



Technical Assistance Consultant's Report

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Republic of Azerbaijan: Microfinance Sector Development (Microfinance Sector Strategy)

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Asian Development Bank

AZERBAIJAN MICROFINANCE SECTOR STRATEGY

I. Introduction

1. Rationale for Microfinance Sector Strategy

Governments develop microfinance sector strategies with the overall goal of ensuring the well-being of the population. The development of a national microfinance sector strategy helps to strengthen sector regulation and supervision, improve the capacity of different players, promote product reform and information, and most importantly, improve the overall quality of services to customers.

This microfinance sector strategy has been developed by the Central Bank of Azerbaijan (CBA) in consultation with all relevant departments, including Banking and Supervision, Credit Registry, Legal, Payments, Consumer Protection, Strategic Management and Research. The microfinance strategy is being developed in alignment with the CBA strategy and the national policy and strategy for Azerbaijan 2015 to 2017.

2. Defining Microfinance Clients

The Azerbaijan Microfinance Association (AMFA) defines microfinance loans as loans less than USD 20,000. Microfinance clients include two specific categories, namely low and middle income households, and micro and small enterprises. Small and medium enterprises are defined by the turnover and number of employees. The turnover of businesses varies by the type of business and sector. Small enterprises are defined by those that have 5 to 19 employees and medium enterprises have 20 to 99 employees.

Customers of non-bank credit institutions (NBCIs) and credit unions are generally excluded or underbanked by traditional formal banks. They are not eligible for bank loans or prefer alternative financial service providers for various reasons. Although these customers are considered un-bankable, given the opportunity, they can demonstrate their capacity to save and repay loans. Like most customers of banks and other financial institutions microfinance clients can benefit from access to the full range of financial services to enhance their lives and livelihoods.

3. Relevance of microfinance inclusion

Globally microfinance sector strategies have become increasingly focused on financial inclusion where financial inclusion is defined as “ a state in which all people who can use them have access to quality a savings, credit, remittance and insurance services, provided at affordable prices, in a convenient manner, and with dignity for the clients.”¹ Financial inclusion is an essential part of the government’s strategy to support poverty reduction goals and promote income equality. An inclusive financial system ensures the sustainable delivery of a range of financial services to all segments of the population with a focus on service quality and consumer protection. A microfinance sector strategy and a comprehensive national financial inclusion strategy can help in building a stronger and more efficient microfinance sector.

¹ As defined by the Center for Financial Inclusion 2015.

II. Background of the Microfinance Sector

1. Microfinance Sector

While the banking sector has had an increasing impact on the overall economy of the country, it is only 5% of the GDP which is relatively small in comparison to other sectors. However, the microfinance sector is recognized as being increasingly relevant to government's economic development strategy. Access to financial services has enabled larger numbers of low and middle income households to improve their living standards, enhance their social safety and financial wellbeing. Business loans provided by microfinance providers have enabled MSMEs to expand and diversify their businesses.

A key constraint for the microfinance sector is that it remains a relatively small percentage of the overall banking portfolio (about 3%) of Azerbaijan and contributes to only 5% of the overall GDP.

Also, while banks are rapidly gaining market share of the microfinance portfolio (more than 57%), the growth in NBCIs and credit unions remains relatively slow. The microfinance sector is concentrated in a few NBCIs that are supported by foreign investors. Growth is limited or negligible in smaller NBCIs and credit unions. The microfinance sector strategy must focus on strengthening the enabling environment and support for smaller NBCIs and the credit union system.

Although the microfinance market in Azerbaijan is relatively small, with a population of 9.5 million, there is scope for credit unions and small NBCIs to serve certain segments of the population who remain beyond the reach of banks, especially vulnerable households, informal micro and small businesses disabled, poor women, economically active youth, and small farmers.

2. Microfinance Providers

Table 1 below shows the entire scope of financial service providers in Azerbaijan and their associated regulatory authority.

Table 1: Financial Service Providers

Financial service providers		Regulatory Body
i)	Banks	CBA
ii)	Non-banks (NBCIs, credit unions)	CBA
iii)	Azerpost	CBA
iv)	Payment service providers	CBA
v)	Money transfer service providers	CBA
vi)	Consumer finance companies	CBA
vii)	Foreign exchange service providers	CBA
viii)	Retail shops (cards, POS-terminals)	-
ix)	Insurance providers	MOF/AIA
x)	Leasing companies	Tax & Civil Code Authority
xi)	Pawnshops, moneylenders, lotteries	-

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The Azerbaijan microfinance sector is served by a diverse set of financial service providers including regulated and non-regulated entities. Banks and non-bank credit organizations (NBCOs) are regulated by the CBA. NBCOs include non-bank credit institutions that offer microfinance as well as credit unions. In addition the NBCO category includes Azerpost, foreign exchange providers, consumer finance companies, payment and money transfer service providers.

Insurance companies are regulated by the Ministry of Finance. Leasing companies are regulated by the Tax and Civil Code Authority of Azerbaijan. Retail shops and informal sector financial service providers like pawnshops, moneylenders, and lotteries (informal savings mechanisms) are not regulated by CBA.

