Bulgarian Ministry of Finance

Ex-ante Assessment of Financial Instruments for the OP Human Resources Development

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Executive Summary

Context and objective of the study

Financial Instruments (FIs) are expected to play a much stronger role in the use of ESI Funds in the programming period 2014-2020. Besides the advantages of recycling funds over the long term, Financial Instruments will help mobilise additional private co-investments in order to address market failures in line with the Europe 2020 Strategy and Cohesion Policy priorities

The ***objective*** of the present study is to perform an ex-ante assessment of Financial instruments (FIs) for Operational Programme "Human Resources Development" for the programming period 2014-2020. The scope of the study is defined in an agreement between PricewaterhouseCoopers Bulgaria EOOD (PwC) and the Ministry of Finance of the Republic of Bulgaria (MoF) from 21 May 2014.

This assessment consists of an analysis of the potential for use of Financial Instruments in Bulgaria during the next programming period. It focuses on determining which FIs can facilitate and amplify the impact of the ESI Funds and to formulate evidence-based recommendations for the implementation of such instruments. As required by the Common Provision Regulation (CPR, Article 37), this ex-ante assessment aims at improving the quality of the design of the new operational programme, by providing guidelines for an investment strategy for the implementation of FIs. The ultimate goal of an ex-ante assessment according to article 37 is to determine the best use of Financial Instruments based on an analysis of the market failures and to ensure that it will contribute to the achievement of the programme's objectives under the Common Strategic Framework (CSF).

The ***structure of the report*** is based on ex-ante assessment methodology for financial instruments in the 2014-2020 programming period, developed by PwC for the European Commission and the EIB Group for and modified to address the country specifics of the Bulgarian market. At the very beginning of the study the used methodology is outlined in greater detail. The study then proceeds:

- Firstly, with an overview of the policy context, relevant to the implementation of FIs, the consistency between the Partnership Agreement, the Thematic Objectives chosen and the Priority Axes developed by the OP Human Resources Development, as well as the applicable regulatory framework.
- Secondly, it describes the market environment highlighting relevant indicators.
- Thirdly, it lists the existing Financial Instruments and grants, used during the last programming period (2007-2013), as well as elaborates on the lessons learned from their use.
- Then the market failures are identified based on qualitative and where possible quantitative analysis of the supply and demand for financing, in order to point out a financing gap that could be bridged through the use of FIs
- The following section provides an analysis of the added value from the use of FIs, including potential co-financing and investors and the expected leverage effect.
- The afterward section offers guidelines for an investment strategy for the use of FIs along with potential management structures for their implementation.
- The last section details the action plan for the implementation, monitoring and evaluation of the FIs.

Methodology

In April 2014, the European Commission issued the ex-ante methodological guidelines[1] that provide a template for the preparation of such studies. The present report follows the specific methodology. However, it has to be

[1] European Commission, 2014. "Ex-ante assessment methodology for the use of financial instruments".

noted that the methodology is used only as an overall framework and road map in order to better take into consideration the country specifics.

During the research conducted, it was revealed that the collection of information was not always evident. On the demand side, the main target groups defined in the report consist of social groups that are difficult to quantify due to the fact that they are not always registered like minority groups, or are underdeveloped like the social economy sector. Respectively, on the supply side, the lack of suitable institutions for the use of FIs in the fields under consideration, limit the availability of quantifiable information.

More specifically:

- On the demand side, quantifications have been provided using several methodologies to compute some figures in order to illustrate the size of demand.
- On the supply side, the lack of specialized institutions that use FIs in the field of social economy, social inclusion and training, limit the availability of data.
- Regarding the gaps, the present report describes the existing gaps mostly based on qualitative information since it is not possible to provide consistent quantitative assessment of the demand and supply sides.

Nevertheless, when possible, quantitative information has be provided to better illustrate these gaps.
The main tools used to gather information and data needed includes literature review, extensive desk research and interviews with relevant stakeholders such as representatives of commercial banks, public financial institutions, international financial institutions, as well as representatives of associations representing Bulgarian actors and other organizations in relation to the target groups defined by the HRD OP. This approach has enabled the sourcing of qualitative and quantitative indicators that are later on used to analyse the context and the situation of financing needs in Bulgaria.
More details on the methodology used are presented in section 2 and when needed further developed in the respective section.

Analysis

Policy overview for the 2014-2020 period

The report provides a detailed policy overview (Section 3), where it presents a summary of the policy context relevant to the implementation of future Financial Instruments for the 2014-2020 programming period. The content of the Partnership Agreement is firstly presented along with the links between national policy and the Thematic Objectives chosen by the MA, and ultimately how this will impact the Operational Programme for 'Human Resources Development'.
In that context four strategic priorities are outlined within the Partnership Agreement between Bulgaria and the European Commission as to the use of the European Structural and Investment Funds. These priority areas are:

- Education, employment, social inclusion and healthcare for uniting growth;
- Scientific research innovations, investments in intelligent growth;
- Connectivity and green economy for sustainable growth; and
- Good governance and access to qualitative administrative services.

Even though, Financial Instruments were not used during 2007-2013 programming period for the 2014-2020 programming period the Managing Authority has identified a need and an opportunity to use them and pointed out Investment Priorities (IPs) were they plan to use FIs. In addition to the IPs that were defined by the MA as areas where FIs can be implemented, the analysis has shown that there are also other IPs where the use of FIs would be relevant and these areas are highlighted in Section 3.3 Financial Instruments in the Operational Programme for 2014-2020 Table 2.

Based on the IPs that may be supported by the use of Financial Instruments, target groups of stakeholders are defined, namely:

- Socially excluded people and people at risk of poverty willing to create a business,
- Employees at risk of unemployment working in newly created enterprises and social enterprises
- People in need of training to create their company or to remain in their current job position
- People starting or developing a cooperative and/or a social enterprise
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Then an assessment of the compatibility between the OP objectives with the ex-ante conditionalities is conducted in order to identify their potential impact on the FI implementation. Based on the performed assessment, there are two conditionalities that are not fully fulfilled at the time of this report, but there are currently no identified issues or otherwise significant risks in this respect. Bulgaria has to assess the fulfilment not later than December 2016 and report their completion in the Annual Implementation Report in 2017.
The section concludes with a summary of the important regulatory considerations that will have to be taken into account in the implementation of FIs to support the HRD OP, such as state aid implication.

Market environment

In order to better understand and assess the county specifics, the report presents detailed information on the market environment in Bulgaria, including analysis of the Bulgarian macroeconomic and political context, the demographics and labour force, the Small and medium enterprises (SMEs) distribution by region and the social economy perspective as well as indicators in relation to the target groups identified by the Managing Authority (MA) under the HRD OP.

The analysis of the market environment in Bulgaria has shown it to be somehow resilient to the crisis and the recovery process, following the 2009 downturn, has been slow but stable. The reform process has been mostly based of fiscal consolidation but several other factors still need to be addressed and improved in order for the Bulgarian economy to gain in competitiveness. The political instability is still a destabilizing factor for the economy also affecting the implementation of social policies.

In summarising the present chapter the following points are highlighted:

- Unemployment rates are persistently high in Bulgaria and persistent. This implies a high need to create new employment opportunities through business creation and entrepreneurship
- The labour cost in Bulgaria is competitive, however skills still need to be improved to link higher education with the actual needs of the business
- Employment rates in Bulgaria are relatively low, thus implying that high rates of people are excluded from employment due to lack of skills that need to be addressed.
- People with disabilities have difficulties accessing the job market as well as minority groups
- Social economy in Bulgaria is underdeveloped and needs to be supported

Existing Financial Instruments and lessons learned

Overall, from EU perspective, a strong momentum for the use of FIs was generated in the last programming period (increased absorption, a number of units set up in 2012).

The use of FIs has been increasingly promoted in the EU over the last 10 years. European institutions such as the European Investment Fund (EIF) and the European Investment Bank (EIB) designed specific policies such as JEREMIE and JESSICA in order to provide simplified procedures and know-how, for Member States to use their allocated European funds into FIs. Other international organisations such as the European Bank for Reconstruction and Development (EBRD) also implemented FIs to support the financing of specific policy areas.

During the last programming period no FIs have been used under HRD OP. Nevertheless, this section of the report lists the grants provided and the existing FIs that could be relevant as the target groups are similar under the two programming periods and the programmes launched are designed to answer the needs of self-entrepreneurs, socially excluded people and the development of the social economy. It has to be noted however that the absorption of funds allocated to grant schemes in the last programming period was low and several deficiencies were observed in the implementation process.

The main lessons learned from the 2007-2013 programming period have been split into 2 groups:

- Lessons learned from the use of grants
    - The design, evaluation, selection and control procedures of grant programmes involves a large and multi-level group of stakeholders causing confusion and delays in the implementation;
    - The stakeholders are national authorities and state-owned companies with limited knowledge of the market;
    - The discussion on the involvement of the private sector in the evaluation procedures is currently not taking place;
    - The private sector is involved only through private consultants supporting potential beneficiaries (mostly SMEs) in the preparation of the application procedure. Beneficiaries (mainly SMEs) have difficulties securing financing for the non-subsidised part of their business plan.
- Lessons learned from the use of FIs:
    - The microfinance segment and especially the existing microfinance institutions were not sufficiently supported by public interventions.
    - Social inclusion FIs were not implemented.
    - In the last programming period FIs did not focus on improving people skills and mentoring.
    - Financial intermediaries, capable of implementing FIs are only limited to banks and some MFIs but more specialized institutions and funds with social objectives are missing.
    - Existing specialized institutions such as Microfinance institutions operate more like commercial banks.

Analysis of market failures, suboptimal investment situations and investments needs

The ***analysis of the supply*** is constrained by the considerable amount of uncertainty in the Bulgarian financial sector. Interviews conducted with relevant stakeholders, including those from the commercial banking sector, revealed that these stakeholders were reluctant to provide figures for the current provision of financing and the anticipated supply of financing for the coming years.

Nevertheless, the supply analysis has identified two main types of financial institutions as potential suppliers of financing for these target groups: (1) commercial banks and (2) Microfinance Institutions (MFIs).

A specific focus has been made on the provision of microcredit from these two financial institutions to the identified final recipients in the HRD OP.
Microcredit, defined as loans up to EUR 25,000 addresses two populations:

- Micro-enterprises, defined as enterprises employing up to 9 employees;
- Disadvantaged people (unemployed or inactive people, receiving social assistance, immigrants, marginalised people and people with special needs) who wish to become self-employed but do not have access to traditional banking services.

Over the past few years, the provision of micro-loans by commercial banks has remained stable, representing an annual supply of about EUR 2.1bn. Detailed figures from the banking sector to the final recipient or target groups identified in the HRD OP were not available.

However, commercial banks consider that financing socially excluded individuals are not part of their mission. They focus on existing micro-enterprises with at least 12 months of business history. Indeed, the difficulties encountered by the micro-enterprises, the need to provide collaterals and the lack of vision of the banks on the future cash-flows lead the banks to reject the loan request, putting the work force at risk of unemployment.

In the light of the risks perceived by the commercial banks that prevent them from providing loans to the target groups identified in the HRD OP for 2014-2020, a second source of funding needs to be considered: microfinance products provided by microfinance Institutions in Bulgaria.

Microfinance Institutions in Bulgaria refer to institutions which are officially licensed to provide very small loans of up to EUR 25,000. They include two types of micro-loans for two kinds of clients:

- Personal micro-loans provided to support unemployed people in their job's hunt.
- Business micro-loans provided to self-employed and micro-enterprises having difficulties to access financing from commercial banks.

The desk top research[2] provides us with information on the Micro Finance Institutions (MFIs) market in Bulgaria in 2012 (data for 2013 are not yet available). In addition to the MFIs, Progress microfinance initiative supported by the EIF makes EU funds available for microfinance to support socially excluded people and help business creation.

The overall supply analysis of financing shows two types of products:

- Micro-loans provided by commercial banks, representing annually at most **EUR 2.1m**
- Microfinance products from Microfinance Institutions, representing annually between **EUR 9.8m and 10.5m**; and Microfinance products for about **EUR 25.5m** available through the Progress initiative.

The ***analysis of the demand*** is based on the quantification of potential need for financing from the target groups mentioned above (section Policy overview) which have been identified as final recipients:

- Individuals – socially excluded persons or individuals at risk of poverty
- Entities – micro-enterprises

For each of the final recipients, this section details the methodology how to calculate the demand related to the final recipients.

The below table[3] summarises the indicative estimation of potential demand but it should be acknowledge that there is an overlapping between the different sets of final recipients as one individual might be part of two or more groups. This is why a total of potential demand for financing has not been computed.

[2] Mix Market MFI Statistics – Microfinance Institutions market in Bulgaria 2012

[3] Detailed calculation are provided under section 6.1.2 to 6.1.7 in the report

	Final recipient	Estimated amount (EUR)
Socially excluded persons or individuals at risk of poverty	Individuals needing financing for a training in view of creating a company or obtaining a new job	11,711,700
	Individuals needing financing to create a company	294,697,603
	Individuals needing financing to find a job	68,208,800
Enterprises	Micro-enterprises needing financing to finance a training for their employees	74,173,982
	Training centres	12,653,100
	Social enterprises	8,834,400

Through the analysis of the difference between supply and demand it is possible to provide an indicative comparison between the major quantitative aspects of supply and demand showing that in the Bulgarian market demand outweighs supply by far.

The identified gap is to be considered as only indicative since:

- It considers all micro-loans provided by commercial banks as used or usable by micro-enterprises;
- All amounts are indicated as annual demand or annual supply;
- Demand for financing is based on a macro-economic background that may evolve in time;
- Demand for financing for entrepreneurs and micro-enterprises may be expressed today but not materialise in the future.

Added value of the Financial Instruments

The study continues with analysis of the added value that FIs could bring in comparison with grants. Co-financing, leverage effect and revolving mechanism reduce the importance of grant-based support and increase the efficiency of the delivery of funds thanks to private expertise and local networks as well as the administrative burden born by the final recipients and other important socio-economic benefit such as promotion of entrepreneur spirit, job creation/reduction of unemployment, job flexibility, employability of job seekers and support to the social economy.

Five OPs are co-financed by ERDF funding and are complementary to the HRD OP. Synergies and cooperation should be put in place especially with Innovation and Competitiveness OP in the microfinance area.

With regard to the leverage effect, since there is to date no Financial Instrument in place, the expected leverage may be difficult to anticipate. However, experience with guarantee funds in Bulgaria and experience with micro-lending supported by Financial Instruments in other Member States may provide ranges of leverage to be expected: ***1:1.4 to 1:5 for the micro-guarantee fund and 1:1.5 to 1:9 for the micro-loan scheme.***

Proposal of structures and guidelines for investment strategies of the FIs

According to the identified market failures and sub-optimal investment situations and the target groups covering two types of beneficiaries namely individuals who have financing needs to be trained, access the labour market or create their own company; and Enterprises facing temporary difficulties and wiling to increase the employability of their staff through training or to sustain their business, or training centres and social enterprises having bother working capital and investment needs. On this basis, the proposed Financial instruments best suited are:

- Micro-guarantee instrument
- Personal micro-loan instrument
- Business micro-loan instrument

The suggested amount to invest as a pilot initiative for the use of FIs is EUR 20m. Half of it is expected to be devoted to micro-guarantees and the other half equally split between the 2 other FIs.
Characteristics of each FIs are detailed in section 8.2 The proposed Financial Instruments including objectives, scope of intervention, target groups, expected advantages, allocation of the initial amount, expected leverage effect and thus budget available, socio-economic benefits along with potential partners and stakeholders to be involved in the process.

In respect to the management and governance structure there are 3 possible options:

- Option 1: Structuring FIs without a Fund of Funds
- Option 2: Structuring FIs with a Fund of Funds
- Option 3: The MA providing FIs support directly to final recipients

Taking into consideration the elements analysed throughout the present study, two structures are proposed:

- For the **Proposed Structure 1**, the leverage of the future ESIF Fund-of-Funds[4] to be developed under the Innovation and Competitiveness Operational Programme (IC OP). This is close to the Option 2 and leverages the experience acquired by the JEREMIE Holding Fund over the 2007-2013 programming period; or
- For the **Proposed Structure 2**, the leverage of the National Guarantee Fund for the micro-guarantee instrument on the one hand and the set-up of personal micro-loan and business micro-loan instruments via commercial banks and microfinance Instruments on the other hand. In this structure, no Fund-of-Funds would be set up. This is close to the Option 1 detailed previously and leverages the experience acquired by the National Guarantee Fund as well as the experience of commercial banks and MFIs with previous Financial Instruments, which may have not been related to micro-loans.

Action plan for the implementation, monitoring and evaluation of the Financial Instruments

First the MA has to validate the FIs by ensuring that they are consistent with the strategy of the Cohesion Policy and the HRD OP. Then it has to launch an awareness campaign in order for the local and regional actors to be familiar with the integrated approach of projects/return on investment/recycle of the funds.
Once the FIs have been validated, if the MA goes for the proposed structure with a Fund of Funds, it needs to be created and the governing body sets up.
The investment strategy will be then designed and should include:

- Target groups and territories;
- Investment products offered;
- Estimates of the amounts to be invested in the fund;
- Limitations of investments and investment controls;
- General criteria for the selection and evaluation of funds (e.g., types of appropriate structure for managing a fund);
- Provisions relating to the recycling of funds.

[4] The name of the Fund of Funds has not been defined yet. That is why a generic name has been preferred to define it.

Then the selection of Financial Intermediaries will take place and the operations will be launched based on the eligibility criteria and procedures of evaluation of the projects defined by the financial intermediaries.

The monitoring and evaluation process will follow the methodology developed by PwC for the European Commission and the EIB Group for the 2014-2020 programming period.

Contents

1. Introduction

The present report consists of an ex-ante assessment for the use of Financial Instruments (FIs) regarding the Operational Programme (OP) Human Resources Development for the programming period 2014-2020. This ex-ante assessment is drafted at a crucial period in time for the preparation of the transition to the new programming period (2014-2020). As required by the Common Provision Regulation (CPR, Article 37), this ex ante assessment aims at improving the quality of the design of the new OP through a clearly defined investment strategy for the use of FIs. In the new programming period, financial instruments will play an important role in achieving the Cohesion Policy objectives, and the present report will contribute toward that direction. The main target of this assessment is to analyse in detail the potential development of FIs supporting HR development in Bulgaria and the establishment and implementation of relevant financial engineering managing structures.

1.1. Background of the study

Since Bulgaria's EU accession in 2007, the country has been provided access to EU funds that are supporting the country's convergence efforts. For the 2007-2013 programming period, Bulgaria had been allocated EUR 6.853bn in total. More specifically, EUR 6.674bn were allocated under the Convergence objective and EUR 179m under the European Territorial Cooperation objective (EC, 2013). The National Strategic Reference Framework 2007-2013 (NSRF), adopted in March 2007, provided guidelines for the use of EU Structural Funds through seven Operational Programmes (OPs): OP Competitiveness, OP Transport, OP Environment, OP Regional Development, OP Technical Assistance, OP Human Resources Development and OP Administrative Capacity. Concerning FIs, Bulgaria has been implementing several initiatives in recent years. Instruments were designed and implemented through different schemes targeting energy efficiency, SME financing, housing renovation and urban development.

Specifically concerning HR development, the European Commission approved back in 2007 an "HR Development" Operational Programme covering specific thematic objectives. The Programme had a total budget of around EUR 1,2bn. In the new programming period the OP HR Development has a reduced budget of EUR 1,092 bn, however its importance in the development of policies related to human capital, training and social inclusion issues remains crucial. In this context, the use of FIs will also be reinforced in order to provide funds of a revolving nature, with the ability to leverage private funds and create stronger added value at regional and national level.

The 2014-2020 programming period provide a more solid legal and operational framework with clear and simplified rules concerning key implementation matters such as the financial management of EU contributions or the combination of financial instruments with grants. Subject to feasibility, financial instruments can be applied to the full bandwidth of policy objectives, in order to support investments in projects that demonstrate appropriate repayment capacity but are in situations of market imperfections.

In order to help define the use of FIs in the new programming period under the OP HR Development, the present report will follow the content required by Article 37 of the CPR including a detailed presentation of the market environment in Bulgaria, a detailed description of existing FIs and lessons learned from their implementation, existing market failures deriving from the analysis of supply and demand, an analysis of co-financing, leveraging and added value from the use of FIs, and others. The target of the study is to provide guidelines for an investment strategy for the use of FIs and potential management structures for these proposed FIs.

1.2. Objectives and scope of the study

The Managing Authority for the OP "HR Development" is seeking support with respect to the implementation of financial instruments and their management in order to better plan the financing of these instruments as well as to define its investment strategy for the period 2014-2020.

According to EU regulation 1303/2013, article 37 point 2, an ex-ante assessment can be considered as a feasibility study to help the Managing Authority to define and set up one or several financial instruments, to determine the best use of Financial Instruments on the basis of market failures, to ensure that they will contribute to the achievement of the OP's objectives and to facilitate the implementation by mitigating the potential risks.

The ultimate goal of an ex-ante assessment according to article 37 is to determine the best use of financial instruments on the basis of market failures and ensure that it will contribute to the achievement of program objectives from funds under the Common Strategic Framework (CSF). In this context, the main objectives of the present report are:

- To capitalised on lessons learned in the course of the 2007-2013 programming period by drawing conclusions from the actual application of FEIs, as well as from previous preliminary evaluations executed in Bulgaria. A description of how these conclusions will reflect on future FEIs in the next programming period;
- To identify the needs for the application of financial instruments in Bulgaria during the 2014-2020 programming period;
- To define the Institutional framework for the implementation of FIs in Bulgaria during the 2014-2020 programming period.

Within each of the above mentioned objectives, some sub-activities aim at fulfilling the key elements required by Article 37 (2) of the CPR such as:

- Identification of market failures (inefficiencies) and/or suboptimal investment situations, finance shortages, or investment needs in policy making and thematic objectives/investment areas to be reviewed in order for them to contribute to the strategy or results of relevant OPs, and for the needs to be satisfied through FIs;
- Analysis of the possible forms of support provided through financial instruments;
- Relevance of state aid rules, proportionality of planned intervention and measures to minimise impact of market distortions;
- Evaluation of options for combining FIs and other forms of support such level of private investment/co-financing;
- Suggestion of investment strategy;
- Listing of measurement indicators for the achieved objectives and results.

Following several discussions with the MA and a constructive workshop held on July 11, 2014, specific policy areas relevant to the present analysis were defined. It is the intention of the MA to promote the use of FIs within these policy areas, thus increasing their importance also for the present report to consider. These policy areas are:

- Social inclusion for unemployed people and people on the verge of poverty
- Training and life-long learning
- Social economy

1.3. Structure of the report

The structure of the report will be based on the ex-ante assessment methodology for Financial Instruments developed by PwC for the European Commission and the EIB Group for the 2014-2020 programming period. However, some adjustments will be made to better reflect the needs of the MA and the market environment in the country.

The analysis will be organised as follows:

- In Chapter 2, the methodology used to provide the analysis in this report will be presented. This will include the tools used to collect information and data and the method used to provide the analysis.
- In Chapter 3, a detailed overview of the relevant regulatory framework will be provided in order to specify the overall framework affecting the use of FIs. Moreover a policy overview defined by important policy documents such as the partnership agreement and the new OP will be provided in order to allow the reader a transition from the general policy orientation to the specific policy priorities under the scope of HR Development and the policy priorities relevant to the use of FIs as defined by the MA.
- In Chapter 4, a detailed presentation of the existing market environment will be provided in order to assess the extent to which these policy priorities and the overall use of FIs could be positively or negatively affected.
- In Chapter 5, a presentation of existing FIs and an evaluation of their implementation will be provided to highlight lessons learned from this experience in Bulgaria
- In Chapter 6, the report will present the market failures that exist in the country relevant to the use of FIs. These market failures will be defined as a result of the analysis of supply and demand for financing relevant to the specified policy objectives in order to identify specific financing gap that could be bridged through the use of FIs
- In Chapter 7, an analysis of the added value from the use of FIs in the specific policy areas will also be provided through the use of specific proposed indicators. This analysis will include the description of potential co-financing and the potential leveraging effect by the use of financial intermediaries.
- In Chapter 8, guidelines for an investment strategy for the use of FIs will be provided along with potential management structures for these FIs.
- In Chapter 9, recommendations for a monitoring mechanism for the above defined FIs will be presented.
- In Chapter 10, the general conclusion of the present report will be presented.

2. Methodology of the study

The goal of this chapter is to present shortly the main methodological techniques used throughout the study. The present study will use different tools and techniques in order to gather information and provide an analysis of market failures in order to quantify, where possible, the market gaps, and propose a suitable investment strategy. More detailed methodological subsections will also be included in later sections of the report.

2.1. Rationale behind the methodology

For the 2014-2020 programming period, European Structural and Investment Funds (ESIF) play a decisive role in reaching the objectives set up in the Europe 2020 strategy for a smart, sustainable and inclusive growth, while promoting harmonious development of the Union and reducing regional disparities. However, fiscal limitations and the scarcity of public funds in Europe oblige governments to use their national budget and the EU contribution in efficient and optimal ways in order to implement their national strategies. In this context, the use of FIs will play a crucial role in achieving these objectives.

In April 2014, the European Commission issued the ex-ante methodological guidelines[5] that provide a template for the preparation of such studies. The present report follows the specific methodology. However, it has to be noted that this methodology is to be used as a road map in order to achieve the expected result. The specifics of each country have to be taken into account. The present report takes into account the market conditions of Bulgaria and the experience with FIs in the country. During the research conducted, it was revealed that the collection of information was not always evident. On the demand side, the main target groups that are going to be defined later on in the report consist of social groups that are difficult to quantify due to the fact that they are not always registered like minority groups, or are underdeveloped like the social economy sector. Respectively, on the supply side, the lack of suitable institutions for the use of FIs in the fields under consideration, limit the availability of quantifiable information. More specifically:

- On the demand side, quantifications will be provided using several methodologies to compute some figures in order to illustrate the size of demand. These methodologies will be described in the relevant sections. The data to be used will be extracted by existing reports and the desk research conducted in order to gather data on unemployed people, people on the verge of poverty, potential entrepreneurs, training centres and others.
- On the supply side, the lack of specialized institutions that use FIs in the field of social economy, social inclusion and training, limit the availability of data. The goal of the present report is to identify the existing supply of financing to the target groups identified, mainly by the banking sector and existing Microfinance institutions. In order to paint the picture of supply more accurately, a description of the existing FIs will be provided along with a description of the relevant grant schemes in place which play an important role in the supply of financing. Normally, the supply side analysis should only contain the supply available in the market without public intervention schemes. However, due to the scarcity of this supply, the market intervention schemes will be used in order to better describe the supply side.
- Regarding the gaps, the present report will describe the existing gaps mostly based on qualitative information since it is not possible to provide consistent quantitative information to measure the demand and supply sides. As mentioned above, where possible, quantitative information will be provided where possible to better illustrate these gaps.

[5] European Commission, 2014. “Ex-ante assessment methodology for the use of financial instruments”.

2.2. Tools used to gather data and information

The main tools used to gather the information needed included the literature review and extended desk research, and the stakeholder interviews.

2.2.1. Literature review-desk research

One of the main elements supporting the analysis is in depth literature review. The literature review aims to gather most of the existing information on the current situation of public initiatives and possible projects to be financed in Bulgaria in addition to information and studies from other EU member states to identify and analyse:

- Existing indicators and information on individual initiatives and incentives to promote self-employment (on both the demand and supply sides) in Bulgaria;
- Information on the economic and political environment of Bulgaria;
- Information on the regulatory environment for state aid and FIs in Bulgaria;
- Insights of previous period on the support of reducing unemployment, fostering social inclusion of disadvantaged groups and minorities and enhancing lifelong learning and vocational training process to give good level of employability to answer to the needs of the business;
- Insights on the policy priorities of the Managing Authority for the next programming period 2014-2020.

The documentation used for the literature review is indicated in Annex 6. The literature review enabled the sourcing of qualitative and quantitative indicators that were used to analyse the context and situation of financing public initiatives in Bulgaria, the sources of which are also presented in Annex 6.

2.2.2. Stakeholder interviews

In order to complement the data collection and the literature review, interviews with stakeholders involved in public initiatives, financing and investments were carried out. When selecting the relevant stakeholders, different groups were defined so as to cover the whole scope of the preparing and financing projects in Bulgaria. Three groups of stakeholders were identified:

- Supply side representatives;
- Demand side representatives; and
- Government officials.

Specifically, this includes representatives of finance suppliers, such as commercial banks, public financial institutions, international financial institutions and fund managers, as well as representatives of associations representing Bulgarian actors and other public initiatives organizations. In total, 20 face-to-face interviews and close to 3 telephone interviews were conducted (list in Annex 2 with the interview guides in Annex 3).

2.3. Data analysis

All the data and information collected through the data collection, the literature review and the interviews with stakeholders have been used and assessed in order to validate the study's findings. The methodology used is based on the principles of triangulation which ensures that all findings presented in the report are supported, to the extent possible, by evidence from these three data sources. Information obtained through these data sources has been compared in order to identify trends or contradictions in the findings.

3. Policy overview for the 2014-2020 period

This section will provide a summary of the policy context relevant to the implementation of future Financial Instruments for the 2014-2020 programming period. The content of the Partnership Agreement will first be presented and the links between national policy[6] and the Thematic Objectives developed by the European Commission for the Cohesion Policy (CP) over 2014-2020, and ultimately how this will impact on the Operational Programme Human Resources Development. The Partnership Agreement being of particular relevance given that it sets out the overall policy as to the use of European Structural and Investment Funds (ESI Funds). It is presented in Section 3.1. With the overall policy context set out, Section 3.2 will provide a detailed overview of the Operational Programme, its different Priority Axes, their Specific Objectives and Investment Priorities. In addition, a breakdown of the anticipated budgetary breakdown between each of these Priority Axes will be provided. Section 3.3 will provide an overview of the FIs that are being envisaged by the MA under the OP and Section 3.4 will assess the compatibility between the OP objectives with the ex-ante conditionalities. Finally, Section 3.5 will provide a summary of the important regulatory considerations that will have to be taken into account in the implementation of FIs to support the OP Human Resources Development.

3.1. The Partnership Agreement: objectives for Human Resource Development and the planned use of Financial Instruments

The main strategic documents outlining the development policies of Bulgaria for the coming years, including the vision and the specific development objectives of the country, are the National Development Programme of Bulgaria 2020, the National Reform Programme, the National Strategy for Regional Development 2012-2022 and the National Spatial Development Concept 2013-2025. These serve as the basis for the development of programming documents for the purposes of the access to specific financial resources. Within these documents, eight priorities for national development policy were identified:

1. Improving access to and quality of education and training and quality characteristics of workforce;
2. Reducing poverty and promoting social inclusion;
3. Achieving sustainable integrated regional development and using local potential;
4. Development of the agricultural sector to ensure food safety and production of products with high added value through sustainable management of natural resources;
5. Support for innovation and investment activities to increase the competitiveness of the economy;
6. Strengthening the institutional environment to achieve higher efficiency of public services for the citizens and business;
7. Energy security and increasing resource efficiency; and
8. Improving transport connectivity and access to markets.

The Partnership Agreement is designed to demonstrate an alignment between the aforementioned national development policies with EU policy so as to ensure that ESI Funds will be used in line appropriately. As such, the priority policy areas enshrined in the Partnership Agreement are in line with:

- The EU Thematic Objectives development for the Cohesion Policy for the 2014-2020 programming period;

[6] By national policy, it is meant the different strategies, reports and policies developed by the national government and mentioned in the Partnership Agreement to demonstrate consistency and compliance with the Europe 2020 Strategy.

- The objectives of the Europe 2020 strategy; and
- The Country Specific Recommendations of the Council.

Four strategic priorities are outlined within the Partnership Agreement between Bulgaria and the European Commission as to the use of the European Structural and Investment Funds. These priority areas are:

- Education, employment, social inclusion and healthcare for uniting growth;
- Scientific research innovations, investments in intelligent growth;
- Connectivity and green economy for sustainable growth; and
- Good governance and access to qualitative administrative services.

Figure 1 demonstrates the alignment of the four strategic priorities as set out in the Partnership Agreement with national policy, and how these tie in with the European Thematic Objectives for the CP over the 2014-2020 programming period. These elements are directly related to the development of the OP Human Resources Development elaborated by the Managing Authority for 2014-2020.

Figure 1: Links between the priorities of the national policy, the EU 2020 Strategy and TO for Cohesion Policy over the 2014-2020 programming period

	8 Priorities of the national policy
1	Improving access to and quality of education and training and quality characteristics of workforce;
2	Reducing poverty and promoting social inclusion;
3	Achieving sustainable integrated regional development and using local potential;
4	Development of the agricultural sector to ensure food safety and production of products with high added value through sustainable management of natural resources;
5	Support for innovation and investment activities to increase the competitiveness of the economy;
6	Strengthening the institutional environment to achieve higher efficiency of public services for the citizens and business;
7	Energy security and increasing resource efficiency;
8	Improving transport connectivity and access to markets.

After summarizing the differences, the needs for development and the potential for growth in Bulgaria, 4 priorities for financing were identified.

		4 strategically complementary priorities for financing	**Main challenges**	**Thematic Objective**
following the directions of the EU 2020 strategy for inclusive, intelligent and sustainable growth	1	***INCLUSIVE GROWTH*** Education Employment Social inclusion Social health	Insufficient number of employed (between 24 and 60 years old) Not enough economic activity of the population High number of employed with high school and lower education, no professional qualification Unsatisfying level of the educational system Low share of population with a university degree Bad health-demographic characteristics, health inequalities and ineffective health sector One of the highest dead rates First place in Europe of poverty Depopulation of big territories in the country	***(8) promoting employment and supporting labor mobility;*** ***(9) promoting social inclusion and combating poverty;*** ***(10) investing in education, skills and lifelong learning;*** ***(11) enhancing institutional capacity and an efficient public administration.***
	2	***INTELLIGENT GROWTH*** Scientifically research Innovation Investment	Low labor productivity Low share of investment in R&D Bad interaction in the knowledge triangle Low level of innovation Low technology sectors with low value added Low level of distribution of high speed broadband internet Low share of households with high speed broadband internet Low level of effectiveness of the scientific sector	*(1) strengthening research, technological development and innovation;* *(2) enhancing access to, and use and quality of, information and communication technologies;* *(3) enhancing the competitiveness of small and medium-sized enterprises, the agricultural sector (for the EAFRD) and the fisheries and aquaculture sector (for the EMFF);*
	3	***SUSTAINABLE GROWTH*** Coherence Green economy	Inefficient use of the resources and energy Inefficient application of the EU legal frame work on the water, atmosphere air and the waste Inefficient systems for prevention, management and addressing the consequences from risks Limited connectivity (infrastructure) Limited freight activity	*(4) supporting the shift towards a low-carbon economy in all sectors;* *(5) promoting climate change adaptation, risk prevention and management;* *(6) protecting the environment and promoting resource efficiency;* *(7) promoting sustainable transport and removing bottlenecks in key network infrastructures;*
horizontal nature	4	Good governance and access to administrative services of good quality	Not finalized modernization of the administration and reform in the public administration Insufficient capacity for planning and realization of projects in the ICT Unfinished infrastructure for the electronic management and electronic social service Unfinished reform in the judiciary system	*(11) enhancing institutional capacity and an efficient public administra*

Related to OP Human Resources Development

Source: Partnership Agreement between Bulgaria and the European Commission, July 2014.

In that context, the Partnership Agreement has also identified socio-economic challenges that the OP Human Resources Development aims to address, along with other OPs developed by other MAs for the 2014-2020 programming period:

- Increase the number of employed people (between 24 and 60 years old);
- Stimulate the economic activity of the population;
- Stimulate life-long learning and provide motives for people to seek professional qualifications;
- Improve the educational system;
- Increase the share of the population with a university degree;
- Reduce inequalities among the population in terms of health services and improve the health sector in the country;
- Address the high rate of people at risk of poverty and social exclusion; and

These challenges, along with the 8 priorities of the national policy, the objectives of the Europe 2020 Strategy focusing on inclusive growth and four of the eleven Thematic Objectives defined by the European Commission for the 2014-2020 programming period supported the development of the Operational Programme Human Resources Development.

3.2. Priorities set in Operational Programme Human Resource Development" in Bulgaria

The Operational Programme Human Resources Development is structured around three main pillars that were based on the needs and challenges of Bulgaria outlined in the Partnership Agreement. These pillars are:

- Achieving higher and better quality employment;
- Reducing poverty and promoting social inclusion; and
- Modernisation of public policies.

In order to address these three pillars, five Priority Axes (PA) were defined in the Operational Programme. For each of these five Priority Axes, specific Investment Priorities (IP) have also been defined and budgets have been set. Support from the European Union is expected to originate from the European Social Fund (ESF) and the Youth Employment Initiative (YEI)[7]. During the 2007-2013 programming period, the OP Human Resources Development benefitted from an overall budget of EUR 1,2bn[8]. For the new programming period EUR 938.7 m have been allocated from the ESF and EUR 153.6 m consist of the national contribution.

For the programming period 2014-2020, the overall budget is indicated by Priority Axis and Thematic Objectives in the table below. Investment Priorities are also mentioned. Finally, Investment Priorities for which the use of Financial Instruments is considered for the programming period are indicated. The latter are more developed in the following section.

7 See: http://ec.europa.eu/social/main.jsp?catId=89&langId=en&newsId=2095&furtherNews=yes.

8 The budget allocated to the OP Human Resources Development over the 2007-2013 programming period included objectives related to education which are now included in an OP fully devoted to education: the Science and Education for Smart Growth Operational Programme (SESG OP).

