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Rural Finance Policy Development in Eastern and Southern African Countries: Contribution of IFAD-Supported Rural Finance Programmes

Annex 1. Country report for the Federal Republic of Ethiopia

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September 2014

Contents

Acknowledgements

The Rural Finance Knowledge Management Partnership (KMP) wishes to acknowledge the contributions of staff of IFAD and various stakeholders who facilitated and participated in the study. Sincere thanks go to Mr Saleh Usman Gashua, Secretary General, AFRACA, and Ms Miriam Cherogony, Rural Finance Specialist and Ms Risper Gekanana, Project Assistant, both of KMP for their coordination and logistics support. IFAD staff and field officers in the targeted Eastern and Southern Africa countries are acknowledged for participating and facilitating the study. In this regard, the contribution of the following officers is well appreciated: Mr Michael Moful Mbulo of Zambia, Dr Mwatima Juma and Mr Bernard M. Ulaya of Tanzania, Mr Colin Agabalinda and Mr Daniel Muganda of Uganda, and Dr Robson Mutandi and Mr Dagmawi Habte-Selassie of Ethiopia. We also thank the following for submitting the questionnaires virtually: Mr Augusto Isabel and Mr Narciso Manhenje of Mozambique, Mr David Myeni and Ms Prudence Mnisi of Swaziland, and Mr Sekoala Molapo and Ms Monehela Tau of Lesotho.

IFAD also wishes to extend sincere gratitude to all the implementing institutions / individuals who contributed to the study either in discussions during the period of study visits or by communicating their ideas and opinions; their inputs and information have given useful insights to the study. Finally, KMP is grateful to independent consultants Mr Biswa Bandhu Mohanty for conducting the study and compiling the draft report, and to Dr Vitalis Musewe for reviewing, editing and structuring it.

Chapter 1

Background to the study

In the backdrop of IFAD's effort to improve livelihoods by enhancing access to financial services among rural communities, the Rural Finance Knowledge Management Partnership (KMP) carried out a study to find out how IFAD-supported rural finance programmes contribute to policy development in the Eastern and Southern African region. The focus of the study was on countries with active rural finance programmes and components—Ethiopia, Kenya, Lesotho, Mozambique, Swaziland, Tanzania, Uganda and Zambia—where IFAD has been increasingly engaged in policy dialogue with a view to influencing policy. The IFAD programme also seeks to influence policy to minimize adverse effects of global trends and maximize incentives and opportunities for the rural poor. Apart from challenges in the area of rural infrastructure, capacity of financial service providers and clients, other factors such as legislative, regulatory, supervisory and overall policy constraints often stand in the way of delivery of need-based financial services in the rural area. IFAD has been supporting capacity building of policy-making bodies, development of appropriate decentralized policy and practices, evolving market-oriented research/studies and dissemination of learning.

Considering the critical importance of creating finance policies that are appropriate to rural settings, KMP proposed to undertake a region-wide *Study of Rural Finance Policy Development in the Eastern and Southern African (ESA) Countries—Contribution of IFAD-Supported Rural Finance Programmes,* and to determine the way forward to addressing the key constraint—insufficient skills in information technology and insufficient exposure to skills required for good information management—mentioned above. The study covered all the eight ESA countries where IFAD had been active. For the study, KMP identified a consultant, Biswa Bandhu Mohanty, on account of his expertise and wide experience in rural finance.

1.1 Purpose of the study

The study was undertaken with the following overall objective: To produce a KM document for use by the stakeholders of RF programmes being implemented by IFAD in the 8 selected ESA countries. The specific objectives of the study were to:

- Identify major policy issues in ESA countries which IFAD projects have enabled to sort out/address during the course of implementation in the countries;
- Bring out successful strategies adopted/institutional mechanism used to influence policy issues, leading to fulfilment of programme objectives;
- List out country-specific policy issues in ESA, which have regional and global implications/impact;

- Suggest sustainable institutional mechanisms that have to be put in place for policy exploration, research, debates and discussions for sharpening and furthering poverty reduction, access to financial inclusion, livelihood promotion and inclusive growth; and
- Suggest ways and means for enhancing knowledge management, sharing of experience/best policy solutions among the IFAD programme managers, partners and stakeholders for better programme implementation and speedier/effective policy development.

1.2 Target organizations for the study

In the 8 selected countries (Ethiopia, Kenya, Lesotho, Mozambique, Swaziland, Tanzania, Uganda and Zambia) the study targeted public and private institutions that have national responsibility for, as well as commercial interests in, rural development. They included Central Banks; Insurance Regulatory Authorities; Co-operative Regulatory Authorities; Ministries of the National Governments including Ministry of Finance (MOF), Ministry of Agriculture/Cooperatives (MOA); MF Associations, Co-operative Unions/ Alliances; Apex Development Banks; Policy Research Agencies; and leading Civic Society Organizations (NGOs, CBO, etc).

