



**USAID**  
FROM THE AMERICAN PEOPLE

# **Institutional Upgrade of HAMAG – Technical Assistance with Assumption of the UNDP/EU Guarantee Fund**

**Fourth Interim Report**

OCTOBER 2005

This publication was produced for review by the United States Agency for International Development. It was prepared by Development Alternatives, Inc., Mary M. Miller



# **Institutional Upgrade of HAMAG – Technical Assistance with Assumption of the UNDP/EU Guarantee Fund**

**Fourth Interim Report**

## Table of Contents

<b>BACKGROUND AND PROGRESS</b>	<b>3</b>
<b>NEXT STEPS</b>	<b>4</b>
<b>ANNEX 1 – MEMO TO TOMISLAV KOVACEVIC</b>	<b>6</b>
<b>ANNEX 2 – SBA TALKING POINTS</b>	<b>8</b>
<b>ANNEX 3 – GUARANTEES ISSUED BY HAMAG</b>	<b>9</b>
<b>ANNEX 4 – OUTLINE OF PROPOSED PREFERRED LENDER PROGRAM (PLP) PROVISIONS</b>	<b>11</b>

## BACKGROUND AND PROGRESS

This visit was conducted immediately after the HAMAG study tour to the US to meet with the US Small Business Administration concerning efficiently issuing guarantees, including instituting a preferred lender program. HAMAG concluded based on these meetings that it would benefit from a preferred lender program, and the early part of my visit was focused on the design of that program, as well as on “selling” the idea to agency staff, including the start of the shift in staff work from analyzing loans to acting as relationship managers for the banks. A summary of the preferred lender program provisions is attached.

The current status of HAMAG’s tasks is summarized in a memo to Director Tomislav Kovacevic, attached as Annex 1. Another item supplied to HAMAG during my visit was a list of SBA talking points (Annex 2), which summarize the SBA’s experience in transitioning from an agency that offered single guarantees to a mechanism that devolves approval authority to the banks, with the SBA taking an oversight role.

In these past few weeks there does appear to be a sea change in the attitude of the agency, and of Tomislav Kovacevic in particular. He has been asking for direction and comments beyond specific program points, and seems to have the big picture that the agency’s job is to facilitate credit and services for SMEs, further that a critical element of this will be to change the perception of the agency as another do-nothing government office. He is committed to reorganizing the agency to meet its purpose.

The objectives for this visit included the following points:

- Projection of HAMAG’s guarantees by number for the remainder of 2005 and for 2006 – An estimate by Veljko Paus of HAMAG, with which we concur, is 100 guarantees by the end of 2005 and 300 for 2006. Thus far 50+ guarantees have been issued, as shown on the attached schedule (Annex 3).
- Comments on how to best collect portfolio information from the banks – see below.
- Finalization of guarantee approval procedures for EU/UNDP fund-guaranteed loans – banks have been supplying information on their approval procedures to Katerina Kuhanec, and both the banks and HAMAG are committed to using HAMAG’s current approval procedure for new loans, as it is considerably more efficient and less time-consuming than the procedure prescribed in the UNDP transfer agreement.

This visit was a part of a series of visits to assist HAMAG in expanding its guarantees. The areas of assistance outlined in the original scope of work, and thumbnail sketches of progress, are summarized below:

1. Upgrading HAMAG’s administrative capacity with respect Agreement between HAMAG and UNDP/UNOPS – HAMAG has been delayed in pressing the participant banks for active participation in generating new loans for this program because the changeover of accounts had been delayed by the long time that it has taken to register Tomislav Kovacevic

as the new executive director for the agency. As soon as the account funds are in HAMAG's control the agency will be able to actively press for new loans, or threaten to transfer funds to banks that may be more active in lending in these sectors.