Table 1: Planned budget for the OP Human Resources Development for the 2014-2020 programming period[9]

Priority axis (in Euros)	Fund	Thematic objective	EU support	National contribution	Total funding	% of total	Investment Priority	Planned use of FIs
PA 1 - Improving the access to employment and the quality of jobs	ESF	TO 8	375,170,167	66,206,500	441,376,667	*40.41%*	IP 1 Access to employment for job-seekers and inactive people, including the long-term unemployed and people far from the labour market; also through local employment initiatives and support for labour mobility IP 2 Sustainable integration into the labour market of young people in particular those not in employment, education or training, including young people at risk of social exclusion and young people from marginalised communities, including through the implementation of the Youth Guarantee IP 3 Self-employment, entrepreneurship and business creation including innovative micro, small and medium sized enterprises IP 4 Enhancing equal access to lifelong learning for all age groups in formal, non-formal and informal settings, upgrading the knowledge, skills and competences of the workforce, and promoting flexible learning pathways including through career guidance and validation of acquired competences IP 5 Adaptation of workers, enterprises and entrepreneurs to changes	IP 2 IP 3
		TO 10	73,159,318	12,910,468	86,069,786	*7.88%*		
PA 1 - Improving the access to employment and the quality of jobs **Related to youth employment initiatives**	YEI	TO 8	110,377,490	9,739,190	120,116,680	*10.99%*		
PA 2 Reducing poverty and promoting social inclusion	ESF	TO 9	285,963,588	50,464,163	336,427,751	*30.80%*	IP 1 Socio-economic integration of marginalised communities such as Roma IP 2 Active inclusion, including with a view to promoting equal opportunities and active participation, and improving employability IP 3 Enhancing access to affordable, sustainable and high-quality services, including healthcare and social services of general interest IP 4 Promotion social entrepreneurship and vocational integration in social enterprises and the social and solidary economy in order to facilitate access to employment	IP 4

[9] Page 209/242 of OP HRD – table 18c

PA 3 Modernising the labour market, social inclusion and healthcare institutions	ESF	TO 11	37,481,085	6,614,309	44,095,394	*4.04%*	IP Investing in the institutional capacity and efficiency of public administrations and public services at national, regional and local level in order to implement reforms and achieve better regulation and good governance	n/a
PA 4 Transnational Cooperation	ESF	TO 8	10,679,347	562,071	11 241 418	*1.03%*	IP 1: Access to employment for job-seekers and inactive people, including the long-term unemployed and people far from the labour market, also through local employment initiatives and support for labour mobility IP 2: Adaptation of workers, enterprises and entrepreneurs to change IP 3: Socio-economic integration of marginalized communities such as the Roma IP 4: Active inclusion, including with a view to promoting equal opportunities and active participation, and improving employability IP 5: Enhancing access to affordable, sustainable and high-quality services, including health care and social services of general interest IP 6: Promoting social entrepreneurship and vocational integration in social enterprises and the social and solidarity economy in order to facilitate access to employment IP 7: Enhancing equal access to lifelong learning for all age groups in formal, non-formal and informal settings, upgrading the knowledge, skills and competences of the workforce, and promoting flexible learning pathways including through career guidance and validation of acquired competences IP 8: Investment in institutional capacity and in the efficiency of public administrations and public services at the national, regional and local levels with a view to reforms, better regulation and good governance	n/a
		TO 9	5,835,992	307,157	6 143 149	*0.56%*		
		TO 10	1,493,047	78,581	1 571 629	*0.14%*		
		TO 11	764,920	40,259	805,179	*0.07%*		
PA 5 Technical Assistance	ESF	n/a	37,740,361	6,660,064	44,400,425	*4.06%*	n/a	n/a
Total			**938,665,315**	**153,582,762**	**1,092,248,077**	***100%***		

Source: HRD OP, Table 18c: Breakdown of the financial plan by priority axis, fund, category of region and thematic objective.

3.3. Financial Instruments in the Operational Programme for 2014-2020

Financial Instruments were not used during the 2007-2013 programming period. For the 2014-2020 programming period the Managing Authority has identified a need and an opportunity to use FIs. As illustrated in Table 1 above, the use of FIs is expected to be focusing on three Investment Priorities and support the financing of specific target groups. The following paragraphs detail the expected use of FIs for these three IPs.

Within **Priority Axis 1**, two IPs may use FIs:

- **Investment Priority 2**: Sustainable integration into the labour market of young people in particular those not in employment, education or training, including young people at risk of social exclusion and young people from marginalised communities, including through the implementation of the Youth Guarantee.

  The target groups of this IP are economically inactive young people in the age group of 15 to 29 years old; youth and unemployed people up to 29 years of age, who are not enrolled in the educational system and youth registered as job-seekers up to 29 years of age.
- **Investment Priority 3**: Self-employment, entrepreneurship and business creation, including innovative micro, small and medium-sized enterprises.

  The target groups for this IP are people willing to start independent business activity; self-employed people; and workers in micro-enterprises, who have benefited from the Operational Programme Human Resources Development.

Within **Priority Axis 2**, one IP may use FIs:

- **Investment Priority 4**: Promoting social entrepreneurship and vocational integration in social enterprises and the social and solidarity economy in order to facilitate access to employment.

  The target groups for this IP are people with disabilities; disadvantaged people in the labour market and other socially excluded people; representatives of different communities employed in social enterprises, cooperatives and specialised enterprises for people with disabilities; people employed in social entrepreneurship institutions and organisations.

Despite the IPs that were defined by the MA as areas where FIs can be implemented there are also other IPs where the use of FIs would be relevant and these areas are highlighted in the table below.

Table 2: IPs and areas where the use of FIs would be relevant

Priority Axis	Investment priority	Planned use of FIs	Potential use of FIs	Degree of relevance
PA 1 - Improving the access to employment and the quality of jobs	IP 1 Access to employment for job-seekers and inactive people, including the long-term unemployed and people far from the labour market;	Yes	Yes	High
	IP 2 Sustainable integration into the labour market of young people in particular those not in employment, education or training, including young people at risk of social exclusion and young people from marginalised communities;	No	Yes	High
	IP 3 Self-employment, entrepreneurship and business creation including innovative micro, small and medium sized enterprises	Yes	Yes	High
	IP 4 Enhancing equal access to lifelong learning	No	Yes	High

	for all age groups in formal, non-formal and informal settings, upgrading the knowledge, skills and competences of the workforce, and promoting flexible learning pathways including through career guidance and validation of acquired competences			
	IP 5 Adaptation of workers, enterprises and entrepreneurs to changes	No	Yes	High
PA 2 Reducing poverty and promoting social inclusion	IP 1 Socio-economic integration of marginalised communities such as Roma	No	Yes	Medium
	IP 2 Active inclusion, including with a view to promoting equal opportunities and active participation, and improving employability	No	Yes	High
	IP 3 Enhancing access to affordable, sustainable and high-quality services, including healthcare and social services of general interest	No	No	Low
	IP 4 Promotion social entrepreneurship and vocational integration in social enterprises and the social and solidary economy in order to facilitate access to employment	Yes	Yes	High
PA 3 Modernising the labour market, social inclusion and healthcare institutions	IP Investing in the institutional capacity and efficiency of public administrations and public services at national, regional and local level in order to implement reforms and achieve better regulation and good governance	No	No	Low
PA 4 Transnational Cooperation	IP 1: Access to employment for job-seekers and inactive people, including the long-term unemployed and people far from the labour market, also through local employment initiatives and support for labour mobility	Yes	Yes	High
	IP 2: Adaptation of workers, enterprises and entrepreneurs to change	No	Yes	High
	IP 3: Socio-economic integration of marginalized communities such as the Roma	No	Yes	Medium
	IP 4: Active inclusion, including with a view to promoting equal opportunities and active participation, and improving employability	No	Yes	High
	IP 5: Enhancing access to affordable, sustainable and high-quality services, including health care and social services of general interest	No	No	Low
	IP 6: Promoting social entrepreneurship and vocational integration in social enterprises and the social and solidarity economy in order to facilitate access to employment	No	Yes	High
	IP 7: Enhancing equal access to lifelong learning for all age groups in formal, non-formal and informal settings, upgrading the knowledge, skills and competences of the workforce, and promoting flexible learning pathways including through career guidance and validation of acquired competences	No	Yes	High
	IP 8: Investment in institutional capacity and in the efficiency of public administrations and public services at the national, regional and local levels with a view to reforms, better regulation and good governance	No	No	Low
PA 5 Technical assistance	n/a	No	No	n/a

Source: PwC analysis, 2014

Based on the IPs that may be supported by the use of Financial Instruments, various target groups of stakeholders may be defined. These target groups can benefit from the policies developed in the IPs that may use FIs for the 2014-2020 programming period.

- Socially excluded people and people at risk of poverty willing to create a business, including:
  - Young inactive or unemployed people up to 29 years old (PA 1, IP 2);
  - People willing to start a business and be self-employed (PA 1, IP 3);
  - Disadvantaged people, such as people in marginalised communities (PA 2, IP 4);
  - People with disabilities (PA 2, IP 4).
- Employees at risk of unemployment working in newly created enterprises and social enterprises:
  - Newly hired employees in micro-enterprises that will benefit from the HRD OP for 2014-2020 (PA 1, IP 3);
  - Newly hired employees in a social enterprise (PA 2, IP 4);
  - Employees in social enterprises, especially people with disabilities and people at risk of unemployment (PA 2, IP 4).
- People needing training to create their company or to remain in their current job position:
  - Young people under 29 years old not enrolled in the educational system and needing training (PA 1, IP 2);
  - Self-employed people needing training to create or develop their company (PA 1, IP 3);
  - Employees in enterprises needing training to remain in their current job position (PA 1, IP 3);
  - Social entrepreneurs needing training (PA 2, IP 4);
  - Employees working in the social economy sector and needing training (PA 2, IP 4).
- People starting or developing a cooperative and/or a social enterprise.
  - Social entrepreneurs (PA 2, IP 4);

In view of supporting the above listed target groups, various entities may benefit from the Financial Instruments to be developed. These beneficiaries correspond to the legal entities that may benefit from the Financial Instruments in view of supporting the identified target groups. These potential beneficiaries are:

- Business creators;
- People seeking support in order to improve their mobility and have access to employment;
- Companies that are employing people and are seeking to improve the skills of their employees and adapt to change;
- Business owners that are looking to improve their skills and adapt to change
- Vocational training centres; education and training organisation and institutions; and information and professional guidance centres that provide counselling services and training on entrepreneurial, managerial and business skills to the target groups identified and listed above;
- Cooperatives, social companies and specialised enterprises;
- Social-entrepreneurs.

3.4. Compatibility between the OP objectives and ex-ante conditionalities

Before proceeding with the detailed analysis of supply and demand of financing in the following sections, a review of the fulfilment of ex-ante conditions is necessary in order to evaluate the status of necessary prerequisites for the implementation of Financial Instruments.

As already mentioned earlier, the Thematic Objectives selected by the Human Resources Development Operational Programme (HRD OP) for the 2014-2020 programming period are the following:

- TO 8 - promoting sustainable and quality employment and supporting labour mobility;
- TO 9 - promoting social inclusion, combating poverty and any discrimination;
- TO 10 - investing in education, training and vocational training for skills and lifelong learning;
- TO 11 - enhancing institutional capacity of public authorities and stakeholders and efficient public administration.

The newest version of the Partnership agreement shows that the ex-ante conditionality required for the programming period 2014-2020, that refer to the HRD OP are fulfilled.

However there are still ex-ante conditionalities that refer to the European Investment and European Structure Funds, which are still pending[10]. Bulgaria as all Member States has to fulfil the ex-ante conditionality not later than 31 December 2016 and will report on their fulfilment not later than in the annual implementation report of 2017 or the progress report in 2017 in accordance with Article 44 (5).

3.5. Regulatory framework – State Aid implication

This section focuses on the regulation at the national level that is relevant for the implementation of FIs in Bulgaria. It points out the conditions that need to be met in order to implement different types of Financial Instruments and gives insights on the restrictions, under which public funds can be used as source of financing and the specific structure and conditions under which the actual payments are made.

The new developments in the course of the State Aid Modernisation (SAM) undertaken by the European Commission are important and have to be taken into account, when executing the actions under the operational programme. This section aims to clear out difficulties with identification and definition of state aid. Public authorities need to be prepared for the challenges which could arise, when applying the new regulations for de minimis and block exemption, as well as a range of further guidelines also revised based on the lessons learned from the previous programing period.

In the general case, provision of State Aid is prohibited, but there are exemptions of the general prohibition. In this context it is essential for the respective authority to check individual cases for compliance with these regulations. For the next programming period 2014-2020, the EC has revised and drafted a new set of exemption.

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[10] Annex 4 of the Partnership agreement – official version of the approved by the EC on the 7th August 2014

3.5.1. General Block Exemption Regulation

On 17 of June 2014 EC adopted the new General Block Exemption Regulation (GEBR) No 651/2014 (GBER) declaring certain categories of aid compatible with the internal market in application of Articles 107 and 108 of the Treaty which become effective as of 1 July 2014. The block exemption regulation frees categories of state aid, deemed to bring benefits to the society, that outweigh the possible distortions of competition in the Single Market triggered by the public funding, from the requirement of prior notification to the Commission. Consequently, Member States may implement measures which fulfil the conditions of the Regulation without prior Commission scrutiny.

According to the current Bulgarian Regulation for Implementation of the State Aid Law, in order to be considered as block exempt the particular state aid has to receive the positive statement by the Ministry of Finance[11] (i.e. the statement which considers the particular state aid as exempt under General Block Exemption Regulation). The new GBER also sets higher notification thresholds and aid intensities. Some of the thresholds can be found in Annex 1. If the particular state aid threshold exceeds the above limits, the GBER shall not apply and the competent bodies (Ministry of Finance, which has been notified by the administrator of the aid and the required coordination on different levels) shall follow the notification procedure under Art.108, paragraph 3 of the Treaty and shall apply for exemption in front of the European Commission.

The GBER shall apply only to the state aid, which can be considered transparent. The table below presents the financial instruments that should be considered transparent and the conditions that have to be met when implementing them:

Table 3: Financial products and conditions to be met for their implementation

Financial product	Conditions to be met
Loans	The gross grant equivalent has been calculated on the basis of the reference rate prevailing at the time of the grant
Guarantees	• The gross grant equivalent has been calculated on the basis of safe-harbour premiums laid down in a Commission notice; or • Before the implementation of the measure, the methodology to calculate the gross grant equivalent of the guarantee has been accepted on the basis of the Commission Notice on the application of Articles 87 and 88 of the EC Treaty to State aid in the form of guarantees or any successor notice, following notification of that methodology to the Commission under any regulation adopted by the Commission in the State aid area applicable at the time, and the approved methodology explicitly addresses the type of guarantee and the type of underlying transaction at stake in the context of the application of this GBER
Risk finance measures	In case the conditions laid down in Article 21 of GBER are fulfilled

Source: Article 5, paragraph 2, sub-paragraphs "b", "c" and "f" of the COMMISSION REGULATION (EU) No 651/2014 of 17 June 2014 declaring certain categories of aid compatible with the internal market in application of Articles 107 and 108 of the Treaty.

Aid intensity and eligible costs

For the purposes of calculating aid intensity and eligible costs, all figures used shall be taken before any deduction of tax or other charge. The eligible costs shall be supported by documentary evidence which shall be clear, specific and contemporary.

[11] If the state aid concerns fishery or agriculture, the statement of the Ministry of Finance has to be coordinated with the Ministry of Agriculture and Foods.

Where aid is granted in the form of repayable advances (a loan for a project which is paid in one or more instalments and the conditions for the reimbursement depend on the outcome of the project) which, in the absence of an accepted methodology to calculate their gross grant equivalent, are expressed as a percentage of the eligible costs and the measure provides, that in case of a successful outcome of the project, as defined on the basis of a reasonable and prudent hypothesis, the advances will be repaid with an interest rate at least equal to the discount rate applicable at the moment the aid is granted. The maximum aid intensities laid down in Chapter III of the GBER may be increased by 10 percentage points. In such cases the maximum aid intensities established in a regional aid map in force, at the moment the aid is granted, may not be increased.

Compliance

To ensure a uniform level of compliance with the criteria of the GBER and limit distortions of competition in the Single Market, the significant increase in exempted aid measures is balanced by several safeguard mechanisms:

- Transparency: national public registers of individual aid awards will ensure peer review and greater accountability.
- Monitoring: strengthened ex post-controls of compliance with the formal conditions for exemption.
- Evaluation: collecting solid evidence will help designing smarter schemes with a better incentive effect (i.e. ensuring that the aid does not simply subsidise a project that the beneficiary would have undertaken without the support) and less competition distortions.
- The intentions of the Bulgarian Ministry of Finance are to implement the above safeguards and especially transparency, through adoption of the above mentioned amendments to the State Aids Act. If this will not be the case some amendments to the local secondary legislations are required.

Taking into account all written above, most of the formal legal issues raised during the previous programing period were solved by the new GBER. However, there could be still issues concerning the practical implementation of the GBER related with the broaden role of the Bulgarian Ministry of Finance – a large number of staid aids shall be subject of exemption under GBER and shall not be a subject of notification to the EU Commission under Art.108 paragraph 3 of the Treaty.

Therefore, it would be advisable for the future amendments to the local legislation based on the new GBER to cover the following practical obstacles raised within the previous programing period:

- Monitoring and coordination of the measures at earlier stage, not only at their final stage in order to avoid their redrafting. In this regard the obligation to follow strictly the three stages (preliminary, veritable and final) coordination procedure, established by the State Aids Act shall be ensured, including for example special penalties in case of breach of this obligation;
- Utilisation of the procedure for granting the state aid and incorporation of the effective from practical perspective mechanisms for checking the compliance of the measures with the applicable regulations. For example, requiring detailed analysis of the impact of the measure on the respective market in different scenarios – conservative, less conservative and liberal; Preliminary (before implementation of the state aid) coordination with the EC; etc. (Statement of the Minister of Finance concerning procedural issues is subject of approval).
- Implementing the reasonable mechanism for monitoring the state aid not only at the stage of its granting, but also in all phases of its implementation; disbursment of the funds step by step after meeting specific criteria, etc.

3.5.2. De minimis exception

On 18 December 2013 the European Commission adopted a revised Regulation on small aid amounts that fall outside the scope of EU state aid control because they are deemed to have no impact on competition and trade on the internal market. This Regulation became effective as of 1st January 2014. Measures that fulfil the criteria of the Regulation de minimis shall be exempt from the notification requirement under Art.108 paragraph 3 of the Treaty.

General ceiling criteria

The EC has set general ceiling criteria for the aid to be considered de minimis, which are the following:

- The total amount of de minimis aid granted to a single undertaking shall not exceed EUR 200,000 over any period of three fiscal years.
- The total amount of de minimis aid granted per Member State to a single undertaking performing road freight transport for hire or reward shall not exceed EUR 100,000 over any period of three fiscal years. This de minimis aid shall not be used for the acquisition of road freight transport vehicles.
- If an undertaking performs road freight transport for hire or reward and also carries out other activities to which the ceiling of EUR 200,000 applies, the ceiling of EUR 200,000 shall apply to the undertaking, provided that the Member State concerned ensures, by appropriate means such as separation of activities or distinction of costs, that the benefit to the road freight transport activity does not exceed EUR 100,000 and that no de minimis aid is used for the acquisition of road freight transport vehicles.

The Regulations de minimis shall apply only to the state aids, which can be considered transparent. Regarding FIs, the conditions to be met in order to be implemented under De minimis regulation are presented in the next table

Accumulation

De minimis aid shall not be cumulated with State aid in regard to the same eligible costs or with State aid for the same risk finance measure, if such accumulation would exceed the highest relevant aid intensity or aid amount fixed in the specific circumstances of each case by a block exemption regulation or a decision adopted by the Commission. De minimis aid which is not granted for or attributable to specific eligible costs may be cumulated with other State aid granted under a block exemption regulation or a decision adopted by the Commission.

Table 4: Financial Instruments and "*de minimis*" conditions to be met for their implementation

Type of Financial instrument	Conditions to be met
Loans	• The beneficiary is not subject to collective insolvency proceedings nor fulfils the criteria under Bulgarian law for being placed in collective insolvency proceedings at the request of its creditors. In case of large undertakings, the beneficiary shall be in a situation comparable to a credit rating of at least B-; and • The loan is secured by collateral covering at least 50 % of the loan and the loan amounts to either EUR 1m (or EUR 500,000 for undertakings performing road freight transport) over five years or EUR 500,000 (or EUR 250,000 for undertakings performing road freight transport) over 10 years; if a loan is for less than those amounts and/or is granted for a period of less than five or 10 years respectively, the gross grant equivalent of that loan shall be calculated as a corresponding proportion of the relevant ceiling laid down in Article 3(2) of the Regulations de minimis; or • The gross grant equivalent has been calculated on the basis of the reference rate applicable at the time of the grant.
Capital injection	The total amount of the public injection does not exceed the de minimis ceiling.
Risk finance measures (equity or quasi-equity investments)	The capital provided to a single undertaking does not exceed the de minimis ceiling.
Guarantees	• The beneficiary is not subject to collective insolvency proceedings nor fulfils the criteria under its domestic law for being placed in collective insolvency proceedings at the request of its creditors. In case of large undertakings, the beneficiary shall be in a situation comparable to a credit rating of at least B-; and • The guarantee does not exceed 80% of the underlying loan and either the amount guaranteed is EUR 1.5 m (or EUR 750,000 for undertakings performing road freight transport) and the duration of the guarantee is five years or the amount guaranteed is EUR 750,000 (or EUR 375,000 for undertakings performing road freight transport) and the duration of the guarantee is 10 years; if the amount guaranteed is lower than these amounts and/or the guarantee is for a period of less than five or 10 years respectively, the gross grant equivalent of that guarantee shall be calculated as a corresponding proportion of the relevant ceiling laid down in Article 3(2) of the Regulations de minimis; or • The gross grant equivalent has been calculated on the basis of safe-harbour premiums laid down in a Commission notice; or • Before implementation, – The methodology used to calculate the gross grant equivalent of the guarantee has been notified to the Commission under another Commission Regulation in the State aid area applicable at that time and accepted by the Commission as being in line with the Guarantee Notice, or any successor Notice; and – That methodology explicitly addresses the type of guarantee and the type of underlying transaction at stake in the context of the application of this Regulation.
Other instruments	The relevant ceiling is not exceeded.

4. Market environment

The purpose of the section is to present the 'macro-economic' environment of the country but also present an overview of economic and social aspects that can affect the financing of projects and the use of FIs in Bulgaria. More specifically, the factors identified in this chapter may influence policies linked to HR development and the relevant targeted groups. The aim of this chapter is to identify the trends that outline the short and mid-term development of the country. This exercise will help to establish the economic framework for analysing the supply and demand for financing of HR policies in Bulgaria, and also to identify the market failures later on in the report.

4.1. Economic and political environment in Bulgaria

Important indicators such as Gross Domestic Product (GDP) growth rates, inflation, and political and regulatory matters (e.g. fiscal conditions and tax policies), which for the most part define existing market conditions (e.g. investments, consumption and export growth) ultimately affect human resource development.

Table 5: Key figures of the Bulgarian economy

indicators	Value	Date
Population	7 245 677	2013
GDP	EUR 41 bn	2013
Real GDP Growth	1,7 %	2014e

Source: NSI, European Economic Forecast European Economy 3|2014, European Commission http://ec.europa.eu/economy_finance/eu/forecasts/2014_spring/bg_en.pdf

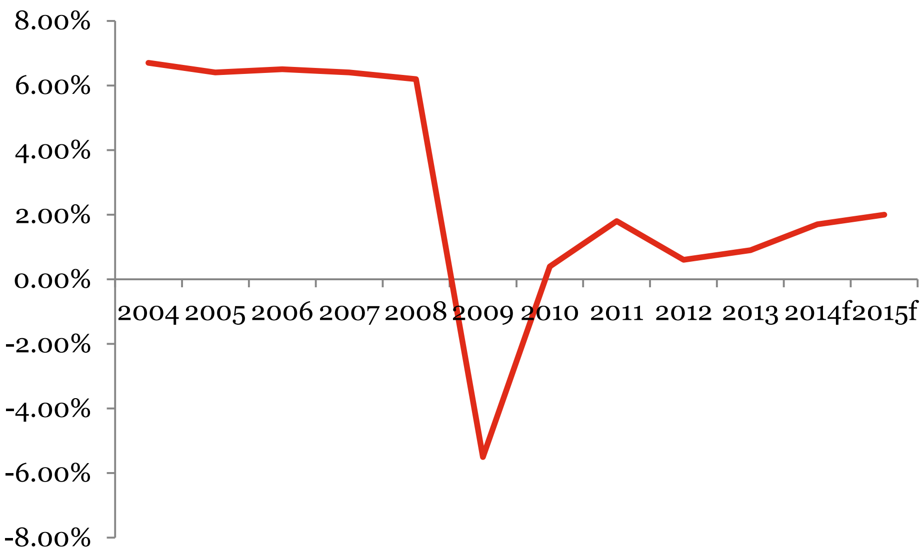
4.1.1. Political context

The political situation, as in every democratic country, has an impact on the Bulgarian market environment and, ultimately, on social policies. Currently, the political situation in Bulgaria is unstable. The political transition, from a caretaker government (13th March - 28th May, 2013) to a coalition government, led by the Bulgarian Socialist Party, created social and political tension. After the government took office in May 2013, a controversial political appointment shook its credibility and sparked demonstrations. As a result, social unrest was apparent in the capital with daily demonstrations of several social and professional groups. As a result of this tension, the coalition government submitted its resignation in July 2014. A caretaker government was set up for the second time in the last two years which will lead the country to elections in October 2014. This lack of a stable government has naturally a negative effect on the economy and the market. This instability has two major direct effects on project financing. On the one hand, banking institutions are more reluctant to finance projects that are linked to national or regional authorities and administrations due to the uncertainty and risk related to the actual implementation of these projects. On the other hand, the political instability has been affecting the country's credit rating which in turn leads to an increase in interest rates and in the cost of financing. Overall, the political instability is affecting the absorption of European funds and the implementation of FIs. However, the prospects are not necessarily negative. Expectations of stakeholders are that the next elections could allow for a reinforced and more stable political coalition

4.1.2. Economic overview

Since the country's accession to the European Union in 2007, and despite the significant setback of the global financial crisis, Bulgaria's economy has recently demonstrated a slow recovery. Recent regulatory changes implemented in the country continue to improve the local business environment. However, the Eurozone's unstable economic situation, combined with the current local political uncertainty, continue to create a volatile environment, which will most likely create barriers to a more stable growth in the medium term.

Figure 2: Historical and forecasted growth for GDP in Bulgaria



** The data for 2014 and 2015 is forecast*

Source: http://ec.europa.eu/economy_finance/publications/european_economy/2014/pdf/ee2_en.pdf , Eurostat, 2014.

Since the decline observed in 2009, the country's economic performance has experienced a gradual but still slow recovery. This has been mainly linked to a disciplined fiscal consolidation effort on the state expenditure side and a gradual increase on the income side, mostly fuelled by a more stabilized real estate market and growing export activities. However in relative terms of GDP per capita, compared to the EU average, the country is still in a weak position. This is an indication that structural reforms are still needed to boost economic growth. Fiscal consolidation is not sufficient to create growth conditions.

Table 6: Contribution from the EU 28 to Bulgaria's and neighbouring nations' GDP per capita

GDP per capita as a % from EU 28							
	2007	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**
Bulgaria	40	43	44	44	46	47	47
Greece	90	93	95	89	81	76	75
Romania	43	49	50	51	51	53	54

Source: Eurostat

4.1.3. Foreign Direct Investments

The level of Foreign Direct Investment (FDI) in Bulgaria over the recent years has been indicative of the overall economic performance of the country. Low labour costs have not been able to attract substantial FDIs, however some foreign investments have supported sectors like tourism and industrial production. Following a peak in 2007, the financial crisis caused a collapse of FDI in 2009 and 2010. Since then, the level of FDI has remained substantially below the pre-crisis levels and is characterised by volatility on a year-by-year basis. In 2012, the FDI temporarily increased but the country appears unable to maintain investors' confidence, thus leading again to a fall in investments in 2013 (BNB, 2013). The table below clearly demonstrates that Bulgaria remains below the EU average in terms of FDI as a percentage of GDP.

Table 7: Direct investment into Bulgaria

Direct investment flows as a % of GDP							
	2007	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**
Bulgaria	0.7	1.5	-0.2	0.5	0.3	0.7	0.3
EU 27 average	4.5	3.0	2.8	2.5	3.7	2.0	2.6

Source: Eurostat

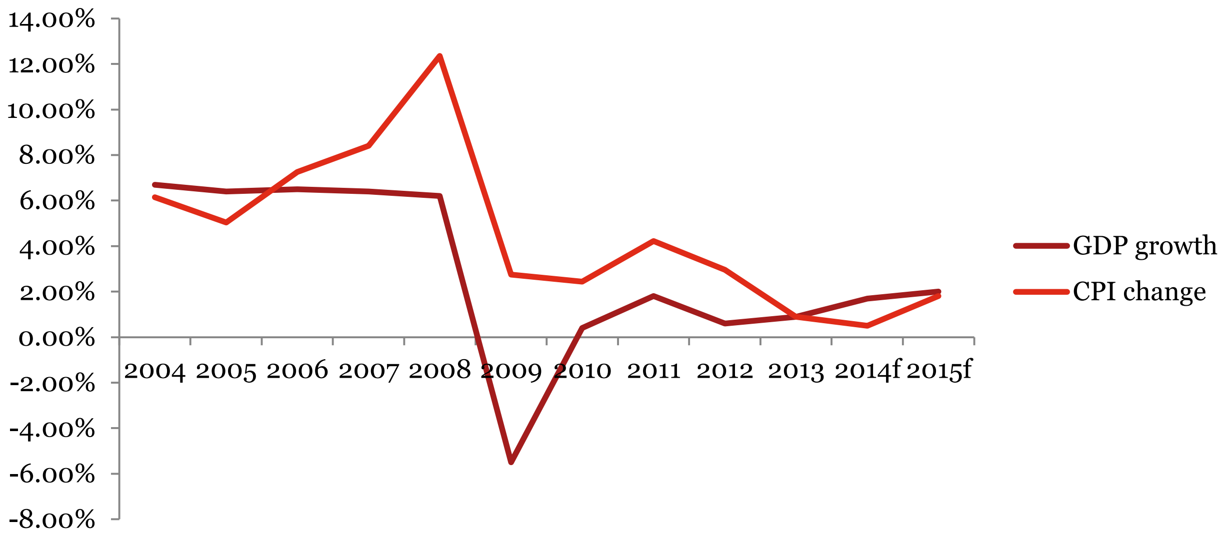
As already mentioned, in some specific sectors FDIs remain particularly important especially at the regional level. However, FDIs need further conditions such as infrastructure, connectivity, industrial areas, and especially labour force skills, in order to show interest. The convergence effort of Bulgaria through the use of European funds and FIs has to focus on the areas to increase the country's competitiveness and attract foreign investors. This is a crucial point since FDIs could support business creation in the country and tackle unemployment.

4.1.4. Inflation

Inflation is one of the major indicators for the economic stability and business environment of any country. When public policy is in question, inflation and interest rates are closely tied especially when it comes to financing public initiatives and projects. Any central bank including the BNB adjusts interest rates according to inflation amongst other factors, thus the use of any FI shall be influenced by the cost of money in the country. Therefore, a brief overview of this indicator is imperative for this report and shall be provided by this section.

According to a recent survey in Bulgaria, (BNP Discussion Papers, 2012), inflation is not perceived by businesses as a main concern. Projections for the coming years also suggest that inflation will be closely aligned with growth rates and within the range of 0%-4%, and thus is not expected to cause concern for human resource development even in the long-run, as shown in the figure below.

Figure 3: Comparison between GDP growth and changes in CPI



Source: NSI, PwC analysis, 2014.

Following the intervention and introduction of the Currency Board in 1997, the inflation rate had remained relatively stable, with the Consumer Price Index (CPI) ranging between 2.3% and 5.0% (6.1% in 2004) over 2003-2005. During the economic boom from 2006 to 2008, the inflation displayed a sharp increase, peaking at 12.3% by the end of 2008. The following years, CPI decreased again, mainly due to weak external demand and low domestic market consumption.

It reached 3% in 2012 and the short-term trend is positive with the first quarter of 2013 data showing a further decrease of 0.7%. Furthermore, the price levels of the "food" and "non-food" category have also declined by 0.2% on average in 2013.Inflation stability in Bulgaria is important when considering the design of social policies since people at risk of poverty are more likely to improve their living standards and secure necessary goods under such an environment.

In August 2013 the inflation falls below zero, with a negative figure of -0.7%, which continues to decrease until the end of the year, reaching -1.6% in December 2013.

In the first six months of 2014 the inflation remains negative (based on the annual averadge CPI for the previous 12 months). The deflation was driven by the fall in the prices of transport fuels, food and services mainly reflecting international prices and some specific factors related to certain groups of services.[12] However according to EC's [13] European economic forecast for the winter 2014 the annual inflation rate for 2014 is expected to be positive and around 1%.

4.1.5. Interest rates and the banking sector

Since the beginning of the crisis, the banking sector in Bulgaria retained high liquidity and despite the strong presence of Greek banks (30% market share in 2009) managed to remain stable. Despite the environment of low investment and decreasing credit activities, the tendency from households to curb consumption and increase savings is securing bank liquidity. Nonetheless, solvency issues related to the uncertainty of the economic environment in Bulgaria, and the lack of credible business plans and bankable businesses, lead to high interest rates, which continue to affect the cost of loans for SMEs.

The banking sector in Bulgaria is dominated by foreign banks, although the share of Bulgarian banks has increased to 25% of the total market mostly at the expense of Greek banks. Increasing deposits have caused the loan-to-deposits ratio to fall from 120% to 105% (2009-2011, IMF), thus gradually shifting bank's funding from

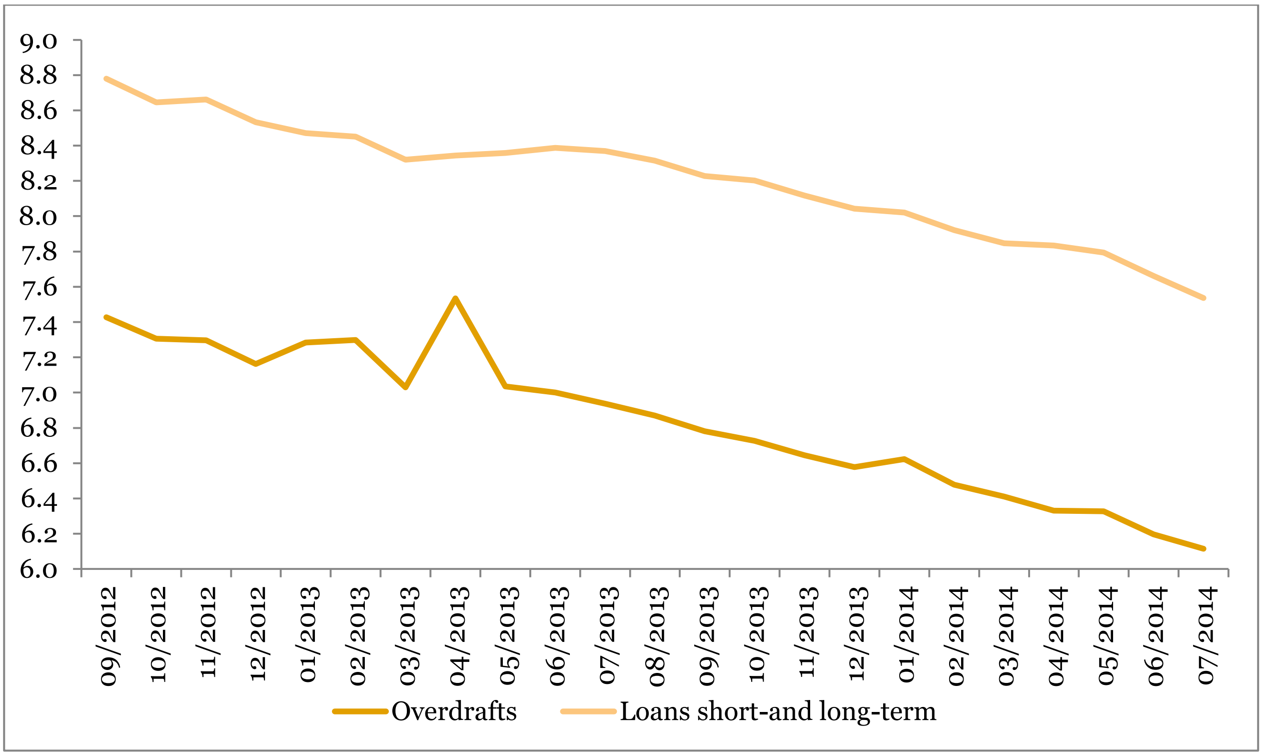
[12] http://www.bnb.bg/bnbweb/groups/public/documents/bnb_publication/pub_ec_r_2014_02_en.pdf

[13] http://ec.europa.eu/economy_finance/publications/european_economy/2014/pdf/ee2_en.pdf

a parent-based to a domestic deposit-based model. The competition between foreign and local banks for household and business savings is having an upward impact on interest rates for savings, which peaked in 2009 (for the local currency savings) at almost 7.5% (average weighted interest rates of new deposits). Nonetheless, since then, the oversupply of savings from households, along with the relative low demand for loans, have caused a gradual decrease in interest rates for savings, reaching 3.5% for new deposits in mid- 2013. Similarly, the low interest rate policies of the ECB have also affected the interbank money market's declining trend. More specifically, the SOFIBOR (Sofia Interbank Offered Rate) has maintained a declining spread as compared to the EURIBOR, which, in turn, has been declining over the recent years. Overall, the lower interest rate levels on the interbank market in Bulgaria and in the Euro area, as well as the gradual fall in interest rates on attracted deposits, are contributing the most to the downward trend in the average cost of financing in the banking system.

As a result, the interest rates on new loans in BGN to non-financial corporations have been gradually decreasing after their peak in 2009, when they almost reached 11%. In the first half of 2013, according to BNB data, interest rates for non-financial institutions are slightly above 8% (weighted average on a 12 month basis for all categories of loans). The interest rates continued to fall over the course of 2013 and the beginning of 2014, until at the beginning of 2014 the interest rate for short- and long-term loans falls below 8%, reaching 7.92 in February 2014. The graph below shows the monthly changes of interest rates for different loan maturities.

