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COLLEGE OF LAW AND GOVERNANCE STUDIES  
SCHOOL OF LAW**

**The Legal and Institutional Framework Governing Small-Scale Farmers  
Access to Credit in Ethiopia; Successes and Failures in the Case of the  
Amhara National Regional State**

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# Approval Sheet

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## I. Acronyms

ACSI	Amhara Credit and Saving Institution
ADLI	Agriculture Development Lead Industrialization
AEMFI	Association of Ethiopian Microfinance Institutions
CBE	Commercial Bank of Ethiopia
ANRS	Amhara National Regional State
DBE	Development Bank of Ethiopia
EACWSE	Ethiopian Agricultural Commodities Warehousing Service Enterprise
ECX	Ethiopian Commodity Exchange
FDRE	Federal Democratic Republic of Ethiopia
FINDEX	Financial Inclusion Index
FI	Financial Institution
GTP	Growth and Transformation Plan
IFAD	International Fund for Agricultural Development
MOA	Ministry of Agriculture
MOFEC	Ministry of Finance and Economic Cooperation
MFI	Microfinance Institution
NBE	National Bank of Ethiopia
NFIST	National Financial Inclusion Secretariat
NFIS	National Financial Inclusion Strategy
NGO	Non-governmental Organization
PASDEP	Plan for Accelerated Development to End Poverty
RLUAP	Rural Land Use and Administration Proclamation
SDPRP	Sustainable Development and Poverty Reduction Plan
SSA	Sub-Saharan Africa
SSF	Small Scale Farmers
WB	World Bank
WR	Warehouse Receipt

## **Abstract**

*Small scale farmers dominated agriculture is the mainstay of the Ethiopian economy contributing 35 % of the total domestic production, employing 72% of the labor force, and constituting 79 % of total export. However, small-scale peasant farmers suffer from poor and unsustainable farming practices aggravated by lack of finance and technology. Ethiopia aspired to realize overall economic development through transformation of the agriculture sector in its development policies and strategies. Despite the policy aspirations, small scale farmers are not backed by affordable rural credit facilities to use modern agricultural technology. Several cross-cutting factors, which are attached to both the nature and regulation of the financial and agricultural sectors contributed to the underdevelopment of rural credit intermediation in Ethiopia. Formal FIs, particularly, banks use collateral based credit appraisal policy, which excludes small scale farmers from accessing affordable credit. Banks consider credit delivery for small scale farming as a risk bearing business and ditched such operation in favor of a less risky and profitable operations in other sectors.*

*Microfinance and banking regulatory and institutional frameworks pledged priority for financial soundness with strict prudential regulation. Ethiopia introduced a one size fits all prudential regulation for all types of MFIs with similar entry, organizational structure, capital, and governance regulations irrespective of their risk bearing potential. However, literature and best experience shows that a tailored microfinance regulation depending on the risk bearing potential of particular MFIs is important to ensure competition and access to credit.*

*The restrictive rural land holding policy and regulatory framework at sub constitutional level, that restricts use of land holding right as collateral, is another major constraint. Underdeveloped normative and institutional capacity in the registration of movable property security rights made a vast majority of small scale framers' assets collateral unworthy. Lack of insurance coverage along with poor credit reference system posed significant challenge for FIs to engage in a prudent rural credit intermediation without being exposed to credit risk. Absence of an enabling micro and index weather insurance regulatory framework, that enables large number of small scale farmers to access universal insurance with lower premiums, is also another major impediment. While the warehouse receipt financing scheme failed to benefit small scale farmers due to strict membership based ECX regulatory framework.*

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Finally, I want to take this opportunity to thank family members, friends and others who directly or indirectly assisted me throughout my study.

## **Chapter One**

### **Introduction**

#### **1.1. Background of the Study**

Agriculture is the mainstay of majority of Ethiopians and the driving force for economic development in Ethiopia.<sup>1</sup> Agricultural contributes 35 % of the total domestic production, employees 72% of the labor force, and covers 79 % of total export.<sup>2</sup> However, the sector is dominated by SSFs who practice rain-fed mixed farming employing traditional technology, and production system. SSFs constitute 94% of the total agricultural production, and 95% of the total agricultural land in the country.<sup>3</sup>

ANRS is the home of predominantly agrarian society with nearly 84% of the total population of 21, 100,000 earning its livelihood from small scale farming and livestock rearing<sup>4</sup>. Poverty is pervasive in the region with about 26.1% of the total population below the nationally defined poverty line.<sup>5</sup>The number of SSF households by 2019 in the region was 3,600,000 out of which only 345,838 farmers accessed agricultural inputs through credit financing arrangement from ACSI.<sup>6</sup>

Ethiopia adopted rural centered development policies and strategies to ensure rapid overall economic transformation. Among others, ADLI, SDPRP, and the highly ambitious GTP pledged a special attention for rural development and agricultural transformation. Despite the policy aspirations, the agriculture sector is not backed by adequate financing that can ensure application of modern technology extensions and transformation.

In Ethiopia, there were 18 commercial banks and 38 microfinance institutions by the end of December 2019.<sup>7</sup>Contrary to the proliferation of FIs, the agricultural sector receives less than 6 % of the banks' lending, the bulk of which is towards the more developed exports oriented

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<sup>1</sup>Atsbeha G/Silassie and Tessema Bekele , “a Review of Ethiopian Agriculture: Roles, Policy and Small-scale Farming Systems,” (2013), Global Growing Casebook. 36

<sup>2</sup>Ministry of Agriculture of FDRE, “4<sup>th</sup> year of GTP II Agricultural Sector Annual Performance Report”, (2019).3

<sup>3</sup> G/Silassie and Bekele, n-1

<sup>4</sup>FDRE Central Statistics Agency , “Population Projections for Ethiopia 2007-2037”, (2013), and UNICEF ANRS Budget Brief, (2016),

<sup>5</sup> FDRE National Planning Commission, “Ethiopia’s Progress Towards Eradicating Poverty; an Interim Report on 2015/16 Poverty Analysis Study”, (2017)

<sup>6</sup> ANRS Bureau of Agriculture, “Successes and Challenges in the Distribution of Credit based Agricultural Inputs in 2019”, Collected from ANRS Bureau of Agriculture on 25/08/2019

<sup>7</sup> NBE, “2018/19 Second Quarter Report”, NBE Quarterly Bulletin, 3& 5

commercial farming sub-sector.<sup>8</sup> Strict collateral based loan appraisal procedure on the side of banks along with absence of specialized rural banks caused about 85% of the Ethiopian rural households to remain without access to formal financial services.<sup>9</sup> IFAD underlined in its 2011 report that lack of credit facilities causes to low level use of irrigation facilities, quality seeds, and fertilizers in Ethiopia.

The quality of legal and institutional framework influences the degree of access to credit services available for the poor.<sup>10</sup> A robust regulatory and institutional framework can create enabling environment through setting the rules of the game for the provision of specific financial products or curtail unnecessary barriers.

The founder of Grameen Bank and Nobel Prize winner Muhammad Yunus emphasized the significance of well-designed inclusive finance in poverty reduction in his statement about Grameen Bank<sup>11</sup>:

*Grameen is a pure meritocracy, providing opportunities for self-advancement based not on class or race or inherited privilege but on character, imagination, and hard work*

In Ethiopia FIs, particularly banks operate extremely under conservative lending policy guided by NBE prudential regulation intended to ensure financial soundness. The credit policy of banks is like ‘for the haves to have more’<sup>12</sup>; instead of extending inclusive finance for the poor and underserved. The microfinance regulatory framework is characterized by a one size fits all prudential regulation, which mainly intends to ensure financial soundness irrespective of the size and risk bearing potential of particular MFIs and transactions.

The characteristics of the agricultural sector along with the restrictive rural land holding regime that restricted use of rural land use right as collateral made credit delivery for SSFs risky and unattractive.<sup>13</sup> Small scale farming in Ethiopia is a loss making activity marred by traditional farming practices, uneconomic land tenure and climate shocks with no insurance

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<sup>8</sup> NBE 2018/19 report, n-7 at 40

<sup>9</sup> Wolday Ameha and Anteneh Kifile, “Assessment of Performance of Microfinance Institutions in Ethiopia”, (2013), Bulletin 9.AEMFI,

<sup>10</sup> WB Group & IMF, “Financial Sector Assessment; A Handbook”, (2010), WB Publications.188

<sup>11</sup> Bornstein D, “the price of a dream: the story of the Grameen Bank and the idea that is helping the Poor to change their lives,” (1996), UNIV CHIK Press 26. I

<sup>12</sup> Ameha and Kifile, n-9

<sup>13</sup> Wolday Ameha and Devid Peck, “Agricultural finance potential in Ethiopia; Constraints and opportunities for enhancing the system”, (2010), AEMFI, 24

coverage.<sup>14</sup>Lack of weather insurance for smallholders, and absence of warehouse receipt financing scheme along with poor infrastructure and lack of commercialization of production further discouraged FIs from engaging in rural credit intermediation.<sup>15</sup>

## **1.2. Statement of the Problem**

In Ethiopia, contrary to the policy aspirations and the role of agriculture to the country's economy, access to credit for SSFs remains the lowest among SSA. SSFs in Ethiopia in general and in ANRS in particular suffer from poor and unsustainable farming practices aggravated by lack of capital and technology. Intertwined legal, institutional, and practical factors contributed to the credit exclusion of SSFs. While Ethiopia achieved a significant milestone in adopting and implementing prudential microfinance regulatory framework to ensure financial sustainability, the strict one size fits all capital, organizational structure, entry, interest rate, and corporate governance requirements negatively affect credit inclusion by imposing extra-burden on infant MFIs. Despite the introduction of banking sector reform since 1994 that leads to expansion and geographical outreach of banks, banks have poor record in availing loan to the rural population. The financial soundness oriented banking regulatory and institutional framework coupled with absence of separate enabling rural credit intermediation framework exposed farmers to strict and unaffordable corporate loan appraisal policies. .

The Restrictive rural land legal framework put farmers without collateral options through outlawing use of rural land use right as collateral for long. Although there are positive developments towards allowing use of rural land use right as collateral, the unreformed rural land regime at federal level remains the major impediment to rural access to credit.

Absence of enabling legal and administrative procedures for perfecting and enforcing security interests over a wide range of rural assets forced FIs to refrain from what they consider it a risky credit operation. Lack of micro insurance package for SSFs is another problem, which discourages FIs from extending credit for SSFs due to high risk of default. The indemnity based property insurance framework as envisaged under the 1960 commercial code is very costly and not compatible to the needs of SSFs. Inadequate credit history of SSFs constrains FIs from expanding responsible lending without being exposed to default risk. The existing credit information Bureau is not strong enough to fetch, systematize and distribute adequate credit

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<sup>14</sup> Ameha and Pick, n-13, at 24

<sup>15</sup> Ibid

history of farmers. While from the perspective of farmers insufficient attitude about credits leads to uneconomic spending of loans and high default rate. Lack of comprehensive national financial literacy strategy resulted in fragmented and ineffective interventions that do not necessarily support credit inclusion.

In ANRS credit products for the rural mass are very limited with no bank credit and very limited competition among MFIs in the region. Absence of competitive MFIs coupled with narrow group guarantee based loans led to an acute shortage of fund for farmers to purchase agricultural inputs and apply technology. While the overall legal and institutional bottlenecks at the national level extend in the case of ANRS, peculiar factors related to rural land use right, land certification, and lack of competitive MFIs, affect rural credit inclusion in the region.

Despite the aforementioned pressing developmental problems, no holistic analysis of policy, regulatory and institutional framework is conducted. Accordingly, under this study financial, agricultural, and related policy, legal and institutional frameworks are analyzed in a comprehensive fashion with a view to come up with working recommendations and interventions.

### **1.3. Research Questions**

In tandem with the statement of the problem, the guiding research question is ‘to what extent the existing legal and institutional framework is conducive enough to ensure SSFs access to credit in Ethiopia in general and in ANRS in particular. Based on this guiding question, the research tried to answer the following specific questions:

- Whether the existing microfinance and banking policy, legislative and institutional frameworks in Ethiopia are conducive enough to ensure SSFs access to credit?
- Whether the existing rural land holding, security rights, insurance, credit reference system, and warehouse receipt financing legal and institutional frameworks are conducive to ensure SSFs access to credit?
- Whether the credit policies and products of MFIs and banks are conducive and responsive enough to address the needs of small SSFs in Ethiopia and ANRS?
- Whether SSFs’ access to credit in ANRS improved after the introduction of the ANRS Rural Land Use and Administration Amendment Proclamation No.252/2017 and second level rural land holding certification? and

- Whether there are adequate and competitive banks and microfinance institutions that deliver broad range of credit products to SSFs at a competitive cost in ANRS?

#### **1.4. Objective of the Study**

The general objective of this study is to undertake a comprehensive assessment of policy, regulatory, and institutional frameworks that affect SSFs' access to credit and forward a set of recommendations and interventions that are necessary to resolve constraints identified. This study is conducted with a purpose to achieve the following specific objectives:

- To scrutinize microfinance and banking regulatory and institutional frameworks in Ethiopia in light of ensuring SSFs access to credit;
- To demonstrate the impact of legal and institutional bottlenecks related to rural land holding rights, security rights, SSFs insurance policy, credit reference system, and similar issues on SSFs access to credit;
- To assess as to whether banks and microfinance institutions are offering flexible credit products at a competitive cost to SSFs in Ethiopia in general and in ANRS in particular;
- To filter regulatory and institutional barriers in ensuring SSFs access to credit in Ethiopia in general and in ANRS in particular? and
- To forward a set of recommendations and interventions that help to enhance SSFs access to credit in Ethiopia in general and in the ANRS in particular.

#### **1.5. Significance of the Study**

A comprehensive scrutiny of policy, regulatory, and institutional frameworks that affect SSFs' access to credit can play a significant role via filtering constraints and providing a set of recommendations and interventions for policy makers. The study will have the following specific significance:

- By listing regulatory and institutional bottlenecks towards SSFs' access to credit, the study helps policy makers at the federal and ANRS level, banks, and MFIs to resolve those problems identified by the study.
- The recommendations and interventions identified by this study can serve as input for policy makers to further develop strategies to enhance SSFs' access to credit.
- The study will serve to bridge knowledge gaps in terms of assessing the role of regulatory and institutional frameworks in ensuring SSFs' access to credit.
- It will serve as a baseline for further or related studies on the same issue.

## 1.6. Review of Literature

Nobel Laureate Muhammad Yunus and founder of Grameen Bank, in his story called “Banker for the Poor (2006),” underlined collateral based credit culture contributed for credit exclusion of the poor mass and recommended creation of enabling policies that empower people to use their creativity and energy through provision of capital in a social capital based credit.

NBE (2019) demonstrated that the agriculture sector in Ethiopia receives less than 10% of total bank loan with almost all banks prioritizing on other less risky and attractive sectors. IMF (2013) blamed the structure and regulation of Ethiopia’s financial system for the prevalent poor financial inclusion in Ethiopia; while World Bank (2014) attributed the problem partly to low level of branch outreach, and limited credit products.

Ameha and Peck (2010) elucidated regulatory and practical factors, which are associated to the nature of the agriculture and financial sectors, contributed to poor rural credit coverage in Ethiopia. They identified limited number of credit providers, narrow credit products, lack of inventory financing, illiquid and perishable collaterals and underdeveloped infrastructures as the major challenges.

Megersa (2013), Getaneh (2005), Yigerem (2010), Wiedmaier et al (2008) applauded the Ethiopian microfinance regulatory framework in ensuring institutional sustainability, while criticizing the one size fits all prudential regulation and quest for multi-tiered microfinance regulatory framework.

Stebek and Abdo (2013), Gebeyehu (2013), and Belay (2003) underlined the misconceptions related to the scope of rural land use rights envisaged under the FDRE constitution led to restrictive rural land administration practice in Ethiopia. They contended that such misconceptions led to enactment of laws that restrict farmers from using their holding right in its utmost limit including use of their holding right as collateral to raise finance.

Bisrat (2011) analyzed the legal and practical significance of warehouse receipt financing in Ethiopia and demonstrated that with banks being the only lenders using warehouse receipt, it is hardly possible to make smallholder farmers beneficiaries from the scheme given the limited rural accessibility of Ethiopian banks. Accordingly, he recommended for the involvement of MFIs in the warehouse receipt financing scheme. He also questioned the law that prohibits warehouse operation in business setup other than Share Company, private limited company, public enterprise and cooperatives as restrictive and unreformed.

Gikey (2018) assessed the proposed movable property security rights proclamation and argues that while the anatomy of the draft law and its general approach are consistent to the theme of enhancing access to credit, it defeated the purpose of comprehensive secured transaction law by adopting personal property security right approach in exclusion of security rights in immovable property from its umbrella.

