

Essentials of Microfinance

YOUR GUIDE TO APPROACHING A MICROFINANCE INSTITUTION



Purpose of this booklet

Microfinance institutions (MFIs) are financial institutions whose purpose is to offer financial services to people that usually do not have access to formal financial institutions, such as banks. This booklet was developed for you to learn more about microfinance in Kosovo. It aims at providing you with a basic understanding of the topic and shall serve as a guideline when approaching an MFI for its services.

In this booklet you will learn:

- What MFIs are and how they operate;
- How using the services of MFIs can benefit you and your family;
- Which products are offered and how to choose those that are most suitable for your needs;
- How MFIs grant loans and what to keep in mind when applying for a loan;
- Which risks and difficulties might occur and should be kept in mind when taking a loan.

In addition, the booklet will:

- Explain what interest rates are and how to calculate different kinds of interest;
- Provide you with a glossary of useful banking terms;
- Explain to you how to calculate your household budget.

This booklet will not provide you with answers to all your questions, but it will help you to become better informed and prepared to approach an institution to apply for a microfinance loan. While we recommend taking some time to read the full booklet, the content is divided into clearly structured sections, which allows you to quickly find the topics you are interested in. Make sure to have the booklet at hand when approaching an MFI.

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1. What is Microfinance?

People with low income often find themselves in a situation where they need access to financial services to improve their quality of life. Usually, those clients only require small-scale financial services, such as microloans to start or further develop their business or improve their housing. Banks often refrain from serving those clients, as they assume that costs for small loans are relatively high and low-income people cannot offer any collateral, i.e. securities that ensure the payment of a loan obligation.

MFIs are organizations that offer financial services to low-income people. Those products can comprise a full range of banking services, including microcredit as well as savings and insurance products or money transfer facilities. An MFI operates like a small bank with the social mission of serving the people that otherwise might not have access to financial services. In Kosovo, the basic purpose of MFIs is to grant loans to different clients, including the rural population, micro and small entrepreneurs, women entrepreneurs, minorities and low income households.

In the near future MFIs are expected to transform into deposit taking institutions, enabling them to offer you additional financial services such as savings products.

MFIs vary in their organizational set up, size, as well as scope of products and services. They differ from banks mostly in their target group orientation and their approach to serve those clients. Usually, MFIs borrow money from banks and other mainstream financial institutions to on-lend those funds to their clients.

There is a number of MFIs in Kosovo which have a proven track record of serving the target group, which are operationally and financially self-sustainable and cover most regions in Kosovo.

2. What are the benefits of microfinance?

Microfinance has the overall objective to foster a deeper and more inclusive financial system by offering financial services to low-income households and micro entrepreneurs. Ultimately microfinance contributes to poverty reduction and economic growth. Microfinance thereby contributes to improvements in the quality of life for individuals and families.

You can benefit from access to microfinance services, as this will help you to:

Develop opportunities – Financing opportunities will offer you a chance to create or expand your own business and to buy assets such as land or housing. Setting up a business is an opportunity to generate income, which leads to an improved quality of life for you and your family.

Manage life-cycle events – Once-in-a-lifetime occurrences such as births, marriages and deaths or periodic incidents such as school fees for children require access to financial services.

Overcome emergencies – Natural disasters like floods, fires and storms as well as personal crisis such as illnesses and injuries lead to a sudden need for financial means.

Promote gender equality and empowerment – The ability to use financial services and to earn income enhances women's capabilities and enables them to address existing gender inequalities. Greater access to finance for women can help to improved children's health and education.

3. Which services do MFIs offer?

At present, MFIs in Kosovo offer different sorts of loan products to their clients. However, in order to increase the range of financial services for the benefit of its clients, MFIs in Kosovo are in the process of transforming into deposit-taking institutions, enabling them to offer you additional products and services such as savings products as well as transfer and payment services.

A loan is money you borrow from a financial institution, which is to be repaid based on a contractual agreement at a later date. Usually, a price has to be paid for the money borrowed, which is called interest. Legally, a loan is a contract between a buyer (the borrower) and the seller (the lender). The terms and conditions for the repayment of the loan, including the interest rate charged, are specified in the loan agreement, which is concluded between the borrower and the lender.

