

# MicroNed - Ethiopia Microfinance Country Strategy, 2008 - 2010

## 1. Introduction

MicroNed is the microfinance network established in 2006 by the four Dutch development organisations Cordaid, Hivos, ICCO and Oxfam Novib. In 2008 Rabobank Foundation joined MicroNed. The motivation to establish this network was triggered by the need to co-operate on a structural basis with respect to the establishment of a specialised sector approach for microfinance. This network is geared towards providing support to starting and emerging microfinance institutions (MFIs) and creating an enabling microfinance environment.

Ethiopia is one of the countries that were identified by MicroNed as focus countries to enhance the structural collaboration. At the moment four MicroNed Members namely, Oxfam Novib, ICCO/Terrafina, Cordaid and Rabobank Foundation provide direct financial support microfinance activities in Ethiopia. The first step towards fostering this collaboration was to undertake a country scan to serve as the base for current and future strategy. Consequently, a baseline survey was commissioned in 2006 leading to the publication of the *Ethiopia Country Scan* in 2007.

One of the key conclusions of the country scan indicates that the Ethiopian microfinance industry is young but quite dynamic and expanding rapidly. On the other hand the local support sector is quite small and less structured to sustain the balance between supply and demand. Donor agencies have a good track record of providing funds for service delivery. However, most of their efforts are on piecemeal, uncoordinated and in most cases confined to individual MFIs. Recently, donor coordination increased in the context of working towards a national microfinance strategy.

In view of the above scenario, the MicroNed members Cordaid, ICCO/Terrafina, Oxfam Novib and Rabobank Foundation have chosen to define a joint microfinance strategy in certain areas in an attempt to increase the value of their support towards enhancing the Ethiopian MFI industry. This document summarises the strategic choices of their microfinance policy for Ethiopia covering the period 2008 – 2010.

## 2. Overview – Microfinance Sector

### Regulated MFIs

The Ethiopian microfinance industry is rapidly coming to maturity. As per the end of the year 2007, the 26 operational MFIs serviced 1.7 million Borrowing clients with an aggregate portfolio of ETH Birr 2.2 Billion (EUR 180,000,000)<sup>1</sup>. Most MFIs are doing remarkably well in terms of financial performance given their relatively short track record. The largest have passed the threshold of financial self-sufficiency (FSS) and the vast majority has moved beyond the operational self-sufficiency (OSS) mark.

The Ethiopia mainstream microfinance industry operates under a regulated environment that was effected in 1996 through issuance of proclamation 40/96. This legislation authorises the National Bank of Ethiopia to register, licence, regulate and supervise MFIs. MFIs are expected to register as limited share companies.

The enactment of the MFI legislation has lead to transformation of the traditional NGO microcredit programmes into full fledged autonomous Microfinance institutions including SFPI, Buussa Gonofa, PEACE, ESHET, Wasasa etc. In such cases the principal shareholder of the concerned MFIs are their mother NGOs. In addition, most regional governments stimulated

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<sup>1</sup> Data obtained from AEMFI's MFI Performance analysis report, Bulletin nr. 4, dated March 2008

establishment of new MFIs or co-invested in existing ones that were previously aligned to NGOs such as ACSI, DECSI, OMO and OCSCO.

The biggest challenges of the Ethiopian MFI sector at the moment are a lack of adequate whole sale funding possibilities (including guarantee facility), weak governance and management capacities to further develop MFIs into more mature institutions with diversified products and the overall availability of local BDS services for clients. MIS systems, Social Performance Management, gender mainstreaming and product innovation are still underdeveloped.

The initial capital investment was obtained mainly from donor capital and/or regional governments. Experiences in the recent past shows that most donor agencies involved in wholesale lending have reached their ceiling. The Rural Financial Intermediation Programme (RUFIP) facility has provided some relief but is not expected to bridge the funding gap in the long run. Funds for wholesale lending under this facility are approximately one-third of the volume of the industry’s outstanding portfolio at EUR 147 million as per year-end 2005. Very few MFIs have access to commercial lending sources. This coupled by the tremendous growth in loan portfolios compared to the marginal corresponding growth in savings, the biggest challenge experienced by the Ethiopian MFI sector at the moment is lack of loan funding.

### **Saving & credit cooperatives**

Savings and credit organizations form a second type of organizations providing financial services to poor also in rural areas in Ethiopia. Traditionally there where no specific savings and credit cooperatives in Ethiopia and this is reflected in the table below.

| <b>TABLE 7: NUMBER OF SAVINGS AND CREDIT CO-OPERATIVES PER JUNE 2006</b> |        |            |                     |
|--------------------------------------------------------------------------|--------|------------|---------------------|
| Type                                                                     | Number | Membership | Average member size |
| Overall cooperatives                                                     | 20.406 | 4.642.034  | 227                 |
| Savings and credit                                                       | 5.437  | 381.312    | 70                  |
| Rural SACCO’s                                                            | 1.166  | 64.655     | ???                 |

The first legal framework for cooperatives was enacted in 1960 through the Farm Workers Cooperative Decree which was followed by a more comprehensive legal framework for the development of cooperative societies in 1966. At the moment, the co-operative sector is governed by provisions enacted through Proclamation No. 147/98.

