OFFICE OF INSPECTOR GENERAL

AUDIT OF USAID/LEBANON'S INVESTMENT IN MICROFINANCE PROGRAM

AUDIT REPORT NO. 6-268-13-015-P
JULY 17, 2013

CAIRO, EGYPT

Office of Inspector General

July 17, 2013

MEMORANDUM

TO: USAID/Lebanon Mission Director, Azza El-Abd

FROM: Regional Inspector General/Cairo, Catherine Trujillo /s/

SUBJECT: Audit of USAID/Lebanon's Investment in Microfinance Program (Report No. 6-268-13-015-P)

This memorandum transmits our final report on the subject audit. We have considered your comments on the draft report and included them, without attachments, in Appendix II.

The final report contains six recommendations to help USAID/Lebanon improve its Lebanon Investment in Microfinance program. In its comments on the draft report, USAID/Lebanon generally agreed with all six recommendations. Based on our evaluation of the management comments, we acknowledge that the mission made a management decision on all six Recommendations and has taken final action on Recommendations 1-5.

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

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CONTENTS

SUMMARY OF RESULTS

While Lebanon enjoys some of the better economic indicators in the region, many Lebanese citizens live in poverty and do not have basic financial services. According to the United Nations International Fund for Agricultural Development, many impoverished Lebanese live in rural governorates and work as farmers, herders, or fishermen. They do not have much access to banks or financial institutions, and therefore they have trouble getting the funds they need to invest in improving their businesses; fishermen cannot buy more efficient boats, and farmers do not have irrigated land.

Complicating matters even more, the banking sector in Lebanon is very conservative, officials at USAID/Lebanon say, requiring high collateral relative to loan value that the poor simply cannot provide.

In April 2009 USAID/Lebanon partnered with the Volunteers for Economic Growth Alliance (VEGA) to start the Lebanon Investment in Microfinance program to help existing micro-finance institutions (MFIs)[1] help the poor as well as small and medium-sized businesses by improving access to credit to increase sales, create jobs, and advance economic growth. In addition, the program provides training to MFIs. Through this program, the mission provides grants to eight MFIs serving various markets and specialties. For example, one is a cooperative that borrowers join when they qualify for a loan. Other MFIs are affiliated with commercial banks. Specialties range from small group loans to women to those that target geographic regions.

In September 2010 USAID/Lebanon awarded International Executives Service Corps (IESC) a 5-year grant extension—bringing the total estimated cost to $12 million—through a leader with associates award with VEGA.[2] As of March 21, 2013, the mission had obligated $8.8 million and spent $7 million.

Regional Inspector General/Cairo (RIG/Cairo) conducted this audit to determine whether the Lebanon Investment in Microfinance program was achieving its goals to increase sales, create jobs, and advance economic growth. The audit found that the program generally improved access to credit by providing loans to more than 6,300 borrowers. While 21 of 25 borrowers interviewed reported increased income and appeared to have benefited from the loans, the sample was not statistically representative and data were not available to confirm their claims. The program contributed to the creation of some jobs but the audit found that in some cases, it took credit for creating jobs that existed before the program began.

While the program contributed to positive outcomes noted above, the audit identified the following problems:

- Program indicators did not measure progress toward goals (page 3). The monitoring and evaluation plan did not have any indicators to measure sales or income.

[1] USAID defines an MFI as an organization whose activities significantly consist of providing financial services to micro-entrepreneurs.
[2] A leader with associates is a grant or cooperative agreement awarded to an organization to address a development problem. A mission can award an associate agreement to the leader's implementer to cover an activity that falls within the scope of the leader award.

- The mission did not obtain sustainability commitments from two of eight MFIs (page 4).

- The mission did not measure training results (page 5).

To address these problems, the audit recommends that USAID/Lebanon:

1. Collect and document data on the number of jobs created separately from data on the number of jobs maintained (page 4).

2. Implement a formula or method to measure income proxies of borrowers (page 4).

3. Define “job created” in writing for micro-finance reporting purposes (page 4).

4. Implement a monitoring procedure to track micro-finance partner progress toward sustainability (page 5).

5. Amend the Lebanon Investment in Microfinance program monitoring and evaluation plan to include an indicator measuring training results (page 5).

6. Collect and evaluate training outcome data already available from International Executives Service Corps (page 5).

Detailed findings appear in the following section. The audit’s scope and methodology are described in Appendix I. Mission’s comments, without attachments, are included in Appendix II, and our evaluation of them is on page 6.

AUDIT FINDINGS

Program Indicators Did Not Measure Stated Goals

USAID's *Performance Monitoring and Evaluation TIPS*, Number 6, "Selecting Performance Indicators," states that all indicators "taken as a group . . . should be sufficient to measure the stated result."

