

## An Analysis of Financial Leasing in Albania

Fatjola Lubonja<sup>1\*</sup>, PhD Candidate    Sllavka Kurti<sup>2\*\*</sup>, PhD

1. Ministry of Internal Affairs, Albania

2. University of Tirana, Faculty of Economy, Management Department, Albania

### Abstract

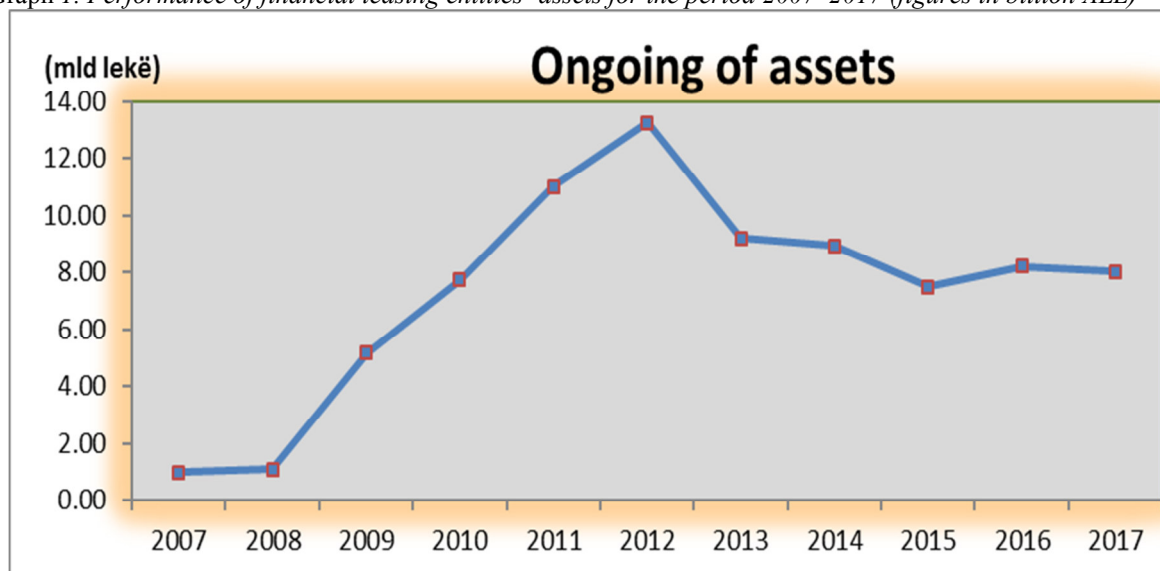
Financial leasing in Albania began in 2001 but its application has been made at a low pace by the public. This article focuses on providing a broad overview of financial leasing in Albania, with a view to understanding how it operates, the development of the financial leasing portfolio over the years, the regulatory and legal framework in which this form of financing has been applied in Albania and further provide a number of conclusions that will focus on the factors that are expected to affect the future of financial leasing in Albania.

**Keywords:** leasing, portfolio, assets, financial leasing

### 1. Introduction. Development of financial leasing in Albania over the years

The first mention of financial leasing in the Albanian legislation was in the “Civil Code of the Republic of Albania”, namely in Article 849 “Financial Leasing”. It is stated that based on a lease agreement, one party shall be bound to make available to the other party, for a certain period, a movable or immovable property, against a payment on recurrent periods, set out in connection with the worth of the property item, contract duration and eventually with other elements referring to the agreement of the parties. In addition, the property item shall be acquired or constructed by the lessor in response to the wish of the lessee and the latter shall, upon the expiry of the contract duration, be entitled to acquire ownership over it, against the payment of predetermined amount. As from 2001, the Bank of Albania has licensed 13 non-banking financial entities to conduct the activity of financial leasing (as a sole activity or along with other ones). The first entity to have been granted the license for carrying out the activity of financial leasing is “Credins Leasing”<sup>1</sup>. Year 2009 can also be called “financial leasing year” in terms of licensed entities. Among the main factors influencing the increase in the demand for a financial leasing license was the change of the law “On financial leasing” and the reaction of banking groups to the effects of the international financial crisis of 2008. This is reflected in the fact that out of five entities licensed in 2009, three belong to foreign banking groups. In addition, it is reflected that after 2008 the performance of financial leasing assets has increased (in absolute terms) until 2012, whereas in relative terms it is difficult to make comparisons due to the low initial level. The increase has coincided with the increase in the number of licensed entities.

