

**“3C4SME”**

**Cross-border Cooperation and Competitiveness for SMEs**

**No: 128/ 1<sup>st</sup> call of standard Project**

**Interreg IPA CBC Italy-Albania-Montenegro 2014-2020**

**“External Expertise and services in the Analysis of the contexts and needs in the credit system and the actual regulatory conditions in the credit system in Albania”**

**Contract no: 9084/6 dated 15.08.2019**

**Prepared by: Albanian Institute for Social Economic Development**

**Accepted by: Beneficiary partner, National Business Center**

## INDEX

### **Abbreviations**

### **Chapter 1: Introduction**

### **Chapter 2: Methodology**

### **Chapter 3: Public Policies for Credit System and Actual Regulatory Conditions**

### **Chapter 4: Study best practices in local credit system**

### **Chapter 5: Focus on institutional framework and implemented policies on practical support to credit**

### **References**

### **WEBSITES**

## ABBREVIATIONS

AAB – Albanian Association of Banks

AIDA - Albanian Investment Development Agency

AP - Action Plan

BoA – Bank of Albania

EBRD - European Bank for Reconstruction and Development

EIB – European Investment Bank

ERP - Economic Reform Program

GDP – Gross Domestic Product

IASME - Integrated Assistance Program for the Development of Albanian SMEs

NPL - Nonperforming Loan

OECD - Organisation for Economic Co-operation and Development

PRODAPS - Programme for Development of the Albanian Private Sector?

SEE – South East Europe

SME – Small Medium Enterprise

## INTRODUCTION

The main objective of the project is the Study on innovative approaches to credit access and the implementation of the same in the involved territories in the project. It is linked to the specific objective of business growth (entrepreneurship). Another main objective is to create regulatory prerequisites to allow local public systems to transfer the new ways of accessing credit.

Under this expertise is provided a report on credit discipline, the credit system, the role of public funds and the tools in support of enterprises. The expert for this assignment supports the concept of the Study on innovative approaches to credit access and the implementation of the same in the involved territories in the project. The expert is committed to contribute in such important project and to demonstrate his ability when it comes to entrepreneurship sector.

The expert interprets the TORs as a request not only in analyzing of the public and private context and needs in Albania, but contributing either to the further collaboration within the project sustainability standards.

The experts tasks consist also on regularly cooperate in terms of gathering information about the public and private context and will approach the tools for supporting the enterprises. The support of the indicated results explained in the ToR's is also provided because through the context analysis is identified the best actors and the best solutions to be adopted on the local credit system.



## METHODOLOGY

Mason (2002) defines methodological strategy as the logic by which one goes about answering the research points. The meaning of this is related to the way the design of the research is done as a potential answer to the research points.

The aim of the project is to verify the conditions to provide to the Albanians and Montenegrin small enterprises a financial instrument that in Apulia and in Molise has been facilitating the enterprises' access to the bank funding, both for the growth and the management. The goal is to be executed a research in order to have a photograph of credit sector in the involved areas.

- Public Policies for Credit System and Actual Regulatory Conditions
- Best practices in local credit system
- Institutional framework and implemented policies on practical support to credit

The expected change the project will have in relation to the current situation is: Ensuring greater access to credit for firms, considering the current unfavorable economic situation.

In order to reach the main goal, the expert was focused on providing relevant and up to date information on the condition of the Albania economy, as it relates to the Public policies for the credit system and actual regulatory conditions. Methodology used in order conduct this analysis was based on:

***Research and Analytical Methodology*** - The research was conducted using a variety of established methods; secondary review of existing reports, literature, and data; interviews with selected stakeholders as well as surveys of businesses and individuals in the local credit system;

***Stakeholder Interviews*** - Structured interviews have been conducted with different stakeholders. Parts of the interviews were also representatives from the public sector dealing with policies for the credit system;

***Information gathered*** on Public policies for the credit system and actual regulatory conditions from the existing reports literature and data.

***Institutional framework and policies analysis on credit***, while conducting meetings with the representatives from different institutions responsible for credit policies.

An effective and well-conducted method creates a firm foundation for advancing knowledge and facilitating theory development. By integrating findings and perspectives from many empirical findings, a literature review can address research questions with a power that no single study has. It can also help to provide an overview of areas in which the research is disparate and interdisciplinary (Snyder, 2019). The research for the above-mentioned points regarding credit sector in Albania is based on a literature review on reports from institution such as Albanian Investment Development Agency (AIDA), Bank of Albania, European Investment Bank (EIB), Organization for Economic Co-operation and Development (OECD), World Bank and scientific research papers. These institutions prepare and publish reports on yearly periodicity regarding the credit sector in Albania regarding policies and regulatory conditions, best practices in local credit system and institutional frameworks. The information from these reports and papers has been reviewed and analyzed in order to be taken only relevant information to fulfill the requirements to obtain information on the objectives of the project. The reports and papers both offer qualitative and quantitative data to support the information presented in the material. Besides that, in credit institution are publish information regarding the credit sector and its development together with the steps undertaken by the institutions to develop the access to credit in Albania both from public/private institutions.

Finally, the expert in order to fulfill the assignment effectively and efficiently was engaged in conducting analysis of the context and needs in Albania; analysis of the public and private context and needs in Albania, with a technical-economical report as well as collection of rules on credit and cooperation.

