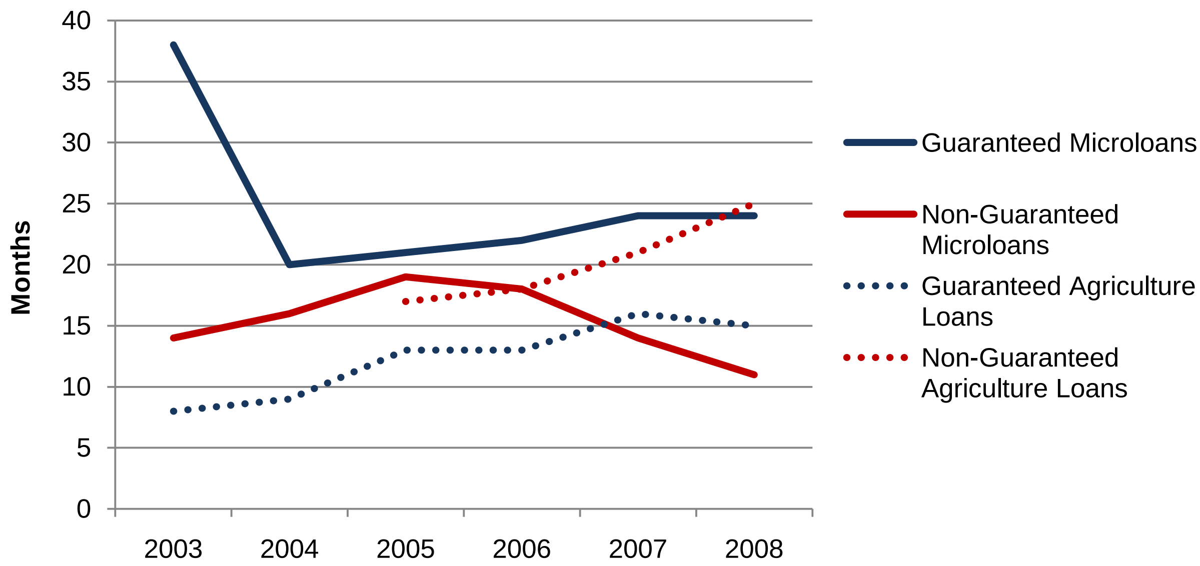
As noted above, USAID expected that access to affordable credit made possible by the DCA guarantees would contribute to expanded revenues on the part of the micro- and small entrepreneurs who borrowed. To help assess whether this effect did in fact occur, we first identified the 53 individuals who (as noted above) had received at least three loans from the Covelo Foundation with the DCA guarantee. We then were able to obtain income and asset data on a random subset of nine of those persons, 17 percent of the total.[27]

On average, persons in this sample reported increases in annual income in recent years of 46.4 percent. This tendency is paralleled by average increases (between first and last loans) in the reported value of borrowers' total assets of 58.4 percent.

A second overall objective for the loan guarantee program with Covelo was to "facilitate Covelo's ability to expand and move up market," meaning larger loan sizes with longer tenors. As discussed above, guaranteed microloans had longer average tenors than the nonguaranteed variety, while guaranteed agriculture loans were mostly shorter in duration. However, between 2005 and 2008, the average tenor of nonguaranteed agriculture loans grew steadily and finally exceeded the average tenor for guaranteed microloans (see Figure 14 below).

[26] Institutional events summarized in Appendix C have largely superseded the strategic direction set forth in this plan. For further discussion of the current plans of the Covelo Foundation and Bancovelo in this sector, see Question 5, below.
[27] Data are from Bancovelo's and the Covelo Foundation's information system, and represent self-reporting by clients at the time of their first and last applications for loans that carried the DCA guarantee. Of the total sample, the following analysis excludes top and bottom outliers.

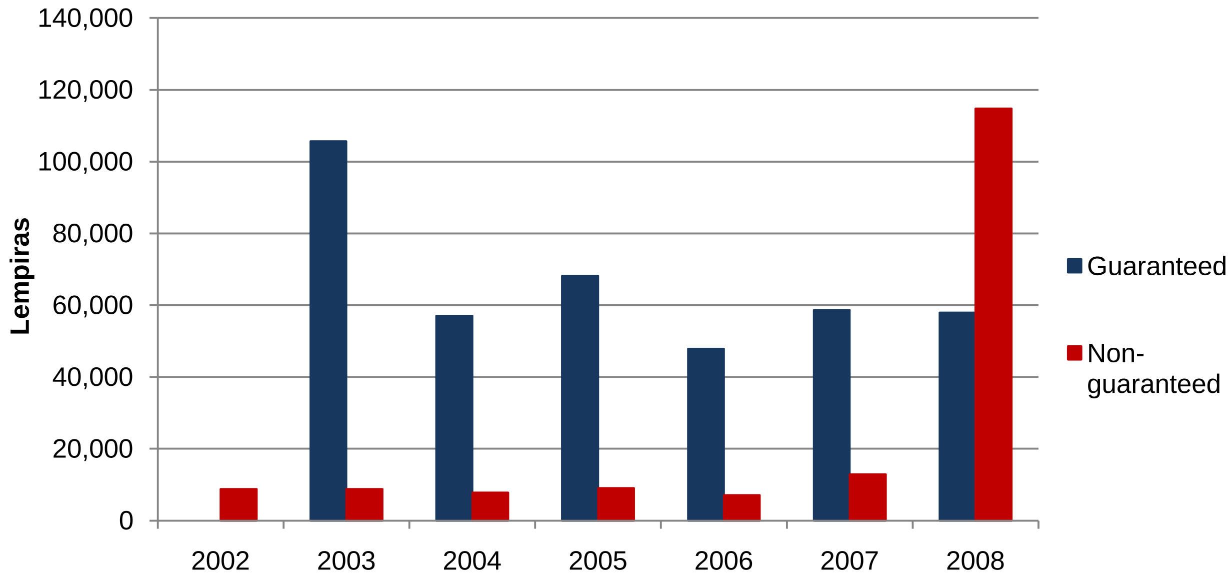
FIGURE 14. AVERAGE TENOR OF COVELO FOUNDATION AGRICULTURE AND MICROCREDIT LOANS



This growth in agriculture loan maturities without the DCA guarantee reflects Covelo's strategic decision to use guaranteed loans to help small farmers with less collateral, while it used its own funds to lend to other agricultural producers.

As shown in Figure 15 below, after a sharp drop in the average guaranteed loan size between 2003 and 2004, the average size hovered between L. 50,000 and 60,000 (approx. $2,700 to $3,200). However, between 2007 and 2008, while the total value of Covelo's *non*-guaranteed microcredit loans jumped by 293 percent, the *number* of customers with such loans actually *decreased* by 61 percent, indicating fewer, but larger, microloans.

FIGURE 15. AVERAGE LOAN SIZE OF GUARANTEED AND NONGUARANTEED LOANS



*Note: *For December of year indicated. Includes microcredit and agriculture loans only.*
Source: Covelo Foundation/Bancovelo, May 2009

CONCLUSIONS

The Covelo Foundation has used the DCA strategically and with additionality. It used the DCA guaranteed loans to enter the agriculture sector and expand its microcredit business. Through targeting farmers with little collateral, increasing the average size and tenor of microloans, and decreasing microcredit interest rates, Covelo expanded access to credit for its customers in the nontraditional agriculture sector and increased lending to entrepreneurs. At least some of the borrowers of DCA guaranteed loans subsequently increased their incomes.

The larger loans with longer maturities to entrepreneurs indicate that the guarantees helped Covelo to move up market in the microcredit sector. In addition, building on experience gained through guaranteed loans, Covelo has been able to move gradually up market in the agriculture sector, too.

Question 3.
How did the Covelo Foundation implement its loan guarantee program? And why?

FINDINGS

An understanding of the operational means by which the Covelo Foundation implemented the DCA guarantee illuminates certain findings presented earlier. First, as noted above, the annual number of *new* loans made covered by the guarantee peaked in 2005 and 2006 and then declined. During 2005 and 2006, the Foundation had the largest unutilized portion of the DCA guarantee to draw from, and also was just gaining experience in agricultural lending. For that reason it applied the guarantee to virtually all credits made to that sector. During 2007, however, Covelo officials reported that a USAID representative advised the Foundation to use its remaining (and dwindling) guarantee facility more strategically. Since then, as noted above, loan officers have used the facility to guarantee credits to borrowers that have relatively less collateral to offer, e.g., those who can provide statements of support, co-signers, contracts to purchase crops and so on, but who cannot offer traditional collateral such as land or housing.

Likewise the Foundation's evolving interaction with other USAID programs, and their own outreach to the agricultural sector, sheds light on the growth in recent years of credits to the traditional (as opposed to the non-traditional and targeted) agriculture sector. The General Manager of the Covelo Foundation explained that, during the first couple of years of the DCA program when the Foundation was just entering the agricultural market, per the intent of the USAID Mission it relied on agronomists from the RED Program to help identify promising candidates for credit. This resulted in the financing of a high percentage of non-traditional agricultural crops. As the Foundation became more familiar with the agricultural sector, however, and as the RED Program scaled back operations due to budget cuts, the MFI began to reach out independently to and build alliances with various rural producers' associations. The associations contacted apparently included both growers of traditional crops such as rice, as well as non-traditional products. (For further discussion of operational procedures for agricultural lending, see Question 7, below.)

CONCLUSIONS

The Covelo Foundation's initial implementation of the guarantee program reflected the objective of lending to non-traditional agriculture sectors. Over time, as it gained more experience in agriculture lending, the Foundation focused on building its own client base without USAID assistance, as well as expanding access to credit for borrowers with less collateral to offer. This evolution suggests that the Foundation is sustainably building an agricultural lending business while increasing access to credit for its customers.

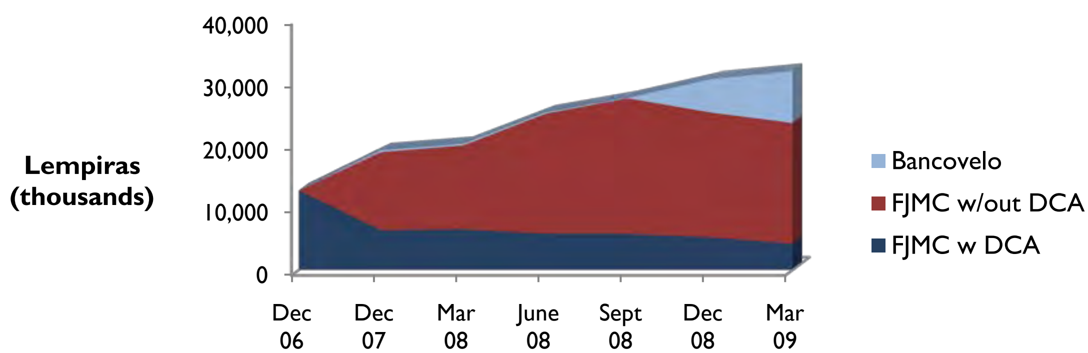
3.2 OUTCOME LEVEL

Question 4: Partner behavior change
Did the Covelo Foundation / Bancovelo improve access to credit to the target sectors outside the DCA guarantees? Did they move into any new sectors/industries, types of borrowers, types of loans, or loan terms? If so, how and why and to what extent were the DCA guarantees responsible for improving the access of their customers to credit outside the guarantees?

