Warehouse Receipt Financing: Lessons from Ethiopia

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IFC Support to Ethiopia WHR Finance Program

Agenda

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II. IFC Support to Ethiopia WHR Finance Program
III. WHR Financing: Product Features
IV. WHR Financing: Key Statistics
V. Key Success Factors
VI. Key Challenges
VII. Key Requirements
IFC: Part of the World Bank Group

IFC is the main driver of private sector development in the World Bank Group

- **Investment Services**
  - Long-Term Debt
  - Equity
  - Trade Finance
  - Risk Management
  - Mobilization

- **Advisory Services**
  - Investment Climate
  - Access to Finance
  - Sustainable Business Advisory
  - PPP Transactions Advisory

- **Asset Management**
  - Launched in 2009
  - IFC Capitalization Fund
IFC Support to Ethiopia WRF-Program

- The main objective of the Ethiopia WHR -F Program is to help Ethiopia develop a functioning Warehouse Receipt (WHR) financing market through a combination of capacity building and financing to the market.

Why AS in WHR Financing?

- **Lack of Access to Finance:** In Ethiopia, the agriculture sector is vital for economic growth, providing more than 60% employment. Yet, producers and farmers have limited access to finance.

- **New Product:** WHR financing is a way for the underserved market, such as producers and farmers, to access to finance. The market (including local banks) needs to understand the advantage of commodity-based financing.

- **Support investment and advisory services synergies:** When the investee bank’s capacity level needs to be improved, the Advisory Services will be implemented.
Various actors benefit from a properly functioning WHR financing system

**Banks:**
Seeking untapped massive potential in agrifinance and secure and easily liquidating collateral

**Farmers:**
Seeking higher Prices, accurate measures, storage and credit

**Traders:**
Seeking credit and storage

**Processers:**
Seeking Constant suppliers of Raw materials

**Input suppliers:**
Seeking financing for stocks, improving quality
WHR Financing in Ethiopia: Product Features

- Short-term working capital loan (2-4 months)

- Uses ECX WHR as collateral (not physical commodity)
  - WHR Guarantees Quality and Quantity

- Agricultural supply-side actors (not Exporters)

- Currently all ECX Commodities except Coffee:
  - Sesame (90 days), P-beans (90 days)
  - Maize (90 days), Wheat (120 days)
ECX WRF: Advantages

• **Current Small Amount of Financing for Supply-side Trade Finance**
  - 600m ($35m) birr of total agriculture loans of 10b birr(6%)

• **Existing Merchandise Loan Disadvantages:**
  - Long set-up process
  - Audited accounts required
  - Expensive for banks with sampling/security, etc

• **Benefits of ECX WHR Financing**
  - Borrower does not require own storage facility
  - Easier access to supply-side credit
  - Bank gets collateral with high liquidity, low cost
  - New business for banks
ECX WHR-F: How does it work?

- Commodity deposited at an ECX warehouse
- E-WHR issued by ECX Central Depository
- Apply for loan
- E-WHR pledged to bank
- Loan disbursed
- WHR sold at ECX
- ECX Clearing House sends cash to bank for settlement of disbursement
Who are the users?

• ECX Members & Clients
  ▪ Co-operative Unions
  ▪ Traders (92% of trade, but 6% of finance)
  ▪ Commercial Farms

• Barriers to Small Farmers
  ▪ Min lot size & loan amount
  ▪ Distance to an ECX Warehouse

• Small farmers will need to come via Co-op Unions or Societies
Summary of WHR Financing-Key Statistics

- ECX dramatically increased the volume traded from the previous year total of 223,000 tons at a value of Birr 6.7 billion ($382m) in 2009/10 to 509,308 tons at a value of Birr 18.7 billion ($1bn) in 2010/11.
Warehouse Receipt Financing has only started recently

- A total of four banks have signed agreements with ECX to start WHR Financing
- Summary of WHR Financing (Nov 2011-Jan 2011) - ETB12 Million ($690,000)
- Number of WHRs Financed: 64
- Main Commodities covered: Sesame and P-Beans
- Projected WHR-F for FY ending June 30: ETB 100 Million ($5.8 million)
- Coffee will be covered once warehouse shortage constraints are addressed
Key Success Factors

- **ECX: A Strong Partner:** ECX assures all market players the security they need in the market through providing a secure and reliable End-to-End system for handling, grading, and storing commodities, and a risk-free payment and goods delivery system to settle transactions.

- **Performance Guarantee:** ECX guarantees Payment, delivery and withdrawal according to WHR Quantity, Quality & Trade Execution Price (minus moisture loss). Price Risks not guaranteed.

- **Price Discovery System in Place:** 300 Rural Electronic Price Tickers (REPT) at local level in a public market space and ECX website by which market information is updated real time.

- **Supportive Legal and Regulatory Framework:** Outlines forms of WHRs, legal status of WHRs, rights and obligations of Warehouse Operators, Rights and obligations of Banks or lending institutions.

- **Public Awareness and Education:** Efforts to educate traders, cooperative unions, commercial unions, processors and millers about benefits of WHR-Financing.
Key Challenges

- **Government Regulations**: Credit Cap imposed by the GoE led to liquidity crunch in the banking sector. Banks in turn are restricting their services to the agriculture sector.

- **Lack of Adequate Warehouses**: Without established 3rd party collateral management entities in Ethiopia, ECX conducts its own warehouses. Warehouse capacity increased by 92%, from 1.4 million bags to 2.8 million this year alone. Yet, because of shortage of WHs, ECX is forced to reduce to duration of deposit in coffee to 30 days.

- **Conservative Banking Practices**: Conventional lending Practices Vs Warehouse Receipt Financing

- **Public Awareness**: No adequate awareness about requirements for WHR Financing by traders and farmers.

- **Lack of supportive regulation**: Directive restricting external loans by banks has negatively impacted demand by local banks for IFC WHR investment.
Key Requirements for successful WHR-F

- Establishing the scope for WHR-F (types of commodities, demand for receipted commodities, etc)
- Designing the Legal and regulatory Framework (legal status of WHRs, rights and obligations of Warehouse Operators, Banks or lending institutions, enforcement in case of default, performance guarantee, etc)
- Identifying robust and cost effective financial performance guarantees providing recourse to depositors and financiers in the event of warehouse failures
- Licensing, oversight and inspection of warehouse operators, training of staff, ensuring adequate warehousing capacity exist
- Establishing system to facilitate sale of warehoused commodities (ex, ECX in Ethiopia)
- Designing and Implementing a communication strategy for relevant stakeholders
Upcoming Activities

• Africa Warehouse Receipt Financing Conference (organized by IFC and ECX - expected in June 2010)
• Warehouse Receipt Financing: A toolkit for Financial Institutions in Emerging Economies (Expected to launched in April, 2011)
• IFC’s Guide to Legal and Regulatory Reform in WHR Financing (Expected to be launched in May 2011)

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