## PUBLIC POLICIES FOR CREDIT SYSTEM AND ACTUAL REGULATORY CONDITIONS

World Bank (2019) evaluated Albanian development by stating that in order to accelerate the pace of equitable growth, Albania is implementing structural reforms that will raise productivity and competitiveness in the economy, create more jobs, and improve governance and public service delivery. Enhanced regional connectivity and access to regional and global markets, coupled with export and market diversification, can also help promote faster growth. Recognizing these challenges, the Government of Albania has embarked on a broad-



based reform program focused on macroeconomic and fiscal sustainability, financial sector stabilization, energy concerns, pensions, and territorial administration. Significant progress, propelled by the ongoing reforms, has created the conditions for rebounding business confidence and domestic demand, including early signs of increased investment and an export-led recovery. The banking and financial sector as from the Bank of Albania Supervision Report of 2018 divides the sector as follows:

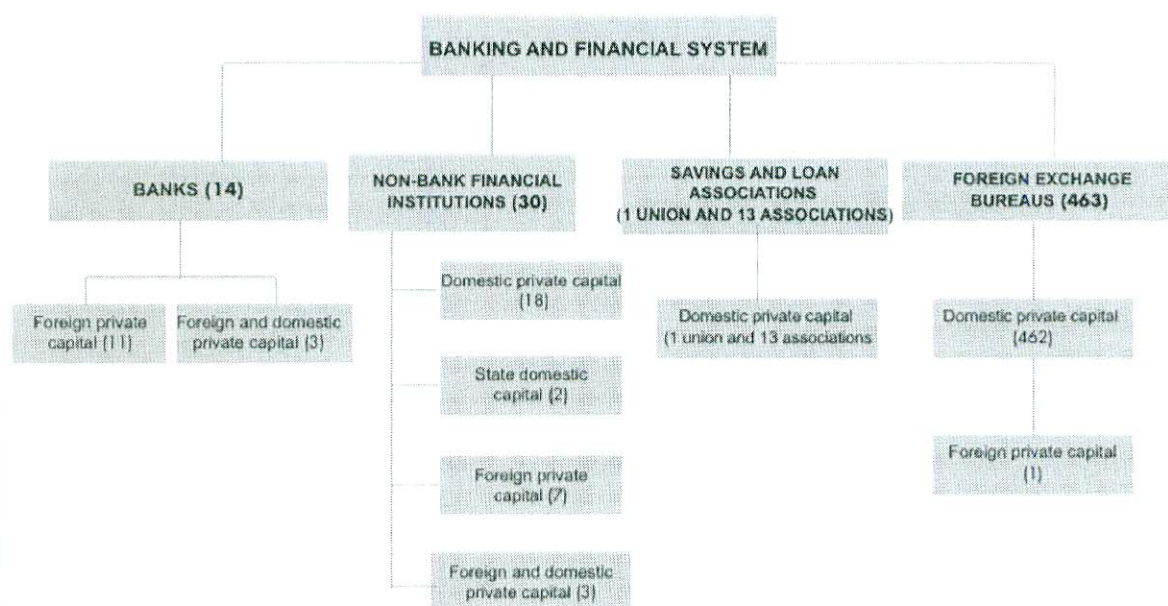


Figure 1 Financial and banking sector structure and ownership

Source: Bank of Albania Annual Supervision Report (2018)

Financing opportunities for Small and Medium Enterprises (SMEs) in Albania are a topic of great importance, since the SMEs play the biggest role in the development of the country. Access to Finance provides the businesses with the financing they need. The financial system as one of the most important pillars for the development of a society has its impact on the functioning of a state. In OECD (2018) it is suggested that the South East Europe economies should also prioritize access to finance by fostering alternative sources of financing and venture capital. A

commitment to making finance accessible would benefit SMEs, as well as improve conditions for all market participants by opening excessively restrictive credit markets.

Likewise, foreign direct investment and SME linkages should be strengthened by prioritizing long-term and sustainable investments in high-skilled and creative sectors. The region should focus on anti-corruption co-ordination, including offering more robust whistleblower protection across the economy. According to ERP (2019-2021) the economic growth rate of Albania has continued to accelerate during the cumulative nine-month period of 2018 and is expected to continue the gradual growth in 2019-2021. After the increase of 3.84% in 2017, the GDP grew 4.35% over the nine-month period of 2018 and is expected to gradually continue some acceleration reaching 4.5% in 2021, supported by improved macroeconomic fundamentals. In the Bank of Albania Quarterly Report 2019/II it is stated that due to the accommodative monetary policy it is enabled the creation of favorable financing conditions. Domestic financial markets operate amid a calm environment, with low interest rates, low risk premiums and a stabilization trend of the exchange rate. As a result, the pace of credit growth has improved. Adjusted for the exchange rate and written off loans, the portfolio of credit to the private sector recorded 6% annual growth in the first quarter of 2019. The performance continues to be supported by the expansion of credit in Albanian Lek, which accounts for around 48% of total credit. Banks eased the credit terms and conditions of loans to households. In parallel, developments in recent months point to a more balanced performance of the credit portfolio, with an upward contribution by both households and enterprises. Furthermore, as the report states, the underway consolidation of the banking sector, the continuous reduction of credit risk, and the expected demand growth create the premises for a sustainable growth of credit in the future. Yet, the materialisation of this projection requires that banks adopt a more active approach to lending. Their approach toward enterprises is more conservative. The balance of risks on their medium-term projections remains tilted to the downside, both in the short and in the medium term. They are related mostly to uncertainties surrounding the external environment, duration and impact from the exchange rate appreciation on inflation, loan supply improvement and, lastly, the tense political situation at home.