FINDINGS

In recent years, the Covelo Foundation has begun to offer agricultural credit without the DCA guarantee. Between December 2003 and December 2006 the Covelo Foundation's agricultural lending increased more than 3000 percent – from L. 380,000 to L. 12,646,000. All or virtually all of those loans carried the DCA guarantee. Beginning in 2007, however, while the Covelo Foundation continued to expand its agricultural portfolio, a progressively smaller proportion of the loans carried the USAID guarantee (see Figure 16). By 31 December 2007, the agricultural portfolio had increased to L. 18,808,000 – but only a third (33.4 percent) of those credits carried the DCA guarantee. And by 31 March 2009, only 17.9 percent of the Foundation's agricultural portfolio (which by then had expanded to L. 23,472,000, roughly USD 1.25 million) carried the partial guarantee.

FIGURE 16. AGRICULTURAL PORTFOLIO OF COVELO FOUNDATION & BANCOVELO (DEC. 2006 – PRESENT)



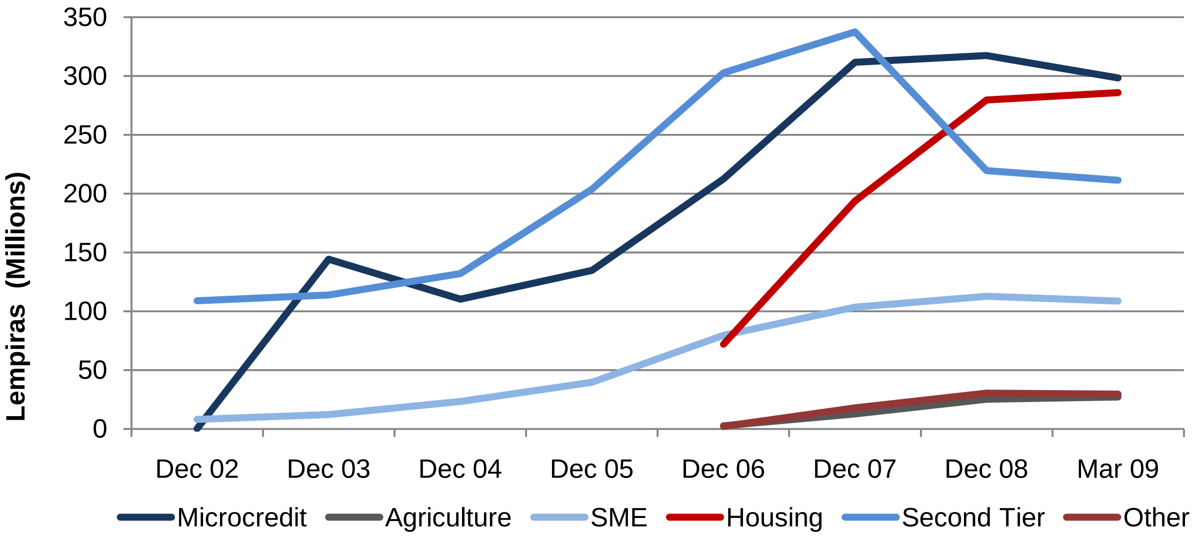
*Note: *For December of year indicated. Includes microcredit and agriculture loans only.*
Source: Covelo Foundation/Bancovelo, May 2009

The increased agricultural lending without the DCA guarantee is even greater if one includes the portfolio of Bancovelo. As shown in Figure 16, between December 2007 and March 31, 2009, Bancovelo has managed to increase its agricultural lending from nothing to a portfolio of L. 8,296,000 (USD 441,277). This portfolio draws upon resources received from the MCC that are lent to farmers at an interest rate of 14 percent; none of those credits carry the USAID DCA guarantee.[28] As of the end of March 2009, the combined agricultural portfolio of the Covelo Foundation and Bancovelo stood at L. 31,768,000 (USD 1.7 million), of which only 13.2 percent carried the DCA guarantee.

[28] In fact DCA resources cannot be used to guarantee other donor funds.

As shown in Figure 17 below, agriculture lending still represents a small proportion of the Covelo Foundation's and Bancovelo's overall lending, but lending to this sector has been steadily increasing. Microcredit has also increased steadily over the guarantee period, to claim the highest value of all loan types in Covelo's overall portfolio in March 2009.

FIGURE 17. COVELO NONGUARANTEED PORTFOLIO (DEC. 2002 TO MAR. 2009) [29]

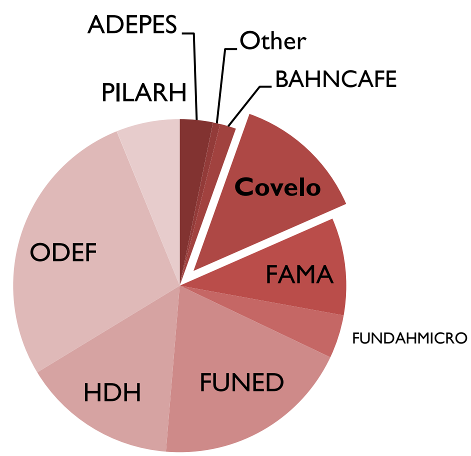


Source: Covelo Foundation/Bancovelo, May 2009. Includes both the Covelo Foundation's and Bancovelo's portfolios.

As of 30 June 2008, the Covelo Foundation and Bancovelo's combined agricultural/ forestry portfolio stood at $ 1.3 million. This represented 13 percent of the $ 10.2 million in agricultural lending reported by members of REDMICROH in that month (see Figure 18).[30] At that time the combined agricultural/forestry portfolio of the Covelo Foundation and BANCOVELO stood in fourth place among members of the Network – after the Organization for Women Entrepreneurs (ODEF, $ 2.8 million); the Foundation for the Development of the Honduras Vision Fund (FUNED, $ 2.0 million); and Brotherhood of Honduras (HDH; $ 1.5 million). This represents a significant change in market position from years before the first DCA agreement in 2003, when the Covelo Foundation provided virtually no agricultural credit, while ODEF and other MFIs were active in the sector (see further discussion below).

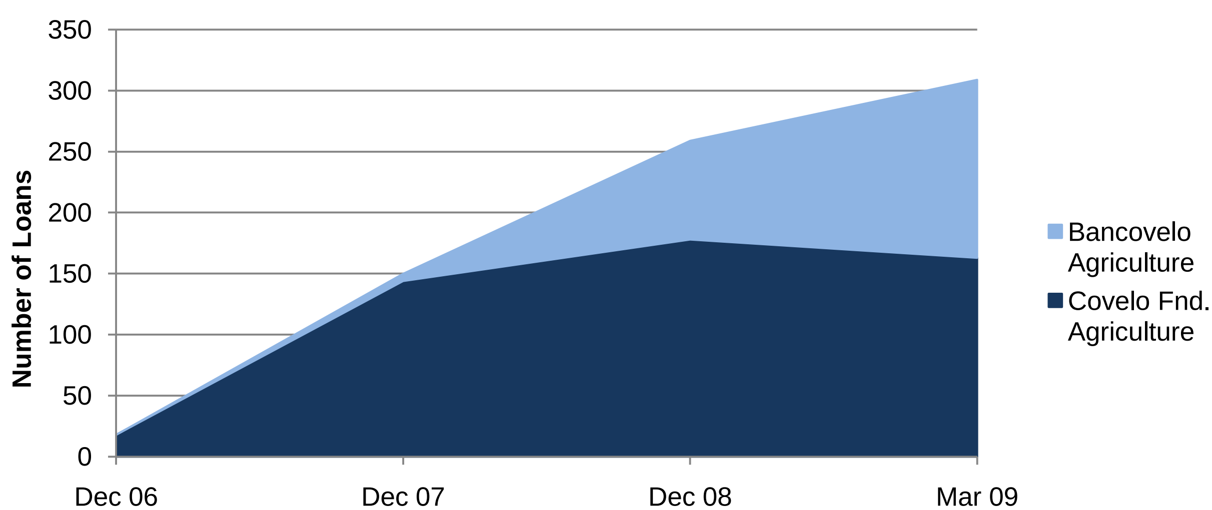
[29] The Covelo Foundation's lending drops dramatically in June 2008 because it sold most of its portfolio to Bancovelo.
[30] Source: REDCAMIF, *Microfinanzas en Centroamérica*, June 2008; and Covelo Foundation, April 2009. Note that additional lending to the agricultural sector occurs outside of the REDMICROH; see below.

FIGURE 18. AGRICULTURAL/FORESTRY PORTFOLIO OF MEMBERS OF REDMICROH (30 JUNE 2008)



The number of loans both the Covelo Foundation and Bancovelo have made to the agriculture sector has also steadily increased over time, from next to none at the end of 2005 to a combined total of 309 outstanding loans at the end of March 2009.

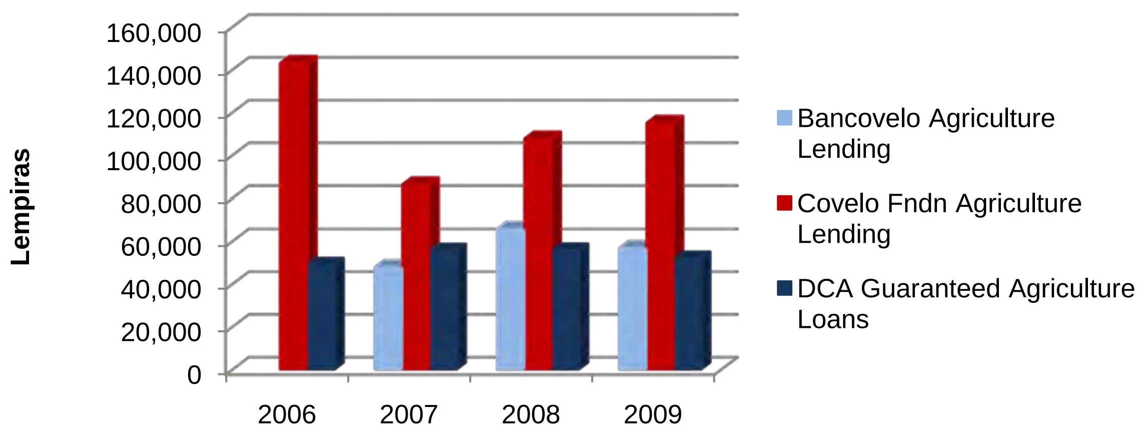
FIGURE 19. NUMBER OF AGRICULTURE LOANS DEC. 2006 TO MAR. 2009



**Loans without the DCA guarantee only*

Although the average loan size has increased only marginally since 2007, nonguaranteed Covelo Foundation loans remain much larger than those under the DCA guaranteed. The March 2009 average loan size at Bancovelo was L. 56,824 ($3,072), while for the Foundation it was L. 115,088 ($6,223) (see Figure 20 below). By contrast, the average DCA guaranteed agriculture loan at that time was L. 51,783 ($2,800).