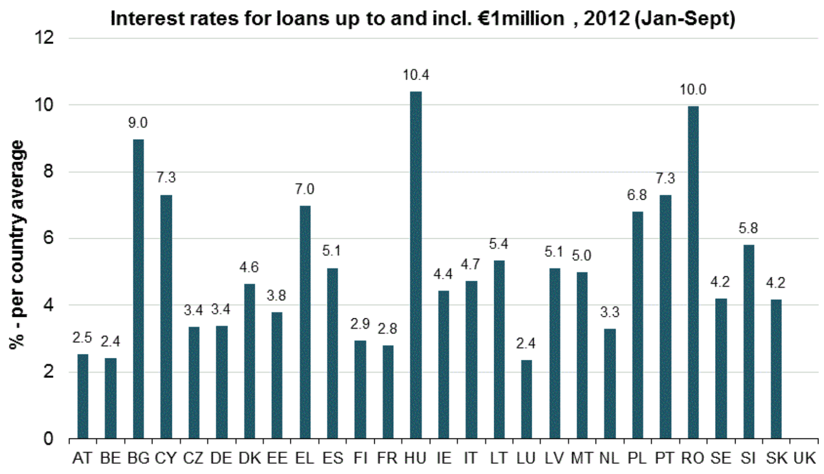
Figure 4: Monthly changes of interest rates for overdrafts, short- and long-term loans



Source: BNB, 2014

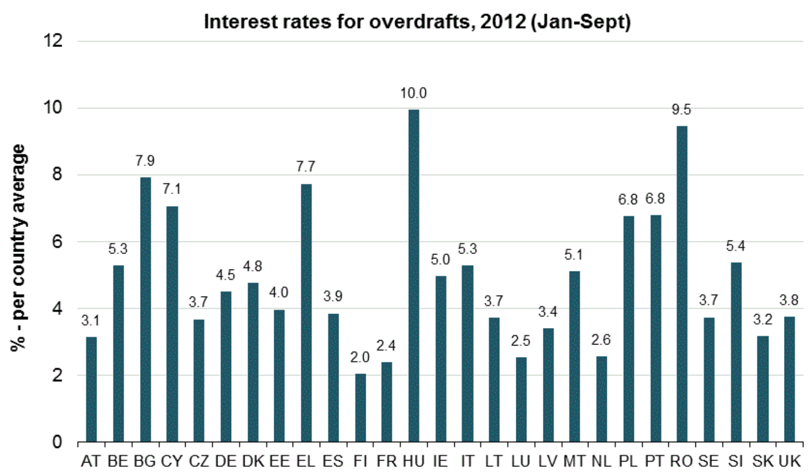
Despite this declining trend in the last months, interest rates for loans to businesses remain high compared to other EU countries. In fact, according to European Commission data (DG Enterprise and Industry), overdrafts and loans of up to EUR 1m in Bulgaria have the third highest interest rates in the EU behind Hungary and Romania as shown in the tables below. These high interest rates form a crucial barrier for access to finance in Bulgaria.

Figure 5: Interest rates for loans up to and including EUR 1m in the EU for 2012 (January to September)



Source: European Commission, 2013

Figure 6: Interest rates for overdrafts in the EU for 2012 (January to September)



Source: European Commission, 2013.

The main focus of the present report is on the lending capacity or the willingness of banks to finance projects related to urban development. On the capacity aspect, as already mentioned banks remain liquid. However, an alarming trend in the Bulgarian market is the rising indebtedness of businesses. The total corporate debt is reported at extremely high levels by the Intentional Monetary Fund (IMF) (at 150% of GDP for 2010). This level corresponds to the more troubled countries in the EU such as Ireland and Greece. By contrast, countries such as Slovakia or Latvia maintain much lower corporate debt levels. Non-Performing loans (NPLs) in Bulgaria are constantly rising and mostly concern the sectors most affected by the crisis, namely construction, manufacturing and services. According to the World Bank, the NPLs as a percentage of total loans between 2009 and 2013, accounted for 16.9%, almost similar to the levels found in Greece or Ireland (17.2% and 18.7% respectively) which are the countries most affected by the financial crisis in Europe. It is worth mentioning here that many peer countries experience rising NPLs to a similar extent. More specifically, Romania has a rate of 16.8%, Hungary 15.8% and Lithuania 18% showing that NPLs have become a main challenge for many economies in the EU. According to BNB[14], the level of NPLs in Bulgaria reached 17.1% in June 2013. This

[14] Bulgarian National Bank, "Banks in Bulgaria January-June 2013".

concern may cause the banking system to become more cautious in the following years and affect their financing capacity.

4.2. Demographics and labour force in Bulgaria

Social indicators and conditions (e.g. the quality and cost of human resources) and the overall outlook of the demographics have a direct impact on the scope for human resource development and remain, as well, crucial components of Bulgaria's economic development.

4.2.1. Demographics

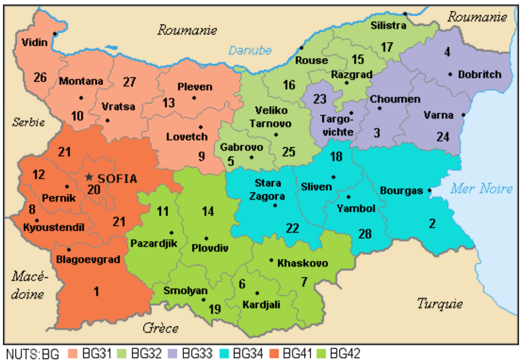
Human capital is one of the most influential and important factors that affects human resource development. Therefore, the country's human resources in terms of demographics merit a close analysis in this report. The demographic trends in Bulgaria deeply shape the output variables of the activities of HRD OP and have had a major impact on defining the specific target groups and objectives of the programme.

In terms of a more aggregate view, total population in the country has declined by 6‰ compared to 2011 (NSI, 2012), and a decrease in the population size is further forecasted until 2060 (NSI, PwC analysis, Census 2011). Bulgaria displays a negative natural growth, -5.1‰ since 2011, which places it last amongst EU-27, where the average was +8‰ for the same period. Moreover, the country ranks relatively high (5th in the EU) for its proportion of aging population - the number of people above the age of 65 represented 19.2% of Bulgaria's population increasing by 4‰ since 2011 (NSI, 2012).

In support of this, the 2011 census discloses a relatively high age-dependency ratio (population under 15 and over 65 years, compared to the population aged 15-65 years), namely 47.5% (representing a rise of 1.5% compared to 2010). This ratio is even lower in rural areas compared to cities: respectively, 63.9% and 42.2%. In fact, despite the rising retirement age, as of the end of 2012, the working population has decreased by almost 20,000 people, or 4‰, in comparison with the previous year. This trend is enhanced by the fact that people seek employment in other countries or in larger cities.

Overall, Bulgaria is facing demographic challenges similar to most other European countries with an aging and decreasing population. These challenges will have to be confronted in the long run to develop a sustainable economic and social system. In this context raising employment levels and improving employment opportunities in particular for young people, women and older workforce members must be a key priority in order to at least partially offset the negative effects of the shrinking working age population. The territorial cohesion, being a prerequisite for the benefits of growth and jobs, may prove a significant factor in the implementation of human resource development policies. Since the difference in the extent and quantity of economic activity between rural and urban areas is so vast, the degree of need for human resource development in some areas may prove different than in others. Idem, the quality, quantity and other characteristics of the population in different regions at the offset might display considerable variance, influencing HR development schemes and progress.
According to the NUTS 2 (Nomenclature of Territorial Units for Statistics) codes of Bulgaria, its territory is divided into 6 planning regions – North-western, North-central, North-eastern, South-eastern, South-central and South-western – subdivided into 28 provinces (Figure 7), the latter corresponding to the respective names of the biggest cities within the area.

Figure 7: Regional division of Bulgaria under the NUTS



Source: Eurostat, 2011

The analysis of the distribution of the population shows considerable disparity in terms of population density between rural and urban areas. In the last ten years the tendency to move to urban areas has led to a concentration of the population in the seven big cities and to the accelerated depopulation of rural areas, which causes severe socio-economic disparities and hiders demographic development in rural regions. The analysis also show that the probability to move abroad after migrating to a large/larger city is much higher and is one of the conditions accompanying the brain drain process, disharmonising the labour market in Bulgaria[15].

The census of 2011 reported that 72.9% of the total Bulgarian population lived in cities and only 27.1% in rural areas. Only seven cities have a population exceeding 100,000 inhabitants. The biggest district in terms of population is the capital Sofia, with 1.213 million inhabitants (17.5% of the total population). The previous census in Bulgaria was conducted in 2001. For the first time in Bulgaria's demographic history, the population in rural areas has fallen below 2 million people. This disparity between cities and rural areas is highlighting a mobility trend to larger cities in search of better opportunities and job prospects. In the period between the two censuses the population in Sofia alone had increased by 120,749 people, or 10.3%.

As a result of this, a very large proportion of economic activity is taking part in Sofia and the surrounding regions. As **Figure 8** shows, the population in the Sofia area is predominantly concentrated (for approximately 50%) in two regions: the south-western (where Sofia is located) and central south regions.

Figure 8: Number of inhabitants per region as of 2011

Regions	Population ('000)	*Share (%)*
North-West	823	*11.3%*
Central North	844	*11.6%*
North-East	957	*13.1%*
South-West	2,128	*29.2%*
Central South	1,462	*20.1%*
South-East	1.067	*14.7%*

Source: NSI, PwC analysis, Census 2011.

In every one of the 28 regions, the rate of the population living in cities exceeds 40% (41.59% in Kardzhali and 45.07% in Silistra to 83.74% in Varna and 95.37% in Sofia-city). The territorial disparities in Bulgaria are also dependant on the level of economic activity in the different regions, which is later used as a base to estimate the population at risk of poverty. The level of economic activity puts eight regions in the ranking of the regions with

15 Socio-economic analysis for the OPRR 2014-2020 bgregio.eu.

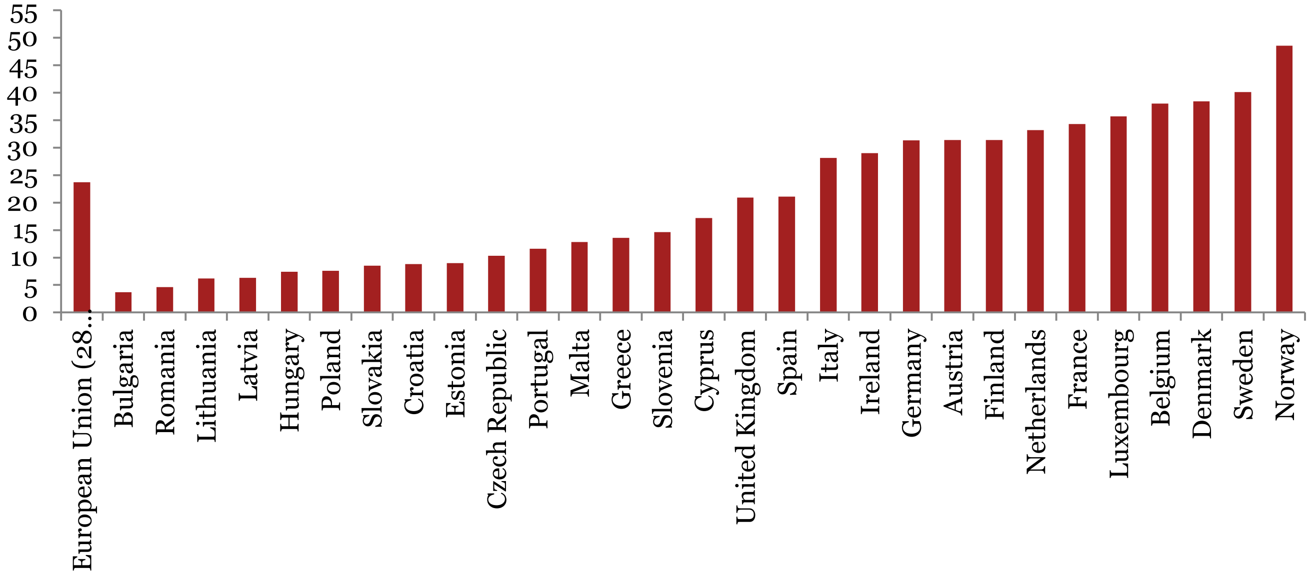
the lowest GDP per capita in the EU in 2011 (all in Bulgaria and Romania): the lowest figures (100% being the EU average) recorded are in North-West in Bulgaria and Nord-Est in Romania (both 29% of the average), followed by Central North in Bulgaria (31%) and Central South in Bulgaria (32%)[16], leading to long-term unemployment and causing a serious social problem.

4.2.2. Labour force

As may be expected, Bulgaria's changing demographics have an extensive influence over most domestic social indicators. The wide availability of inexpensive labour force could represent a competitive advantage for the country, and could serve as a lever to attract investment, thus promoting employment. In fact, Bulgaria has the lowest hourly labour cost in the EU. Figure 9 shows the labour cost per hour in EURO for the whole economy excluding agriculture and public administration for 2013 with the EU-28 average. The data for the period 2008-2013, provided by Eurostat, shows that the labour cost in Bulgaria is not only significantly lower than the EU-28 average, but remains the lowest in the EU.

However, this advantage cannot produce results without being combined with other qualitative aspects of the labour force. The competitiveness of Bulgarian labour force has been threatened mainly by issues such as aging population and the ongoing "brain drain", both profoundly reflected in the country's demographic footprint.

Figure 9 : Labour cost per hour in EUR for EU-28 in 2013



Regional distribution of the labour force

As was already emphasized, aging population and the brain drain could become causes for concern for HR development (evident by the small percentage of working population at the age from 15-24 – only 25%); this being an issue especially for less developed regions. The work force in Bulgaria is distributed unevenly to a great extent – 79% of the working population of Bulgaria as of the first quarter of 2014 is located in cities, while at the same time the economic activity in cities represents 57.7% of the total for the country.

[16] http://epp.eurostat.ec.europa.eu/cache/ITY_PUBLIC/1-27022014-AP/EN/1-27022014-AP-EN.PDF

Figure 10: Labour force and rates of economic activity as of Q2 of 2014

	Population ('000)	*Rate of economic activity (%)*
In cities	2 631.6	58.0%
In villages	730.0	43.5%

Source: NSI, 2014.

In terms of quality of the labour force, there are significant differences in the educational level between urban and rural populations. Almost three quarters of the population in urban areas (71.6%) have secondary education; while the rural population is relatively less educated (40.3% have obtained a degree in secondary education).

The economic crisis has exerted a much stronger negative effect on the labour market in the northern part of Bulgaria. In 2012, five of the country's districts with employment rates below 40% were in North Bulgaria: Vidin, Vratsa, Lovetch, Montana and Silistra. Some of the poorest regions (in terms of GDP per capita) are there as well – Targovishte, Lovech and Montana. Among the key factors for the negative impact of the crisis on those districts are the unfavourable demographic situation, lower degree of urbanization in many of the districts, the relatively low inflow of foreign investment and the inadequate level of development of the economy and infrastructure, which in turn has a negative impact on workforce mobility. The increase of the minimum social insurance thresholds by individual economic activities during the years of the crisis had an additional negative effect on employment in many of those districts, already characterized with low wages. On the contrary, the labour market in South Bulgaria is better balanced. This can be attributed to a number of factors, amongst which, the higher workforce mobility, the more available population at work age and the fact that the economically leading cities are located in this part of Bulgaria including Sofia (capital), Plovdiv, Stara Zagora and Bourgas. The table below presents information on the distribution of the work force by region in Q2 2014:

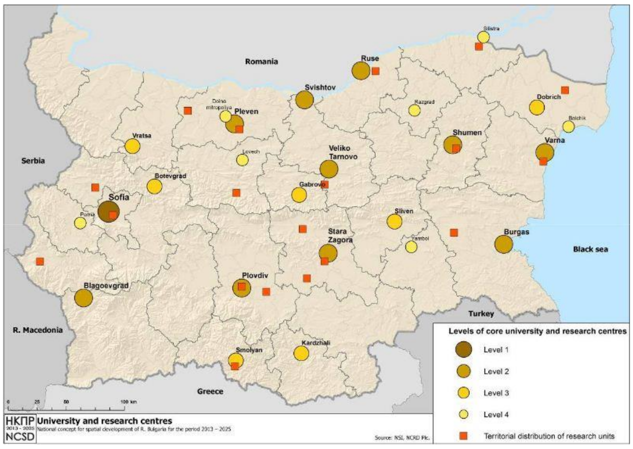
Table 10: Distribution of the workforce by region in Bulgaria

Region	Employed people in thousand	Coefficient of employment (%)	Unemployed people in thousand	Coefficient of unemployment (%)
North-west	328.8	47.2%	53.8	16.4%
Central-north	368.7	50.8%	50.4	13.7%
North-east	433.7	53.3%	50.0	11.5%
South-east	461.2	51.5%	51.6	11.2%
South-west	1077.3	58.6%	97.8	9.1%
Central-south	691.8	55.5%	78.2	11.3%

Source: NSI

As already mentioned, the quality of the work force is highly dependent on the educational opportunities the specific regions offer. In this regard, the uneven distribution of universities within the territory of the country (see Figure below) has a further negative impact on the quality of the work force in some regions.

Figure 11: Distribution of universities in Bulgaria



Source: National Concept for Spatial Development 2013-2025.

Education and training

In addition to the negative demographic growth in Bulgaria, one of the main pillars of the human resources development and respectively quality, remains the education. The close link between the level of education of the population and the market needs turns into a bottleneck for the sustainable and inclusive growth that the country is perusing. According to the studies conducted in regards to the National strategy for demographic development 2012-2030, some of the major reasons (despite the increasing number of people with higher education) are on the one hand the lack of priority areas for the development of the economy and the link between education and the demand for professionals in this areas; and on the other hand the quality of the education (especially the professional and the higher). Bulgaria ranks among the last 30 countries in the world for the “quality of labour force preparation”[17] according to the World Economic Forum.

Figure 12: Labour force and rates of economic activity as of Q2 of 2014, by gender, age and education

	Population ('000)	*Rate of economic activity (%)*
	By sex	
Male	1 800.4	60.1%
Female	1 561.2	48.4%
	By age	
15-24	202.1	27.3%
25-34	765.1	78.0%
35-44	942.6	87.5%
45-54	824.8	84.2%
55-64	570.0	55.7%
65 and above	56.8	4.0%

[17] The Global Competitiveness Report 2012–2013, World Economic Forum

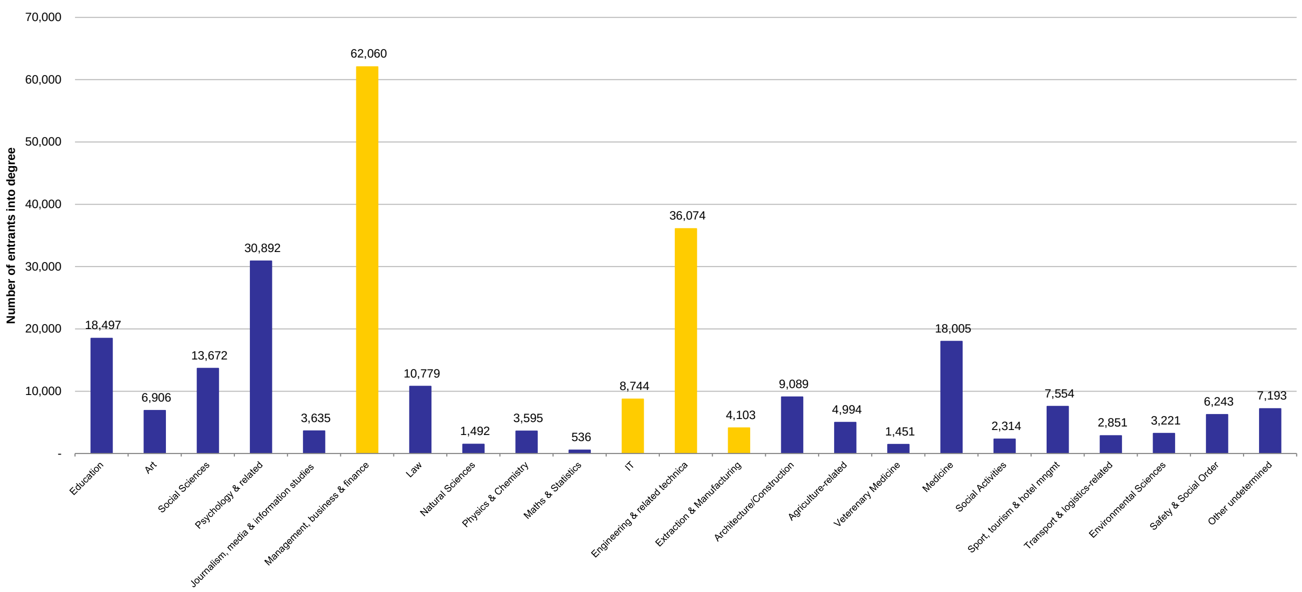
By level of education		
Higher	1 003.9	73.7%
Secondary	1 897.6	61.6%
Secondary with an acquired professional qualification	1 236.4	68.1%
Primary	388.2	27.7%
Elementary and lower	71.9	19.1%
Total	**3 361.6**	**54.1%**

Source: NSI, 2014.

Despite the satisfactory levels of the overall education of the population, the level of the illiterate persons and the persons, who have never visited school, grows. 1.2% of the population over 7 years has never visited a school and population above 9 years is 1.5%. Moreover there is significant difference in the levels of illiteracy among the three main ethnic groups in Bulgaria: 0.5% of the self-defined as Bulgarians; 4.7% by the self-defined as Turks and 11.8% by the self-defined as Roma. As main reasons for this numbers the research shows among others the difficult access to schools and financial difficulties. It is disturbing that the increasing number of illiterate persons and early school leavers is concentrated in the low income part of the population and in specific ethnic groups, which is very often accompanied by social risk and leads to rising number of socially excluded or at risk of social exclusion persons.

The Bulgarian workforce can be viewed as skilled and competent in areas such as medicine, science, engineering and economics. More specifically, as shown in Figure 13 below, within a total of 263,900 students in Bulgaria, management, business and finance were the subjects most often studied during the academic year of 2012-2013, accounting for 62,060 or 24% of students. It is followed by engineering (36,074 students, or 14%), IT (8,744 students, or 3%) and manufacturing/technical studies (4,103 students, or 2%).

Figure 13: Number of students entering into Higher Education by degree type, 2012-2013



Source: NSI, PwC analysis, 2013.

Despite the high number of students studying natural sciences in Bulgaria, including the large number of management students, a clear transfer of skills from the theoretical to the entrepreneurial and managerial has not yet taken place in the market. According to several business stakeholders interviewed, the market is still lacking sophisticated management practices that are crucial to the development of high value-added and technology-intensive sectors.

During the last ten years, Bulgarian universities seem to have been struggling with limited resources, outdated technological equipment, and ageing staff. Younger people have little interest in research careers. There is also low demand for research services and insufficient investment to improve infrastructure and research facilities.

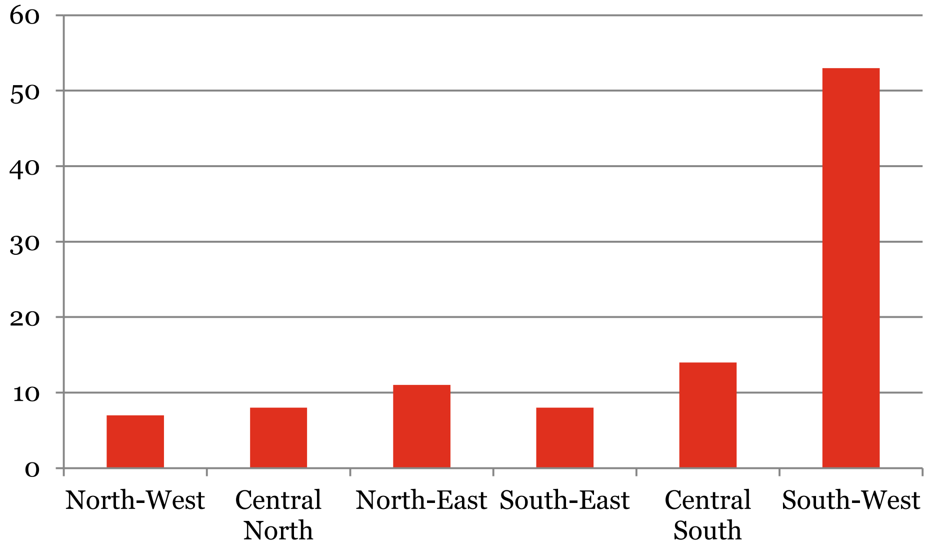
As a potential revenue-generating social structure, training centres may be considered as a potential beneficiary of the HRD OP. As previously mentioned, a high number of people do not have higher or sufficient education to successfully enter the labour market. Due to lack of technical competencies and specific education amongst target group, it may be beneficial to redirect certain target group members to vocational training and lifelong learning in order to give them the opportunity to apply for a larger number of vacancies and enhance their success rate given current labour market needs.

In Bulgaria there are currently 934 licensed training centres (exclusive of another 38 currently in a licensing procedure).[18] This number however should be discounted when estimating the number of eligible beneficiaries under HRD OP as not all of the above-mentioned training centres provide training for adults with lack of skills or education.

According to the NAVET catalogue for training centres providing professional/vocational training, there are currently 101 centres providing such services in Bulgaria across a number of regions and industries. However, apart from that, there is no available information as to the total number of such entities in Bulgaria. The participation in the NAVET catalogue is voluntary and upon application, which does not guarantee that all eligible training centres have been included and registered.

From training centres providing vocational training included in the NAVET catalogue, one may draw the following picture based on their distribution across regions. Unsurprisingly the largest number of registered training centres has been recorded in the South-west region, where the capital of Sofia is located.

Figure 14: Number of training centres per region in Bulgaria



[18] NAVET is the Training centre register of Bulgaria, 2014

Source: NAVET catalogue of training centres providing vocational centres, http://cpobg.com/catalogue.htm?ReadForm

In the annual report of the National Employment Agency for 2013[19], the total number of persons participating in trainings already completed was 9,928:

- 5,461 training for motivation for job searching;
- 3,698 training for professional orientation;
- 414 training for professional qualification;
- 231 training for key competences;
- 124 training for increasing the literacy.

The average number of hours for training is the following:

- Language on average 300h for a level
- Cosmetician, hairdresser and similar professions around 500.
- More complicated trainings as graphic designer and other IT around 900h (approximately 6 months)

According to the Ministry of Labour and Social Policy[20], the average price of a training disbursed for one person in 2013 was BGN 900, corresponding to EUR 450.

4.3. Small and medium sized enterprises in Bulgaria

Small and medium sized enterprises in Bulgaria are the back bone of the economy and are also the main employer in the country. Therefore, the development and sustainability of SMEs is a crucial component for the success of social policies and policies related to HR development. The business structure in Bulgaria has remained largely unchanged in recent years. In 2011, 99.8% of the total companies were SMEs, They generate 59% of the added value, 67% of the revenues and 76% of the employment21.

From the SMEs 92% are micro-enterprises. Under the thematic objective 8 (Promoting sustainable and quality employment and supporting labour mobility) of the EU 2020 strategy one of the main selected investment priorities is encouraging self-employment, entrepreneurship and business creation including SMEs. The number of companies by regions basically reflect the situation with the GDP by regions – the South-West region has the biggest number of companies (118,185 as of 2012), while the North-West region has the smallest (23,714 as of 2012).[22] . With respect to companies by cities (per 1000 residents), as of 2011, the most companies are located in Sofia, followed by Varna and Bourgas[23].

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[19] http://ophrd.az.government.bg/voucher.asp?type_id=3
[20] http://www.mediapool.bg/dopalnitelni-78-mln-lv-za-obucheniya-po-shemata-az-moga-poveche-news219171.html.
[21] NSI.
[22] Source: NSI.
[23] Source: Institute for Market Economics,2014.

Figure 15: Absolute number of non-financial enterprises per region across 2010 to 2012 and percentage change year-on-year

	2010			2011			2012		
	Total non-financial enterprises	Micro-enterprises	Change 2009-2010	Total non-financial enterprises	Micro-enterprises	Change 2010-2011	Total non-financial enterprises	Micro-enterprises	Change 2011-2012
North-West	28,621	26,379	*-1%*	27,974	25,706	*-3%*	28,271	26,005	*1%*
Central North	34,888	31,790	*-1%*	34,470	31,393	*-1%*	34,580	31,551	*1%*
North-East	50,454	46,700	*0%*	49,859	46,144	*-1%*	50,509	46,832	*1%*
South-East	52,186	48,307	*0%*	52,409	48,539	*0%*	53,689	49,808	*3%*
South-West	135,114	123,730	*2%*	136,264	124,958	*1%*	138,998	128,020	*2%*
Central South	65,666	60,241	*0%*	65,264	59,891	*-1%*	65,989	60,718	*1%*
Total	**366,929**	**337,147**	*0%*	**366,240**	**336,631**	*0%*	**372,036**	**342,934**	*2%*

Source: NSI, 2014.

As mentioned in table above, the highest concentration of micro enterprises is in South-West region (which includes Sofia), there the relative percentage of the microenterprise is 37% (percentage of the total number of microenterprises in Bulgaria), and this is also the region with the highest rate of employment 53% (47% average for the country for 2012). Same positive relationship applies also for the North-West part of Bulgaria, where the level of employment is the lowest (40%), as well as the number of microenterprises - 26,005 (8%).

Considering this positive relationship, the focus therefore should be put on the promotion of micro entrepreneurship in the regions with low concentration of micro companies, which at the same time are the regions with the highest rates of unemployment. As the data show, such measures are expected to reduce social exclusion and risk at poverty people.

4.4. Social economy

According to the European Commission's Social Business Initiative (SEC (2011) 1278), a social enterprise is an operator in the social economy whose main objective is to have a social impact rather than make a profit for their owners or shareholders. It operates by providing goods and services for the market in an entrepreneurial and innovative fashion and uses its profits primarily to achieve social objectives. It is managed in an open and responsible manner and, in particular, involves employees, consumers and stakeholders affected by its commercial activities. The concept of social enterprise overlaps with the traditional social economy organisations and cuts across legal forms, as an entity that operates as a social enterprise might choose to be registered as an association, cooperative, charity organisation, foundation or NGO, as a private enterprise, or as one of the specific forms set up in recent years under national legislation[24].

What distinguishes social enterprises from traditional associations or charities is the fact that social enterprises earn a substantial proportion of their income through trading, rather than being dependent on grants or donations. A benchmark sometimes used for a social enterprise is that at least 50 % of its turnover is earned income, although opinions vary on what the best threshold would be. The table below maps the fields of activity of the social enterprises in Europe:

[24] Communication from the commission to the European parliament, the council, the European economic and social committee and the committee of the regions social business initiative, creating a favourable climate for social enterprises, key stakeholders in the social economy and innovation {sec (2011) 1278 final}

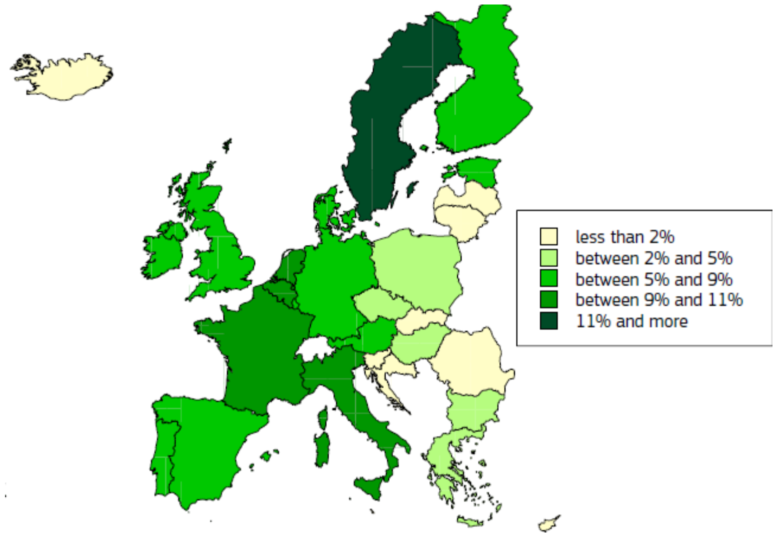
Figure 16: Fields of activity of social enterprises in Europe

Social services	16.7%
Employment and training	14.9%
Environment	14.5%
Education	14.5%
Economic, social and community development	14.3%
Culture, the arts and recreation	7.1%
Health	6.9%
Housing	2.7%
Business associations	2.0%
Law, advocacy and politics	1.6%
Other	4.7%

Source: SELUSI data (research project funded through the 7th Framework Programme of the European Commission) including all observations across 5 representative countries and 581 enterprises. Further information: www.selusi.eu

Based on available evidence[25], it is estimated that the social economy in Europe (measured as the aggregate of cooperatives, associations and foundations) engages over 14.5 million paid employees, equivalent to about 6.5% of the working population of the EU-27 and about 7.4% in EU-15 countries. These figures also include the vast majority of social enterprises, as they include all social enterprises using social economy legal forms, such as social cooperatives and entrepreneurial associations. The figure below shows the social employment share by country.

Figure 17: Employment in the social economy sector



Source: Social economy and social entrepreneurship Social Europe guide- Volume 4- Directorate-General for Employment, Social Affairs and Inclusion- March 2013

In Bulgaria, social enterprises are not well developed and information on the existing companies is scarce. In the Bulgarian legislation there is no concrete definition of a social enterprise. The social economy and social

[25] It is very difficult to come by accurate data on the social economy and the organisations that compose it, partly due to the lack of standardisation of the organisation types across countries and partly due to the scant attention that statistical offices have traditionally paid to these types of entities. Still, the most recent estimates enable a first analysis of its makeup.

entrepreneurship are relatively new concepts in Bulgaria, but in April 2012 a national social economy concept was adopted with a framework document to support the development of the social economy[26].

According to the MoLSP website, the objectives of the concept are:

1. To enable introduction of indicators for identification of Social Economy entities;
2. To serve as a source of norms, supporting SE-development and helping stakeholders to widespread and apply the spirit of social economy.
3. To be a ground for streamlining legal and administrative environment for development of SE-entities

The application of the present Concept is expected to identify possible legislation and institutional gaps and provide a basis for legal proposals but its successful implementation depends to a significant extend on the role of the Government for the legal recognition of Social Economy entities under the valid national legislation

Social economy in Bulgaria is mostly expressed through Co-operatives, associations and foundations. There are almost 2,000 co-operatives and they are employing at least 50% of people with disabilities. There are around 9,000 associations and foundations and these are becoming more entrepreneurial and developing social enterprise models in employment and welfare service provision. The main challenges currently focus on improving the support and training for social enterprise, promoting social entrepreneurship and improving the context for the creation of jobs and work integration. However it has to be noted that according to the official definition of social enterprise there are only 126[27] registered specialised enterprises, which are enterprises with employ between 20% to 50% employees with disabilities.

According to a recent research comparison between the Bulgarian social enterprise sector and the one in the province Baden-Württemberg in Germany[28], most social enterprises in Bulgaria are municipal entities delivering social services. Only few of all social enterprises are collaborating among themselves or with a specific network in relation to their activity. As per the same source, only 18% of social enterprises employ 100% of people in vulnerable groups, and 27% employ none. Furthermore, merely 3% of social enterprises have between 31 to 100 employees belonging to vulnerable groups, and 32% employ between 6 and 10 people from these groups.

The table below shows the percentage of social enterprises by area of business and the percentage of social enterprises that provide employment to people of vulnerable groups in their relevant area of business.

Table 8: Percentage of existing social enterprises by areas of business

Area of Business	Percentage social enterprises providing services in the respective area of business in Bulgaria	Percentage social enterprises providing employment to people of vulnerable groups in the respective area of business in Bulgaria
Social services	85%	82%
Health	3%	3%
Education and training	65%	62%
Employment of people with disabilities	38%	21%

[26] http://seconomy.mlsp.government.bg/en/page.php?c=1&d=54
The National Social Economy Concept ("the Concept") is an expression of the political involvement of the Government institutions of Bulgaria for creation of favourable environment for development of social economy models and practices.
[27] http://ahu.mlsp.government.bg/portal/se.
[28] Results from the research of the social entrepreneurship in Bulgaria compared to the province Baden-Wьrttemberg in Germany, conducted by the Centre for sustainable social development, contracted by the Ministry of labour and social policy, 2014

Manufacturing and trade	6%	6%
Consulting	18%	12%
Informational or prevention campaigns	6%	3%
Other	2%	4%

Source: Results from the research of the social entrepreneurship in Bulgaria compared to the province Baden-Wurttemberg in Germany, conducted by the Centre for sustainable social development, contracted by the Ministry of labour and social policy, 2014

In terms of sources of funding for the social economy in Bulgaria[29], funds come primarily from EU funds, then donations, municipalities, the state and lastly in the form of income generated by the enterprise itself. In comparison according to SELUSI data[30], the main source of funds for social enterprises in Romania and Hungary is grant finance followed by sales and/or fees and private donations, while in the UK, Sweden and Spain the primary source of capital is sales, followed by grant finance and investor capital.

Focusing on the primary source of social enterprise funding in Bulgaria – EU funds, the Ministry of Labour and social policy[31] has declared that in 2013, 32 projects from programmes dedicated to social entrepreneurship were approved and the disbursed grants have amounted to BGN 541,000. For the previous programing period 2007-2013, the OP financed three programmes that were directly related to social enterprises and social entrepreneurship[32]:

Table 9: Programmes supporting social initiatives during the 2007-2013 programming period

Name of the programme	Enterprises created	Employment created	Financing
Social entrepreneurship - popularization and support for a social enterprises - pilot phase	29 new created 10 old supported	3,612	8,017,057
New opportunities	35 new created	181	4,425,637
Chance for all	5 specialises enterprises 2 co-operatives		545,864

Source: Monthly bulletin of Ministry of Labour July 2013

The average amount of grant size which is usually around 95% of the total project volume during the last programming period was 140,000 Euros and for this specific segment, only grants were used to support the social economy

In conclusion, the main challenges currently facing the Bulgarian social economy are improving the support and training for social enterprise, promoting social entrepreneurship and improving the context for the creation of jobs and work integration. In that respect, the following problem areas should therefore be tackled in order to spur development in the sector:

- Lack of visibility – lack of awareness and recognition of the social value that is generated by the sector
- Lack of specialised training and education with the respective networks and infrastructure – disadvantage that the social economy organisations have in comparison to conventional businesses
- Demand of financing by social enterprises

[29] Research conducted by the Centre for sustainable social development, contracted by the Ministry of labour and social policy, 2014
[30] SELUSI data (research project funded through the 7th Framework Programme of the European Commission). Further information: www.selusi.eu.
[31] http://www.mlsp.government.bg/bg/news/news.asp?newsid=3492&catid=1.
[32] Source: http://seconomy.mlsp.government.bg/upload/docs/2013-07//Buletin_1.pdf.

4.5. Overview of sensitive social groups

The HRD OP has defined specific target groups for its priority axes as mentioned in previous section. These target groups are:

- Unemployed people;
- People at risk of poverty and socially excluded;
- People with disabilities; and
- The Roma population.