According to Kalluci (2019) bank lending after 2004 was mainly performed in foreign currency (initially in Dollars and then in Euros). There were two main reasons for foreign currency lending: first, the cost of foreign currency loans was lower for borrowers, as interest rates were



significantly lower for these currencies ; and second, the borrowers filed more claims high for foreign currency loans. Business borrowers needed foreign currency funds, for finance the purchase of raw materials (working capital loans or in the form of overdrafts), to invest in new product lines or technologies expanded the buildings where they operated. Even individual borrowers preferred foreign currency loans to finance the purchase of their homes, the price of which was also quoted in foreign currencies (first in Dollars and then in Euros). But later banks began to lend in local currency also, contributing to the increase in the credit weight of Albanian Lek, in the total portfolio from a share of 16% in 2004, to about 44% at the end of 2017. The BoA in their 2019/II Quarterly report state that non-price terms and conditions of new loans to enterprises, according to commercial banks, tightened slightly in 2019 Q1, compared with the previous quarter. The main factors that led to the tightening of credit conditions to enterprises were the reduction in loan size and the increase in collateral requirements relative to the size of the loan.

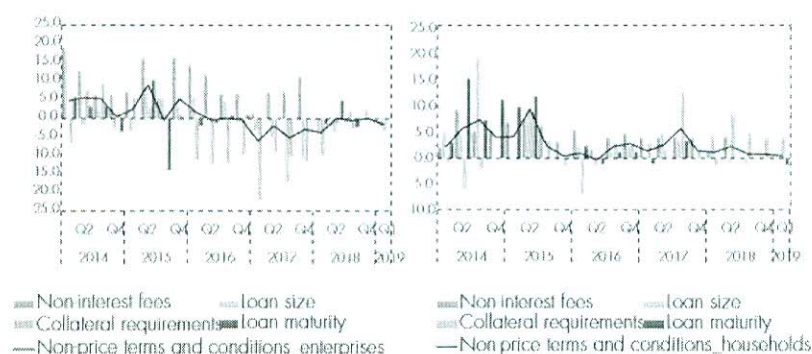


Figure 2 Non-price terms and conditions of lending determinant for loan to enterprises and households

Source: Source: Bank of Albania Annual Supervision Report (2018)

However, as from ERP (2019-2021) the quality of bank credit has continued to improve mainly as a result of write-offs, repayments and ensuing loan reclassification. The decline in the stock of NPLs has been accompanied by a larger decline in the loan loss provisioning, which has resulted in a moderate drop in the NPL coverage ratio (with specific provisions).

ERP (2019-2021) also when focused on bank lending explains that at the end of September 2018, the total loan portfolio of the banking sector was equal to ALL 586 billion. In nominal terms, the credit portfolio shrunk by about ALL 20 billion or by 3.5% yoy. After a period of modest annual



growth in the range of 1-2% between mid-2016 – end of 2017, the growth in the total credit stock came to a halt in Q1-2018 and turned negative over Q2- and Q3-2018. The amount of lost loans that were written off from the banks' balance sheets in the last 12 months to September was ALL 10 billion. This resulted in an annual decline of 33% in the stock of lost loans. Foreign currency loans continue to account for more than half of the total credit stock (57%). The stock of Lek loans contracted by 2.1% yoy and credit in foreign currency contracted by 4.6% yoy mostly as a result of the appreciation of Lek against the Euro. In the absence of the exchange rate effect, the annual change in the foreign currency credit would be +0.7% (instead of -4.6%) and total credit contraction would be equal to -0.5% (instead of -3.5%). Long term loans and loans for the purchase of real estate combined, represent about 53% of the total amount of outstanding loans. Both types of long term loans have recorded a steady, albeit small annual growth rate over the last three years. The stock of credit to the private sector has been declining steadily over the last 4 years, partly as a result of weak new lending and partly due to the reduction in the stock of nonperforming loans. During the first 9 months of 2018 the stock of loans held by the private sector shrunk by about 5% or ALL 11 billion. Credit to households has continued to increase at an average annual rate of 5-6% and its share to the total stock of loans has jumped to 31% in September 2018, from 25% in December 2014.

Regarding the risks, the credit risk quality has continued to improve over the first nine months of 2018 although at a slower pace, liquidity risk in the Albanian banking sector is low, the exposure of the banking sector to market risks remains significant although it has diminished slightly over the first half of 2018.

Returning on the assessment of access to finance efforts from EIB (2016) and OECD (2018) it is stated that although the actors of the economy could increase their efforts to have a better development of credit system. One significant reason for the evidence gap is that most SME economies lack statistical information on SME financing as the data are not disaggregated by enterprise size. Data on the stock and flow of SME loans, interest spreads between large and small enterprises, collateral requirements for SMEs, and non-performing loans would help to build a better understanding of SME-specific financing gaps to identify suitable and evidence-based SME financing policies. Albanian government is making efforts to ensure policy coherence and co-ordination in designing programs to support SME financing and to improve SMEs' access to finance. Also, the coverage of credit information services could be expanded.

Credit information services compile data on the credit histories of borrowers who are active in a financial system. They help to improve risk management for lenders by decreasing information asymmetries on the default risk of all borrowers. Public credit bureaus are usually managed by the central bank, mainly for supervisory purposes, while private credit bureaus are often established by financial institutions. From BoA, AAB and its member banks and EBRD the recommendations of the Feasibility Study agreed that the establishment of such a credit bureau shall address the lack of a credit scoring system in Albania.