FIGURE 20. AVERAGE AGRICULTURE LOAN SIZE DEC. 2006 TO MAR. 2009



Covelo's microloan portfolio has shifted from smaller to larger loans with no significant difference in the number of loans, as depicted in Figures 21 and 22 below. As these figures suggest, the value of Covelo's microloan portfolio has grown 158 percent between December 2002 and March 2009. Despite this growth, the average nonguaranteed loan size remains significantly below the average guaranteed loan. In fact, the average nonguaranteed loan represents only a quarter of the value of an average loan with the DCA guarantee.

FIGURE 21. NUMBER OF MICROLOANS DEC. 2003 TO MAR. 2009

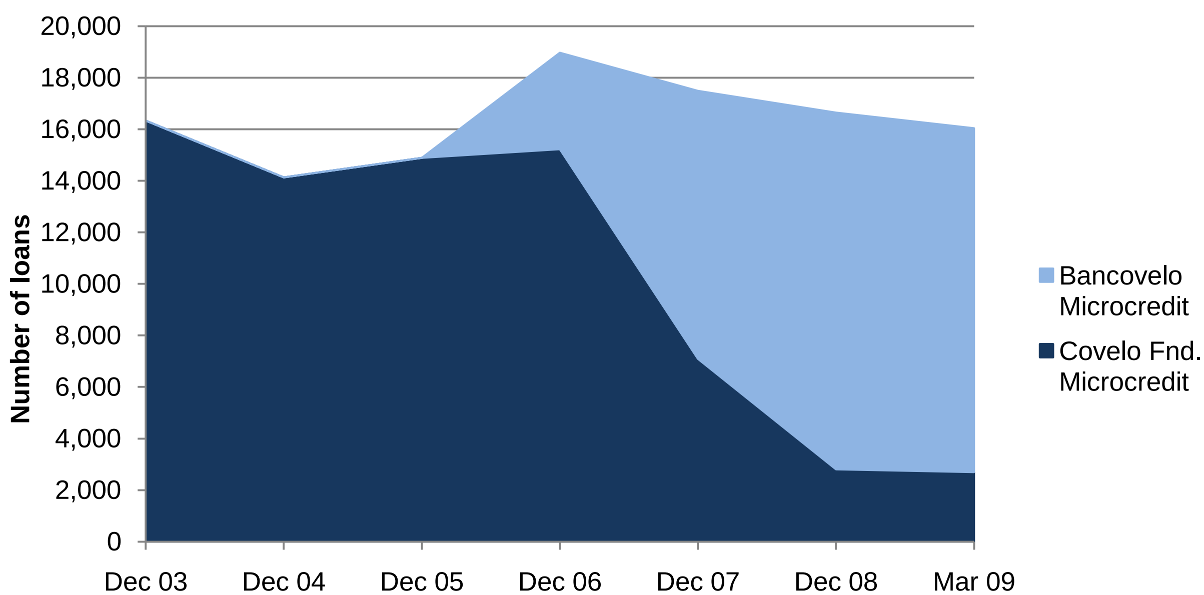
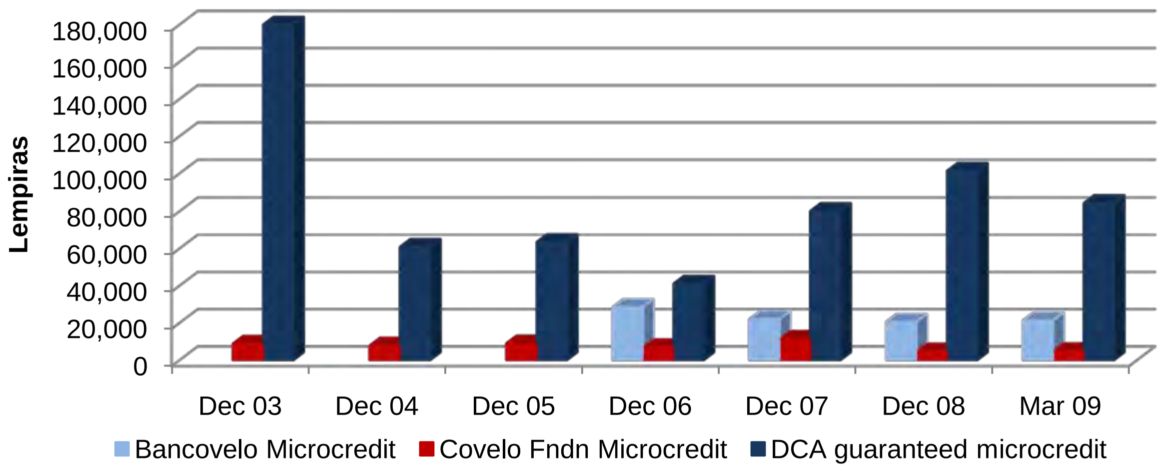
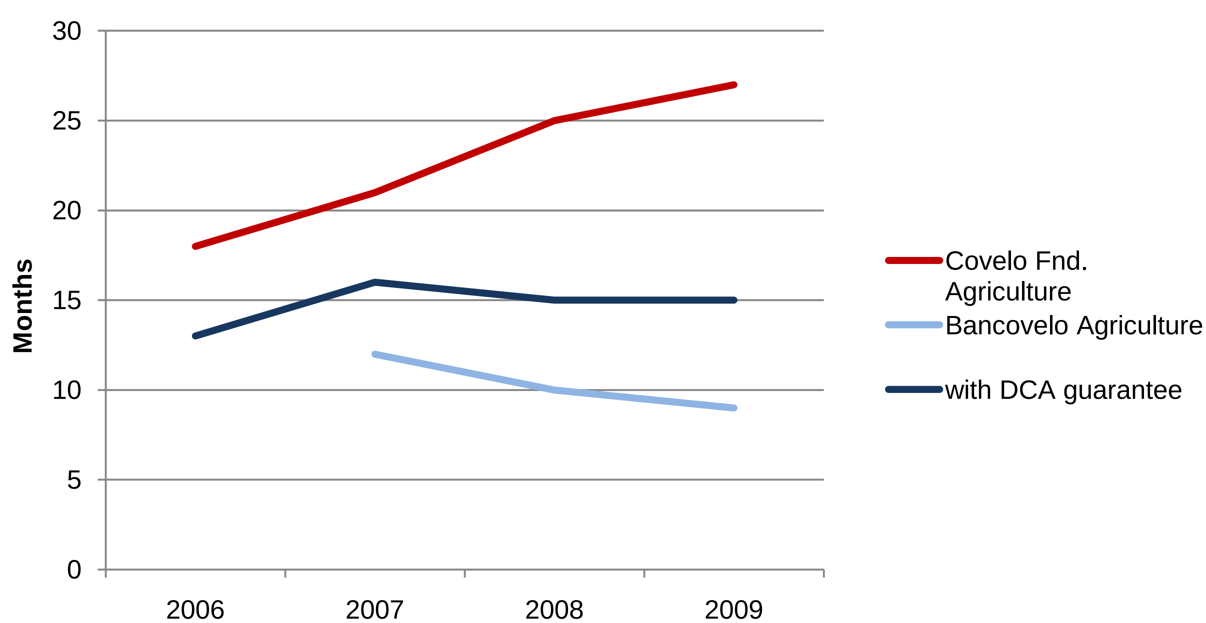


FIGURE 22. AVERAGE MICROLOAN SIZE DEC. 2003 TO MAR. 2009



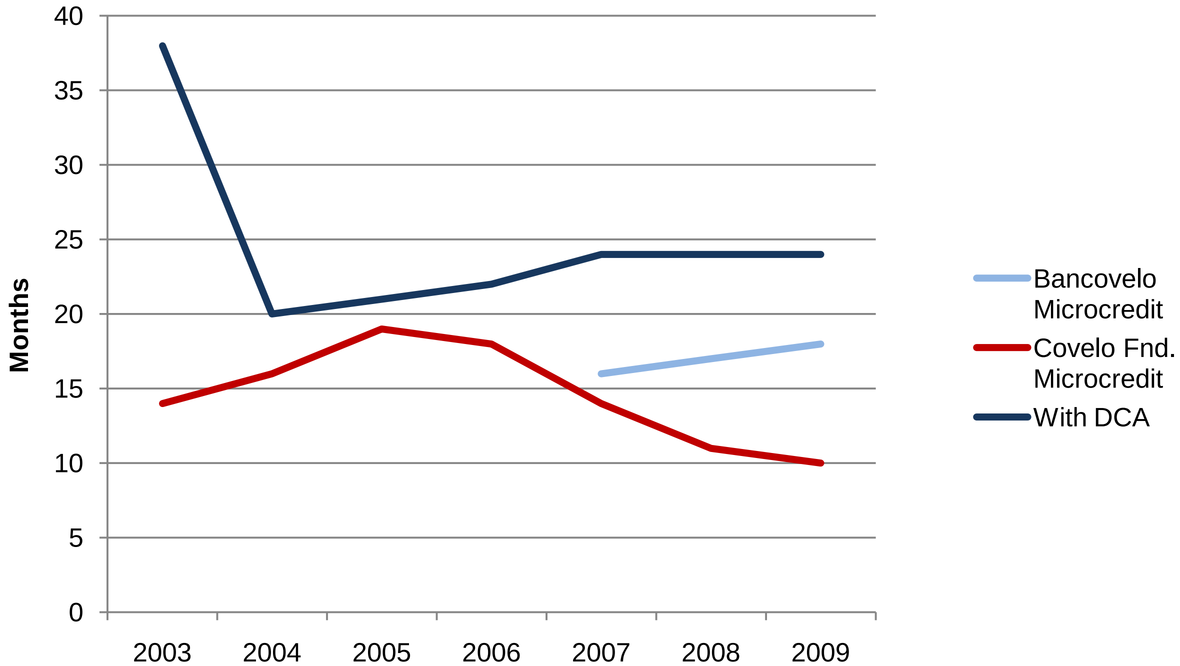
The average tenor of agriculture loans from the Covelo Foundation has been steadily increasing since it introduced nonguaranteed lending in 2006, reaching 27 months in March 2009. Bancovelo's agriculture loans, by contrast, have seen gradually shorter tenors (12 to 9 months) and have remained below the average for both microcredit (16 to 18 months) and SME loans (57 to 51 months). However, the growth in the Covelo Foundation's average tenor (50 percent) has outstripped the rate of decline in Bancovelo's average loan tenor (-25 percent).

FIGURE 23. AVERAGE AGRICULTURE LOAN TENOR, BANCOVELO AND COVELO FOUNDATION, DECEMBER 2006 TO MARCH 2009.