1.3 Data collection methods and tools

Three main methods or tools were used in gathering data. (i) The questionnaire shown in Appendix 1.1 was designed to solicit views/inputs from the concerned IFAD officers at the project level in all eight countries targeted for the study. (ii) Interviews and consultations were used through face-to-face meetings and by e-communication. The consultant visited the capital cities of five of the target countries from 23 June to 9 July 2014; they, included Lusaka (Zambia), Dar es Salaam (Tanzania), Kampala (Uganda), Addis Ababa (Ethiopia) and Nairobi (Kenya). The visits facilitated interviews and discussions with officials of the institutions targeted in those countries. During the short period of 2-3 days at each centre, 84 persons from these select institutions were consulted. The list of institutions visited and persons met and consulted through face-to-face interviews in Ethiopia is given in Appendix 1.2. (iii) Intensive literature survey was used to collect information at country / institutional as well as regional and global levels. Documents spelling out regional, national and institutional RF policies, strategies and programmes were studied. In the case of Ethiopia the list of documents consulted is given in Appendix 1.3**.**

1.4 About this report

This report focuses on the study findings with respect to RF development efforts, the contributions of IFAD RF programmes and the emerging policy issues and challenges and recommendations for addressing them for furtherance of rural finance policy in Ethiopia. Although presented as a standalone report, it is intended that this report be read alongside the main study report which addresses RF issues that prevail regionally and globally.

It is also envisioned that the reader will seek to benefit from the following Case Study Reports attached to the main report as appendices: MFI Supervision

Directorate (MFSD) of the National Bank of Ethiopia (Appendix 7), Association of Ethiopian MFIs (AEMFI) (Appendix 8), Micro Finance Forum in Uganda (Appendix 9) and Developing Rural Finance Policy and Strategy in Zambia (Appendix 10). For the sake of comparison and regional learning, the reader should also seek to benefit from *Country Reports* for other ESA countries which constitute an important output of this study. The full list Country Reports includes Federal Republic of Ethiopia (Annex 1), Republic of Kenya (Annex 2), Kingdom of Lesotho (Annex 3), Republic of Mozambique (Annex 4), Kingdom of Swaziland (Annex 5), United Republic of Tanzania (Annex 6), Republic of Uganda (Annex 7), and Republic of Zambia (Annex 8).

Chapter 2

Study findings

2.1 Rural finance policy initiatives and positive developments

2.1.1 *Overall socio-economic scenario*

Over the past two decades, the Government of Federal Republic of Ethiopia (GOE) has carried out far-reaching institutional policy reforms to transform/facilitate a stable market economy. Since 2007, Ethiopia has achieved strong economic growth, making it one of the highest performing economies in sub-Saharan Africa. Notwithstanding the efforts, the country remains one of the poorest in the region. For example, Ethiopia ranks 174th out of 198 countries on the UNDP HDI while its average per capita income is less than half of the current sub-Saharan average. The agriculture sector greatly influences the economy. It is also the primary source of income for more than 85% of country's population. The largest group of poor people in Ethiopia is composed of small scale farmers. About 12.7 million small holder farmers account for 95% of agricultural GDP. The incidence of poverty in rural areas is greater and poverty is more severe than in urban areas. Thus, rural financial services assume critical importance in the rural context.

The financial Sector in Ethiopia consists of formal financial institutions (commercial banks, MFIs and insurance companies), semi-formal institutions (credit unions and RUSACCOs) and informal sector (iddir, private money lenders, and traders). With its predominantly rural population, high level of poverty and agriculture-led economy pose challenges and opportunity to the financial sector of Ethiopia. As on 30 June 2014, the commercial banks (16 privately owned) had a network of 2176 branches, each serving a population of 39,949. The CBs' own 90% of total assets in the country. They have registered high profits as well as enhanced resources, capital levels and loans dispensation. However, 36% of the CB branches were located in Addis Ababa. There were 31 MFIs which were contributing significantly to the provision of loans and mobilizing of savings from the low income segment of the population. The top five largest MFIs (Amhara, Dedebit, Oromia, Omo and Addis credit and savings institutions) accounted for 84.8% of total capital, 93.1% of the savings, 89.3% of credit and 89.5% of the total assets of MF industry, signifying high concentration of sectoral capacity in the 5 top MFIs.