Unlike other formal financial institutions (banks and micro finance institutions), saving and credit cooperatives are owned, controlled and capitalized by their members. This implies that the savings and credit cooperatives are not subjected to supervision and regulation of the Nationals bank of Ethiopia. The ministry of co-operatives is responsible for the coordination of their activities.

One of the weaknesses reflected in the co-operative sector is poor administrative and financial management. On the other hand the government through the relevant ministry is not adequately equipped to monitor and control the cooperative movement. Recently the discussions around the legal framework for savings and credit cooperatives have started as well as discussions on the role of the central bank in supervising the financial cooperatives. The priority support for this sector is to enhance its coordination, create a central database, institute a national federation which is related to the microfinance network and facilitate appropriate monitoring, review and control.

## **The microfinance support sector**

Ethiopia's microfinance support sector is relatively small. There is a very limited number of support institutions like credit bureaus, consultancy firms, rating agencies, specialised auditors, training institutions, microfinance programs in universities and organisations specialised in wholesale funding and guarantees, and their expertise in microfinance is limited or not existing at all.

The Association of Ethiopian Microfinance Institutions (AEMFI) is the network of all registered microfinance Institutions (MFIs) in Ethiopia. AEMFI's has three main objectives. *First and foremost* is to provide a forum and structure through which MFIs can share their experiences and exchange information. *Secondly*, it strives to enhance the capacity of the member MFIs through offering training and negotiation for alternative funding resources from both local and international sources. *Finally*, it seeks to strengthen the entire MFI sector development through undertaking research, advocacy, promotion of the industry, engage dialogue with the government and other relevant international institutions with the view to positively influence MFI policy and practises.

Building on the successful networking within the mainstream MFI sector, AEMFI has expanded its scope of work to incorporate the co-operative sector as well.

AEMFI is one of the best working microfinance networks in Africa but has limited means and capabilities to address all the needs of the sector.

### **3. Intervention Strategies and action plans**

With respect to the needs of the Ethiopian microfinance sector on the one hand and the goals, focus and capabilities of the MicroNed members on the other hand, microNed's interventions will be directed at:

1. Increased outreach and improved performance of MFIs and S&C cooperatives by supporting individual MFIs and S&C cooperatives;
2. Increased product innovation and strengthened local product development capacities;
3. Increased attention for Social Performance Management (SPM) and strengthened local SPM support capacities;
4. Enhance Gender Mainstreaming in Microfinance services
5. A more diversified support sector, including strengthening network and encouraging development of BDS providers for Micro-finance.
6. Improved regulation and supervision for MFIs and S&C Cooperatives

#### **3.1 Increased outreach by supporting individual MFIs and S&C cooperatives**

The last decade has seen the Ethiopian microfinance industry grow rapidly towards maturity. Despite all this significant gains, the general outreach is still very low estimated at 20-25% of the demand with most of the underserved areas being felt in the rural areas. Besides the general disparity between the rural and urban areas, there are no formal microfinance services in three administrative regions i.e. Afar, Somali and Gambella regional states, which are characterised by pastoralist engagements. There is no single licensed MFI operating in any of these three regions.

Increased outreach will be realised through financing existing MFIs to expand their programmes by replicating their current financial services in areas that are not served yet or, in case where there are significant difficulties to expand existing programmes such as in the three deficient regions, facilitate the establishment of new MFIs.

Most of the MFIs that are supported not only receive loan or grant funding for portfolio growth (increased outreach) but also grant funding for capacity building in order to enhance the MFIs performance. Capacity building grants are normally adapted to the needs of each MFI and included in their Business Plans. For capacity building in certain areas, activities are directed at several MFIs at the same time, either through collaboration with AEMFI or through programmes that include different MFIs, like for product innovation and SPM (see below).

Detailed plans:

*Oxfam Novib (ON).* ON will support three MFIs (PEACE, ESHET and DECSI) through a mix of both grant (EUR 450,000) and loan funding (EUR 1.1 million) to enable the three MFIs expand their outreach by roughly 35,000 additional clients.

In addition to financing the specific MFIs, Oxfam Novib in collaboration with AEMFI has commissioned a research study to explore possibilities of introducing microfinance services to the currently non-MFI served and pastoralist dominated areas of Afar, Somali and Gambella regions. A clear investment strategy in this regard has not yet been developed. This will be work out in consultation with other interested stakeholders and potential investors.

