Photo: Sean Hawkey Photography

Performance Report

Q1 2016

rootcapital

OVERVIEW

Through the first quarter of 2016, Root Capital reached a total of 246 agricultural enterprises,[1] providing higher incomes and stable employment for more than 535,000 farmers and artisans in Africa, Asia, and Latin America. At the same time, market challenges reported in previous quarters, and discussed in detail below, persisted through Q1, and we — along with our peers — continued to experience lower credit demand as well as elevated portfolio risk.

Many of the challenges we face are felt, often to a much larger extent, by our clients. Difficult market conditions — whether fueled by shifting buyer patterns, price volatility, adverse weather, or a combination of all three — carry significant and layered impacts for agricultural businesses and the farmers they serve. When a business is unable to maintain or fulfill buyer contracts, for example, farmers are not able to make sales and are often forced to explore difficult alternatives, like migration, to make ends meet.

As we have done in the past, we continue to put our clients front and center, investing in their continued resilience. Readers will remember that in 2013, as our coffee clients in Latin America were grappling with the coffee leaf rust blight, we launched the Coffee Farmer Resilience Initiative. We are pleased to report that two weeks after the close of Q1 2016, during this year's Specialty Coffee Association of America (SCAA) Expo, the Coffee Quality Institute recognized Root Capital and our founder and CEO Willy Foote with its 2016 Leadership Medal of Merit, in large part to honor Root Capital's work through that initiative. This report, published in Q1, explores how the Coffee Farmer Resilience Initiative has mobilized a blend of capital from leading coffee companies, donors, and impact investors to help nearly 850 coffee farmers renovate more than 1,600 hectares of land. While these numbers are still small relative to total need, it is our hope that the report sets forth a compelling blueprint that encourages financing for farm renovation at scale.

Portfolio Performance and Impact

The 246 enterprises we reached in Q1 2016 connected more than 535,000 small-scale producers to local, regional, and global markets. These clients are on track to generate $1.1 billion in revenue this year, about $900 million of which will be paid directly to producers.

Notably, more than 43 percent of the clients we served in Q1 2016 were considered gender inclusive per Root Capital's definition (see Terms and Acronyms on page 4). Through our lending to all clients, we reached 206,000 women through the first quarter of the year, a 5 percent year-over-year increase.

Yet as we celebrate the significant reach and impact of our lending during the first part of 2016, we continue to face significant challenges.

[1] *Starting in Q1 2016, "clients reached" includes the total number of clients with an outstanding balance at any point in the quarter. Previously, only clients with current loans were included as reached in that quarter.*

In previous quarters, we have explained how volatile commodity prices, depreciating currencies, and the effects of a changing climate have negatively affected portfolio size and quality and have also elevated provisioning expenses. In Q1, each of those three factors continued to impact our portfolio and, as industry sources have indicated, the portfolios of other agricultural lenders and commodity financiers around the world. In the first quarter of 2016, with this challenging lending environment as our backdrop, Root Capital experienced both lower credit demand and higher credit risk.

Specifically, adverse coffee market dynamics in the following two regions affected our clients' credit needs and contributed to a 5 percent year-over-year decrease in Root Capital's average outstanding portfolio balance ($108.5 million in Q1 2016 compared to $114.3 million in Q1 2015) and a 24 percent decrease in disbursements ($34.0 million in Q1 2016 compared to $44.5 million in Q1 2015):

- **Central America**: After the 2015 season, during which some major coffee buyers were "long" (overprojected and subsequently overbought), many farmer cooperatives and other coffee enterprises in the region struggled to secure purchase contracts for this year's harvest. These changes resulted in a lower-than-expected demand in credit from our Central American clients this harvest, which primarily occurs in Q1. Industry intelligence, however, indicates that key buyers plan to resume normal purchasing patterns by next harvest season.