However, the focus of the existing literature is economic analysis of access to credit with significant gap in analyzing the legal and institutional frameworks. While at ANRS level no comprehensive study is conducted to demonstrate the status of SSFs' access to credit in the region and identify the prevalent bottlenecks. Accordingly, this research tries to scrutinize microfinance, banking, rural land holding, security rights, insurance, warehouse receipt system, and similar regulatory and institutional frameworks in light of ensuring access to credit in Ethiopia in General and ANRS in Particular.

### **1.7. Methodology of the Study**

The purpose of this research is to analyze policies, laws and institutional frameworks that affect SSFs' access to credit. Extensive analysis of microfinance, banking, security rights, insurance, warehouse receipt and rural land holding policies and regulations is conducted to identify the barriers and gaps in policy and regulatory frameworks. The major national policies including ADLI, PASDEP, SDPRP, and NFIS are assessed to elucidate the priorities and strategic directions of the country to ensure SSFs access to credit. Credit inclusion aspects of NBE Directives are also analyzed under this study.

Primary data is also collected through institutional based questioner and interview on banks, MFIs, NBE, Ministry of Agriculture, and ANRS Bureau of Agriculture to demonstrate the impact that the aforementioned legal and institutional frameworks created on SSFs' access to credit. Target banks for this study namely CBE, and Abay Bank SC are selected based on their scale of operation in ANRS, while Wogagen Bank is chosen randomly. The following specific research methodologies are employed to answer the research questions identified:

- i. Institutional based questioner and interview is conducted on CBE, Abay Bank, Wogagen Bank, DBE, ECX Authority, ACSI, NBE, MOA, and ANRS Bureau of Agriculture to:
  - elucidate the credit policy of FIs in terms of providing credit products for SSFs;
  - To enlist regulatory and institutional barriers that hurdles FIs from providing wide range of credit products for SSFs; and

- To analyze as to whether the existing credit products are adequate and responsive to the demand of SSFs.
- ii. Reports of NBE, commercial banks, ACSI, World Bank, MOA, ANRS Agriculture Bureau and other organizations are assessed thoroughly to assess as to whether there is adequate credit supply for SSFs in ANRS and in Ethiopia at large.
- iii. An in-depth review and analysis of literature is conducted to elucidate the overall background about SSFs' access to credit.

### **1.8. Scope and Limitation of the Study**

The study will assess the policy, legislative and institutional framework governing SSFs' access to bank and microfinance credit in Ethiopia at large and in ANRS in particular. Accordingly, the study is limited to assessment of bank and microfinance credit facilities to SSFs and does not discuss informal credit and credit from other FIs. The study covers only SSFs and does not cover commercial farmers. For the purpose of this paper SSFs are those farmers that have no business license or investment permit and produce crops on a small piece of land without using advanced and expensive technologies.

### **1.9. Organization of the Thesis**

The thesis is organized under six chapters. Chapter one constitutes an introduction, which comprises mainly background, literature review, statement of the problem, objectives, significance, the scope and methodology of the study. Chapter two extensively discusses the policy considerations related to SSFs' access to credit in Ethiopia. While under chapter three banking and microfinance regulatory framework is scrutinized in light of insuring SSFs' access to credit. Chapter four assesses institutional frameworks governing SSFs' access to credit in Ethiopia. Chapter five evaluates the status of SSFs' credit coverage in Ethiopia and analyzes the corresponding barriers towards ensuring access to credit for SSFs. While Chapter six expounds SSFs' access to credit in ANRS elaborating the successes and failures in ensuring access to credit in the region. Finally, the thesis concludes with a set of recommendations and interventions that should be taken to resolve the problems identified by the study.

## Chapter Two

### Small Scale Farmers Access to Credit in Ethiopia; Policy Considerations

FDRE developmental policies and strategies recognized the role of credit inclusion to ensure agricultural development and poverty reduction. In consideration of the overreaching role of agriculture in the economy, development policies<sup>16</sup> prioritized the need for an improved rural credit in the transformation of the traditional small scale peasantry farming in Ethiopia. However, most of policies and strategies are limited to generic recognition of the need for an improved credit for SSFs and failed to provide details of strategies on the execution of the general aspirations. Absence of subsequent programs of actions or detailed roadmaps poses a challenge to understand the implementation directions of generic aspirations.

#### 2.1. Agriculture Lead Industrialization Policy and Strategy

ADLI was adopted with a major objective of reducing pervasive poverty through transformation of smallholder dominated peasantry agriculture.<sup>17</sup> ADLI identified affordable credit delivery instrumental to develop the capacity of SSFs through the application of technology extensions, improved seeds, and fertilizer.<sup>18</sup> MFIs were mandated to play significant role in rural financial intermediation as banks were considered unsuitable to reach SSFs due to the risky nature of SSFs financing.<sup>19</sup> Coordinating banks and rural FIs, diversification of microcredit products, and introduction of crop insurance scheme were identified as areas of improvement.<sup>20</sup>

ADLI mandated NBE to develop an appropriate legal framework to promote the development of rural banks and coordinate their operations. However, NBE failed to introduce separate rural financing regulatory framework that establishes rural banks or encourage existing banks to engage in rural credit delivery services. Despite ADLI's generic aspiration, a framework that enables banks to deliver rural credit through the intermediation of MFIs and cooperatives is not yet developed.

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<sup>16</sup> MOFED, "Government of FDRE Rural Development Policy and Strategies", (November 2002), MOFED, "SDPRP", (July, 2002), FDRE National Planning Commission, "GTP II of Ethiopia", (2015)

<sup>17</sup> FDRE Rural Development Policy and Strategies, n-16 at 10

<sup>18</sup> FDRE Rural Development Policy and Strategies, n-16

<sup>19</sup> FDRE Rural Development Policy and Strategies, n-16 at 48-51

<sup>20</sup> FDRE Rural Development Policy and Strategies, n-16 at 60-61

## **2.2. Sustainable Development and Poverty Reduction Program**

SDPRP outlined agricultural development as one of the key measures to fight against poverty and ensure sustainable development.<sup>21</sup> Commercialization of agriculture through increasing marketable output and decreasing corresponding self-consumption ratio was the target to transform the economic sector. Extension of credit to SSFs was viewed as an instrument to realize commercialization of agriculture. SDPRP underlined “lack of financial resources threatens farmers' productivity and put them into a vicious circle from which it is almost impossible to extricate them”.<sup>22</sup> Accordingly, development of strong rural financial system that enables accumulation of capital, which in turn can be used to develop other non-agricultural sectors, thereby help to attain overall accelerated and sustainable economic development.<sup>23</sup> Taking account formal banks in the country are not in a position to extend loans and credits due to high coast of transaction; SDPRP recommends extensive application of rural finance through MFIs.<sup>24</sup>

## **2.3. Plan for Accelerated and Sustainable Development to End Poverty**

Understanding the central role of agriculture to the overall economic growth, PASDEP pledged its focus to commercialization and intensification of agriculture development through introduction of high yielding technologies supported by agricultural research and extension services.<sup>25</sup> Improving rural financial services through development of MFIs was identified as a pillar to enhance agricultural commercialization, which was missing in the previous development endeavors.<sup>26</sup> PASDEP sets a financial strategy that geared towards ensuring a favorable environment for the banking sector through reducing information asymmetry, strengthening credit information sharing system, encouraging loan repayments and creating internal dynamism.<sup>27</sup> PASDEP tasked MFIs with a mission to expand financial services to low-income groups who are not eligible for bank credit. PASDEP underlined the need for financial education and skills development to tackle problems related to capacity to utilize funds and mandated NBE to take necessary measures towards creating competitive FIs. However, most of the aspirations under PASDEP are not supported with detailed implementation plans and regulations. The

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<sup>21</sup> SDPRP, n-16 at V

<sup>22</sup> Ibid

<sup>23</sup> Ibid

<sup>24</sup> Ibid

<sup>25</sup> MOFED, “Plan for Accelerated and Sustained Development to End Poverty”, (September, 2006). 67

<sup>26</sup> PASDEP, n-25 at 60

<sup>27</sup> Ibid

National financial literacy development program is not yet designed and implemented. In terms of building competitive FIs, particularly in rural areas, there are only limited regional governments owned MFIs that operate rural credit delivery services.

#### **2.4. Growth and Transformation Plans**

GTP I took a major shift towards intensification of large scale commercial farming and private sector investment.<sup>28</sup> Scaling up of best practices from model farmers and entrenching specialization among SSFs was the fundamentals of the agricultural development program of GTP I. Diversification of income of SSFs from non-farm income generating activities was also the other strategic direction of GTP I. With the focus on private sector investment in the agricultural sector, GTP I failed to pledge attention for SSFs' access to credit. Credit delivery for SSFs is barely cited as part of the safety net program and not overall agricultural sector development. Following GTP I, Development Bank of Ethiopia turned its attention to financing large scale farming as a strategic lender.<sup>29</sup>

GTP II was adopted in 2015 to ensure economic structural transformation and sustain accelerated growth towards the realization of the national vision to become a low middle-income country by 2025.<sup>30</sup> GTP II underlined fast transformation of smallholder farmer production units and addressing the challenges of innovations, technology adaptation, input supply, and expanding financial access through inclusive finance provision mainly through MFIs.<sup>31</sup> In this regard it was planned to expand branches of MFIs at kebele level through provision of incentives during the implementation timeframe of GTP II.<sup>32</sup>

#### **2.5. Homegrown Economic Reform Program**

The new and yet not applied home grown economic reform program emphasized on increment of agricultural production through supplying of modern agriculture inputs to SSFs and developing their capabilities.<sup>33</sup> Lack of credit facilities is identified as the major factor for underdeveloped agricultural practices in the country.<sup>34</sup> The previous trend of spending domestic credit facilities on public enterprises is considered one of the contributing factors towards limited

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<sup>28</sup> MOFED, "GTP I, 2010/11-2014/15", (2010), 8

<sup>29</sup> A Short Guide to Access DBE Loans, available at <file:///C:/Users/user/Downloads/DBENewPolicyEng.pdf>

<sup>30</sup> FDRE National Planning Commission, "GTP II", (September 2015). 16

<sup>31</sup> GTP II, n-29 at 27

<sup>32</sup> GTPII, n-29 at 23

<sup>33</sup> FDRE Office of the Prime Minister, "Home Grown Economic Reform Agenda", (August 2019).26

<sup>34</sup> Ibid

credit opportunities for the private sector.<sup>35</sup> Legislative reform towards the introduction of rural land lease right system that allows farmers to use their land use right as collateral to borrow credit is identified as one of the strategic pillars.<sup>36</sup> Introduction of micro loan and micro-insurance legal framework is also identified as the other strategic plans.<sup>37</sup>

## **2.6. National Financial Inclusion Strategy**

NFIS was developed after an extensive analysis on the status of financial exclusion in Ethiopia and provides a cogent framework for financial inclusion based on the developmental priorities of the country.<sup>38</sup> NFIS aims to improve access to and usage of formal financial services through ensuring adequate and suitable financial products, improving infrastructure, building strong financial consumer protection and developing financial capability.<sup>39</sup>

NFIS depicted underdeveloped infrastructure, inadequate supply of suitable products, geographic inaccessibility of formal financial services and low level of financial awareness are the major challenges impeding financial inclusion.<sup>40</sup> Improving credit infrastructure through holistic revision of institutional and regulatory constraints including designing of movable property security rights regulatory framework and electronic based collateral registry system was identified one aspect of strategic pillars.<sup>41</sup>

All the policies and strategies emphasized on the need to improve access to credit to the agriculture sector; however, there is inconsistency among such policies in terms of priority given to whether SSFs or commercial farming. ADLI and SDPRP prioritized on SSFs' development through an improved SSFs financing scheme. While, PASDEP and GTP turned their focus to commercialization of agriculture and large scale commercial farming, NFIS is generic and does not give special dedication for SSFs or agriculture for that matter.

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<sup>35</sup> Ibid

<sup>36</sup> Ibid

<sup>37</sup> Ibid

<sup>38</sup> NBE, National Financial Inclusion Strategy, (April 2017) .V

<sup>39</sup> Ibid

<sup>40</sup> NFIS, n-38 at 11

<sup>41</sup> NFIS, n-38 at 10

## Chapter Three

### Credit Inclusion Aspects of Microfinance and Banking Regulation in Ethiopia

#### 3.1. Introduction

Financial sector regulation plays significant role to ensure inclusive and affordable finance through protection of consumers against inappropriate products, deceptive practices, and aggressive collection practices.<sup>42</sup> However, financial inclusion, without good quality of supervision and regulation, has been traditionally considered as a contributor to higher credit risk and the trend is strict regulation of credit operations.<sup>43</sup> Ensuring credit inclusion through provision of basic financial services for the poor while maintaining financial stability poses significant challenge in designing of sound financial policy and regulation. Prudential regulation and supervision, which involves mandatory minimum capital, capital adequacy, liquidity management ratio, asset quality standard and similar controls serves to ensure financial soundness.<sup>44</sup> A sound financial regulation strives to ensure financial outreach and inclusion while maintaining sustainability and health of FIs.<sup>45</sup>

The financial sector in Ethiopia is highly regulated with limited competition and closed for foreign financial operators. The regulatory framework that governs the financial system, among others, consists of NBE Establishment Proclamation No. 591/2008, Banking Business Licensing and Supervision Proclamation No. 592/2008 as amended by Proclamation No. 1159/2019, Microfinance Business Licensing and Supervision Proclamation No. 626/2009 and series of NBE directives.<sup>46</sup>

#### 3.2. Microfinance Business Regulation

Microfinance refers to a small-scale financial service, including the provision of small loans and savings services to low-income clients who cannot access conventional bank credit.<sup>47</sup> Microfinance is a useful means of intervention to realize Ethiopia's development strategy and

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<sup>42</sup> Naoyuki Yoshino and Peter Morgan, "Overview of Financial Inclusion, Regulation, and Education," (September 2016), 591 ADBI Working Paper Series.28

<sup>43</sup> United Nations Economic and Social Commission for Asia and the Pacific, "Financial Regulatory Issues for Financial Inclusion", (April 2017) 1, available at [file:///C:/Users/user/Downloads/S6\\_Regulatory-Issues-for-FI.pdf](file:///C:/Users/user/Downloads/S6_Regulatory-Issues-for-FI.pdf) last accessed 09/10/2019

<sup>44</sup> Anand Sinha, "Financial Sector Regulation and Implications for Growth", (November 2011), 62 BIS Papers.47

<sup>45</sup> UNESCAP, n- 43 at 1

<sup>46</sup> Yigrem Kassa, "Regulation & Supervision of Microfinance Business in Ethiopia; Achievements, Challenges & Prospects", (2010). 34

<sup>47</sup> Bornstein D, n-11 at 26

reduce poverty through provision of credit to the poor who are unable to offer collateral to access formal banking loans.<sup>48</sup> Almost all rural development policies and strategies of Ethiopia considered microfinance as indispensable mechanism to ensure subsistence farmers access to farm inputs including improved seeds, fertilizer and production tools.<sup>49</sup>

In Ethiopia, before the coming to effect of Microfinance Licensing and Supervision Proclamation NO 40/1996, credit extension to SSFs was mainly undertaken by cooperatives and NGO Microcredits. However, NGO based microcredit was characterized by highest rate of non-repayment, fragile governance structure, only limited to credit delivery and unsustainable.<sup>50</sup> Proclamation No 40/1996 and subsequent Amendment Proclamation NO 626/2009 along with series of NBE directives laid the ground for the establishment and operation of complete MFIs that engage in a full scale financial activity. Microfinance Business Licensing and Supervision Proclamation NO.40/1996 was replaced by Proclamation No. 626/2009 which defines microfinance business as the provision of financial services such as accepting savings, extending credit, drawing and accepting drafts payable, and provision of money transfer services.<sup>51</sup>

Transformation of MFIs from mere credit delivery institutions into full-fledged FIs necessitated prudential regulation in order to prevent a systemic failure of the financial system and protect depositors' savings. However, inappropriate regulatory approach leads to misallocation of scarce resources in the attempt to impose prudential standards and requirements.<sup>52</sup> Rather than providing one size fits all type of regulation for all varieties of MFIs, introduction of tiered regulation based on the nature and risk bearing potential of MFIs is significant.<sup>53</sup> A tier based regulation approach recommends gradual regulation including minimum capital, capital adequacy, and organizational setup of rural MFIs depending on their size and risk

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<sup>48</sup> Fekadu Yehualashet, "Outreach Services and Sustainability; the Case of Amhara Credit and Saving Institution", (June, 2011 ), MA Thesis, Addis Ababa University

<sup>49</sup> ADLI, SDPRP, GTP I, and GTP II, n-16

<sup>50</sup> Fite, M. D, "Strengthening Regulation and Supervision of Microfinance sector for Development in Ethiopia", (2013), Law, Soc Just & Glob Dev J. 13

<sup>51</sup> Microfinance Business Licensing and Supervision Proclamation, 2009, Proc. No. 626/2009, Federal Negarit Gazette, 15<sup>th</sup> Year No.33, Article 2(10)

<sup>52</sup> WB Group & IMF(2010), n-10 at 197

<sup>53</sup> Patrick Meagher, "Microfinance regulation in South Africa: A comparative perspective", (2002), 57 Development Bulletin.48-52

exposure.<sup>54</sup> Many of developing and transition countries designed tiered regulation using a variety of regulatory techniques to encourage commercialization of MFIs, institutionally support MFIs, allow non-profit MFIs to function without difficulty, oversee the conduct of micro lenders and give funding facilities for MFIs.<sup>55</sup> A case in point is Bangladesh which regulates MFIs depending on the institution's size and risk bearing potential.<sup>56</sup> The risk bearing potential of MFIs which depend on donors, MFIs that depend on money from their members, and MFIs that leverage money from the public pose different level of risk that begs for different levels of regulation.<sup>57</sup>

In Ethiopia similar prudential regulation related to entry, organizational setup, interest rate, and capital requirements is adopted irrespective of the risk bearing potential of particular MFIs. The law made saving mobilization the sole source of microfinance funding as all MFIs are required to be formed in a share company format. While, regulation can contribute for the realization of sustainable MFIs, the process of integrating MFIs in a prudential regulation must be a gradual one.<sup>58</sup> Tiered regulation that involves defining of different tiers of financial institutions with different degrees of regulatory requirements based on risk bearing potential is necessary to foster competition and outreach.<sup>59</sup> MFIs that engage in financial intimidation service other than credit delivery need prudential regulation. However, non-deposit taking credit delivery microcredit institutions should be regulated in a relaxed fashion to ensure credit inclusion.

