

ASSESSMENT OF MSE FINANCIAL NEEDS IN YEMEN

FINAL REPORT
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ABBREVIATIONS AND EXCHANGE RATE

AMF	Aden Microfinance Foundation
ATM	automated teller machine
CAC	Cooperative and Agricultural Cooperative Bank
CBY	Central Bank of Yemen
GNI	gross national income
GDP	gross domestic product
GTZ	Gesellschaft für technische Zusammenarbeit (German Technical Development Co-operation)
HCB	Housing Credit Bank
HQ	headquarters
IBY	International Bank of Yemen
ICD	Islamic Corporation for the Development of the Private Sector
IFC	International Finance Corporation
MF	microfinance
MFI	microfinance institution
MIS	management information system
MoF	Ministry of Finance
MoIT	Ministry of Industry and Trade
MoPIC	Ministry of Planning and International Cooperation
MSE	micro and small enterprises
MSME	micro, small and medium enterprise
N/A	not available
na	not applicable
NBMFI	non-bank microfinance institution (i.e., an MFI that has the right to accept deposits)
NMF	National Microfinance Foundation
NGO	non-governmental organization
NPL	non-performing loans
PAR	portfolio at risk
PPSC	Post and Postal Savings Corporation
SEDF	Small Enterprise Development Fund
SEDU	Small Enterprise Development Unit
SFD	Social Fund for Development
SFSD	Social Fund for Sustainable Development
SMEPS	Small and Micro Enterprise Promotion Service
SMS	short messaging service
SPSS	Statistical Package for the Social Sciences
SWF	Social Welfare Fund
TA	technical assistance
TIIB	Tadhamon International Islamic Bank
UNCDF	United Nations Capital Development Fund

UNDP	United Nations Development Programme
USD	U.S. dollar
USDA	U.S. Department of Agriculture
WU	Western Union
YBRD	Yemen Bank for Reconstruction and Development
YCB	Yemen Commercial Bank
YGB	Yemen Gulf Bank
YKB	Yemen Kuwait Bank for Trade and Investment
YR	Yemeni Rial

Exchange Rate

US\$ 1 = 199 YR (fixed rate)

EXECUTIVE SUMMARY

This report was commissioned by the International Finance Corporation (IFC) to assess the financial needs of micro and small enterprises (MSEs) in Yemen and evaluate existing service providers in this market segment. The report analyzes the gap between supply and demand for MSE financial services and makes recommendations on how to improve access to finance in the country.

Background

This study is based on a market survey of 405 MSEs in Yemen conducted in summer 2007. The survey was held in six governorates with large populations (Taiz, Ibb, Hodeidah, Sana'a, Hajjah, and Dhamar) and consisted of one-on-one interviews with owners and/or managers of registered and unregistered MSEs. These interviews were supplemented by five focus group meetings held in the cities of Dhamar, Taiz, Hodeidah, and Ibb.

Yemen is the least developed country of the Middle East, with a GDP per capita of US\$ 650. A largely rural country, 75 percent of its population of roughly 21.6 million¹ resides in small, scattered villages. Nearly 40 percent of the population lives below the poverty line.

A large proportion of economic activity in Yemen appears to be unregistered, making it difficult to estimate the number of MSEs. Many businesses operate on a micro scale, employ only family members, and are based in rural villages. Due to high registration costs, cumbersome procedures, and tax requirements, an unknown number of MSEs do not register and consequently have no legal status.

This report estimates that there are 400,000 MSEs in Yemen.² This estimate is consciously conservative. It does not, for example, consider the financial demands of the country's 1.4 million farmers and 10,000 medium-sized enterprises. Nor does it differ greatly from an estimate made in 1998, when the population of the country was only 16 million.³ In the absence of more reliable data on unregistered micro- and small enterprises, however, the estimate provides a reasonable foundation for market projections.

Of the MSEs surveyed, the overwhelming majority (90.7 percent) were microenterprises (only 9.3 percent were small enterprises) and owned by men (98.5 percent).

¹ The Economist Intelligence Unit Limited, *Country Report: Yemen*, October 2007, 5.

² This figure is derived from Rochus Mommartz, "Microfinance Options Analysis—Yemen," for Kreditanstalt für Wiederaufbau (KfW), October 2006. Mr. Ali Abdulatif of the Yemen Ministry of Industry and Trade concurs with estimate of 400,000 MSEs. In fact, the Ministry of Industry and Trade counted 400,000 registered MSEs in 2004. The Ministry of Finance of Yemen also believes the estimate to be realistic.

³ See Koos van Elk and Paul Wijmenga, "MSE Baseline Survey: Yemen," Netherlands Economic Institute (NEI) in association with EIM Business and Policy Research and the Central Statistical Organization (CSO) of Yemen; Rotterdam, The Netherlands and Sana'a, Yemen, 2000. Report commissioned by the World Bank for the Yemen Social Fund for Development. English- and Arabic-language versions in possession of Jürgen Kathmann.

Financial Sector

The formal financial sector in Yemen is highly underdeveloped. It consists of 15 active banks,⁴ of which four are fully foreign-owned,⁵ three are public, and eight are private financial institutions (four of the latter are Islamic banks). Commercial banks have a strong tendency to invest in treasury bills and their ratio of credits to deposits is just 39 percent. Virtually all banks interviewed for this report regard SME lending as a strategic future goal, but have not yet elaborated plans to address this market.

The great majority of the population does not have access to formal financial services. Only 800,000 people (3.5 percent of the population) have an account with a formal financial institution. The outreach of the formal financial sector is concentrated in the main cities and sub-cities. Commercial banks have roughly 200 branches nationwide and the Post and Postal Savings Corporation, 240.

Formal bank loans are associated with high interest rates and sizable collateral requirements. Annual interest rates can run as high as 60 percent and banks can request collateral (preferably in the form of houses or land) in amounts 400 percent greater than a given loan.

There are 13 active microfinance institutions in Yemen,⁶ most of which were created by the government's Social Fund for Development (SFD). Together, these MFIs have an outreach of roughly 31,000 clients, a combined loan portfolio of US\$ 6.9 million, and an average loan size of US\$ 97. Only one MFI has national outreach, the rest are restricted to one or two governorates of the country. Most of these institutions practice group lending and do not require tangible collateral; none has yet achieved financial sustainability.

MSE Use of Banking Services

Most small entrepreneurs lack any information about financial products and services. Yemeni commercial banks do not actively market services to MSEs and have a reputation of serving only the big companies and big families of the country. A significant number of micro and small business owners are unaware even of the existence of formal loans. An even greater number are unaware that they might qualify for a loan, whether with a bank, a microfinance institution (MFI), or the government's Small Enterprise Development Fund (SEDF).

A sizeable majority of MSEs surveyed (71.1 percent) do not use formal financial services. National transfers are the most commonly used service among survey respondents (14.8 percent), with only 12.8 percent having a current account with a bank.

Only 10.6 percent of the MSEs interviewed have ever applied for a loan and only 5.9 percent have ever obtained one. In contrast, 57.7 percent have received informal

⁴ In total there are 18 banks. However, Watani Bank (private) is in liquidation and the Housing Credit Bank (public) is due to merge with CAC Bank according to a decree issued in 2004 (implementation has yet to start). Al-Rafadein Bank, a public bank from Iraq, only facilitates remittances.

⁵ The national banking law stipulates that foreign banks can only set up branches in Yemen.

⁶ This total consists of 11 MFIs, the microfinance department of Tadhamon International Islamic Bank, and the Small Enterprise Development Fund (SEDF).

loans, typically provided by family members and friends. Survey respondents identified the biggest obstacles to obtaining formal loans as lack of a guarantee (59.5 percent), high interest rates (46.4 percent), and religious reasons (45.8 percent).

Future Loan Demand

Despite the low frequency of loan usage to date, 52.6 percent of the enterprises surveyed would like to obtain a loan in the future. The majority of the survey sample (60.1 percent of microenterprises and 40.0 percent of small enterprises) expressed interest in loans of up to US\$ 2,500.

The savings habits of MSEs indicate a capacity to repay microloans. Survey results show that the majority of both microenterprises (71.4 percent) and small enterprises (90.3 percent) saved more than US\$ 500 over the past year. Among the latter, 70.9 percent had saved more than US\$ 2,500.

The potential market size for MSE services in Yemen is conservatively estimated at 210,400 enterprises, excluding farmers. Based on the demand survey, only 5.9 percent of these potential customers are presently served by existing financial institutions.

The market for MSE loans with terms greater than one year appears to be even bigger. Such loans are especially needed for investment purposes and are rarely offered by either banks or MFIs in the country.

Key Findings

There is a promising microfinance market in Yemen. Repayment rates at existing MFIs are high, the potential demand for microcredit is sizeable, and the current supply of financial services for the poor is very limited. Given the low level of literacy in the country (50 percent), new MFIs entering the market might consider providing financial services together with training in accounting and entrepreneurial skills—either directly or in partnership with specialized providers.

A planned law on NBFIs gives the Government of Yemen an invaluable opportunity to create a legal and regulatory framework that encourages the development of strong, permanent providers of microfinance. If MFIs are to achieve sustainability over the long term and reach growing numbers of the poor, it is crucial that the new law allow them to accept deposits. Deposits will enable these institutions to increase the amount of credit that they can offer, as well as drive down the cost of on-lending.

The government's US\$ 1 billion government initiative to support MSEs offers another important opportunity to develop the microfinance sector. Certain MSE-related projects may, in fact, be delegated to existing financial institutions, driving demand for better training in the operation and management of NBFIs.

The success of new MFIs will depend on good client education. Given that a large part of the population of Yemen is unaware of the existence of formal credit, new MFIs will need to educate clients about the difference between grants and credits and make clear that microloan borrowers must repay both capital and interest.

Microfinance products in Yemen need to be easy to understand, appropriate to client needs, and capable of being processed rapidly. Clients without economic training must, for example, be able to easily calculate the price of (and interest on) microfinance services. Products must also respond to perceived client needs, which current MFI clients have identified as individual loans, higher loan amounts, longer maturities, products for start-up enterprises and Islamic products (mainly *morabaha*). Microleasing is another product with future potential, although the microfinance sector does not presently have the capacity to support it.

Several distinct microloan sizes could be attractive on the Yemen market, including consumer loans of up to US\$ 100, offered on the basis of pawned goods; micro and small business loans of up to US\$ 2,500; and larger loans of up to US\$ 7,000 for clients with a good credit history and appropriate bookkeeping practices.

Good training systems and coherent career tracks will be essential to the success of new MFIs in Yemen. Any new MFI that does not want to draw on the limited pool of qualified staff working in existing MFIs must invest heavily in the training and education of both staff and management. This imperative creates an opportunity for an MFI with sufficient training resources to set the standards of the financial industry in Yemen.

INTRODUCTION

The objectives of this report are to assess the financial needs of micro and small enterprises (MSEs) in Yemen, evaluate existing providers of financial services to MSEs, analyze the gap between the supply of and demand for financial services, and make recommendations on how to improve access to finance in the country.

Country Background

Economic background. Yemen is the least developed country of the Middle East, with GDP per capita of US\$ 650 and GNI per capita of about US\$ 500. The country's population of approximately 21.6 million⁷ is one of the most ethnically homogenous in the region.⁸ Life expectancy is fairly low (59 years for men and 62 years for women) and the literacy rate very high (50 percent according to a 2003 estimate).

A rural country where most of the population lives in small scattered villages, Yemen has a population density of 37 people per square kilometer—only half the density of the average low-income country. Approximately 25 percent of the population lives in urban agglomerations. Overall, social and economic circumstances in Yemen create a very homogeneous traditional society where many decisions are influenced by the religious considerations.

Strong population growth has negated any real improvement in overall economic conditions in recent years, despite an annual real GDP growth rate of 2.5 to 3 percent.⁹ Although the official inflation rate was 14.8 percent in 2006, the Economist Intelligence Unit estimated the rate at 20.8 percent.¹⁰

Services, construction, industry, and commerce account for less than one-quarter of the labor force. Crude oil production and petroleum refining are important sources of state revenue. The country's principal industries are small-scale production of cotton textiles and leather goods; food processing; handicrafts; small aluminum products; cement production; and commercial ship repair. Among registered businesses in the country, 66.2 percent operate in the trade sector and 20.7 percent, in the service sector. Only 14.3 percent of enterprises work in production, nearly 30 percent of which are involved in agricultural production.¹¹

With nearly 40 percent of the population living below the poverty line, Yemen faces severe development challenges. Rapidly decreasing oil resources (which currently provide 70 percent of government revenues) are intensifying the need to promote other economic activities, and a severe scarcity of water resources poses a grave medium-term threat. The growing population has severely stressed many governmental services, including education and health, making the family the only reliable social infrastructure in the country.

⁷ The Economist Intelligence Unit, *Yemen Country Report*, October 2007, 5.

⁸ Approximately 99.7 percent of the population is Muslim and Arabic is the official and most widely spoken language.

⁹ The World Bank Group Sana'a Office; Yemen Economic Update; Fall 2007.

¹⁰ The Economist Intelligence Unit Limited; Country Report August 2007; page 5

¹¹ Among the 405 enterprises, 5 operate in more than one sector, thus the percentages above exceed 100.

The economy suffers from great unemployment, with only 5.8 out of 21.6 million people formally employed. (The national unemployment rate in 2003 was estimated at roughly 35 percent.) Most people accordingly work in agriculture and herding.¹² The country's principal agricultural products are grain, fruits, vegetables, pulses, qat, coffee, cotton, dairy products, livestock (sheep, goats, cattle, and camels), and poultry.

The interviews conducted for this study indicate that a large part of economic activity in the country is unregistered. Many businesses operate on a micro scale and employ only family members. The majority of microenterprises operate in rural areas. Poor road conditions and lack of adequate infrastructure make it expensive to serve potential clients.

The low level of professional training and the absence of larger enterprises forces most young people to look for employment opportunities within their own family. Successful entrepreneurs are expected to provide jobs to and share their wealth with less successful relatives. This tradition hampers the accumulation of capital and results in a low investment rate. Given that the economic basis for large parts of the population is weak, people are generally risk averse. Any change has the potential to endanger the only source of income for an entire family.

Political background. Formerly separate countries, North and South Yemen reunified in 1990. Recent political tradition in both areas—communism in the South and tribal society (Sheikhdoms) in the North—has encouraged a traditional reliance on higher authority for decision making and personal support, even in business decisions. The population tends to view the state (be it the government or the sheikh of a given area) as being in charge of all aspects of life.

The country appears to be politically stable at present. A long-standing system of balances exists between the central government (including the president), the main opposition parties, and the ruling sheikhs outside the main cities. This system is without doubt rather fragile, but manages to balance the interests of the different players most of the time. The political balance is enhanced by financial transfers made by the central government. Should such transfers be cut due to declining government revenues, however, the political balance could potentially change quickly.

Structure of the Report

The study begins with an overview of current financial services offered by the formal financial sector in Yemen (chapter 1), followed by an examination of the country's informal financial sector (chapter 2). Chapter 3 describes the findings of the MSE market survey and then estimates the size of the potential microfinance market in the country. The study concludes with a very brief overview of key findings and offers suggestions for new MFIs entering the market (chapter 4).

¹² This is true despite the fact that only 3 percent of the land is arable and agricultural productivity is low due to small properties, poor-quality soil, and an absence of technical resources.

1. THE FORMAL FINANCIAL SECTOR

The formal financial sector in Yemen is highly underdeveloped. The majority of the population does not have access to financial services and only about 800,000 people, or 3.5 percent of the population, have an account with a formal financial institution. A large number of these accounts are with the Post and Postal Savings Corporation (PPSC).

?

The banking sector consists of 15 active banks, of which 14 have a current credit portfolio:¹³ four are fully foreign owned,¹⁴ three are public, and eight are private institutions. Among the private institutions, four are Islamic banks that were created under the national investment law. The outreach of these banks is concentrated in the main cities and sub-cities of the country, with public banks serving smaller towns in rural areas to a certain extent. Commercial banks have approximately 200 branches, and the PPSC, 240.

Box 1. Snapshot of the formal banking sector in Yemen

Fourteen banks currently conduct active in lending in Yemen. All banks interviewed for the study had a significant liquidity surplus. A snapshot of the banking sector reveals:

- total deposits of US\$ 2.6 billion
- an outstanding net loan portfolio of all public and private banks of US\$ 998 million
- total bank investment in treasury bills and government bonds of US\$ 761 million

Source: Project research, 2007.

Overview

Table 1 below lists all commercial banks in Yemen (public and private) according to their overall assets.

¹³ There are 18 banks in all. However, Watani Bank (private) is in liquidation and accordingly to a decree issued in 2004, the Housing Credit Bank (a public bank) is due to merge with CAC Bank. However, implementation of this merger has yet begun. One foreign bank, Al-Rafadein Bank, a public bank from Iraq, is only facilitating remittances, and Qatar Bank does not presently offer loan products (i.e., it was not actively lending as of October 2007.)

¹⁴ These are the Arab Bank (Jordan), Calyon Cr dit Agricole CIB (France), United Bank (Pakistan) and Qatar National Bank. According to managers of the non-foreign banks, the Arab Bank is the biggest bank in Yemen in terms of assets and Calyon is somewhere between second and fourth. United Bank is the smallest of the four. None of these banks has plans to venture into the MSE segment. Unfortunately, the research team was unable to obtain their most recent annual reports during its stay in Yemen.

Table 1. Operational comparison of commercial banks in Yemen (in US\$ millions)

<i>Name</i>	<i>Total assets</i>	<i>Deposits</i>	<i>Loan Portfolio (gross)</i>	<i>Loan Portfolio (net)</i>	<i>% gross of deposits</i>	<i>% net of deposits</i>	<i>Treasury bills, CBY deposits^a + gov. bonds</i>	<i>% of deposits</i>
Tadhamon	930	600	473	450	79	75	na	na
IBY	500	460	141	100	31	22	242	53
YBRD	418	368	71	41	19	10	177	48
National Bank	409	358	44	35	12	10	190	53
Saba Bank	351	139	114	96	82	69	na	na
CAC Bank	278	242	90	77	37	32	82	34
YCB	249	217	117	64	54	29	72	33
Yemen Kuwait Bank	196	179	63	54	35	30	57	32
Shamil Bank	95	63	34	31	54	49	na	na
Islamic Bank	78	46	44	33	96	72	na	na
Gulf Bank	57	48	29	25	60	52	13	27
Totals (rounded)	3.4	2.6	1.2	998	46	39	761	29

Source: Annual reports of various banks, 2006, except for YBRD (June 2007) and Gulf Bank (2004).

Notes: ^aExcluding reserve balances at the Central Bank of Yemen (CBY).

Banking law. The main requirements of the banking law of Yemen (Central Bank Law No. 14 of 2000 and Banking Law No. 38 of 1998) are:

- new banks must meet a minimum capital requirement of US\$ 32 million
- existing banks must in theory increase their existing capital base to US\$ 32 million by 2009
- foreign ownership of a Yemeni bank is restricted to 49 percent of shares
- a single shareholder is limited to 10-percent ownership¹⁵
- banks must meet a liquidity requirement of at least 20 percent of current assets/current liabilities
- in-house loans are restricted to one year's salary for staff members and 0.5 percent of total capital for board members and owners
- open currency positions are restricted to 15 percent of total capital
- a bank's exposure to a single client may not exceed 15 percent of total capital

Investment law. Institutions set up under the investment law of Yemen do not have to comply with the abovementioned rules for equity and shareholder participation, but must adhere to with the remainder of regulations that govern banking institutions in general. A financial institution created under this law, therefore, can be 100 percent owned by a foreign entity and does not have to comply with any restrictions on the participation of single shareholders.

Leasing law. A long-awaited leasing law was approved by the government in the first half of 2007, opening the way for leasing to become an alternative to conventional loan products. The IFC plans to establish a leasing company with a technical partner as soon as the commitment of the government is secured and certain adjustments have been

¹⁵ This rule is aimed at preventing one person or family from dominating a bank. Nevertheless, there are strong indications that private banks are family dominated, as it is possible to circumvent the ownership restrictions.

made to the legal environment. Technical assistance, as well as a market assessment, will be provided to a number of stakeholders (e.g., banks, commercial companies, etc) in the initial project phase. Cooperation with the Ministry of Industry and Trade (MoIT) is also planned regarding the establishment of a registry for leased assets, together with a registry for land and real estate.

Client data. The Central Bank of Yemen provides certain client data to banks through a special unit. Although this unit is not comparable with a credit bureau, it handles a client blacklist and provides banks with a rough overview of the credit history of certain individuals (i.e., where and when they have accessed loans, loan amounts, and repayment records). Data is collected by the CBY during regular on-sight bank inspections.

Regulation. Central Bank of Yemen Circular No. 10 (1997) requires banks to adhere to minimum credit risk management standards. Provisions for loans, overdrafts and contingent liabilities—calculated on net exposure—are set out in Circulars No. 6 (1996) and No. 5 (1998). In addition, banks must make general risk provisions for total outstanding loan amounts (including overdrafts and contingent liabilities). They are also obliged to carry out periodic and comprehensive reviews of loans, advances, and contingent liabilities. Accordingly, bank provisions are set at the minimum rates shown in table 2.

Table 2. Loan loss provisions required by Central Bank of Yemen

<i>Category</i>	<i>Days overdue</i>	<i>Percentage</i>
Performing loans (including watch list loans)	1–30	1%
Substandard debts	31–90	15%
Doubtful debts	91–180	45%
Bad debts	Over 180	100%

Source: Banking Inspection Department, Central Bank of Yemen.

Loans are written off if legal procedures to collect the outstanding amount prove to be fruitless. In addition, the CBY may instruct a bank to write off loans after a review of its credit portfolio. According to the CBY, most commercial banks comply with its provisioning policy.¹⁶

Clientele and Products

The lending activities of all banks are concentrated on corporate clients, their principal shareholders, and related parties. Only recently have banks in Yemen begun to seek additional investment opportunities, causing most to venture into the retail market.

All commercial banks offer a range of classical banking products, including loans for trade, bridge financing, and working capital. The financing of assets is less common. Most loans are short term and usually do not exceed 12 months. Overdrafts, letters of credit and letters of guarantee are widely available. Reflecting the structure of the Yemeni economy, the majority of loans are for trade financing. Bridge loans for

¹⁶ For more detailed information on the various banks, see annex 2.

companies dealing with the government account for another significant share of the loan portfolios of most banks.

Consumer lending started recently, with all banks attempting to obtain a good share of the market. This type of lending is mainly payroll based, with only a few banks serving employees of private companies. The retail segment includes car loans and, increasingly, housing loans; these loans are guaranteed by mortgages and assessed according to the repayment capacity of a client's salary. Whereas retail banking has increased the number of bank accounts, retail loans represent only a limited share of overall bank portfolios.

Islamic Banks offer financial products based on Islamic principles, the most common of which are *morabaha*, *Musharaka* and *mudaraba* (see box 2 in chapter 2). Other commercial banks offer conventional interest-bearing loan products. The regulations of the Central Bank of Yemen prevent conventional banks from offering Islamic banking products.

Overall, the gross loan portfolio of commercial banks increased by 18 percent (and the net portfolio, by 20 percent) in 2006.¹⁷ Certain banks, especially the smaller (Islamic) banks, recorded a slight decrease in their loan portfolios, between 3 and 10 percent, that same year. At the same time, the deposits of all banks increased nearly 35 percent and assets grew 31 percent. Most banks were accordingly able to extend their asset base.

Commercial banks also offer customers current accounts, savings accounts, and time deposits. Several kinds of cards are available: ATM cards and cards for point-of-sale transactions, debit cards, credit cards, and cards for specific purposes (e.g., payments over the Internet). Telephone banking and SMS banking have been introduced, although these services are not widely used. The number of the ATMs in Yemen is increasing. So far the technical systems used for ATMs and point-of-sale cards are not harmonized, with each bank is running its own system.

Banks also make national and international money transfers available to account holders. Non-account holders are required to use the services of Western Union for national as well as international transactions. Negotiations are currently being held, however, to offer Western Union account-to-recipient services to recipients without an account. Negotiations are also underway to cut the fees on national money transfers in half, to US\$ 2 or 2.5 per transaction. National money transfers through the commercial banks are, however, limited by the geographic outreach of the banks.

Most banks require insurance on financed assets, goods, real estate, and cars. Only two banks offer residual debt insurance and one bank uses a foreign insurance company. Nevertheless, there are at least two insurance companies¹⁸ in Yemen able to insure most risks, either alone or in cooperation with international partners. Given that competition in the national insurance market in general is not very high and international partners might classify Yemen as a high-risk country, premiums can be high.

¹⁷ Comparative data is based on 2006 annual reports, with the exclusion of Gulf Bank (for which no annual reports were available for 2005 or 2006).

¹⁸ Due to time constraints, the research team was only able to interview two insurance companies.

Operations

Investment profile

Save for the Islamic Banks, most banks in Yemen have a strong tendency to invest in treasury bills and other governmental bonds, as this investment provides a safe income. On average, 45 percent of the net portfolio of all banks is held in these instruments, even by private banks (where the ratio is almost 42 percent).

The loan-to-deposit ratio for all banks, including the Islamic banks, is 39 percent. If the latter are removed from the analysis, the ratio is much lower—21 percent. Excluding public banks, the ratio rises slightly to 27 percent.

Given persistent rumors that the government will soon limit or cease the emission of treasury bills,¹⁹ commercial banks are preparing themselves to diversify their investment portfolios. One part of their diversification strategy is to expand their engagement in the already competitive retail market.

Interest in MSE Market

Although the MSE market segment is still nearly untapped, lending to MSEs is not expected to be the first priority of banks seeking to diversify. Although most banks in Yemen expressed interest in lending to MSEs, with the exception of Tadhamon Islamic Bank and to a very limited extent, Shamil Bank of Yemen and Bahrain, no bank has yet created special operations for this market segment.

Certain banks currently offer small loans through their corporate loan departments, but these institutions have not adjusted their procedures to meet the special circumstances and needs of MSE clients. No detailed figures were available, but loans extended to MSEs amount to only a couple of hundred credits in the entire banking sector (excluding Tadhamon Bank).

The clearest vision for providing services to MSEs has been expressed by the Yemen Kuwait Bank for Trade and Investment. This bank is in negotiation with the government's Social Fund for Development (SFD) to obtain technical assistance for downscaling. However, the bank appears to be motivated by social responsibility, not the need to diversify its portfolio and venture into alternative areas for profit.

Most of the remaining banks in Yemen have yet to develop a strategic vision or clear idea of how to enter the SME market. Nevertheless, they all concur on the importance of this sector and acknowledge that lending to it has proven successful in other countries. However, most view engagement in this sector as part of the social responsibility of big commercial entities, rather than as a business opportunity.

In light of the fact that the government is placing a high priority on developing the MSE sector as part of an action plan for fighting unemployment, some banks are expecting the government to support the development of SME commercial lending facilities as well.

¹⁹ Several sources provided this information to the researchers, but could not confirm whether the government has made an official decision.

2. THE INFORMAL FINANCIAL SECTOR

The informal sector in Yemen can be divided into three main segments:

- microfinance institutions (MFIs)
- the Small Enterprise Development Fund (SEDF) of the government,²⁰ which delivers loans to formal MSEs; and
- informal providers of credit (e.g., wholesalers²¹ that provide finance through sale on credit, together with family lending).

Pawnshops are rare in Yemen, although some inter-family financing works according to the principles of pawning.²² Due to historic reasons and religious feeling, the informal commercial lending sector in Yemen is less developed than in other countries with a similar financial system.

To date, the Yemeni government has not created any microfinance programs except through its Social Welfare Fund (SWF), which extends no-interest loans to beneficiaries for the purpose of on-lending to start-up, income-generating enterprises. According to the Yemen National Microfinance Policy Statement, the SWF should “abstain from direct provision of microfinance and will focus its efforts on capacity building of beneficiaries (training, financial education, etc.) and linking them with professional microfinance providers.”

There are a dozen MFIs operating in Yemen serving approximately 31,000 clients. The majority of these institutions are considered projects of another development agency of the government: the Social Fund for Development (SFD). The MFIs created with SFD funding are independent in operation, but have to report to the SFD on a regular basis to receive technical assistance (i.e., training, consulting, or in-kind transfers). For most of these MFIs, the SFD is their main or only source of funding.

At present there is no supervisory body responsible for MFIs in Yemen, hence most are registered as NGOs or foundations. Lack of an adequate legal and regulatory framework restricts the ability of these institutions to reach sustainability. At present, for example, MFIs are not allowed to collect savings for on-lending or investments. In the event that an MFI collects savings from borrowers or guarantors, these funds are considered part of the loan (early repayment) or part of the guarantee (deposit), but cannot be used as source of financing. However, the Yemeni government, Central Bank, and international donors are currently working on a regulatory framework that would permit deposit-taking non-bank financial institutions (NBFIs).²³

The Yemen government announced a US\$ 1 billion government initiative in August 2007 to support MSEs, the major aim of which is to facilitate employment creation in the

²⁰ For detailed information about SEDF, see annex 3.

²¹ For more details, see chapter 3.

²² If an MFI accepts gold or jewellery as a guarantee, this process could be also understood as a form of pawning.

²³ For further information on the regulatory framework, please refer to Rochus Mommartz, “Establishment of a Prudentially Regulated Non-bank Microfinance Institution (NBFi) in Yemen,” KfW, Eschorn, Germany, April 2007.

country. The scope of the new program could mean that MSE-related projects will in the future be delegated to existing financial institutions.

Social Fund for Development (SFD)

The Social Fund for Development was established in 1997 by the Yemeni government as an independent governmental institution to pool donor funding and improve the efficiency of the administration of this funding, as well as to facilitate the implementation of the government's own social and economic plans. The mission of the SFD is to “[support] long-term development opportunities for the poor, establishing and promoting innovative participative approaches in delivering basic services.”

While it has been mandated by the Government of Yemen to support the microfinance industry, microfinance is only one component of a larger portfolio of activities supported by the SFD. These activities include large social programs, notably in the agricultural and rural sectors. The SFD formally began working with MFIs in 2002, facilitating the implementation of the Microstart program in Yemen, and currently works with ten MFIs.

Neither the government's Social Fund for Sustainable Development (SFSD), nor the Small Enterprise Development Fund (SEDF) are formally linked to SFD. Even though the SEDF is currently the largest borrower from the SFD, is not considered an MFI or an SFD project.

The SFD's approach to microfinance has been to provide both loan capital for on-lending and technical assistance to its partner MFIs, including the SEDF. These loans must usually be repaid within a two- or three-year period, with the first installment due six or twelve months after loan signing. Although originally loans were often extended at no costs to MFIs, they currently bear a 10 percent interest rate.²⁴ The SFD believes that charging interest will help MFIs demonstrate their ability to access funds on a commercial basis.

