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The need for supporting the Albanian agriculture with loan (and other problems encountered)

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Abstract

The agricultural sector is one of the sectors with the highest perspective and impact on the Albanian economy. The sector employs about 50% of the labor force in the country. However, the sector is underdeveloped after 1990s. There are numerous factors and problems that emerged, ranging from lack of funding, to the structural and legislative problems. Regarding this, the main purpose of this paper is that it serves as a further contribution to identify financial problems and other issues in the agricultural sector, and it also serves as a reference point for further studies to solve the problems in the future. The applied methodology is a mixture of both quantitative and qualitative methods. The qualitative method consists of the review and analysis of various studies about this specific area of research from different authors. On the other hand, according the indicators of GDP and agricultural lending, we construct a regression model to predict the need for agricultural loans in the next 5 years. The main findings show that the loans level will be increased. Other Several main problems are: the lack of funding, failure to register the land, the low rate of cooperation among stakeholders and as a result: the farmers difficulties in reaching the market, the land fragmentation, constructions made in agricultural land, the migration of the laborers from villages to big cities and the lack of insurance policies in agriculture.

Keywords: financial institutions, microfinance, agriculture, loan

1. Introduction

Agriculture is the sector that can generate more incomes in albanian economy. This sector is presented as the main pillar of poverty reduction and development of a country. About 96% of farm owners are men and only 4% are women, even though women are the main labor force in the farms¹. Also, this research found that there is a reduction of the agricultural laborforce skills due to aging, migration and lack of opportunities for education and training new members. Only 3% of farm holders have higher education and 37% of them have completed secondary education. Actually, the increase of productivity in farms encourages extensive entrepreneurial activities through diversification into new products, growth of rural services sector, emergence of agro-processing industry, as well as exploring new export market (Harvey, 2006). However,

¹ Ministry of Agriculture, Rural Development and Water Administration, Republic of Albania, Rural Development Programme 2014-2020, Under Instrument for Pre-Accession Assistance (IPA), 28 May 2015.

productivity is conditioned by lack of funding at the sector. Although the agricultural sector employs about 50% of employees in the country, it contributes about 22% of Albania's GDP. Moreover, exports are increasing every year, but there are still difficulties of accessing various financial services. Thus, the difficulty arises with funding support and not only.

According to the finding of studies in other countries, the main obstacles that farmers have the most effective supplies are structural improvements - limited access to markets, credit and inadequate infrastructure (Danielson, 2002). This issue is similar in Albania. On the other hand, loans have high interest rates. Referring to many authors, this has the impact that loans delayed will have higher interest rates and significantly increases the cost of borrowing and can also adversely affect the performance of their settlement (Olomola, 1999). However, in recent years the financial institutions are attaching more and more importance into lending at this sector as a way to diversify their lending portfolio. In this context, competition is intensifying due to increased level of lending to this sector from banks and other financial institutions and microfinance banks. Besides the funding from these institutions, the sector also benefits subsidies from government and from EU funds. However, the banking system is the main financial intermediary in Albania. The financing of the agricultural sector is very low, about 2% of the total loan portfolio in Albania.

The main purpose of this study is to make this research important as a further contribution to the identification of financial problems and other issues of agricultural sector, and to serve as a reference point for further studies. Thus, our main focus will be in the above research objectives: (a) to evaluate the request for the loan in the agriculture sector, (b) to point out and appreciate the problems of the agricultural sector and (c) to give valuable recommendations to encourage the development of agricultural sector. While, the hypothesis for this study will be: the loans growth in the agricultural sector will bring a higher GDP.

Constraints and Macroeconomic Environment

Albanian banking system is composed of 16 private banks, where the majority of them are foreign-owned. Non-bank financial institutions are numerous but only a part of them offer loans. The banks that lend to agriculture are ProCredit Bank, Credins Bank, BKT and Intesa Sanpaolo Bank. Procredit bank has devoted 20-25% of their portfolio in rural areas. Credins and BKT have increased their presence in agriculture and their portfolio from 5 million euros in the rural areas, recently has reached in 20 million euro. Intesa Sanpaolo Bank has a portfolio in these areas, approximately 4-5 million euro. This is due to the support of banks with Guarantee Funds. The Penetration rate of micro financing in Suburban and Rural areas is FAF 80-85%, ASCU today FED Invest is 95-97% , Besa Fund is 5-7% and NOA is 28-30%.