2. Assisting HAMAG to further develop its database and MIS so that it can accommodate the additional guaranteed loans from the UNDP/EU funds and increased organic growth – Only now does HAMAG seem to be persuaded that it does need to keep its records updated, through current loan information provided by the banks. There are five or six banks, including PBZ, ZABA, and HBOR, whose portfolios are large enough that they will need to transfer information electronically (in some fashion) rather than manually. Silvana Bandalo and HAMAG's external IT consultant will be meeting with these banks to discuss how this can be accomplished. A contact has already been set up at ZABA bank, and PBZ has promised to pass on a contact name.
3. Helping develop an efficient mechanism to conduct annual reviews of HAMAG's entire guarantee portfolio – necessary loan status information is starting to be collected. This is dependent upon getting the information described in point 2.
4. Assessing and making suggestions for improving HAMAG's guarantee origination and approval process – This was the principal purpose of the study tour, and progress has been made on getting the agency, and particularly Kovacevic, to rethink how the agency issues guarantees. See discussion in the memo to Kovacevic.
5. Assessing the feasibility of developing for HAMAG and the Croatian commercial banks a program similar to the U.S. Small Business Administration Certified or Preferred Lender Programs – HAMAG is now committed to developing a preferred lender program. See summary of proposed PLP terms (Annex 4) and memo to Kovacevic.
6. Training a HAMAG Croatian counterpart, who will assume responsibility for overseeing the UNDP/EU Guarantee Fund portfolio – Katerina Kuhanec, the new HAMAG finance officer for these guarantee funds, has been in place for a few months now. She has a strong banking background, and appears to be establishing a good rapport with several of the participant banks.

## **NEXT STEPS**

1. I will continue to follow on certain points from a distance, including:
  - Followup on UNDP progress
  - Followup on data update process
  - Commentary on bank requests for changes in guarantee provisions
2. ESP project staff should be present at the negotiating meetings with PBZ and ZABA and provide support as necessary to negotiate the acceptance of a PLP program.
3. As HAMAG staff transition to a relationship manager role with the banks, they may need to focus on providing better training to the banks about the role that a guarantee can play (i.e., a guarantee is a substitute for collateral, not for a lack of cash flow for loan repayment). It

- would be useful for a 1-2 hour training module to be developed to present to the banks to make this point, and ESP could assist in this.
4. HAMAG could benefit from a management planning session that ESP could assist in developing. This point should be pursued with Tomislav Kovacevic as he reorganizes the agency
  5. I am available to come back to Zagreb for a couple of days in early November for followup (I will be traveling through Europe in transition from another assignment). I think scheduling two days of visits at that time would be useful to keep change momentum going.

## ANNEX 1 – MEMO TO TOMISLAV KOVACEVIC

To: Tomislav Kovacevic, President, Executive Board, HAMAG  
From: Mary Miller, Consultant, DAI  
Date: 15 October 2005  
Re: Discussion of 5 October 2005  
CC: Tocher Mitchell, Financial Advisor, and Jim Winkler, COP, ESP Project

As we discussed, HAMAG recognizes its role in supporting small businesses in Croatia by encouraging credit for these businesses through providing guarantees to banks. We have discussed various steps that HAMAG can take to increase the number of guarantees that it issues, and are agreed that it is critical that HAMAG act quickly and decisively to make it clear that it means business. Specific areas that require attention include:

Institution of a preferred lender program in Privredna Banka Zagreb and/or Zagrebacka Banka – response to the initial presentation of a PLP was fairly well received, but both banks indicated that they had requested changes in the terms of the guarantee, and had not received responses to these inquiries<sup>1</sup>. HAMAG needs to respond immediately to these requests, as well as to hold followup meetings to further explain the program. The target should be to enlist at least one of these banks in the PLP. In this way HAMAG will have country-wide coverage, and it is likely that the bank that has not joined will do so, to keep up with the other.

Review non-paid requests for activation of guarantees from PBZ and ZABA – HAMAG staff in the bank meetings need to be fully aware of all the details of non-payment to respond when this subject comes up in meetings. HAMAG should also consider “repairs” of the guarantees, making at least partial payments. This will show that HAMAG is committed to working with the banks, and will also show flexibility.

