



## POLICY RECOMMENDATION SUMMARY

# Good Practice Workshop – Theme 1 – Micro Loans

6 September 2012 – Tallinn Estonia

## 1. BACKGROUND

Focusing on the development and implementation of non-grant financial based instruments, the overall aim of the DIFASS PROGRAMME is to improve access to finance for innovative SMEs by exchanging good practice on innovative business support measures. This project originates from a previous 2008 Interreg Project where it became clear that non-grant financial support instruments are less likely to succeed on their own and need to be integrated with other non-financial support services to be successful.

Run in conjunction with 26 European Partners the project covers 8 themes – Micro Loans, Internationalisation, Guidance to Finance and Loan Guarantee Schemes, Mixed Grant/Non Grant, Intellectual Property and Human Capital, Spin offs/Start up/Early stage, Jeremie and other Revolving Funds, Mezzanine/Equity/Venture Capital.

## 2. MICRO FINANCE – OVERVIEW

Micro Finance is defined by the offer of financial services (e.g. savings, loans, insurance etc.) to economically disadvantaged people; individuals on a low income who may have no access to formal financial systems and who may have no regular paid employment.

Exclusion from banking services often constitutes a major obstacle to the launch of new business activities. Micro Finance can help foster entrepreneurship by facilitating business start-ups. Granting micro loans to the unemployed and marginalised can help them become more economically independent players able to participate more fully in a financial society.

Sources of Micro Finance include credit and savings cooperatives, Non-Governmental Organisations (NGOs), programmes implemented by international institutions, regulated micro finance institutions, micro finance and commercial banks.

Filling a gap for loans for people needing to enhance their own livelihood in **Central and Eastern Europe**, the micro finance sector continues to expand and become more highly structured with commercial banks increasingly interested in downscaling in order to provide micro loans for economically disadvantaged groups. In **Western Europe**, however, the sector's growth has been more limited, despite increasing interest in its potential.

More than 85,000 micro loans for a total value of approximately €828M were granted in 2009; with around 26% made in Eastern Europe and 74% in Western Europe. With typical loans ranging from €200 to €37,000 and an average reimbursement rate of 83%, a 6% fall on previous years attributed to the impact of the financial crisis. More recent surveys show a decrease in the number and value of loans of around 20%.





#### **FURTHER INFORMATION:**

**DIFASS:** Code of Good Conduct for Microcredit Provision <http://www.difass.eu/downloads>

**DIFASS YOU TUBE CHANNEL** Overview of Micro Finance – Simeon Karafolas, Scientific Partner:

<http://www.youtube.com/watch?v=QWyuCpE0rDQ&feature=youtu.be>

### **3. OVERVIEW OF WORKSHOP DISCUSSION/KEY LEARNING POINTS**

Aiming to improve access to finance for innovative SMEs, the DIFASS project is tasked with identifying and encouraging take-up of programmes and innovative mechanisms that support SMEs. Partners in the programme are looking to establish how the examples of good practice presented and discussed at each workshop can help them develop policies and programmes and support businesses in their own region.

The key issues to be considered when assessing each particular theme and good practice programme include:

- Overall Impact: Are Micro Loan programmes providing the support needed by SMEs? Have the programmes presented improved the current situation?
- Are the programmes presented responding to the difficulties encountered by those SMEs without a lending history and no collateral i.e. those who find it particularly difficult to access finance?
- Are funds supporting ‘innovative’ firms? Those firms most likely to contribute to longer term economic growth.
- What, if any, other non-financial support services have been integrated into the programme to improve the success rate of the businesses involved?
- Has the approach taken helped to influence commercial lenders i.e. banks to overcome their reluctance to help SMEs?
- Are Micro Loan programmes sustainable, transferable solutions that can be used to help small businesses?
- Key Recommendations: Dos and don’ts, what would the programme players do differently next time?

#### **Good Practice Micro Loans – Overall Impact**

Providing an estimated total of €22M plus for more than 2,300 firms, each of the schemes presented either directly or indirectly helps micro businesses and SMEs (not necessarily start-up businesses) gain access to finance that may not have been available from other sources. The Good Practice schemes presented were:

- **Loan Guarantee Scheme** – KredEx, Estonia
- **Credinfo: Internet Based Micro Finance Management System** – Zala County Foundation for Enterprise Promotion (ZMVA) Hungary
- **Entrepreneurship Promotion Fund** – INVEGA, Lithuania
- **Opportunity Microcredit** – Regional Development Agency Centru, Romania





Two of the good practice schemes have been set up to support businesses in their region and two of the schemes presented, Credinfo and Microcredit, were set up as mechanisms to help other agencies and regions, as well as support their own clients.

