



Research on Financial Needs of Agro-Processing Industry

Report by: CBS CREATIVE BUSINESS SOLUTIONS

(Submitted in March 2014)

(Edited by RisiAlbania- October 2014)

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List of Abbreviations

AB	Agro Business
AIDA	Albanian Investment Development Agency
ALL	Albanian Lek
AP	Agro-Processor
APP	Application Data Entry
ASC Union	Albanian Savings and Credit Union
AZHBR	Agriculture and Rural Development Agency
BKT	Banka Kombetare Tregtare
BSP	Business Service Providers
CBS	Creative Business Solution
CCI	Chamber of Commerce and Industry France -Albania
CCIA	The Italian Chamber of Commerce in Albania
DCA	Developing Credit Authority
FDI	Foreign Direct Investments
FI	Financial Institution
FIAA	Foreign Investors in Albania
MFI	Micro Finance Institutions
IPARD	Instrument for Pre-Accession Assistance for Rural Development (EU)

WHY AREN'T AGRO-PROCESSORS ACCESSING ADEQUATE FINANCIAL SERVICES?

Agro-processors Perception and their Needs for Financing

AP's see their business growth related to new investments in working capital, equipment and technology. Unlike other businesses, however, there is a disconnection between financial products and AP's business needs. A total of 176 AP businesses representing 7 sub-sectors from over 11 main regions, representing 8% of total industry and 19% of total sector employees were interviewed to identify reasons, needs and potential solutions. High pricing, one-size fits all loan products and lack of eligible collateral are some of the main reasons contributing to an uneasy current relationship between the demand for credit (AP's) and FI's as providers of credit. While pricing is a complex topic with many dependencies, the need to provide tailored financial service solutions that address the complexity of AP businesses is imperative. In order for these solutions to enthusiastically be adopted, however, they must be sustainable, impactful and systemic, in order to add value for both providers of the services and its recipients.

AP's are generally unsatisfied with providers of financial services. According to them, the following reasons and immediate suggestions for improvements will increase access to financing:

- Simplification of the loan application process. According to 26% of the interviewees, the application process until approval time is too long and complicated due to documentation required and verification of financial statements. Typically a loan application takes a long time, cost money and the bureaucracy level is considerably. A revision of the list of document required for bigger loans would also be critical.
- Improvement of pricing policy of the credit application from FI's. Lower interest rates were one of the hottest topics during the interviews. Interesting proposals for lower interest rates up to 5% for loans in Euro, and up to 9 % for loans in ALL (Albanian Lek) came out from the interviews. Also, ten AP's proposed applying Fix Interest Rates from FI's, since it would be more convenient in terms of controlling and budgeting monthly expenses of the businesses.
- Collateral eligibility and acceptance from Banks and FI's is one of the main restrictions for AP's. Many businesses encounter barriers offering agriculture land as collateral, due to unmet eligibility criteria set by banks. Restrictions on agriculture land, as eligible collateral, exclude many new credit applications, thus policy changes in this regard will be conducive to agro-businesses.
- ¹Longer tenor for the investment loan would be desirable (up to 15 years) providing lower monthly installments and reflecting seasonality of the business activity.
- Increased level of transparency and no hidden costs related to credit application. Lack of information and transparency from bank employees leave customers quite often unclear for the interest to be paid, repayment plan and other general terms and conditions of the credit limit. AP's suggest fix administration fee for loan application instead of floating in percentage as actually happens. Those with longer experience in the market propose waving ²early repayment fees for lending products. Quite often the information related to prepayment fee and related penalties are missing.