3. Microfinance Products and Services

Table 2 demonstrates the range of products and services offered by the various financial institutions that serve the microfinance segment.

Table 2: Microfinance Service Provision

	Banks	NBCIs	Credit Unions	Azerpost	Other*
Savings					
Current	xxx				
Term deposits	xxx				
MSME Credit					
Working capital	xxx				
Investment	xxx				
Micro loans	xxx				
Small loans	xxx				
Medium loans	xxx				
Agricultural loans	xx	xxx	xxx		
Line of credit	xx				
Other credit products					
General purpose	xxx	xx	x		x
Retail	x	x	x		x
Education		x	xx		
Health					
Home purchase	xxx	x			
Home improvement	xxx	xx	x		
Other financial products					
Leasing					xxx
Insurance					x
Payments	x	x	x	xxx	xxx
Money transfers	xxx	xx	x	xxx	xxx
Technology based products and services					
Credit cards	xxx	x		x	x
Debit cards	xxx				
Prepaid cards	xxx	x		x	x
ATMs	xxx				
POS-terminals	xxx			x	x
Kiosks	xxx			x	x
Internet banking	xxx	x			x

*other category - consumer finance, leasing and insurance companies, retail shops

Source: various including AMFA, website research, annual reports of banks, NBCIs, interviews.

As fully licensed entities commercial banks are licensed to offer a complete range of financial services. They can offer a wide range of credit and savings products, credit cards, foreign exchange services, payments, and transfer services. Banks can offer services through branches and branchless banking mechanisms such as ATMs, credit cards, and POS-terminals. As credit only organizations, NBCIs and credit unions cannot offer savings and deposit services, but can offer various other services, including a range of credit products, payments and money transfer services. Banks, as well as NBCIs and credit unions can offer leasing and insurance services only in partnership with other licensed providers. Currently insurance and leasing companies do not focus on the microfinance clients, and consumer finance companies do not serve the low-income segment.

Banks usually focus on large and medium enterprises and wealthy individuals, while NBCIs and credit unions focus on the low and middle income households, micro and small enterprises. Banks are required to serve legal entities, including self-employed individuals and registered or formal businesses whereas NBCIs and credit unions have greater flexibility and can lend to informal entities.

Table 3 demonstrates the typical profile of customer that is served by the various financial institutions.

Table 3: Target audience for financial service providers

	ME	SE	Micro	Upper Income	Middle Income	Low Income	Vulnerable Poor
Banks	XXX	XXX	XXX	XXX	XXX	XX	X
NBCIs	X	XX	XXX		X	XXX	XXX
Credit Unions	X	X	XXX		X	XXX	XX
Azerpost		XX	XX	X	XX	XXX	XXX
Payments services	XXX	XXX	XXX	XXX	XXX	XXX	XXX
Money transfer services	XXX	XXX	XXX	XXX	XXX	X	X
Leasing companies	XX	X		XXX	XX	X	
Insurance providers	XX	XX	X	XXX	XXX	X	
Consumer finance companies	X	X	X	XXX	XXX	X	
Credit card providers	XXX	XX	X	XXX	XX	X	
Prepaid cards	XXX	XXX	XXX	XXX	XXX	XXX	X
Debit cards	XXX	XXX	XXX	XXX	XXX	XXX	X

4. Outreach and access

According to the CBA data for 2014, NBCIs and credit unions collectively serve 426,000 (57%) out of the total 706,000 active micro credit clients. Credit union members are less than 4% of the total number of microfinance clients. The AMFA microfinance portfolio data for 2014 above shows that NBCIs and credit unions are less than 50% of the microfinance portfolio, with credit unions having a smaller share of the portfolio.

Table 4: Delivery and outreach infrastructure of microfinance sector

Table 5: Number of Institutions, Total Number of Borrowers and Portfolio

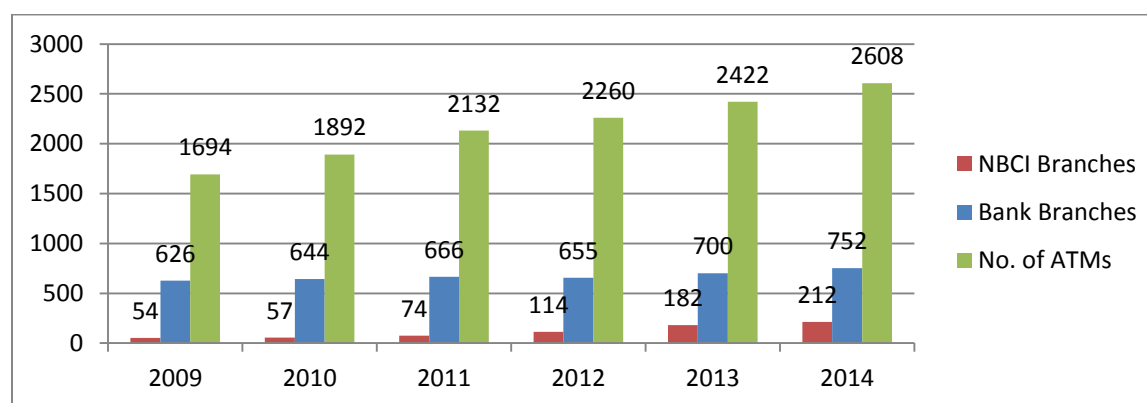
CBA Statistical Bulletin 2014			AMFA Portfolio Data December 2014		
Institutions	Number of Institutions	Number of Borrowers	No. of Institutions	No. of Active Borrowers	Microfinance Portfolio in AZM
Banks	43	280,000	8	260,877	667,767.575
NBCIs	47	400,000	16	344,934	400,501,931
Credit Unions	109	26,000	3	7,744	19,906,925
TOTAL	199	706,000	27	613,555	AZN1,088,176,432