Most MFIs now working in Yemen are trying to find additional or alternative sources of funding so as not to be dependent solely on the SFD, thus becoming more independent in their operations. The SFD is regularly criticized for charging interest because the MFIs assume that it receives its own funding without paying interest.

A key element of the SFD's strategy has been to work to consolidate the microfinance sector, assisting compatible MFIs to merge into larger, potentially more effective organizations. Recently, for example, the Beit Al-Fakih Program was successfully integrated into the much bigger Hodeidah Microcredit Program to make administration and supervision more efficient, take advantage of potential synergy effects, and move towards economies of scale. Although Beit Al-Fakih's portfolio is still under the responsibility and supervision of the former Beit Al-Fakih program, the program is now officially a branch of Hodeidah and new loans are considered part of the portfolio of Hodeidah. The SFD considered this consolidation successful and is now in ongoing discussions to integrate the Hais Credit and Savings Program (also in Hodeidah governorate) into the Hodeidah Microcredit Program.

²⁴ The interest rate increased from 5 to 10 percent in recent years.

Microfinance Institutions

The first microfinance programs in Yemen were established by the Microstart Program of the United Nations Development Programme (UNDP) in the mid 1990s. They were later transformed into NGOs or foundations under the guidance of the SFD. Other NGOs involved in microfinance have been funded by private initiatives or social foundations. Still others remain programs of NGOs that are active in several areas.

Today there are 11 MFIs operating Yemen, together with the Small Enterprise Development Fund (SEDF) of the government and the microfinance outlet of Tadhamon Islamic Bank (see annex 3 for details on individual institutions). Only one MFI has national outreach, the rest are restricted to one or two governorates. They serve the main cities and sub-cities that service rural areas in around half of the governorates of the country.

Most MFIs practice group lending, do not require tangible collateral, and provide some kind of social or economic training to clients. (The training is integrated into the group meetings conducted by loan officers.) Because many MFIs were established with the mission of empowering women through finance, women account for more than 87 percent of customers.

The aim of MFIs in Yemen is to finance income-generating activities, enabling their clients to improve the situation of their families. Certain MFIs also finance consumption (e.g., refrigerators, washing machines, TVs, etc.), as well as housing improvements, to enhance their clients' living conditions. Most MFIs do not explicitly finance start-up businesses, but "income-generating activities," such as handicraft and small-scale services production, including small grocery shops, beauty saloons, and telephone shops. In rural areas, microfinance loans often finance livestock. The economic activities of most microfinance clients are not formally registered. Accordingly, the only documentation that most MFIs require, especially for group lending products, is a valid national Identity Card.

Yemeni MFIs presently serve nearly 31,000 clients in most governorates of the country. Client and portfolio development were both rather stagnant in the first half of 2007, with the combined loan portfolio of all 12 institutions remaining constant at nearly US\$ 3 million and active borrowers falling by 2.5 percent. Since year-end 2005, however, these institutions have experienced an increase of nearly 20 percent in active borrowers and 13 percent in overall portfolio size. When measured from year-end 2004 to June 2007, these growth rates are 70 and 80 percent, respectively.

MFIs offer loans ranging from YR 5,000 to YR 250,000 (US\$ 25 to US\$ 1,250). The average loan of various institutions varies between US\$ 77 and US\$ 200; the average loan size for the sector as whole is US\$ 97. The only exception is the SFSD, the average loan size of which is US\$ 400. Two MFIs offer individual loans, one in amounts up to US\$ 2,000 and the other in amounts up to US\$ 5,000. The outstanding portfolio of all MFIs combined was US\$ 3 million as of July 2007.

Some MFIs have complained about restrictions on their internal regulations and credit risk policies that hinder them from disbursing the higher-value loan amounts needed by clients. To avoid these limits, some institutions violate internal restrictions and international best practice by extending more than one loan to one client or commercial activity at a time.

Loan products do not differ much among individual MFIs, all of which principally offer group lending to women and individual lending to men and repeat female clients in need of higher loan amounts. Most MFIs offer the Islamic banking product *morabaha*,²⁵ some also offer conventional loan products. Around half of these institutions offer (compulsory) savings accounts and some offer compulsory life insurance,²⁶ with several more intending to offer life insurance.

Box 2. Islamic banking products offered by MFIs

Morabaha is a very popular Islamic banking product in Yemen that finances the purchase of essential materials, such as computers, small equipment (e.g., sewing machines), raw materials, small office furniture, etc. The *morabaha* model is similar to trade financing (think working capital) and leasing (think fixed capital loans). The client in this transaction chooses the product and then signs a “promise-to-buy” contract with the NBF. The financial institution purchases the product and re-sells it to the client on a deferred basis, adding an agreed markup for administrative costs. The client pays the sale price for the goods either in installments or one lump sum at the end of the period. The NBF owns the product until the last installment is paid.

Mudaraba financing is a partnership structure consisting of one or more partners. An NBF invests money and the entrepreneur, management and labor. The entrepreneur shares in the profits of the enterprise and receives an additional reward for work delivered; the NBF only shares in the profits. Profit-sharing rates are predetermined, but the amount of profit is unknown. The *mudaraba* model has certain difficulties. First, the profit that will be generated by the partnership is uncertain, and second, the product requires a great deal of administration and monitoring on the part of the NBF. Finally, the model is relatively difficult to understand, both for the client and the loan officer. These difficulties can, however, be overcome if the NBF and client agree on a weekly or monthly profit prior to disbursement.

Musharaka is a partnership in which the entrepreneur and the financial institution both provide capital to finance a project, with the entrepreneur also providing management and labor. Both share in the profits based on a pre-agreed ratio; losses are shared on the basis of equity participation.

Ijara is the Islamic equivalent of a conventional lease and permits a client to use an asset owned by a financial institution for a specific period in return for rent. Because leasing rates cover only the right to use and not eventually own an asset, lease payments are lower than loan installments.

Source: Project research, 2007.

²⁵ The administrative process for this product is straightforward, although it does not fully follow the exact principles of *morabaha*. Often, for example, the MFI does not purchase the goods itself, but sends a check directly to the supplier in order to hand over the agreed goods. Certain MFIs work principally with designated suppliers in their area.

²⁶ These MFIs demand residual debt insurance in case of death. It is managed by the institution itself and not by an insurance company.

The interest or fee on conventional lending or *morabaha* is a flat rate between 18 and 36 percent per year. Usually there is no difference between interest on conventional loans and *morabaha*. Repayment rates are very high—95 percent on average—with some MFIs achieving 100 percent. Only one MFI reported a repayment rate of less than 90 percent.

For group lending, the group guarantee is sometimes combined with a payroll deduction. Individual loans are commonly guaranteed by a commercial guarantee,²⁷ payroll deduction,²⁸ or gold. Two MFIs also accept pension checks as guarantees.

The main internal weaknesses of MFIs in Yemen are a lack of appropriate monitoring procedures; insufficient information technology (IT) systems; lack of experienced, well-trained staff; and insufficient funding. Nevertheless, it should be remembered that the microfinance is still very young in Yemen and that most institutions are ready to learn from their mistakes.

A number of MFIs understand the importance of increasing their professionalism and adopting a commercial business approach to become sustainable. They are also aware that the capacity of their management and staff is an important constraint in reaching this goal. MFIs that were established recently are able to draw on this accumulated wisdom; they also have the advantage of being able to recruit experienced staff.

To date, none of the MFIs working in Yemen has reached financial sustainability. Three (Al Awael, Taiz, and the Abyan Credit and Savings Program) claim that they have reached operational sustainability, and the Abyan Credit and Savings Program claims to have achieved 99 percent financial sustainability.

Most MFIs now seek to extend their outreach, increase client numbers, and introduce new products. Not all appear to have a clear growth strategy, however; only a few had formulated clear next steps. Product development to date remains largely a matter of copying existing products of other institutions.

Lack of capacity

To date, there is no training institute for non-bank financial institutions (NBFIs) in Yemen. All of the MFIs presently working in the country have been training their staff on the job.²⁹ The SFD does offer regular trainings for MFI employees, including those of the SEDF, free of cost.³⁰ Whereas the Institute for Banking Studies offers curricula for employees of commercial banks, it has no specialized training for NBFI employees. This Institute's courses are free to employees of commercial banks (which finance the institute through membership fees), but offered on a fee basis to all other interested parties.

Finding qualified managers is an even more crucial problem for MFIs in Yemen than finding competent line staff. MFIs cannot compete in salary with bigger companies or banks in the country and also unable to attract Yemeni graduates who have studied abroad. Educated youth in the country could, however, be trained as loan officers and

²⁷ MFIs in Yemen accept the personal guarantee of a business owner.

²⁸ Payroll deduction is accepted from people with a regular salary, preferably government employees.

²⁹ Certain recently established institutions have been fortunate enough to attract staff with experience at other MFIs in Yemen, but this is a relatively new phenomenon.

³⁰ In the future, SFD plans to charge small fees for such training.

accountants. Graduates of universities or institutes for higher education in Yemen are currently entering the job market in greater numbers than the government and private companies can absorb. Many of these graduates are either underemployed or doing odd jobs. Even if employed, they are frequently not adequately paid. Accounting, business administration, and other business-related subjects (e.g., computer science), are popular subjects with Yemeni students, as is the English language.

Any new MFI that does not want to draw on the limited pool of qualified staff working in existing MFIs must invest heavily in training and education. This imperative creates an opportunity for an MFI with sufficient training resources to set the standards of the financial industry in Yemen.

Table 3. SWOT analysis of the Yemeni MSE finance market

Strengths:	Weaknesses:
<ul style="list-style-type: none"> › Safe environment › Relatively low set-up costs for MFIs › High demand for financial products (especially by the MSE segment) › Vast market with reliable clients (high commitment to repaying credits) 	<ul style="list-style-type: none"> › Weak legal environment and enforcement in general › Lack of a legal framework for NBFIs › Difficult to liquidate real estate submitted as collateral, making financial institutions reluctant to accept family residences as a guarantee › No central land registry or registry authority; land titles not secure › Lack of awareness of credit. Most people are unaware that a product called credit exists, nor do most understand the difference between a loan and a grant › Risk-averse entrepreneurs and population › Large percentage of the population has weak technical skills and low levels of education › MFIs and banks lack of capacity and capability for MSE lending
Opportunities:	Threats:
<ul style="list-style-type: none"> › Availability of educated youth that could be trained as loan officers and accountants › Innovative loan products, including Islamic banking products and leasing › Additional innovative financial services for MSEs › Investment opportunities for financial institutions › Technical support by donors › Young, under-served financial market › Low level of market competition, although banks will provide increasing competition as they seek alternative investment opportunities › SMEs are currently a priority of the government 	<ul style="list-style-type: none"> › Political stability could erode › Law for NBFIs under discussion, not yet formulated; content not yet known › Apart from the SFD, no clear commitment to microfinance on the part of a government institution › Strong interference by government in economic activities › Increasingly unstable economy with rising prices › Local investors do not understand the microfinance business › Banks under the supervision of the Central Bank must meet collateral requirements

Source: Research team analysis.

3. MSE MARKET DEMAND STUDY

This chapter discusses the market demand study of MSEs in Yemen in detail, including their size, age, ownership structure, and management, as well as their relationships with suppliers and clients. The financial situation of these enterprises is then analyzed by looking at their turnover, profit margins, and past and future investments. Finally, their current use and future demand for formal and informal financial services, including credit, is presented.

Box 3. Summary of the MSE Market Demand Survey

Among the individual entrepreneurs and MSEs interviewed for the demand study:

- 7–8% of all entrepreneurs are illiterate
- 46.4% of MSEs do not have any kind of bookkeeping system
- 71.1% of enterprises do not use banking services
- National transfers are the most commonly used financial service among enterprises; 14.8% of enterprises in the survey sample use this service
- Only 12.8 % of enterprises have a current account in a bank
- Yemen Bank for Reconstruction and Development and Tadhamon Islamic Bank are the most active banks in the MSE market (21.1% of enterprises that use bank services use these banks)
- Only 10.6% of enterprises that were interviewed have ever applied for a loan, and only 5.9 % have ever obtained one
- 57% of enterprises are unaware of any type of loan
- 76.3% of enterprises consider the loan process difficult, very difficult, or impossible
- Among enterprises that have ever obtained a loan, 45.9% still find the process difficult OR very difficult
- MSEs identify the main difficulties in obtaining a loan as lack of a guarantee (59.5.2%), high interest rates (46.4), and religious reasons (45.8%)
- MSEs that received a loan were unable to cite the effective interest rate on the loan
- 57.7% of enterprises have obtained informal loans
- 52.6% of enterprises would like to obtain a loan in the future; 36.9% of this group would prefer to borrow from Islamic institutions

Source: IFC survey data, 2007.

Methodology

The market survey was conducted in six governorates of Yemen with large populations (Taiz, Ibb, Hodeidah, Sana'a, Hajjah and Dhamar), with due consideration of urban and rural areas. The survey consisted of face-to face interviews with the owner or manager of 405 MSEs. As a large proportion of the MSEs in Yemen are not formally registered, both formal and informal MSEs were included. Prior to conducting the survey, five focus groups were held in Sana'a, Dhamar,³¹ Taiz, Hodeidah and Ibb.

³¹ This focus group consisted of members of the board of directors of the Dhamar Chamber of Commerce, all of whom work in the trade sector.

The survey used a semi-structured questionnaire to solicit data that would allow the research team to estimate MSE demand for financial services, including:

- socioeconomic characteristics of existing MSEs: structure of ownership, type of business, management and employee characteristics
- financial performance and perspectives: current MSE financial situation and performance; profit margin; major internal and external constraints perceived by MSEs; previous investments; future perspectives, plans and strategies
- current patterns and sources of finance: relationships with formal and informal financial providers, existing financial products, constraints to accessing financial services, currently used and necessary financial products, etc.
- future demand for credit: MSE financing needs and potential demand for financial services

Interviews were conducted by an international consultant with the help of a trained and closely supervised by the chief consultant on the research team in Yemen. Interviewers were recruited, trained, instructed, and monitored throughout the survey implementation by the consultant, who is an expert in micro, small, and medium enterprise. Data compilation and encoding were carried out using the Statistical Package for the Social Sciences (SPSS).

In addition to the survey and focus groups, personal interviews were conducted with the main stakeholders in Yemen's financial sector (i.e., commercial banks, MFIs, governmental institutions, international organizations).

MSE Socioeconomic Characteristics

Size, Age, and Gender Distribution

The vast majority of MSE respondents (90.7 percent) were microenterprises (only 9.3 percent were small enterprises)³² and owned by men (98.5 percent). Only 1.5 percent of the enterprises surveyed were owned by females, reflecting the fact that men dominate the economic sector.³³

Regional and Sectoral Distribution

The majority of enterprises interviewed were located in urban areas of Taiz, Ibb, Hodeidah, Sana'a, Hajjah and Dhamar, where the concentration of MSEs is the highest in the country.

³² This study follows the definitions of the Yemen Social Fund for Development, which classifies enterprises with up to 4 employees as microenterprises and those with between 5 and 50 employees, as small enterprises.

³³ The number of female respondents in the study is much too small for statistical evaluation. The study intended to involve more women respondents in the sample group, but this goal proved impossible. Due to social and religious reasons, interviews with female entrepreneurs could only have been conducted by female interviewers. Given that interviewers had to travel throughout the country to conduct the study and that women are not allowed to travel without their a close relative (i.e., husband or brother), there was no possibility to employ female interviewers and thus no opportunity to approach female entrepreneurs at home.

Enterprises were selected from all economic sectors in order to accurately represent the structure and regional patterns of the economy. The largest group of MSEs worked in the trade sector: 268 of the 405 enterprises (66 percent). Another 84 (20.7 percent) were in the service sector, 58 (14.3 percent) in production, and 7 in other sectors.

Among enterprises in the trade sector, most (82.8 percent) worked in retail. Enterprises in the services sector included business such as restaurants, tailoring, hairdressing, repairs, driving, and other services. The production sector represented enterprises in food production, carpentry, agricultural production, and metal workshops.

Legal Status

The majority of enterprises in the survey were registered (76.3 percent), but a significant share (23.7 percent) was not.³⁴ Of all enterprises surveyed, 68.3 percent were registered as an enterprise belonging to one man. The majority of unregistered companies were microenterprises.

MSE Age and Employment Structure

Of the sample size of 405 enterprises, most (90.5 percent) employed between one and four people. Specifically, 46.5 percent employed only the owner and 44 percent employed between two and four employees. Only 7.4 percent of enterprises employed between 5 and 10 employees and even fewer (1.7 percent) employed 11 to 25. Only 1 enterprise employed more than 25 employees. All woman respondents were owners of microenterprises that employed only the owner.

The majority of non-owner employees were family members. In fact, among the 216 enterprises that employed more than 1 employee, only 8 did not employ family members (see table 1 in annex 4). Focus group meetings confirmed that paid employees are uncommon among MSEs in Yemen. Due to the high unemployment rate, people do not have many alternatives to working with their families, hence the majority of enterprises are family businesses.

The majority of MSEs (308, or 76 percent) had not expanded their staff in the past year. Among the remaining MSEs, 38 had recruited one new employee; 36, two new people; and 19, more than three.

The greatest number of enterprises surveyed were between one and three years old (130 out of 390 responses, or 33 percent), followed by enterprises that were between four and 10 years old (121 out of 390, or 31 percent). Among small enterprises, 74.2 percent had been in operation more than three years, whereas as only 50.4 percent of microenterprises had been in operation that long. Finally, only a small percentage of businesses interviewed (7.7 percent) had been in operation more than 20 years.

Most very young enterprises that had been in operation less than one year were found in the service and trade sectors. The production sector consisted of more established enterprises, with 20.5 percent having been in operation for 11–20 years (compared to 11 percent for the trade sector and 14.1 percent for the service sector), and over 13 percent

³⁴ It can be assumed that the percentage of unregistered business in the country is much higher than 23.7 percent, as unregistered business are unlikely to participate in official interviews or reveal their “illegal” status in interviews. The *minimum* percentage of unregistered business is thus assumed to be 23.7 percent.

had been in operation for more than 20 years (compared to 8.7 percent for the service sector and 2.6 percent for the trade sector).

The oldest enterprises were located in Dhamar, the historical trade center of Yemen, where family businesses are more common.³⁵ In contrast, the capital of Yemen, Sana'a, had some of the youngest enterprises surveyed: 69.3 percent of enterprises surveyed there had been established within the last three years. These numbers may be explained by the rise in migration to Sana'a, which has led to an increasing number of new start-up businesses. In addition, recent infrastructure investments in the capital have expanded transportation and communication facilities, making it the preferred city for newly established businesses.

Investors and Management

In most cases, MSEs were launched using the owners' own funds (71.6 percent), with no significant differences between small and microenterprises. In an indication of the acute scarcity of investment capital, only 1 percent of all respondents had started their business activities with credit provided by an institution.

Of the six female respondents, four cited their own money as the source of start-up funding, one cited funds provided by family and friends, and one borrowed a loan from private moneylenders.

Regarding the educational level of entrepreneurs, the vast majority (91 percent) had completed primary education and only 33 (8 percent) were illiterate. The biggest group had completed both primary and secondary education (152 respondents, or 37.5 percent), with roughly equally numbers having completed only primary education (112, or 27.7 percent) and university (86, or 21.2 percent).³⁶

Of the six female respondents, five were illiterate and the remaining respondent had a primary school degree. Among male respondents, 93 percent were literate. Given that only 50 percent of the population is literate, this finding implies that less than half of the female population is literate.

Client and Supplier Relations

Suppliers

Most MSEs surveyed paid cash upon receipt for supplies (43.7 percent), followed by those who paid an advance against supplies, with the balance paid after delivery (37.9 percent), and those who paid in cash sometime after delivery (14.1 percent). Only two enterprises used checks as a payment instrument, as this financial product is not common in the market (not all banks issue or accept checks). There were no significant differences in how micro and small enterprises paid for supplies.

Altogether, half of the enterprises surveyed (205 out of 405) used some form of supplier credit to acquire supplies (i.e., an advance with balance upon receipt, or making a delayed

³⁵ This information was provided by the Chamber of Commerce in Dhamar.

³⁶ It appears that 4.6 percent of MSE owners either completed a level of education that was not specified in the questionnaire or avoided answering this question. Bearing in mind that many adults are embarrassed to admit that they are illiterate, as well as the country's high illiteracy rate (50 percent), it may be assumed that the percentage of illiterate entrepreneurs in Yemen is closer to 12.5 than 8 percent.

cash payment after delivery). The term of most delayed payments was limited to three months (mentioned by 192 out of 205 respondents), with terms of up to one year available in some cases. Among enterprises that accessed supplier credit of up to three months, 29.2 percent reported a payment period of 1–15 days; 37.5 percent, 16 days to one month; and 31.2 percent, 1–3 months.

A large majority of MSEs (81.9 percent) reported that there was no price difference on goods whether they were paid for in cash upon receipt or with a delay. A small group, 13.6 percent or 55 respondents, received a reduced price if they paid immediately and an even smaller share (4.4 percent) paid interest on late payments. Of those who reported a price reduction for immediate payment, most reductions were between 1 and 5 percent. Among enterprises that paid interest on late payments, most also cited an interest rate between 1 and 5 percent. Interest rate penalties are less common in general in Yemen than in non-Islamic countries, primarily due to Islamic rules.

**Table 4. Reductions/interest rate penalties on supplier payments
(N=62)**

	<i>Reduction for immediate cash payment</i>	<i>Interest rate penalty on late payment</i>
1–5 %	31	10
6–15%	14	6
16–25%	1	0
Total responses	46	16

Source: IFC survey data, 2007.

Consumers

An overwhelming majority (94.3 percent) of MSE clients are final consumers. Similar to suppliers, the greatest share of entrepreneurs surveyed (276 out of 403 responses, or 68.5 percent) asks clients to pay cash upon receipt for goods and services. Only 39 MSEs (9.8 percent) permitted clients to make cash payments sometime after delivery; 79 (19.6 percent) requested an advance with the balance upon receipt; and 14 (3.5 percent) required a complete cash advance. Lack of alternative payment products, such as credit cards or checks, means that most sales are cash oriented throughout the economy.

Clients pay MSEs in local currency; only two respondents accepted U.S. dollars and one accepted euros. As could be expected, entrepreneurs allow their customers less time to pay outstanding balances than they themselves are granted by suppliers. Out of 38 responses, 27 mentioned one to three months, 10 noted 16 days to one month, and one noted 1 to 15 days.

The vast majority of MSEs (389 out of 405 respondents, or 96 percent) do not offer discounts for early payment or charge interest on delayed payments. Only 10 offer a reduction for immediate cash payment and 1 charges interest on late payments. Due to Islamic rules, moreover, enterprises rarely apply interest to payments received after delivery. Again, most discounts are less than 5 percent.

Financial Performance and Perspectives

Bookkeeping

Almost half of the MSEs surveyed (46.4 percent) do not have a bookkeeping system, more small than micro enterprises maintaining such systems (84.2 versus 50.4 percent).

**Table 5. Do you have a bookkeeping/accounting system?
(N=405, in %)**

<i>Type of enterprise</i>	<i>Yes</i>	<i>No</i>
Micro	50.4%	49.6%
Small	84.2%	14.8%
All enterprises	53%	46%

Source: IFC survey data, 2007.

Turnover

The greatest number of MSEs (41.8 percent) had a yearly turnover of between US\$ 10,000 and US\$ 50,000. Turnover of the remaining enterprises fell more below than above that range. Only 3.8 percent of the enterprises surveyed had a yearly turnover in excess of US\$ 250,000. The highest turnover range was found among enterprises in the production sector, 66.7 percent of which had an annual turnover greater than US\$ 10,000.

Table 6. Yearly MSE turnover (N=393, in %)

<i>Yearly turnover (US\$)</i>	<i>% of all MSEs</i>
0–500	0.5%
501–2,500	9.4%
2,501–5,000	12.5%
5,001–10,000	17.0%
10,001–20,000	20.9%
20,001–50,000	20.9%
50,001–250,000	15.0%
>250,001	3.8%
<i>Total</i>	100.0%

Source: IFC survey data, 2007.

Turnover in Yemen changes significantly depending on the season. Winter was identified as the best season for turnover, with January receiving the best rating from all respondents (45.5 percent), followed by December (40.3 percent.) The worst months were identified as May and June.

With respect to days of the week, Saturday was considered the best working day by 46.4 percent of the survey sample, followed by Friday (43.0 percent) and Thursday (44.6

percent). Although Thursday and Friday are official holidays, the majority of MSEs operate during these days, which increases their sales.

Profits

When asked about their profit margin, most respondents were able to provide a gross profit margin in the form of a percentage. If a respondent had difficulty answering this question, the research team calculated the margin based on the buying and selling prices of a respondent's two most active products.

The average profit margin was 38.3 percent for all MSEs, 37.9 percent for microenterprises, and 41.8 percent for small enterprises. For female-owned enterprises in the survey, however, it was 72.8 percent. Although this profit margin was the highest in the survey, it should be noted that turnover of female-owned enterprises is considerably lower, on average, than that of male-owned enterprises (see text below, as well as table 29 in annex 4).

Using the margins cited above, the average yearly profit was calculated at US\$ 26,216 for all MSEs, US\$ 14,835 for microenterprises, US\$ 149,657 for small enterprises, and US\$ 1,481 for female-owned enterprises. It should be noted that these are gross profit calculations from which operating expenses and other expenses have not been deducted.

Table 7. MSE average profit margin and yearly profits

<i>Type of enterprise</i>	<i>Annual profit margin (%)</i>	<i>Average yearly profit (gross, in US\$)</i>
Micro	37.9%	14,835
Small	41.8%	149,657
Female-owned	71.8%	1,481
All MSEs	38.3%	26,216

Source: IFC survey data, 2007.

Constraints

MSEs identified their biggest constraints as high taxes³⁷ (265 out of 405 responses, or 65.4 percent) and tough competition (176, or 43.5 percent). Other constraints included a decrease in the number of clients and lack of financing (the latter reason was ranked fifth in importance). Among all respondents, 32.2 percent of microenterprises and 21.1 percent of small enterprises experienced lack of financing to be constraint.

The fact that lack of financing was rated fifth among other reasons can be interpreted in two ways. On the one hand, MSEs may face more significant constraints than lack of finance on their growth. Thus even if they had money to invest as working capital, they would not necessarily have a better chance of growing. On the other hand, lack of access to formal financing does not necessarily mean lack of access to financing altogether, as informal sources play an important role in the financial management of MSEs in Yemen (see below). This type of financing may, in fact, offset the lack of access to formal finance.

³⁷ It should be mentioned that businesses in Yemen pay only a 20-percent corporate tax.

Both micro and small enterprises considered taxes too high, although not by the same measure (63.8 percent versus 81.6 percent). Given that unregistered enterprises do not pay taxes and the share of unregistered enterprises among microenterprises is much higher, it should be no surprise that small enterprises appear more concerned about the tax problem.

With respect to regional concerns, 75.5 percent of enterprises in Sana'a (the most developed region of the country) named competition as their biggest constraint, followed by high taxes (50 percent). In all other regions, high taxes were found to be the most important challenge to growth, although transportation problems and lack of infrastructure were also identified as important problems in Hajjah (the most rural region in the survey).

Future Perspectives, Major Constraints, and Investments

Not quite half (42.3 percent) of all enterprises surveyed saw their future was positive, with the majority (57.7 percent) believing that their businesses would either remain stable or decrease. The most optimistic enterprises were located in the capital, Sana'a, 52.1 percent of which foresaw an increase in their businesses. In Hajjah, by contrast, the most rural region in the survey, only 29.2 percent foresaw an increase. As noted earlier, 69.3 percent of enterprises in Sana'a were established within the last three years, making them more likely to have more positive expectations of near-term development.

In contrast to their personal expectations for their businesses, the majority of MSEs (62.3 percent) expected the national economy to worsen in the near future. Only 19.7 percent expected a stable economy and 18 percent expected positive economic development. There was no difference between the views of micro and small enterprises on this topic.

Past Investments

Out of 405 respondents, 340 enterprises (84 percent) had not made any investments in their businesses in the last two years. Broken down by size, 86.1 percent of microenterprises and 63.2 percent of small enterprises had made no investments.

MSEs that did invest over the past two years mostly invested in expansion (23.7 percent of small enterprises and 7.1 percent of microenterprises). Equipment took the lowest share (2.6 percent) of investments by all MSEs, with no microenterprises investing in equipment. When asked about the source of their investments, 7.5 percent of MSEs had used credit only and 32.1 percent, a combination of their own funds and a credit. Surprisingly, credit use was more common among micro than small enterprises. Of note, a majority (60.4 percent) had used their own funds for past investments.

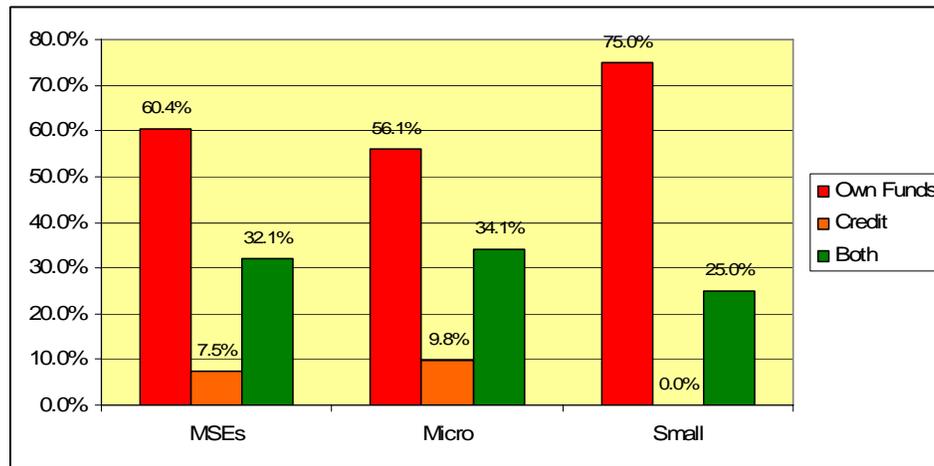
The biggest share (40.4 percent) of past investments made by microenterprises fell between US\$ 501 and US\$ 2,500, while the biggest share (53.8 percent) made by small enterprises fell between US\$ 5,000 and US\$ 10,000. None of the respondents made investments of greater than US\$ 50,000.

Table 8. Average MSE investment in last two years (US\$)

Type of MSE	Investment amount (US\$)
Micro	CR\$ 5,028
Small	\$ 8,153
All MSEs	\$ 5,683

Source: IFC survey data, 2007.

Figure 1. Source of recent MSE investments (N=65, in %)



Source: IFC survey data, 2007.