2.1.2 Initiatives in the financial sector

Supportive government legislations and regulations

On various dates the Government of Ethiopia issued comprehensive legislations affecting the financial sector; these were on banking business and on establishment of NBE (August 2008); Money-laundering and financial terrorism (December 2009); Insurance Business (August 2012); MF Business Proclamation (2009) that repealed the 1996 Act;, National Payment System Proclamation (July 2011); and amendments to Proclamation of 1998 on capital goods leasing business (July 2013). The NBE is the regulator for deposit-taking CBs, MFIs and Cooperative Banks as well as insurance companies. The Ministry of Finance and Economic Development (MOFED) in GOE plays a critical role in framing and finalizing various proclamations, in consultation with NBE.

A consultant was engaged by NBE for drafting micro insurance law and regulations. While Insurance business Proclamation was passed in 2013, no separate micro insurance law has been evolved.

Issue of directives by NBE (NBE regulations)

The NBE has issued a series of regulations for CBs, MFIs and insurance companies. The recent (January 2012) regulatory directives included relationship between financial institutions and agent banking services/technology service providers, regulation of mobile and agent banking services. In respect of MFIs, recent directives include Fit and Proper criteria, financial and operational information reporting (issued in 2012), investment and equities of allied activities (issued in 2013), minimum capital requirement of MFIs (for licensing and supervision of MFIs) (issued in 2013). NBE has been taking recourse to a very systematic, transparent and consultative approach in evolving and finalizing various regulations. The supervised institutions and industry associations are duly consulted in the policy and regulation-making process.

Improved supervisory arrangements for CBs, MFIs and insurance companies)

NBE has separate Directorates for supervision of CBs, MFIs and Insurance companies. It has introduced risk-based supervision for all supervised entities. NBE's Micro Finance Institutions Supervision Directorate (MFISD) has upgraded the supervisory tools and processes for improving quality and effectiveness of supervisions over MFIs. Bank has undertaken business process reengineering (BPR) for more effective service delivery. A case study on MFISD is given as Appendix 14 in main report of the study.

Expansion and growth of MFIs

The statute of 2009 has empowered MFIs with greater scope and opportunities for growth and diversification. MFIs are mandated to mobilize deposits, undertake micro-insurance business, lease finance, housing, etc. There is steady and appreciable growth of their business portfolio. Over the years, the MFIs mobilized total savings deposits of Birr 8.7 billion, credit business of 13.7 billion Birr by the end of December 2013. The prudential regulation has improved performance standards, risk management and financial transparency of MFIs.

AEMFI – expanding services

AEMFI has grown from strength to strength and has been engaged in performance review of the member institutions, conducting studies and research, bringing about publications, developing self-regulatory practices, MIS, pursuing policy advocacy and undertaking training/capacity building interventions. Recently, it set up the Ethiopian Inclusive Finance Training and Research Institute (EIFTRI) to give focused attention to training and research activities, in micro finance. A case study on MFISD is given as Appendix 15 in main report of the study.

2.1.3 Initiatives to enhance financial inclusion

Financial co-operative sector development and regulations

The co-operative sector has been developed over the years through a series of proclamations since 1958. There are around 27,000 multipurpose co-operatives out of which about 30% are SACCOs. The Federal Co-operative Agency (FCA) was established in 2002 with a mandate for promotion, regulation and supervision of all types of co-operatives under the Proclamation No.274 of 2002. The co-operative sector comes under the jurisdiction of Ministry of Agriculture with FCA at the national level for overall regulation and supervision. Regional Co-operative Bureau (Agency) offices, zonal co-operative offices and district co-operative offices at different levels are involved in co-operative development and supervision of SACCOs. Efforts have been directed to forge convergence of these agencies. The weaknesses and challenges with respect to organizational arrangements, data building, audit, supervision and regulation of credit unions/RUSACCOS have existed. Considering the useful role played by the financial co-operatives and their potential in providing increased access to financial services in difficult and remote areas, policy, promotional and facilitative measures have been initiated by FCA, with support from IFAD-funded RUFIP I and II. Since 2003, IFAD and other donors' efforts have been directed at the level of GOE to evolve separate legal code for financial co-operatives. The sustainability of 245 co-operative unions and 6792 primary financial co-operatives has received attention of the policy-making authorities. Development of resources (human and financial), governance, members' education, and leadership development are the challenges. A comprehensive co-operative development policy and strategies need to be evolved and put in place.

Risk management policy / architecture in MFIs

Consequent to issue of comprehensive risk management guidelines in 2010 by NBE, there had been continued efforts at various levels to operationalize the guidelines. The MFIs have taken initiatives to internalize the guidelines with regard to risk identification, measurement, monitoring and control. Policies, processes and systems initiated in this regard include ensuring Board and senior management oversight, placement of risk Management Committees/Risk Mangers, strengthening MIS and capacity building in the related areas. NBE and AEMFI have also been undertaking training and knowledge management programmes for MFIs for the purpose. Increased appreciation of risk management policy is evident.

