



SUPPORTING “GENERATION START-UP”: OPPORTUNITIES FOR ALBANIAN MFIs

This case note presents our research findings and analysis on the start-up enterprise landscape in Albania. This research was designed to identify current good practice among financial services providers and international organizations serving start-ups; understand the future potential role of microfinance vis-a-vis start-ups; and propose concrete and practical steps to bring about more support for start-ups. This project is being implemented within the four-year Framework Partnership Agreement of MFC and the European Commission within the EaSI Programme.

THE BIG PICTURE

Albania, an EU candidate country, is home to a population of 2.8 million and an upper-middle income economy that is dominated by the service sector (followed by industry and agriculture). Its transition from a centrally-planned economy is viewed as having been comparatively successful, and today the country has a GDP per capita of \$4,470 (2017 est.). Its levels of income inequality are low compared to the EU-28 and the United States (with a GINI index of 29, compared to 31 and 45, respectively). Overall, Albania presents a picture of both stability and growth.

Albania's official unemployment rate is high compared to the EU average (14.6% compared to 7.8% in the region), although this statistic omits income generation activities in the informal economy, which by some measures account for 40-50% of total economic output. Inflation within the economy is modest (2%) and economic growth is reasonable (3.94% annual GDP growth), although nowhere near its pre-2009 rates.

The size of Albania's small and medium enterprise (SME) sector is on par with the EU-28 (accounting for 99% of enterprises), although within this it contains relatively more micro-enterprises (rather than small and medium ones). SMEs account for 81% of national employment (compared to 66.9% in the EU-28), and within this micro-enterprises account for 43.4% of employment (compared with 29.2% in the EU-28). Albanian SMEs also contribute relatively more

value to the economy compared to the EU-28 (67.7% compared to 57.8%).

Important within the context of the start-up landscape is the make-up of the workforce: it is young and well-educated. Under-35s make up 57% of the Albanian population, and 85% of high school students go to university. Both English and Italian are taught as compulsory courses in Albanian high schools; Greek and Spanish are also widely studied. Thus the country comes ready-made with a workforce that is skilled and ready to do business across borders.

THE START-UP LANDSCAPE

Albania boasts a new but growing start-up scene that is concentrated in Tirana, the capital. The start-up ecosystem is supported by a number of incubators, accelerators, co-working spaces, online resource centres, regular meet-ups and information-sharing sessions, as well as annual conferences, trade fairs and competitions.

The barriers to entry for new start-ups in Albania are very low: registration can be completed in one day, and the start-up capital requirement is 1 Euro. However, taxes must be paid yearly in advance based on projected profits; and declaring bankruptcy isn't as easy as starting up a business.

Another word of caution for Albanian start-up entrepreneurs comes from StartUs magazine writing in 2015: “Although Albania is a beautiful country it holds a small population of around 3 million people. Also, the purchase power outside main cities like Tirana, Durrës, Vlorë, Fier, Elbasan, Shkodër decreases drastically. Unless you are starting small and thinking global, “Albanian speaking local” (Albania & Kosovo), be aware of this fact.”

THE SURROUNDING ECOSYSTEM

Domestic sources of seed funding aren't as plentiful as foreign sources; fortunately Albanian law doesn't restrict foreign investment in national businesses (either in terms of sector or percentages). Four national funds currently provide seed funding:

- Agricultural guarantee fund from EBRD for young farmers in partnership with BESA and NOA
- The UNDP runs an education program for youth with a small grant for starting a business
- Albanian-American Development Fund has an enterprise fund with Crimson Capital
- in Tirana there is a fund with a TA component

The Yunus Social Business Fund (Balkans) also invests in social business start-ups in Albania. While the majority of funding/support is directed towards IT start-ups, two other potential client segments are worth noting. These are: returning migrants, who have professional skills but lack savings, assets and collateral; and young farmers, to help them engage in business in rural areas (agriculture or tourism) and keep them from moving to urban areas.

Few microfinance service providers currently specifically target the start-up sector, although most of them have start-ups among their clients. In the early years of microfinance in Albania, MFIs served mostly start-up enterprises as there was large demand for credit from emerging enterprises. With years, these clients matured, so the demand shifted from investment to growth capital. At the moment the majority of MFI clients are mature enterprises. The start-up enterprises which are served by the MFIs are at least 6 months old and can provide sufficient guarantee. MFIs do not perceive that they have the risk margins or the capacity to adequately assess and support nascent enterprises.