### **3.2.1. Organizational Structure Regulation**

Microfinance Licensing and Supervision Proclamation 626/2009, and 40/1996 require MFIs to be constituted only in the form of share companies in accordance with the commercial code of

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<sup>54</sup> Ian Davis, "Rural Banking; Designing an Effective Legal Framework for Microfinance", (2009), 2 BUS. INT & the Law J .2. 399

<sup>55</sup> Alliance for Financial Inclusion, "the AFI survey on financial inclusion policy in developing countries: Preliminary findings", (2010), 7, available at <<http://www.g24.org/Workshops/afisur.pdf>> , last accessed 18/11/2019

<sup>56</sup> Bangladesh Micro Credit Regulatory Authority Act, (2006), Available at <http://www.microfinancegateway.org/>

<sup>57</sup> Hennie Van Greuning et al. , "a Framework for Regulating Microfinance Institutions", (Dec. 1998), I, available at [http://www.mfc.org.pl/doc/backgroundmaterials/A\\_Framework\\_for\\_Regulating.pdf](http://www.mfc.org.pl/doc/backgroundmaterials/A_Framework_for_Regulating.pdf)

<sup>58</sup> Robert Peck Christen & Richard Rosenberg , The Rush To Regulate: Legal Frameworks For Microfinance, (2000), Occasional Paper No. 4, CGAP, Washington, DC

<sup>59</sup> Joselito Gallardo, Korotoumou Ouattara, Bikki Randhawa, and William F. Steel, "Comparative Overview of Micro Finance Regulatory Framework issues in Benin, Ghana and Tanzania," (2005), Africa Region Financial Sector Group Financial Sector Operations and Policy Department of the WB, ix

Ethiopia.<sup>60</sup> Proclamation No.40/1996 made a swift overhaul of NGO micro credits as it requires MFIs to be established in the form of commercial business organizations. The move towards commercialization is too broad in a sense that, unlike many jurisdictions that allow NGO MFIs to engage in credit provision business, it outlaws any type of service with NGO and other organizational setup in Ethiopia. However, regulatory frameworks designed for objectives other than regulation of deposit taking MFIs often result in standards that are disproportionately restrictive and unmanageable.<sup>61</sup> Complete ban of NGO based credit institutions creates adverse impact on credit accessibility for the poor by closing the windows through which NGO owned micro-credits operate. NGO MFIs with poor friendly credit policies constitute a useful complement to regulated MFIs, particularly in an economic environment like Ethiopia where there is high excess demand for microfinance and where outreach is low and demand for microcredit cannot be satisfied.<sup>62</sup>

### **3.2.2. Foreign Ownership Restrictions**

Only Ethiopian nationals and/or organizations that are fully owned by Ethiopian nationals and registered under Ethiopian laws with their head office in Ethiopia can be shareholders of micro-finance in Ethiopia.<sup>63</sup> Recent reforms under Banking Amendment Proclamation No 1159/2019 allowing foreign nationals of Ethiopian origin and organizations fully or partially owned by foreign nationals of Ethiopian origin to acquire shares in the Ethiopian banks or open banks failed to include MFIs. Foreign capital restrictions poses significant impediment for MFIs to raise adequate funding that enables them to operate a wide range of credit intermediation with geographic outreach. The foreign ownership and capital restrictions, forced NGOs to find loopholes of maintaining their involvement in the sector that in turn results in lack of transparency in capital ownership. Some MFIs equity structures are sponsored by foreign donors with nominal shareholders who are not investing their own capital.<sup>64</sup> This arrangement makes nominal shareholders to run as fronts, while the real owners are not listed as shareholders as they

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<sup>60</sup>Proclamation 626/2009, n-51, Articles 2(3), 2(11)

<sup>61</sup> Joselito Gallardo et al, “Comparative Overview of Micro Finance Regulatory Framework issues in Benin, Ghana and Tanzania”, (2005), Africa Region Financial Sector Group Financial Sector Operations and Policy Department of the World Bank, ix

<sup>62</sup>Fite, n- 50 at 20

<sup>63</sup> Licensing and Supervision of Micro Financing Institutions Proclamation, 1996, Proc. No. 40/1996”, Federal Negarit Gazeth , 2<sup>nd</sup> Year No. 30, Article 2(2) and n-58, Article 2(3)

<sup>64</sup>Bekele Shiferaw &Wolday Amha, “Revisiting the Regulatory and Supervision Framework of the Micro-finance Industry in Ethiopia”, (2001), NOR.CENT.for.INT.ENV&DEV.ST.30

are foreign nationals. Shareholders are the only eligible to be board members that in turn exclude donors that provide large amounts of equity to MFIs from being represented as shareholders, board members, or in management.<sup>65</sup> Absence of private capital in the industry and dominance of shareholders who may not have strong economic incentives to strive for excellence and serious interest for the success of the microfinance business contributes for the underdevelopment of the sector.<sup>66</sup>

### **3.2.3. Capital Related Regulations**

Capital regulations in the form of minimum capital and capital adequacy control are indispensable regulatory instruments that ascertain the financial competence of new entries to provide sustainable financial intermediation. Too high minimum capital requirement may discourage new entrants and thereby affect financial inclusion towards the poor, while too low minimum capital requirement makes eligible everyone to establish a deposit taking financial institution thereby challenging both the financial soundness of the system and expose depositors for financial risk.

In the Ethiopian case, Minimum Capital Requirements Directive No MFI/27/2015 requires at least 10 million Ethiopian Birr paid-up capital to commence microfinance business and the existing MFIs are also under obligation to raise their capital to 10 million until 2021.<sup>67</sup> Capital adequacy regulation is another capital related prudential regulation that has significant bearing on access to finance. NB Directive NO MFI/27/2015 requires every MFI to maintain at least 12% of their capital to total risk weighted assets. MFIs are subject to one and the same capital requirement irrespective of their size and risk bearing potential. Capital requirements are applicable to all types of MFIs irrespective of whether they are deposit taking or mere credit delivery institutions. Increase in the minimum capital requirement may be burdensome for new entrants, while it may not pose significant impact on already established big MFIs like ACSI.<sup>68</sup> Minimum capital and capital adequacy requirements should focus primarily on the risk of a run on MFI by requiring differing levels of capital for different forms of MFI assets rather than setting a one size fits all capital requirements for all types of MFIs like the case of Ethiopia.

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<sup>65</sup> Commercial Code of Empire of Ethiopia, Negarit Gazette, 19th Year No.3, Article 347

<sup>66</sup> Ibid

<sup>67</sup> NBE, Minimum Capital Requirements Directive No MFI/27/2015, Article 4

<sup>68</sup> Interview with Tewabe Aysheshim, Training and Research Directorate Director at ACSI, Conducted on 12/30/2019, Bahirdar

### 3.3. Banking Business Regulation

Banking Business Licensing and Supervision Proclamation No 84/1994 marked a new chapter in the development of banking industry in Ethiopia. Since 1991, NBE undertook substantial banking sector reform to ensure the development of the sector. Banking and Insurance Business Licensing and Supervision Proclamation No. 84/1994 and the subsequent Banking Business Licensing and Supervision Proclamation NO 592/2008 along with series of NBE Directives make a comprehensive body of banking business regulation in Ethiopia. NBE regulates banks with the aim of insuring sustainability and soundness while reducing systematic risk as envisaged under Proclamation No. 592/2008.<sup>69</sup>

Banking regulation in Ethiopia failed to envisage developmental objectives that can create an enabling environment for banks to operate rural credit intermediation. Lack of enabling regulatory framework created an opportunity for banks to adopt a rigid loan appraisal policy that excludes farmers. With no special credit policy or regulation that sets out details of rural credit intermediation for banks, banks use similar collateral based credit policies just like other sectors.<sup>70</sup> However, farmers cannot afford to borrow credit in compliance with the strict loan appraisal policies of particular banks. Nature of collaterals, size of microcredit, its duration, terms and conditions of repayment require separate enabling policy and regulation for rural banking in Ethiopia. Cultural change on the part of financial regulators is necessary, because the existing banking regulatory norms frequently do not meet the credit needs of the rural poor.<sup>71</sup>

Proclamation 592/2008 limits foreign nationals and/or banks from engaging in banking business conditions which is the main contributor to the concentration of the banking services and lack of competition. Lack of competition can cause financial exclusion as monopolies are not under pressure to deliver competitive credit facilities at affordable price. The increase in the minimum capital requirement to Birr 500 million in 2011 forced Private Banks to raise their paid up capital in order to increase their single borrower limit and hence scaled up their loans portfolio to the large and corporate entities away from the small borrowers.<sup>72</sup> It also constrains new banks from joining the industry that in turn creates market monopoly and lack of competition<sup>73</sup>

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<sup>69</sup> Melesse Asfaw, "Financial Regulation and Supervision in Ethiopia", (2014), 5 J.ECO.SUST.DEV17.64

<sup>70</sup> Interview with Mr. Tesfahun Tiruneh and Mulugeta Chekol, "Customer Relations Manager at CBE and Appraisal and Loan Recovery Manager at Abay Bank respectively", Conducted on 09/01/2020 and 10/01/2020

<sup>71</sup> Yoshino and Morgan, n- 49 at 18-19

<sup>72</sup> Getnet Alemu, "Financial inclusion, regulation and inclusive growth in Ethiopia," (November 2014), 20

<sup>73</sup> Ibid

## Chapter Four

### Institutional Framework

The type of institutional vehicle used to undertake rural credit intermediation and the agency that regulates such institutions is the central issue that determines the overall success or failure of any rural credit inclusion endeavor.<sup>74</sup> Public authorities often lead the establishment of specialized banks and categorization of FIs to achieve specific policy goals.<sup>75</sup> Different institutional setups including community rural banks, MFIs, agricultural banks, central banks, rural credit cooperatives, and commercial banks play a role in the sea of rural credit market. Analysis of the typical goals and roles of different kinds of FIs is important to understand their current performance and recommend working institutional reforms. In Ethiopia, while, commercial banks, MFIs and DBE are the available credit vehicles that need institutional assessment, NBE is the sole supervisor of all FIs.

#### 4.1. National Bank of Ethiopia

National Bank of Ethiopia is the sole regulator of FIs in Ethiopia with separate banking, insurance and microfinance business supervision directorates.<sup>76</sup> NBE regulates MFIs with a direction and mind setup of bank regulation that mainly aspires for financial soundness, profitability and risk avoidance on the cost of developmental goals.<sup>77</sup> However, considering the nature and purpose of MFIs and rural banks, countries established separate regulatory authority.<sup>78</sup> In this regard, Bangladesh is a pioneering example that established an independent microfinance regulatory authority with a mandate to support and supervise MFIs.<sup>79</sup> While in India a specialized National Bank for Agriculture and Rural Development supervises cooperative banks and regional rural banks.<sup>80</sup> Similarly in Ghana, a separate apex bank is established to supervise rural community banks and lend to those that face financial challenge.<sup>81</sup> Separate rural

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<sup>74</sup> WB Group & IMF, n-10 at 188

<sup>75</sup> Ibid

<sup>76</sup> Banking Business Proclamation, Proc. No. 592/2008, Federal Negarit Gazette, 14<sup>th</sup> year, No. 57

<sup>77</sup> Martina Wiedmaier et al., "Access to Finance in Ethiopia; Sector Assessment Study, (2008), GTZ Report 2. 44

<sup>78</sup> Heywood W. Fleisig and Nuria de la Peña, "Legal and Regulatory Requirements for Effective Rural Financial Markets", (2003), Center for the Economic Analysis of Law, 12

<sup>79</sup> W.A. Wijewardena, "Microfinance Policy and Regulatory Framework: Experience and Perspective of South Asian Region – Sri Lanka, Bangladesh, Nepal and India", (2004)

<sup>80</sup> Priya Basu, "Improving Access to Finance for India's Rural Poor", the World Bank, (2006), xviii

<sup>81</sup> Ajai Nair and Azeb Fisseha, "Rural Banking; the Case of Rural and Community Banks in Ghana", (WB 2010), Discussion Papers. 7

and agricultural bank supervisory authority presents an opportunity to give undivided attention and purposeful direction to integrated rural development through coordinating different rural development agencies. It also enables the supervisory authority to cater expertise with skills and knowledge of rural development and agriculture that can formulate financial policies and regulations in compatible with developmental aspirations. In India NBRAD played significant role to improve access to credit through designing uniform rural credit policies.<sup>82</sup> It also provides credit for promoting developmental programs for rural development; co-ordinates rural credit financing activities of all sorts of institutions engaged in developmental activities; prepares annual national rural credit plans; and promotes research in rural banking, and the field of agriculture and rural development.<sup>83</sup>

In Ethiopia, successful rural development financing requires overall regulation and supervision of financial institutions beyond one directional objective of ensuring financial soundness. A specialized regulatory institution that designs rural financing policies and guidelines, coordinates rural development financing institutions and programs, and extends credit for rural FIs can play significant role to create a better rural credit environment. Separate national bank for rural and agricultural development can serve as an organizational device to provide undivided attention, forceful direction and a pointed focus to the credit problems arising out of an integrated approach to rural development. It also enables to develop specialization for solving the problems relating to agriculture and rural development efforts.

## **4.2. Banks**

In Ethiopia institutional bottlenecks are not limited to the regulatory authority; rather neither there is separate rural bank nor do the existing commercial banks have separate units that design loan appraisal methodologies, which are peculiar and suitable for the rural mass.<sup>84</sup> DBE on the other hand is established with a mandate of financing viable investment projects with no special mandate to work on rural development.<sup>85</sup> With the existing banks not engaging in rural credit operations and no other separate bank mandated to undertake such operations, occurrence of market failure that needs a special government intervention is inevitable. Such government

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<sup>82</sup> Samydurai Balamurgan, "National Bank of Agriculture and Rural Development; in Socio economic Development, (2011, LAP. Lambert Academic Publishing), 154-157

<sup>83</sup> Ibid

<sup>84</sup> Interview with Mr. Tesfahun and Mr. Mulugeta, n-70

<sup>85</sup> DBE Reestablishment Council of Ministers Regulation, Reg. No. 83/2003, Federal Negarit Gazette, 9<sup>th</sup> year, No. 28, 2003, Article 6(1)

intervention could be either through direct involvement by establishing rural and agricultural banks and/or crafting a regulatory framework that encourages new entrants to engage in rural credit intermediation services. For instance in India there are a variety of rural and agricultural specialized banks ranging from the community level primary agricultural credit societies to regional and central land development banks.<sup>86</sup> While primary agricultural credit societies provide short and medium term credit at the village level, central cooperative banks arrange regular credit for primary credit societies and undertook ordinary commercial banking in rural areas. Regional rural banks on the other end provide agriculture oriented medium and long term special credit and banking facilities. There are also central and primary land development banks at state and district levels respectively that supply long-term credit to the farmer.<sup>87</sup> Whereas, in Ghana there are more than 127 rural community banks that provide credit intermediation service based on “credit with education” approach, where banks educate and sensitize potential clients for about six weeks before disbursing the loan.<sup>88</sup>

#### **4.3. National Financial Inclusion Council and Secretariat**

NFIS established a broad range of institutions including National Council for Financial Inclusion, which is chaired by the Prime Minister. The council constitutes members from different sector ministries and agencies including the minister of MOA, Commissioner of the National Plan and Commission, the Governor of NBE, Director of Ethiopian Developmental Research Institute, and representatives of MOFEC. The council is mandated to play active role in leadership and coordination of public and private stakeholders towards advancing financial inclusion in Ethiopia.<sup>89</sup> It is specifically mandated to formulate NFIS and secure government approval, secure political support for the implementation of NFIS action plan, monitor the implementation of the NFIs, set overall policy directions, determines and approves the reports, and leads legislative reforms intended to improve access to finance.<sup>90</sup> The Council Established a Secretariat housed under the NBE. The secretariat is tasked to undertake regular monitoring, documentation, reporting of the implementation of NFIS action plan. It is also mandated to build and maintain financial inclusion information database, set-up coordinators, propose improvement

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<sup>86</sup> Samydurai, n-82 at 127

<sup>87</sup> Ibid

<sup>88</sup> Nair and Fisseha, n-81 at 15

<sup>89</sup> NFIS, n-38 at 42

<sup>90</sup> Ibid

areas to the council, and carries out other activities given by the council. Financial inclusion steering committee consisting of members drawn from around 20 stakeholder institutions is also established with a mandate of consulting the council and the secretariat on a range of policy and strategic measures to be taken in order to implement the strategy.<sup>91</sup>

However, institutions do not work in synergy as each institution is confined with piecemeal and disorganized works. In this regards the NFIST, which has a duty to monitor the implementation of the Strategy, confirmed that it only works on development of financial infrastructures within its mandate and does not follow-up other institutions.<sup>92</sup> Lack of details of norms and codes of conducts caused lack of sustainable commitment on the side of committee based institutions. Successful implementation of rural credit inclusion requires decentralization of concerned institutional machinery and clear mechanism of coordination at local level along with local participation. NFIS, failed to forge some regional or local level institutional setup to implement the strategy.