Planned Future Investments

Over half of MSE respondents (221 enterprises out of 404, or 54.7 percent) were not planning to make an investment in the future. The percentage of enterprises not anticipating a future investment did not vary greatly by sector (52.1 percent of MSEs in trade, 59.5 percent in service, and 58.6 percent in production). Among enterprises that were planning a future investment, the largest share of respondents (31.1 percent in trade, 15.0 percent in service, and 22.4 percent in production) planned to invest in expansion.

Among the 183 enterprises that planned to invest in the future, only 163 specified an amount. Almost half this number (77 enterprises, or 47.2 percent) planned an investment of up to US\$ 2,500. Among the six female respondents, only one planned to make an investment, which she estimated at US\$ 1,000.

Table 9. Average planned investment, by MSE size (N=163, in US\$)

Type of MSE	Investment amount (US\$)
Micro	\$ 10,647
Small	\$ 25,916
All MSEs	\$ 11, 957

Source: IFC survey data, 2007.

With respect to future investments, 35.7 percent of all MSEs indicated that they intended to use their own funds, whereas 27.9 percent intended to use credit alone and 36.4 percent, a combination of credit and their own funds. While only 31.7 percent of microenterprises sought to finance future investments with their own funds, 71.4 percent of small enterprises intended to do so. This difference may indicate a greater willingness to use (or need for) credit among microenterprises.

Table 10. Source of planned investments, by MSE size (N=163, in %)

<i>Type of enterprise</i>	<i>Own Funds</i>	<i>Credit</i>	<i>Both</i>
Micro	31.7%	31.0%	37.3%
Small	71.4%	0.0%	28.6%
All MSEs	35.7%	27.9%	36.5%

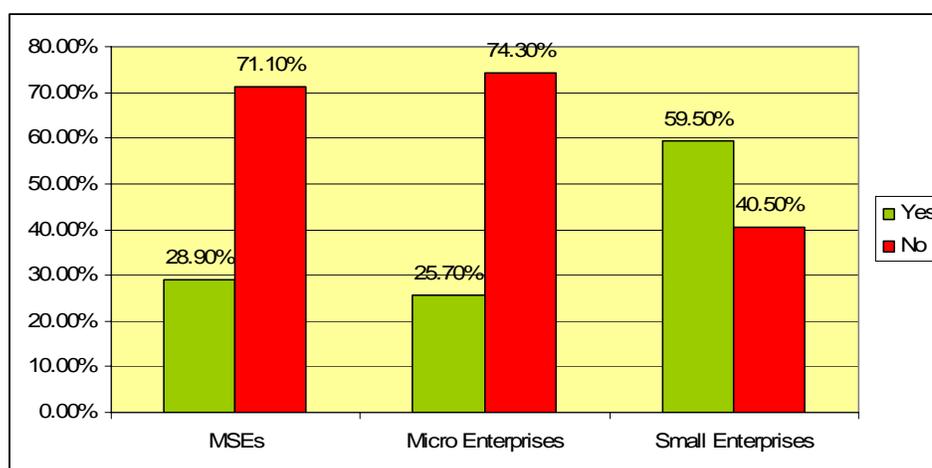
Source: IFC survey data, 2007.

MSE Use of Formal and Informal Financial Services

Banking Services

It is a striking fact of financial sector development in Yemen that only 28.9 percent of all MSE respondents in the survey use some kind of banking service. This means 71.1 percent operate completely outside the formal banking sector. Bank usage differs significantly between micro and small enterprises: only a quarter (25.7 percent) of all microenterprises surveyed used banking services, whereas over half (59.5 percent) of small enterprises did so.

Figure 2. Do you use banking services? (N=387, in %)



Source: IFC survey data, 2007.

Among the small sample of enterprises that regularly used banking services, the most common financial service was national transfers (used by 49.1 percent of this group),³⁸ followed by current accounts (46.4 percent) and savings accounts (31.3 percent).

³⁸ Apart from banks, it should be noted that many transfer companies offer this service at a reasonable fee.

Among the MSEs that use banks, there is a clear preference for the Yemen Bank for Reconstruction and Development (YBRD) and the Tadhamon Islamic Bank, both of which are used by 21.1 percent of this group. After these two institutions, microfinance institutions were the next most-used financial institution. Transfer companies and exchange offices, including the Post and Postal Savings Corporation (which MSEs use to make national money transfers), also had a considerable market share (18.2 percent) among this group.³⁹

Regional differences were notable in this area. The Cooperative Agricultural Credit Bank (CAC Bank), for example, was preferred by 78.4 percent of MSEs that used banks in the rural region of Hajjah, followed by a microfinance institution (28.6 percent of respondents). It must be pointed out, however, that these institutions are the only financial service providers in that region.

With respect to other banking services, 15.2 percent of all respondents indicated that they regularly used Islamic products and another 14.3 percent said that they used checks. However, only two respondents reported that they used checks as a payment instrument. This inconsistency may imply that checks are not used properly in Yemen, given that they are new to the market, or that checks are sometimes used to ensure the payment of credits to related parties.⁴⁰

The 275 MSEs that do not use banking services (i.e., the majority of MSEs) showed little interest in banking services. Only 6.5 percent of this group was interested in a current account, 8 percent in a saving account, 6.2 percent in Islamic products, and 5.1 percent in national transfers.

Savings

Virtually all respondents (395 out of 405) provided information about their regular savings habits. The majority of enterprises saved on a regular basis, but the share of savers differed according to size: 60.1 percent of microenterprises saved on a regular basis, while 84.2 percent of small enterprises did.

While the biggest share of microenterprises (37.4 percent) saved at home, the biggest share of small enterprises (31.6 percent) preferred to save at a bank. Only 23 enterprises did not save at home or a bank, but invested in their enterprise, i.e., used their savings as working capital. This investment habit was reported by 23.7 percent of small enterprises, but only 8.1 percent of microenterprises. Finally, 12 microenterprises, but no small enterprises, saved at a co-operative or an association.

The largest number of MSEs surveyed (38.9 percent) saved between US\$ 500 and US\$ 2,500 over the past year. Among microenterprises, 70.5 percent saved less and 29.5 percent saved more than US\$ 2,500 on an annual basis.

Among the six female respondents, only one saved on a regular basis—US\$ 75 per month (at home).

³⁹ Because the PPSC currently does not offer credit services to the public, it has been put in the same category with transfer and exchange offices.

⁴⁰ MSE occasionally sign checks that carry a future date, enabling the holder of the check to cash it and thereby recover money given as credit.

Table 11. Average MSE annual savings (US\$)

<i>Type of MSE</i>	<i>Annual savings (US\$)</i>
Micro	\$ 905
Small	\$ 9,899
All MSEs	\$ 3,422

Source: IFC survey data, 2007.

When the savings capacity of MSEs is compared with their annual profit, it can be seen that small enterprises are able to save 13.3 percent of their annual profit and microenterprises, 6 percent.

Credits

The majority of MSE respondents (57 percent) were unaware of any type of loan. Small enterprises were more familiar with loans than microenterprises, with a working capital loan the most-recognized type of credit among all respondents (19.1 percent). Among small enterprises, 36.8 percent knew about this type of loan. The Islamic product *morabaha* was also fairly well known among small enterprises, recognized by 36.8 percent of this group.

A large share of respondents (76.3 percent) considered the loan process difficult, very difficult, or even impossible, with no real differences on this answer between micro (76.1 percent) and small (73.7 percent) enterprises.

Respondents were asked to name the three most important problems of obtaining credit in Yemen. An especially high share of respondents (182 out of 306, or 59.5 percent) cited lack of collateral, followed by high interest rates (142, or 46.4 percent), and religious reasons (140, or 45.8 percent). Among small enterprises, high interest rates were the greatest concern (60.7 percent), with religious reasons second (57.1 percent), and overly long and complicated procedures, third (50 percent).

Table 12. Most important difficulties in obtaining a bank loan (N=347, in %)

<i>Reason</i>	<i>% of all MSEs</i>
Lack of collateral	59.5%
High interest rates	46.4%
Religious reasons	45.8%
Overly long and complicated procedures	38.6%
I don't know anyone in the bank	29.4%
Fear of being unable to repay	21.9%
Accessibility of the bank	13.7%
Administrative constraints	9.8%
Corruption	9.0%
Lack of knowledge of staff	4.9%
Difficulty in presenting figures	2.9%
Other	4.0%

Source: IFC survey data, 2007.

Formal Loans

Out of 404 total respondents, only 43 MSEs (10.6 percent of the survey sample) had ever tried to obtain a loan at a financial institution, and only 24 (5.9 percent) had obtained one. These rates were virtually the same for both micro and small enterprises. This means that 94 percent of all MSEs interviewed for the demand study have never obtained a formal loan. Interestingly, among the 24 MSEs that did receive loans, only 16 had an accounting system.⁴¹ At the time of the survey, 6 of the 24 still had a loan outstanding.

Enterprises that had never applied for a loan—meaning the majority of MSEs interviewed for this study (89.4 percent)—ranked their reasons for not applying as follows: no need for a loan (31.8 percent), followed by lack of or improper collateral (27.7 percent), religious reasons (24.3 percent), high interest rates (17.6 percent), and overly long and complicated procedures (9.5 percent). Of note, 8.1 percent of respondents—mainly microenterprises—answered that they had never asked for a loan because they did not know where to obtain one.

Micro and small enterprises differed in how they responded to the question of why they had not applied for a loan. More small enterprises than microenterprises, for example, said they had not applied because they did not need a loan (52.9 percent versus 31.8 percent), while less small enterprises regarded the lack of collateral as a problem than did microenterprises (5.9 percent versus 29.9 percent).

Among the 24 loan recipients, 20 specified the amount of their credits. The average amount of these loans was US\$ 3,576. Overall, 90 percent were less than US\$ 5,000, and

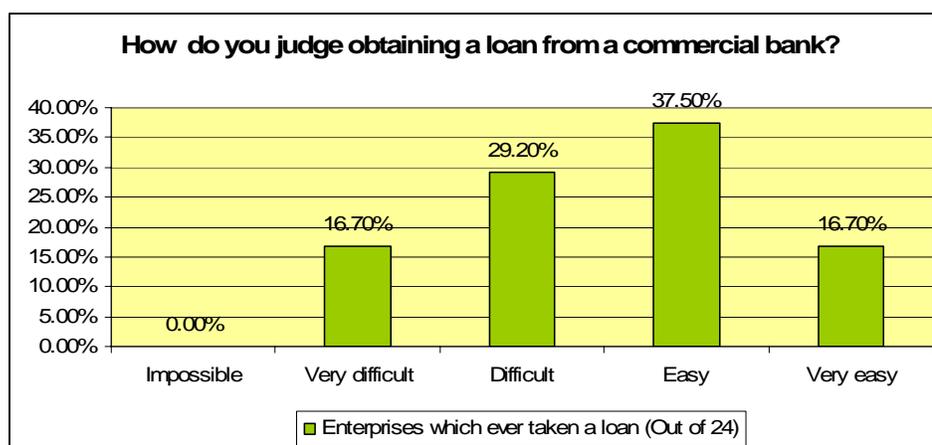
⁴¹ It should be reminded that any storage of sales or revenues on a daily, weekly or monthly basis was regarded as bookkeeping.

50 percent fell between US\$ 500 and US\$ 2,500. The highest-value loan was US\$ 35,000. None of the enterprises borrowed an amount that exceeded their yearly turnover.

Although the success rate of respondents that actually applied for formal credit was 55.8 percent (24 out of 43), this rate cannot be generalized, given that many enterprises decided a priori not to apply for a loan due to the abovementioned constraints. It was apparent to the research team that only businesses which regarded themselves as sufficiently strong and which owned adequate collateral entered into the time-consuming process of applying for credit. Even then, almost half of this group (45.9 percent) found the loan application process difficult or very difficult.

When unsuccessful loan applicants were asked why they did not obtain loans, 50 percent named a lack of guarantees and the other 50 percent said that loan conditions were difficult to fulfill.

Figure 3. Evaluation of application process by MSEs that have obtained a loan (N=24, in %)



Source: IFC survey data, 2007.

Among the respondents who received a loan, 17 borrowed from either the Yemen Bank for Reconstruction and Development (YBRD) or the Credit and Agricultural Cooperative (CAC) Bank. Another six borrowed from the government’s Small Enterprise Development Fund (SEDF) and one borrowed from the Islam Charity Association.⁴² Of note, 68.4 percent of this group borrowed only once, with the balance of respondents borrowing between two and four times.

The low rate of repeat borrowing may mean that the experience of the loan process was unsatisfactory for the entrepreneur or the bank, or both, therefore one party decided not to continue the relationship. Perhaps the bank was unwilling to provide a second loan due to repayment problems, or perhaps the entrepreneur was dissatisfied with the conditions of the loan (e.g., loan amount, maturity, repayment method, etc.). Regardless of the reasons for the low rate of repeat borrowing, most enterprises that had obtained a loan were interested in obtaining another.

⁴² The microfinance operation of this association is called the Nama’a Program.

In terms of collateral, enterprises that obtained loans primarily used real estate and land (30.4 percent) or personal guarantees (26.1 percent). Some enterprises indicated that they provided jewelry and gold, goods in turnover, or even private belongings, which implies that financial institutions in Yemen are open to accepting various types of collateral.

Interest Rates, Maturity, and Grace Periods of Formal Loans

The majority of loan recipients did not remember the interest rate on their loans. Based on the research team’s calculation, most of these loans bore interest rates between 8 and 20 percent. One loan was obtained from an Islamic bank, but because such banks do not disburse cash loans, rather, they finance the purchase cost of materials and/or products, the respondent was unable to estimate the overall financing cost of the credit.

It should be emphasized that the pricing policy of financial institutions in Yemen is not transparent. Clients find it difficult to estimate the real costs of credit and in most cases, forget one or two the costs associated with a loan, such as the study fee, disbursement fee, or fees for the credit account. The cost of credit calculated by the research team for this report may thus be too low, as it is likely not all costs were considered.

The maturity of the largest group of loans (47.86 percent) was between 7 and 12 months, a smaller sub-set (23.8 percent) had a maturity of more than 18 months.

Informal Loans

While only 5.9 percent of respondents in the survey sample had obtained a loan from a formal source, 229 out of 397 respondents (57.7 percent) had obtained a loan from an informal source. The majority of these loans (57.1 percent) were less than US\$ 500. Because the total number of loans fell between an extreme range of US\$ 5 to US\$ 50,000, however, the average loan amount was much higher (see table ___ below).

Table 13. Average MSE informal loan (N=229, in US\$)

<i>Type of MSE</i>	<i>Average loan (US\$)</i>
Micro	\$1,379
Small	\$ 1,494
All MSEs	\$ 1,388

Source: IFC survey data, 2007.

Maturity, Interest Rates, and Grace Periods of Informal Loans

Survey responses show an extreme variety in the duration of informal loans, from a few days to several years. The largest share (39.2 percent) of informal loans had a maturity of more than 18 months.⁴³ In most cases this type of loan can be repaid whenever the entrepreneur has sufficient financial resources, often in one or two installments. The grace period for an informal loan is therefore often equal to its maturity.

Informal loans in Yemen appear to be characterized by an almost complete absence of interest rates. Only three respondents who had received such loans paid interest on the

⁴³ This is a much longer maturity than most clients can get from commercial banks and MFIs. However, it should be remembered that informal money providers are often not motivated by economic goals.

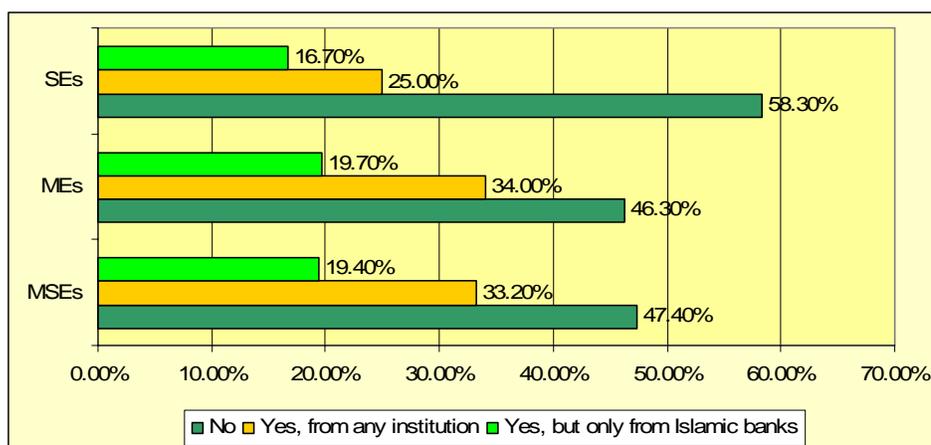
credit. Unlimited maturity and flexible payment schedules also appear very common. For example, out of 229 respondents, 163 (71.2 percent) indicated that they repaid a past informal loan depending on their payment ability.

The reasons given by the 137 survey respondents who said they had never received an informal loan varied: 69 said they didn't need money, 32 mentioned a lack of money among family and friends, and 19 were afraid of being unable to repay a loan.

Future Loan Demand

As figure 4 below shows, 203 out of 386 respondents (52.6 percent) said they would be interested in obtaining a loan if it were possible to do so. Of note, 75 of these respondents (or 19.4 percent) were only interested in obtaining a loan from an Islamic institution. Microenterprises were more interested in applying for loans than were small enterprises (34 percent versus 25 percent), with a greater percentage of small (58.3 percent) than micro enterprises (46.3 percent) not interested in applying for a loan at all.

Figure 4. MSE interest in obtaining a loan, given the possibility (N=386, in %)



Source: IFC survey data, 2007.

Among the 203 respondents that indicated interest in a future loan, 168 indicated the desired amount. The largest number of these respondents (42.3 percent) specified an amount between US\$ 500 and US\$ 2,500, with 17.7 percent of microenterprises seeking loans of less than US\$ 500.

Table 14. Average loan desired, by MSE size (US\$)

<i>Size of enterprise</i>	<i>Desired loan amount</i>
Micro	6,571
Small	30,325
All MSEs	7,985

Source: IFC survey data, 2007.

Most MSEs sought loans for expansion (120 out of 187 respondents, or 64 percent) or to purchase machinery or vehicles (12.8 percent). Of note, most small enterprises were unwilling to obtain a loan for working capital or construction, but 14.3 percent would obtain one for product diversification.

When asked what interest rate they would find appropriate on a loan, the answers of the MSEs surveyed were extremely varied. This should not be surprising, given that enterprises in Yemen do not have any idea of market conditions or interest rates. However, among the sample that indicated interest in obtaining a loan, the majority sought an interest rate of between 1.1 to 5 percent per annum. With respect to maturity, the majority of loan-seekers (146 out of 194, or 75.3 percent) preferred a term of more than 18 months. None sought to borrow for less than four months, and 10.3 percent sought a maturity of up to one year.

When asked about potential collateral for a loan, the largest share of loan-seeking MSEs said they could provide a piece of land (38.9 percent), followed by a commercial guarantee (34.7 percent)⁴⁴ or house (24.2 percent). Finally, 69.1 percent of these respondents said they could provide a personal guarantee. The ability to find a personal guarantor differed little among micro (68.8 percent) and small enterprises (73.3 percent).

The 181 MSEs that were uninterested in obtaining a future loan said they were not interested either because they didn't need a loan (44.8 percent) or for religious reasons (40.2 percent). Another 15.5 percent said that they did not have confidence in banks or other financial institutions.

Future MSE Loan Demand

When the loan amounts desired by survey respondents were compared to their annual average turnover, the amounts appeared are realistic. Out of 162 respondents, for example, only 12 sought loans greater in value than the annual turnover of their enterprise. A loan in excess of US\$ 2,500, moreover, would expose a lender to great risk, given that this sum already represents almost five times average capita GDP and that only 53.6 percent of Yemeni enterprises claim to do any bookkeeping.

Because the sample size of formal loan borrowers was too small to use to estimate future demand, the desired amount of future loans was compared to that of previous informal loans. Of note, out of 112 respondents who specified the amount of past informal loans (see figure 43 and table 32 in annex 4), only 2 sought to borrow less than previously borrowed loan amounts. On the basis of this finding, it could be argued that MSEs in Yemen are unable to obtain loans in the desired amount from informal sources because the latter lack sufficient financial resources. Of course, informal providers that do not charge interest and extend terms of up to 18 months are not driven by economic interest. In many cases, however, these sources are either reluctant or unwilling to risk comparatively large amounts of money in interest-free loans.

As shown in table 15 below, a comparison of average desired loan amounts with MSE financial indicators is very revealing. While the average desired loan for all MSEs (US\$ 7,895), for example, represents only 11.7 percent of respondents' average annual

⁴⁴ Commercial guarantees are widely used within the Yemeni financial system to secure credits.

turnover, 30.5 percent of their average annual gross profit, and 66.7 percent of planned investments, it represents 233 percent of average annual savings, 139 percent of average past investments, 223 percent of average past formal loans, and 575 percent of average past informal loans.

Table 15. Average desired loan amounts and financial indicators, by MSE size

	<i>All MSEs</i>	<i>Micro</i>	<i>Small</i>
Average turnover (US\$)	68,450	39,248	358,032
Average profit margin (%)	38.3	37.9	41.8
Average yearly profit (US\$)	26,216	14,835	149,657
Average savings (US\$)	3,422	905	19,899
Average past investment	5,683	5,028	8,153
Average future planned investment (US\$)	11,957	10,647	25,916
Average amount of past formal loans (US\$)	3,576	NA	NA
Average amount of past informal loans (US\$)	1,388	1,379	1,494
Average desired loan amount (US\$)	7,985	6,571	30,325

Source: IFC survey data, 2007.

Estimated Microfinance Market in Yemen

Based on the findings of the demand survey, it is estimated that the overall MSE sector in Yemen consists of 300,000 to 400,000 micro and small enterprises. Given that 52.6 percent of MSEs interviewed for the survey sought to obtain a loan, it is estimated that a minimum of 210,400 MSEs are potential loan borrowers. Currently, only 5.9 percent of this market is served by existing institutions. Assuming that the amount of microloans is set at an upper limit of US\$ 2,500, overall MSE loan demand in Yemen is estimated at US\$ 526 million.

4. KEY FINDINGS

The formal financial sector in Yemen is highly underdeveloped. It consists of 15 active banks,⁴⁵ of which four are fully foreign owned, three are public, and eight are private financial institutions (four of the latter are Islamic banks). Commercial banks have a strong tendency to invest in treasury bills and their ratio of credits to deposits is just 39 percent. Virtually all banks interviewed for this report regard SME lending as a strategic future goal, but have not yet elaborated plans to address this market.

The great majority of the population does not have access to formal financial services. Only 800,000 people (3.5 percent of the population) have an account with a formal financial institution. The outreach of the formal financial sector is concentrated in the main cities and sub-cities. Commercial banks have roughly 200 branches nationwide and the Post and Postal Savings Corporation, 240 branches.

The country has a large potential microfinance market of reliable clients committed to repaying credits. Women currently comprise 87 percent of all MFI customers in the country and are the source of the relatively high repayment rates of Yemeni MFIs. Given that women are dedicated to using microloans for income-generating purposes and spending profits to improve family living conditions, an expansion of the microfinance sector would help improve the quality of life of families nationwide.

The value of the microfinance market in Yemen is estimated at US\$ 526 million, based on 210,400 potential MSE borrowers and an average loan size of US\$2,500. According to the market study conducted for this report, existing financial institutions are currently serving only 5.9 percent of this market.

The savings habits of MSEs indicate a capacity to repay microloans. Survey results show that the majority of both microenterprises (71.4 percent) and small enterprises (90.3 percent) saved more than US\$ 500 over the past year. Among the latter, 70.9 percent had saved more than US\$ 2,500.

The major constraint to building strong, self-sustaining microfinance institutions is the absence of a legal and regulatory framework for non-bank financial institutions (NBFIs). Lack of efficiency and transparency in the legal system, combined with a time-consuming court system and the absence of both a land registry and registry authority, are all obstacles to the development of a viable microfinance sector. Most MFIs in Yemen currently work under the auspices of the MoIT or the Ministry of Social Affairs and Labour, although neither ministry has supervisory power.

A planned law on NBFIs gives the Government of Yemen an invaluable opportunity to create a legal and regulatory framework that encourages the development of strong, permanent providers of microfinance. If MFIs are to achieve sustainability over the long term and reach growing numbers of the poor, it is crucial that the new law allow them to accept deposits. Deposits will enable these

⁴⁵ In total there are 18 banks. However, Watani Bank (private) is in liquidation and the Housing Credit Bank (public) is due to merge with CAC Bank according to a decree issued in 2004 (implementation has yet to start). One foreign bank, Al-Rafadein Bank, a public bank from Iraq, is only facilitating remittances.

institutions to increase the amount of credit that they can offer, as well as drive down the cost of on-lending.

The success of new MFIs will depend on good client education. Given that a large part of the population of Yemen is unaware of the existence of formal credit, new MFIs will need to educate clients about the difference between grants and credits and make clear that microloan borrowers must repay both capital and interest.

Microfinance products in Yemen need to be easy to understand, appropriate to client needs, and capable of being processed rapidly. Clients without economic training must, for example, be able to easily calculate the price of (and interest on) microfinance services. Products must also respond to perceived client needs, which current MFI clients have identified as individual loans, higher loan amounts, longer maturities, products for start-up enterprises and Islamic products (mainly *morabaha*). Microleasing is another product with future potential, although the microfinance sector does not presently have the capacity to support it.

Several distinct microloan sizes could be attractive on the Yemen market, including consumer loans of up to US\$ 100, offered on the basis of pawned goods; micro and small business loans of up to US\$ 2,500; and larger loans of up to US\$ 7,000 for clients with a good credit history and appropriate bookkeeping practices. Although survey respondents on average sought loans of up to US\$ 7,985, this value far exceeds that of past formal and informal loans, as well as the typical microloan currently offered on the Yemeni market (US\$97).

In light of a low national literacy rate (50 percent), **new MFIs entering the market might consider providing financial services together with training in accounting and entrepreneurial skills**—either directly or in partnership with specialized providers.

Set-up costs for new MFIs are relatively low in Yemen when compared to other countries. By international standards, the cost of rental contracts, salaries, social insurance, and equipment (e.g., telephones, office equipment, etc.) are all very low.

New MFIs are advised to start with branches in areas with high demand and good infrastructure. Where rural demand is significant, these branches could evolve into regional hubs that serve larger areas. It should be noted that the existing formal bank network is so thin in cities that even many suburbs have no easy access to financial services.

Good training systems and coherent career tracks will be essential to the success of new MFIs in Yemen. Any new MFI that does not want to draw on the limited pool of qualified staff working in existing MFIs must invest heavily in the training and education of both staff and management. This imperative creates an opportunity for an MFI with sufficient training resources to set the standards of the financial industry in Yemen.

Annex 1: Overview of Financial Institutions in Yemen

Table 16A. Banks operating in Yemen

<i>Name of Institution</i>	<i>HO/Branches</i>	<i>Active clients/loans</i>	<i>Active Portfolio/loans (gross)</i>	<i>Average loan size</i>	<i>Products</i>	<i>Interest Rate or Fee/Loan annually</i>	<i>NLP (% of outstanding portfolio (gross))</i>
Tadhamon Islamic Bank	Sana'a/13 branches in Sana'a, Taiz, Aden, Hodeidah and Mukalla	160.000 customer accounts	US\$ 473 million	N/A	Corporate Finance Retail Loans L/C and L/G Current Accounts Savings Accounts National money transfers International Remittances ATM and credit cards Islamic Lending	15% - 24% for SME Finance	4% for Morabaha (67% of the loan portfolio)
International Bank of Yemen	Sana'a/10 branches in the main cities	300 corporate clients over US\$ 10,000/ 6.000 retail clients	US\$ 141 million	N/A	Corporate Finance Retail Loans L/C and L/G Current Accounts Savings Accounts National money transfers International Remittances ATM and credit cards Phone and SMS banking Conventional Lending	19% retail	61%
Yemen Bank for Reconstruction and Development	Sana'a/44 branches in the main and sub cities	3.444	US\$ 71 million	US\$ 20,615	Corporate Finance Micro Loans Retail Loans L/C and L/G Current Accounts Savings Accounts National money transfers International Remittances Conventional Lending	19% and more	41%

Table 16A. Banks operating in Yemen - continued

<i>Name of Institution</i>	<i>HO/Branches</i>	<i>Active clients/loans</i>	<i>Active Portfolio/loans (gross)</i>	<i>Average loan size</i>	<i>Products</i>	<i>Interest Rate or Fee/Loan annually</i>	<i>NLP (% of outstanding portfolio (gross))</i>
National Bank of Yemen	Aden/29, mainly in the South and Sana'a, Hodeidah and Taiz	N/A	US\$ 44 million	N/A	Corporate Finance ⁴⁶ Small Commercial & Retail Loans L/C and L/G / Bank Guarantees Current and Savings Accounts National money transfers International Remittances ATM and credit cards Conventional Lending	15%-16%	23%
Saba Islamic Bank	Sana'a/14 branches in all governorates	N/A	US\$ 114 million	N/A	Corporate Finance Retail Loans L/C and L/G Current and Savings Accounts National money transfers Credit cards Islamic Lending	10% - 11%	4,3% for Morabaha (98% of the loan portfolio)
CAC Bank	Sana'a/44 branches in the main cities and sub cities, also serving the rural areas	N/A	US\$ 90 million	N/A	Corporate Finance including agriculture Retail Loans L/C and L/G Current and Savings Accounts National money transfers International Remittances ATM and credit cards Conventional Lending	N/A	28%
Yemen Commercial Bank	Sana'a/13 branches in the main cities of the north	10.000 corporate clients/ 20.000 retail clients	US\$ 117 million	N/A	Corporate Finance Retail Loans L/C and L/G Current and Savings Accounts National money transfers International Remittances ATM including a Mobile ATM Truck and credit cards Conventional Lending	18%	30%

⁴⁶ For all listed banks: Includes trade finance, asset finance, project finance and bridge finance.