The analysis of lacking credit applications or application refusals indicated the following reasons:

- a) High risk perception of agriculture and rural economic activity.
- b) Absence/lack of guarantees, which itself face a lack of uniformity in the various policies and standards that banks define and list items acceptable as collateral. For example some banks and NBFIs do not accept agriculture land and real estate as collateral, while others do [ProCredit, FAF, ASCU].
- c) Heterogeneity of banking products to be classified as micro loans or micro financing. A significant gap in product design was found. For example, Raiffeisen Bank considers as

microcredit a loan up to EUR 100 000, ProCredit up to EUR 20 000, etc. Non-standard conceptions and practices determine different bank policies on micro lending. There are several banks and NBFIs in Albania that offer micro loans, but only in urban areas and much less in suburban and rural areas.

- d) Banks lack comprehensive marketing strategies. The majority of banks does not promote the entire product portfolio but only advertise what they currently are in need for i.e., collecting deposits.
- e) In the past, no bank had specific rural lending marketing plans, but in the last two to three years some commercial banks (BKT, Credins Bank, Intesa Sanpaolo Bank, etc) have started to particularly promote their rural loan products, reflecting a demand for loans in mountain and rural areas of Albania. The attitude of individuals and businesses in rural areas - that they are non-eligible to apply for loans - has started to change for good reason. The country has a contradictory economic structure because the agricultural sector accounts for 20% of Albania's GDP, for about 50% of employment, but only 2% of the total outstanding loan portfolio is allocated to agriculture.
- f) The physical inventory of rural natural resources according to geo-economic structure of Albania shows high level, while the labor force to make use of these natural resources is low.
- g) There is a rural/urban gap between deposit mobilization and credit provision.
- h) Missing linkages of value chains are a major reason for the chronic poverty in rural Albania.

2. Literature Review (microfinance)

Microfinance institutions, consulting the literature, are any financial institution that offers not only small loans to micro-enterprises, SMEs, groups and individuals, but also other financial services such as savings, insurance and investment advice, including training programs for its customers. Schreiner and Colombia (2001) identified microfinance as an effort to improve access to small deposits and small loans for poor neglected by banks. Also, microfinance is the provision of financial services to the self-employed and people with low income (Otero, 1999). People who live in rural areas generally have a low level of living. Providing working capital to a poor material, their sense of dignity is strengthened and this can help to empower them to participate in the economy and society (Otero, 1999). Often, the low incomes create problems with repayment of the loan. The loan failed can be defined as the inability of a borrower to meet its obligations or its credit, at the right time (Balogun and Alimi, 1990). Pearson and Greeff (2006) define a "failed loan" is on the brink of danger describes the borrower's point in the history of the settlement, where he or she missed at least three installments within a period of 24 months. A loan is delinquent when payment is late (CGAP, 1999). A delinquent loan becomes a failed loan when the opportunity of repayment becomes minimal. Delinquency shows an increased risk of loss warnings operational problems and may help to predict how the portfolio will eventually be lost. Before beginning the process of collecting information on the client to determine the credit limits, loan officer must have specific information available. This will guarantee that after the data and figures provided by the client will have a margin of error (Sheila, 2011). Kebir (2003) states that the assessment of the wider social impact is important for the internal process of learning about the organization. Also, a microfinance institution should be aware of the full range of changes associated with its efforts. According to the author, the dimensions of change to be evaluated are behavioral change, material change, change relational and institutional change.

