Armenia Micro Lending Programme

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Quarterly Report

October – December 2006

1. General situation

As in the previous reporting period, the Armenian Dram (AMD) continued to appreciate against the USD. Indeed, from the beginning of October until the end of the year, the AMD gained another 5% against the dollar, appreciating from 382 to 363 AMD per USD. The substantial appreciation of the local currency, which began in May, clearly affected Armenia's trade balance in 2006: Foreign trade during the period January – November was up by 13.6% compared with the same period in 2005; however, imports rose by 20% to USD 1.95 billion, while exports increased by only 0.3% to USD 895 million. Since Armenia's central bank claims that the appreciation of the local currency is the result of market forces, it is most likely that the AMD's gains were both triggered and fuelled by the substantial rise in foreign investment, which was up by 32%, and by a significant increase in remittances compared with previous years.[1]

Over the same period, Armenia's GDP rose by 13.2%. It appears that the changes in output for key sectors were in line with what one might have expected, given the appreciation of the AMD: industrial output and power production were down by 1.2% and 6.6% respectively, whereas an increase of 23% was reported for the service sector. In addition, output in the construction sector was up by 37%.[2]

It appears that the developments outlined in the preceding paragraphs are having two main impacts on the Armenian financial market: First, the huge inflow of remittances is making the already large consumer lending market even larger, and various banks, including the AMP's partner banks, are trying to position themselves so that they can benefit from the growth in this area. Given that the available financial, human and management resources are limited, MSME lending clearly has to struggle in order to compete for resources with the banks' strong consumer lending departments. Second, the boom in the construction sector might create risks for the banks' loan portfolios in the future, and thus it might be advisable to closely monitor future developments in this area.

[1] The Centre for National and Strategic Studies expects overall remittances in 2006 to be about 15% higher than in 2005, with the total most likely amounting to USD 1.5 billion (24% of GDP).
[2] All figures have been taken from the Armpress News Agency, 21 December 2006, and the web site of the National Statistical Service.

As was indicated in the previous quarterly report, Converse Bank, which is a major player in the Armenian banking market, came under massive pressure from the Armenian Central Bank, and this pressure was intensified during the reporting period. In October the Central Bank even urged Converse's shareholders to sell their stakes in the institution by the end of the year, stating that if they did not do so, the bank would lose its licence. Now, however, it appears that Converse will be bought by an Armenian investor.

During the reporting period, MSME lending results were much better than they had been in the previous period. Indeed, record disbursement levels were achieved in November and December in terms of both volume and numbers. These results were attributable mainly to the fact that the peak agricultural lending season began during the reporting period, and the fact that Ineco Bank became much more active after it was clear that this institution would soon receive a new EBRD credit line.

In consultation with the EBRD it was decided in November to phase out technical assistance to ACBA Credit Agricole by the end of the year. Thus, at the beginning of December the AMP closed its office in the southern part of Armenia – which had been set up to assist ACBA in its efforts to develop its MSME lending activities in the Sjunik region, which was underserved at the time – and to open a second office in northern Armenia in order to assist Ineco Bank with its MSME operations in that part of the country.

In December, Armeconom Bank finally expressed an interest in resuming its collaboration with the AMP. During a meeting with its CEO, Mr. Sukiasyan, a decision was taken to carry out classroom training measures for Armeconom's lending staff. This training will be provided to both current lending staff and the new loan officers whom the bank plans to recruit in January 2007.

2. General information on the Consultant's activities

As in the preceding months, the AMP's priorities differed depending on the specific needs of the individual institutions: At Cascade Bank, the AMP's consultants focused on operational issues, whereas at the mature partner banks, the programme focused on institutional capacity building. At Ineco, the two areas were given equal priority. At Cascade Bank the AMP's consultants worked hard in order to establish MSME lending as a part of the bank's daily operations. After it became clear that Ineco will be receiving additional resources from the EBRD, the AMP concentrated its efforts at this bank on re-establishing MSME lending structures and re-launching MSME lending operations at all of its branches. At ACBA, which is the AMP's most mature partner institution in terms of MSME lending, the programme assisted in coaching the bank's three regional managers, monitored the introduction of back-office staff functions and made preparations for the introduction of the position of head of the credit department for MSME lending departments – positions which will in each case be filled by a local staff members.