According to ERP (2019-2021) credit developments, in terms of currency, confirm higher growth of credit in lek compared to credit in foreign currency. Despite this, the credit portfolio in lek recorded a lower growth rate in the second quarter (6.3%) compared to the first quarter (7.0%). This slowdown partially reflects the impact of lower lending to enterprises, which peaked in the second quarter of the previous year. The performance of credit in foreign currency carries to a large extent the impact of the exchange rate. Banks report a tightening of lending policies to enterprises, which reflect the costs of the funds, bank's capital and liquidity positions, their perception on risk exposure as well as their risk appetite. On the other hand, banks eased their lending standards to households during this quarter. The generally more positive approach of banks toward households is reflected by the eased collateral requirements for credit coverage. The other standards of these loans remained like the standards of the previous quarter. Based on the semi-annual Survey on "Financing and Borrowing of Enterprises in Albania" for the first half of 2018, it is noted that the cost of credit continues to be considered as the main factor that makes it difficult to obtain a bank loan, especially for small and medium-sized enterprises. Following the cost of the loan, the cost of meeting the requirements of the bank continues to be a considerable difficulty, for all three groups of enterprises in size allocation, followed by an assessment of the conditions for loan guarantees and the uncertainty of the bank's claims; bureaucratic procedures. However, even for the latter, small and large enterprises give downward estimates, expressing improvement over the period analyzed compared to the previous one. Enterprises that have decided not to apply consider the loan process to a bank to be difficult, and this seems to be most often claimed by small and medium-sized enterprises. For the first semester, 2018 there is an increase in the share of those who consider this process difficult or who claim that it is easier to borrow from alternative sources.



According to the Law "On the Bank of Albania" and the Law "On banks in the Republic of Albania", the Bank of Albania may issue sub-legal acts in the form of regulations, guidelines, decisions and orders, to be implemented by all banks and other institutions licensed by the Bank of Albania. The set of the sublegal acts constitutes the regulatory framework of supervision, which limits the risk taken by banks and other institutions licensed by the Bank of Albania in the course of their activity. Basel Committee Documents, as well as European Union Directives, Regulations and the Guidelines serve as the main guideline for compiling this regulatory framework. Regulatory acts approved are licensing, supervisory and general regulatory acts. The Bank of Albania approves regulations setting out the conditions, requirements, deadlines, and documentation and procedures for the licensing, approval of additional activities, obligation for informing the Bank of Albania, prior approvals for exercising the activity and legal reorganizations of licensed institutions, supervised by it. Each of the regulations will feature the decision of its approval, subsequent decisions for amendments to the relevant regulation over the years (if any), and an integrated version. As of the Bank of Albania Licensing regulations there exist the following regulations:

- Regulation 14/2009 "On granting the license and the exercise of banking activity of banks and branches of foreign banks in the Republic of Albania", integrated version
- Regulation 1/2013 "On the granting of license to non-bank financial institutions", integrated version
- Regulation 31/2007 "On licensing, organization, activity and supervision of foreign exchange bureaus", integrated version
- Regulation 104/2016 "On licensing and activity of savings and loan associations and their Unions".

As of the supervision department the Bank of Albania approves regulations that define the requirements, deadlines, and procedures in order to conduct a safe and stable activity by licensed and supervised entities.

Each of the regulations will feature the decision of its approval, subsequent decisions for amendments to the relevant regulation over the years (if any), and an integrated version.

- Regulation 59/2008 “On the transparency for banking and financial products and services”, integrated version
- Regulation 72/2017 "On Banks Recovery Plans"
- Regulation 4/2017 "On the consolidated supervision"
- Regulation 105/2016 "On risk management in the activity of savings and loan associations and their Unions"
- Regulation 67/2016 "On minimum security requirements regarding premises where banking and financial activities are conducted and transportation of monetary values", integrated version
- Regulation 67/2015 “On internal audit system”, integrated version
- Regulation 48/2015 “On consumer credit and mortgage credit"
- Regulation 69/2014 "On the bank’s regulatory capital", integrated version
- Regulation 10/2014 "On the risk management from large exposures of banks", integrated version
- Regulation 48/2013 "On capital adequacy ratio", integrated version
- Regulation 2/2013 "On risk management in the activity of non-bank financial institutions", integrated version
- Regulation 63/2012 “On the core management principles of banks and branches of foreign banks and the criteria on the approval of their administrators”, integrated version
- Regulation 27/2012 “On the establishment, licensing and functioning of the bridge bank”
- Regulation 62/2011 “On credit risk management from banks and branches of foreign banks”, integrated version
- Regulation 42/2011 “On the authorized chartered auditors of banks”
- Regulation 3/2011 "On the operational risk management"
- Regulation 67/2010 "On the Content of Information and Operation of the Credit Registry at the Bank of Albania"
- Decision 69/2010 “Fees for using information in the Credit Registry of the Bank of Albania”
- Regulation 48/2010 “On open foreign exchange positions risk management”
- Regulation 71/2009 “On liquidity risk management”, integrated version