Loans are obtained for different purposes. MFIs therefore offer different loan products that are characterized through differences in amounts, maturities, and repayment terms. In addition, the features of products for the same purpose might differ between different institutions. It is therefore important that you inform yourself well on the different products which are offered by different MFIs. It is of utmost importance to find out which product is best to serve your needs.

4. Which lending methodologies do MFIs apply and which loan products do they offer?

Financial institutions employ two general lending methodologies: group and individual lending. The two methodologies mostly differ in terms of client selection, the loan application and approval process, product design, repayment monitoring, and delinquency management. Loans are either provided to you through individual or group lending, depending on the design of the specific loan product:

- **Individual lending** - Loans are granted to individuals who provide the MFI with an assurance of repayment in the form of traditional collateral or alternative means of managing credit risk. Individual lending relies on an detailed assessment of the client's financial and economic information. In addition, loan decisions are individually tailored based on the specific needs of the applicant.
- **Group lending** – Groups of borrowers are involved in granting and recovering loans. While loans are usually granted to individuals, the group forms a guarantee mechanism, reducing risks and costs associated with providing small loans to low-income persons who lack traditional collateral.

The following descriptions are provided to you to better understand different types of loans offered by MFIs. However, please keep in mind that the loan conditions and terms vary between MFIs. You should therefore inform yourself well to make the best decision on the product that fulfills your needs.

Rural Loan

If you are a farmer, there are so called Rural Loans or Agriculture and Livestock Loans you might consider. With this loan for productive purposes, you can increase your production capacity, e.g. by purchasing machinery, or by ensuring the access to inputs for agricultural activity. Individual – as well as group loans are available to further develop your farming activities.



Business Loan

If you are a businessman or a young entrepreneur, a loan can help you to expand or set up your own business. Every new or growing business needs capital, either for the accession of equipment (fixed asset) or the purchase of materials and inputs (working capital).



Home (Improvement)/Housing Loan

If you want to buy or renovate your house or apartment, special home (improvement)/housing loans are offered. Investments in housing help you to improve the current living conditions for you and your family. Renovations such as improvements in insulation can furthermore help you to bring down costs for utilities and help to protect the environment.



Loan for Women

Many MFIs offer loans which are especially designed for women entrepreneurs. If you are a woman, such a loan can help you creating or further developing your business.

Consumer Loan

If you intend to buy a new stove or washing machine, a consumer loan can help you to address your personal needs. To be granted a consumer loan, you need to have a bank account and a regular income that is transferred to this account.

5. How do you choose the right institution?

It is important for you as a customer to understand which MFI can best serve your specific needs. Prior to choosing the right MFI, you need to understand the institution's approach to doing business, its product range and its capability of offering such products and services in the long-term. The points below provide you with a guideline of what to keep in mind when choosing your MFI.

Terms and conditions

A customer can choose the right institution based on the loan conditions offered, for example the price (interest and other fees), the loan amount offered, repayment conditions etc. While the interest rate is a decisive factor, you should be suspicious of unrealistically low rates, as in those cases there will often be some additional hidden costs. In addition, the speed of the institution's services is crucial. The loan approval process should be quick and efficient. However, a responsible MFI needs some time to process all the information received from you, in order to avoid a situation in which you might not be able to repay the loan after a certain period. As variable loan terms, installments and fee structures make comparison tricky, you should take your time to carefully check the conditions and responsible finance practices (such as their transparency in disclosing lending terms and conditions) of different MFIs before deciding which one to go for.

Transparency

A responsible MFI should be open to explaining the rationale behind its policies and conditions and take care of the adequate disclosure of lending terms and conditions. An MFI should be fully transparent to clients with regard to the loan conditions such as interest rates and all fees that apply to your loan. A responsible finance institution should always strive to make its services as understandable to you as possible and should responsibly handle consumer complaints. For example, your MFI should offer you the possibility to anonymously file a complaint i.e. you should find complaint boxes in the branches of the MFI you have approached.

Reputation

If you know anyone who has taken a loan from an MFI such as your friends, colleagues or relatives, ask for their opinion and their experiences with the respective institution. Ask if their services are reliable and professional. One of the best ways to find out which institution to choose is by looking at their reputation and credibility with their existing borrowers and the community.



Friendliness

Friendliness is more than just being nice to a client. It means to understand the customer and his/her questions, being patient and being ready to assist the customer whenever questions come up. Therefore, make sure that your contact person at the institution is available for your needs and questions and that he/she provides you with all information that is needed to apply for a loan. Also keep in mind that you have the option to change your loan officer, in case you do not feel comfortable with the provided services.