Request a ruling from the Central Bank concerning the strength of HAMAG’s guarantee – this has been a major concern for the banks, and needs to be clarified. HAMAG’s guarantee is irrevocable, and is not conditional beyond the bounds of what is considered normal practice.

Management information system – needs to have information on the status of guaranteed loans updated regularly, so that HAMAG can accurately estimate its contingent liability. This information is needed to determine the adequacy of HAMAG’s reserves, therefore the quality of its guarantee. For the banks with the largest portfolios of guaranteed loans (including PBK, ZABA, and HBOR) this

---

<sup>1</sup> Both Mary Miller and ESP staff are prepared to review these requests, and comment concerning “best practice”.

will require meeting with the banks along with HAMAG's IT specialist/firm to determine how the information can be transferred electronically.

Use information reports – Despite having a robust IT system, HAMAG needs to start using the information that the system generates. Reviews of regular reports by all staff members is the basis of setting performance standards and targets for the agency and for individual staff members, and build team motivation.

Speedup of processing for other banks – HAMAG needs to streamline its regular review process for issuing guarantees, so that it can process more work. The major recommendation here is that HAMAG institute a relationship manager system so that individual staff members are responsible for marketing to specific banks, and spend less of their time reviewing applications, and more time encouraging the banks to submit applications that are complete and well-analyzed already. ESP can provide support in developing additional short term training modules for presentation to bank staff. Internal streamlining is best accomplished by creating a task force among those staff members who do loan analysis.

Followup on UNDP loan programs – HAMAG is just now getting the collateral funds transferred to accounts under its control. Once this is complete HAMAG should be more forceful in seeking information and action from the banks on past due loans, but more important, on generating new loans. It would also be appropriate to send a courtesy followup report on progress to UNDP and the EU, in large part to maintain good relations with the EU.

## ANNEX 2 – SBA TALKING POINTS

### U.S. Small Business Administration – Talking Points on Preferred Lender Program

- Over the past few years the SBA has transformed its way of doing business from providing loan guarantees on a case by case basis to authorizing banks to apply the guarantee themselves through a preferred lender program.
- This change in work flow and approval flow was developed in response to complaints from the banks about the great amount of paperwork required, and well as the time needed, to get an SBA guarantee.
- The banks have responded well to this approach, and bank participation with the SBA, as well as the volume of guarantees issued, has increased substantially as the new programs have been introduced.
- In SBA's experience, the claims rate (activation rate of guarantees) is the same under the preferred lender program as under the standard program. Overall, about 8-9% of guarantees are paid, and the SBA is later reimbursed for 2-3% (from later sale of collateral or other payments) for a final loss rate of about 6%.
- The typical job in the SBA regional office has transformed from loan analysis to relationship management with the banks. The Lender Relationship Specialist (formerly the credit analyst) is assigned to manage the relationship with specific banks, including providing information and training, encouraging participation, and monitoring bank performance.
- The change in the work procedure means that the SBA can handle a much greater volume of business than it did in the past. At the same time the number of SBA staff has been dropping.
- Statistics for 2001-2003 indicate that the SBA only approved 5% of its guarantees under its standard approval procedure (in which it reviewed the bank's loan analysis) for 22% of the value of guarantees. All other guarantees are issued through a delegation of authority to the banks. In other words, SBA is only involved in the analysis process for the largest loans, and for the occasional bank request from a bank that does not regularly issue SBA-guaranteed loans.
- In the SBA's review of requests for payment under guarantees, it expects the loan to be secured and documented in accordance with the bank's original authorization. If documentation is not complete, and the SBA concludes that collections have been limited because of this, the SBA will require a "repair" of the guarantee, i.e., will reduce its payment in an amount equal to the error. The repair experience, however, is quite low. SBA indicates that 18% of guarantees require a repair, which totaled only 6% of the guarantee funds paid out.
- A repair is only required if an error or omission is deemed to have caused the collection amount to be lower. An error or omission that has no effect on the collection amount does not require a repair.
- SBA only reviews the use of funds (i.e., were loan funds disbursed for use, or acquisition of assets, as required by loan terms) in activations of guarantees in the first 18 months of the loan. Thereafter an incorrect use of proceeds is not considered to affect the repayment of the loan.
- SBA requires monthly reporting from the banks, and particularly monitors those loans with payments that are 60 days or more past due.