Source: AMFA Portfolio Report December 2014 and CBA Statistical Bulletin January 2015

The relatively low outreach of credit unions is an area of focus for the microfinance sector strategy, including addressing the key constraints of capital, institutional strengthening, and enhancing the internal systems to improve operations, portfolio management, and reporting. Governance and improving professional management at the head office and field level are important for all organizations, but particularly essential for small NBCIs and credit unions.

Branch networks in Azerbaijan have been expanded significantly over the past five years, to reach 752 bank branches and 212 NBCI branches. Credit unions do not have branches. Branch penetration in Azerbaijan is high, with 8.6 commercial bank branches per 1000 square km (higher than the global average of 8.03) and 9.9 commercial bank branches per 100,000 adults.

Figure 1: Growth of branch and branchless banking networks



Source: CBA Statistical Bulletin January 2015

Banks serve microfinance customers through 2608 ATMs. The ATM penetration rates in Azerbaijan are 25.82 ATMs per 1000 square km which is significantly higher than the global average of 15.92. Clients are also served by 29.82 ATMs per 100,000 adults. In addition, banks and other financial service providers have expanded services through various types of cards, including debit, credit and prepaid cards. In addition retail customers offer POS-terminals for payments and transfers.

Liquidity is a major concern in smaller NBCIs and credit unions. The lack of domestic capital and the difficulties in attracting foreign investment is limiting institutions from scaling up and achieving profit margins and financial sustainability. The microfinance sector strategy must focus on identifying capital for refinancing smaller NBCIs and credit unions, including domestic and international sources and/or charting a path towards a licensing structure that would allow the organizations to capture deposits as commercial banks.

5. Usage of and Supply of financial services

The current menu of financial products and services offered by NBCIs and credit unions includes a range of credit products to meet personal, household and business needs. Banks are focused on traditional retail and consumer loans and lend primarily to wealthy individuals and large businesses. Microfinance banks lend to micro, small and medium enterprises, providing loans to meet both investment and working capital needs. They also provide home improvement and general purpose loans to meet personal and household needs, but the focus is on MSME lending.

Table6: Financial inclusion statistics

Financial inclusion indicators	2014
Access to credit	
% adults* who have borrowed some money	46%
% adults who borrowed from a formal financial institution	19%
% adults who are women and borrowed from formal financial institution	15%
% adults who borrowed for business or farms	5%
% youth aged 15 to 24 with accounts in formal financial institution	10%
Access to savings	
% adults who save	40%
% adults who saved with a formal financial institution	5%
Usage of financial products	
% adults who hold accounts at formal financial institution	29% (14.9%)
% adults who are women who hold accounts at formal financial institution	26%
% adults who have sent remittances	20%
% adults who have sent remittances using formal financial institutions	5%
% adults who have received remittances	19%
% adults who have received remittances using formal financial institutions	3%
% adults who have received remittances using money transfer	8%
Debit and credit cards	
% adults who have used debit cards	6.3%
% adults have used ATMs as their mode of withdrawal indicating demand for credit products	57
% adults who have used credit cards	8.1%
% adults who have used credit cards to make payments	6%
% adults who have used a formal financial institution to pay utility bills	1.6%
% adults who have used accounts to receive government transfers	4.3%
% adults who have used internet banking to pay bills or make	4.2%

purchases	
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*adults are defined as those who are above 15 years of age
Source: World Bank, Global Findex

NBCIs and credit unions focus on low and middle income households. While NBCIs are mostly focused on urban, several have expanded their services to rural areas. Credit unions are located mostly in the rural communities and focus on farmers and rural households. NBCI and credit unions provide both working capital and investment loans. NBCIs and credit unions focus less on retail and consumption loans, but rather on loans to meet social expenditures such as education, health expenditures and essential household expenditures such as improvement of living conditions, expansion of living and business premises.

All three types of service providers offer loans for agriculture, with a distinction between micro and small enterprises in the agriculture and related sectors. The large portion of microfinance loans are in the trade and services sectors with a small percentage in industry (manufacturing).

Loan terms and conditions depend on the type of institutions, with NBCIs and credit unions offering short-term (3 to 18 months) and medium-term loans (up to 36 months), and banks offering loans of up to 60 months. Interest rates vary by institutional type and by product with credit unions offering comparatively lower average rates of interest while NBCIs and banks are comparable. Interest rates vary from 27% to 36% per annum depending on the product.