The program's indicators were not sufficient to measure the stated result. While the primary goals include increasing sales and income of micro-credit loan borrowers and creating jobs, the monitoring and evaluation plan does not include indicators that measure sales or income.

Additionally, IESC included all jobs in all businesses in the indicator that tracks jobs created because of the program. While the loan likely helped these businesses in some cases, many of the jobs they had were stable before receiving the loan. Therefore, the reported results did not reflect the number of jobs created. With no attempt to measure sales or income and overstated, unclear jobs results, program indicators did not measure the desired outcomes.

The agreement officer's representative (AOR) said the mission did not measure sales or income data because borrowers in general did not have adequate bookkeeping and mission employees did not think they could get accurate information. Audit site visits to loan recipients' businesses confirmed this difficulty. For example, the owner of a small convenience store said her sales grew by 50 percent because she used loan funds to buy a refrigerator (shown in the photograph below). However, she had no documents to support this claim, and refrigerated items were a small fraction of goods available in the store.

A shopkeeper used her USAID-funded loan to buy this commercial refrigerator. (Photo by RIG/Cairo April 23, 2013)

In addition, while the Agency has developed official methods that other missions implementing micro-finance activities use to assess poverty, none exists for Lebanon. The methods allow missions to collect information on things such as education level and ownership of various items that could be used to establish baseline proxies for sales and income. Actual and potential borrowers receive a score, which can then be compared to a subsequent score as a rough proxy for whether sales, income, or wealth have increased. While USAID/Lebanon is not required to use an official poverty assessment method, using an informal one could help the staff estimate changes in sales and income.

Monitoring plans and accompanying indicators should guide managers in making decisions (for example, where to focus financial and human resources), provide objective evidence of progress, and motivate staff. When plans lack adequate indicators, these goals cannot be met. Unclear definitions also led to unreliable reporting. For example, 11 of 25 borrowers visited had been in business for several years prior to receiving a loan, yet the program took credit for creating their jobs.

> ***Recommendation 1.*** *We recommend that USAID/Lebanon collect and document data on the number of jobs created separately from data on the number of jobs maintained.*
>
> ***Recommendation 2.*** *We recommend that USAID/Lebanon implement a method or formula to measure income proxies of borrowers.*
>
> ***Recommendation 3.*** *We recommend that USAID/Lebanon define in writing "job created" for micro-finance reporting purposes.*

Mission Did Not Obtain Sustainability Commitments

USAID's Automated Directives System (ADS) 219, "Microenterprise Development," instructs missions to partner with MFIs that are committed to sustainability. Before signing an agreement, a potential MFI partner must provide a written commitment to achieve sustainability within 7 years of receiving Agency funds. Sustainability is understood as profitability, which is defined as revenue an MFI makes from interest and fees on its loans that exceeds their cost. This number is captured by the operational sustainability ratio. A ratio of more than 100 percent (or a ratio of 1) is considered sustainable.

Based on the operational sustainability ratio, six of eight MFIs were sustainable when approved to work with Lebanon's Investment in Microfinance program. Two—Association d'Entraide Professionnelle (AEP) and Association for the Development of Rural Capacities (ADR)—were not. AEP had no data available, and officials there told auditors they were not sustainable and that their model for staying in business was to rely on contributions. A third-party agency reported ADR having an operational sustainability ratio less than 50 percent in 2011. Officials at ADR claimed the report was inaccurate and that they were indeed sustainable. They provided income statements to support this claim. However, the statements contained internal inconsistencies, such as different revenue totals from one page to the next. Accordingly, the mission should have obtained sustainability commitments from AEP and ADR.

In the case of AEP, mission officials said they did not obtain a sustainability commitment because they believed it was a reputable organization that had never struggled to receive sufficient donations. They did not provide a reason for not obtaining the commitment from ADR. Nevertheless, all partners should have provided a credible commitment to sustainability. Without obtaining commitments, the mission provided $1.2 million to potentially unsustainable development partners. During audit fieldwork, and in response to this finding, the mission obtained written sustainability commitments from AEP and ADR.

Recommendation 4*. We recommend that USAID/Lebanon implement monitoring procedures to track micro-finance partner progress toward sustainability.*

Mission Did Not Measure Training Results

USAID's ADS 253.3, "Participant Training for Capacity Development," requires missions that implement training financed by the Agency to "design, implement, and track the training . . . for results and impact, with the ultimate aim of strengthening institutional or organizational capacity." ADS further defines "training impact" as "improvements in job or organizational performance attributable to new skills, knowledge, and attitudes . . . acquired during training and applied at work settings."

