

microLINKS SPEAKER'S CORNER:

Microfinance in Central Asia

The second microLINKS Speaker's Corner e-conference took place from December 14-16, on **Microfinance in Central Asia**. The host was Janice Stallard of the Central Asia Microfinance Alliance, who presided over the conference from Tashkent, Uzbekistan. Discussion ranged from general questions about the particularities of microfinance in Central Asia to very specific challenges around regulations and legal complexities that have played out in specific countries.

microLINKS is the knowledge sharing system for USAID's microfinance projects. For more information, visit <http://www.microlinks.org>.

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"Event Welcome"

12-14-2004

Janice Stallard

Hello and welcome to our Speaker's Corner event, "Microfinance in Central Asia". I'm Janice Stallard, and I work as ACDI/VOCA's Chief of Party for the Central Asia Micro Finance Alliance (CAMFA). CAMFA is a four-year, USAID-funded project that is designed to support and strengthen the micro finance organizations in Central Asia.

We have a very broad definition of micro finance in Central Asia. Our project includes not only typical MFIs, but also credit cooperatives, credit unions, and farmer's associations. As such, CAMFA works with a whole host of different organizations providing technical assistance and mini grants to strengthen governance systems, accounting and MIS, internal control, management practices, and lending systems.

I'd like to kick off the event with a first topic.

We have a very interesting situation in Central Asia for micro finance. Each country has taken a different approach to formalizing the industry. For example, in Kyrgyzstan and Tajikistan there is a formal MFI Law that allows for non-profits as well as for-profit deposit mobilization. In Kazakhstan, there is an MFI law that is fairly restrictive and a Non-Bank Financial Institution (NBFI) regulation that allows for reporting to the Central Bank. In Uzbekistan, MFIs have a fairly informal status and there is still much work to be done to legalize the industry.

Do you have any questions about how the legal and regulatory environment works in Central Asia? Do you have any specific experiences in the region you would like to share with the audience?

"How do the Central Asian countries differ? How does microenterprise vary across the region?"

12-14-2004

Tony Pryor

Hi, Janice! Let me ask some more general questions, as part of this introductory thread, which are more "backgrounders", compared to Barry's very thoughtful, and specific, thread. For those of us not familiar with the region, in a nutshell (ie a short para.) can you summarize the similarities and differences between the CAR countries, in terms of variables that affect the spread, profitability and sustainability of micro enterprises?

Are such activities more vibrant in countries with more growth prospects and a strong(er) policy framework, or are they more vibrant where the state is weaker, and the economy more vulnerable (as sometimes happens in Africa). And if you can, based on ACDI's experience, how do MED (and especially micro-fi) programs) differ in terms of impact and ease of implementation between CAR and other regions (including Europe to the west and the rest of Asia to the east and south). Many thanks.

Tony Pryor, IRG

12-15-2004

Janice Stallard

Hello Tony,

Thank you for the question. There are so many differences among the countries we work in -- but at the same time -- many similarities.

All of the countries (Kazakhstan, Kyrgyzstan, Tajikistan and Uzbekistan) are faced with existing financial systems that do not serve small or micro businesses. Although this is slowly changing (much to the support of EBRD's credit lines to local commercial banks), small businesses that have no collateral are usually faced with the options of borrowing from friends or money lenders.

There are other similarities regarding poverty, access to cross border trading (due to custom's restrictions, working in isolated locations,

etc), and limited exposure to business skills.

I believe one of the issues that makes each country distinct is its legal and regulatory environment. As described in my opening statement, the differences are significant.

I would say it is my opinion that we have found more MFI/NGO programs in the weaker economies (Kyrgyzstan and Tajikistan). However, Uzbekistan stands out as its own example.

I hope I have somewhat answered your questions. Please ask follow-on questions if you would like more clarity.

Janice

"Lessons from Tajikistan's uneven development of laws and regulations?"

12-15-2004

John Berry

Dear Janice,

A specific question about lessons learned from the Tajikistan experience at developing a legal and regulatory framework.

