OFFICE OF INSPECTOR GENERAL

# AUDIT OF USAID/EGYPT'S MICROFINANCE ACTIVITIES

AUDIT REPORT NO. 6-263-08-004-P
MAY 27, 2008

CAIRO, EGYPT

*Office of Inspector General*

May 27, 2008

**MEMORANDUM**

**TO:** USAID/Egypt Director, Hilda Arellano

**FROM:** Regional Inspector General/Cairo, Lloyd J. Miller /s/

**SUBJECT:** Audit of USAID/Egypt's Microfinance Activities (Report No. 6-263-08-004-P)

This memorandum transmits our final report on the subject audit. We have considered your comments on the draft report and incorporated them where appropriate. They are included in their entirety as appendix II.

This report includes 10 recommendations to USAID/Egypt: (1) to develop procedures for future agreements to ensure that the mission receives written commitments from microfinance institutions to attain full financial sustainability within 7 years before an agreement is signed, (2) to receive written commitments to attain full financial sustainability within 7 years from existing microfinance institutions with signed agreements, (3) to require all microfinance institutions to develop business plans that incorporate performance targets, (4) to approve an implementation plan which identifies activities with clear baselines and targets to assess progress, (5) to approve performance indicators for technical assistance that align with established performance indicators in the USAID/Egypt's performance management plan, (6) to require the implementer to report on approved performance indicators in its quarterly progress reports, (7) to develop a written action plan for oversight by the cognizant technical officer including documented site visits to assess progress against targets and the completion of tasks stipulated in awards or annual plans, (8) to establish and document specific procedures, including data entry and verification, to ensure the accuracy of microfinance information reported to Congress, (9) to assess the technical assistance for microfinance institutions to determine if the unique needs of each microfinance institutions are being met and revise the unique assistance for each microfinance institution accordingly, and (10) to establish a branding strategy for microfinance institutions as defined in ADS 320.6.

As a result of missions actions to implement each of the recommendations, management decisions and final actions have been completed for recommendations nos. 1, 2, 3, 4, 5, 6, 7, 8, 9. Determination for final action for recommendation no. 10 will be made by the Audit Performance and Compliance Division (M/CFO/APC) upon completion of the actions planned by the mission.

Thank you for the cooperation and courtesy extended to the audit team during this audit.

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# SUMMARY OF RESULTS

In calendar year 2006, USAID/Egypt's microfinance project was the second-largest USAID microfinance loan provider worldwide. USAID/Egypt is the largest financier of microfinance initiatives in Egypt, supporting an estimated 70 percent of all Egyptian microfinance activity. Since 1997, USAID/Egypt has provided microfinance assistance at a cost of $86.6 million. USAID/Egypt implemented its microfinance project through seven not-for-profit microfinance institutions operating in different regions of the country, two banks, and one private organization, the Credit Guarantee Company to assist in the delivery of credit to small businesses that lack sufficient collateral to obtain loans. This audit reviewed the loan portfolio and operations of three microfinance institutions—Alexandria Business Association, Assiut Businessmen Association, and the Lead Foundation—each with a current cooperative agreement supported by USAID/Egypt. In addition, the audit reviewed the operations of the private Credit Guarantee Company. The reviewed institutions had 212,144 active clients (35 percent) of the 614,899 active clients served by all of the USAID-supported institutions (see page 3).

As part of a worldwide audit, the Regional Inspector General/Cairo (RIG/Cairo) performed this audit to answer the following questions (see page 4):

- Did USAID/Egypt implement its microfinance activities efficiently?
- Did USAID/Egypt's microfinance activities achieve planned results?

Regarding the efficiency of activities, for calendar year 2006, USAID/Egypt did not implement its microfinance program efficiently, having met 7 of 18 international benchmarks for the three microfinance institutions reviewed. Over 2005 and 2006 for the three microfinance institutions reviewed, USAID/Egypt has increasingly managed its microfinance activities efficiently, as shown by indicators measuring financial efficiency, portfolio quality, and staff productivity (see page 5). However, the audit found that the USAID/Egypt Mission did not receive financial sustainability commitments before agreements were signed with the microfinance institutions (see page 8).

Regarding results, USAID/Egypt microfinance activities achieved planned results for fiscal years 2005 and 2006 (see page 9). Furthermore, a statistically projectable sample, at the 95 percent confidence level, tested supporting documentation and purposes of each loan with the borrowers themselves, including data on loan amounts, loan types, loan terms, funding sources, fees, and program awareness. The audit team found one exception: one of the microfinance institutions was not acknowledging the source of funds from the American people (see page 17). Based on USAID/Egypt's reported results and the statistical survey of sampled microfinance borrowers, RIG/Cairo determined that the microfinance project was making a positive impact for its beneficiaries (see page 10).

However, not all the results were positive. For example, a cooperative agreement with the Credit Guarantee Company resulted in 17 new branches providing credit instead of the 30 planned in the agreement. Given that this agreement has ended, this audit does not make a recommendation. However, the audit identified several issues that, if addressed, could improve USAID/Egypt's management of its microfinance project (see page 10):

- Microfinance institutions need performance-based business plans.
- The mission has not monitored the progress of technical assistance to microfinance institutions.
- Site visits to financial institutions and technical assistance contractor need strengthening.
- Microfinance reports to Congress were inconsistent with USAID/Egypt financial records.
- Recipients questioned the value of technical assistance.
- Branding strategy is needed.

USAID/Egypt agreed with all the report recommendations and outlined its actions to implement each recommendation (see pages 23 to 31).

# BACKGROUND

In calendar year 2006, USAID/Egypt's microfinance project was the second-largest USAID microfinance loan provider worldwide. USAID/Egypt has funded its current $86.6 million microfinance[1] project since 1997. The purpose of the project is to increase employment and income for Egypt's low-income entrepreneurs, particularly women heads of household. USAID/Egypt is the major financier of microfinance initiatives in Egypt, supporting an estimated 70 percent of all Egyptian microfinance activity. Microfinance activities in Egypt focus on providing loans to the economically active poor. To illustrate, this audit report contains photographs of five recipients who received loans for their small business in making shoes, selling textiles, raising chickens and ducks, manufacturing boxes, and running a barbershop. USAID/Egypt implemented its microfinance project through seven not-for-profit microfinance institutions operating in different regions of the country, two banks, and the private Credit Guarantee Company to assist in the delivery of credit to small businesses that lack sufficient collateral to obtain loans.

These USAID-supported institutions (the seven microfinance institutions, two banks, and the private Credit Guarantee Company) issued 1,024,051 loans valued at $145 million during calendar year 2006. In addition, they have an outstanding loan portfolio of $25 million. The portfolio serves approximately 593,000 active borrowers, with a default rate of less than 3 percent. Women's participation has been consistently above 64 percent, and most of these women are heads of households in Egypt's economically disadvantaged areas.

This audit reviewed the loan portfolio and operations of the three microfinance institutions—Alexandria Business Association, Assiut Businessmen Association, and the Lead Foundation—each having a current cooperative agreement supported by USAID/Egypt. The cooperative agreements for the Alexandria Business Association ($9.3 million) and the Lead Foundation ($17.2 million) covered start-up costs, training, and graduation amounts. The cooperative agreement for Assiut Businessmen Association ($1.0 million) covered only start-up costs and training. The graduation amounts for the Assiut Businessmen Association were covered by the cooperative agreement between USAID/Egypt and the Credit Guarantee Company.

This audit also reviewed the operations of the technical assistance contractor Chemonics International and the private Credit Guarantee Company. In January 2006, USAID/Egypt entered into a $5.4 million contract with Chemonics International to provide technical assistance for microfinance institutions funded by USAID/Egypt. In March 2003, USAID/Egypt awarded a cooperative agreement for $27.5 million to the Credit Guarantee Company to provide support for microenterprise and small and medium-sized enterprise development activities. This award ended in September 2007. The reviewed institutions had 212,144 active clients (35 percent) of the 614,899 active clients served by all of the USAID-supported institutions.

[1] Microfinance is a part of microenterprise development. Microenterprises are small, informally organized commercial operations owned and operated mostly by the poor. They constitute the majority of businesses in many countries, account for a substantial share of total employment and gross domestic product, and contribute significantly to the alleviation of poverty.