The mission had not determined how the program's training strengthened capacity. It was on track to meet the target for the number of training participants and collected some training data. For example, IESC had trained more than 400 MFI managers and employees, and estimated that it had conducted pre- and post-training assessments for approximately 70 percent of training sessions. Nevertheless, the mission had not collected these available data and had not measured training results. Furthermore, the mission did not include a training results indicator (in addition to training participants) in the performance monitoring plan.

Mission officials said training results were not measured because the original 1-year program did not include a significant training portion. When the program was extended and the training element expanded, the mission did not update program indicators to reflect these changes because the extension was executed under a compressed timeline.

The program has spent $360,000 on training activities with an additional $400,000 budgeted. While training may improve participants' skills, knowledge, or attitudes, without measurement the mission cannot assess whether training outcomes are being achieved or whether these funds could be put to a better use. Therefore, we make the following recommendations.

Recommendation 5. *We recommend that USAID/Lebanon amend the Lebanon Investment in Microfinance program monitoring and evaluation plan to include an indicator measuring training results.*

Recommendation 6. *We recommend that USAID/Lebanon collect and evaluate training outcome data already available with International Executives Service Corps.*

EVALUATION OF MANAGEMENT COMMENTS

In its comments on the draft report, USAID/Lebanon generally agreed with all six recommendations. Based on our evaluation of management comments on our draft report, we acknowledge management decisions for all six Recommendations. Final action has been taken on Recommendations 1-5, and they are closed upon issuance of the audit report. A detailed evaluation of management comments follows.

Recommendation 1. On June 25, 2013, the mission modified the program's performance management plan to include an indicator to collect data on the number of jobs created separately from the collection of data on the number of jobs impacted. In the revised plan, the term "jobs impacted" relates to the number of jobs that existed at the inception of the loan and continued through the length of the loan. Based on the mission's comments and supporting documentation provided, we acknowledge that the mission made a management decision and final action has been taken on Recommendation 1.

Recommendation 2. On June 25, 2013, the mission modified the program's performance management plan to include a custom indicator that tracks the percentage increase of direct beneficiaries that report increases in average daily income because of loans provided through U.S. Government assistance. Based on the mission's comments and supporting documentation provided, we acknowledge that the mission made a management decision and final action has been taken on Recommendation 2.

Recommendation 3. On June 25, 2013, the mission modified the program's performance management plan and included a revised definition for "jobs created." Based on the mission's comments and supporting documentation provided, we acknowledge that the mission made a management decision and final action has been taken on Recommendation 3.

Recommendation 4. The mission has taken several actions to address the sustainability of MFIs. First, any institution with unsustainable financial ratios will have to sign and abide by a commitment to sustainably or not receive U.S. Government funds. Second, financial records of unsustainable MFIs will be monitored on a semiannual basis rather than annually, as is the current practice. Finally, as MFIs sign new contracts, the mission intends to include commitments to sustainability as well as commitments to submit semiannual financial records to VEGA as part of the contract terms. These new monitoring procedures were communicated to VEGA on July 2, 2013. Based on the mission's comments and supporting documentation provided, we acknowledge that the mission made a management decision and final action has been taken on Recommendation 4.

Recommendation 5. On June 25, 2013, the performance monitoring plan was modified to include two new custom indicators to measure training impact and results—*Number of management and/or staff of financial intermediaries showing increase in knowledge from before to after the USG-funded training experience* and *Number of financial intermediaries showing improved performance as a result of USG-funded training to their managers and/or staff*. Based on the mission's comments and supporting documentation provided, we acknowledge that the mission made a management decision and final action has been taken on Recommendation 5.

Recommendation 6. On June 20, 2013, USAID/Lebanon collected all training outcome data available at IESC. Mission officials said they intend to collect these data after each training session. In addition, the performance monitoring plan was modified to include an indicator that measures training—*Number of management and/or staff of financial intermediaries showing increase in knowledge from before and after the USG-funded training experience*. IESC will analyze the data and track them quarterly.

IESC will conduct a follow-on training needs' assessment that will be the basis for planning future training. This assessment will evaluate how past training provided to MFIs have affected participants' job performance and how participants have used the training to increase their daily work performance and quality. This assessment is due for submission to the Mission by the end of September 2013. Based on the mission's comments and supporting documentation provided, we acknowledge that the mission made a management decision.

SCOPE AND METHODOLOGY

Scope

We conducted this performance audit in accordance with generally accepted government auditing standards. They require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions in accordance with our audit objective. We believe that the evidence obtained provides that reasonable basis.