Proximity

Depending on your needs and habits, i.e. whether you visit the bank frequently or only on an occasional basis, a good option is to choose an MFI near your home or business. Physical accessibility makes it easier for you to visit the MFIs whenever there is a need. The advantage of considering proximity in your decision for the right institution is that it lowers your transactions costs, i.e. direct and indirect costs of the loan arising for you through transportation and the time spend for travelling.

6. How do you approach an MFI for a loan?

Based on the recommendations in the previous chapter, you should always compare the offers of several MFIs. The first thing that you need to do, before applying for a loan, is to think about the right product. If you have chosen an MFI that offers a product that best suits your

needs and the institution can provide a level of quality you are satisfied with, the next steps will help you in approaching the selected institution.

If you are applying for a **business loan** or other similar loans, usually, the following steps will apply:

Create a business plan

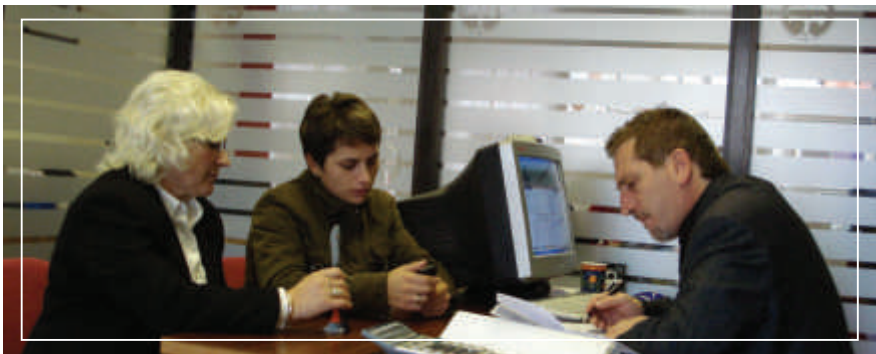
- To approach an MFI for a loan to start or expand a business, you need to provide a business plan to your loan officer. A business plan is a well written plan that explains in detail the goals of a (new) business and the plan for reaching those goals. This includes the strategic orientation, management goals, the business environment and market to be tackled, as well as the financial goals (financial projections) during a certain period. This plan will also explain how you will use the loan you are applying for. It is very important that your business plan is well thought through and that you have thought about how you will repay the borrowed funds.

Approach the MFI

- Make a visit to the MFI and find out who the responsible person is that provides information and handles loan applications.
- Once you have talked to that person, he/she will help you to make an appointment with the loan officer who is assigned to you.

Meet with the loan officer

- If the MFI wants to disburse a loan in a responsible manner, they will need to have detailed information about you. It is therefore very important that you are adequately prepared for



the interview. During your meeting with the loan officer, you need to be honest, and you should not provide false information. It is important for you to critically analyse your financial situation together with the loan officer to avoid situations in which you might later on not be able to serve your loan obligations.

Visit of loan officer

- The loan officer will pay a visit to your business premises shortly after the application was filled out. During the visit, the loan officer will get an impression of whether the loan can serve the indicated purpose and if the business is run on a sustainable basis. It will help the loan officer to verify the information provided in the application and to gain a greater insight into the operations of your business.

Loan approval

- Usually, you should receive the MFI's decision whether the loan is approved within 2 weeks.

If you are applying for a **home improvement** or **consumer loan** (or other similar loans), usually, the following steps will apply:

Approach the MFI

- Make a visit to the MFI and find out who the responsible person is that provides information and handles loan applications.
- Once you have talked to that person, he/she will help you to make an appointment with the loan officer who is assigned to you.

Meet with the loan officer

- If the MFI wants to disburse a loan in a responsible manner, they will need to have detailed information about you. During your meeting with the loan officer, you need to be honest, and you should not provide false information. Describe your current situation and explain the reason for applying for a loan. Provide some background information about yourself and your current financial situation.

Start the application process

- After the first interview, additional questions might be raised by the loan officer. Once they are clarified and you are in principle deemed eligible for a loan, you will fill out the loan application form and submit it to the loan officer together with the

required documents (such as a copy of your ID-card, a salary statement etc.). The MFI will then process the information provided.