Nonguaranteed microloan tenors have remained below all DCA guaranteed microcredits. The average tenor for the Covelo Foundation's microloans has actually decreased every year since 2005.

FIGURE 24. AVERAGE MICROLOAN TENOR, BANCOVELO AND COVELO FOUNDATION, DECEMBER 2007 TO MARCH 2009.



Average interest rates for agriculture loans have not changed much for either the Covelo Foundation or Bancovelo, varying between 17 and 23 percent for the former and 14 and 22 percent for the latter. In both cases, however, average interest rates for agriculture loans have mostly remained below those for both SME and microcredit loans from both organizations.

FIGURE 25. AVERAGE COVELO FOUNDATION INTEREST RATES

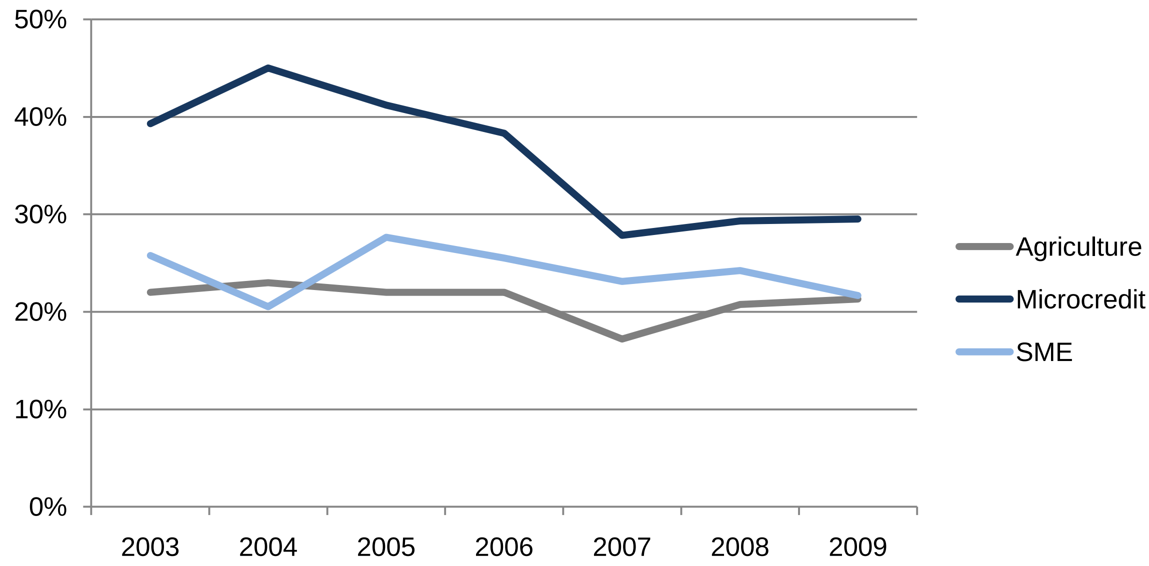
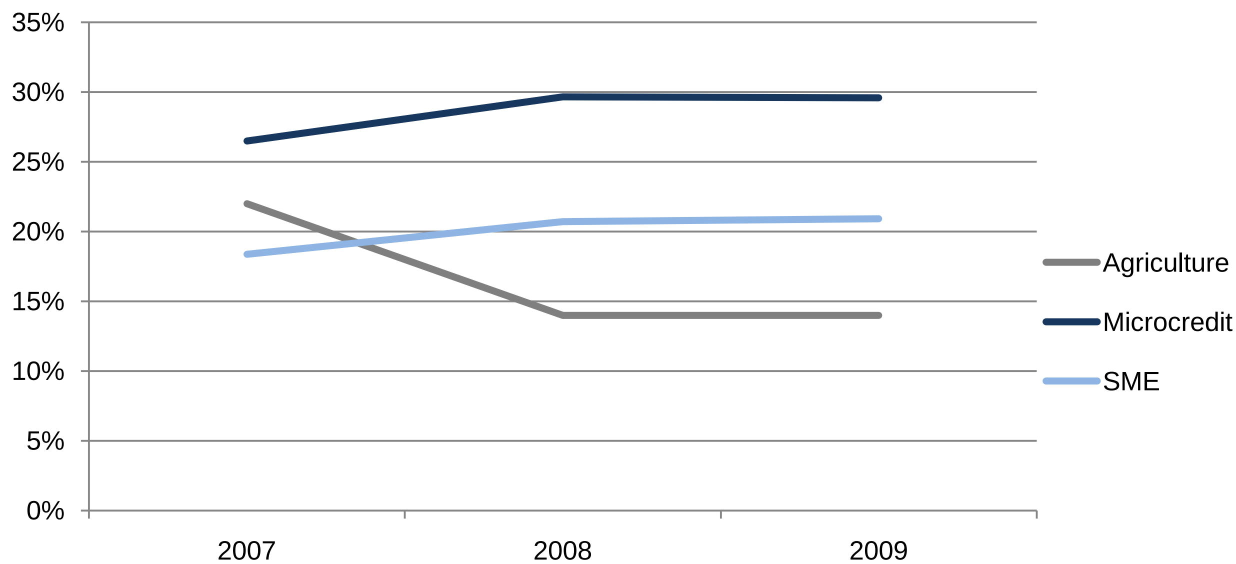


FIGURE 26. AVERAGE BANCOVELO INTEREST RATES



Both organizations have charged higher average interest rates for microloans than they have for either agriculture or SME loans. As stated under Outputs above, Bancovelo explained that it makes many small, short-term microcredit loans, which are probably made to small entrepreneurs with little collateral to offer. Therefore, we can expect that the loans would carry higher average interest rates. The large drop in the Covelo Foundation's microcredit interest rates seen in Figure 25 is most likely because the Covelo Foundation's (nonagriculture) interest rates had to come into conformity with Bancovelo's interest rates prior to sale of the portfolio. Bancovelo, as a more highly regulated institution, must adhere to government-set caps (see Impact Level findings, below).

Examples of Increased Access to Credit

Aside from the statistical averages discussed above, Covelo's files offer specific examples of regular clients for whom they have expanded access to credit. Eight persons who initially received a DCA-guaranteed loan from the FJMC (three farmers, five micro-entrepreneurs) went on to obtain housing loans from Bancovelo. At least one farmer who initially borrowed under the DCA guarantee went on to obtain a non-guaranteed agricultural loan (derived from MCC resources) from Bancovelo. Covelo officers confirmed that a successful credit history with the Covelo Foundation and/or Bancovelo could (and did in such cases) lead to further loan approvals.

For example:

- *Henry Edgardo Figueroa Q.* took out 13 guaranteed loans between June 2004 and December 2006. The five loans he initially undertook, in 2004, were for an average value of USD 3249, with less than a half year (171 days) tenor. In 2006, however, he undertook three loans that averaged USD 13,365 in value, with a slightly longer (202 days) average tenor.

- *Remburto Alonso Betancourth L.* began borrowing in March 2005, with two guaranteed loans of USD 2154 each, with tenors of five months or less. He progressed to larger guaranteed loans, including three worth more than USD 13,000 each, with tenors of ten months to a year.

- *Jorge Alberto Palma G.* took out a total of 10 guaranteed loans between June 2004 and May 2006. His initial eight loans were all for periods of 200 days or less. In August 2005, however, he took out a long-term loan (for USD 5302, comparable in size to earlier credits) with a tenor of 637 days.

CONCLUSIONS

The DCA guarantees to the Covelo Foundation achieved their goals of increasing lending to agriculture-focused SMEs and helping Covelo to expand and move up market in the agriculture sector.

The DCA guarantee clearly helped both the Covelo Foundation and Bancovelo jumpstart their lending to the agricultural sector. They have expanded access to credit for their customers in this sector by increasing the number of loans available, the average size of those loans, and the average tenor, as well as keeping interest rates low. The Covelo Foundation appears increasingly confident in risking its own capital in the sector without a guarantee. Rapid increases in agricultural lending building on the DCA guarantees have helped the Covelo Foundation and Bancovelo become a significant actor in the agricultural microcredit sector.

At least so far, Covelo's microlending behavior has not followed the patterns of its DCA-guaranteed microcredit and there is no evidence that Covelo microloans without the guarantee have either expanded access to microcredit or moved Covelo upmarket. However, since most of the guaranteed portfolio went to the agriculture sector (see response to Question 1), we would not expect as much change in Covelo's microcredit behavior to result from using the DCA guarantees.

Question 5
What factors at the Covelo Foundation / Bancovelo were responsible for achieving desired outcomes (e.g., TA, bank staff training, revised bank strategy, new procedures, changed structure, new management, etc.)?

FINDINGS

Officials reported that the Covelo Foundation's initial success in lending to the agricultural sector *with* the DCA guarantee was a primary cause of increased agricultural lending by the FJMC *without* the guarantee. The MFI has experienced a fairly low rate of defaults in the sector; for example, as of 31 December 2007, the Covelo Foundation reported only 12 out of 259 agricultural borrowers (4.6 percent of the total) in default. By that point the MFI had developed financial products and procedures suited to the sector (for more information see Section 3.4), and established relationships with farmers. This cumulative knowledge helped it expand its non-guaranteed portfolio. In turn, Bancovelo obtained resources from the MCC to lend to the agriculture sector.

We must close the present discussion by noting that the long- and even short-term prospects for agricultural lending, both for the Covelo Foundation and for Bancovelo, are uncertain. To manage risk, decision-makers already have set ceilings on agricultural lending for both the Covelo Foundation (L. 30 million) and Bancovelo (L. 10 million). Both entities are already close to those limits – and in Bancovelo's case the ceiling will preclude any further agricultural lending outside of those resources already provided by MCC for this purpose. Furthermore, while the original plan was for Bancovelo to acquire the Foundation's/AAP's agricultural portfolio after it was established, to date its owners have declared themselves disinclined to do so. At the time of our visit to Honduras, a decision was pending as to whether the Foundation would retain its agricultural portfolio or seek approval to sell it to a third party.

CONCLUSIONS

The Covelo Foundation's initial success in lending to the agricultural sector *with* the DCA guarantee, along with development of new procedures, products and related know-how, were primary causes of their increased lending to the agriculture sector *without* the guarantee.

However, it seems unlikely that these positive outcomes of the DCA guarantees will be sustained. With caps on the amount of agricultural lending Covelo is willing to undertake and the possible sale of the bulk of the organization's agriculture portfolio, Covelo has neither the intent nor the scope for continuing its lending support to producers.

3.3 IMPACT LEVEL

Question 6: Market demonstration effect
Did other, non-partner banks initiate or increase lending to the target sector(s)? If so, to what extent was the DCA guarantee to Bancovelo responsible? How and why?

Question 7
Did access to credit (or the terms of credit) improve for loans to the target sectors? If so, how and why? What role if any did the DCA guarantee play as a demonstration model?

FINDINGS

Answering these questions involves first understanding how the microfinance sector is organized. Table 14 shows the different types of entities and key actors that are active in the sector. In general those shown in columns to the left are more closely regulated, and have access to more diverse and/or greater sources of capital, than those to the right.