- **East Africa**: Credit demand in East Africa was also below expectations, as the coffee harvest in Rwanda, originally projected for Q1, was significantly delayed. Our loan officers and Rwandan clients cited this delay as yet another disturbing indicator of reduced predictability for farming communities.

In Q1 2016, loans to coffee businesses made up slightly more than half (52 percent) of Root Capital's average outstanding balance. Following coffee, cashew and cocoa were our next largest industries, respectively comprising 7 percent and 6 percent of the quarter's average outstanding balance.

Collectively, loans to clients classified in all "other agriculture" industries, such as cocoa, nuts, seeds, and dried beans, made up 40 percent of Root Capital's Q1 average outstanding balance. During the quarter, for example, Root Capital closed five loans to macadamia businesses in Kenya, one of which was to a private enterprise called PAEM Nuts. The company, which employs around 120 seasonal employees, will use a $500,000 trade credit loan to purchase the harvests of 500 macadamia farmers — 60 percent of whom are women. Loans to clients classified in "non-agriculture" industries like handicrafts and textiles accounted for 8 percent of the Q1 average outstanding balance.

Portfolio Quality

In Q1, Root Capital downgraded loans totaling $3.9 million to three non-coffee clients, the primary driver of a quarter-end Portfolio-at-Risk (PAR) greater than 90 days of 9.5 percent. The total outstanding balance in PAR over 90 days was $10.1 million, compared with $5.7 million in Q4 2015 and $5.4 million during the same period last year.

More than half of the loans in PAR over 90 days in Q1 were undergoing a restructuring, a process that is often complex and lengthy, and there is no guarantee that each restructure will be successful. In light of the persistently challenging lending environment and these larger-than-expected losses, we are beginning to implement lower lending limits and we continue to incorporate lessons learned from such lending experiences into our credit standards and risk management practices.

Advisory Services

Root Capital clients are operating on the front lines of many massive challenges — from shifting buying patterns to volatile commodity prices to climate change. Given these factors, investing in our clients' capacity and resilience is more important than ever. As such, we have redoubled our efforts to provide our clients with enhanced technical assistance, including financial management training, agronomic planning, and mobile technology interventions that strengthen management and operations, lowering risk and setting up their businesses, and the farm families they serve, for success.

Notably, the first quarter of 2016 was the biggest opening quarter ever for our Advisory Services team: the program delivered 366 days of training to 96 groups in 12 countries. This represents an 8 percent increase over training days delivered in Q1 2015, in large part due to efforts to begin training earlier in the year in Mexico and Central America. In West Africa, where our clients have been faced with challenges like terrorism and political and health crises, we launched a very promising partnership with Partners in Food Solutions (PFS) to deliver food science consulting to our processing clients on topics such as food safety, processing equipment selection, system design, nutritional enhancement, and packaging.

Q1 2016 DASHBOARD

Metric	Result	Full Year Target (unless otherwise noted)	Results as % of Target
Social and Environmental Metrics			
Number of Producers Reached	663K	760K	87%
Producers supplying business	536K	601K	89%
Producers buying inputs	128K	159K	80%
Purchases from Producers	$909M	$1050M	87%
Total Revenue of businesses	$1.1B	$1.3B	87%
Sustainable Hectares under Management	615K	669K	92%
Lending Program			
Loan Disbursements	$34.0M	$137.9M	25%
Average Outstanding Portfolio Balance [1]	$108.5M	$104.8M	104%
Average Outstanding Balance per Active Loan	$377K	$397K	95%
Number of Clients Reached [2]	246	323	76%
Clients Reached, Current	191	247	77%
Portfolio-at-Risk Over 90 Days *	9.5%	< 7.0%	
Net Write-off Ratio *	4.3%	< 6.0%	
Advisory Services			
Number of Businesses Served	96	277	35%
Days of Training Delivered	366	2107	17%
Operating Results			
Total Operating Expense	$3.4M	$15.8M	21%
Debt to Equity Ratio*	4.00	< 5.00	
Capital Utilization *	91%	90%	101%

[1] Average Outstanding Balance Target is a quarterly target.
[2] Starting in Q1 2016 "Clients Reached" includes the total number of clients with an outstanding balance at any point in the quarter. Previously, only clients with current loans were included as reached in that quarter.
** Figures represent performance on last day of quarter.*

Terms and Acronyms

Clients Reached: We report "clients reached" to capture the number of businesses reached by our capital. Clients reached are those that had an outstanding balance at any point in the quarter, including clients that did not receive a disbursement in the quarter. This is a cumulative metric; clients are added to the annual total in the quarter in which they are first reached.