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<sup>91</sup> NFIS, n-38 at 43

<sup>92</sup> Interview with Mr. Fikremarkos Abebe , Financial Inclusion Officer at NFIST of the NBE, Conducted on 15/01/2020, NBE Head Office

## **Chapter Five**

### **Small Scale Farmers Access to Credit in Ethiopia**

#### **5.1. General Overview**

Access to credit from formal FIs in Ethiopia is very low and below the average sub-Saharan index.<sup>93</sup> According to 2016 household survey on selected respondents, 45.7% of households face severe financial pressure to buy agricultural inputs, while the remaining 38.5 face moderate pressure to purchase agricultural inputs.<sup>94</sup> However, only less than 10 % of the adult population borrows money from formal FIs.<sup>95</sup> The 2019 WB Ease of Doing Business Index further demonstrated the difficulty in accessing credit from FIs as Ethiopia ranked 175<sup>th</sup> out of the total 189 countries in easiness of accessing credit.<sup>96</sup>

Agricultural financing in Ethiopia is characterized by gaps in terms of access to finance, product quality, and quantity with only MFIs operate in rural areas with a very narrow and short term credit facilities.<sup>97</sup> According to the NBE annual report during the second quarter of 2019, agricultural loans constitute only Birr 24.5 billion (5.5%) out of the total outstanding loans of Birr 448.4 billion.<sup>98</sup> With no commercial bank loan facilities for SSFs, the 5.5 % loan share is mainly distributed to commercial and large scale farming.<sup>99</sup> This figure is lower than the national target envisioned by NFIS, which is to improve the proportion of agricultural loans to total bank and microfinance loans from 10.4% by 2016 to 15% by 2020.<sup>100</sup>

#### **5.2. Microfinance Credit**

Microfinance institutions are the major rural credit providers in Ethiopia compared to other FIs particularly banks. According to NBE, MFIs distributed more than 50% of their outstanding microcredit to the agriculture sector in the last five years on average.<sup>101</sup> In Ethiopia, there were 38

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<sup>93</sup> Tilahun Dessie, “Access to Credit and the Impact of Credit constraints on Agricultural Productivity in Ethiopia: Evidence from Selected Zones of Rural Amhara,” (February, 2015), MS Thesis, Addis Ababa University.6

<sup>94</sup> Tewdros Hailu and Yishak Mengesha, “Rural Financial Services in Ethiopia: Some Evidence from a Household Survey”, Papers and Proceedings of the 9<sup>th</sup> Biennial AEMFI Conference, (November 23-26 2018, Jijjiga), 126

<sup>95</sup> WB Group, Measuring Financial Inclusion and the Fintech Revolution, (2017), Global FINDEX Database.77

<sup>96</sup> WB Group, “Comparing Business Regulation for Domestic Firms in 190 Economies”, 2019 Global Doing Business Index. 171

<sup>97</sup> Amheha and Peck, n-13

<sup>98</sup> NBE 2018/19 Second Quarter Report n-7 at.39,

<sup>99</sup> ACCSA , Business Finance Guide, (2016), 10 , available at file:///C:/Users/user/Downloads/Business-Finance-Guide.pdf

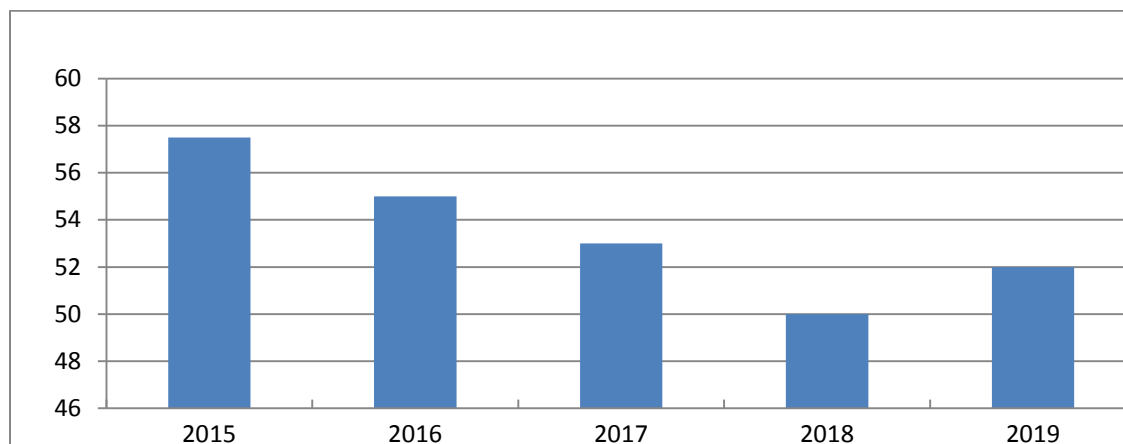
<sup>100</sup> NFIS, n-38 at 39

<sup>101</sup> NBE loan by sector database, See Annex 1,

MFIs with 933 branches and 1035 sub-branches respectively as of June 2019.<sup>102</sup> Regional government owned MFIs dominated the sector with 437 and 937 branches and sub-branches respectively.<sup>103</sup> In this regard, Amhara, Dedebit, Oromia, Omo and Addis Credit and Savings Institute together account for 90% of the total microcredit delivery in the country.<sup>104</sup> However, with a significant population growth in Ethiopia, the branch to population ratio of microfinance in Ethiopia is not yet proportional. A single microfinance branch remains burdened to entertain more than 100, 000 people while the existing microfinance outreach only covers around 15% of Kebeles on average.<sup>105</sup>

Product wise MFIs basically provide compulsory saving and group lending facilities. Compulsory savings involve mandatory deposits made for the purpose of enabling individuals or groups to qualify to receive loans from an authorized institution and to serve as collateral against the loans so obtained.<sup>106</sup> Individual lending was introduced only recently in the aftermath of amendment of Proclamation No.40/1996, and plays a minor role.<sup>107</sup>

**Percentage of microcredit for the agricultural sector in the last five years**



Source: Author’s computation from NBE Database, See at annex 2

<sup>102</sup> NBE, Microfinance Branch Database, Annex- 1

<sup>103</sup> Ibid

<sup>104</sup> Peter Mackie et al, “Microfinance and Poverty Alleviation in Ethiopia”, (2015), Ethiopia Country Report.12

<sup>105</sup> The Ethiopian Population is projected around 110, 000,000 according to the 2019 WB population projection, while there are around 15,000 Kebeles in Ethiopia

<sup>106</sup> Proclamation No 626/2009, n- 51, Article 2(4)

<sup>107</sup> Deutsche Gesellschaft für Technische Zusammenarbeit, “Access to finance in Ethiopia; sector assessment study”, (July 2008), at 26

### 5.3.Commercial Bank Credit

The Ethiopian commercial banking sector, as of December 2019, consists of 17 commercial banks among which 16 are privately owned and the remaining one is government owned CBE. The rising number of banks along with large scale branch expansions broadened their geographic reach over the past two decades thereby improving key access to finance indicators. The increase in bank branches from 2,208 five years ago to 4,757 branches substantially improved the population-to-branch ratio over the years, from a situation where each branch served 126,000 people back in 2008 to the current status where each branch is on average serving just 20,000 people.<sup>108</sup>

However, traditional bank branches are not a cost-effective channel to serve Ethiopia's large but mostly poor rural population.<sup>109</sup> According to the summery of loan products and conditions guide of 17 banks prepared by ACCSA, no commercial bank in Ethiopia offers credit for SSFs.<sup>110</sup> All the 17 banks covered by the guide provide credit only for commercial oriented sectors and require collateral amounting 70% to 200% of the loan granted.<sup>111</sup>

Banks neither offer credit using group guarantee model as collateral, nor do they use assets of farmers as security to extend credit.<sup>112</sup> It can be concluded that commercial banks in Ethiopia have no credit facilities for SSFs as all the respondent banks confirm they have no separate credit package for SSFs.<sup>113</sup> Applicants for agricultural loan are required to present certificate of land holding, investment permit, project study, and equity contribution cumulatively.<sup>114</sup> Banks have no separate loan conditions for SSFs and they use similar loan appraisal mechanisms just like other commerce oriented loans.<sup>115</sup> High quality collateral and guarantees as prerequisites, complicated procedures to access credit, and strict lending policy of FIs are some of the factors that hinder SSFs' access to bank credit.<sup>116</sup>

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<sup>108</sup> NBE, 2017/18 Annual Performance Report, (2018), 45

<sup>109</sup> Amha, and Peck, n-13 at 30

<sup>110</sup> ACCSA Business Finance Guide, n-99 at 10

<sup>111</sup> Ibid

<sup>112</sup> Table 1, Bank Credit Products for SSFs, See Annex 1

<sup>113</sup> Ibid

<sup>114</sup> Interview with Mr. Tesfahun Tiruneh and Mr.Mulugeta Chekol , n-70, and Interview with Mr. Addis Hassen, Litigation Manager at Wogagen Bank SC, conducted on 17/02/2020

<sup>115</sup> Ibid

<sup>116</sup> Etana Ayana, "Credit Policy, Financial Institutions and Private Investment in Ethiopia, 8

#### 5.4. Development Bank Credit

“DBE is a specialized FI established to promote the national development agenda through development finance and close technical support to viable projects from the priority areas of the government.”<sup>117</sup> In line with GTP II, the Bank provides finance to encourage investment in Commercial Agriculture, and Agro-processing Industries, while terminating provision of agricultural input loans for SSFs and started specializing in medium term credit.<sup>118</sup> Currently the Bank finances large scale irrigable and rain fed agricultural farms with minimum equity capital of Birr 7.5 million and above.<sup>119</sup>

DBE recently began a lease financing arrangement through which farmers can access machines such as tractors and combines.<sup>120</sup> However, the lease financing scheme is available only for farmers who registered a capital of ETB 500, 000.<sup>121</sup> DBE extends loan only for farmers who have more than 20 and 300 hectares of land for permanent crops and cereal crops respectively.<sup>122</sup> DBE requires first-degree collateral security for all loans, and in case of projects operating on rented premises additional collateral outside the project amounting for 100% of the loan.<sup>123</sup>

DBE is established with a mission to provide strategic investment credits to viable projects that contribute to the country's economic development.<sup>124</sup> DBE reestablishment regulation excluded SSFs, as it confined the credit operation of the bank only to the provision of investment loans for viable projects. DBE being the policy bank of the government, its credit policy changes depending on the policy directions of the government.<sup>125</sup> Following the introduction of GTP I, the focus of the government turned to commercial agriculture, agro processing, and manufacturing which in turn forced the bank to revisit its credit policy.<sup>126</sup> However, the drift in the government's strategic direction is overwhelming to the extent of sidelining SSFs from all of DBE credit facilities. DBE complained that it become impossible to recollect billions of its

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<sup>117</sup> DBE Loan Guide, n-29

<sup>118</sup> USAID, “ACSI”, (2006), Micro report No 58.13

<sup>119</sup> DBE Loan Guide, n-29

<sup>120</sup> Interview with Abol Mehammed, Senior Loan Officer at DBE Bahirdar Branch, Conducted on 30/12/2019, Bahirdar

<sup>121</sup> Ibid

<sup>122</sup> Ibid

<sup>123</sup> ACCSA Business Guide, n-99

<sup>124</sup> Regulation No.83/2003, See n-85, Articles 5 and 6

<sup>125</sup> DBE Loan Guideline, n-29

<sup>126</sup> Ibid

credit extended for the agricultural sector.<sup>127</sup> DBE planned to make its loans for agriculture more stringent as its debtors who took credit in a lease financing arrangement failed to pay their debt.<sup>128</sup>

### **5.5.Barriers to Small-Scale Farmers Access to Credit in Ethiopia**

Several cross-cutting factors ranging from policy and regulatory constraints to the unattractiveness of the agriculture sector marred by traditional production and climate shock contributed to poor rural credit inclusion in Ethiopia.<sup>129</sup> Low level of competition in the financial sector, gaps in regulation of FIs, and high transaction costs have led to limited financial product offering in rural areas.<sup>130</sup> Uneconomic land holding system, lack of credit history, rigid collateral requirements, non-existent SSFs' insurance package, underdeveloped infrastructure and high transaction cost are the major impediments contributing for the existing poor rural finance in Ethiopia.<sup>131</sup>

#### **5.5.1. Restrictive Rural Land Use Legal Framework**

The FDRE constitution exclusively vested ownership right over rural and urban land in the state and peoples of Ethiopia.<sup>132</sup> Land being the common property of nations, nationalities and peoples of Ethiopia, it cannot be subjected to sale or other means of exchange.<sup>133</sup> While the constitution prohibits sale or mortgage of ownership right over a land, it vests the right to usufruct over rural land for the Ethiopian peasants and pastoralists.<sup>134</sup> FDRE RLUAP No 456/2005 expressly vested usufruct right over rural land to farmers; however, it is silent as to whether farmers can use their holding right as collateral. While the proclamation expressly allows land holders to lease their right or enter into a sharecropping agreement with investors, the use of land holding right as collateral is not cited as one of bundles of rights.<sup>135</sup> Misconceptions of public ownership of land, which is envisaged under the FDRE Constitution, contributed to implementation of the law in a

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<sup>127</sup> Dawit Taye, ልማት ባንክ ከ 4 ቢሊዮን ብር በላይ ያበደረገው የሊዝ ፋይናንስ ችግር ገጥሞታል, Ethiopian Reporter, March 4

<sup>128</sup> Ibid

<sup>129</sup> Ameha and Peck, n-13 at 1&2

<sup>130</sup> Ameha and Peck, n-13 at 32

<sup>131</sup> Haileleul Getahun, "Financing Small Farmer Development in Ethiopia", (2001), International Conference on African Development Archives, Paper 42. At 4

<sup>132</sup> FDRE Constitution, 1995, article 40(3,4)

<sup>133</sup> Ibid

<sup>134</sup> Ibid

<sup>135</sup> FDRE RLUAP, Proc. No, 456/2005, Federal Negarit Gazette 11<sup>th</sup> year, No.44, Article 8

manner that extremely narrow the scope of land use rights in Ethiopia.<sup>136</sup> The constitution has been implemented with an understanding that it does not allow use of rural land holding right as collateral. The lack of clarity in the Ethiopian land holding policy and legislative framework related to use of rural land use right as collateral posed serious impediment towards credit inclusion as it led to confusion that use of rural land use right as collateral is prohibited.<sup>137</sup>

MOA is preparing RLUAP that expressly allows farmers to use their land in the form of collateral up to 10 years and provide perfection mechanisms for such purpose. Land use right based credit is effective after conclusion of collateral agreement over the use right and upon authentication of such agreement by the Woreda Land Use and Administration Bureaus. Ministry of agriculture also developed a National Rural Land Information System which is very vital in updating rural land transaction including security contracts over collateralization of rural land use rights.<sup>138</sup>

### **5.5.2. Underdeveloped Legal and Institutional Framework on Security Rights**

Strong real property and secured transaction legislative framework that expansively defines assets that can be used as collateral plays indispensable role in fostering access to credit. In modern systems, collaterals ranging from tangible property, such as tractors and processing equipment, livestock, land, and buildings to intangible property such as future crops or long-term contracts can serve as collateral.

In Ethiopia there was no legislative framework governing particulars related to use of movable property as collateral without dispossessing the holder until the introduction of Movable Property Security Rights Proclamation No 1147/2019. Although the Proclamation is a new introduction, which is not implemented, it recognized list of agricultural products including crops, future harvest, forest, timber, livestock, bees, poultry and rural land holding right as assets eligible for collateral.<sup>139</sup> The Proclamation reformed the traditional possession based pledge framework by introducing registration of security right as a perfection mechanism.