4.5.1. Unemployed people and poverty

Growth of employment and poverty reduction are two of the most prominent headlines targets of Europe 2020. In Bulgaria, the employment target rate for 2020 has been set at 76% of the target population aged 20-64, with the latest figure (2012) at 63%. Year 2000 saw the peak of unemployment in Bulgaria within the timeframe reported by Eurostat (55.3% of those aged 20-64), with a slow upward trend since then until 2012. Yet, 12.5% of the target population in Bulgaria lived in households with very low work intensity in 2012, compared to the equivalent year EU-28 average of 10.4%, with 7.4% for Romania, and 8.2% for the EU 12 New Member States . Importantly, this trend has grown over 2009-2012, from 6.9% to 12.5%, respectively.

As unemployment and poverty often go hand in hand, it is perhaps not surprising to see that Bulgaria is, again, among the EU countries with the highest rate of material deprivation caused by a lack of resources (44.1%, 2012), compared to the estimated 9.9% for EU-28, with 29.9% for Romania, and 19.7% for the EU 12 New Member States (all data for 2012). Historically, and once again, material deprivation in Bulgaria affected almost 60% of the population over 2006-7, and fluctuated from 44.1% to 45.7% within the time series of 2008-12.

As seen from the table below, the number of unemployed people in cities (in the second quarter of 2014) is over twice as high as the same number in villages in absolute number. However, the unemployment rate in villages is 16.2% as compared to 10% in cities (Q2 2014): representing the percentage of unemployed people from all individuals of the labour force.

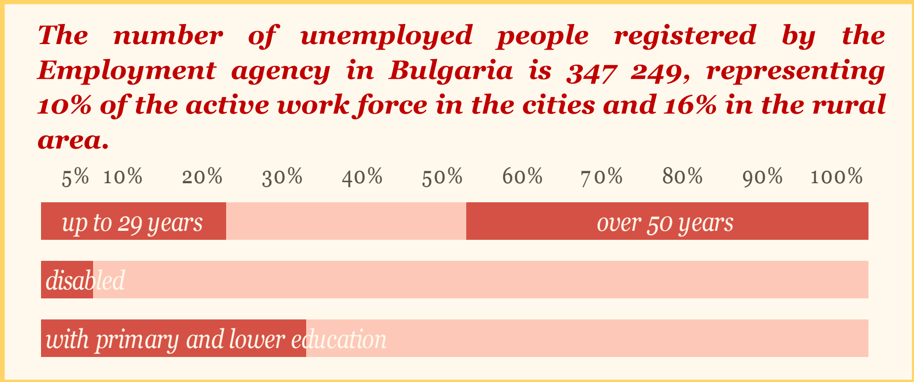
Table 10: Unemployed and rates of unemployment of the population of 15 or over years of age as of Q2 of 2014

	Unemployed people ('000)	*Unemployment rate (%)*
In cities	263.6	10.0%
In villages	118.1	16.2%

Source: NSI, 2014.

As of 2011, the rate of unemployment for residents of 15 or over years of age was highest in Shumen (26.6%), followed by Smolyan (21.9%) and Razgrad (21.4%), while Stara Zagora (7.1%) and Sofia-capital (7.3%) have the lowest rates (IME, 2014). The current number of unemployed people registered by the Employment agency represents 11% of the active work force. The highest percentage is among the young people (up to 29 years) and above 50 years. More than 30% of the work force has primary, elementary or lower education.

Figure 18: Overview of unemployed people in Bulgaria



Source: Employment Agency, July 2014.

Table 11: Unemployed and rates of unemployment by gender, age and education as of Q2 of 2014

	Population ('000)	*Share (%)*
	By sex	
Male	224.0	12.4%
Female	157.8	10.1%
	By age	
15-24	47.0	23.3%
25-34	95.5	12.5%
35-44	92.3	9.8%
45-54	77.4	9.4%
55 and over	69.6	11.1%
	By level of education	
Higher	51.8	5.2%
Secondary	204.7	10.8%
Secondary with an acquired professional qualification	126.1	10.2%
Primary	96.1	24.8%
Elementary and lower	29.2	40.7%
Total	**381.8**	**11.4%**

Source: NSI, 2014.

Only around 90% of the unemployed population in Bulgaria is registered with the National Employment Agency. Around the country there are 98 employment centres of the National Employment Agency and the data shows that 40% of the total unemployed population contact the governmental employment desks during the process of job seeking.

Figure 19: Unemployed people in the population segment of 15 years or over as of May 2014

	May 2013	May 2014
People registered at the employment agency	386,625	367,499
Newly registered	24,552	28,357
Newly registered 15-24	4,157	3,319
Newly registered 25-29	8,437	6,926
Found employment	-	27,626
Disadvantaged groups		
Young unemployed 15-24	33,018	27,881
Young unemployed 24-29	71,163	62,320
Disabled unemployed	-	17,744

Source: Employment agency monthly bulletin for May 2014. http://www.az.government.bg/bg/stats/view/2/123.

Youth unemployment - According to the latest data form Eurostat for the Q1 2014 the level of youth unemployment (up to 24 years) is 28.3% and Bulgaria holds the 8th place in the list of 15 countries with rate over the average for the EU-28. The highest level is still recorded in Greece (56.8%), Spain (54.1%), Croatia (49.0%), Cyprus (43.2%), Italy (42.8%), Portugal (35.0%) and Slovakia (32.5%), and the lowest – in Germany (7.9%), Austria (9.8%), the Netherlands (11.3%) and Denmark (13.0%). Compared to the same period in 2013 the level of youth unemployment has increased with 0.7 percentages.

The ethnic minority of the Roma people has been among those most severely affected by poverty and unemployment. While suffering extreme levels of social exclusion, with high illiteracy rates, and approximately 80% of them living in “segregated neighbourhoods”, the unemployment rate among the Roma hovers around 100% in Bulgaria, according to a recent press report[33].

4.5.2. People at risk of poverty or socially excluded

In the Eurostat news release 184/2013 dated December 5, 2013, the estimation of the population at risk of poverty or social exclusion in the EU28, amounts 125 million persons in 2012, which is a quarter of the overall population.

The highest shares have been recorded in:

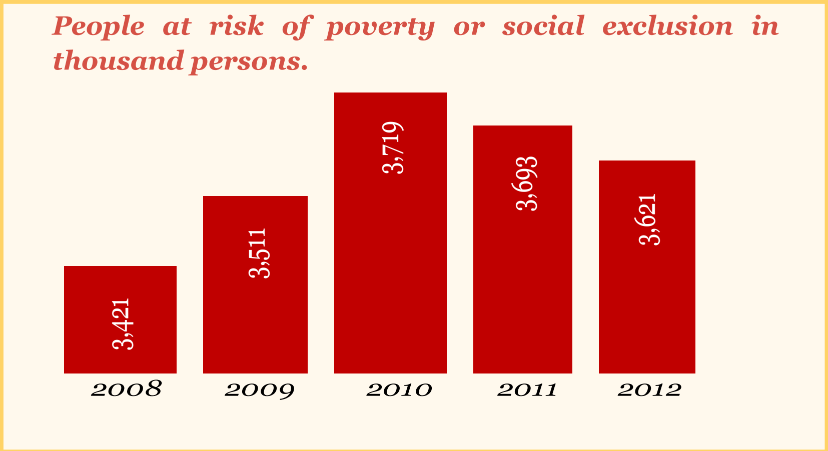
- Bulgaria (49%)
- Romania (42%)
- Latvia (37%) and
- Greece (35%)

These data are based on the EU-SILC survey. These figures include people at risk of poverty, persons severely materially deprived and persons aged 0-59 living in households with very low work intensity. In Bulgaria, Eurostat[34] gives the below data regarding the group of people under risk at poverty or social excluded.

[33] Bildung, Bildung, Bildung?, Roma in Südosteuropa, Michael Martens, , Frankfurter Allgemeine, Politik, 07.01.2014: http://www.faz.net/aktuell/politik/ausland/europa/roma-in-suedosteuropa-bildung-bildung-bildung-12739724.html.

[34] http://epp.eurostat.ec.europa.eu/tgm/refreshTableAction.do?tab=table&plugin=0&pcode=t2020_50&language=en

Figure 20: Overview of the people at risk of poverty in Bulgaria



Source: EUROSTAT news release Dec, 5 2013 - at risk of poverty or social exclusion at EU-28

The estimate from Eurostat in 2012 for Bulgaria is:

- 21.2% Persons at risk of poverty
- 44.1% Persons severely materially deprived
- 12.4% Persons aged 0-59 with very low work activity
- 49.3% (or 3.6 m) falling under one of the three criteria (at risk of poverty or social exclusion)

4.5.3. People with disabilities

Concerning people with disabilities, the total number of women is higher than the one of men – 483.5 thousand compared to 394.8 thousand. From the total number of women, 40.35% are employed, compared to 43.95% for men. At the same time, the rate of unemployment with respect to females with disabilities is smaller (5.67%) than the one for males (7.98%). In Bulgaria the people with disabilities amount of 878,000 people of which 8% are in the age group 15-24 years old. Of the total number of the people with disabilities 6.7% (or 59,000) are registered as unemployed actively looking for employment.

Figure 21: Unemployed disabled people in the labour force – May 2014 in absolute number

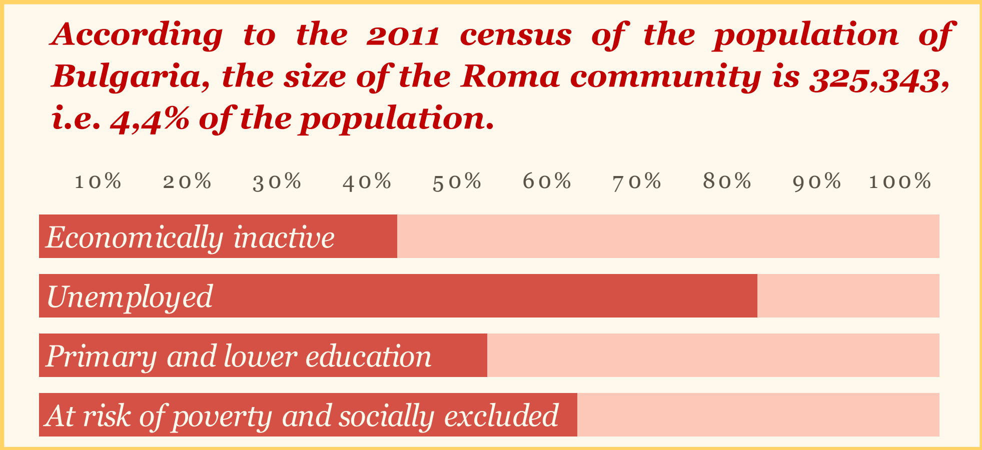
	Population
Women	8,695
Young up to 29	1,153
Over 50 years old	10,522
With no education or qualification	7,257
With primary and lower education	5,838
Total number of disabled people	**17,744**

Source: Employment agency monthly bulletin for May 2014. http://www.az.government.bg/bg/stats/view/2/123.

4.5.3.1. The Roma community

The last census performed in 2011 shows that the total of Roma Community amounts to 325,343 i.e. 4.4% of the population but this figure seems not to reflect the real number. The Council of Europe provides an average estimate of 750.000 persons[35]. Among those which have been registered and declared themselves as belonging to the Roma community, the employment agency has given the following distribution:

Figure 22: Overview of the Roma community in Bulgaria



Source: 2011 census/ HRD OP p70 – National Employment Agency

4.6. Summary of market environment

Bulgaria has proved to be resilient to the crisis and the recovery process, following the 2009 downturn has been slow but stable. The reform process has been mostly based of fiscal consolidation but several other factors still need to be addressed and improved in order for the Bulgarian economy to gain in competitiveness. The political instability is still a destabilizing factor for the economy also affecting the implementation of social policies. In summarising the present chapter the following points are highlighted:

- Unemployment rates are high in Bulgaria and persistent. This implies a high need to create new employment opportunities through business creation and entrepreneurship
- The labour cost in Bulgaria is competitive, however skills still need to be improved to link higher education with the actual needs of the business
- Employment rates in Bulgaria are relatively low, thus implying that high rates of people are excluded from employment due to lack of skills that need to be addressed.
- People with disabilities have difficulties accessing the job market as well as minority groups
- Social economy in Bulgaria is underdeveloped and needs to be supported

35 http://ec.europa.eu/justice/discrimination/files/roma_implement_strategies2014_en.pdf.

5. Existing Financial Instruments and lessons learnt

This chapter aims at presenting the Financial Instruments that were or still are available in the Bulgarian market in recent years and the lessons learned from the use of these FIs. During the 2007-2013 programming period Bulgaria implemented FIs in SME financing, urban development and energy efficiency. The present report focuses on the FIs addressing the groups targeted in the HRD Operational Programmes for both 2007-2013 and 2014-2020. The Operational Programme for “Human Resources Development” for the 2007-2013 programming period proposed only grants to support the OP’s target groups. However, the target groups identified in the HRD OP as envisaged beneficiaries of Financial Instruments for the 2014-2020 programming period (detailed in Chapter 3) may have access to the existing Financial Instruments and mostly those in the area of SME financing. For instance, these Financial Instruments that are potentially available to SMEs from various sectors and sizes could be also available to micro-enterprises working in the social economy sector. In order to provide an overview of the use of FIs that could be relevant to the priorities and target groups of the HRD OP, the present chapter presents the grants provided in the last programming period, existing FIs that could be relevant, and the lessons learned from the use of these FIs.

5.1. Grants for the target groups of HRD OP

The HRD OP for 2007-2013 was focusing on increasing the quality of life of the Bulgarian population, improving the access to education and lifelong learning of the population and increasing the investment in social capital (social and health services). This OP was a pilot programme using ESF funding. In light of the low level of maturity of the social economy in Bulgaria, a choice was made to use exclusively grants to finance the OP’s priorities.

As no FI has been used over the 2007-2013 programming period, the grant schemes used to address the priorities are presented in the following paragraph. A table indicating the grants with the respective active and completed projects is also presented in Annex 7.

The HRD OP for the 2007-2013 programming period aimed at setting the ground for a sustainable social economy sector. It was meant to promote the involvement of economically inactive persons in the labour market and to facilitate the social inclusion of people belonging to disadvantaged and vulnerable groups. For the purpose of the analysis the grant schemes used in the HRD OP for 2007-2013 have been reviewed and are presented in the table below. A distinction is made between the grants that were used during the previous period and would still be in the scope of the HRD OP for 2014-2020 (Priority Axes 1 and 5) and the grants that would now be under the scope of the Operational Programme focusing on education and managed by the Ministry of Education (previously Priority Axes 3 and 4 under HRD OP for 2007-2013).

Table 12: Grants distributed under the HRD OP for the 2007-2013 programming period

	Amount (EUR)	*Share (%)*
Grants distributed (and still relevant to HRD OP 2014-2020)	**813,114,539**	**65%**
Not active projects	*87,271,450*	*7%*
Still in action	*725,843,089*	*58%*
Grants distributed (not relevant to HRD OP anymore)[36]	**436,993,047**	**35%**

Source: Ministry of Labour and Social Policy, 2014.

In the table below, some relevant grant schemes are presented.

Table 13: Grants distributed per priority axis

Priority axis / Programme	Activity	Total amount disbursed
Priority Axis 1: Promotion of economic activity and development of inclusive labour market		
Promotion of project commence for development of self-dependent economic activity-component 1	helping young entrepreneurs to start a business	6,001,916
Promotion of project commence for development of self-dependent economic activity-component 3		2,556,459
Promotion of project commence for development of self-dependent economic activity-component 2		11,056,091
Priority Axis 5 Social inclusion and promotion of social economy		
Social entrepreneurship - popularization and support for a social enterprise - pilot phase	29 social enterprises are created and 10 are further supported. Employment for 3612 persons is created	8,017,056
New opportunities	35 social enterprises are created and 181 persons are employed	4,425,636
Chance for all	5 specialises enterprises and 2 co-operatives employing people with disabilities	545,864
TOTAL		**32,603,025**

Source: Ministry of Labour and Social Policy, 2014.

The above priority axes from the previous programming period are close to the priority axis 1 & 2 of the new programming period and are focusing on social inclusion. The target groups are similar and the programmes launched are designed to answer to the needs of self-entrepreneurs and the development of the social economy. It has to be noted however that the absorption of funds allocated to grant schemes in the last programming period was low and several deficiencies were observed in the implementation process. Further insight will be provided in the section about lessons learned.

[36] Priority Axes 3 and 4 are no more relevant for the HRD OP for the 2014-2020 programming period since they are now under the management of the Ministry of Education.

5.2. Financial Instruments

The use of FIs has been increasingly promoted in the EU over the last 10 years, and especially in the last programming period several EU countries chose to design and implement FIs in the areas mentioned above. European institutions such as the European Investment Fund (EIF) and the European Investment Bank (EIB) designed specific policies such as JEREMIE and JESSICA in order to provide simplified procedures and know-how, for Member States to use their allocated European funds into FIs. Other international organisations such as the European Bank for Reconstruction and Development (EBRD) also implemented FIs to support the financing of specific policy areas.

Overall, a strong momentum for the use of FIs was generated in the last programming period. However, absorption rates varied between countries. In order to improve the performance of FIs and the accuracy of set targets but also the relevance of proposed structures with the environment and needs of each country, new regulation has been introduced in the EU as mentioned previously. In the next programming period, countries willing to implement FIs will have to prepare Ex-ante assessments such as the present report.

Financial Instruments including microfinance, debt, guarantee, Private Equity and Venture Capital facilities have been designed and implemented in Bulgaria during the current programming period by the EIF, the EIB, the EBRD and the National Guarantee Fund. It has to be noted again that these FIs mostly concern companies; however they are also relevant to social inclusion, business creation and entrepreneurship which are relevant to HRD OP, and thus should be described.

5.2.1. The European Investment Fund

JEREMIE Holding Fund is a fund-of-funds managed by the EIF and funded by the OP "Competitiveness" in priority axis 3. Below are the products within this initiative.

The First Loss Portfolio Guarantee (FLPG) product is implemented through five commercial banks and aims at reducing the risk for banks and subsequently also collateral requirements for SMEs. This is the most successful financial engineering product in Bulgaria so far as it was well targeted in terms of covering the existing, realistic needs of SMEs and especially of micro-enterprises. The average collateralisation rate of SMEs which receive loans remains below 50%. In addition, guarantees are typically high leverage products, allowing for large disbursements with fewer available funds. For the FLPG product, a total leverage of 1:5 has been achieved. The programme has already supported more than 4,400 SMEs and still has available funds. Overall around 60% of companies supported by the product are micro-companies and many of those would not have had access to bank financing without the guarantee.

The Portfolio Risk Sharing Loan product aims to provide - through seven commercial banks - investment loans to SME applicants with interest rates reduced in half compared to the market practices. This product primarily aims at reducing the cost of loans for SMEs since 50% of each loan is financed by JEREMIE funding at 0% cost with the balance funded through the bank at market rate, thus respectively reducing the interest rates by at least 50% on the entire loan. The leverage for this programme is 1:2 with an initial budget of EUR 200m and a total commitment by banks reaching EUR 400m. The product has already supported more than 1,200 SMEs. Nonetheless in contrast to FLPG which mainly supports micro-companies, the risk sharing loan is a product which has collateral requirements and is thus favouring small and medium companies to a larger extent (almost 60% of supported companies).

The Venture Capital Fund is managed by NEVEQ which has experience in the Bulgarian VC market, having been the sole VC fund in the country in recent years. The aim of the fund is to support early stage high technology companies, able to demonstrate market leadership capacity and scalability beyond their domestic market. The fund focuses on information technology, biotechnology, green energy and other sectors with high growth potential.

The Acceleration and Seed Funds have allocated EUR 21m to two fund managers namely Eleven and LAUNCHub for supporting the commercialisation and internationalisation efforts of start-ups.

The Mezzanine Capital Fund is co-financed by the JEREMIE Holding Fund with EUR 30m while another EUR 30m will be raised from institutional and private investors (EBRD, the Black Sea Trade and Development Bank and other private investors). The mezzanine fund provides mezzanine financing for growth and expansion, export orientation and capital restructurings in the Bulgarian lower mid-market, across a wide range of sectors.

The Co-Investment Fund has been launched in 2014. The aim of the fund will be to support companies in growth stages with potential internationalization of their activities through a EUR 40m commitment (50% from JEREMIE, 50% from private investors).

The EIF is also supporting the liquidity of financial intermediaries providing loans and guarantees to SMEs through the **Competitiveness and Innovation Framework Programme (CIP)** and **Progress Microfinance** facilities. These are directly negotiated and financed by the EIF following a due diligence process with each financial intermediary. More specifically, under CIP, the EIF provides guarantees to Raiffeisen bank for loans earmarked for SMEs. Discussions were held recently with the National Guarantee Fund for a possible cooperation under CIP but they have concluded without results. The EIF has also financed three financial intermediaries (through structured loans) under Progress (including the Bulgarian Development Bank's subsidiary JOBS MFI[37]) in order to facilitate access to finance for sensitive social groups such as recently unemployed people or small family businesses.

5.2.2. The European Investment Bank

The EIB is also providing direct financing to financial intermediaries for the provision of debt products to SMEs. Currently the EIB is cooperating with eight financial intermediaries from the private sector which, in turn, are providing loans and leasing products to SMEs. Like the EIF, the EIB has the opportunity to lend to financial intermediaries with more competitive rates than the interbank money markets.

Overall between 2008 and 2012, the EIB financed Bulgarian intermediaries with EUR 660m, while between 2011 and 2013 eight intermediaries have received credit lines up to EUR 370m for SME loans[38].

5.2.3. The European Bank for Reconstruction and Development

Since Bulgaria's transition period, the EBRD has been one of the largest indirect investors in the country's infrastructure projects. In this respect, the bank has also provided liquidity through loans to several financial intermediaries for the support of SMEs. More specifically, 24% of EBRD's financing is targeted at financial institutions[39] for the provision of loans to SMEs. Since 2011, 7 financial intermediaries have received EUR 245m (according to interviews and research in Banks websites).

[37] The Bulgarian Development Bank has prepared a new Strategy for the period 2014-2019 that is now under approval by the Government as owner of the Bank. The Strategy foresees the transformation of the Bulgarian Development Bank into a fully-fledged development institution and includes the full acquisition of the JOBS Micro-Financing Institution.

[38] http://www.eib.org/projects/loans/regions/european-union/bg.htm.

[39] http://www.ebrd.com/downloads/research/factsheets/bulgaria.pdf.

5.2.4. The National Guarantee Fund

The National Guarantee Fund (NGF) provides guarantees to financial intermediaries. In fact, NGF is the only state owned national institution implementing FIs to support Bulgarian SMEs companies in their efforts to improve their access to finance.

The initial guarantee scheme of the Fund was launched in 2008 and was backed up by the facility's own capital with the purpose to provide guarantees to start-ups and existing companies with 50% coverage of loan exposure. Guarantees were provided both for working capital (41% of portfolio) and investment loans (56% of portfolio) with an average portfolio's guarantee maturity at 44 months[40].

The Fund's total volume[41] of guarantees and counter-guarantees amounts to EUR 57.4m which have supported 4,200 companies. Currently, NGF's portfolio of guarantees backed by own capital is only amortising, since its funds were fully absorbed by the 11 commercial banks contracted as financial intermediaries.

The National Guarantee Fund recently attempted to launch a new guarantee scheme. A call for banks was held concerning a guarantee scheme funded by CIP which would have generated a total commitment of EUR 30.7m, but the scheme was abandoned due to a lack of interest from banks to participate. During interviews, stakeholders raised concerns about the efficiency of NGF mostly due to a complicated guarantee approval procedure imposed by the fund which hinders the implementation process. These procedures are considered lengthy and bureaucratic by the banks due to a second round of approval (following the loan approval by the bank) necessary to provide the guarantee. In contrast to NGF the EIF's FLPG has supported more than twice the number of SMEs in two years demonstrating that banks are willing to provide guaranteed loans if procedures are transparent and products are set to complement the normal activity of a bank.

The Fund also provides guarantees to SMEs in the agricultural sector and in fishery with funds from the respective operational programmes. These guarantees are provided to SMEs which are eligible and have been approved to receive grants from other programmes. Nonetheless both the delays linked to grant programmes and the problems related to the NGF have been causing a slow implementation of these programmes. Currently, only 230 companies have been supported with average guarantees of EUR 230,000.

5.2.5. Microfinance in Bulgaria

Microfinance in Bulgaria will be elaborated in the supply side analysis. However, it has to be noted in the present chapter that microfinance has been provided in Bulgaria through commercial banks and specialized institutions such as JOBS MFI (which is also financed by the EIF under the Progress facility). Microfinance in Europe is a Financial Instrument that is necessary to implement social policies either to target business creation or social exclusion in general. For instance microfinance can be used to finance socially excluded people in order to them to support their mobility and help them have access to employment, or improve their skills.

Unfortunately, the implementation of microfinance in Bulgaria is a market failure since, these instruments are mainly provided under banking conditions, with collateral and high interest rates. As a result, microfinance is perceived in the market as a banking product rather than a socially oriented instrument. The main reason for this is the lack of specialized institutions that would truly target sensitive social groups and create a social impact.

All these schemes are listed in Table 14 below.

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[40] Source: NGF management report for 2012 as part of the Fund's financial statements.

[41] AECM, 31/12/12. http://www.aecm.eu.

Table 14: Existing financial instruments in Bulgaria

	Institution	Source of Funding	Scheme	Product Name	Product Type	Financial Intermediary	Initial Budget (mEUR)	Leverage by Intermediary (mEUR)	Total Available Funds (mEUR)	Disbursement (mEUR)	Targeted type of SMEs	Number of SMEs supported	Start Date
1	EIF	Structural Funds	JEREMIE	First Loss Portfolio Guarantee	Guarantee	CIBANK	60.1	71	71	51.0	SMEs	4.400	Q3/2011
						Procredit		40	40	40.0			
						Raffeisen		65	65	63.0			
						Unicredit		50	50	49.7			
						United Bulgarian Bank		75	75	73.3			
						Sub-total	**60.1**	**301**	**301**	**277.2**			
2	EIF	Structural Funds/EBRD/Black Sea Trade and Development Bank/Private Investors	JEREMIE	Mezzanine	Mezzanine	Bulgarian Mezzanine Capital	30	30 (From private investors)	60	-	Established companies with export orientation,, stable cash flows		2014
						Sub-total	**30**	**30**	**60**	-			
3	EIF	Structural Funds	JEREMIE	Portfolio Risk Sharing	Loans	Societe Generale Expressbank	30	30	60	20.1	SMEs	1.254	Q1/2013
						Procredit	50	50	100	30.2			
						Raffeisen	20	20	40	10.4			
						Unicredit	25	25	50	42.2			
						FIB	50	50	100	50.2			
						DSK	20	20	40	8.6			
						Allianz Bank	15	15	30	8.5			
						Sub-total	**200**	**200**	**400**	**131.6**			
4	EIF	Structural Funds	JEREMIE	Acceleration and Seed Funds	Equity	Eleven	21	120.000		3.0	Young & innovative companies in the ICT, TMT and engineering sectors;	90	Q4/2012
						LaunchHub		90.000		2.0			
						Sub-total	**21**	**0.2**	**21.2**	5.0			
5	EIF	Structural Funds	JEREMIE	Co-Investment	Equity	**Fund Manager(s) selected**	**20**	**20**	**40**	-	Growing SMEs		2014
6	EIF	Structural Funds	JEREMIE	Venture Capital	Equity	NEVEQ (II)	**21**	**9**	**30**	-	Early stage SMEs		2013
7	EIF	EIF	CIP	SMEG	Guarantee	National Guarantee Fund	(30.7)	Cancelled due to lack of interest from banks			SMEs		-
						Raffeisen1	-	18	18	3.2	Micro		16/03/09
						Raffeisen2	-	18	18	11.3	SMEs		16/03/09
						Sub-total	**-**	**36**		**14.5**			
8	EIF	EIF	Progress	Progress	Loans	Mikrofond	3				SMEs, micro & start-ups with emphasis on		Feb 2011
						Jobs MFI-Bulg. Dev. Bank	6	3	9				Sept 2011

						Societe Generale Expressbank	8				areas with high unemployment.		
						Sub-total	17						
9	EIB	EIB	EIB SME Loans	EIB SME Loans	Loans and Leasing	Societe Generale Expressbank	100				SMEs		25/06/ 2013
						Unicredit Bulbank	60						17/12/ 2012
						Allianz Bank	30						18/10/2012
						Raiffeisen	50						19/12/2011
						UC Leasing	50						16/05/ 2013
						Sub-total	**290**						
10	EIB	EIB	EIB SME Loans	SME Finance Facility	Loans	Sogelease	10				SMEs		28/12/ 2011
						Procredit	20				SMEs		27/04/ 2011
						CIBANK	50				SMEs including agricultural		26/09/ 2013
						Sub-total	**80**						
11	Bulgarian Development Bank/ National Guarantee Fund	National Guarantee Fund	Guarantees for SMEs	Guarantee	Guarantee	Unicredit DSK UBB Raiffeisen FIB SG ExpressBank Pireaus CiBank MKB Unionbank Allianz Bank International Asset Bank	41	57.4	57.4	57.4	Micro + SMEs	1471	2008-2013
12	Bulgarian Development Bank/National Guarantee Fund	National Guarantee Fund	NGF Guarantees for Fisheries under OP Development of Fishing Sector	NGF Guarantees for Fisheries	Guarantee	First Investment Bank Raiffeisen CiBank Unicredit Central Cooperative Bank (CKB)	15	5	20	9	Micro + SMEs grant beneficiaries under OP in Fishing sector	18	2012-2015
13	Bulgarian Development Bank/National Guarantee Fund	National Guarantee Fund	NGF Guarantees for Agricultural sector under Rural Development OP	NGF Guarantees for Agricultural sector	Guarantee	DSK Bank Pireaus Bank BG-American UBB (United BG Bank) Raiffeisen Bank CiBank Central Cooperative Bank (CKB) Eurobank BG (Postbank) Piraeus	121	605	726	45	Micro + SMEs grant beneficiaries under OP in Agricultural sector	213	2013-2015
14	EBRD	EBRD	Partnership for Growth	EBRD Loans	Loans and Leasing	Sogelease	10	5	15	5	SMEs	64	30/04/2013
						Societe Generale	75	n/a	n/a	n/a		n/a	n/a

programme	Express Bank							
	Raiffeisen	10	n/a	n/a	n/a		n/a	n/a
	Raiffeisen Leasing	20	n/a	n/a	n/a		n/a	11/05/2011
	Sub-total	**95**	n/a	n/a	n/a			
	Sub-total	**150**	n/a	n/a	n/a			

Source: Multiple sources, PwC analysis, 2014[42]*-.*

[42] PwC analysis, EIF, EIB, NGF, Banks, AECM. SME access to finance analysis

5.3. Lessons learnt from the use of Grants and Financial Instruments

As already mentioned, on the one hand the implementation of grant schemes in the last programming period proved to be slow and insufficient while, on the other hand, the use of FIs remained limited, and although the existing FIs contributed in increasing awareness for this form of financing, their impact remained weak in the market. Some lessons learned from the use of grants and FIs are outlined below.

Lessons learned from the use of grants:

- The design, evaluation, selection and control procedures of grant programmes involves a large and multi-level group of stakeholders causing confusion and delays in the implementation;
- The stakeholders are national authorities and state-owned companies with limited knowledge of the market. This often leads to unsustainable project plans being approved for a grant but later rejected by a bank for further financing;
- The discussion on the involvement of the private sector in the evaluation procedures is currently not taking place;
- The private sector is involved only through private consultants supporting potential beneficiaries (mostly SMEs) in the preparation of the application procedure. The fees of consultants are often covered by the grant but this market is poorly regulated and often a source of corruption. Some consultants, who might not have the business or technical expertise to produce quality work, require down payments and fail to deliver services. In other cases the cooperation is based on false expectations from the consultant by the beneficiary rather than on the quality of the services;
- Beneficiaries (mainly SMEs) have difficulties securing financing for the non-subsidised part of their business plan. Often projects which have been approved by the evaluating authority are later rejected by banks for further financing for being non-marketable projects.

Lessons learned from the use of FIs:

- In the last programming period, the equity related FIs managed to stimulate a new market in Bulgaria, also motivating business angel investors and other institutional investors to finance business projects.
- The microfinance segment and especially the existing Microfinance institutions were not sufficiently supported by public interventions.
- Social inclusion FIs were not sufficiently implemented, while their scope remains limited to business creation and does not support other areas such as mobility and social microfinance.
- In the last programming period FIs did not focus on improving people skills and mentoring.
- Financial intermediaries, capable of implementing FIs are only limited to banks and some MFIs but more specialized institutions and funds with social objectives are missing.
- Existing specialized institutions such as Microfinance institutions, proved in recent years to operate more closely to what is expected from commercial banks.

A SWOT analysis table is provided below to illustrate lessons learned from the use of FIs in Bulgaria.

Table 15: SWOT analysis of existing FIs

	Strengths	Weaknesses	Opportunities	Threats
All FIs	• Willingness of the State to implement FIs in Bulgaria	• Weak institutional framework related to PPPs and equity investment that are relevant to the use of FIs • Heavy administrative burden related to the disbursement of EU funds	• New programming period • High demand for financing • Positive prospects for sectors such as tourism, social enterprises and micro enterprises	• Low absorption of EU funds • Political instability • Reluctance of banks to finance projects (too risky) • Limited financial information for beneficiaries • Limited awareness of the use of FIs
JEREMIE	• Know how provided by the EIF • Flexibility, less administrative burden; • Efficient management provided by the JEREMIE Holding Fund and the fund managers selected for the equity instruments.	• Late start causing still insufficient absorption rate • Limited experience in the country in equity investments • Insufficient capacity of the market to absorb the funds efficiently	• Build on the experience acquired from the last programming period • Network of commercial banks	• Reluctance of banks to finance projects (too risky) • Limited financial information of potential beneficiaries
National Guarantee Fund	• Experience in the market and in the implementation of guarantees	• Reluctance of banks to use the provided guarantees • Limited scope of the existing guarantee instruments, they remain generic	• High number of people unable to provided collateral and in need of guarantee	• Administrative burden related to the procedures; • Political instability
EBRD	• Strong local and international experience; • Credibility of an international institution; • Attractive for commercial banks; • Existing programmes to support SMEs		• Opportunity to build on accumulated experience in the use of FIs	• Political instability • Reluctance of banks to finance projects (too risky) • Limited financial information for beneficiaries

EIB	• Strong international experience; • Credibility of an international institution • Attractive for commercial banks;	• Limited presence in Bulgaria in terms of public projects and SMEs support compared to other IFIs	• Opportunity to build on accumulated experience ;	• Political instability • Reluctance of banks to finance projects (too risky) • Limited financial information for beneficiaries

Source: PwC, analysis 2014

5.4. Good practices in other countries

Social Economy

France:

According to the Discussion paper Peer Review on Social Economy, France 2012[43], the first important point mentioned is that the social economy in France is highly developed and well supported. It represents about 10% of GDP, 10% of employment, and over 13% of private employment.

This level is directly linked to the fact that it is well supported by the government within the policy framework thus higher level strategies are being developed in line with EU policy. Nevertheless, still the sector faces challenges such as knowledge, recognition, generational renewal of staff, securing an appropriate legislative and financial framework and of course funding mechanism.

The French social economy is exemplary in many ways thanks to well-established institutions and policy frameworks. The concept of co-governance on policy matters proves to be a good system delivering excellent strategies and policies, with the active collaboration between local/regional government and the social economy stakeholders.

Since 2009, social companies have benefitted from the status of "social and solidarity company"[44] offering preferential access to public procurement, including investment funds for social projects and social innovation facilities of Bpifrance; the national public investment bank.

- **Bpifrance** is a public investment bank created in 2013. It results from the merge of three institutions ("OSEO", "CDC Entreprises" and "Fonds Stratégique d'Investissement – Régions") and is funded by the "Caisse des Dépôts" (for 50%) and the French government (for 50%). It is responsible for supporting SMEs and innovative businesses. In so doing, Bpifrance has developed a multitude of products and intends to be more and more active in the financing of the social economy sector. In terms of financial support to the social economy sector, the actors that later merged into Bpifrance disbursed EUR 95m of loans, bank guarantees and innovation aid to social economy companies in 2012. For the future, Bpifrance reiterates its commitment to social economy, introducing new instruments and products dedicated to the sector.

  Below envisaged Financial Instruments and products of Bpifrance for the social economy sector:

Instrument	Product	Target	Estimated capacity (mEUR)	Comments
Fund-of-funds	Equity and quasi-equity		50 - 100	
Debt instrument	"Prêt participatif social et solidaire" (PPSS)		Several dozen	
Guarantee	Bank loan guarantee	Associations		Initiative of Bpifrance and SOGAMA Crédit Associatif
Social Innovation Fund	Repayable advance	Socially innovative projects		In cooperation with the State, CDC and regional authorities
Crowdfunding website	Facilitates provision of loans, donations and equity			

[43] ec.europa.eu/social/BlobServlet?docId=9636

[44] Following the conditions of the recognition defined in the decree n°2009-304 of 18 March 2009 applicable to solidarity enterprises governed by the Article L.3332-17-1 of the Employment Code.

- **ADIE** was created in 1989 and was originally funded by public and private institutions. Nowadays, ADIE continues to be financed by a large number of private and public sources. Since ADIE is an association and does not have a banking license, it can borrow funds for lending only thanks to an authorisation given by the Prudential Control Authority ("Autorité de Contrôle Prudentiel" - ACP). This authorisation defines the maximum loan amounts that can be provided. This authorization allows ADIE to provide loans to SMEs through commercial banks.

  ADIE is the only national microfinance provider that is legally authorised to be refinanced by the banks. Overall, ADIE is the most active non-bank provider of micro-loans in France, having disbursed nearly 11,000 micro-loans to companies by the end of 2012, with the total loans outstanding of EUR 58m.
  ADIE provides three types of micro-loans:
  - Personal micro-loans;
  - Professional micro-loans; and
  - Interest-free loans.

- **NEF** is a cooperative bank established in 1988. Loans provided by NEF usually finance initiatives in the social economy. The financed projects aim to support the creation and development of professional activities with potential social and environmental benefits.

  NEF offers two types of products:
  - Professional loans;
  - Solidarity loans ("crédit solidaire").