Table 16A. Banks operating in Yemen - continued

<i>Name of Institution</i>	<i>HO/Branches</i>	<i>Active clients/loans</i>	<i>Active Portfolio/loans (gross)</i>	<i>Average loan size</i>	<i>Products</i>	<i>Interest Rate or Fee/Loan annually</i>	<i>NLP (% of outstanding portfolio (gross))</i>
Yemen Kuwait Bank for Trade and Investment	Sana' /11branches in the main cities	976 loan clients and 316 overdrafts	US\$ 63 million	N/A	Corporate Finance Retail Loans L/C and L/G Current and Savings Accounts National money transfers International Remittances ATM and credit cards Conventional Lending	18% - 20%	35%
Shamil Bank of Yemen and Bahrain	Sana'a/2 branches in Aden and Hodeidah	N/A	US\$ 34 million	N/A	Corporate Finance Retail Loans L/C and L/G Current and Savings Accounts National money transfers International Remittances ATM and credit cards Islamic Lending	9,75% Corporate lending, 15% for SME, but still under discussion	N/A
Islamic Bank of Yemen	Sana'a/5 branches in the main cities	176 corporate loans/	US\$ 44 million	US\$ 29,225 (corporate loans)	Corporate Finance Retail Loans L/C Current and Savings Accounts National money transfers International Remittances Islamic Lending	N/A	48%
Yemen Gulf Bank	Sana'a	N/A	N/A	N/A	Lending activities are restricted for the time being to long standing clients Trade Finance Credit Lines L/C and L/G Current and Savings Accounts Credit Cards Internet/Tele/SMS Banking Conventional Lending	N/A	N/A

All data between 12/2006 and 08/2007, except Gulf Bank 12/2004

Table 16B. Microfinance institutions operating in Yemen

<i>Name of Institution</i>	<i>HO/Branches</i>	<i>Active clients/loans</i>	<i>Active Portfolio/loans</i>	<i>Average loan size</i>	<i>Products</i>	<i>Interest Rate or Fee/Loan annually</i>	<i>Women/Men %</i>	<i>Urban/Rural %</i>
National Microfinance Foundation	<i>Sana'a</i> , Abs, Al Quaida, Dhamar, Hajja, Ibb, Lahj, Taiz, Yarim 9 branches	8.500	YR 153 million US\$ 765.000,--	YR 18.000,-- US\$ 90,--	Group Loans Individual Loans Compulsory Savings Residual Debt Insurance Islamic and Conventional	24%	99%/1%	55%/45%
Hodeidah Microcredit Program ⁴⁷	<i>Hodeidah (3)</i> , Bagel, Al Ziadia, Beit Al Fakih, Al Marawa and Al Zuhrah 8 branches	4.075	YR 46,5 million US\$ 232.670,--	YR 32.450,-- US\$ 162,--	Group Loans Individual Loans Seasonal Loans Islamic Lending	24% - 36%	77%/23%	40%/60%
Namaa – Microfinance Development Program	<i>Sana'a</i> and Taiz; Aden (01.01.2008) 2 branches	3.080	YR 77 million US\$ 385.000,--	YR 25.000,-- US\$ 125,--	Group Loans Individual Loans Savings Islamic Lending	20%	32%/68%	80%/20%
Aden Microfinance Foundation	<i>Aden (5)</i> and Lahj 6 branches	2.819	YR 45 million US\$ 225.000,--	YR16.000,-- US\$ 80,--	Group Loans Individual Loans N/A	18% - 36%	97,5%/2.5%	55%/45%
Al Awael Taiz	<i>Taiz (3)</i> 3 branches	2.810	YR 44 million US\$ 220.000,--	YR 15.400,-- US\$ 77,--	Group Loans Individual Loans Seasonal Loans N/A	36% 28% 30%	100% women	100% urban
Azal – Sana'a Microfinance Program	<i>Sana'a (3)</i> 3 branches	2.800	YR 60 million US\$ 300.000,--	YR 21.000,-- US\$ 105,--	Group Loans Individual Loans Islamic Lending	24% - 30%	95%/5%	100% urban
Abyan Credit and Savings Program	<i>Abyan</i> one branch	2.019	YR 46 million US\$ 230.000,--	YR 40.000,-- US\$ 200,--	Group Loans Islamic and conventional	24%	100%	100% rural
Social Foundation for Sustainable Development	<i>Sana'a</i> one branch	1.800	YR 58 million US\$ 290.000,--	YR 80.000,-- US\$ 400,--	Group Loans Individual Loans Seasonal Loans Islamic Lending	18%	91%/9%	75%/25%

⁴⁷ Including Bait Al-Fakieh Credit and Savings Program.

Table 16B. Microfinance institutions operating in Yemen – continued

<i>Name of Institution</i>	<i>HO/Branches</i>	<i>Active clients/loans</i>	<i>Active Portfolio/loans</i>	<i>Average loan size</i>	<i>Products</i>	<i>Interest Rate or Fee/Loan annually</i>	<i>Women/Men %</i>	<i>Urban/Rural %</i>
Wadi Hadramaut Credit and Savings Program	<i>Seyun</i> one branch	1.120	YR 42 million US\$ 211.000,--	YR 40.000,-- US\$ 200,--	Group Loans Individual Loans Seasonal Loans Islamic Lending	18%	N/A	100% rural
Hais Credit and Savings Program	<i>Hais</i> N/A	1.067	YR 16 million US\$ 80.000	YR 16.000,-- US\$ 80,--	N/A	N/A	93%/7%	100% rural
Sana'a Microstart SOFD	<i>Sana'a</i> one branch	566	YR 8.4 million US\$ 42.000,--	YR 40.000,-- US\$ 200,--	Group Loans Individual Loans Conventional Lending	36%	59%/41%	100% urban
All MFIs		30.656	YR 595,9 US\$ 2,98 million	YR 19.438 US\$ 97,--		18% - 36%	87,1%/12,9%⁴⁸	
SEDF – Small Enterprise Development Fund	<i>Sana'a</i> , Aden, Hodeidah, Ibb, Mukalla, Taiz 6 branches	1.900	YR 724 million US\$ 3,6 Mio	YR 380.000,-- US\$ 1.900,--	Individual loans for small businesses (assets and working capital) Conventional Lending	12,5% + 3% study fee	3%/97%	N/A
Tadhamon Bank	<i>Sana'a</i> ; Taiz, Aden (2), Hodeidah, Mukalla 6 branches	600	YR 60 million US\$ 500.000,--	YR 100.000,-- US\$ 500,--	Individual loans Group loans (Grameen Model for Women) Seasonal Loans Islamic Lending	15% 18%	60%/40%	99%/1%
Accumulated all institutions		33.156	YR 1.379,9 million US\$ 6,9 million	YR 41.618,-- US\$ 208,--		15% - 36%	81,6%/18,4%	

All data between 01/2007 and 07/2007
US\$ 1 – YR 199

⁴⁸ Without Hais Credit and Savings Program.

Annex 2: Information on Public and Private Banks in Yemen

National Bank of Yemen

The National Bank of Yemen is the only bank in Yemen with its Headquarter in Aden. It emerged in 1967 from the nationalization of the international banks in the South after the Socialistic Republic of Yemen was established. It is fully owned by the Yemeni government. It has 29 branches, all but four (Sana'a (two), Hodeidah and Taiz) are in the former south. The branches are well distributed also in the rural areas. The bank has around 500 employees.

The National Bank was able to collect US\$ 358 million of deposits from its customers, but only US\$ 44 million (12%) is converted to credits. Nearly 37% of the deposits are invested in treasury bills. The loan portfolio increased from 2005 to 2006 by 72% (gross) and 85% (net).

In the lending business the National Bank of Yemen focuses mainly on corporate clients (with loans in average over US\$ 1 million) and retail customers. Nevertheless there is no minimum amount for commercial loans, but they consider only 22 clients in Sana'a branch belonging to the MSE sector⁴⁹.

As all data is administered in the headquarter (HO) in Aden, the branch was not able to give any information about number of clients, portfolio, and others.⁵⁰

Loan Loss Provisioning Policy: N/A

Non Performing Loans (NPL): The auditors' report 2006 shows NPL and advances amounting to US\$ 10,2 million, reaching 29% of outstanding portfolio (net) or 23% of the gross loans.

Based on the increase of the gross portfolio the percentage of NPL decreased from 27% in 2005 to 23% in 2006, though the absolute amount of NPL increased between 2005 and 2006 by 7%,.

Provisioning: The management of the National Bank decided to make provisions for performing loans and contingencies including watch list loans at a rate of 2% (CBY regulation: 1%).

MSE related activities and strategy: No information could be obtained regarding the strategy of the bank. The National Bank considers its corporate loan product open for any kind of business. Nevertheless only 22 clients in the branch are considered MSE clients. No definition of MSE was given and they did not express any strategy to attract this clientele.

MSE related products: The bank has a corporate loan product open for any kind of business, with no expressed minimum loan amount, commercial guarantee or real estate (rented) required. They provide retail lending mainly for cars and household appliances and furniture, guaranteed either through payroll deduction or a commercial guarantee.

⁴⁹ This number is an estimation by the National Bank.

⁵⁰ The Consultant will try to collect more detailed data during a second visit to the bank in October as we regard our current data basis on the National Bank of Yemen as unsatisfactory.

The National Bank offers also housing finance without a fixed loan size. As guarantee they accept either fixed deposits or mortgage. The loan size for housing finance is fixed by the value of the mortgage provided. Clients can receive up to 75% of the value of their property. In case of fixed deposits clients can receive up to 80% of the value. The interest rate is 15 – 16% and slightly less than for corporate or small loans.

Current products: Corporate (trade finance, assets and project finance) and small commercial loans, retail loans for cars and home appliances and furniture, L/Cs and L/Gs as well as bank guarantees. On the liability side they offer current accounts, savings and time deposits, as well as national payment services, international remittances, ATM and VISA cards (so far through another bank).

Yemen Bank for Reconstruction and Development (YBRD)

The Yemen Bank for Reconstruction and Development (YBRD) is the oldest bank in Yemen, it was established in 1962. Since its foundation the Yemeni Government is the majority shareholder with 51%, whereas 49% are distributed among 30,000 private shareholders.

In its first decade YBRD acted also as the Central Bank of Yemen until the current CBY was established in 1972. Until 1992 YBRD continued to hold all governmental accounts but in 1992 the Ministry of Finance issued a decision that all governmental accounts have to be transferred from the commercial banks to the CBY.

According to the assets it is the 3rd biggest Yemeni bank and the biggest public bank. With its 44 branches it has the same amount of branches as CAC Bank and the widest distribution network among the commercial banks in rural areas.

According to their definition they offer loans to MSE, meaning the minimum loan amount starts with US\$ 2,500 up to 50,000. This product is especially successful in Hajja, Mahwit and Sada. Currently they have around 600 – 800 loans in this category. The overall number of outstanding loans is 3,444 at the end of June 2007. Loan duration for corporate loans and MSE loans is between 12 and 24 months, with an interest rate of 19%. Interestingly, YBRD charges a higher interest rate for repeated clients as they estimate the risk for a repeated loan higher than for the initial loan. As guarantees gold, payroll deduction, pension cheques and commercial guarantees are accepted. Exact numbers for retail loan accounts were not available but are estimated at round 8.000 – 10.000. The loan portfolio increased between 2005 and 2006 by 17% (gross) and 38% (net).

Since 1985 all loans are provided to the private sector due to unsatisfactory experience with financing public entities. A large portion of the NPL is related to the public sector although recently 31% of the outstanding amount could be recovered (US\$ 8.9 million). The NPL related to the public sector account for 100% of the bad loans.

Loan Loss Provisioning Policy: According to CBY regulation. The auditors' report 2006 shows performing and non performing loans provisions amounting to US\$ 26.3 million and uncollected interest sums up to US\$ 3.2 million The overall amount reaches 41% of the gross portfolio.

Non Performing Loans: The amount of NPL is not stated in the Annual Report⁵¹ The Bank's NPL concept is according to the CBY regulation. For the defaulted loans from the public entities, provisions of 110% were set aside.

MSE⁵² related activities and strategy: YBRD expressed a strong interest in extending its lending activities to small business owners. The management considers this segment less risky than the corporate customers. According to the management the repayment rate in the MSE segment is between 90% - 95%, whereas the repayment rate for the corporate customers is around 80%. The management is surprised why not more MSEs ask for financing through YBRD as they consider their products suitable for the target group. The management links this to the lack of knowledge of the clients and too little marketing and awareness rising by the government. They expressed their intention to do more marketing by themselves. They did not articulate any adjustments to their procedures nor any development of new services. In the retail segment the bank has no data on the purpose of the disbursed credit. There are no estimates, how many loans are used for income generation activities and how many loans are for consumption.

MSE related products: Loans for small businesses from US\$ 500 up to 50,000 (around 800 clients) and consumer loans up to US\$ 1,500 for governmental employees only (around 8,000 to 10,000 customers, with an outstanding portfolio of US\$ 1 million). To qualify for a consumer loan the client needs the guarantees of two colleagues from the same institution or he needs to offer a payroll deduction. 90% of the loans are guaranteed by payroll deduction.

Current products: YBRD offers all kinds of banking services. All lending activities are according to conventional lending. Loan products are divided into retail, micro and corporate finance including overdraft, L/C and L/G and promissory notes. On the liability side, the bank offers call accounts (current and savings) and term deposits. International money transfer is either available through SWIFT (current account needed) as well as through Western Union.

Credit and Agricultural Cooperative Bank (CAC Bank)

The Credit and Agricultural Cooperative Bank (CAC Bank) was established in 1982, following a merger of the Agriculture Credit Bank (est. 1975) and National Cooperative Bank (est. 1979). The CAC Bank is fully owned by the Yemeni Government. The bank is undergoing a far-reaching restructuring process to avert liquidation by the CBY due to high non-performing loans and limited capital base. The process started in 2004 when a new chairman was appointed. Most of the bad debts were bought out by the government and the bank was re-capitalised.

Following the restructuring process CAC Bank launched an image campaign and managed to establish its name as a brand. The banks image appears to be modern and professional. CAC Bank is the most visibly and known bank in Yemen.

Having the largest outreach in the country (shared with YBRD), it has 44 branches, distributed in the whole country, covering also rural areas.

⁵¹ The Annual Report provided no information about the NPL. The consultant will try to get more detailed information for the final report.

⁵² YBRD calls their small loans "microfinance"; the loan amount is from US\$ 500 to US\$ 50,000.

Until 2004, CAC Bank focused on lending to the agricultural sector and fisheries. Nowadays 80% of the portfolio is dedicated to commercial lending; the rest is divided between loans to the agricultural sector and personal loans. The focus is on big projects although small amounts are also theoretically available⁵³. Due to bad experience with the public sector lending to public entities is very limited and restricted. CAC Bank was able to get a good share of the retail business to governmental employees and is planning to enlarge this segment significantly. The loan portfolio increased from 2005 to 2006 by 64% (gross) and 76% (net).

CAC Bank is holding 24,659 current accounts, 1,957 savings accounts and 181 time deposits. Figures for loan accounts were not available. The bank was able to increase its deposits by almost 130% in 2006 (US\$ 242 million) compared to 2005 (US\$ 109 million). Overall assets doubled in the same period.

CAC Bank is regularly approached by the government to support fighting unemployment through not yet clearly defined initiatives. Financial support was promised by the government already in 2006; however it is not allocated yet. For these initiatives CAC Bank is supposed to work closely together with the Al-Saleh Program (for more information about Al-Saleh Program see chapter 3). As CAC Bank was asked to start even without governmental financing they introduced around 500 offices in Sana'a and Taiz under the CAC Bank corporate design. These offices are staffed with university graduates and offer limited services as salary disbursements and payment facilities for electricity, water and Yemen Mobile phone bills. The office staff is encouraged to acquire further business opportunities as selling prepaid mobile cards.

Loan Loss Provisioning Policy: According to CBY policy. The auditors' report 2006 shows performing and non performing loans provisions amounting to US\$ 11.3 million and uncollected interest to US\$ 3.7 million. The overall amount reaches 16% of the gross portfolio

Only three clients account for more than 85% of the provisions.

Non Performing Loans: The auditors' report 2006⁵⁴ shows NPL and advances amounting to US\$ 25.6 million (slight decrease compared to 2005, reaching 33% of outstanding portfolio (net) or 28% of the gross loans. Considering the growth in loan portfolio, the percentage of NPL decreased by 4%. The overall amount of NPL decreased between 2005 and 2006 by 1%.

According to CBY regulation and the Council of Ministers Resolution No. 145 of 2006, it was agreed that the Ministry of Finance will buy the agricultural loans portfolio of the CAC Bank. Regarding the bank's financial statements the portfolio amounts to YR 5,086,132,327. The Ministry of Finance will issue government bonds of the same amount with interest rate and maturity dates to be agreed upon between Ministry of Finance and the banks. CAC will manage and follow up the collection of these loans, and will transfer amounts collected to the Ministry of Finance. In addition, it was agreed that foreign long-term debts as of 31 December 2005, that were given to CAC by the Ministry of

⁵³ No figures available for average loan size for big loans, or any estimation of the amount of active clients in the MSE segment as well as loan sizes and application.

⁵⁴ The Balance Sheet is only available in Arabic and in paper copy.

Finance, will be transferred back to the Ministry of Finance as part of the settlement of the agricultural loans.⁵⁵

MSE related activities and strategy: CAC Bank used to give small loans to small farms and fisheries a couple of years ago. Due to bad experience and low repayment this product was stopped completely. They do not plan to venture into the MSE segment unless the government will support them with additional funding. In the retail business, CAC Bank has a remarkable share of consumption loans mainly to governmental employees. Currently they have around 36,000 active accounts in consumer loans with an outstanding amount of around US\$ 30 million with an average outstanding amount of US\$ 830. There are no estimates, how many consumer loans are used for income generation activities.

MSE related products: In theory loans with small amounts are available for any kind of commercial needs. No details or statistics could be obtained for this segment. Consumer loans can be obtained up to ten times the net salary, with a maximum duration of two years and guaranteed by payroll deduction, supported by a guarantee letter of the employer and two personal guarantees of colleagues of the same entity.

Current products: CAC Bank offers mainly short term loans for commercial activities and agriculture, mainly trade finance and investments, L/C and L/G as well as consumer loans. All lending activities are according to conventional lending. On the liability side they offer current accounts with ATM cards and a separate card to be used for points of sale. Additionally they started to issue VISA Electron for their current account holders. National and international money transfers are also offered.

Housing Credit Bank (HCB)

The Housing Credit Bank (HCB) was founded in 1978 by the Yemeni Government to allocate finance for the construction of houses. The government still holds a share of roughly 90% in the HCB; the other 10% are distributed among private shareholders.

The HCB has two branches in Sana'a and Hodeidah and according to the Central Bank it is not very active in the market. Currently it provides very few loans to governmental employees for house improvement.

By a presidential decision HCB is to be merged with CAC Bank. So far no procedures for implementation of the decision are defined.

Current product: The maximum loan amount of YR 300,000 was set in 1978 and was never adjusted. In 1978, YR 300,000 had a value of US\$ 67,000; today it equals to just US\$ 1,500. The initial capital was YR 300 million with a value in 1978 of US\$ 67 million. The capital was never increased and today it represents around US\$ 1.5 million.

⁵⁵ Source: Annual Report 2005 (in 09/2007 the Annual Report 2006 has not been available. So far only the balance sheet of 2006 has been published)

Yemen Post and Postal Savings Corporation (PPSC)

The Yemen Post and Postal Savings Corporation (PPSC)⁵⁶ was established in 1991 after the unification of the postal services of South and North Yemen. It is a deposit taking institution offering additional financial services. With its savings product it targets mainly middle class customers. A big share of its current account holders are the recipients of the social benefit payments of the Social Welfare Fund.

The PPSC is fully governmental and governed by the Ministry of Communication. It has 240 fully computerized branches with online facilities; nearly half are in rural areas. PPSC is considered to be the fourth best managed postal services institution in the region after Morocco, Algeria and Tunisia.

They have 290,000 savings accounts, with an overall portfolio of US\$ 70 million (average amount US\$ 240). Additionally, they were able to attract several governmental entities as customers to use the PPSC for the payment of salaries. In some governorates all governmental salaries are paid through PPSC. Likewise, all governmental pension payments (194,000) are channeled through the PPSC as well as the social benefit payments of the Social Welfare Fund (SWF) (around 600,000 beneficiaries receive payments every three months).

All recipients are obliged to hold an account with PPSC although beneficiaries of the SWF have to withdraw their money in one sum at the day of disbursement.

Currently PPSC invests roughly 50% of its deposits in treasury bills. The rest is invested or deposited in commercial banks in Yemen or in Yemen Mobile and Teleyemen.⁵⁷ These investments are made under supervision and with the approval of the CBY.

MSE related activities and strategy: PPSC is in discussion with the SFD through international consultants⁵⁸ about the possibility to link Microfinance services to already existing delivery channels, such as the branch network of the PPSC. It has the broadest outreach in the country, covering large parts of the rural areas. Additionally it seems that it has a well developed computer platform which would be able to deal with the additional services or which can be integrated into the existing Management Information System (MIS) of an MFI.

Nevertheless the consultant's impression was that the PPSC is not fully convinced about any form of potential partnership for microfinance services or its benefits for PPSC. It was stressed, that PPSC will not accept to take any risks related to the MF operations, and they will only serve as a distribution channel. Venturing into a partnership is not first priority as they are foremost looking into extending their network, introducing additional services and preparing themselves to face an increasing customer base in a professional manner.

Current products: Savings accounts, current accounts, ATM (planned for end of 2007), national money transfer as well as international money transfer. The international

⁵⁶ As the PPSC is only a deposit taking institution it is not listed in the table of crediting banks in chapter 2.1.

⁵⁷ Governmental Telecommunication entities

⁵⁸ ACCION International and Microserve, for more information see presentation „Linking Microfinance Services to Alternate Delivery Channels“

transfers will be offered through Western Union and will start at the beginning of 2008. Additionally they facilitate payments of water, electricity and Yemen mobile bills.

Private Banks

Tadhamon Islamic Bank (TIB)

The Tadhamon Islamic Bank (TIIB) is the largest Yemeni Bank according to the total assets. It is an Islamic Bank, founded according to the investment law in 1996. It is regarded as one of the fastest growing banks in Yemen with one of the highest degrees of popularity in the country. It is owned by one of Yemen's biggest business families with diversified and widespread activities.

Outreach is still limited to the main cities. Tadhamon has 13 branches in Sana'a, Taiz, Aden, Hodeidah and Mukalla (operational in 09/2007).

Tadhamon had around 160,000 accounts at the end of 2006. Its main activities include corporate and investment banking and retail banking. The savings and time deposits amount to US\$ 600 million and the loan portfolio⁵⁹ to US\$ 450 million, accounting of 75% of savings and time deposits. The loan portfolio increased from 2005 to 2006 by 35% (gross) and 39% (net).

Loan Loss Provisioning Policy: According to CBY regulation.

Non Performing Loans: The portfolio for Morabaha contracts (68% of the loan portfolio) stands at US\$ 305 million, with US\$ 12,1 Mio NPL (4%).

Based on the increase of the gross portfolio for Morabaha investments (67% of the overall portfolio) the percentage of NPL increased from 9,0% in 2005 to 12,2% in 2006, the absolute amount of NPL for Morabaha investments increased between 2005 and 2006 by 36%.

MSE related activities and strategy: As the first commercial bank in Yemen Tadhamon established a separate unit for its MSE operations at the end of 2006. The unit is regarded as a commercial investment by Tadhamon and is supervised by a committee of three high ranking members of the management (Deputy General Manager, Assistant of the General Manager and the Director of the Foreign Investment Department). The unit was endowed with US\$ 1,5 million equity from Tadhamon. Legally it is part of the bank but it has its own organizational structure. For example the unit has its own loan tracking system, accounting system, human resource policy and will mainly operate out of separate branches. The unit is organized as an independent profit center. It became operational the end of 2006. Before that Tadhamon had a pilot branch in Taiz offering MSE loans, but it did not succeed. Break even is planned for 2010/2011.

The offered loan products are similar to the MFIs in Yemen, although no saving schemes are provided up to now. The growth of the unit is quite slow but according to the business plan. However, since start of operations it was able to build up a customer base of 600 small businesses (1.000 are planned until the end of the year), thereof around 55%– 60% are women. The average loan size is US\$ 500. In 07/2007 they introduced consumer lending in the unit, restricted to 10% of the loan portfolio. Repayment is

⁵⁹ The loan portfolio comprises of Morabaha, Mudaraba, Muscharaka and Istisna'a products

100%. An Islamic insurance scheme (Takafa) is planned to be introduced to cover outstanding installments in case of non-payment (similar to residual debt insurance). Tadamon was able to attract several employees with experience in MF to set up this unit and to benefit of the experience of the MF-market. Still, lack of qualified staff is the biggest constraint in extending the MF operations and ensuring sustainability. Tadamon sees potential in the market as the segment is underserved and the risks are regarded as acceptable.

MSE related products: Through its MF-Unit Tadamon offers group loans for women according to the Grameen Model, individual (business and consumption) as well as seasonal loans. Loan amounts range from US\$ 200 to 1,000 for group lending and US\$ 250 to 2,500 for individual lending. Loan duration varies between one and 24 months. The price for loans varies between 15% flat for individual loans, 18% for group loans to 24% (or 2% per month) for seasonal loans.⁶⁰ Collateral is used like MFIs do accepted are commercial guarantee, pay roll deduction, gold as well as bank guarantee and personal guarantee of two colleagues from the same private company or governmental entity.

Current products: All lending products according to Islamic banking for trade finance, investments and consumption as well as L/C and LG. On the liability side current accounts, savings, time deposits as well as ATMs and credit cards are offered. National and international money transfers are facilitated by the bank.

International Bank of Yemen (IBY)

In terms of assets International Bank of Yemen (IBY) is the second biggest Yemeni bank. It was established in 1979 by several Yemeni business men and two international shareholders (Bank of America (20%) and the National Commercial Bank (NCB) of Saudi Arabia (Khaled Bin Salem Bin Mahfooz – 25%). Bank of America sold its shares to the Yemeni Shareholders in 1990. Currently the NCB holds 15%, the rest is distributed amongst 400 local shareholders.

Outreach is limited to the main cities in Yemen. As a fast growing bank IBY plans to expand its branch network to access new markets.

In lending operations IBY serves two main target groups: retail and corporate customers. IBYs definition of corporate is divided into three categories. Small businesses have an annual turnover of US\$ 250,000 onwards; medium sized businesses are considered to have an average annual turnover of US\$ 2.5 million and large businesses have an annual turnover of more than US\$ 5 million Corporate loans start with US\$ 10,000 and should not exceed 20% of the yearly income of the customer. On exceptional base the bank provides loans less than US\$ 10,000 for well known customers. At the end of 2006 IBY had 300 corporate borrowers. There are no numbers available for loans less than US\$ 10,000. The loan portfolio increased from 2005 to 2006 by 31% (gross) and 31% (net).

⁶⁰ It should be mentioned that all interest rates given in this report are information provided by the banks and MFI. They do not contain costs like management fees, costs for disbursement and other costs. As the answers in the demand study show these additional costs are not made transparent to the customer and may increase the effective interest rates to 40% or even 60%.

At the end of 2006 IBY counted 6,000 retail accounts, including car loans. Loans are offered on the base of two personal guarantors and proof of regular salary, the loan amount is limited to ten net salaries. For cars the loan duration is between 4 – 5 years (used and new cars), for other purposes it is usually 2 – 3 years. Most of the retail clients are governmental employees, although IBY offers retail loans also to employees of private companies.⁶¹

Loan Loss Provisioning Policy: According to CBY standards. The auditors' report 2006 shows performing and non-performing loans provisions amounting to US\$ 32 million and uncollected interest to US\$ 6 million. The overall amount reaches 27% of the gross portfolio.

Non Performing Loans: The auditors' report 2006 shows NPL and advances amounting to US\$ 86.2 million, reaching 83% of outstanding portfolio (net) or 61% of the gross loans. Based on the increase of the gross portfolio the percentage of NPL increased slightly from 59% in 2005 to 61% in 2006, the absolute amount of NPL increased between 2005 and 2006 by 34%.

MSE related activities and strategy: The management of IBY stated that they want to develop a strategy how to tap the MSE market. They have no clear idea how to approach the segment and which part of the target group they want to focus on. Most probably it will be on a small scale only, aiming to offer additional services and products to clients already being well known to the bank. Two main ideas expressed were, clients wanting to exchange their assets (e.g. hotels and restaurants needing new furniture or fridges) or supporting existing clients through indirect services as bank guarantees. Before starting to serve the MSEs they want to develop a scoring system for the MSE lending operations and doing a thorough market research. Being successful in the retail business they want to transfer their good experience to the MSE lending business.

Additionally YBI will be involved through its General Manager in Al-Amal Bank, a MFI being operational the end of the year. The General Manager of YBI is the advisor to the Chairman of Al-Amal. For more information about Al-Amal see Annex 3.

MSE related products: It is not tracked how many of the retail loans are used for income generating purposes. Loans are offered on the base of two personal guarantors and proof of regular salary, the loan amount is limited to ten net salaries. An interest rate of 19% declining is charged on loans in YR, 10% declining for loans in USD.⁶² On a very small scale IBY offers loans less than US\$ 10,000 to well known customers. Commercial guarantees (from the same type of business) or real estate are required as collateral for these kind of loans.

Current products: IBY offers a broad range of financial services. Loans for trade activities, working capital and assets as well as retail, L/Cs and L/Gs. Current accounts, savings accounts including savings accounts for children (less minimum balance required) and time deposits are products on the liability side. The bank has an ATM network and around 600 points of sale in the country, also issuing cards (Master and American

⁶¹ Before IBY offers retail loans the banks signs usually an agreement between the bank and the customer's company (respectively the employer).

⁶² Most loans in Yemen are calculated as annuity loans. All interest rates provided by banks are nominal interest rates.

Express, will offer VISA soon) as debit or credit cards, depending on the client. Phone banking and SMS services are also available.

Saba Islamic Bank

Saba Islamic Bank, a private bank was established in 1997. The Dubai Islamic Banks holds 15%, 10% of the shares are hold by the Islamic Corporation for the Development of the Private Sector (ICD), a Development Bank based in Jeddah. The rest is distributed among 6,400 shareholders. Saba Bank works according Islamic principles and offers the whole range of Islamic products. Saba Bank is present in all governorates, having 14 branches.

Saba Bank signed an agreement with ICD for US\$ 3.5 million for lending to MSE, although the minimum loan size under this agreement is US\$ 75,000. The purpose of the loans is divided into 40% for trade, 30% for retail, 20% for real estate and around 10% for fixed assets and working capital. Saba Bank did not reveal any account numbers as they are regarded as confidential. The loan portfolio decreased from 2005 to 2006 by 9.5% (gross) and 11.5% (net).

Loan Loss Provisioning Policy: According to CBY standards. In 07/2007 US\$ 9 million provisions were budgeted.

Non Performing Loans: The portfolio for Morabaha contracts (98% of the loan portfolio) stands at US\$ 94 million, with US\$ 4.8 Mio NPL (4.3%). Based on the decrease of the gross portfolio of Morabaha contracts the percentage of NPL increased from 1,9% in 2005 to 4,5% in 2006. The absolute amount of NPL did more than double between 2005 and 2006 (220%).