### **Help for young business without a lending history and no collateral**

Having some form of collateral is a requirement of all schemes studied. Mindful of the difficulty of customers paying back micro loans in the recession, safeguards in the form of careful checks are features of all programmes. All applicants need to submit a realistic, viable Business Plan and also need to demonstrate their individual creditworthiness; that they are able to meet their financial obligations and **have some form of collateral**. Low credit scores from a high percentage of start-ups in the Kredex scheme in particular made it difficult to approve loans; with only half of applications getting a positive guarantee decision. Although aimed at start-ups, trading criteria for the programmes featured varies from viable business trading for less than a year, to companies less than 3 years old.

### **Have funds been directed to Innovative businesses?**

The nature of the client group that micro loans are targeted at helping means that the businesses involved may not necessarily be considered innovative. Two of the schemes have an equally strong social purpose with agricultural businesses amongst the four key sectors targeted by the Microcredit scheme and KredEx concentrating activity on commercial enterprise.

### **What other non-financial support services have partners integrated into the programme to help businesses?**

Business skills training formed part of the integrated support package for three of the schemes, with applicants for the Microcredit scheme provided with help to develop viable Business Plans before submitting their application. Joining up with other stakeholder programmes, these additional benefits included help from the local Science Park through to access to optional training and consultancy support all aimed at helping companies develop the knowledge needed to improve their chance of success.

### **Have any of the schemes influenced Banks, encouraging them to get more involved in helping small firms access finance?**

Only one of the schemes, KredEx, was delivered in association with the banking sector who although operating the scheme at a loss because of relatively high overheads at the outset of the programme, viewed its involvement as having a longer term payback. This payback included the market intelligence gained, helping them to identify good risks in the future, an improved profile/brand, as well as long term commercial gains arising from those successful businesses supported.

### **Are Micro Loan programmes sustainable transferable solutions?**

The impact of the recession on new programme funding makes development of sustainable programmes that can support businesses now and in the future, a crucial factor. The inability of customers to pay back micro loans in the recession, withdrawal of creditors and the challenging political climate are key concerns for all programmes.





Set up as a self-sustaining public organisation by the government, **KredEx** operates as a self-financing loan initiative operated in conjunction with Banks, a careful approval process means that reimbursement rates are 75%, representing a good loss ratio for KredEx, who are able to absorb losses of up to 20-30%. Having compared the scheme to grants, they consider the scheme much more effective. Companies awarding grants have a different mindset, it changes their thinking, and seen to be not so business-like and not so likely to survive.

Selecting the right financial intermediaries, in this case the Lithuanian Credit Union network rather than larger stakeholders has played a key role in the sustainability of the **Entrepreneurship Promotion Fund**. Equally committed to supporting and financing micro start-ups, contributing members funds to the project enabled the Credit Union to offer more favourable terms. Both the guarantee, compensation of interest payments and 'smart money' (funds that come with training attached), all help to mitigate the risk for financial partners and make the scheme more attractive to unemployed and self-employed entrepreneurs. Debt finance was not common practice in Lithuania before the programme and has filled a gap in the market; unemployed, self-employed entrepreneurs and companies now have access to capital in the form of microcredits.

Sustainability of the online **Internet Based Credinfo** tool developed for delivery stakeholders is supported by two key factors; the availability of a tailored product with the potential for partners to adapt and set up their own eligibility criteria and key terms for micro loans making it an ideal readymade solution for stakeholders; and the use of a built-in management information software package enabling easy comprehensive financial analysis of individual applicants as well as access to real time management information on their clients and overall status of their funding scheme.

**Opportunity Microcredit** has the backing of a proven global micro finance model operated by the OIN. They provide the technical assistance and links to the financial systems and processes needed to implement the programme as well as funds for the loans, minimising the set up costs and risks for the Regional Development Agency promoting the scheme through their own networks. With the backing of international best practice to draw on, Romanian stakeholders consider the scheme represents a good return.

### **Transferability**

Each programme was considered by partners to have potential for transfer. Two of the programmes, **Credinfo** and **Opportunity Microcredit** are ready made programme models that can be tailored and adapted to meet the needs of each partner's circumstances, with the other two programmes presented; the **Entrepreneurship Promotion Fund** and **Loan Guarantee Scheme**, transferable subject to market conditions and stakeholder engagement, in part or in full.