As discussed in the previous report, the AMP attempted to implement new loan products. As had been anticipated, ACBA's efforts were not successful, but the bank has expressed a firm interest in introducing the products in question as soon as the necessary management capacity and the other resources required to launch them are available. Ineco, which started to move faster from November on, has adopted the AMP's proposal regarding credit lines and is now able to offer this product to its SME clients.

In the following, a brief overview will be given of the progress made during the reporting period in implementing various key activities discussed in the previous quarterly report.

a) Implementing the customer relationship management (CRM) approach

ACBA had not been able to recruit any potential CR managers during the third quarter, and during the period covered by this report its efforts to recruit staff for these positions were also unsuccessful. Although many candidates were interviewed, none had the required experience and qualifications as defined by the bank and the AMP. In the process of reviewing the applications received and interviewing the candidates, it became clear that there simply are not any trained CR managers available on the local labour market who could be recruited; it appears that the whole idea of CRM is still a very new concept for the financial sector in Armenia. In addition, ACBA seemed to be sceptical about the advisability of recruiting and training people who have just completed their university studies for the position of CR manager. ACBA's management thought that it would be risky to entrust "strangers", i.e. people with no previous connection with the bank, who also have no previous work experience with the task of managing ACBA's relationships with its most important clients.

In early November it was decided to launch a pilot project in ACBA's big Shengavit branch in Yerevan using an individual who was already employed by the branch and who had previously been responsible for the acquisition of deposits and who also appeared to be sufficiently qualified to meet the criteria for a CR manager. Under the guidance of the AMP's consultants and managers from ACBA who had been assigned to the pilot project, the branch's 140 largest clients were analysed in terms of their potential as purchasers of non-credit products.[3] The clients who were deemed to have the most potential in this regard then received a promotional letter in which ACBA's products were presented and a meeting with the client was requested. In the end, of the 30 enterprises that were contacted, a sizeable number indicated that they were interested in non-credit products, and by the end of November no fewer than 10 of these companies had decided to have their employees' salaries paid directly into accounts held at ACBA. Although the AMP's active support for ACBA was phased out at the end of December, the programme's consultants are confident that despite all of the difficulties encountered in the introduction of the CRM approach, the successes achieved by this pilot branch have had a "demonstration effect", and that, as a result, ACBA will actively use this approach in future and thus serve SME clients more comprehensively.

b) Supporting regional expansion

During the first half of the reporting period, support for regional expansion was provided only to ACBA because initially it was the only bank which was interested in regional expansion, i.e. in either opening new branches or developing MSME lending in existing regional branches. As noted in the previous report, the AMP had provided two consultants to support ACBA's expansion efforts: In the northern part of the country, one consultant helped ACBA to make the necessary preparations for the establishment of MSME lending activities in its new branches there, which were originally supposed to be opened earlier in the year. In December ACBA was finally able to launch its operations in the cities of Spitak and Tashir. In the south, the AMP's consultant was able, in collaboration with the bank's newly introduced regional manager, to boost disbursements from 12 loans for a total of around USD 100,000 in August to 43 loans totalling around USD 300,000 in December. During the reporting period, ACBA's southernmost branch took on three new loan officer trainees and the AMP is confident that even after the consultant is no longer available to personally support operations, MSME lending activities there will continue to develop favourably.

When Ineco decided in early November that it wanted to once again become more actively involved in MSME lending, the AMP's regional consultants began concentrating their efforts more on

[3] Key criteria for the inclusion of clients in the group that was analysed were the size of their existing loans, the monthly turnover on their current accounts, and the number of employees. Ninety percent of the clients analysed clearly fall within the target group of MSMEs as defined by the EBRD.

reactivating and developing MSME lending activities in the bank's three regional branches. In early December it was decided to transfer one of the AMP's consultants from the south to the Shirak region in north-western Armenia to oversee MSME operations at Ineco's branch in Gyumri. For a month now, the programme has been providing intensive support to Ineco at its two northern regional branches, and, as a result, MSME lending activities at these offices have increased considerably: In October, these two branches together disbursed a total of 9 MSME loans with a combined volume of USD 13,000. In December, their level of disbursements was already significantly higher, with a total of 30 loans amounting to USD 250,000 being issued by the two branches. Moreover, all of Ineco Bank's regional branches have either already recruited and begun training new loan officer trainees or will recruit additional LO trainees during the initial months of 2007. Ineco's third regional branch, in Armavir, never stopped disbursing MSME loans, and thus at this branch it was not necessary to reactivate AMP lending activities. Nevertheless, the branch is being given the requisite level of support by the programme, with the necessary services being provided directly by the programme's office in Yerevan, which is relatively close to Armavir.