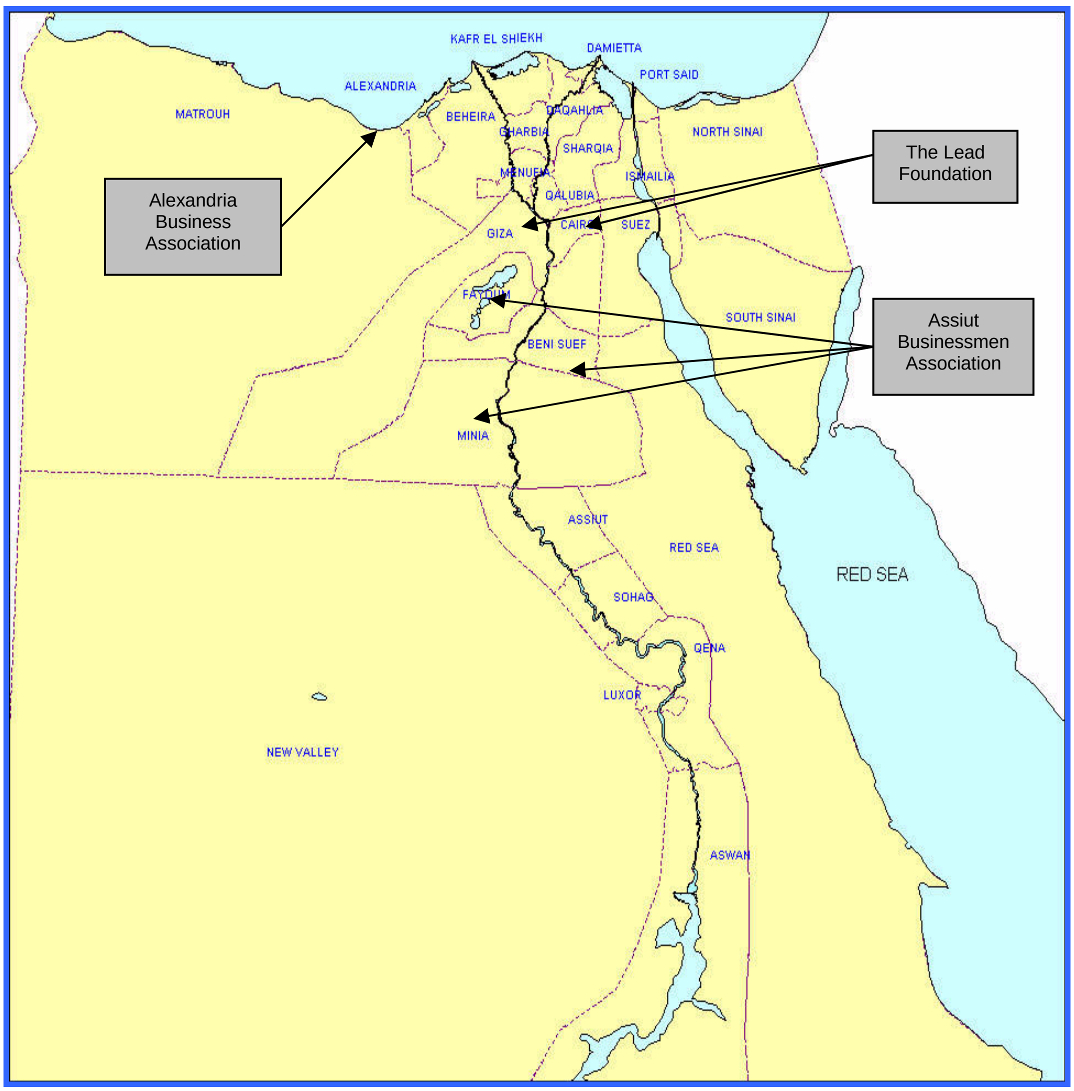
## AUDIT OBJECTIVES

This audit was conducted at USAID/Egypt as part of a worldwide audit of USAID's microfinance activities included in the Office of Inspector's General's fiscal year 2007 annual audit plan. The audit was conducted to answer the following questions:

- Did USAID/Egypt implement its microfinance activities efficiently?
- Did USAID/Egypt microfinance activities achieve planned results?

Appendix I contains a discussion of the audit's scope and methodology.

**Locations in Egypt of Microfinance Activities Reviewed**



# AUDIT FINDINGS

## Did USAID/Egypt implement its microfinance activities efficiently?

For calendar year 2006, USAID/Egypt did not implement its microfinance program efficiently, having met 7 of 18 international benchmarks for the three microfinance institutions reviewed. From calendar year 2005 to calendar year 2006, USAID/Egypt's microfinance program did show improvements in efficiency. This audit's determination was based on a comparison of results for six indicators,[2] with benchmarks for 2006 established by the Microfinance Information eXchange Market—a global, Web-based microfinance information platform that USAID/Egypt uses to measure the efficiency and performance of its microfinance institutions.

With regard to financial efficiency for both calendar years, all three microfinance institutions exceeded benchmark standards for the indicator "cost per active client" but did not meet the benchmark for "operating expense ratio." Even so, the operating expense ratio for each of the three institutions showed an improvement from 2005 to 2006. For the other four indicators for portfolio quality and staff productivity, in 9 of 12 cases the indicator benchmarks either did not change or improved from 2005 to 2006. Tables 1, 2, and 3 provide the results of the efficiency measures for the three microfinance institutions: Alexandria Business Association, Assiut Businessmen Association, and the Lead Foundation.

Table 1 shows that the Alexandria Business Association improved its operating expense ratio (which measures personnel and administrative expenses relative to the loan portfolio) from 18.5 percent in 2005 to 16.7 percent in 2006. The cost per client also slightly improved from 2005 to 2006. Other indicators also showed improvement.

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[2] The definitions for the six indicators were developed under USAID's Accelerated Microenterprise Advancement Project—"Measuring Performance of Microfinance Institutions: A Framework for Reporting, Analysis, and Monitoring."

- "Operating expense ratio" is measured by dividing operating expenses by the average gross loan portfolio of the institution.
- "Cost per active client" is measured by dividing operating expenses by the number of active borrowers.
- "Write-off ratio" is measured by dividing the value of loan written off by the average gross loan portfolio.
- "Portfolio at risk > 30 days" is measured by dividing portfolio outstanding over 30 days late by the gross loan portfolio.
- "Borrowers per loan officer" is measured by dividing the number of active borrowers by the number of loan officers.
- "Borrowers per staff member" is measured by dividing the number of borrowers by the number of personnel.

**Table 1: Alexandria Business Association—Indicators Measuring the Efficiency of Microfinance Activities for Calendar Years 2005 and 2006**

| Indicators | 2005 | 2006 | 2006 Benchmark | Benchmark Met |
|---|---|---|---|---|
| **Financial Efficiency** | | | | |
| Operating expense ratio | 18.5% | 16.7% | 14.9% | No |
| Cost per active client | $40 | $38 | $61 | Yes |
| **Portfolio Quality** | | | | |
| Write-off ratio | 1.1% | 1.1% | 0.5% | No |
| Portfolio at risk > 30 days | 2.4% | 1.8% | 0.5% | No |
| **Staff Productivity** | | | | |
| Borrowers per loan officer | 112 | 133 | 289 | No |
| Borrowers per staff member | 66 | 78 | 185 | No |

Table 2 shows that the Assiut Businessmen Association improved its operating expense ratio from 27.9 percent in 2005 to 25.3 percent in 2006. Another improvement was the cost per client, which was significantly less than benchmarks for both 2005 and 2006. The other indicators showed both positive and negative changes.

**Table 2: Assiut Businessmen Association—Indicators Measuring the Efficiency of Microfinance Activities for Calendar Years 2005 and 2006**

| Indicators | 2005 | 2006 | 2006 Benchmark | Benchmark Met |
|---|---|---|---|---|
| **Financial Efficiency** | | | | |
| Operating expense ratio | 27.9% | 25.3% | 14.9% | No |
| Cost per active client | $14 | $18 | $61 | Yes |
| **Portfolio Quality** | | | | |
| Write-off ratio | 3.0% | 5.2% | 0.5% | No |
| Portfolio at risk > 30 days | 12.9% | 3.8% | 0.5% | No |
| **Staff Productivity** | | | | |
| Borrowers per loan officer | 49 | 54 | 289 | No |
| Borrowers per staff member | 174 | 118 | 185 | No |

Table 3 shows that the Lead Foundation improved its operating expense ratio from 41.6 percent in 2005 to 35.1 percent in 2006. The other indicators showed both positive and negative changes.

