



Report and Recommendation of the President to the Board of Directors

Project Number: 50239-001
January 2017

Proposed Equity Investment CreditAccess Asia (Regional)

This is an abbreviated version of the document approved by ADB's Board of Directors that excludes information that is subject to exceptions to disclosure set forth in ADB's Public Communications Policy 2011.

Asian Development Bank

CURRENCY EQUIVALENTS

(as of 31 December 2016)

Currency unit – Indian rupee/s (Re/Rs)

Re1.00	=	€0.01376	or	\$0.01471
\$1.00	=	Rs67.97	or	€0.9506
€1.00	=	Rs72.36	or	\$1.052

Currency unit – rupiah (Rp)

Rp1.00	=	€0.0000704	or	\$0.0000741
\$1.00	=	Rp13,492	or	€0.9506
€1.00	=	Rp14,172	or	\$1.052

Currency unit – peso (P)

P1.00	=	€0.01885	or	\$0.02016
\$1.00	=	P49.61	or	€0.9506
€1.00	=	P52.98	or	\$1.052

ABBREVIATIONS

ADB	–	Asian Development Bank
BSP	–	Bangko Sentral ng Pilipinas
CAA	–	CreditAccess Asia
CEO	–	chief executive officer
JLG	–	joint liability group
MFI	–	microfinance institution
NBFC	–	nonbank financial company
NGO	–	nongovernment organization
OST	–	operations support team

NOTES

- (i) The fiscal year (FY) of CreditAccess Asia ends on 31 March. “FY” before a calendar year denotes the year in which the fiscal year ends, e.g., FY2017 ends on 31 March 2017.
- (ii) In this report, “\$” refers to US dollars.

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PROJECT AT A GLANCE

1. Basic Data		Project Number: 50239-001	
Project Name	Equity Investment in CreditAccess Asia	Department /Division	PSOD/PSFI
Country	REG		
2. Sector		ADB Financing (\$ million)	
✓ Finance	Inclusive finance		50
		Total	50.00
3. Strategic Agenda		Subcomponents	Climate Change Information
Inclusive economic growth (IEG)	Pillar 2: Access to economic opportunities, including jobs, made more inclusive		Climate Change impact on the Project Low
4. Drivers of Change		Components	Gender Equity and Mainstreaming
Private sector development (PSD)	Promotion of private sector investment		Gender equity (GEN) ✓
5. Poverty and SDG Targeting		Location Impact	
Geographic Targeting	Yes	Rural	High
Household Targeting	Yes	Urban	Medium
SDG Targeting	Yes		
SDG Goals	SDG8		
6. Nonsovereign Operation Risk Rating - NA			
7. Safeguard Categorization		Environment: FI-C	Involuntary Resettlement: FI-C
			Indigenous Peoples: FI-C
8. Financing			
Modality and Sources		Amount (\$ million)	
ADB		50.00	
Nonsovereign Direct Investment: Ordinary capital resources		50.00	
B-Loans		0.00	
None		0.00	
Official Cofinancing^a		0.00	
None		0.00	
Others^b		35.00	
Total		85.00	

^a Concessional financing from external sources.

^b Derived by deducting ADB financing, B Loans and Official Cofinancing from Project Total Cost.

I. THE PROPOSAL

1. I submit for your approval the following report and recommendation on a proposed equity investment of up to €45,000,000 in CreditAccess Asia (CAA) to provide growth capital to support CAA's pan-Asia microfinance operations.¹