d) Strengthening partner banks' institutional capacities

At ACBA, the individuals who had been appointed to the newly introduced position of regional manager got off to a very good start. The AMP's consultants worked very intensively with the three managers over the reporting period. The overall aim was to enable them to work independently, i.e. without assistance from the programme's consultants, as soon as possible. Thus, right from the beginning the AMP's approach focused more on coaching than on providing training in the usual sense. In the meantime, ACBA's regional managers are overseeing – and, if necessary, actively managing – the full MSME credit cycle in every regional branch; they are involved in strategic planning in terms of generating business plans; they are planning recruiting activities; and they are organising and conducting micro seminars. Now that this structure is in place, ACBA will in future be able to expand its regional branch network and also its regional MSME lending operations without the assistance of the AMP's consultants.

With a view to improving internal control and increasing the loan officers' efficiency, ACBA introduced back office personnel functions, with at least one back office staff member being assigned to nearly all of its branches. In the near future ACBA will also be able to recruit back office staff for the remaining branches, i.e. those offices where this function has not yet been introduced.

In order to assist the regional managers at an operational level, and thus to ensure that they are able to focus on high-level tasks while the branch network is expanding, the AMP's consultants proposed to ACBA that it introduce the position of head of the MSME department at its regional branches. A job description for this position and a set of written procedures were provided to the bank and the concept was discussed with ACBA's top management. The AMP is confident that ACBA will implement the concept in the very near future.

The programme plans to implement an institution building concept for Ineco which is basically similar to the one just discussed, but at Ineco the AMP decided to go back one step and temporarily exercise more control in credit committees and daily operations than it did at ACBA. In November and December it was important to get operations started again and to re-familiarise branch managers with IPC's technology and lending principles. The programme was able to persuade the bank's management to shift some of the existing loan officers away from the bank's consumer-lending activities and reallocate them to its MSME lending operations on a full-time basis. At present, Ineco is still looking for a qualified individual to serve as head of the MSME department in its head office. The AMP is confident that this vacancy will be filled in early January.

e) Seminars and training

In addition to on-the-job training, especially for the loan officers at Ineco and ACBA, and coaching provided to the banks' regional managers, several seminars were conducted during the reporting period.

At the beginning of October, a three-day seminar was organised to prepare the individuals selected to serve as ACBA's regional managers for their new responsibilities. At the same time, this seminar was used to generate, in collaboration with the participants, a number of management tools such as reports and checklists in order to help them organise their activities using a set of standardised procedures.

In October a three-day seminar was held for ACBA's lending staff, including some branch managers, in a resort town near Yerevan. This seminar was planned and organised by ACBA itself and most of the presentations were given by ACBA's regional managers. In supporting both the preparatory work for the seminar and its implementation, the AMP's consultant focused in particular on developing the regional managers' presentation skills and providing additional training materials.

In November the AMP's consultant in southern Armenia, working in collaboration with the responsible regional manager, conducted a four-day basic training seminar for ACBA's three new loan officer trainees and for two loan officers; the seminar was held in the city of Kapan.

In December another four-day basic training seminar was held at the AMP's head office in Yerevan. Thirteen loan officer trainees from ACBA, Anelik and Ineco received their initial classroom training at this seminar.

3. Outlook

Given that the AMP's active co-operation with ACBA was phased out in December, the programme will restrict its activities at ACBA, focusing exclusively on monitoring the bank's MSME portfolio and on continuing the ongoing dialogue with the institution's executive management.

Over the next few months, the AMP's main focus will clearly be on Ineco. Here it will be important to train new lending staff, to increase the scope of Ineco's lending activities at every single branch and to create an efficient, well-organised MSME lending department at Ineco's head office to oversee the bank's activities in the framework of the programme. Moreover, efforts will be made to further streamline lending procedures and in particular to establish a genuine "express lending culture" for very small loan amounts.

As will be discussed in greater detail below, the feasibility of continuing MSME lending activities at Cascade Bank will depend on whether the bank is able to implement the lending procedures recommended by the programme, which are appropriate for credit extension to the MSME target group. If the bank succeeds in implementing these procedures and the EBRD gives its approval, the AMP will continue its efforts to turn MSME lending at Cascade Bank into a line of business which is accepted by its management and also generates a profit for the bank.