Graph 1. Performance of financial leasing entities' assets for the period 2007–2017 (figures in billion ALL)



As from 2013, there has been a merging of some of the key financial leasing entities, which were part of banking groups operating in Albania. The main reasons relate to entity shareholders' assessments of the effectiveness of operational cost management, capital and other resources, as well as strategic plans for the presence in Albania. These processes resulted in the absorption of financial leasing entities by the banks of the group they were part of (Credins Leasing and Sogelease), or the sale of their portfolio to other entities (Tirana

<sup>1</sup> Until 2012 there was no division between the volume of financial leasing activities and other activities.

Leasing).

The most noticeable (negative) effects on the reduction of activity levels appear in 2013 (when Credins Leasing was absorbed by Credins bank), whereas the sale of Tirana Leasing portfolio to another entity performing this activity (Raiffeisen Leasing), had a minimal impact on the market.

Meanwhile, from 2015 onwards there is a stagnation of financial leasing activity, which reflects to some extent the slowdown in market demand for credit. However, the interest of entities to be licensed for the lease financing activity has not disappeared. During 2013-2017, 6 new non-banking entities were licensed to perform some of the activities provided by law (lending, factoring, etc.), including financial leasing. The only entity licensed for financial leasing activity, which has never exercised it, is Transit entity (this entity performs other activities).

#### *Regulatory framework*

At the beginning of 2013, the Bank of Albania approved the new regulation “On supervising the risk in the activity of non-bank financial institutions”, introducing new reporting requirements, which provide more detailed information, among other things, for financial leasing activities. This regulation has set the requirements for classification of the financial leasing portfolio, as well as the relevant rates for its provision, which did not exist in the previous regulatory framework. With the changes made to the above regulation in 2017, among the factors influencing the financial leasing activity, we can mention the increase *Table 1. This table shows the financial leasing entities licensed by the Bank of Albania as from 2001.*

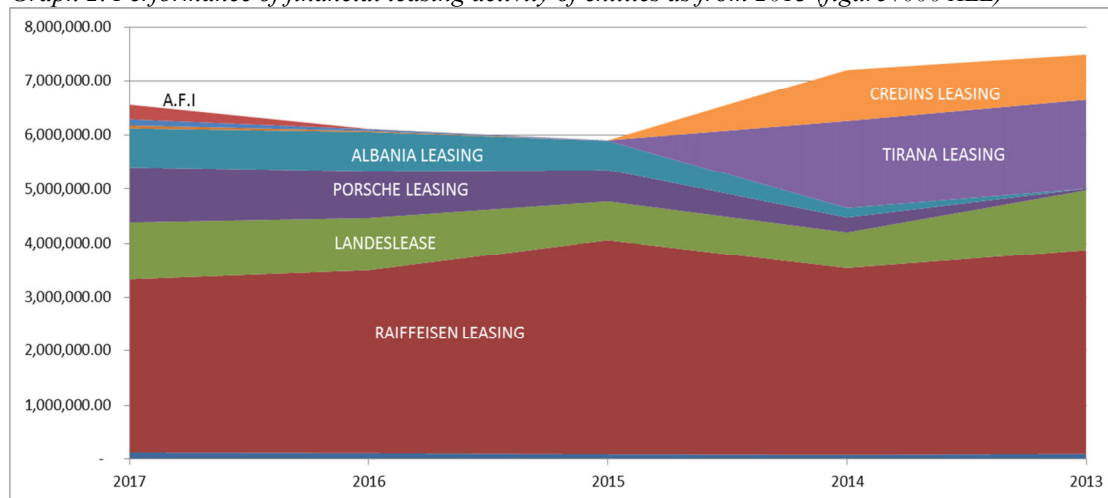
No.	Financial Leasing Entities	License date	License revocation	Part of banking group	Share of financial lease (September 2017)
1	Credins Leasing	13.06.2001	22.04.2016	YES	n/a
2	Raiffeisen Leasing	15.07.2009	-	YES	100%
3	FIN – AL	20.02.2009	-	NO	80%
4	Tirana Leasing	11.12.2009	30.11.2016	YES	n/a
5	Landeslease	24.12.2009	-	YES	100%
6	Sogelease	25.01.2010	30.05.2013	YES	n/a
7	Tranzit	04.08.2010		YES	0%
8	Tirana Factoring & Lease	28.03.2013	-	NO	21%
9	Porshe Leasing	29.10.2013		YES	100%
10	Albania Leasing	21.04.2014	-	YES	100%
11	Crimson Finance Fund Albania (CFFA)	02.10.2015		NO	52%
12	Albanian Financial Institution	30.05.2016		NO	99.6%
13	MOGO Albania	10.11.2017	-	NO	n/a

