

Small and Micro Enterprise Development (SMED)

of the

Social Development Fund of Yemen

Strategic Plan 2011 – 2015

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Acronyms

BDS	Business Development Services
GoY	Government of the Republic of Yemen
KfW	German Financial Corporation
MFIs	Microfinance Institutions
MOPIC	Ministry of Planning and International Cooperation
SFD	Social Fund for Development
SME	Small and Micro Enterprises
SMED	Small and Micro Enterprise Development Unit
SMEPS	Small and Micro Enterprise Promotion Service
YMN	Yemen Microfinance Network

Executive Summary

This strategic plan of the “Small and Micro Enterprise Development Program” (SMED) defines the strategic directions i.e. vision, mission, core values, strategic goals, objectives and activities to achieve those objectives. This document is result of series of individual meetings and discussions with key stakeholders including the SFD, the Central Bank, microfinance banks and companies, YMN, SMEPS as well as donor organizations involved in technical assistance and development of microfinance Institutions.

SFD, represented by its unit “Small and Micro Enterprise Development Program” (SMED), has pioneered the initiation of microfinance programs in different governorates of the country with the help of different donors. Successful programs later transformed into microfinance institutions. Currently there are 13 microfinance players including NGO/MFIs, one specialized microfinance bank, one commercial banks and one microfinance company offering microfinance services to the formal and informal micro businesses of the country.

Yemen’s microfinance industry developed favourably in the last decade. Yet irrespective thereof, the industry is still very much in its infancy. Only about 50,000 of the estimated one million potential Yemeni client benefit from microfinance services, thereof around only 25% located in rural areas. Current active clientele of each MFI except two is less than 5,000 clients. Even though the majority of the clientele are women, yet the low loan amounts not exceeding USD 150 on average serve predominantly only subsistence purposes and do not allow the establishment of sustainable, job creating businesses. The limited expansion of Yemeni microfinance is typically caused by the small size and institutional weaknesses of the MFIs, the heavy reliance on SFD funding, the lack of formal credit but also entrepreneurial culture, low population densities particularly in rural areas and the lack of - even though improving - involvement of the private and banking sector. Overcoming these weaknesses remains a key goal of the SMED in the coming years.

Whilst the SMD has exerted substantial efforts in nurturing the establishment of MFIs, now the SMED will shift its strategic focus towards improving the enabling environment of the industry as a whole. The consolidation and institutional upgrading of MFIs, the broadening of the range of microfinance products, the introduction of innovative outreach methodologies and technologies as well as a continued improvement of the regulatory and operating environment will be the key goals of the SMED towards promoting a market oriented and sustainable microfinance industry in Yemen.

Introduction:

This strategic plan of the Small and Micro Enterprise Development Program" (SMED) defines the strategic directions i.e. vision, mission, core values, strategic goals, objectives and activities to achieve those goals. This document is result of series of individual meetings and discussions with key stakeholders including the SFD, the Central Bank, microfinance banks and companies, the YMN, the SMEPS, commercial banks, and donor organizations. These meetings were conducted as part of a situation analysis mission with the aim of assessment of key challenges of the industry and expectations of key stakeholders from the network.

Situation Analysis – Profile of Microfinance Sector in the Republic of Yemen

Microfinance was first introduced to Yemen in 1997 by the Social Fund for Development (SFD), which was established by the GoY in the same year as an independent apex level institution to absorb the shocks of market reform initiatives by the GoY. SFD, represented by its unit "Small and Micro Enterprise Development Program" (SMED), has pioneered the initiation of microfinance programs in different governorates of the country with the help of different donors. Successful programs later transformed into microfinance institutions. Currently there are 13 microfinance players including NGO/MFIs, one specialized microfinance bank, one microfinance company and one commercial banks offering microfinance services to the formal and informal micro businesses of the country.