**Table 3: The Lead Foundation—Indicators Measuring the Efficiency of Microfinance Activities for Calendar Years 2005 and 2006**

| Indicators | 2005 | 2006 | 2006 Benchmark | Benchmark Met |
|---|---|---|---|---|
| **Financial Efficiency** | | | | |
| Operating expense ratio | 41.6% | 35.1% | 23.5% | No |
| Cost per active client | $24 | $24 | $155 | Yes |
| **Portfolio Quality** | | | | |
| Write-off ratio | 0.0% | 0.0% | 0.4% | Yes |
| Portfolio at risk > 30 days | 0.0% | 0.1% | 2.9% | Yes |
| **Staff Productivity** | | | | |
| Borrowers per loan officer | 246 | 263 | 167 | Yes |
| Borrowers per staff member | 123 | 152 | 105 | Yes |

Although USAID/Egypt increasingly improved the efficiency of its microfinance activities, the mission had not received financial sustainability commitments from microfinance institutions as required by USAID regulations. Microfinance institutions that are not required to prepare this commitment letter may not be aware that they need to operate efficiently to ensure their long-term sustainability. This concern is discussed below.

OIG photograph of Assiut Businessmen Association borrower who received a loan of $175 to expand his shoemaking store in Fayoum, Egypt.

## The Mission Did Not Receive Financial Sustainability Commitments From Microfinance Institutions

According to Automated Directives System (ADS) 219.3.5.2, before a mission signs an agreement to provide assistance to any microfinance institution, the management of the institution must provide the mission with a “credible written commitment” to attain full financial sustainability on that institution’s financial service activities within 7 years of the initial provision of USAID assistance.

USAID/Egypt has not received these required written commitments from any of its seven microfinance institutions. According to mission officials, they did not understand that the ADS required commitment~~s~~ letters apart from and before the cooperative agreements were signed by microfinance institutions.

The three microfinance institutions reviewed all had USAID/Egypt cooperative agreements that included language upholding the general goal of financial sustainability. However, none of the cooperative agreements adhered to the rigid requirements of ADS 219.3.5.2, which specify prior written commitments that sustainability be achieved within 7 years of the initial provision of USAID assistance. Without these written commitments, USAID/Egypt and existing microfinance institutions with ongoing agreements may not understand that full financial sustainability is to be achieved within 7 years. Further, with regard to future agreements, without being required to prepare this commitment letter, microfinance institutions may not be aware that they need to operate efficiently to ensure long-term sustainability. Noncompliance with this USAID policy also increases the risk that unqualified microfinance institutions could receive assistance. Thus, this audit makes the following recommendations to strengthen the sustainability of USAID/Egypt’s microfinance program.

*Recommendation No. 1: We recommend that USAID/Egypt develop procedures for future agreements to ensure that the mission receives written commitments from microfinance institutions to attain full financial sustainability within 7 years before an agreement is signed.*

*Recommendation No. 2: We recommend that USAID/Egypt receive written commitments to attain full financial sustainability within 7 years from existing microfinance institutions with signed agreements.*

OIG photograph of an Alexandria Business Association borrower who received a loan of $140 to expand her business selling textile products in Alexandria, Egypt.

## Did USAID/Egypt's microfinance activities achieve planned results?

USAID/Egypt achieved its overall planned results for its microfinance program in fiscal year 2005 and fiscal year 2006. One major exception was a $27.5 million cooperative agreement that resulted in expanding only 17 of 30 planned new branches for microfinance institutions to provide microfinance credit. This audit's determination of overall planned results was based on planned and reported results within the mission's performance management plan covering the seven microfinance institutions, as table 4 shows.

**Table 4: USAID/Egypt Microfinance Activities—Planned Versus Reported Results Fiscal Years 2005 and 2006**

| | Fiscal Year 2005 | | | Fiscal Year 2006 | | |
|---|---|---|---|---|---|---|
| **Performance Indicator** | **Planned** | **Reported** | **Percent Achieved** | **Planned** | **Reported** | **Percent Achieved** |
| Value of small and micro enterprise loans disbursed | $132 million | $193 million | 146% | $140 million | $246 million | 176% |
| Annual number of loans at the poverty level (under $350) | 400,000 | 639,052 | 160% | 450,000 | 789,052 | 175% |

Mission officials said that the number of poverty loans greatly surpassed their expectations because they entered into a new cooperative agreement and because several other microfinance institutions kept expanding their operations. As a result, the scale of lending was much greater for group and poverty lending programs during fiscal years 2005 and 2006 than the mission had anticipated.

Based on the results achieved during 2006, activity managers for the mission's microfinance activities adjusted their planned targets for 2007. For example, they increased the planned number of poverty loans from 450,000 to 870,000 and the planned amount of loans disbursed from $140 million to $281 million to reflect USAID/Egypt's planned future program expansion.

In addition, to determine the accuracy and validity of data from the three microfinance institutions that had ongoing agreements with USAID/Egypt, the audit team selected and performed a statistically projectable sample at the 95 percent confidence level. The resulting sample consisted of 84 beneficiaries from a universe of 212,144 active loans as of December 31, 2006. The audit sample validation consisted of testing supporting documentation and purposes of each loan with the borrowers themselves, including data such as loan amounts, loan types, loan terms, funding sources, fees, and program awareness. The audit team found one exception. One of the microfinance institutions was not acknowledging the source of funds from the American people. Based on

USAID/Egypt's reported results and the statistical survey of sampled microfinance borrowers, this audit determined that the microfinance project was making a positive impact for beneficiaries.

However, some results were not positive. For example, in March 2003, USAID/Egypt awarded a cooperative agreement for $27.5 million to the Credit Guarantee Company to provide support for microenterprise and small and medium-sized enterprise development activities. According to the agreement, within 3 years, the Credit Guarantee Company was tasked to open 30 new branches for microfinance institutions to provide microfinance credit. However, as of July 2007, only 17 new branches, or 56 percent of the agreement planned results, were providing credit. Given that this agreement has ended, this audit does not make a recommendation on the matter.

In addition, as discussed in the following report sections, the audit identified the following issues requiring USAID/Egypt management attention.

- Microfinance institutions need performance-based business plans.
- The mission has not monitored the progress of technical assistance to microfinance institutions.
- Site visits to financial institutions and technical assistance contractor need strengthening.
- Microfinance reports to Congress were inconsistent with USAID/Egypt financial records.
- Recipients questioned the value of technical assistance.
- Branding strategy is needed.

OIG photograph of an Assiut Businessmen Association borrower who received a loan of $428 to expand her chicken and duck raising operation in Minia, Egypt.

## Microfinance Institutions Need Performance-Based Business Plans

The ADS requires microfinance institutions to use indicators for portfolio, outreach, and interest rate policy (please see Mandatory Reference, *Microenterprise Development*, Annex – Minimum Reporting for Microfinance Institutions, sections A and B). Specifically, missions are responsible for monitoring and reporting on the performance of microfinance institutions in terms of (1) the organization's outreach to the poor and the proportion of women among its clients and (2) the organization's performance, including its progress toward financial sustainability and operational efficiency.

None of the three microfinance institutions reviewed had a business plan[3] to assess and track performance information according to USAID policy. An April 2006 USAID-contracted study revealed that even though the three microfinance institutions prepared forecasts, detailed budgets, or expansion plans, this information could not be considered business plans because it lacked performance targets or an overall strategy.

The agreements with each of the microfinance institutions did not require the reporting of performance information such as targets and associated indicators. Officials from both USAID/Egypt and the management of the three microfinance institutions did not perceive the need for performance targets within a business plan that goes beyond institutional financial information. A business plan that incorporates performance targets would provide managers of microfinance institutions with an important tool to monitor the institution's progress and compare it with the targets, and would also allow USAID managers to effectively monitor the progress of microfinance institutions. Without this information, USAID/Egypt's management decisions would not be based on established performance-based business plans.