Czech Republic:
The social economy and social entrepreneurship has some recognition in government policy documents. Most of the existing social enterprises are concerned with work integration of people with disabilities and disadvantaged groups. They are gradually orienting their activities towards market income generation to ensure their sustainability.

Hungary:
The concept of social economy is not well established but it is emerging within the employment policy dialogue.

In 2009, the government launched a social land programme covering 10 counties, 44 rural areas, and in 194 settlements. The target was to address the most disadvantageous areas and half of the beneficiaries reached were from Roma community.

The innovative solutions proposed through different schemes made them successfully as they were also sustainable.

As a practice it should be noted that the laws regarding the taxation have been arranged for the third sector and some examples of rules mentioned below might be considered as good practices to support the social economy[45]:

- Tax exemption of the social enterprises of participants which has followed such programme.
- Tax benefits for supporters and users of services provided by social enterprises.
- Income related to social services is subject to taxation if it does not exceed 10% of the overall income of the company.
- Several discounts laid down in different laws such as law on personal income tax

Microfinance and micro-guarantee

Microfinance institution's best mission is to be a sustainable institution providing financial services to the lowest-income entrepreneurs so they can create jobs or be self-employed, build assets and improve their

[45] Study : National+report+on+social+economy+sector+in+Hungary 2010 – Innovative social enterprises development network and SouthEast Europe, transnational cooperation programme

standard of living and to the disadvantaged groups excluded from the labour market. The target groups are mainly entrepreneurs or micro-enterprises lacking access to finance from the classic banking system.

The goal of microfinance institutions is to give unemployed or low income individuals or groups an opportunity to become self-sufficient by providing access to finance, a means of saving money, borrowing money and insurance.

France:

- **ADIE**

Personal microloans

ADIE provides personal micro-loans to unemployed people. These loans (called personal microcredit for employment) concern amounts up to EUR 3,000 and target to finance expenses which are mostly linked to mobility in order for people to have access to employment or to maintain a job. These personal micro-loans cover a very wide scope of unemployed people or people on the verge of unemployment and exclusion. Since 2009, ADIE provided 463 personal micro-loans amounting to more than EUR 917m.

Professional micro-loans

ADIE provides professional micro-loans up to the maximum amount of EUR 10,000. These micro-loans are addressed at two target groups which cannot benefit from commercial banking:

- Unemployed and/or people at risk of poverty who are willing to create their own business as a mean of economic and social integration;
- Existing micro-enterprises which want to develop.

Most of the beneficiaries belong to the first group. The second group usually includes companies that have already been supported by ADIE at the start-up stage.

Interest-free loans

ADIE provides two types of interest-free loans: “prêts d’honneur” (considered by commercial banks as quasi-equity financing) and interest-free loans, funded at the national level (NACRE loans). These two products are loans with no interest rate and do not require collateral. Hence, they can be considered a repayable grant.

- **France Active**

France Active is also an association that covers all the area of France and acts regionally through local branches. Similarly to ADIE, France Active is funded primarily by public funds (up to 75% in 2012). More specifically, France Active is financed by the CDC, the French national government through the Social Cohesion Fund, private investors and the EU (for 1% in France).

The main products provided by France Active are guarantee schemes that help newly created companies and entrepreneurs to access commercial bank financing. Among these guarantee schemes, there are:

- The France Active Guarantee (FAG) is financed by national resources and aims to facilitate access to bank loans to finance working capital needs of micro-enterprises.
- The Guarantee Fund for Women’s Businesses’ Creation, Transfer and Development is financed from national resources and aims at financing working capital needs or investments by companies managed by women (excluding lease).

- **Réseau Entreprendre (RE)**

The “Réseau Entreprendre” is a network of company owners who provide mentoring to the aspiring entrepreneurs who wish to create SMEs or re-launch them. The RE consists of 47 associations which form a

network financially supported by the CDC and the French local administration[46]. In 2012, other contributors included the European Social Fund, the Ministry of Economy, commercial banks and private investors.
The Réseau Entreprendre is another provider of the "prêts d'honneur" in the amounts ranging from EUR 10,000 to EUR 50,000.

In France there are interactions between the main actors mentioned above; Annex 11 presents a table with the sources of funding for main institutions involved in the microfinance market and/or the financing of the social economy sector in France.

In addition to Bpifrance and the microfinance providers, French regions have Regional Unions of Cooperative Companies (URSCOP) which propose Financial Instruments to the local social economy sector.

Sardinia – Financial Instruments using ESF funding over the 2007-2013 programming period

- **ESF Micro-credit Fund** has been established in 2009 with EUR 65.5m from the ESF regional Operational Programme, in order to promote social inclusion and cohesion by facilitating access to credit by disadvantaged individuals and women for the creation and development of micro-enterprises and 0 employee enterprises. The instrument supports individuals with difficulties in accessing traditional credit channels and who want to start up a new business or intend to invest on expansion of initiatives already existing.

The products provided by ESF Micro-credit Funds have the following characteristics:
- Micro-credit loans of maximum EUR 25,000;
- The loans are reimbursable at zero-rate and without guarantees;
- Pay-back are based on a monthly basis with no interest, except for delays; and
- The pay-back period is of 5 years with a 6 or 12 month grace period.

The Fund also support tutoring activities provided to the funded enterprises.

The Fund Manager is a publicly-owned company[47]. It is in charge of the following main activities:
1. To target the investment and planning strategy;
2. To select beneficiaries through public calls for projects;
3. To manage the Instrument portfolio of projects;
4. To monitor and control the funding transferred to beneficiaries; and
5. To inform the ESF Managing Authority on the implementation progress of the Financial Engineering Instrument.

The essential part of SFIRS SpA's activities is carried out with the Managing Authority (i.e. the Labour Department of the Sardinia Region).

Over the implementation of the Financial Engineering Instruments, the main difficulties encountered are related to:
- The lack of experience of the applicants with Financial Instruments and project submission in general; but this issue has been resolved by creating a single dedicated e-mail address to receive doubts and requests regarding the procedure
- Insufficient communication and networking activities to ensure an adequate awareness of the instrument among all potential beneficiaries but this has been solved by intensifying the support

[46] Referred to as "Conseils Généraux" in France, i.e. regional governments and administration at department level.
[47] The Sardinia Region has selected SFIRS SpA as Fund Manager of the ESF Micro-credit Fund, in coherence with Art. 44 of General Regulation and Art. 43 of Implementing Regulation. SFIRS is a financial institution, in house provider, acting for 45 years in the development and support of Sardinian enterprises. SFIRS is responsible for the evaluation of applicants' projects and for the monitoring and control of the financed projects.

offered by territorial contact points of the Fund Manager to the SMEs (and so potential beneficiaries of the instrument).

As of October 2014, out of the EUR 65.5m, EUR 11.4m remain available. The expected number of SMEs which could be beneficiaries is of 2,600 enterprises

- **PISL-POIC ESF Fund** aims at supporting enterprises and promote entrepreneurship in depopulated small urban. The Fund received EUR 50.3m from the ESF 2007-2013 Operational Programme and comprises two operations:
- The PISL operation ("*Progetti Integrati di Sviluppo Locale*": Integrated Projects for Local Development) which provides reimbursable incentives (through micro-loans) for the requalification of municipalities' areas or assets (for municipalities with less than 3,000 inhabitants)
- The POIC operation ("*Progetti Operativi per l'Imprenditorialità Comunale*": Operational Projects for Municipal Entrepreneurship) which provides a combination of reimbursable incentives (micro-loans) with local tax exemption

The Fund provides micro-credit loans of up to EUR 25,000 with no interest rate.
As of October 2014, out of the EUR 50.6m, EUR 35.5m remain available. The Fund expects to address 198 municipalities and 1,650 enterprises.

- **ESF Fund for inclusive finance.** The Fund[48] provides direct guarantees and counter-guarantees to disadvantaged beneficiaries unable to directly access any form of guarantee in order to support the financing of investments and other financial operations. The objectives are:
- To encourage business creation by disadvantaged people, improving their ability to access credit;
- To strengthen the guarantees offered by the traditional credit system;
- To help SMEs facing credit crunch by strengthening guarantees offered to companies;
- To encourage the financial intermediaries operating in Sardinia to develop alternative lending instruments; and
- To promote access to grants for beneficiaries of the ESF 2007-2013 Operational Programme.

The Fund received EUR 5m from the ESF 2007-2013 programming programme and as of October 2014, the total funding of EUR 5m remains available. It is expected to cover 125 enterprises for the end of the 2007-2013 programming period.

[48] The ESF Fund for inclusive finance was implemented thanks to the Regional Council Deliberation n°46/26 of November 21st, 2012.

6. Analysis of market failures, suboptimal investment situations and investments needs

This chapter provides analysis of the market failures and suboptimal investment situations based on the analysis of the potential demand and existing supply for financing expressed by the four target groups identified in the HRD OP for 2014-2020.

In order to reach specific conclusions on the market failures, different methodologies have been used to quantify demand and supply, to the extent possible. The aim of this exercise is to demonstrate the existence of suboptimal investment situations in the form of financing gaps. The quantification will provide a picture of the existence of such gaps, however due to the fact that several assumptions have been made, the gaps will not be demonstrated in a numerical manner but will instead be based on a qualitative analysis. The methodologies used for the quantifications will be described in the sections below.

6.1. Analysis of the demand

The demand analysis will provide an indication of the qualitative and quantitative aspects of demand for support through FIs that will complement the supply-side analysis conducted in the next section and contribute towards the identification of a financing gap as well as of the market failures. Ultimately this analysis will provide the elements with which to develop meaningful recommendations in the proposed investment guidelines.

Before it is possible to proceed to the analysis of demand for financial support through FIs in the coming 2014-2020 programming period, it is necessary to translate the policy objectives of the OP into differentiable target groups. This was done through the analysis of the HRD OP for 2014-2020 conducted in Chapter 3. The four target groups identified previously that may benefit from Financial Instruments under the HRD OP for 2014-2020 are:

- Socially excluded people and people at risk of poverty willing to create a business;
- Employees at risk of unemployment working in newly created enterprises and social enterprises;
- People needing training to create their company or to remain in their current job position;
- People starting or developing a cooperative and/or a social enterprise.

Based on these target groups, different final recipients of a potential intervention scheme have been defined. These final recipients correspond to the entities (individuals or companies) that seek and receive finance from financial institutions to achieve their objectives. Two large groups may then be identified: on the one hand, individuals who seek financing for their own development and companies which seek financing to develop their activity or support their employees. The final recipients that will be analysed in the following paragraphs are presented in the table below.

Table 16: Final recipients for the demand analysis of access to finance under HRD OP

	Description
Socially excluded persons or individuals at risk of poverty	• Individuals needing financing for a training in view of creating a company or obtaining a new job
	• Individuals needing financing to create a company
	• Individuals needing financing to find a job
Enterprises	• Micro-enterprises needing financing (to finance a training for their employees, working capital or other forms of investment)
	• Training centres
	• Social enterprises

Source: PwC.

With the above-mentioned final recipients identified, an analysis is conducted in order to demonstrate the demand for support via FIs. This analysis is based on the available indicators for the different final recipients and the interviews conducted with the key stakeholders. The demand for financing calculated in the following paragraphs may include overlaps between the different populations and therefore should primarily be considered as an indication of the financing needed by the final recipients identified.

The methodology used to quantify demand and the analysis of the potential demand expressed by these final recipients is analysed in the following paragraphs.

6.1.1. Methodology to quantify demand

As previously mentioned, the methodology to quantify demand is based on two sets of information: indicators and interviews. The methodology consisted of the following steps:

1. The population composing each final recipient is estimated based on macroeconomic indicators, specific indicators (for instance sector specific indicators for the social economy) and stakeholders estimates indicated during the interviews;
2. Each population is considered stable and would compose the annual population to consider for each recipient composing the demand-side;
3. When feasible, an annual amount of financing to be sought by a single entity composing a target group is estimated (e.g. a training centre or a social enterprise);
4. The total population of each target group is multiplied by the annual amount estimated for one single entity composing this population. The figure obtained by this final calculation constitutes the potential demand for financing to be annually sought by the considered final recipient.

When different sources of information are available, they are used to propose more detailed analysis and ranges for the demand for financing of a specific final recipient.

The rational of the computations that are provided in the following sections is to present an estimate of potential demand of financing for the main groups of potential recipients of a public intervention scheme. In order to provide such an estimate, the methodologies use proxies in order to define a realistic population of these recipients. Proxies are rates that have been obtained by different sources (reports or surveys) that are relevant to the populations under consideration. These computations are providing an estimate based on assumptions deriving from these proxies and should be treated as such. The estimates of demand presented are estimates of financing that should be financed by the private sector and not necessarily by an FI or a public intervention scheme.

The detailed analysis of each final recipient identified for the HRD OP is provided in the following paragraphs.

6.1.2. Individuals needing financing for a training in view of creating a company or obtaining a new job

Among the different target groups addressed by the HRD OP, the largest population is composed of the people at risk of poverty and social exclusion who are away from the labour market and would need to receive training either to create their company or to obtain the job they seek. They are detailed in the HRD OP for 2014-2020 as:

- Young people under 29 years old not enrolled in the educational system and needing training;
- Self-employed people needing training to create or develop their company; and
- Social entrepreneurs needing training.

As discussed during the interviews, this type of need is currently not financed by banks or MFIs since it is considered as an activity that does not generate revenues and that should be covered by grants.

The methodology followed to calculate the demand for financing for training from this population includes 3 steps:

1. Take the population (P) size of people who are statistically qualified as being at risk of poverty or social exclusion in Bulgaria (i.e. low-income households, socially and/or financially excluded).
2. Multiply (P) by proxy (PR)-1.4% of the unemployed persons in the age group 25-64-to obtain the number of potential people who may look for a training (PLFT)
3. Multiply (PLFT) by an average price for a training in Bulgaria (PT).

The product of step 3 is the potential demand for financing for training from people at risk of poverty or social exclusion in Bulgaria.

Following this methodology and based on the most recent statistical and financial market data available in the country, the demand for such financing was calculated:

1. Bulgarian population at risk of poverty in the age-group 25-64 = 1,859,000[49].
2. 1.4% of the unemployed persons in the age group 25-64 participate in education and training in Bulgaria[50]; corresponding to 26,026 people.
3. The average price for training in Bulgaria is EUR 450[51].
4. The total potential demand for financing from people at risk of poverty and social exclusion needing financing for a training is thus:

1,859,000 x 1.4% x EUR 450 = **EUR 11,711,700**

The estimated potential demand figure above represents the total amount of financing that could be needed by people at risk of poverty and socially excluded to finance training in order to create a company or obtain a job in Bulgaria. This represents about 26,026 people in Bulgaria who would need EUR 11,711,700.

49 People at risk of poverty or social exclusion by age and sex, Eurostat, 2014. Year used: 2012. http://epp.eurostat.ec.europa.eu/statistics_explained/index.php/People_at_risk_of_poverty_or_social_exclusion, http://appsso.eurostat.ec.europa.eu/nui/submitViewTableAction.do , age 25-49 together with age 50-64

50 Participation rate in education and training by type, sex, age, and labour status. For formal and non-formal education and training. All genders. From 25 to 64 years old. For unemployed persons. Year used: 2012. Last update: 21.07.2014. Accessed on 16.09.2014. The assumption is that the participation rate for unemplyed persons and for people at risk of poverty and social exclusion are similar, which is likely since people at risk of poverty are often unemployed.

51 http://www.mediapool.bg/dopalnitelni-78-mln-lv-za-obucheniya-po-shemata-az-moga-poveche-news219171.html.

6.1.3. Individuals needing financing to create a company

This second set of final recipients is composed of various stakeholders unemployed or at risk of poverty and/or socially excluded and willing to develop their own activity to lift out of poverty. They are detailed in the HRD OP for 2014-2020:

- Young inactive or unemployed people up to 29 years old;
- People willing to start a business and be self-employed;
- Social entrepreneurs;
- Disadvantaged people, such as people in marginalised communities; and
- People with disabilities.

Demand for financing from this population is to be understood as funding for social inclusion, i.e. people at risk of poverty or socially excluded who are potential business creators if better supported in their access to finance. As discussed during the interviews with representatives of financial institutions and representatives of minorities, these stakeholders have a very difficult access to financing because commercial banks consider their projects to be non-bankable and no specific financial institutions currently provide the micro-loans or micro-guarantees that these potential entrepreneurs might need to start their business.

Financial exclusion is defined as "*a process whereby people encounter difficulties accessing and/or using financial services and products in the mainstream market that are appropriate to their needs and enable them to lead a normal social life in the society in which they belong*"[52]. When applied to enterprises, this definition covers self-employed people creating their business to escape poverty as well as nearly bankable micro-enterprises, such as young companies and newly created micro-enterprises without a sufficient track record or without relationships with financial institutions. Other categories of entrepreneurs in this situation may be young inactive people, disadvantaged people and people with disabilities.

As underlined in Chapter 4, Bulgaria has a high level of unemployment (13%) and a large part of its population is considered at risk of poverty (49%).

Following this, demand for financing from this population is important. Similar to the first set of final recipients, the methodology used to compute the potential demand for financing for social inclusion is first presented. The calculation is then presented in detail. Moreover, 29% of the Bulgarian respondents to the 2012 Flash Eurobarometer explain that they do not regard self-employment as feasible on the grounds that they do not have enough capital or financial resources. This proportion is higher than the EU average of 21%[53]. Considering that the Flash Eurobarometer is not exclusively using answers from people at risk of poverty or socially excluded, and that these people tend to have worse access to finance than the rest of the population, access to finance is consequently one of the main reasons why people at risk of poverty or socially excluded are not able to develop their activity and become self-employed. This situation is even more pronounced in Bulgaria as compared to the EU average.

The calculation of the demand for social inclusion follows the methodology used in the SME Access to Finance Market Assessment conducted by the European Investment Fund in 2014[54]. It derives from an EC paper issued in 2007 and includes 4 steps:

1. Take the population (P) size of people who are statistically qualified as being at risk of poverty in Bulgaria (i.e. low-income households, socially and/or financially excluded).

52 European Commission (2008), *Financial services provision and prevention of financial exclusion*, Directorate-General for Employment, Social Affairs and Equal Opportunities Inclusion, Social Policy Aspects of Migration, Streamlining of Social Policies.

53 The 2012 Flash Euro Barometer, http://ec.europa.eu/enterprise/policies/sme/facts-figures-analysis/eurobarometer/

54 European Investment Fund (2014). SME Access to Finance Market Assessment for Bulgaria.

2. Multiply (P) by proxy PR-1% to obtain the number of potential micro-business creators (PMBC).
3. Multiply (PMBC) by proxy PR-2%[55] to obtain the number of people who might start a business (SB) if they had better access to finance.
4. Multiply (SB) by an average loan size in a given country/region, i.e. Bulgaria.

The result of step 4 is the potential demand for financing for social inclusion in Bulgaria.

That methodology was adapted to the current socio-economic conditions in Bulgaria, based on the most recent statistical and financial market data available:

1. Bulgarian population at risk of poverty in the age-group 25-64 = 1,859,000[56].
2. 49% of respondents in Bulgaria declared that if they could choose between different kinds of jobs, they would prefer to be self-employed[57].
3. 12% of respondents declared that it would be very feasible for them to become self-employed within the next five years[58].
4. The average micro-loan in Bulgaria is EUR 2,696[59].
5. The total potential demand for financing from potential business creators is thus:

1,859,000 x 49% x 12% x EUR 2,696 = **EUR 294,697,603**

The estimated potential demand figure above represents the total amount of financing that could be needed to facilitate access to finance for the people at risk of poverty or socially excluded who see themselves as self-employed potential business creators in Bulgaria. This represents about 109,309 people in Bulgaria who would need EUR 294,697,603 to create their own company and escape poverty.

A more detailed view of two populations within this target group is possible:

- Young unemployed people under 29 years old; and
- Socially excluded people and members of minorities, and more specifically members of the Roma minority.

According to the OECD and Eurostat[60], 4% of the young people (below 29 years old) are willing to start a business in Bulgaria. Considering that 75,313 people below 29 years old are currently unemployed in Bulgaria (NSI, Q1 2014), the estimated number of young unemployed people willing to start a business is:

75,313 x 4% = 3,012

This calculation indicates that 3,012 Bulgarian young people below 29 years old would be interested in creating their own business to escape poverty.

As already mentioned, the Roma community in Bulgaria is composed of 325,343 persons (NSI, 2011 census). Among this population, between 60% and 70% of them are at risk of poverty or socially excluded according to the employment agency. For calculation purposes, an average number of 65% will be used. If considering that

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55 Proxies PR-1% and PR-2% are to be adapted to the Bulgarian macro-economic environment.

56 People at risk of poverty or social exclusion by age and sex, Eurostat, 2014. http://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=ilc_peps01&lang=en

57 Entrepreneurship in the EU and Beyond, Country Report, Bulgaria, Fieldwork June 2012, Flash Eurobarometer 354, p.2, op. cit.

58 Ibid (Institute for Business & Industry Development), p.4.

59 The value of an average micro-loan was computed by taking the 2013 values of the gross loan portfolios of the most active microfinance providers (MFIs) in Bulgaria, i.e. Mikrofond, USTOI and Nachala, and dividing them by the number of the borrowers in each: i.e. Gross loan portfolio of the three MFIs = EUR 5,419m / Number of borrowers in the three MFIs = 2,010 = Average loan value disbursed = EUR 2,696. This figure is broadly in line with the average microloan-size that can be derived from the responses to the latest EMN survey. EMN, Overview of the microcredit sector in the European Union, December 2012: http://www.european-microfinance.org/docs/emn_publications/policy_notes/3.PN%20_Dec_2012.pdf and http://www.european-microfinance.org/index.php?rub=publications&pg=emn-policy-notes&spg=overview-microcredit.

60 Entrepreneurship at a Glance 2013, a product of the OECD-Eurostat Entrepreneurship Indicators Programme.

the Roma community has the same characteristics as the entire Bulgarian population with regards to business creation and self-employment, 49% of the people among the Roma community would prefer to be self-employed and 12% would consider that it would be feasible to become self-employed in the next five years. Following this, the estimated number of people within the Roma community at risk of poverty willing to start a business is:

325,343 x 65% x 49% x 12% = 12,435

This calculation indicates that 12,435 people belonging to the Roma community in Bulgaria would be interested in creating their own business to escape poverty.

6.1.4. Individuals needing financing to find a job

This third set of final recipients (and last set related to individuals) corresponds to the individuals who need financing for job searching. This financing aims at covering expenses which are mostly linked to mobility in order for people to have access to employment.

In the European Union, such financing is commonly named personal micro-loans. These micro-loans are not directly linked to the creation of a company or the support of self-employment but aim at reducing unemployment and consequently need to be considered in the scope of the HRD OP. As discussed during the interviews, commercial banks and MFIs today do not provide such financing in Bulgaria since both financial institutions tend to require between 6 and 12 months of business activities when deciding to finance an activity.

Similar to the first two sets of final recipients, the methodology used to compute the potential demand for financing for personal micro-loans is first presented. The calculation is then detailed.

The methodology followed to calculate the demand for such financing includes 2 steps:

1. Take the population (P) size of unemployed people seeking work but not immediately available in Bulgaria.
2. Multiply (P) by an average micro-loan size in Bulgaria.

The product of step 2 is the potential demand for financing from individually needing micro-loans to have a better access to the labour market in Bulgaria.

Following this methodology and based on the most recent statistical and financial market data available in the country, the demand for such financing was calculated:

1. Bulgarian unemployed population seeking work but not immediately available = 25,300[61].
2. The average micro-loan in Bulgaria is EUR 2,696[62].
3. The total potential demand for financing from individuals seeking finance to find a job is thus:

25,300 x EUR 2,696 = **EUR 68,208,800**

The estimated figure above represents the total potential demand for personal micro-loans in Bulgaria. It concerns about 25,300 people in the country who would need in total EUR 68,208,800.

61 Supplementary indicators to unemployment by sex and age groups. Persons seeking work but not immediately available. All genders. From 25 to 74 years old. Eurostat, Year used: 2013. The assumption is that individuals seeking personnal micro-loans are unemployed, seeking work and not immediately availbale because of lack of mobility.

62 The same average loan as for social inclusion is used as proxy. This is also close to personal micro-loans disbursed in other Member States: between 2,5000 and 3,000 in France for instance.

6.1.5. Micro-enterprises needing financing to finance a training for their employees

This fourth set of final recipients (and first set related to companies) corresponds to micro-enterprises that need financing to provide training to their employees or pay for it in order to adapt their workforce to a changing economic environment. These employees may be at risk of unemployment if they do not improve their skills. They are detailed in the HRD OP for 2014-2020 as employees in micro-enterprises that will benefit from this specific OP.

These employees are to date employed by companies – including social enterprises - that may face temporary difficulties in the future, notably due to difficulties in accessing finance. Interviews with stakeholders have revealed that financial institutions are often reluctant to finance enterprises so as to maintain employees and labour force during temporary difficulties, despite the fact that the situation of the company may positively evolve in the coming months. Maintaining these employees would however help the enterprises to cope with new clients and new orders when the temporary difficult times are over. A financing scheme aiming at supporting enterprises in maintaining their labour force during temporary difficulties – and especially newly created micro-enterprises which are the most at risk– would have a positive impact on employment and would help the companies to cope with growth and development. That is why an estimate of the financing needed by these micro-enterprises would provide insight on the amount that the latter would need to maintain their workforce.

The methodology used to calculate the demand for such financing includes 7 steps:

1. Take the number of micro-enterprises in Bulgaria (N).
2. Consider only the active micro-enterprises in Bulgaria (aN).
3. Take the number of employees in micro-enterprises in Bulgaria (NE).
4. Calculate the average number of employees in active micro-enterprises in Bulgaria by dividing NE by aN to obtain (aNE).
5. Multiply (aN) by proxy (PR) to obtain the number of active micro-enterprises providing any form of training (T)[63].
6. Multiply (aNE) by (T) to obtain the average number of employees that may receive training from their micro-enterprise (aNE-T).
7. Multiply (aNE-T) by an average price for a training in Bulgaria (PT).

The product of step 7 is the potential demand for financing from Bulgarian micro-enterprises willing to provide training to their employees in order to increase their skills and employability.

Following this methodology and based on the most recent statistical and financial market data available in the country, the demand for such financing was calculated:

1. Number of micro-enterprises in Bulgaria = 342,934[64].
2. According to the stakeholders interviewed the number of active micro-enterprises can be considered half of those registered by NSI, corresponding to 171,567.
3. Number of employees in micro-enterprises in Bulgaria = 568,383[65].
4. The average number of employees in active micro-enterprises in Bulgaria is 3.3.

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63 Supplementary indicators to unemployment by sex and age groups. Persons seeking work but not immediately available. All genders. From 25 to 74 years old. Eurostat, Year used: 2013. The assumption is that individuals seeking personnal micro-loans are unemployed, seeking work and not immediately availbale because of lack of mobility.

64 NSI, 2014.

65 NSI, 2014. The number of employees working in micro-enterprises is not revised as the number of micro-enterprises since no element from the interviews supported that this number had to be changed.

5. On average 29% of enterprises in Bulgaria provide any type of forms of continuing vocational training. A proxy of the number of active micro-enterprises providing any form of training is 49,725[66].
6. The average number of employees that may receive training from their micro-enterprise is 164,831.
7. The average price for training in Bulgaria is EUR 450[67].
8. The total potential demand for financing from micro-enterprises to provide training to their employees is thus:

$$[568{,}383 / (342{,}934 \times 50\%)] \times (342{,}934 \times 50\% \times 29\%) \times \text{EUR } 450 = \textbf{EUR 74,173,982}$$

The estimated figure above indicates the potential demand for financing from micro-enterprises to finance training to their employees. It concerns about 164,831 employees and 49,725 micro-enterprises which would need in total EUR 74,173,982.

Part of this financing is to be used to incentivise the micro-enterprises and provide them with financial support to develop their training and propose these to their employees. Indeed, developing an internal training is time-consuming and resource intensive, due to the wide spectrum of training needs and may not be immediately rewarded. However, no financing support currently exists to support companies developing and proposing training to their employees. Only the larger companies may consequently propose these trainings, while the majority of the enterprises in Bulgaria are micro-enterprises that require employees with multi-skills. That is why some incentives – including financial incentives – may consequently be needed to lead these companies drafting the trainings and proposing them to their employees. This is even more important for micro-enterprises where a few employees may endorse different responsibilities that require various skills which may be provided only through training.

6.1.6. Training centres

The fifth set of final recipients includes the training centres that are meant to provide training to all types of population that might require it. They are detailed in the HRD OP for 2014-2020 as vocational training centres, education and training organisation and institutions, as well as information and professional guidance centres that provide counselling services and training on entrepreneurial, managerial and business skills. They would provide these services to potential self-employed entrepreneurs and employees.

As discussed during the interviews, these training centres may encounter difficulties in accessing finance to cover their working capital needs, since they may not always be profitable but provide high added value to the supported companies and employees as well as to the overall skill level of the labour force in the country. Training centres may also need financing to invest: renovate their infrastructure, buy furniture and equipment, and create another training centre for example. This would be valuable for the whole country. For instance, 9% of the people in Bulgaria feel they lack the skills to be self-employed. This is aligned with the EU average (8%) (Eurobarometer, 2012). Among the main potential beneficiaries of training centres are new self-employed people who decided to create their own job. They were 10,400 people in 2012 in Bulgaria (Employment agency, 2014). These new self-employed people are one of the main beneficiaries of the training centres. There are currently 910 licensed training centres in Bulgaria[68]. These training centres are currently financed by the revenues and profit generated by the fees paid by the trainees and provide added value to the country in terms of support to the entrepreneurial spirit, employability of employees, adaptability of the labour force and management skills. However, it has become clear during the interviews conducted and the desk research, that the training centres participate in the voucher scheme launched by the Employment Agency, due to delays in

66 Enterprises providing any form of training by form of training and size class. Any types of other forms of continuing vocational training (in comparison with continuing vocational training in work situation which was conducted by 21% of enterprises in Bulgaria). All size classes. Year used: 2010. Last update: 04.09.2014. Accessed on 16.09.2014. Since data for micro-enterprises only is not available, the assumption is that the proportion of micro-enterprises providing training is similar to the proportion of all class sizes of SMEs.

67 http://www.mediapool.bg/dopalnitelni-78-mln-lv-za-obucheniya-po-shemata-az-moga-poveche-news219171.html.

68 Navet, Training centre register.

the reimbursement of the vouchers, the majority of the training centres are suffering from short term working capital and liquidity deficit. The training centres in Bulgaria may therefore be considered as one of the beneficiaries of the public support provided by the HRD OP for 2014-2020 in view of improving the skills and employability of future entrepreneurs and employees.

In order to estimate the population that may address the training centres, only the most at risk people will be considered, in order to avoid at best overlapping with vocational training that existing micro-enterprises may decide to conduct internally.

The people at risk of poverty or socially excluded willing to receive training are consequently taken into consideration. A population of employees at risk is also taken into consideration. Employees working in newly created micro-enterprises will be considered as the most at risk of unemployment. As explained during the interviews, the most fragile micro-enterprises are the newly created companies which may encounter difficulties to remain sustainable during their first three years of business activity. Employees hired in newly created micro-enterprises may consequently be considered as the employees that may encounter risks of unemployment if the company encounter temporary difficulties and does not have the financial history to cope with these difficulties. The number of employees in the newly created enterprises in Bulgaria was 12,083 in 2012. Considering that 31% of employees are working in micro-enterprises in Bulgaria, the number of employees working in newly created micro-enterprises in Bulgaria was of 3,746 in 2012 (Employment agency, 2014). This population is to be considered as one of the populations that may benefit from the HRD OP for 2014-2020.

Another subgroup of employees at risk of unemployment could be the newly hired employees in micro-enterprises. No quantitative data on this subgroup is currently available in Bulgaria. These employees may however be considered as one of the main final beneficiaries of the public support provided by the HRD OP for 2014-2020.

Following this, the population of training participants that will be considered in the calculation will include:

- The people at risk of poverty or social excluded who may look for training in Bulgaria (estimate already computed in Section 6.1.2); and
- The employees in the most at risk enterprises which cannot conduct training internally. For these people a proxy will be considered: the employees working in newly created micro-enterprises.

Similar to the other set of final recipients, the methodology used to compute the potential demand for financing from training centres is first presented. The calculation is then detailed.

The methodology used to calculate the demand for such financing includes 5 steps:

1. Take the people at risk of poverty or social excluded who may look for training in Bulgaria (N1).
2. Take the number of employees working in newly created micro-enterprises in Bulgaria (N2)
3. Add up N1 and N2 to obtain the total population (TP)
4. Take the cost of continuing vocational training courses per participant in Bulgaria (C)
5. Multiply (TP) by an average price for a training in Bulgaria (C).

The product of step 5 is the potential demand for financing from training centres.

Following this methodology and based on the most recent statistical and financial market data available in the country, the demand for such financing was calculated:

1. Bulgarian population at risk of poverty in the age-group 25-64 who may look for training = 26,026[69].

[69] NSI, 2014. See Section 6.1.2.

2. Number of employees working in newly created micro-enterprises in Bulgaria = 3,746[70].
3. The total population that may need training is 29,772.
4. The cost of continuing vocational training courses per participant in Bulgaria is 425[71].
5. The total potential demand for financing from training centres is thus:

(26,026 + 3,746) x EUR 425 = **EUR 12,653,100**

The estimated figure above indicates the potential demand for financing from training centres to cover their internal costs. It concerns the 910 licensed training centres, in order to provide training to people at risk of poverty or at risk of unemployment (29,772 people) and would represent a total amount of EUR 12,653,100.

6.1.7. Social enterprises

The sixth set of final recipients corresponds to the social enterprises. They include the existing cooperatives and specialised enterprises in Bulgaria as well as the social entrepreneurs, who are people starting or developing a company in the social economy sphere or an NGO in the country.

As mentioned in Chapter 4, there are almost 2,000 cooperatives in the country. There are also 126[72] registered specialised enterprises which employ between 20% and 50% of employees with disabilities. In addition, there are about 9,000 associations, foundations and other form of structure providing social services and/or employing people from vulnerable groups and/or disabled in Bulgaria. Overall, about 11,126 entities may be considered as composing this set of final recipients. As discussed during the interviews, these entities are developing in number and propose more and more diverse services. They are also becoming more entrepreneurial and propose new models of governance. Interviews also revealed that all of them are not active. It is to be assumed that half of the associations are either inactive or do not need financing for their functioning since their activities do not require financing. Following this, the active population of social enterprises may be estimated at 6,626.

When considering interactions with other sets of final recipients, social enterprises are also meant to avoid people at risk of unemployment to lose their job. Indeed, a few social enterprises may encounter difficulties – including financial difficulties – that would force them to reduce their workforce. For that reason, social enterprises are meant to be supported by the HRD OP to develop the social economy sector in the country and help disabled and socially excluded people not to lose their job in a social enterprise. The HRD OP for 2014-2020 indicates that 3,681 people are employed in the social economy sphere.

Interviews revealed that companies and NGOs working in the social economy sphere may encounter difficulties to obtain finance. Up to date, social enterprises where financed via grants and obtained on average EUR 140,000, which represent about 95% of each project supported. The great majority of the social enterprises created in Bulgaria (93%) were created during the 2007-2013 programing period (mainly in 2011 and 2012). According to the Centre for sustainable social development, most of them were supported by grant schemes for their creation (Centre for sustainable social development, 2013). According to the stakeholders interviewed, social enterprises only marginally benefit from other financing sources. Indeed, when considering their access to finance, social enterprises often have only access to grant schemes and very limited access to commercial banks which consider their business as too risky because not-profit oriented. Banks are also not incentivised to finance the social economy sphere in Bulgaria.

70 Employment agency, 2014. The assumption is made that the distribution of employees per company size in newly created entreprises is similar to the proportion of employees per company size in the overall enterprise population.

71 CVTS, Continuing vocational training survey 2010. Statistics Finland. http://www.stat.fi/til/cvts/2010/03/cvts_2010_03_2013-10-03_en.pdf Since data for micro-enterprises only is not available, the assumption is that the cost for training centres that are micro-enterprises is very close to the proportion of all class sizes of SMEs.

72 See: http://ahu.mlsp.government.bg/portal/se.

Social enterprises however have financing needs that the available grant schemes may not always cover, as discussed with the stakeholders interviewed. Moreover, if social enterprises are not-profit oriented they may generate revenues that enable them to reimburse loans and develop relations with commercial banks to finance these revenues-generating activities. The use of debt products to finance social enterprises' activities is however not yet common, despite the fact that grants may not always be sufficient to finance the development of the social enterprises' activities. Social enterprises would use this financing to cover their internal costs and invest if needed: renovate their premises, acquire new equipment and/or expand by providing services in new locations.

Similar to the other final recipients, the methodology used to compute the potential demand for financing from social enterprises is presented first. The calculation is then explained.

The methodology used to calculate the demand for financing to be sought by social enterprises includes 4 steps:

1. Take the number of employees in social enterprises in Bulgaria (N).
2. Take the monthly average salary of an employee in a social enterprise in Bulgaria (maS).
3. Multiply (amS) by 12 to obtain an annual average salary for an employee in a social enterprise in Bulgaria (aaS)
4. Multiply (N) by (aaS).

The result of step 4 is the potential demand for financing from social enterprises.

Following this methodology and based on the most recent statistical and financial market data available in the country, the demand for such financing was calculated:

1. Number of employees in social enterprises in Bulgaria = 3,681[73].
2. Monthly average salary of an employee in a social enterprise in Bulgaria = EUR 200[74].
3. Then, the annual average salary for an employee in a social enterprise in Bulgaria is EUR 2,400.
4. The total potential demand for financing from social enterprises is thus:

3,681 x EUR 200 x 12 = **EUR 8,834,400**

The estimated figure above indicates the potential demand for financing from social enterprises to cover their human capital costs, which are their main costs. It is to be needed by the 6,626 social enterprises in order to cover their human capital costs for a total amount of EUR 8,834,400.

6.1.8. Overall demand from target groups under the OP Human Resources Development for 2014-2020

The paragraphs above have analysed the potential demand for funding from each of the final recipients identified in the HRD OP for 2014-2020 which may benefit from Financial Instruments. These final recipients correspond to the entities which may receive funding from the HRD OP. They may be companies or individuals.