Entities that offer microcredit include one government bank (the National Bank of Agricultural Credit, BANADESA) and different forms of private entities. The first three types of private entities shown (all of which are regulated by the National Commission for Bank and Securities [CNBS]) are banks, *financieras* (organized and able to raise private capital as anonymous societies), and financial private development organizations (OPDFs). The government established the category of OPDF in 2000, as a way to strengthen and more closely regulate the microfinance sector. The Regulatory Law of OPDFs (Decree No. 229-2000) established minimum capital, reporting and other requirements for these entities. To help encourage OPDs to "graduate" to this more highly regulated status, the law allows OPDFs – but not OPDs – to raise capital by receiving deposits from members. At the same time the law bars OPDFs from charging an interest rate that is "more than three percent higher than the maximum prevalent in the national banking system" (Art. 47). This is a practice that does not accord with international best practices for MFIs, and in fact (as interviews suggest) may have deterred some OPDs from seeking this organizational status. Less closely regulated entities are OPDs, savings and loan cooperatives, rural savings groups (*cajas rurales*) and other entities.

Table 14 also shows members of REDMICROH (in shaded box). We would expect to find the strongest evidence for any demonstration effect by the Covelo Foundation's agricultural lending within the REDMICROH, whose members exchange information and where the Covelo Foundation traditionally has played a leadership role.

TABLE 8. ENTITIES THAT OFFER CREDIT TO MICRO- AND SMALL ENTREPRENEURS

Public	Private Banks	Private Financial Institutions (*Financieras*)	Financial Private Development Organizations (OPDFs)	Private Development Organizations (OPDs)	Private Savings & Loan Cooperatives	Other Private
National Bank of Agricultural Credit (BANADESA)	**BANCOVELO** BANHCAFE	FINCA/Honduras ODEF	FUNED HDH PILARH FAMA CREDISOL	**Covelo Foundation** IDH Care FAMA FHA World Relief of Honduras @ 10 others	Cooperativa Ocotepeque Cooperativa Ceibeña Others	@ 1000 Rural savings groups (*cajas rurales*) *Prestamistas*
	Banco ProCredit <u>*SME only:*</u> BAC-BAMER Banco Atlántida Banco de Occidente	FINSOL		Others		Others

<u>*Notes:*</u>
See text of main report for descriptions of categories, acronyms, etc. Second tier lending to sector not shown.
Entities in box with grey outline are members of the Microcredit Network of Honduras (REDMICHROH).
All serve micro sector unless otherwise indicated. Banks that only serve small- and medium-sized enterprises (SMEs) do not serve micro-entrepreneurs.
*Covelo Foundation (in **bold**) is the partner financial institution for the DCA guarantee agreements under study, and owner of that loan portfolio; however the guaranteed loans are now "under administration" by BANCOVELO (also in **bold**).*

Table 9 gives an order-of-magnitude idea about the relative importance of each major category of entity in the micro-and small enterprise (MSE) finance sector. As shown, members of REDMICROH provide about a quarter (24.6 percent) of the documented credit (excluding housing and consumer credit) that is provided to the MSE sector.[31] Note the surprisingly large proportion of credit provided by savings and loan cooperatives.

[31] Note that definitions of micro- and small entrepreneurs vary in Honduras. Not only do the formal definitions differ in two laws (i.e., the Regulating Law for OPDFs [Decreto No. 229-2000] and the Law for the Promotion and Development of the Competitiveness of the Micro-, Small and Medium Enterprise [Decreto No. 135-2008]), but providers of micro-credit also may report data using their own definitions. Further note the earlier definition used in the DCA guarantee agreements that diverged from Honduran legal definitions.

TABLE 9. CREDIT PROVIDED TO MSE SECTOR (31 DECEMBER 2008)*

Type of Entity	Active Credit Port-folio (USD million)	*Percentage (%)*
BANADESA	$ 95.7	*21.3*
Members of REDMICROH	$ 110.6	*24.6*
Other banks & *financieras***	$ 39.6	*8.8*
Savings & loan cooperatives***	$ 204.3	*45.4*
TOTAL	$ 450.2	*100 %*

Notes:

**Except for members of REDMICROH, whose data are for 30 June 2008 (source: REDCAMIF, Microfinanzas en Centroamérica, June 2008). Credit portfolios include agricultural, productive and commercial uses. For BANADESA and ProCredit, assume no housing or consumer credit in totals provided; for other entities those types of credit removed from totals. Double reporting may occur within REDMICROH, which includes both first- and second-tier entities. Also see footnote 23. Sources: BANADESA, interview; others as cited in notes.*

*** FINSOL and ProCredit. Sources: interview notes and "Executive Summary 2008" (FINSOL).*

**** Members of FACACH. Source: 2008 "FACACH: Información Financiera y Estadística".*

Lending by MFIs to the agricultural sector has increased substantially during the period in which the Covelo DCA agreements have been in effect. This has been due almost exclusively to increased credit provided by existing providers of agricultural credit, rather than new entries. From 31 December 2004 to 30 June 2008 (the period for which data are available), members of the REDMICROH increased lending to the agricultural and forestry sectors by some 300 percent, from USD 2.2 million to 8.9 million, respectively (see Table 16).[32] This sectoral increase kept pace with a broader rise in total lending by those MFIs during this period (again around 300 percent), and an expanded membership in and reporting to REDMICROH. Representatives of MFIs interviewed likewise asserted that access to credit for micro- and small-scale farmers generally had expanded during this period.

TABLE 10. MEMBERS OF REDMICROH: AGRICULTURE/FORESTRY LENDING (2004-2008)*

Period Ending	Active Credit Portfolio (in thousands)			Members of Network	
	Agriculture/ Forestry	Total	*Ag/Forestry as % of total*	Reporting Ag/Forestry	Total Reporting
12/04	$ 2,206.9	$ 41,303.9	5.3 %	10	16
6/05	1,595.6	36,348.3	4.4	12	20
6/07	5,943.3	127,314.6	4.7	16	24
12/07	8,054.0	151,140.7	5.3	15	24
6/08	8,872.8	171,324.4	5.2	13	22

*Note: * Disaggregation of agricultural and forestry lending not available.*

[32] Dates and sectors for which data are available. Source: REDCAMIF, *Microfinanzas en Centroamérica*, June 2008. Note however that, as shown in Table 14, other entities not in REDMICROH also provide significant volumes of credit to the MSE sector, including small-scale farmers.

Five of the eight respondents to our REDMICROH survey agreed that farmers have more access to credit now than they used to. They gave the following reasons for their response:

- greater participation of microfinance institutions in the agriculture sector (4 responses),
- producers have obtained capacity building and access to credit through the value chain, and
- some microfinance organizations have altered their requirements to enable small producers to qualify for loans.

However, two of the respondents who said that agricultural producers have more access to credit added that providing such credit is difficult because capital investors do not provide funds under conditions appropriate to the agriculture sector or small producers. The respondent who said producers have the same access to credit agreed, explaining that most MFIs have credit offerings geared towards larger producers because small-scale farmers present more risk.

Interviews with selected members of REDMICROH, coupled with the email-based survey of all members, revealed various reasons for their entrances into agricultural lending over the past several years.[33] Most survey respondents indicated that "very important" and "important" reasons included: social motivation, desire to expand portfolio, increase in competition in urban areas, cumulative organizational experience in the sector, and the increased collateral that farmers are now able to offer.

The Covelo Foundation's activities in the agricultural sector supported by the DCA *did* help facilitate the entrance of one MFI into the agricultural sector: the Association for Integrated Community Development (ADICH). ADICH began to report agricultural/forestry lending only in June 2005, after the DCA guarantee program had begun; they did not report any such lending previously (i.e., in December 2004). Further, a representative of ADICH indicated that a packet of information on agricultural credit (an "Instructional Guide on the Agricultural Credit Process"), distributed electronically and via a workshop to members of REDMICROH,[34] was an "important factor" in their entrance into the agricultural credit market. This information packet was developed by the Covelo Foundation and based primarily on their experience with DCA-supported agricultural lending. At the same time, ADICH described other information and support provided by REDMICROH (e.g., via periodic meetings, REDMICROH periodical) as "very important" to their entrance into this sector.[35] At its peak (30 June 2007), ADICH had an active agricultural/forestry portfolio of $ 54,000. This represented seven percent of their total active portfolio at that time ($766,000), and one percent of all loans outstanding from members of REDMICROH to the agricultural/forestry sector ($5,943,300). As of 30 June 2008, ADICH reported $27,700 in outstanding loans to the sector.[36]

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[33] From an email-based survey of 22 members of REDMICROH, we received responses from 8, representing a 36 percent response rate.

[34] Foundation representatives report that they distributed a free electronic version of this packet of procedures, templates, guidelines, etc. (which was developed with donor support) to REDMICROH members – then offered on a fee basis to help members modify and institutionalize this packet. To date, however, no MFIs have taken them up on this offer.

[35] Source: SEGURA/IP3 electronic survey of members of REDMICROH, April-May 2009.

[36] Source: REDCAMIF, *Microfinanzas en Centroamérica*, June 2008 and previous periods.

Of survey respondents, only ADICH listed the packet of information or other support provided by REDMICROH as "very important" or "important." Nor did other persons interviewed (including the representative of one of the two MFIs where the Covelo Foundation originally tested the agricultural credit packet) indicate that such support was a factor in their allocation of credit to the agricultural sector. This lack of a broader influence on the part of the FJMC is explained in part by the fact that the Foundation, while being a leading member of the MFI community as noted earlier, was by no means a "first mover" when it came to agricultural-sector lending. While the Foundation only began its agricultural-sector lending after signing its first DCA agreement in September 2003, and had only inked some 61 loans as of 30 September 2004, Table 15 shows that at least nine other MFIs already were active in the agriculture and forestry sectors in that year. Looking back even further, several MFIs (e.g., World Relief of Honduras) were active in agricultural lending in the early 1990s – before the havoc wrought by Hurricane Mitch (1998) and the subsequent influx of grant resources. While those factors forced a temporary retreat of MFIs from the sector, some MFIs retained institutional knowledge of lending to that sector that allowed them to reactivate their agricultural lending in the 2000s.

Nevertheless, Covelo's activities supported by the DCA guarantee can potentially help *individuals* to access more credit through other MFIs. Prompt repayment of loans that carry the DCA guarantees has allowed borrowers (mostly farmers) to build up positive credit histories. The Covelo Foundation (and Bancovelo) periodically reports such data to the Government's Credit Bureau (*Central de Riesgos*) and at least one private credit bureau; other MFIs and banks then reference such information as part of their loan decision processes. Available data, however, do not permit us to precisely define or estimate the number of farmers who had first received DCA-guaranteed loans from the Covelo Foundation, who then were able to access credit from *other* MFIs (outside of Bancovelo). To attempt to answer this question, we reviewed the current credit history records from the *Central de Riesgos* for 21 of the 83 persons with outstanding loans that carry the DCA guarantee (25 percent of the total).[37] Records showed that thirteen of those persons also have borrowed from other lenders, while the other eight had not. Data did not permit us, however, to determine which borrowers if any had received DCA-backed loans from the Covelo Foundation *prior* to borrowing from other sources.