Gender-Inclusive Clients: By Root Capital's definition, a gender-inclusive business either has a supplier and nonmanagerial employee base composed of 30 percent women or more, or is made up of 20 percent women or more and has a woman leader.

Net Write-off Ratio: A trailing 12-month figure representing the previous 12 months' write-offs, net of recovered funds, as a percentage of the average outstanding balance during the same period.

Debt to Equity: Notes payable and other debt, divided by lending net assets. Our calculation treats long-term subordinated debt as equity, reflecting its equity-like characteristics.

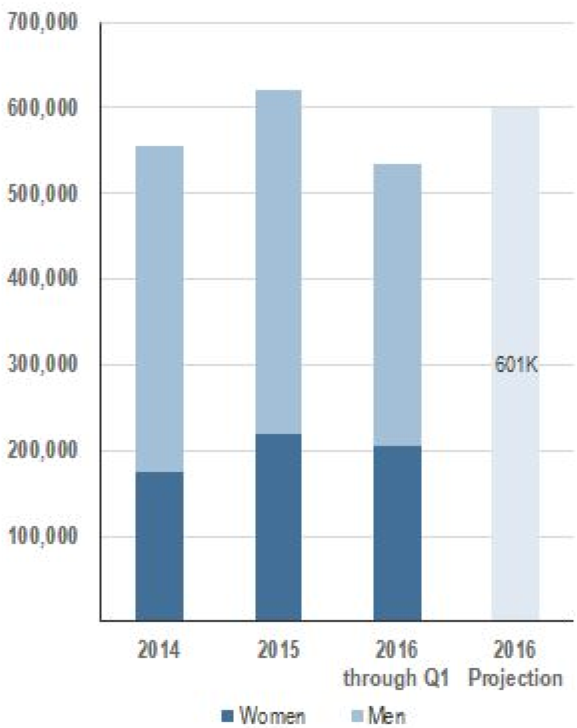
Capital Utilization: Capital utilization measures the proportion of available capital that is deployed in our lending portfolio at a point in time, calculated as: (Gross loans outstanding) / (Notes payable + lending net assets).

Region Acronyms: MAC (Meso America & Caribbean), SAM (South America), EAF (East Africa), WAF (West Africa), ASI (Asia [currently Indonesia only]).

