Armenia Micro Lending Programme

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Quarterly Report

March – June 2006

1. General situation

In conjunction with the launch of the EBRD Armenia Micro Lending Programme (AMP) at the end of February 2006, IPC resumed its role as a consultant in the Armenian banking market, returning to this market for the first time since the phase-out of active technical assistance for the German-Armenian Fund at the beginning of 2005. Under the Armenia Multi Bank Framework Facility (AMBFF), the EBRD had already disbursed onlending funds to four Armenian banks – ACBA, Anelik, Ineco and Armeconombank – to finance credit extension to MSEs. The EBRD's terms of reference for the AMP now call for the gains made under the AMBFF to be consolidated, while substantially expanding the institution-building component and also launching MSME lending operations in at least two additional partner banks. At the end of the assignment the AMP is expected to have achieved the following deliverables:

- → institution-building measures fully implemented in at least four partner banks;
- → graduation of 75% of participating branches from technical co-operation support;
- → at least additional 65 new loan officers fully trained;
- → monthly disbursements of 2,000 loans worth USD 8 million achieved;
- → MSME lending expanded to an additional 15 new cities and towns, with an additional 30 MSME lending outlets established;
- → level of past-due loans (overdue by more than 30 days) less than 3% for the AMP's portfolio.

In view of the current situation at the existing partner banks and the general situation in the Armenian banking market, it makes sense to review these deliverables and assess the likelihood of their realisation under the constraints imposed by the AMP's current operating environment, most notably the liquidity problems faced by Anelik, ACBA and Ineco.[1] As a result of these liquidity shortages, the scope of lending is limited to what can be financed with the inflow of funds from current borrowers' interest and principal payments, lending must frequently be discontinued altogether, and the implementation of planned regional expansion activities and recruitment initiatives to hire new lending staff has either been postponed or cancelled altogether. Moreover, Armeconombank showed such a striking lack of interest in MSE lending operations that it was decided not to provide it with technical assistance on any significant scale unless there was a fundamental change in the situation at this partner institution. Given the impact of these constraints, one is forced to conclude that there is a substantial risk that it will not be possible to achieve certain of the deliverables. In particular, the feasibility of the envisaged expansion of the programme's activities to an additional 15 new cities and towns, and the establishment of an additional 30 MSME lending outlets, might be questionable. In view of the fact that ACBA plans to carry out a very ambitious regional expansion programme over the next twelve months with the help of the AMP, it might very well be possible to launch MSME lending operations in 15 additional towns and cities.[2] But given that ACBA is the only partner bank that is currently planning to undertake a major regional expansion, and also considering that there are no potential new partner banks in Armenia that have either a substantial branch network or large-scale expansion plans, it will clearly be difficult to achieve the goal of opening an additional 30 MSME lending outlets.

The situation outlined in the preceding paragraph could be successfully addressed if (a) the current partner banks, i.e. those which are still actively involved in the programme, are able to resolve their liquidity problems and are also willing and able to change their strategies with regard to regional expansion; or if (b) Armeconombank, which has a very large branch network (more than 40 outlets), can be persuaded to give priority to MSME lending; or if (c) at least one ambitious new partner bank can be found which either already has a sizeable branch network or would like to expand rapidly to the regions and also has the financial resources needed to undertake a major expansion programme.

Re scenario (a) – the current partner banks, i.e. those which are still actively involved in the programme, are able to resolve their liquidity problems and are also willing and able to change their strategies with regard to regional expansion:

Due to the limited absorptive capacity of the existing partner banks, it is unlikely that additional credit lines from the EBRD and other international financial institutions would have a major, long-lasting impact on the banks' overall liquidity situation. The unsatisfied demand for credit is so large that additional onlending funds obtained through credit lines would be disbursed to MSMEs within a few weeks or months. A viable alternative to additional credit lines would be the implementation of major capital increases, and given that the ability and/or willingness of the current investors to substantially increase their stakes in the institutions is said to be limited, the attraction of new potential investors might be a solution. In any case, however, a high priority will have to be assigned to the increased mobilisation of funds on the local deposit market. Therefore, in an effort to help the partner banks to develop a sustainable solution to the liquidity problem, the AMP's consultants are working closely with their counterparts at the various institutions to promote the sale of more non-loan products to current MSME clients. A so-called customer relationship management (CRM) approach is being utilised with a view to boosting both deposits and non-interest income, which would contribute to increased liquidity levels at the banks.

[1] The specific situation at each partner bank will be discussed below in the sections dealing with the individual institutions.

[2] Some of the towns that have been targeted have a population of less than 6,000.