After a good bit of wrangling, donors in TJ eventually funded consultants to prepare draft legislation for MFIs. They got buy in from the MF community and the law eventually passed. However, there appears to now be an issue because the regulatory framework wasn't developed at the same time and now no one wants to register under the law until they see how the regulations turn out.

What have we learned from this? How can we do better next time? And what do we do next?

John

12-15-2004
Janice Stallard

Hello John,

Nice to hear from you! I am glad that you stepped in since you have recently visited the region.

To tell everyone honestly, I think that we have not done such a great job learning from each other in Central Asia regarding what has already been achieved on the legal and regulatory front. I know right now, when we try and talk to the Uzbek officials about the Kyrgyzstan experience, they are not interested. It seems a bit strange -- but true.

It is also true that the MFIs in Tajikistan do not want to register under the new MFI law because they are afraid of what the normatives might have in them (in terms of reporting requirements and restrictions on their activities). From the CAMFA side, we have been telling them that they need to go ahead and register because they will have to eventually. And, since most groups want to register at the bottom level of this law (that is, as a non-profit) they are likely to have almost no regulation from the Central Bank.

But, this is new to all the MFIs in Tajikistan that have never been regulated. They are nervous and it is somewhat understandable. We have tried to tell the Tajik groups that in Kyrgyz the Central Bank doesn't really do much in terms of regulating the lowest level, non-profit MFIs. But, we have not been able to convince anyone to register... yet.

The lessons learned here. I am not sure. Right now, it is the Central Bank holding up everything because ... we do not know why.

The Tajik MFI Coalition has been instrumental in getting the MFI community's views to the Government. To me, they have proven how powerful they can be and I think that is a positive thing. CAMFA is helping all four countries develop their own MFI Coalition/Association that will be able to lobby the Government and advocate for change.

What to do next?? I am not sure! We had heard that the ADB was going to take over the final drafting and approval of the MFI normative acts but our contacts in Dushanbe can tell us nothing right now.

I have tried to include the USAID/Dushanbe Mission folks into this discussion and it would be great if they could give us some direct feed-back on this issue.

Janice

12-15-2004
Scott Kleinberg

Greetings Janice,

I am enjoying this dialogue. I have a follow-on question on the Tajik experience. When the legislation was drafted, there was a camp that, at the time, felt that the process was moving too quickly and had not provided sufficient time for dialogue between the government and MFIs, or even among the MFIs themselves.

Do you think that a longer period of dialogue at that time would have promoted a higher degree of confidence among MFIs today, and perhaps resulted in a higher rate of registration?

Thanks and Happy Holidays,

Scott

12-15-2004
Janice Stallard

Hello Scott,

Nice to hear from you. I did not know that so many folks follow the activities going on in Tajikistan. That is interesting!

Yes, I know that some of the MFIs complained about lack of time to comment. However, if you look back over the timing given to the writing, review, editing and finalization of the MFI Law in Tajikistan there was in fact a 6-month window for this process. I do think that IFC gave everyone adequate time to comment.

It is my impression that the MFIs remain hesitant about the law because they still do not understand what the process will be. Most importantly, because the normative acts are not finished, they are concerned about how they will be regulated.

As I said before, based on the Kyrgyzstan experience I do not think that the Central Bank is going to highly regulate the MFIs in Tajikistan. But change is difficult and when you take that first step off a cliff -- it can sometimes be scary.

Please stay in touch.

Janice

"Organized crime and BDS?"

12-14-2004

Ernest Parker

I have only a limited experience in central asia. Here's my question. First, would you say that in any of the Central Asian states there is a problem with organized crime?

If so, does that pose an interesting challenge to the guidance that you give to enterprises? I was wondering if, for instance, among your BDS offerings was some sort of counseling or policy pertaining to pressures on a business that could arise from organized crime.

12-14-2004

Janice Stallard

Hello Ernest,

It is an interesting question that you raise about organized crime. I honestly do not think I am qualified to answer this question. I would say in general we are faced with an environment that is not transparent in Central Asia. Clients are used to paying bribes and that attitude can be translated to their work with MFIs.