PORTFOLIO PERFORMANCE

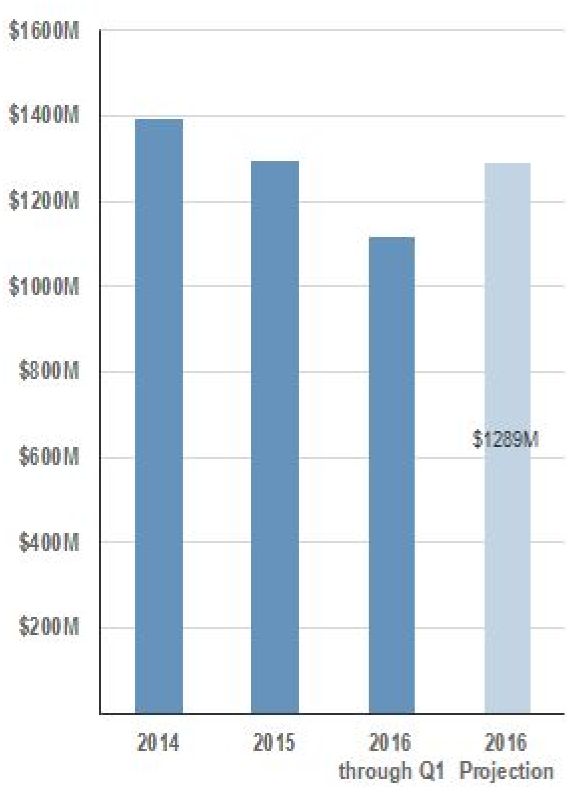
Social and Environmental Metrics

Producers Supplying Business

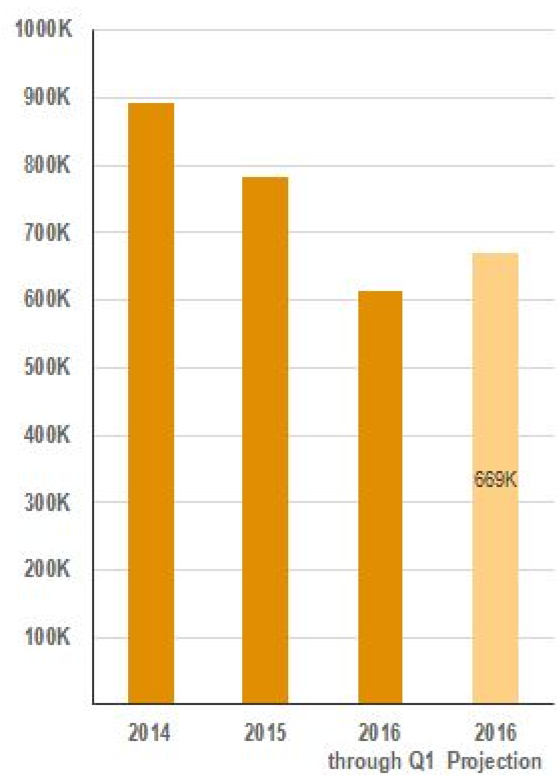


Purchases from Producers

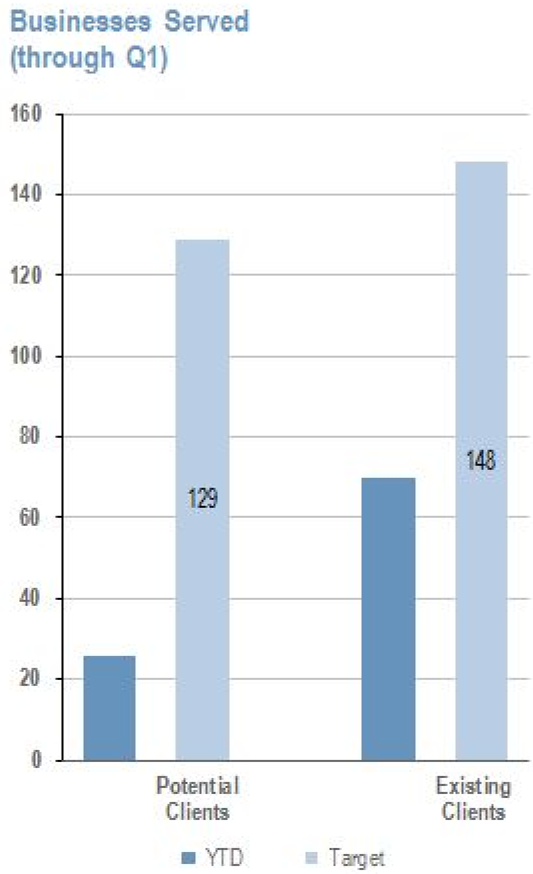