II. THE FINANCIAL INTERMEDIARY

A. Investment Identification and Description

2. **Microfinance subsector overview: India.** As of 31 March 2016, the microfinance subsector in India provided microcredit to 33.2 million customers through 9,781 branches across the country, disbursing 34.7 million loans amounting to Rs670 billion (average loan size of \$265).² Disbursements in FY2016 grew 78.2% over FY2015, while the aggregate gross loan portfolio growth increased 91.0% during the same period. Since FY2013, there has been a compound annual growth rate of 88.6% in disbursements and 93.7% in the gross loan portfolio in the sector.³ Due to continuing demand and large underserved segments, CRISIL, a rating agency, expects the aggregate microfinance institution (MFI) loan portfolio to grow 30%–34% annually from FY2016 to FY2020. Problem loans among MFIs have been steadily decreasing, falling from 0.50% in FY2013 to 0.33% in FY2016 for 30 days past due. However, high growth rates, partly driven by an increase in client leverage in the top 10 states for microfinance lending, might put pressure on portfolio quality by 2020.⁴

3. **Microfinance subsector overview: Indonesia.** Commercial banks dominate Indonesia's financial system, have wide access across various areas of the country, and account for 98% of the system's loans. As banking regulations require customers to have proof of a permanent job, income, and physical collateral, a significant portion of microfinance demand is met by a large number of nonbank financial institutions, including rural banks, regional cooperatives, multifinance companies, and venture capital companies.⁵ Consequently, few large-scale MFIs have national coverage. Large nationwide institutions that cater to individuals earning \$2–\$6 per day are (i) BTPN Syariah, a commercial bank that uses the joint liability group (JLG) methodology to serve around 2 million clients; and (ii) Mitra Bisnis Keluarga Ventura, a venture capital company and the largest JLG lending nonbank MFI in Java, with a client base of almost 600,000.⁶

4. **Microfinance subsector overview: Philippines.** According to the Bangko Sentral ng Pilipinas (BSP), banks are a source of borrowing for only 4.4% of the Philippine population, while financing companies lend to 12.0% of the population, cooperatives to 10.5%, microfinance nongovernment organizations (NGOs) to 9.9%, and government entities to 6.1%. NGOs typically

¹ The Asian Development Bank (ADB) will make an initial investment of up to €30 million in CAA.

² The information pertains to nonbanking financial company MFIs, which constitute over 90% of the microfinance subsector's total business in India on aggregate. The data excludes Bandhan, which was the largest MFI in the country and converted to a full-fledged bank in August 2015.

³ Microfinance Institutions Network. 2016. *Micrometer: Data as of 31st Mar 2016*. Issue 17. Gurgaon. This figure excludes the portfolio of Bandhan and the microfinance portfolio in Andhra Pradesh.

⁴ India Ratings and Research. 2016. *Microfinance: Borrower Overleverage Warrants Course Correction from MFIs*. Mumbai.

⁵ Venture capital companies in Indonesia are private companies allowed to provide financing to micro, small, and medium-sized enterprises in the form of capital or working capital. They can also be an insurance agent.

⁶ A JLG is a group, typically of 4–10 people from the same village, who come together to take out loans without providing any collateral. Each member of the group is jointly and severally liable for the repayment of loans taken by all group members.

serve the portion of the population with the lowest income and hold a total portfolio of P11.6 billion with about 2.5 million borrowers (up from P2.6 billion in 2002).⁷ Since 2000, the BSP has been improving the National Framework for Microfinance Regulation, which was rated third best in the world (at the same level as India) by the Economist Intelligence Unit.⁸ The strong regulatory environment has led to an approved national strategy for financial inclusion, which further promotes access to finance and financial stability.

5. **Gender and microfinance.** Women are one of the most vulnerable groups in the world's poorest populations, and a significant number of them remain unbanked. According to the World Bank's financial inclusion data, in 2014 women lagged behind men in terms of borrowing from formal financial institutions in India, with 7.8% of men and only 4.9% of women accessing credit. In Indonesia, 15.1% of men and 11.2% of women had access to credit. In the Philippines, while more women were able to borrow from financial institutions than men (13.6% for women compared to 9.9% for men), the unbanked female population remains significant.⁹ Businesses owned by women remain unevenly constrained by a lack of access to credit. Constraints include lack of a land title, lack of collateral needed to obtain credit, low income, lack of financial documents, and unfamiliarity with paperwork and procedures.¹⁰ Nonbank microfinance models have provided an alternative channel for provision of financial services to women because they address the constraints of traditional banking models by, for example, having limited or no collateral requirements.¹¹ Well-designed microfinance products provide an opportunity for women to enter the formal finance sector, build microfinance credit histories, and increase economic activities.

