

What is Securitization?

“Pooling a group of assets, such as loans, and selling securities backed by these assets”

An increasing number of MFIs are paying more attention to developing commercial sources of funding to finance their growth. In addition to mobilising deposits and accessing debt and equity, MFIs can use securitization to access capital markets, improve liquidity and lend more money. Securitization allows the selling MFI to receive instant cash while earning income through administration of the securitized loan portfolio.

Securitization offers MFIs a number of advantages:

1.	Ability to raise finance at low cost	4.	Access to capital markets
2.	Diversification of funding sources	5.	Access to liquidity
3.	Partial or total removal of assets from balance sheet	6.	Foreign exchange and interest rate risk hedging

Securitization of microfinance loans is gaining momentum across the industry, with Grameen, ICICI Bank, and JP Morgan pioneering the way. Some examples include:

- In 2004, ICICI Bank (one of the largest commercial banks in India) paid \$4.2 million for a portfolio of 42,500 loans from Share Microfin Ltd., a leading Indian MFI. This deal was facilitated by a collateral deposit of \$325,000 made available by the Grameen Foundation-USA. The securitization enabled Share Microfin Ltd. to obtain funds at a cost that was 3-4% cheaper than it would have paid for a bank loan.
- Opportunity banks in Russia and Albania have been selected to participate in the recent Blue Orchard Global Securitization of \$106 million for 22 MFIs around the world (a bond offered by Morgan Stanley). While the end-point client will pay interest rates of between 15%-35% on a loan of around £100-£200, investors in the bond will be repaid at an annual interest rate of 6.17%.
- Opportunity entered into the first securitization deal made by a microfinance Network. In 2006, it completed something called a “multi-seller collateralized debt obligation” (CDO) transaction with the European Investment Fund. This CDO was issued for Opportunity MFIs in Eastern Europe. The transaction pools loans granted to Opportunity MFIs in an aggregate amount of up to 28 million Euros.

Securitization demonstrates that traditional financial institutions can be active players in the industry on a commercial basis. Some sources estimate that the sector could ultimately generate \$10 billion in annual volume. However, despite the rapid growth of securitization, its acceptance by the capital markets will probably be a gradual process. This is because only the most mature, professional MFIs are capital-markets material (i.e. they are a good credit risk).

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