of the allowed limit for open foreign exchange positions, the recognition of the exchange rate risk mitigating instruments, the increase of the elements recognized as part of the capital, etc

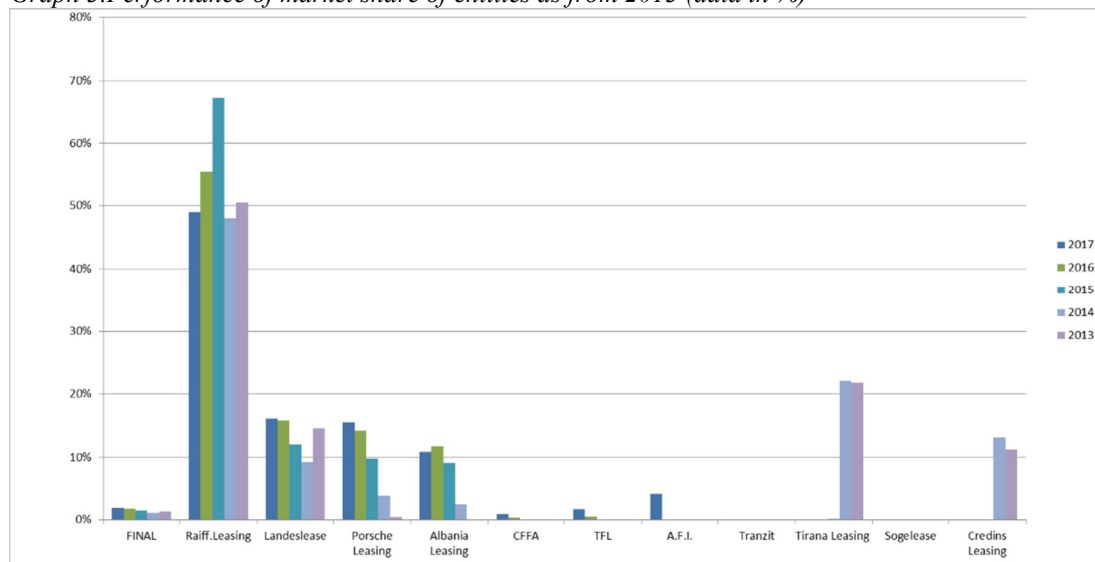
## **2. Financial leasing portfolio over the years and its financing**

In September 2017, the gross financial leasing portfolio for non-banking financial institutions reached 6.55 billion ALL (about EUR 50 million). The entity that has dominated the market for years is "Raiffeisen Leasing" (49%), with significant distance from other entities (Landeslease -16% and Porsche Leasing -15.5%). Due to the quality of information before and after 2013 (explained above in the *Regulatory Framework*), the comparative information on the performance of the financial leasing activity is divided into two periods: 2007-2012 and 2013-September 2017.