¹ Longer Tenor - Longer Maturity Period of the Loan

² Early repayment Fees - Fix Commissions Applying From Banks For Repayment Of The Loan Outstanding Before Maturity Date

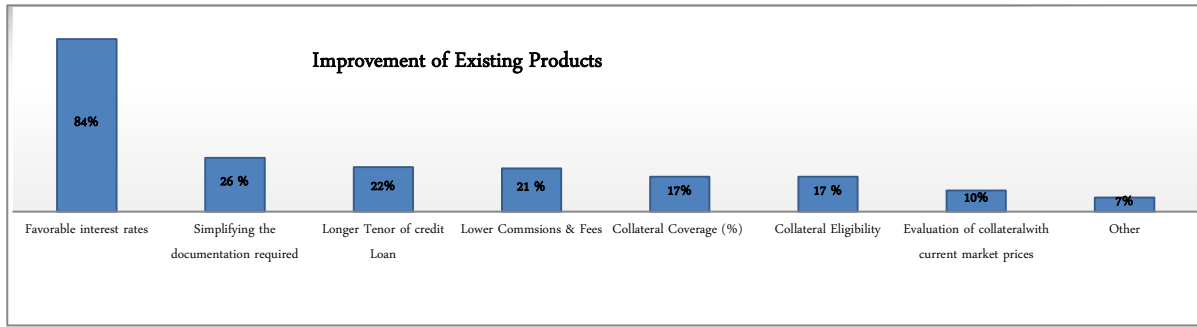


Figure 1 - The graph shows the answers in % over 176 interviews Based on frequent and combined answers

As a result of financing obstacles some AP's are not investing in new business opportunities. The reasons for keeping away from new investments in the business were mainly attributed to "lack of financial resources" and "uncertainty on overall macroeconomic situation in the country."

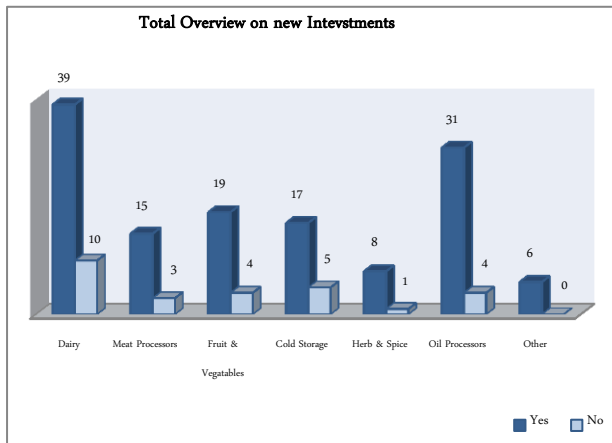


Figure 2: The graph shows the % over the total number of each sub sector

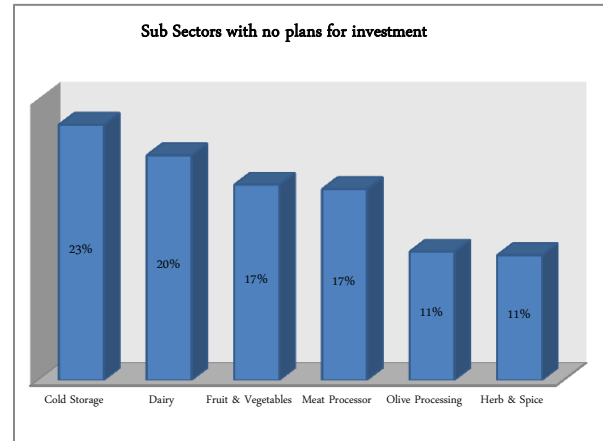


Figure 3: The graph shows the number over 176 interviews

Potential for Improvement of banking services (not loans) as seen from AP's

AP's do not possess adequate information about bank's financial services. This is reflected not only in their perception (highest problem reason) but also in their misunderstanding of banking products. According to them, banks should be more informative about service products offered to agro-businesses. "Bank employees never explained to me the whole range of other financial services offered to businesses", one of the women AP's interviewed says. They inform and explain in details only loans in certain time periods" she continues. This is due to internal strategies banks have for selling lending products at times of lower activities. Banks are slowly moving toward a more customer-oriented strategy vs product-oriented. Business customers expect banks to provide services that are simple to understand, tailored to their needs, and rapidly delivered. They also expect to connect in real time and on demand through whatever channel they prefer. According to the interviews, either AP's have no information (27% of them) about bank services or they are misinformed (73% of AP's) about banks services due to the following reasons:

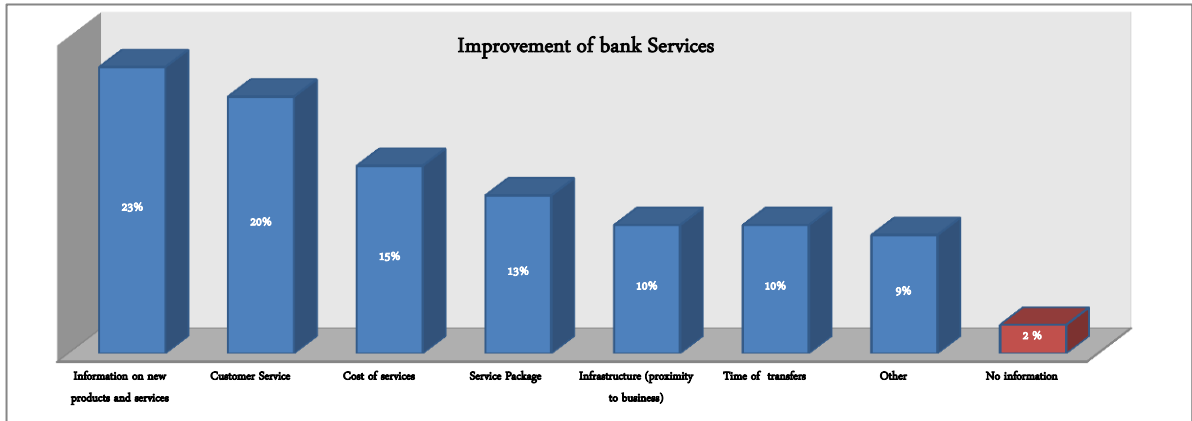


Figure 4 - The graph shows the answers in % over 128 interviews on what should be improved of existing services from banks

- Lack of updates and detailed information about financial services related to agro-business from front office bank employees. AP's require bank employees to be more informative about services in general and change their existing attitude, which is mainly focused towards lending products to customers. .
- Missing customer feedback (Voice of the customer) in designing and developing of financial products and services
- Lack of technical knowhow from the bank employee related to specific activities of agro-business
- Lack of transparency and detailed information explaining costs of services;
- Logistical distance or the distance between AP's and bank branches which are mostly located in urban area missing distribution channels. Bank's branches are typically located in key urban areas while agriculture lending requires physical presence in rural areas.
- Unsuitable e-banking products for agro-processors. Some of the AP's with a certain level of education, mainly located in rural areas away from bank-outlets, consider e-channels as a good solution to perform their daily routine banking activities. However, they consider the existing internet products offered from banks as not very good and user friendly. Several restrictions and limitations of the systems on performing payments and daily routine transactions have transformed the usage of e-banking mainly account viewer purposes
- AP's in rural areas appear to face the same obstacles on accessing financial products as their peers in urban areas. AP's in rural areas, however, face extra challenges performing daily or routine banking transactions – e.g. payment transactions - given that most banks are located in urban areas. Services performed by MFI's are only loan oriented and not applicable to payments.

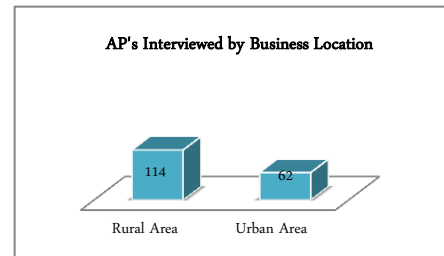


Figure 5 - The graph shows AP's location over 176 interviews

Underlying reasons identified by Agro-Processors as Obstacles for their Business Activity

The main obstacle faced by AP's is informality and unfair competition from unlicensed subjects operating in local markets. The unfair competition distorts the market competition rules. Product delivery at lower prices is due to lower costs of production, lack of food safety standards, deviation from taxes and lack of standards fulfillment. Another sensitive issue is financial liquidity of the business. Liquidity issues come mainly due to high level of receivables from their customers and low capital injection from Financial Institutions. Furthermore, lower capital injection from FI during the last years has significantly prevented new investments, especially in new technologies.