I think that all the MFIs struggle with the issue of dealing with corruption. In fact, CAMFA thinks this is such an important issue we are organizing a special workshop on how MFIs handle things like "ghost" clients, loan officers taking a 'share' of clients' loans, and general bribe taking.

Does anyone know of other specialized courses on dealing with corruption within MFIs?

I appreciate your question and welcome more thoughts from others on the subject.

12-14-2004

Mike Field

Hello everyone,

I am Michael Field and I work on the BDS Team in MD.

While it is probably better to limit this discussion as it is a bit off track from micro-finance in Central Asia. I did want to provide a comment or two. I just returned from Central Asia where I was working with the Mission to review their current BDS program the Enterprise Development Program - run by PRAGMA -- which is heavily involved in addressing BDS and policy constraints. From what I saw there, organized crime is a loaded term and may not be the right descriptor for what I saw was a huge problem - a poor enabling environment that has fostered a lot of informality. Informality in the Central Asia context includes everything from tax authorities shaking down business people, to business people avoiding onerous regulatory requirements and inconsistent enforcement practices, to some organized groups targeting businesses for protection money (e.g., roofs). The mix and extent of informality is different for each country as they vary greatly in terms of how closed or controlling the government is with the private sector.

In general, EDP counsels firms to try and stay as formal as possible and still stay in business, and to organize through associations in order to lobby government for greater transparency and accountability. While I would question some of the specifics of what EDP is doing, I would say that it is important to maintain a two prong strategy that fosters greater (faster growth) and broader (more people benefiting) private sector growth (within the current environment), as well as participatory policy reform at the macro and micro levels.

Maybe, we can take up this issue in another forum, if people are interested??

Mike

"Defining microfinance in Central Asia - Which institutions count?"

12-14-2004

Kate Druschel

Hi Janice,

I'm so glad to see you opened this up with a comment on legal and regulatory issues. At the IRIS Center, we've been thinking about these things for quite a while and I spend a bit of time recently in Georgia looking at their regulatory environment.

I should let anyone interested know that IRIS has been working with CGAP to develop a database of legal and regulatory information on some 50 different countries. It will eventually form the backbone of a Regulation and Supervision Resource Center on the Microfinance Gateway, but until then is housed in an interim site at <http://www.cgap.org/regsup/index.shtml>. Information on the leg/reg environment in Kyrgyzstan, Kazakhstan, Tajikistan and 47 other countries, including the relevant laws and regulations, can be found there.

I'm curious about your definition of microfinance in Central Asia and notice that it does not include more formal types of financial institutions, including commercial banks. In Georgia, we saw that 3 of the 4 largest banks were moving significantly into the lower income markets, offering smaller loans with less paperwork, access to the payments services, and other services to customers and enterprises traditionally served by the NGO type MFIs. This was happening in the midst of increased emphasis on market-oriented strategies among the banks, who began to realize that the large corporate market just doesn't exist there and the only way to survive is to find new markets among less traditional customers. They'll soon begin expanding to agricultural products as well.

Why do you think there is such a focus on the traditional NGO model in Central Asia? Are banks beginning to serve these markets as well? Do you think the legal system is too rigid in limiting the work of "microfinance" to a designated type of institution?

Thanks,

Kate Druschel, The IRIS Center at the University of Maryland

12-15-2004

Janice Stallard

Hello Kate,

You made really good points! Yes, there are several big down-scaling programs going on in Central Asia with EBRD funding. The largest and most successful of these is in Kazakhstan. These programs have not gone as far as what you are describing in Georgia. However, I can see that happening in the coming years.

In Kazakhstan, there is also one large MFI (the Kazakhstan Loan Fund - KLF) that is transforming into an MFI Bank. In the long-term they hope to do things like payment services, etc.

I would say, however, that most of the MFIs in Central Asia are based on an NGO model. Many are fairly small and working in limited geographical areas. This is a reflection of how these groups were started -- from donors interested in a specific target market.

As CAMFA, we expect to see more and more mergers of these smaller groups in the coming years (and we hope to facilitate some of these).