The Albania Investment Development Agency (AIDA) was launched in 2010, and its objectives are 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 (particularly technology transfer). AIDA has a number of funding schemes, including ones for innovation, arts and

crafts, tourism/historical SMEs, start-ups, and increasing competitiveness.

Box 1: Innovation Hub (www.incubator.al)

The Innovation HUB Tirana project is being developed by the Ministry of Innovation and Public Administration (MIAP) together with two major partners, the Barleti Institute for Research and Development (BIRD) and Partners Albania (PA), in the framework of Italian – Albanian Debt for Development Swap Program (IADSA).

The project's objective is to promote and support the social inclusion and sustainable employment programmes for young people by enhancing their active involvement both in the ICT entrepreneurship, as well as in creative, innovative and competitive actions through capacity building, partnership development and growth of entrepreneurial activity, start-ups and SMEs.

The Innovation HUB intends to create an incubator to enable the innovation community to develop market accepted ideas that have scalable commercial potential by fostering collaboration among the SMEs and ICT innovative people and by introducing business and financing expertise to through training, coaching, and pitching.

There are currently three business incubators in the country: a ministry-supported incubator, an IT incubator in Tirana, and a social business incubator for Roma people.

At a government level, the action plan for the National Employment and Skills Strategy (2014-2020) includes a number of activities related to start-ups and entrepreneurship:

- 1) Foster decent job opportunities through effective labour market policies
 - Specific identification of young female and male unemployed jobseekers who can be potential entrepreneurs.
 - Establishment of start-up programmes for young female and male potential entrepreneurs supporting their self-employment.
- 2) Offer quality vocational education and training for youth and adults
 - Promotion of entrepreneurial learning and women's entrepreneurship as a key competence.
 - Development and implementation of tailor-made/target group specific entrepreneurship programmes specifically targeting girls and women, including in rural areas.
 - Development and implementation of leadership and management skill programmes specifically targeting women and girls.

3) Promote social inclusion and territorial cohesion

- Promoting social entrepreneurship (social economy and the third sector jobs) and women's economic empowerment
- Composition of comprehensive start-up strategies including one-stop-shop consultancy, professional business idea assessment.
- Provision of modularized, gender-sensitive capacity development measures for clients in preparation of a start-up, and on-going consultancy for at least the first year of self-employment.
- Basic & practical business skills courses on management, marketing, use of technology, adding value, building business, and start-up offered particularly for women and girls and especially in rural areas.
- Establishment of linkage between basic & practical business skills courses to special programmes supporting clusters of women-run businesses and start-ups.
- Development of special programmes for supporting clusters of women-run business and start-ups, including in rural areas.
- Conducting a longitudinal study on women and girls benefiting from measures/programmes in relation to social entrepreneurship and women's economic empowerment, including in rural areas.

NEEDS OF ENTREPRENEURS

In Albania, support organizations and funders recognise that new entrepreneurs have needs similar to those in other countries: namely know-how in running a business on a daily basis. This includes: understanding tax law and relevant legislations, and business management. As there are no special tax breaks or incentives for new businesses in Albania (and because closing a business is harder than starting one), business acumen is a must from day one.

There is an important cultural shift to be made in terms of fostering that entrepreneurial ethos in the young generation. History plays an important role here: whilst other Balkan nations (e.g. Macedonia, Montenegro, Serbia and Kosovo) became part of Yugoslavia following the Second World War, Albania "fell into a deep isolation, at the behest of its Marxist-Leninist dictator Enver Hoxha. His regime banned religion, beards and almost all foreign travel. So afraid of 'revisionist' outside influences was Hoxha that he had 750,000 machine-gun pillboxes erected all round Albania. While people across the rest of the Balkans received traditionally high technical training under

Yugoslav, or Soviet, rule, Albania remained an educational backwater. Early human rights successes, like gender equality and healthcare, were squandered from the 1960s on as Hoxha severed ties with all of his communist allies. By the time his Party of Labour fell, in 1992, Albania was Europe's poorest nation. Almost a quarter of a century on, the legacies of isolationist rule are still evident, despite [more stable] politics in recent years. In fewer places is it felt more acutely as in SME development, which requires not only an injection of cash and tax breaks, but a complete cultural shift", in a country where job stability meant working for the state, and starting a business is seen as unethical or shady practice.