- Regulation 70/2009 “On foreign exchange transactions”, integrated version
- Regulation 45/2009 “On the reports at the Bank of Albania accordingly to the Unified Reporting System”, integrated version
- Regulation 44/2009 “On prevention of money laundering and terrorism financing”, integrated version
- Regulation 60/2008 “On the minimum requirements of disclosing information from banks and foreign bank branches”, integrated version
- Regulation 57/2007 "On risk management of the activity of branches of the foreign banks", integrated version
- Regulation 32/2006 “On the use of information and communication technology in entities licensed by the Bank of Albania”
- Regulation 28/2005 "On supervision of electronic banking transactions"
- Regulation 42/2001 " On bank's investments in the equity of commercial companies"

Regarding the access to bank finance as in OECD (2018) publication is stated that Bank lending is the most common source of external finance for all kinds of SME activities: starting up a company, meeting regular cash-flow and working capital requirements, expansion, innovation, and internationalization. In the Albanian economy could be eased security rights over non-fixed assets and weighted the benefits of expanding the use of intangibles as collateral against the potential risks. The economy could also consider introducing more flexible definitions of collateral and provision requirements for smaller loans. It should be reconsidered the use of subsidized interest rates given their market-distorting effects. While subsidies did help prevent a larger credit crunch during a period of financial distress, a more sustainable policy solution for the longer term could be the wider use of credit guarantee schemes. Public credit guarantee schemes should be designed based on international good practice standards such as those outlined by the World Bank and the Financial Sector Reform and Strengthening Initiative (World Bank, 2015). They should involve reasonable administrative costs and be targeted on under-served SMEs, such as innovative, female-led or export-oriented businesses. New schemes should include regular monitoring and evaluation to assess whether their objectives are being achieved. A new framework for cooperation between banks for a permanent solution of common borrowers is under consultation with the banking industry. Such initiative for out-of-court

settlement agreements is expected to enhance the cooperation between banks and bring them in a common ground against borrowers to avoid asymmetries of information in the decision-making process (ERP 2019).

## STUDY BEST PRACTICES IN LOCAL CREDIT SYSTEM

SMEs sector development is considered one of the main contributors of economic growth, employment and to chasten poverty. According to World Bank (2018) access to financial sources varies sharply around the world and due to data gaps it is difficult to measure the access to finance. However, the Banks have been focused in emphasizing the barriers that limit access to financial sources and offering solutions that might help the development of access. Collins et. al (2013) state that alternative financing sources, offered as financing opportunities, play an increasingly important role in helping business to access the finance they need in order to grow and contribute to the economy. So besides traditional credit coming from the banks there exist also institutions that offer sources of financing for SMEs. World Bank reports (2008; 2016) and OECD publications (2016; 2018) support the fact that without inclusive financial systems and policies that help enterprises overcome the access barriers it is difficult to obtain stability, growth, poverty reduction and fair distribution of resources and capacities. In a number of publications that focused on access to finance for SMEs and the extension of Alternative Financing Sources sub-dimension and Bank Financing from the World Bank, the OECD, and research papers from several authors, the emphasis has been put onto the fact that access to finance is crucial in today's world for businesses to start and grow and this can be done by traditional lending ways, public funds and by having the businesses presented to alternative sources of financing. Non-bank financing is growing but still plays a modest role in funding for SMEs (EIB, 2016). In Albania actually, non-bank institutions offer leasing, factoring, microfinancing and there is a small development of crowdfunding mostly of interest to the non-profit organization that prepare talk-shows and online funds gathering events for different purposes. There are various issues between the banking system and the shareholder companies such as the interest rate on loans, banks demand for collateral, banks' bureaucracy, banking commissions (Merollari, 2012). Alternative financing mechanisms are crucial for overcoming



- The Business Support Program has been developed to provide the Albanian small and medium enterprises (SME) with access to financing, in order to enable them to receive professional consultancy services tailored to their relevant circumstances, by providing

in Italy (PRODAPS 2019).

- The Credit Line of 36 million Euro, to support with soft loans the development of Albanian small and medium enterprises, will be used to finance SMEs project investments, business expansion or technology innovation. The Credit Line for SMEs provides for the provision of a more favorable interest rate and repayment period compared to those in the market for SMEs that want to purchase goods and services made

additional guarantee for the part covered by the Fund (PRODAPS 2019).

- The Albanian Guarantee Fund of 5 million Euro is a financial instrument created by the Government of Italy and Government of Albania under the Italian-Albanian Program for the Development of Albanian SMEs, which enables the provision of guarantees in the form of collateral to stimulate crediting from financial institutions for micro, small and medium (SME) enterprises that face difficulties in accessing to bank loans due to insufficient guarantees. In practice, the Albanian Guarantee Fund substitutes those guarantees mainly required from micro, small and medium enterprises to obtain a loan, thus reducing the risk in the guaranteed amount. By means of this credit guarantee SMEs have the possibility to obtain cheaper loans compared to those in the market without any

SMEs (PRODAPS).

is for the implementation of the Italian-Albanian Program for the Development of Albanian processing sector. The SME lending scheme established by the governments of Albania and Italy budget supports different grant schemes for the promotion of SMEs, agriculture and the agro-However, there are steps being taken to improve and boost the local credit system. The state

presented to non-bank financing options (OECD 2018).

individual business projects and efforts need to be made in this direction so that business can be gaps in bank financing, as well as to help SMEs find adequate funding models for their

good experiences and practices, which will have an impact in increasing their economic performance and competitiveness. The Business Support Program (BSP) is an initiative regulated by the "Integrated Assistance Program for the Development of Albanian SMEs" (micro, small and medium enterprises) – IASME” (an Italian - Albanian cooperation program) ratified by the Parliament of Albania with Law 19/2014 on 27/02/2017 (PRODAPS 2019).

