

This newsletter is published semi-annually and is targeted to microfinance investment practitioners. It reviews and highlights key facts of Symbiotics' research and investment activity during the past semester.

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Research, knowledge & innovation

Business intelligence platform

www.symbiotics.ch is meant to highlight symbiotics research and investment work, and contribute to its transparency, development and innovation.

Symbiotics is concentrating its current research and development on what it has identified as key challenge for the facilitation of microfinance investments. The list focus items include fund indexes, fund ratings, fund social impact reporting, MFI benchmarks, MFI credit analysis, MFI live performance tracking, transaction risk assessments, investment pricing structures, general industry news, trends and research. •

Fund index: USD, EUR, CHF

Symbiotics has launched a series of fund indexes, meant to track the risk-return profiles of key investment funds.

The Symbiotics fund index methodology follows the practice of index professionals. The challenge of designing a microfinance fund index resides in fund industry structure and maturity. Funds are many, diffuse and often very different; the level of transparency and standardization does not allow yet for the construction of an exhaustive industry index. Symbiotics has designed a set of eligibility criteria and a calculation methodology fitting with the industry current status.

Index eligibility criteria include: (1) being a legal entity registered as an investment fund or sub-fund with shares denominated in USD; (2) publishing a monthly net asset valuation or rate of return; (3) having a majority of investments directly or indirectly related to micro, small and medium enterprise financing;

(4) having a majority of fixed income assets; and (5) having a multi-country focus.

The index is calculated by the 10th of each month. Each constituent fund or sub-fund is equally weighted in the index. The index return is calculated using the average monthly return of each constituent fund or sub-fund share price and assumes full capitalization of earnings.

The index volatility is calculated as the annualized monthly standard deviation of the index rate of return, using data since the index inception. The volatility should be treated with caution if used as a measure of risk as the underlying implied rating of the portfolio would induce a much higher level of risk than the money market type track records of the underlying funds composing the index. None of them have yet experienced any payment default, which would induce loan valuations below par.

The SMX USD currently includes the performance of (1) Dual Return Fund Vision Microfinance USD Cap, (2) responsAbility Global Microfinance Fund B Cap, (3) Dexia Micro-Credit Fund Sicav BlueOrchard Debt USD Cap, (4) Finethic Microfinance SCA SICAR USD.

The SMX EUR currently includes the performance of (1) Dual Return Fund Vision Microfinance EUR Cap, (2) responsAbility Global Microfinance Fund HC Cap, (3) Dexia Micro-Credit Fund Sicav BlueOrchard Debt EUR Cap, (4) ST Honoré Microfinance A EUR Cap.

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The SMX CHF currently includes the performance of (1) responsAbility Global Microfinance Fund H CHF Cap, (2) Dexia Micro-Credit Fund Sicav BlueOrchard Debt CHF Cap. •

MFI benchmark

Symbiotics has launched a microfinance institution benchmark, called the 'Symbiotics 50', which tracks key performance indicators and data of a selection of 50 microfinance institutions representative of the industry.

The benchmark offers investors and fund managers with a tool to compare the performance of any single MFI and therefore acts as a guiding tool in their investment decisions.

The benchmark is composed of seven reports and more than 200 output reporting lines. It covers financial, operational and clientele information. •

Credit risk & investment analysis reports

Symbiotics' credit risk and investment analysis team visits and evaluates microfinance institutions. The result is a 25 page report on each institution that enables the investment or fund manager a complete assessment of all aspects of an institution performance and risks. The team has currently published 76 reports on 65 institutions.

Each report also includes an internal rating, using a "S&P/Fitch" rating scale as the final output. The internal rating is meant as a proxy for the investor/fund manager to evaluate and classify the risk of its investment in its portfolio. It is also used as a benchmark for negotiating the terms of the investment.