Agricultural Transformation Agency (ATA)

To increase the number of smallholder farmers benefiting from participation in co-operative enterprises and to ensure that they receive the support and regulatory oversight needed to succeed, the Ethiopian Agricultural Transformation Agency (ATA) has been working closely with the Ministry of Agriculture, the FCA, Regional co-operative promotion agencies and other key stake holders to identify a varieties of systemic interventions. As part of the agricultural co-operative sector development strategy, it has been pursuing advanced certification for agricultural co co-operatives which help to indicate the effective and self-sustaining nature of particular co-operatives and the existence of a professional governance structure. A comprehensive study was envisaged to develop a relevant framework. It also envisages upgrading Co-operative College to a fully dedicated centre of excellence and evolving a comprehensive business plan. It also plans to expand and strengthen public sector audit capacity for agricultural co-operative societies and their unions. The GOE has developed a 5-year Growth and Transformation Plan (GTP), which aims to maintain strong economic growth of about 11% per year that has been achieved over the past years. The GTP focuses on (a) equitable growth, (b) agriculture in rural areas development and (c) Promotion of women and youth development.

Co-operative Development Programme (CDP) – KM objective

The USAID-funded programme CDP focuses on five Unions located in the districts of Amhara, Benshangul – Gumuz, Oromia, SNND and Tigray, as well as select primary co-operatives (3 from each region). The CDP draws an expertise of international partners (Overseas Co-operative Development Council and Communications Co-operative International) and local agency (FCA). The 5-yearprogramme will establish Co-operative Learning Information Centre (CLIC) to benefit co-operatives from distance learning and best practices dissemination.

Legal and regulatory framework for leasing

The capital goods leasing business (amendment) Proclamation 2013 envisages clear demarcation of responsibilities of the NBE and the Ministry of Trade in lease finance. NBE is mandated to license and supervise the capital goods finance companies in providing financial lease and hire purchase. On the other hand, Ministry of Trade is authorized to continue licensing and supervising leasing entities engaged in operation leases. Accordingly NBE set up a unit in MFSD with responsibility for licensing and supervision of capital goods finance companies. It has issued two directives envisaging minimum initial paid up capital required for the concerns and requirement of licensing. These laws and directives intend to create an enabling environment to establish alternative sources of financing SMEs and to address the gap of the existing financial institutions.

Enhanced financial inclusion efforts

GOE is a signatory to Maya Declaration for financial inclusion. With a view to fulfilling the commitments of NBE, multi-pronged efforts for creating an enabling policy environment is needed. Besides GOE, NBE, FCA, etc., donor agencies like IFAD, World Bank, UNDP, UNCDP, ILO, etc., are integrating with efforts in this regard.

2.2 Role and Contributions of IFAD's Rural Finance Programmes

2.2.1 Laying strong foundations for RF through RUFIP I

Since 1980, IFAD has invested a total of US$ 398 million in 16 programmes in Ethiopia and out of a total expenditure of more than US$ 1 billion. IFAD has also provided US$ 28 million in debt relief to the country under the Heavily Indebted Poor Countries Debt Initiative. One of the landmarks of IFAD's support includes the successful implementation of Rural Finance Intermediation Programmes [RUFIP] in the country commencing from 2003. The four principal components of RUFIP I included (i) institutional developmental support to Microfinance and Cooperative sub-sectors, (ii) improved regulation of MFIs, (iii) institutional capacity of NBE and AEMFI, equity and credit funds for MFIs and RUSACCOs and (iv) co-ordination and management support. The programme facilitated access to 1.5 million rural households through 20 MFIs and 9 RUSACCOs/Unions. Apart from expansion of the clients of these institutions, the programme brought about improvement in the management, rules and regulations guiding the delivery of financial services in rural areas [for farm and non-farm activities] by MFIs and co-operatives. It provided the much needed support to NBE's supervision wing, for carrying out supervision of MFIs and thereby improved prudential performance, governance, and management of MFIs. The GOE brought out a revised and more comprehensive MF Act in 2009. Before the new Act 2009, NBE had issued 19 directives. The improved legislative, regulatory and supervisory framework enhanced compliance to the prudential and regulatory norms at the end of RUFIP I. The positive impacts of RUFIP I have been brought out in the country evaluation report of IFAD (IFAD, 2011). The COSOP 2010-2017 (IFAD, 2008) prepared by IFAD stated: "The second phase of RUFIP will build on successes achieved under the IFAD initiative Phase I in scaling up and expanding outreach in the delivery of financial services to rural households". The COSOP identified opportunities for Ethiopia which included rural finance as an important sector for intervention.