Visit of loan officer (home improvement loan)

In case of a housing/home improvement loan, the loan officer will pay a visit to your property shortly after the interview to verify the information provided and to get an impression of whether the loan can serve the indicated purpose, i.e. if renovations are required.

Loan approval

- Usually, you should receive the MFI's decision whether the loan is approved within 2 weeks.

7. How does the loan approval process work?

There are a lot of steps between your application for a loan and the actual disbursement of funds. This chapter provides you with an overview of the different steps, which may slightly vary from one institution to the other.

Step one: **Personal meeting**

- A personal discussion with the credit or loan officer is the first step of the loan application process. He/she will ask various questions related to your personal background, the purpose of your loan, your current financial situation and your work and possibly business experience. In addition, the loan officer will ask you questions to find out more about your credit history, your repayment capacity and if you already have other loans. At this stage, it is very important that you know and clearly express the reason for approaching the MFI. The loan officer will then help you to decide which loan product is best for you.

Step two: **Loan application**

- Once you have decided which loan you are applying for, you will fill out the application form provided to you by the MFI. You will be asked to fill in your personal information such as contact details, current job etc. These questions will depend on the type of loan you are applying for. It is very important that you fill in accurate information.



Step three: **Provision of proper documentation and visit of loan officer**

- Providing proper documentation is a very critical and important step for obtaining a loan (see Chapter 6). Ask your loan officer which documentation has to be submitted together with your loan application form. Once the application form was filled out, the loan officer will visit your business to verify the information provided, to analyze your business and to get an impression of whether the loan will serve its purpose.

Step four: **Loan processing**

- At this stage, the MFI will decide whether you are eligible for the loan that you have applied for, by looking at your application and the documents that you have provided. First of all, the data you provided is entered into the MFI's electronic system, which is set up for this purpose. The institution will analyse the information and run a thorough check of you creditworthiness. Depending on the loan amount, the decision on your loan application may be taken by several persons or even a credit committee. After the completion of the process, the loan will be approved or denied.

Step five: **Contract Signing**

- Once you were informed that the loan is approved, you will be requested to sign a loan contract. This document will explain the loan terms and conditions. Before signing the agreement, carefully read the contract and make sure that you have fully understood the information it contains. If you still have any questions, ask your loan officer for help.

Step five: **Contract Signing**

- Once you were informed that the loan is approved, you will be requested to sign a loan contract. This document will explain the loan terms and conditions. Before signing the agreement, carefully read the contract and make sure that you have fully understood the information it contains. If you still have any questions, ask your loan officer for help.

Step six: **Loan disbursement**

- Once all the formalities are completed, the MFI will disburse the borrowed amount to you in cash.

Step seven: **Loan repayment**

- After the loan amount was disbursed, make sure that the loan is repaid as stipulated in the loan contract. Interest, other costs and the principal are usually paid at regularly scheduled intervals, i.e. monthly installments.

8. What documents do you need to provide when applying for a loan?

Every loan application requires you to present specific documents to the MFI. The documentation required depends on the particular institution and loan product you are interested in. In principle, you should be prepared to provide the following documents to your loan officer:

ID Card: An ID card is your personal identification card that is issued to you in Kosovo.

Passport: A photocopy of your passport will help the institution identify who you are.

Work certificate: A work certificate or work contract is issued by your employer and states what position you have in a company, your contract term and your salary.

Bank statement: A bank statement is a detailed record of your account. It summarizes all your financial transactions over a certain period of time on your deposit account, your credit card or any other type of account you hold at a financial institution.

Salary statement: A salary statement is a letter provided by your employer which provides detailed information on your salary, i.e. how much you earn, how frequently you are paid, etc.

Business certificate: A business registration certificate is a written statement issued by the Register of Companies that confirms a company's registration number and if it is a company that has fulfilled the necessary legal requirements.

Collateral documents: This document is a legal document which covers the item(s) pledged for a loan as security, i.e. a car, a mortgage and other assets.

	ID Card	Passport	Work Certificate	Bank Statement	Salary Statement	Business Certificate	Collateral Documents
Rural Loan	X		X	X		X	X
Business Loan	X	X	X			X	X
Home Loan	X		X	X	X		
Consumer Loan	X		X	X	X		X
Loan for Women	X					X	
Handcraft Loan	X						

9. What are the risks related to a microfinance loan?

While taking a loan offers a lot of benefits and opportunities, such as starting or expanding a business, buying or renovating your house and helping you to manage times of crisis or emergencies, there are also some risks involved when borrowing money.