A term known as "banks villages", which relates to non-profit organizations, established to provide access to financial services for communities, loans and savings, are groups of auxiliary community and help other members provide savings (Holt, 1994). Microfinance has a very important role in the development of a country. United Nations Capital Development Fund (2004), states that studies have shown which microfinance plays three major roles in development. Firstly, it helps very poor households to meet basic needs and protect against risks. Secondly, it is linked to economic welfare of families and thirdly, helps in empowering women, supporting women's economic participation and thus promotes gender equity. In fact, according to Mayoux (2001) microfinance has great potential and major effects on poverty were: (1) credit by making a significant contribution to the growth of incomes of the poor, (2) finance services contribute to poverty alleviation (3) costs incurred enabling facing unpredictable shocks and emergencies. Sinha (1998) argues that it is extremely difficult to measure the impact of microfinance programs on poverty. It argues that money is fungible and therefore it is difficult to isolate the impact of credit, but also because of the definition of poverty. However, some error statements are made for microfinance (Rogaly, 1996): (a) they promote a single-sectoral approach to the allocation of resources to fight poverty, (b) microcredit is irrelevant to poor people, (c) is using an over-simplicity notion of poverty, (d) learning and changes that are taking place are insufficient. Author Wright (1999) summarizes this shortcoming about focusing only on increasing revenues, as a measure of the impact of microfinance on poverty. Finally, international organizations are supporting microfinance institutions (MFI) by ensuring the effectiveness of the implementation of their programs, especially in poverty alleviation projects and the necessary knowledge of the interests of the poor (Okumadewa, 1998). Microfinance institutions in Albania play an important role in lending to agriculture such as the FED invest, NOA, FAF, where the majority of their funding is in the agriculture field.

3. Methodology

To assess the demand for loan products in rural areas, we conducted a desk research and held direct meetings with representatives of selected banks that are active in financing micro, small and medium enterprises, representatives of all microfinance institutions in Albania and other stakeholders of the sector with a particular focus on rural areas for data collection and processing. For banking institutions, the Consultant assessed a representative sample of banks by including and contacting BKT, Pro Credit, Credins Bank, Intesa Sanpaolo. The criteria applied for this selection are based in the following Rural MSME loan portfolio and products and Geographic outreach of banking services and products. All banks selected possess a relatively large network of branches, agencies and points of sale, almost all over the territory of Albania. So, the realization of this research is based on primary and secondary sources. The methodology used is a mixture between the qualitative and the quantitative method. As secondary sources were used earlier studies by different authors, periodic reports from government agencies and consulting corporation. The purpose of the analysis of these data is the identification of problems encountered by farmers perspective. An important part of the methodology is to build a regression analysis between the variables of GDP and loans issued for the agricultural sector. The data used are the type of time series data and are taken from the World Bank and Bank of Albania for the years 2007-2015.

4. Analysis of findings

The banking institutions do not have a big penetration in rural market, recently there is noted a growing interest in providing loans in rural areas. A positive effect is given in this sector by the guarantee funds financed by USAID and the EU. Microfinance institutions have made financial services to millions of clients due to new financial instruments. They have until today a greater extent the failure in order to achieve the poorest rural areas and/or small agricultural producers, whose livelihoods are characterized by highly seasonal investments, risks and returns (Peacock et. Al., 2004). Even, the possibility that a microfinance institution, can not get his money back from borrowers (plus interests) is the most common and serious weaknesses of a microfinance institution (Warue, 2012). Akinwumi and Ajayi (1990) found that farm size, family size, scale of operation, family living expenses and exposure are some of the techniques of management factors that may affect the repayment capacity of farmers. The supply of credit for agriculture is limited by structural problems of the sector, including small farms, aging population, lack of assets to be offered as collateral, the land market is underdeveloped, lack of information about applicants, etc². Problems were found in the agricultural sector as numerous and often connected with each other. Development of the agricultural sector is low by lack of financing from lending institutions. On the other hand, there are several factors and structural problems that lead to difficulties in financing this sector. In fact, the level of borrowing in rural areas is estimated to be rather low. A previous study shows that 27% of farms have ever applied for a loan, while 73% of them have not tried to get a loan (EFSE, 2009). Also, about 70% keep their savings at home (EFSE, 2009) not deposited in financial institutions.