4. Results of lending activities:

- During the reporting period, portfolio growth in volume terms was about 23%. At the end of December the outstanding portfolio totalled nearly USD 56 million.

- Disbursements in terms of number were high in November and December. In November 2,541 loans and in December 2,559 loans were disbursed.

- The quality of the portfolio improved, with arrears of more than one day amounting to 0.9% and arrears of more than 30 days coming to 0.7%.

Table 1: **Development of the outstanding loan volume over the period October 1 - December 31, 2006 (in USD)**

	Micro Loans			Small Loans			Total				
Region	30 September, 2006	31 December, 2006	Growth - (%)	30 September, 2006	31 December, 2006	Growth - (%)	31 May, 2006	30 September, 2006	31 December, 2006	Growth - 3 months (%)	Growth - 7 months (%)
Yerevan	2,984,176	3,774,136	26%	15,995,477	16,790,977	5%	16,722,006	18,979,653	20,565,113	8%	23%
Lori	490,835	526,958	7%	3,202,428	3,108,936	-3%	3,110,060	3,693,263	3,635,894	-2%	17%
Armavir	3,149,991	5,198,240	65%	2,986,773	4,153,795	39%	6,613,254	6,136,764	9,352,035	52%	41%
Ararat	2,365,655	3,423,818	45%	2,279,408	3,238,908	42%	4,614,093	4,645,063	6,662,726	43%	44%
Shirak	885,165	1,078,095	22%	1,805,243	2,060,583	14%	1,744,667	2,690,408	3,138,678	17%	80%
Kotayk	855,808	1,146,867	34%	2,184,982	2,947,349	35%	2,342,146	3,040,790	4,094,216	35%	75%
Tavush	402,949	437,322	9%	874,021	1,167,902	34%	1,084,666	1,276,969	1,605,224	26%	48%
Sjunik	346,391	518,600	50%	950,331	1,537,679	62%	1,059,944	1,296,722	2,056,279	59%	94%
Gegarkunik	635,746	899,187	41%	835,269	1,090,020	30%	1,172,523	1,471,015	1,989,207	35%	70%
Vayots Dzor	239,446	276,573	16%	426,851	648,226	52%	628,355	666,297	924,799	39%	47%
Aragatsotn	326,575	442,761	36%	1,211,467	1,519,863	25%	1,170,775	1,538,042	1,962,624	28%	68%
TOTAL AMP	**12,682,736**	**17,722,557**	**40%**	**32,752,251**	**38,264,238**	**17%**	**40,262,490**	**45,434,987**	**55,986,795**	**23%**	**39%**

Table 2: **Development of the number of outstanding loans over the period October 1 - December 31, 2006**

Region	Micro Loans			Small Loans			Total				
	30 September, 2006	31 December, 2006	Growth - (%)	30 September, 2006	31 December, 2006	Growth - (%)	31 May, 2006	30 September, 2006	31 December, 2006	Growth - 3 months (%)	Growth - 7 months (%)
Yerevan	1 247	1 459	17%	469	481	3%	1 644	1 716	1 940	13%	18%
Lori	269	268	0%	111	113	2%	449	380	381	0%	-15%
Armavir	2 954	3 712	26%	130	167	28%	4 392	3 084	3 879	26%	-12%
Ararat	2 614	3 079	18%	94	107	14%	3 473	2 708	3 186	18%	-8%
Shirak	432	503	16%	71	81	14%	601	503	584	16%	-3%
Kotayk	611	682	12%	88	126	43%	577	699	808	16%	40%
Tavush	229	224	-2%	50	65	30%	258	279	289	4%	12%
Sjunik	215	225	5%	46	68	48%	266	261	293	12%	10%
Gegarkunik	377	474	26%	32	43	34%	336	409	517	26%	54%
Vayots Dzor	149	148	-1%	13	19	46%	168	162	167	3%	-1%
Aragatsotn	178	191	7%	61	78	28%	243	239	269	13%	11%
TOTAL AMP	**9 275**	**10 965**	**18%**	**1165**	**1348**	**16%**	**12 407**	**10 440**	**12 313**	**18%**	**-1%**