In case you have taken a loan there are several risks affecting your business, i.e. your income source, that you should be aware of.

- Economic crises can greatly affect business activities, directly and indirectly.
- Unstable markets that affect the demand and supply for goods will affect the sales of your business.
- Any natural disaster, such as floods, fires and storms will have an impact on the agricultural sector which might affect your business.
- An instable political situation can affect your business. It can also have an impact on the MFI's ability to offer you their services.

You should therefore keep in mind that

- Taking a loan requires a lot of responsibility, as you are the one who is fully responsible to repay the borrowed amount. If you have a clear idea how to use and repay the borrowed funds, it will show your MFI that you know how to manage credit.

- A loan is always provided to you at a certain cost (such as interest and fees). While taking a loan provides you with more income at the point when the loan is disbursed, it means that you have less money to spend in the future, as you have to repay the loan amount in regular installments. A loan will have an impact on your business or household budget every month.
- A loan may tempt you to spend more money than you can afford. You might be more tempted to buy things that you could otherwise not afford and which you do not really need.
- In case you will not manage to pay off your loan, the MFI has the right to sell the asset you pledged as collateral or the guarantor will have to compensate the lender. In this case, you also run the risk of being classified as bad debtor at the Credit Registry of Kosovo, which will make it more difficult for you to take a loan in the future.
- In case you will not be able to serve your loan obligations, you might be tempted to approach another MFI for a second loan that seems to help you to serve your loan obligations. Be aware that this can lead to your over-indebtedness, aggravating your situation.

10. How to deal with loan risks and repayment difficulties?

Difficulties in serving a loan is something that no one wants to face. Late and missing payments can hurt your credit score and can expose you to additional costs, like increased interest rates and late payment fees. Also, when the MFIs find out that you are having trouble to pay your bills, they may not grant you a new loan in the future.

Here are some useful tips that will help you to prevent loan difficulties:

For borrowers of business- and other loans:

- ✓ Educate yourself well about microfinance loans, read and consult with competent people.
- ✓ Borrow money to use it for productive activities, so that the return ensures the repayment of the loan.
- ✓ Use the borrowed money for the approved purpose only.
Know your market and continuously respond to market demands and make adjustment (e.g. adapt your marketing strategies).

- ✓ Understand basic principles of money and asset management, including basic practical accounting topics. Analyse and monitor your cash flow on a regular basis.
- ✓ Maintain business sustainability and ensure that your business flourishes.

For borrowers of consumer- and other loans:

- ✓ Borrow only when there is a need and not only a want.
- ✓ Borrow according to your financial capacity to repay the loan.
- ✓ Take one loan at a time and do not take multiple loans.
- ✓ Control your expenses and manage your budget well.

In case you have problems with the loan repayment, make sure that you:

- ✓ Call your loan officer and talk to him/her directly to find a solution. Everyone can, for different reasons, get into financial difficulties at some point. If your MFI is a responsible partner, they will try to help you with your difficulties or even arrange an adjusted repayment schedule.



11. How to calculate interest rates

There are several ways to calculate interest on a loan. This chapter will explain to you in a simple manner how interest is calculated and will teach you more about the two most common methods applied: the declining balance- and the flat method. In addition, calculating the effective interest rate will help you to better understand the real costs of you loan.

Below are examples for calculating interest according to the different methods. However, please consider asking your loan officer to explain to you in more detail how to calculate the respective interest rates.

Flat interest

This method calculates interest as a percentage of the initial loan amount, i.e. that interest is always calculated as a percentage on the total amount of the loan initially disbursed. Usually, the interest rate is indicated as an annual rate. To calculate your interest rate payments you need to know the amount borrowed, i.e. the principal (P), the nominal interest rate (R), and the duration or time (T) for which the loan amount is borrowed.

Interest = Principal x rate of interest x loan term or

$$I = P \times R \times T$$

Example 1:

You are borrowing EUR 1,000 from your MFI, at an annual nominal interest rate of 10%. The loan term is two years with monthly loan installments to be paid.