But who are some factors that influence the loan to finance agriculture? The main difficulties to obtaining a loan are: (a) higher interest rates, (b) procedures are too long and complicated and (c) the lack of collateral. High interest rates bring difficulties in paying the instalments on time. In fact, the generation of income and profits in agriculture are lower than most other sectors. Moreover, the problem lies in the difference in time when the loan has to be paid and the harvest, because the loan repayment starts earlier than the production. Some agricultural products enter in production after 2 or 5 years. Here arises the difficulty of the time to pay the loan. Another problem is the prolonged and multiple number of documents to obtain credit in this sector. The complexity of procedures arises for two reasons. Firstly, the failure to develop agricultural sectors brings high bureaucracy and documentation and secondly relates to the non-recognition of different lending products by farmers. As mentioned earlier, it is a very low percentage of farmers applying for loans and the majority, keep their savings at home. In fact, the main difficulty is finding a collateral that is acceptable by the lenders. Most of the farmers use as collateral their lands and residential homes. Lenders evaluate low-value lands and homes in rural areas. Here you can exclude locations near coastal areas, highways and urban centers. Another difficulty is a lack of access to financial services in rural areas. There are no bank branches in villages to provide services (EFSE, 2009). A farmer needs to take a bus into the nearest town to access a bank branch, this lack of service is present even today. The banks own the majority of the financial sector in Albania. Despite that, most banks offer numerous services to clients in this sector, they offer limited services in these areas. As cited earlier, the reasons are lack of collateral and various structural problems of the agricultural sector. One solutions found

² Ministry of Agriculture, Rural Development and Water Administration, Republic of Albania, Rural Development Programme 2014-2020, Under Instrument for Pre-Accession Assistance (IPA), 28 May 2015.

by the farmers are informal loans, which are provide to them by family members. The above restrictions are added to the lack of adequate business plans (especially for large value loans) and the lack of a credit history in this sector. Furthermore we will discuss below.

However, this sector is not financing a number of issues related to emerge. Agricultural system in Albania continues to suffer from shortcomings (EFSE, 2009), which are relevant in today's findings: (a) small farms have a surface and production activity is fragmented, (b) coordinating agro-processing industry development in the embryonic stage, (c) insufficient security on land ownership, (d) partially destroyed irrigation systems, especially in mountainous areas, (e) high input prices (seeds and fertilizers). Also, other problems found by the study are: (a) the separation of farm has any unconsolidated land in 3-4 locations, (c) the farm is inseparable from farm families, (c) the lack of insurance in agriculture, (d) a very low cooperation among stakeholders, etc. Also in this sector is necessary to have technical expertise in agriculture in order to improve the efficiency of enterprise production, land use and reduce risks associated with their activities (EFSE, 2009). In fact today some problems as low quality of infrastructure, transport, energy, the price of fuel for agricultural machines, etc have been improved. Over recent years there has been an internal migration, moving population from rural to urban areas. Also, for many years investment in this sector was abandoned due to low earnings offered by this sector, affecting the structure of planting and cultivating cultural preference for less physical job seekers. Even more people are receiving incentives to invest in agriculture.

To bring a treatment in quantitative level and the forecast in our paper, we analyzed two important indicators of macroeconomic and financial. It shows the right relationship between GDP and loans issued by banks and other non-banking institutions to the agriculture sector. Based on historical data of the last decade, we have made a prediction for the next five years using time series. This prediction is shown in the table below, in which the independent variable is "X" - year and the dependent variable is "Y" - lending for agriculture in Euro. It is evident that the level of agricultural loans grows.

Table 1: Forecasting of agriculture loans for 2016-2020

Years	Years [X]	Agriculture Loans (Euro) [Y]
2007	1	17,614,286
2008	2	23,100,000
2009	3	25,921,429
2010	4	34,907,143
2011	5	47,300,000
2012	6	46,864,286
2013	7	50,192,857
2014	8	50,614,286
2015	9	54,471,429
2016		63,204,365
2017		68,045,556
2018		72,886,746
2019		77,727,937
2020		82,569,127
Regression	$Y = 14,792,460 + 4,841,190 X$	

Source: Authors Calculations, data from World Bank and Bank of Albania 2016

While the linkage between indicators of GDP and the level of agricultural loans expressed in Euro and their forecast for the next five years is shown in Table 2, where we can distinguish the expected impact on GDP by the performance of agricultural loans. In this case, the independent variable “X” is agricultural lending and the dependent variable “Y” is GDP. Both values are expressed in Euro. Given the forecast made for increasing agricultural credits and knowing the immediate effect of agriculture in GDP, and this indicator will be increased.

