DCA LOAN GUARANTEE ETHIOPIA

IMPACT BRIEF

On the Cover: Women sorting coffee beans at a coffee washing station.



BACKGROUND

Ethiopia is blessed with approximately 107,600 square kilometers of arable land (about 11 percent of its territory); yet, it has struggled for many years to feed its people.

One problem Ethiopia's farmers face is lack of access to finance, which they need to modernize their practices and purchase machinery. Ethiopian banks generally require collateral valued at a minimum of 100 percent of the value of the loan plus interest, which is unreachable for most farmers. Since all Ethiopian land belongs to the government, farmers cannot use the farmland they lease as collateral and banks do not accept crops or other farm stock as collateral. As of June 2000, agricultural lending made up only 8 percent of the total value of outstanding loans in Ethiopia.

ABOUT DCA

USAID's Development Credit Authority (DCA) was created in 1999 to mobilize local private capital through the establishment of real risk sharing relationships with private financial institutions in USAID countries. The tool is available to all USAID overseas missions and can be used as a vehicle for providing much needed credit to an array of enterprises and underserved sectors. The evaluation in Ethiopia is part of a set of evaluations EGAT/DC is undertaking in different countries, to test a series of developmental hypotheses related to the DCA guarantees.

USAID responded to this lack of finance by providing a series of Micro- and Small Enterprise Development (MSED) and Development Credit Authority (DCA) loan portfolio guarantees (LPGs) to the Bank of Abyssinia (BOA), a long-standing, private Ethiopian bank. USAID designed the LPGs to support BOA lending, first to agricultural cooperative unions, and then to the agriculture sector in general. The LPGs with BOA span 15 years, from the end of 1999 through 2014.

EVALUATION OBJECTIVES

USAID's Office of Development Credit (EGAT/DC), which administers the DCA guarantees, commissioned an evaluation of the BOA guarantees in 2009. This evaluation assesses the performance of the guarantee relative to its objectives as defined in the Action Package developed by USAID/Ethiopia, i.e., increasing access to credit for agricultural cooperative unions and producers in the coffee, food grains, horticulture, and livestock sectors. The evaluation assesses the outputs, outcomes, and impacts of the guarantee.

The evaluation covers BOA's lending behavior and potential demonstration effects in the banking sector. It does not examine EGAT/DC's or USAID/Ethiopia's administration of the guarantee, nor does it examine the guarantee's contribution to USAID/Ethiopia's strategic objectives.

EVALUATION METHODOLOGY

This evaluation used a mixed methods approach, including statistical analysis of loan data, key informant and group interviews, and document review. It began with a review of background documents on BOA and its MSED and DCA guarantees, and continued in Ethiopia from December 7 to 19 with semi-structured interviews with BOA staff and clients, the USAID Mission, and other financial sector experts. The evaluator used comparative analysis, statistical analysis, and content pattern analysis to draw findings from the collected data, from which conclusions were drawn.

KEY FINDINGS AND CONCLUSIONS

OUTPUTS

Conclusions Bank of Abyssinia wanted to lend to the agriculture sector because it plays a major role in the country and economy and because export sub-sectors, such as coffee, generate desired foreign currency.

BANK OF ABYSSINIA LOAN GUARANTEES

Starting Year	Ending Year	Ceiling Amount ($)	Number of Loans *(as of 1/2010)*	Aggregate Amount ($)	Utilization Rate	Median Loan Size ($)	Average Loan Tenor (months)
1999	2004	1.3 million	27	2,705,538	100 %	69,606	4.71
2003	2004	500,000	6	383,546	76.71 %	66,125	1.37
2004	2014	9 million	39	8,178,511	90.87 %	172,414	15.35


At the same time, the bank saw agricultural producers and cooperatives as risky borrowers because they lacked collateral. Therefore, BOA used the LPGs to subsidize collateral requirements for guaranteed borrowers.

Between 2000 and 2008, the USAID guarantees were responsible for increasing BOA's lending to the agriculture sector from 0 to an average of 2.3% of its total value of loans disbursed during the period.

The USAID guarantees enabled agriculture sector borrowers to obtain loans larger than they would otherwise have received, if they could have qualified for any loan at all.

Findings in support of these conclusions include:

- BOA statistics show it had not lent to the agriculture sector prior to 1999 and it only began to do so with its first MSED guarantee.
- BOA's Vice President said the bank was interested in lending to the agriculture sector as a vital part of the country's economy and because agricultural exports have the potential to generate foreign currency.
- All four of the private banks interviewed said they require at least 100 percent collateral from their borrowers.
- BOA said it would not have lent to the guaranteed borrowers without the guarantee.
- BOA counted the USAID guarantees as fulfillment of 50 percent of the standard collateral requirement, thereby enabling agricultural borrowers short of collateral to obtain credit.
- The value of USAID-guaranteed loans disbursed during 2001 to 2007 represented between 0.3 and 6.7 percent of the total value of loans disbursed.

OUTCOMES

Conclusions The USAID guarantees encouraged BOA to enter the agriculture finance sector and the bank will likely continue to lend to this sector, but only to exporters for the near future. BOA continued to lend to 20% of the formerly USAID-guaranteed borrowers because they were profitable businesses. Loan terms have changed somewhat, as some former USAID-guaranteed borrowers received preferential loan terms.