Albanian Investment Development Agency (AIDA) was funded and works to attract foreign investment, increase the competitiveness of the Albanian economy through the support for small and medium-sized enterprises (SMEs), as well as through innovation. The direct contribution of AIDA in the economic development is evidenced through:

- Facilitation and support of direct investments in Albania;
- Increase the competitiveness and innovation capacity of Small and Medium Enterprises (SMEs);
- Encouragement and support to exports of goods and services (AIDA 2019).

The Albanian Government in support of small and medium enterprises (SMEs), is providing these financial schemes managed by AIDA, to increase the competitiveness of SMEs, strengthen their productive capacities and facilitate the access to the market.

- Competitiveness Fund
- Creative Economy Fund
- Enterprise Support Fund for "Start - Up " Initiative
- Innovation Fund (AIDA 2019).

Apart from that, AIDA helps the SMEs to increase the competitiveness and in order to evaluate the problems of the business it creates a tour of activities called “Info DAY” and B2B meetings with Albanian Companies. The goal of these projects as the experts explained is to promote and inform on the funds that AIDA manages for Albanian SMEs, identification and creation of contacts with new companies, increasing access to finance and cooperation with business actors



(Municipalities, Chambers of Commerce, and Business Associations). Each year, the persons that obtained the funds are controlled using a questionnaire that included information regarding the activity, use of funds, problems, etc. Moreover, these activities are also done with the approval from the Ministry of Economy. In Albania, as already mentioned more than 99.9% of enterprises are small and medium-sized enterprises, or otherwise called SMEs. As such, this sector is of particular importance to the country's economy and support for the SMEs sector is one of the major priorities of the Albanian government.

- The European Fund for Southeast Europe aims to foster economic development and prosperity in the Southeast Europe region and in the European Eastern Neighborhood region through the sustainable provision of additional development finance, notably to micro and small enterprises (MSEs) and private households.

Regarding the financing opportunities from banks and non-bank financial institutions in Albania, the alternative financing sources are new to the financing opportunities offered to SMEs and actually make up only a small part of the financing portfolio, the major part is dedicated to loans. The gross credit portfolio by NBFI's from the Bank of Albania Annual Supervision Report (2018) is as follows :

Financial activities (in ALL bln)	December 2017	December 2018
Lending	11.1	12.7
Financial leasing	6.6	6.9
Microcredit*	5.8	8.4
Factoring	0.74	0.56
Gross Portfolio	24.21	28.6

Source: Bank of Albania.

\* Compared with the previous year, the methodology of the classification of loans has changed.

Figure 3 Gross Credit Portfolio by NBFI's from the Bank of Albania

Source: Banks of Albania Annual Supervision Report (2018)

Leasing is one of the first instruments that are available to SMEs. Factoring can broaden access to finance since it is based on a business' accounts receivables rather than on its overall creditworthiness. An often cited, means of financing is micro-finance. It is particularly useful for small business owners with restricted access to more institutionalized sources of finance. It can help them in the initial business idea stage that requires only modest investment. A more

contemporary means of raising funds – away from either the traditional banking system or equity markets – is crowdfunding. It involves raising capital by asking a large number of individuals for small amounts of capital which may take the form of a donation, loan or an equity stake. The state institutions even though are not responsible for offering leasing, factoring, microfinance and crowd funding, help by defining regulations, procedures, reforms that affect financing opportunities offered to businesses. The role of BoA is to license, regulate and supervise: Banks, Non-Bank Financial Institutions that provide leasing, factoring, microfinance, money exchange and foreign exchange bureaus. The Bank of Albania provides the protection of financial stability. Also, the Bank of Albania implements risk-based supervision on institutions licensed by it. The financing of SMEs in Albania is controlled by the Ministry of Economy. From the Ministry are designed projects with the approval from the government to help SMEs access finance. Furthermore, on the part of alternative finance sources the duty to further develop them is in the hand of the financial institutions and the Bank of Albania. Ministry of Economy functions regarding financing are related to the work of AIDA (Albanian Investment Development Agency) for some projects. Apart from other objectives the ministry is responsible for the completion and steps that lead to the completion of SEE 2020 strategy so that the promotion of access to finance as part of the pillars of the strategy is developed.

In line with the recently adopted Macroprudential Policy Strategy, BoA has worked on finalizing methodologies, indicators and databases related to signalling indicators and assessment of systemic risk, as well as the implementation of a number of macroprudential instruments. Over Q3-2018 BoA has started the consultation process with the banking sector and other stakeholders with a draft regulation that introduces several macroprudential capital buffers (conservation, countercyclical, systemic risk and systemic importance buffers). The approval of the framework, which is expected during H1-2019, will allow for the implementation of these buffers over a period 5 years. The overall framework, in line with EU directives, will represent a solid approximation with international standards and guidelines in this area (ERP 2019). Part of the reforms for 2019 has been also the implementation of the remaining measures of the NPL resolution strategy, also with a view to addressing factors hampering access to finance for corporates and focus on Credit Registry in order to facilitate and to establish the appropriate infrastructure in the context. Regarding loans to enterprises they slowed down its growth rate to 3.5%, in 2018 Q2. It appears volatile, both in terms of short-term monthly developments and



annual terms, due to unsteady developments in the liquidity loan portfolio (2.6%). This portfolio is generally characterized by large fluctuations, depending on the short-term financing needs of enterprises. Investment loans (4.3%) performed better and they largely support the growth of credit to enterprises. However, the improvement on Credit registry will impact the way banks can rate their borrowers and increase their quality of information, hence improve the way clients compete for bank financing. The framework agreement on debt restructuring out-of-court will reduce administrative burden for both the borrower and the banks, and again will positively affect competition for bank financing.