5. Co-operation with partner banks

5.1 ACBA

During the reporting period, ACBA finalised all of the steps needed to register as a closed joint stock company, thus finally making it possible for Credit Agricole to become a shareholder of the bank. Credit Agricole now holds 28% of the capital, 1% is held by ACBA's CEO, Mr. Gishyan, and the remainder is held by ACBA's regional entities. ACBA's total capital is now equivalent to around USD 45 million. So far, Credit Agricole does not appear to have intervened much in ACBA's daily operations. Unfortunately, the entire process of re-registering and then renaming the bank (it is now officially known as "ACBA-Credit Agricole") caused delays with regard to the implementation of certain AMP activities, including ACBA's regional expansion.

All in all, co-operation with the bank was very good, and in the final analysis it proved possible to carry out nearly all of the institution building tasks which had been defined by the AMP in collaboration with the bank. Today, ACBA's MSME lending operations are based on much more solid structures than were in place when the programme was launched. Now that regional managers have been successfully introduced and this function is firmly established, ACBA has a structure with which it can incrementally increase the scope of its MSME lending operations, including their geographical scope, without the assistance of the AMP's consultants. In addition, the introduction of a functional separation between back- and front-office staff in nearly all of the bank's MSME lending departments is a step forward in terms of enhancing internal control and improving loan officer efficiency. As has already been noted, ACBA was not able to introduce the position of head of the credit department for the MSME lending departments at all branches – a step which would clearly improve the effectiveness of the bank's regional mangers and which would also improve the overall quality of lending in its branches. If ACBA is able to close this managerial gap, in the future it will also be highly successful in its efforts to serve the credit needs of MSMEs in Armenia.

In the end, the efforts to introduce CRM at the bank led to the implementation of a pilot project at ACBA's large Shengavit branch in Yerevan. As indicated above, this pilot project achieved good results in a comparatively short time, and thus it had a strong demonstration effect as regards the bank's top management. Apart from the fact that it generated favourable results, the project is considered to have been a very important step because it enabled the bank's management, all the way down to the branch managers, to understand the idea of CRM and why it can make such valuable contributions to the overall success of the bank. The fact that CRM turned out to be effective in such a short time may go a long way towards ensuring that in future ACBA will undertake a systematic effort to begin providing more comprehensive service to MSME clients in all its branches.

In consultation with the EBRD it was decided to phase out technical assistance to ACBA by the end of the year. Taking into consideration what has been achieved at ACBA since the launch of programme activities, it can be concluded that today MSME lending at ACBA is firmly established and based on a secure, solid foundation, and that if it makes good use of the resources it already has, ACBA might very well be able to expand and enhance its MSME activities even further without having to depend much on the support of external consultants.

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

	Yerevan	Vanadzor	Spitak	Tashir	Echmiadzin	Ararat	Vedi	Gjumri	Abovyan	Ijevan	Kapan	Gavar	Yeghegnadzor	Ashtarak	Total
Output over last 3 months															
Disbursed loans - September 30, 2006	46	12			294	130	69	23	68	28	29	21	9	20	749
Disbursed loans - December 31, 2006	49	29	0	6	1148	290	349	21	94	25	43	26	22	38	2140
Disbursed loans (volume USD) - September 30, 2006	633,716	392,832			628,464	429,540	101,920	168,208	307,228	128,027	161,782	125,636	43,906	127,261	3,248,521
Disbursed loans (volume USD) - December 31, 2006	504,151	249,986	0	20,908	2,163,980	840,934	377,464	72,188	642,133	169,546	305,934	174,198	191,896	193,906	5,907,226
Development of outstanding portfolio															
Outstanding loans - September 30, 2006	589	354			2967	1558	1150	212	595	279	261	173	162	239	8539
Outstanding loans - December 31, 2006	577	333	3	6	3705	1977	1209	201	672	289	293	196	167	269	9897
Growth (%)	-2.04%	-5.93%			24.87%	26.89%	5.13%	-5.47%	12.94%	3.58%	12.26%	13.29%	3.08%	12.55%	15.9%
Outstanding loans (volume USD) - September 30, 2006	8,026,024	3,444,939			5,675,206	3,625,154	1,019,909	1,610,016	2,530,981	1,276,969	1,296,722	1,026,709	666,297	1,538,042	31,736,968
Outstanding loans (volume USD) - December 31, 2006	9,042,604	3,255,839	4,831	20,887	8,551,375	5,352,529	1,310,197	1,799,602	3,320,756	1,605,224	2,056,279	1,278,523	924,799	1,962,624	40,486,070
Growth (%)	12.66%	-5.48%			50.68%	47.64%	28.46%	11.78%	31.20%	25.71%	58.58%	24.53%	38.80%	27.61%	27.57%
Portfolio quality															
Arrears rate (volume) - September 30, 2006	2.5%	2.5%			0.2%	0.5%	1.3%	1.2%	3.1%	4.2%	0.5%	12.3%	0.5%	0.2%	1.2%
Arrears rate (volume) - December 31, 2006	1.9%	0.4%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.7%	7.0%	0.5%	7.0%	0.1%	0.4%	1.1%
Loan officers															
No. of LOs under training (up to 6 months)	3	2	1		2	2			1	1	4	1		2	19
No. of trained LOs (> 6 months)	6	4		1	4	3		2	5	2	1	1	2	4	35
Total no. of LOs	9	6	1	1	6	5		2	6	3	5	2	2	6	54
No. of LOs financed by partner bank	9	6	1	1	6	5		2	6	3	5	2	2	6	54