Findings to support these conclusions include:

- According to BOA's loan data, the bank has given nonguaranteed loans to eight of the borrowers who first came to the bank under the USAID guarantee program. Six of the eight borrowers were coffee processors and/or exporters and the remaining two handled grain and livestock.
- BOA's lending to agriculture grew 102 percent between 2001 and 2009.
- The Vice President/Operations of BOA said that the bank's nonguaranteed lending to the agriculture sector has focused primarily on export crops, especially coffee and sesame and recently, cattle. The focus on exportable goods results from the bank's need for foreign currency.
- Of the eight borrowers who graduated from the USAID guarantees, seven provided collateral valued at less than 100 percent of the loan amount plus interest they received.
- The Vice President/Operations of BOA said that while the bank has been lending to the agriculture sector without the guarantee, it has only been to those enterprises with solid lending histories with other banks. The bank is not comfortable providing loans to new customers with insufficient collateral.

IMPACTS

Conclusions All Ethiopian banks have increased their lending to the agriculture sector since 2000. Government-owned banks' behavior results from government policy focusing increasingly on supporting agriculture. The attractiveness of certain Ethiopian agricultural exports has motivated private banks to engage increasingly with the sector, along with a professed desire to support a sector that plays a large role in the country's economy. The USAID guarantees to BOA did not play any perceptible role in other banks' decisions to lend to the agriculture sector.

Loan access has improved somewhat over the last 10 years, mainly because of the efforts of the government banks, which provide collateral-free loans to agricultural exporters.

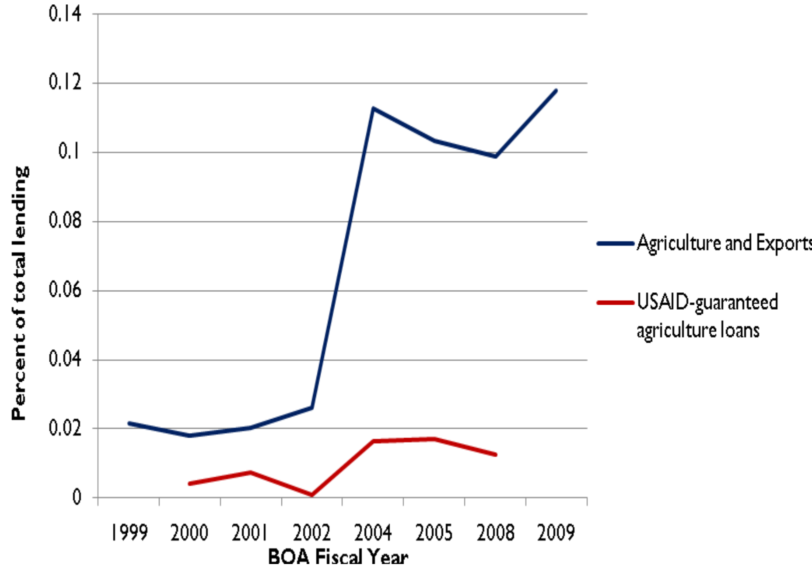
Private banks lower collateral requirements for some exporters to increase their foreign currency holdings. In addition, some agriculture sector borrowers have increased their capital and are therefore able to qualify for larger loans.

The USAID guarantees clearly influenced BOA to increase lending to the agriculture sector. However, the agriculture finance sector appears to be still largely underserved.

Findings to support these conclusions include:

- Agriculture's share of total Ethiopian bank lending has increased from 16 percent in 2001 to 20 percent in 2008.
- The state-owned Development Bank of Ethiopia began lending to the agriculture sector when it was first established 100 years ago. Recently, the government has asked it to focus on supporting agricultural exports.The state-owned Commercial Bank of Ethiopia is following Ethiopian Government policy to increase the country's self-sufficiency by lending to agriculture.
- In interviews, private banks emphasized the desire to help support the agriculture sector, and highlighted the fact that they can obtain foreign currency by lending to agricultural export sectors.
- Five BOA borrowers interviewed have received larger loans more recently than previously with little or no change in the collateral requirement, which suggests that they built up enough collateral to qualify for more credit on their own.
- Six borrowers, four banks, and the Federal Cooperative Commission (FCC) said that cooperatives, cooperative unions, and individual farmers still lack sufficient collateral to qualify for the loans they need.

BOA AGRICULTURE AND EXPORT LENDING AS % OF TOTAL LENDING



- Four coffee processors said that because the price of raw coffee has risen over the last four years, the purchasing power of borrowed funds is lower.
- Four banks and three borrowers said that banks lack the capacity to assess the creditworthiness of agricultural borrowers and therefore still rely on collateral to guard against the perceived riskiness of the agriculture sector.
- Two cooperative union representatives, a government bank, and the FCC said that cooperatives need training to help them produce more profitably and manage loans they receive.
- Two cooperative representatives and two banks said that lack of rural infrastructure poses a serious problem to both cooperatives' capacity to produce and transport their products, as well as to banks' ability to reach agricultural producers

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