



Azerbaijan: Microfinance Sector Development

Project Name	Microfinance Sector Development						
Project Number	46536-001						
Country	Azerbaijan						
Project Status	Closed						
Project Type / Modality of Assistance	Technical Assistance						
Source of Funding / Amount	<table border="1"><tr><td colspan="2">TA 8621-AZE: Microfinance Sector Development</td></tr><tr><td>Technical Assistance Special Fund</td><td>US\$ 300,000.00</td></tr><tr><td>Financial Sector Development Partnership Fund</td><td>US\$ 300,000.00</td></tr></table>	TA 8621-AZE: Microfinance Sector Development		Technical Assistance Special Fund	US\$ 300,000.00	Financial Sector Development Partnership Fund	US\$ 300,000.00
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Technical Assistance Special Fund	US\$ 300,000.00						
Financial Sector Development Partnership Fund	US\$ 300,000.00						
Strategic Agendas	Environmentally sustainable growth Inclusive economic growth Regional integration						
Drivers of Change	Governance and capacity development Knowledge solutions Partnerships Private sector development						
Sector / Subsector	Finance - Finance sector development						
Gender Equity and Mainstreaming	No gender elements						
Description	The TA will assist the government to develop a financial inclusion policy and strategy, enhance regulatory rules and practices to support the strategy, and improve the availability of financial inclusion data. It is expected that this policy work will enable and potentially attract strategic investments in new services such as payments, saving products, microinsurance, and new delivery mechanisms for these services such as branchless banking.						

Project Rationale and Linkage to Country/Regional Strategy

Bolstered by strong hydrocarbon export revenues, the Government of Azerbaijan has been able to increase budget expenditure substantially since 2001, boosting economic growth. However, growth has not diversified regionally and across economic sectors, leading to large income disparities and higher poverty levels in rural areas and secondary cities. Economic activity is concentrated in Azerbaijan's capital, Baku; and in the Sumqayit region, which is the center of the oil and gas, chemicals and metallurgy, and food processing industries. Azerbaijan's economy is dominated by large enterprises, with micro, small, and medium-sized enterprises contributing less than 10% to GDP. Spurring economic activity outside Baku and addressing development constraints facing micro, small, and medium-sized enterprises is essential to make growth more inclusive and to reduce poverty. It will also help support new sources of economic growth outside the traditional oil and gas sector. The government prioritizes development of the non-oil sector and economic diversification to achieve more balanced and sustainable economic development, including increasing access to financial services and a more balanced development of financial service providers, such as nonbank credit institutions (NBCIs). Inclusive financial systems in which all working age adults have effective access to credit, savings, payments and insurance from formal service providers, are crucial to broad-based growth. Access to finance is a key development constraint for micro, small, and medium-sized enterprises, especially in rural areas of Azerbaijan. Despite recent progress, Azerbaijan's bank-dominated financial sector is still small, with private credit equivalent to only 18% of GDP. This level is well behind other transition countries in the region and countries of similar GDP per capita. Banks mainly provide services in Baku and Sumqayit, which receive close to 90% of bank loans. Less than 15% of the adult population has a bank account, and only 2% save in a formal financial institution—a very low level of household savings.

At the end of 2012, Azerbaijan had 28 microfinance organizations and 104 credit unions, collectively called NBCIs. An increasing number of banks also provide microloans. The microcredit portfolio amounted to \$1.4 billion for banks and \$0.6 billion for NBCIs, with over 600,000 borrowers (one-third of them with banks and the remainder with NBCIs). However, their combined assets still represent less than 2% of GDP. Only nine out of 28 microfinance providers have over \$10 million in microfinance assets. Portfolios have been growing rapidly in recent years, but institutions still report a large un-serviced demand that they cannot meet, partly because of funding limitations. NBCIs obtain most of their funding from international investors and development agencies, mainly in foreign currency. The two largest providers of microfinance, Access Bank and the Foundation for International Community Assistance (FINCA), account for close to 40% of the microcredit clients. The 33 leading providers of microloans are members of the Azerbaijan Microfinance Association (AMFA), an NGO. At the end of April 2013, AMFA members had an outstanding microfinance credit portfolio of \$0.9 billion equivalent and almost 490,000 active borrowers, up from 100,000 in 2006. Their average portfolio at risk was less than 2%.

NBCIs in Azerbaijan have a very limited product range (mainly short-term credit), constrained by regulations and low investment in product development. The average loan size of AMFA members is \$1,800. NBCI loans are usually smaller than that, while bank loans are larger. Individual loans dominate, but some institutions make intensive use of group lending. Female borrowers represent less than 30% of the clients. Loan interest rates are 20%–50% per annum. While small, NBCIs play a crucial role in facilitating access to financial services in rural areas, since banks and ATMs remain heavily concentrated around Baku. Some larger microfinance organizations are interested in becoming banks to offer their customers a broader range of services, but attempts have failed in the past. No tiered licensing framework exists.