6. **Rationale.** Access to finance is a key challenge in Asia, with estimated unbanked populations of 46% in South Asia and 69% in East Asia and the Pacific. Access to credit is even more limited in these regions, with less than 14% of borrowers accessing credit through formal channels in South Asia and 27% in East Asia and the Pacific (footnote 9). Given the continued need to address access to credit for many customer segments across developing Asia, the Asian Development Bank (ADB) has sought to identify partner financial institutions that have demonstrated the ability to reach underbanked segments profitably and sustainably. Through a microfinance holding company model, ADB will support financial inclusion across several markets where access to finance is severely restricted. ADB will be able to do so without taking direct exposure on higher risk early-stage entities in these markets and will benefit from the larger and more profitable Indian operation, Grameen Koota, which is the largest asset on CAA's balance sheet, thus lowering ADB's portfolio unsystematic risk. This allows for greater development impact with greater risk diversification, as failure of any one of the new subsidiaries will not significantly impact the overall operations of CAA, thus also protecting ADB's interests. The investment also allows greater diversification of ADB's microfinance exposure by geography and currency. The holding company model also allows the newer operating subsidiaries to draw on the experience of the established subsidiaries, while simultaneously offering more agility to innovate and pilot initiatives that can be later adopted by larger MFI subsidiaries. Holding companies add value to their subsidiaries by providing stronger branding and support to the operating MFIs in areas such

⁷ BSP. 2015. *National Baseline Survey on Financial Inclusion*. Manila.

⁸ Economist Intelligence Unit. 2016. *Global Microscope 2016: The Enabling Environment for Financial Inclusion*. New York (sponsored by the Multilateral Investment Fund, a member of the Inter-American Development Bank Group; Accion; and the Metlife Foundation).

⁹ World Bank (WB). Global Findex (Global Financial Inclusion Database). <http://databank.worldbank.org/data/reports.aspx?source=1228> (accessed 8 December 2016).

¹⁰ ADB. 2013. *India: Gender Equality Diagnostic of Selected Sectors*. Manila.

¹¹ International Finance Corporation. 2014. *Micro, Small, and Medium Enterprise Finance: Improving Access to Finance for Women-Owned Businesses in India*. Delhi.

as access to funding, human resource processes, risk control, and information technology functions. Microfinance holding company models have been successfully tested in other instances. ADB has worked with AccessHolding as a lender to AccessBank Azerbaijan, and has also worked with FINCA International, which operates under a similar model with 23 operating subsidiaries. CAA's track record of supporting highly successful MFIs, such as Grameen Koota and Equitas Holdings, and commitment to expanding the model to other markets in Southeast Asia with a strong focus on women make it an excellent partner for ADB. ADB will support CAA's expansion of its operating subsidiaries in ADB's developing member countries, while reinforcing the network's governance, technology, and innovative product development. The role of ADB as CAA's first development financial institution investor is also expected to attract further funding, which will be channeled to Asian microfinance markets.

B. Business Overview and Strategy

7. **Business overview.** CAA, a holding company headquartered in Amsterdam, operates MFIs across Asia, serving approximately 1.8 million clients (99.8% of whom are women) with JLG loans (loan sizes of €200–€500), individual loans (€500–€2,000), and other financial services such as life and health insurance. CAA started operations in 2006 under the leadership of Paolo Brichetti and a group of Italian investors. At the start of its operations, CAA took minority stakes in MFIs and was an early-stage investor in Grameen Koota and Equitas Holdings in India. In 2011, the company changed its strategy to an operator model and started new MFIs in Indonesia (Bina Artha Ventura) and the Philippines (One Puhunan), while acquiring a majority stake in Grameen Koota.¹² As of August 2016, the CAA Group had a loan portfolio of about €440 million distributed across 692 branches in three countries, and employed 7,325 people worldwide. CAA also holds a 5.21% stake in Equitas Holdings, India's fourth-largest MFI.