You would then calculate your monthly installments as follows:

$$P = 1,000.00 \text{ (principal)}$$

$$R = 10\% \text{ (interest rate)}$$

$$T = 2 \text{ years (time)}$$

Step one: Calculate the total amount of interest that has to be paid by multiplying the loan principal with the interest rate and by the loan term (in years).

$$\text{EUR } 1,000 \times 0.10 \times 2 = \text{EUR } 200$$

In this case, you have to pay a total of EUR 200 of interest for a loan amount of EUR 1,000, taken for a period of two years.

Step two: Add the amount of interest and the loan principal to calculate how much money you owe the MFI.

$$\text{EUR } 1,000 + \text{EUR } 200 = \text{EUR } 1,200$$

Step three: To calculate your monthly installments to the MFI, convert the loan term into months by multiplying the number of years by twelve.

$$2 \text{ years} \times 12 \text{ months} = 24 \text{ months}$$

Step four: Divide the total amount to be repaid to the MFI by the number of months to calculate your monthly loan installments.

$$\text{EUR } 1,200 / 24 \text{ months} = \text{EUR } 50 / \text{month}$$

Under the given assumptions (10% annual interest rate), you will have to pay back the loan (EUR 1,000) at a monthly rate of EUR 50 for a period of two years.

Declining interest

The declining balance method is used by most financial institutions. This method calculates interest as a percentage of the outstanding amount over the loan term, i.e. interest is only calculated on the amount that the borrower still owes and is characterised through the following:

- Loan installments remain the same for each installment during the loan term. However, the ratio between the payment of interest and the principal changes.
- The principal, repaid in regular intervals, declines with every installment. As interest is always calculated based on the outstanding amount, interest payments decrease with each installment, i.e. that a greater share of the monthly interest payment is paid.
- As installments remain constant during the loan term and interest payments decrease, the repayment of the principal increases.

To calculate interest on the declining balance requires a more complex calculation. You should therefore approach your loan officer for advice. Make sure to find out whether interest is calculated on the flat or declining balance method. With all variables remaining the same, the amount of interest paid on a declining basis is lower than interest calculated on a flat basis.

Effective interest rate

In addition to charging interest, many MFIs charge fees or so called service charges when disbursing a loan. Those fees or charges increase the total costs of your loan. The effective interest is usually indicated as an annual rate and reveals the true costs of borrowing e.g. including loan insurance costs, costs for processing the loan application etc.

The effective interest rate is the most important rate, as it reveals the true costs of a loan. You should therefore always compare effective interest rates of loans offered by different MFIs. When talking to your loan officer, always make sure that he provides you with a detailed calculation of the effective interest of the loan you would like to apply for.

12. In a nutshell: when dealing with an MFI, always make sure that you . . .



Inform yourself

- You are responsible for informing yourself about MFIs and their services and products. Get informed by reading and talking to the MFI staff, such as the loan officer and other competent people.

Seek information

- Seek information from friends or relatives who already have taken a loan from an MFI. You may find out that those people will give you a basic understanding and examples of their current or past experiences with taking a loan. From this, you will learn which sort of loan you need and where to get it from.

Understand MFIs and their products

- Make sure that you understand the policies of the financial institutions, particular the lending terms and conditions. Ensure that you understand the full costs (see Chapter 11) of the loan you intend to apply for.
- If you do not understand those, ask questions, and the MFI will gladly help you with your needs. Also, get to know the market, inform yourself about different MFIs and their offers.

Ask yourself questions

Ask yourself questions before you apply for a loan such as:

- What is the purpose of loan and where do I want to invest in?
- Does my current financial situation allow me to borrow money?
- Will I be able to repay the loan on time?
- Have I taken all necessary risks/possible events taken into account?

If you know the answers to these questions and you have talked to your loan officer, than it can be expected that you will positively gain from the loan.

Analyze your financial situation

- Analyze the cash flow (income and expense) of your current or future business. Develop a business plan that proofs realistic financial planning for the next 5 years. Develop clear goals where you see yourself and your business in 5 years.

Also, always keep in mind

- Not to take loans from different MFIs at the same time.
- Make your payments on time.
- Never borrow more money than you can afford to pay back.

Glossary of banking terms

You have most likely seen advertising campaigns that stress different interest rates, repayment terms, fees and guarantees, but maybe you do not exactly know the meaning of such terms. Below are a few important terms that you need to understand when applying for a loan.

- **Assets**

An asset is anything owned by a person or organization that has a value. For example, an asset may be a specific property or an enforceable claim against others.