Graph 2. Performance of financial leasing activity of entities as from 2013 (figure /000 ALL)

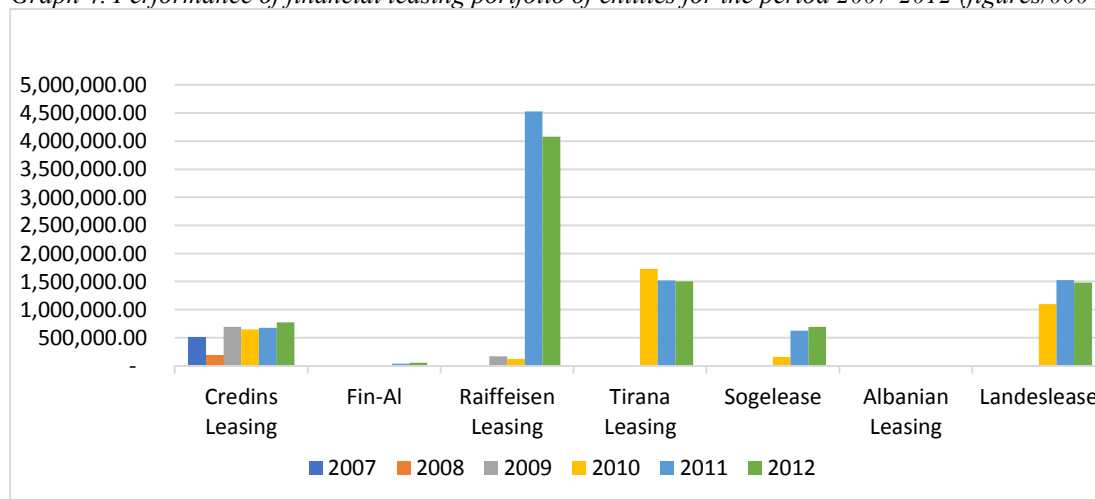


Graph 3. Performance of market share of entities as from 2013 (data in %)



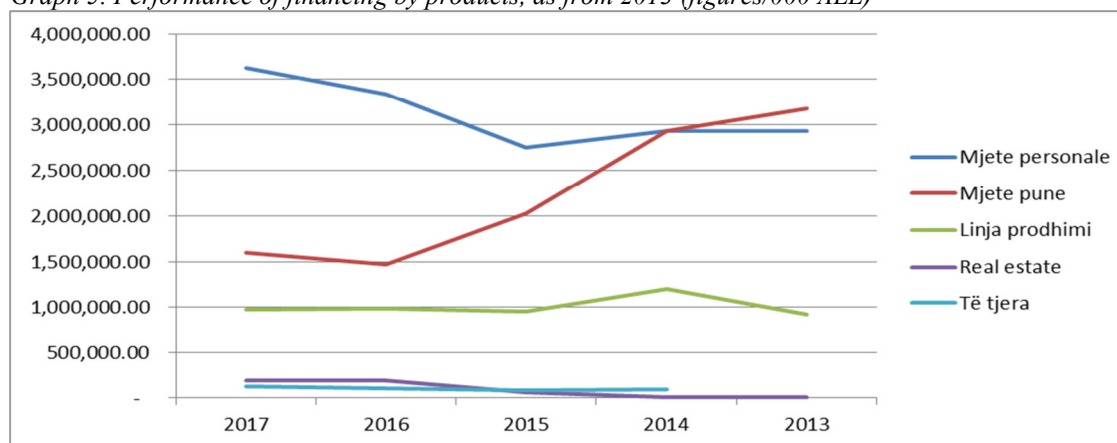
For the first part of 2007-2012, the picture shows a slight shift in market dominance, but since 2011 and onwards, Raiffeisen Leasing is clearly distanced from other entities.