The purpose of this audit was to determine whether the Lebanon Investment in Microfinance program was achieving its goals of increasing sales, creating jobs, and advancing economic growth. Through a leader with associates award with VEGA, the mission gave IESC a 5-year, $10.5 million grant extension, making it a 6-year, $12 million program overall. As of March 21, 2013, the mission had obligated $8.8 million and spent $7 million. We audited supporting documentation for a statistically valid sample of 83 program loans ($4.5 million).

The audit covered the program from its inception date of May 8, 2009, through December 31, 2012. In planning and performing the audit, we assessed management controls related to documentation and data verification; reporting; and establishment and review of performance measures and indicators. We assessed the following significant controls: the program's performance management plan, site visit reports, semiannual portfolio implementation reviews, quarterly reports, and IESC's agreement and subawards, including modifications.

We conducted audit fieldwork from April 8 to April 30, 2013, at USAID/Lebanon in Beirut, and IESC and its MFI partners also in Beirut. We visited with borrowers in the governorates of Mount Lebanon, North, and Bekaa. However, four planned site visits were cancelled due to security concerns.

Methodology

To answer the audit objective, we met with personnel from USAID/Lebanon, IESC, and the MFIs. We reviewed documentation provided by USAID/Lebanon and IESC, including the performance management plan, monitoring and evaluation plan reports, the agreement, and subsequent modifications. We also reviewed progress and site visit reports.

To assess whether the program was achieving its goals, we interviewed IESC and MFI officials and reviewed supporting documentation of reported results. We inspected loan applications and associated documents for a statistically representative sample of borrowers. The results of document testing can be generalized across all loan applications. We interviewed a judgmental sample of 25 out of 6,300 borrowers at their place of business. We selected beneficiaries for site visits based on loan size, geography, and gender (we visited the largest, smallest, and at least one female borrower in each governorate in which security permitted). Site visit observations cannot be generalized to the population of borrowers.

MANAGEMENT COMMENTS

USAID | LEBANON
FROM THE AMERICAN PEOPLE

July 2, 2013

MEMORANDUM

To: Regional Inspector General/Cairo, Catherine Trujillo

From: USAID/Lebanon Acting Mission Director, Lyn Dunn/S/

Subject: Audit of USAID/Lebanon's Investment in Microfinance Program (Report No. 6-268-13-01X-P)

USAID/Lebanon is in general agreement with all of RIG's recommendations. The Mission has taken corrective measures and final actions have been completed on of all of the six audit recommendations. Accordingly, the Mission requests closure of all audit recommendations as per the corresponding responses provided below:

Recommendation No. 1: We recommend that USAID/Lebanon collect and document data on the number of jobs created separately from data on the number of jobs maintained.

Mission Response: On June 25, 2013, the Performance Management Plan (PMP) of the Lebanon Investment in Microfinance Program (LIM), under a Leader with Associate Award, Cooperative Agreement No. 268-A-00-09-0003, was modified to include an indicator to collect data on the number of jobs created separately from the collection of data on the number of jobs impacted, *(Attachment A*). In the revised PMP, the term "jobs impacted" is being used instead of "jobs maintained" to show the correlation between the new loans provided and the recurrent loans maintaining jobs.

Based on the above, the Mission believes that final action has been completed and requests closure of Audit Recommendation No. 1 upon report issuance.

Recommendation No. 2: We recommend that USAID/Lebanon implement a method or formula to measure income proxies of borrowers.

Mission Response: Based upon consultations between the Agreement Officer Representative (AOR), Social Impact (implementer of the monitoring and evaluation contract), and the Microfinance Institutions (MFIs), LIM's PMP was revised on June 25, 2013 *(Attachment A)* to include an custom indicator that tracks the percentage increase of direct beneficiaries' income as a result of loans provided from USG assistance. To track the loan effect on income, MFIs will collect income data on the loan at the inception of the loan and at the loan's termination, in order to obtain a measure of income change. Beneficiaries who experience a difficulty in measuring their income or even provide a proxy of it, will receive assistance from the MFI staff on how to maintain proper book-keeping in order to provide a proxy of their income. For existing loans issued a survey will be initiated, a random sample of current borrowers, in FY14 by the implementing partner that will provide results on the impact of loans issued on beneficiary's livelihood and jobs created and or maintained.

Based on the above, the Mission believes that final action has been completed and requests closure of Audit Recommendation No. 2 upon report issuance.

Recommendation No. 3: We recommend that USAID/Lebanon define in writing, "job created" for micro-finance reporting purposes.

Mission Response: On June 25, 2013 USAID/Lebanon defined in writing, "job created" for micro-finance reporting purposes to read "New job positions created as a result of new loans issued which is disaggregated by sex and age of employee". This definition has been included in the revised PMP *(Attachment A)*.