Total Revenue of Businesses

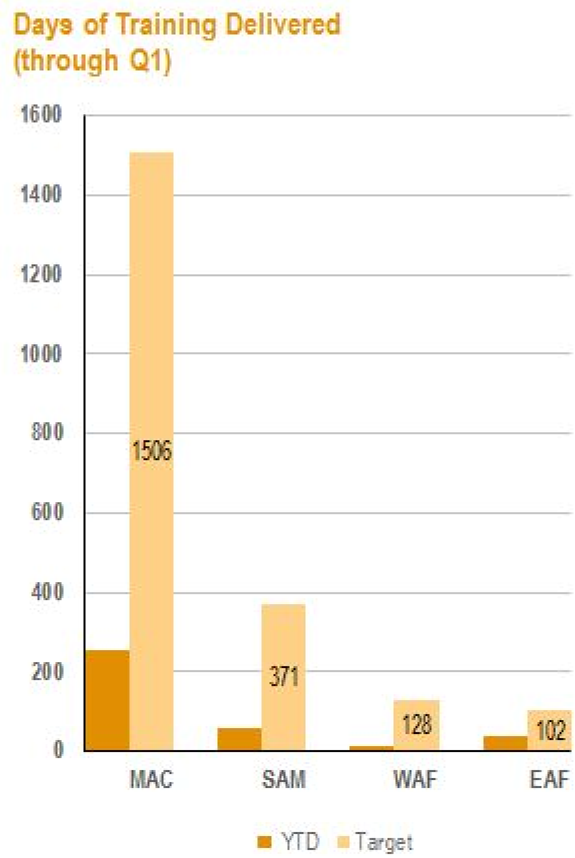


Sustainable Hectares Under Management

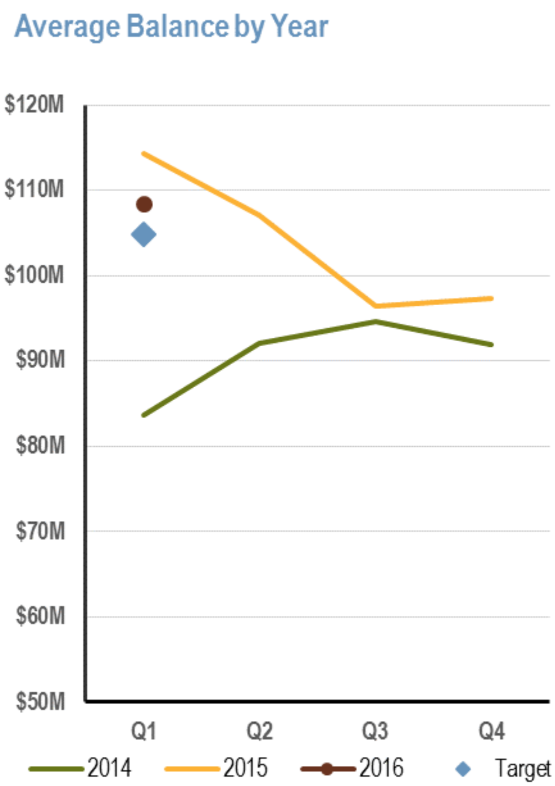


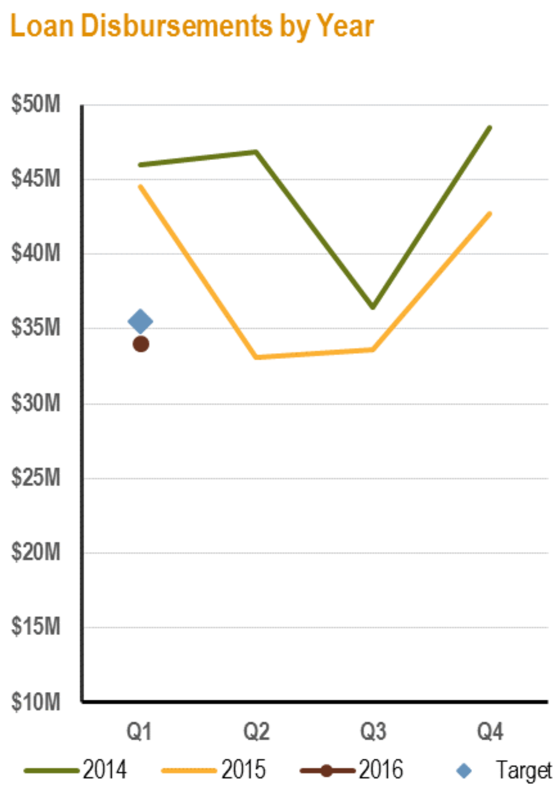