The challenge arises because Albania has a very young and well-educated population, which serves as a massive potential source of energy and innovation in terms of economic growth. However, while 10,000 students graduate from university every year, only 4,000 jobs that require higher education are on offer across the country (a quarter of these in public administration). Artan Hoxha (no relation), Dean of Tirana Business University, reflects that SME growth isn't very high in the country, and there are only a handful of larger corporations (no more than 20) in the country offering employment. Thus, self-employment via a start-up is often driven by necessity rather than entrepreneurial spirit—and the training/funding needed by new businesses to succeed can be difficult to access.

CURRENT INITIATIVES

Against this backdrop of needs, opportunities, and challenges — we wanted to understand efforts currently underway to encourage new entrepreneurs and accompany them (financially and otherwise) through their first vulnerable few years. For this initial landscape mapping exercise, we began with our members and partners. We identified those who had experience (or interest) in the start-up sector, and using semi-structured qualitative interviews we explored their insights around their own work, and their perspective on other actors in the start-up sector.

Albanian Investment Development Agency (AIDA)

AIDA implements the support to SMEs envisioned in the government's National Employment and Skills Strategy (described above). Their work is implemented under the supervision of the Ministry of Economy.

AIDA manages a fund for start-ups, launched in 2016, for firms with up to 2 years of experience. 100 firms applied, and 50 were chosen for funding, most in the tourism, production, manufacturing sectors. This program includes grants for 2K EUR per firm, which they can use on training and equipment. Grant projects typically last for 3 months,

and businesses are monitored for a year. Half of the grant is disbursed up front, and half at the end upon proof of expenditure (invoices, etc.) by the business.

AIDA's SME fund operates under similar principles, but with larger amounts and more experienced firms. The SME fund also includes advice services on selling abroad, technology transfer and intellectual rights.

AIDA's women's entrepreneurship fund existed in the past but is now on hold due to a lack of uptake. The organization has launched a study (in cooperation with GTZ) to ascertain the reasons behind this, so it can plan next steps.

AIDA is also involved in a number of smaller projects to support entrepreneurship, in line with the national plan. These are:

- Co-organizing competitions for the start-up sector, SME and tourism sectors. To date, 4 winners have received grants from AIDA as prizes.
- Hosting a B2B platform, where users can find out information about Albanian companies. Importantly too, Albanian companies can also find out information about fairs abroad, and get funding to participate.
- Creating an agricultural exports guide, with support from GTZ.
- Training trainers to help start-ups write business plans

UNDP

The UNDP's work with start-ups in Albania falls in two main categories: vocational training for 18-29 year olds, and policy work with the ministry of labour and its employment creation programs.

Its start-up project began in March 2016, with the aim of providing grants (5K USD), mentoring and business plan development support. 600 people applied to the training programme, of which only half had prior work experience, and half were women. 150 people signed up for the training, and only 75 people showed up. Reflecting on why so few people came, UNDP sees that there are many 'start-up weekends' available in Albania, and their project represents a long-term time commitment. However, the first round of start-up grant and mentoring reached 37 enterprises (mostly in IT, tourism and agriculture). A second round is starting now, and 400 applications were received. The UNDP noted a regional difference in the pool of applicants: those coming from the regions were more persistent and more grounded in their business ideas, and the IT applications were mostly from Tirana.

In future, the UNDP would like to work more closely with financial institutions on start-ups. To date, it has noted that there is little growth potential in many of its start-ups, and

that perhaps better selection is needed in future. Also, entrepreneurs rarely leverage horizontal business growth (adding new dimensions to current businesses), opting to start new ones instead.

Agro & Social Fund

Agro & Social Fund (formerly VisionFund Albania) is a financial institution oriented toward social and economic development, especially in agro, small and medium business sector, in rural and urban areas. It offers quality services, value, respect and transparency in communication, confidentiality, non-discrimination and avoidance of over-indebtedness.