Banks are required to take collateral; however, the regulation has been relaxed and some banks are accepting movable collateral. The key constraint is the implementation of the collateral norms, and the lack of a movable collateral registry. NBCIs and credit unions are more flexible. While most microcredit loans especially group loans offered by NBCIs are provided collateral free, NBCIs and credit unions take some form of collateral for larger micro and small enterprise loans. All three types of institutions insist on third party guarantors even for long-term clients with good track records.

Leasing and insurance are relatively under developed in the market. Micro leasing has not been developed as a product and pilot projects in leasing implemented by NBCIs and credit unions have failed as loan amounts are too large, and terms and conditions are not appropriate.

Banks offer savings and deposit products. Credit unions and NBCIs are credit only institutions and are not permitted to mobilize deposits. All three types of institutions are permitted to offer credit cards and prepaid cards. All three may offer insurance and leasing services in partnerships with other licensed or recognized providers.

6. Key constraints in the microfinance sector

Interviews with stakeholders, stakeholder consultations with individual institutional types and mixed group discussion and interviews with clients through focus group discussions have highlighted the following as key constraints in the microfinance sector:

a) Macro-level

1. Lack of clear guidelines for credit unions and gaps in the existing guidelines for NBCIs, particularly in relation to capital adequacy, liquidity and loan loss provisions
2. Weak off-site and on-site monitoring and supervision of NBCIs and credit unions
3. Lack of data for sound analysis and informed decision-making and planning
4. Lack of a microfinance sector strategy
5. Need to expand the existing centralized credit registry into a private bureau to enhance the quality of reports and enhance credit risk assessment
6. Lack of a movable collateral registry to ensure effectiveness of reform on collateral norms (focus of credit approval remains collateral, especially for banks)
7. Inefficiencies in the sector as a high ratio of cash is retained outside the formal banking system as compared to bank savings
8. There is a need to ensure proper implementation of consumer protection rules and guidelines and monitoring providers to ensure compliance
9. Lack of enabling environment for mobile money and e-banking
10. Weak regulatory framework and inadequate product development in insurance and leasing

b) Meso level

11. Banks, NBCIs and credit unions currently have a strong bias towards selling traditional credit products – there is a real need to shift focus towards cross-selling and offering a wider range of products and services to clients
12. As credit only institutions NBCIs and credit unions cannot offer savings and deposit services and are focused on offering social loans as alternative
13. Liquidity is the major concern for small NBCIs and all credit unions – they need access to capital (debt and equity) at sustainable rates of interest and suitable repayment terms than what is currently on offer
14. Although there is a strong preference for Azerpost's financial services among the low income population, the sector is not tapping the potential of the postal service provider, especially for mobilizing savings from the poor especially in rural areas
15. Demand for training of management and staff at all levels in areas of customer service, client acquisition, loan origination, cash flow based credit analysis, monitoring and supervision and relationship management with specific target groups such as women, rural poor, farmers, etc.
16. Need to respond to the non-financial needs of customers to enhance use of formal financial services and positive impact, especially for women, youth and rural poor.
17. Need to enhance the use of technology-based financial products such as credit and debit cards, by providing financial education and awareness building at the regional level
18. Need for gender disaggregated data and improved quality of reporting on both financial and social performance to inform decision-making, operational and strategic planning and policy formulation
19. Lack of sensitization about gender, poverty and financial inclusion is a constraint in most financial institutions

20. Market-based product research and product innovation is an area of weakness in the sector, and greater investments are needed in designing leasing and micro-insurance products.

c) Micro level

21. Products and services are not geared to the diverse needs of microfinance clients – based on their diversity of needs and different customer segments – need for product reform, modification and innovation
22. Demand for incentives such as rebates on interest rates, promotional rates for new products, etc.
23. The continuing insistence on third party guarantors even for long-term customers with good repayment track records is a deterrent
24. Customers with longer terms are demanding extension of loan tenures for ensuring easier repayments and reducing pressure
25. Demand for bank savings is limited and there is a need to develop strategies for attracting customers to bank savings especially self-employed youth, poor women and low income households in the regions
26. Need to continue efforts to encourage use of technology based products such as plastic cards, ATMs, kiosks, and internet banking
27. Need to educate clients on potential linkages between products, e.g. pension cards and use of balances for payments for goods and services, use of debit cards for payments of good and services, etc.
28. Credit bias among the public is a key constraint which requires greater emphasis on financial education, on the advantage of using formal financial services, the advantage and use of specific products and training on household and business financial management using the full range of financial products and services
29. Customers are deterred by lack of understanding about costing and pricing and continued lack of transparency in the disclosure practices of financial institutions especially on interest rates on loans
30. Demand for non-financial services for women entrepreneurs is essential to enable successful participation in the formal financial sector

III. Building the Microfinance Strategy

The Microfinance Sector Strategy offers a framework for various stakeholders in the microfinance sector to support sector development. The Strategy includes a vision statement including a clear set of goals followed by an articulation of the strategic objectives and strategies to respond to the constraints and gaps listed above. The strategy will include a road map with action steps and allocation of roles and responsibilities by specific stakeholders. The strategy will be in alignment with broader sector policies and strategies. It will include a timeline for action corresponding with the overall national country strategy and the financial sector strategy (i.e. Strategic Plan for the CBA leading up to Vision 2020).