MSE related activities and strategy: Saba Bank introduced a special department in all branches for MSE operations, but it has assigned only 5 loan officers to MSE activities. Small loans start at US\$ 1,000 with no upper limit. There were no statistics available about the number of customers in the MSE segment or for the use of the loans. In theory MSE loans can be used for assets, working capital or consumption.

For the future they plan to use simplified procedures and reduced guarantees for the MSE products, however, the strategy was kept very vague. Nevertheless they plan a “permanent fair” for start ups active in handicrafts mainly. Saba Bank is already in negotiations for purchasing a piece of land in the outskirts of Sana’a and will provide the clients with all facilities they need including finance.

Customers asking for less than US\$ 1,000 are sent to the Social Fund for Sustainable Development, an MFI supported through a commercial loan by Saba Bank. The loan was facilitated and guaranteed through the reputation of the founders of SFSD. Saba Bank expressed their willingness for continuous support for SFSD. For more details on SFSD see chapter 3.

MSE related product: Small loans start at US\$ 1,000 with no upper limit. Loans can be denominated in YR or in USD, the interest rate for loans in YR is around 10% to 11%, for loans in US\$ 2% less.⁶³ There is no limitation of the purpose; it can be for assets,

⁶³ An interest rate of 8% is surprisingly low for a country like Yemen. This low interest rate is an indication that there are extra costs like disbursement fees and study charges. As the demand side study revealed

working capital and consumption. Loan duration can go up to 36 months for loans in YR, up to five years for US\$ loans. Accepted guarantees are real estate, commercial guarantee and payroll deduction (for governmental employees only)

Current products: Saba Bank offers the whole range of banking products. Islamic banking products for trade, retail, housing and assets including L/Cs and L/G. In addition they offer current accounts, savings and time deposits as well as credit cards.

Yemen Commercial Bank (YCB)

Yemen Commercial Bank (YCB) is fully Yemeni owned, with the Yemen Petroleum Company being one of the shareholders with 10%. The beginning of 2007 they had 8 branches, in August 2007 the number increased to 13 and they plan to open 15 more branches. Outreach is concentrated on the main towns in Yemen as Sana'a, Aden, Mukalla, Dhamar, Ibb and Hodeidah. Currently they employ 370 staff.

Currently corporate loans account for 80% of the assets, whereas they want to increase the retail share of 20% significantly. The corporate loans segment is saturated compared to the retail market where they see a lot of potential. The loan portfolio increased from 2005 to 2006 by 15% (gross) and 29% (net).

YCB managed to attract around 10,000 corporate customers. The corporate portfolio consists mainly of trade finance (60% of the corporate portfolio) and of bridge loans, financing the period between delivery to and payment by the governmental sector. Only few loans are used for assets. The loan duration is short term even for asset financing credits do not exceed one year.

The interest rate for the lending business is according to the interest rate of the treasury bills, which is 16% at the moment. The spread between deposits and credits is around 2% however interest rates may depend on the customer. YCB invests a big share of its deposits in treasury bills as they are a secure investment.

Guarantees are usually required for all credits except for huge loans especially in trade finance. For these loans the cash flow of the business, combined with the integrity and reputation of the person and his long standing credit history with the bank is regarded as sufficient. The bank does not require real estate as collateral for trade finance as the loan amount usually exceeds the value of the mortgage by several million USD. For other or smaller loans banks accepts real estate or an individual guarantee of a person the bank knows well.

In the retail business YCB serves at present 20.000 clients, concentrating on the employees of the bigger and well reputable private companies. The client has to have his salary account with the bank. Depending on the company he is working for he can receive a loan up to 25 times of his salary. The purpose of the loan is asked in the application but it is not followed up except with car loans. In case of car financing the car will be registered with the bank until the last installment is paid. Insurance of the car is compulsory. According to the estimation of the management most loans are used for

these hidden costs increase the effective interest rate significantly to 40% or even 60%. The consultant has experienced this pricing strategy in all banks in Yemen.

housing purposes. The retail loans are guaranteed either by one employee of the same company or by the employer through a check over the full amount. ⁶⁴

Apart from offering the usual products as call accounts, ATM, VISA and Tele banking, YCB offers a credit card under its own name with a revolving credit line, available also for non account holders. The card can be used at their ATMs and points of sale, the debts can be paid directly at the bank. Another innovative product is the Cashu Card only for payments in the internet. They also run the only mobile ATM machine (on a small truck) in the country.

Loan Loss Provisioning Policy: According to CBY standards. The auditors' report 2006 shows performing and non performing loans provisions amounting to US\$ 26 million and uncollected interest to US\$ 26 million The overall amount reaches 44% of the gross portfolio.

Non Performing Loans: The auditors' report for 2006 shows NPL and advances amounting to US\$ 32 million, reaching nearly 63% of the outstanding portfolio (net) or 31% of the gross loans. Based on the increase of the gross portfolio the percentage of NPL decreased from 42% in 2005 to 31% in 2006. The absolute amount of NPL decreased between 2005 and 2006 by 22%.

MSE related activities and strategy: So far CBY has limited experience in MSE lending, although they give loans of YR 1 million (US\$ 5,000) or less to business entities they know already for specific purposes. The management of CBY agreed that MSE lending is an effective tool to attract new customers and that it proved to be successful in other countries and that it has great benefits for the lending institution and the economy in general. However they have no plan to venture deeper into MSE lending at the moment.

MSE related products: CBY offers a corporate loan product of less than US\$ 5,000 and has consumer loans with no minimum limit and up to 25 times the salary, guaranteed by one colleague or the employer by check.

Current products: Conventional loan products for trade and assets, bridge finance, consumer loans as well as L/C and L/G. Current accounts and savings including time deposits, ATM cards, credit cards (VISA and own product as well as card only for the use in the internet) and a mobile ATM on a truck.

Yemen Kuwait Bank for Trade and Investment (YKB)

Yemen Kuwait Bank for Trade and Investment (YKB) was established by Kuwaiti investors. By their own decision they sold their shares in 1989 to Yemeni investors. Today the main shareholders are the YBRD, the Social Security Fund, and four important business families. The rest of the shares are well distributed. YKB outreach is concentrated on the main governorates, with 11 branches Sana'a, Taiz, Aden, Mukalla and Ibb.

YKB was the first bank to work closely with SFD. In 1995, before SFD was founded, the government discussed with YKB and YCB to coordinate the donor money allocated for

⁶⁴ It is unclear if this widely used custom violates Yemeni law. However it should be mentioned that most of the banks and MFI do not use the cheque as a kind of collateral but as a method to ensure punctual payment. In this case however the check is used as collateral.

the financial sector. With the establishment of SFD this idea was abandoned. Now SFD is in charge to manage the donor funds.

Overdraft loans account for nearly 80% of the loan portfolio, the remaining amount is mainly for corporate and individual loans. Mortgage with coverage of 150% and commercial guarantees with coverage between 125% and 140%, in exceptional cases 100% are accepted as collateral.

The outstanding gross portfolio mid of August 2007 amounts to 75 million The percentage for retail is very low as this product was introduced recently, targeting the upper segment of the employees in the private sector, guaranteed by two staff of the same company. Car loans are also available for up to 5 years, available for customers with a minimum income of US\$ 750. Mid of August 2007 YKB had 976 loan accounts (including the retail loans) and 316 overdrafts.

At present YKB has in total 18,605 active clients (or 25,000 clients if unused accounts are included). Most clients use current accounts (around 11,000) and savings and time deposit accounts (around 7,500) with an outstanding portfolio of US\$ 195 million Up to know they issued around 500 credit cards. The loan portfolio decreased from to 2005 to 2006 by 6% (gross) and 10% (net).

National money transfer is available from account to account within the banks. At the moment YKB is in negotiations with Western Union to facilitate national money transfer through Western Union, from account to recipient, processed through phone banking.

Loan Loss Provisioning Policy: According to CBY standards. The auditors' report 2006 shows performing and non performing loans provisions amounting to US\$ 8.7 million and uncollected interest to US\$ 0.3 million The overall amount reaches 14% of the gross portfolio.

Non Performing Loans: The auditors' report for 2006 shows NPL and advances amounting to US\$ 22 million, reaching 37% of outstanding portfolio (net) or 35% of the gross loans.

Based on the decrease of the gross portfolio the percentage of NPL increased from 10% in 2005 to 35% in 2006 The absolute amount of NPL increased more than threefold between 2005 and 2006 by 328%.

MSE related activities and strategy: According to their definition YKB does not do any MF lending⁶⁵ so far but they plan to do so. They are in discussion with SFD to downscale their operation with the technical assistance of SFD and Planet Finance⁶⁶. In general, SFD confirmed to support YKB in their efforts. Additionally they have sent a letter to Mr. Al Arhabi, Managing Director of SFD and Minister for Planning and International Cooperation asking for support to realize their MF strategy.

YKB has allocated the required funds and is waiting for SFD to do the next step.

⁶⁵ Loans of US\$ 2,500 to US\$ 5,000 are regarded as MSE finance in Yemen. YKB has a different definition and considers these loans as Microfinance.

⁶⁶ Planet Finance is a French NGO specialized in trainings for MFIs on a commercial base. The TA and trainings of Planet Finance will be paid by YKB. Additionally SFD will open its training courses for staff of YKB.

The MF strategy of YKB is targeting a loan size between US\$ 2,500 and 5,000 for commercial purposes only. The interest rate and loan duration are not set yet, but will be around 18% or-20% declining. The duration may not exceed one year as for corporate loans.

Which kind of guarantees will be accepted for MSE is not decided yet. One possibility are group guarantees as they plan to apply a kind of group lending whereas colleagues from the same sector will guarantee the loan, mainly members of associations or committees (e.g. fishermen). Alternatively the association or committee can issue a “Letter of Guarantee” for the loan. There are no plans for individual loans so far.

After introduction of the lending activities they also plan to provide savings products suitable for MF. Insurance available for existing operations, might be applied for MF as well.

YKB has already allocated some resources for the MF operations. Two loan officers were sent to India for training. They want to start slowly with not more than 2 – 3 people. YKB plans to open offices in areas where a lot of beneficiaries of SFD can be found. The offices will be able to offer all banking transaction, but will not be entitled to do loan approvals)

YKB does not expect nor want profits out of its MF operations. The social aspect to develop the economy is more important. Additionally it will be a very small portion of their portfolio. Nevertheless the bank considers small loans as less risky than corporate loans, especially as the risk is more diversified.

MSE related products: Retail loans focusing on the upper segment of the market.

Current products: Loans and overdrafts for trade, retail and assets as well as L/Cs and L/G. On the liability side they offer current accounts, savings accounts including some innovative savings products and time deposits. ATM cards and cards for point of sales as well as VISA and Master Card. They are in process of becoming an associate with VISA cards enabling YKB to issue their own credit cards. National and international money transfer is available, either account to account or through Western Union. It is planned to offer national transfers through Western Union from account to recipient via phone banking.

Shamil Bank of Yemen and Bahrain

Shamil Bank of Yemen and Bahrain (Islamic Bank) is owned by Shamil Bank of Bahrain (24%) and Saudi and Yemeni Business People. It was established in 2002 as an Islamic banking institution. It is one of the smaller banks in Yemen according the overall assets. Its outreach is limited to three branches in Sana’a and one branch each in Aden and Hodeidah.

The overall loan portfolio of the bank consists mainly of Morabaha and Muscharaka investments, accounting for 97% of the portfolio. The loan portfolio decreased from to 2005 to 2006 by 3% (gross) and 6% (net) for these two products.

MSE related activities and strategy: The bank started to discuss the set up of a specialized unit for MSE lending activities in June 2007 and the first customers were served in July 2007. Until the end of August 2007 they disbursed 7 loans. In the experimental phase of 3 – 6 months MSE loans are only available at Sana'a main branch. During the experimental phase 6 customers per month are planned.

At the end of the experimental phase Shamil Bank will decide if the MSE lending activities shall be transferred to a separate unit or if they stay integrated in the corporate loan division. Independent from the decision, MSE lending will continue in one of the two possible institutional set-ups. In case the results of the experimental phase are satisfying for the management, all branches will be providing MSE services. There are also discussions about a special program for women according to the success of the MSE lending activities.

In providing MSE loans Shamil Banks main aim is to offer additional services and not to expand or to compete with existing suppliers of microfinance in the market.

Loan Loss Provisioning Policy: According to CBY regulation. The ratio for provisions for Murabaha, Mudarabah and Musharaka investments stands at 3.5%.

Non Performing Loans: The amount of NPL is not stated in the Annual Report.

MSE related products: Individual loan product (Morabaha) with a loan range between US\$ 1,000 and 2,500. Loan duration is limited to one year, the price for the loan is set by the General Manager at 15%, but this price is under discussion as the responsible people for the MSE operations are convinced that they can offer the loans for much less. Corporate banking operations charge 9.75%. Commercial guarantee, payroll deduction (currently only for governmental employees), real estate and gold are accepted as guarantees. The guarantees have to cover 120% of the loan amount.

Current products: All lending products according to Islamic banking for trade finance and investments as well as L/C and LG. On the liability side current accounts, savings, time deposits as well as ATMs and credit cards are offered. National and international money transfers are facilitated by the bank.

Islamic Bank of Yemen

Islamic Bank of Yemen is one of the smaller private banks in Yemen. The bank was established in 1996 as the first Islamic Bank in Yemen, following the banking principles of the Shari'a. Its shareholders are Yemeni business people mainly from the construction sector and several Yemeni institutions and Arab banks.⁶⁷ The bank has 5 branches in the major cities.

Basically they serve the corporate sector with Islamic finance products. The main target groups are medium sized companies, traders (including importers) and the branches of foreign companies in Yemen. The minimum loan amount is US\$ 2,500. Morabaha is the most requested product (95% of the portfolio), as the predominant purpose is financing trade activities. Very few investments are directed into assets. Currently they have 176

⁶⁷ General Authority for Pension and Social Security, Ministry of Religious Endowments, Islamic Development Bank, Bahrain Islamic Bank, Jordan Islamic Bank and Qatar International Islamic Bank (holding together 16%)

corporate loan clients, with an average loan size of outstanding US\$ 29,225. Real estate, commercial guarantees, deposits or bank guarantees as well as gold are accepted as collateral. Requested coverage is 150% for real estate, 130% for gold and 100% for commercial guarantees (if the guarantor agrees and his creditworthiness is sufficient⁶⁸) and deposits or bank guarantees. The loan portfolio decreased from 2005 to 2006 by 10% (gross) and 12% (net) for the Morabaha product.

On the liability side, the Islamic Bank holds 55,532 accounts, whereas 18,295 are current account holders, 22,491 have a savings account and 14,746 hold a time deposit account.

Loan Loss Provisioning Policy: According to CBY standards

Non Performing Loans: The portfolio for Morabaha contracts (97% of the loan portfolio) stands at US\$ 30 million, with US\$ 14.3 Mio NPL (48%). The bank considers loans with late installments of 91 days and more as non-performing loans in case no settlement has been reached with client.⁶⁹

Based on the decrease in Morabaha contracts the percentage of NPL for Morabaha increased from 11% in 2005 slightly to 14% in 2006. The absolute amount of NPL for Morabaha contracts increased between 2005 and 2006 by 30%.

MSE related activities and strategy: Currently they do not offer MSE lending, nevertheless in theory loans from US\$ 2,500 onwards are available. Housing improvement and consumption loans are also provided. Currently the Islamic Bank serves 1297 clients in the retail segment. Just recently they started to discuss the possibility to offer services for MSEs. The bank considers the biggest problem insufficient guarantees from MSEs. So far for small loans the bank asks for the same guarantees as for corporate loans (guarantee of a main client of the bank, deposits or real estate). However, it is understood by the management, that for MSE products procedures and requirements for guarantees have to be revised and adjusted.

MSE related products: The bank offers corporate loans starting from US\$ 2,500 onwards, as well as housing improvement and consumption loans.

Current Products: Different loan products according to Islamic principles for trade (including imports), assets and working capital. L/Cs are also offered. As a fully fledged bank Islamic Bank also offers current and savings accounts as well as time deposits. National and international money transfers are readily available, however, for account holders only. The bank will start to cooperate with ez-remit, an international money transfer company (London based). The comparative advantage of ez-remit is the door-to-door service they offer and seemingly competitive fees, charging less than Western Union. ATM services will be started the end of the year as well as issuing credit cards.

Yemen Gulf Bank (YGB)

⁶⁸ However, it should be mentioned that the analysis of the financial creditworthiness of an entity does not always follow international best standards. Most clients are rated according to the value of collateral or assets and regarding to social standing instead of cash flow and other financial criteria.

⁶⁹ According to the requirements of the Central Bank, loans overdue more than 180 days have to be classified as bad debts. The banks have to make provisions of 100% on these loans.

Yemen Gulf Bank (YGB) was founded in 2001 by several Yemeni businesspeople and two investors from the Gulf as a fully fledged commercial bank, licensed, supervised and regulated by the Central Bank of Yemen.

MSE related activities and strategy: YGB is not active in MSE lending and has no plans to enter this segment. Its current lending activities are restricted to longstanding clients also in the corporate segment. The restriction will be lifted as soon as a planned increase of equity is concluded.

Current Products: It services mainly corporate clients offering trade finance and credit lines as well as L/C and L/G. For corporate and private customers they offer current account services including Credit Cards and Internet/Tele/SMS Banking.

Calyon (formerly known as Crédit Agricole Indosuez)

Calyon is the corporate and investment bank of group Credit Agricole, France biggest bank and one of the greatest financial groups worldwide; it is the only bank in Yemen with an AA rating. Calyon is still better known as Crédit Agricole Indosuez. Calyon Yemen Branch (170 people) has been an important player in the corporate and retail banking sectors for the past 30 years. The main focus is on providing financial services to large Yemeni corporations and to local subsidiaries of international companies. The bank is also running a retail banking activity mainly dedicated to upper class customers. Calyon Yemen's network comprises of five branches in the main cities, namely Sana'a, Aden, Hodeidah, Mukalla and Taiz.

MSE related activities and strategy: Calyon has no plans to venture into the MSE lending segment. *Current products:* Corporate financial services as trade finance and project finance, short term working capital facilities as well as payment transactions and foreign exchange services for their clients. Retail services comprise mainly deposits and classical banking products for private customers.

Qatar National Bank (QNB)

The QNB is part of an international network with the mother company in the country Qatar. It started providing services to customers in September 2007. So far the bank is in the process to build up a credit portfolio and a customer base.

The management wants to focus on corporate clients and project finance. It has mentioned a package of international projects to be invested in Yemen worth 7.1 billion US\$ and financed by the Gulf States as one of the reasons why Qatar National Bank has founded a bank in Yemen.

MSE related activities and strategy: At the moment QNB does not plan to provide services to the MSE market.

Current products: Corporate financial services as trade finance and project finance, short term working capital facilities as well as payment transactions and foreign exchange services for their clients.

Annex 3: Information on Microfinance Institutions in Yemen

The National Microfinance Foundation (NMF)

The National Microfinance Foundation (NMF) is regarded as the largest MFI in Yemen. It was founded in 2002 as a project of SFD, one of the initiators was Mr. Abdulkarim Al-Arhabi, the Managing Director of SFD and at that time Minister of Social Affairs and Planning, now Minister for Planning and International Cooperation. In 2004 it was transferred into a NGO as an initiative of several private people and three institutions (SFD, Yemen Gulf Bank and YBRD). All founders except the YBRD are represented in the Board. The NGO is registered with the Ministry of Social Affairs and Labor.

The founders contributed YR 20 million (US\$ 100,000) to the equity of the NMF in 2004. Additionally NMF was able to secure a grant from AgFund of YR 8 million (US\$ 40,000) at the beginning of the operation with the consent to transfer the amount to the equity after one year if the investment proves successful.

In 2006 NMF decided to take a loan from SFD to expand its operations and to be able to serve the increasing demand. The loan amount is YR 49 Mio (US\$ 245,000) with a duration of 36 months and an interest rate of 7 percent flat per year.

In 2004, when the NMF was transferred from a dependent project of SFD to an independent NGO, SFD covered the operational costs for the transition period. It was a non-recurring subsidy. Since 2005 the operational costs have to be covered by the MFI.

NMF has the largest regional outreach of any of the MFIs in Yemen with nine branches in eight governorates and also the largest customer base with currently 8,500 active borrowers. It targets predominantly women following its mission to support the empowerment of women. Client base increased by 7 percent since the beginning of 2005, with a peak in mid 2006 (increase from 2005 by 22 percent). The outstanding active portfolio increased by 17 percent in the same period with a peak in mid of 2006. The decrease of clients and portfolio was due to operational problems that NMF faced because of the introduction of an IT system.

NMF provides group lending and individual loan products, seasonal loans as well as compulsory savings and life insurance (= residual debt insurance). The client is able to choose between a conventional loan product and Morabaha.

The minimum loan amount is YR 5,000 (US\$ 25), the maximum loan amount is YR 250,000 (US\$ 1,250). However, the average loan amount is US\$ 90 with a duration between 4 and 12 months. The price charged for loans is 24 percent flat per year resp. 2 percent per month.

The loans are supposed to be used for income generating activities as handicraft and small scale production, small grocery shops and service. In rural areas loans are often given for livestock. Applications for consumption purposes are also accepted as long as the investment improves the living conditions of the household (e.g. fridge, washing machine, TV et al.). They also foster housing improvement through their lending.

Loan applications are processed through the loan officers, who constitute more than 50 percent of the staff. The loan decision is made by the loan officer.⁷⁰

Before the first approval and disbursement of loans in a group, the group has to go through 3 – 4 weeks of training; this includes regular attendance at the weekly meetings, loan awareness and education and compulsory saving at each meeting. Repeated loans can be processed and disbursed within a day. Apart from the disbursement of the loan, the client does not have to come to the branch. The instalments are collected during the group meetings.

For individual loans NMF accepts commercial guarantees and payroll deduction. In Sana'a branch they started to accept gold in 07/2007 as a pilot scheme.

Strategically, the main focus lies currently on the implementation of an up-to-date IT system. Other strategic issues are on hold so far until implementation is completed successfully.

The repayment rate amounts to currently 96 percent. NMF makes provisions of 2 percent calculated on the basis of the outstanding portfolio. The current amount of provisions is YR 11 million. However 7.2 percent of the 7.8 percent of Loan Loss Provisions (resp. YR 10 Mio of non performing loans) were caused by one loan officer.

Table 17. National Microfinance Foundation: Key figures

Portfolio Quality	
Loan Loss Provision Ratio	7,8%
Repayment Rate	96%
PAR	12,37
Outreach Indicators	
Number of Active Loans	8.500
Active Portfolio (US\$)	765.000
Accumulated Loans since inception	33.941
Accumulated Portfolio (US\$)	5.000.000
Number of Depositors	11.240
Average Loan Size (US\$)	90
Average Deposit Size (US\$)	19
Number of Female Borrowers	8.400
Percentage of Female Borrowers	99
Number of Staff	87
Number of Branches	9
Number of Loan Officers	50
Loan Officers as Percentage of Total Staff	57
Productivity	
Number of Outstanding Loans per Loan Officer	170
Average Loan Portfolio per Credit Officer	15.500

⁷⁰ The management of NMF was proud to stress the independence and responsibility of its Loan Officers. The management gave no information about any immediate checks or monitoring systems installed to prevent fraud and misuse of funds.

Hodeidah Microcredit Program

The Hodeidah Microcredit Program was established in 1997 as one of the first credit programs through an agreement between SFD and the Yemen Women Association. It is an independent NGO supervised by the association and SFD.

The program is well established in Hodeidah governorate with eight branches. Three are located in Hodeidah, the others are broadly spread in the governorate, serving the rural areas around Hodeidah. Recently the program of Beit Al Fakih was incorporated in the program. The formerly independent program now represents a branch of Hodeidah. Serving 4,075 borrowers it is the second largest MFI in Yemen. The client base increased constantly by 63 percent since the beginning of 2005 the outstanding active portfolio doubled in the same period.

Currently the program is financed through a loan from SFD for 7 percent flat per year.

Group, individual and seasonal loans are provided according to the Islamic principles. Loan sizes ranges between US\$ 50 and US\$ 1,250 with a maximum duration of 12 months. Fees constitute between 24 percent for loans of more than US\$ 100 and 36 percent for loans of less than US\$ 100. The usual guarantees are accepted, including pension check. A solidary service is available for the clients to cover the outstanding instalment in case of death or accident (= residual debt insurance). Expansion of the solidary service is planned.

The repayment rate is better than the national average with 98 percent, PAR amounts to 1 percent. Operational sustainability is stated with 73 percent.

Table 18. Hodeidah Microcredit Program: Key figures

Portfolio Quality	
Loan Loss Provision Ratio	3%
Repayment Rate	98
PAR	1,1
Outreach Indicators	
Number of Active Loans	4.075
Active Portfolio (US\$)	232.676
Accumulated Loans since inception	26.900
Accumulated Portfolio (US\$)	1.760.000
Number of Depositors	na
Average Loan Size (US\$)	162
Average Deposit Size (US\$)	na
Number of Female Borrowers	3.137
Percentage of Female Borrowers	77
Number of Staff	73
Number of Branches	8
Number of Loan Officers	38
Loan Officers as Percentage of Total Staff	52
Productivity	
Number of Outstanding Loans per Loan Officer	107
Average Loan Portfolio per Credit Officer (US\$)	6.123

Nama'a Microfinance Development Program

Nama'a was founded by the Islah Foundation in 2000. The Islah foundation is an NGO closely linked to the largest and most important opposition party in Yemen. Islah itself is active not only in Microfinance but runs activities in health issues, supporting handicapped people, poverty alleviation and religious studies.

At establishment the program was successful in attracting equity contribution from several donors. UNDP contributed US\$ 85,000, the Islah Foundation US\$ 100,000 and AgFund allocated US\$ 65,000.

Another source of funding used to be the Group of Development Projects, Kuwait granting the program a loan without interest, which was fully paid back. Negotiations are going on for a new loan of US\$ 125,000.

Currently the program is supervised by the chairman of the Islah Foundation. To gain more independence they are working on installing a board at the Program itself. They are not a SFD program, although they received US\$ 90,000 of finance from SFD and US\$ 10,000 to be used for TA. The loan is according to Islamic principles; the profit at the end of the year on this specific portfolio will be shared equally between the Program and SFD. Additionally they are offered to take part in the training program of SFD.

Outreach is still limited to a branch in Sana'a and Taiz. In Aden, they will open a new branch in January 2008. However, with a client base of 3,080 Nama'a is the third biggest MFI in Yemen with the largest percentage of male borrowers (68 percent). Nama'a has developed itself constantly since the end of 2005, doubling its portfolio and increasing the number of clients by two thirds.

The common products are offered: Individual loans for commercial projects according to Islamic principles, as well as group loans, ranging from US\$ 100 to US\$ 250. The loan sizes offered are low compared with the other MFIs. Although the average loan size of US\$ 125 is within the average of all MFIs. Up to one year of loan duration is offered, the fee for all loans is 20 percent. Savings were introduced in 2006 and are only available for group members. That means they are exclusively offered to women. Training how to enhance income generating activities are also provided by the program and facilitated by the loan officers. Gold, commercial and bank guarantees are accepted as collateral.

The repayment rate is calculated separately for Taiz (100 percent) and Sana'a (90 percent). The portfolio is almost equally distributed between Sana'a and Taiz. 88 loans are classified as non-performing with an outstanding amount of US\$ 6,500 (1,7 percent of the overall portfolio). Provisions are made for 5 percent of the overall portfolio.

Table 19. Nama'a Microfinance Development Program: Key figures

Portfolio Quality	
Loan Loss Provision Ratio	5%
Repayment Rate	95%
PAR	1,53
Outreach Indicators	
Number of Active Loans	3.080
Active Portfolio (US\$)	385.000
Accumulated Loans since inception	14.844
Accumulated Portfolio (US\$)	2.810.000
Number of Depositors	816
Average Loan Size (US\$)	125
Average Deposit Size (US\$)	13
Number of Female Borrowers	976
Percentage of Female Borrowers	32%
Number of Staff	30
Number of Branches	2
Number of Loan Officers	17
Loan Officers as Percentage of Total Staff	57%
Productivity	
Number of Outstanding Loans per Loan Officer	181
Average Loan Portfolio per Credit Officer	22.500

Aden Microfinance Foundation (AMF)

Aden Microfinance Foundation was reorganized in 2006. Three smaller programs were merged due to weak performance. One of the main reasons was loan officers misunderstanding their tasks and weak management. A team by SFD was sent for a field check. Upon approval by SFD AMF started to work with a new portfolio in March 2007 and improved management structures and hired new staff. Additionally, a new credit manual was introduced and loans for consumption are no longer available. The old portfolio is kept separately but is closely followed up. AMF managed to recover part of the old portfolio due to new management and follow up procedures but the performance of the old portfolio continues to be unsatisfactory. The foundation is financed by a loan of SFD with an interest rate of 10 percent.

AMF is the only MFI present in Aden, with five branches distributed within the city and one located in Lahj, ca. 50 km to the north of Aden. Including the old portfolio it has a customer base of 2,819 borrowers and 6,666 savers. Its clients are predominantly women. Before the consolidation the client base and portfolio was in constant decline, the portfolio and amount of clients peaking in the first quarter of 2006.⁷¹ The biggest outstanding portfolio was US\$ 665,000. According to the statement of SFD the consolidated institution looks promising to stabilize and to improve its performance.

AMF offers group loans and individual loans as well as savings. The loan size ranges between US\$ 50 and US\$ 1,000. Credits may have a duration of up to 12 months. The interest rate depends on the size of the loan and ranges between 18 percent and 36 percent. A residual debt insurance is planned.

⁷¹ The reason for less disbursement during the second period of 2006 and in 2007 is the consolidation and the merger after the problems with the quality of the portfolio in 2006.

Loans are exclusively given to income generating activities due to bad experience with consumption loans in the past. AMF targets mainly women through the group lending approach. The group as guarantee as well as commercial guarantee and payroll deduction are accepted as collateral.

The performance of the old portfolio is not satisfactory. Repayment rate is far less than average. However no data on the performance of the old portfolio was revealed by the MFI. As the new portfolio was only established a few months ago the current repayment rate of 100 percent has no significant meaning. No information was given regarding sustainability due to the restructuring process.

Table 20. Aden Microfinance Foundation: New portion of portfolio

Portfolio Quality	
Loan Loss Provision Ratio	N/A
Repayment Rate	New portfolio 100
PAR	N/A
Outreach Indicators	
Number of Active Loans	480
Active Portfolio (US\$)	55.090
Accumulated Loans since inception	480
Accumulated Portfolio (US\$)	57.525
Number of Depositors	480
Average Loan Size (US\$)	178
Average Deposit Size (US\$)	5
Number of Female Borrowers	468
Percentage of Female Borrowers	97.5
Number of Staff	74
Number of Branches	5
Number of Loan Officers	36
Loan Officers as Percentage of Total Staff	49
Productivity	
Number of Outstanding Loans per Loan Officer	Incl. old portfolio 78 New portfolio 13
Average Loan Portfolio per Credit Officer (US\$)	1.530

Al Awael Taiz

Al Awael was established in 2000 by the MicroStart Program of UNDP. As the first MF program it was transformed in 2004 into a private company with a Board of Shareholders and a Board of Directors, also with the support of UNDP.