Other important issues AP's are facing are as following:

- Lack of supporting state policies as controlling, monitoring and application of penalties for rules breakers. Specific incentive schemes in support of production and sales are missing or are not appropriate for specific activities
- Low capacity of production to satisfy market demand
- High price of fuel used for equipment and machineries used in production process
- Infrastructure (bad roads, missing energy and water) and connection to small farmers in the remote areas are identified as problems mostly in rural areas
- Lack of knowhow, especially on the advanced techniques of production and new technology;
- Freezing of the Construction's permission from the state authorities is becoming a constraint in new investment on business premises and crediting form FIs. The need for investments is forcing businesses to construct even without a permission

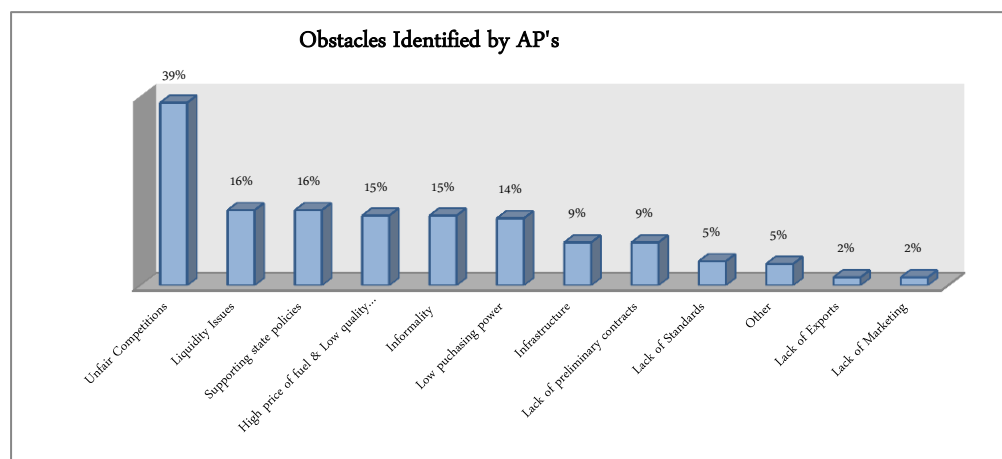


Figure 6 - The graph shows the answers in % over 176 interviews on obstacles are facing AP's

Financial Institutions Perception and Approach for Agro-Processors

FI have had slow procedures in relation to agro-lending. Agro-businesses receive only 4% in credits, despite the high contribution of agriculture to the GDP (40%). A gap of approximately €600 Million in financing is estimated for the sector to generate adequate growth. While a general perception exists that the Agro-business sector is a high-risk sector, interviews with banking managers in charge of credit loan portfolios reveal the opposite. Agro-business can be considered risky due to weather or other external factors, but not as a business activity. Furthermore a low NPL (non-performing loans)

level confirms the narrative. With few exceptions, FI's do not formally distinguish between agro-processors and other agro-businesses. Lending to agribusiness is not considered cost effective in terms of time and other expenses related to activity.

Financial Institutions determine their pricing policy based on industry credit risk, loan size, operational costs and collateral quality. Lending to agriculture and agro-processing is perceived as a high risk; therefore loan prices are relatively high as compared to other business segments. The negative perception comes from a lack of experience with the sector and a lack of substantial data to analytically evaluate the risk. Lower interest rate loans for AP's are inversely related to lending volume that the banking sector is willing to provide. In other words, the more FI's lend to AP's the lower the loan pricing will be. A positive momentum started by the government, as it increased the focus on agro-businesses. Sophisticated tools from FI's as well as further incentive policies by the government, donor and NGO projects assisting AP's to get more financing will positively affect loan interest rates.

The main challenge for banks remains the overall informality, including lack of financial statements, record keeping, ownership certification of buildings and equipment. Banks encounter several challenges financing AP's, because of a lack of adequate business plans for loan applications, collateral documentations and ownership to ensure banks guarantee requirements. Legislation for agricultural land has been an issue, causing many problems for banks. Other challenges of APs concern their lack of technical expertise related to new investments as well as their lack of organization and structuring (bookkeeping practices, financial statements, licenses, etc.); improvements would make them more attractive and reliable to financial institutions. Banks also recognize the lack of necessary investments on their side in development of adequate and sophisticated products addressing AP's specific business needs. Below is a more detailed list of challenges financing AP's:

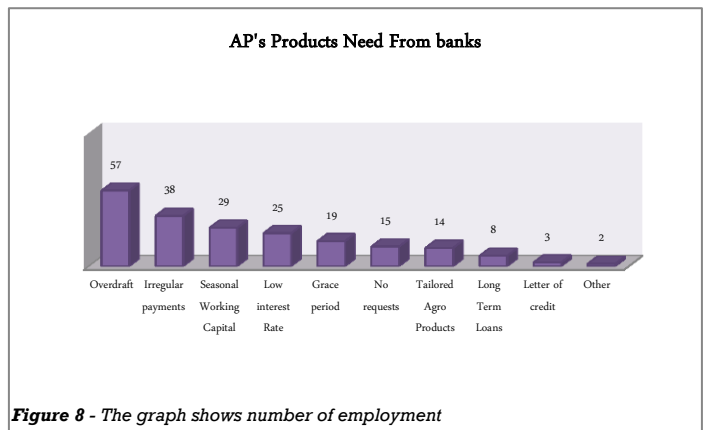
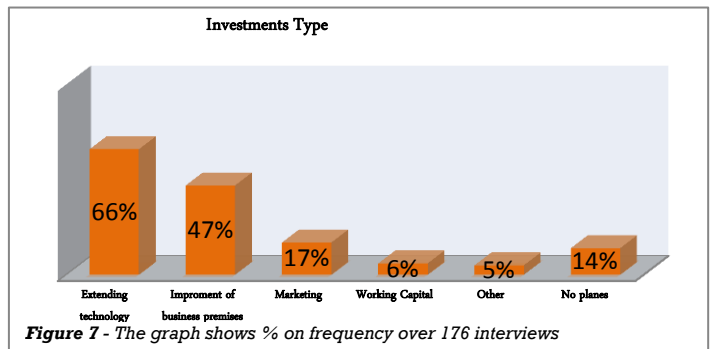
- Informality of the business related to lack of proper financial statements and record keeping of the business activity
- Collateral documentations related to collateral eligibility and ownership certification for land, buildings and equipment to ensure banks to pledge on the property. Legislation for the agricultural land has been a constraint and has created problems for banks in the lending process.
- Business Plan Development: Development of adequate business plans not only as a requirement for loan application, but using it as a guide for managing business activity in the future.
- Lack of formal business structures related to Accounting, Human Resource, Legal statuses, etc.
- Seasonality of the business activity, which increases the risk of default on monthly payments
- Coordination and cooperation between supply and demand in the market often is missing, which as a consequence increases the risk of the companies to create unnecessary stock and liquidity problems
- Low-level financial education of agro-processor and lack of technical expertise related to new technologies concerning their activity.

- Lack of a holistic marketing plan including specific branding for maintaining a unique standard of production for maintaining sustainable level of sales.

AGRO-PROCESSORS NEED FOR GROWTH AND TAILORED FINANCIAL SERVICES

Given the need for technology and product upgrade to reflect higher standards, both AP's and FI's see the continuous need for new investment as a necessity for a sustainable business growth. As a result, 86% of the interviewees are planning three new types of investments:

- Investment on extending **new technologies** and/or improvement of the existing ones in order to improve productivity and lower costs. New investments in technology do not necessarily imply reduction of employees despite an expected automation in AP processes. The new technologies may shift the type of jobs - more automated as opposed to manual. The notion is supported by AP's themselves. AP's see automation/new technologies connected to the improvement of quality and standards as key points to ensure sustainability in long terms, expanding local markets and penetrate into foreign markets. Increase market penetration and volumes of new sales will eventually require higher number of employees.
- Construction of business premises and new facilities in accordance to business activity to meet standards and sustain business growth
- Marketing investments for improving packaging, branding, product innovation and distribution. According to the interviews conducted, 135 AP's that are planning to make new investments said that they expect to increase the total number of employment with 1,770. In total, out of which 1,000 will be women and 1,139 young employees up to 29 years old. The below graphs shows the current employment for each sub-sector and each category (total employees, women and up to 29 years old). Unfortunately, this appetite for new investments does not reflect financial services supply to meet the demand.