The identified beneficiaries often face similar difficulties when seeking finance. The interviews with the stakeholders have underlined that the financial institutions consider these groups as too risky with regards to their standards. When considering the micro-enterprises and self-employed people, they are often newly created which leads them not to have available the collateral required by the financial institutions to access debt. They also have often very weak financial structures because they are under-capitalised and with very

73 HRD OP, 2014.

74 Bulgarian Ministry of Labour, website, 2014.

limited knowledge of the equity financing market and actors. Most of the time, they also lack financial history with the commercial banks. When considering the training centres and the social enterprises, since both of them do not have profit objectives, the financial institutions do not have incentives to finance them.

The table below details the population, financing needs and the estimated amount for financing for each final recipient detailed in the previous sections. As already mentioned, there is overlapping between the different sets of final recipients, that is a why a total potential demand for financing has not been computed.

Table 17: Estimation of potential demand per final recipient under HRD OP

	Final recipient	Population	Financing needs	Estimated amount (EUR)
Socially excluded persons or individuals at risk of poverty	Individuals needing financing for a training in view of creating a company or obtaining a new job	26,026 people	• Loan and/or grant to pay for training	11,711,700
	Individuals needing financing to create a company	109,309 people	• Business micro-loan to start a company	294,697,603
	Individuals needing financing to find a job	25,300 people	• Personal micro-loan for job-hunting	68,208,800
Enterprises	Micro-enterprises needing financing to finance a training for their employees	49,725 micro-enterprises	• Loan or grant to pay for training for employees	74,173,982
	Training centres	910 licensed training centres	• Cover working capital needs • Invest	12,653,100
	Social enterprises	6,626 social enterprises	• Cover working capital needs • Invest	8,834,400

Source: PwC.

The supply of financial products at the disposal of the identified final recipients is analysed in the following section.

6.2. Analysis of the supply

The supply-side analysis provides an overview of the current situation regarding the supply of financial products that are available to support the target groups identified in the HRD OP for the 2014-2020. In the sections below, first the methodology used to quantify supply will be presented. Then, the supply of financial products provided by the main financial institutions to the final recipients presented in the previous setion will be detailed. A quantification of supply of financing from each financial institution will be calculated. A summary of the supply side analysis will then conclude this section.

It is important to note that the supply analysis is constrained by the considerable amount of uncertainty in the Bulgarian financial sector. Interviews conducted with relevant stakeholders, including those from the commercial banking sector, revealed that these stakeholders were reluctant to provide figures for the current provision of financing and the anticipated supply of financing for the coming years. In light of these constraints, the methodologies and assumptions described in the ensuing section were used to provide a meaningful indication of supply.

As detailed in the previous section, the six final recipients identified in the HRD OP for 2014-2020 have financing needs that may be perceived as not covered by the products provided by the financial institutions. In order to assess to what extent the supply of financial products provided to these groups is able to answer their needs, an analysis of the financial products provided to the unemployed persons looking for a job, the micro-enterprises (including the self-employed people), the training centres and the social enterprises is conducted in the following section.

Two main types of financial institutions may be considered as potential suppliers of financing for these target groups: (1) commercial banks and (2) Microfinance Institutions (MFIs). Both markets are detailed in the following paragraphs, along with their provision of financing to the final recipients identified in the HRD OP for 2014-2020.

Overall, the legal framework of the Bulgarian financial market requires official licences from the Bulgarian National Bank (BNB) for any type of credit activities. As a result, only legally registered institutions can provide financial services. Following that, the supply of financial products to the target groups identified in the HRD OP for 2014-2020 is currently provided in Bulgaria by:

- 29 commercial banks including 6 branches of foreign banks; and
- 10 microfinance institutions (including JOBS MFI)

Both markets are detailed in the following paragraphs. A specific focus will be made on the provision of microcredit from these two financial institutions to the identified final recipients in the HRD OP for 2014-2020. As described by the European Commission, microcredit is recognised as an effective financing channel for job creation and social inclusion, and may be a mean to attenuate the adverse effects of the current financial crisis while contributing to entrepreneurship and economic growth in the EU[75]. Microcredit, defined as loans up to EUR 25,000 addresses two populations:

- Micro-enterprises, defined as enterprises employing up to 9 employees (0 to 9 employees included);
- Disadvantaged people (unemployed or inactive people, receiving social assistance, immigrants, marginalised people and people with special needs) who wish to become self-employed but do not have access to traditional banking services.

The supply of microcredit by commercial banks and MFIs is detailed in the following paragraphs. No data is however available at a detailed level for the different recipients identified in the HRD OP and the interviewed financial institutions were not able to determine or approximate this supply per final recipient or target groups.

6.2.1. Methodology used to quantify supply

As mentioned above, detailed figures from supply side actors were not available from which to quantify the potential supply of financing from the banking sector to the final recipient or target groups identified in the HRD OP. In order to develop the quantification of supply the following methodology was used:

1. First, an overview of the banking sector and the MFI sector are provided in order to provide qualitative information on the capacity or the willingness of banks to finance the identified target groups.
2. Two sources of financing will be considered for quantification: (1) micro-loans below EUR 25,000 provided by commercial banks and (2) microfinance products provided by MFIs.
3. An annual quantification of the supply of financing is estimated for the two financing sources, considering that entirety of the financing will be provided to the final recipients identified in the HRD OP.
4. Then, a qualitative estimate of future supply will be provided through projections made, by taking into account the perception and expectation of the financing actors collected during the interviews.
5. The obtained supply for both micro-loans and microfinance product may be considered annual.

[75] European Commission (2012), Report from the Commission to the European Parliament and the Council on the application of Directive 2006/48/EC to microcredit, COM(2012) 769 final.
http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2012:0769:FIN:EN:PDF.

6.2.2. Commercial banks

The financial sector in Bulgaria is dominated by commercial banks. Although branches of foreign banks appear to maintain a competitive advantage, local banks are gradually increasing their market shares. Overall and according to the stakeholders interviewed from both the supply and demand sides, the banking sector is stable and has liquidity, but interest rates and collateral requirements remain relatively high compared to the other neighbouring EU Member States, increasing the cost of financing and making access to finance more difficult. In recent years, and especially after the crisis, non-performing loans have dramatically increased in Bulgaria to almost 20%, introducing additional tension to banks' lending activity and increasing the difficulties for the companies to access to financing. The entry into force of Basel III in January 2014 has further increased the requirements for capital adequacy in the banking system, further intensifying the risk-averse attitude of lending institutions in the near future.

The main financial product proposed by banks to the identified target groups are loans. They cover the whole scope of available loan products including:

- Standard loans (short-, medium, long-term and revolving loans);
- Bank overdrafts;
- Credit lines; and
- Conditional loans.

Most often, loan products are fully collateralised and, as a result, banks tend to design and offer asset-based products such as:

- Mortgage business loans;
- Quick loans for newly created micro-enterprises; and
- Mortgage loans for hotel and restaurants.

These products proposed to the identified target groups of the HRD OP for 2014-2020 do not differ from the ones usually proposed to Small and Medium-Sized Enterprises (SMEs) in the country. The following paragraphs detailed the provision of loans and micro-loans (below EUR 25,000) by banks in Bulgaria.

6.2.2.1. Loans

Commercial banks provide loans at market interest rate level in Bulgaria. These interest rates may amount between 9% and 28%. They also have typical eligibility criteria such as collateral, which in most of the cases is hard to be provided by a newly established company lacking assets. Key characteristics of loan provision in Bulgaria are:

- Commercial banks differentiate themselves from the so-called fast credit providers, that are poorly regulated by BNB and which interest rates may reach 400% *per annum* and above.
- Loan products offered by commercial banks to start-ups are not very popular among entrepreneurs and newly created micro-enterprises due to the costs and requirements that are beyond the strength of most of them. In most of the cases the products that are marketed as loans for start-up companies actually require from 6 to 12 months of business activity after which the purpose of the funds is assumed to be working capital instead of seed capital.
- Most of the micro loans provided by the banks are for enterprises in the trade and service sectors.
- According to the interviewed stakeholders from both supply and demand sides, small loan borrowers in Bulgaria such as self-employed and micro-enterprises have a low level of financial culture and do not quite differentiate corporate loans from consumer loans.

- Another consequence of this low level of financial culture of entrepreneurs in Bulgaria is the development of poor business plans with future cash-flows (very often part of the required documents for application), in combination with a high level of administrative illiteracy of the applicants.
- Another product offered by the commercial banks in Bulgaria is a micro-loan for liberal professions. Normally these micro-loans are up to EUR 20,000[76].

The loan amounts sought by entrepreneurs for social inclusion, micro-enterprises having temporary difficulties and social enterprises are considered very small by commercial banks. For that reason, the latter are meant to provide micro-loans of up to EUR 25,000 to such entities. This loan provision is detailed in the following section.

6.2.2.2. Micro-loans

Micro-loan is an important product for individuals looking for a job and micro-enterprises. It is also generally recognised as an effective financing channel for job creation and social inclusion. As explained by the European Commission, it could possibly attenuate some of the adverse effects of the current economic and social crisis, while contributing to entrepreneurship and economic growth in the EU[77].

As discussed during the interviews with commercial banks, the latter have difficulties finding bankable projects and eligible clients according to their rating standards in the micro-lending market. Even banks which specialise in financing micro-enterprises appear to be reluctant to provide micro-loans because of the risks associated to the companies and their difficulties to produce appropriate business plans. Banks also do not provide financing to individuals looking for a job or seeking finance for training.

Over the past few years, the provision of micro-loans by commercial banks has remained stable, representing an annual supply of about EUR 2.1bn. The table below provides the annual supply of loans below EUR 25,000 in Bulgaria.

Table 18: Supply of micro-loans in Bulgaria over the 2006-2013 period

	2007	2008	2009	2010	2011	2012	2013
Total supply of micro-loans (up to EUR 25,000) in EUR	1,505,969	2,198,531	2,280,689	2,117,691	2,054,520	2,045,308	2,103,513
Change year-on-year		*46.0%*	*3.7%*	*-7.1%*	*-3.0%*	*-0.4%*	*2.8%*
Total number of micro-loans (up to EUR 25,000)	240,350	323,403	350,749	345,376	344,303	360,594	374,147
Change year-on-year		*34.6%*	*8.5%*	*-1.5%*	*-0.3%*	*4.7%*	*3.8%*

Source: Bulgarian National Bank, PwC analysis, 2013.

The amounts and number of micro-loans indicated in the table above cover the whole Bulgarian economy (SMEs, mid-caps and large companies). They also cover all types of sectors and all types of legal entities. It is however to be assumed that the majority of these loans are used to cover working capital purposes, which is the main purpose of funding indicated by the representatives of the groups targeted and final recipients by the

[76] Liberal professions being not under the scope of the HRD OP for 2014-2020, these specific micro-loans for liberal professions are not taken into consideration in the analysis.

[77] European Commission (2012), Report from the Commission to the European Parliament and the Council on the application of Directive 2006/48/EC to microcredit, COM(2012) 769 final. http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2012:0769:FIN:EN:PDF.

HRD OP for 2014-2020. According to the financial stakeholders interviewed, the supply of micro-loans provided by commercial banks for the coming years (2014-2016) is meant to remain stable and consequently may be considered at around EUR 2.1m per annum. This supply however will be provided to all sizes of companies from all economic sectors.

A more fine-tuned analysis is needed to detail the provision of loans to the final recipients identified in the HRD OP for 2014-2020. This analysis is conducted in the following section.

6.2.2.3. Loan provision to the final recipients identified in the HRD OP for 2014-2020

The supply of financing to the identified target groups may raise specific issues from the banks' side. These issues are detailed in the following paragraphs.

Commercial banks consider that it is not their role to finance socially excluded individuals willing to have training or needing funding when looking for a job. When considering the target groups under HRD OP, the banks focus only on existing micro-enterprises or newly created micro-enterprises. However, even to these groups of companies, commercial banks do not necessarily provide the funding sought.

Indeed, for the people at risk at poverty who are willing to create their own business and become self-employed, commercial banks are one possible source of financing. Most of the projects proposed by these entrepreneurs with the aim of social inclusion are however often considered as too risky or non-bankable and consequently rejected by the commercial banks. The reasons evoked by the banks to reject these projects are:

- The lack of available collateral to this target groups. Like in most of the cases of debt financing, commercial banks require collateral that people at risk of poverty developing businesses do not have. These entrepreneurs are willing to start a business but often lack assets (personal and corporate) and most of the time set-up an under-capitalised corporation. They consequently do not fulfil the collateral requirements that would have made them eligible to receive a loan.
- The lack of financial history with the banks. Debt financing often require history with a bank in order to have support in difficult times. In the case of people at risk of poverty developing business, entrepreneurs do not have such history and may face difficulties to build it in regards to the socially-oriented aspects of their projects, namely social inclusion and escape from poverty.
- The weak business plans proposed by the entrepreneurs. Most of the people composing the target group lack business knowledge and skills. They have technical capacities that enable them to propose goods and services to clients but lack competences in developing sound business plans for banks. Interviews conducted with stakeholders from both demand and supply sides have underlined this aspect and more specifically the lack of cash-flow analysis in the business plans. Without these key elements, banks consider the projects as too risky and with a high-probability of default. This results in the rejection of the loan.
- The time and resources required to create and monitor a portfolio of micro-loans provided to newly created micro-enterprises. The interviews conducted with banks revealed that processing the documentation for new micro-enterprises requires too much human capital and is too much time-consuming to be profitable. Moreover, maintaining a profitable portfolio of micro-loans requires an extensive network and a large number of agents, who would know and monitor the newly created businesses to ensure they are appropriately managed and able to reimburse.

For all the reasons mentioned above and the high-risky profiles of the newly created micro-enterprises, projects initiated by people at risk willing to escape poverty through social inclusion are most of time not considered by commercial banks.

Interviews with micro-enterprises representatives and commercial banks also underlined the extent to which banks do not currently provide financing for existing micro-enterprises experiencing temporary difficulties (sometimes resulting from the post-crisis situation) and needing financing to maintain their work force, not necessarily as full-time employees. Despite an optimistic and coherent strategy (consisting in maintaining the knowledge, competences and experience of the work force during temporary difficult times in view of coping with growth when new opportunities emerge), commercial banks consider these projects too risky to be financed. These projects involve risks for the banks – which translates into collateral requirements, costs, terms and conditions for the loans - that micro-enterprises are not able to bear, because they are actually experiencing difficulties. This may be despite previous good relationships with the banks. Indeed, the difficulties encountered by the micro-enterprises and the lack of vision of the banks on the future cash-flows lead the banks to reject the loan request, putting the work force at risk of unemployment.

As detailed in the previous section on demand, another subgroup of the potential recipients of funding from the HRD OP for 2014-2020 are the training centres which provide counselling and vocational training to different groups and especially to: (1) unemployed people needing training either to start their own business or to find a job and (2) employees needing training to keep their current job position and increase their employability. As detailed during the interviews with NAVET, training centres mostly generate revenues thanks to the fees provided by the trainees. Most of these fees are funded by grants provided under various programmes (either developed at national level or benefitting from the HRD OP for the 2007-2013 programming period). Such training centres are currently not benefitting from loans provided by commercial banks. This is because neither banks nor training centres have the habit to propose or use this type of financing for this purpose, despite the fact that training centres generate revenues and would be able to reimburse the obtained loans. Indeed, commercial banks do not consider the training centres as profitable enough to be financed by loans. The financing of training centres by commercial banks consequently involves a reduction of the perceived risk taken by the bank when financing the training centres. In that perceptive, the development of a public intervention using Financial Instruments may provide added value in comparison with the grants.

The last set of recipients identified in the HRD OP for 2014-2020 corresponds to social enterprises. Despite clear demand from the entities of the group (cooperatives, specialised enterprises and associations) detailed in the previous section and the nearly exclusive use of grants, social enterprises may also benefit from loans provided by commercial banks. The latter however do not provide such products to social enterprises in Bulgaria. According to the banks interviewed, their not-for-profit purpose, their newly creation (as previously mentioned 93% of the Bulgarian social enterprises were created during the 2007-2013 programming period and more specifically in 2011 and 2012) and their absence of financial history with financial or banking institutions are barriers for the banks to consider them as potential clients. Social enterprises however may generate revenues and could consequently reimburse a loan. Furthermore, as for micro-enterprises and training centres, developing, providing and monitoring micro-loans for social enterprises require a network, human resources and time that commercial banks are not currently willing to devote. An increased access of social enterprises to commercial banks would therefore imply a reduction of the risk perceived by the banks. Similar to training centres, the use of Financial Instruments may provide added value in comparison with the grants currently provided to such enterprises.

In the light of the risks perceived by the commercial banks that prevent them from providing loans to the target groups identified in the HRD OP for 2014-2020, a second source of funding needs to be considered: microfinance products provided by Microfinance Institutions in Bulgaria.

6.2.3. Microfinance Institutions

According to the 2007 Communication “A European initiative for the development of microcredit in support of growth and employment”[78], microcredit in the EU means loans under EUR 25,000, tailored to the needs of

[78] http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2007:0708:FIN:en:PDF.

micro-enterprises employing fewer than 10 people and, unemployed or inactive people who need financing in their job-hunt or willing to go into self-employment but not having access to traditional banking services. As illustrated in the previous section, the provision of micro-loans from commercial banks in Bulgaria is low. Microfinance Institutions are consequently a key financing supplier for the groups targeted by the HRD OP in view of supporting unemployed people looking for a job, self-employment of socially and financially entrepreneurs as well as nearly bankable micro-enterprises needing small loans to maintain their activity during difficult times.

Microfinance Institutions in Bulgaria refer to institutions which are officially licensed to provide very small loans of up to EUR 25,000. They include two types of micro-loans for two kinds of clients:

- Personal micro-loans provided to support unemployed people in their job-hunt. These clients are individuals. MFIs may provide personal micro-loans to these persons having difficulties finding a job in order to foster their social inclusion. This financing is meant to support a person experiencing difficulties in entering the labour market, such as disadvantaged populations (women, young people, and vulnerable minorities) and/or persons who may be socially or financially excluded due to their socio-economic status. These microfinance products may finance mobility costs (bus ticket and car for instance) in order to have a greater chance of accessing the labour market. While the activities or object financed would generate no revenue in the short-term, they may improve their social and economic inclusion in the mid-term thanks to better access to the labour market.
- Business micro-loans provided to self-employed and micro-enterprises having difficulties being financed by commercial banks. These clients are enterprises. They comprise self-employed people, newly created companies and existing micro-enterprises which may use business micro-loans in their creation or development phase.

According to the stakeholders interviewed, MFIs in Bulgaria currently favour microfinance for enterprises in comparison with microfinance for individuals. The provision of personal micro-loans is scarce in Bulgaria.

Business micro-loans provided by MFIs are meant to cover working capital needs and, to a lesser extent, investment. Similar to other EU Member States, microfinance in Bulgaria implies:

- Higher interest rates compared to the standard interest rates on the market resulting from the risks taken by the MFIs;
- Detailed due diligence based on the viable business plans proposed by the entrepreneurs and the existing micro-enterprises; and
- Support services and training provided by MFIs to business creators and existing micro-enterprises to develop and make their activity sustainable.

Despite existing for more than 15 years in the country, MFIs are not very well-known in Bulgaria and often confused with the consumer lending institutions which are not meant to provide finance for business creation or support in job accession. Some MFIs and stakeholders interviewed however acknowledge a raise in the awareness of the MFI market. MFIs may also benefit from a relative lack of confidence expressed by micro-enterprises towards commercial banks which often refrain from financing them. On the other hand, other stakeholders consider the MFI market in decline and do not expect this trend to evolve.

The microfinance market currently experiences a lack of funding resulting from the withdrawal of funding from USAID after Bulgaria's accession to the EU. These limited resources result in difficulties for MFIs to have the administrative capacity and human resources to process and monitor the projects that could be financed and/or develop their distribution networks throughout the country.

As reported by the MFIs in 2012, 2,914 companies were active borrowers from these institutions, comprising both new and existing micro-loans (Table). Considering that Bulgaria has more than 336,000 micro-enterprises, a high potential exists for funding such enterprises, including the target groups of the HRD OP for 2014-2020. As illustrated in Table below, the average amount provided by the ten MFIs active in Bulgaria in 2012 according to MixMarket is less than EUR 4,000. This table presents core operating indicators of the main active MFIs for 2012. They exclude JOBS MFI, which is backed by financing from the European Investment Fund (EIF). JOBS MFI received a loan from the Progress programme of EUR 6m and also committed further funds amounting to EUR 3m. Total disbursement prior to 2013 reached EUR 1.44m. JOBS MFI is currently in the process of becoming part of the Bulgarian Development Bank (BDB) as a separate department.

Overall, when considering the remaining funds of JOBS MFI and the estimates of stakeholders, the lending capacity of Microfinance Institutions in 2013 did not exceed EUR 11m in total.

Table 19: Microfinance Institutions market in Bulgaria in 2012[79]

	Gross loan portfolio (in mEUR)	Number of active borrowers	Average loan value disbursed (in EUR)
Mikrofond	3.607	985	3,662
KSK RPK	2.806	196	14,319
USTOI	1.262	688	1,834
Doveriye - Bulgaria	0.818	171	4,781
Doverie Finance	0.704	80	8,801
General Toshevo	0.623	150	4,152
Nachala	0.550	337	1,632
Popular Kasa-Kystendil	0.260	140	1,859
Ustrem 96	0.220	167	1,315
Total	**10.850**	**2,914**	**3,723**[80]

Source: Mix Market MFI Statistics, 2014.

Concerning the supply of microfinance over the next years (2014-2016), there is a strong disparity among the stakeholder forecasts. While some market stakeholders estimate a decline of the microfinance market at around 2%, others are more optimistic and consider that the market could actually grow up to 5%. In the coming months and years, JOBS MFI with the support from the EIF, to a large extent, and, Mikrofond to a lesser extent, will be the main drivers of the microfinance market in Bulgaria and the main suppliers of microfinance products. When considering the market estimates provided by the stakeholders, the lending capacity of MFIs for the coming years may amount between EUR 9.8m and EUR 10.5m per annum. This supply may potentially be provided to all micro-enterprises from all economic sectors.

In addition to these MFIs, there is the Progress microfinance initiative supported by the EIF. The objective of this initiative is to make EU funding available for microfinance, support socially excluded people and help business creation. Based on the information in Table 14 relative to Progress and the leverage generated by JOBS MFI (a leverage of 1:1.5 with the total micro-loan provision of EUR 9m with an initial budget of EUR 6m), it is to be assumed that Progress may provide a total of EUR 25.5m in Bulgaria, i.e. 1.5 times the EU contribution of EUR 17m. This total amount includes co-investment from the three financial intermediaries (Mikrofond, JOBS MFI and Societe Generale).

79 Data on microfinance supply for 2013 is not available.

80 If KSK RPK were considered as an outlier due to a comparatively high average loan amount provided and so if its figures were removed from the calculations, the average loan provided by MFIs in Bulgaria would decrease to EUR 2,960.

When considering the six final recipients identified in the HRD OP for 2014-2020, microfinance is the main alternative financing beside loan financing from commercial banks. Interviews with MFIs and other stakeholders have however indicated that MFIs may have similar conditions than commercial banks and conduct strict financial analyses of the micro-enterprises before providing finance. This tends to create confusion between the role of MFIs and of commercial banks, since MFIs should finance more risky projects in comparison with commercial banks and provide finance to non-bankable micro-enterprises. It also indicates that MFIs may require support to increase their risk appetite and provide more products to unemployed persons, newly created micro-enterprises by people at risk of poverty or micro-enterprises having temporary difficulties. The supply of microfinance products to the four target groups identified in HRD OP for 2014-2020 is detailed in the following paragraphs.

As already mentioned, personal micro-loans are scarce in Bulgaria. Only few micro-loans are provided to individuals seeking for a job and/or needing training to obtain a job.

Moreover, apart from offering micro-loans, MFIs are close to their clients to understand their business and have strong experience in assessing projects which are helpful to entrepreneurs willing to create their companies to escape poverty. MFIs are also a key financing source to provide the first loans to be used by these new entrepreneurs in order for them to start building relationships with financial institutions. Future relationships with commercial banks can therefore be facilitated. Based on the interviews conducted with MFIs and micro-enterprises, microfinance products are however not very well-known or used in the country. At the European level, about one third of micro-loans provided by MFIs are directly addressed to start-ups (European Microfinance Network, 2012)[81]. On average in Europe, 38% of all micro-loans are provided to women and 12% are offered to ethnic minorities and immigrants. In parallel, 17% of micro-loans are provided to people living in rural areas. Clients below the poverty line are also targeted, and they represent 13% of the whole lending activity in 2011.

MFIs are also not meant to provide finance to micro-enterprises having temporary difficulties. For that reason, no data is available for this specific support. However, considering that MFIs are providing financing that may be used for working capital purposes, micro-enterprises experiencing temporary difficulties could benefit from them. MFIs in Bulgaria however do not currently consider this type of micro-enterprises as potential clients and may be inclined to reconsider this position if they were supported in so doing. By supporting micro-enterprises experiencing temporary difficulties but willing to keep their workforce in prevision of growth, this would positively impact unemployment. These companies would also benefit from the guidance, counselling and mentoring proposed by the MFIs to improve their profitability and sustainability.

MFIs could provide training centres or companies developing training for their own staff with micro-loans and be reimbursed through the fees required to trainees in the case of training centres or thanks to the added value resulting from new business generated by more skilled people. This possibility is currently not implemented in Bulgaria, despite its potential high impact on employability and employees' skills.

As already mentioned about social enterprises, the latter are currently only funded with grants. Bulgarian MFIs do not currently provide them with micro-loans.

6.2.4. Overall supply by type of products

Two types of products may be considered as potential sources of funding for the six final recipients indicated in the HRD OP for 2014-2020:

- Micro-loans provided by commercial banks, representing annually at most EUR 2.1m;

[81] European Microfinance Network (2012), Overview of the microcredit sector in the European Union, http://www.european-microfinance.org/data/file/overview2010-2011-final.pdf.

- Microfinance products from Microfinance Institutions, representing annually between EUR 9.8m and 10.5m; and
- Microfinance products for about EUR 25.5m available through the Progress initiative and provided by JOBS MFI, Mikrofond and Societe General.

However, as described in the sections above, in most cases, neither the commercial banks nor the MFIs consider the target groups of the HRD OP as potential clients. As far as new entrepreneurs creating their business to escape poverty are concerned, commercial banks consider that it is not their role to finance them and consequently provide only marginally micro-loans to them. Banks estimate too risky, too much time and resource consuming and not enough profitable the provision of micro-loans to newly created micro-enterprises. On the other hand, MFIs, which are the main finance providers of this target group, acknowledge difficulties in processing applications and managing projects because of limited resources and little networks in the country. For the coming years, only two main actors may be considered as microfinance suppliers: JOBS MFI supported by the EIF and Mikrofond benefitting of the Progress initiative. The current imperfections of the microfinance market have led over the past years to the development of consumer-lending organisations which propose financing at high interest rates to individuals but often used for business creation.

The provision of personal micro-loans for unemployed people needing finance during their job-hunt is scarce in Bulgaria and would help these people to better access the labour market.

Micro-enterprises experiencing temporary difficulties are not financed by either commercial banks or MFIs as these consider them as too risky. This may put at risk of unemployment the employees of companies that have growth perspectives despite knowing difficult times currently.

Neither training centres nor social enterprises are currently financed by commercial banks or by MFIs. They keep being quasi-exclusively financed by grants while they could reimburse loans thanks to the revenues they generate.

6.3. Market failures, suboptimal investment situations and financing needs

With the results of the supply-side and demand-side analysis it is possible to properly understand the situation in the Bulgarian market and identify the presence of market failures, suboptimal investment situations and unmet investment needs. This is an important requirement in the justification for public intervention through the creation and implementation of Financial Instruments. This is also in line with Article 37(1) and (2) of the Common Provisions Regulation (CPR), which states that FIs are to be implemented to support investments that are expected to be financially viable but unable to raise sufficient funding on the market due to the presence of market failures or suboptimal investment situations.

The concept of a ***market failure*** is that of a situation where non-functioning aspects of the market lead to an inefficient allocation of resources and entail the underproduction or overproduction of certain goods and services. Market failures can generally be classed as failures that arise from a structural issue in the market, on the side of the supplier, or on the side of demand. Market failures can also be typical in certain sectors like microfinance for social inclusion or social enterprises financing for example. ***Suboptimal investment situations*** on the other hand are a specific type of market failure for which FIs are well suited to address based on past evidence. These situations occur when investment activities do not perform according to expectation by failing to achieve a policy objective, often with a history of longstanding failure to do so.

The purpose of this section is to unify the results of the supply analysis and the demand analysis in order to better understand the difference between the availability of supply in the market for projects aiming at developing Human Resources in Bulgarian companies and the demand for these financial products. By comparing these it is possible to develop an indicative financial gap which could be bridged by FIs, thus justifying their creation. However, as previously mentioned, because of the limited amount of information made available by the relevant stakeholders, a full quantification of supply and demand is not possible, but it is nonetheless possible to develop a good understanding of the market situation by compiling the data gathered from the interviews with stakeholders, desk research[82], and analyses.

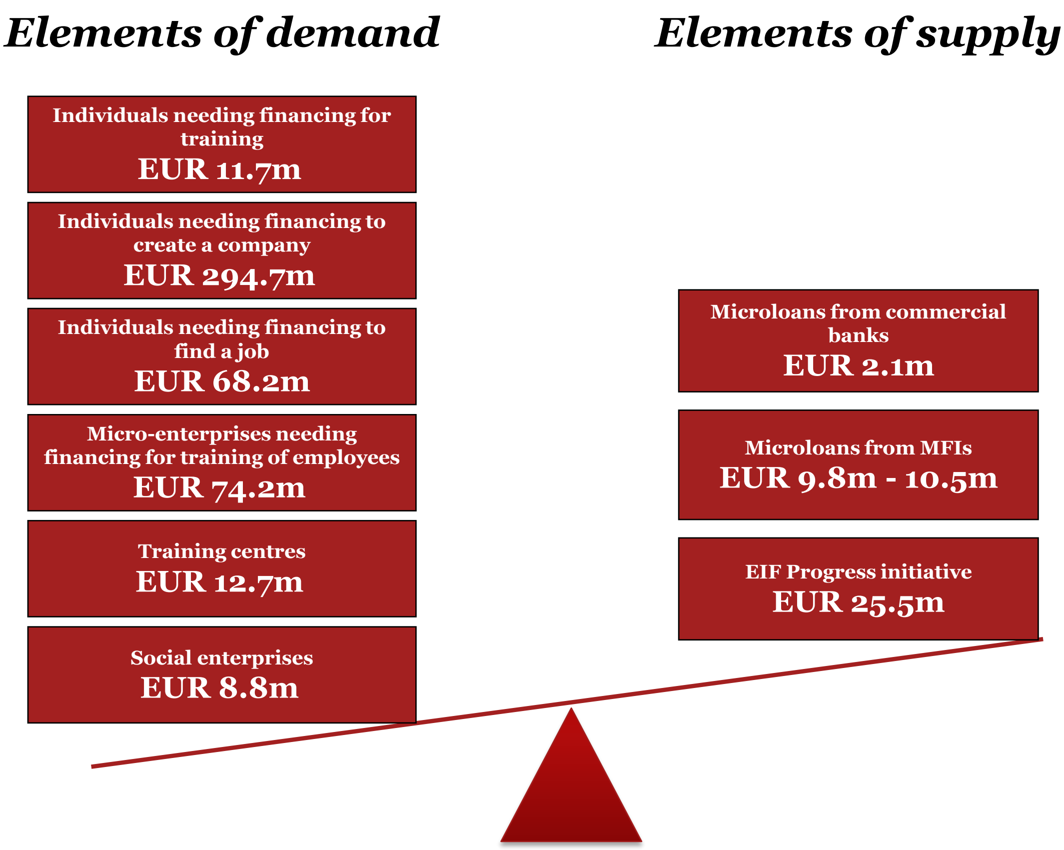
6.3.1. Quantitative aspects of the financing gap

As explained earlier in this section of the study, the quantification of the overall market demand and supply is limited to a fragmented view of the point where the supply meets demand, which makes the quantification of the investment gap problematic. Some of the elements taken into consideration to calculate the demand and supply-sides may sometimes overlap, that is why a total financing gap has not been calculated. As such the analysis of the difference between supply and demand has been based on the material elements that constitute demand and supply. This incorporates the most representative information available in the market of Human Resources Development, gathered through a wide range of interviews with stakeholders, a review of the existing literature and with desktop research. Through this analysis it is possible to contrast the major quantitative aspects of supply and demand, providing an indication of the on market in Bulgaria.

This comparison between demand and supply is indicated in the figure below.

[82] Research and surveys, conducted over 2004-2005 by the Sofia-based Institute for Social and Trade Union Research (ISTUR) and the International Labour Organisation (ILO), examined the state of play in microfinance provision in Bulgaria, with a view of implementing public assistance programmes and Financial Instruments to bolster social inclusion and support for self-employment. For details see: (1) Social Finance in Support of Self-Employment in Bulgaria: Legal and Institutional Framework of Micro-Finance and Development of Small and Medium Sized Enterprises in Bulgaria, ILO & ISTUR, October 2004. (2) Social Finance for Support to Self-Employment: Unemployed People's Needs and Attitudes to Self-Employment (Findings from an Empirical Sociological Survey), ILO & ISTUR, February 2005. (3) Social Finance for Support to Self-Employment: Main Actors and Institutions in the Area of Microfinance in Bulgaria, ILO & ISTUR, September 2005.

Figure 23: The indicative gap in the Bulgarian market for the HRD OP



Source: PwC, 2014.

This above-illustrated gap is to be considered as only indicative since:

- It considers all micro-loans provided by commercial banks as to be used by micro-enterprises as of social inclusion funding;
- All amounts are indicated as annual demand or annual supply when this demand or supply may be sought or provided over a period longer than 12 months, depending on the anticipations and expectations of individuals, the micro-enterprises and the financial institutions;
- Demand for financing is based on a macro-economic background that may evolve in time and modify expectations of future entrepreneurs as well as micro-enterprises; and
- Following this, demand for financing expressed by entrepreneurs and micro-enterprises may be expressed today but not materialise in the future.

Nevertheless, as graphically represented in Figure 23, it is evident that the elements of ***demand outweigh supply***. As such, this is an indication for a ***material investment gap***. It indicates the extent to which financial products presently provided by commercial banks and MFIs do not cover the financing needs of the target groups identified in the HRD OP for 2014-2020. This suggests failures at the market level of a structural nature which have a pervasive effect on the whole market. A gap of this magnitude illustrates the need for reforms on all market levels in order to allow the market to function properly. This quantitative aspect of the financing gap is also supported by qualitative aspects which are detailed in the following section.

6.3.2. Insights on market failures and suboptimal investment situations

Having taken into consideration the findings of the literature review, from extensive desk research, and from the interviews held with relevant stakeholders, and combining this with the analysis of the market supply, and demand, several market failures were identified. Having demonstrated that there is a financing gap in the Bulgarian market for the target groups identified in the HRD OP for 2014-2020, a comprehensive list of the market failures justifying the creation of FIs to help address them and catalyse private funding so as to create added value. This subsection will list these identified market failures and suboptimal situations, some being general and others specific to a market segment, such as social economy.

General problems faced by the target groups

Most projects developed by the ***target groups identified in the HRD OP are considered as non-bankable*** by the commercial banks and consequently do not receive the financing they seek. In parallel, some MFIs may have strict criteria when assessing the projects, potentially leading to financing rejection. Following this, no financial actor currently consider financing non-bankable projects proposed by socially excluded entrepreneurs, people at risk of poverty or disadvantaged people.

The analysis also highlighted that new self-employed people and newly created micro-enterprises experience ***difficulties in creating relationships with financial institutions***. Indeed, commercial banks and sometimes MFIs do not provide financing for business creation. The absence of previous business activity is one of the main reasons why financial institutions refuse to provide financing. The latter may request between 4 and 12 months of business history to provide finance, in addition to collateral. That is why entrepreneurs prefer to ask relatives and friends for funds or even apply for consumer loans with high interest rate but without collateral required or delay. This consequently hinders business creation in Bulgaria and creates market distortions with the development of consumer lending institutions replacing banks and MFIs.

In addition to market failures related to business creation, the majority of ***existing micro-enterprises in Bulgaria are so much in debt*** that commercial banks refuse to provide them with financing even though they experience temporary difficulties and have good growth forecasts and positive perspectives.

Unemployment among young people in Bulgaria is high (21.8%[83]) and increased over the past years due to the crisis. One of the reasons for this situation is that ***young people in Bulgaria lack career guidance*** after higher education, often lack professional experience to be re-employed once unemployed and, in many cases, their skills mismatch the changing business needs of the companies. In that context, the employability and job adaptation of young entrepreneurs and young unemployed is a barrier to their future access to employment or to their willingness to create a business. Young unemployed are today lacking appropriate training to get hired by a micro-enterprise or do not receive support in their projects aiming at creating their own business.

Another important barrier to the uptake of financial supply is the ***administrative barrier*** faced by entrepreneurs and micro-enterprises when apply for finance. The administrative requirements are often too great, demanding too much time and effort (and as such too costly) to be fulfilled by a single business creator or a very small micro-enterprise. This issue was raised repeatedly by stakeholders during the interviews. It is a particularly important issue for self-employed and small micro-enterprises, for whom resources are limited and the time spent fulfilling administrative requirements potentially outweighs the benefits of the funding itself. This administrative barrier may even be aggravated by the low level of administrative literacy of the applicants among self-employed and micro-enterprises. For most potential business creators, it is difficult to follow the required administrative process for credit application.

[83] Eurostat, 2010.

The administrative burden is present through the entire project cycle:

- From the pre-award stage (e.g. identifying the most appropriate source of financing which often leads self-employed and micro-enterprises to ask for financing from family and friends instead of formal financial institutions such as commercial banks and MFIs);
- Through the application process (e.g. producing abundant amounts of documentation as part of the application process and responding to calls in short timetables);
- To the realisation phase (e.g. dealing with various requirements, such as monitoring requirements).

Interviews also revealed a ***lack of capacity and management skills*** among self-employed people and within micro-enterprises, in particular the smaller ones. The main skills quoted by interviewed stakeholders were: business plan development, financial management skills and HR management skills. Most of self-employed enterprises and micro-enterprises are set-up by professional entrepreneurs who often lack the management skills needed, as well as financial and legal expertise. They often face the issue of having a limited headcount which makes it difficult to manage the company financing while producing goods or providing services to clients.

