

MICROCREDIT PROGRAMS AND SMEs DEVELOPMENT IN KOSOVO

Qefsere Kupina¹ & Professor Drini Salko²

ABSTRACT

Microcredit was defined as a loan below €25,000 that is considered important to help developing small and medium enterprises, which, as many other businesses needs a variety of financial services, in order to be able to build assets, stabilizes consumption and protect themselves against risk position. However, there are the cases that not all benefit from microcredit programs. In the European Union, microloans are provided by banking institutions and non banking entities. Microfinance institutions as non bank entity provide microloans to SMEs and low –income people, with limited access to traditional banking services. Kosovo as a country in transition achieved to be in range with countries that has improved, providing microcredit through a number of financial institutions. Small and medium enterprises (SMEs) are valued as the backbone of Kosovo economic development by increasing the number up 46,000 since 1999 with approximately 190,000 people employed. In this line, SMEs is seen as good potential to be served with a microcredit program provided by financial institutions. Therefore, by reviewing the SMEs development during the last period and accessibility of microcredit programs we see that Kosovo can benefit in aspect of economic growth, employment and poverty alleviation by well funded SMEs. At the end of this paper, we will add some comments for potential and future improvements to microcredit programs in Kosovo.

Keywords: Microcredit program, microfinance institutions, small and medium enterprises (SMEs).

INTRODUCTION

Because, microcredit programs are designed to help the poor become self-employed and thus escape poverty (Khadker, 1998) also favorable for improving and generating of employment and revenue for Small and Medium Enterprises (SME), is the relevant topic to be studied. The development of SMEs is important for worldwide, particularly in developing countries. The same, access to financial services is a crucial for SMEs, as it is for microenterprises and corporation enterprises, even if, access to credit has been much difficulty (Frankiewicz and Churchill, 2011)

In Kosovo, especially after the war ended in 1999³, a priority for the World Bank and the European Agency for Reconstruction was to develop a credit line scheme “SME program credit “from which small and medium-sized enterprises (SMEs) should benefit. The establishment of first institution in Kosovo that provide micro loans to micro enterprise and SMEs dates from late 1999, starting with the Micro Enterprise Bank (MEB)⁴.

Microfinance Institutions (MFIs) established to operate as non-governmental organization (NGO), supported by international donors, thus becoming an important factor for economic

¹ Phd Candidate in European University of Tirana , email ; qefsere@gmail.com

² Lecture at Agriculture University of Tirana ,email ; drinisalko61@gmail.com

³ Support with capital projects for reconstruction, for economic, social, and political development, was unavoidable

⁴ Microcredit Enterprise Bank (MEB) is the first financial institutions established in Kosovo. Today this bank operate as one of the larger Bank Kosovo as ProCredit Bank (for more: <http://procreditbank-kos.com>)

growth. Accordingly, the Association of Microfinance Institution of Kosovo (AMIK) got established, with the aim to engage together the group of MFIs in order to support the needs of Kosovo's small and micro business sector (SMS) and to push facilities growth in the microfinance industry.

Sustainable position of the financial system is a good booster for increasing continuously the value and number of financial institutions in Kosovo. In terms of financial institutions during the period 2010-2014, the number of financial institutions has been increased up to 17. The periodical reports (2014)⁵ have shown that the financial sector in Kosovo operates with, 10 commercial banks, 13 insurance companies, 2 pension funds, 41 financial auxiliaries, and 18 microfinance institutions.

Different views of studies and researches offer a broad perspective on the concept of microcredit and microfinance. Furthermore, we cannot avoid from e many debates about the benefits and vulnerability in connection with the functioning of the microcredit program in relation with SMEs development. Hence, the first part of this paper provides some description about differences between microcredit and microfinance, importance and the expansion, to continue with the discussion on the microcredit program in a more specific manner.