Janice

"Scale of intervention - Any luck in 'Up-scaling down-scaling?'"

12-15-2004

Tony Pryor

The experience with the banks moving to "reengineer" themselves is interesting, but so is the tendency for the NGO model to stay the dominant model in CAR.

On the downscaling/upscaling issue, let me ask a related question, which is a chronic issue for any donor supporting microfi programs: success at the entrepreneur level almost requires a "retail" approach, getting the level of intervention down to a scale (and level of trust) that works for the individual. The problem of course is that we all seek to impact millions of such individuals, and figuring out how to "ramp up down-scaling" to my mind is one of those operational conundrums affecting many sectors in development, including micro-fi.

Just how is individual success in this region being ramped up? What are the successes, near misses, and clear failures (without being too specific, of course!)? Are lessons being shared across the region, and lessons that include both what not to do, as well as successes? (And again, differences between these countries would be worth highlighting for us all).

12-15-2004

Janice Stallard

Hello Tony,

This is a really tough question Tony. I hope others can join in this dialogue.

There is at least one large MFI (by large I mean with somewhat national coverage) in Kazakhstan, Kyrgyzstan, and Tajikistan. It is interesting to note that these were started with various methodologies, levels of technical assistance, and economic-political environments. As such, it is hard to draw too many parallels.

What I do see happening with the larger groups in Central Asia, as well as in other parts of the world, is a general trend towards commercialization. Whether that means becoming a for-profit and

taking deposits -- or just becoming more focused on the bottom line. These things are happening.

As a result, I think the industry is maturing and will achieve even greater successes. Compared to S-E Asia, we are still working in an infant industry here in Central Asia. There has been a great deal of building on the lessons learned from other regions. And, unfortunately, there have also been some failures (in my opinion, these are most often seen when a lack of appropriate levels of TA are given to start-up MFIs).

All is all, I think there is a ramping up. It will take time, money, and a great deal of effort by the MFI community, donors, and people working on the ground. But, I do think we are moving in the right direction.

Janice

"What are the Central Asian MFI's like? Big or small, foreign or domestic?"

12-15-2004
Chris Dragisic

Hello Janice,

I'm curious whether most MFIs in Central Asia are homegrown, foreign, or a mixture of the two? Are they primarily small or large? I always think it's interesting to compare the mix of MFIs in different countries. Local MFIs may be most successful, at least at first, at matching local needs and customs. Yet some of the international microfinance support organizations bring a wealth of experience and knowledge. Thanks!

12-15-2004
Janice Stallard

Hello Chris,

Nice to hear from you. In fact, most of the MFIs in Central Asia have started with some outside funding. Unfortunately, this has not always

been supported through technical assistance and as a result there are lots of small groups that are not functioning as effectively as we'd like to see.

There has been a trend, however, in Kazakhstan for 'homegrown' MFIs to start popping up. This is a direct result of a new MFI law passed in Kazakhstan that provides a profit tax waiver for several years. There are now 152 locally registered MFIs in Kazakhstan; all very small and localized. According to the registration records that we have checked, many of these have been started by government officials and others who are seeking unofficial ways to distribute funds and make some profits. CAMFA does not work with these groups.

Really interesting question and I'd be curious to hear from others regarding different regional experiences.

Janice

12-19-2004

George Borugu

Thank you for your information and advice. It is my view that MFIs should be operated under a formal legal framework. This is important because MFIs everywhere grow and develop into something that is always different from the original. Some MFIs become so big they are bigger than some formal banks in the country. Hence to ensure that members' funds are managed under a system that is financially and legally secured and credible it is my view that each country should establish a formal and legal framework within which the further development and growth of the industry can be directed.

George Borugu

"Who can mobilize deposits? Who can operate independently?"

12-14-2004

Barry Lennon

Hi Janis,

I have a couple of questions about microfinance in the Central Asia region. First, I think you mentioned Kyrgyzstan and Tajikistan as having legislation that permits non-bank financial institutions to mobilize and intermediate deposits? How many MFIs are actually mobilizing deposits, and of those, to what degree are deposits financing total assets?