*ICCO/ Terrafina:* Will support seven MFI's with a mixture of loans and guarantees to enable outreach to an additional 110.000 clients and will support 5 cooperative union structures to grow their clientele from 12.000 to 30000 in 2010. Furthermore Terrafina works together with CIDR to develop a special facility to reach out to rural areas.

*Cordaid:* will support one MFI (Wasasa) through a guarantee (EUR 500,000) and a grant (EUR 100,000). Cordaid is interested to explore possibilities of introducing microfinance services to pastoralists dominated areas together with other Microned members or potential investors. Cordaid is also interested to explore possibilities of reaching other vulnerable client groups or small agricultural producers.

### **3.2 Increased product innovation and strengthened local product development capacities;**

Both group and individual lending methodologies are commonly used. However, there is a high level of homogeneity between the financial products particularly savings and loans, offered by various MFIs despite de non-homogeneity among their clientele. There is need for adaptation of various products to suit different categories of clients.

Product innovation will be facilitated at both the national level through the AEMFI network and/or directly with the specific partners MFIs as deemed appropriate.

Through the joint financing support by Oxfam Novib and ICCO/Terrafina, AEMFI in collaboration with Microsave, Kenya recently undertook a baseline research study on potential financial product services for rural households in Ethiopia. Arising from this, new financial products are under development and are due for pilot testing with a selected group of MFIs during the year 2008. This will be followed by actual implementation of the new products in the following years.

Terrafina has started a product innovation initiative with 5 of its MFI partners in 2005. The MFI's are guided through a cycle of market research, product identification and design and pilot testing. The program will be evaluated towards the end of 2008.

### **3.3 Increased attention for SPM and strengthened local SPM support capacities;**

ICCO/Terrafina, in collaboration with Oxfam Novib and AEMFI will enhance implementation of the Social Performance Management (SPM) concept to the entire MFI sector in Ethiopia. Building on previous, albeit not well developed experiences with individual MFIs, a

comprehensive tool will be developed in the course of the year 2008 and tested with a selected group of MFI's after which this framework will be availed to the entire sector in following years. This process will entail the following steps;

- a) Developing a social performance strategy: clarify social goals, set clear performance objectives, identify strategies to reach the objectives and set targets
- b) Monitoring and assessing social performance; and
- c) Using social performance information for management purposes.

### **3.4 Gender Mainstreaming in Microfinance**

Oxfam Novib, in collaboration with AEMFI, will undertake a needs assessment including a comprehensive baseline study to get an overview of the current status of all the AEMFI members concerning gender aspects. It will also include an in-depth study of any existing gender innovations by AEMFI members. The needs assessment will focus on the following aspects:

- ◆ Review gender and development issues in Ethiopia (Background)
- ◆ Identify the causes of low female participation in financial services
- ◆ Assess the suitability of existing financial products and service delivery to potential and existing female clients
- ◆ Assess any other challenges facing women for improvement in gender inequality in livelihood and provide recommendations to address this situation
- ◆ Selecting and adapting the methodologies (which ones) to be used for the needs assessment
- ◆ Conduct the needs assessment, including baseline data and in-depth study of at least 6 different gender innovations
- ◆ Review gender policy and practices of AEMFI
- ◆ Design action plan to implement the selected recommendations of the study.

The baseline study will be undertaken towards the end of the year 2008. Thereafter, there will be a dissemination workshop to AEMFI members and possibly other stakeholders in the course of the year 2009. One of the main outcomes of the process will be the identification, development and implementation of specific action plans for the selected AEMFI members.

### **3.5 A more diversified meso level support sector**

Support to MFIs is almost limited to AEMFI which does not have the means and capabilities to satisfy all needs. A support sector with more and more diversified players would accelerate positive developments in the sector, allow AEMFI to focus more on a few, typically network activities and increase the possibilities for MFIs to choose the support they need and prefer.

### **3.6 Improved macro level environment**

The macro level microfinance environment includes regulation and supervision for MFIs and S&C Cooperatives, a government that plays the right role and a well informed general public. The Microfinance policy and regulation for MFIs in Ethiopia are rather well elaborated and appropriate. Certain elements however still need to be improved, like the MFIs' income and taxation policy. Furthermore it may occur, like examples in the past show that the government interferes directly in the microfinance sector in a non appropriate way. MicroNed will support lobby and advocacy activities of AEMFI or other relevant stakeholders, possibly in collaboration with other donors, in case of need.

#### **Annexes:**

#### **MicroNed members' Strategies for Ethiopia**






- I. Oxfam Novib;**
- II. Cordaid; and**
- III. Terrafina**

## **Oxfam Novib Microfinance Strategy for Ethiopia, 2007-2010.**

### **Objectives:**

Increase access to financial services through outreach expansion both geographically and in number of clients.