*Recommendation No. 3: We recommend that USAID/Egypt require all microfinance institutions to develop business plans that incorporate performance targets.*

## The Mission Has Not Monitored the Progress of Technical Assistance to Microfinance Institutions

Summary: USAID policy requires performance management to monitor and assess progress. However, USAID/Egypt has not monitored the progress of its technical assistance to microfinance institutions. For example, the mission has not approved an implementation plan with associated indicators for its technical assistance contractor because the plans did not meet USAID requirements. In addition, indicators within the implementation plan did not align with performance indicators in USAID/Egypt's performance management plan and quarterly progress reports did not report progress against approved indicators. The contractor has started to report more useful performance information, but this information still did not align with the unapproved implementation plan. Consequently, the mission does not have an objective basis to assess progress of technical assistance provided by a contractor to the microfinance institutions.

[3] Given that these microfinance institutions are nongovernmental organizations, this report refers to their performance-based plans as business plans.

ADS 203.3.2 states that missions are responsible for establishing systems to measure progress toward their intended objectives. In addition, ADS 200.6 defines performance management as "the systematic process of monitoring the results of activities; collecting and analyzing performance information to track progress toward planned results; using performance information to influence program decisionmaking and resource allocation; and communicating results achieved, or not attained, to advance organizational learning and tell the Agency's story."

In January 2006, USAID/Egypt entered into a contract with Chemonics International to provide technical assistance for microfinance institutions funded by USAID. This contract required an implementation plan within 2 months after the start of the contract as well as quarterly progress reports. Although Chemonics has developed three implementation plans, USAID/Egypt has not officially approved any of these plans. Chemonics prepared its first implementation plan in March 2005 for the first 5 months of activity. Chemonics prepared its second implementation plan in May 2006. Chemonics prepared its third implementation plan, the most comprehensive of the plans to that date, in April 2007. According to mission officials, they had not approved and were not using these implementation plans because the plans did not meet USAID requirements. For example, the April 2007 plan did not include baselines or targets to determine progress and compare actual and planned results.

The plans had two other faults. First, the objectives of the implementation plans did not align with USAID/Egypt performance indicators to report progress for its microfinance project in its performance management plan. To illustrate, in its third implementation plan, Chemonics started to report results using performance indicators from USAID/Egypt's performance management plan. However, these reported results did not align with the still unapproved implementation plan. Second, the mission did not require Chemonics to include performance data that measured actual results against expected results in its quarterly progress reports during the first year of the contract.

As evidenced by lack of approval of the technical assistance implementation plan, mission staff members were not using the implementation plans and associated progress reports as a tool to assess progress. The mission had not taken steps to incorporate indicators in performance monitoring of technical assistance provided to microfinance institutions. Consequently, the mission could not be assured that progress for technical assistance to microfinance institutions was meeting expectations. As a result, the audit team is making the following recommendations.

*Recommendation No. 4: We recommend that USAID/Egypt approve an implementation plan which identifies activities with clear baselines and targets to assess progress.*

*Recommendation No. 5: We recommend that USAID/Egypt approve performance indicators for technical assistance that align with established performance indicators in the USAID/Egypt's performance management plan.*

*Recommendation No. 6: We recommend that USAID/Egypt require the implementer to report on approved performance indicators in its quarterly progress reports.*

OIG photograph of an Assiut Businessmen Association borrower who received a loan of $263 to expand his manufacturing of boxes for fruits and vegetables in Fayoum, Egypt.

## Site Visits to Financial Institutions and Technical Assistance Contractor Need Strengthening

Summary: USAID policy states that the cognizant technical officer is responsible for ensuring that USAID exercises prudent management of assistance awards and for monitoring and evaluating the recipient and its performance. USAID's *Guidebook for Managers and Cognizant Technical Officers on Acquisition and Assistance* states that the cognizant technical officer should document all significant actions. Over 2½ years, the cognizant technical officer documented 17 site visits to microfinance institutions but none to the technical assistance contractor. Nor did the cognizant technical officer follow up with implementing partners to address performance targets that were either not established or not met. Mission staff cited workload requirements as hindering the ability of the cognizant technical officer to fulfill oversight responsibilities. Without adequate oversight, mission management may not have timely information on performance to measure progress and influence program decisionmaking and resource allocation.

ADS 303.2 (f) states that the cognizant technical officer is responsible for ensuring that USAID exercises prudent management of assistance awards and for making the achievement of program objectives easier by monitoring and evaluating the recipient and its performance. USAID's *Guidebook for Managers and Cognizant Technical Officers on Acquisition and Assistance* states that the cognizant technical officer should document all significant actions including any technical directions given to the contractor in the work file or a separate action file. The *Guidebook* also notes that site visits are a key element in the cognizant technical officer's ability to monitor and verify progress and compliance with the contract. ADS 303.3.17.b states that site visits are an important part of effective award management.

During calendar years 2005, 2006, and 2007, the cognizant technical officer documented 17 site visits. The cognizant technical officer documented seven site visits in calendar year 2005, six in calendar year 2006, and four during the first 4 months of calendar year 2007. All of these site visits were to microfinance institutions; no site visits to the technical assistance contractor were documented. Furthermore, the cognizant technical officer did not document followup with the implementing partners to address performance targets that were not established or were not met or tasks that were not completed as stipulated in agreements.

According to the cognizant technical officer, the oversight role covers all seven microfinance institutions and the technical assistance contractor—all with distinct agreements. As a result, the heavy workload has limited documentation of site visits and related oversight responsibilities. However, without adequate oversight, mission management may not have timely information on program performance to measure progress and influence program decisionmaking and resource allocation. Therefore, this audit makes the following recommendation.

*Recommendation No. 7: We recommend that USAID/Egypt develop a written action plan for oversight by the cognizant technical officer, including documented site visits to assess progress against targets and the completion of tasks stipulated in awards or annual plans.*

OIG photograph of an Alexandria Business Association borrower who received a loan for $243 to expand a barbershop in Alexandria, Egypt.

## Microfinance Reports to Congress Were Inconsistent With USAID/Egypt Financial Records

Summary: According to USAID guidance, performance data should be accurate and reliable. However, the fiscal year 2006 Microenterprise Results Reports to Congress contained information that was inconsistent with USAID/Egypt financial records. USAID/Washington relied on USAID/Egypt to ensure the accuracy of entered data. In turn, USAID/Egypt relied on the implementer to ensure the accuracy of entered data. As affirmed in the Microenterprise Results and Accountability Act of 2004, without data quality control and data verification, decision makers may draw erroneous conclusions regarding the performance of the program, leading to improper management decisions.

ADS 203.3.5.2 states that the operating units should be aware of the strengths and weaknesses of data and the extent to which data integrity can be trusted to influence management decisions.

In annex A of its fiscal year 2006 annual report entitled Microenterprise Results Reporting, USAID reported data to Congress that were inconsistent with data recorded by USAID/Egypt. As table 5 shows, USAID reported fiscal year 2006 funding (in obligations) for two institutions. However, for one of the two institutions, the amount differed from USAID/Egypt financial records by 34 percent.

**Table 5: Fiscal Year 2006 Funding Reported to Congress for Two Institutions Compared to USAID/Egypt Financial Records**

| Institution | Reported to Congress | USAID/Egypt Financial Records | Difference | Percent Different |
|---|---|---|---|---|
| **Chemonics International** | $5,352,000 | $3,538,150 | $1,813,850 | 33.9% |
| **The Lead Foundation** | $9,811,000 | $9,811,776 | $776 | 0.0% |

In addition to the actual fiscal year 2006 report to Congress, the database supporting Microenterprise Results Reporting to Congress contained several apparent errors for two of the three microfinance institutions, table 6 shows.