CONCLUSIONS

The Covelo Foundation's DCA-supported agricultural sector lending helped facilitate the entrance of one MFI into the agricultural sector: ADICH. We did not, however, find evidence of any broader impact on agricultural sector lending. However, since the DCA guarantees have not even ended yet, it is too early to ascertain impact, which by definition is a long-term phenomenon. In general, early movers in the sector have continued to expand and have been in a better position to offer a leadership example to others than was the newcomer Covelo Foundation. Positive credit histories with Covelo, however, likely help first time borrowers to access credit from other MFIs.

[37] Credit histories at given dates in the past were not available.

3.4 EXTERNAL FACTORS

What are the exogenous factors that have affected the financial sector? How have they done so? Have these factors affected the performance of the DCA guarantee(s)?

Obviously Honduran micro- and small entrepreneurs and small-scale farmers operate in an environment that is influenced by a number of factors outside of the supply of microcredit by private MFIs. While the Covelo Foundation has been able to utilize the DCA successfully for agricultural and agro-industrial lending, and overall lending to the agricultural sector has increased in recent years, external factors have influenced the sector. Consistent with our survey findings (see previous section), exogenous factors that influenced the supply and demand for agricultural and agro-industry credit during the period when the DCA guarantees have been in operation (2003-present) include the following.

FACTORS THAT INCREASED THE SUPPLY OF AND DEMAND FOR AGRICULTURAL CREDIT

USAID & MCC technical assistance (TA) programs that help small-scale farmers. As suggested above, a number of MFI representatives interviewed noted that TA provided by the USAID Rural Economic Diversification (RED) program and predecessor projects, as well as the MCC's EDA and ACA programs, had allowed participating farmers to access credit. In particular many MFI loan officers look favorably upon letters from those programs that indicate that farmers are receiving TA, and/or contracts with international companies (obtained via program assistance) to purchase future crops. Several MFIs have signed agreements with one or both of those programs that provide for closer working relationships. Persons interviewed that cited collaboration with these programs included representatives of HDH, Solidarity Financier (FINSOL), and Projects and Local Initiatives for the Regional Self-Development of Honduras (PILARH).

Increased competition among MFIs in urban areas; demand by rural customers. Representatives of the Covelo Foundation and USAID expressed their belief that in recent years the market for microcredit in urban areas has been attended to relatively well, and that the rural market had a higher level of unmet or pent-up demand. Four survey respondents said that such considerations contributed substantially to their increased interest in agricultural lending. Representatives of MFIs noted that credit for working capital was relatively easy to provide to small-scale venders in urban markets, and that therefore there was a "fierce competition" for such clients, whereas the higher risks and transaction costs in rural areas (e.g., transportation to visit a remote farm) had left this sector relatively unattended to until recent years. A representative of FINSOL, for example, indicated that they had begun to offer rural (including agricultural) credit as they entered smaller municipalities and gradually began to attend more closely to local demand.

FACTORS THAT DECREASED THE SUPPLY OF AND DEMAND FOR AGRICULTURAL CREDIT

Agricultural debt forgiveness and subsidized lending programs by the Government. Virtually all MFI representatives interviewed (e.g., the Executive Director of World Relief of Honduras) cited past debt forgiveness schemes as a major deterrent to providing credit to the agricultural sector. Representatives indicate that in the past politicians have generally announced such schemes during election years. (The Vice President of BANADESA, however, asserted that the term debt forgiveness "isn't in the vocabulary" of the current administration.) While some such decrees have only forgiven debt to public banks, others also have covered credits provided by *private* MFIs. Obviously such practices erode a hard credit culture and can hurt MFIs' balance sheets.

Similarly, MFI representatives are reacting cautiously to a recent Law for Financial Assistance for the Productive Sectors of Honduras (promulgated 23 December 2008). This law provides for L 5,000 million to be provided for various uses, including L. 2,000 million (around USD 106 million) for "microcredit and other productive sectors." Representatives report that elected officials have announced that these resources will be offered to micro-entrepreneurs and others at a seven percent interest rate – a rate far below that currently offered by MFIs. Such large shocks to the supply of microcredit can affect the results of private MFIs, as micro-entrepreneurs postpone borrowing decisions in hopes of obtaining more favorable terms. For such reasons as well as concerns about the inherent risk of agricultural debt, CARE, for example, is curtailing its rural (including agricultural) sector lending.

Fluctuations in world prices for agricultural goods. The General Manager of the OPDF PILARH, for example, cited a recent drop in the price of coffee as a major reason why they have cut their agricultural lending from 70 percent to 35 percent of their portfolio over the past three years. Similarly, even BANHCAFE has curtailed its lending to the coffee sector.

One of our REDMICROH survey respondents nicely summarized major constraints to increased supply of agricultural credit: lack of guarantee funds, legalization of land, crop securities and climate risk.

FACTORS WITH UNCERTAIN IMPACT ON THE SUPPLY OF AND DEMAND FOR AGRICULTURAL CREDIT

Economic growth with structural change during period. Up until the current (beginning in late 2008) financial crisis, the Honduran economy generally has grown during the period when the DCA has been in operation. In 2003-2007, real gross domestic product (GDP) expanded at an annual average rate of 5.9 percent, much higher than the average for the previous 20 years.[38] This growth was supported by dynamic global demand.

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[38] This pre-2003 period was affected by (among other factors) Hurricane Mitch (1998). Note also that Honduras is a poor country: in 2006 gross national income was estimated at USD 1,200, just over a quarter of the average for countries in Latin America and the Caribbean (USD 4,767). Since 1999 remittances have increased substantially.

While the total economy has grown during the study period, the agricultural sector has been in a slow decline; hence the mixed impact on demand for agricultural credit. Most of the growth over the past several years was in the industrial (including *maquila*) and services sectors. Together those sectors accounted for 86.2 percent of Honduran GDP in 2006 – up from 79.4 percent from a decade before. From 1986 to 2006 agriculture proportionately declined in relative importance, from 20.6 to 13.8 percent of GDP, respectively. This pattern, however, has not been constant over time, but rather has fluctuated annually. For example agriculture declined by 0.3 percent between 2004 and 2005, but actually increased 8.1 percent the following year.[39] Over the entire study period, however, the benefits of overall economic growth have been canceled out by a long-term decline in the importance of the agricultural sector, leading to a mixed impact on the demand for agricultural credit.

DR-CAFTA. Eventually the U.S.-Dominican Republic-Central America Free Trade Agreement (DR-CAFTA) is expected to exert a far-reaching effect upon the Honduran economy and producers' demand for credit; however those impacts are just starting to become apparent. DR-CAFTA is recent: the agreement was signed by the U.S. in August 2005; by Honduras, El Salvador, Nicaragua and Guatemala in March-July 2006; and by Costa Rica in January 2009. Moreover, while the agreement reduces the tariffs for some categories of goods immediately to zero, the reductions for other categories of goods are phased in over periods of up to two decades. For example rice producers – a number of whom have received DCA-supported credits from the Covelo Foundation – will not see any changes in tariff levels for five years, and then will experience only a gradual decline over the next fifteen years, until tariffs are phased out completely in year 20 of the agreement. Moreover, as an economist with the International Food Policy Research Institute (IFPRI) recently concluded, "Past trade liberalizations in Honduras reduced average tariffs [on agriculture-based products] to a level where the further reductions resulting from the CAFTA agreement simply are not large enough to have much of an impact."[40] On the other hand, the IFPRI economist expects that DR-CAFTA's liberalized rules of origin for maquila products eventually will "have a significant impact on the growth rate" of that sector."[41]

3.5 CONCLUSIONS ON ACHIEVEMENT OF AGREEMENT OBJECTIVES

EGAT/DC provided two partial portfolio guarantees to the Covelo Foundation with the expectation that a number of specific objectives would be achieved, as described in the guarantee agreements. We summarize here our conclusions regarding the achievement of those objectives.

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[39] Sources: World Bank, "Project Appraisal Document for a Rural Competitiveness Project," May 2008, pp. 81-2; and Economist Intelligence Unit, "Country Profile 2008: Honduras," p. 18.

[40] On the other hand Dr. Dante Mossi, Country Operations Officer of the World Bank mission in Honduras, argued that DR-CAFTA has substantially lowered *non-tariff* barriers to trade, e.g., by allowing produce to travel for quickly to other countries, to the benefit of perishable agricultural export commodities, and that such effects (on exports, credit patterns, etc.) will become increasingly apparent over time.

[41] Samuel Morley, *et al*, "The Impact of CAFTA on Employment, Production and Poverty in Honduras," IFPRI, January 2008, pp. 2-5 and 17-20.

Objective 1: Facilitate MFIs' Ability to Expand and Move Up-Market

(Larger Loan Sizes with Longer Maturities)
At the output level, the Covelo Foundation used its DCA guarantees to provide larger, longer microloans to its customers, but this trend did not carry over to Covelo's non DCA guaranteed portfolio. On the agriculture side, especially in recent years, Covelo strategically geared its guaranteed loans to riskier clients—smallholder farmers with little collateral—which were consequently small and short. However, based upon the experience it gained under the DCA guarantees, Covelo used its own funds to provide larger, longer agriculture loans to producers. It created an agriculture portfolio. Therefore, we conclude that through its DCA-supported agriculture experience and its DCA-guaranteed microlending, Covelo did expand and move up market.

Objective 2: Increased Abilities of Borrowers to Expand their Revenues

At least nine recipients of DCA guaranteed loans increased their incomes, but we do not have enough evidence to determine what percentage of all Covelo loan recipients did so. We can say without question that Covelo's DCA guaranteed and nonguaranteed loans increased access to credit for agricultural producers through more available loans, larger and longer loans, lower interest rates, and (for guaranteed loans) lower collateral requirements. Presumably, this access to credit helped recipients expand their businesses and, consequently, their revenues.

Objective 3: Contribute to Increased Levels of Investment

Covelo has certainly been an active contributor to increasing investment in the agriculture sector, particularly for smallholder producers who are too risky to qualify for loans from banks. Based upon interviews with Covelo representatives, it is unlikely that Covelo would have contributed so substantially to agricultural lending without the DCA agreements.

Objective 4: Facilitate Increased Provision of Loans to Rural Borrowers

Similarly, Covelo has increased the number and amount of loans to rural producers. The organization also encouraged at least one organization to enter the agriculture sector, thereby further increasing loans to rural borrowers. While Covelo cannot claim credit for the explosive growth of Honduran agriculture sector lending over the last decade, it has certainly been a valuable contributor.