With the recent stronger growth of microfinance portfolios, concerns about consumer protection have been rising. This is important as financial literacy is very low. Cases of multiple borrowing and risks of over-indebtedness are becoming apparent in some regions. In 2013 NBCIs were granted full access to the public credit registry, which should help mitigate the risks. In early 2013, the CBA reduced the costs of accessing the registry to encourage more frequent use in the loan underwriting process. The AMFA has initiated the development of industry consumer protection standards and has signed on to the SMART Client Protection principles, which it is disseminating to its members. An ongoing project, supported by the World Bank and funded through the Swiss State Secretariat for Economic Affairs, is looking at financial consumer protection and financial literacy issues. Recent CBA guidelines to enforce transparency of effective interest rates (applicable to all credit institutions) have been a first step toward improved consumer protection. Regulation in this area is still weak.

Sustainable finance growth and outreach to rural low-income households requires better strategy, policy, and market understanding. The government does not yet have a policy statement or national strategy for financial inclusion, or consensus about the needs and types of acceptable delivery mechanisms for different financial products and services for households, microenterprises, and smaller businesses. The CBA has limited reliable and comparable data to understand the state of financial inclusion.

A strategic approach for financial inclusion is needed, which considers the introduction of new services such as microinsurance, remittances and payment services, and micro leasing through NBCIs. As deposit mobilization is limited for NBCIs, strategic partnerships between NBCIs and other forms of financial institutions should be explored. Some agreements to provide payments services are in place. These partnerships may be combined with branchless banking. As agents, NBCIs could provide a wider array of services, including deposit and payment services.

The issues to be addressed under the TA include (i) government understanding of the market and the need for a strategy for growth; and (ii) regulatory practices that will facilitate responsible market growth and better outreach, with more services.

Impact

Improved access to a wider range of finance services by low-income individuals and microenterprises outside Baku

Project Outcome

Description of Outcome	Improved policy, regulatory and supervisory framework for microfinance service provision
Progress Toward Outcome	Ongoing
Implementation Progress	
Description of Project Outputs	<ol style="list-style-type: none">1. Financial inclusion diagnostic report and related assessments completed2. Financial inclusion strategy and related implementation road map on regulatory and supervision reforms presented to CBA and other stakeholders, and implementation initiated3. CBA staff capacity to regulate and supervise microfinance sector operations, institutions, development, and deepening of service provision improved
Status of Implementation Progress (Outputs, Activities, and Issues)	<ol style="list-style-type: none">1. Subsector diagnostics (credit and savings, microinsurance and payments) prepared and shared with CBA, industry and other relevant stakeholders.2. Household survey implemented and draft report prepared3. A Framework for Developing a National Financial Inclusion Strategy (2016 - 2020) has been developed but has not yet been discussed with CBA. The current challenging macroeconomic scenario is shifting government priorities.4. Several workshops with CBA and industry representatives have been held in 2015.5. With support of the TA, NBCI and Credit Union reporting changed from quarterly to monthly basis6. With support of the TA, a new circular on enhanced supervision of Credit Unions was introduced7. Training needs assessment of CBA NBCI staff conducted and on-the-job training implemented.
Geographical Location	Baku

Summary of Environmental and Social Aspects

Environmental Aspects	
Involuntary Resettlement	
Indigenous Peoples	
Stakeholder Communication, Participation, and Consultation	
During Project Design	Results of consultations with relevant government institutions, banks, nonbank credit institutions, microfinance association and other development partners have been considered in project design. TA implementation is expected to support a strong partnership with the Azerbaijan Microfinance Association.
During Project Implementation	Stakeholders (industry representatives and regulators have been consulted and participated in workshops and seminars conducive to the development of a financial inclusion strategy. Household survey implemented

Business Opportunities

Consulting Services	The TA will require the services of three international consultants (for a total of 10.5 person-months) and two national consultants (for 11 person-months) to be recruited as individual consultants in accordance with ADB's Guidelines on the Use of Consultants (2013, as amended from time to time).
Procurement	There are no procurement of goods under the TA.

Responsible Staff

Responsible ADB Officer	Martinez, Inmaculada
Responsible ADB Department	Central and West Asia Department
Responsible ADB Division	Public Management, Financial Sector and Trade Division, CWRD
Executing Agencies	<i>Central Bank of Azerbaijan 32 R Behbutov Street Baku 370014, Azerbaijan Financial Markets Supervision Authority 27, Bulbul Avenue, AZ1000</i>

Timetable

Concept Clearance	04 Jul 2013
Fact Finding	23 Jul 2013 to 31 Jul 2013
MRM	-
Approval	21 Feb 2014
Last Review Mission	-
Last PDS Update	23 Sep 2016

TA 8621-AZE

Milestones					
Approval	Signing Date	Effectivity Date	Closing		
			Original	Revised	Actual
21 Feb 2014	24 Mar 2014	24 Mar 2014	31 Oct 2016	31 Dec 2016	-

Financing Plan/TA Utilization						Cumulative Disbursements		
ADB	Cofinancing	Counterpart				Total	Date	Amount
		Gov	Beneficiaries	Project Sponsor	Others			
300,000.00	300,000.00	150,000.00	0.00	0.00	0.00	750,000.00	21 Feb 2014	432,699.12

Project Page	https://www.adb.org/projects/46536-001/main
Request for Information	http://www.adb.org/forms/request-information-form?subject=46536-001
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