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<sup>136</sup> Elias N. Stebek and Muradu Abdo, “Property Right Protection and Private Sector Development in Ethiopia”, (2013), Private Sector Development Hub, ACCSA, 57

<sup>137</sup> LIFT, “Leveraging improved land security to improve access to credit: how the LIFT project in Ethiopia promotes financial inclusion”, (October 2017)

<sup>138</sup> Ibid

<sup>139</sup> Movable Property Security Right Proclamation No. 1147/2019, Federal Negarit Gazette, 25<sup>th</sup> year No.76, Article 2(26)

Security right over a movable property can be enforced against third parties only if notice as to the existence of security right is registered on the electronic collateral registry.<sup>140</sup> The credit has priority right over competing claimants, and can enforce his claim irrespective of in whose hand the secured property is and subsequent transfers.<sup>141</sup> The Proclamation established an electronic collateral registry system that receive, store, and avail information about encumbered assets.<sup>142</sup> However, Ethiopia being the third in the world in access to electricity deficit,<sup>143</sup> an exclusive electronic collateral registry with no parallel paper based registration is out of touch with the reality in Ethiopia. The rural population have no the necessary internet facility and know-how to check assets encumbered online before entering into any transaction over such assets.

NBE issued Operationalization of Movable Property Collateral Registry Directive No MCR/01/2020, which obliges lenders to register and verify the legal validity of every security agreement over a movable property.<sup>144</sup> However, the obligation of FIs should be limited to notice filling as leaving the whole registration process to FIs paves the way for FIs to restrict public accesses to reduce administrative costs.

The key legal elements for improving enforcement in secured rural credit lies in laws that permit non-judicial enforcement of claims over secured property in case of default.<sup>145</sup> Proclamation No 1147/2019 empowered secured creditors to obtain possession of the collateral in case of default without the need to go to court and with giving a 10 day notice.<sup>146</sup> The law gives huge relief for MFIs as MFIs were not eligible for extra-judicial enforcement scheme under proclamation No 97/1998.<sup>147</sup>

Respondent FIs declared that they do not extend credit to farmers using agricultural products, livestock and to some extent land use right.<sup>148</sup> Despite the registry that sets priority claims, it is difficult to trace and enforce claims in case the debtor sells agricultural products or livestock held as collateral. In the traditional Ethiopian market transactions with no receipt, it is impossible to trace to whom a certain agricultural product is sold and thereby enforce claims. Extending

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<sup>140</sup> Proc. 1147/2019, n-139, article 45

<sup>141</sup> Ibid

<sup>142</sup> Proc. 1147/2019, n-139, article 20

<sup>143</sup> WB, Institutional Bank for Reconstruction and Development, state of Electricity Access Report, (2017). V

<sup>144</sup> Ibid

<sup>145</sup> Fleisig and Peña, n-78 at 11

<sup>146</sup> Proclamation No 1147/2019, n-139, articles 81,82

<sup>147</sup> Property Mortgaged or Pledged with Banks Proclamation, Federal Negarit Gazette, 4th Year No. 16, Article s 3 &4

<sup>148</sup> See Table 1; Bank credit for SSFs; Annex 1

credit using agricultural products and livestock is not in banks' plan, even after the implementation of the movable property security rights law, as they still consider such business risky.<sup>149</sup> Further steps must be done in addition to the collateral registry to reduce risks arising from the perishable nature of such products.<sup>150</sup> The risk attached to perishability of agricultural products, and sell after collateral agreement cannot be resolved only by providing priority right, rather it also require standard warehouse receipt system and insurance schemes.

### **5.5.3. Underdeveloped small scale Farmers Insurance Framework**

In Ethiopia 50% of households who earn their livelihood from small scale farming and livestock breeding experienced bad harvest or significant loss of livestock in the last 5 years.<sup>151</sup> However, only less than 10 % of those households received compensation for bad harvest or significant loss of livestock.<sup>152</sup> Insurance products play a very important role in mitigating the high risk of the agricultural sector for both customers and FIs.<sup>153</sup>

The traditional indemnity based insurance is not feasible for countries like Ethiopia with large number of SSFs and underdeveloped insurance markets as it requires multiple field inspections to fix premiums and determine actual losses.<sup>154</sup> An alternative Index insurance, which is based on an index that is correlated with agricultural losses,<sup>155</sup> is an ideal model to overcome the problems of SSFs in Ethiopia. Under index insurance fragmented farms will be aggregated, for the purpose of fixing premium and compensation, based on rainfall during a defined period, yields sampled over a larger region, and remote sensing of vegetation conditions or flood extent. However, index insurance necessitates availability of adequate and quality data on agriculture and weather related indexes including rainfall and temperature predictions to fix proportional premium and compensation for damages.<sup>156</sup> In Ethiopia, lack of data makes the implementation of the index insurance package at SSFs' level very difficult.

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<sup>149</sup> Interview with Mr. Tesfahun , Mr.Mulugeta and Mr. Addis, n-114

<sup>150</sup> Ibid

<sup>151</sup> World Bank Group, Global Financial Inclusion Database, (2017), 83

<sup>152</sup> Ibid

<sup>153</sup> Ameha and Peck, n- 13 at 14

<sup>154</sup> Maria Castillo et al, "Index Insurance: Using Public Data to Benefit Small-Scale Agriculture", (2016), 9 INT Food and AGRI MANT REV A. 2

<sup>155</sup> Jon Hellin et al., "Scaling-up Agricultural Adaptation through Insurance Bringing together insurance, big data and agricultural innovation", (May 2017), 4

<sup>156</sup> Maria Castillo et al, n-154

Developing insurance industry capacity to scale index insurance for smallholder agriculture requires attention to incentives, support through public-private partnerships, and enabling regulatory frameworks.<sup>157</sup> In Ethiopia, the regulatory framework as envisaged under the 1960 Commercial Code is confined to indemnity based property insurance.<sup>158</sup> Index insurance requires special regulatory framework attached to its peculiar attributes. Unlike property insurance, liability under the index insurance model is determined based on the measured value of independent index and not based on the actual proof of a specified loss or an assessment of the insured's actual loss.<sup>159</sup> Under the Ethiopian insurance regime, however, premium and compensation is determined based on the statements made by the applicant and assessment of actual damage respectively.<sup>160</sup> Definition of index contracts, nature and description of index based insurance products, the contents and form of index insurance policy and the valuation methods are some of the issues that need to be dealt with separate regulation. There should also be clear product approval guideline through which insurers submit their product approval application to protect farmers from exploitative practices.

Another insurance related problem is attached to absence of micro-insurance regulatory framework. Despite NFIS's plan for the introduction of micro insurance package for the poor who cannot afford the conventional insurance; no micro-insurance regulatory framework is yet designed.<sup>161</sup> The Licensing and Supervision of Insurance Business Proclamation No. 86/994 govern all insurance activities in Ethiopia. The proclamation does not pledge separate definition of micro-insurance and failed to make any concessions for micro-insurance. Microfinance Business and Supervision Proclamation No 626/2009 expressly allowed MFIs to undertake micro-insurance business in accordance with a directive to be issued by NBE<sup>162</sup> However; no directive is issued to implement Proclamation No 626/2009 and NFIS through setting enabling detailed provisions.

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<sup>157</sup> Jon Hellin et al., n-155 at 10

<sup>158</sup> Commercial Code, n-63, Article 67

<sup>159</sup> Kenyan Insurance Regulatory Authority, The Kenyan Index Based Insurance Policy Paper, (2015)

<sup>160</sup> Commercial Code, n- 63, Articles 667,668

<sup>161</sup> NFIS, n- 38 at 20

<sup>162</sup> Proclamation No. 626/2009, n-51, Article 3(2(d))

#### 5.5.4. Lack of Warehouse Receipt Financing Scheme

A warehouse receipt is a document that provides proof of ownership of a specific volume of a commodity, with specific characteristics, that is stored in a specific warehouse.<sup>163</sup> Legally issued warehouse receipt can serve as collateral for accessing loans.<sup>164</sup> Farmers can store their agricultural products in a warehouse upon payment of fees and the warehouse in turn issue a receipt that can serve as a security for farmers to access credit from FIs. A well-functioning WRS provides farmers a choice to decide whether to sell their product immediately after harvest with lower price or to store it in a licensed store and apply for short term credit.<sup>165</sup> On the other end, WR is an ideal perfection mechanism for FIs through which agricultural products can serve to access loans from formal FIs.

Ethiopia introduced Warehouse Receipt Financing Proclamation No. 372/2003, which makes licensed warehouse operators the sole bona fide issuer of a valid WR.<sup>166</sup> The Proclamation allows any share company, private limited company, public enterprise, or cooperative society, complying with the requirements provided under the proclamation, to engage in a warehouse operation business.<sup>167</sup> However, warehousing business is not open for sole proprietors and other business organizations.<sup>168</sup> EACWSE and ECX were established by the Council of Ministers Regulation No. 331/2014 and Proclamation No 550/2007 respectively to provide an innovative warehouse management service. While EACWSE's WR operation has not still truly taken off, private warehouses are not accredited by the ECX Authority to issue WR.<sup>169</sup>

Currently ECX is the major warehouse operator that issues WR with all the odds. ECX provides storage services and issue WR only to members "for the purpose of exchange trading" and prohibits non-members from trading in the exchange.<sup>170</sup> SSFs are not beneficiaries of ECX market as they cannot afford to be member of ECX.<sup>171</sup> Any person seeking to be a member must maintain net worth equal to or in excess of 500,000 Birr and must pass the appropriate Member

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<sup>163</sup> Varangis, P. and D. Larson. "How Warehouse Receipts Help Commodity Trading and Financing", (1996) WB brief, 123

<sup>164</sup> Thomas Jayne & Alexander Sitko, "Agricultural Commodity Exchanges and the Development of Grain Markets and Trade in Africa: A Review of Recent Experience", (2014), Working Paper 88.

<sup>165</sup> International Maize and Wheat Innovation Center, Financial Products for Farmers and Service Providers Report from Ethiopia, (September 2015).20

<sup>166</sup> Warehouse Receipt Proclamation, Proc. No 372/2003, Federal Negarit Gazette, 10<sup>th</sup> year No. 2, Articles 6(1)

<sup>167</sup> Warehouse Receipt Proclamation, n-166, Articles 5 and 26

<sup>168</sup> Ibid

<sup>169</sup> Sally Pauw, Agricultural Commercialization in Ethiopia: A Review of Warehouse Receipts in the Maize, Wheat, Sorghum and Teff Value Chains,(August 2017), 3

<sup>170</sup> ECX Establishment Proclamation, Proc. No 550/2007, Federal Negarit Gazette, No 61, Articles 20, 24

<sup>171</sup> Jayne &Stinko (2014),N-164 at 22

Certification Examination administered by the Exchange.<sup>172</sup> In terms of the WR' current provisions, coffee and sesame can only be stored in an ECX warehouse for 20 and 30 days, respectively, before being exported.<sup>173</sup> In ECX WR financing system, a single receipt cannot be pledged for more than one loan account contrary to Proclamation No 1147/2019.<sup>174</sup> With the existing warehouse operators excluding SSFs, an initiative should be taken to establish a warehouse receipt system that is responsive to the needs of farmers. Farmers' cooperatives can serve as ideal institutions that need to be empowered and accredited to provide warehouse receipt service.

#### **5.5.5. Underdeveloped Credit Reference System**

Credit reference system involves fetching of comprehensive credit information derived from previous credit history, utility payments, and other assets and thereby exchange of such information among FIs. Such information induces FIs to expand responsible lending without being exposed to default risk through calculating risks. Respondent FIs confirmed information scarcity is one of the major factors that prevent banks and MFIs from lending to SSFs.<sup>175</sup>

NBE established credit reference bureau through Directive No CRB/01/2012 to build adequate, timely and reliable credit information about borrowers and ensure prudent lending decisions on the side of banks. This directive was repealed by Directive No CRB/02/2019 with an intention to broaden the scope of application of the credit reference system from just only banks to MFIs and capital goods finance companies. The Credit Reference Bureau is with a mandate to gather credit history of borrowers from each FI, systematize and share it among FIs. All FIs are required to register for credit information system by the Bureau and once registered to provide credit history of their borrowers. However, information is not available for FIs for free; rather any registered FI for credit reference purpose can access credit information upon payment of fee.<sup>176</sup>

The credit reference regulatory framework failed to create positive impact towards financial inclusion covering only 0.2 % of the Ethiopian adults.<sup>177</sup> Only 18 banks were covered by the credit reference system until April 2019 and MFIs were not beneficiaries of the system.

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<sup>172</sup> ECX Authority Directives 01/2008, Part Six, 6(1-4)

<sup>173</sup> Pauw, n-169 at 4

<sup>174</sup> Bisrat Mulugeta, "Warehouse Receipt System in Ethiopia: Its Legal and Practical Significance with Emphasis on Its Role in Securing Transactions", (2011), LLM Thesis, Addis Ababa University.80

<sup>175</sup> Interview with Mr. Tesfahun, Mr. Mulugeta and Mr. Addis, n-114

<sup>176</sup> NBE Directive No CRB/02/2019 for the Establishment and Operation of Credit Reference Bureau, Article 7

<sup>177</sup> NFIS, n-38 at 10

Exclusion of MFIs from the credit reference system negatively affects rural financial inclusion in Ethiopia. Even after the enactment of Directive No CRB/02/2019 MFIs are not yet included in the credit reference system.

#### **5.5.6. Rigid Collateral Based Bank Credit Policies**

Strict collateral based bank credit policy is one of the major reasons that constrain access to credit with adverse impact on growth and employment creation.<sup>178</sup> Banks require collateral and the value of collateral is higher compared to the amount of credit granted.<sup>179</sup> The potential collaterals in the agricultural sector are largely illiquid and perishable collaterals such as agricultural output, land, farming equipment, and livestock. Poor agricultural product standardization and lack of storage facilities together with prohibition of use of rural land use right as collateral left farmers without any option other than the group guarantee based microcredit. Even after the introduction of movable property security rights proclamation No 1147/2019, absence of movable property registry and the practical risk considerations makes use of movable property as collateral very risky.<sup>180</sup> Accordingly, respondent banks under this study do not accept agricultural output, livestock and rural land use right as collateral.<sup>181</sup>

Regulatory and institutional reforms in the area of movable property security rights, warehouse receipt financing and credit reference system can play indispensable role to reduce risks attached to rural credit operation that in turn induces banks to extend loans for SSFs. Ongoing reforms in the area of movable security rights that introduced electronic based registration should be adapted to paper based registration to be responsive for the demand of SSFs. The membership based warehouse receipt financing scheme is not inclusive enough for SSFs and needs a reform. However, apart from creating favorable conditions for rural credit intermediation, there need to be national rural credit policy that obliges banks to spend a proportion of their overall lending for rural credit facilities.

#### **5.5.7. Poor Financial Literacy**

Financial literacy involves a broad range of concept that includes the perception of the public about FIs, their products, financial terms and conditions as well as prudent use of loans.