APPENDIX A – LIST OF PERSONS MET IN HONDURAS (APRIL 13-24)

USAID/Honduras
William Brands, Mission Director
Daniel M. Smolka, Deputy Mission Director
Donald R. Soules, Jr., Supervisory Program Officer, Strategy & Program Support Office
Carlos R. Solís, Program and Financial Analyst, Strategy & Program Support Office
Eduardo Chirinos, Senior Program Management Specialist
Todd Hammer

U.S. Government Programs
Ing. Antonio Coello, USAID Rural Diversification Program
Lorna Grace, MCC Farmer Access to Credit Program
Enrique Hennings, MCC Farmer Access to Credit Program
Andrew Medlicott, MCC Training and Development for Farmers Program

Government of Honduras
Lic. Ana Murillo Reina, Assistant Secretary, Ministry of Industry and Trade
Manuel de Rodríguez Luque, Banco Central de Honduras
Efraín Suárez, Banco Central de Honduras
Dina L. Ruiz, Superintendencia de Bancos, Financieras y Asociaciones de Ahorro y Préstamo
Alex Lagos, Superintendencia de Bancos, Financieras y Asociaciones de Ahorro y Préstamo
Hector Rene Rodriguez, Comisión Nacional de Bancos y Seguros
Ramón Rosalio Rosales, Banco Nacional de Desarrollo Agrícola

The Covelo Foundation
Juan José Lagos, General Manager
María Victoria Lagos
Maria Elena Carias

Bancovelo
Walter Chávez
Carlos W. Cruz
Victor Rheinboldt
Omar Rivera

Other Honduran Financial Institutions and Development Organizations
Indiana Flores de Sanabria, REDMICROH
Rodrigo Pineda, Federación de Cooperativas de Ahorro y Crédito de Honduras (FACACH)
Esther Gravenkotter, Banco ProCredit
Zadik López, BAC / BAMER

Violeta Pacheco, Banco Atlántida
Juan Humberto Paredes, Banhcafe
Robert Ruiz Pineda, World Relief of Honduras
José René Banegas, PILARH OPDF
Francisco Madrid Reyes, Financiera Solidaria
Nancy Goyburo Reeves, Care Centroamérica
Jackson Argeñal Aguilar, Fundación Microfinanciera Hermandad de Honduras

International Financial Institution

Dante Mossi, Country Operations Officer, The World Bank

APPENDIX B – SURVEY OF MEMBERS OF REDMICROH: SURVEY FORM

Encuesta
USAID / Asistencia a la Fundación Covelo y al Crédito Agropecuario

Estimado miembro de la REDMICROH:

Durante los últimos años, USAID ha brindado apoyo a la Fundación Covelo para incrementar el acceso al crédito de los micro y pequeño empresarios, principalmente en el sector agropecuario. Actualmente, USAID ha contratado un consorcio (Segura/IP3) para realizar una evaluación del impacto que ésta asistencia ha tenido en el sector.

Por lo tanto quisiera pedirle a usted que responda a la siguiente encuesta. (Este instrumento complementa una serie de reuniones que un representante de USAID y un consultor han sostenido en los últimos días, con varios representantes del sector microfinanciero.) Sus respuestas serán utilizadas para complementar la información recopilada hasta la fecha. Le agradeceré muchísimo sus respuestas, y asimismo, el envío de la encuesta por correo electrónico, a más tardar el viernes el 1 de mayo. Gracias de antemano por su asistencia.

Su nombre (opcional): ____
El nombre de su organización: ____

Su organización es (favor marcar con una "x"):
- organización privada de desarrollo (OPD): ( )
- organización privada de desarrollo financiero (OPDF): ( )
- banco: ( )
- financiera: ( )
- otro (explicar): ( ) ________________________________

Fecha: ______________

Pregunta 1. ¿En qué año comenzó su organización a ofrecer créditos al sector MIPYME? ______

Pregunta 2. ¿Ha ofrecido su organización microcréditos al sector agropecuario? (sí o no) _____. Si es así, ¿en qué año? _______

Pregunta 3. A finales del año 2002 (31 de diciembre), ¿aproximadamente cuál era el valor de su cartera de crédito total en el sector MIPYME? (en lempiras) _________.
De esta cantidad, ¿aproximadamente qué porcentaje (%) estaba en créditos al sector agropecuario? _____% ¿En el sector de agroindustria? _______%

Pregunta 4. A finales del año pasado (31 de diciembre de 2008), ¿aproximadamente cuál era el valor de su cartera de crédito total en el sector MIPYME? (en lempiras) _________. De esta cantidad, ¿aproximadamente qué porcentaje (%) estaba en créditos al sector agropecuario? _______

Pregunta 5. Si actualmente su organización está ofreciendo créditos a los productores agropecuarios en el sector MIPYME, ¿cuáles son factores, de los señalados en el recuadro siguiente, que los han impulsado o han contribuido para que entren al sector o aumenten su oferta crediticia al mismo? Favor responder a cada factor mencionado a continuación:

Factor	**Importancia**			
	Muy importante	**Impor-tante**	**No impor-tante**	**No se**
La motivación social / para asistir a las personas de su región				
El deseo de crecer / buscar nuevos clientes / la rentabilidad del sector				
La competencia creciente en el área urbana				
El ejemplo exitoso de otra organización en este campo (si es así, el(los) nombre(s) de la(s) organizacion(es)): ____________________________				
Su propia experiencia acumulada en el sector				
Un paquete de información relevante (formatos, procedimientos, etc.) que la REDMICROH ha distribuido (bajo el nombre "Instructivo del proceso crédito agrícola", etc.)				
Alguna otra información o herramienta ofrecida por la REDMICROH (Favor especificar: __________________________)				
Alguna información, herramienta, asistencia técnica y/o capacitación que su organización ha recibido en los últimos años de otra organización, el gobierno o un donante, que los ha fortalecido (Favor especificar: __________________________)				
La mayor competitividad mostrada hoy en día por los				

Factor	**Importancia**			
	Muy importante	**Impor-tante**	**No impor-tante**	**No se**
productores del sector MIPYME				
Mejores garantías (ej: carta de constancia, contrato de compra, etc.) que hoy en día los productores pueden ofrecer / la asistencia técnica que ellos reciben del gobierno o un programa				
Reformas legales y/o de las políticas del Gobierno				
La entrada en este sector es una condición de algunos de los recursos o asistencia que su organización recibe de un donante o institución financiera				
Otros factores (favor especificar): ________________________________				

Pregunta 6. Para finalizar, opinaría usted que hoy en día, en comparación con la situación a finales del año 2002, los productores agropecuarios del sector MIPYME tienen (favor elegir *una* respuesta):
( ) más acceso al crédito
( ) menos acceso al crédito
( ) el mismo acceso que antes

Favor explicar su respuesta:
____
____
____

Pregunta 7. Otros comentarios u observaciones relevantes:
____
____
____

¡Muchas gracias!

APPENDIX C – INSTITUTIONAL EVOLUTION OF COVELO FOUNDATION & RELATED ENTITIES (1991-PRESENT)

TABLE C-1. EVOLUTION OF COVELO FOUNDATION & RELATED ENTITIES (1991-PRESENT)

Year	Development
1991	José María Covelo Foundation (FJMC), a private development organization (OPD), established.
1995	FJMC begins to provide direct credit.
2003	Grupo Microfinanciero Covelo (GMC) established. At this point the FJMC is a "holding" of the GMC. The holding includes the Fundación Microfinanciera Covelo (a distinct legal entity from the FJMC), a savings and loan association (AAP) Popular, a second tier MFI, and other entities.
2006/2007	The reengineering and a new strategic orientation of GMC approved. The creation of Bancovelo is approved internally.
Sept. 2006	The Fundación Microfinanciera Covelo is authorized by the Government to operate as a financial OPD (i.e., an OPDF).
1 Jan. 2007	The Fundación Microfinanciera Covelo OPDF effectively ceases to function as it transfers its portfolio to Popular AAP (an interim measure before Bancovelo is licensed).
Jan. 2008	Bancovelo is formally licensed; it opens its doors on 1 February. Subsequently the Fundación Microfinanciera Covelo OPDF is dissolved.
June 2008	Most of the Foundation's/AAP's loan portfolio is transferred to Bancovelo. Ownership of the agricultural portfolio, as well as of other loans that carry DCA guarantees, and loans in default, remains with FJMC; however these loans are administered by Bancovelo. At the same time the FJMC provides technical assistance and other services to the microfinance sector.

Sources: Grupo Microfinanciero Covelo, "Fundación José María Covelo," 14 April 2009; and communications with María Victoria Lagos, 28-30 April 2009.

APPENDIX D – HONDURAS EVALUATION FRAMEWORK AND INDICATORS

EVALUATION QUESTIONS* [Note that text in **bold** below corres-ponds to the **pyramid**, "Measuring success of DCA guarantees"]	DATA SOURCES (1) pre-field activities (2) field activities	DATA COLLECTION METHODS (1) pre-field activities (2) field activities	HOW DCA WILL USE EVALUATION FINDINGS, CONCLUSIONS & RECOMMENDATIONS
OUTPUT LEVEL			
1. **Loans disbursed –** Did Bancovelo use the guarantee facility? Did guaranteed loans correspond to initial objectives and parameters?	(1) Credit Management System (CMS) data (1) DCA documents: - Action Memoranda - Guarantee Agreements - Credit Review Board (CRB) minutes - Biennial Review (1) or (2) Bancovelo annual report (2) Mission/ contractor/ staff (2) Bank staff (2) Other bank documents	(1) & (2) Interviews of cognizant USAID and contractor staff (2) Review of bank documents (2) Guided interviews with bank staff (HQ & branches)	Purposes 2, 3 & 4 above. To enhance discussions with potential guarantee partners. (Output data will respond to Purpose 1, above.) This question is primarily *descriptive*.
2. Additionality – What potential market did the DCA guarantee help open for the partner bank? How did the DCA guarantees fit into Bancovelo's ongoing strategy? Did Bancovelo's use of the DCA guarantee improve access to credit for the target sectors? If so, how much local private capital was mobilized ("**leveraging**")? Did characteristics of	(1) CMS (1) DCA biennial reviews (1) DCA portfolio managers (1) or (2) Bank annual reports (1) or (2) Industry/Central bank studies	(1) Analysis of CMS data (1) Documents review (1) Interviews of cognizant DCA staff (2) Guided Interviews of partner bank staff (2) Analysis of bank electronic files on borrowers covered by	Purposes 1, 3 & 4, above. The question is primarily *explanatory*, i.e., the extent to which the DCA guarantees directly influenced change. Secondarily it is *descriptive* and *comparative*; it addresses what happened with loans under guarantees vs. what would likely have happened without the guarantees. What we learn can affect what DCA does when: talking to potential and actual guarantee

EVALUATION QUESTIONS* [Note that text in **bold** below corres-ponds to the **pyramid**, "Measuring success of DCA guarantees"]	**DATA SOURCES** (1) pre-field activities (2) field activities	**DATA COLLECTION METHODS** (1) pre-field activities (2) field activities	**HOW DCA WILL USE EVALUATION FINDINGS, CONCLUSIONS & RECOMMENDATIONS**
guaranteed loans differ from other loans in ways that improved access?	(2)Mission technical officers and TA providers (2) Bank managers/staff (HQ & branches) (2) Bank electronic files (as available) or samples of files	guarantee (either sample of or full DCA loan portfolio)	partners (e.g., asking them what they would change with a guarantee; encouraging banks to do x, y, or z); providing technical assistance (TA) and training to banks; and encouraging missions to provide TA and training to banks.
3. How did Bancovelo implement its loan guarantee program (e.g., marketing campaigns, changed terms, training, revised staff structure and responsibilities, improved communications with branch offices, etc.)? And why?	(2) Mission/ contractor/ staff (2) Bank staff (2) Bank documents	(1) & (2) Interviews of cognizant USAID and contractor staff (2) Review of bank documents (2) Guided interviews with bank staff (HQ & branches)	Purposes 2, 3 & 4. The response will inform the training that DCA provides to guarantee partners, missions, et al.