According to the sector assessment, the areas of focus include the need to strengthen the regulatory framework for microfinance, with a particular focus on guidelines for NBCIs and credit unions.

There is also a need to enhance the capacity of the CBA to develop a risk-based approach to microfinance supervision with a focus on improving data collection, processing, consolidation and analysis, and using the data to support off-site and on-site supervision.

Continued support of the microfinance sector growth will require addressing the gaps, especially in liquidity and demand for capital for smaller NBCIs and credit unions, strengthening the governance and management capacity of microfinance institutions, as well as the improvements in the operational area, such as customer service, marketing and client acquisition, risk appraisal and risk management, and product reform and innovation in products and delivery mechanisms.

Focus on these areas is expected to achieve the broader goals of financial inclusion and deepening of impact of financial services on the population, including existing clients and potential clients that have been excluded from the formal financial system. The desired outcomes include a larger outreach – increase in the number of clients served by microfinance institutions, especially credit unions; efficiency in the delivery and expansion in the different types of access points; wider uptake of specific products and services, as well as a use of a wider range of products and services to optimize the impact of financial services on households and enterprises; and, improved quality of services with a particular emphasis on protecting customers against unfair practices, over-indebtedness, and fraud.

The microfinance sector strategy will focus on ensuring the provision of a wider range of financial products and services not only by bank, but also by NBCIs and credit unions, through partnerships and collaborations. The demand for products in the Azerbaijan market includes various types of savings accounts, including current accounts, pensions, and micro deposits. Credit products would go beyond traditional business and retail loans to focus on loans to meet social needs such as education, housing and home improvements. Business loans would include specialized products for micro and small enterprises, with particular packages for specific target groups such as women, rural enterprises, and start-ups. There is a particular demand for payments services, in particular electronic fund transfers, payment cards, and other innovative payment products. The sector strategy will also focus on the development of the insurance sector, with an emphasis on micro insurance in addition to life, health, property, agriculture insurance.

The microfinance sector policy, regulation and supervisory strategies must be reviewed and revised to support an inclusive financial system that is both secure and sustainable. The strategy will also contribute to the development of an enabling environment with market-based solutions leading to broader access and usage of a range of appropriately designed financial products and services, particularly the unserved and underserved markets such as the low-income and marginalized household and MSMEs, as well as

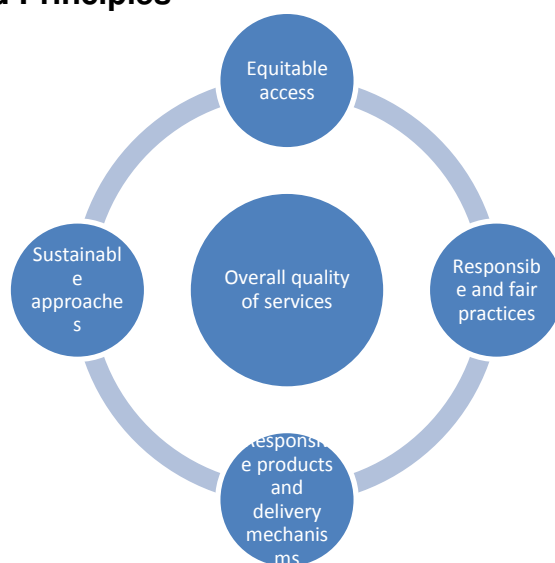
specific groups that have been excluded by formal financial institutions, e.g. women, youth, IDPs, small farmers, etc.

A. Vision Statement (needs to be developed by the CBA with stakeholders)

The vision for the microfinance sector strategy is to ensure the development of a well regulated sector consisting of a range of sustainable, efficient and effective financial service providers that can provide a full range of financial services to a larger number of people, in a fair and sustainable manner, particularly to those who have been traditionally excluded or underserved by the banking sector, including economically active women, youth, small farmers and vulnerable populations.

The overall approach of the microfinance sector strategy will be on strengthening the enabling environment, developing institutional and human resource capacity for sustainable outreach to larger segments of the population through a wider range of financial products and services, and enhancing the overall quality of customer service provision and safety of consumers.

B. Core Values and Principles



C. Specific Objectives

The microfinance sector strategy will consist of specific objectives and policy actions to respond to goals:

1. Establishing an enabling environment for all types of financial service providers, enabling improved access to financial services, better use of financial products and services, and overall safety and quality of service provision
 - i) Design and develop the capacity for risk-based supervision of microfinance providers, with a focus on NBCIs, credit institutions and credit unions
 1. Develop clear guidelines for credit unions