**Table 6: Fiscal Year 2006 Program Data in the Microenterprise Results Reporting (MRR) Database Compared to USAID/Egypt Program Records**

| Institution | Data Source | Number of Loans | Amount of Loans | Number of Poverty Loans | Amount For Poverty Loans |
|---|---|---|---|---|---|
| **Alexandria Business Association** | | | | | |
| | MRR Database | 59,526 | $15,084,649 | 46,802 | $5,214,741 |
| | Mission Records | 59,526 | $15,117,729 | 33,431 | $1,695,406 |
| | Percent Difference | 0.0% | 0.2% | 28.6% | 67.5% |
| **Assiut Businessmen Association** | | | | | |
| | MRR Database | 164,533 | $19,394,015 | 151,712 | $12,224,935 |
| | Mission Records | 164,533 | $19,394,015 | 151,080 | $11,829,550 |
| | Percent Difference | 0.0% | 0.0% | 0.4% | 3.2% |
| **The Lead Foundation** | | | | | |
| | MRR Database | 57,143 | 4,556,521 | 52,904 | 2,827,461 |
| | Mission Records | 57,143 | 4,582,606 | 52,904 | 2,843,583 |
| | Percent Difference | 0.0% | 0.57% | 0.0% | 0.57% |

The USAID Bureau for Economic Growth, Agriculture, and Trade in Washington, DC, did not specifically request USAID/Egypt to validate the quality and accuracy of the reported information. However, according to a bureau program manager, the mission is responsible for entering and verifying the data in the microenterprise results reporting system. The bureau does not validate the accuracy of the information by any other means. USAID/Egypt officials stated that they relied on the implementer to validate the data. Without data quality control and data verification, decision makers may draw erroneous conclusions regarding the performance of the program, leading to improper management decisions and the reporting of incorrect information. Furthermore, the Microenterprise Results and Accountability Act of 2004 affirmed the importance of database accuracy by stating that the monitoring system provides a basis for recommending adjustments to enhance the sustainability and the impact of the assistance for the very poor, particularly for poor women. To ensure the reliability of the reported information, this audit makes the following recommendation.

*Recommendation No. 8: We recommend that USAID/Egypt establish and document specific procedures, including data entry and verification, to ensure the accuracy of microfinance information reported to Congress.*

## Recipients Questioned Value of Technical Assistance

Summary: In January 2006, USAID/Egypt entered into a contract with Chemonics International to provide technical assistance for microfinance institutions funded by USAID. However, according to both a midterm evaluation of the project and interviews with the heads of microfinance institutions, the value of technical assistance for microfinance has been limited. For example, training was not relevant to Government of Egypt laws and regulations, and training was not targeted to the needs of the organization. As a result, the heads of microfinance institutions stated that they were not fully using the technical assistance services. As noted earlier, the USAID/Egypt mission had not monitored the progress of technical assistance to microfinance institutions. As a result, the mission was not aware of the limited usefulness of technical assistance provided to the microfinance institutions. Mission officials also confirm that they were not aware of this issue. Underutilizing technical assistance lessens the ability of USAID/Egypt's microfinance project to expand outreach to underserved areas and vulnerable populations, particularly women.

In January 2006, USAID/Egypt entered into a $5.4 million contract with Chemonics International to provide technical assistance for microfinance institutions funded by USAID. However, according to both a midterm evaluation of the project and interviews with the heads of microfinance institutions, the value of technical assistance for microfinance has been limited. The USAID microfinance project has been using the same local contractor, Environmental Quality International, for technical assistance since 1993. In December 2004, USAID/Egypt received a midterm evaluation of the microfinance project that highlighted the following:

- The quality of the local technical service provision is low and has not evolved with the needs of the microfinance institutions.
- Major providers of technical assistance are not aware of and do not apply established international best practices.
- Technical assistance is better suited for startup branches than for growing or established institutions.
- Future technical assistance should be based on microfinance institutions identifying their needs.

In addition, the heads of four microfinance institutions identified issues with the technical assistance and questioned its value. For example, according to these management officials, training was not relevant to Government of Egypt laws and regulations, and training was not targeted to the needs of the organization. As a result, the same officials stated that they were not fully using the technical assistance services. As noted earlier, the lack of approved tools to assess progress by USAID/Egypt had hindered the mission from monitoring the progress of technical assistance to microfinance institutions, including approving implementation plans, approving performance indicators for technical assistance, and requiring the implementer to report performance data in its quarterly progress reports. Given these issues, the mission was not aware of the limited usefulness of technical assistance provided to the microfinance institutions. Mission officials also confirm that they were not aware of this issue. Underutilizing such assistance lessens the ability of USAID/Egypt's microfinance project to expand outreach to underserved areas and vulnerable populations, particularly women. This audit makes the following recommendation to address this issue.

*Recommendation No. 9: We recommend that USAID/Egypt assess its technical assistance for microfinance institutions to determine if the unique needs of each microfinance institution are being met and revise the unique assistance for each microfinance institution accordingly.*

## Branding Strategy Is Needed

According to ADS 320.3.3, "USAID's policy is that programs, projects, activities, public communication, or commodities implemented or delivered under co-funded instruments - such as grants, cooperative agreements, or other assistance awards that usually required a cost-share - generally are "co-branded and co-marked"."

During site visits to program beneficiaries in Alexandria, survey results disclosed that 13 of 24 (54 percent) of the beneficiaries were not aware that USAID or the American people have subsidized the establishment and operations of the institution. According to the management of the microfinance institution, Alexandria Business Association, there was no need for its beneficiaries to be aware of its source of funds, because if they were, they would not repay the loans. In contrast, beneficiaries of the other two microfinance institutions were generally aware of USAID's assistance to the microfinance institutions, as table 7 shows.

**Table 7: Number of Beneficiaries Unaware That USAID Was the Source of Microfinance Funding**

| Microfinance Institution | Beneficiary Sample Size | Number of beneficiaries who did not know that USAID was the source of funding |
|---|---|---|
| Alexandria Business Association | 24 | 13 |
| Assiut Businessmen Association | 36 | 2 |
| The Lead Foundation | 24 | 5 |
| Total | 84 | 20 |

Information should be available to let Egyptians know that these and all other USAID-funded microfinance institutions and their lending programs for poor Egyptian microentrepreneurs are substantially the result of the USAID/Egypt assistance at a cost of $86.6 million since fiscal year 1997. As a result, this audit makes the following recommendation.

*Recommendation No. 10: We recommend that USAID/Egypt establish a branding strategy for microfinance institutions as defined in ADS 320.6.*

# EVALUATION OF MANAGEMENT COMMENTS

In its response to the draft report, USAID/Egypt agreed with all the report recommendations and outlined its actions to implement each of the recommendations, which will strengthen measures to better manage the USAID-funded activities.

Regarding recommendation no. 1, the mission cognizant technical officer has developed procedures to receive written commitments from participating institutions to attain full financial sustainability, separate from the signed agreements and before officially signing new agreements.

Regarding recommendation no. 2, the mission outlined actions taken by the cognizant technical officer to attain the written commitments to attain full sustainability from existing microfinance with signed agreements.

Regarding recommendation no. 3, the mission required business plans from all microfinance institutions. The mission expects to have all plans finalized by June 30, 2008. The three microfinance institutions reviewed already have finalized their business plans.

Regarding recommendation no. 4, the mission approved a technical assistance implementation plan for calendar year 2008. Specific targets and indicators are broken down quarterly and reported within the technical assistance quarterly reports.

Regarding recommendation no. 5, the mission approved performance indicators for technical assistance that are aligned with USAID/Egypt's performance management plan.

Regarding recommendation no. 6, the mission's cognizant technical officer required the technical assistance provider to report on approved indicators in its quarterly progress reports. The performance indicators are tracked by the cognizant technical officer to review progress against targets.

Regarding recommendation no. 7, the mission acknowledged the importance of documenting site visits and outlined several measures, including (1) a performance monitoring checklist that includes data to be tracked, frequency of collection, and data quality assessments and (2) a plan for site visits that ensures complete coverage with appropriate frequency. Since the beginning of fiscal year 2008, the mission has already documented more than 80 site visits.

Regarding recommendation no. 8, the mission has taken steps to ensure the accuracy of microfinance information reported to Congress, including (1) upgrades to the microfinance institutions software system, (2) letters to each USAID-supported microfinance institution that outline responsibilities, including Microenterprise Results Reporting data, (3) clear instructions to the technical assistance provider to all the USAID-supported microfinance institutions regarding reporting procedures, and

(4) verification by the technical assistance contractor management and approval by the cognizant technical officer before reporting to the Microenterprise Results Reporting database.

Regarding recommendation no. 9, the mission requested the technical assistance contractor to conduct an assessment of the needs of the USAID-assisted microfinance institutions. Based on this assessment, USAID has assigned specific tasks to the technical assistance contractor under its work plan. The mission's cognizant technical officer is monitoring the performance of the technical assistance provider against the planned results.

Regarding recommendation no. 10, the mission stated that the technical assistance provider is assisting the Lead Foundation—the only ongoing agreement at the present time—to establish a branding strategy. The mission intends to complete the branding strategy by May 31, 2008. In addition, the cognizant technical officer instructed the technical assistance provider to provide training sessions on branding directed to loan coordinators who are in direct contact with the beneficiaries.

