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Amhara Credit and Savings Institute (ACSI), Ethiopia—A State-Owned Financial Institution[1]

ACSI operates in a tough environment with the majority of its clients being the rural poor. ACSI's average loan size hovers close to $100, is heavily state influenced, and has poverty alleviation as its ultimate goal. In many other settings, this would lead to political patronage and financial disaster, yet ACSI has managed to achieve high levels of sustainability and financial independence.

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ABOUT ACSI

ACSI began operations in 1995 as a department of the Organization for the Rehabilitation and Development of Amhara (ORDA), an Ethiopian local nongovernmental organization (NGO), and was licensed as a separate microfinance share company in April 1997. Its primary mission is to improve the economic situation of the low-income, productive poor in the Amhara region, primarily through increased access to lending and savings services. ACSI seeks to maintain cost effectiveness in service delivery and integrates its activities with the government and NGOs working toward achieving food security and poverty alleviation. In fact, from the outset, ACSI has had a strong link with government: the state government holds 25 percent of ACSI's shares.

ACSI could be described as an anomaly when compared to the conventional wisdom on microfinance institution (MFI) performance and efficiency. During its first decade of operations, ACSI has grown its loan portfolio to US$44.5 million, with deposits totaling $21.1 million. Portfolio quality has consistently been excellent (even though the majority of the portfolio is agricultural in nature), and operational efficiency has tended to improve every year—even though efficiency levels are already high. The key measure of operating efficiency, the

[1] This microNOTE is based on the Accelerated Microfinance Advancement Project (AMAP) Financial Services Knowledge Generation (FSKG) state-owned retail banks report, *Amhara Credit and Savings Institute: Ethiopia,* by Phetsile Dlamini and Neil Brislin of ECI*Africa*. It is based primarily on the information gathered and reports generated from the 2003 MicroRate visit and rating. The team was accompanied by USAID and Swedish International Development Agency representatives as well as a management information systems specialist. This paper has been updated with additional information from ACSI management and discussions with MicroRate subsequent to their August 2005 ACSI rating update. The full report is available on http://www.microlinks.org.

Amhara Credit and Savings Institute

Summary Stats	US$, in thousands, except as indicated				
	Dec-01	Dec-02	Dec-03	Dec-04	Jun-05*
Net Operating Income	(148.6)	541.3	1,494.2	2,829.9	1,681.9
Gross Loan Portfolio	13,868.7	18,121.8	24,403.2	36,206.4	44,488.9
Savings	9,919.6	11,564.1	14,924.5	19,999.7	21,186.4
Cash & Equivalent	6,284.3	4,430.1	6,834.4	12,372.6	12,166.0
Portfolio at Risk, 30 days (%)	2.5	3.5	3.1	1.7	1.3
Operating Expense Ratio (%)	8.3	9.2	7.8	6.2	6.0
Average outstanding loan size (US$)	90.9	83.9	84.5	103.1	112.8
Portfolio Yield (%)	13.3	17.8	18.5	18.0	17.8
Return on Equity (%)	(1.9)	11.2	16.6	24.4	29.9
Debt/Equity (:1)	3.1	3.2	1.1	2.0	2.0
Total Capital/Risk Weighted Assets (%)	33.5	28.7	58.1	50.1	52.4
Cash and Liquid Assets/Total Deposits (%)	63.4	38.3	45.8	61.9	57.4

* Represents a six-month period. Relevant ratios have been annualized. Source: MicroRate Africa.

operating expense ratio, has dropped to 6.0 percent, which is among the lowest in the world for an MFI[2]. In the past, high levels of efficiency have typically been associated with MFIs operating in urban areas and targeting the upper end of the typical MFI market.

ACSI operates in a tough environment and the majority of its clients are the rural poor. ACSI's average loan size hovers close to $100, is heavily state influenced, and has poverty alleviation as its ultimate goal. In many other settings, this would lead to political patronage and financial disaster, yet ACSI has managed to achieve high levels of sustainability and financial independence. This note examines how they have achieved these results and what lessons can be learned.