2. Address gaps in the guidelines for NBCIs, e.g. loan loss provisioning and write off policies
- ii) Enhance current methods for monitoring and supervision
 1. Develop guidelines for risk-based supervision of NBCIs and credit unions
 - a) Train the NBCIs and credit unions on guidelines for compliance and action
 - b) Provide clear feedback and timelines for action on recommendations for improvement
 - iii) Strengthen capacity of staff in all departments within CBA, with particular emphasis on non-bank supervision team. Refer to the section on training below for details.
 - iv) Enhance access and inclusion through the following strategies or actions:
 1. Establishment of movable collateral registry to ease the constraints related to collateral to promote access and efficiency
 2. Establishment of a private credit bureau which can integrate additional data from non-bank and other financial service providers and improve credit risk assessment and protect customers against bad-debt
 3. Support product innovation by supporting branchless banking and technology based mechanisms, including:
 4. Implementation of payment service law
 5. Supporting interoperability in technology-based solutions, and inclusive and efficient payment system that will make use of electronic payments, such as G2P and P2P.
 - v) Strengthening overall quality of services by:
 1. Further development of consumer protection practices by monitoring and supervision and ensuring compliance with existing norms
 2. Development of framework and procedures for improved consumer education and develop advocacy programs with focus on specific target groups, e.g. women, youth, elderly, rural households, IDPs, informal sector businesses, etc.
 3. Design activities especially in the regions, to promote financial literacy with the goal of increasing uptake and financial inclusion targets
 4. Improve coordination with line ministries to promote and expand information
 5. Leverage the use of public information networks and social media
 6. Collaborate with private entities and local community based organizations
 - vi) Strengthening the capacity of the microfinance sector with a focus on training and sensitization at all levels, including regulatory bodies, support institutions, service providers, and the consumers to support a sustainable industry and achieve greater outreach and impact.

- vii) Address the need for capital in the sector especially for credit unions and small NBCIs to expand outreach both in terms of volume and outreach
- viii) Improve the coordination between public sector agencies and support public-private partnerships to ensure access to essential social and non-financial services to enhance the impact of financial services on vulnerable poor, and achieve desired results
- ix) Promote the wider usage of other financial services, going beyond business credit, by motivating banks and NBCIs and credit unions to explore other credit and financial products including:
 - Specialized loans for social expenditures, e.g. health, education, emergencies
 - Instruments for improved financial management and financial planning
 - Encourage agent banking and partnerships to support the provision of insurance and leasing
- x) Market-based approach to design of products and delivery mechanisms with a particular emphasis on branchless banking
- xi) Efforts to enhance responsible and responsive lending with a focus on:
 1. Cashless transactions
 2. Reduced transaction costs
 3. Easy access, simplified procedures, and quick delivery (time)
 4. No hidden costs and transparent pricing
 5. Competitive pricing
- xii) Improve overall operational efficiency by managing overhead costs and increasing productivity (staff productivity)
 1. Better client acquisition
 2. Improved client screening
 3. Improved risk assessment by credit analyst
 4. Improved credit appraisal for moving away from collateral based approvals
- xiii) Motivating practitioner's efforts to promote consumer education, financial literacy to ensure better uptake of financial products and services, reduce losses, and enhance overall quality of services
- xiv) Promote capacity of financial institutions and staff to create wider awareness on financial products and services to build confidence

IV. Microfinance Sector Strategy to Support Financial Education and Consumer Protection

A well-informed public that is adequately protected against risks is an essential element for sustainable growth in the microfinance sector. Financial education and consumer

protection are relevant for enhancing financial inclusion. A framework for financial education and consumer protection can support the targeting of excluded and underserved populations and help them acquire knowledge, develop skills to make well-informed economic and financial decisions, and be confident to exercise their rights and responsibilities as financial consumers. A framework for monitoring and evaluation of financial education and consumer protection programs with indicators for monitoring can improve the impact and effectiveness of the strategy on the population.

Financial education interventions must focus on fair and ethical industry standards, fair practices and also take into account the diversity of the client base when designing financial education and communication strategies.

1. Policy Actions for Enhancing Financial Education for Responsible Lending

- Partnership and collaboration among the main departments within Central Bank
- Coordinate all relevant stakeholders in the industry and institutionalize the collective and individual responsibility among stakeholders.
- Identify different delivery mechanisms for financial education that take into account the diversity in the target group.
- Explore new methods, techniques and role of media to deliver materials that could achieve financial literacy of different customer segments, including women, youth, elderly, rural populations, populations with lower education
- Establish a monitoring system for evaluating impact and use analysis for continuous improvement.
- Address gaps in technical competence for the efficient and effective delivery of financial education programs through capacity-building activities, and sharing of information, either directly or in partnership with relevant entities.
- Ensure banks, NBCIs, credit unions and other practitioners adopt financial education strategies and activities within their capacity.

2. Promoting Inclusion through Awareness Creation and Advocacy Programs

Effective advocacy will require collaboration between the CBA and various government agencies and private agencies, with an aim to create awareness about the benefits of financial products and services and develop confidence in the formal financial sector.

The advocacy efforts in the microfinance sector strategy will include the following:

- Design campaigns to promote existing and new products and services especially to underserved and unserved markets, motivate the public to access formal financial services especially savings, insurance, and technology enabled financial services.
- Inform the public about the rights of consumers of financial services and redress mechanisms
- Identify, recommend, and/or initiate programs that promote and advocate financial inclusion among various stakeholders—from policymakers to the client level—to

address the wide range of financial needs of underserved and unserved markets, especially the poor and marginalized sectors of the society.

- Develop and strengthen partnerships and institutional arrangements among policymakers, government entities, and private sector stakeholders to maximize resources in implementing advocacy programs
- Incorporate evaluation mechanisms in financial inclusion advocacy programs to ensure that design and implementation of advocacy programs are based on data, evidence and knowledge products.

