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

Fifth Interim Report

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

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BACKGROUND AND PROGRESS

This was a brief, two day visit to review progress to date. A summary of points of discussion with HAMAG are contained in a memo sent to Executive Director Kovacevic, attached as Annex 1.

HAMAG has issued 67 guarantees in 2005, through September 26. 37 of these have been issued for HBOR. Most recently, Hypo Bank has been particularly active with nine guarantees issued. A list of guarantees by bank and purpose is attached as Annex 2.

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** – Transfer of depository accounts from UNDP to HAMAG control are finally taking place. The banks do report in regularly on the status of the guaranteed portfolios, and are asking for HAMAG assistance in identifying local entrepreneurship centers to work with to seek out new borrowers. The banks have also been requesting payment of guarantees on past due loans, which we have encouraged as a goodwill gesture. This program is being well-managed by Katarina Kuhanec, a banker who was brought in to handle this task. She further has become an important resource within HAMAG on banking practice.
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** – HAMAG is now finally working out an electronic reporting procedure with Zagrebacka Banka (ZABA), which it will then introduce to the rest of the banks with substantial portfolios. Staff have also met with HAMAG's computer consultant to determine the best way to electronically pick up the monthly reports of the UNDP loans.
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** – See discussion in the memo to Kovacevic. He is particularly inhibited by some staff who do not want the agency to change, thus is dealing with substantial morale and management problems. We have suggested starting with those staff members who will embrace change, and hope that they will set a model for the others.
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** – Kovacevic is now meeting with the two largest banks in Croatia, Privredna Banka Zagreb and ZABA, and expects to sign up one or the other bank shortly. He has backed off on immediately offering a preferred lender status to these banks, as he finds it more acceptable, in terms of dealing with other banks, to first draft them into the program and later offer them preferential terms.

6. Training a HAMAG Croatian counterpart, who will assume responsibility for overseeing the UNDP/EU Guarantee Fund portfolio – As noted above, 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

At this point HAMAG needs to implement changes in its organization to encourage more small business lending by the banks, through issuing more guarantees. In the eleven months that ESP has been working with HAMAG we have seen a major shift in attitude, from a complacent government office to an agency that recognizes its role in facilitating credit for small businesses. While the book is not closed on providing additional technical assistance to HAMAG, at this point such assistance will be more effective if requested by HAMAG than if offered by the project.

ANNEX 1 – MEMO TO KOVACEVIC

To: Tomislav Kovacevic, President, Executive Board, HAMAG
From: Mary Miller, Consultant, DAI
Date: 8 November 2005
CC: Tocher Mitchell, Financial Advisor, and Jim Winkler, COP, ESP Project

This is a summary of the points that we consider important for HAMAG's continued development as an agency to serve SMEs through issuing guarantees.

Reorganization of the agency to a relationship manager structure, away from its current focus on individual loan analysis – this implicitly includes setting targets and responsibilities, as well as doing projections of performance. We recognize that some agency staff are reluctant to change their ways. However we do feel that bringing along certain individuals as relationship managers (for instance, bringing them to meetings with all banks, then to meetings with individual banks, and then designating them as the point of contact for those individual banks) will be motivating, and may encourage greater interest in change in the rest of the staff. We also recommend that certain reports, such as the number and amount of guarantees, and the banks for which these are issued, be printed out and regularly reviewed in staff meetings, so that all staff members are aware of the agency's performance.

Information technology – it is important that the agency develop the means to update its records with current information from the banks. In the near future the Basel II standards will be implemented, which will require the banks to estimate the likelihood of default (therefore need for reserves) on loans. In turn, HAMAG needs to be able to properly estimate its contingent liability, so that its guarantee can be properly valued by the banks. This can only be done with accurate, timely information from the banks. For the banks with a great number of guarantees (PBZ, ZABA, HBOR) this means that electronic reporting of some sort will be necessary, as the number of loans that have been guaranteed is too large to update manually. Silvana Bandalo and SLON – ing are pursuing this. Note that this does need immediate attention.

The assumption of the UDNP loan portfolio is going along as expected, and we are particularly pleased that this is being handled by Katarina Kuhanec, whom we regard as very competent, and a good resource for the agency. HAMAG does need to encourage the banks to make more loans under the program. In turn it should willingly pay guarantees as requested, as a goodwill gesture. We also recommend that you report to UNDP and EU about the progress of the program, including new loans guaranteed (if any), guarantees activated, collection efforts of the banks, and cooperation with entrepreneurship centers. While the handover agreement does not require that HAMAG report on progress we feel that this would be particularly good for building a relationship with the EU.

Meetings with PBZ and ZABA – we are pleased to see that you have scheduled these, and we expect that you will be able to conclude an agreement with at least one of these banks shortly. We recommend that you bring specific information with you to the meeting about all requests for activation of guarantees, so that you can respond to any complaints that guarantees have not been paid.

HBOR – We recognize that there is some value-added benefit to providing guarantees for HBOR, and we further acknowledge that HAMAG is required to provide guarantees to HBOR under certain circumstances. However, we think that HAMAG's main role is in encouraging the private commercial banks to be lending to Croatian SMEs. Therefore we suggest that you find some shortcuts to dealing with HBOR such as minimizing analysis time, providing a standardized analysis format to them, and even giving them a preferred lender status, so as to not devote additional time and resources to dealing with them.

ANNEX 2 – GUARANTEES ISSUED BY HAMAG

Annex 2 HAMAG Guarantees - New Program - 1 January to 26 September 2005				
Lender	Loan Type	Amount of Guarantee	Average Gtee Amount	# Loans
Credo Banka	13	1,500,000	1,500,000	1
Croatia Banka	14	151,312		
	14	144,000		
	13	563,508		
	14	131,920		
	Totals	990,740	247,685	4
Erste Bank	14	271,448		
	12	304,292		
	14	27,509		
	14	1,176,225		
	12	395,603		
	Totals	2,175,077	435,015	5
Hypo Alpe-Adria	12	1,399,897		
	14	849,902		
	12	446,151		
	12	446,151		
	11	1,125,000		
	14	102,582		
	13	640,015		
	14	794,760		
	14	960,000		
		6,764,458	751,606	9
Karlovacka Banka	13	2,500,000	2,500,000	1
Nova Banka	14	120,000		
	12	1,400,000		
	14	1,200,000		
	14	640,000		
	14	72,000		
		3,432,000	686,400	5
Podravska Banka	14	1,200,000	1,200,000	1
Slatinska Banka	11	200,000	200,000	1
Slavonska Banka	14	80,000		
	13	140,000		
	14	320,000		
		540,000	180,000	3
Totals, Excl HBOR		19,302,275	643,409	30
Totals by Loan Type excl HBOR				
Agriculture	11			2
ASSC	12			6
Growth and Devel	13			5
New Business	14			17
Working Capital	15			0
			Total	30

HBOR Loans				
Agriculture	11	21,012,502	656,641	32
ASSC	12	1,385,072	692,536	2
Growth and Devel	13	3,500,000	3,500,000	1
New Business	14	688,486	344,243	2
Total HBOR Loans		26,586,060	718,542	37
Total All Loans		45,888,335	684,901	67