ENVIRONMENT

Ethiopia is a country of 71 million people with a gross domestic product per capita of $112.70. The Amhara National Regional State, where ACSI operates, has the highest poverty levels in the country and has a population of 18 million, of whom most live in rural areas. The mountainous terrain, combined with limited roads and transport networks make it hard to access. As a result, delivery of financial and other services is difficult.

Legislation allowing the establishment of deposit taking microfinance, liberalization of financial markets, and the removal of a number of existing controls in the economy created an environment conducive to the development of ACSI. But even with the favorable legislative context, the financial sector remains under-developed, foreign investment is prohibited, and a gap in the market exists in terms of the delivery of financial services throughout the country.

[2] Defined as operating expenses for the period divided by the average outstanding portfolio for the period.

The changes in government policy away from a socialist orientation toward free market principles helped to influence the establishment of MFIs by creating opportunities for self-employment and income generation for the poor to escape poverty. These changes prompted some NGOs in Ethiopia—initially involved in the provision of relief and humanitarian support—to extend their services to the provision of credit to microenterprises for the rural and urban poor.

TARGET MARKET AND PRODUCT OFFERINGS

In line with government policies, ACSI's target focus is the low income, rural-based, productive poor, with a special emphasis on women. Priority is given to those areas that are food insecure, and a combination of poverty assessment and targeting methods is used to identify prospective clients.

The organization is committed to providing innovative and diversified products to its clients, including a variety of savings and credit products. ACSI now offers three types of credit products (installment, term, and asset loans), savings accounts (both passbook and term/time deposits), money transfers (currently limited to institutions), and pension fund payments on behalf of the government. It is exploring the provision of money transfers for individuals, micro insurance, and credit services to water point construction groups for re-building or maintenance of their water points.

ACSI has remained focused on its target market, with an average outstanding loan size just above $100 in 2004 and 2005. To date, almost 70 percent of the Kebeles (villages) in Amhara have participants. However, the number of people serviced—394,374 clients at the end of June 2005—is only about 10 percent of the poor people in the state, leaving considerable scope for continued growth, particularly if ACSI introduces a vertical growth strategy to include more than just the poorest of the poor.

ORGANIZATIONAL STRUCTURE

Largely reflecting the rugged environment in which it operates and its manual management information systems (MIS), ACSI has decentralized operations to the sub-branches, the only client-facing part of the operation. The sub-branches report to branch offices, which then forward consolidated information to the head office. While this system is effective, it is time consuming (taking a month to produce consolidated reports) and costly in terms of the number of staff required to capture data. ACSI does recognize that it is open to errors and fraud, and an automated system would be more efficient.

While operations are decentralized—subject to the strict implementation of policies and procedures—strategic decision making is centralized at the head office, with a strong tier of management and senior staff. Staff are recruited at entry level, and offered growth prospects through a clear and well-understood career path from field offices to branch offices. The lack of a computerized MIS has made it difficult to implement individually based performance incentive schemes (apart from tertiary education for select, high performers), and current incentives are based on branch and sub-branch performance, and are limited to annual salary increases.

CRITICAL SUCCESS FACTORS

ACSI's accomplishments are the product of a number of factors.

Operational Efficiency. ACSI is operationally highly efficient, and has been so since inception, reaching scale quite quickly. In large part, the ability to intermediate savings and government support more directly in the earlier years helped the institution scale up its operations. The operational efficiency is the result of the decentralization of operations and the accompanying standardization of processes across the organization, a stable and committed workforce, low staff costs, and volunteer community involvement in the screening of loan applications.

Financial Independence. Good management has translated operational achievement and efficiency into financial success. By capitalizing its profits as retained earnings, ACSI has built up its reserves and a strong balance sheet, further fueling the institution's ability to grow. Importantly, this has led to financial independence. As ACSI is not dependent on government or other outside funding, it is largely insulated from negative political influence on its operations, which has allowed it to chart its own course and stay true to its vision and mission.

