

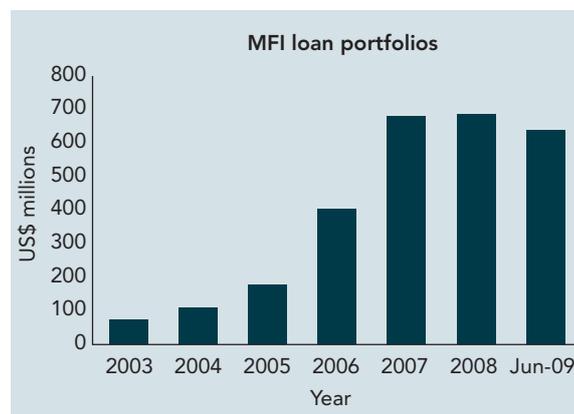
## The Rise, Fall, and Recovery of the Microfinance Sector in Morocco

Morocco is a recognized microcredit champion, boasting 40 percent of client outreach in the Arab world and host to some of the best performing microfinance institutions (MFIs) in the world. But since 2007, the microcredit sector has been confronting a crisis. There are 12 licensed MFIs<sup>1</sup> in Morocco, serving close to 1 million clients<sup>2</sup> with combined assets of 5.7 billion dirham (US\$705 million<sup>3</sup>) as of December 2008. The industry is heavily concentrated, and the four largest MFIs account for 90 percent of client outreach.

The Moroccan microcredit sector has enjoyed one of the most extraordinary growths seen in the microfinance industry. In just four years, from 2003 to 2007, MFI loan portfolios multiplied 11 times and client outreach by four, according to MIX. This exuberant growth was driven by four leading MFIs—Zakoura, Al-Amana, Fondation des Banques Populaires, and Fondep. These institutions scored remarkably well on all microfinance performance metrics, including scale, depth of outreach, asset quality, and profitability. These impressive results did not go unnoticed, and Al-Amana and Zakoura were awarded several international prizes (including MIX's world's best performing MFI and the European prize for microfinance). In 2007, Morocco had one of the most vibrant and successful microfinance sectors in the world.

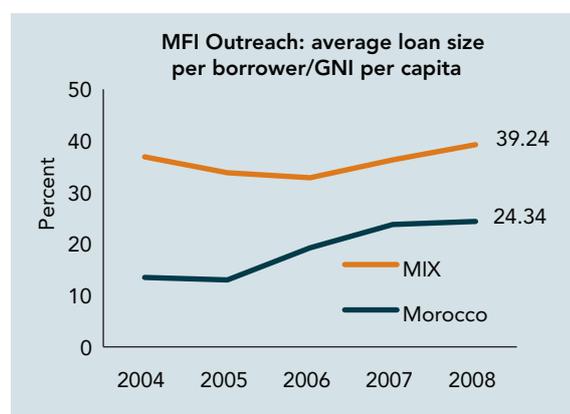
This success could not have happened without the continued support of the Moroccan Government. The Microfinance Law of 1999 provided a clear framework<sup>4</sup> for the development of the industry, and the Moroccan Government provided financial support through a government fund—Le Fonds Hassan II helped to capitalize the first MFIs. The Ministry of Finance ensured close monitoring, and the Central Bank, Bank Al-Maghrib (BAM), took over supervision in 2007. The sector also benefited from the support of the international donor community, most notably USAID and the European Commission, now relayed by development finance institutions (DFIs) such as IFC and KfW. A unique characteristic of the Moroccan microcredit sector is the commitment of local banks: Commercial banks are important backers of the industry, having created two of the largest MFIs and funding 85 percent of the sector's assets in 2008.

**Figure 1: High growth**



Source: BAM and JAIDA.  
Note: Total loan portfolio for all 12 Moroccan MFIs, converted to US\$ at end of year exchange rate.

**Figure 2: Deep client outreach**



Source: MIX.  
Note: Average loan size weighted by borrowers. MIX average, all MFIs reporting to MIX 2004–2008.

1 Association de Microcrédit in French.  
2 The Central Bank of Morocco reported 1.3 million credit accounts for an estimated client base of 1 million as of December 2008.  
3 31 December 2008 US\$/Moroccan Dirham Exchange Rate (1US\$/8.08 MAD).  
4 Law 18-97 of 1999. MFIs are nonprofit associations licensed by the Ministry of Finance. They are allowed to provide microcredit services for income-generating activities as well as housing and social loans with a maximum of 50,000 dirham.