### **Strategies:**

- 1) Support existing MFIs to expand outreach through set up of financial delivery services in MFI deficient areas;
- 2) Sector support - Support the national Network in the following thematic areas;
  -  Product research and Development
  -  Research and development of financial services in pastoralist areas
  -  Lobby and Advocacy
  -  Gender mainstreaming in microfinance
  -  HIV/AIDS mainstreaming in microfinance
- 3) Geographic focus – Mainly rural agricultural sector
- 4) Product innovations through Linking & Learning – Explore intervention strategies for Remittances, Micro insurance and Social Performance Measurement.

### **Portfolio:**

- 1) ESHET MFI – Rural areas of Oromia region
- 2) PEACE MFI – Rural areas of Oromia and Amhara regions
- 3) DECSI MFI – Rural and urban areas of Tigray region
- 4) Association of Ethiopian Microfinance Institutions (AEMFI) Network - Ethiopia MFI sector support

### **Relevant Microned Themes**

- i) Rural Financial Services
- ii) Remittances
- iii) Social Performance Measurement and Impact
- iv) Micro Insurance

### **Budget**

- Loan funding – EUR 1.1 million
- Grant funding – EUR 750,000

## **Cordaid Microfinance Strategy for Ethiopia 2008-2010**

### **Objectives:**

To increase outreach and quality of financial services for informal sector workers and micro and small enterprises (MSEs). As the core of Cordaid's involvement in microfinance lies in reaching vulnerable groups of clients Cordaid prefers MFIs with a clear social mission as partners.

### **Strategies:**

1. Support established MFIs that want to serve geographically remote areas or new vulnerable client groups (people living with HIV/Aids, pastoralists, slum dwellers)
2. Support (pilots on) agricultural finance.
3. Where there are no financial service providers yet, Cordaid seeks to support young (start-up) and emerging MFIs through capacity building and initial funding, sometimes on the basis of seed capital.
4. MSE finance (missing middle). To finance investor vehicles that focus on an enhanced access to financial services for MSEs.

As Ethiopia hasn't been chosen as a focus country for Cordaid's microfinance programme (a country where she wants to contribute to the development of the microfinance sector on a national level), priorities lie on the 1<sup>st</sup> and 2<sup>nd</sup> strategy. There is limited grant funding available for Ethiopia.

### **Portfolio:**

Wasasa (loan and grant)

### **Relevant Microned Themes**

- v) Rural Financial Services
- vi) Social Performance Measurement and Impact
- vii) HIV/AIDS

### **Budget 2008**

- Loan funding – EUR 500,000
- Grant funding – EUR 100,000

## **Terrafina Microfinance Strategy for Ethiopia, 2007 - 2010**

### **Objective**

Main aim of the TERRAFINA program in Ethiopia is to deepen rural pro-poor financial services through financial and technical support. TERRAFINA wants to contribute towards pro-poor, inclusive and gender-sensitive economic development, build a rural profile and expertise and focus on institutional capacity building, rather than on mere funding.

### **Strategies:**

1. Support to 7 emerging and growing microfinance institutions, through seed capital funding, product development interventions and guarantees to facilitate loans from banks to MFI's Wasasa, Buusaa Gonofaa, AVFS, Eshet, SFPI, Metemamen and Harbu, as well as CIDR.
2. the development of Rusacco's. Rusacco's are fast growing service providers in rural Ethiopia and they often operate in areas where more formal MFI's not yet reach. This program is developed with Rabobank input.
3. The third area for strategic alliances is the collaboration of the MF and Sacco programs with the Fair economic development programs of ICCO. Aim of this program is to create long term sustainable impact on the livelihood of small producers by linking them to sustainable local and international markets.
4. Sector support in the area of institutional support with AEMFI and special support for SPM and learning on member based models for rural outreach in collaboration with AEMFI.

### **Portfolio:**

Wasasa, Busaa Gonofaa, AVFS, Eshet, SFPI, Metemamen, Harbu, 5 cooperative Unions, AEMFI, CIDR,

### **Budget:**

Annual grant budget: 750.000 flexible

Annual guarantee budget: flexible

### **Specific targets:**

- 9 MFI's will be supported with seed capital or project grant
- 4 MFI's will be facilitated with a guarantee agreement.
- Rusacco Unions will be supported with a seed capital grant
- 1 Network will be supported.
- 3 product innovation efforts will be supported: innovation fund, CIDR, and VC development with Harbu.
- Learning events on SPM, member based organizations and financial products in VC will be developed.
- Benefits on cross cutting issues (insurance for agriculture) with West Africa.