In Uzbekistan, I had understood (perhaps mistakenly) that the only microfinance organizations that are actually operating independently are the credit unions. I thought all the other MFIs were being run by international PVOs who are using the U.S. Government's bi-lateral agreement (as grantees) to avoid what some consider to be onerous tax liabilities. I'm sure there are indigenous NGOs engaged in microfinance lending, but to what degree are U.S.-supported organizations legally registered to operate in Uzbekistan? And, is this a potential longer term problem once USAID funding ends.

To be more specific, I'm thinking of the ACDI VOCA microlending operation in Ferghana Valley. I remember that program as being very successful in lending to the owners of green houses. In fact, so successful the ACDI VOCA manager was seeking more grant funding to finance more lending. The question I didn't see answered was -- What happens to the assets of that project when the Agreement between USAID and ACDI VOCA ends? Who will "own" those assets, and how will they be used post-USAID?

Sorry about all the questions, but I'm taking advantage of your availability to bring myself up-to-date.

In closing, I hope you and your staff have a very Merry Christmas.

Best from Washington,
Barry

12-15-2004

Janice Stallard

Hello Barry,

Great questions. Yes, there are laws in Kyrgyz and Tajik that allow for the mobilization of deposits by MFIs. In neither Kyrgyz or Tajik are any MFIs yet taking deposits. In Tajik, the law was only recently passed and (as far as I know) no groups have registered under the new law. In Kyrgyz, there are several groups interested in starting to take deposits but none do so yet (as there is a 2-year waiting period).

Uzbekistan always requires a separate discussion. Yes, there are locally registered NGO/MFIs in Uzbekistan that operate independently. These have been funded by the UNDP and NOVIB - among others. The two big USAID-funded programs (FINCA and ACIDI/VOCA) still work as Representative Office/Branches of their HQ. Mercy Corps also has a large program funded by various sources and operates as a Representative Office.

In Uzbekistan, MFIs operate under "Resolution 309" which allows 'named' institutions to disburse loans up to \$3,000. This resolution provides these groups protection from paying profit taxes until 2006.

CAMFA has joined an effort by several of the larger MFIs in Uzbekistan to establish an Uzbekistan MFI Coalition/Association. We call it the MTA. We are hoping that the MTA will be able to provide lobbying support and a venue to organize trainings for the MFIs. Most urgently, the MTA is coordinating with the IFC, UNDP and others to pass a revision to Resolution 309.

Regarding your very specific question on the Fergana Valley Project, I am sure Emile Soule will jump in. However, I can say that it is ACIDI/VOCA's position to always localize institutions and transfer all of the assets and ownership to the local institution. Emile is working hard to do that.

Let me know if you I have answered your questions.

Janice

"Lending services and Technical Assistance: Separate recipients, or the same?"

12-15-2004
Andy Reuter

Hi Janice. I have some general, high level questions about CAMFA, more for my personal understanding and interest than anything else. As I understand it, CAMFA is structured to provide both business services to MFIs as well as lending services through Frontiers. Is the demand you're seeing for TA in business services coming from the same MFIs who are borrowing through the Frontiers lending vehicle? If not, what are some of the differences between the two groups?

Thanks in advance!

Andy

12-15-2004
Janice Stallard

Hello Andy,

Super question and you let me talk about my project.

CAMFA works with competitively selected MFIs throughout the region. To date, we have funded and provided TA to 17 MFIs. We select these MFIs based on: (1) a set of selection criteria; (2) financial statements and general financial health; (3) openness to change (and CAMFA's recommendations).

Once we have initially selected an MFI, the CAMFA team conducts a field-level diagnostic (similar to the CGAP Institutional Assessment). Based on our findings from this diagnostic we conclude a formal partnership agreement and make a set of recommendations to the MFI. Actually, these recommendations come more in the form of a work plan, with specific tasks (for the MFI and CAMFA), deadlines and benchmarks.

I say all this because we are not providing BDS services in the true form. The only generalized assistance we give to the MFI community at

large is: translations of best practice articles, regional conferences in Russian, and co-financed trainings.