Graph 4. Performance of financial leasing portfolio of entities for the period 2007-2012 (figures/000 ALL)

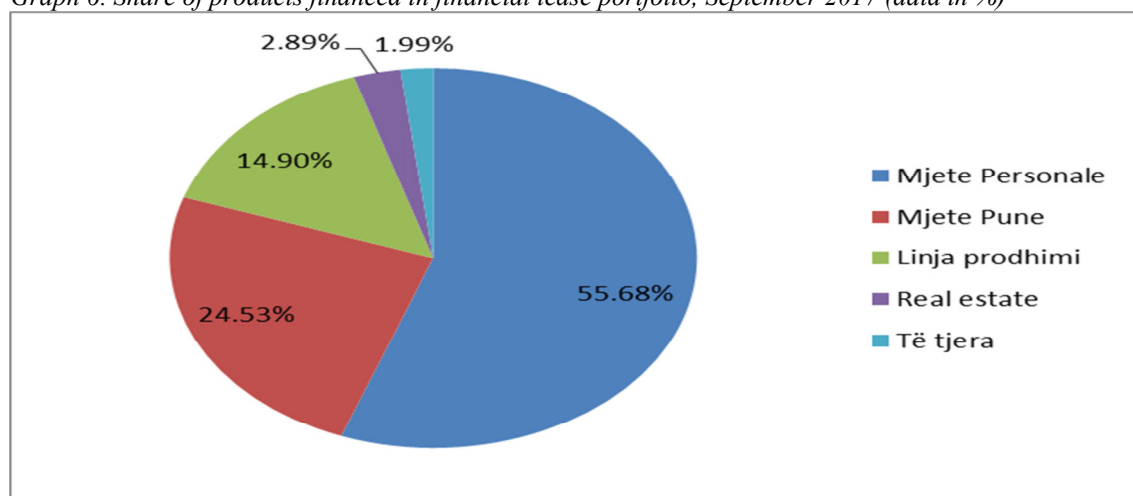


Raiffeisen Leasing's positioning is influenced by the strategy<sup>1</sup> of the banking group it is part of. This strategy has provided abundant financing resources for the entity, as well as a willing customer market, transferred by Raiffeisen Bank (the bank itself does not provide the financial leasing product or other loan products for the financing of personal or work goods, aimed at channeling customers to the financial leasing entity). On the other hand, this strategy has also affected the non-performing financing indicator, which has followed almost the same performance as that of Raiffeisen Bank's non-performing loan portfolio. The main reasons relate to the financing of big bank customers, mainly for working machineries and production lines, as well as the fact that the deterioration of client's quality at the bank is also reflected in the financial leasing entity, as the analyses are carried out in a consolidated manner. The other important entities in the financial leasing market are also bank-related entities, with presence in Albania or abroad (such as Porsche Leasing). The main advantage of such entities lies in the fact that they are highly financed by loans from group banks, thus increasing the leverage. The data reported during the analyzed period show that credit financing fluctuates within the limits of 50-90% of liabilities for bank-related entities and 0-75% for entities that are not related to banks. It has to be underlined that financing of real estate, although still with a low share in the portfolio, has had a significant increase in the last two years, especially by new entities. Currently, this product is financed only by two entities (Albania Leasing and A.F.I.) and in the following year it is expected to be provided by another entity (Landeslease). As it turns out from the analysis of financing by sectors (see below), real estate financing is the second sector with the highest share in the financial leasing portfolio. With regard to the age of financed products, new products remain dominant (60-70%) compared to used products. This structure reflects the careful attitude of the entities to the value of the financed asset (collateral, mostly movable), which is reduced (depreciated) within a relatively short time.