Re scenario (b) – Armeconombank can be persuaded to give priority to MSME lending:

Since Armeconombank has a very large branch network with many outlets in the various regions of the country, it has the potential to become a very valuable partner bank. Unfortunately, however, both Armeconombank's performance as a partner bank of the German-Armenian Fund and the initial indications which it gave to the AMP's consultants regarding its attitude towards the programme were not very promising. At the beginning of June, Armeconombank's top management changed and there were certain indications that the change in the bank's management might also have led to a change in its attitude towards micro lending. But given that Armeconombank's views on the importance of micro lending have also changed frequently in the past, it remains to be seen whether it really has decided to approach micro lending differently and is serious about making the changes that would be necessary to put a different approach into practice. Based on the Consultant's long experience with Armeconombank in the area of MSE lending, it is, to say the least, unlikely that this bank will change its attitude towards serving the programme's target group and make a substantial contribution to the achievement of the AMP's objectives.

Re scenario (c) – at least one ambitious new partner bank can be found which either already has a sizeable branch network or would like to expand rapidly to the regions and also has the financial resources needed to undertake a major expansion programme:

The programme has assessed the Armenian banking market with a view to identifying new partner banks which, in terms of financial stability, integrity and the potential for regional expansion, could become valuable partners for the AMP, and so far only two potential partner banks have been found which appear to meet these criteria to a more or less satisfactory degree. These potential partners would be Converse Bank and Armsavingsbank. Both banks have expressed an interest in co-operating with the AMP. However, since the EBRD has not yet decided to initiate co-operation with either of them,[3] the AMP has so far not taken any action in terms of involving these two banks in the programme's activities. If the programme wished to initiate co-operation with either Converse Bank or Armsavingsbank, both of which are among the country's larger banks, it would be crucial to arrive at a decision in a relatively early stage of the project in order to ensure that all of the necessary measures could be implemented in a sustainable manner. The AMP's new partner bank, Cascade Bank, also has plans to expand its branch network in the future, but given that it currently does not have a single branch, the impact of Cascade within the AMP will probably be rather modest.

2. General information on the Consultant's activities

2.1 Analysis of initial situation and planning to facilitate regional outreach

The first few weeks after the launch of the programme were used to analyse the partner banks in terms of what may have changed at the individual institutions following the phase-out of the German-Armenian Fund's technical assistance activities. The AMP's consultants resumed their intensive dialogue with the partner banks' top management staff, their counterparts at all levels and the micro lending staff both at the banks' head offices and also at numerous regional branches. The following aspects were analysed:

- → MSME lending structures and the procedures that are currently in place;
- → the use of MSME loan products, especially Express loans;

[3] As regards Armsavingsbank, the EBRD might take a decision concerning a possible co-operation once its relationship with the Russian institution "Vneshtorg Bank", Armsavingsbank's principal shareholder, has been clearly defined.

→ the partner banks' operating environment;

→ the qualifications of lending staff and the allocation of such personnel to branches in the regions;

→ internal control mechanisms that are in place;

→ MSME portfolios and portfolio quality;

→ the partner banks' willingness and ability to expand their MSME lending operations to the regions.[4]

In March a considerable amount of time and effort was devoted to establishing a data information system. This system is designed to enable the banks to provide to the AMP all of the information required for reporting purposes and for controlling. The objective is to report all loans disbursed by the banks which meet the eligibility conditions defined by the EBRD and which are analysed by IPC-trained lending staff using the IPC lending methodology (the lending methodology is sometimes also referred to as the "credit technology"). The source of funding for the individual loan is not relevant. At the same time, the new approach has been designed in such a way as to facilitate the smooth integration of the new system into the individual software packages used by the various banks without significantly increasing the partner institutions' already very substantial workload in terms of meeting the data-collection and reporting requirements established by various donors and international financial institutions.

Since regional outreach is one of the programme's key deliverables, the AMP's consultants conducted discussions with all partner banks to assess their willingness and ability to expand MSME lending operations to the regions. With the exception of Armeconombank, all of the partner banks operate MSME lending departments in all of their existing branches. If lending operations are to be further expanded in the regions, the partner banks must be persuaded to open new branches in new cities and towns. When it became clear that at least one of the partner institutions – namely ACBA – was both willing and able to open new branches in new cities and towns, and that ACBA had already bought and refurbished premises for branches in various new cities in both the northern and southern parts of Armenia, a decision was taken to send AMP's local trainers on permanent assignments to the regions in question; one was assigned to Vanadzor in order to facilitate the expansion of the partner banks' branch networks in the north and one was sent to Kapan in order to do the same thing in the south. The tasks of these two trainers are to help banks which are expanding in the regions to recruit and train new loan officers, to improve the qualifications and performance of the institutions' existing loan officers, and to help them to build sound new loan portfolios in the respective regions. These two trainers started their activities in June 2006.

2.2 Developing new loan products

Given that regional expansion had been defined as one of the programme's key priorities and taking into account the results of the analysis of the partner banks' operating environment, it became clear that the institutions would probably serve MSME clients even better if, in addition to the standard loan products – i.e. Express, Micro and Small loans – they also offered other, non-standard loan products, such as agricultural loans, credit lines, overdrafts and a new type of Express loan, the semi-automated Express loan.