As a result of the mission's actions to implement these recommendations, management decisions and final actions have been completed for recommendation nos. 1, 2, 3, 4, 5, 6, 7, 8, and 9. Determination for final action for recommendation no. 10 will be made by the Audit Performance and Compliance Division (M/CFO/APC) upon completion of the actions planned by the mission. USAID/Egypt's comments for the draft report are included in their entirety in appendix II.

# SCOPE AND METHODOLOGY

## Scope

The Regional Inspector General/Cairo conducted this audit in accordance with generally accepted Government auditing standards. This audit was part of a worldwide audit of USAID's microfinance activities. The audit was designed to determine whether (1) USAID/Egypt implemented its microfinance activities efficiently and (2) USAID/Egypt's microfinance activities achieved planned results.

USAID/Egypt implemented its microfinance project through seven not-for-profit microfinance institutions, two banks, and the private Credit Guarantee Company to assist in the delivery of credit to small businesses that lack sufficient collateral to obtain loans. This audit reviewed the loan portfolio and operations of the three microfinance institutions—Alexandria Business Association, Assiut Businessmen Association, and the Lead Foundation—each with a current cooperative agreement supported by USAID/Egypt. In addition, we reviewed the operations of the private Credit Guarantee Company. The reviewed institutions had 212,144 active clients (35 percent) out of the 614,899 active clients served by all of the USAID-supported institutions.

We conducted our audit from May 6 through December 17, 2007, at the principal offices of USAID/Egypt, the technical contractor Chemonics International in Cairo, the microfinance institution Alexandria Business Association in Alexandria, the microfinance institution Assiut Businessmen Association in Assiut, the microfinance institution Lead Foundation in Cairo, and the Credit Guarantee Company in Cairo. We also visited suboffices of these organizations in Minia, Fayoum, and Beni Suef. In addition, we conducted 84 site visits to microfinance recipients in Alexandria, Cairo, Minia, Fayoum, and Beni Suef.

The audit scope included assessing significant management controls over the efficiency of microfinance activities and the achievement of planned results. Such controls included the following:

- The collection of financial sustainability commitments from microfinance institutions.
- The collection, verification, and reporting of data supporting results for financial efficiency, portfolio quality, and staff productivity.
- The collection, verification, and reporting of data supporting reported program results and financial data.
- The preparation of business plans for microfinance institutions.
- The review and approval of an implementation plan for the technical assistance contractor.
- Monitoring by the mission's cognizant technical officer.
- The approval of key personnel, as required by cooperative agreements.
- Requirements for microfinance institutions to have closeout audits at the point of reaching full sustainability.

Audit evidence included cooperative agreements, regulations, mission performance plans, quarterly progress reports by the technical assistance contractor, monthly progress reports by the institutions, financial statements for three microfinance institutions, project files, field trip reports, USAID/Egypt financial records, implementation plans of the technical assistance contractor, a midterm evaluation of the microfinance project, an independent assessment of the microfinance institutions, data reported on the Web-based tool Microfinance Information eXchange Market, as well as meetings and interviews with management and staff from USAID, the technical assistance contractor, the microfinance institutions, and the Credit Guarantee Company.

Two prior audits were relevant to this review[4]. However, none of the prior audit findings for these two audits affected the areas under our review.

## Methodology

To answer the audit objectives, we met with the implementing partner, microfinance institution officials, and borrowers in Egypt, and USAID officials in Egypt and Washington, DC. We interviewed the appropriate officials and reviewed relevant documentation produced by USAID/Egypt such as award documents, including cooperative agreements and amendments, mission correspondence, the mission performance plan, financial reports, and field visit reports. We reviewed microfinance institutions and implementing partner–prepared documentation such as annual work plans and quarterly and monthly reports. In addition, we reviewed the operations of the private Credit Guarantee Company and the contractor providing technical assistance to the microfinance institutions.

We selected and reviewed three microfinance institutions that have current cooperative agreements supported by USAID/Egypt. Two institutions (Alexandria Business Association and Assiut Businessmen Association) had large-scale outreach programs, and one institution (The Lead Foundation) had a medium-scale outreach program. The large-scale and medium-scale outreach programs have different international benchmarks for operational and financial performance.

To answer the first audit objective, we selected six indicators for each of the three selected microfinance institutions, looked for changes from calendar years 2005 to 2006, and compared results to international benchmarks for 2006 established by the Microfinance Information eXchange Market—a global, Web-based microfinance information platform that is used by USAID/Egypt. To answer the second audit objective, we compared missionwide reported results with planned results for fiscal years 2005 and 2006 in the mission's performance management plan. We could not limit our review under the second audit objective to only the three microfinance institutions because USAID/Egypt did not have data disaggregated by microfinance institution. We also conducted site visits to observe operating activities and assess the impact of the microfinance programs.

Specifically, to determine the accuracy and validity of data from the three microfinance institutions that have ongoing agreements with USAID/Egypt, we selected and performed a statistically projectable sample at the 95 percent confidence level with a 4

[4] The two prior audits were the USAID Inspector General "Audit of USAID/Egypt's Small and Microenterprise Development Activities" (Audit Report No. 6-263-03-002-P, March 12, 2003) and the Government Accountability Office "Microenterprise Development: USAID's Program Has Met Some Goals; Annual Reporting Has Limitations" (GAO-04-171, November 2003).

percent precision. The resulting sample consisted of 84 beneficiaries (totaling approximately $32,000 in loans) from a universe of 212,144 active loans totaling $28 million as of December 31, 2006. The audit sample validation consisted of testing supporting documentation and purposes of each loan with the borrowers themselves, including data such as loan amounts, loan types, loan terms, funding sources, fees, and program awareness. We also interviewed 27 branch managers and 4 executive managers. We found one exception. One of the microfinance institutions did not acknowledge the source of funds from the American people. To assist with this testing, USAID/Egypt contracted with an independent public accounting firm in Egypt to assist our staff with the statistical survey. We developed the scope of work, managed the work, and directly received the results from the accounting firm's staff auditors. USAID/Egypt paid the costs of the accounting firm's services.

# MANAGEMENT COMMENTS

## Memorandum

**Date**: March 27, 2008

**To:** Lloyd Miller, Regional Inspector General/Cairo

**From:** Hilda Arellano, Mission Director /s/

**Subject:** Audit of USAID/Egypt Microfinance activities
Audit Report No. 6-263-08-00X-P February XX, 2008 – Draft report

Following is USAID/Egypt's response to the RIG Microfinance activities program audit report recommendations.

*Recommendation No 1: We recommend that USAID/Egypt develop procedures to ensure that the mission receives written commitments, to attain full financial sustainability within seven years, from microfinance institutions before an agreement is signed.*

Mission Response:

Since inception of the micro credit program in 1990, the USAID/Egypt Mission had developed strict procedures to commit USAID-assisted microfinance institutions (MFIs) to attain full sustainability at the earliest practical time. The Mission was keen to include sustainability as a vital element of every agreement signed with the USAID-assisted MFIs. As an example: the cooperative agreement signed with Assiut Business Association (ASBA) on November 13, 2001, stated as follows: under article B.4. "Deliverables and Results to be Achieved: The Foundation's infrastructure for providing services to micro-entrepreneurs, shall be increased from the current four branches to seven branches, all of which will be operating as individual profit centers and it is understood and agreed upon that the Recipient will continue to operate the program in a financially self-sustainable manner" (Exhibit 1).

Another agreement, signed with the LEAD Foundation on August 5, 2003, under article B.5. Planned Results, stated as follows: "At the end of the agreement, it is expected that the Recipient would have accomplished the following results: The Recipient would have established and operated a head office and up to five branches active in providing sustainable credit, technical assistance, training, and other related services to the targeted entrepreneurs subject this agreement" (Exhibit 2).

In addition, a letter from LEAD Foundation dated September 15, 2005, proposing to amend the agreement with USAID to increase outreach and expand to new underserved areas, stated the following: "We strongly believe in the importance of becoming self-sustainable in the shortest possible time, and regard donor funds only as a transit means to putting the foundation on its way to long term sustainability. We also believe in the importance of investing in solid capacity building as the only means to achieving a long-term sustainable activity" (Exhibit 3).

As requested under recommendation no. 1, the Mission CTO developed a checklist of procedures to be considered before signing any new agreement under the microfinance program. The checklist includes receiving written commitments from MFIs to attain full financial sustainability within no more than seven years from the date of signing the agreement (Exhibit 4).