Yemen's microfinance sector has evolved rapidly since its inception in 1997. Its development hereby underwent three key phases:

Phase 1: Piloting of MFIs and IGP in Rural Areas

The earliest Yemeni microfinance programs were established in 1997 and focused entirely on rural areas. Over 70% of the population, and an even larger share of the poor, lives in rural areas with effectively no access to modern financial services. Two types of programs were offered: (1) standard MFIs that provided microloans to poor rural women and (2) specialized income generating programs (IGPs) that provided financing for the purchase of productive agricultural assets (e.g. animals, beehives, etc.). Both types were gradually phased out by 2002 due to weak institutional capacity of the partnering rural NGOs and the high transaction costs due to the sparsely populated rural areas of Yemen.

Phase 2: Emergence of Urban Microfinance

Yemen's first urban microfinance programs emerged towards the end of 1997 and, as rural programs began to show their limitations, grew to dominate Yemeni microfinance by the end of the 1990s. Urban areas offered better-developed infrastructure and services, the availability of qualified employees, possibilities for economies of scale, and a high population density that reduced overhead costs significantly. Additionally, the medium-term strategy was to build on these urban programs and expand into rural areas. The rapid expansion of these urban programs beginning in 2000 was driven by a series of strategic partnerships between SFD and local NGOs and extended to nearly all regions of the country. Irrespective thereof, the range of financial services remained limited to a few lending products.

Phase 3 – Institutionalization of MFIs

The institutionalization of the microfinance industry took place on different levels. A regulatory level for microfinance institutions in Yemen was completely missing until 2009. Microfinance institutions were

required to register as NGOs or non-profit companies, with no entitlement to deposit taking and restriction on their interest rates. In 2009, the Yemeni Parliament passed the Microfinance Banks Law – again the first of its kind in the Arab world, allowing the establishment of specialized banks that could offer a wide range of banking products. The 2009 Law also established a microfinance supervisory unit within the Central Bank of Yemen whose specific responsibility was to monitor these microfinance banks. Conversely, non-bank MFIs still lack proper regulation and supervision. Microfinance companies are licensed by the Ministry of Industry and microfinance NGOs are licensed by the Ministry for Social Affairs, none of whom have the capacity for proper supervision. On meso level the microfinance sector was enriched by two initiatives of SMED, namely the establishment of SMEPS and YMN. Both organizations operate complementary. While YMN supports the institutional strengthening of MFIs, SMEPS contributes to enhancing the creditworthiness of MSEs through business development services. On micro resp. grass-root level Tadhamon International Islamic Bank was the first to downscale to small and microenterprises through specialized lending arms albeit on a limited basis. The industry received a boost in 2008 by the establishment of Al-Amal Bank as the first microfinance bank not only in Yemen but in the Arab world with a diversity of finance products. Finally, the upgrading of the Kuraimi exchange office to the Kuraimi Bank marks the emergence of the first fully private microfinance bank.

Conclusion and Outlook

Yemen's microfinance industry developed favourably in the last decade. Yet irrespective thereof, the industry is still very much in its infancy. Only about 50,000 of the estimated one million potential Yemeni client benefit from microfinance services, thereof around only 25% located in rural areas¹. Current active clientele of each MFI except two is less than 5,000 clients. Even though the majority of the clientele are women, yet the low loan amounts not exceeding USD 150 on average serve predominantly only subsistence purposes and do not allow the establishment of sustainable, job creating businesses. The limited expansion of Yemeni microfinance is typically caused by the small size and institutional weaknesses of the MFIs, the heavy reliance on SFD funding, the lack of formal credit but also entrepreneurial culture, low population densities particularly in rural areas and the lack of - even though improving - involvement of the private and banking sector. Overcoming these weaknesses remains a key goal of the SMED in the coming years.

Strategic Directions of the SMED

Vision

To contribute to the MDGs through employment creation, improvement of livelihood and gender equality.

Mission

To establish an enabling environment that provides inclusive financial and non-financial services to low-income people and micro and small businesses in general with a special focus on women and rural areas.