## The sector in crisis

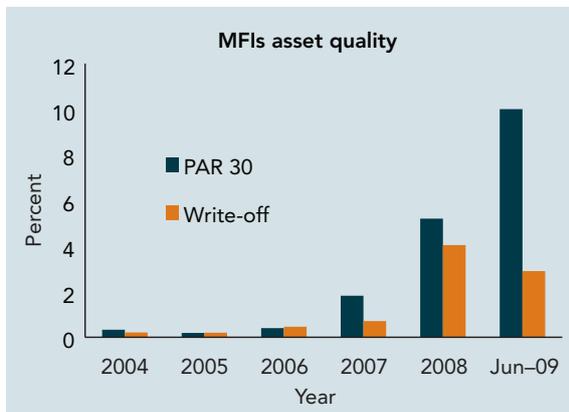
In 2007 some signs of stress—notably loan delinquency and multiple lending (clients with loans from two to five different MFIs)—started to emerge. A 2006 Planet Finance study<sup>5</sup> highlighted the concentration of microfinance loans in large cities, such as Casablanca, Fez, and Marrakesh, and the development of multiple lending in urban areas. Nonperforming loans started to rise significantly from one of the lowest levels in the world, 0.42 percent in 2003 to 1.9 percent in 2007.<sup>6</sup>

In December 2007, the global credit crisis had already started, but its extent was hidden by the astonishing growth of the loan portfolio. Delinquency was significant for loans granted in early 2007, but the bulk of the portfolio was originated in the past six months and not exposed to arrears yet. Portfolio at risk greater than 30 days (PAR 30) at 1.9 percent was still far below the world average of 2.7 percent reported by

MIX.<sup>7</sup> MFI managers, funders, and even rating agencies were complacent and did not see the looming delinquency crisis coming. The sharp rise in nonperforming loans took place in 2008 and affected all MFIs. PAR 30 increased significantly to 5 percent in December 2008 and reached an alarming level of 10 percent in June 2009.<sup>8</sup> Write-offs also increased dramatically with a negative impact on MFI profitability and solvency. In May 2009, Zakoura, one of the Moroccan flagship institutions, reported a PAR 30 of over 30 percent and decided to merge with another MFI, Fondation des Banques Populaires.

The causes of the crisis are well known and can be summarized in two words: unsustainable growth. The global financial crisis is not to blame.<sup>9</sup> It is primarily a crisis of the MFIs themselves. This unprecedented growth had overstretched MFI capacity, translating into lenient credit policies, obsolete management information systems (MIS), lack of internal controls, and substandard governance. In early 2007, Zakoura undertook aggressive growth to catch up with its main competitor, Al Amana, even though it did not have a well-functioning MIS.<sup>10</sup> At the same time some leading MFIs diversified their loan products and offered larger loans with poor underwriting policies. A 2008 research study concluded that 40 percent of loan delinquency could be attributed to changes in credit methodology (a shift to individual lending, increase in loan size, and shift from weekly to monthly installment frequency).<sup>11</sup> Multiple lending to the same clients is also an aggravating factor although not the origin of the crisis. A 2008 BAM study estimated that 40 percent of microcredit beneficiaries have more than one loan. The problem is particularly acute in urban areas.

**Figure 3: Fast-growing delinquency**



Source: MIX.

Note: Weighted average ratio for MFIs reporting to MIX, CGAP, and JAIDA estimates for June 2009 write-off.

5 Etude sur les endettements croisés au Maroc, June 2006, Planet Finance.

6 Based on MIX data and MFI audited reports.

7 PAR 30 2007 is 2.7 percent, *MicroBanking Bulletin* 17 August 2008.

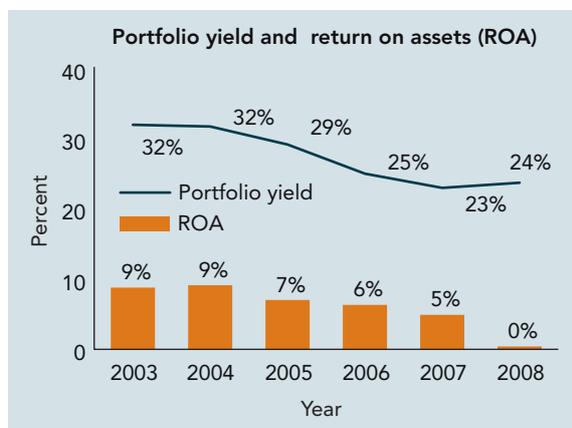
8 Interview with BAM officials, September 2009.