[4] Some of the preliminary results of this analysis will be outlined in section 5, in which the co-operation with the individual partner banks is discussed.

a) Agricultural loans

Except for ACBA, which has been lending successfully to farming operations and other agricultural businesses for many years, the AMP's partner banks have so far been quite reluctant to become actively involved in agricultural lending. During the first few weeks following the launch of the programme, the AMP's consultants conducted a market study with a view to developing a sound overall approach to agricultural lending, including an appropriate design for a possible new agricultural loan product, especially for Anelik Bank and Ineco Bank. After the agricultural lending methodology was modified to make allowance for the specific characteristics of the Armenian market, a seminar was held at each of these two banks to present the approach that had been developed to their executive management personnel and to selected branch managers. Unfortunately, however, due to the liquidity problems it faces and the resulting reluctance on the part of the management to enter a relatively new market, Ineco decided that, for the time being, it did not wish to initiate agricultural lending on a large scale. The bank indicated that it would not seriously consider introducing agricultural loans on a significant scale unless it was able to resolve its liquidity problems and could count on having sufficient funds available to enable it not only to serve the conventional demand for loans but also to successfully develop the agricultural loan market. At Anelik, liquidity problems did not seem to be a major concern at the outset, and it decided to initiate agricultural lending in its rural branches, especially in the town of Gavar in northern Armenia. After loan officers had been trained in the application of the new credit technology via seminars and on-the-job-training, the bank began accepting applications for agricultural loans. In the meantime, Anelik has disbursed some of the agricultural loans which were approved during the initial phase of the programme, and although it is continuing its agricultural lending operations, disbursements are frequently postponed when onlending funds are scarce.

b) Credit lines and overdrafts

In order to serve micro clients even better, credit lines and overdrafts are to be made available to the target group. Even for clients with a good credit history and larger businesses, in cases where flexible repayment schemes and short-term financing are required, these two products will supply a demand which has so far remained unsatisfied in the Armenian micro credit market. Following discussions with the partner banks of both the specific needs which these products will be intended to meet and the various features that will have to be incorporated in their design, the AMP's consultants developed product descriptions and credit policies for both credit lines and overdrafts which will ensure that they are marketed and distributed to the members of the target group in a responsible manner. These two products will be introduced during the next few months, and in the beginning all aspects of the process will be monitored extremely closely by the AMP.

c) Automated Express loans

After they had analysed the day-to-day lending practices and operations of the partner banks, it became clear to the AMP's consultants that all of the institutions have so far been relatively reluctant to become involved in Express lending on a significant scale.[5] With the automated Express loan, credit analyses for clients who have a good credit history and whose business operations have not experienced any structural changes are carried out using an abbreviated procedure which does not include visits to the applicant's business premises and home. The

[5] The Express loan, which is designed for amounts of up to USD 5,000, may be issued without the provision of collateral by the borrower and is supposed to be disbursed within two days after the loan application has been submitted.

introduction of this new procedure is intended to increase disbursement efficiency and to encourage the partner banks to reassess their approach to dealing with their clients who operate very small businesses – a segment of the target group which, overall, has proved to be extremely reliable and has an excellent repayment record – and thus to help them understand that taking a less risk-averse approach to lending to these clients will enable them to increase the profitability of their Express loan operations without significantly increasing their risk exposure.

The requisite procedures have been developed and will be discussed with the partner banks during the coming weeks. It is expected that, with the exception of Anelik, all of the banks will introduce the automated Express loan.

2.3 Helping to increase liquidity: CRM

In order to facilitate efforts to improve the banks' liquidity situation, they are being given support in the establishment of customer relationship management (CRM). The goal here is to try to sell more non-credit products to current business clients of the banks who have either already received a loan for an amount of at least USD 20,000 or who meet certain structural requirements, such as having a certain minimum number of employees or a certain minimum monthly turnover. In the framework of marketing and business development activities carried out with the help of a Customer Relationship Manager and aimed not only at such clients, but also at their business partners and employees, the banks will promote a broad range of non-credit banking products. The sale of these products will, first of all, increase the institutions' liquidity base; second, it will increase the overall profit earned per client; and third, it will serve to broaden the scope of clients' business relationships with the respective banks so as create ties to the institutions which are based on more than just the fact that they have received a business loan.

Because nothing which is in any way comparable to a CRM-based approach has ever been utilised at the partner banks, the AMP's consultants have developed a CRM manual for the institutions which defines the nature of CRM and its objectives, as well as providing job descriptions and setting forth procedures. The general idea behind CRM and what it is intended to accomplish have already been discussed with the banks. Over the next few weeks, the CRM manual will also be discussed with the banks, people will be given the requisite training in customer relationship management techniques, and specialised software to support CRM will be introduced – all of which will enable the banks to actually begin using this new approach. Once CRM has been fully implemented and is functioning properly, it is expected to help improve the banks' liquidity situation.