- **Bad Debt**

Bad debt is debt that is not collectible and for that reason does not have any value to the creditor. Those loans are past due in terms of loan installments to be paid. For you as a debtor, this bad debt creates an unhealthy financial situation.

- **Collateral**

Collateral is an asset pledged as security to ensure the repayment of a loan. The collateral serves as a protection for the lender against the borrower's risk of default. If the borrower defaults, the asset pledge may be taken and sold by the lender to fulfill the completion of the original contract.

- **Debt**

Debt is the amount owed for the funds borrowed. This debt is owed to the MFI from which the loan is retrieved.

- **Due Date**

Every principal balance of a loan will have to be paid back on a certain due date. This date is usually at the end of the loan term. You have to make sure that there sufficient time fixed in the loan contract so that you meet your payment obligations.

- **Fees**

A fee is a charge for a service performed. The MFI usually charges fees like processing fees, applications fees, and transactions fees. When you are checking your loan agreement prior to signing, make sure that you pay attention to any additional fees which are charged by the MFI.

- **Guarantor**

MFIs often ask for a guarantor, who is a person who guarantees the payment of another person. This is a way through which the lender assures that the loan will be repaid. The guarantor assumes liability in the event of default and takes the risk that his/her assets will be used for the repayment of the loan.

- **Interest rates**

Interest is the price that you pay for the temporary use of borrowed funds, expressed as a percentage rate for the period of time in use, usually an annual rate. In addition to the loan amount (principal), you will pay interest. It is important that you thoroughly understand what interest rates are used because it can greatly affect the amount that you owe the MFI.

- **Loan Agreement**

A loan agreement is a written contract entered into between the lender (MFI) and the borrower that regulates the terms of a loan. The agreement stipulates the rights and obligations of both parties. For example, the contract will include the loan amount, the due date, as well as interest rates and fees. This sometimes lengthy document contains all details about your loan and should be read carefully. The loan enters into force once it is signed by all contracting parties.

- **Prepayment**

A prepayment is when you pay off your loan before maturity, i.e. earlier than the due date. When taking a loan, carefully check the loan agreement for any prepayment penalties that might be incur. Prepayment penalties are fees that have to be paid to the lender for the privilege of paying off a loan prior to maturity.

- **Repayment Terms/Repayment Schedule**

Repayment terms are the conditions that you have agreed to by signing the loan agreement. Those terms can include the time that you have to repay your debt obligations, the minimum payment that has to be made within a certain period, or the penalties levied for late payments.

- **Terms of Default**

The terms of default define the conditions and consequences of a loan default, i.e. when you have failed to meet your contractual obligations, such as the repayment of the loan. Those terms are stipulated in your loan agreement and should be carefully read, especially if the loan was granted against any collateral.

How to prepare a household budget?

Before you decide to apply for a loan, you should carefully analyse your financial situation. In order to manage your household funds well, you should compare your monthly (household) income with your expenses. You should only apply for a loan if your income exceeds your expenses and if the remaining balance is sufficient to cover monthly loan repayments. If you are considering taking a loan necessary to solve a short-term financial crisis, keep in mind that a loan is always an additional expense. In addition, be aware that your monthly loan installments should never exceed 1/3 of your monthly salary.

The preparation of a household budget can help you to keep track of your finances during a specific period of time and can serve as a tool to better compare income and expenses. A well calculated budget will help you to make sure that you know your current and future financial capacity.

The attached template will help you to calculate your household budget. It also enables you to compare planned with actual figures, providing you with an indication of you have realistically planned your budget.

To determine your household budget, just follow these simple steps:

- Document your expected income (“budget amount”) and record your actual monthly income (“actual amount”) for each item under the category “income”;
- Document your expected expenses (“budget amount”) and record all of your actual monthly expenses (“actual amount”) for each item under the category “expenses”;
- At the end of the month, calculate the balance (“difference”) for each item. Comparing your planned and actual costs will give you an indication whether you have realistically planned the amounts received or spend for a particular item. It will enable you to analyse the flow of your funds.
- Compare the difference between your “total income” and “total expenses”. It will give you an indication if you should consider taking a loan from an MFI.
- Adjust your budget on a monthly basis to reflect changes in income and expenses.

Please keep in mind that:

- You should always try to save some money, as this will help you to manage unexpected situations and emergencies.
- In case you conclude that you are spending more money than you should, you should think about options to lower some of your expenses. You should try to find the right balance between consumption (voluntary expenses), fixed expenses and saving. In the long run your monthly income has to cover your monthly expenses.