Table 2. Forecasting of GDP in relation to the progress of agricultural loans

Years	Agriculture (Euro)	Loans	GDP (Euro) [Y]
2007	17,614,286		8,917,509,880
2008	23,100,000		10,734,460,573
2009	25,921,429		10,036,844,086
2010	34,907,143		9,939,127,716
2011	47,300,000		10,742,389,803
2012	46,864,286		10,266,487,323
2013	50,192,857		10,650,858,036
2014	50,614,286		10,652,880,528
2015	54,471,429		10,769,679,591
2016	63,204,365		11,034,123,726
2017	68,045,556		11,180,720,971
2018	72,886,746		11,327,318,215
2019	77,727,937		11,473,915,460
2020	82,569,127		11,620,512,704
Regression	$Y = 9,120,217,260 + 30.28 X$		

Calculations, data from World Bank and Bank of Albania 2016

Based on the above calculations, the potential demand for loan is closely linked to macroeconomic indicators. Thus, the total lending for suburban and urban areas in the agriculture sector will be 63,204,365 million for year 2016; 68,045,556 million for 2017 and respectively 72,886,746; 77,727,937; 82,569,127 million euro for the years 2018, 2019 and 2020.

5. Conclusions

The study concludes that these constraints are created precisely because of the level of real economic and social contribution of the private sector in rural areas has not been taken seriously into consideration and so far the response of aggregate supply of loans by banking institutions and NBFIs ignored the potential entrepreneurship which might be powered from the presence and use of opportunities and resources available in rural Albania. The study covered the experiences of developing and developed countries that have implemented similar solutions applicable when they faced similar problematic circumstances. The above constraints have been tackled in many countries with improvements in legislation.

The agricultural sector is the backbone of the economy in Albania. However, it is the least developed. Despite that the agricultural sector employs about 50% of employees in the country, it contributes to about 22% of Albania's GDP. His low development comes from low level of lending to microfinance institutions. The main problem that have these institutions is collateral.

While farmers problem is the high rates of financing these loans and the repayment time. In fact, the dose added to the difficulties of this sector and lending are: (i) the surface of the small farm; (ii) the allocation of land since every farm has unconsolidated land in 3-4 locations; (iii) the farm is inseparable from farm families; (iv) lack of insurance in agriculture; (v) very low cooperation among stakeholders; (vi) it's partially destroyed irrigation systems, especially in mountainous areas; (vii) high prices of inputs (seeds and fertilizers); (viii) low quality of infrastructure, transport, energy, the price of fuel for agricultural vehicles; (ix) lack of technical expertise in agriculture; (x) the reduction of desire to work in agriculture due to low bonuses. From our forecast within time series on the basis of historical data showed that demand and need for loan will be growing in the next five years.

6. Recommendations

This study provided evidence for the problems of the agricultural sector, mainly focused on the financing of this sector. In fact, these issues need to pay attention because they are the key to develop agricultural sector. These recommendations are directed primarily to policy makers. Some of them are: (a) provide technical assistance and training continued to increase the level of knowledge to invest more in agriculture; (b) enhancing cooperation between policy-mechanisms; (c) increasing the level of cooperation between the supply chain that have the orientation of the agricultural sector; (d) financial institutions should have lower rates of interest for the provision of banking products sectors, as well as co-financing in projects in this sector; (e) logistical support for farmers from financial institutions and (f) increasing the role of associations to protect the rights of farmers and businesses. Above all, the establishment of an institution for financing their development of agriculture sector. Specifically, it is important to be designed and implemented differentiated credit policy according to the type of family farms and regional development projects. This would bring consolidation, regionalization and specialization of agricultural holdings, will bring incentives for alternatives and cooperative development, increase supply and partnership, better integration between the parties and increase the effectiveness of the system of agribusiness.

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