To answer your question about Frontiers. To date, Frontiers has been lending for 5 months. We have 2 Frontiers' clients that are also CAMFA partners. We'd like to see that increase - as that was much of the theory behind the project (build the MFIs up to the point where they could take a commercial loan).

We've been surprised, however, at how many MFIs have applied to Frontiers in these initial 5 months that were not CAMFA partners. To us, we feel that this re-affirms the huge need for an MFI wholesale lending facility for the region.

I hope I was able to answer your questions.

Janice

"Challenges, mobilizing savings, and foreign ownership restrictions"

12-15-2004

Janice Stallard

Here is a second question for our event:

In my experience, Central Asia is faced with several key challenges. First, the legal and regulatory environment does not always allow for the transparent operation of micro finance institutions. This is the case in Uzbekistan (where CAMFA is headquartered).

We are also faced with situations, such as in Kazakhstan, where high performing groups that want to take deposits are faced with the single option of becoming a bank. As such, these MFIs must meet all of the physical security requirements, minimum charter capital norms (\$15 million) and MIS/accounting reporting standards of second tier banks.

A second challenge is limited lending capital that will allow MFIs to achieve scale of outreach. This challenge is being partly addressed by CAMFA. We have established the first wholesale lending entity for MFIs in the region - Frontiers. Frontiers is physically located in Kyrgyzstan and makes wholesale loans to MFIs across country borders.

What are the challenges to micro finance specific to your region?

12-16-2004
Getaneh Gobezie

Dear Janice Stallard,

You are touching an important topic in the microfinance sector.

I am working for the Amhara Credit & Saving Institution (ACSI), one of the largest MFI in Ethiopia, with over 340,000 active credit clients and well over 127,000 "voluntary" saving clients. The regulatory framework on microfinance here is such that it allows MFIs to mobilize savings both from their own microcredit clients as well as from the public at large. This has helped many of us to finance about 50-60% (or even over) of the loanable fund from domestic saving mobilization. But as the loan size taken by the clients grow, or if you are targeting the "vulnerable non-poor" who may take higher loan size, domestic saving mobilization alone may not enable you to achieve your outreach objectives. You have to look for donor money or commercial funding, if you can afford it.

On the other hand non-Ethiopians are not allowed to enter into the microfinance industry, or into any banking activity. May be the industry is suffering in some respect? I would like to get some more elaboration from your experience in the field.

Regards,

Mr. Getaneh Gobezie (M.Sc. Econ.)

12-16-2004
Janice Stallard

Hello Getaneh,

Thank you for your question and it is great to hear from someone in Africa. I agree that we have many experiences and lessons learned to share.

Your situation in Ethiopia sounds very MFI friendly. Given what I've

read about the delinquency issues occurring in some of the MFI programs in Africa, it is wonderful to hear about the success of Amhara Credit and Savings Institution (ACSI).

In Central Asia, we currently have no MFIs that are legally mobilizing savings for redistribution. In order to meet client demand, several of the larger MFIs have been able to borrow commercially. This has included mostly borrowing from international sources -- such as Dexia, Triodos and IFC. However, there are two cases of borrowing from commercial banks in Kazakhstan (in one case, borrowing from a local commercial bank).

It is clear from these experiences that MFIs will have to seek multiple sources of funding -- from both international and local sources. This can hopefully be supplemented by some savings mobilization, however, in the former Soviet Union there is a great mistrust of banks and I think it is going to take some time to address this and capture large volumes of savings from the public. As such, MFIs must be able to meet international borrowing standards to gain access to needed lending capital.

There are some restrictions on foreign ownership in some of the banking sectors in Central Asia. As far as I know, this does not affect the MFI industry as many have been founded by international NGOs. In Krygyzstan, there is a maximum 20% ownership restriction by any one investor for joint stock companies (which is the only legal form an MFI can take if it wants to mobilize savings).

I would like to end this by saying thank you to everyone that submitted questions over these past few days. It has been a really interesting experience for me. My first time doing an interactive forum like this. I hope it was useful for everyone.

Janice