5.2 Cascade

Co-operation with Cascade Bank is difficult, and compared with the previous reporting period, the situation did not improve significantly. The very frustrating situation at Cascade Bank can best be summed up by describing the two most obvious problems at this partner bank: a) lack of loan applications, and b) lack of top management support.

a) Lack of loan applications

So far, Cascade has not been able to attract a sufficient number of appropriate loan applications. Up until October, the small number of applications which the bank had managed to attract were either generated by direct marketing activities initiated by the AMP’s consultants or through personal contacts initiated by the head of Cascade’s credit department. For many of the latter applications, it became clear during the credit analysis process that the head of credit had already agreed with the clients on loan terms well before the applications had been submitted to the credit committee, and thus many of these applications had to be rejected by the AMP’s consultants. Over the last three months the AMP’s consultants also worked very hard to convince Cascade’s management that the lack of good applications was a problem which could only be solved by the initiation of massive multi-channel marketing efforts by the bank. Cascade finally did produce a marketing plan and a budget for its MSME lending activities, but only in December, even though this issue had already been raised by the AMP’s consultants in April. From the very beginning, the bank’s attitude towards marketing was very passive. As mentioned in the previous report, direct marketing did not seem appropriate to the bank’s management, as they felt that clients should come to the bank and not the other way around. In the meantime, after endless meetings, this attitude appears to have changed slightly. In addition, in mid-October the bank finally managed to place advertisements for MSME loans in local newspapers – but only after the programme’s consultants produced a text and offered to take it to the newspapers themselves and personally arrange for publication of the advertisements if the bank was unable or unwilling to do so. In November the programme was also able to persuade the bank to begin advertising on the radio, and in December Cascade installed its first-ever street banner to advertise its loan products. Using the set of marketing instruments which has now been created, Cascade finally managed to make itself somewhat better known among the members of the AMP’s target group, and toward the end of December the number of loan applications started to increase. At this point, however, it is unclear how successful Cascade Bank will be in the future in terms of attracting loan applications from the target group, given that it is still not a very well-known institution. Thus, a sustained marketing campaign will be required in order to increase the bank’s name recognition and its overall visibility in the market.

b) Lack of top management support

Now that the programme has been working with Cascade Bank for 10 months, it must be noted that, in the final analysis, the bank’s management has been insufficiently willing to co-operate with the AMP. Since the programme is not really supported by Cascade’s top management, this attitude regularly “trickles down” to the bank’s middle management – and to lower-level staff as well. Suggestions made by the programme’s consultants at the level of middle management or to the loan officers are either ignored or executed in such a way that it is clear right from the beginning that the resulting measures will not have a long-lasting impact. Middle managers and loan officers can afford to act in this way because they implicitly know that, as far as they personally are concerned, their actions will not have any adverse consequences. Although the AMP’s consultants make presentations to the top management in which they systematically explain what has to be changed in order to make MSME lending a fully operational part of the bank’s activities, and although, at the meetings at which the AMP’s suggestions are discussed, the members of the bank’s top management indicate that they understand why the proposed measures are necessary and say that they will co-operate with the programme to ensure that they are implemented, in the end only very little of what the consultants have proposed is in fact carried out. In addition – and this is an even more serious problem – it appears that almost nothing is communicated from top to bottom within the organisation. The clearly inadequate level and quality of communication is also reflected in the correspondence between the programme's management and the bank: as a rule, the bank does not even respond to written proposals and recommendations submitted by the AMP.

