



Construction of JESH Slaughterhouse in Somali Region of Ethiopia – one of the IIF recipient companies.

BACKGROUND

Ethiopia has one of the lowest financial inclusion rates in sub-Saharan Africa with only 14 percent of the adult population having access to formal financial services, a figure that drops as low as 1 percent in rural areas (World Bank, 2012).

This fact is surprising, considering Ethiopia's economy has grown on average 10.9 percent annually over the past decade (World Bank, 2014). While this growth is impressive, creating a thriving private sector remains a challenge for the country. Ethiopia is ranked 132/189 in World Bank's Doing Business 2015 index. Access to finance is cited as one of the top challenges for businesses in Ethiopia. The financial sector is highly regulated and closed off for foreign investors. Domestic credit to the private sector is constrained by government requirements to invest 27% of their gross loans in National Bank of Ethiopia (NBE) bonds and high collateral requirements

Innovation Investment Fund

To bridge this finance gap and increase pastoral communities' household income levels while enhancing their resilience to climate change, USAID-PRIME manages a \$6 million Innovation Investment Fund (IIF) that supports medium to large-scale enterprises operating within or directly benefitting PRIME-targeted areas in Oromia, Afar and Somali regional states. The fund provides matching grants and technical assistance to sustainably improve enterprises' performance and strengthen the overall market system to benefit pastoral households. The fund leverages local capital for investments in a range of market development activities that improve market linkages, generate

employment, and increase financial inclusion with the aim of increasing pastoral community household incomes and enhancing resilience to climate change. Given that more than 95 percent of the population in Afar and Somali regions is Muslim, the IIF serves as an important tool in bridging the conventional and interest-free finance gap by facilitating finance to growth-oriented businesses.

\$6M investment fund

Supports: Livestock value chain actors, financial institutions, business expansion plans, innovation research

-Minimum 50 percent co-investment requirement (24.8M USD leveraged to date)

In 2013, Ethiopia's private credit ratio was only **15.9%** compared to an average of **30%** in Sub-Saharan Africa (African Economic Outlook: Ethiopia, 2014)

HOW IT WORKS

PRIME issues tenders and a review committee rewards successful proposals, from eligible enterprises, with a grant or contract.

Recipients are required to comply with strict guidelines and to share at least 50 percent of the investment cost.

An important note is that the IIF tries to facilitate loans from financial institutions before providing a grant, so as not to bias the market and to build linkages between loan providers and the business community.

Direct Versus Indirect Support

If PRIME's objective is to increase household incomes and enhance resilience to climate change of pastoral communities, why not provide support directly to these households? Why support "big" companies? Households are part of systems, including market systems. Therefore, strengthening market systems (the right way) will also positively impact households. PRIME uses a facilitative approach to strengthening the market systems within which households operate. A recent report provides additional insights into, not only why market systems matter when it comes to building resilience and sustaining livelihoods, but also why they are absolutely necessary: "To be resilient, individuals and households must engage with market systems and those systems must have the capacity to withstand, adapt and transform in the face of shocks and stresses" (Leveraging Economic Opportunities Report #6, 2015).

Necessary Conditions for Partnership Success

Not every partnership with the private sector will be successful, unless you pay close attention to a number of factors. Here are some success factors we have found absolutely necessary:

- Finding the right business: One that is growth-oriented, run by someone who expects to work hard, and has the capacity to manage a sub-award (capacity-building is imperative).
- Extensive due diligence: The existing screening mechanism is designed to assess non-governmental organizations (NGOs), rather than private businesses. Improved private business engagement toolkits are needed.
- Having the right NGO team with the right skills. Business understanding is critical, especially when designing, selecting or sourcing deals, working with the companies to help them understand the different components involved in receiving grants, knowing what makes a good investment and what does not, and understanding minimum requirements when companies look for investors.
- Putting a good monitoring and evaluation plan in place from the design stage. Reporting timeliness must align with those for donors.

The owner of Barwako Milk Processing Factory, Amir Mukhtar, is optimistic about the prospects of the company. He says, *"While the completion of this project poses numerous challenges, the vision of working together with the milk producing communities and the support we are getting from PRIME and USAID keeps us confident that what we are doing will bring tremendous benefits to the households- who we create markets for, the consumers, and the national economy."*

What Are the Right Incentives

- Grant, contract, loan, equity: Given Mercy Corps is registered as an NGO in Ethiopia, we are legally unable to provide anything other than grants. We looked into other mechanisms, but the legal structure does not make it feasible. If possible, choose a loan or equity stake so not to negatively influence the existing market structure.
- Deal size: Based on our experience, anything below \$400,000 will not have the desired impact on indirect beneficiaries.
- Cost-share: So far, for the larger investments (above \$500,000), we are allocating PRIME 30 percent and private sector 70 percent of costs. But, depending on the activity, we are willing to share costs 50:50.
- Types of costs covered: Fixed assets only. Providing working capital will jeopardize the sustainability of the business, as it will be subsidizing rather than supporting expansion/start up or growth. Having sufficient working capital from the private sector side is crucial for the success of the project.
- Right agreement/contract format: The typical sub-award template is designed for NGOs, but is not a good fit for private sector engagement.

Besides conditions listed above, expect to spend a considerable amount of time sensitizing the private sector, local government, and the donor before initiating any new and innovative funding models.

Anticipated Outcomes

What kind of impact are we talking about? To date, the IIF has signed agreements with six companies through five cost-shared grants and one cost-shared contract. The total value of USAID' support to these companies is around \$6 million USD, with private sector cost-share of \$24.8 million USD, or 80 percent!

Anticipated outcomes in the short-term include

- Creation of over 4,000 full time and 1,000 temporary jobs
- Improved market linkages for over 500,000 households
- Increased incomes benefitting more than 30,000 households
- Access to financial services for 50 percent of mobile phone owners in the Somali Region
- Establishment of 1.1 million new bank accounts through more than 4,000 mobile agents.
- Facilitation of 12 additional private investment deals



Women Milk groups benefit from increased demand from IIF-supported milk processors.

IIF Grants and Sub-Contracts (Project Commitment/Total Project Value)

Jijiga Export Slaughter House: \$1.5M/\$6.5M

Establishment of a slaughterhouse in Faafan, Somali regional state to process meat for export.

Somali Microfinance Institute & BelCash Technologies: \$350K/ \$1.5M

Establishing mobile banking through an agent model in Ethiopia.

Renew Investment Advisory: \$2M/ \$8M

Encouraging private equity investment in PRIME targeted areas for promising livestock-related ventures facing capital constraints.

AGP Poultry (Mekele Farms): \$1.2M/\$6.5M

Expanding operations to pastoral communities in Oromia region to produce and market day old chicks, feed and medicine via franchise model.

Barwako Milk Processing Factory: \$370k/ \$1.3M

Establishing cow and camel milk processing plant in Jijiga for both local and export consumption. The plant has capacity to process 15,000 liters of cow and camel milk per day.

Addiskidan Milk Processing Factory \$500k/ \$1M

Expanding production capacity for a medium-sized milk processing factory currently producing 10,000 liters per day.

Where Are We Now?

Now that we have signed all of the matching sub-grants and contracts, we are closely monitoring recipients' progress and providing technical support where needed.

PRIME is a 5-year, \$62 million USAID-funded initiative to increase household incomes and promote resilience to climate change through innovative, scalable, market-driven approach in pastoralist areas of Afar, Somali and Oromiya regional states in Ethiopia.

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