Although some microfinance institutions, such as large regulated banks already have public ratings, the vast majority of microfinance institutions lack such credit risk assessment. This is also the case in any small caps market segment, whatever the industry. Where large institutions get rated and issue public placements, smaller actors raise private placement and get assessed by their investors. The Symbiotics credit risk and investment analysis reports are meant to fulfil this function in the lower segment of the market, on behalf of its investor clientele.

Symbiotics credit risk assessment methodology is based on a credit scoring encompassing 60 indicators about half of which are quantitative. •



Pricing based on risk

A key challenge for the microfinance investment business is to evaluate the price and risk of fixed income investments. The industry is still young and has a double bottom line, with large volumes of seed money focusing more on the social development aspect than on the financial profitability. The Symbiotics February 2006 newsletter has shown an example of the important diversity of pricing in the Peruvian microfinance market, compared to Peruvian corporate bond issuances. This

example shows no correlation between risk and interest rate pricing (R^2 is nil), compared to an R^2 close to 1 for corporate bond market.

To contribute to helping investors understand the price-risk correlation and find adequate pricing structures, Symbiotics discloses for all fixed income transactions it originates, their respective risk premium, country ceiling, internal rating, volume and maturity.

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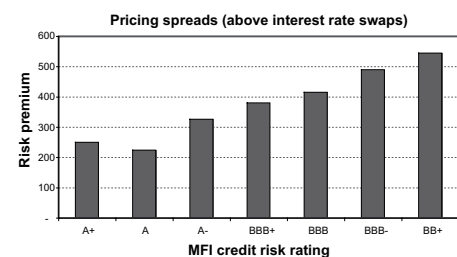
Another challenge in the pricing of microfinance investments is their low correlation to country risk. Rating agencies haven't yet established the relevance (or not) of rating microfinance banks above the sovereign ratings or notching them down such sovereign rating for off-shore investments. Symbiotics uses as a country risk proxies the most conservative rating of either Fitch Ratings or Moody's country ceilings or Standard & Poor's sovereign rating. Such country risk rating induces at any given date a market-determined country risk premium that would normally need to be charged on any given transaction.

Symbiotics also uses its internal ratings or public ratings when available to assess the credit risk premium that would be implied by any given transaction.

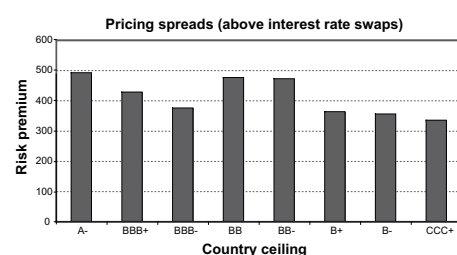
Symbiotics' past 79 transactions can be distributed as follows according to both country risk and credit risk:

		Credit Risk								Total
		A+	A	A-	BBB+	BBB	BBB-	BB+	NR	
Country Risk	A+									3
	BBB+				2		3			5
	BBB				1			1		2
	BB			2	5	8	9	4		28
	BB-				6					6
	B+					2	3			5
	B-	2	2	2		1	2	3		12
	CCC+			2	1					3
	NR		1		3	3	5	1	2	15
	Total	2	3	6	18	14	25	9	2	79

This theoretical pricing setting guideline is of course challenged by both market reality and competitive pricing. An analysis of Symbiotics' pricing structure broken down by credit risk shows a natural correlation between higher risk and higher credit risk premiums.



The same analysis with a breakdown by country risk shows nevertheless no real correlation between risk and premium, maybe pointing to the lower considerations given to political risk in microfinance investment decisions.



Whether this validates the assumption that microfinance sectors are not correlated to political risks or whether it highlights the young stage of development of the industry is still to be shown. •

Fund reporting, rating & social impact

Where the transparency on microfinance institution risk and performance has greatly improved over the past years, the transparency on investment vehicle reporting and analysis is still very low.