Accordingly, the Mission received the above mentioned written commitment from Aga Khan Agency for Microfinance (AKAM) (Exhibit 5), the only new agreement planned at this time as part of its required documentation for the Global Development Alliance (GDA). The letter of commitment will be required for potential future agreements with MFIs.

**In view of the above, the Mission believes that measures have been taken to address Recommendation 1 and final action has been fully implemented; thus, we request closure of the recommendation upon final report issuance.**

*Recommendation No 2: We recommend that USAID/Egypt receive written commitments to attain full financial sustainability from existing microfinance institutions with signed agreements.*

Mission Response:

The only ongoing agreement between USAID/Egypt and partner institutions is one with LEAD Foundation. The agreement's completion date is September 30, 2009. As mentioned above, LEAD Foundation's agreement confirmed its commitment to sustainability. LEAD Foundation was recently rated by Planet Finance, a global microfinance rating agency, and received the highest ever rating at this development stage.

As requested under recommendation no. 2, the Mission CTO received on March 14, 2008, from LEAD Foundation's management, a written commitment to attain full financial sustainability within seven years from the date the Cooperative Agreement was signed (Exhibit 6). The commitment letter stated the following: "The LEAD Foundation's mission is to provide its clients with sustainable access to quality microfinance services and thus is fully committed to achieving full financial sustainability by September 2010, seven years from the date of its Cooperative Agreement with USAID."

**In view of the above, the Mission believes that measures have been taken to address Recommendation 2 and final action has been fully implemented; thus, we request closure of the recommendation upon final report issuance.**

*Recommendation No. 3: We recommend that USAID/Egypt require all microfinance institutions to develop business plans that incorporate performance targets.*

Mission Response:

Since the inception of the micro credit program, USAID-assisted MFIs developed business plans yet they were not up to the internationally recognized standards. The business plans contained projections, milestones, and budgets but lacked performance targets and indicators.

During the audit process, all USAID-assisted MFIs were requested to develop business plans that incorporate performance targets and are now developing such plans. The Mission CTO is monitoring the MFIs to ensure that the plans are in compliance with internationally recognized standards. USAID received comprehensive business plans from the following four MFIs: Alexandria Business Association (ABA) – (Exhibit 7), Dakahleya Business Association for Community Development (DBACD) – (Exhibit 8), the LEAD Foundation (Exhibit 9), and the Small Enterprise Development Association in Port Said (SEDAP) – (Exhibit 10). Additionally, USAID received a draft business plan for Assiut Business Association (ASBA) – (Exhibit 11). Sharkeya Business Association for Community Development (SBACD) and North Sinai Business Association (NSBA) are finalizing their plans and will submit their plans to USAID by May 31, 2008. As per the attached MFIs Business Plan Tracker (Exhibit 12), Egyptian Small Enterprise Development Association (ESED) will finalize their plan on June 30, 2008. It is worth noting that the agreements with SBACD and ESED ended in February, 2000.

The current business plans include strategic objectives, target market and strategy, products and services, including new product development, technical assistance, financing projections, ratio analysis and indicators, benchmarking and yearly percentage of operational and financial self-sufficiency. Moreover, the LEAD Foundation, DBACD, SBACD, and SEDAP developed operational plans with detailed projections for each department. ABA and ASBA are in the process of developing their operational plans.

The MFIs will report to the Mission CTO on a quarterly basis on actual performance versus targets. The business plans will be reviewed by the MFIs on an annual basis and will be included in their annual reports.

**In view of the above, the Mission believes that measures have been taken to address Recommendation 3 and final action will be fully implemented by June 30, 2008; thus, we request closure of the recommendation upon final report issuance.**

*Recommendation No. 4: We recommend that USAID/Egypt approve an implementation plan which identifies activities with clear baselines and targets to assess progress.*

Mission Response:

Despite the fact that the Technical Assistance (TA) provider submitted three implementation plans since January 2006, the effective date of the TA contract, through April 2007, yet none of the implementation plans had clear baselines and targets to assess progress. Consequently, the USAID/Egypt Mission did not approve the implementation plan and provided directions to make the required changes.

The fourth implementation plan was first submitted to USAID/Egypt in December 2007 and revised in January 2008 based on feedback from the Mission. The USAID/Egypt Mission approved the TA implementation plan for option year 2008 (Exhibit 13). The TA provider, Chemonics International, adjusted its performance reporting to more clearly demonstrate progress towards meeting targets in a format that is useful to the

USAID/Egypt Mission. The implementation plan was designed in accordance with the Mission's Strategic Objective 16 and its related Intermediate Results, and is in response to the contract tasks and ADS 219 requirements. The implementation plan included a matrix with performance indicators, baseline and targets, timeline of activities, specific interventions, key milestones and deliverables within the 12-month option period.

Specific targets and indicators are broken down quarterly, and reported within the TA quarterly report. The report is reviewed and evaluated by the Mission to assess progress toward achieving the planned results. Adequate measures to review plans and evaluate results are conducted quarterly, and targeted plans are reviewed accordingly.

**In view of the above, the Mission believes that measures have been taken to address Recommendation 4 and final action has been fully implemented; thus, we request closure of the recommendation upon final report issuance.**

*Recommendation No. 5: We recommend that USAID/Egypt approve performance indicators for technical assistance that align with existing performance indicators for the microfinance project.*

Mission Response:

The USAID/Egypt Mission approved performance indicators for technical assistance that are aligned with USAID/Egypt's SO16 performance monitoring plan (PMP) as detailed in the email, dated April 29, 2007, from the TA provider addressed to the Mission CTO and the USAID/Egypt Program Office (Exhibit 14). The performance indicators are detailed in Annex B of the approved TA work plan for option year 2008. Additional indicators were developed by the TA provider, in response to ADS 219.5 and the TA contract deliveries.

The performance indicators are broken down quarterly and are reported within the TA quarterly reports. The indicators are tracked through review targets versus actual performance.

**In view of the above, the Mission believes that measures have been taken to address Recommendation 5 and final action has been fully implemented; thus, we request closure of the recommendation upon final report issuance.**

*Recommendation No. 6: We recommend that USAID/Egypt require the implementer to report on approved performance indicators in its quarterly progress reports.*

Mission Response:

The USAID/Egypt Mission CTO required the TA provider to report on approved performance indicators in its quarterly progress reports. The TA quarterly report for the period of October to December 2007 reported on 15 performance indicators that respond to the Mission requirements and ADS 219. The performance indicators are broken down quarterly and are tracked by the Mission CTO through review progress against targets. A summary table of indicators is also included with the quarterly report (Exhibit 15). The indicators are reviewed by the Mission CTO to adjust deviations.

**In view of the above, the Mission believes that measures have been taken to address Recommendation 6 and final action has been fully implemented; thus, we request closure of the recommendation upon final report issuance.**

*Recommendation No. 7: We recommend that USAID/Egypt develop a written action plan for oversight by the cognizant technical officer including documented site visits and the use of a performance monitoring checklist to assess progress against targets and the completion of tasks stipulated in awards or annual plans.*

Mission Response:

The Mission CTO acknowledges the importance of documenting site visits and has taken specific measures to document all site visits. Since the beginning of fiscal year 2008, more than 80 site visit reports have been documented, including site visits to the TA provider, MFIs, donors, and other stakeholders. Samples of the documented site visits are attached (Exhibit 16).

Mission Order number 203-1 issued on February 8, 2004, entitled Performance Management and Evaluation, specifies a system to be followed by all Mission CTO's regarding program monitoring, field visits, documentation, etc. (Exhibit 17).

As a result of recommendation 7, the Mission CTO has developed a performance monitoring checklist which includes data to be tracked, frequency of collection, data source, data quality assessments, more special studies or researches, and more (Exhibit 18). The Mission CTO prepared a plan for site visits that ensures complete coverage with appropriate frequency (Exhibit 19).

**In view of the above, the Mission believes that measures have been taken to address Recommendation 7 and final action has been fully implemented; thus, we request closure of the recommendation upon final report issuance.**

*Recommendation No. 8: We recommend that USAID/Egypt establish and document specific procedures, including data entry and verification, to ensure the accuracy of microfinance information reported to Congress.*

Mission Response:

The USAID/Egypt confirms the accuracy of information, either reported to the Congress or recorded by the Mission Financial Management Office. In regards to the two cases reported by the audit team, the Mission response is as follows:

1- On January 3, 2006, the USAID/Egypt Mission signed a TA contract with Chemonics International that included a base period through September 30, 2007 and two option years. The budget allocated to the base period amounted to $5,352,131 which was reported to the MRR in year 2006, as an obligation under TA services.