Given that none of the targets defined for this institution have been met so far, and that there has also not been any significant change in the management's attitude since the programme activities were initiated, it is very unlikely that in the near-term future Cascade Bank's performance will improve sufficiently to make it a truly successful partner bank.

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

	Yerevan
Output over last 3 months	
Disbursed loans - September 30, 2006	6
Disbursed loans - December 31, 2006	8
Disbursed loans (volume USD) - September 30, 2006	15,203
Disbursed loans (volume USD) - December 31, 2006	27,785
Development of outstanding portfolio	
Outstanding loans – September 30, 2006	8
Outstanding loans – December 31, 2006	27
Growth (%)	237.5%
Outstanding loans (volume USD) - September 30, 2006	18,349
Outstanding loans (volume USD) - December 31, 2006	120,793
Growth (%)	558.3%
Portfolio quality	
Arrears rate (volume) - September 30, 2006	0.0%
Arrears rate (volume) - December 31, 2006	0.0%
Loan officers	
No. of LOs under training (up to 6 months)	3
No. of trained Los (> 6 months)	
Total no. of Los	3
No. of LOs financed by partner bank	3

5.3 Ineco

As mentioned above, since November Ineco has known that it will be getting additional MSME lending resources from the EBRD. From this point on, Ineco's attitude towards the programme changed significantly and the bank's management started working with the AMP's consultants to produce a business plan detailing how the additional resources could be disbursed and what would be expected of every single branch. During this planning process it also became clear to the bank's management that in many areas of MSME lending the AMP's consultants would have to start from scratch when they resumed their activities at Ineco – a view which had already been expressed by the AMP in the previous report. This is mainly due to the fact that most of the remaining loan officers who were trained by IPC during the 10-month co-operation with the German-Armenian Fund have in the meantime been shifted to other areas of the bank's lending operations, i.e. they are no longer dealing with MSME loans, and as a result they no longer have the technical and communication skills which are needed in order to successfully serve MSME clients. In addition, Ineco has lost, and continues to lose, very valuable staff due to the fact that the salaries it is willing to pay are significantly lower than those offered by its competitors in the market.

The main focus of the AMP's work at Ineco during the reporting period was on the recruitment and training of additional lending staff and on reactivating the current lending staff's MSME lending skills, and this will continue to be the primary emphasis over the next few months. In December an assessment centre with more than 200 candidates was organised, and as from the beginning of January 2007, at least 9 new trainee loan officers will start their training in the bank's branches. In addition, the AMP's consultants determined that there was a need for additional training on the part of branch managers, and over the last month and a half they devoted a significant amount of time to assessing the performance of branch managers at credit committee meetings, and also provided advice and guidance to them during the meetings to help them to address the deficiencies that had been identified.

The outflow of personnel has created many vacancies at the level of the bank's middle management. Thus, for example, at present the position of head of the bank's business loan department is vacant, which means that there is no one at the bank who is directly responsible for managing its operations on a day-to-day basis. As it is the approach of the AMP to fully integrate its operations into the partner bank's own organisational structure, this also means that at present Ineco does not have a middle manager who is directly responsible for MSME lending. With assistance from the AMP's consultants, the bank has in the meantime identified two internal candidates who would be qualified for the job, and the programme is confident that by the end of January this position will have been filled. In the coming months, the AMP will focus on providing intensive training and coaching to this individual so as to enable Ineco to quite rapidly acquire the ability to develop its MSME lending operations on a centralised basis from the head office, and to continue to do so even after the AMP's assistance has been scaled back. Unfortunately, the introduction of CRM was put on hold when Ineco lost the person it was planning to appoint as its first CR manager to a competitor. During the recruitment event in December which was mentioned above, all candidates were also assessed in terms of their potential to become CR managers. However, it remains to be seen how quickly, and how systematically, the CR approach can be implemented at Ineco Bank.