Along with the progress of the financial system of Kosovo and inclusion of microcredit programs, will be reviewed. However, the aim of this paper is to review the effects of the microcredit program, especially in the development of SMEs in Kosovo. In the context of this paper, we suppose that the SMEs sector needs a support with the purpose to improve conditions in relation to employment and productivity, whereby can impact on country economic growth and poverty alleviation also. By reviewing increases of the importance of the microcredit and the SMEs expansion the conclusion and recommendation for the future studies will be given.

LITERATURE REVIEW

The importance of the microcredit has been increased since 1980, although early experiments dated back 30 years ago in Bangladesh, Brazil and some other countries (Robinson, 2001). The microcredit program is an important contributor in developing countries where this program is applied. Beneficiaries of the microcredit are groups of people, such farmers, small business, self employed, women, those who have limited access to credit because of lack of collateral. Credit institutions ask for collateral, usually a personal guarantee or a mortgage on real estate⁶.

Because of lack access to credit, is seen as one of the main reasons why many people in developing economies remain poor (Hermes and Lensink, 2007). According to, Vetrivel and Kumarmangalam, (2010), this limited access to credit for the poor, is directly connected to practical difficulties arising from the discrepancy between the way of operation followed by financial institutions and the economic characteristics and financial needs for low income households.

⁵ Banking Periodic Overview of the Financial Sector in Kosovo

⁶ Report on , Microcredit for small business and business creation: bringing a market gap , November (2003) European Commission

Since 1997, the number of people around the world who benefits from microcredit has increased significantly. The attention to this growth of microcredit is obvious since Professor Muhammad Yunus of Bangladesh⁷ achieved to establish in 1976 the first bank “Grameen Bank”. The importance of the credit project was to provide small loans focusing on individual and group of people that have the capacity to work, but lack of money prevents them. Ensuring of income through microcredit is assessed as important tool almost for the poor people who live in developing countries and economic development also.

Khandger (1998), states that “Yunus believes that with appropriate support, the poor can be productively employed in income-generating activities”. In his conclusions Roy(2003), stated that, the provision of credit to the poor has proved to be a powerful tool in development. Around 2 million members are served by Gramme’s credit programs in 2000, according to Lengerwod (2013). Further to this progress on the credit project, Professor Yunus and Gramen Bank were awarded in 2006 with Nobel Peace Prize, “for their efforts through microcredit to create economic and social development from below”. However, not always financial products offered by Microfinance Institutions (MFIs) fit the needs of poorer, while many MFIs cater mostly to the non-poor clients (Roy, 2003)

Microcredit and microfinance are defined from different perspectives. Almost all studies about microcredit emphasize that this refers to the provision of credit services to low income clients, usually in the form of small loans to invest in small enterprises and income generating activities. While for microfinance is oriented to provide financial services to the poor people and low income people, such as loans, savings, insurance, money transfer, etc. and also microcredit loans. Two types of differences between microcredit and microfinance are examined by Elahi and Rahman, 2006. They concluded, in terms of function, differences are “semantic rather than substantive”, while conceptual difference is “fundamental and far - reaching”. Looking through historical view, poverty alleviation through microcredit was tied primarily to one product, invested in a microenterprise, provided by a microfinance institution (MFI) (Lendgerwood, at al 2013), which is not always accepted in reality. In addition, Wang (2013) noted that “SMEs that have participated and received micro financing before are very likely to apply for and receive micro financing in the future again”.

Strengthening of the microcredit programs

It is the Micro Credit Summit in 2005, which encourages and supports the growth of microcredit and microfinance sector to better serve the demands and to fulfill the needs of a wide range of clients. Small and medium enterprises like many other businesses needs a variety of financial services, in order to be able to build assets, stabilizes consumption and protect themselves against risk position. Such needs probably make the concept of microcredit to be more inclusive for a long period. Microcredit is valued as an area where the market gap should be regulated by encouraging financial institutions to play a greater part, and effective for political and social inclusion, employment and economic development (Commission of the European Communities, 2003). Microcredit to small enterprises is defined there as a loan below € 25,000⁸. As it stated in the report, most of these micro-enterprises are self-employed people who do not create additional jobs, do not have the resources or do not want to grow. Those micro-enterprises wishing to grow, however, often do not have access to the necessary external financing.