#### FOCUS ON INSTITUTIONAL FRAMEWORK AND IMPLEMENTED POLICIES ON PRACTICAL SUPPORT TO CREDIT

In the OECD (2018) competitiveness report it is evaluated that in the country are taken steps to establish institutional and regulatory frameworks for access to finance; Have developed frameworks for timely payments and insolvency and also made progress in developing asset registers and credit information systems; Efforts have been made to improve insolvency frameworks to tackle lengthy bankruptcy procedures and reduce administrative backlogs; Progress has also been made in delineating between liquidation and restructuring, and introducing clear priority schemes; Have implemented SME financing support programs. These are primarily credit guarantee schemes and grants or loans at reduced interest rates.

However, as in the OECD (2018) is explained the demonstrated financing gap in the SEE economies results from constraints on both the supply and demand sides. On the supply side, frequent issues arise from a lack of available credit, punitive interest rates and unattractive market opportunities, while on the demand side, a lack of entrepreneurial training, ineffective business strategies and inadequate private assets all hamper business growth. Although demand-side barriers represent an important constraint on access to finance, supply-side barriers, including high upfront collateral requirements, are often responsible for immediate restrictions on credit. Ultimately, both demand- and supply-side constraints on finance should be addressed through strategic policy interventions.

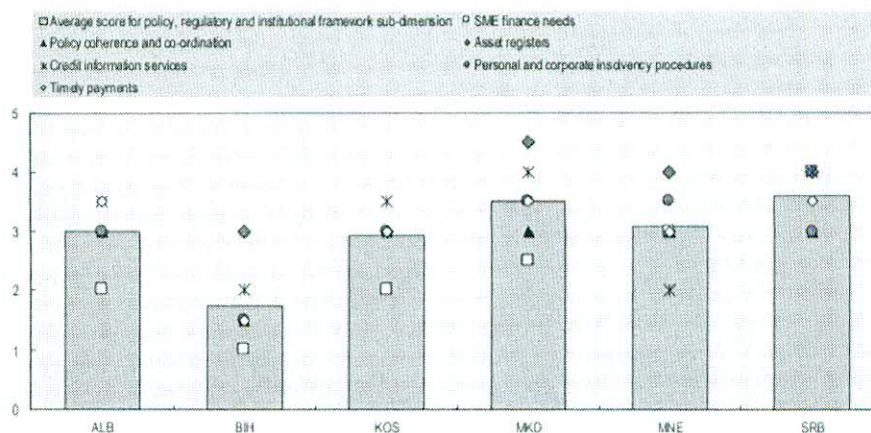


Figure 4 Policy, regulatory and institutional framework

Source: Competitiveness in South East Europe: A Policy Outlook 2018, Competitiveness and Private Sector Development (OECD 2018)

From OECD (2018) publication on competitiveness, in the access to finance dimension, it is stated that efforts to ensure policy coherence and co-ordination in designing programs to support SME financing are being done, but there is room for improvement. Asset registers and credit registries/bureaus (discussed in the next section) are two important institutions that help to level the playing field in lending relationships by providing information on the creditworthiness and business performance of SMEs. When this information is more limited for SMEs than for larger enterprises, banks can perceive SMEs as presenting greater risk. This can mean that SMEs have to meet high collateral requirements for secured transactions and have more limited access to credit. Albania has cadastral system to register land and real estate, and record its value and ownership, as well as any existing pledges over the asset but this service is not yet offered online making it more difficult to access information and it does not yet cover the whole territory, although it is making efforts to provide both online access and full coverage within the next few years. In Albania, exist a notice-based register making it easier to administer and has lower costs. Besides that, important institution are also the ones offering credit information services that compile data on the credit histories of borrowers who are active in a financial system.

	ALB
Coverage of public credit registry	38.9
Coverage of private credit bureau	0



Figure 5 Coverage of public and private credit bureau

Source: Competitiveness in South East Europe: A Policy Outlook 2018, Competitiveness and Private Sector Development (OECD 2018)

Albania has a public credit registry which covers around 40% of adult population but doesn't have yet a private credit bureau. Both the BoA and the Albanian Association of Banks (AAB) and its member banks, agree that the establishment of such a credit bureau shall address the lack of a credit scoring system in Albania, which is foreseen as a measure for the reduction of NPLs in the country in the Inter-Institutional Plan of Measures drafted by the authorities for this purpose. Hence, the AAB has undertaken the initiative of developing a private credit bureau in Albania. EBRD (European Bank for Reconstruction and Development) now intends to support the AAB with technical assistance during the setting-up phase of the credit bureau. Besides that, commercial banks together with the Albania Agribusiness Support Facility are joining forces to increase local farmers' and agribusiness companies' access to finance, especially in remote regions of the country. The EBRD, with the government of Albania, is supporting a portfolio of up to €35 million of eligible loans to the sector, risk-shared with its partner Raiffeisen Bank Albania. The instrument benefits from a First Loss Risk Cover contributed by the government of Albania. Agribusiness is a vital sector of Albania's economy. It provides employment for more than 50 per cent of the population in rural areas and accounts for around 20 per cent of the country's GDP. However, the sector remains underserved by financial institutions, with loans to agribusiness accounting for only 2 per cent of total lending to the economy. Launched by the EBRD and the government of Albania in 2016, the Albania Agribusiness Support Facility (AASF) is addressing this challenge by improving access to finance for local agribusinesses through dedicated credit lines or by sharing the risk of lending to the agribusiness sector.