Investors have expressed a strong desire to not only track a fund's performance, but to also evaluate its risk and its social impact as most microfinance investors are attracted by the double bottom line of their investments (or even in some cases only by its social impact). Symbiotics has developed a fund fact sheet and analysis concept which includes structural data, a social impact assessment, an asset risk evaluation, portfolio distribution information and performance indicators.

use monthly valuation figures, to offer constant tracking and trend analysis to investors and fund managers.

Symbiotics' fund reporting is offered as a service to any fund specialized in microfinance desiring a standardized and expert reporting and analysis pack. •

Industry newsroom

Symbiotics tracks industry news; it offers on its public website a selection of microfinance news, updated several times a week. Visitors can also register to the RSS feed to receive constant news updates. •

Books & articles

Jean-Michel Servet publishes "Barefoot bankers – microfinance"

Jean-Michel Servet, Director of Symbiotics and Professor at the Institute of Development Studies in Geneva, has published in October his latest book on microfinance "Barefoot bankers – microfinance" (Odile Jacob, 511 p.)



The book traces fifteen years of his research and microfinance field experience in Asia and Africa. Compiled during the Year of Micro-Credit and published just before the 2006 Nobel Peace Prize nomination, the book analyses the industry and challenges its limits in a period of "exponential leap". The book reflects on the roots of microfinance, the increasing influence of finance in social interactions (the increasing 'financiarisation' of societies as the author refers to) and the function of money in development. It collects examples of financial models for the poor which are either inherited

The social impact of any given fund is analysed at the micro-enterprise level, the microfinance institution level and the country level. The assumption is that the more the fund is inclusive the more social value it generates. Symbiotics thus tracks the capacity of a fund to reach out horizontally and vertically for the democratization of access to capital.

Fund asset risk assessments are done over the composition of the portfolio, using the available credit ratings of each underlying investment in the portfolio. The fund governance, management, information systems and operations are not taken into account in the asset risk assessments.

Fund performance and volatility calculations

from local traditions or imported from abroad. The book develops on the core value of microfinance for development and emphasizes on its intrinsic contribution to development. It nevertheless insists on its focused and limited goal and impact, pointing to the risk of forgetting the big picture by pushing all development responsibility on the back of single vulnerable individuals. Jean-Michel Servet roots for the inclusion of microfinance in a larger framework of development finance and cooperation, emphasizing the determinant role of public and systemic development. As he quotes from a peer philosopher “selling candle sticks has not created electric light bulbs”.

Although only available in French language today, the book is a delight for newcomers to the industry or experienced practitioners wanting to revisit some of the current common sense on the industry. •



Cédric Lombard publishes an article in “Property Rights and Microfinance”



“Realizing Property Rights” is the first volume of a set of books exploring Human Rights. (Article 17 of the Human Rights Declaration states that “*everyone has the right to own property alone as well as in association with others*” and “*no one shall be arbitrarily deprived of his property*”).

The book was published at the initiative of the Swiss Department of Foreign Affairs, and edited by Hernando de Soto, the leading advocate of the recognition of such rights in developing countries, with a particular focus on the inclusion of the informal sector, and Professor Francis Cheneval, teaching political philosophy at the University of Zurich.

Cédric Lombard, head of credit risk and investment analysis at Symbiotics, contributed to the book in an article showing that MFIs have been able to provide financial services to micro-entrepreneurs without any asset backed collateral or property, contrary to general credit practice. Indeed MFIs are considering the person, its household and its entrepreneurial risk before considering the collateral, and have also been able to develop new modes of guarantee such as solidarity groups.

The article also shows how access to microfinance services have enabled people to progressively build assets and value them, in their daily life but also to leverage off them.

The article reviews how client driven changes have generated changes in the nature of the MFIs, in their legal structure, in their ownership and sometimes in their very mission and vision. As clients increase their fixed assets and skills, their needs and aspirations evolve in parallel. Access to property rights is a good example of such client development and the micro-banker’s need for more sophisticated products and often reengineered internal processes and skills.