The contract was funded incrementally as follows: the first obligation of $3,538,150, the second obligation of $1,027,666 and the third obligation of $786,315. The total amount recorded by the USAID/Egypt Financial Management Office corresponds with the amount reported to the MRR, at the end of the base period of the contract.

The Mission has also reported in 2006 to the MRR an amount of $9,811,000 as an obligation covering an extension of the Cooperative Agreement (CA) with the LEAD Foundation. The CA amendment extended the completion date of the program to September 30, 2007. The USAID/Egypt Financial Management Office recorded the fully obligated amount of $9,811,000 in fiscal year 2006.

As shown above, there is no inconsistency between the data reported to the MRR and the data recorded by USAID/Egypt, since the total amounts under the two activities are the same.

2- Concerning the data reported by the USAID-assisted MFIs, except for the estimated amounts of poverty loans, there is no difference between the figures reported to the Congress and the Mission records. As indicated by the audit team, the total number and amount of loans reported by the three MFIs that had existing cooperative agreements with USAID/Egypt are the same in the Mission records and those reported to the MRR.

Under the individual lending program, the MIS of the USAID-supported MFIs tracks the number and amount of loans under poverty lending category issued during a certain period of time (normally a month), which is reported to USAID in the monthly progress reports. The active number of loans and outstanding portfolio under the poverty lending category were not tracked by the MIS, thus were not reported to USAID. Therefore, the MFIs estimated the percentages of loan amounts and numbers disbursed under poverty lending category.

As indicated in the audit report, the only difference in poverty lending figures was reported by the Alexandria Business Association (ABA). When requested to complete the MRR reports, ABA management submitted their estimated figures, which they believed to have been more realistic than those calculated by the TA provider. By reviewing the figures, and comparing them with the average poverty lending portfolio submitted by other MFIs, the TA provider accepted ABA's figures which were reported to MRR.

In order to minimize the use of estimated figures in future reporting, the Mission CTO has taken proactive steps to ensure MRR 2007 (submitted in 2008) will be more complete and accurate. The steps taken are as follows:

1- Strict instructions were given to the Technical Assistance MIS team to provide assistance to the software developers of the MFIs to upgrade their systems to incorporate many of the MRR areas that are currently estimated by the MFIs. The MIS was upgraded in five MFIs (the LEAD Foundation, SBACD, SEDAP, DBACD, and ESED) to calculate poverty lending figures as well as gender segregated figures. ABA's MIS is currently being developed and will be upgraded by the end of April, 2008 to perform same two functions. This will be replicated by other institutions during 2008 (Exhibit 20).

2- The Mission CTO has requested that the TA provider develop a Letter of Agreement (LOA) for each USAID-supported MFI (Exhibit 21). The LOA outlines the general responsibilities of both the TA provider and the MFI that would maximize the outreach of financial services, on a sustainable and best practices basis, in its markets. The LOA also illustrates the types of activities that should be undertaken by the MFI and the type of assistance required by the TA provider to accomplish that goal. The LOA outlines the agreement of the MFI to cooperate in completing and sharing various tasks including MRR reports. To date, five MFIs signed their LOA.

3- The TA provider will assist the MFIs to prepare the MRR reports and to determine an appropriate estimate for the poverty lending category. Accordingly, for MRR 2007, the TA provider has sent individual emails to all USAID-supported MFIs who report to MRR with clear instructions regarding the reporting procedures to be submitted to MRR by May 2, 2008 (Exhibit 22).

4- The reports will be verified by the TA Chief of Party and submitted to the Mission CTO for approval before reporting to MRR.

**In view of the above, the Mission believes that measures have been taken to address Recommendation 8 and final action has been fully implemented; thus, we request closure of the recommendation upon final report issuance.**

*Recommendation No. 9: We recommend that USAID/Egypt assess its technical assistance for microfinance institutions to determine if the unique needs of each microfinance institution are being met and revise the unique assistance for each microfinance institution accordingly.*

Mission Response:

The USAID/Egypt Mission conducted annual Contractor Performance Reviews which assessed the overall TA performance. The USAID/Egypt Mission requested that the TA provider conduct an assessment for the needs of the USAID-assisted MFIs, and based on this assessment (Exhibit 23) has assigned specific tasks to aggressively respond to the needs of the MFIs. This has been recorded as specific tasks under the TA work plan for the option year. Moreover, the above mentioned LOA outlines the unique areas of TA needs of each MFI.

At the end of year 2007, USAID/Egypt requested feedback from the supported MFIs on the adequacy of the TA services, by conducting a survey on the TA performance (Exhibit 24). Responses to the survey revealed a remarkable improvement on the TA performance and responsiveness to the MFIs' needs. The Mission CTO will ensure responsiveness to the MFIs' observations.

The Mission CTO is also continuously monitoring the performance of the TA provider and whether it responds to the needs of the MFIs, by providing the following:

1. Review and evaluation of the implementation plan progress toward achieving planned results;
2. Regular contact with the MFIs for the CTO to confirm that services are completed;
3. Review of work plans and evaluation of results are conducted quarterly;
4. A monthly activity tracker is being provided to the Mission CTO on each TA unit, describing each activity, milestones, person in charge and percentage of completion. This activity tracker is included with the TA quarterly report. A sample of the activity tracker for February 2008 is attached (Exhibit 25);

5. Regular TA staff meetings to discuss progress with individual implementing units, and review of accomplishments of assigned tasks, in response to the MFIs needs; and
6. Weekly meetings with the TA COP and senior staff are conducted to discuss pending issues and resolve program implementation problems.

**In view of the above, the Mission believes that measures have been taken to address Recommendation 9 and final action has been fully implemented; thus, we request closure of the recommendation upon final report issuance.**

*Recommendation No. 10: We recommend that USAID/Egypt establish a branding strategy for microfinance institutions as defined in ADS 320.6.*

Mission Response:

The Mission CTO has regularly monitored compliance of contractors and assistance recipients with USAID branding and marking requirements in accordance with the relevant provisions in the contract, grant or cooperative agreement, as per ADS 320.

The Mission CTO circulated reminders and updates regarding the branding and marking requirements, which includes sending updated regulations as they become available. On November 4, 2007, the TA provider conducted branding capacity building sessions for all MFIs. 22 representatives from all nine USAID-supported MFIs participated in the session which highlighted the importance of branding and marking and discussed USAID policies in that regard. An overview for this session is attached (Exhibit 26).

As a result of Recommendation 10, the Mission CTO requested that the TA provider assist the LEAD Foundation, the only ongoing agreement at the present time, in establishing a branding strategy which will be finalized by May 31, 2008.

Regarding the beneficiaries' awareness of USAID support to MFIs, the Mission CTO has closely monitored all MFIs to increase such awareness. However, due to political concerns which may lead to adverse reaction, ABA chose not to inform some of their beneficiaries in specific areas of USAID support. CTO has taken specific measures to inform ABA and all other MFIs of the necessity of the awareness of the beneficiaries of USAID support. This message was clearly emphasized by the CTO to the MFIs management during the branding capacity building sessions that were conducted by the TA provider.

The Mission CTO gave specific instructions to the TA provider to start training sessions on branding directed specifically to loan coordinators who are in direct contact with the beneficiaries. The loan coordinators will be trained to make beneficiaries aware of USAID support to MFIs. It is worth noting that 76% of beneficiaries in the audit sample were aware of USAID support to the three MFIs: LEAD Foundation (79% were aware of the USAID support to the MFI), ASBA (94%) and ABA (45%).

**In view of the above, the Mission believes that measures have been taken to address Recommendation 10 and final action will be fully implemented by May 31, 2008; thus, we request closure of the recommendation upon final report issuance.**

Finally, USAID/Egypt would like to extend its appreciation to RIG/Cairo Audit Team for its assistance in strengthening measures to better manage the USAID microfinance activities.

Attachments: a/s

**U.S. Agency for International Development**
**Office of Inspector General**
1300 Pennsylvania Ave, NW
Washington, DC 20523
Tel: (202) 712-1150
Fax: (202) 216-3047
**www.usaid.gov/oig**