The stakeholders interviewed also mentioned the fact that entrepreneurship could be better stimulated in the country. These campaigns would demonstrate the extent to which self-employment is a viable option to escape poverty or social exclusion.

Insufficient supply of existing products

The quantitative analysis of the financing gap revealed that ***micro-loans are under-provided*** in Bulgaria, as commercial banks do not consider the self-employed, the micro-enterprises, the training centres and the social enterprises as potential clients. The perception of interviewed stakeholders is that neither commercial banks nor MFIs are presently financing the different target groups identified in the HRD OP, leading them to be financed by lending consumer institutions and/or family and friends.

Moreover, the financing of Human Resources projects often necessitates microfinance for newly-created or existing micro-enterprises. ***MFIs however experience internal difficulties*** when processing applications and monitoring the clients they finance. Microfinance products are also not used to finance training centres and social enterprises nowadays. Supporting the own financing of MFIs and indicating them new market opportunities/clients which would be the training centres and the social enterprises would help the MFIs financing more self-employed, micro-enterprises and social enterprises thanks to more human resources and a strengthened network in the country. This would help reaching self-employed and micro-enterprises which are currently not identified as potential clients by MFIs.

Absence of provision of key financial products

The capacity to provide the collateral required by the commercial bank and/or, sometimes, by the MFIs is the main challenge for the entrepreneurs and the micro-enterprises. There is to date ***no micro-guarantee facility*** in Bulgaria that provide guarantees to banks and MFIs for micro-loans to new companies and self-employed people.

Most of self-employed companies and micro-enterprises are under-capitalised in Bulgaria. This situation is even more striking for newly created companies which often start their business with an insufficient level of equity. This leads them to experience difficulties after two or three years of business activity when seeking finance from banks and/or MFIs, despite positive forecasts for their business. There is currently ***no micro-equity financing*** available in Bulgaria that may support new micro-enterprises and ensure they receive the equity finance required to develop and secure their future debt financing and relationships with commercial banks and MFIs.

Insufficient financial support for social economy

Some market failures have been identified that are specific to social enterprises, and the social economy sector as a whole.

To begin with, there is to date ***no specific financial product and no specialised financial actor financing the social economy sector*** in Bulgaria. Social enterprises (including cooperatives, specialised enterprises and foundations) are today financed exclusively by grants. Neither the commercial banks nor the MFIs consider the social enterprises or the training centres as potential clients which could reimburse micro-loans thanks to their revenue generated by their activities or by the fees received from trainees.

This clear market gap results from the absence of actors willing to finance social enterprises. This notably results from the fact that no risk-sharing financing scheme currently exists in Bulgaria to mitigate the risks that commercial banks or MFIs would accept to take if financing social enterprises. If such financing schemes existed, commercial banks and MFIs would be incentivised to finance the social economy sector. Their risk appetite would be increased and social enterprises would have access to further financing sources, apart from grants schemes which would remain to finance very risky projects where no added value brought by Financial Instruments could be envisaged.

In addition to risk-sharing financing schemes for social enterprises, the social economy sector would benefit from a clear and more stable regulatory (including fiscal) framework. A clearer definition of the entities composing the social economy – and consequently the future users of potential Financial Instruments – would help the finance suppliers to identify, define and target their clients in the sector, which would be new clients for them. These new clients' needs would need to be defined and clarified so as to make the best use of the Financial Instruments. In that regards, discussions and follow-up meetings with the main future financing suppliers of the social economy sector would be needed to ensure there is an appropriate use of the Financial Instruments, that added value is generated in comparison with grants and that the main financing needs of the social enterprises are addressed.

6.4. Identification of possible solutions to answer to market failures and suboptimal investment situations

Table 20 presents an overview of the identified market failures, along with potential solutions to overcome them through the use of FIs. These recommendations are based on the interviews conducted with stakeholders, desk research and expertise in the field.

Table 20: Identified market failures and potential solutions to overcome these

Market failures	Potential solutions
Target groups identified in the HRD OP are considered as non-bankable	• Develop risk-sharing finance schemes to increase the risk appetite of financial intermediaries • Propose micro-guarantee schemes to commercial banks and MFIs to incentivise them financing currently non-bankable companies by making them becoming nearly bankable enterprises
Target groups identified in the HRD OP have difficulties in creating relationships with financial institutions	• Support MFIs in financing business creation in order to help micro-enterprises establishing relationships with financial institutions • Provide newly-created micro-enterprises with micro-loan financing schemes that are supported through Financial Instruments in order for these companies to leverage micro-loans from commercial banks (micro-loans supported by FIs to be used for leveraging commercial banks' loans)

Existing micro-enterprises are in so much debt they cannot obtain more loan products	• Develop risk-sharing financing schemes to increase the risk appetite of commercial banks and MFIs, and so incentivise them to take more risks • Develop a micro-guarantee funds for commercial banks and MFIs to provide collateral to (1) micro-enterprises which have already collateralised their assets and so rely on family and friends to sustain and/or develop their business and (2) to business creators seeking loan financing to start their business • Develop micro-loan financing schemes to facilitate future loan financing from commercial banks for existing micro-enterprises (micro-loans supported by FIs to be used for leveraging commercial banks' loans)
Young people in Bulgaria lack career guidance	• Encourage and incentivise MFIs to propose training and mentorship to support young entrepreneurs
Business creators and micro-enterprises experience administrative barriers when seeking finance	• Provide support to entrepreneurs and micro-enterprises on business plan drafting, research for finance (i.e. provide information on available finance and facilitate relationships with financial institutions) and support the provision of mentorship by MFIs • Provide legal and fiscal advice to entrepreneurs and micro-enterprises • Develop predefined application forms for standardised requests for microfinance products provided by MFIs • Develop and distribute guidelines to entrepreneurs and micro-enterprises on simple financial information that is needed by financial institutions (with hard copies and via internet)
Target groups identified in the HRD OP lack of capacity and management skills	• Provide advisory assistance to entrepreneurs and micro-enterprises, such as: legal and fiscal advice, support on accounting, marketing and sales, as well as training on Human Resources management • Provide support to entrepreneurs and micro-enterprises on business plan drafting, research for finance (i.e. provide information on available finance and facilitate relationships with financial institutions, including knowledge on the role of the equity structure for loan financing, and the equity financing actors in Bulgaria) and support the provision of mentorship by MFIs • Develop and distribute guidelines to entrepreneurs and micro-enterprises on simple financial information that is needed by financial institutions (hard copies and via internet)
Micro-loans are under-provided	• Develop a micro-guarantee funds for commercial banks and MFIs to provide collateral to (1) micro-enterprises which have already collateralised their assets and so rely on family and friends to sustain and/or develop their business and (2) to business creators seeking loan financing to start their business • Develop micro-loan financing schemes to facilitate future loan financing from commercial banks to existing micro-enterprises and entrepreneurs (micro-loans supported by FIs to be used for leveraging commercial banks' loans)
MFIs experience internal difficulties that need to be overcome to increase the provision of microfinance products	• Leverage the Progress initiative supported by the EIF • Provide technical support for MFIs' institutional capacity building • Support the financing of MFIs' internal administration: support the financing of MFIs' Human Resources, support MFIs in developing their networks throughout the country, support MFIs in their communication strategy and support MFIs develop more standardised and automated credit assessment and due diligence methods
No micro-guarantee facility exists in Bulgaria	• Develop a micro-guarantee fund for commercial banks and MFIs to provide collateral to (1) micro-enterprises which have already collateralised their assets and so rely on family and friends to sustain and/or develop their business and (2) to business creators seeking loan financing to start their business • Develop risk-sharing financing schemes to increase the risk appetite of commercial banks and MFIs, and so incentivise them to take more risks. These schemes may take the form of micro-loans offered to micro-enterprises newly created for social inclusion, to social enterprises and to entrepreneurs
No micro-equity financing exists in Bulgaria	• Develop micro-loan financing schemes to facilitate future loan financing from commercial banks to existing micro-enterprises and entrepreneurs (micro-loans supported by FIs to be used for leveraging commercial banks' loans)

No specific financial product and no specialised financial actor finance the social economy sector in Bulgaria	• Clearly define social economy, social enterprise, and social entrepreneur thanks to the evolution of the social economy sector in the European Union and more advanced existing regulatory frameworks existing in other EU Member States • Stabilise the regulatory (including fiscal) framework establishing the social economy sector • Improve the access of social enterprises to financing sources other than grants schemes in order to favour a better use of public funding while ensuring the access to finance of companies which are currently not targeted by commercial banks or MFIs • Develop risk-sharing financing schemes to increase the risk appetite of commercial banks and MFIs, and so incentivise them to take more risks. These schemes may take the form of micro-loans offered to social enterprises and social entrepreneurs • Develop a micro-guarantee fund for commercial banks and MFIs in order to provide collateral to social enterprises which cannot receive grants anymore and social entrepreneurs seeking loan financing to start their business • Develop micro-loan financing schemes to facilitate future loan financing from commercial banks to existing social enterprises and social entrepreneurs (micro-loans supported by FIs to be used for leveraging commercial banks' loans) • Facilitate discussions and follow-up meetings with the main future financing suppliers of the social economy sector (potentially MFIs or other financial intermediaries) to ensure that the Financial Instruments are correctly calibrated to the Bulgarian social economy sector and that they provide added value in comparison with grants

Source: PwC analysis, 2014

The financing gap, market failures and suboptimal investment situations have revealed that the design and implementation of three FIs could support the access to finance of the target groups identified in Chapter 3. These potential Financial Instruments are:

- Personal micro-loans provided by MFIs to facilitate the access to the labour market of unemployed people;
- Business micro-loans provided by commercial banks and MFIs to facilitate future loan financing from commercial banks. These micro-loans would be supported by FIs to be used for leveraging commercial banks' loans; and
- Micro-guarantee schemes using commercial banks and MFIs as financial intermediaries in order to provide collateral to the final recipients.

The final recipients of these FIs would be the ones identified at the beginning of the Chapter, namely:

- Individuals needing financing for a training in view of creating a company or obtaining a new job;
- Individuals needing financing to create a company;
- Individuals needing financing to find a job;
- Micro-enterprises needing financing to finance a training for their employees;
- Training centres (Vocational training centres; education and training organisation and institutions; and information and professional guidance centres that provide counselling services and training on entrepreneurial, managerial and business skills); and
- Social enterprises (existing social enterprises and social-entrepreneurs).

7. Analysis of added value generated by Financial Instruments

The previous chapter has highlighted the financing gap between supply and demand for financing for the target groups identified in the HRD OP for 2014-2020. In view of addressing this financing gap, the OP intends to use Financial Instruments in addition to grants, as recommended in the Europe 2020 Strategy. This constitutes a change in the use of funding provided by the HDR OP in comparison with the 2007-2013 programming period where only grants were used. Indeed, the objectives to be achieved by the HRD OP for 2014-2020 may be attained through different ways and may involve different types of support. For these reasons the added value of the envisaged FIs has to consider both quantitative and qualitative aspects to objectivise that the use of FIs would deliver the goals to be achieved in the most efficient and effective way. These quantitative and qualitative aspects would also substantiate the rationale behind the design and implementation of the envisaged FIs, in comparison with the sole use of grants under the HRD OP for 2014-2020.

After identifying the financing gaps, the market failures and suboptimal investment situations, the identification of the potential added value of Financial Instruments will provide the necessary justification for their development and implementation in the 2014-2020 programming period. The benefit brought about by them will also play an important role in devising of the investment strategy and of the FIs, and provide justifications for the indicators used in their monitoring and ex-post evaluation.

This added value is composed of several components that have to be considered to found the rationale behind the use of FIs:

- The dimensions of added value brought by the FIs in comparison with grants, implying:
  - A quantitative dimension, such as the leverage effect and the revolving aspect of the FI; and
  - A qualitative dimension, such as the promotion of entrepreneurship, the support to job creation, the reduction of unemployment and the increase in the efficiency in the delivery of funds as opposed to grant provision.
- The consistency with other forms of public interventions, such as support programmes for excluded people or for SMEs;
- The additionally between grant schemes and the FIs;
- The use of public and private resources at different levels of the FI, namely: at the Fund-of-Funds, at the fund and at the recipient levels. In that matter, FIs are meant to allow a greater implication of the private sector as opposed to grants; these private actors playing the role of financial intermediaries;
- The implication of other stakeholders to support the implementation and promotion of the FI; and
- The State Aid aspects related to the FI to avoid market distortion.

The added value to be brought by the FIs comprises both quantitative and qualitative dimensions. When the quantitative aspects relate to the potential leverage effect and the revolving aspects of the FI, the qualitative aspects consider the overall access to finance for the target groups facilitated by the FIs, including for instance the promotion of entrepreneurship among socially excluded people or the support to employability of employees to reduce unemployment.

Another aspect of the added value of the FIs is their consistency with other public interventions related to the support of excluded people and people at risk of poverty, along with initiatives to support training and social enterprises in Bulgaria.

Financial Instruments may be blended with grants, considering that both financing products would have different aims but are meant to be used in a complementary manner to reach the overall objectives of the HRD OP.

Following this, Financial Instruments, as opposed to grants, may blend together public EU, national and regional funding as well as private funding. For that reason, it is important to identify the additional public and private resources that may be used in addition to the ESF funds provided through the HRD OP. These additional resources are to be considered either as potential resources to be included in the FIs at various levels (Fund-of-Funds, funds and final recipient) or as other resources that will be available to the target groups of the HRD OP and may complement the funding provided by the FIs.

Other stakeholders to consider are also presented in the following paragraphs. These stakeholders may not be blended in the FIs but are part of the general framework concerning HR development in Bulgaria, and, for that reason, have to be considered in the set-up of the FIs to be designed for the HRD OP for 2014-2020.

Finally, FIs have to be designed in such a manner that they comply with State Aid requirements to avoid market distortions and deadweight effect. The envisaged FIs under the HRD OP are meant to facilitate the access to finance of excluded people willing to create their company, micro-enterprises experiencing temporary difficulties, training centres and social enterprises. In doing so, they need to avoid creating market distortion such as providing finance to companies that could have received finance without the support of the Financial Instrument.

7.1. The dimensions of added value for the envisaged FIs for the Operational Programme "Human Resources Development"

The following sub-section will present the different dimensions of added value that FIs could generate under the OP for Human Resources Development. As per the ex-ante assessment methodology, these can be of a quantitative or qualitative nature. Since no specific FIs currently exist in Bulgaria to support the financing of the target groups identified in the HRD OP, experience from other Member States will be used to determine the potential added value of the envisaged FIs for 2014-2020 in the country. In so doing, the key questions to be answered in this section are:

- Will the ESIF-supported FI generate value that would not be possible through existing FIs or solutions available to the market such as grants?
- How much additional public and private sector financing could a newly created FI leverage?
- Would this additional financing be displaced from some other source?
- What other value would be created by the FI in terms of financial and socio-economic benefits?

The financing gap detailed in Chapter 6 has made emerged two different needs in terms of Financial Instruments:

- Micro-loans (business and personal) to facilitate future loan financing from commercial banks. These micro-loans would be supported by FIs to be used for leveraging commercial banks' loans; and
- Micro-guarantee schemes using commercial banks and MFIs as financial intermediaries in order to provide collateral to the final recipients.

The quantitative and qualitative dimensions of these two FIs will be considered in the following paragraphs.

Co-financing

The co-financing effect is achieved by an FI at the first level of the structure and more specifically when a fund is created to implement an FI. The legitimacy and credibility of a fund created as a public intervention mechanism, reinforces investor's confidence and provide motivation for private resources to co-finance the FI and thus complement the European and public funds initially allocated to the fund. The co-finance effect will also be further described later on in the present chapter.

Leverage effect

Another important dimension of added benefit is the leverage effect that FIs could help achieve, through the use of intermediary institutions in the implementation of the FI. The leverage effect is achieved when an FI is channelled to the final recipient through an intermediary institution that finances part of the financial product that is provided to the recipient. The managing structure of the FI and the intermediary agree on the portfolio of finance products to be built in a certain amount of time. The use of intermediaries increases the number of potential recipients and reinforces the respective markets where these intermediaries operate in. For instance, in the case of a risk sharing loan instrument, the final product is a loan that originates partly from the FI and partly from the commercial bank that is used as intermediary. The higher the leverage achieved by the FI, the higher the quantitative value added.

A leverage effect however is also achieved at the project level. The final recipient of the FI has to invest its own resources for the project that otherwise (without the FI) would probably not have found the way to be invested in the market. This leverage effect is often more difficult to quantify since it depends on the project, however it often consists of a 20% to 30% of the project. In the case of more socially oriented interventions, the leverage effect at the project level is often weaker than in cases where the beneficiaries are companies.

As for the target groups of the HRD OP, these final recipients have been identified in Chapter 3. They are:

- Business creators;
- Self-employed business creators;
- Companies supported by the HRD OP for 2014-2020 that develop or finance training to improve the employability of their employees;
- Vocational training centres; education and training organisation and institutions; and information and professional guidance centres that provide counselling services and training on entrepreneurial, managerial and business skills to the target groups identified and listed above;
- Cooperatives and specialised enterprises; and
- Social-entrepreneurs.

Since these recipients may have different business plans and needs, it is complicated to anticipate a leverage effect that would cover all the target groups. As already mentioned, the financing gap detailed in Chapter 6 has made emerged two different needs in terms of Financial Instruments:

- Micro-loans provided by commercial banks and MFIs to facilitate future loan financing from commercial banks. These micro-loans would be supported by FIs to be used for leveraging commercial banks' loans; and
- Micro-guarantee schemes using commercial banks and MFIs as financial intermediaries in order to provide collateral to the final recipients.

The leverage effects to be expected for these two instruments may be different. They however follow the same logic. The leverage effect is a calculation of the estimated additional public and private resources raised divided by the nominal amount of the ESIF funds expenditure. It is one of the components of the quantitative added value to be considered for a Financial Instrument. The calculation of the leverage effect integrates different financing sources apart from the ESIF funds, such as public national and regional financings or private financing. However: (1) own contributions from the final recipient are not taken into account; (2) the face value of the expenditure is counted irrespective of the financial nature (e.g. repayable or non-repayable); and (3) future investment cycles are not considered if there are any (e.g. revolving instruments).

An example for the leverage of funds reached in the last programing period of funds dedicated to similar initiatives as the ones of the HRD OP for 2014-2020 is the Progress microfinance initiative supported by the EIF. The aim of this Progress initiative is to make EU funding available for microfinance and create a leverage effect. Based on the information in Table 14 relative to Progress and the leverage generated by JOBS MFI (a leverage of 1:1.5 with the total micro-loan provision of EUR 9m with an initial budget of EUR 6m), it is to be assumed that Progress may provide a total of EUR 25.5m in Bulgaria, i.e. 1.5 times the EU contribution of EUR 17m. This leverage effect is achieved by co-investment from other financial institutions (Mikrofond, JOBS MFI and Société Générale), by the revolving nature of the funds, and by the products offered (i.e. a micro-loan to be reimbursed by the final recipient).

Since there is to date no Financial Instrument that targets the groups identified in the HRD OP for 2014-2020 in Bulgaria, the expected leverage effect may be difficult to anticipate. However, experience with guarantee funds in Bulgaria as illustrated in Chapter 5 and experience with micro-lending supported by Financial Instruments in other Member States may provide ranges of leverage to be anticipated:

- Guarantee funds in Bulgaria achieve leverage effects of 1:1.4 to 1:5.
- Micro-loans funding provided by commercial banks and MFIs to socially excluded and social enterprises in other Member States achieve leverage effects of 1:2 to 1:9[84]. And JOBS MFI in Bulgaria expects a leverage effect of 1:1.5.

Following this, it is assumed that a ***leverage effect of 1:1.4 to 1:5 for the micro-guarantee fund and of 1:1.5 to 1:9 for the micro-loan scheme*** **could be achieved through the use of FIs under the HRD OP**. It should be noted that these values are derived from information provided by experienced institutions in Bulgaria (including the National Guarantee Fund and the European Investment Fund) or abroad where the MFI market is more structured and developed, such as in France. For that reason, the leverage effects for the two envisaged FIs should be considered with a conservative approach.

Revolving effect

The revolving effect of the FI is generated by the fact that the support handed to the final recipient is provided in the form of repayable products. In the case of all FIs, either loans (generated by guarantee and risk sharing instruments) or equity, consist of repayable forms of support that will eventually be return to the fund or the governing structure of the FI and thus will be able to be reinvested in other causes.

The two envisaged FIs will have a revolving effect since they will enable the financial intermediaries to be refinanced through the activity generated by the new entrepreneurs, the supported micro-enterprises, the training centres and the social enterprises. All these final recipients will generate activity and revenues that will enable the reimbursement of the loans. These gains will then be injected in the Financial Instrument that will be able to generate new guarantees or new micro-loans. These returns generated by the revenues of the final recipients may consequently be invested back into the economy through other projects consistent with the objectives of the HRD OP. For HR development this is particularly relevant as this could help support more socially excluded entrepreneurs, training centres and social enterprises. This revolving effect increases the

[84] Information from French MFIs providing micro-lending has been used. Information from different French regions (Rhône-Alpes, Lorraine, Languedoc-Roussillon) and different institutions (ADIE, France Active, Initiative France and Réseau Entreprendre) have been used for benchmark and for estimating the anticipated leverage effect in Bulgaria.

efficiency and effectiveness of the FIs in comparison with grants since it aims at making the funding of the target groups more sustainable.

The revolving effects of the micro-loans provided by commercial banks and MFIs or supported by a micro-guarantee scheme depend on the characteristics of the loans. In other EU Member States, these microfinance schemes are usually designed for very short maturity (for instance up to 24 months) in order to help the micro-enterprises covering their working capital needs. These characteristics have however to be discussed and designed by the fund manager and the financial intermediaries.

Introduction of a risk-sharing approach to finance nearly-bankable projects

The use of Financial Instruments instead of grants enables to align the interests of both public and private entities. Following this, commercial banks may start considering financing projects that they previously considered non-bankable. In parallel, risks are shared between the funds managing the ESIF funding and the private entities, like banks and MFIs.

Reduction of the importance of grant-based support

The intensity of grant is an important dimension to be considered in the anticipated added value of a Financial Instrument. The lower the intensity of grant for a given final recipient, the higher the quantitative added value. If grants are not meant to disappear during the 2014-2020 programming period (as detailed in Section 7.3 below), the use of FIs is to be considered as another source of funding provided through market financial intermediaries (namely commercial banks and MFIs) in order to improve the use of public funding. In that respect, the more FIs are used when they are relevant and provide added value, the more final recipients are likely to receive financing.

As such, there could be scope for an intensity of grant that is significantly lower than the alternative grant option. Based on the anticipated budgetary allocation for the HRD OP, the total of up to EUR 845m is envisaged for the ESIF and YEI support for the two Priority Axes that intend to use FIs (PA 1 and PA 2). Since a detailed budget per Investment Priority is not available, if the total of funding of EUR 845m was used under Financial Instruments instead of grants, this would constitute another quantitative aspect of the added value brought by the FIs, in comparison with the use of grants.

Increase of the efficiency of the delivery of funds thanks to private expertise and local networks

Experience with Financial Instruments and the use of financial intermediaries to finance entrepreneurs and social enterprises have revealed in other Member States that leverage their own expertise in the selection of projects and mobilise their networks throughout a country is more efficient (i.e. less costly) and is able to address more final recipients than a centralised institution providing grants. In this context, such networks are more efficient because they work at a local level, are more knowledgeable of the regional difficulties and are able to mobilise their experienced staff to identify and attract potential local clients. In addition, entrepreneurs and social enterprises may acquire the habit to ask for financing to commercial banks and MFIs close to their activity more easily than to a centralised national entity. Following this, the disbursement and absorption of European funds that were provided through FIs and financial intermediaries over the 2007-2013 programming period to support micro-enterprises in other EU Member States may have been higher than those providing only grants. The mobilisation of banks' and MFIs' networks in the provision of micro-loans to the final recipients identified in the HRD OP would then help increasing the use and absorption of the ESIF funds planned.

Increase of flexibility and reduction of the administrative burden on final recipients

Since FIs are meant to be implemented and managed by private experienced entities, both private and public funding could be managed by professional financial institutions. This would increase flexibility by using the resources and inherent efficiency of these financial institutions; in addition to their local networks as already mentioned.

Moreover, if both the grants and FIs components are provided by one and the same institution this can ease the process and make it faster. If this option seems inappropriate for commercial banks which are not designed to provide grants, the MFIs, which are often associations, could provide FI-supported micro-loans along with grants to the targeted entrepreneurs and micro-enterprises. This would increase the efficiency of the product delivery and would improve the disbursement and absorption of the ESIF, for both the funds using FIs and those delivered through grants. However, there should be proper monitoring and controlling mechanisms put in place by the Managing Authority, the FI funds and the financial intermediaries in order to ensure that the ESIF funds are provided in an appropriate manner.

Improvement of cash flow management for final recipients

Grants are often provided "ex-post": the final recipient needs to advance the funding before receiving the grant that would reimburse his/her initial spending. This implies cash and treasury management that may create difficulties for the micro-enterprise. For that reason, having better access to micro-loans and collateral may be of better interest for the micro-enterprises which do not have to advance the funding but have to reimburse a loan. This enables the enterprise to have access to financing before its use and facilitates the overall cash and treasury management of the company. It also enables the company to have access to working capital financing while the set-up of grants is more adapted to investment funding.

Moreover, if the setting-up of FIs may be lengthy, once implemented, the latter have simple and short procedures. A loan can be granted to final recipients within a short period and through standardised procedures operated by selected financial intermediaries. On the other hand, grants may have complex and lengthy procedures. Grants may be granted several months after the application/payment request has been submitted. This time lag, in addition to specific regulations related to the amount of the advanced, interim and final payments of the grants, may be seen as a barrier to a successful and in time project completion.

Provision of working capital financing to final recipients

The target groups identified in the HRD OP for 2014-2020 firstly need financing to cover their working capital needs. These needs are currently covered neither by the available financing from commercial banks and MFIs which do not provide enough financing nor by grants whose set-up is more adapted to investment funding. The design and implementation of the envisaged FIs aims at improving the access to working capital financing of target groups which currently lack such financing (entrepreneurs from socially excluded populations and micro-enterprises needing short-term financing to retain their staff) or which are currently exclusively financed by grants.

Improvement of MFIs' capacity

The use of the ESIF funds through the MFIs would help them structuring and deepening the microfinance market in Bulgaria which is currently under-developed in regard to the number of potential clients, i.e. newly created companies and micro-enterprises. This new source of financing may be used by the MFIs to finance their day-to-day activity: finance their Human Resources spending, finance their initiatives to develop their networks throughout the country, and financially support their communication strategy. In parallel, having more clients would incentivise the MFIs to develop more standardised and automated credit assessment and due diligence methods. These new methods would help manage more projects and finance more entrepreneurs and micro-enterprises.

Moreover, since MFIs are meant to provide entrepreneurs and micro-enterprises with support on business plan drafting, mentorship, legal and fiscal advice, and research for finance (such as facilitating relationships with other financial institutions), supporting MFIs structuring the market will have a direct impact on the quality of the projects proposed by entrepreneurs and facilitate their future financing by banks; in addition to the micro-loans received from the MFIs.

Other important socio-economic benefits

Financial Instruments may also play an important role in addressing socio-economic aspects of the market failures identified in Chapter 6. In addition, they could serve in the fulfilment of the policy objectives highlighted in the HRD OP and presented in Chapter 3. The progress and achievement of these objectives may also serve as indicators to monitor the qualitative dimensions of the FIs' added value. These benefits include:

- ***Promotion of entrepreneurs and the entrepreneur spirit***. The number of micro-enterprises in Bulgaria is stable over the past few years. It is even decreasing in 2011 in comparison with 2010 (-0.2%). This evolution is different from the rest of the European Union where the number of micro-enterprises, and especially 0 employee companies, is increasing. This is one of the reasons why the Managing Authority aims at promoting entrepreneurship and support business creation in Bulgaria over the 2014-2020 programming period. The use of Financial Instruments in that perspective may add value since it may complement the grants already provided and use channels (i.e. commercial banks and MFIs) that entrepreneurs may have better knowledge of and better access at the local level. Facilitating the access to finance for entrepreneurs and removing barriers such as collateral requirements thanks to a micro-guarantee fund may incentivise socially excluded people to create their own company. Moreover, previous experience in the EU has illustrated that diminishing the use of grants in favour of FIs favour the entrepreneurship spirit.
- ***Job creation***: The HRD OP aims at creating jobs through business creation (entrepreneurs from socially excluded populations creating their company, including in the social economy sector) and staff hiring in existing micro-enterprises (micro-enterprises supported to develop their business and hire new people). Financial Instruments may support this objective thanks to better access to loan financing for entrepreneurs and existing companies already heavily in debt which are rejected by commercial banks. FIs that may be developed and implemented over the 2014-2020 programming period would aim at leveraging loan financing from commercial banks either with micro-loans or with a micro-guarantee fund.
- ***Reduction of unemployment***. Unemployment is one of the main socio-economic challenges of the Bulgarian economy, especially for socially excluded populations. Most of the measures proposed in the HRD OP for 2014-202 aims at reducing unemployment in the country. This implies job creation as detailed previously but also staff retention. In order to do so, Financial Instruments may be used to support micro-enterprises willing to keep their staff in order to improve their employability through training. FIs may consequently support micro-enterprises accessing loan financing to develop or finance training for their employees. This would incentivise the companies to retain their staff and obtain financing despite their indebtedness while improving the overall employability of their employees.
- ***Employability of employees and job flexibility***. Similar to the rest of the European Union, employees in Bulgaria have to become more and more flexible to adapt to a changing working environment. Support the access to finance for training centres and micro-enterprises willing to finance training for their staff would consequently improve the employability of the employees the most at risk of unemployment. The use of FIs would provide added value since commercial banks and MFIs currently do not finance these training sessions. Moreover, the training centres that are working with the Employment Agency are mostly financed by the fees paid by the trainees (under the voucher scheme), which as previously pointed out are not immediately reimbursed. This requires administrative procedures and "ex-post" financing while micro-loans may be easier to manage because they do not involve the cash and treasury management difficulties posed by grants.

- ***Improvement in the quality of the financed projects***. In comparison with projects financed by grants, it is to be expected that the projects financed via Financial Instruments and consequently by private financial intermediaries (commercial banks and MFIs) are of better economic quality and more sustainable. This is due to the fact that these projects have to reimburse loans and consequently need to be sustainable. They have also been previously assessed by commercial banks and MFIs during the evaluation process conducted by experienced financial experts.
- ***Reduction of the urban exodus and promotion of the polycentric model through local financing support***. Leveraging the networks of commercial banks and MFIs to finance entrepreneurship and the social economy would be more efficient than using grant in a centralised manner. It would also avoid entrepreneurs having to move to urban areas and especially to Sofia region to develop their projects and find financing.
- ***Support and structuring of the social economy sector***. Up to now, the social economy sector in Bulgaria is not clearly defined and would require more structuring. Support the financing of social enterprises would imply to clearly define the latter, identify their main needs in terms of working capital and investment, and to facilitate the understanding of financial specialists among commercial banks and MFIs who would focus on the financing needs of social enterprises in order to address them. In parallel to a more clearly defined legal framework, the support to financing for social enterprises would help these companies to develop and provide services and offer jobs to unemployed people.
- ***Foreign direct investment***: The development of entrepreneurship, improvement of employees' employability and development of the social economy sector can help Bulgaria being more attractive to FDI. In return, this would bring further funding to Bulgarian companies.
- ***Reduction of poverty***. The overall objective of the HRD OP for 2014-2020 is to reduce poverty in the country. Bulgaria has the highest rate of people at risk of poverty in the EU (49%) and the funding under the HRD OP is aimed at financing actions to reduce this rate and increase the living standard of the poorest population in the country. Improving the access to finance of the target groups identified in the Operational Programme for Human Resources Development is one of the available means to reduce poverty. The rationale behind the use of FIs has been detailed in the different dimensions of the added value and illustrates the extent to which FIs supports business creation and existing micro-enterprises experiencing difficulties in accessing finance.

7.2. Assessment of consistency with other forms of public intervention

Analysing the consistency between the envisaged FIs under the HRD OP for 2014-2020 and other forms of public intervention addressed to similar markets aims at identifying conflicting elements or overlaps. It requires considering two types of public interventions:

- Existing Financial Instruments addressing the target identified in the HRD OP for the 2014-2020 programming period in Bulgaria;
- Other public interventions that may target the groups identified in the HRD OP but not with Financial Instruments.

Considering the first set of public interventions, the only FI currently implemented in Bulgaria and targeting socially excluded people is the Progress initiative initiated with EIF funding and leveraging financing from JOBS MFI, Mikrofond and Société Générale. As already described, this initiative started in 2011 and has an estimated leverage effect of 1.5 with an estimated total provision of micro-loans of EUR 25.5m. The envisaged FIs for the HRD OP would be complementary to the existing Progress initiative because:

- The envisaged FIs would provide not only micro-loans but also micro-guarantees which currently do not exist in Bulgaria. In that sense, they would provide a better access to loan financing from commercial banks, something that the Progress initiative does not provide nowadays.

- The envisaged FIs would be provided to final recipients through a very limited number of financial intermediaries. For that reason, there will be no crowding-out effect because several Financial Instruments providing microfinance products (micro-loans and micro-guarantees) may coexist in Bulgaria.
- The financing gap estimated in Chapter 6 is very important. This factor justifies the co-existence of several Financial Instruments providing micro-loans or supporting the provision of loans through micro-guarantees.

Since no conflicting element or overlap emerges from this analysis with the Progress initiative, no duplication of work or additional administrative burden is to be expected for the Managing Authority or for the final recipients which may receive their financing either via the Progress initiative or via the envisaged FIs under the HRD OP for 2014-2020.

These envisaged FIs are consequently consistent with the existing FI addressing the same targets in Bulgaria. They consequently comply with Article 37 (2) (b) of the CPR.

Considering the second set of public interventions, the HRD OP is to be considered in the framework of several public initiatives that address disadvantaged people, but do not include FIs to pursue their purpose. These interventions are detailed below.

The other Operational Programmes co-financed by ESF funds

Two other OPs are co-financed by ESF funding. Both of them are complementary to the HRD OP and the envisaged FIs under this Operational Programme.

- The Science and Education for Smart Growth Operational Programme (SESG OP) for 2014-2020

  The SESG OP will be co-financed by ESF funds, like the HRD OP. This OP aims at addressing the needs of the market in terms of education of the future labour market entrants. It will notably finance vocational education for students. Since the two OPs aim at improving the access to the labour market of two different populations (students on the one hand and disadvantaged people on the other hand, including young unemployed people) and unemployment is one of the most important challenges of the Bulgarian economy, these two public interventions are complementary and not overlapping. While the first one (SESG OP) addresses students to avoid them becoming at risk of exclusion, the second one (HRD OP) aims at financing vocational training for socially excluded people. The two OPs may however have the same final recipients: training centres which may propose training to both populations. For that reason, it is important to consider the administrative requirements that the training centres may have to fulfil to receive financing from both OPs in view of reducing these requirements or aligning them. The use of FIs offer however simplified procedures for final recipients since they would receive financing from commercial banks or MFIs which is expected to require less administrative requirements than grants and enable ex-ante disbursement.

- The Governance Operational Programme (GG OP) for 2014-2020

  The GG OP aims at improving the Bulgarian administration and in so doing will support capacity building in the administration. Similar to the analysis between the SESG OP and the HRD OP, the GG OP and HRD OP are complementary and to the largest extent do not overlap since they address two different populations. The only situation where both OPs could overlap concerns young unemployed needing training to enter the administration. The level of unemployment in Bulgaria is however so high that the two OPs are more complementary than overlapping even for this specific situation.

The Operational Programmes co-financed by ERDF funds

Five OPs are co-financed by ERDF funding. All of them are complementary to the HRD OP and the envisaged FIs under this Operational Programme.

- The Innovation and Competitiveness Operational Programme (IC OP)

  Both the IC OP and the HRD OP support entrepreneurship and business creation. The IC OP is however more oriented towards sectors related to technology and innovation. For that reason the FIs envisaged for both OPs appear complementary: those under the IC OP are meant to support ICT while those under the HRD OP are meant to support social inclusion, improve staff employability and help the social economy sector. Moreover, when considering the important financing gap related to social inclusion, the capacity to call upon the FIs envisaged under both OPs can be help in order to promote entrepreneurs and support social inclusion.

  For these reasons, synergies between the FIs planned to be designed and implemented for the IC OP and those envisaged for the HRD OP are possible. The table below indicates the extent to which the objectives of the FIs of both OPs are complementary and how synergies may be created between them, as well as close cooperation for microfinance.

Objectives of FIs under IC OP	Objectives of FIs under HRD OP
1. Support to innovation; 2. Business creation from all types of business creators; 3. Support to existing SMEs of all sizes; 4. Support to all sectors.	1. Support to social inclusion either via business creation (business micro-loans) or via support to access to the labour market (personal micro-loans) 2. Business creation from people at risk of poverty and socially excluded persons; 3. Support to micro-enterprises in difficulties; 4. Support to training centres and social enterprises.

- The Regions in Growth Operational Programme (RG OP)

  Since the RG OP and the HRD OP have different scope and targets, they are not overlapping. They are however complementary with regards to the support to social infrastructure envisaged in the RG OP.

- The Environment Operational Programme (EOP)

  Synergies between the EOP and the HRD OP may be found in the area of the lifelong learning and training, where a combination of professional training in the environmental sector under the OPE are meant to promote employment and creation of new jobs, including jobs in the environmental and green sector. Such cooperation will also suggest the support for start-up businesses in sectors relating to environment protection, sustainable consumption and other eco-friendly-activities. Following this, both OPs are complementary and not overlapping.

- The Rural Development Programme (RDP)

  The analysis of the Bulgarian market environment has identified high level of unemployment in rural areas (see Chapter 4 above). A synergy between the RDP and the HRD OP may be realised in the area of training and job creation in rural areas. Moreover, promoting self-employment and job creation in sectors such as the food industry are in the scope of both OPs. This implies more complementarities than overlapping since disadvantaged or socially excluded people in rural areas may benefit from financing provided by both OPs. And, since unemployment is high in these areas, it is to the benefit of these disadvantaged populations to have access to both OPs' funding.