So far, co-ordination with Ineco has been very constructive and straightforward. The bank has signalled that it would be willing to think about fundamental changes to its express loan technology once local branch managers and senior loan officers have gained some more experience with the technology. While the AMP would like for all of the partner banks to eventually begin offering uncollateralised express loans, it has set itself the goal of ensuring that at least Ineco is both willing and able to issue such loans to its clients. In terms of introducing new loan products, during the reporting period Ineco disbursed its first credit lines to small loan clients within the framework of the programme.

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

	Yerevan	Lori	Armavir	Shirak	Total
Output over last 3 months					
Disbursed loans - September 30, 2006	10	0	5	3	18
Disbursed loans - December 31, 2006	31	10	19	11	71
Disbursed loans (volume USD) - September 30, 2006	40,688	0	14,941	3,801	59,430
Disbursed loans (volume USD) - December 31, 2006	312,873	82,193	158,714	105,132	658,912
Development of outstanding portfolio					
Outstanding loans - September 30, 2006	208	26	105	32	371
Outstanding loans - December 31, 2006	199	39	105	50	393
Growth (%)	-4.32%	50%	0%	56.25%	5.93%
Outstanding loans (volume USD) - September 30, 2006	1,605,618	248,324	214,193	61,029	2,129,165
Outstanding loans (volume USD) - December 31, 2006	1,636,751	354,338	322,970	187,281	2,501,340
Growth (%)	1.94%	42.70%	50.78%	206%	17.47%
Portfolio quality					
Arrears rate (volume) - September 30, 2006	0.8%	0.0%	7.8%	0.5%	1.4%
Arrears rate (volume) - December 31, 2006	0.4%	0.0%	0.0%	0.6%	0.1%
Loan officers					
No. of LOs under training (up to 6 months)	1				
No. of trained LOs (> 6 months)	4	2	2	3	
Total no. of Los	5	2	2	3	12
No. of LOs financed by partner bank	5	2	2	3	12

5.4 Anelik Bank

The programme provided general portfolio monitoring services to Anelik Bank and invited its loan officers to attend seminars. In addition, the AMP's consultants are engaged in an ongoing dialogue with the bank concerning the application of the lending technology, the bank's somewhat conservative approach to express lending and the organisation of MSME lending operations.

In the meantime it appears that the bank is also internally discussing the possibility of restructuring its lending operations, and the programme is confident that if Anelik is able to establish a well-designed, highly efficient structure at the head office for the management of its credit operations, MSME lending has the potential to play a significant role in the bank's business in the future as well; indeed, it might even gain in importance. Unfortunately, as it always does toward the end of the year, Anelik faced liquidity problems, and was thus unable to fully supply the demand for its loans during the reporting period. If it had additional onlending resources, Anelik could easily increase the size of its MSME portfolio in all of its branches.

Table 6: **Overview of the performance of AMP lending operations at Anelik**

	Yerevan	Armavir	Shirak	Kotayk	Gegarkunik	Total
Output over last 3 months						
Disbursed loans - September 30, 2006	139	12	34	11	34	230
Disbursed loans – December 31, 2006	188	27	43	26	56	340
Disbursed loans (volume USD) - September 30, 2006	1,426,680	247,364	135,727	37,851	126,920	1,974,542
Disbursed loans (volume USD) - December 31, 2006	1,019,558	100,275	120,715	149,794	159,560	1,549,901
Development of outstanding portfolio						
Outstanding loans - September 30, 2006	911	12	259	104	236	1522
Outstanding loans – December 31, 2006	1137	69	333	136	321	1996
Growth (%)	24.80%	475%	28.57%	30.76%	36.02%	31.14%
Outstanding loans (volume USD) - September 30, 2006	9,329,663	247,364	1,019,363	509,809	444,306	11,550,505
Outstanding loans (volume USD) – December 31, 2006	9,764,965	477,690	1,151,796	773,460	710,683	12,878,593
Growth (%)	4.66%	93.11%	12.99%	51.71%	59.95%	11.50%
Portfolio quality						
Arrears rate (volume) - September 30, 2006	0.6%	0.0%	0.1%	0.0%	2.1%	0.5%
Arrears rate (volume) – December 31, 2006	1.9%	0.0%	0.0%	0.0%	1.4%	0.5%
Loan officers						
No. of LOs under training (up to 6 months)		1		2		3
No. of trained LOs (> 6 months)	21	3	5	4	3	36
Total no. of Los	21	4	5	6	3	39
No. of LOs financed by partner bank	21	4	5	6	3	39