MMM 9/27/05

## ANNEX 3 – GUARANTEES ISSUED BY HAMAG

HAMAG Guarantees - New Program - 1 January to 26 September 2005

Lender	Loan Type	Loan Amount in HRK	Amount of Guarantee	Average Loan Size	# Loans
Credo Banka	13	3,000,000	1,500,000	3,000,000	1
Croatia Banka	14	189,140	151,312		
	14	180,000	144,000		
	13	1,127,017	563,508		
	14	164,900	131,920		
	Totals	1,661,057	990,740	415,264	4
Erste Bank	14	339,311	271,448		
	12	894,977	304,292		
	14	34,386	27,509		
	14	1,470,281	1,176,225		
	12	879,119	395,603		
	Totals	3,618,074	2,175,077	723,615	5
Hypo Alpe-Adria	12	1,999,853	1,399,897		
	14	1,062,378	849,902		
	12	892,301	446,151		
	11	2,250,000	1,125,000		
	14	128,228	102,582		
	14	1,172,960	821,072		
		7,505,720	4,744,604	1,250,953	6
Karlovacka Banka	13	5,000,000	2,500,000	5,000,000	1
Nova Banka	14	150,000	120,000		
	14	1,500,000	1,200,000		
	14	90,000	72,000		
		1,740,000	1,392,000	580,000	3
Podravska Banka	14	1,500,000	1,200,000	1,500,000	1
Slatinska Banka	11	400,000	200,000	400,000	1
Slavonska Banka	14	100,000	80,000		
	13	280,000	140,000		

	14	400,000	320,000		
		780,000	540,000	260,000	3
Totals, Excl HBOR		25,204,851	15,242,421	1,008,194	25
Totals by Loan Type excl HBOR					
Agriculture	11	2,650,000	1,325,000	1,325,000	2
ASSC	12	4,666,250	2,545,943	1,166,563	4
Growth and Devel	13	9,407,017	4,703,508	2,351,754	4
New Business	14	8,481,584	6,667,970	565,439	15
Working Capital	15	none			
Totals		25,204,851	15,242,421	1,008,194	25
HBOR Loans					
Agriculture	11	30,853,999	15,427,002	1,285,583	24
New Business	14	860,608	688,486	430,304	2
Total HBOR Loans		31,714,607	16,115,488	1,219,793	26
Total All Loans		56,919,458	31,357,909	1,116,068	51

## **ANNEX 4 – OUTLINE OF PROPOSED PREFERRED LENDER PROGRAM (PLP) PROVISIONS**

These terms were presented to HAMAG employees on 26 September 2006, then were informally presented to Privredna Banka Zagreb and Zagrebacka Banka in early October 2005. These terms are subject to negotiation. It is expected that more formal meetings will take place with the banks to further discuss this prospective program.

Eligible banks: PBZ and ZABA

Guarantee limit: HRK 20 – 30 million

Bank to provide a one page application form with borrower information, as well as current and prospective employment. HAMAG would have one day to review the application, and would substantially use that time to check that the borrower was not in default on another guaranteed loan.

Loans eligible for guarantee: Up to 50% of regular program amounts. (Example: the program for growing businesses has a ceiling of HRK 5 million, with a 50% guarantee. A loan of up to HRK 2.5 million could be approved under the PLP program.)

Loan Requirements:

Monthly reporting of loan status

- Loan must be for new credit – no refinancing
- Bank would certify that any other loans to the borrower are current and paying as agreed.
- Regular program requirements apply

Bank Requirements to maintain PLP status:

- Maximum activation %
- Maximum % of portfolio with payments over 60 days past due
- Overall bank strength and quality

Requirements to activate guarantee: same as regular program