¹ Yemen has an estimated total population of 22.198 million, thereof nearly 35% living below the poverty line, which corresponds to more than one million households in need of micro loans

Core Values:

Mission of SMED will be achieved by observing its core values and its code of conduct will also be based on these values, which are derived from values of its members and the best practices of industry:-

- Commitment to alleviation of poverty
- Responsibility, accountability and transparency
- Fairness and equality in the treatment of all players relevant to the microfinance industry
- Observance of best practices of the industry
- Gender equity and non-discriminatory services to all
- Good governance and performance excellence

Strategic Goals:

Based on the strategic directions of SMED, the results so far achieved in building a microfinance sector in Yemen as well as the lessons learnt thereof the vision and mission of the SMED are translated into following strategic goals:

1. Financial institutions provide effective and sustainable financial services to SMEs.
2. New entrants and sector innovations contribute to closing the demand gap and encourage competition
3. The SMED institutional initiatives are well established and provide effective, efficient and sustainable support to the microfinance industry.
4. Macro and meso-level institutions provide effective business support to the SME industry.

SWOT Analysis

<u>Strengths</u>	<u>Weaknesses</u>
<ol style="list-style-type: none"> 1. SMED is well established within the SFD organization and may draw fully on its infrastructure. 2. Highly motivated and diversely qualified staff, mix of experienced senior staff and new fresh, energetic employees, open and collaborative working environment. 3. SMED objectives and policies are strongly supported by the Government and the SFD management. 4. SMED is the main driver behind the evolvement of the microfinance sector in Yemen. 5. SMED is the main microfinance donor in Yemen. 6. SMED offers tangible technical expertise to the MFIs (MIS modules on loan tracking, accounting, HR; credit bureau) 7. SMED is the ideal local partner for donor interventions in the microfinance sector 	<ol style="list-style-type: none"> 1. Research and development in the unit is still insufficient but expected to improve by the appointment of an R&D officer. 2. The SMED unit is inadequately staffed but additional staffing of 4 officers is under way. 3. Non-financial support mostly to small, i. e. not to micro businesses. 4. Hardly any non-financial support in rural Yemen. 5. The visibility of SMED with respect to its importance for the microfinance industry is constrained by its integration in the SFD organization. A spinoff may be subject to consideration.

<u>Opportunities</u>	<u>Threats</u>
<ol style="list-style-type: none"> 1. Weak coverage of the microfinance demand – particularly in rural Yemen – is indicative of strong market potential 2. Market prospects have additionally and significantly improved following the enactment of the MF Law 3. The spinoff of SMED functions through SMEPS and YMN enable SMED to focus on general sector support 4. The establishment of YMN enhances a solid capacity building for MFIs as well as sector transparency 5. SMEPS is complementary to YMN by strengthening the capacity building and hence the creditworthiness of the SMEs. 6. The introduction of innovative technologies as well as the capitalization on innovative outreach methodologies in MF supports accelerated market coverage. 7. The entry of Amal Bank and Kuraimi Bank documents the achieved and rising interest of the private sector in a market oriented microfinance business. 8. The SMED's increased focus on microfinance services to the youth takes account of the country's substantial population increase 9. Increased focus of donors on improvement of livelihood and good governance in Yemen 	<ol style="list-style-type: none"> 1. Weak infrastructure and enabling environment for SMEs constraints growth chances and hence credit demand. 2. Lacking regulation and supervision of the non-bank MFIs hinders transparency and a level playing field 3. Low credit culture in Yemen hinders an accelerated sector growth 4. The extreme scattering of the rural population is a substantial hindrance to outreach 5. High inflation rate and resultant high interest rate levels not conducive to economic development. 6. Political and security risks are equally non-conducive to economic development and frightens off international microfinance partners. 7. Yemeni culture vis-à-vis entrepreneurship and microfinance. (women working out of home and only be served by female officers, reluctance towards dealing with banks) 8. Strong population growth bears risk of increased poverty, unemployment and social unrest if not complemented by proportionate economic growth and job creation 9. Market distortion by donors providing microfinance funding below market levels or even grants. 10. Persistent red tape hinders efficient private business development, but showing signs of improvement.

Strategic Objectives, Activities and suggested Priorities (whereby 1 is highest):

Goal 1: Financial institutions provide effective and sustainable financial services to SMEs.

Objective 1: MFIs transform into larger and stronger specialized financial institutions.