When established Al Awael was endowed with a grant of UNDP for its lending activities. Recently it was able to get a credit facility from a commercial bank at a market interest rate interest of 14 percent.

Al Awael operates three branches in Taiz and serves 2,810 borrowers. Only women qualify for a loan from Al Awael. Since the end of 2005 Al Awael is serving a constant client base between 2,500 and 2,800, increasing the portfolio in the same period by 70 percent. The loans are used for income generation activities, according to the latest figures, 49 percent are used for manufacturing, 40 percent for trade and 11 percent for services.

The loan amounts range from YR 6,000 (US\$ 30) to 200,000 (US\$ 1,000), with a diversified interest rate between 28 percent and 36 percent. Loan duration can be up to one year. Repayment is weekly for the group loans and monthly for the individual clients. The usual regulation for guarantees is applied.

Repayment rate is 93.6 percent and the PAR 4.4 percent. Al Awael reaches operational sustainability (103 percent) and financial sustainability is 83 percent.

Table 21. Credit portfolio of Al Awael Taiz

Portfolio Quality	
Loan Loss Provision Ratio	N/A
Repayment Rate	93,6
PAR	2,52
Outreach Indicators	
Number of Active Loans	2.810
Active Portfolio (US\$)	220.000
Accumulated Loans since inception	9.543
Accumulated Portfolio (US\$)	1.756.000
Number of Depositors	na
Average Loan Size (US\$) ⁷²	77
Average Deposit Size (US\$)	na
Number of Female Borrowers	2.810
Percentage of Female Borrowers	100%
Number of Staff	N/A
Number of Branches	3
Number of Loan Officers	15
Loan Officers as Percentage of Total Staff	N/A
Productivity	
Number of Outstanding Loans per Loan Officer	187
Average Loan Portfolio per Credit Officer (US\$)	14.667

Azal

Azal is founded and owned by the Sol Foundation. The board of Azal is located in the Foundation but Azal is planning to separate the board from the foundation to reach more independence. For management issues Azal established a management board within the institution including the managers, the General Manager, the External Auditor and a representative from Sol Foundation. Operations started in 2002.

The only source of funding Azal could secure are the loan facilities of SFD according to Islamic principles. One of their main targets in their strategic plan is to find alternative sources of funding.

Azal has three branches in Sana'a and they want to expand their presence in Sana'a within the next five years according to their strategic plan. If the expansion in Sana'a proves successful they want to venture into other governorates. Their client base amounts to around 2,800 borrowers and nearly as much savers, as savings are compulsory for group loans. Portfolio mid of 2007 accounts to nearly the same as the end of 2005, with deviations of around 25 percent and a peak in the last quarter of 2006 and first quarter 2007. In the same period the amount of clients increased by one third.

⁷² Outstanding.

Azal offers group loans and individual loans, with loan amounts between YR 5,000 (US\$ 25) and 100,000 (US\$ 500) for group lending and up to YR 400,000 (US\$ 2,000) for individual loans. The price for the loan depends on the loan amount, up to YR 50,000 it is 2.5 percent per month, up to YR 100,000 (US\$ 500) it is 2.25 percent per month and over YR 100,000 it amounts to 2 percent per month. Insurance for death and accident in the form of residual debt insurance is planned but not implemented yet.

The loans are mainly for income generating activities, some old clients are still granted loans for consumption.

The repayment rate is calculated independently for group lending (100 percent) and individual loans (93 percent). Operational sustainability reaches 95 percent.

Table 22. Azal: Key figures

Portfolio Quality	
Loan Loss Provision Ratio	1,0
Repayment Rate	Group: 10 Individual: 93
PAR	1,5
Outreach Indicators	
Number of Active Loans	2.800
Active Portfolio (US\$)	300.000
Accumulated Loans since inception	11.500
Accumulated Portfolio (US\$)	1.400.000
Number of Depositors	2.660
Average Loan Size (US\$)	107
Average Deposit Size (US\$)	7
Number of Female Borrowers	2.660
Percentage of Female Borrowers	95
Number of Staff	45
Number of Branches	3
Number of Loan Officers	21
Loan Officers as Percentage of Total Staff	47
Productivity	
Number of Outstanding Loans per Loan Officer	133
Average Loan Portfolio per Credit Officer	14.285

Abyan Credit and Savings Program

The Abyan Credit and Savings Program was established in 2003 as an NGO by the Abyan Branch of the Yemeni Women Federation with the assistance of SFD. The program aims at improving the living conditions of the poor families in Abyan Governorate, particularly women by providing high quality financial services at low costs.

SFD provided the program with a loan for their lending purposes. It has to be repaid, with an interest rate of 5 percent.

The program has so far only one branch in Abyan but plans to open two branches, one in Mukalla and the other in Ahwar. The number of active borrowers amounts to 2,019, the number of depositors is 2,343. The program targets only women through its group

lending facilities. The number of clients increased constantly by one third since the end of 2005 and the portfolio increased in the same period by 43 percent.

The program provides group lending only, the group is able to choose if they prefer Morabaha or conventional lending. The maximum loan amount per group is YR 500,000 (US\$ 2,500). Repayments are collected monthly during the group meetings.

According to the latest data, the program reckons to be almost financially sustainable (99 percent). It has a repayment rate of 100 percent

Table 23. Abyan Credit and Savings Program: Key figures

Portfolio Quality	
Loan Loss Provision Ratio	N/A
Repayment Rate	100%
PAR	0
Outreach Indicators	
Number of Active Loans	2.019
Active Portfolio (US\$)	230.000
Accumulated Loans since inception	6.375
Accumulated Portfolio (US\$)	1.055.000
Number of Depositors	2.434
Average Loan Size (US\$)	200
Average Deposit Size (US\$)	N/A
Number of Female Borrowers	2.019
Percentage of Female Borrowers	100
Number of Staff	N/A
Number of Branches	1
Number of Loan Officers	9
Loan Officers as Percentage of Total Staff	N/A
Productivity	
Number of Outstanding Loans per Loan Officer	224
Average Loan Portfolio per Credit Officer (US\$)	25.555

Wadi Hadramaut Credit and Savings Program

The Wadi Hadramaut Credit and Savings Program was initiated in 1997 as a NGO in response to a request from a number of associations in Wadi Hadramaut to establish a program able to provide financial services to micro enterprises. It is under the supervision of the Women Union and SFD.

The only source of funding is SFD. The loan from SFD has to be paid back, with an interest rate of 1.5 percent per month.

The program is the only MFI present in the Wadi Hadramaut with one branch in the main town of the Wadi, Seyun. They plan to open two more branches in the area, Al Qaten and Sah. Currently they have 1,120 borrowers. The number of savers is a bit higher. The program was able to attract almost 50 percent more clients since the end of 2005. However, the overall portfolio increased only slightly by 10 percent.

The program offers a Morabaha product for group, individual and seasonal loans. Different from most of the MFIs, start ups are also financed by the program, reaching 70 percent of all loans. The loan size varies between US\$ 100 and US\$ 750 for individual

loans and less for group loans. Maturity can reach up to 18 months. The price charged for the loans is 18 percent. Accepted guarantees are commercial guarantee, payroll deduction and gold.

The repayment rate is currently at 98 percent and the PAR at 5.5 percent. No information was available regarding sustainability.

Table 24. Wadi Hadramaut Credit and Savings Program: Key figures

Portfolio Quality	
Loan Loss Provision Ratio	N/A
Repayment Rate	98
PAR	5,5
Outreach Indicators	
Number of Active Loans	1.120
Active Portfolio (US\$)	211.000
Accumulated Loans since inception	3.687
Accumulated Portfolio (US\$)	1.251.000
Number of Depositors	1.267
Average Loan Size (US\$)	188
Average Deposit Size (US\$)	30
Number of Female Borrowers	N/A
Percentage of Female Borrowers	N/A
Number of Staff	22
Number of Branches	1
Number of Loan Officers	17
Loan Officers as Percentage of Total Staff	77
Productivity	
Number of Outstanding Loans per Loan Officer	66
Average Loan Portfolio per Credit Officer (US\$)	12.411

Sana'a Microstart Program SOFD

Sana'a Microstart Program SOFD is one of the programs started by the Microstart program of UNDP in collaboration with SFD in 2000. It is not an independent institution, rather than a unit of the SOFD association. This association focuses mainly on social activities for women.

Due to weak management and interference by the General Manager of the association the performance of the Sana'a Microstart Program was not satisfying. The focus was set more on social activities and supporting the people in need than following sustainability.

SFD used to finance the Sana'a Microstart Program through loans but due to the weak performance they did not disburse new loans after the last loan was repaid. Currently SOFD is using up its grants it got allocated from UNDP when the program was established as well as a grant from AgFund they were able to attract at the beginning of their operations.

Negotiations between SFD and the association took place to assess how to deal with the troubled portfolio. Two alternatives were discussed, either to consolidate the portfolio with another MFI or to sell the portfolio. In principle an agreement was reached, when the General Manager of the SOFD association vetoed against it.

Due to the internal problems a lot of employees left the institution and joined other MFIs with a brighter prospect. The Sana'a Microstart Program has currently only one branch, all other branches had to be closed.

They have 566 active clients with an outstanding portfolio of US\$ 42,100. Lending activities continue on a very small scale. From May 2006 to June 2007 the program managed to keep the number of clients and the portfolio stable after a steep decline in 2005 when the number of clients and the overall portfolio was cut to one fourth of the number and amount compared to one year earlier. Their loan amounts are comparatively small with a maximum of US\$ 400 for individuals and US\$ 175 for group members with loan durations of up to 8 months and an interest rate of 36 percent. They do not offer any other services. Additional to the usual guarantees as commercial guarantee and payroll deduction, property is also accepted as collateral.

Non performing loans reach US\$ 10,000. Still they claim to have an operational sustainability of 82 percent. According to the manager the portfolio at risk is 12.1 percent.

Table 25. Sana'a Microstart Program: Key figures

Portfolio Quality	
Loan Loss Provision Ratio	N/A
Repayment Rate	80
PAR	12,1
Outreach Indicators	
Number of Active Loans	566
Active Portfolio (US\$)	42.100
Accumulated Loans since inception	8.795
Accumulated Portfolio (US\$)	825.790
Number of Depositors	na
Average Loan Size (US\$)	200
Average Deposit Size (US\$)	na
Number of Female Borrowers	334
Percentage of Female Borrowers	59
Number of Staff	12
Number of Branches	1
Number of Loan Officers	4
Loan Officers as Percentage of Total Staff	33
Productivity	
Number of Outstanding Loans per Loan Officer	141
Average Loan Portfolio per Credit Officer (US\$)	10.525

Hais Credit Savings Program

The Hais Program was established in 2001 by an initiative of the ADRA'A, an NGO active in Yemen and supported by SFD. As the manager was not in the office during the mission, no further details could be obtained.

According to the statistics of SFD, Hais Program has 1,067 borrowers the end of June 2007, accounting for slight decrease since the end of 2005, but recovering from a lower client base mid of 2006 by 20 percent. However, the portfolio declined constantly between the end of 2005 and June 2006, currently accounting for less than 30 percent of the amount the end of 2005.

SFD plans to integrate Hais Program into the Hodeidah Microcredit Program to make the administration of the MFIs more efficient and cost effective. The process will be according to the integration of Beit Al Fakih by the Hodeidah Microcredit program. Nevertheless no decision is made so far when this process will start.

Table 26. Hais Credit Savings Program: Key figures

Portfolio Quality	
Loan Loss Provision Ratio	N/A
Repayment Rate	N/A
PAR	47
Outreach Indicators	
Number of Active Loans	1.067
Active Portfolio (US\$)	80.000
Accumulated Loans since inception	6.658
Accumulated Portfolio (US\$)	1.250.000
Number of Depositors	3.435
Average Loan Size (US\$)	80
Average Deposit Size (US\$)	N/A
Number of Female Borrowers	854
Percentage of Female Borrowers	80
Number of Staff	N/A
Number of Branches	N/A
Number of Loan Officers	N/A
Loan Officers as Percentage of Total Staff	N/A
Productivity	
Number of Outstanding Loans per Loan Officer	N/A
Average Loan Portfolio per Credit Officer (US\$)	N/A

Social Foundation for Sustainable Development (SFSD)

The Social Foundation for Sustainable Development (SFSD) was founded in August 2006 by several Yemeni business men aware of the need of creating financing opportunities for income generating activities. The SFSD is one of the very few MFIs not related to SFD.

SFSD was able to secure two loans from commercial banks (Shamil Bank and Saba Bank) due to the lobbying of its founders. It is on a profit sharing base according to Islamic principles. The loans are secured by the reputation of the founders. Currently they are in negotiations with Tadhamon Bank for another loan under the same conditions. The agreement is not signed yet but Tadhamon signalled its approval although they have started their own MSE unit.

At present, SFSD has one branch in Sana'a but plans to open 13 branches in the governorates of Aden, Hodeidah and Taiz. Its current customer base is 1,800 but they want to reach 10,000 customers the end of 2010. As they were able to attract staff with experience from other MFIs and have learned from the mistakes of other MFIs this goal might be realistic.

SFSD provides group lending, individual loans, seasonal loans, loans for housing improvement as well as two innovative loan products, the opportunity loan and the school loan. The opportunity loan should serve already active clients to make use of a

sudden chance through getting additional finance on top of their existing loan. The school loan should enable active clients in group lending to provide their children with the necessary outfit (uniforms, books, bags etc) for the start of the new school term. All loans are in form of Morabaha.

Loan amounts start with US\$ 100 and can amount up to US\$ 2,500 for group lending or up to US\$ 5,000 for individual loans. However, the average loan amount is around US\$ 400. The price charged for loans amounts to 18 percent flat for all kinds of loans except for the school loan, which is offered for 10 percent flat. Loan duration can be up to 16 months, whereas the average is 8 months.

Repayment has to be done in the branch. Any client who is one day late with repayment has to pay back the whole outstanding amount in one instalment immediately as punishment. Before the first disbursement of a group loan the group has to meet at least three times, mainly for educational purposes. The duration between application and disbursement in a group is around two weeks, for individual loans it is around 4 days. The loan officers or other staff visits each client individually at least once every second month for monitoring purposes.

For individual loans SFSD accepts commercial guarantee and gold.

The repayment rate so far is 100 percent, with no client even one day late. Nevertheless provisions are made of 0.5 percent on the overall portfolio.

Table 27. SFSD: Key figures

Portfolio Quality	
Loan Loss Provision Ratio	0,5%
Repayment Rate	100%
PAR	0
Outreach Indicators	
Number of Active Loans	1.800
Active Portfolio (US\$)	290.000
Accumulated Loans since inception	2.845
Accumulated Portfolio (US\$)	570.000
Number of Depositors	Na
Average Loan Size (US\$)	400
Average Deposit Size (US\$)	Na
Number of Female Borrowers	1638
Percentage of Female Borrowers	91%
Number of Staff	28
Number of Branches	1
Number of Loan Officers	20
Loan Officers as Percentage of Total Staff	71%
Productivity	
Number of Outstanding Loans per Loan Officer	90
Average Loan Portfolio per Credit Officer (US\$)	14.500

Small Enterprise Development Fund (SEDF)

The Small Enterprise Development Fund (SEDF)⁷³ is a governmental financial institution providing loans to small and medium sized enterprises (SMEs) in Yemen. SEDF was set up as a department of the governmental Yemen Industrial Bank in 1991. The institution needed to re-launch its operations after the collapse of the Industrial Bank with the current organizational structure through a presidential decree (No. 39) in 2002. Currently it is independent governmental institution. It is not subject of supervision and regulation by the CBY; however, it is under the auspices of the Ministry of Industry and Trade. The Ministry does not have a supervisory function.⁷⁴

Represented by the Chairman and managed by an Executive Technical Manager, SEDF is supervised by a Management Committee (Board of Directors). The Board is comprised by seven members, representing the Ministry of Industry and Trade, the Ministry of Planning and International Cooperation, the Ministry of Finance, the Ministry of Social Affairs and Labour, one International Donor and two representatives of SEDF's customers. The Chairman is appointed by the Ministry of Industry and Trade.

Established as the first institution in Yemen to be specialized in delivering financial services, especially loans, to formal sector MSEs, it is today the main institution serving the business segment of the MSEs. Although governmental, SEDF is performance and profit oriented as well as following international best practices.

In 1992/1993 the predecessor of SEDF, SEDU⁷⁵, was endowed by the United Nations Capital Development Fund (UNCDF) with US\$ 2 million for on-lending and US\$ 250,000 for technical assistance. In the same year, the Government of the Netherlands granted a further US\$ 500,000 for lending activities and US\$ 1.5 million for technical assistance. In 1999 the Government of the Netherlands allocated an additional US\$ 2 million for technical assistance, financing and an international long term expert from 1999 until 2002 to support SEDF. Due to little improvement in the fund, the Government of the Netherlands decided not to continue its support.

With the current chairman taking office in 2002, the performance of SEDF improved step by step, especially the repayment rate. First discussions started how to support SEDF either with technical assistance or funds for on-lending. In 2004 SEDF was able to negotiate US\$ 225,000 from SFD for technical assistance and qualified to take several loans from SFD under the same conditions as the MFIs. The outstanding amount with SFD in July 2007 was US\$ 900,000; the overall amount was US\$ 1.8 million. The interest rate varies between 5 percent and 7 percent.

Within the frame of the so called "Counterpart" Fund of the US Food Aid Program for Yemen, SEDF was able to secure a US\$ 500,000 grant in 2006, 95 percent for on-lending and 5 percent for administrative costs. Counterpart Funds are revenues generated by the Yemeni government through selling food donations by the US Department of Agriculture (USDA). The funds generated through this program are allocated to different

⁷³ For more detailed information see the report of the German Savings Bank Foundation for International Development "The Financial Sector in Yemen with Emphasis on Small Enterprise Finance", December 2006

⁷⁴ The Small Enterprise Development Fund is active in providing credits to MSEs but is not classified as a Microfinance Institution.

⁷⁵ Small Enterprise Development Unit, Unit of the Yemen Industrial Bank

projects after approval by MoPIC and the USDA. For 2007 additional US\$ 700,000 are allocated to SEDF, though the money has not been disbursed yet.

Another source of funding for SEDF is the Yemeni government, mainly through the Ministry of Finance. Until 2006 the MoF provided budget support to fill the gap between revenues and operational costs. In 2006 this support ended according to an earlier announcement by MoF.

SEDF was established following the initiative of the President Abdullah Saleh in mid 2006 to allocate US\$ 100 million to support the MSE sector to fight unemployment and create employment opportunities. SEDF could secure a share of US\$ 5 million in three equal tranches for onlending. The first tranche was disbursed in the first half of 2007; the remaining tranches are on hold at the moment after a change of ministers in the MoF. SEDF's equity the end of 2006 stands at US\$ 2.15 million

Additionally SEDF staff is usually invited to all trainings of SFD and since August 2007 SEDF is supported by the German Savings Bank Foundation for International Cooperation with a TA package financed through the GTZ program "Private Sector Development Program (PSEDEP)".

According to its decree SEDF is not allowed to take deposits as a source of funding. Nevertheless for the future the management plans to amend the decree to be able to collect deposits and to use them for onlending. Alternatively the management waits for the announced regulation for NBFi that enables all MFI to use deposits.

SEDF has a broad regional coverage with six branches (Sana'a, Aden, Hodeidah, Ibb, Mukalla and Taiz). SEDF plans to extend its outreach through establishing new branches and opening offices (supervised by one of the branches). Currently SEDF serves 1,900 active clients and holds an active portfolio of around US\$ 4 million. Since 2002 the development showed continuity, having a client base of just 299 in 2002, increasing to 549 in 2004 and 1,482 the end of 2006. The active portfolio increased almost accordingly from US\$ 1.2 million to US\$ 2 Mio and US\$ 3.2 million at the end of 2006.

Offering only individual loan products, SEDF is focusing on the formally registered micro and small business owners⁷⁶ as target group. The MSE has to be in operation since at least six months to qualify for a loan. Two loan products are available, loans of up to 18 months for assets and 12 months for working capital for women and men and a seasonal loan product of up to 6 months, all loans are conventional lending products. The introduction of an Islamic loan product to widen the possible client base is planned. Start-ups are not financed at present.

The minimum loan amount is US\$ 1,000 although loan sizes of US\$ 2,000 and more are preferred. The maximum loan amount is US\$ 20,000 with an average loan size of US\$ 3,000. The interest rate is 12.5 percent and a 3 percent study fee which has to be paid even if the application is rejected. However there may be exceptions insofar that SEDF resigns to collect the study fee. For the seasonal loan an interest rate of 1.5 percent per month is charged. A grace period of up to 3 months is possible.

⁷⁶ Any kind of formal registration is accepted

The biggest share of the loans (around 75 percent) is used to finance trade related activities, around 15 percent are used for production and the rest is allocated to service providers. Typical businesses in manufacturing are carpenters, metal workshops including the production of water tanks and aluminium fittings, handicrafts and food processing.

Loan approvals are made by the branch managers for loans up to US\$ 3,000. Up to 5,000 are approved by the Head of Operations in the HO and credits higher than US\$ 5,000 have to be approved by a loan committee in the HO.

The usual guarantees are accepted. The most common is the commercial guarantee by a business owner, but also gold, real estate and payroll deduction are possible guarantees. Gold and payroll deduction are used to a small extent only as these two alternatives are often not sufficient to cover the relatively high loan amounts. Real estate is accepted more as a moral guarantee. Due to the inefficiency of the legal system liquidation of real estates might be very time consuming.

SEDF's strategy focuses currently on the development and implementation of additional products (Islamic banking product, leasing in cooperation with IFC, indirect consumer loans including housing and loan products for start-ups) and increasing its outreach through setting up new branches and improving its overall lending procedures. However, product development was discussed at least since two years but no new products were finalized or implemented. Only one new branch was opened recently, in August 2007, although according to the strategy at least three new branches were planned for 2006 and 2007.

Although as mentioned at the beginning of the chapter, SEDF is an "independent" governmental institution it is not free of interference from different political stakeholders. Currently it is heavily involved in the initiative of the president to fight unemployment. SEDF is requested to develop programs to create employment opportunities for the unemployed. These programs should not only allocate and channel the financing for the programs but they should also include employment possibilities themselves.

Performance increased significantly since the restart in 2002. Repayment rates are varying between 99 percent and 94 percent on the portfolio since 2002⁷⁷. Portfolio at risk stands at 7 percent, however, the provisions are quite high with 25 percent of the overall portfolio. Also operational sustainability reaches so far only 67 percent. For the end of 2008 operational sustainability of 90 percent is planned.

⁷⁷ With the re-start in 2002 SEDF had to take over also the old portfolio of SEDU which consisted mainly of non-performing loans. Still SEDF is not allowed to write off bad loans. The stated repayment rate is calculated on the portfolio of 2002 and onwards. The overall repayment rate including all loans since 1991 is around 80%.

Table 28. SEDF: Key figures

Portfolio Quality	
Loan Loss Provision Ratio	25
Repayment Rate	94
PAR	7
Outreach Indicators	
Number of Active Loans	1900
Active Portfolio (US\$)	4.065.000
Accumulated Loans since inception	18.660.000
Accumulated Portfolio (US\$)	6.087
Number of Depositors	na
Average Loan Size (US\$)	3.000
Average Deposit Size (US\$)	na
Number of Female Borrowers	3%
Number of Staff	80
Number of Branches	6
Number of Loan Officers	17
Loan Officers as Percentage of Total Staff	21%
Productivity	
Number of Outstanding Loans per Loan Officer	< 100 ⁷⁸
Average Loan Portfolio per Credit Officer (US\$)	215.000

Al-Amal Bank (Bank of Hope)

A new Microfinance provider, Al Amal Bank, is supposed to start operations the beginning of 2008. For its establishment a governmental law was issued in 2002, though due to problems in the coordination and common understanding of functioning between the parties involved only recently the needed measures were taken to start operations. Nevertheless Al Amal started to recruit its staff and the board is optimistic and announced recently to be operational at the beginning of 2008.

Al Amal is set up as an independent governmental institution, its shares are held by the Yemeni Government through SFD (45 percent), AgFund (35 percent) and by private investors (20 percent). Al Amal is endowed with US\$ 5 million capital. The board is constituted according to capital participation. The Yemeni Government is entitled to send four representatives to the board, AgFund three representatives and two representatives are selected by the private investors, whereas one of them was appointed as chairman. The chairman is one of the largest business owners in Yemen.

Appointing one of the largest business owners in Yemen as chairman is linked with the expectations to raise awareness among the private commercial sector and to encourage its players to invest in the Microfinance sector. The founders want the commercial sector to regard MF as a business opportunity and not only as a kind of charity.

Not much is known about the strategy as the strategy will be developed by the executive management. As not all positions of the management have been staffed yet there is only limited information available on the strategy of the MFI. However it was shared that Al-

⁷⁸ The numbers result from the approach that loan officers keep their portfolio if they change jobs within SEDF: Three of the branch manager kept the portfolio they accumulated while being loan officers. One branch manager took over the portfolio of a released loan officer. Back office employees who used to be front loan officers follow up on their old portfolio.

Amal will be acting as a retail lending institution according to its law.⁷⁹ However, providing wholesale facilities to existing MFIs could be included in the array of products. As one of its main principles, Al Amal will be following commercial principles and apply international best practices in Microfinance. According to the new decree, Al Amal will be allowed to take deposits and might do so.

Not much information is available regarding the design of the products. Conventional and Islamic banking principles could be applied in accordance with the law. Corresponding to best practices the interest rate or fee should be oriented at market conform interest rates. The loan size will most probably be according the demand of the microenterprises and home based businesses. The guarantees should be adjusted to the circumstances of the target group.

No strategy was revealed how to facilitate the outreach or how many clients should be targeted within the next years.

⁷⁹ To facilitate the foundation of Al-Amal Bank a special decree has been issued by the Ministry.

Annex 4: MSE Demand Analysis—Additional Data

This annex provides extra information, charts and background material on the demand study in chapter 3 of the report.

Figure 5. Male and female respondents (N=405, in %)

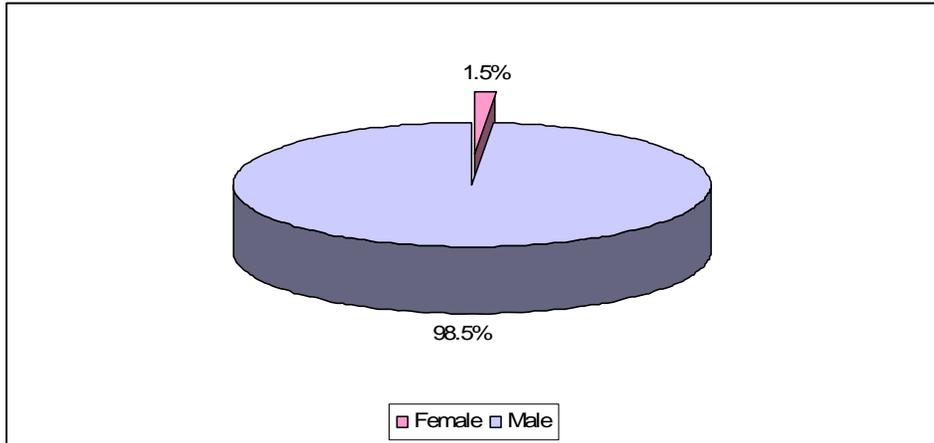


Figure 6. Sample MSE breakdown by region and sector (N=405, in %)

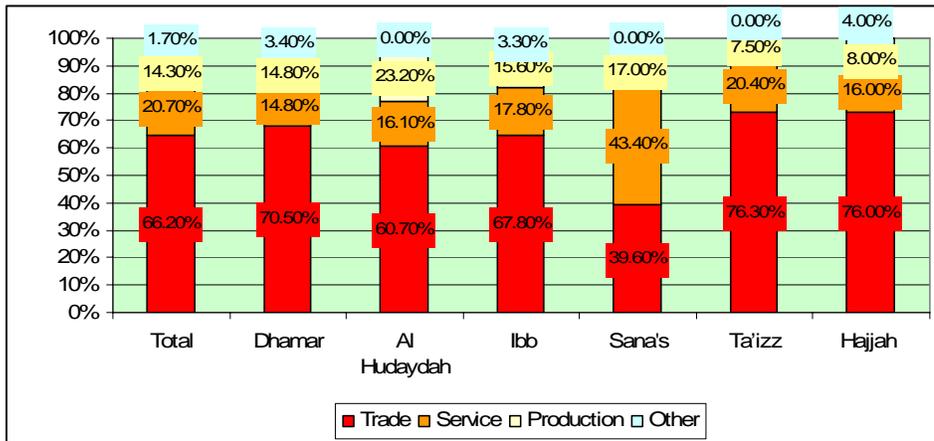
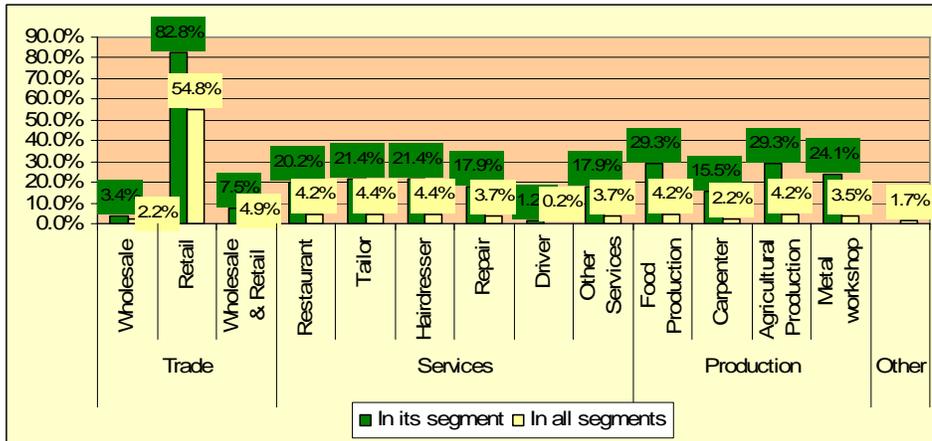


Figure 7. Sub-sectors of survey sample MSEs (N=405)



Of six female owned enterprises, four of them are not registered and two are sole owned enterprises.