2.4 Seminars and training

During the period under review, seminars were held for loan officer trainees, Micro loan officers, Small loan officers, branch managers, middle managers and members of the banks' executive management teams. Two one-week-seminars for loan officer (LO) trainees were held at the AMP's headquarters in Yerevan, and at these seminars a total of 26 LO trainees received instruction in all aspects of micro lending, including the credit cycle, financial analysis, assessment of relevant socio-economic factors as part of the credit analysis process, client acquisition and loan recovery. A total of 46 Micro loan officers received training in the areas of cash-flow analysis, financial cross-checking and loan recovery which was provided in the form of three separate one-day seminars. Two one-day seminars were conducted for Small loan specialists, focusing on cash-flow analysis and project finance; these seminars were attended by a total of 33 Small loan officers. During the period covered by this report, a total of 5 loan officers from Anelik and Ineco received both classroom and on-the-job training in agricultural lending. On separate occasions, the AMP conducted a total of four different workshops for these two banks which dealt with agricultural lending as well as customer relationship management and which were attended by middle-management staff, members of the banks' top management teams and branch managers. Thus, a total of 110 loan officers and about 25 branch managers and other management personnel from the various partner banks – including members of their executive management teams – attended training seminars and workshops during the period under review.

3. Outlook

As indicated above, the next quarter will be used to introduce the new loan products, to make progress in terms of implementing customer relationship management, and to support the banks, especially ACBA, in their efforts to broaden the regional scope of their MSME lending activities. In order to facilitate the regional expansion activities, plans call for a sizeable number of new loan officer trainees to be recruited and begin their training.

The AMP's consultants will also work with the head offices of all of the partner banks to initiate necessary processes of institutional strengthening. Especially as regards the co-ordination of activities within the banks' MSME departments, with respect to personnel policy and in terms of internal control and internal audit functions, there is room for improvement at the partner banks. At the same time, plans call for appropriate job descriptions for every relevant MSME position to be introduced at all of the banks in order to increase the level of formalisation in the allocation and delineation of responsibilities in this area.

At the beginning of the new reporting period, Cascade Bank is expected to disburse its first MSME loans within the framework of the AMP.

4. Results of lending activities:

- Portfolio growth by volume was relatively modest within the reporting period. From April till June the loan portfolio grew by 10%.

- Portfolio growth by number stagnated. Since portfolio by volume increased, the average loan amount also increased from USD 3,128 in April to USD 3,474 in June.

- The quality of the portfolio remained satisfactory, with arrears by more than one day of 1.7% and by more than 30 days of 1.0%.

Table 1: **Development of the outstanding loan volume over the period April 1 - June 30, 2006 (in USD)**

City	Micro Loans			Small Loans			Total			
	31 May, 2006*	30 June, 2006	Growth - (%)	31 May, 2006*	30 June, 2006	Growth - (%)	30 April, 2006	31 May, 2006	30 June, 2006	Growth - (%)
Yerevan	2,323,426	2,451,780	6%	14,398,580	14,888,148	3%	16,283,561	16,722,006	17,339,929	6%
Lori	644,471	663,354	3%	2,465,590	2,713,048	10%	2,687,100	3,110,060	3,376,402	26%
Armavir	4,213,678	4,178,785	-1%	2,399,576	2,572,578	7%	6,680,152	6,613,254	6,751,363	1%
Ararat	2,819,357	2,830,920	0%	1,794,735	1,995,912	11%	4,335,175	4,614,093	4,826,833	11%
Shirak	642,488	698,127	9%	1,102,179	1,359,121	23%	1,671,212	1,744,667	2,057,248	23%
Kotayk	855,307	903,560	6%	1,486,839	1,618,524	9%	2,208,205	2,342,146	2,522,084	14%
Tavush	387,815	423,696	9%	696,851	745,551	7%	1,068,585	1,084,666	1,169,247	9%
Sjunik	387,665	398,134	3%	672,279	777,842	16%	956,423	1,059,944	1,175,976	23%
Gegarkunik	420,229	428,523	2%	752,294	831,908	11%	1,063,426	1,172,523	1,260,431	19%
Vayots Dzor	208,000	222,029	7%	420,356	543,485	29%	671,659	628,355	765,514	14%
Aragatsotn	362,040	370,883	2%	808,735	980,151	21%	991,768	1,170,775	1,351,035	36%
TOTAL AMP	**13,264,475**	**13,569,792**	**2%**	**26,998,015**	**29,026,270**	**8%**	**38,617,266**	**40,262,490**	**42,596,062**	**10%**

*Accurate data for April not available

Table 2: **Development of the number of outstanding loans over the period April 1 - June 30, 2006**