⁷ Since in the beginning Bangladesh was treated “ as a leader among low-income countries offering microcredit”

⁸ Microcredit for small business and business creation: bridging a market gap; Report ,2003

In the European Union, microloans are provided by banking institutions and non banking entities. Today, tens of millions of people in all around the world (more than 100 countries) have access to financial services through microfinance institutions (MFIs). The role of microcredit with the aim to contribute to poverty alleviation, especially for the people who live with 1.5 \$ per day, continues to be debated through a number of activities, projects and campaigns, such as “Microcredit Summit Campaigns”. In latest Microcredit Summit Camping it was underlined that there are more than 175 million of the poorest families with microfinance and ensuring that 100 million of those that rise out of poverty. Focus on poverty alleviation is almost the most important strategies of the international community, by strengthening the ideas of positive effects on economic development. A small amount of money can contribute significantly to poverty alleviation, as attested to by the many successes, particularly amongst women, in villages and in remote areas⁹. However, according to Hulme (2000) “not all microcredit produces favorable results, especially for poor people working in low-return activities in saturated markets that are poorly developed and where environmental and economic shocks are common”, this because “ microfinance services to poor people is only a part of a poverty reduction strategy” (Hulme, 2000).

Contribution of the financial sector in Kosovo

By applying the best practice and international standards, Kosovo is characterized by the rapid development of the financial sector. Banking sector, with 89.2 % of total assets is managed by foreign banks, and with the increasing trend on lending activities¹⁰, contributes in the modernization of the financial sector and by indicating that the larger percentage of loans went to SMEs¹¹. The number of financial institutions that are licensed to operate in a Kosovo market (CBK, 2014) has been increased from Jun-2011 until June 2014. As per the table below, the structure of financial institutions remains positive changes in yearly basis, excluding MFIs that is reduced to 18 from 19 that were in 2012.

Table1. Number of financial institutions

	Jun-11	Jun-12	Jun-13	Jun-14
Commercial Banks	8	8	9	10
Insurance Companies	11	13	13	13
Pension Funds	2	2	2	2
Financial Auxiliaries	32	39	40	41
Microfinance Institutions	17	19	18	18

Source: CBK¹², *Financial Stability report (2014) Number 6*

Further to this, the development actors have realized that microcredit is an important instrument for poverty reduction, economic growth and especially in increasing Small and Medium Enterprise (SME) sector. The scheme of loans dedicated to SMEs is launched in 2014 with a local private bank. However, in context of private sector development, especially for the SMEs emphasized, that there are still some obstacles to development, considering restrictions on access to finance¹³, particularly in the rural areas outside of the main cities¹⁴.

⁹ <https://www.icdf.org.tw/web>

¹⁰ Banking Sector: Facilitator or Barriere: Riinvest Institution and supported by Kosovo Foundation for Open Society(KFOS), Forum 2015

¹¹ Ibid pg.20 “out of total loans, 67.4% of these loans went to the SMEs”

¹² CBK, Central Bank of Kosovo

¹³ Kosovo Progress Report ,2014 – European Commission , <http://ec.europa.eu/>

¹⁴ Strategy for Kosovo,2013

Private sector – SMEs in Kosovo

It is reported that, Kosovo's private sector remains small based on the region's standards¹⁵. With about 80% of employment, the SMEs sector as a main part of the private sector is a priority policy of the Kosovo government. Kosovo Investment and Enterprise Support Agency (KIESA) have been established by the Ministry of Trade and Industry (MTI), with the aim of supporting policies and programs for micro, small and medium enterprises (Report on SMEs, 2014)¹⁶. Micro, small and medium enterprise, according to (Kume, et al 2009)¹⁷ are the engine of the economy, which generate sustainable economic, growth, employment and poverty alleviation.