Figure 8. Legal status of enterprises (N=405, in %)

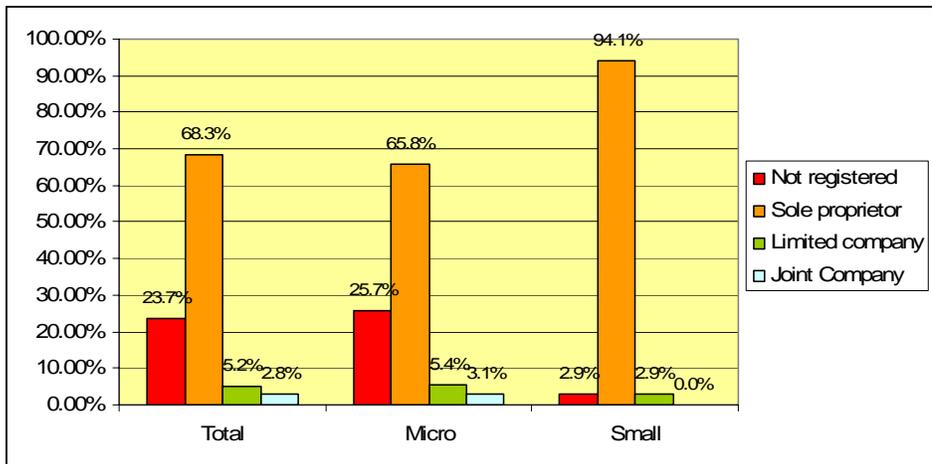
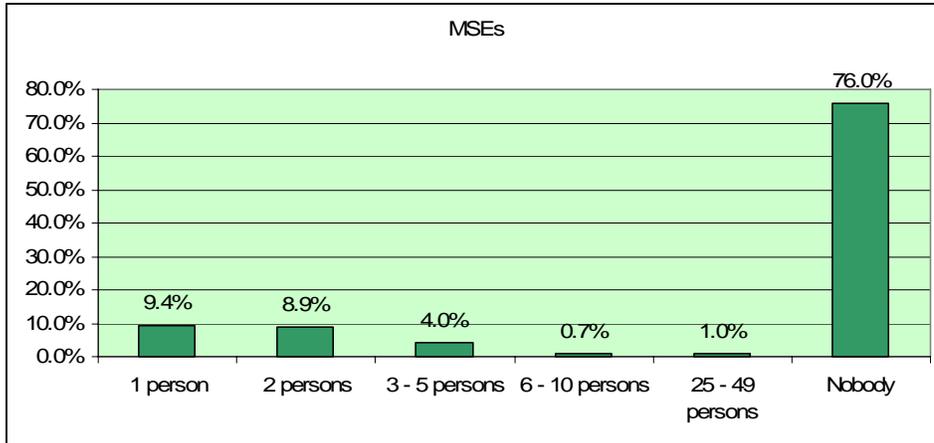


Figure 9. Last year's increase in total number of staff



Of the female sample, out of six, three have been in operation between 4-10 years and three between 11-20 years.

Figure 10. Age and size of enterprises (N=390, in %)

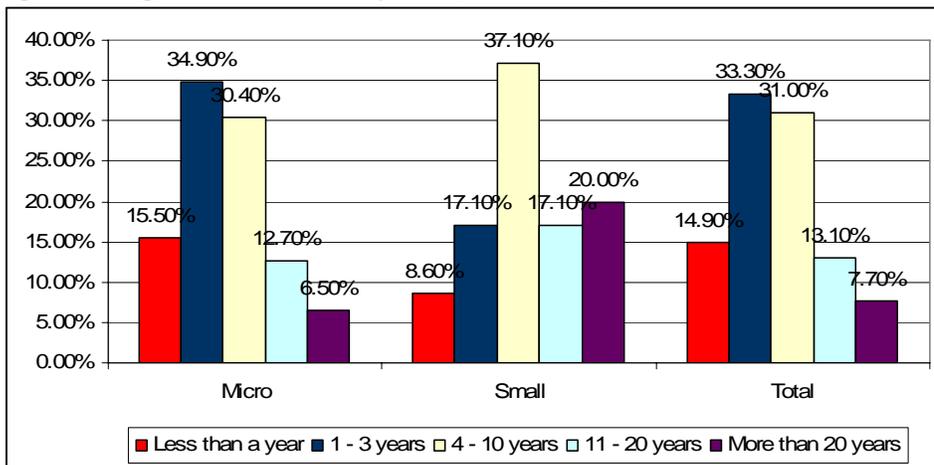


Figure 11. Age and sector of enterprises (N=390, in %)

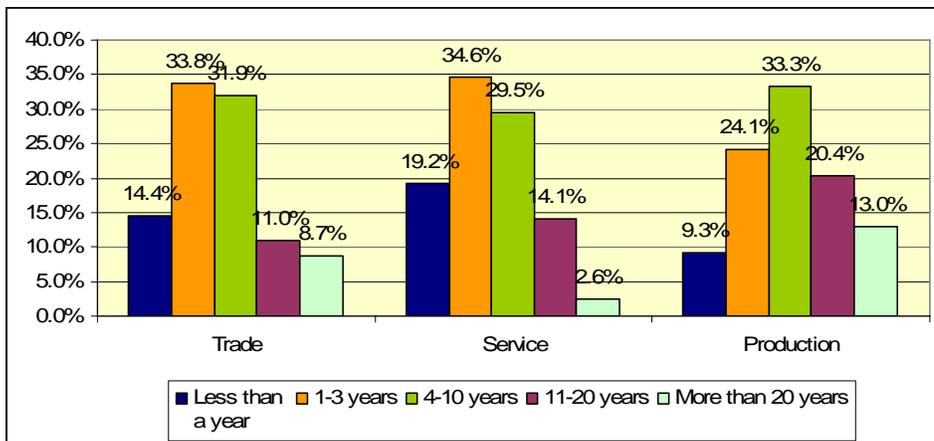
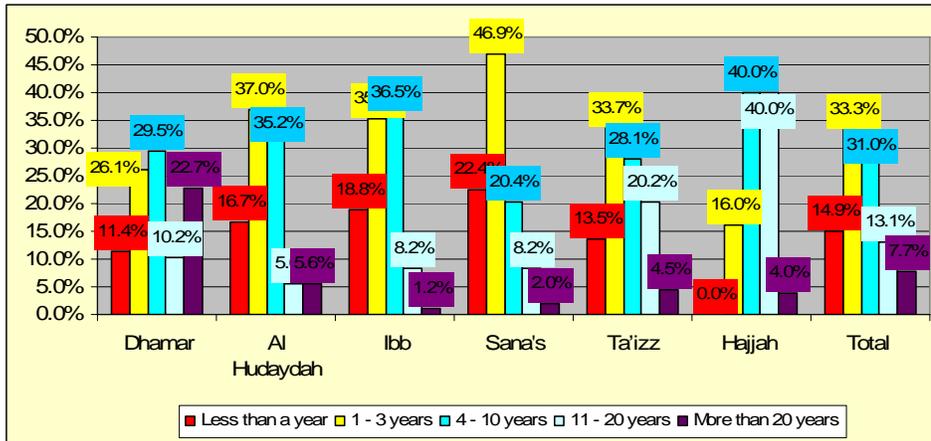


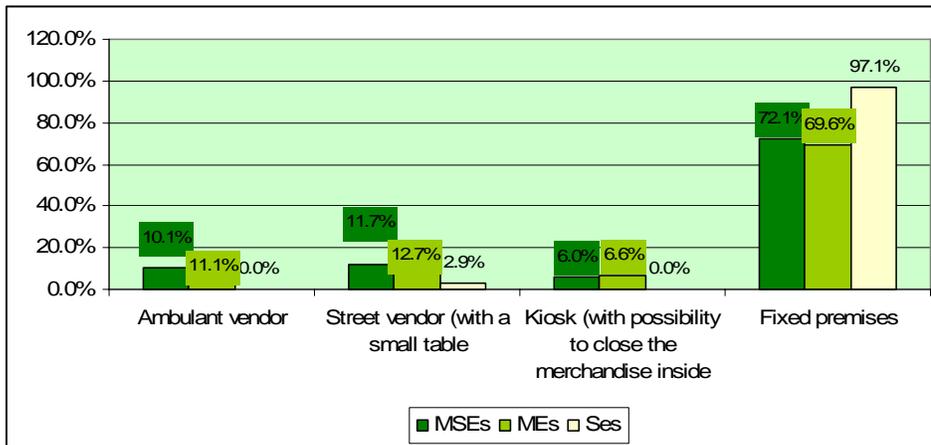
Figure 12. Age and region of enterprises (N= 390, in %)



In overall sample, the majority, 72.1 percent are operating in fixed premises, while 10.1 percent of interviewed enterprises are ambulant vendors, 11.7 percent are street seller and 6 percent are using kiosks. Small enterprises mainly operate in fixed premises. 97.1 percent of interviewed enterprises are operating in fixed premises.

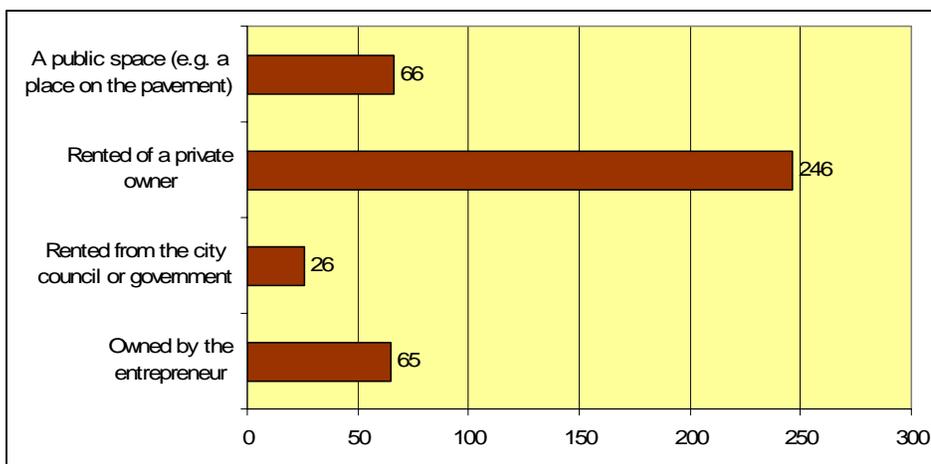
Of female respondents, out of six, none of the enterprises operates in a fixed place or using a kiosk.

Figure 13. Premises of enterprises (N= 405, in %)



Out of 405 respondents, only 65 (16.1 percent) operate in their own business premises. Whilst 246 rented from a private owner, 66 enterprises use public space.

Figure 14. Business premises of survey MSEs (N=403)

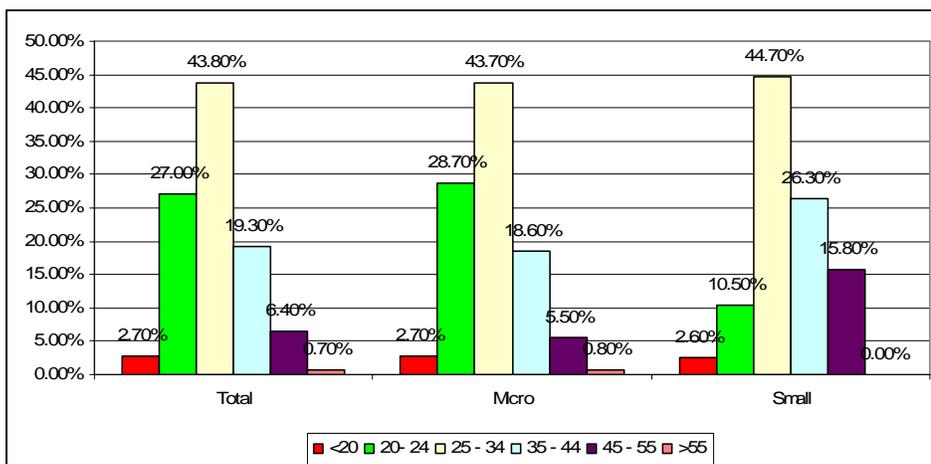


In most cases, the owner is working in the enterprise; 99.5 percent of the interviews were carried out with the owner. Considering the age of entrepreneurs, the majority of entrepreneurs (73.5 percent) are less than 34 years old. Only 7.40 percent of entrepreneurs are more than 45 years and they are mainly owners of small enterprises.

Having so many young owners may be a result of having a high population growth rate, as explained in chapter 4.3 many young people have to start their own business in order to find employment. This reduces the overall share of older entrepreneurs.

Three of the six woman respondents are between 35 and 44, one is over 45 and two are younger than 35.

Figure 15. Age of entrepreneurs (N=404, in %)

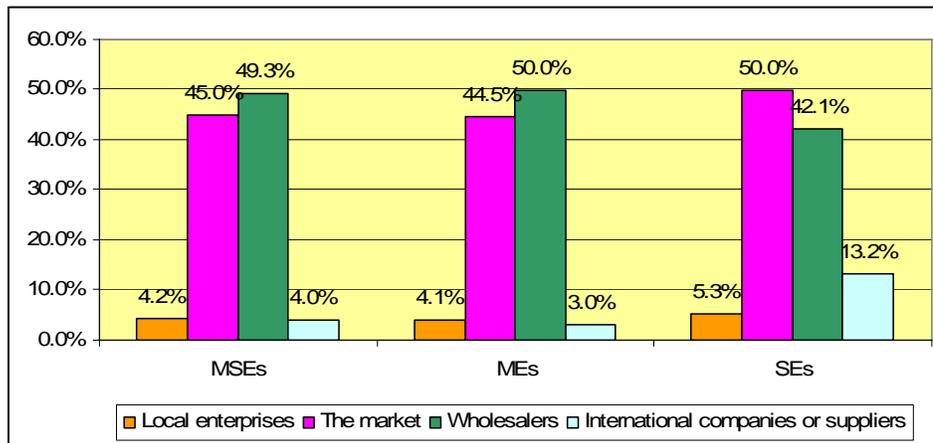


While only 4.0 percent of enterprises are using international suppliers, 49.3 percent are using wholesalers, 45 percent are using the market and 4.2 percent are using local enterprises. 13.2 percent of small enterprises use international suppliers. Out of 16 companies which use international suppliers, seven are located in Dhamar, which was expected as Dhamar is Business premises of survey MSEs an important and historical trade center in Yemen. It seems that an increase in the import industry in recent years

(total import reached \$5.042 billion as of end 2006), will make enterprises more depended to international suppliers in the next years.

During our research we found out that the majority of international suppliers for SMEs are from China, followed by UAE, Egypt and India.

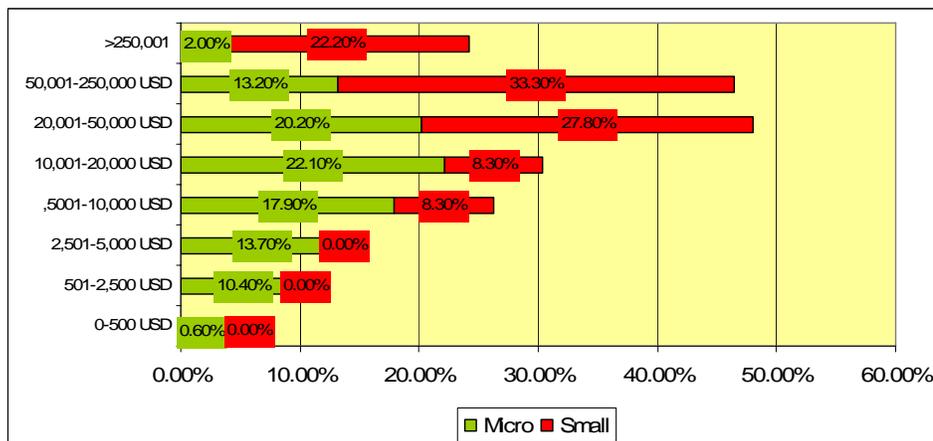
Figure 16. Suppliers of enterprises (N=405, in %)



The majority of respondents indicate that 391 out of 405 payments to suppliers are done in local currency. While 15 entrepreneurs use U.S. dollars in their payments to suppliers, six respondents use Saudi Riyal. Only one respondent uses euros to pay suppliers.

As we defined micro enterprises according to the number of employees, the chart shows the correlation between turnover and size of enterprises. While 24.7 percent of micro enterprises have a yearly turnover less than US\$ 5,000; none of the small enterprises (SE) has a turnover less than US\$ 5,000. 55.5 percent of the small enterprises and 15.2 percent of the micro enterprises have a turnover more than US\$ 50,000.

Figure 17. Yearly turnover of micro and small businesses (N=393, in %)



Based on our sample group and our MSE definition, average turnover of MSEs in Yemen is calculated US\$ 68,450. The amount is US\$ 39,248 for micro enterprises and US\$ 358,032 for small enterprises. The average turnover of the six woman entrepreneurs is significantly lower, with an amount of US\$ 2,038.

Table 29. Average yearly turnover (In US\$)

Type of enterprise	Yearly turnover (US\$)
Female-owned	2,038
Micro	68,450
Small	358,032
All MSEs	68,450

Figure 18. Yearly turnover by sector (N=393, in %)

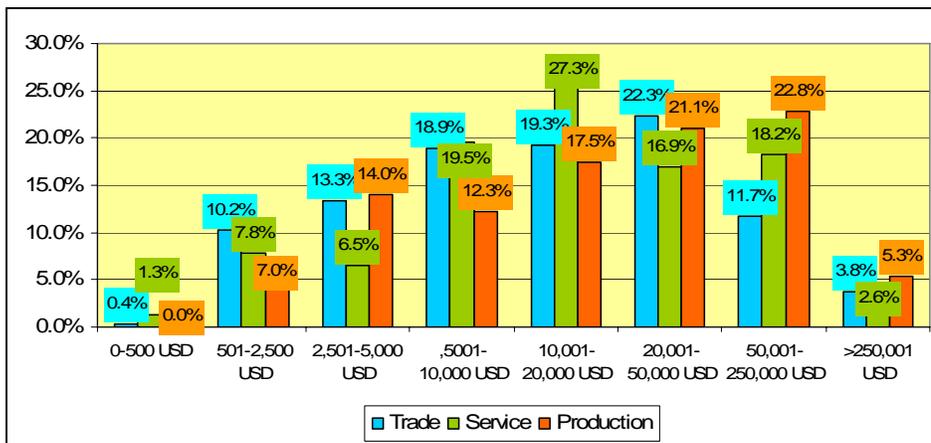


Figure 19. Seasonality of yearly turnover (N=405, in %)

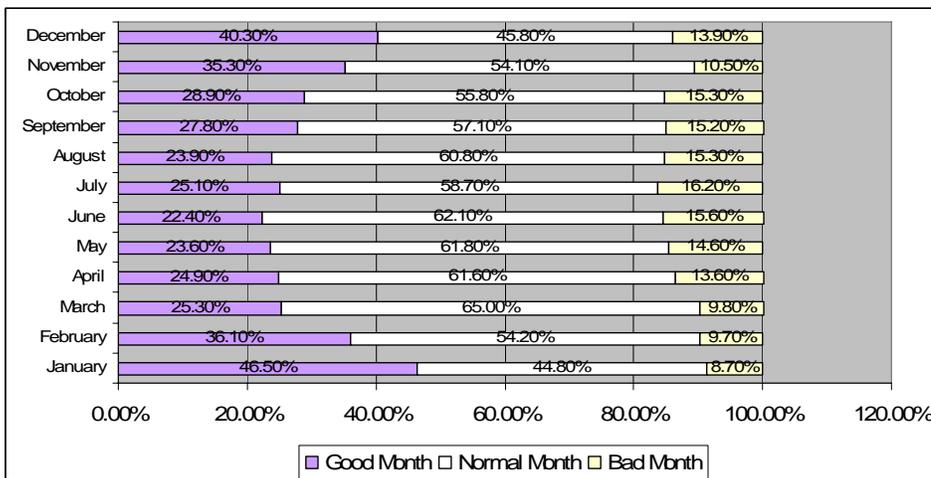


Figure 20. Weekly turnover (N=405, in %)

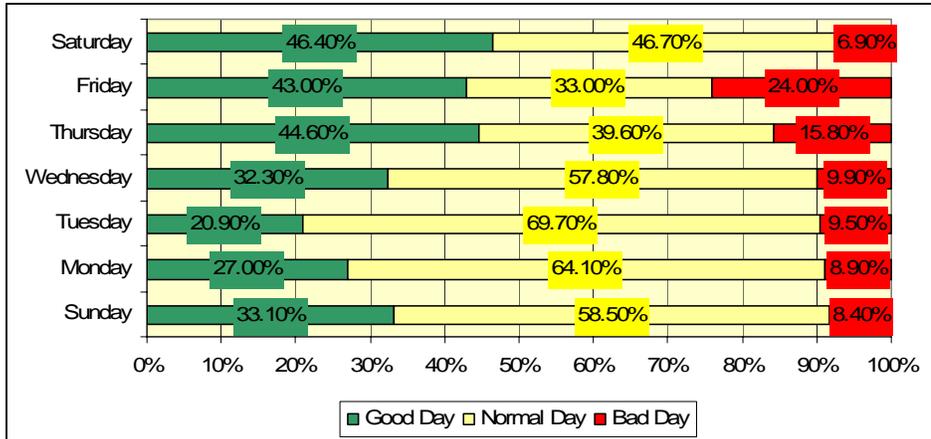


Figure 21. Profit margins of enterprises for best product (N=379, in %)

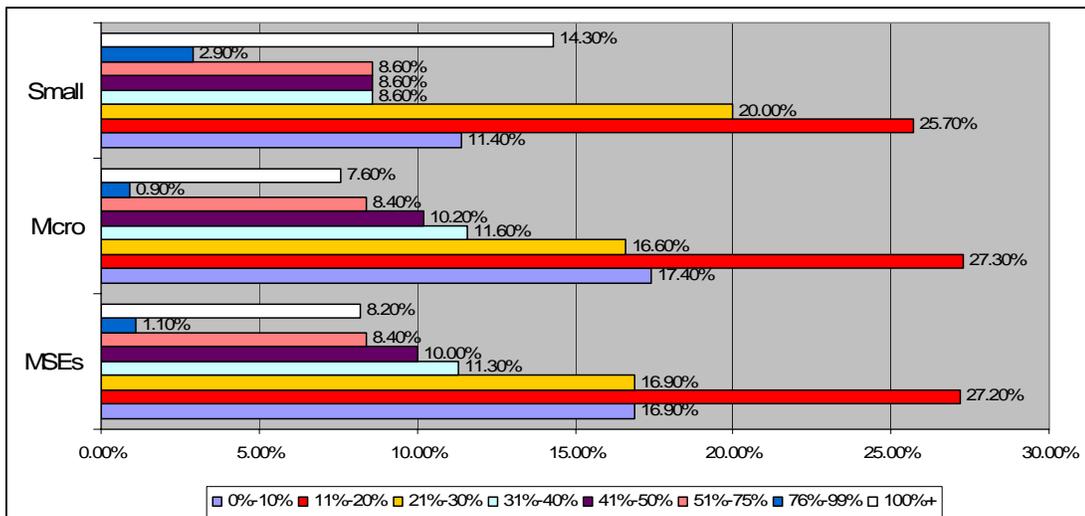


Figure 22. Profit margins of enterprises for second-best product (N=179, in %)

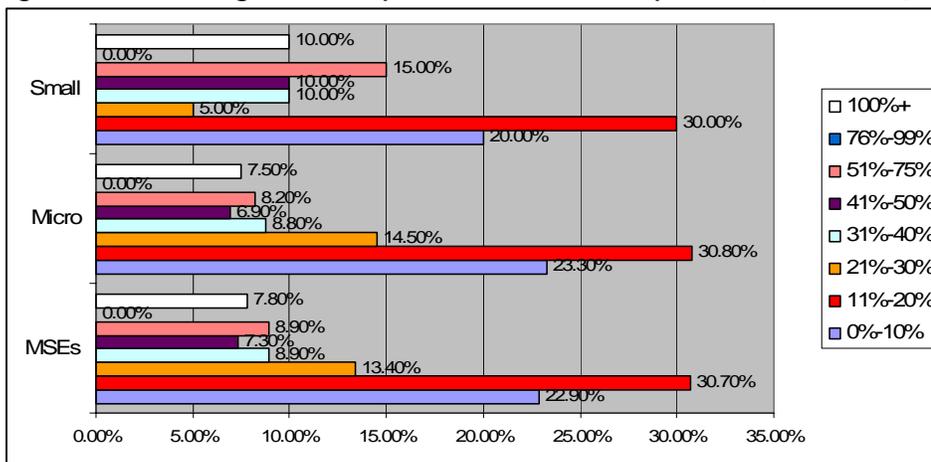


Figure 23. Constraints preventing the enterprise from growing (N=405, in %)

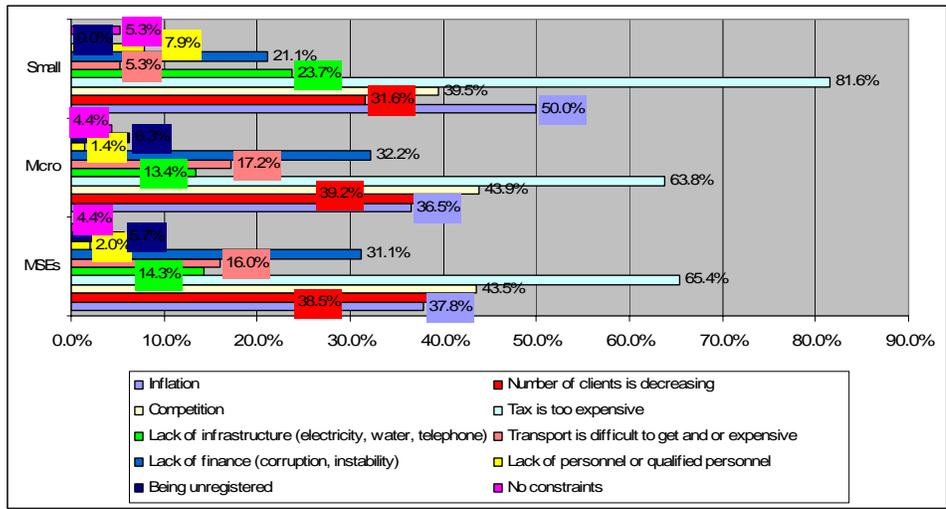


Figure 24. Constraints preventing enterprises from growing, by region (N=405, in %)

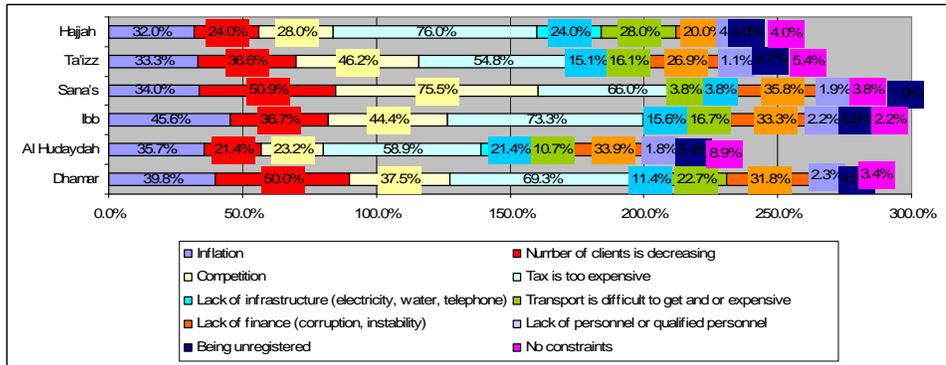


Figure 25. Expectations regarding enterprise development, by MSE size (N=390)

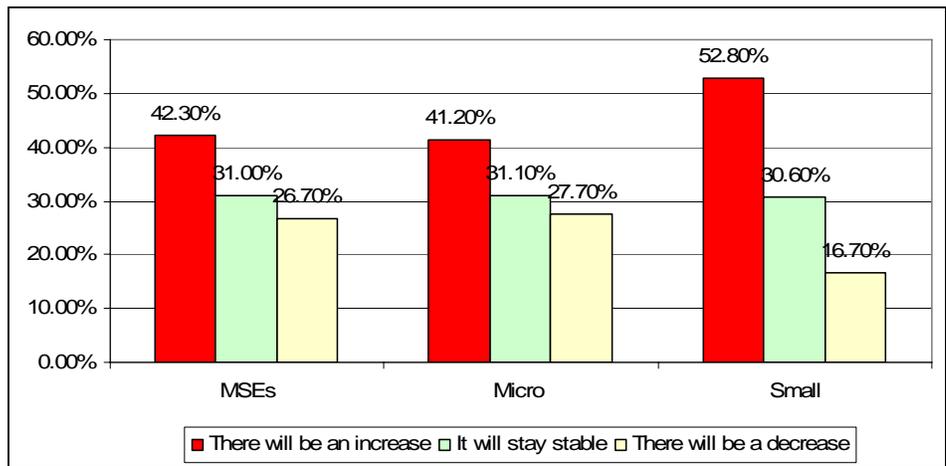
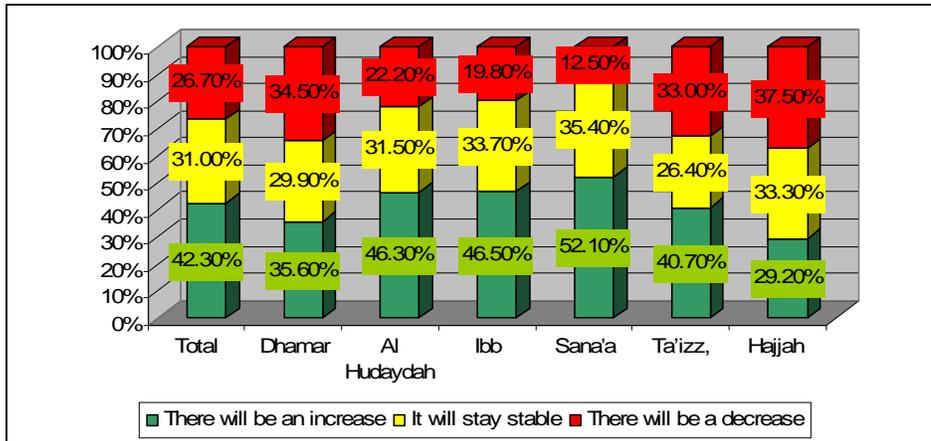


Figure 26. Expectations regarding enterprise development, by region (N=390)



Categorizing respondents according to their perspectives both the development of the company and the country, only 13 percent of respondents foresee an increase in the company's and the economy's development. About 22 percent of respondents have a negative opinion regarding the future of the company and the country, and 22 percent expect a positive development in their company despite to negative expectations regarding to the country's development.