City	Micro Loans			Small Loans			Total			
	31 May, 2006*	30 June, 2006	Growth - (%)	31 May, 2006*	30 June, 2006	Growth - (%)	30 April, 2006	31 May, 2006	30 June, 2006	Growth - (%)
Yerevan	1,186	1,180	-1%	458	450	-2%	1,771	1,644	1,630	-1%
Lori	368	356	-3%	81	90	11%	468	449	446	-1%
Armavir	4,286	4,148	-3%	106	120	13%	4,427	4,392	4,268	-3%
Ararat	3,404	3,353	-1%	69	77	12%	3,304	3,473	3,430	-1%
Shirak	441	432	-2%	45	50	11%	503	486	482	-1%
Kotayk	630	648	3%	62	66	6%	669	692	714	3%
Tavush	221	225	2%	37	39	5%	266	258	264	2%
Sjunik	239	231	-3%	27	32	19%	257	266	263	-1%
Gegarkunik	306	311	2%	30	30	0%	271	336	341	1%
Vayots Dzor	152	155	2%	16	16	0%	169	168	171	2%
Aragatsotn	203	204	0%	40	47	18%	239	243	251	3%
TOTAL AMP	**11,436**	**11,243**	**-2%**	**971**	**1,017**	**5%**	**12,344**	**12,407**	**12,260**	**-1%**

*Accurate data for April not available

5. Co-operation with the partner banks

5.1 ACBA

ACBA is the AMP's most dynamic partner bank. Unfortunately, though, after the German-Armenian Fund was phased out, the bank basically did nothing to further develop key institutional aspects of MSME lending. Except for a modest increase in the size of the loans which the branch managers are authorised to approve, no effort was made to further develop the organisational structure of MSME lending operations, lending procedures or MSME loan products. One characteristic of ACBA is the very high degree of centralisation in decision-making: the CEO, Mr. Gishyan, handles nearly every single issue of any importance. This regularly leads to a temporary cessation of activities in many individual projects when he is not in Yerevan, but on the other hand, because in practice the CEO cannot actually deal with all, or even nearly all, of the issues on which decisions must be taken, it creates a certain degree of decentralisation within the second and third levels of management, especially in terms of co-ordinating the branch network.

The co-operation with ACBA is quite productive. Especially Mr. Gishyan and his deputy for lending operations, Mr. Andreasyan, are very open to new ideas and are eager to make use of the AMP's support as much as possible. ACBA would like to have the AMP's support in particular to help with the realisation of its plans to open 12 new branches by the end of 2006 (further branch openings are projected for 2007). ACBA's regional expansion plans are so ambitious that this project appears to be making excessive demands upon the bank's management staff, with the result that, to a certain extent, they are apparently neglecting other important issues.

The most significant constraints as regards the regional expansion are in the area of personnel recruitment and training. Many of the new branch managers are recruited from among the bank's high-potential MSME loan officers, and thus, on the one hand, this procedure will facilitate the smooth implementation of MSME lending operations in the new branches and help ensure the sound management of the MSME portfolios which are to be generated. On the other hand, this approach leads to a "brain drain" among the loan officers at nearly every single branch which is already operating and hinders urgently needed capacity building at ACBA's head office, in particular the creation of a strong co-ordination department to oversee all of the bank's MSME lending operations.

The absence of a strong co-ordination department for MSME lending has become the major obstacle to the implementation of a systematic approach to training, loan officer recruitment and the organisation of MSME lending activities in the regional branches. As long as ACBA was a comparatively small bank, its existing management structure was adequate to deal with most of the challenges posed by the institution's growth and development. But considering the scale of the growth which ACBA has experienced, and given that it is now in the process of launching an ambitious regional expansion programme, the old management structure is no longer sufficient and it is now time to make the appropriate changes. These issues have been discussed with ACBA and over the next few weeks assistance will be provided in order to help the bank make the requisite modifications. It is envisaged that the head of the Department for Commercial Loans, who is also responsible for the co-ordination of all MSME operations and clearly has an excessive workload, will be supported in future by three regional managers – one for northern Armenia, one for central Armenia and one for the southern part of the country – who will be given the task of co-ordinating

MSME operations in the individual regions for which they are responsible. In addition, at the end of June ACBA was in the process of conducting a large-scale recruitment campaign to fill new positions created in conjunction with the regional expansion. Given that the AMP has now assigned two local trainers to the regions – one to the northern part of the country and one to the south – once the regional managers have taken up their duties, they will receive assistance from the AMP in training the new staff in the regional branches.

Over the last few months, even after the end of the period of high demand for agricultural loans, ACBA also faced severe liquidity problems. The result was that the scope of lending to business clients was limited to the volume that could be financed with the inflow of funds from borrowers' principal and interest payments. It would seem that the aggressive regional expansion strategy, and especially the purchase of real estate and the refurbishment of premises for new branches, exacerbated the situation. It might well be that the expected involvement of Credit Agricole as a shareholder in ACBA, and the sizeable injection of new capital which this will presumably provide, has played a crucial role in the financial planning undertaken by the management, particularly in terms of alleviating the current liquidity problems.

In early July, the AMP's consultants will conduct a one-and-a-half-day seminar for all of ACBA's branch managers and for the bank's executive management at which key issues with regard to regional expansion, the credit technology and CRM will be discussed.