Approximately, 46,000 enterprises are in the private sector during 2013 with about 190,000 people employed. The so-called 'solo entrepreneurs' accounted for about 56% (or 26,000) of all businesses and almost 14% of employment. Based on the categorization, micro enterprise structure starts mainly from 2-9 persons employed, which constitute the most important size category in terms of employment as they account for almost one third of jobs in private sector businesses. The employment also shares the other three size categories, small companies with 10-49, medium-sized ones with 50-249, and large ones with 250 or more workers – are quite similar and vary between about 16% and 19%¹⁸. In the latest World Bank Report Doing Business, Kosovo is ranked in 98th position. Notwithstanding as it stated "many efforts remain un-coordinated and lack sufficient resource, and therefore continue to be heavily donor-dependent" (Strategy for Kosovo, 2013).

Microcredit and the role in Kosovo SMEs development

The interest for improvement of the SMEs is high in Kosovo. However, there are numbers of obstacles founded that SMEs in Kosovo in regard to finance. Cost of financing and restricted access to finance¹⁹, inters rate is too high (average 12.3 percent), short average repayment period- less than three years²⁰ are estimated as main factors to SMEs future development. The majority of the SMEs are finance by the company's own resources as a primary source of finance, with bank loans and other external factors as the second most important sources²¹. Improvement of the microcredit program, especially microfinance industry has proved importance for the development of the large number of Small and medium enterprises (SMEs) after the war ended in 1999 in Kosovo. This, because the banks do not have the confidence that this level of business can generate sufficient income which will be able to restore credit borrowed. SMEs have had restricted access to finance and banks impose exceptionally high risk premiums given poor governance standards at most firms²².

According to the CBK (2014), "Concerning the rate of loan approval, banks are expecting an easier approach of bank financing for the SME's and households". In other hand it has been stated that in the MFIs loan structure have a growth of enterprise lending, which can be impacted from the growth of requirements for loans.

¹⁵ Strategy for Kosovo ,2013

¹⁶ Report on SMEs in Kosovo ,2014

¹⁷ SMEs - A Key Factor for Economic Growth and Employment

¹⁸ Report on SMEs in Kosovo ,2014

¹⁹ Riivenst Institution Survey (see footnote 11)

²⁰ <http://www.bsckosovo.org/publikimet>, research report

²¹ BSCK ,Research Report ,2010

²² [http://www.ebrd.com/downloads/country/strategy/kosovo-strategy.pdf\(13\)](http://www.ebrd.com/downloads/country/strategy/kosovo-strategy.pdf(13))

CONCLUSIONS and REMARKS

By studying the SMEs development in Kosovo, we noticed that SMEs are facing with the number of challenges in access to finance. While, continues development and increases of SMEs number, identifies demand on improving microcredit programs by financial institutions in Kosovo. Thus, because banks do not have the confidence that SMEs can generate sufficient income which will be able to restore credit borrowed. In other hand, SMEs can be seen as a good producer of workplaces, avoid the informal economy, poverty reduction, economic growth, therefore facilitation of access to finance with reasonable cost is important.

For improving the microcredit programs in relation to the development of SMEs, some modest suggestion can be added.

- In conditions of the economic crisis that has had its impact on the SMEs sector in Kosovo; commercial banks have reduced lending to them. Under these circumstances, we think it is important to implement the Guarantee Loan Fund. These funds will increase security for commercial banks that will increase SMEs financing.
- Commercial banks and microfinance institutions should increase the amount of loans for SMEs by aiming to support SME, which aim to produce in the open market.
- Because the microcredit is a part of microfinance, now is the time to move from microcredit to microfinance related to SMEs. This implies the involvement of other financial services alongside the microcredit for this level of business.
- It is important for this period to require being designed fiscal policy incentives for SMEs in Kosovo, which should be reflected in the 2016 budget.

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