Advisory Services



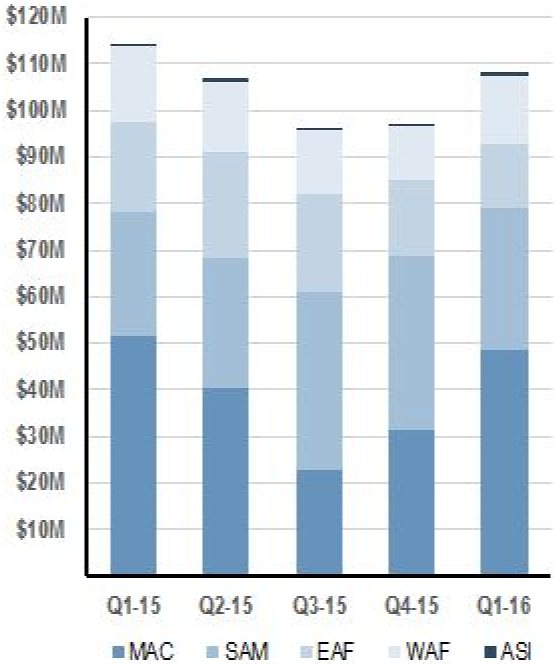


Lending Performance

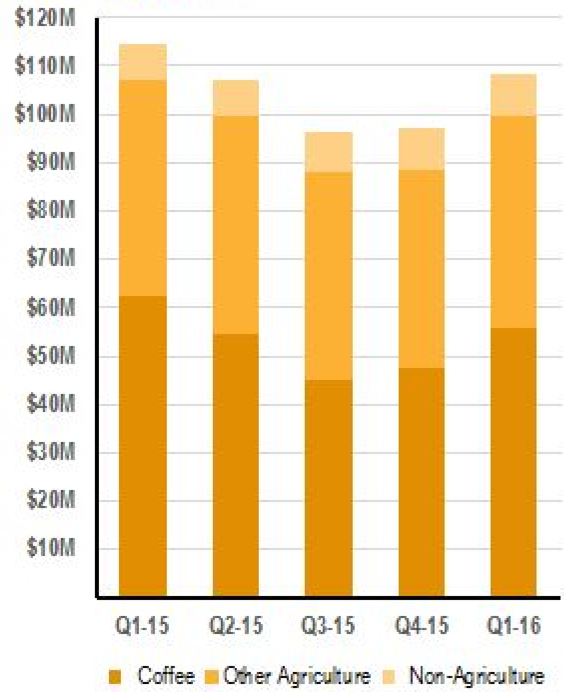




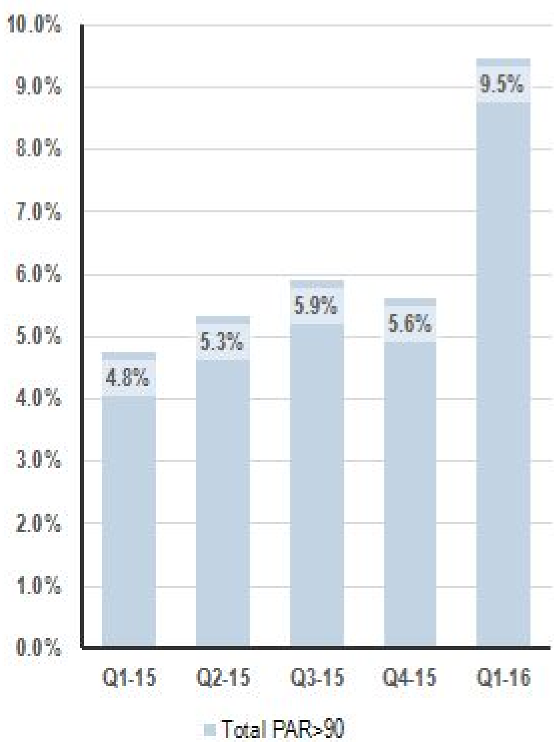
Average Balance by Region (Trailing 5-Quarters)