Table 3: **Overview of the performance of AMP lending operations at ACBA**

	Yerevan	Lori	Armavir	Ararat	Shirak	Kotayk	Tavush	Sjunik	Gegarkunik	Vayots Dzor	Aragatsotn	Total
Output over last 2 months												
Disbursed loans - May 31, 2006*	65	44	79	239	9	59	29	33	21	12	32	622
Disbursed loans - June 30, 2006	59	48	74	53	29	58	34	28	21	17	26	447
Disbursed loans (volume USD) - May 31, 2006*	859,184	580,837	222,424	496,922	104,240	218,417	91,007	185,163	110,953	22,450	259,070	3,150,667
Disbursed loans (volume USD) - June 30, 2006	494,180	484,855	526,590	474,919	223,377	305,200	183,266	214,389	288,605	259,773	262,925	3,718,079
Development of outstanding portfolio												
Outstanding loans - May 31, 2006*	588	417	4279	3473	195	577	258	266	169	168	243	10,633
Outstanding loans - June 30, 2006	597	416	4151	3430	199	608	264	263	174	171	251	10,524
Growth (%)	1.53%	-0.24%	-2.99%	-1.24%	2.05%	5.37%	2.33%	-1.13%	2.96%	1.79%	3.29%	-1.03%
Outstanding loans (volume USD) - May 31, 2006*	7,870,213	2,815,208	6,358,085	4,614,093	1,101,562	1,966,264	1,084,666	1,059,944	972,902	628,355	1,170,775	29,642,067
Outstanding loans (volume USD) - June 30, 2006	7,845,809	3,093,943	6,499,715	4,826,833	1,252,795	2,084,186	1,169,247	1,175,976	1,056,630	765,514	1,351,035	31,121,682
Growth (%)	-0.31%	9.90%	2.23%	4.61%	13.73%	6.00%	7.80%	10.95%	8.61%	21.83%	15.40%	4.99%
Portfolio quality												
Arrears rate (volume) - May 31, 2006*	1.42%	1.74%	0.39%	0.42%	0.54%	4.21%	4.41%	2.55%	13.22%	7.64%	0.94%	1.88%
Arrears rate (volume) - June 30, 2006	2.09%	1.36%	0.33%	0.50%	1.41%	4.37%	1.05%	2.29%	16.22%	5.71%	0.74%	2.01%
Loan officers												
No. of LOs under training (up to 6 months)	1	0	2	0	0	0	0	0	0	1	0	4
No. of trained LOs (> 6 months)	12	6	4	6	4	4	2	2	2	0	5	47
Total no. of LOs	13	6	6	6	4	4	2	2	2	1	5	51
o. of LOs financed by partner bank	13	6	6	6	4	4	2	2	2	1	5	51

*Accurate regional data not available for April

5.2 Anelik

Unfortunately, Anelik Bank is the weakest partner bank in the AMP. During the active phase of the German-Armenian Fund, i.e. while technical assistance was being provided to the partner banks, the former deputy CEO for lending, Mrs. Tadevosyan, successfully co-ordinated all of the bank's MSME lending activities. In July 2005 Mrs. Tadevosyan had to leave the bank, and the remaining deputy CEOs did not show any particular interest in MSME lending; since then, the co-ordination of MSME lending operations at the head office has been severely neglected. Due to this absence of management interest and co-ordination, MSME lending at Anelik is clearly in decline. Regional loan approval limits have not been increased over the past year, nothing has been done to further develop procedures or products, no significant effort has been made to increase the number of loan officers, and a systematic training and professional-development programme has not been implemented for the existing lending staff. All in all, it is therefore not surprising that Anelik is steadily losing loan officers. The best LOs are leaving to join other banks, and others are taking jobs in various other sectors.

Also in terms of serving the target group, the situation at Anelik has deteriorated during the past year. The collateral requirements for Express clients have been increased and the overall strategy seems to be focused more and more on issuing loans for larger amounts. It is therefore not surprising that Anelik will probably not introduce the quasi-automated Express loan.

Although the overall institutional situation at Anelik has deteriorated significantly, it is important to note that the remaining members of the MSME lending staff still exhibit a surprisingly high level of motivation. With the approval of Anelik's CEO, several loan officers and branch managers attended a workshop and a seminar dealing with the credit technology used in agricultural lending. Shortly after these training measures were completed, the AMP's consultants provided additional classroom training in agricultural lending techniques and accompanied loan officers from Anelik's branch in Gavar and a responsible person from the head office on several visits to agricultural clients in order to supervise and support the credit analysis process for the loan applicants in question. However, after a number of loan applications had been approved, all agricultural lending operations had to be put on hold again because, for a few weeks, Anelik also faced severe liquidity problems. After a month had elapsed and the situation appeared to have improved due to the inflow of funds from borrowers' principal and interest payments, some of the agricultural loans that had been approved were disbursed, albeit with a certain delay. The liquidity situation was eased somewhat thanks to the approval of another credit line by the EBRD in mid-May. Unfortunately, though, by the end of June these additional funds had all been disbursed and MSME lending, including agricultural lending, was again put on hold.