IV. Implementation of Microfinance Sector Strategy

1. Coordinating Body

The responsibility for the governance, management and supervision of the sector is divided across several departments of the CBA. Therefore, there is a need to establish a representative working group or committee for the finalization, and implementation of the microfinance strategy and action plan, as well as ongoing monitoring, evaluation and continuous improvement.

The proposed composition of this committee or working group is as follows:

- Licensing and regulation
- Legal
- Finance and administration
- Bank and non-bank supervision
- Payments
- Consumer protection
- Credit registry
- Consumer protection
- Consumer education
- Research
- Strategic planning
- Monitoring and evaluation
- Other

2. Coordination

The CBA should appoint an appropriate department and individual with a team to take responsibility for driving the process, and for developing the draft strategy and implementation plan to an operational plan with clear targets, and procedures. Each department or division will have its own plan and targets which have to be consolidated and integrated into the overall microfinance strategic plan and targets to ensure accurate monitoring and supervision, and most importantly evaluation for continuous improvement.

3. Meetings and Reporting

The committee should meet once a quarter. More frequent meetings may be required in the early stages of the design and implementation period.

The reporting should be simple and user friendly to enhance usage, as well as for efficient integration into existing reporting formats, and publications including a special section annually on microfinance for the CBA website and the CBA Statistical Bulletin.

V. Targets for Outreach and Inclusion

Initial discussions have suggested an increase of 15% by different types of financial service providers in terms of number of clients. The percentage of women served by microfinance sector will be raised to 50% by end of 2020.

In addition to the existing targets for financial performance, being used by the CBA, the microfinance sector strategy will also include social performance and financial inclusion targets. There is a need for data disaggregation by gender, age, income level, and type of business and sub-sector, to enhance analysis and future planning.

	Actuals 2014	Projections				Vision Vision 2020
		2015	2016	2017	2018	
Relevance in the overall economy						
% microfinance to overall GDP	5%					
% microfinance to banking sector	3%					
banks microfinance portfolio market share	61%					
NBCIs microfinance portfolio market share	38%					
credit unions microfinance portfolio market share	1%					
Number of providers						
Banks offering microfinance	8					
NBCIs offering microfinance	16					
Credit unions	109					
Azerpost	1					
Leasing companies	11					
Insurance providers	21					
Delivery channels/outreach mechanisms						
Total number of bank branches	752					
Total number of NBCI branches	212					
Total number of credit union branches	0					
Total number of Azerpost branches	1500					
Total no. of ATM machines	2608					
Total no. of POS-terminals	38,000					
Total no. of active credit card users	525,000					
Share total no. of active payment cards	10.1%					
Total no. of social cards	2.6 million					
Total no. of wage cards	1.4 million					
% of population using mobile banking	60%					
Penetration rate	107%					
% of population using internet banking	18%					
Active micro credit customers/borrowers						
Total number of active borrowers	706,000					
Total number by banks	400,000 (57%)					
Total number by NBCIs	280,000 (40%)					
Total number by credit unions	26,000 (3%)					
% women served by MFIs	26%					
Segmentation of enterprises						
% of MSMEs as part of overall portfolio						
% of micro enterprises						

% of SEs
% of MEs
% of women owned MSMEs
Sub-sector distribution
% MSMEs in trade
% MSMEs in services
% MSMEs in industry
% MSMEs in agriculture

Source: various, including GPFI, Global Findex data base, World Bank

V. Data Collection

The Microfinance Sector Strategy will focus on improving the quality of data currently available in the sector on microfinance, particularly on NBCIs and credit unions.

This will require investment in the improvement of the technology and human resource capacity of the CBA non-bank supervision division to collect, sort, and consolidate data, with a focus on data disaggregation, especially by gender, sub-sector, institutional type and product type.

The CBA will also develop capacity to enhance the quality of data analysis and the use of data by various stakeholders to inform evidence-based policymaking and planning.

Data and measurement activities can include:

1. Developing the required information technology, infrastructure
2. Recruiting the essential human resources to support data gathering, consolidation and reporting
3. Institutionalizing measurement and reporting of information, based on international indicators, contextualized to the Azerbaijan environment, including institutional, financial, sector, social and financial inclusion indicators. An emphasis must be placed on data disaggregation by gender, income level, age and geographic location (rural/urban). MSME data should be disaggregated by the different segments, with clear definitions of each category
4. Ensuring effective communication strategies to ensure information sharing between and across different types of stakeholders
5. Promoting research to complement data analysis and monitor progress, and using data in policymaking, decision-making and planning

VI. Capacity Building

A major emphasis of the microfinance sector strategy will be on training and developing capacity both at the institutional and human resource base levels. Training would focus on all relevant levels, for various stakeholders depending on training needs analysis.

There will be a focus on human resources, including governance, senior management, operational staff, as well as support and administrative staff. Institutional development will focus on the information technology, systems, policies and procedures for each type

of stakeholder and for relevant departments that handle microfinance sector support or operations. These may include policy, finance and funding, administration, audit, credit operations, marketing, market research, product development, human resource development, personnel, legal, monitoring, evaluation and reporting, information technology/management information systems, etc.