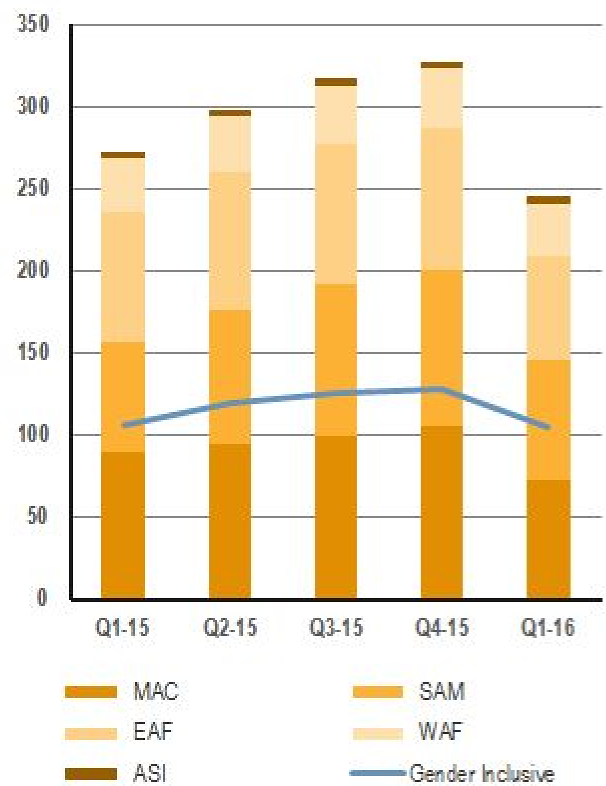
Average Balance by Industry (Trailing 5-Quarter)



Portfolio at Risk > 90 Days



Number of Clients Reached by Region



FINANCIAL RESULTS

Balance Sheet

Balance Sheet Highlights All numbers in thousands	03/31/16 Actual	03/31/15 Results	Yr/Yr Growth
Cash and Short-Term Investments	27,779	24,400	14%
Total Loans Receivable	106,474	112,815	-6%
Less: Allowance for Credit Losses	(6,720)	(4,785)	40%
Loans Receivable (net)	99,754	108,030	-8%
Grants Receivable	3,499	8,736	-60%
Other Assets	5,825	6,882	-15%
Total Assets	**136,858**	**148,048**	**-8%**
Senior Debt	102,416	111,261	-8%
Subordinated Debt	6,700	900	644%
Other Liabilities	4,298	4,851	-11%
Total Liabilities	**113,414**	**117,011**	**-3%**
Lending Net Assets & Op Reserve	19,612	24,372	-20%
T/R Net Assets (Purpose & Time)*	3,833	6,665	-43%
Total Net Assets	**23,445**	**31,037**	**-24%**
Total Liabilities & Net Assets	**136,858**	**148,048**	**-8%**

Key Financial Ratios	03/31/16 Actual	03/31/15 Results	Yr/Yr Growth
Debt-to-Equity Ratio**	4.0	4.4	-41 bps
Capital Utilization	91%	94%	-3% pts

** $4.1M of conditional grants are excluded from the T/R Net Assets, as required by US GAAP. These grant conditions will be met after Q1 2016, which will allow us to add these grants to the T/R Net Assets.*

*** Debt-to-equity treats long-term subordinated debt ($6.2M) as equity, reflecting its equity-like characteristics.*

Balance Sheet Growth

Assets declined by 8 percent year-over-year. The period-ending loan portfolio balance declined by 6 percent year-over-year due to lower-than-expected disbursements during the Central America coffee harvest season and delayed disbursements to Rwanda's coffee sector resulting from a later-than-expected harvest. Assets were further reduced by a 40 percent year-over-year increase in the allowance for loan losses, reflecting elevated credit risk in the loan portfolio.