The cost of RUFIP I project was US$ 88.73 million inclusive of the IFAD loan US$ 25.69 million, with African Development Bank [AfDB], GOE, Development Bank of Ethiopia [DBE], commercial banks, AEMFI, FCPB and RCPBs as con-financiers. The programme design was in line with the strategies of IFAD and AfDB, and national policies of GOE. The co-operative sub sector had increased substantially with establishment of 4337 RUSACCOS, with a membership of 105 272, by December 2010 compared to 134 with a membership of 4586 at the beginning of RUFIPI. MFIs were able to provide loans to 2.3 million rural households taking up small farm, off-farm and non-farm enterprises to diversify their income opportunities.

MFIs had trained more than 14,000 rural centre and group leaders, and MFI clients including 40,000 women. The clients' sensitization efforts generated a better sense of credit discipline and raised financial discipline and operational sustainability of MFIs. RUFIP played key role in sensitizing Government about the need and significance of rural financial services. It had led to the development of saving culture among the poor households. It brought about a change in the mindset of policy makers and promoters of rural financial institutions, particularly RUSACCOs/Credit Unions. There was thus, a paradigm shift in the whole approach to rural finance in the country. Fourteen supervision Missions were engaged for review of the progress of the RUFIP I and these Missions gave considerable policy inputs and ideas for furtherance of rural finance in the country.

2.2.2 Designing RUFIPI II framework

RUFIP-II was designed based on the lessons learnt and the foundations laid during RUFIP I with the following components: (a) Institutional development in the micro fiancé and financial co-operatives sub sectors including knowledge management and capacity building and MIS; (b) Improved regulation and supervision of MFIs and co-operatives; (c) Providing financial support to MFIs and RUSACCOS to bridge their liquidity gap and thereby enhance their capacity to provide access to financial services; and (d) Programme Management and Co-ordination.

The overall objective of the programme was to ensure sustained access to a range of financial services for rural poor agricultural households. Continuation of exclusive component of improved regulation and supervision of MFIs and co-operatives" facilitated continued thrust on policy development and development focus on the policy-making institutions and regulated entities. The total programme cost was envisaged at US$ 248 million over 7 years of implementation, from July 2012 to June 2019. The MOFED, NBE, FCA and DBE, MFIs, Regional Governments, Cooperative Unions/RUSACCOS and AEMFI continued to be the key implementing agencies/stake holders of the programme.

2.2.3 Creating policy development forum

The National Rural and Micro Finance Policy Steering Committee [NRMMFPSC] was constituted under the Chairmanship of Vice-Governor, NBE [in-charge of the supervision of financial institutions]. It is conceived to be the key pillar in the management structure of RUFIP II for guiding overall development and direction of the micro finance sector. The TORs of the Policy Steering Committee include institutional arrangement for financial inclusion, Micro insurance policy, MFI's integration with National Payment System, market development, improvement of governance, technological up-gradation of MFIs, development and integration of rating agencies, deposit insurance, credit information with MFIs, risk management framework, lending appraisal system, audit system improvement, review and refinement of the legal code for micro finance sector. Thus, the Committee created under RUFIP II, and which comprises of all policy-making institutions, would provide a powerful policy development platform to steer development/ reform in rural finance. The Programme Management Committee constituted under the Chairmanship of Programme Director, RUFIP II, monitors programme implementation.

2.2.4 Supporting capacity building of MFIs, AEMFI and NBE

The programme envisaged human resource development (HRD) measures [national and international training programmes, overseas explosive visits, etc., for NBE staff, policy seminars, auditors' sensitization, preparation of supervision manual, technology-based offsite surveillance system [OSS], MFIs' participation in payment and settlement system, branchless/mobile banking, MFIs' integration with

Credit Bureau, Governance code development, etc. The programme under RUFIP II and I provided opportunities to NBE for national and international trainings and exposures to enhance capacity in risk-based supervisions, preparation of forward-looking regulations and introduction of best practices in audit and policy development. It has facilitated stake holders' consultation, consultants 'service for studies and documentation, etc. Introduction of risk-based supervision, issue of several regulations from time to time through participating process, introduction of supervision tools, and improving quality of inspection by NBE evidenced its increasing capacity and pro-activeness.

2.2.5 Eliciting continuing GOE commitments to RUFIP

Government of Ethiopia has been consistent in its commitment to rural development, poverty reduction, and food security through greater access to finance and accordingly; it has owned up the implementation of RUFIP I and II over the years. GOE has been supportive of MFIs in terms of creating enabling policy environment, owning major shares of leading MFIs, extending government guarantees for facilitating resource support to MFIs and implementing government programmes through them. Similar level of commitment exists for the co-operative sector. The Agriculture Transformation Agency [ATA] is engaged in evolving new strategies for supporting agricultural/co-operative credit system.