The BoA is the administrator of credit registry system, since its start of operation on 3 January 2008. The registry provides the reporting institutions during the process of credit analysis and decision-making with additional information on the borrower's history. Reporting institutions to the Credit Registry are all the banks and other lending non-financial institutions, licensed by the Bank of Albania. The Credit Registry generates the Borrower's Report with information on the amount of loan, its repayments, overdue amounts, warranties, data on the loans in which the borrower appears as a related person, and loan classification. Since April 2016, this Report

identifies loans under an execution order, restructured loans and issued loans (BoA 2019). Since 27 July 2012, the Bank of Albania publishes interest rates and commissions for products and services that banks offer to the public, on its website in an aggregated and simplified table. Banks report these data every three months. The publication of these data aims to improve transparency standards and consumer protection by informing them on the most convenient options for loans, deposits, current accounts, bank cards, etc. The published information helps clients to find a favorable and convenient option in accordance with their financial situation, and contributes to fostering market competitiveness.

At the institutional level, the Bank of Albania, in accordance with the legal hierarchy of the objectives regarding the policies and the functions it implements, ensures their maximal synergy. For this purpose, the organization of the internal institutional structure supports the definition of responsibilities at each stage of drafting and implementing policies and promotes the timely exchange of information and critical assessments. As a result of this process, the final decision-making of the Bank of Albania is expected to be well informed and to reflect the contribution by the relevant policies. The Bank of Albania's structures that are more directly and sequentially involved in the implementation of the macro-prudential policy are:

- *Financial Stability Department* - monitors systemic risk indicators, develops the methodologies for its assessment and the operationalization of macro-prudential instruments; proposes the Financial Stability Advisory Committee the instrument and manner of implementation, monitors the impact of the instrument, prepares reports and analyses for the systemic risk performance, as well as assesses the stability of the financial system;
- *Financial Stability Advisory Committee* - assesses the performance of systemic risk, selects the macro-prudential instrument and determines its implementation; monitors the coordination of work for discussion within the institution and the preparation of legal and sub-legal acts necessary for the implementation of the instrument; formulates the macro-prudential stances for the Governor or the Supervisory Council in the framework of the Bank of Albania's role in safeguarding financial stability;



- *The Governor* - communicates the stance of the Bank of Albania on systemic risks and the financial system stability, and decides on the implementation of the macro-prudential instrument if this is possible according to the decision-making procedures;
- *Supervisory Council* - reviews and approves the reports and analyses of the Bank of Albania on the assessment of the financial stability situation; is informed on the assessments on the manner of implementation of the macro-prudential policy; approves sub-legal acts necessary for the implementation of the relevant instruments of macro-prudential policy.

The actors that help boost the development of credit system in Albania are implementing each year policies that help access to credit for SMEs. There are policies designed to increase the enterprises possibility to access bank funding. Agencies that offer micro-credit have helped SMEs to obtain small loans. Microfinance and credit unions especially in the recent years have increased their activity and small enterprises receive help also from foreign fund investments. However, the upcoming procedures and policies taken to meliorate the access to bank funding are expected to increase the level of loans given to SMEs. The EBRD has made available a fund intended for on-lending to women-led small businesses in Albania, this loan will help to narrow the gender gap in access to finance and know-how that can hold women back from fuller participation in the economy.

## REFERENCES

- The World Bank in Albania Country Snapshot (April 2019) <http://pubdocs.worldbank.org/en/555781555015319241/Albania-Snapshot-Apr2019.pdf>
- Bank of Albania Annual Supervision Report (2018) [https://www.bankofalbania.org/Publications/All\\_publications/Annual\\_Supervision\\_Report.html](https://www.bankofalbania.org/Publications/All_publications/Annual_Supervision_Report.html)
- Bank of Albania (2016). *Annual Supervision Report*
- Bank of Albania (2018). *Annual Supervision Report*
- Bank of Albania (2019). *Quarterly Report 2019/II*
- European Investment Bank. (2016). Assessment of financing needs of SMEs in the Western Balkans countries; *Country report: Albania*.

- Kalluci, I. (2019). Credit in Albania: Trends, Characteristics, Equivalent and the factors that determine.
- Totojani, O. (2010). SME'S ROLE IN THE ALBANIAN AGRICULTURAL ECONOMY AND THEIR LEGAL FRAMEWORK BEHIND IT. *Research Journal of Agricultural Science*, 42(3), 888-897.
- OECD (2016), Competitiveness in South East Europe: A Policy Outlook, Competitiveness and Private Sector Development, OECD Publishing, Paris. <http://dx.doi.org/10.1787/9789264250529-en>
- OECD (2018), Competitiveness in South East Europe: A Policy Outlook 2018, Competitiveness and Private Sector Development, OECD Publishing, Paris. <http://dx.doi.org/10.1787/9789264298576-en>

## WEBSITES

- <http://aida.gov.al/home>
- <https://aab.al/>
- <https://www.bankofalbania.org/>
- <https://www.prodaps.al/index.php/en/sme-financing/sme-guarantee-fund>