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<sup>178</sup> Getnet, n-72 at 23

<sup>179</sup> ACCSA, n-99

<sup>180</sup> Table 2, the reason why selected FIs do not extend credit for SSFs, Annex 1

<sup>181</sup> Table1; Credit products of selected banks for SSFs, Annex 1

Inadequacy of information about the available credit products, and inability to compare such products is the cause of financial exclusion in Ethiopia.<sup>182</sup>In Ethiopia, according to the 2014 WB Findex Survey 78% of population covered by the survey have insufficient information about funds from formal FIs.<sup>183</sup> Lack of financial education contributes to poor credit culture thereby causing farmers to use the credit for nonproductive purposes.<sup>184</sup>

Ethiopia has not yet developed national financial literacy strategy, which in turn led to “fragmented and ineffective interventions that does not necessarily support financial inclusion.”<sup>185</sup>Although NFIS provided for the development of national financial education strategy, it failed to provide details of institutional mandates and implementation mechanisms to develop and implement the plan.<sup>186</sup> Apart from the ongoing initiative of NFIST, to develop national financial education strategy, no other policy or legislative framework is available governing financial literacy.<sup>187</sup>Many Countries established a special agency of financial education and capacity development. For instance in Australia there is Financial Literacy Foundation, while in Canada Financial Consumer Agency is mandated to work on financial literacy and education.<sup>188</sup> In South Africa the financial Sector Charter requires FIs to spend 0.2% of their annual post-tax profits in consumer education aimed at capacitating consumer to make optimal personal financial decisions.<sup>189</sup>

#### **5.5.8. Underdeveloped Infrastructure**

Ethiopia has one of the lowest road and telephone densities per inhabitant in sub-Saharan Africa.<sup>190</sup>Poorly developed rural infrastructure contributes for increasing operational costs that discourage formal FIs from expanding their services to the rural areas.<sup>191</sup> In Ethiopia, the rural access to road index was 21.6 percent in 2016, signifying that only around 22 percent of the rural population had access within a 2 km distance of them to a “decent” road, while this figure is

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<sup>182</sup> NFIS, n-38 at 23

<sup>183</sup>WB Group, “Measuring Financial Inclusion around the World”, (2014), Global Financial Inclusion Index

<sup>184</sup> Interview with Mr. Yirga Getnet, Rural Customer Relations Manager at ACSI, conducted on 30/12/2019, Bahir Dar

<sup>185</sup> Ibid

<sup>186</sup> Ibid

<sup>187</sup> Interview with Mr. Fikremarkos, n-92

<sup>188</sup>Matewos Kebede & Navkiranjit Kaur, “Financial literacy for developing countries in Africa: A review of concept, significance and research opportunities”, (2016), 8 J.AF.ST & DEV. 1. 7-8

<sup>189</sup> Ibid

<sup>190</sup> Bekele and Wolday, n-64 at 1

<sup>191</sup> Table 1, reasons why FIs do not extend credit for SSFs, Annex 1

even worse in the case of ANRS.<sup>192</sup> Only 9 percent of people living in rural areas have access to electricity with an estimated 14.4 million households in the country have no access to electricity.<sup>193</sup> With a telecom density of around 18%, the country has one of the lowest rates of penetration, lower even by East African standards.<sup>194</sup> Infrastructure is the major impediment that discourages FIs from penetrating to rural areas as 89% of respondents concluded lack of infrastructure affects their endeavor towards financial outreach.<sup>195</sup>

The regulatory framework contributed its part to the underdevelopment of infrastructure particularly telecommunication and electricity. Electricity distribution and telecommunication services remained closed for private sector involvement for so long. Market entry is effectively prevented by the licensing regime where only a state-owned operator can be licensed to provide the basic telecom and electricity services.<sup>196</sup> Recently the government is moving towards liberalization of these sectors for private sector investment with the introduction of Investment Proclamation No 1180/2020 as it left areas of joint investment between the government and the private sector to be determined by regulation.<sup>197</sup>

While the role of the government in ensuring access to electricity and telecommunication is vital, total closure of the sectors for private investment led to monopoly and failure to meet the demand. Private investment in those sectors could create an opportunity for the government to intensively work on rural electrification and telecommunication, while the private sector could fill the gap in the cities and towns.

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<sup>192</sup> WB, “What Studies in Spatial Development Show in Ethiopia-Part II, (September 2017), Available at <https://blogs.worldbank.org/african/what-studies-in-spatial-development-show-in-ethiopia-part-ii>

<sup>193</sup> WB, “Beyond Electricity Access: Output-Based Aid and Rural Electrification in Ethiopia”, (November 2016), 15, World Bank, (February 2018), Report No: 119032-ET, 2

<sup>194</sup> Mehrt Alemayehu, “The Regulation of Telecommunications in a Monopoly Market Structure: The Ethiopian Experience”, (2012) LLM Thesis, University of Oslo.66

<sup>195</sup> Table 1; reasons why FIs do not provide credit for SSFs, Annex 1

<sup>196</sup> Investment Proclamation, Proc. No.769/2012, Federal Negatit Gazette, 18<sup>th</sup> year, No. 63,, Article 6

<sup>197</sup> Investment Proclamation, Proc. No.1180/2020, Federal Negarit Gazette, 26<sup>th</sup> year, No. 28, , Article 6(2)

## Chapter Six

### Small Scale Farmers Access to Credit in ANRS

#### 6.1. General Background

ANRS is located in the northern, northern east and central parts of Ethiopia covering an area of 170,752km, which is 11% of Ethiopia's total area.<sup>198</sup> ANRS has a population of 21,136,526 among which 17,454,720 or 83% residing in rural areas.<sup>199</sup> Among the total rural population of 17,454,720 in the region only 4 million are land holders with 18 million parcels of land.<sup>200</sup> ANRS comprises of 13 Administrative zones, 185 Woredas and 3400 Kebeles.<sup>201</sup> The region's topography along with limited roads and transport networks makes delivery of financial services in the region very difficult.<sup>202</sup>

The number of MFI branches in the region is extremely limited compared to the size of the region and its population with 43 microfinance branches and 482 sub-branches as of Jun 2019.<sup>203</sup> The microfinance sector in the region is highly monopolized with ACSI comprising 471 sub-branches among the total of 482 sub-branches.<sup>204</sup> In rural Amhara, in particular, it can be concluded that ACSI is the only microfinance business operator.

ACSI was established as a replica of the Grameen Bank of Bangladesh, adopting its fundamental principle of using group collateral to provide loans, peer pressure to ascertain repayment, and center meetings to disseminate information.<sup>205</sup> Currently, ACSI is one of the largest MFs in Ethiopia, with around 1493,561 active borrowers, 43 branches, and 471 sub-branches.<sup>206</sup> By December 31<sup>st</sup> 2018 ACSI disbursed an outstanding loan of Birr 19,498,889, 742 of which 10,059,185,800 was distributed to the agriculture sector.<sup>207</sup>

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<sup>198</sup> ANRS Bureau of Fiancé and Economic Development, Available at <http://www.amharabofed.gov.et/ANRS/> , Last Viewed 10/03/2020

<sup>199</sup> FDRE Central Statistical Agency, n-4 at 82

<sup>200</sup> ANRS Communications Affairs, በአሜሪካ ክልል የ 2ኛ ደረጃ የ ሜት ይዞታ ማረጋገጫ ስልጠና በተሰጠው አካባቢዎች ከሜት ጋር በተያያዘ የ ማከሰቱ የ ሚኒስቴር አስተዳደር ችግሮች መኮከል አሳይተዋል ተባለ፤ (መስከረም 6፣ 2012)፤ Available at <https://liftethiopia.com/news/second-level-land-certification-reduces-land-management-issues-and-increases-economic-opportunities-in-areas-of-amhara-regional-state/>

<sup>201</sup> Interview with Mr. Shumtaly Kebede, Rural Finance Supply Expert at ANRS Bureau of Agriculture, Conducted on 31/12/2019, Bahirdar

<sup>202</sup> USAID, “Amhara Credit and Saving, ACSI Historical Development”, (February 2006).2

<sup>203</sup> NBE 2017/18 report, n- 102

<sup>204</sup> Ibid

<sup>205</sup> Esayas Bekele, “Microfinance and women's empowerment: an ethnographic inquiry, Development in Practice”, (2016) .93

<sup>206</sup> Interview with Tewabe Aysheshim, n-68

<sup>207</sup> AEMFI, MFI Loan Distribution Data for the 4<sup>th</sup> Quarter, (December 31<sup>st</sup> 2018)

## 6.2. Credit Facilities for Small Scale Farmers in ANRS

ACSI offers a range of credit facilities for SSFs in a group guarantee model, while it also offers asset, and post-harvest loans based on collateral based individual lending. It offers such facilities in short, medium and long terms based on the type of the credit facility.

### Loan Products, terms and conditions for small scale farmers as of June 2019

Type of Loan Product	Loan Size ( Birr)		Maximum Loan Period	Interest Rate	Security
	Min	Max			
Group loan	150.00	75,000.00	3 years	17-19%	Group guarantee
Asset loan	500.00	75,000.00	3 years	17%	Second Level Land Holding Certificate
Agricultural Input loan	500.00	As per the recommendation of expert of agriculture office	1 year	17%	Group Guarantee
Post-harvest	500.00	75,000.00	3 years	17%	Permanent Crops

In ANRS the group lending facility is the major option for SSFs with individual lending still a new product line. Individual loans for SSFs made up just 2.6% of ACSI's lending portfolio for the agricultural sector.<sup>208</sup> Screening for individual loans is based on a traditional appraisal mechanism that relied heavily on the existence of fixed asset collateral, such as houses or buildings.<sup>209</sup> The individual lending model is available for clients upon producing acceptable collateral such as vehicles, urban house, or urban land in which SSFs cannot afford.<sup>210</sup>

### Agricultural loan disbursement of ACSI by credit facility

Credit Products	Amount of Loan by credit Product	In percentage	Interest rate
Group Lending	9,796,185,800	97.4%	17-19 declining
Individual Lending	263,000,000	2.6%	17% declining
Total Agricultural Loan	10,059,185,800	100%	

Data obtained from AEMFI 4<sup>th</sup> quarter data of 2018

<sup>208</sup> Credit Products of ACSI for SSFs, Annex 2

<sup>209</sup> Ibid

<sup>210</sup> Fekadu , n-48 at 38

### 6.2.1. Group Lending

Group lending is a credit scheme based on group guarantee through which people who have no collateral can access an institutional credit.<sup>211</sup> It involves group guarantee mechanism whereby a group of borrowers undertake to be liable jointly and severally for the repayment of a loan taken from an authorized institution in the event of default by any one of them.<sup>212</sup> In case of default, MFIs use the social network among the group members to pressure the defaulting member to pay his debt.<sup>213</sup> However, if the defaulting member refuses/fails to pay, the remaining members will report the assets of their defaulting colleague to the particular MFI, so that the latter can enforce its claim. Whenever, the property of the defaulting member is not enough to satisfy the claim, MFIs can force the remaining members to pay the debt of the defaulting member in accordance with the rules of joint and several liability.<sup>214</sup> MFIs can satisfy their claim only against cash, accounts, livestock, and agricultural assets of the defaulter with rural land use right cannot be used to satisfy their claim.<sup>215</sup>

In ANRS, the group lending mechanism is the dominant, if not the only, model of extending credit for the rural mass that cannot furnish acceptable collateral for long period of time.<sup>216</sup> By December 2019, from the total of Birr 10,059,185,800 outstanding loan distributed for the agriculture sector by ACSI, ETB 9,796,185,800 distributed in a group lending arrangement.<sup>217</sup> This figure accounts more than 97% of the total outstanding agricultural loan for SSFs.<sup>218</sup> Proclamation 626/2009 opened a range of credit operations for MFIs to lend either in the form of individual/group lending secured by collateral or without collateral.<sup>219</sup> Proclamation No.626/2009 also removed the maximum loan ceiling requirement that restricts loans extensions more than ETB 5000.<sup>220</sup>

Farmers applying for credit in a group lending facility must be in a productive age of between 18 and 65 with low annual income and good reputation within the community.<sup>221</sup> The applicant

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<sup>211</sup> Haileleul, n-131 at 6

<sup>212</sup> Proclamation No 626/2009, n-51, Article 2(9)

<sup>213</sup> Interview with Mr. Tewabe, n-68

<sup>214</sup> Civil Code of Empire of Ethiopia, Negarit Gazette, 19<sup>th</sup> year No.2, Article 1897

<sup>215</sup> Interview with Mr. Tewabe, n-68

<sup>216</sup> Ibid

<sup>217</sup> Credit Products of ACSI for SSFs, n- 208

<sup>218</sup> Ibid

<sup>219</sup> Proclamation No 626/2009, n-51, Article 16

<sup>220</sup> NBE, Directive No MFI/5, 1996

<sup>221</sup> Interview with Mr. Tewabe, n-68

must be the resident of the community within the jurisdiction the particular sub-branch operates and should be free from mental and/or physical illness. Then after the applicant must make a group and save some percentage of his income at ACSI, and present business plan. If the applicant is married his/her spouse is required to sign for the loan.

“In the formation of micro-groups, individual loan candidates rely on the networks, associations, contacts, friendships, lineage, and blood links that they have.”<sup>222</sup> However, members often evaluate their peer’s economic capital, such as land or oxen, as well as his capability to run a successful business considering the joint and several liabilities in case of default.<sup>223</sup> Many farmers, especially vulnerable groups such as single or widowed women, people with disabilities and elders, get excluded from group lending due to the perception they are high risk.<sup>224</sup>

The joint and several liability attached to the group lending model sometimes presents significant socio-economic damage to farmers. Farmers make groups in a very short period of time mostly to access seasonal agricultural input credit with little financial information about their peers and pay on behalf of them in case of default. This creates conflict among group members and social shocks as most of group members are neighbors or members of particular community.

### **6.2.2. Individual Lending**

Individual lending is a recent phenomenon which is a modality of extending credit using asset of the borrower as a security. MFIs’ heavy reliance on the group-lending approach seems to have discouraged experimentation on other modalities that may be useful to those who cannot form groups or want to take individual liabilities for their loans.<sup>225</sup> Proclamation No 626/2009 introduced individual lending facility as one area of operation for MFIs. The individual lending model is increasing in terms of population coverage despite its recent introduction. ACSI extended individual credit using collateral amounting 263,000,000 Birr which constitutes 2.6% of its total outstanding loan of Birr 10,059,185,800 as of December 2019.<sup>226</sup> However, individual lending is collateral based, which is available for clients only upon production of acceptable

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<sup>222</sup> Esayas, n-205 at 118

<sup>223</sup> Esayas, n-205 at 95

<sup>224</sup> Ibid

<sup>225</sup> Bekele and Wolday, n-64 at 62

<sup>226</sup> Credit Products of ACSI for SSFs, n-208

collaterals.<sup>227</sup> ACSI's conservative collateral policy coupled with lack of acceptable collateral on the side of farmers attributed for the exclusion of farmers from accessing individual based credit facilities. In this regard, ACSI mainly accepts urban houses, car, land and other fixed assets as collateral to extend individual loans.<sup>228</sup> ACSI does not extend individual credit using agricultural products including livestock, grains, and future harvest as collateral.<sup>229</sup> ACSI's individual lending operation in rural areas is limited to extension of credit using rural land use right as collateral.<sup>230</sup> Extension of credit using rural land use right as collateral is a very recent phenomenon in the aftermath of the enactment of ANRS RLUAP No 252/2017 and the introduction of second level landholding certifications. Coordinated and map based rural land holding certificate is only given in 17 Woredas of the region. By December 2019, around 7,000 farmers in the region accessed individual credit using their second level landholding certificate. ACSI also started extending credit using permanent crops like eucalyptus and mango trees as collateral. Generally, individual lending is at its infancy stage with a potential of expansion backed by financial infrastructure development. ACSI has emphasized that the individual loan product has shown success in bringing in those dissatisfied with group lending, as well as attracting new clients who have an entrepreneurial mindset.<sup>231</sup>

### **6.3. Success of Small Scale Farmers Access to Credit in ANRS**

#### **6.3.1. Collateralization of Rural Land Use Right**

The Amhara regional state is one of few states in Ethiopia, which introduced a regulatory framework that expressly allows farmers to use their land use rights as collateral even before the federal government. RLUAP No 252/2017 provides that any land holder in the region can use his/her land holding right as collateral to get credit from FIs recognized by the NBE.<sup>232</sup> While the FDRE Constitution mandated regional states to administer rural land and natural resources in accordance with federal laws, ANRS issued legislation, which expand the right of farmers allowing them to use their land holding right as collateral. Save the generic constitutional provision granting farmers the right to usufruct over rural land, the FDRE RLUAP No 456/2005

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<sup>227</sup> ANRS RLUAP No 252/2017, Zikre Hig, Article 19, Interview with Mr. Tewabe, n-68

<sup>228</sup> Interview with Mr. Tewabe, n-68

<sup>229</sup> Ibid

<sup>230</sup> Ibid

<sup>231</sup> Ibid

<sup>232</sup> Proclamation No 252/2017, n-227, Article 19

does not expressly allow such right. However, the issue as to whether ANRS has a constitutional mandate to issue a law that expands the rights of farmers beyond what is provided by the federal law is contentious.

Proclamation No 252/2017 allows farmers to use their land as collateral to access credit from FIs for duration of up to 30 years.<sup>233</sup> The proclamation answered concerns related to perfection in that every collateral agreement over rural land use right must be registered by the respective Woreda Land Use and Administration Offices. The registration serves to prevent potential transfer of the use right held as collateral to third parties. MOA developed a National Rural Land Information System (NRLAIS) which updates rural land transactions including collaterals over rural land use right.<sup>234</sup> Any collateral arrangement using land use right as collateral must be authenticated by the respective Woreda Land Use and Administration Offices and uploaded on NRLAIS.<sup>235</sup> NRLAIS blocks all lands which are attached by MFI, and it will not be used for other transactions until the blocking is released. This arrangement presupposes only one collateral contract over a given time and restricts the right of the holder to use his land use right to cater utmost finance. Once the use right is blocked it is impossible to use such right for accessing another loan or transfer it until it is released from blockage. The defining feature of a reformed legislation is to allow optimum use of a particular asset by as many creditors as possible through rules of priority. The practice in ANRS, however, is uneconomic and contradictory to the principle of security rights as it prohibits use of rural land holding right to cater more than one loan in a given period of time.