8. **The operating subsidiaries.** With an income-generation capacity of over €1 million in net profits monthly, Grameen Koota is the backbone of the CAA Group. It started operations in 1999 as a nonbank financial company (NBFC) in India. As of August 2016, it had a loan portfolio of €409 million with over 1.5 million women customers in 390 branches spread across 74 districts in five states (Chhattisgarh, Karnataka, Maharashtra, Madhya Pradesh, and Tamil Nadu) and 4,610 staff members. Grameen Koota was awarded MFI of the Year in the Large MFI category in the Microfinance India 2015 Awards. Grameen Koota has been part of ADB's Microfinance Risk Participation Program since 2012. Bina Artha started operations as a venture capital company in December 2011. As of August 2016, it had a loan portfolio of €20.4 million with 195,353 clients served by 192 branches and 1,715 staff members. One Puhunan started operations in February 2014. As of August 2016, it had a loan portfolio of €10.7 million with 109,225 clients served by 110 branches and 1,000 staff members.

III. THE PROPOSED ADB ASSISTANCE

A. The Assistance

9. ADB funding consists of up to €45 million in equity investment in CAA, with an initial investment of up to €30 million. Depending on the total equity raised by CAA in the current capital-raising round, ADB's final stake in CAA is estimated to be 9%. CAA will use ADB's proceeds to capitalize the existing subsidiaries and support their growth. Under separate approval, ADB will

¹² CAA is also starting operations in Viet Nam, where it commenced a pilot in November 2016 and expects to start full-fledged operations by the end of April 2017.

provide capacity building technical assistance of up to \$500,000, which will accompany ADB funding and will support CAA's institutional strengthening with initiatives such as the roll out of strategic information technology projects, including data mining and cashless processes.¹³

B. Implementation Arrangements

10. ADB will monitor the project throughout its duration.¹⁴ CAA will provide ADB with financial reports at predetermined regular intervals and on demand (both at a consolidated and subsidiary level), including (i) quarterly unaudited financial statements, (ii) annual audited financial statements, (iii) reports on CAA's loan portfolio characteristics, (iv) annual reports on selected development indicators agreed between ADB and CAA, and (v) annual reports on safeguards and social protection compliance.

C. Value Added by ADB Assistance

11. **Supporting finance sector development and financial inclusion.** The proposed transaction seeks to support a private financial institution's growth as it expands its operations across some of Asia's most significantly underserved markets where financial outreach is lowest. While CAA has been able to access other sources of funding, ADB will provide a high quality stable source of capital with a long term vision aligned with CAA's goal to contribute to closing the financial gap currently unmet by mainstream financial institutions and investors.

12. **Support inclusive growth as a strategic shareholder.** ADB will be CAA's first multilateral institutional partner. CAA specifically approached ADB because (i) CAA's areas of operations align with ADB's regional focus, and (ii) a partnership with ADB can help facilitate dialogue with governments to foster a more conducive environment for microfinance. Through ADB's nominee director on CAA's board and broader shareholder engagement, CAA hopes to benefit from ADB's experience with other financial institutions in the region.¹⁵ Having ADB as a strategic shareholder will send a positive signal to potential new investors.