9 The financial crisis is not to blame but the increase in food prices in early 2008 did impact poor households.

10 Zakoura grew by 137 percent in 2007, but its homegrown MIS was poorly designed and did not have the proper checks and balances in place. Zakoura later acquired Evolan, a robust system from SOPRA that was rolled out in the second half of 2007.

11 Private IFC research, December 2008.

**Figure 4: Profitability declined in 2008**



Source: MIX.

Note: Weighted average ratio of Moroccan MFIs reporting to MIXmarket.

The response of the Moroccan microfinance sector has been swift and timely. The government organized the acquisition of Zakoura by the Fondation des Banques Populaires, a large MFI backed by a solid state bank, in record time to restore confidence and avoid contagion effects on loan delinquency. Lenders also have been cooperative. Local commercial banks have maintained their credit allocations, and DFIs have not called their loans. At the same time, MFIs have slowed down their growth considerably and reduced their balance sheet size. Total assets shrank by 1.2 percent in 2008 and by 7 percent during the first six months of 2009.<sup>12</sup> As a result, MFIs' cash position has reached record levels (over 15 percent at the end of 2008), and large MFIs are not expecting liquidity shortages until mid 2010.

MFIs also have put in place an aggressive recovery plan, including, in some cases, senior management changes. MFIs are tightening their credit processes, putting together teams dedicated solely to loan recovery, and taking judicial action against delinquent borrowers. They are also exchanging

credit information weekly to control cross-lending. The share of clients with multiple loans has dropped from 39 percent in October 2008 to 29 percent in September 2009.<sup>13</sup> Finally, small and medium-size MFIs are planning to cut costs and share resources by merging or sharing back office systems. These efforts are slowly paying off, and a recovery is expected in the first semester of 2010. While some MFIs are severely hit and will have to be restructured, others are emerging stronger and are well positioned for another phase of growth.

## The government's response

The government has also developed a plan in close collaboration with BAM and the Federation of MFIs (FNAM) to consolidate the microcredit sector.

The first priority is to strengthen MFIs. BAM produced a new directive to strengthen the governance of MFIs and improve transparency. The Moroccan Government also secured US\$46 million from the Millennium Challenge Account to provide MFIs with capital and technical assistance to strengthen MFIs' systems and internal controls.

The second priority is to control multiple lending and prevent over-indebtedness. To that end, the four largest MFIs will be integrated into the credit bureau set up by BAM before the end of 2009. This is a major step forward to improve credit analysis as well as to control clients' over-indebtedness.

The third priority is to secure liquidity for the sector beyond 2009. The government is encouraging linkages between MFIs and banks. Two of the largest MFIs already have been established by local banks, and smaller MFIs are being encouraged to find bank sponsors.

<sup>12</sup> JAIDA report, "Microfinance un an apres l'annonce des turbulences," (June 2009) based on total microfinance portfolio in Moroccan dirham.

This is in sharp contrast with the high growth rate of 66 percent per year witnessed during 2003–2007.

<sup>13</sup> CGAP research based on credit information from the five largest MFIs.

The fourth priority is to improve the regulatory framework. The Ministry of Finance has launched a survey with funding from the Millennium Challenge Corporation to assess the strengths and weaknesses of the sector and to provide recommendations to improve the regulatory framework for microfinance. The study also will look at the transformation of some of the largest institutions into commercial, prudentially regulated, entities. The results of the survey

should be available in the second quarter of 2010; it will be discussed with FNAM and the industry in the second half of 2010.

These measures are helping to restore confidence in the sector; they are also building the foundation for a more solid and mature microfinance industry that is capable of providing affordable financial services to millions of poor families in Morocco.

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