EVALUATION QUESTIONS* [Note that text in **bold** below corres-ponds to the **pyramid**, "Measuring success of DCA guarantees"]	DATA SOURCES (1) pre-field activities (2) field activities	DATA COLLECTION METHODS (1) pre-field activities (2) field activities	HOW DCA WILL USE EVALUATION FINDINGS, CONCLUSIONS & RECOMMENDATIONS
OUTCOME LEVEL			
4. **Partner bank behavior change** – Did Bancovelo improve access to credit to the target sectors outside the DCA guarantees? Did it move into any new sectors/industries, types of borrowers, types of loans, or loan terms? If so, how and why and to what extent were the DCA guarantees responsible for improving access of Bancovelos' customers to credit outside the guarantees?	(1) CMS data review (1) DCA documents: Risk assessments, Action Packages, Legal Agreements, CRB minutes, biennial reviews, OMB PART (1) or (2) Mission documents (2) Bank electronic files (as available) or samples of files (2) Bank annual reports (2) Mission/ contractor/ staff (2) Bank staff	(1) Analysis of CMS data (1) Documents review (2) Interviews of cognizant Mission / contractor staff and other stakeholders (2) Guided Interviews of partner bank staff (2) Analysis of bank electronic files on borrowers covered by guarantee (either sample of or full DCA loan portfolio)	Purposes 1, 2, 3 & 4 above; to identify ways to achieve desired outcomes when dealing with potential guarantee recipients; to enhance the training that DCA provides to guarantee partners, missions, et al. The first part of the question is both *descriptive* and *comparative* – actual outcomes achieved through guarantees vs. intended outcomes. The second part of the question is *explanatory* in nature – to identify factors associated with why desired outcomes were achieved or not.
5. What factors at Bancovelo were responsible for achieving desired outcomes (e.g., TA; bank staff training; revised bank strategy, procedures and structure; new management, etc.)?	(1) TA documents (2) Mission/ contractor/ staff (2) Bank staff	(1) Document review (2) Interviews of cognizant Mission / contractor staff and other stakeholders (2) Guided Interviews of partner bank staff	The question is *explanatory* in nature – to identify factors associated with why desired outcomes were achieved or not.

EVALUATION QUESTIONS* [Note that text in **bold** below corres-ponds to the **pyramid**, "Measuring success of DCA guarantees"]	**DATA SOURCES** (1) pre-field activities (2) field activities	**DATA COLLECTION METHODS** (1) pre-field activities (2) field activities	**HOW DCA WILL USE EVALUATION FINDINGS, CONCLUSIONS & RECOMMENDATIONS**
IMPACT LEVEL			
6. **Market demonstration effect** – Did other, non-partner banks initiate or increase lending to the target sectors? If so, to what extent was the DCA guarantee to Bancovelo responsible? How and why?	(1) and (2) Sector/banking reports (if available) (2) Guarantee partner (bank) managers/staff (2) Industry/bank associations in the country/sector (2) Non-partner banks (2) USAID TA providers (2) Other key stakeholders	(1) and (2) Documents review (2) Interviews of cognizant USAID / other donor staff /other stakeholders (2) Interviews of apex organizations and bank staff	Purposes 1 & 2. This question will be answered qualitatively, for the most part, citing available sectoral data as appropriate.
7. (**Same**) Did access to loans (or loan terms) improve for loans to the target sectors? If so, how and why? What role if any did the DCA guarantee play as a demonstration model?	(2) Associations of micro- and small enterprises (MSEs) and related Otherwise, same as for Question 6.	Same as for Question 6.	Same as for Question 6.

EVALUATION QUESTIONS* [Note that text in **bold** below corres-ponds to the **pyramid**, "Measuring success of DCA guarantees"]	**DATA SOURCES** (1) pre-field activities (2) field activities	**DATA COLLECTION METHODS** (1) pre-field activities (2) field activities	**HOW DCA WILL USE EVALUATION FINDINGS, CONCLUSIONS & RECOMMENDATIONS**
QUESTION THAT APPLIES TO ALL THREE LEVELS—OUTPUT, OUTCOME AND IMPACT			
What are the exogenous factors (e.g., financial sector reform, government intervention, lender industry competition, financial shocks, etc.) that have affected the financial sector? How have they done so? Have these factors affected the performance of the DCA guarantee(s) (i.e., at output, outcome and impact levels)? If so, how?	(1) Review of World Bank, and other donor or research documents / web sites (2) Cognizant USAID / contractor staff / other donors (2) Guarantee partner managers/staff (2) Key stakeholders (e.g., central banks, banking associations, etc.)	(1) Documents review (2) Interviews of cognizant USAID / contractor staff (2) Guided interviews of partner bank staff (2) Other donor / key stakeholder interviews	To set in context the evaluation findings. This question is *explanatory* in nature.

EVALUATION QUESTIONS	INDICATOR	ANALYSIS
OUTPUT LEVEL		
1. Did Bancovelo use…?	Number and volume (in USD) of guaranteed loans	Rate of use over time. If did not use, why?
2. …How much local private capital was mobilized ("leveraging")?... Did characteristics of guaranteed loans differ from other loans in ways that improved access?	Ratio of total private capital resources that are leveraged in the form of loans, relative to the guarantee ceiling	Leveraging of development resources
	Loan Portfolio	
	Number and total value of guaranteed loans to target sectors, relative to all loans to target sectors (beginning with pre-guarantee baseline)	Comparison of *number and total value* of guaranteed loans to all loans to target sector.
	Percentage of new borrowers in guaranteed loans to target sectors, relative to all loans to target sectors	Comparison of % of *new borrowers* for guaranteed loans relative to all loans in portfolio to target sector.
	Loan Terms	
	Average, median, and largest loan size and frequency distribution of guaranteed loans to target sectors, relative to all loans to target sector	Comparison of *loan sizes* of guaranteed loans to all loans in portfolio to target sector.
	Average and longest loan tenor for guaranteed loans to target sectors, relative to all loans to target sector	Comparison of *loan tenor* of guaranteed loans relative to all loans in portfolio to target sector.
	Average interest rate for guaranteed loans to target sectors, relative to pre-guarantee baseline	Comparison of *interest rates* for guaranteed loans relative to all loans in portfolio to target sector.
	Loan Collateral	
	Average percentage collateral requirement for guaranteed loans to target sectors, relative to all loans to target sectors	Comparison of *collateral requirement* of guaranteed loans relative to all loans in portfolio to target sector.
	% of collateral that is land for guaranteed loans to target sectors, relative to all loans to target sectors	Comparison of *land as a % of collateral* of guaranteed loans relative to all loans in portfolio to target sector.
3. How did Bancovelo implement…?	n.a.	n.a.

EVALUATION QUESTIONS	INDICATOR	ANALYSIS
OUTCOME LEVEL		
4. Did Bancovelo improve access to credit to the target sectors outside the DCA guarantees? Did it move into any new sectors/industries, types of borrowers, types of loans, or loan terms? If so, how and why and to what extent were the DCA guarantees responsible for improving access of Bancovelos' customers to credit outside the guarantees?	**Loan Portfolio**	
	--	Extent of DCA influence on access to credit without DCA guarantee, to: (i) target sectors, (ii) other sectors
	Number and value of non-guaranteed loans to target sectors relative to pre-guarantee baseline (*absolute* improvement in access)	Comparison of pre-guarantee value to annual values during guarantee period. Increase may mean that entire portfolio has increased while relative access for target sectors remains unchanged.
	Value of all loans to target sector relative to total loan portfolio (*relative* improvement in access)	Evolution of relative importance of lending to target sector versus other sectors. Increase implies improved access relative to other sectors.
	Percentage of new borrowers in target sectors relative to pre-guarantee baseline	Comparison of pre-guarantee proportion of *new borrowers* in target sectors to proportion of new borrowers during guarantee period.
	Number of new sectors developed by Bancovelo	Development of new sectors/industries
	Loan Terms	
	Average (and median) size and frequency distribution of all loans to target sectors relative to pre-guarantee baseline	Comparison of pre-guarantee distribution of *loan sizes* to distribution during guarantee period.
	Average tenor for all loans to target sectors relative to pre-guarantee baseline	Comparison of pre-guarantee *loan tenors* to tenors during guarantee period.
	Average interest rate for all loans to target sectors relative to pre-guarantee baseline	Comparison of pre-guarantee *interest rates* of loans in target sectors to interest rates during guarantee period.
	Loan Collateral	
	Average percentage collateral requirement for all loans to target sector relative to pre-guarantee	Comparison of pre-guarantee *collateral requirements* to requirements during guarantee period.

EVALUATION QUESTIONS	INDICATOR	ANALYSIS
	baseline	
	Percentage of collateral that is land for loans to target sectors relative to pre-guarantee baseline	Comparison of pre-guarantee proportion of *collateral in land* in targeted sectors to proportion of collateral in land during guarantee period.
5. What factors at Bancovelo were responsible for achieving desired outcomes (e.g., TA; staff training; revised strategy, procedures and structure; new management, etc.)?	Extent of DCA influence on expansion into new sectors/industries/types of borrowers	Influence of DCA.
	Importance of TA relative to other factors	Relative importance of TA.
IMPACT LEVEL		
6. Did other, non-partner banks initiate or increase lending to the target sectors? If so, to what extent was the DCA guarantee to Bancovelo responsible? How and why?	Number of non-partner banks initiating or increasing lending to target sectors since DCA Extent of DCA influence on expansion into new sectors/industries/types of borrowers	--
7. Did access to loans (or loan terms) improve for loans to the target sectors? If so, how and why? What role if any did the DCA guarantee play as a demonstration model?	Improved target sectors access to loans from banking sector (yes/no) Extent of DCA influence on improved access to credit	--
QUESTION THAT APPLIES TO ALL THREE LEVELS – OUTPUT, OUTCOME AND IMPACT		
What are the exogenous factors…?	n.a.	Note that, per Figure 1, the "influence of exogenous factors" is low for outcomes and high for impacts.