Community Involvement. A key factor behind ACSI's success is that it draws on the support of the local community (the Credit and Savings Committee) to prioritize service delivery according to poverty levels and to screen all loan applications. Interestingly, these screenings are conducted in open forums, and the whole community can have a say. The committees also facilitate follow-up and monitoring. These committees are an effective way of using local knowledge to assess creditworthiness and strengthens ACSI's portfolio quality.

Committee members are representatives of the community and there is no financial or material benefit derived from their involvement other than respect and recognition for being transparent and fair, and displaying a wealth of local knowledge and wisdom. This minimizes the threat of collusion and any distortion by the committees.

Portfolio Quality. Portfolio quality is good, reflecting the community involvement and customized products. The peer group pressure is still effective and plays a key role in ensuring that all loans are repaid. In addition, clients are encouraged to settle their debts whenever they have the money, and staff provides close follow-up and group monitoring.

Product Development. ACSI has been able to successfully replicate products in a way that adapts and designs products to fit into the existing environment and community structures, and making optimal use of what is already in place.

Staff Commitment. Underlying all of this success is the dedication and commitment of ACSI's staff. Faced with a challenging and physically demanding work environment, they are committed to what they are doing, and by and large share the institution's vision and mission. However, the difficult working conditions lead to staff turnover—trained staff from sub-branch and branch levels find employment in government departments where the salaries are the same but working conditions much easier.

Relationship with Government. While the risks of a close relationship with government for financial institutions are well documented, this specific relationship does work to ACSI's advantage. The risks remain, but ACSI's financial independence strengthens its position as does the presence of a strong management team.

Competition. There are 23 licensed MFIs in Ethiopia and 900,000 credit clients. The majority of these MFIs' operations are located in urban and semi-urban areas with little or no competition for clients in rural areas. ACSI, therefore, is a leader in financial services provision in Amhara. Although the threat of competition always exists, ACSI is well ahead of its peers, by far the largest MFI in Amhara.

REMAINING CHALLENGES

Although its results to date lay a strong foundation for future success, real challenges remain. The following is a summary of key lessons from ACSI that may serve others developing rural and state-owned financial intermediaries.

Infrastructure. ACSI operates in an environment that is characterized by low levels of infrastructure. This poses many operational challenges. One of its biggest challenges is the implementation of a computerized MIS, a process they recently began.

Information Flow. Probably a result of the manual systems, ACSI has perfected the upward flow of information in the organization, but needs to improve the amount and regularity of feedback down to branches and sub-branches, which often do not have access to the information they need to make decisions.

Ownership and Investment. With no foreign financial investment permitted in Ethiopia, the regional government and local NGOs own ACSI. This restriction limits inflows of capital into Ethiopia and forces MFIs to focus only on local sources. Only 2.5 percent of ACSI's equity base is made up of paid-in equity. If ACSI is unable to attract local investments, the restriction of foreign financial investment is a potential barrier to ACSI's growth and development prospects. Although ACSI has significant local funding lines open that have not been drawn on, the potential positive influence of external shareholders on good governance and limiting undue interference should not be underestimated.

Risk Management. Without a comprehensive risk management framework in place ACSI is not well equipped to identify, quantify, and manage the risks to which it is exposed. While it is not uncommon among small MFIs to have no risk management policies in place, it is more of concern for ACSI because of the millions of dollars in client savings in their custody. ACSI would benefit from assistance in undertaking a comprehensive risk assessment exercise that will result in a detailed review of risks facing the institution and strategies aimed at mitigating those risks.

Diversification. ACSI has made some headway in terms of increasing its array of products, however it needs to further diversify its product range to reduce the risk exposure of its current portfolio, which is concentrated in agriculture. To sustain its growth ACSI would benefit from a more diversified portfolio.

State Control and Influence. Despite its financial independence, two out of eight of ACSI's Board Directors are government officials. Their influence has been witnessed in their ability to keep interest rates low despite the obvious high costs associated with lending to this target market and although the ceiling on rates was lifted some time ago.