Since Anelik received technical assistance over a period of many years, and given that at present this institution does not appear to regard MSME lending as a priority area of its operations, the AMP is not devoting a very significant portion of its time or resources to support measures for this bank.

Accordingly, the AMP's consultants are focusing primarily on co-ordination activities at Anelik's head office with a view to persuading the bank to once again take a genuine interest in MSME lending operations and make the necessary commitment to this area of activity at the operational level. In addition, the AMP is helping to develop a new credit policy, inviting lending staff to attend its training seminars and supporting the bank in its efforts to open two new branches, one in Yerevan and one in Ejmiadzin, a city near Yerevan.

Table 4: **Overview of the performance of AMP lending operations at Anelik**

	Yerevan	Shirak	Kotayk	Gegarkunik	Total
Output over last 2 months					
Disbursed loans - May 31, 2006*	78	38	7	15	138
Disbursed loans - June 30, 2006	84	40	13	0	137
Disbursed loans (volume USD) - May 31, 2006*	669,340	107,003	61,512	29,820	867,675
Disbursed loans (volume USD) - June 30, 2006	1,279,955	252,901	92,263	0	1,625,118
Development of outstanding portfolio					
Outstanding loans - May 31, 2006*	813	253	115	167	1,348
Outstanding loans - June 30, 2006	800	248	106	167	1,321
Growth (%)	-1.60%	-1.98%	-7.83%	0.00%	-2.00%
Outstanding loans (volume USD) - May 31, 2006*	6,722,063	558,355	375,882	199,621	7,855,921
Outstanding loans (volume USD) - June 30, 2006	7,485,739	728,324	437,898	203,801	8,855,762
Growth (%)	11.36%	30.44%	16.50%	2.09%	12.73%
Portfolio quality					
Arrears rate (volume) - May 31, 2006*	1.39%	0.42%	0.00%	3.25%	1.31%
Arrears rate (volume) - June 30, 2006	0.45%	0.31%	0.00%	3.25%	0.48%
Loan officers					
No. of LOs under training (up to 6 months)	3	0	0	0	3
No. of trained LOs (> 6 months)	21	5	4	2	32
Total no. of LOs	24	5	4	2	35
o. of LOs financed by partner bank	24	5	4	2	35

*Accurate regional data not available for April

5.3 Ineco

The co-operation with Ineco is very satisfactory. The bank's executive and middle management staff are always open to positive and constructive criticism and are willing to discuss any issues raised by the AMP in conjunction with the programme's efforts to make MSME lending operations in Ineco more efficient. On the other hand, it must be noted that Ineco has traditionally given priority to consumer lending, and that in the future the bank will continue to regard consumer lending as the most important segment of its credit business. The implications of this preference for consumer lending are underscored during periods when liquidity is scarce: at such times, the scope of MSME lending is limited to what can be financed with the inflow of funds from borrowers' interest and principal payments, whereas consumer lending operations continue to be funded at more or less the normal level, i.e. without a significant reduction in the number or volume of disbursements. In June the situation with regard to MSME lending had become so bad that Ineco sent most of the MSME lending staff on vacation, as there was no point in processing or approving new loan applications, given that the bank was not prepared to make funds available for the disbursement of any new MSME loans.

The constraints posed by the liquidity situation were also the reason why, after having initially discussed the introduction of the new agricultural lending methodology with the AMP, the bank decided in the end not to implement the methodology. As Ineco's management stated, it would make no sense at all to enter a new market without having first satisfied the potential demand in the bank's traditional MSME market.

In view of the overall shortage of liquidity, it is imperative to make every effort to also introduce an active CRM approach for current MSME clients at Ineco. In addition, the liquidity situation at Ineco might be eased in the near future through the provision of funds by the IFC, which has plans to acquire a stake in the bank and open a USD 3 million credit line for Ineco. However, given the extent of the unmet demand for MSME loans at present, it is expected that these additional funds would also be disbursed in only a few months.

At this point it is not clear whether the inflow of new capital and the opening of the credit line would enable Ineco to begin carrying out its plans for the expansion of its regional branch network. In discussions held with the bank in April, the AMP's consultants presented scenarios for regional expansion involving various regions of the country, showed how the programme could provide assistance to the bank in terms of loan officer recruitment and training in the regions, and carried out a break-even analysis for potential new branches. Unfortunately, however, once it became clear that the bank would encounter severe liquidity problems in the summer, the entire project was put on hold. And given that Ineco's plans initially called for it to open new branches in cities where other partner banks of the AMP do not currently operate, its decision not to open additional branches is clearly a setback for the AMP as regards its objective of expanding the scope of programme operations to cover regions in Armenia which have so far been undersupplied in terms of MSME finance.