13. **Strengthening capital adequacy of CreditAccess Asia's subsidiaries.** CAA will need to further capitalize its subsidiaries to support their growth as they expand in response to the significant demand for credit from their targeted underserved and unserved segments and the needs of their clients. The proceeds from ADB's investment will have a multiplier effect. Following ADB's investment, CAA plans to infuse capital in its operations in India, Indonesia, and Viet Nam.¹⁶

14. **Gender equity theme.** The World Bank's Global Findex reveals that women lag behind men in financial access, with a gap between men and women of 4% in East Asia and 18% in South Asia.¹⁷ According to a Goldman Sachs study, if the credit gap is closed by 2020 in Brazil, Russia, India, and the People's Republic of China plus the Next Eleven countries (including Indonesia, the Philippines, and Viet Nam), per capita incomes could be 12% higher on average

¹³ The technical assistance will be approved separately and will be financed on a grant basis by ADB's Technical Assistance Special Fund (TASF-other sources).

¹⁴ Details of Implementation Arrangements (accessible from the list of linked documents in Appendix 2).

¹⁵ ADB will only be entitled to nominate a director for so long as it retains a shareholding above a certain threshold.

¹⁶ Assuming a target capital adequacy ratio of 20%, ADB's initial investment is expected to support disbursements of €150 million in these jurisdictions.

¹⁷ WB. Global Findex Data: Gender. <http://datatopics.worldbank.org/financialinclusion/indv-characteristics/gender> (accessed 18 November 2016).

by 2030.¹⁸ CAA's subsidiaries target primarily women with services adapted to their needs, including loans for income-generation purposes, sanitation, health, and education. ADB has provided expert advice in the preparation of a gender action plan to help CAA become more effective in serving women clients' needs. CAA's institutional capacity on this domain will be further reinforced with ADB's technical assistance. The project is expected to benefit at least 3.5 million women borrowers directly by 2021 and is classified as a gender equity project.¹⁹

IV. DEVELOPMENT IMPACT AND STRATEGIC ALIGNMENT

A. Development Impact, Outcome, and Outputs

15. **Impact.** The impact will be strengthening the capacity of domestic financial institutions to encourage and expand access to banking, insurance, and financial services for the underbanked and unbanked population.

16. **Outcome.** ADB's equity investment will allow increased uptake of financial services by women to narrow the gender gap in financial inclusion.

17. **Outputs.** The project's outputs will be (i) the increase in CAA's capacity to provide loans and other financial services to micro entrepreneurs and micro businesses by investing up to €45 million in MFIs, (ii) the introduction of a new financial product, and (iii) the expansion of CAA's business into new markets.

B. Alignment with ADB Strategy and Operations

18. The Midterm Review of Strategy 2020 emphasizes ADB's support for the finance sector.²⁰ The proposed investment contributes to finance sector development by supporting the growth of an institution that is dedicated to delivering access to finance to the significantly unserved and underserved population in Asia. The Midterm Review of Strategy 2020 also seeks to promote inclusive growth. Without access to formal financial services, people with lower income or in underserved segments will be excluded from the growth process and its benefits. The proposed equity investment will support microfinance in India, Indonesia, the Philippines, and Viet Nam. Microfinance is one of the financial infrastructures identified as a high priority for the governments of the target countries. The investment also aligns with ADB's country partnership strategies for India, Indonesia, the Philippines, and Viet Nam; and with ADB's Gender Equality and Women's Empowerment Operational Plan, 2013–2020.²¹

¹⁸ The Next Eleven countries, according to Goldman Sachs, are Bangladesh, Egypt, Indonesia, Iran, Republic of Korea, Mexico, Nigeria, Pakistan, the Philippines, Turkey, and Viet Nam. Goldman Sachs, Global Markets Institute. 2014. *Giving Credit Where It Is Due: How Closing the Credit Gap for Women-Owned SMEs Can Drive Global Growth*. <http://www.goldmansachs.com/our-thinking/public-policy/gmi-folder/gmi-report-pdf.pdf>.

¹⁹ Gender Action Plan (accessible from the list of linked documents in Appendix 2).