Graph 5. Performance of financing by products, as from 2013 (figures/000 ALL)

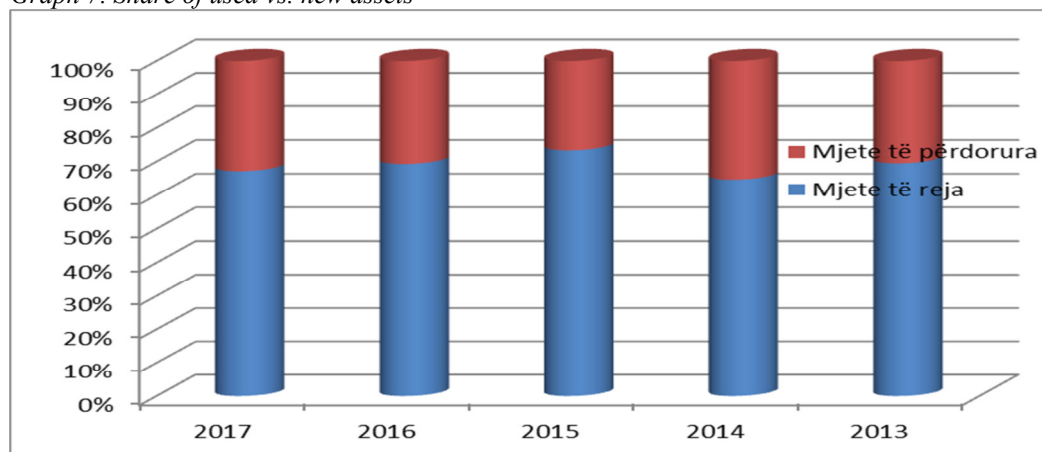


Graph 6. Share of products financed in financial lease portfolio, September 2017 (data in %)



<sup>1</sup> RBI Banking Group, since 2011, has been under the pressure of European supervisory authorities to reduce risk assets, including banking activity in Albania. For this reason, the group has decided that part of the activity is channeled into the financial leasing entity, to save short-term capital, and in the long run, if necessary, be able to sell this entity to secure capital, without affecting the bank's normal activity.

Graph 7. Share of used vs. new assets



**Sectors.** During the analyzed period, financial leasing has been consistently focused on financing businesses, with over 80% of the portfolio. The most financed sectors of the economy are “Car and household appliances trade and repair” (14%), “Real estate, leasing” (12%) and “Processing industry” (11%). It is worth noting that the distribution of financing by sectors has a satisfactory diversification.

**Maturity.** The financial leasing portfolio during the analyzed period is mainly focused on medium-term financing (1-5 years). Throughout the analyzed period we notice that the share of medium-term financing has increased from 65% to 85% in September 2017.

**Currency.** Currency analysis shows that almost the entire financial leasing portfolio is financed in Euro. This trend reflects the way suppliers provide financing facilities (vehicle and machinery prices are generally paid in Euro). Its effect is reflected in increased exposure of financial leasing entities to risk in two main directions:

- 1) In the case of foreign currency appreciation, the amount of the payment installment for customers would increase, whose income may be in local currency;
- 2) VAT receivable<sup>1</sup> that accumulates in the balance sheet is recorded in the national currency and creates an open foreign exchange position that has not been fully managed by all entities (treated below in supervisory norms).

### Performance indicators

**The financial result** for 2009-2017 is positive for most of the entities. Raiffeisen Leasing is the most profitable and sustainable entity. Credins Leasing and Tirana Leasing, in spite of their positive results, because of the strategies<sup>2</sup> of the banking groups they were part of, have interrupted their activity. Even the Sogelease entity has achieved a positive and growing financial result over its short 3 year period of activity.