Figure 27. Expectations regarding enterprise development and the Yemen economy (N=405, in %)

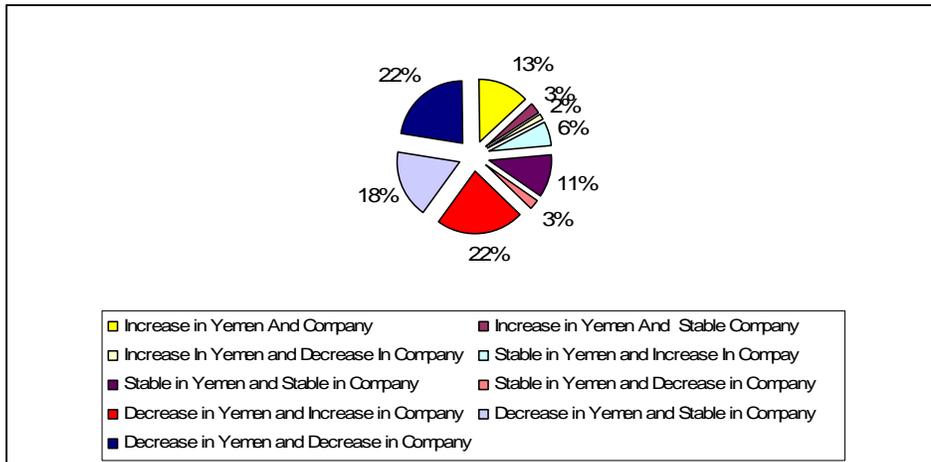


Figure 28. Type of investment made in last two years, by MSE size (N=405, in %)

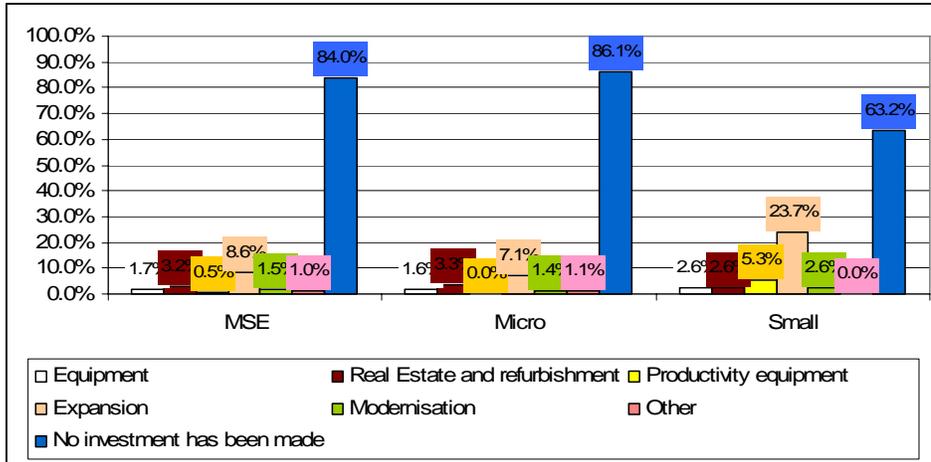


Figure 29. Amount of past investment (N=65, in %)

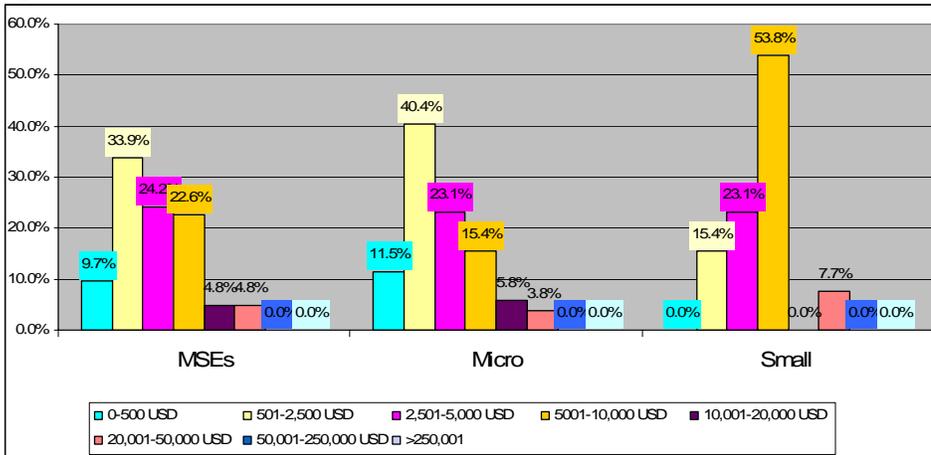


Figure 30. Type of planned future investment, by MSE size (N=404, in %)

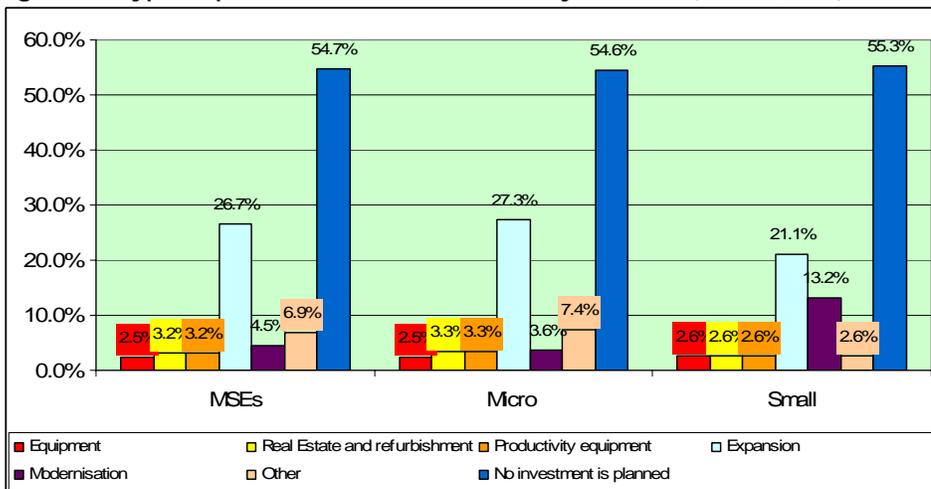


Figure 31. Type of planned future investment, by sector (N=404, in %)

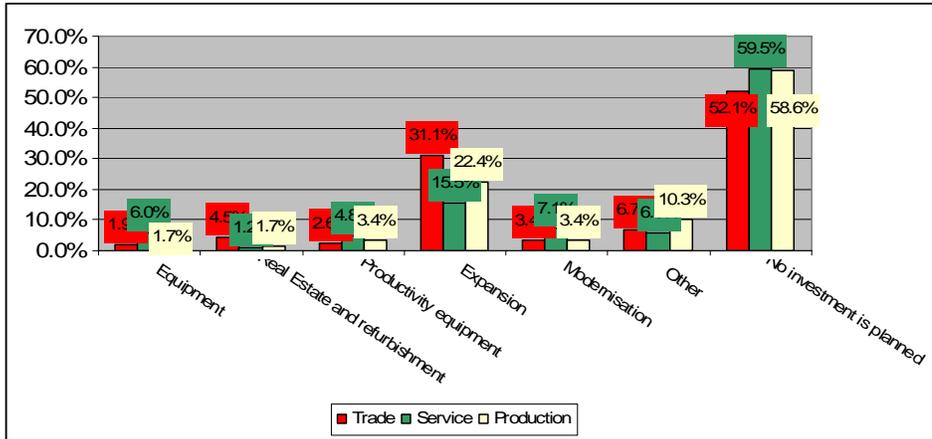
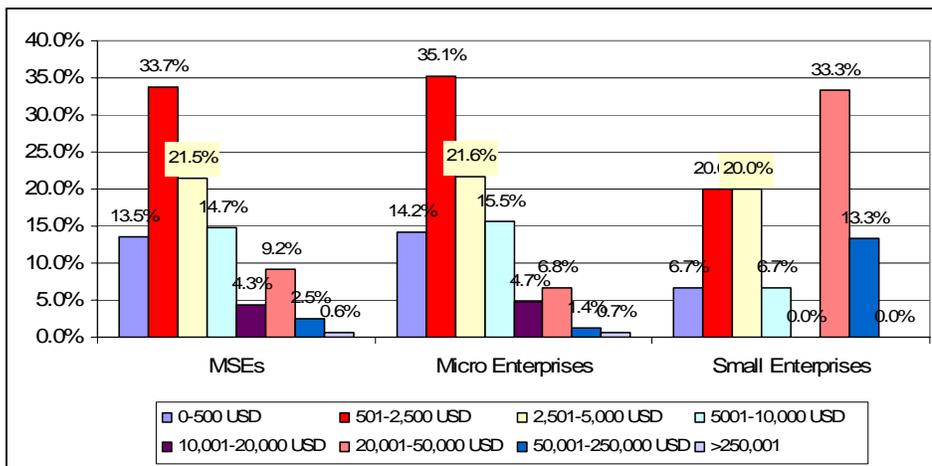


Figure 32. Amount of planned future investment (N=163, in %)



While questioning the MSEs about the kind of banking services the enterprises use, have used or would be interested to use, the following results were found:

Figure 33. Bank services used by MSEs (N=112, in %)

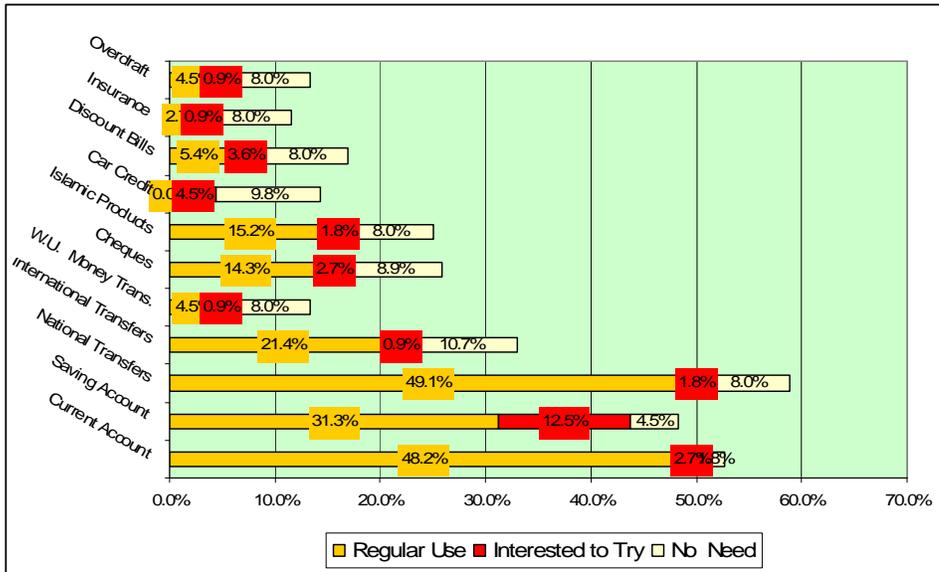


Figure 34. Name of banks or institutions usually used, by region (N=99, in %)

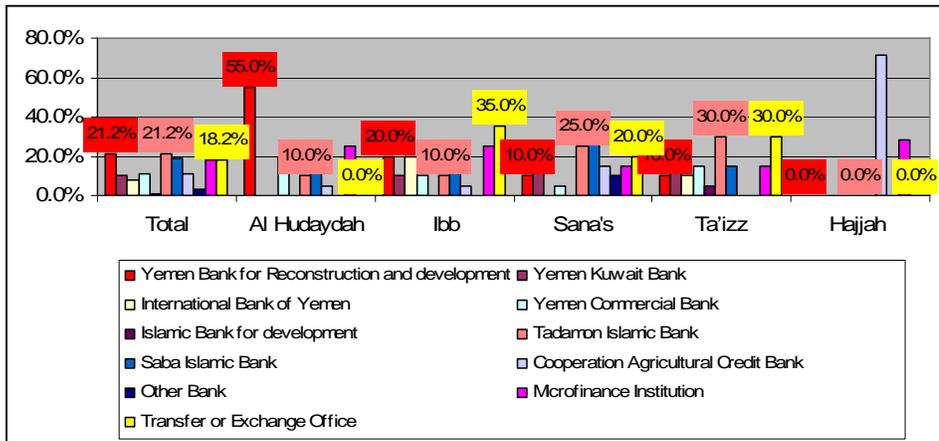


Figure 35. Type of regular savings, by MSE size (N=395, in %)

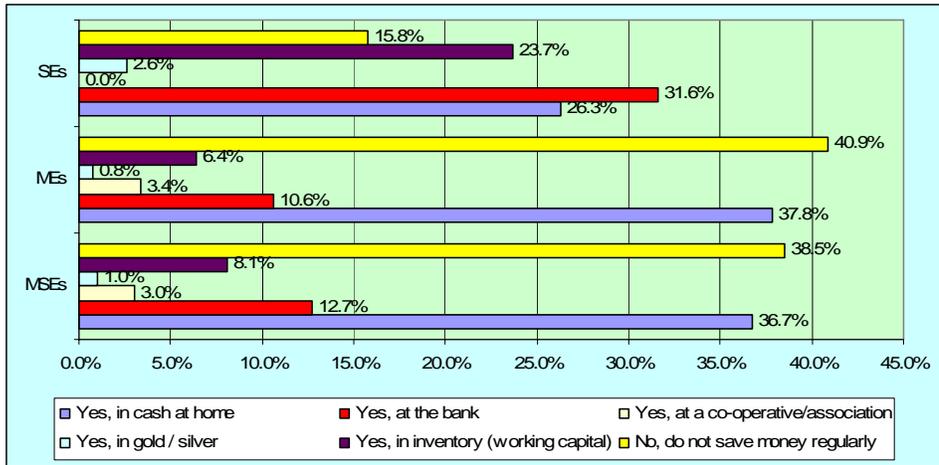


Figure 36. Amount of yearly savings (N=234, in %)

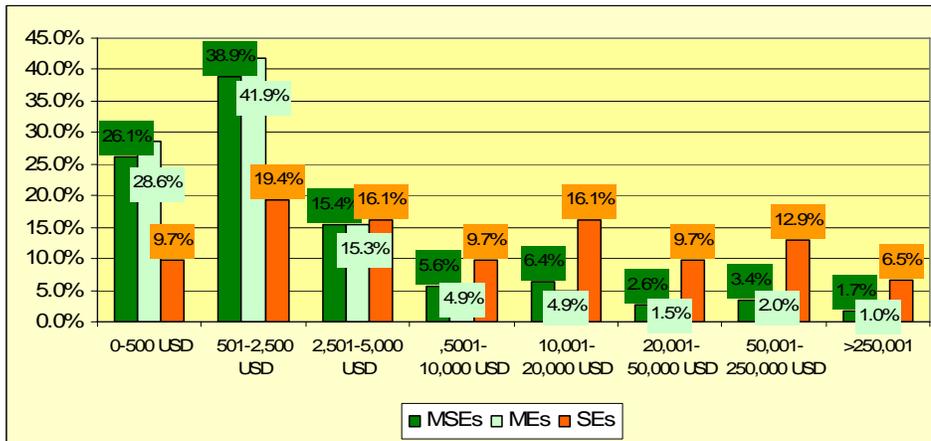
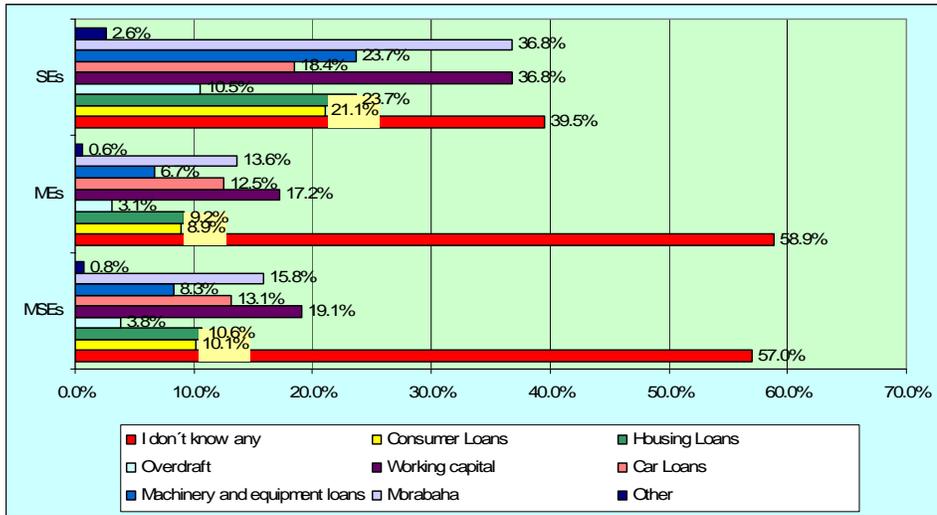


Figure 37. Type of loans known among MSEs (N=398, in %)



With regard to the access to finance according to gender, the share of respondents who think that it is more difficult for a woman than for a man to obtain a loan is as big as the share that thinks that it is not more difficult for a woman than for a man to get a loan. The number of people who don't know is also roughly the same (33.3 percent). However, it should be mentioned that the overwhelming majority of entrepreneurs asked were men.

Although we have limited female entrepreneurs in our sample size, out of six women asked three think that it is more difficult for a woman and two of them don't know.

Figure 38. Is it more difficult to obtain a loan for a woman than for a man? (N=403, in %)

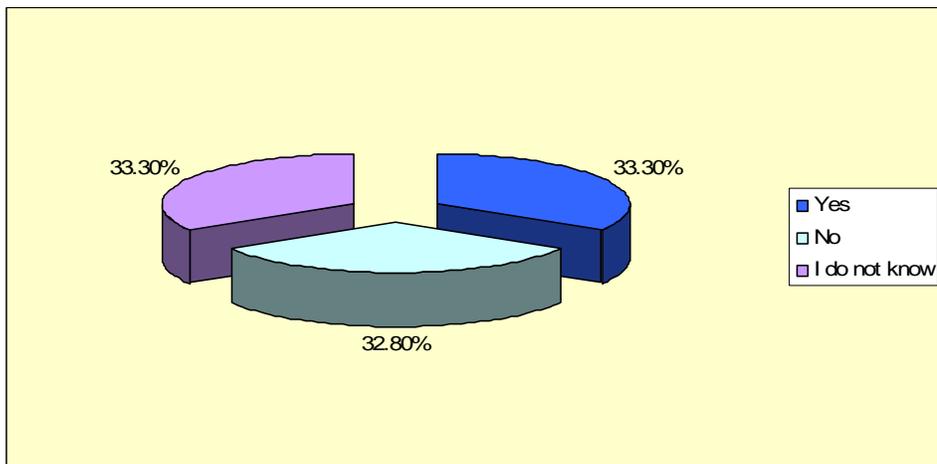
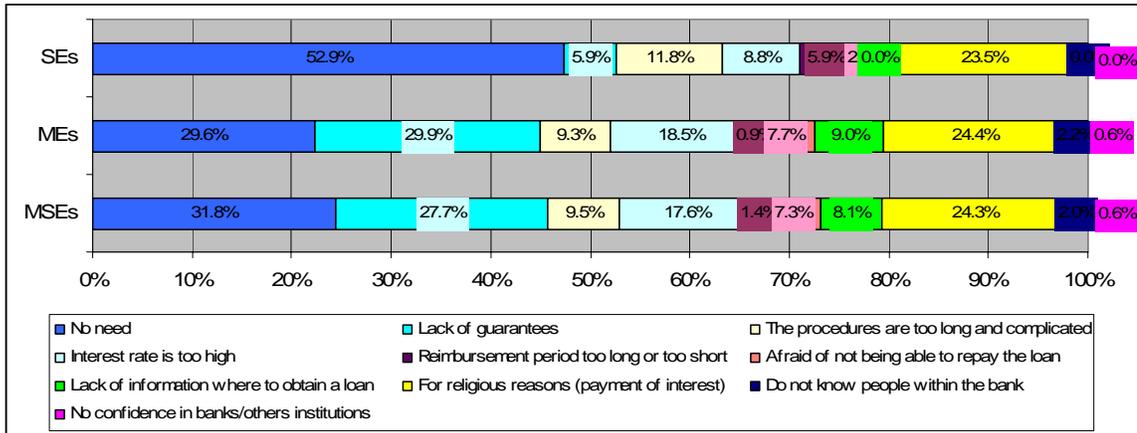


Figure 39. Reasons for never applying for a loan, by MSE size (N=361, in %)



In our sample, micro enterprises appeared to be more successful than small enterprises in obtaining a loan. However as the sample size is very small (only 4 small enterprises had applied for a loan) it would not be fair to generate the argument that micro enterprises are more successful in obtaining loans comparing to small enterprises in general.

Figure 40. Enterprises that received a loan when applying for it, by MSE size (N=43, in %)

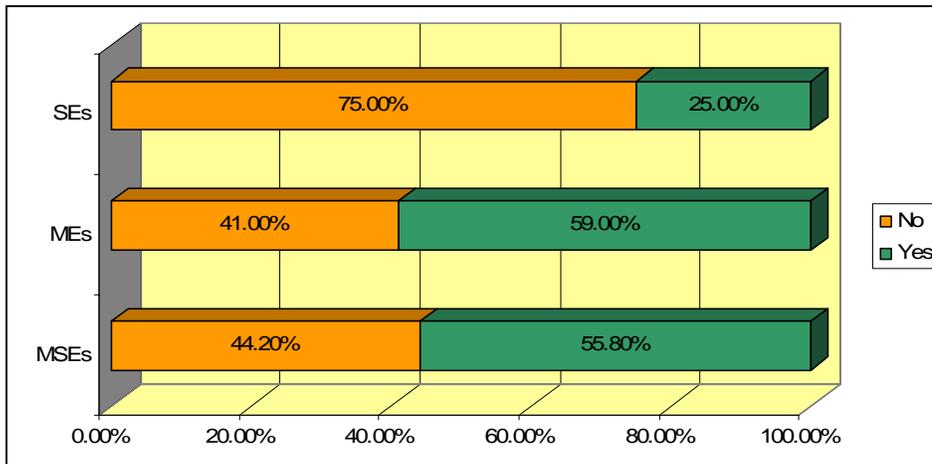
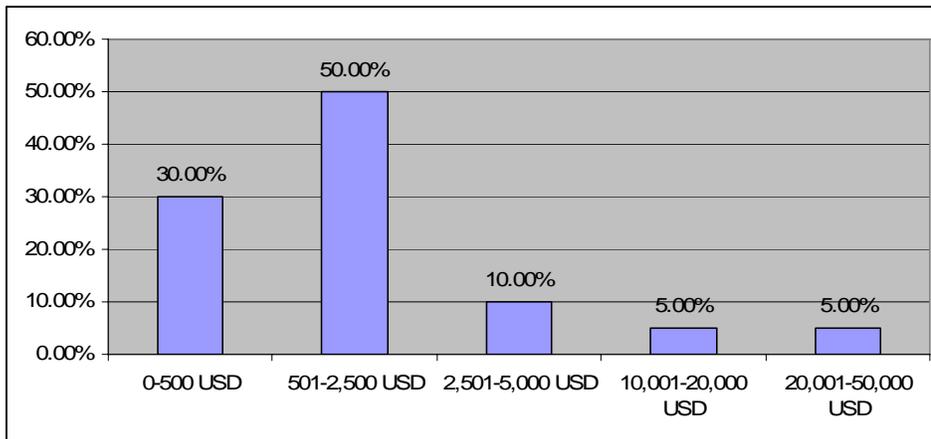


Figure 41. Loan amount received from formal institution (N=20, in %)



The majority (60.9 percent) of entrepreneurs who have already obtained a loan is thinking of obtaining a new loan in the near future. This figure is surprisingly high when compared to the statistics concerning the number of loans obtained. This attitude shows that the MSEs do not have the habit of obtaining loans in sequence.

Figure 42. Do you want to obtain a new loan soon? (N=23, in %)

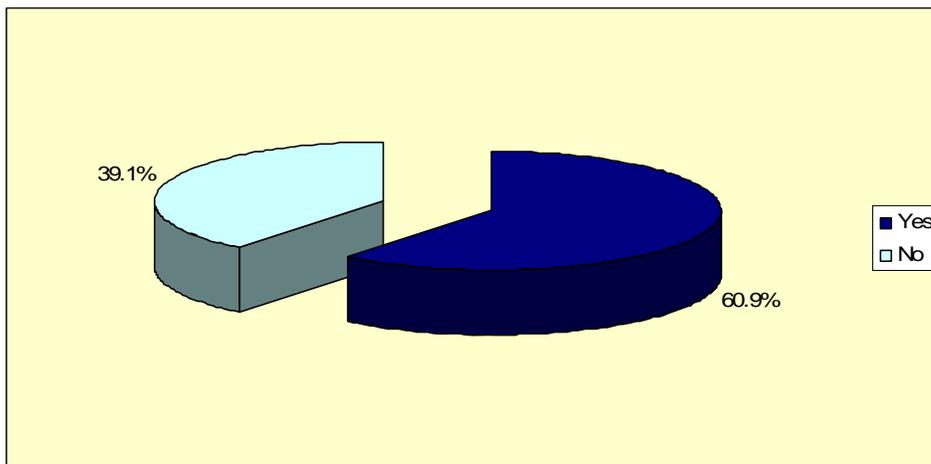
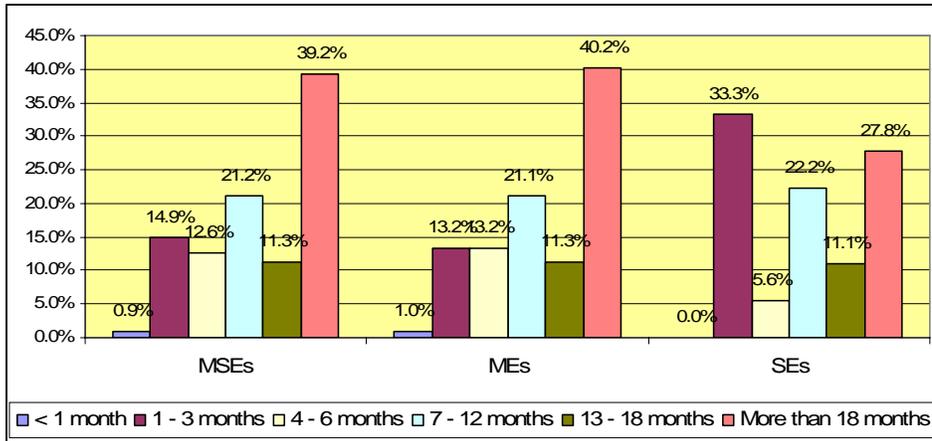


Figure 43. Maturity of informal loans (N=229, in %)



The desired loan interest rate was categorized into two groups as enterprises would like to borrow from any institution and enterprises would like to borrow from only Islamic Banks. As seen the table below, entrepreneurs that would like to borrow only from Islamic Banks are ready to pay only slightly higher interest rates compared to the rest of the respondents.

Figure 44. Desired loan interest rate (N=185, in %)

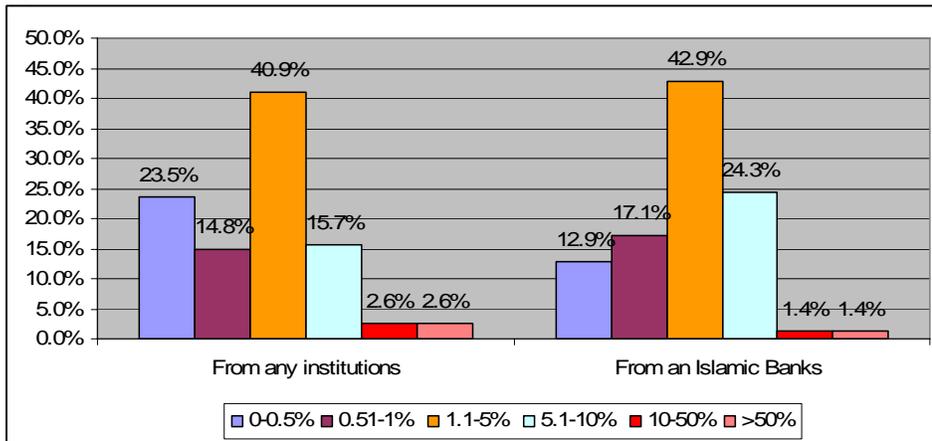


Table 30. Correlation between total employees and family members

		<i>Number of employees including the owner</i>				
		<i>1 person</i>	<i>2 – 4 persons</i>	<i>5 – 10 persons</i>	<i>11 – 25 persons</i>	<i>26 – 50 persons</i>
number of family members as employees	nobody	189	8	0	0	0
	1 - 5 persons	0	8	0	0	0
	6 - 10 persons	0	169	9	1	0
	11 - 25 persons	0	1	21	6	0
	26 - 50 persons	0	0	0	0	1
	total	189	178	30	7	1

Table 31. Desired loan amount and yearly turnover (in US\$)

		<i>Yearly turnover</i>							
		<i>0-500</i>	<i>501-2,500</i>	<i>2,501-5,000</i>	<i>5001-10,000</i>	<i>10,001-20,000</i>	<i>20,001-50,000</i>	<i>50,001-250,000</i>	<i>>250,001</i>
Loan Amount Desired	0-500 US\$	0	7	10	4	5	2	0	0
	501-2,500 US\$	0	5	7	13	20	11	12	0
	2,501-5,000 US\$	0	3	2	3	10	7	8	0
	5001-10,000 US\$	1	3	2	0	3	5	3	2
	10,001-20,000 US\$	0	0	0	1	1	2	2	0
	20,001-50,000 US\$	0	0	0	1	1	0	2	1
	50,001-250,000 US\$	0	0	0	0	0	1	0	2
	>250,001	0	0	0	0	0	0	0	0
Total	1	18	21	22	40	28	27	5	

Table 32. Desired loan amount and past informal loans (in US\$)

		<i>Past informal loans</i>							
		<i>0-500</i>	<i>501-2,500</i>	<i>2,501-5,000</i>	<i>5001-10,000</i>	<i>10,001-20,000</i>	<i>20,001-50,000</i>	<i>50,001-250,000</i>	<i>>250,001</i>
Loan Amount Desired	0-500 US\$	13	1	1	0	0	0	0	0
	501-2,500 US\$	27	20	0	0	0	0	0	0
	2,501-5,000 US\$	12	8	4	0	0	0	0	0
	5001-10,000 US\$	2	10	0	0	0	0	0	0
	10,001-20,000 US\$	1	2	2	1	0	0	0	0
	20,001-50,000 US\$	2	1	1	0	0	0	0	0
	50,001-250,000 US\$	0	0	0	0	0	1	0	0
	>250,001	0	0	0	0	0	0	0	0
	Total	57	42	8	1	0	1	0	0

Annex 5: List of Interviews
(according to date of interview)

<i>Institution</i>	<i>Name</i>	<i>Position</i>	<i>Contact Details</i>
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