Agro & Social Fund offers business and agricultural loans of up to 15,000 Euro, energy efficiency loans of up to 7,500 Euro as well as social and consumer loans. It has a dedicated start-up loan product, with 21 active loans that are funded by KIVA (which provides funds and guarantees the risk), compared to 736 older enterprises. However, this number only accounts for companies that were started from scratch at the time of the loan; were it to include businesses that are less than two years old (commonly used definition of a start-up) the number would undoubtedly be higher (although this data is not available in the information systems). The average loan value for start-up loans is 218K Lek, compared to 303K Lek for older enterprises; its PAR (>30 days) for start-ups is 4.76% by number of loans, and 0.04% by portfolio at risk (compared with 6.29% and 4.05% respectively for older enterprises). In this way, its experience seems to contradict the expectation that start-ups are a riskier investment than established firms.

At the present time, Agro & Social Fund serves clients with businesses older than 6 months, and has a lot of clients with businesses younger than 2 years. While general loans are assessed based on the last 12 months of trading history, start-ups are assessed on their 12-month projections. Agro & Social Fund is finding that many of its clients are former economic migrants, who are bringing their business know-how back with them from their host countries.

Agro & Social Fund identifies a number of potential solutions to expanding MFI support to start-ups in Albania. These are:

- Providing clients with insurance to shield the client from the risk of damage or fatality on account on their business activity, naming the MFI itself the beneficiary of the insurance policy (to cover loan losses)
- Lobby lenders to create a special start-up funding mechanism with rates and guarantees that make start-up lending more attractive to MFIs.

Besa Fund

Besa Fund's mission is to contribute to economic growth in urban and semi-urban areas, by promoting and financing the small and medium enterprises sector in Albania. Clients of Besa Fund come from all socio-economic groups, including unemployed and start-up businesses. It offers micro, small and medium loans to individuals, supporting them to start, extend and further improve their income-generating activities. Working out of 74 offices all over Albania, it aims to support clients to become financially and economically independent, so that they can ultimately realise their own ambitions of prosperity and well-being without its support in the future.

While Besa Fund targets SMEs, it does not have a dedicated SME loan product, nor does it track data on the percentage of its portfolio invested in start-ups. It reflects that having a special start-up product (with lower interest rates and bundled business management training) would help it to target this segment more effectively. It also sees a role for a special guarantee scheme for start-ups, which the institution could use to mitigate its risk in working with these types of businesses.

FED Invest

FED Invest is a financial services provider, which covers 1,080 villages and about one third of rural Albania. It was set up through the merger of 70 savings and credit associations. FED Invest was formerly known as Albanian Savings and Credit Union (ASCU). FED Invest's mission is to provide financial services for rural people, who are excluded from the traditional banking system, in order to promote productive activities, the improvement of their living standards and rural development.

As of the time of writing, FED Invest did not have a dedicated start-up product, nor does it particularly target them due to the higher risk involved in doing so. It perceives that most start-ups can only launch thanks to grants from UNDP, AIDA, and others. FED Invest has supported a few start-ups with small grants (1-2K EUR), but recognises that the cost, as well as its own capacity to assess and support start-ups, is a key barrier to reaching more.

It was however poised for rapid growth, owing to the fact that the Development Facility of the European Fund for Southeast Europe (EFSE DF) together with the Netherlands Ministry of Foreign Affairs and Rabo International Advisory Services (RIAS) have confirmed their commitment to facilitate FED Invest's transformation to a leading financial institution for rural areas and enterprises. EFSE DF will cover part of the costs of a multi-year capacity building plan to reach the objective of fostering economic development

and improving the standard of living in Albania's rural areas. As part of this, FED Invest will be able to deliver better data on its work with start-up enterprises in rural areas.

UniFin

UniFin's mission is to provide full financial services to its members, with professionalism and dedication to everyone, operating as a non-profit institution with a guiding principle of cooperation and mutual assistance.

UniFin defines a start-up as any business with less than 1 year of activity. It does not automatically reject applications from start-ups, but looks for another source of income in addition to project income for the start-up. Most of its start-up clients seek loans to cover 90-100% of their investment costs, rarely seeking working capital.

UniFin had considered training, but does not currently have a strategy to cover the costs of providing it.