2.2.6 Integrating with other donors' initiatives

Participation in donors' forums

IFAD continues to be a prominent player in the rural fiancé sector although there have been initiatives from other development partners such as World Bank GIZ, UNDP, KfW, African Development Bank, Irish League, Bill Gates, etc. The GOE convenes Donors' Forums and IFAD participates in such meetings, particularly on issues of rural financial services, micro insurance, etc.

Drawing ILO / UNCDF Joint Supplementary Project for RUFIP II

With a view to supplementing RUFIP II, a project on financial inclusion has been prepared by ILO/UNCDF with a financial outlay of US$ 20 million. The project envisages technical and financial support covering mapping demand and supply data for financial services, simplified data reporting systems by co-operatives/ MFIs, strengthening product development, financial education, micro insurance, branchless banking/mobile money and lease financing. UNDP, WFP and FAO are expected to provide technical and financial support for the initiatives.

Engaging Irish League for Cooperative Union Foundation to look into all issues of financial cooperatives

With RUFIP II support, FCA has made twinning arrangements with the Irish League. The League is expected to study training needs, MIS, regulatory arrangements, financial products and services, linkage with banks and MFIs and provide necessary tools, and technical assistance within a period of 18 months, by March 2015**.** Hopefully, they would provide qualitative and timely inputs, leading to practical interventions for remedying the issues of RUSACCOS/Unions. However, the League had only completed training needs assessment by July 2014.

2.2.7 Looking forward to expected outcomes of RUFIP II

Micro insurance policy framework status, regulation and supervision are likely to get greater attention, leading to positive impact. Policy dialogues and consultative process should be enhanced through NRMFPSC. Micro insurance, improved governance codes in MFI/Financial Cooperatives, self-regulation, MIS, ICT and disclosures would complement prudent regulations.

Chapter 3

Emerging issues, challenges and recommendations

3.1 Separate legal code for financial co-operatives

Notwithstanding the efforts being directed to provide institutional focus for supervision and audit of RUSACCOS/Credit Unions by the FCA/RPCBs within the existing statute with support from RUFIP, it would be more effective and appropriate if a separate proclamation for financial co-operatives is evolved/ enacted to ensure independent, adequate and exclusive institutional arrangement for regulation, supervision, audit and orderly development of SACCOS sub-sector. A national policy and strategy document on the cooperative sector should be prepared and put in place, prior to the proposed new legislation on Financial Cooperatives**.**

3.2 Institutional deposit protection scheme for co-operatives

"Deposit safety and institutional protection system" should be put in place for Financial Co-operatives Societies/Unions. Through this mechanism, both the institutions and members' funds with the institutions can be protected from adverse situations and vulnerabilities. Institutional protection would protect the tangible assets of SACCOS from impairment. A Protection Fund could be created through contributions by SACCOS and other stakeholders including government, to be managed by an independent authority, to ensure deposit safety by way of compensation to co-operative members.

3.3 Board of supervision for co-operatives

A Board of Supervision comprising of regulation and supervision experts, practitioners, representatives of NBE, GOE, and Regional Governments/RPCBs may be set up under the coordination of FCA to review the policy, regulations and supervisory issues, progress and trends in supervision and audit and provide directions and guidance to FCA in the tasks of regulation and supervisions for financial cooperatives. Similar professional bodies can be set up at the regional levels. This will help in building up quality and professional neutrality in regulation and supervision.

3.4 Need to strengthen self-supervision in SACCOs

With a view to putting in place co-operative principles, best practices in customer services and high ethical values, it would be appropriate to strengthen self-supervision in the SACCOS sub-sector. The setting up of *Federations/Unions* at various levels and Association on the lines of AEMFI would facilitate the same. The sector should evolve voluntary *codes of standards and fair practices* and ensure their compliance, on sustainable basis.

3.5 Need to strengthen MIS

With a view to putting in place a robust MIS in the co-operative sector, initiatives like streamlining reporting and disclosures, accounting and audit system, introducing ICT tools, integrating with “credit reference bureau system”, etc., need to be stepped up. ICT infrastructure is very critical for the purpose.

3.6 Supervisory policy, process, system and tools for co-operatives

The whole supervisory policy, process and system need review and overhauling. The FCA and RPCBs have mutual obligations in the direction (particularly with regard to approach and modalities of onsite and offsite supervision), compliance and competence-building of supervisors. Based as the relevant policy and regulations in force, the documents like comprehensive Manuals for supervision, audit, governance, risk management, rating, etc., should be prepared for guidance of supervisors, auditors, risk managers, Board of Directors and executives of the co-operative credit structure. There is need for a planned and systematic approach for the purpose.