When the plans for regional expansion were discussed, it once again became clear that the bank's overall organisational structure is not optimal in terms of the allocation of tasks, project organisation and follow-up mechanisms. In the meantime, the bank has developed certain structural modifications and the board has given approval for their implementation, but it remains to be seen whether they will in fact lead to an improvement in the situation. Moreover, during the period under review the AMP's consultants, working in collaboration with the bank, developed a new lending policy which was approved by the board in June. This new policy now governs not only MSME lending operations but all lending operations for business clients throughout the bank. The new policy ensures that the bank's lending methodology incorporates the principal features of IPC's credit technology, and it also establishes a binding, clearly defined set of rules and procedures for the use of the lending methodology which in turn ensures that it is correctly applied.

Table 5: **Overview of the performance of AMP lending operations at Ineco**

	Yerevan	Lori	Armavir	Shirak	Total
Output over last 2 months					
Disbursed loans - May 31, 2006*	31	3	17	2	53
Disbursed loans - June 30, 2006	13	0	14	3	30
Disbursed loans (volume USD) - May 31, 2006*	386,444	12,162	39,527	4,327	442,460
Disbursed loans (volume USD) - June 30, 2006	35,006	0	35,817	2,388	73,211
Development of outstanding portfolio					
Outstanding loans - May 31, 2006*	243	32	113	38	426
Outstanding loans - June 30, 2006	233	30	117	35	415
Growth (%)	-4.12%	-6.25%	3.54%	-7.89%	-2.58%
Outstanding loans (volume USD) - May 31, 2006*	2,129,730	294,852	255,169	84,749	2,764,501
Outstanding loans (volume USD) - June 30, 2006	2,008,381	282,459	251,648	76,129	2,618,618
Growth (%)	-5.70%	-4.20%	-1.38%	-10.17%	-5.28%
Portfolio quality					
Arrears rate (volume) - May 31, 2006*	2.04%	6.27%	6.57%	1.99%	2.91%
Arrears rate (volume) - June 30, 2006	0.92%	5.19%	6.29%	0.35%	1.88%
Loan officers					
No. of LOs under training (up to 6 months)	1	0	1	0	2
No. of trained LOs (> 6 months)	6	2	1	3	12
Total no. of LOs	7	2	2	3	14
o. of LOs financed by partner bank	7	2	2	3	14

*Accurate regional data not available for April

5.4 Armeconombank

When the AMP was launched, the management of Armeconombank did not show any interest in co-operating with the programme. The bank's CEO, Mr. Osipyan, even claimed that Armeconombank had never received funds from the EBRD to finance MSE lending, and said that, for its part, the bank was unwilling to initiate MSE lending in collaboration with the EBRD. As a result, it was agreed with the EBRD to terminate the co-operation with Armeconombank in April.

At the end of May, Mr. Osipyan left the bank – his departure came unexpectedly – and his deputy, Mr. Suksysian, was appointed as the new CEO. Shortly after that, the bank signalled to the AMP's consultants that it was thinking about once again becoming involved in MSME lending, and thus that it would be willing to co-operate with the AMP. It was agreed with the EBRD that it would only make sense to allocate technical assistance resources to Armeconombank if this institution were to provide proof of its renewed commitment to MSME lending by developing ambitious plans with regard to the growth in the number of loan officers, portfolio growth, enhancing its outreach to the target group and utilising its very large branch network for MSME lending.

5.5 Cascade Bank

Cascade Bank is the AMP's newest partner bank. This institution, which is a rather small bank in terms of total assets and the size of its branch network, is part of Cascade Capital Holding. The holding company, which, in addition to the bank, also comprises an insurance company, a credit union and various investments in media enterprises, is owned by the Gafesyan Family Foundation, a foundation which was set up by Mr. Gafesyan, a wealthy Armenian businessman who made a fortune in the United States.

Working together, the AMP's consultants and the management of Cascade Bank selected six loan officer candidates in mid-June. Immediately after they were selected, all six attended a one-week seminar held by the AMP's consultants, following which they took an examination which was designed to gauge their suitability to serve as MSME loan officers. After the results of this examination had been evaluated, it was decided to launch MSME lending operations with three of these six candidates.

At the end of June, an MSME credit policy was in the process of being approved by Cascade's management, an office had been set up for the staff who will be involved in MSME lending operations and a business plan had been established; this business plan calls for MSME credit operations to be launched at the beginning of July, with the first disbursements being carried out in mid-July.

At this point it is not clear how much operational independence the bank's management will be given by the management of the holding company, and it is also unclear whether the MSME loan department can be fully integrated into the bank's overall institutional structure.

The co-operation with the bank's top management is very good and Cascade's management has said that MSME lending is to become one of the bank's priority areas of activity in the future. At present, Cascade has only one outlet, i.e. it conducts all of its business operations from its head office, but the bank's management plans to open branches in both northern and southern Armenia in 2007.