Based on the above, the Mission believes that final action has been completed and requests closure of Audit Recommendation No. 3 upon report issuance.

Recommendation No. 4: We recommend that USAID/Lebanon implement monitoring procedures to track microfinance partner progress toward sustainability.

Mission Response:
Under the Lebanon Investment in Microfinance Program, USAID Lebanon is currently supporting eight MFIs. Since the inception of the program, four MFIs have been sustainable based on their operational sustainability ratio. These are Al Majmoua'a, VITAS, EMKAN, and Makhzoumi Foundation. Two MFIs, namely the Lebanese Cooperative for Development (CLD), and the Entrepreneurial Development Fund (EDF), have recently become sustainable and this is mostly due to the support they received from USAID in terms of funds and/or technical assistance. CLD and EDF received USAID funds in the second and third rounds of financing but not during the first round. As for the remaining two MFIs, AEP and ADR, they remained to be unsustainable to the date the audit was conducted, based on their operational sustainability ratio. On April 22, 2013, and April 29, 2013, USAID/ Lebanon received commitments to sustainability from two MFI's, "Association D'Entraide Professionelle" *(Attachment B)* and "Association for the Development of Rural Capacities" *(Attachment C)*, respectively. USAID Lebanon has previously ensured that MFIs receiving USG supported funds were sustainable one way or another whether through their financial results or their presence in the market, or even through other factors that might influence the sustainability of the MFI, such as the level of donor support the MFI receives. Moving forward, USAID will enforce stricter measures to track the sustainability of MFIs based solely on their financial performance as per the audit recommendation. Any MFI with unsustainable financial ratios will either have to sign and abide by a commitment to sustainably or not receive USG funds. Furthermore, USAID Lebanon, through its implementing partner IESC/VEGA, will guide these MFIs towards sustainability through technical assistance. Under the LIM program, financial records of MFIs are monitored on an annual basis. Moving forward, and to help unsustainable MFIs reach sustainability, financial records of unsustainable MFIs will be monitored on a semi-annual basis. MFIs will sign new sub-contracts in September 2013, and these new sub-contracts will include commitments

to sustainability as well as commitments to submit semi-annual financial records to IESC/VEGA. On July 2, 2013, the AOR sent an email to the implementing partner indicating this new procedure (*Attachment D*).

Based on the above, the Mission believes that final action has been completed and requests closure of Audit Recommendation No. 4 upon report issuance.

Recommendation No. 5: We recommend that USAID/Lebanon amend the Lebanon Investment in Microfinance program monitoring and evaluation plan to include an indicator measuring training results.

Mission Response: On June 25, 2013, the PMP was modified to include two new custom indicators to measure training impact and results, (*Attachment A).* The first indicator is “Number of management and/or staff of financial intermediaries showing increase in knowledge from before to after the USG- funded training experience.” This indicator is based on training outcome data already available at IESC. The second custom indicator is “Number of financial intermediaries showing improved performance as a result of USG-funded training to their managers and/or staff.” This indicator will be based on feedback received from MFI management. Targets have been established for these indicators for FY14 and FY15 and are available in the revised PMP.

Based on the above, the Mission believes that final action has been completed and requests closure of Audit Recommendation No. 5 upon report issuance.

Recommendation No. 6: We recommend that USAID/Lebanon collect and evaluate training outcome data already available with International Executives Service Corps.

Mission Response: On June 20, 2013, USAID/Lebanon collected all training outcome data available at IESC and this data is now available on a CD at USAID offices *(Attachment E).* A sample of these surveys, is enclosed *(Attachment F*). Going forward, after each training session, USAID Lebanon will collect all training outcome data. On June 25, 2013, the PMP was modified (*Attachment A*) to include an indicator that measures training “Number of management and/or staff of financial intermediaries showing increase in knowledge from before to after the USG- funded training experience.” IESC/VEGA will analyze the data and track it using the indicator, as per the revised PMP, (Attachment A).

Based on the above, the Mission believes that final action has been completed and requests closure of Audit Recommendation No. 6 upon report issuance.

List of Attachments

Attachment A: Modification of PMP on June 25, 2013

Attachment B: Commitment to Sustainability (AEP)

Attachment C: Commitment to Sustainability (ADR)

Attachment D: E-mail from AOR to implementing partner addressing the issue of MFI Sustainability.

Attachment E: E-mail from implementing partner indicating that training data was sent to USAID on a CD Sample survey available at USAID offices

Attachment F: Sample survey available at USAID offices

Attachment G: AOR approval of revised PMP

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