3.7 Enhancing HR capacity of regulator and regulated entities

Notwithstanding the initiatives and support of RUFIP I and II so far, the sector needs continued and systematic interventions in HRD for implementation of policies, regulatory and supervisory guidelines. A revisit of training needs, training modules, materials, delivery etc., on policies and practices of regulatory and supervisory importance is necessary for carrying out capacity building interventions. Development of HRM and HRD policy, setting up of exclusive and dedicated institutions for training, training of trainers [TOT] should be undertaken.

3.8 Integrating co-operatives into financial inclusion policy and plans

The co-operative sector should be at the centre stage of financial inclusion policy and plans. The Financial Literacy campaign should include members of financial co-operatives to enable them to have effective participation in the governance and management of SACCOS.

3.9 Resource support for MFIs

With growing and expanding MFIs as also upcoming MFIs, resource mobilization is critically important. In view of the reluctance of CBs to provide lending support to MFIs and the difficulties in obtaining government guarantee for the purpose, there is emergent need to revisit the relevant policies. A policy for relaxation of government guarantee norms by lenders, the mandatory policy prescription for CBs for providing certain percentage of their portfolio for MF sector including loans to MFIs, etc., is considered necessary. Secondly, setting up of an apex development bank as suggested in the design report of RUFIP II would ease the resource constraint of MFIs. Besides the use of collateral substitutes, popularization of guarantee fund mechanism and institution of national Guarantee Fund to support MFIs, etc would also be useful and relevant. GOE and NBE should also track the financial support extended by CBs for MFIs/RUSACCOS and Credit Unions.

3.10 System for deposit insurance

The savings that are presently made by the depositors with MFIs, either compulsorily or voluntarily, do not enjoy any protection. There is need for deposit protection policy and deposit protection facility by way of insurance scheme and institutional support mechanisms. A Deposit Insurance Fund with a relevant policy and operational mechanism should be put in place in the interest of depositors of the financial institutions including MFIs.

3.11 Enactment / review laws and policies to improve competition

Apart from Financial Co-operative Laws, Proclamations for national identity system, moveable asset registry system, consumer protection, micro insurance [alternatively revised insurance law with a chapter on micro insurance] and micro pension are considered necessary. Three fundamental policies continued to exist, leading to difficulties for MF Sector: (i) the denial of dividend on contributed equity in MFIs; (ii) foreign nationals are excluded from owning equity in MFIs (in the financial sector); and (iii) the donated capital is not recognized as core capital and can be deemed as Tier II Capital. These stand in the way of competition in the financial sector and as such, need policy dialogue and review/relaxed.

3.12 Micro insurance development

Micro insurance sub-sector should be given focused attention in terms of policy-making and development intervention with due support form donor agencies. The Directorate of Insurance should have Micro Insurance Division to give exclusive and focused oversight on supervision of micro insurance under the new law/proposed regulations besides supervision initiatives for development of the insurance sub-sector.

3.13 Policy research and KM focus

AEMFI through its EIFTRI have undertaken research studies having bearing on rural finance policies besides continuing capacity building interventions for MFIs and other related institutions. There is need to augment and upgrade policy research and institutional mechanism on contemporary issues, as well as training infrastructure for conducting training programmes for HR in the financial sector in the emerging areas. The potential institutions, including the Ethiopian Institution of Financial Studies (EIFS) of NBE, ARDIATA Cooperative Institute, etc., can be tapped for the purpose.

3.14 Upgrading risk-based supervision and audit

MFSD and NBE have taken considerable initiatives for introducing risk- based supervision of MFIs. The efforts with respect to strengthening RBS tools, approach, and the risk management/mitigation architecture in the supervised institutions need to be continued. A good policy environment, coupled with sound system and process, and compliance to regulatory and supervisory standards enhance the ability of MFIs to develop demand-driven products, to reduce transaction cost, manage risks, attend to growth and the goal deepening financial inclusion, maintain operational and financial sustainability and protect customers' deposits.

3.15 Transformation of financial institutions

The policy should be supportive of MFIs and financial co-operatives to graduate to higher level of performance and greater standards of quality of services. Innovations and development and adoption of technology-based services backed by regulatory safeguards are key to transformation process. Very strong SACCOS, with potential for growth should be nurtured to graduate as cooperatives which could eventually lend financially to smaller SACCOS. Five top-most MFIs share over nearly 90% of MF industry. With a view to broadening their scope of contributions to the financial sector in all fronts and enabling them to provide fully-fledged financial services, these leading MFIs should be upgraded as Community Banks. A separate set of legislation and prudential regulations may be evolved for them on the lines similar to those used in some of the countries such as Tanzania.