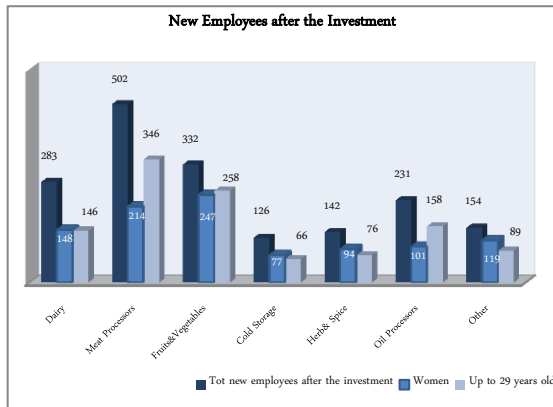


Figure 9 - The graph shows employment after the investment interviews

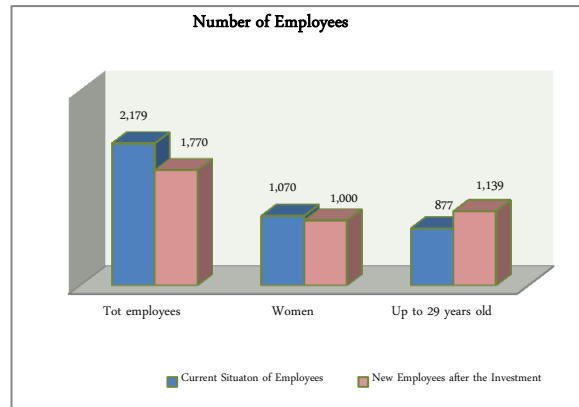


Figure 10 - The graph shows the frequency over 136 interviews for bank products needed from AP's

AP's use standard business loans, Investment Loans and Working Capital offered to all business customers (Micro, SE & Corporate). There is not any different approach applicable for agro-processing. While these products seem to be more appropriate for established businesses, they do not address specific deficiencies in agriculture such as lack of collateral, seasonality and informality. Interviews with banking managers and existing studies show that the following new products (or improvements) would make a great impact in providing much higher levels of financing for AP's:

- Overdraft with seasonal turn-over in the account related to specific business cycle
- Irregular repayment schedule of loan installments and grace period associated to seasonality of production and sales
- Seasonal Credit Line for working capital purposes.
- Tailored Agro Loans customized with seasonal production cycle. Tailored products are sub-sector specific, meanwhile irregular repayment plans are very common (for instance once every 3 months).
- Long term loans and very flexible in terms of application and repayment schedule
- Increase usage of Bank Guarantees and 3Letter of Credit for exports. Banks need to develop a simple and practical product for businesses that export their production abroad and/ or import of raw materials. A Letter of Credit is typically used by larger companies that export products out of the country. As there is a positive exporting trend and an increase in new investments in technology to meet European standards of production, it is expected that the number of AP's exporting their products will continue to increase. Exports growth will increase usage of LC, which as result will seek out FI's development of flexible and suitable product according to market needs.

Both banks and AP's agree that due to different business activity characteristics, AP's must be offered customized products and services. To deliver these products/services FI's must build internal capacities including dedicated organizational structures for managing and developing the business with agro-processors.

³ LC is a letter issued by a bank to another bank (especially one in a different country) to serve as a guarantee for payments made to a specified person under specified conditions. A written commitment to pay, by a buyer's or importer's bank (called the issuing bank) to the seller's or exporter's bank (called the accepting bank, negotiating bank, or paying bank)

Access to Finance for Women Entrepreneurs in Agro-Processing

Twenty out of the 176 interviewees that participated in the study were women entrepreneurs. The overall perception is that women face similar barriers accessing financial products, yet access to information and financing opportunities is more challenging for women. There was no evidence of gender discrimination – deliberate or hidden - from FI's. Women's concerns are related to the overall conditions of the whole sector and they require lower interest rates and longer maturity periods for loans. Often the access to information is limited, because business associations are typically “old boy's network” offering favors to each other. Networking among women entrepreneurs almost doesn't exist. More than 72% of AP's include their wife in the business in several roles, but usually not in a leading function. In most cases these are family businesses. While gender discrimination in financing does not seem to be present, cultural obstacles and lack of access to information and opportunities lead to a much lower rate of women entrepreneurs than men. The possibility of developing women's tailored financing approach could lead to a successful initiative from a business and social perspective.