### **Key Recommendations: Dos and Don'ts – Top Tips**

Key success factors identified by programme leads and partners included:

#### **Client Support**

- ✓ Make the repayment period of the micro loan scheme as flexible as possible to help meet the challenges of entrepreneurs with innovative ideas having a longer development journey. Additional grace period – providing innovative firms in particular with an additional grace period e.g. 6 months, gives them the time to develop and test their product or service before going out to market.
- ✓ Providing companies with mandatory Business Planning support and optional business skills training helps companies develop the knowledge they need and improve their chances of success.
- ✓ Make training programmes and consultant support compulsory, rather than optional.
- ✓ Provide as much training and support as possible for those start-ups needing to overcome financial illiteracy
- ✓ Keep the microloan approval process as short as possible and paperwork involved in proportion to the value of the loan.

#### **Programme Strategy**

- ✓ Adding a range of features to the package such as a loan guarantee, compensation of interest payments and 'smart money' all add up to helping to mitigate the risk for the financial intermediary and make the scheme more attractive to unemployed and self-employed entrepreneurs.
- ✓ Minimise the administrative requirements connected to the loan; keep the paperwork involved, regulations, and state support requirements etc proportionate to the value of the loan.
- ✓ Selecting the right financial intermediaries at the outset i.e. partners committed to supporting and financing micro start-ups, rather than large stakeholders, is critical to the success of the programme.

#### **4. NEXT STEPS – PARTNER POLICY IMPLEMENTATION PLANS/ APPLICATION OF GOOD PRACTICE**

Each region is to develop its own Policy Implementation Plan, taking into account the lessons learnt from Workshop discussions, the findings from the scientific analysis and the assessment of the pilot implementations, all of which will be used to implement or improve their own policies for supporting SMEs in different themes.

#### **FURTHER INFORMATION:**

**DIFASS:** <http://www.difass.eu/downloads>

**DIFASS YOU TUBE CHANNEL:** <http://www.youtube.com/user/difassworkshops>





## ANNEX 1: MICRO LOANS WORKSHOP – METHODOLOGY

The initial presentation on the micro loans theme from the project’s technical partner was followed by presentations and discussion on four areas of good practice:

- **Loan Guarantee Scheme** – KredEx, Estonia
- **Credinfo: Internet Based Micro Finance Management System** – Zala County Foundation for Enterprise Promotion (ZMVA) Hungary
- **Entrepreneurship Promotion Fund** – INVEGA, Lithuania
- **Microcredits** – Regional Development Agency Centru, Romania

Facilitated using a World Café technique partner discussion then focused on three key questions:

- What opportunities can you see for transfer?
- What challenges would need to be overcome?
- What policy recommendations will you make?

With rotated discussion groups used as an opportunity to discuss each programme, the fit with existing partner programmes, key learning points and opportunities for transfer delegates voted for the Good Practice of most interest, with results as follows:

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|--|---------|
| ▪ Micro Loan Scheme                              | 4 Votes |
| ▪ Internet Based Micro Finance Management Scheme | 9 Votes |
| ▪ Entrepreneurship Promotion Fund                | 9 Votes |
| ▪ Micro Credits                                  | 3 Votes |

**Good Practice 2, the Internet Based Micro Finance Scheme and Good Practice 3, the Entrepreneurship Promotion Fund** were identified as the schemes generating the most interest in terms of taking forward

## ANNEX 2: MICRO LOANS WORKSHOP – PROGRAMME SUMMARY

PARTNER	GOOD PRACTICE SUMMARY – PROGRAMME, KEY OBJECTIVES & INNOVATIVE FEATURES AT A GLANCE	POLICY IMPLEMENTATION – KEY RECOMMENDATIONS ARISING FROM THE WORKSHOP
<p><b>KredEx Estonia</b> In association with: Swedbank, Tallinn Science Park Tehnopol</p>	<p><b>PROGRAMME:</b> Delivered in association with five Banks in Estonia and support from Tallinn Science Park Tehnopol, the <b>Start-Up Loan Guarantee Scheme</b> is a loan guarantee initiative run by KredEx on behalf of the Estonian Government.</p> <p><b>KEY OBJECTIVES: To improve the number of successful start-ups in Estonia by alleviating the four problems associated with new businesses;</b> high failure rates, lack of credit history, lack of collateral and the owners' unwillingness to bear risks.</p> <p><b>INNOVATIVE FEATURES:</b></p> <ul style="list-style-type: none"> <li>✓ Run in association with Banks, encouraging them to play a more active role in SME finance</li> <li>✓ KredEx Loan Guarantee means limited liability (30-40%) for Clients</li> <li>✓ Programme operating costs financed from percentage of the loan amount and guarantee fee</li> </ul>	<ul style="list-style-type: none"> <li>▪ <b>Provide flexible terms.</b> Make the micro loan scheme more flexible to help meet the challenges of entrepreneurs with innovative ideas having a longer development journey.</li> <li>▪ <b>Provide more training and support for those start-ups needing help to overcome financial illiteracy.</b></li> </ul>