3.16 RF unit in MOFED

In MOFED, there is no dedicated unit for rural finance/MF development, although they have been supportive of rural development programmes**.** GOE may like to consider setting up Rural Finance Department/Division for focused attention for rural financial sector. Such unit would facilitate co-ordination and convergence of various policy and developmental interventions in RF.

Appendices

Appendix 1.1. Study questionnaire

1) Who are you? (Country Project Officer, Country Programme Manager, senior Policy Adviser, PTA, Policy researcher, etc).

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2) In which country are you working?

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3) Using the format given below, please name IFAD-supported projects in your country, segregating those in operation and the completed ones.

Project no.	Project title	Project period	Project's broad components

4) According to you which are the most successful IFAD's intervention in your country? Please specify reasons.

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5) Were there any major policy issue(s) pertaining to the project's implementation in your country/ESA?

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6) If yes, what did the Government, regulatory agencies and other policy-making authorities do to resolve and subsequently improve the project's implementation. (Please mention the project, policy constraints and the improvement made as indicated in the table)

Project name	Policy constraints	Changes/improvements made

7) What methodology/approach was adopted to change/develop the *relevant* policy?

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8) Have there been any separate documentation done on new policy introduced, policy issues resolved and/or policy refinement/development contributed under the project implemented? If so, specify.

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9) Do you have any separate institutional mechanism in the project framework for review, debate, resolution and dissemination of policy issues? If so, specify.

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10) Was regulation and supervision of financial services institutions embedded within the Rural Finance Project as core component? If so, outline major interventions effected for improvement in regulatory and supervisory policy?

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11) How has regulation and supervision of financial services embedment in the Rural Finance Project been helpful in policy reforms in financial sector?

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12) What are the difficulties faced by IFAD in pursuing with policy-making authorities/promoting innovative policy framework?

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13) What could be the best/most feasible ways of bringing about necessary policy changes/reforms for a donor agency?

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14) Are there any seminar/ workshop, training, sensitization, exposure programmes which are organized for stakeholders' capacity to look into policy issues/ explorations as part of project implementation? If so, cite a few models.

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15) (a)What are the means adopted for dissemination of information/experience in policy issues at various levels including grass root level?

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(b)In your project, has there been a participatory approach as a method in making policy decisions? If so, cite instance(s)

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16) Is there any exchange forum(s) put in-place in your country/ESA for projects to exchange knowledge/experience? If so, how effective is the forum(s)?

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17) Is there any institution(s) in your country which can be banked upon for knowledge management in policy issues pertaining to project themes of IFAD? If so, give details.

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18) (a) Identify five major IFAD's contributions in policy areas/issues in your country?

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(b)Give brief outlines of the above identified policy areas/issues.

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(c) Do you think any of the above is/are best practices/innovative which can be replicated in other countries?

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19) Name five major unresolved policy issues (theme-wise) hindering project implementation in your country?

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20) Would you advocate for policy development in core areas of IFAD support framework in your country/ESA? Give reasons for your answer

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21) Do you have any other input having relevance to IFAD's policy contribution in your country/ESA?

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Appendix 1.2. References

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Appendix 1.3. Institutions visited and persons consulted

Sl. no.	Name	Designation	Institution	Date
1	Mutandi Robson	Country Project Manager, Ethiopia & South Sudan	IFAD	03.07.2014
2	Tessema Legebo	Country Programme Officer	IFAD	05.07.2014
3	Habte Salessi Dogamni	Programme Officer	IFAD Country Office	03.07.2014
4	Chiara Romano [Ms]	Gender & Targeting Consultant	Do -	03.07.2014
5	Ruby Wairimu Mburathi [Ms]	Knowledge Management Officer	Do -	04.07.2014
6	Bahiru Haile	Director RUFIP II	Devt. Bank of Ethiopia	03.07.2014
7	Dr Wolday Amha	Executive Director	AEMFI & EIFTRI	03.07.2014
8	Bethlehem Girma	Manager	Do -	04.07.2014
9	AbateMitiku	Advisor for Vice Governor, Financial Institutions Supervision	NBE	04.07.2014
10	Temesgun Zeleke	Director, Insurance Supervision Directorate	NBE	04.07.2014
11	Asfan Abera	Principal Examiner, Directorate of MFI Supervision	NBE	04.07.2014
12	Tezore Kebode	General Manager	PEACE MFI,	04.07.2014
13	Berhane Kidanu	Technical Advisor Policy	ATA(Agricultural Transformation Agency), GOE	05.07.2014
14	Joseph Asafa	Special Officer, Micro Insurance	International Labor Organization [ILO]	03.07.2014
15	Abeba Ayalew	Programme Coordinator, RUFIP II	FCA	05.07.2014