²⁰ ADB. 2014. *Midterm Review of Strategy 2020: Meeting the Challenges of a Transforming Asia and Pacific*. Manila.

²¹ ADB. 2013. *Country Partnership Strategy: India, 2013–2017*. Manila; ADB. 2016. *Country Partnership Strategy: Indonesia, 2016–2019—Towards a Higher, More Inclusive and Sustainable Growth Path*. Manila; ADB. 2011. *Country Partnership Strategy: Philippines, 2011–2016*. Manila; ADB. 2016. *Country Partnership Strategy: Viet Nam, 2016—Fostering More Inclusive and Environmentally Sustainable Growth*. Manila; ADB. 2013. *Gender Equality and Women's Empowerment Operational Plan, 2013–2020: Moving the Agenda Forward in Asia and the Pacific*. Manila.

V. POLICY COMPLIANCE

A. Safeguards and Social Dimensions

19. The investment is classified category FI treated as category C for impacts on the environment, involuntary resettlement, and indigenous peoples. The potential environmental and social impacts of the proposed investments and associated risks of CAA and its subsidiaries' business activities have been assessed, and there are expected to be minimal or no adverse environmental impacts, and impacts on involuntary resettlement and indigenous peoples are unlikely. The lending portfolio of CAA's operating subsidiaries comprises small loans of \$200–\$2,000 to JLGs and individual micro entrepreneurs. Projects classified category A for the environment and category A or category B for involuntary settlement or indigenous peoples will be excluded from its portfolio. CAA and its subsidiaries will apply ADB's prohibited investment activities list, ensure that its lending activities abide by applicable national laws and regulations, and comply with ADB's Safeguard Policy Statement (2009). CAA and its subsidiaries will confirm this in their periodic report to ADB.²² They will comply with national labor laws and will take measures to comply with internationally recognized core labor standards. CAA will collect the reports of its operating subsidiaries and submit a consolidated report regularly to ADB on its compliance with such laws, and the measures taken.

B. Anticorruption Policy

20. CAA was advised of ADB's policy of implementing best international practice relating to combating corruption, money laundering, and the financing of terrorism. CAA's draft know-your-customer and anti-money-laundering policy, which is subject to board approval, mitigates the risks of money laundering and the financing of terrorism. ADB will ensure that the investment documentation includes appropriate provisions prohibiting corruption, money laundering, and the financing of terrorism, and remedies for ADB in the event of noncompliance.

C. Investment Limitations

21. The proposed equity investment is within the medium-term country, industry, group, and single investment exposure limits for nonsovereign investments.

D. Assurances

22. Consistent with the Agreement Establishing the Asian Development Bank (the Charter),²³ ADB will proceed with the proposed assistance upon establishing that the governments of Indonesia, the Philippines, and Viet Nam have no objection to the proposed investment in CAA. ADB will enter into suitable finance documentation, satisfactory to ADB, following approval of the proposed assistance by the Board of Directors.

VI. RECOMMENDATION

23. I am satisfied that the proposed equity investment would comply with the Articles of Agreement of the Asian Development Bank (ADB) and recommend that the Board approve the equity investment of up to €45,000,000 from ADB's ordinary capital resources in CreditAccess

²² Summary Poverty Reduction and Social Strategy; Safeguards and Social Dimensions Summary (accessible from the list of linked documents in Appendix 2).

²³ ADB. 1966. *Agreement Establishing the Asian Development Bank*. Manila.

Asia, with such terms and conditions as are substantially in accordance with those set forth in this report, and as may be reported to the Board.

Takehiko Nakao
President

30 January 2017

LIST OF LINKED DOCUMENTS

<http://www.adb.org/Documents/RRPs/?id=50239-001-4>

1. Sector Overview
2. Contribution to the ADB Results Framework
3. Country Economic Indicators
4. Summary Poverty Reduction and Social Strategy
5. Safeguards and Social Dimensions Summary