Financial Leverage

During Q4 2015, the Investor Relations team successfully secured covenant modifications with major investors to include subordinated debt as part of the equity calculation (i.e., alongside grant-funded net assets) in debt-to-equity ratio calculations, more accurately reflecting the equity-like nature of our long-term subordinated debt. By this measure, our debt to equity stood at 4.0x at quarter-end, flat with Q4 2015 and down from 4.4x at March 31, 2015.

Outstanding Debt and Capital Utilization

We ended the quarter with $109 million in debt under management and finished the quarter with a 91 percent capital utilization rate, slightly below the 94 percent rate we reported at year-end 2015. We typically manage to a 90 percent capital utilization rate, allowing us to effectively manage liquidity and volatility in our lending portfolios.

Temporarily Restricted Net Assets

Temporarily restricted net assets contracted $0.7M since Q4 2015, and declined $6.6M year-over-year as operating deficits eroded our net asset balance, outpacing our ability to release contingent net assets onto the balance sheet. Note that balance sheet net assets understate our funding as we hold $5M of contingent net assets off the balance sheet. At the end of March 2016, our “grant net asset” balance, the sum of on-balance-sheet temporarily restricted net assets and off-balance-sheet contingent net assets, equalled $8.8M.

Statement of Activities

In thousands of USD	Consolidated Statement of Activities		
	2016 YTD Results	2015 YTD	Yr/Yr Growth
Loan Interest and Fees	2,560	3,231	-21%
Gain (loss) on FX Lending	(183)	(606)	-70%
Interest & Fee Revenue	**2,377**	**2,625**	**-9%**
Net Interest Expense	651	648	1%
Net Interest & Fee Revenue	**1,725**	**1,977**	**-13%**
Provisioning Expense	2,275	1,825	25%
Net Revenue after Provisioning	**(549)**	**152**	**-462%**
Operating Expenses	3,382	3,420	-1%
Contributions for Operations	2,106	3,317	-37%
Other Income	164	18	816%
Operating Surplus / (Deficit)	**(1,662)**	**66**	**N/A**

Loan Interest and Fee Revenue

Loan Interest and Fee Revenue fell by 9 percent year-over-year as low coffee prices and reduced demand led to weaker-than-expected coffee harvest season lending in Central America and a later-than-expected coffee harvest in Rwanda.

Funding Costs

Interest expense was 6 percent above plan for the first quarter of 2016 as we maintained excess available credit to fund the Central America coffee harvest.

Net Provisioning Expense

First-quarter 2016 net provisioning expense of $2.3M exceeded the target by 14 percent due to independent, client-specific issues adversely affecting our borrowers’ ability to service their debt. Three large non-coffee loans drove two-thirds of the provisioning expense as they were downgraded due to client-specific factors, including weaker-than-expected financial management and debt servicing challenges related to localized drought.

Operating Expense

Quarter-end total operating expenses were 10 percent lower than target, due primary to lower-than-forecast personnel expenses. Professional services and discretionary travel expenses remain tightly controlled to reduce overall operating expenses during this period of heightened credit risk.

Contributions for Operations

Q1 recognized $2.1M in contribution revenue. Root Capital is currently shifting to a broader cohort of contribution funders, as previous multiyear grants come to a close and new multiyear grants begin. During this transition period, contribution revenue remains lean, but future outlook is healthy. During Q1, for example, we approved for $6.4M in new multiyear grants, which will close in Q2 (and will therefore be reflected in the next Quarterly Performance Report).

For additional information, please go to www.rootcapital.org or email info@rootcapital.org.