In case of default, the lending institution will seize the use right and either it can develop such land by itself or rent such right.<sup>236</sup> If the FI does not develop the land by itself, the original holder of the land will be given priority to rent such right over third parties.<sup>237</sup> The law takes a policy position in favor of keeping the land for the holders even in case of default by giving them priority to rent over third parties. The law is not clear about as to how the price of rent at which

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<sup>233</sup> Ibid

<sup>234</sup> Interview with Mr. Abebaw Abebe, Legal Officer at the Ministry of Agriculture, Conducted on 25/01/2020, Addis Ababa

<sup>235</sup> Ibid

<sup>236</sup> Proclamation No 252/2017, n-227, Article 19 (2,3)

<sup>237</sup> Ibid

the holder can exercise his priority right is set. However, if the holder is not interested to rent the use right, the FI is free to rent it for anybody.<sup>238</sup>

### **6.3.2. Credit Oriented Rural Land Certification**

ANRS Agriculture Bureau together with other development partners mainly LIFT<sup>239</sup> project undertook an encouraging reform that has significant bearing on SSFs' access to credit. Among 18 million parcels occupied by over 3.6 million landholders, SLLHC is given to 1.2 million landholders in 17 woredas covered so far. SLLHC involves registering the geographical locations and sizes of individual parcels using geographically referenced aerial photography.<sup>240</sup> SLLHC is prepared in the name and photo of the holder or in case of married spouses the name and photo of both spouses will appear on the certificate as joint holders.<sup>241</sup> This practice is in line with the requirements of ANRS RLUAP 252/2017.<sup>242</sup> However, continuing polygamous marriage coupled with the silence of federal and regional RLUAPs related to the registration of polygamous families further complicated the registration process.<sup>243</sup> SLLHC is a precondition for FFIs to extend credit using land use right as collateral. By September 2019 over 7,000 land holders in ANRS have received loans from ACSI, amounting to 263 million Birr using their SLLHC as collateral. SLLHC is map based and coordinated system that enables to identify each plot of land covered by the certificate.<sup>244</sup> FIs can register certificate of the land held as collateral and write a letter to the Woreda Land Administration Bureaus so that the land holder will not transfer his right to third parties.

### **6.3.3. Agricultural Input Credits**

The ANRS Agriculture Bureau in cooperation with the Regional Finance and Cooperation Bureau, ACSI and farmers' cooperative unions established a system through which farmers can access credit necessary to purchase agricultural input during harvest season.<sup>245</sup> In the 2018/19 season, 345, 838 out of the total 3, 600,000 farmers in the region took agricultural input through

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<sup>238</sup> Ibid

<sup>239</sup> LIFT, n-137

<sup>240</sup> Ziade Hailu et al, Protecting Land Tenure Security of Women in Ethiopia; Evidence from LIFT Program, (2019).14

<sup>241</sup> Ibid

<sup>242</sup> Proclamation No.252/2017, n-227, Article 32

<sup>243</sup> Ziade et al., n-240 at 30

<sup>244</sup> Interview with Mr. Shumtaly, n-201

<sup>245</sup> Interview with Mr. Shumtaly , n-201

agricultural input loan arrangement.<sup>246</sup> In terms of quantity, 961, 629 sacks of agricultural input with a price of 897, 487, 837 Ethiopian Birr was distributed through credit.<sup>247</sup> Introduction of Input Voucher System addresses a critical problem of financial mismanagement by intermediaries which necessitates regional governments to cover unpaid loans to honor the 100% guarantee requirement from FIs.<sup>248</sup> It enables ACSI to handle the financial transactions, while recruitment of eligible farmers is made by the agriculture bureau in accordance with the ACSI client recruitment criteria.<sup>249</sup>

ACSI extend agricultural input loans ranging from a minimum of ETB 500 to the maximum amount to be determined by ANRS Bureau of Agriculture at a declining interest rate of 17%.<sup>250</sup> Impute loans are short term loans availed to farmers using group-lending methodology with a repayment period in the post-harvest season.<sup>251</sup> Input Credit Coordinating Committee at each sub-branch monitors the agricultural input credit repayment together with Kebele Administrations.<sup>252</sup> At the beginning of every December farmers informed to settle their debt up to end of February and in case of default, defaulters will be sued. Group members will be forced to pay the debt of the defaulting member if the latter's asset is not enough to satisfy the claim. This, in turn, forces farmers to sell their agricultural product with lower price during a season where supply of agricultural products is very high. The agricultural input credit scheme is available for farmers after the cash based purchase is completed and farmers who cannot afford to purchase are forced to wait until the whole purchase based input is distributed.<sup>253</sup> This creates tremendous problem on farmers as they cannot access the inputs on due time to cover their farm with seeds.

#### **6.3.4. Women Coverage**

ACSI developed client targeting principle that prioritizes rural and urban poor women.<sup>254</sup> ACSI lending principle gives special focus to women considering their vulnerability to poverty and

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<sup>246</sup> ANRS Agriculture Bureau, n-6

<sup>247</sup> Ibid

<sup>248</sup> The Ethiopian Agricultural Transformation Agency formulated Input Voucher system and currently the system is under Implementation, Available at <http://www.ata.gov.et/programs/agribusiness-markets/rural-financial-services-projects/>

<sup>249</sup> Interview with Mr. Shumtally, n-201

<sup>250</sup> Table 3, ACSI loan terms and conditions,

<sup>251</sup> Interview with Mr. Teawabe, n-68

<sup>252</sup> Ibid

<sup>253</sup> ANRS Agriculture Bureau, n-6

<sup>254</sup> Interview with Ms. Mulusew, Gender Department Officer at ACSI, Conducted on 30/12/2019, Bahirdar

deprivation. Women centered credit is identified as a means to improve women’s income thereby creates a positive trickledown effect on reduction of household poverty and improvement of nutrition. In view of the aforementioned justifications, the percentage of women clients increased from just 36% by 2005 to 66% by December 2018.<sup>255</sup> As of December 2018, among the total of 1,484,643 borrowers 985, 309 were women.<sup>256</sup>

Table 5: Percentage of ACSI borrowers by gender as of December 31<sup>st</sup>, 2018

	Total Borrowers	Male	Female
In Figure	1,484,643	489334	985,309
In percentage	100%	34.6%	66.4%

Source: Author’s Computation of data obtained from AEMFI 4<sup>th</sup> quarter data of 2018

ACSI instituted a gender department in its institutional structure ranging from its head office to sub-branch level to monitor the implementation of women oriented client targeting principles, and provide financial education for women.<sup>257</sup> ACSI integrated gender auditing in its annual performance audit and reporting system, which further pushes it towards the provision of women centered credit.<sup>258</sup> However, some women clients of ACSI do not utilize and manage the credit they took themselves; rather they just transfer it to their husband and their husbands will have a say on the utilization and management of such credit.<sup>259</sup>

## 6.4. Failures of Small Scale Farmers Access to Credit in ANRS

### 6.4.1. Limited Number of Credit Providers

MFIs are the only formal FIs that extend credit to SSFs in ANRS with FIs being largely urban based and urban oriented.<sup>260</sup> Banks and MFIs fail to avail flexible and responsive credit products and mostly stick with the traditional collateral based loan appraisal mechanism. FIs, banks in particular, accept urban houses, vehicles, or other manufacturing industries as the only eligible collaterals that in turn totally excludes SSFs from accessing credit. Even after the introduction of the RLUAP No 252/2017 and the second level land holding certification, banks are not extending loans using land use right as collateral. Despite financial inclusion being one of the

<sup>255</sup> Ibid

<sup>256</sup> Percentage of ACSI Borrowers by Gender as of December 2018, Annex 2

<sup>257</sup> Interview with Ms. Mulusew, n-255

<sup>258</sup> Ibid

<sup>259</sup> Esayas, n-205 at 95

<sup>260</sup> Haileleul, n-131 at 9

strategic plans that NBE is expected to ensure its implementation, it failed to supervise banks from the perspective of ensuring financial inclusion and its effort is negligible compared to its effort of maintaining financial soundness. In fact NFIST is only confined to development of policies and regulatory framework intended to ensure financial inclusion.<sup>261</sup>

Abay Bank and CBE are the only commercial banks that extend agricultural input credit for farmer cooperatives in ANRS together with the Agriculture Bureau of the ANRS.<sup>262</sup> In a triangular relationship Abay Bank and CBE extend credit to farmer cooperatives that distribute fertilizers, seeds and other technologies to farmers, through the sovereign guarantee of the regional government.<sup>263</sup> Banks do not directly extend credit for farmers; rather it is limited to financing farmer cooperatives in their endeavor to distribute agricultural inputs and technology to farmers. In case of default of farmer cooperatives to return their debt, the regional government will pay the debt to the extent it guaranteed. Lack of acceptable collateral on the side of farmers coupled with underdeveloped security rights, land law regime, and similar infrastructures forced banks to refrain from extending credit for SSFs.

The number of microfinance operators in the ANRS is also extremely limited with ACSI being the only formal FI that provides rural credit facility. ACSI being the monopoly SSF credit provider in the region, it can set any loan conditions including very high interest rate that can maximize its profit margins. This is partly due to the regional government preferential support of ACSI ranging from allocating fund to empowerment of ACSI as a sole agricultural impute credit service provider in the region.<sup>264</sup> Unlike privately owned MFIs, the administration of ACSI is markedly influenced by the involvement of the ANRS government with majority of its board members assigned by the government.<sup>265</sup> However, taking the advantage of market power, dominant firms in the industry may charge higher rates in different forms for financial products.

#### **6.4.2. Narrow Credit Products**

Group lending was the only credit product offered by ACSI until the introduction of Proclamation No 626/2009. Even after 10 years from the introduction of Proclamation No.626/2009, the group lending product facility is almost the only product for SSFs in the

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<sup>261</sup> Interview With Mr. Fikremarkos, n-92

<sup>262</sup> Interview with Mrs. Mulugeta, Tesfahun, and Addis, n-114

<sup>263</sup> Interview with Mrs. Mulugeta, Tesfahun, n-70

<sup>264</sup> Kassa Teshager, "Microfinance as a Strategy for Poverty Reduction: A Comparative Analysis of ACSI and Wisdom Microfinance Institution in Ethiopia", (2008), Hague Institute of Social Studies, 44

<sup>265</sup> Esayas, n-205 at 94

ANRS. Lack of collateral makes non-group lending product facilities very difficult to implement. Although there are encouraging developments in individual lending using SLLHC, the number of farmers who took credit using SLLHC is only 7,000. FIs including ACSI do not extend credit using movable property including agricultural products, future harvest and livestock as there is no perfection mechanism for such products. Narrow credit products are attributable to poor financial infrastructure such as absence of movable property registration, credit reference system, warehouse receipt system, national ID system and poor financial literacy.<sup>266</sup> Limited collateral options among SSFs forced FIs to stick with the group lending modality.<sup>267</sup>

#### **6.4.3. Poor Client Support, Education and Monitoring**

Majority of ACSI clients in the region get little or no business development support, skill training, and modern agricultural technology extension.<sup>268</sup> The most practical problem faced by ACSI is the very low absorptive capacity of the business of the poor in rural areas.<sup>269</sup> Credit alone, without the necessary infrastructure to enhance the skill capacity of the potential borrower, would not reach the intended goal of reducing poverty.<sup>270</sup>

ACSI officials underlined that there is an increase in the number of defaulters due to mismanagement of credit.<sup>271</sup> Lack of business development skills training and limited agriculture extension programs contributed to credit mismanagement.<sup>272</sup> ACSI requires potential clients to submit business plan before they took credit and one credit extended to them it is expected they will use it to implement the business plan. However, farmers use the credit for consumption purposes due to lack of follow-up and monitoring. Financial education should be given to farmers to ensure that they benefit from access to microfinance, avoid over-indebtedness, properly manage investments, strengthen bargaining position, and know how FIs work.

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<sup>266</sup> Table 2, Why Selected FIs do not extend credit for SSFs, Annex 1

<sup>267</sup> Interview with Mr. Tewabe, n-68

<sup>268</sup> Getaneh Gobezie and Carter Garber, “Impact Assessment of the Microfinance Program in Amhara Region of Ethiopia”, 17

<sup>269</sup> Getaneh Gobezie, “Successes in Expanding Microfinance Opportunities in Rural Ethiopia; can the entrepreneurship Challenge be Overcome?” (2008), African Review of Money Finance and Banking .122

<sup>270</sup> Ibid

<sup>271</sup> Interview with Mr. Yirga, n-184

<sup>272</sup> Interview with Mr. Tewabe, n-68

#### 6.4.4. Short Term Credit Facilities

NBE Directive No MFI/28/2016 extended term limit of loan repayment for agricultural loans up to five years.<sup>273</sup> Recently, ACSI began to extend loans to farmers with a repayment term of up to three years.<sup>274</sup> However, long and medium term loans are not available for farmers to purchase agricultural inputs. Short term loans pose a serious problem for MFIs, which provide agricultural loans like for purchase of oxen for traction, dairy cattle and so forth. Short term loans increase administrative cost of MFIs as it requires significant human resource and capital to recollect such loans each season. From the perspective of farmers, short term loans force them to repay their loan before their investment began to reap fruits. The pressure to repay in a single year encourages borrowers to focus on micro-economic activities that bring immediate returns and discourages investments that have longer gestation period and higher capital requirements such as agricultural and environmental conservation activities.<sup>275</sup>

#### 6.4.5. Geographical Inaccessibility of Financial Institutions

In ANR, people in the rural areas are expected to travel a distance ranging from five to twenty kilometers to access microfinance branches.<sup>276</sup> In terms of cost people spend 10 up to 30 Birr for transport in the endeavor to access branches.<sup>277</sup> ACSI is trying to be physically accessible to the rural community through expanding its branches from time to time.<sup>278</sup> However, 471 sub-branches for a region with around 3400 Kebeles are very limited. Financial service outreach in the region is significantly below the goal aspired by GTP II, which is to open microfinance access points in each Kebele.<sup>279</sup> Low level of access points of FIs in the countryside is one of the factors that negatively affect SSFs' access to finance.<sup>280</sup> Poor infrastructure particularly absence of electricity, telecommunication and road networks are the major reasons behind MFIs' reluctance to open their branches in rural kebeles.<sup>281</sup>

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<sup>273</sup> NBE, Limits on Loans, Repayment Periods and Provisioning Requirement Directive No, MFI/28/2016, Article 6 (3).

<sup>274</sup> Interview with Mr. Tewabe, n-68

<sup>275</sup> Bekele and Wolday, n-64 at 61

<sup>276</sup> Tewabe Aysheshim, "Banking the unbanked rural population of Amhara region", (2012), Available at [file:///C:/Users/user/Downloads/Amhara%20Regionbanking\\_the\\_unbanked\\_rural\\_population\\_of\\_amhara\\_region\\_et\\_hiopia\\_-\\_2012-09-12.pdf](file:///C:/Users/user/Downloads/Amhara%20Regionbanking_the_unbanked_rural_population_of_amhara_region_et_hiopia_-_2012-09-12.pdf)

<sup>277</sup> Ibid

<sup>278</sup> Interview With Mr. Yirga, n- 184

<sup>279</sup> GTP II, n-30

<sup>280</sup> NFIS, n-38 at 12

<sup>281</sup> Ibid

#### **6.4.6. Poor Institutional Coordination**

Development of working small SSFs credit intermediation framework require an integrated effort from different stakeholders including particular FIs, regional agriculture bureau, fiancé and economic cooperation bureau, NGOs and other stakeholders. The institutional framework envisaged by the NFIS need to be replicated at the ANRS level. The financial inclusion institutions established by NFIS are nonexistent at ANRS level. The effort towards SSFs credit inclusion is piecemeal and fragmented which is mainly undertaken by ACSI. ACSI is facing challenge in recollection of seasonal agricultural input loans as a result of poor coordination with the regional agriculture bureau. The agriculture bureau's main intention is on farmers getting agricultural products, and gives little attention on the repayment potential of such farmers.<sup>282</sup>The agriculture bureau mainly focuses on farmers getting credit that leads to desperate client recruitment.<sup>283</sup> Poor recruitment coupled with lack of follow-up from the side of the agriculture bureau leads to increase of the number of defaulters.<sup>284</sup>

## **II. Conclusions and Recommendations**

SSFs, in Ethiopia in general and in ANRS in particular, are credit constrained both in terms of physical accessibility of FIs and credit facilities. Commercial Banks have one size fits all collateral based loan appraisal policy that totally excludes small scale farmers from being eligible for bank credit. Absence of specialized rural banks that operate with a priority in rural credit intermediation worsened the problem as no existing bank operates rural credit intermediation. The microfinance sector is monopolized by few government owned MFIs with no cross-regional operation. MFIs also offer very narrow group guarantee based credit facilities for SSFs, which are not responsive to their needs. Absence of competition leads to geographic inaccessibility of MFIs and lack of diversified and flexible credit products for small scale farmers.

Microfinance Business Licensing and Supervision Proclamation No 40/1996 and subsequent Amendment Proclamation NO 626/2009 along with series of NBE directives completely closed all the windows through which NGOs can operate non-risk bearing credit delivery services. In a country with significant gaps in credit supply NGO based microcredit could play positive role.

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<sup>282</sup> Interview with Mr. Yirga, n-184

<sup>283</sup> Ibid

<sup>284</sup> Ibid

All microfinance including non-deposit taking MFIs are subjected to similar capital, entry, and governance prudential requirements irrespective of their risk bearing potential. While, banking regulation in Ethiopia failed to envisage developmental objectives that can create an enabling environment for banks to operate rural credit intermediation. A case in point is there is no regulatory framework that mandates banks or a particular bank to engage in rural credit provision.