1. Training Needs

- i. Microfinance and financial inclusion
- ii. Institutional models – country and international practice
- iii. Risk-based supervision
- iv. Off-site and on-site monitoring
- v. Data collection, processing and analysis
- vi. Reporting
- vii. Use of data for risk management, crisis management, and operational and strategic planning, informing policy and decision-making

2. Training Opportunities

Training opportunities in the sector can be accessed in the country as well as regionally and internationally.

The opportunities at present include:

- National microfinance conferences, e.g. AMFA conference
- Other national conferences on themes, e.g. ADB Insurance Workshop, July 2015
- International microfinance conferences, e.g. MFC, SEEP
- Conferences on specific themes, e.g. financial inclusion, regulation, mobile banking and digital finance, agricultural credit, insurance, etc.
- Global training facilities, e.g. Boulder in Turin
- Technical training organized in the country, e.g. AMFA training programs
- Process consulting for the institution
- Custom designed group training for specific audiences
- Field exposure training for different levels or in a team based on learning objectives and goals

The impact of training depends on good needs assessment to address gaps in the capacity of departments and individual candidates, good training needs assessments of individuals, and matching candidates to the programs. The impact of training also requires commitment from candidates to share their learning and adopt their knowledge to improvements, and developing the capacity of others.

Internal training departments may not be possible for all institutions, therefore, it is useful to develop a training faculty that consists of individuals from various departments and areas of specialization, and call on individuals and teams as required.

Impact of training also requires periodic evaluations of individual participants and departments to ensure impact and to plan investment in additional training. The impact of training must be observed on portfolio performance, enhanced efficiency and quality of business. Other essential elements of training include link of training to annual staff evaluations and staff performance incentive mechanisms.

3. Check List

- Departmental strategy
- Action plan, targets and budget for three years (with projections)
- Training needs assessment
- Organizational structure
- Job descriptions for staff in each department
- Information technology to support operations
- Impact evaluation and monitoring framework
- Incentive schemes for motivating staff, and plan for self-improvement

VI. Microfinance Sector Strategy – Road Map for Implementation

The first step in the Road Map for implementation of the microfinance sector strategy is to identify a focal point for the coordination of the consultative process culminating in the finalization of the draft sector strategy. While the Non-bank Supervision Division is a key stakeholder, it has a limited role in the overall sector strategy, and has other commitments. The coordination of the sector strategy implementation is best given to a department that has responsibilities related to research, capacity building, monitoring and evaluation, and coordination of planning and knowledge for policy making and planning. The consultation process may extend to a period of up to three months and longer.

The consultation process can be made efficient by establishing not only a focal point department for the coordination, but also a representative working group or committee, which includes representatives from all the relevant departments/divisions of the CBA. These may include:

The sector strategy must also include other stakeholders, outside the CBA, including ministries, such as Ministry of Finance, Ministry of Agriculture, Ministry of Justice, Ministry of Information Technology and Communication, Ministry of Economic Planning, etc. Other important stakeholders include the private sector, industry associations such as AMFA, ACCU, AIA, etc. and the individual institutions. International finance institutions, donors and technical service providers are also important to include in the consultation process, and later in the implementation process.

The consultative process must include mechanisms to engage with these different groups of stakeholders one-on-one, or in a group mechanism.

Road Map

Activity	Timeframe
Industry assessments and recommendations	October 2014 to July 2015
Consultations to build strategy	June and July 2015
Draft strategy	July to August 2015
Consultations in the sector for finalization on the draft strategy	August to September 2015
Capacity building	June to October 2015
Establish working group	September 2015
Presentation of final strategy	October 2015
Implementation roll out	October 2015
Review and evaluation	Quarterly from first quarter 2016 until ???

1. Industry assessments (six month period, October 2014 to July 2015)

The first step in the process involved industry assessments, to identify the current state of the market, assess gaps, and identify areas of improvement to develop recommendations and a framework for the sector strategy. The assessments were conducted under the ADB Microfinance Sector Development Strategy Technical Assistance. The methodology for assessments combined interviews with stakeholders, desk research and field research (focus group discussions and a household survey).

2. Consultative Sessions (ongoing, to be completed by September 2015)

The findings from the assessments were shared initially in June and July 2015 with stakeholders both internally at the CBA as well as with stakeholder groups. Additional consultations will be held between July and October 2015.

3. Finalizing the Microfinance Sector Strategy (October 2015)

The draft strategy prepared by mid-August 2015, will be shared with the CBA and other stakeholders for comments and finalized for a presentation to the sector in October 2015.

4. Implementation of the Strategy

The CBA will finalize the Microfinance Sector Strategy and then appoint a focal point for implementation. The original working group or committee will continue to support the focal point for implementation. The working group will prepare a detailed work plan and calendar, with specific outputs, targets and a budget, as well as allocate specific roles and responsibilities for specific CBA departments and other stakeholders. Capacity building initiatives need to be scheduled for CBA departments and sector stakeholders based on assessments and priority during the period of the action plan.

5. Monitoring and evaluation

Results will be evaluated in a regular manner including a review of key performance indicators. Reporting will include portfolio performance as well as select financial inclusion indicators.