The article is a good summary journey, at both the micro-entrepreneur level, “from survival to growth via collateral”, at the MFI level, through client driven transformation.

For more information:

Philipp Jung contributes to “Innovation in Securitisation – Yearbook 2006”

Philipp Jung, head of structured finance at Symbiotics, has contributed together with Per-Erik Eriksson from the European Investment Fund (EIF) to the Yearbook 2006 “Innovation in Securitisation” (Kluwer Law International) with an article on “Microfinance Loan Obligations – Structured finance for microfinance”.

The article sets the stage for a microfinance CDO platform and describes the first series of issuance through this platform: “Opportunity Eastern Europe 2005-1”.



The platform, “Microfinance Loan Obligations S.A.”, is a Luxembourg securitization company, issuer of asset-backed notes whose proceeds are used to extend fixed income investments to microfinance institutions worldwide.

On October 18th, 2006 the third closing arranged by EIF and Symbiotics enabled a total EUR 25 million financing for Opportunity International affiliates in Russia and the Balkans. The transaction included term loans and a credit derivative that secured funds for an equivalent additional 10,000 micro, small and medium enterprises.

Investor notes were issued in three classes of seniority. Senior notes are fully guaranteed by the European Investment Fund and sold to institutional investors. Mezzanine and Junior notes were sold to specialized investment funds.

The full article is available at



Investment brokerage, servicing & monitoring

Brokerage

Symbiotics started originating investments in the second quarter of 2005, although its brokerage activity really started a year later with USD 20 million in the second quarter 2006, USD 29 million in the third quarter and USD 24 million in the fourth quarter as of date of publication.

The current broker list includes seven transactions ready to close, for a total of USD 5-6 million. Investment range from 12 to 36 months and from BB to CCC+ country ceilings and A+ to BB+ credit risk ratings. Clients access the broker list on Symbiotics web interface and book investments match-

ing their investment strategy and guideline. Each booking gives access to an investment proposal, including full underwriting and credit risk analysis. In parallel to closing discussion, the on-line system allows for constant status tracking and document archiving. ▶

Servicing

Breakdown of the cumulative transactions by disbursement date and region

Since inception, Symbiotics has originated more than USD 80 million of investments through its brokerage platform.

Just about half of the volume is concentrated in Central & Eastern Europe and another quarter in Russia, Caucasus & Central Asia. In terms of number of transactions though, these two regions represent about half with a larger amount of smaller transactions in Latin America and Asia. ▶

Monitoring

The following credit risk and investment analysis reports have been published during the past semester.

<u>Institution</u>	<u>Country</u>
Aceda Bank	Cambodia
AFK	Kosovo
AMA	Peru
Banco Solidario	Ecuador
BancoSol	Bolivia
BTFF	Kyrgyzstan
Cáritas del Perú	Peru
CCAMETRO	El Salvador
CMAC Ica	Peru
COAC Progreso	Ecuador
Confianza	Peru
Crear Arequipa	Peru
Crecer	Bolivia
CredAgro	Azerbaijan
Ecofuturo	Bolivia
FINCA Azerbaijan	Azerbaijan
FINCA Kosovo	Kosovo
FINDESA	Nicaragua
FMCC	Kyrgyzstan
Forus Bank	Russia
KLF	Kazakhstan
Kompanion	Kyrgyzstan
MFBA	Azerbaijan
MFW	Jordan
Microinvest	Moldova
Mikrofond	Bulgaria
Moznosti	Macedonia
OBM	Montenegro
OMRO	Romania
Pro Mujer Bolivia	Bolivia
PSHM	Albania
RWMN NDCO	Russia
Satin	India
TSKI	Philippines

Symbiotics tracks today over 80 institutions on a monthly basis and over a hundred on an annual basis. It published over 65 credit risk and investment opportunities reports.

The full list is available at www.symbiotics.ch ▶

Please feel free to contact us if you have any questions or comments.

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