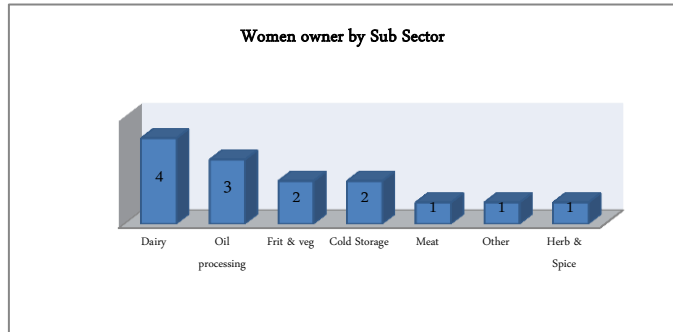


Figure 11 - The graph shows women owner by sub sectors

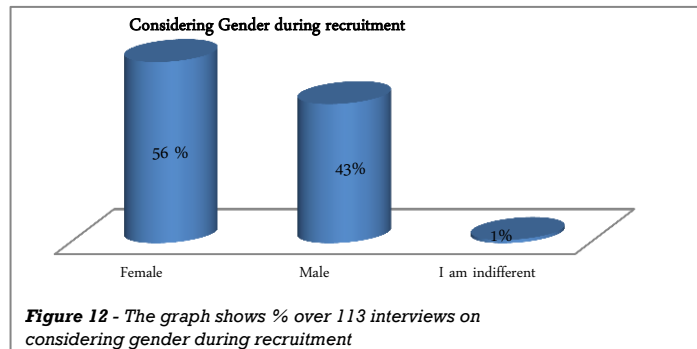


Figure 12 - The graph shows % over 113 interviews on considering gender during recruitment

OVERVIEW ON FDI'S ACTIVITY RELATED TO AGRO-BUSINESSES

Foreign Direct Investments remains crucial for the development of economy in Albania. The actual volume of FDI in agro-processing, however, continues to be limited, mainly due unclear strategies and action plans by the Albanian government. FDI agencies or the Chambers of Commerce are performing certain activities, for example providing information or establishing contacts, but their activity is not specifically oriented towards agro-processing. There is general interest on agro-processing sector, but focus and strategic objectives are missing.

Albanian Investment Development Agency (AIDA) remains the most important player in the market, which possesses the necessary capacities and capabilities to attract foreign investors.

However, due to the recent political changes that have implicated AIDA as well, it was impossible to conduct an interview and provide relevant information for development strategy of the institutions in the future.

Currently, neither Chamber of Commerce nor AIDA has a clear strategy dedicated to the development of agro-processors. Therefore, CBS suggests postponing the development of the intervention strategy related to FDI to a later period in time.

General Information of FDI Providers in Albania and Focus on Agro-Business

AIDA (Albanian Investment Develop Agency) is the largest institution dedicated to attracting foreign Investors focused on supporting FDIs, Innovation and SMEs. AIDA provides information and services to foreign companies seeking to invest in Albania. Generic information is provided on the business climate, investment opportunities and local partners. AIDA provides support to Albanian Small and Medium Enterprises, in order to enhance their competitiveness on the domestic and foreign markets, particularly to develop the export potential and stimulate innovation. AIDA's provides technical support to SME's through services like Market analysis, Networking, Special Grant for Albanian companies, Competitiveness Fund and Administrative procedures. Another important initiative is the Innovation Fund implemented through BRIC (Business Innovation and Technology Strategy). The Innovation Fund's role is to build and promote an innovation culture among businesses in Albania, by raising awareness about the benefits of innovation and technology.

The Albanian institution dedicated to attract foreign investors, AIDA couldn't provide information regarding institution strategy or future plans, because of the uncertain organisational structure of the organization related to new government changes.