Contrary to the usufruct right vested to the Ethiopian peasants under the FDRE constitution, subsidiary legislations and the practice denied farmers the right to use their use right as collateral. Lack of map based and coordinated land holding certification is another barrier that discourages FIs from extending credit using land use right.

Major assets of SSFs including agricultural products, future harvest, livestock and land use right remained collateral unworthy due to absence of movable property collateral registry. The new Movable Property Security Rights Proclamation No 1147/2019 recognizes wide range of agricultural products and land holding right as eligible to be used as collateral. NBE operationalization of collateral registry Directive No MCR/01/2020 introduced electronic registration of movable assets and burdens financial institutions to undertake registration of collaterals they take and verify their legality. Considering the rural population has no access to internet and electricity, it will be difficult for the rural population to be beneficiary of such electronic based data.

Lack of warehouse receipt for farmers presented a significant challenge for FIs to extend credit using agricultural products as collateral. ECX is the only institution that is accredited to issue warehouse receipt and its warehouse operation limited with short term service for commercial produces destined for export and available only for members.

In Ethiopia, provision of credit for SSFs is risky business with majority of SSFs experiencing bad harvest or significant loss of livestock with no insurance coverage, which is partly attributable to lack of index and micro-insurance regulatory framework. The credit reference system covers only 0.2 % of the Ethiopian adults with MFIs not included in the system. Exclusion of MFIs from the credit reference system negatively affects rural financial inclusion in Ethiopia.

Information asymmetry regarding the nature of credit products contributed to credit diversion for non-productive purposes and an increase in defaulters. Lack of financial education contributes to

poor credit culture thereby causing farmers to use the credit for nonproductive purposes. Ethiopia has not yet developed national financial literacy strategy, which in turn leads to “fragmented and ineffective interventions that does not necessarily support financial inclusion.

In ANRS, ACSI is the only operator as far as rural credit extension is concerned. The microfinance sector in the region is dominated by government owned ACSI with no potential market competition. Credit supply in the region is entangled with problems associated with very limited number of operators and absence of competition, narrow group based credit products, expensive interest rate, poor infrastructure, lack of financial education and monitoring, and limited fund.

Based on the problems identified under the study, the researcher recommends the following measures and interventions:

The government should take an initiative to establish specialized rural and agricultural banks and craft a regulatory framework that encourages new entrants to engage in rural credit intermediation services. Incentive packages and/or mandatory proportional lending for SSFs should also be considered to encourage banks to engage in rural credit intermediation and attract the private sector investment. For such purpose a separate rural and agricultural development policy bank that designs rural development financing policies and national rural credit plans, allocate fund for MFIs and rural banks, co-ordinate rural credit financing activities, and promotes research in rural banking, and rural development needs to be established. Separate national bank for rural and agricultural development can serve as an organizational device to provide undivided attention, forceful direction and a pointed focus to the credit problems arising out of an integrated approach to rural development.

Tiered regulation that sets flexible regulatory measure ranging from mere licensing to prudential supervision should be in place depending on the risk bearing potential of services. Different level of capital, ownership, governance, and organizational structure requirement should be introduced based on their risk bearing potential. The requirement that outlaws microfinance operation in an organizational set-up other than Share Company should be amended. NGOs and other organizations should be allowed to provide non-deposit taking micro-credit services. Non-deposit taking credit only MFIs should be regulated in a flexible fashion without the requirement of prudential regulation.

Recent credit friendly rural land use legislative reforms in ANRS, and being underway at the federal level should be implemented through issuance of second level rural land holding certificates extensively. However, the ANRS RLUAAP should be amended in a manner that allows farmers to use their holding right to cater more than one loan in a given period of time.

The legislative reforms on areas of movable property security rights needs to be implemented ranging from commencement of the registration process, which is not yet started. A Parallel paper based mechanism parallel to the electronic registration is necessary considering the rural population has no access to internet and electricity. Operationalization of Movable Property Collateral Registry Directive NO MCR/01/2020 should be amended in a manner that limits the burden of FIs to filling notice about the assets they took as collateral and removing the burden of registration and verification. Bank foreclosure Proclamation No.97/1998 need to be reformed to include MFIs as beneficiaries of non-judicial enforcement of their claim.

Index and micro insurance legal framework, which enables to determine premium and damages based on an index that is correlated with agricultural losses need to be introduced in order to avail insurance packages with affordable premium and minimum cost. Unlike the indemnity based insurance that require physical examination of each fragmented plot to determine premium and damage, the index insurance can reduce cost as it uses aggregated data over large area to determine damage and premium. Central database related to rainfall, weather condition, flooding, agricultural yields, and similar factors must be available to determine accurate premium and damage indexes over large area.

The regulatory framework related to warehouse receipt needs amendment to embrace the need of SSFs. ECX Establishment Proclamation No 550/2007 that limited ECX warehouse receipt system only to members need to be amended to allow non-members to be beneficiaries of such scheme. With the existing warehouse receipt financing scheme limited to ECX, other warehouse operators and particularly farmers' cooperatives must be empowered and accredited to operate warehouse receipt financing business.

The credit reference system should encompass MFIs to include credit history of the rural population. National ID system should be also implemented so that it will be easy for FIs to track the credit history of credit applicants, and enforce repayment of their loans.

National rural credit policy should be designed to contain the discretionary bank credit policies that exclude SSFs from accessing bank credit. Uniform national rural credit policy can play

significant role to induce banks to spend a proportion of their overall lending for rural credit facilities.

The government should promote competition of MFIs through expansion of inter-regional operation of government owned MFIs and supporting new entries. Introduction of proportional capital requirement can enhance new entries to the microfinance sector by reducing barriers related to lack of funding to commence operation. The government should support MFIs in the form of revolving funds, subsidies, and incentives so that they can extend credit to farmers with lower interest rate.

A comprehensive financial literacy strategy that mandates particular institution with a power to implement programs on public financial literacy and sets out the obligation of particular FIs to educate their clients should be adopted. A mandatory requirement that obliges FIs to spend certain percent of their profit on client education can be an option. After adoption of national financial literacy program, FIs should be supervised as to whether they implemented financial literacy programs.

In ANRS, the institutional apparatus that is set up by the NFIS is not established, while the effort towards SSFs' credit inclusion is piecemeal and fragmented which is mainly undertaken by ACSI. Institutions including the National Financial Inclusion Council and Secretariat should be operational at the regional level. The regional government should consider establishment of rural and agricultural banks along with an institution that designs rural financing policies at the regional level. While, ACSI need to work credit product development to broaden credit facilities available for SSF

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## VII. Appendixes

### Annex 1- Tables

**Table1; Credit products of selected commercial banks to SSFs**

No	Credit Product	Name of Bank	Available/not available
1	Credit using rural land holding right as collateral	CBE	Not available
		Abay Bank	Not available
		Wogagen Bank	Not available
2	Credit using agricultural products, future harvest or livestock as collateral	CBE	Not available
		Abay Bank	Not available
		Wogagen Bank	Not available
3	Credit without collateral using group guarantee based security	CBE	Not available
		Abay Bank	Not available
		Wogagen Bank	Not available

Source: Author's assessment of questioners collected from FIs, See Annex 3

**Table 2: Reasons why selected FIs do not extend credit for farmers**

No	List of Barriers	Yes/No	Repetitions	Percentage
1	Restrictive rural land holding regime	Yes	7	78
		No	2	22
2	Unreformed security rights framework	Yes	7	78
		No	2	22
3	Prudential bank and microfinance regulations	Yes	6	67
		No	3	33
4	Poor Infrastructure	Yes	8	89
		No	1	11
5	Lack of collateral registry	Yes	8	89
		No	1	11
6	Farmers cannot produce acceptable collaterals	Yes	6	75
		No	2	25

Source: Author's assessment of questioners collected from FIs, See Annex 3

## Annex 2- ACSI and NBE Reports

<b>ACSI Loan by Sector as of December 31<sup>st</sup>, 2018</b>				
Sector	Outstanding loan	Total outstanding loan	Loan Disbursed	Total Loan Disbursed
Agricultural Loan	10,059,185,800.00	19,498,889,742.54	44,824,146,985.00	74,891,113,925.00
Manufacturing	971,665,552.00		4,105,764,931.00	
Trade & Commerce	2,761,236,487.54		8,992,749,128.00	
Transport & Com	490,777,710.00		1,670,859,977.00	
Electricity & Water	438,480,333.00		1,828,323,354.00	
Building & Cons	1,238,484,895.00		2,930,302,692.00	
Other services	3,539,058,965.00		10,538,966,858.00	

### ACSI Loan Products, (terms and conditions summary; June 2019)

Type of Loan Product	Loan Size ( Birr)		Maximum Loan Period	Interest Rate
	Min	Max		
Group loan	150.00	75,000.00	3 years	17-19%
Micro enterprise	500.00	150,000.00	5 years	17%
Asset loan	500.00	75,000.00	3 years	17%
Agricultural Input loan	500.00	As per the recommendation of expert of agriculture office	1 year	17%
Revolving youth loan	30,000.00	1,000,000.00	3 year	8%
Islamic loan	150.00	71,850,000.00	5 years	15-17%
Technology loan	500.00	50,000.00	3 years	17%
Post-harvest	500.00	75,000.00	3 years	17%
Housing loan	10,000.00	One third of gross salary of the loan client or the required amount for construction whichever is lower	10 years	15-17%
HABP/Livelihood	500.00	75,000.00	3 years	15%
SME	150,000.00	71,580,000.00	5 years	10-17%

**Bank Outstanding Loan by Sector for the Last 8 Years**

Sector	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20
Total	54,251.5	59,965.4	75,481.0	88,023.1	109,011.2	115,398.1	164,493.9	#REF!
Agriculture	9,709.2	10,867.5	13,077.1	13375.7	13133.7	11401.9	17954.7	#REF!
Industry	19,298.4	20,391.1	23,437.4	25495.6	25035.6	30503.0	41585.8	#REF!
Domestic Trade	8,325.0	9,104.1	15,589.0	15040.5	23608.9	19935.9	32873.5	#REF!
International Trade	6,290.8	7,280.7	8,415.0	9528.0	13494.8	18606.2	27673.1	#REF!
Export	2,569.1	2,973.3	3,780.4	4404.9	6062.2	11603.2	17409.4	#REF!
Import	3,700.5	4,307.3	4,634.6	5123.1	7432.7	7003.0	10263.7	#REF!
Hotel and tourism	882.6	1,190.6	1,620.3	1893.8	2213.4	2197.9	4937.1	#REF!
Transport and Communication	1,575.7	1,555.5	3,625.5	4494.1	6924.9	4525.6	2654.6	#REF!
Housing and Construction	6,322.9	6,695.8	6,720.1	13641.9	13583.6	12281.4	19635.0	#REF!
Mining, Energy, Water	82.4	265.6	165.2	341.2	363.4	319.5	848.3	#REF!
Others	1,529.5	1,899.8	2,163.8	3160.8	8450.9	12674.1	4898.6	#REF!
Personal	256.3	268.4	667.5	1051.4	2201.8	2952.6	11433.4	#REF!

**Five Years Microfinance Loan by Sector**

Period of Ending	Agriculture	Trade	Manufacturing	Construction	Service	Others	Total
June 2015	12,457,615.9	4,128,156.3	1,215,090.5	969,153.2	1,148,948.9	1,719,242.2	21,638,207.3
June 2016	13,943,815.2	4,197,334.7	2,452,299.6	1,407,495.4	2,445,563.5	792,705.1	25,239,213.4
June 2017	17,096,865.8	6,459,128.8	2,027,584.1	2,068,075.3	1,978,011.4	2,610,313.5	32,239,978.8
June 2018	22,386,710.7	8,944,941.2	2,470,618.7	3,342,412.4	5,457,246.9	2,106,614.1	44,708,544.1
June 2019	26,271,309.75	9,923,181.50	2,385,267.34	2,586,973.31	6,386,858.46	3,034,742.52	50,588,332.88

**MFIs Outreach Data for the Third Quarter, December 31<sup>st</sup>, 2018**

No.	Name	No of Active Borrowers	No of Woman Borrowers	Loans Outstanding	Voluntary Saving	Compulsory Saving	Total Saving
1	ACSI	1,484,643	985,309	19,498,889,747	14,401,124,360	1,254,093,510	15,655,217,870
2	ADCSI	274,538	130,923	2,496,448,317	745,120,000	786,351,000	1,531,471,000
3	Aggar	16,101	4,379	303,111,064	94,932,016	36,500,347	131,432,363
4	AVFS	11,262	6,982	17,683,516	695,590	6,096,613	6,792,203
5	Benshangul	37,583	5,566	143,051,701	41,074,006	31,321,964	72,395,970
6	Bussa Gonofa	67,787	50,840	161,153,151	3,721,017	25,697,494	29,418,511
7	DECSI	412,546	102,905	3,323,805,730	2,461,457,122	157,170,485	2,618,627,607
8	Dire	10,352	6,460	254,577,759	153,779,232	96,614,861	250,394,093
9	Digaf	223	182	572,599	332,915	283,867	616,782
10	Eshet	15,406	5,162	53,534,199	15,349,209	9,026,791	24,376,000
11	Gasha	5,544		17,697,629		5,298,377	5,298,377
12	Harbu	30,802	10,823	152,117,208	24,369,243	23,210,597	47,579,840
13	Letta	1,637	574	6,499,590	726,870	1,211,640	1,938,510
14	Meklit	7,464	3,050	123,084,284	12,503,061	28,573,589	41,076,650
15	Metemamen	20,473	13,307	153,149,980	55,129,529	23,085,156	78,214,685
16	Ocssco	1,009,158	339,805	8,815,441,930	2,569,873,895	1,543,360,380	4,113,234,275
17	Omo	1,276,163	384,549	4,115,224,123	2,068,411,188	565,801,086	2,634,212,274
18	PEACE	24,021	17,923	181,192,101	30,956,357	52,805,764	83,762,121
19	SFPI	22,956	13,270	254,366,820	59,791,099	45,862,934	105,654,033
10	Kendil	4,049	1,042	45,259,606	7,518,694	5,712,293	13,230,987
21	Sidama	60,404	18,121	174,325,888	59,812,677	30,785,317	90,597,994

22	Wasasa	57,681	24,454	409,046,359	97,274,368	104,854,414	202,128,782
23	Vision Fund /Wisdom	176,296	86,419	1,205,062,646	366,423,061	185,675,162	552,098,223
24	Harar	9,355	4,860	95,398,756	43,469,508	8,513,006	51,982,514
25	Lefayeda	350	262	1,197,684	1,478,793	173,557	1,652,350
26	Dynamic	1,105	248	53,771,386	11,308,277	6,705,598	18,013,875
27	Gambella MFI	12,446		44,909,933	11,211,151	11,763,261	22,974,412
28	Tesfa	269		407,041	14,460	51,544	66,004
29	Somali	31,079	21,476	959,622,934	126,693,477	142,424,939	269,118,416
30	Lideta	3,073	2,576	9,006,495	2,994,174	2,040,012	5,034,186
31	Nisir	720	182	49,255,211	100,859,549	3,919,364	104,778,913
32	Afar	4,209	2,045	122,828,365	112,224,394	25,846,387	138,070,781
33	Adeday	15,868	14,541	107,482,247	48,336,254	13,265,779	61,602,033
34	Debo	135	40	6,464,332	1,080,853	20,280	1,101,133
	<b>TOTAL</b>	<b>5,105,698</b>	<b>2,258,275</b>	<b>43,355,640,331</b>	<b>23,730,046,400</b>	<b>5,234,117,368</b>	<b>28,964,163,768</b>

	MFI Data 2011-2018							
Name	Jun-11	Jun-12	Jun-13	Jun-14	Jun-15	Jun-16	Jun-17	Jun-18
Number of Branch	1,133	1,224	1,341	1,489	1,593	1,680	1,755	1,873
Number of Employee	NA	NA	18,167	20,947	26,792	30,785	32,048	34,215
Number of MFIs(Total MFI)	31	32	31	34	35	35	35	37
Number borrowers	2,495,660	2,887,043	3,243,433	3,761,072	4,270,887	4,326,422	4,695,393	5,130,115
Number of saving account	NA	NA	5,860,598	8,157,518	9,821,440	12,585,614	17,145,943	17,719,292







8. Do you think the existing land regulations are one of the constraints for farmers to access bank credit?

A) Yes

B) No

9. If your answer is yes, please list down land laws that are constraints for access to credit

10. Does your institution have policies and strategies to develop rural finance?

A) Yes it has

B) No, it has not

11. What are the activities that your institution has done in order to ensure small holder farmers access to finance to use improved technologies, fertilizer, and other inputs?

12. List down the challenges that your institution has faced in its effort to ensure smallholder farmers access to credit and measures that should be done to solve the problem