NOA

NOA's mission is to offer suitable financial products in professional way to ambitious clients outside the focus of other financial institutions, by solving their needs and demands 'Fast and Easy'. Its small business loan product start at 3m Lek (27K USD) and extend up to 14m Lek (125L USD), in terms ranging between 6 and 84 months. Its collateral requirements are flexible and it offers loan serving at the client's place of business for maximum convenience.

NOA defines start-ups as companies with fewer than 6 months of trading experience. While it does not typically lend to what it defines as 'start-ups' (i.e. less than 6 months) it does lend to young companies: 6% of its portfolio is invested in businesses below 2 years old at the present time, and 4% of its client outreach. Average loan sizes for start-ups are 322K Lev, a quarter less than for more established companies.

In NOA's view, start-up entrepreneurs need business planning skills, as well as guidance on tax and legal matters (advice is available in the marketplace but not free of charge, and new companies don't invest in this knowledge).

Owing to the larger perceived risk associated with start-ups, NOA only invests with caution in young businesses. That having been said, much like VisionFund Albania, NOA's start-up investments are performing well: with a PAR>1 of 4.8% (vs. 7.5% for older firms) and a PAR>30 of 1.92% (vs. 4.16% for older firms). Its application rejection rate for start-ups is 20%, compared to 24% for older firms.

That said, it reflects that MFI support to the start-up sector would potentially increase if a national guarantee facility was made available to them by the government to see start-ups through the first stage of business. MFIs would also benefit from an effective methodology to assess the future cash flow needs and trends in different sectors of the economy—and discounted funding rates so they could offer cheaper credit products to new companies.

Crimson Finance Fund Albania

In 2009, the American-Albanian Development Foundation (AADF) in partnership with Norfund, Crimson Capital Corp and the Municipality of Tirana established Crimson Finance Fund Albania, a non-banking financial institution which provides developmental financing for micro, small and medium-sized businesses. CFF Albania is designed to improve access to finance for under-served small and medium enterprises (SMEs), entrepreneurs, innovators, women-owned businesses and farmers in Albania in order to catalyze business growth and job creation.

Since 2016, when it began lending, the AADF has invested in 22 businesses, 6 of which had less than 2 years of experience, and most of which were in the manufacturing or IT sector. AADF only invests in registered businesses. The leadership profile of its start-up investments is younger than for its older businesses, interestingly enough. AADF does not typically provide training, focusing narrowly on financial support in the form of leasing (up to 100K EUR, averaging 20-23K EUR). The choice to offer leasing rather than credit was driven by risk-mitigation: Crimson can take possession of the equipment in the case of business failure in order to liquidate the amount outstanding.

Crimson's management reflects that the most common challenge they encounter with start-ups is that they cannot produce their own financial projections, and require support from Crimson to do this. So too is routine financial reporting uncommon; financial statements are prepared at tax time, but not at other times of the year. In addition to business planning and management, start-ups also need help undertaking market analysis. Even for Crimson it's hard to find data about the market in Albania. They also see a role for creating a positive enabling environment for start-ups, in the form of tax incentives, grants and guarantees.

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NEXT STEPS

The stakeholders that we interviewed identified a number of potential next steps to support the development of the start-up sector, as follows:

Funding

- Focus on providing access to finance for start-ups of less than 6 months old which are currently not served by microfinance institutions
- Launching a national-level guarantee fund separate from Easi guarantee fund that will be tailored to MFIs' needs and capacity
- Lower taxes for MFIs to encourage lending to riskier segments such as start-ups
- Preferential interest rates for MFIs to serve the start-up sector
- Changing regulations on deposit-taking for NBFIs: collecting savings would provide a cheaper source of funding for start-ups
- Grant funding for MFIs to provide capacity building to start-ups

Government support

- Nationally-agreed definition of 'start-up enterprise', and segment start-ups into sub-groups (first-time entrepreneurs, seasoned entrepreneurs, and unemployed entrepreneurs)
- Tax incentives for new businesses (for a minimum of six months)

Service development

- At a sector level, develop methodology for working with start-ups, including how to assess the business without cash flow and historical records. This might be achieved with funding from EasiTA.
- Partnerships with public institutions or NGOs, whereby MFIs provide loans and the partner institution provides capacity building to start-ups.



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