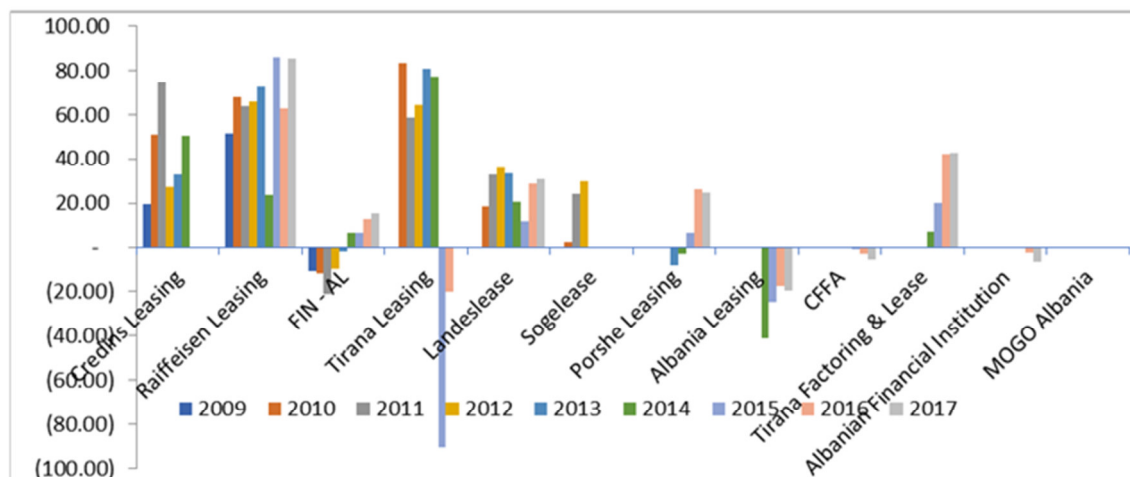
As regards new licensed entities from 2013 until today, it is noticed that due to start-up costs, they record average losses over the first 3 years, and generally turn to a positive direction after this period (Albania Leasing, Porsche Leasing, Crimson Finance Fund Albania, Albanian Financial Institution).

*Financial results performance of entities as from 2007 (figures in mln ALL)*

<sup>1</sup> Pursuant to the legislation in force, entities register deductible VAT as being entitled to an asset, as they pay this amount in full at the time of financing lease. The tax law provides that taxes and fees in the Republic of Albania are paid in ALL, thus bringing the forced conversion of this asset and creating a foreign exchange position. On the other hand, entities should collect the VAT paid by customers on each installment (in foreign currency) and pay it to tax authorities. The growth of the financing portfolio, as well as the long delays in the reimbursement of deductible VAT, have contributed to the expansion of the open foreign exchange position of the entities.

<sup>2</sup> Tirana Leasing has withdrawn from the market due to the withdrawal strategy from the Albanian market of the Piraeus group and Credins Leasing has joined the Credins bank to meet the bank's capital needs.

Graph 8: Profitability of financial leasing entities as from 2009 (in mln ALL)



### 5. Conclusion

Financial leasing activity, after a period of stagnation, seems to be regarded as a not fully unexplored opportunity for financial intermediation. Some of the key factors that are expected to affect the future of the development of this activity can be listed as follows:

1. Strengthening the enforceability of the legal framework and the revival of economic activity is expected to bring a positive impact on the development of financial leasing activity too.
2. The tightening of financing criteria by banks has led to new opportunities for financial leasing entities. Increase in the average amount of financing and increase in the share of new products (real estate) are some of the signs of orientation in this regard.
3. At a time of increase in capital demand, banks themselves may be interested in transferring certain assets to these entities (e.g. repossessed assets), because capital demands for them are less conservative.
4. The combination of the above elements, along with the growth of activity, is also expected to bring risks, reflected in non-performing financing. In addition, the combination of their activity with that of banks is expected to increase the complexity of the activity.
5. Using a high financial leverage (borrowing) may not allow these entities to lower the cost of products, at a time when market interest rates are declining. Moreover, the high leverage also affects (decreases) their ability to cope with risks or decreases in the business cycle, as well as the application of regulatory indicators at all times.
6. The inability to timely reimburse VAT remains a problem that affects not only the risk of an open foreign exchange position but also the limitation of liquid assets available to entities.

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- to determine the specific cost of each resource or to help minimise the aggregate cost of production.