Chamber of Commerce and Industry France -Albania (CCI) aims to strengthen the connections within the French speaking community in Albania. CCI France Albania counts among its members the largest companies in Albania, such as Societe Generale Albania , Green Technologies (CNR /GDF-Suez, Eurocopter/EADS) , Ally (SAFRAN Group) , Legal office Boga & Associates, Amadeus Group etc. The objectives are to unite, inform, encourage and assist the French business community and the French speaking community in Albania, and also to strengthen connections between Albanian and French companies by promoting economic / trade relations with France. Chamber of Commerce and Industry France - Albania contributes by organizing meetings that focus on exchange of experience among its members.

It distributes reliable information and provides logistical support services and assistance to its members and companies wanting to invest or develop a new business between France and Albania. The main aim of the Chamber of Commerce is to assist companies in their project implementation to develop trade relations in Albania or France. Chamber of commerce and industry offers to Albanian businesses expertise and information in four fields: services, information, prospect, development, and communication.

The Chamber of Commerce and Industry France -Albania are interested in providing services to agro-processors in Albania. In this regard, C.I.I is organizing the French Fair of Food and Agriculture, which will take place in Tirana on 24th of April. The objective of the fair is to permit French companies to explore the market of Balkan region countries such as Albania, Kosovo, Fyrum (Macedonia) and Montenegro.

This fair is addressed to the French companies from all sectors of food industry.

Nevertheless, CCI has not developed a strategy for supporting investments and commercial relationships dedicated to agro-processing.

Foreign Investors in Albania (FIAA) was established by several foreign investors in Albania. FIAA's mission is to support the success of its members by promoting a healthy business environment in the country, and providing high-quality business information and resources.

FIAA represents most of the FDI in Albania from different nationalities, including Italy, Greece, France, Germany, Austria, Turkey, Canada, Norway, UK, Switzerland, US, and a range of economic sectors such as banking and finance, construction, consulting, telecommunication, mining and oil and gas, energy, trading, hospitality. FIAA provides assistance to stimulate foreign direct investment in the country, promote communication between the FIAA Members and the Albanian Authorities, provide a meeting place for Foreign Investors to discuss mutual problems and solutions, offer after care services for foreign investors who are already doing business in Albania, business consulting, and offer a rich database of the Albanian & Foreign investors.

During the meeting with FIAA, CBS was informed that agro-business is out of the scope of the organization.

The Italian Chamber of Commerce in Albania (CCIA) was founded in December 1995 as an Advisory Committee of Italian Entrepreneurs, on the initiative of the Italian Ministry of Foreign Affairs and with coordination of the Italian Embassy in Tirana . Its aim is to support, promote and develop the activity of the Italian business community in Albania. The Association, which is considered as the main organization of the Italian presence in Albania, has always been the system of representation of economic and commercial operators and enterprises producing goods and / or services. The CCIA has numerous members in various sectors of the Albanian economy, mainly in banking, manufacturing, construction, energy, and services.

The main effort of the Italian Chamber of Commerce in Albania is to create a structure that is able to provide services to all businesses, foreign organizations and associations and penetrate in the Italian-Albanian market.

There is a momentum in the economic relationship between these two countries and agro-businesses are part of the initiatives for supporting businesses. However, there is not a clear strategy on how this sector of businesses will be supported.

Other issues not directly addressed in this document

- o Overall title ownership and land fragmentation issues are subject to governmental policies and are not addressed in this document. While attempts to address and support these issues are needed, the high dependency on government and state policies make the outcome uncertain. The issues of agricultural land will be addressed indirectly through banking products - banks will be advised to make agricultural land as eligible collateral to internal banking criteria. Banks will be provided with an evaluation guide to include it in their collateral evaluation process.

- o Solutions for Longer tenor products are not directly addressed in this document, because banks have strict internal rules that define the life of the loan based on loan types. AP's tie longer tenor with smaller monthly installments, which are more seasonal business activities and cash collections. Maximum tenor offered for Agro Investment loans from several Financial Institutions is 10 years. Usually, risk policy for such changes as longer tenor is complicated and quite often is subject of approval from head quarter of European mother banks. This issue is indirectly addressed, however, by supporting irregular payments tailored to specific AP business activities, which in turn lowers the loan installment at times of lower production activity.