	Budget Amount	Actual Amount	Difference
INCOME (per month)			
Wages/ Salary	_____	_____	_____
Bonuses/Vacation Payments	_____	_____	_____
Other Income	_____	_____	_____
Total Income	_____	_____	_____
(Calculate these expenses per month.)			
HOUSING:			
Mortgage or rent	_____	_____	_____
Utilities (Water/Electricity)	_____	_____	_____
Telephone	_____	_____	_____
Cell phone & internet	_____	_____	_____
Cable & Satellite	_____	_____	_____
House repairs/maintenance	_____	_____	_____
Others	_____	_____	_____
INSURANCES:			
Health insurance	_____	_____	_____
Pension payments	_____	_____	_____
Others	_____	_____	_____
LOAN OBLIGATIONS (if applicable):			
Loan installments	_____	_____	_____
Credit card installments	_____	_____	_____
Others	_____	_____	_____
SAVINGS (if applicable):			
Monthly savings (such as a savings plan)	_____	_____	_____
VEHICLE/TRANSPORTATION:			
Repairs/maintenance	_____	_____	_____
Fuel	_____	_____	_____
Public transportation (e.g. bus or train)	_____	_____	_____

FOOD

Groceries _____
Meals out _____

CLOTHING EXPENSES

Purchasing _____

FAMILY EXPENSES

Expenses for children _____
Others _____

PERSONAL EXPENSES

Presents _____
Hairdresser _____
Other personal expenses _____

MEDICAL

Dental _____
Pharmaceutical products _____
Check-ups _____

ENTERTAINMENT

Sports & recreation _____
Hobbies _____
Vacations _____

Total Income: _____

Total Expenses: _____

Income After* Expenses: _____

**Only if your income after expenses is high enough to cover your loan installment, you should consider taking a loan. If this income is negative or not sufficient to cover those costs, you are not eligible for a loan.*



AMIK is the Association of Microfinance Institutions of Kosovo. Its mission is to facilitate sustainable economic development and job creation by supporting the microfinance sector in Kosovo. AMIK supports the development of strong and effective Kosovo-based microenterprise programs to assist underserved entrepreneurs in starting, stabilizing, and expanding businesses.

AMIK Member Microfinance Institutions providing access to financial products and services for low income entrepreneurs mainly living in rural areas are: Agency for Finance in Kosovo , Beselidhja/Zavet Microfinance, FINCA-Kosovo, Kosovo Enterprise Program, Kosovo Grameen Mission Arcobaleno Micro Credit Fund, Kreditimi Rural i Kosoves, KosInvest, START and QELIM.

AMIK Key function areas are: Advocacy and Policy, Best Practices of Microfinance and Coordination of activities for the purpose of developing microfinance sector.

Advocacy and Policy –Advocacy is a key function of AMIK. Under its advocacy mandate, AMIK promotes an awareness of and a commitment to best practices among donors, government bodies and microfinance practitioners in Kosovo. Under AMIK, MFIs have a platform from which they can speak with one voice. **Best Practices** – AMIK facilitates the exchange of best practices with a particular emphasis on encouraging financial transparency among its members. **Coordination** – AMIK coordinates activities such as joint trainings, exchange visits between other established MFIs in the Region, and other activities as requested by the member institutions.

AMIK Activities:

Trainings for the development of microfinance sector supported by EFSE Development Facility in 2008/09 and World Bank in 2009/2010

Supported by:



The European Fund for Southeast Europe (EFSE) was established in Luxemburg on December 15, 2005 as an investment fund with the aim to foster economic development and prosperity in the region of Southeast Europe. EFSE offers long-term funding instruments to qualified local financial institutions for on-lending to micro and small enterprises as well as private households with limited access to financial services. As the successor to the European Fund for Kosovo, EFSE currently cooperates with six financial institutions in Kosovo. EFSE is one of the first three microfinance investment funds worldwide which were awarded the prestigious microfinance investment label “LuxFlag” on February 1, 2007.

Moreover, the EFSE Development Facility, the Fund’s trust fund, offers complementary, non-financial services in support of EFSE’s financial investments, including technical assistance, consulting and training. In this regard, EFSE supports initiatives promoting responsibility in rendering financial services, such as this educational brochure.



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