<p><b>Zala County Foundation for Enterprise Promotion (ZMVA) Hungary</b></p>	<p><b>PROGRAMME:</b> An online application, assessment and credit management facility, the <b>Internet Based Micro Finance System* (Credinfo)</b> was developed to provide an online facility for Hungary's Local Enterprise Agency network helping SMEs to access funds.</p> <p><b>KEY OBJECTIVES:</b> To accelerate the credit application process, helping for-profit and not-for-profit SMEs to access finance. To provide a one-stop internet based client application and management solution for any agency managing micro funding schemes for SMEs.</p> <p><b>INNOVATIVE FEATURES:</b></p> <ul style="list-style-type: none"> <li>✓ Online client application and tracking system (optional help available for preparation of required business plan)</li> <li>✓ Enables an easy and comprehensive financial analysis of the applicant</li> <li>✓ 'Ready to go model' easily adapted and tailored to meet individual stakeholder circumstances/specific client groups</li> <li>✓ Provides subscribers with real time information and funders with status reports</li> </ul>	<ul style="list-style-type: none"> <li>▪ <b>Develop appropriate administrative systems</b></li> </ul> <p>If /where public money is involved, make sure the paperwork (regulations, state support, roles etc.) do not become too heavy compared to the size of the loan.</p>
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\* One of two programmes from the eight themes covered by the DIFASS Programme selected for pilot transfer and implementation to other regions, the Internet based Micro Finance System (Credinfo) from Hungary will be transferred to regions in Estonia, Spain, Italy and the Slovak Republic.

<p><b>INVEGA</b> Lithuania</p>	<p><b>PROGRAMME:</b> Set up in 2009 and delivered through a network consortium of Credit Unions the <b>Entrepreneurship Promotion Fund</b> is a microcredit loan scheme aimed at supporting start-ups and viable micro companies trading for &lt; 12months.</p> <p>Using 'smart money', loans are accompanied by additional benefits; help with Business Planning and access to <u>optional</u> training across a range of six key business skills units.</p> <p><b>KEY OBJECTIVES:</b> To provide finance for start-ups as well as businesses looking to expand.</p> <p><b>INNOVATIVE FEATURES:</b></p> <ul style="list-style-type: none"> <li>✓ Use of 'smart money'; loan plus proactive Business Planning and six key business skills units to improve success</li> <li>✓ Delivered through a consortium of 57 Credit Unions enabling more favourable micro credit terms.</li> <li>✓ Use of a tailor made financial grant instrument enabling companies considered higher financial risks at the outset to recover compensation for higher level interest rates, (means they can recover up to 95% of interest paid.</li> </ul>	<ul style="list-style-type: none"> <li>▪ <b>Make training programmes and consultant support compulsory</b> i.e. rather than optional for programme beneficiaries.</li> </ul>
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<p><b>Regional Development Agency Centru Romania</b></p>	<p><b>PROGRAMME:</b> Operated by <b>Opportunity Microcredit</b>, a non-banking financial institution set up to support micro and small size enterprises in Transylvania, <b>Microcredits</b> are flexible loans granted to creditworthy micro businesses unable to access bank finance. Micro firms can use loans to pay off their debits, refinance their enterprise and/or fund capital or working capital expenditure.</p> <p><b>KEY OBJECTIVES:</b> To provide companies with the financial resources needed to enable them to widen their business opportunities, helping them to grow and achieve more efficient sustainable development.</p> <p><b>INNOVATIVE FEATURES:</b></p> <ul style="list-style-type: none"> <li>✓ Specialise in building long term relationships with their client base, includes the agricultural sector</li> <li>✓ ‘Ready to go model’ and backed by a highly experienced international funders/organisation and funders with expert knowledge and experience of microcredits</li> </ul>	<ul style="list-style-type: none"> <li>▪ Have a social purpose in micro-crediting. Can be used to support agricultural sector.</li> <li>▪ Aim for a short turnaround on loan applications (Opportunity Microcredit aims for a 7 day response).</li> </ul>
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**FURTHER INFORMATION**

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