Activities:

- | | |
|--|---|
| • Develop an institutional sustainability strategy for MFIs | 2 |
| • Execute the strategy | 2 |
| • Build institutional frameworks for the merged respectively upgraded MFIs | 2 |

Objective 2: The institution building and financial base of each of the MFIs is conducive to growth

Activities:

- | | |
|--|---|
| • Provide funding to eligible MFIs to support portfolio growth | 1 |
| • Provide grants to MFIs for institution and capacity building | 1 |

Objective 3: MFIs have improved their outreach especially to rural areas

Activities:

- | | |
|--|---|
| • Support the introduction of new MFI products subject to YMN research results | 1 |
| • Support market awareness for microfinance services | 1 |

Goal 2: New entrants and sector innovations contribute to closing the demand gap and encourage competition

Objective 1: New initiatives work in the microfinance industry.

Activities:

- | | |
|--|---|
| • Encourage local commercial banks to enter the market (Downscaling) | 2 |
| • Encourage MFIs to service the Missing Middle (Upscaling) | 3 |
| • Encourage and facilitate the establishment of new MFIs through local and / or international players. | 2 |

Objective 2: New methodologies to deliver financial services efficiently and on a large scale are introduced.

Activities:

- | | |
|---|---|
| • Capitalize on the rural outreach infrastructure of the General Postal Savings Authority | 1 |
| • Capitalize on the outreach infrastructure of the Social Welfare Fund (SWF) | 2 |
| • Introduce the mobile branchless technology (mobile banking) in Yemen | 1 |

Goal 3: The SMED institutional initiatives are well established and provide effective, efficient and sustainable support to the SME sector

Objective 1: SMEPS is well established and is financially and administratively independent

Activities:

- | | |
|--|---|
| • Monitor and advise SMEPS | 1 |
| • Fund SMEPS operations | 1 |
| • Provide technical support to SMEPS | 1 |
| • Secure international and donor funding for SMEPS | 3 |

Objective 2: The BDS demand gap for micro businesses and rural areas narrowed

Activities:

- | | |
|---|--|
| • Facilitate BDS for micro businesses | |
| • Facilitate BDS for rural and agriculture purposes | |

Objective 3: MFIs have the capacity to coordinate with BDS providers the facilitation of BDS for their clients.

Activities:

- | | |
|---|---|
| • Train employees in BDS facilitation. | 3 |
| • Encourage the MFIs to facilitate BDS to their clients through BDS providers | 2 |

Objective 4: YMN is well established and supports the MFIs effectively and efficiently

- | | |
|---|---|
| • Monitor YMN | 1 |
| • Complete the institution and capacity building of YMN | 1 |

Goal 4: Macro and meso-level institutions provide effective business support to the microfinance industry.

Objective 1: The sector allows a level playing field and prudent business conduct of the MFIs

Activities:

- | | |
|--|---|
| • The MFIs are properly regulated | 1 |
| • The MFIs are properly supervised | 1 |
| • Establish the credit bureau in a manner serving all FIs engaged in micro lending | 1 |
| • Create awareness for SME promotion on macro level | 1 |
| • Establish a policy dialogue platform for "Access to Finance" | 2 |

Objective 2: Meso-level institutions (in addition to YMN and SMEPS) facilitate MFI operations effectively

Activities:

- | | |
|------------------------------|---|
| • Qualify external auditors. | 2 |
|------------------------------|---|

- | | |
|---|---|
| • Qualify IT experts or companies for the financial information, loan tracking, and HR computerized system. | 2 |
| • Support YMN in establishing a training institute for MFIs | 3 |

Objective 3: The dissemination of information ensures acceptable sector transparency

Activities:

- | | |
|---|---|
| • Support YMN in dissemination of information | 1 |
| • Ensure regular and periodical news updates on the microfinance industry | 3 |

Strategy Statement

Whilst the SMD has exerted substantial efforts in nurturing the establishment of MFIs, now the SMED will shift its strategic focus towards improving the enabling environment of the industry as a whole. The consolidation and institutional upgrading of MFIs, the broadening of the range of microfinance products, the introduction of innovative outreach methodologies and technologies as well as a continued improvement of the regulatory and operating environment will be the key goals of the SMED towards promoting a market oriented and sustainable microfinance industry in Yemen. Particular emphasis will be placed on servicing women and reaching out to rural areas.