- The Maritime and Fisheries Programme (MFP)

  Both MFP and HRD OP have a strong focus on promoting human capital, job creation and social dialogue. Similar to EOP, the MFP will support vocational training of unemployed people in the field of fisheries in order to promote self-employment and job creation. The envisaged FIs under the HRD OP may support access to finance for this population and complement the actions envisaged under the MFP.

In parallel to the Operational Programmes currently under preparation in Bulgaria, two public interventions may have similar target groups as the HRD OP. These interventions are implemented at the European level and are detailed in the following paragraphs.

The European Union Programme for Employment and Social Innovation (EaSI)

EaSI is managed directly by the European Commission. It brings together three EU programmes managed separately between 2007 and 2013: PROGRESS, EURES and Progress Microfinance.

As of January 2014, these programmes form the three axes of EaSI. They support:

- the modernisation of employment and social policies with the **PROGRESS axis** (61% of the total budget);
- job mobility with the **EURES axis** (18% of the total budget);
- access to micro-finance and social entrepreneurship with the **Microfinance and Social Entrepreneurship axis** (21% of the total budget).

The total budget for 2014-2020 is EUR 919,469,000 in 2013 prices.

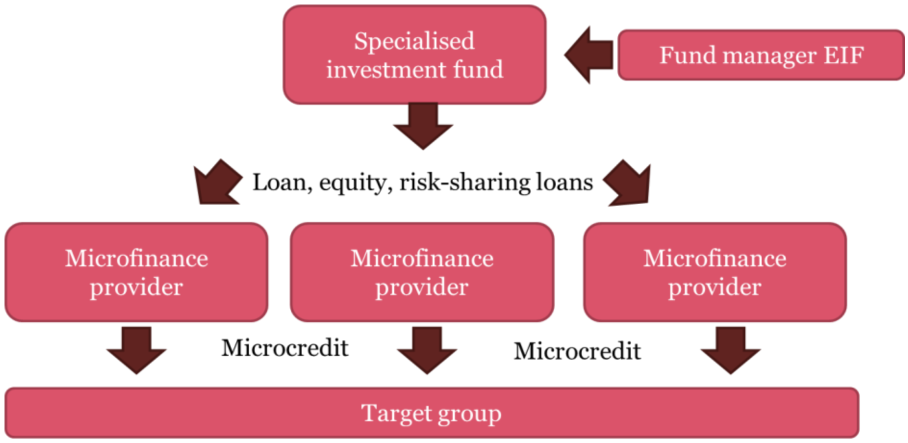
The **PROGRESS axis** will propose microfinance financing at the EU level. In that respect, stakeholders interviewed for the present study explained they would prefer apply to this fund managed in Luxembourg instead of MFIs at the national level. This illustrates the extent to which the Bulgarian microfinance market needs better structuring and simplified administrative processes, two elements that the envisaged FIs under the HRD OP for 2014-2020 may help to achieve.

As described in the HRD OP, attention will be made to avoid overlapping between financing provided via the PROGRESS axis and via the HRD OP. This control will be made at the individual project level. The HRD OP has also envisaged complementary between the two interventions since it considers that the objective is that a project first receive financing from the HRD OP before asking for financing from the PROGRESS axis managed centrally in Luxembourg[85]. Following this, the envisaged FIs under the HRD OP and the financing provided through the PROGRESS axis are complementary and will finance different stages of development of micro-enterprises.

The structure of the PROGRESS axis is presented below.

[85] HRD OP, 2014.

Figure 24: Structure of the PROGRESS axis of the EaSI



Source: Current and future use of financial instruments within the ESF, 26 October 2012, European Comission.

The purpose of the **EURES axis**[86] is to provide information, advice and recruitment/placement (job-matching) services for the benefit of workers and employers as well as any EU citizen wishing to benefit from the principle of the free movement of persons in the European Union. The EURES initiative is consequently aligned with the objectives of the HRD OP aiming at favouring labour mobility in Europe and facilitating access to the labour market. Another synergy between the HRD OP and the EURES initiative lies in the fact that the latter has a network of more than 850 advisers that are in daily contact with jobseekers and employers across Europe. The disadvantaged people who may benefit from the envisaged FIs under the HRD OP may also benefit from this network to find a job.

The **Microfinance and Social Entrepreneurship axis** supports actions in two thematic sections:

- microcredit and microloans for vulnerable groups and micro-enterprises;
- social entrepreneurship.

Its objectives are to increase access to, and the availability of, microfinance for vulnerable groups who want to set up or develop their business and micro-enterprises, enhance capacity of microcredit providers and support the development of social enterprises by facilitating access to finace in particular.

The Youth Employment Initiative (YEI)

Another public intervention having an EU scope is the YEI. The Council adopted the recommendation establishing a Youth Guarantee in April 2013. It calls on Member States to ensure that all young people under 25 years old receive a good quality offer of employment, continued education, an apprenticeship or a traineeship within four months of leaving formal education or becoming unemployed. It includes guidelines for setting up such actions, covering in particular the need for stronger partnerships between all concerned stakeholders, early intervention and activation, and making full use of the EU funding.

The YEI fund included in the overall initiative is already meant to co-fund the HRD OP and notably Priority Investment 1 which is expected to use Financial Instruments. Following this, there is no overlapping of the two

[86] EURES - European Employment Services - is a cooperation network designed to facilitate the free movement of workers within the European Economic Area. Switzerland is also involved. Partners in the network include public employment services, trade union and employers' organisations. The network is coordinated by the European Commission. The main objectives of EURES are: (1) to inform, guide and provide advice to potentially mobile workers on job opportunities as well as living and working conditions in the European Economic Area; (2) to assist employers wishing to recruit workers from other countries; and(3) to provide advice and guidance to workers and employers in cross-border regions.

interventions considering that they are both considered in parallel and meant to finance the same target groups in a complementary manner[87].

7.3. Combination of Financial Instruments with grant schemes

The CPR sets the possibility of combining FIs with grants. This combination may take different forms and implies consistency and complementarity between the two financing products in order to avoid overlapping and market distortion.

When considering the market failures and suboptimal investment situations previously identified in Chapter 6 as well as the activities meant to be supported under the HRD OP (such as business creation, training and mentoring), blending grants with the envisaged FIs would provide added value since it would enable to finance complementary activities. For instance, the envisaged FIs (i.e. business micro-loans, personal micro-loans and micro-guarantees) would finance activities generating revenues conducted by the final recipients while grants would finance activities that do not generate revenues. In that perspective, grants can be developed to support micro-enterprises willing to finance training while micro-loans could be provided to training centres in view of covering their working capital needs. If both approaches aim at improving the access to training for employees in micro-enterprises, since the activity does not generate revenues in the first situation the use of grants is more appropriate while the second activity generates revenue to the training centres.

The grants to be blended with the Financial Instruments may consequently finance activities such as:

- Activities improving the capacity and employability of employees within existing micro-enterprises: training, coaching, and mentorship
- Activities improving the sustainability of the existing micro-enterprises: training of micro-enterprises' managers, support in business plan drafting, and information on existing financing opportunities
- Costs not generating revenues for social enterprises and training centres such as: Human Resources

In parallel, FIs would for instance support self-employed, newly created micro-enterprises, social enterprises and training centres in building and developing a financial history with financial institutions such as commercial banks and MFIs. This financial history would help them having better access to finance when they would sought for more financing in the near future.

The design and implementation of both FIs and grants under the HRD OP for 2014-2020 have consequently to be considered in a comprehensive and coherent manner in order to ensure the complementarity and coordination of the two financing products.

7.4. Additional public and private resources to be potentially raised by Financial Instruments

One of the expected benefits of FIs is to attract private investment and other public funding, notably thanks to risk-sharing financing schemes. As a general rule, these additional resources can come from public sources at European, national, regional and local levels, as well as from private investors and financial institutions. This is particularly relevant in the context of budgetary constraints or when private investors show restrictions on their risk appetite, their risk bearing capacity or are not fully confident in the market and would like to share risks. Pooled resources may lead to synergies and a more efficient use of the funding available. It may also help

[87] European Commission, EU measures to tackle youth unemployment.

structuring markets thanks to a more advanced involvement of financial institutions that become financial intermediaries.

The following paragraphs present the potential additional public and private resources that could co-invest in the envisaged FIs under the HRD OP.

7.4.1. Additional public resources

In addition to the funding provided via the HRD OP, several public actors may co-invest in the envisaged FIs at different levels (Fund-of-Funds if any, fund, project). These actors may be working at national or regional level. At national level, the identified potential co-investors are:

- **The Bulgarian Development Bank (BDB)**. The BDB is a financial institution owned at 99.9% by the Bulgarian State. Its main objective is to support Small and Medium-sized Enterprises and especially start-ups.
- **The National Guarantee Fund (NGF)**. Up to date, the NGF of Bulgaria has been able to leverage funds with a leverage effect of up to 1:3. In that context, the NGF is a potential financial intermediary for the envisaged FI focusing on micro-guarantee under the HRD OP.
- **JOBS MFI** as part of the BDB is a financial intermediary of the Progress initiative and could also be a financial intermediary for the envisaged FIs under the HRD OP.
- **The future Fund-of-Funds managing ERDF funds (following the existing JEREMIE Holding Fund)**. Following the experience of the JEREMIE initiative in Bulgaria, new FIs could be developed under the Innovation and Competitiveness Operational Programme (IC OP). These FIs may be developed under a new Fund-of-Funds in view of managing ERDF funding. ESF funding from the HRD OP could be co-invested in this future Fund of Funds in order to create synergies between the two ESIF funds and the two OPs (HRD OP and IC OP).

7.4.2. Additional private resources

Financial Instruments also aim to attract private investors in order to create leverage. In that perspective, incentives such as risk-sharing schemes have to be designed to ensure risks are diversified and balanced between the public and private entities.

As mentioned in Chapter 6 focusing on the supply-side of financing, there is to date in Bulgaria:

- 29 commercial banks including 6 branches of foreign banks, and
- 9 microfinance institutions (excluding JOBS MFI as already mentioned).

If selected via a call for proposals by the Managing Authority in order to participate in the structure of the envisaged Financial Instruments and maybe manage a part of the FI, these private actors may bring additional resources to the funding planned in the HRD OP. Some of these potential financial intermediaries have previous experience with EU funding such as the JEREMIE or the Progress initiatives over the 2007-2013 programing period.

The interviews conducted under the present study however revealed that important incentives will be needed to involve these private actors and integrate them in the envisaged schemes and Financial Instruments under the HRD OP for 2014-2020. As detailed in Chapter 6 previously, the target groups identified in the OP do not constitute a specific interest for the potential financial intermediaries (commercial banks and MFIs) and the final recipients analysed in Chapter 6 do not generally receive financing from these financial institutions since they are most of the time financed by grants only.

7.5. Other stakeholders to consider

This section focuses on stakeholders working at the international, EU or national level which may not be considered as potential co-investors in the envisaged FIs but need to be taken into consideration in the general implementation framework of the FIs under the HRD OP. They may: (1) provide networks to facilitate exchange of ideas, experience and best practices and/or (2) help raising awareness of the benefits in the use of Financial Instruments for Human Resources Development.
The benefits of transnational cooperation are first presented. The different stakeholders to consider in the implementation of FIs under the HRD OP are then listed.

Transnational cooperation

Over the 2007-2013 programming period, the ESF could benefit from the EQUAL initiative to promote transnational and innovative actions. It budget was of EUR 3bn and represented around 2.5% of the total ESF budget. In contrast to the 2007-2013 programming period, where the European Commission had the lead for stimulating and supporting cooperation between Managing Authorities, the latter have to date the responsibility to coordinate, exchange lessons learnt and good practice and, when necessary and feasible, work together for the development and implementation of Financial Instruments.

Other cooperation and network supporting the development of Financial Instruments

Hereafter is a list of cooperative schemes and networks promoting Financial Instruments in the European Union.

- **The European Venture Philanthropy Association (EVPA)**
  The EVPA is an association of social investors, venture philanthropists and foundations committed to using venture philanthropy and social investment tools to target societal impact. Their members' focus is to offer efficient funding to Social Purpose Organisations (SPOs) such as social enterprises in Bulgaria. They focus on enterprises and NGOs at all stages of development, where venture philanthropy and social investment complement and strengthen other forms of funding. The network's aim is to provide them with both financial and non-financial support in order to increase their societal impact. In so doing they use both social investment and grants. These two forms of funding - social investment and grants – may be complementary to the grants and envisaged Financial Instruments under the HRD OP.

- **Communities of Practice on Inclusive Entrepreneurship (COPIE)**
  COPIE is a network of ESF Managing Authorities and implementing bodies actively involved in opening up entrepreneurship to all parts of the society.

- **The ESF - Age Network**
  The aim of the network is to make more effective use of ESF opportunities for age management strategies, programmes and projects through networking and mutual learning between Managing Authorities.

- **The European Network on Empowerment and Inclusion**
  The Learning Network on Empowerment and Inclusion builds on work from the platform "EQUALising the Workplace – Diversity in Action" funded by the EQUAL initiative. This notably involves the organisation of exchange events and the conduction of policy forums to produce recommendations about diversity at work, social inclusion, anti-discrimination and employment policies.

- **The Gender Mainstreaming Network**

  This network supports Managing Authorities to make better use of the gender mainstreaming strategy in improving the implementation of Operational Programmes using ESF funding.

- **The Increasing the participation of migrants and ethnic minorities in employment (IMPART) initiative**

  IMPART is a learning network aiming at proposing solutions to increase the participation of migrants and ethnic minorities in employment. In so doing, it proposes diagnostic and diffuses lessons learnt. It focuses on the validation of migrants' skills, the fostering of anti-discrimination approaches at work and the development of integrated territorial approaches.

- **The Social Economy Network**

  This network addresses five key themes in relation to the social economy: (1) community law and social services of general interest; (2) measurement of social added value and quality standards; (3) development of socially responsible public procurement and public social partnership; (4) social franchising; and (5) Financial Instruments and mechanisms of the ESF allocation to the social economy.

- **The European Network on Youth Employment**

  The aim of this network is to identify good practices through the execution of baseline studies, peer reviews and study visits. It has also developed a common reference framework for employment policies for the young. Finally, the network proposes recommendations for national and European policies in the field of youth employment. The network has three working groups focussing on the following themes: (1) entrepreneurship, (2) education and vocational counselling, and (3) mobility.

In addition to these networks, the implementation of FIs may also benefit from the actions of ***Invest in Bulgaria*** which aims at raising the awareness of potential investors about the investment opportunities in the country.

7.6. State Aid dimension

It is important to assess the State Aid implications and dimension of the envisaged FIs upfront right at the beginning of the design phase. This is because the applicable State Aid compatibility legal base is relevant for the main parameters of the design of the FIs, in particular as regards eligible undertakings, maximum amounts per beneficiary, the financial conditions attached to them, and the governance structure.

State Aid control consists of three assessments:

1. Assessment of whether the measure constitutes State Aid within the meaning of Article 107 (1) of the Treaty on the Functioning of the European Union (TFEU); e.g. State Aid can be excluded if the FI respects the market economy investor principle, i.e. if the FI is market-conform;
2. If the measures constitutes State Aid, assessment whether it can be found compatible without notifying it to the European Commission, e.g. because it fulfils the requirements of a *de minimis* Regulation or a Block Exemption Regulation or if the if the envisaged FI is set up as an off-the-shelf instrument (FIs complying with the standard terms and conditions laid down by the Commission - Art 38 (3) of the Common Provisions Regulations, CPR), since the design of such instruments ensure that they do not need to be notified to the Commission; and
3. If the measures constitutes State Aid, and does not fulfil all the conditions of the rules that exempt it from notification, it has to be notified to the European Commission which carries out a compatibility assessment

of the aid measure with the internal market according to the provisions of Article 107 (3) TFEU and its implementing rules, prior to the implementation of the FI.

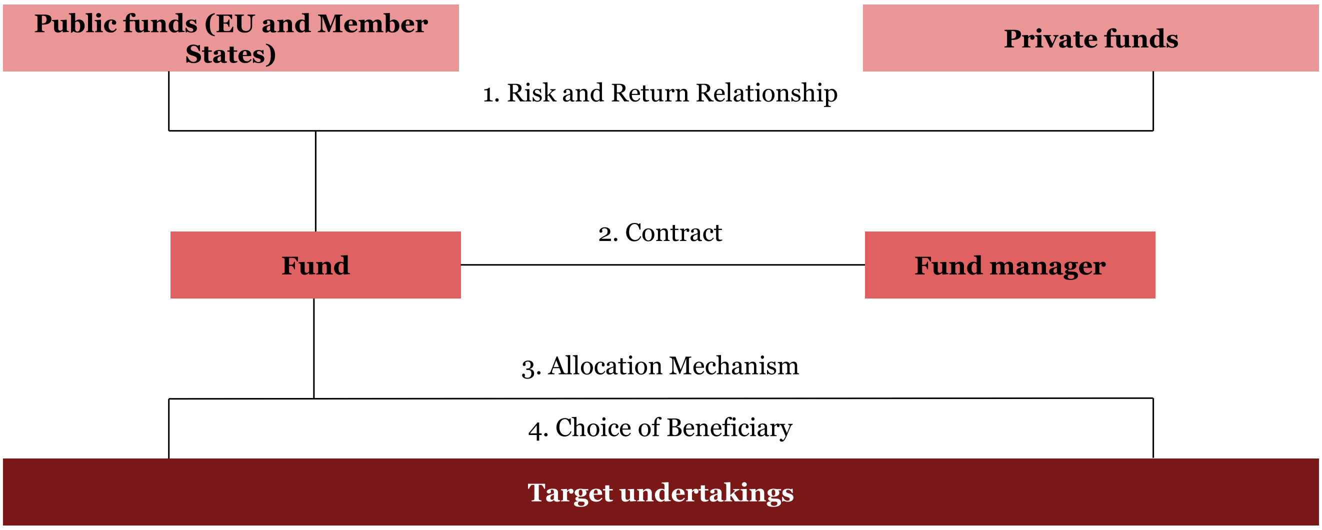
The State Aid assessment shall answer the following questions:

- Is the aid measure aimed at a well-defined objective of common interest?
- Is the aid well designed to deliver the objective of common interest, i.e. does the proposed aid address the market failure or other objectives? Is there a need of intervention?
- Is the aid an appropriate policy instrument – more appropriate than other possible instruments?
- Is there an incentive effect, i.e. does the aid change the behaviour of the aid recipient?
- Is the aid measure proportionate to the problem tackled, i.e. could the same change in behaviour not be obtained with less aid?
- Are the distortions of competition and effect on trade limited, so that the overall balance is positive?

Article 37 (2) of the CPR not only refers to the possible State Aid implications but explicitly mentions two of the key elements of the State Aid assessment, namely the proportionality of the envisaged intervention and the minimisation of the market distortions by the intervention. Therefore the design of each FI has to follow the detailed rules set out in the applicable State Aid legal basis.

Managing Authorities should determine whether the envisaged FIs constitute State Aid at any level. If the MA is not sure, it can always notify the planned measure for legal certainty to the European Commission (DG Competition), which can provide assurance in that regard ultimately in the form of a decision. Since the FI will be controlled by the MAs (shared management, with or without national budget resources) and as the private undertakings involved might operate in competitive cross-border markets, the assessment will focus on the existence of a selective economic advantage within the meaning of Article 107 (1) TFEU. Such an advantage can be granted at different levels, as described in figure below.

Figure 25: Classification assessment of the FI



Source: Ex-ante assessment methodology for financial instruments in the 2014-2020 programming period

First level: private investors (risk and return relationship of the contributions)

At the first step, the analysis aims to determine whether the State Aids are granting to private investors. State Aid could be excluded at this level if there is a *pari passu* and *pro rata* distribution of risk and rewards between the public and private investors and the contribution of the private operators is economically significant.

According to the Risk Finance Guidelines, the Commission will consider the investment to be effected *pari passu* between public and private investors, and thus not to constitute State Aid, where its terms would be acceptable to a normal economic operator in a market economy in the absence of any State intervention. This is assumed to be the case only if public and private investors share exactly the same upside and downside risks and rewards and hold the same level of subordination, and normally where a significant proportion of the funding of the measure is provided by private investors, which are independent from the companies in which they invest. The Commission considers that, in the case of risk finance measures, 30% independent private investment can be considered economically significant.

In order to attract private investors where situations of market failure exist, FIs may need to provide preferential remuneration, i.e. grant sub-commercial terms for private investors. For instance, the public investor may accept to assume the first loss, invest on less advantageous terms than private investors (i.e. non *pari passu* investment), or the private investor may receive more from the returns. It is to be noted that in the case of certain types of FIs, e.g. typically loan or guarantee measures, the financial intermediary, like a bank or a MFI, is the private investor at the same time.

Second level: Financial intermediary and its management

The second step will analyse whether the terms of the contract between the Managing Authority and the financial intermediary on the one hand, and the manager/management and the financial intermediary on the other hand, reflect normal market conditions. MAs should carry out this analysis under the “market economy operator principle”.

It will also be examined whether all ESIF funds contributed are passed through to the target undertakings. The question is whether the fund is a mere clearing mechanism or an intermediary vehicle for the transfer of aid as opposed to an entity which profits from Member States’ contributions. State Aid could be excluded at this level if it becomes clear that all funds are forwarded to the selected final recipients.

In many cases of former experience in the use of EU funds, not all funds were transferred to the final recipients. In most of these cases, management costs and fees were paid by the programmes. In such cases, market-conform remuneration, including for the administrative costs, is not considered as state aid, if the intervention is otherwise *pari passu* or market conform.

Third level: Target Undertakings (final recipients)

For final recipients, State Aid can be excluded if the FI respects the “market economy investor principle”. If not, the eligibility criteria and the maximum amounts play an important role. State Aid for them is not subject to notification if it is covered by a block exemption regulation or does not exceed the *de minimis* threshold. Therefore, the design of the FI including maximum amounts of support will play a crucial role in determining whether the final recipient will be considered as aid recipient or not, and whether the FI will require a notification.

The figure in Annex 8, presents an overview of the process followed by the European Commission when performing the compatibility assessment for an FI according to Article 107 (3) (c) TFEU. It is of importance that Managing Authorities know this process when developing the FIs.

Overall, FIs may be better suited to overcome some market failures than grants if:

- The FI is set up to cover multiple sectors and to address multiple issues it could minimise the overall level of State intervention, since this set up facilitates risk mitigation.
- The risk of the portfolio can be reduced with the involvement of experienced intermediaries through the establishment of professional incentives to achieve public goals.

8. Proposed guidelines for an investment strategy

This study has provided an analysis of supply and demand for financial products to human resources development. It has also proposed the different aspects of added value that could be benefitted from if FIs were to be implemented to support it. Existing Financial Instruments have been described, along with the lessons learnt from them in the last programming period.

Taking into account the findings presented in the aforementioned analyses, this section will present the proposal on how best to deliver the products demanded by the market under the HRD OP. Section 8.1 will summarise the market failures identified in the analysis and detail the financing needs currently not covered by the financial products available on the market to date. This section will consequently detail the envisaged FIs to improve access to finance of the target groups identified in the HRD OP for the 2014-2020 programming period. Section 8.2 will present the different governance structures that could be employed in line with current European regulations. Finally, Section 8.3 will present the proposed governance structure for dedicated FIs under the HRD OP.

8.1. The proposed Financial Instruments best suited to overcome identified market failures and suboptimal investment situations

The target groups identified in the HRD OP cover two types of beneficiaries:

1. Individuals who have financing needs to be trained, access the labour market or create their own company; and
2. Enterprises facing temporary difficulties and wiling to increase the employability of their staff through training or to sustain/expend their business, or training centres and social enterprises having bother working capital and investment needs.

On the supply side, it has been highlighted that commercial banks express low interest in lending small amounts to these target groups and/or final recipients, estimating they are non-bankable. In addition, the microfinance market in Bulgaria is weak and in decline despite the Progress initiative benefitting from the support of the European Investment Fund. These two types of financial institutions (commercial banks and MFIs) are however potential financial intermediaries in the set-up of the envisaged FIs under the HRD OP.

On the demand side, the priority for the individuals is to secure short-term financing to access training or the market labour and/or start a business. Micro-enterprises, training centres and social enterprises need micro-loans to cover their working capital needs and, to a lesser extent, invest.

The analysis has highlighted difficulties in accessing finance for all sets of final recipients. More particularly, there is a strong potential demand for inclusive finance either for personal micro-loans (finance for job seekers to support them accessing the labour market) or for business micro-loans (finance for entrepreneurs to support them creating a business). Business micro-loans would also be needed by existing micro-enterprises which currently do not have access to commercial banks or face MFIs having similar criteria then the banks. These loans would also be needed by training centres and social enterprises.

Following this analysis, clear market failures and suboptimal investment situations have emerged. These indicate that public assistance and the use of Financial Instruments may be required to facilitate the access to finance of the target groups indicated in the HRD OP for the 2014-2020 programming period. Recommendation may therefore be made to set-up and implement specific Financial Instruments for these target groups by using the ESIF funds under this OP in Bulgaria. In the following paragraphs, the market failures and suboptimal investment situations are first detailed. The major challenges related to the implementation of FIs under the HRD OP are also indicated. Then, the envisaged Financial Instruments aiming at reducing these market failures are presented.

8.1.1. Incentivise the banking sector to finance the target groups through risk-sharing financing schemes.

Over the 2007-2013 programming period, the banking sector has been active in using FEIs thereby developing a certain level of capacity. No Financial Instrument has however been developed for social inclusion or for financing the social economy via micro-loans or micro-guarantees. The exception is the Progress initiative which uses Microfinance Institutions and banks as financial intermediaries but its results are not available and not clearly visible on the market. Overall, commercial banks are reluctant to finance the identified target groups because the latter are considered as non-bankable. As a consequence, a public intervention and Financial Instruments enabling to transform non-bankable projects into nearly-bankable projects would benefit to the target groups. In that perspective, risk-sharing financing schemes could be developed to incentivise banks and MFIs providing their own funding in addition to the ESIF funds, and so create leverage. This would also enable the target groups and final recipients to receive the required funding for their projects and development.

8.1.2. Develop specific financial instruments to improve the supply of microfinance and help structuring the microfinance market.

The microfinance market is to date underdeveloped in Bulgaria in comparison to (1) the population socially excluded or at risk of poverty and (2) the number of micro-enterprises and the companies working in the social economy sector. The level of microfinance products provided by MFIs (entities without banking licenses) has gradually reduced, while the network of Microfinance Institutions remains inefficient, as most of the MFIs are lacking funding. In addition, the specialised Microfinance Institutions often operate like commercial banks in terms of risk, terms and conditions, while they should have an increased risk appetite and finance more risky projects. Over the past years, the microfinance market has not been sufficiently supported by public interventions and no Financial Instrument has been developed at the national or regional levels to support the MFIs providing more micro-loans to individuals, newly created business or existing micro-enterprises. Furthermore, the MFIs in Bulgaria currently provide only financing for newly created businesses and existing micro-enterprises. They do not provide personal micro-loans to support job-seekers, like other MFIs in the European Union. Finally, MFIs in Bulgaria are often under-capitalised and have difficulties covering their internal administrative costs. This translates into fewer projects financed and high interest rates for borrowers. Support to MFIs on that matter would help them develop their network in the country, better address the potential beneficiaries and be able to handle more projects. Developing standard administrative processes for all MFIs could also help providing more microfinance products to the target groups. Financial support to MFIs to cover administrative costs could for instance be financed via grants while the own financing provided by the MFIs could be supported by Financial Instruments under public interventions.

In the future, the development of microfinance products supported by Financial Instruments will need to build on the available financial intermediaries, namely the commercial banks and the MFIs, including the institutions already involved in the Progress initiative. Indeed, there is today no institution specialised on social inclusion proposition financing to the identified target groups and final recipients.

8.1.3. Support the access of training centres to micro-loans and promote training within micro-enterprises.

Training centres in Bulgaria are currently financed via the fees their trainees are paying, which make the ones working with the Employment Agency indirectly dependent by the grants funding the voucher scheme and thus as already explained in previous sections, often create a short term capital needs. In addition, micro-enterprises are currently not incentivised to train their staff when they experience temporary difficulties, while such training would be beneficiary to the company (better skilled workforce) and to the employee (improved employability). Coordination between grants and Financial Instruments could be envisaged in this general framework: while micro-enterprises could receive grants to finance training for their employees, the training centres could have access to micro-loans to cover their working capital and invest when needed. However, it has to be highlighted that grants remain the most relevant support to promote training and life-long learning.

8.1.4. Support the financing and structuring of the social economy sector.

The notions of “social economy”, “social enterprise” and “social entrepreneur” are currently not sufficiently defined in Bulgaria to allow financial institutions and public interventions to target them specifically in view of addressing their needs. In addition, these entities are to date exclusively financed via grants while some of them generate revenues from their activity and would be able to reimburse a loan. Clear definition could be determined thanks to more advanced regulatory frameworks existing in other EU Member States. With regards to financing, showing the banks and the MFIs that social enterprises may generate revenues and be considered as bankable, would support their access to finance and would diminish their dependency on grants. In order to do so, risk-sharing financing schemes would increase the risk appetite of banks and MFIs, and would facilitate the access of social enterprises and social entrepreneurs to micro-loans. A micro-guarantee fund available to commercial banks and MFIs would also enable the public and private stakeholders to share risks and facilitate the access of existing and newly created social enterprises to bank loans.

8.1.5. Develop a comprehensive strategy for a coordinated use of grants and FIs.

As mentioned in the analysis, the Managing Authority may continue using part of its available resources to support the target groups with grants in addition to the envisaged Financial Instruments funded under the ESIF funds. The design and implementation of both financing instruments should be determined in a complementary and comprehensive manner in order to create synergies and avoid overlapping and duplication of work. They need to be considered together as an integrated public intervention. This needs to be achieved not only to avoid overlapping, but also to optimise benefits for each instrument. For instance, while FIs are meant to finance revenue generating activities, grants could target activities that do not generate revenues but a key for the development of the company, such as the training of employees.

8.1.6. Support the initiatives and stakeholders providing mentoring and skills support to business managers and entrepreneurs.

Business environment is currently challenging in Bulgaria, especially for the target groups identified in the HRD OP. Most of those which become entrepreneur do not have enough financial knowledge and are not well-equipped to negotiate with financial institutions and build a financial history with them. They also lack knowledge of the financial monitoring tools and managerial best practice in such areas as business development, accounting, human resources, commercial and marketing skills, legal requirements, and business plan preparation.

The use of the ESIF funds for technical assistance, most probably in the form of grants, with built-in mechanisms to support mentoring, support and counselling to job-seekers and entrepreneurs is strongly recommended for the 2014-2020 programming. This technical assistance would support the sustainability of the new and existing companies managed by socially excluded people or working in the social economy sector.

As guidelines for an investment strategy, it is advised to the Managing Authority to devote a part of the ESIF funds in the following framework:

- With financial institutions (commercial banks, Microfinance Institutions, guarantee funds) having experience in Financial Instruments and able to manage EU funding (in terms of efficiency, risk management and audit);
- By orientating the use of the ESIF funds to the target groups identified in the HRD OP and the final recipients defined in the analysis and detailed in Chapter 6;
- By leveraging previous experience with the JEREMIE Holding Fund set-up over the 2007-2013 programming period.

The final recipients to be considered for the design and implementation of the Financial Instruments are:

- Individuals needing financing for a training in view of creating a company or obtaining a new job;
- Individuals needing financing to create a company;
- Individuals needing financing to find a job;
- Micro-enterprises needing financing to finance a training for their employees;
- Training centres (Vocational training centres; education and training organisation and institutions; and information and professional guidance centres that provide counselling services and training on entrepreneurial, managerial and business skills); and
- Social entreprises (existant social entreprises and social-entrepreneurs).

As the market for FIs in the HR development was underdeveloped, in terms of infrastructure and capacity it may not be considered mature enough to absorb the fund needed to bridge the potential gap between the supply and demand, where the application of FIs were relevant. Therefore a pilot investment is proposed following the same proportion as the funds allocated for Priority Axis 1: Promotion of economic activity and development of inclusive labour market and Priority Axis 5 Social inclusion and promotion of social economy during the last programing period (EUR 32,603,025).

Considering the ESIF resources to be devoted under Financial Instruments for the 2014-2020 programming period, it could be suggested to invest a total of EUR 20m in the following products:

1. A micro-guarantee instrument to support access to loan financing for all final recipients detailed above;
2. A personal micro-loan instrument to support individuals financing a training and finding a job; and
3. A business micro-loan instrument to support individuals creating a company and micro-companies (including training centres and social enterprises) to cover their working capital needs and invest.

The following table synthetises the characteristics of the proposed Financial Instruments, including their expected impact.

Table 21: Overview of the proposed Financial Instruments under HRD OP

Financial Instrument	Amount (mEUR)	Expected leverage effect	Expected amount available to the target groups (mEUR)
Micro-guarantee instrument	10	From 1.4 to 5	From 14 to 50
Personal micro-loan instrument	5	From 1.5 to 2.5[88]	From 7.5 to 12.5
Business micro-loan instrument	5	From 1.5 to 2.5	From 7.5 to 12.5

Source: PwC, 2014.

These proposed Financial Instruments are detailed in the following section.

8.2. The proposed Financial Instruments

The three proposed are detailed in the following paragraphs. The technical characteristics of these FIs will have to comply with the State Aid regulation and could be inspired by the “off-the-shelf” Financial Instruments that the European Commission will develop and propose to the Managing Authorities of the European Union. As already mentioned, they can be blended with grants. Moreover, the proposed Financial Instruments could be completed by technical assistance programmes designed and implemented by the Managing Authority.

8.2.1. The micro-guarantee instrument

The first proposed Financial Instrument consists of micro-guarantees. The table below synthesises the characteristics of this proposed instrument under the HRD OP for 2014-2020.

Table 22: Characteristics of the micro-guarantee instrument

	Characteristics of the the micro-guarantee instrument
Nature / type of product	Micro-guarantee
Objectives	• Reduce the specific difficulties of the target groups and final recipients when accessing finance because (1) the financial institutions consider their project as too risky and/or not bankable and (2) they lack collateral • Support the provision of loan financing and potentially leasing financing to the target groups, especially for very small amount • Offers to cover credit risk of the financial intermediary (such as first-losses of a previously defined portfolio)
Scope of intervention	The FI is meant to over the whole country
Target groups	All final recipients identified (individuals and enterprises)
Expected advantages	• Decrease of the collateral required by the financial institution when seeking loan financing • Decrease of the interest rate of the loan (in comparison with a loan that does not benefit from the micro-guarantee) • Reduced cost for collateral, in comparison with market price
Details	• This instrument enables the provision of a guarantee to a financial intermediary that will be selected through a call for tender

[88] The range of the leverage effect expected for both the personal and business micro-loan instruments derives from the leverage effects observed for the Progress initiative in country and other micro-loan instruments in the European Union, considering also that the lack of experience in the use of micro-loan instruments in Bulgaria leads to a conservative approach in the definition of the leverage effect to be expected for the two instruments.

	• This guarantee may cover a significant part of the risk (*element to define during the due diligence with the financial intermediary*) related to loans inserted into a portfolio that would have been previously defined • This guarantee may cover the losses (losses related to the non-payment of the capital and the interests of the loan) that the financial intermediary may have • In line with the EU regulation, the types of financing that could be covered by the micro-guarantee are investment financing (fixed assets) and working capital financing • Steps relative to the reception, analysis, documentation and provision of loans to the final recipients will have to be handled by the financial intermediary, according to the existing and required market procedures. The financial intermediary will therefore have a direct credit relation with the final recipient
Initial amount provided by ESIF funds (mEUR)	EUR 10m
Expected leverage effect	From 1.4 to 5
Expected amount available to the target groups	From EUR 14m to EUR 50m
Socio-economic benefits	• Promotion of entrepreneurship • Job creation • Creation of new enterprises • Reduction of unemployment • Reduction of the urban exodus and promotion of the polycentric model through local financing support • Support and structuring of the social economy sector • Reduction of poverty • Improved quality of life
Consistency with the Common Strategic Framework	The micro-guarantee instrument would be consistent with the following thematic objectives (non-exhaustive list of Thematic Objectives): • TO 8 - promoting sustainable and quality employment and supporting labour mobility; • TO 9 - promoting social inclusion, combating poverty and any discrimination; and • TO 10 - investing in education, training and vocational training for skills and lifelong learning.
Potential partners	• Potential managers: the National Guarantee Fund, the existing JEREMIE First-Loss Portfolio Guarantee Fund, private fund managers • Potential contributors: NGF, future ERDF funds-of-fund, private financial institutions • Potential members of the investment committee: NGF, impacted ministries like the Ministry of Finance, the Ministry of Labour, the Ministry of Economy, the future ERDF funds-of-fund, and private financial institutions

Source: PwC, 2014.

Given the lack of experience with FIs providing micro-guarantees in Bulgaria, it is suggested that this new Financial Instrument be done through existing guarantees such as the Bulgarian National Guarantee Fund (NGF) or the guarantee schemes currently managed under the existing JEREMIE First-Loss Portfolio guarantee scheme. This would be beneficial for the following reasons:

- The increased budget would improve the advantage of an economy of scale in both cases; and
- Both guarantee funds have already gained the necessary experience and capacity to work with it.

8.2.2. The Personal Microfinance Instrument

The second proposed Financial Instrument provides micro financing to individuals under the HRD OP for the 2014-2020 programming period. It is synthesised in the table below.

Table 23: Characteristics of the personal microfinance instrument

	Characteristics of the personal microfinance instrument
Nature / type of product	Microfinance instrument below EUR 25,000
Objectives	• Reduce the specific difficulties of the target groups and final recipients when accessing finance because the financial institutions consider their project as too risky and/or not bankable • Establish a risk-sharing financing scheme with financial intermediaries in view of providing loans of very small amount to non-bankable individuals needing financing to have an improved access to the market labour (this is mostly to finance training or to improve the mobility of unemployed and disadvantaged people by financing bus tickets and/or car expenses)
Scope of intervention	The FI is meant to over the whole country
Target groups	• Individuals needing financing for a training in view of obtaining a new job • Individuals seeking a job or in need for financing to access the labour market (mobility).
Expected advantages	• Provision of micro-loans, potentially with no collateral requirement • Since the micro-loan will be on interest, the interest rate could be decreased thanks to the use of the micro-guarantee instrument proposed previously (the new interest rate would be lower in comparison to the one from a loan that does not benefit from the micro-guarantee)
Details	• Once selected, the financial intermediary will define a portfolio of predetermined micro-loans (this definition will be made with a predetermined volume and amount) • This portfolio will be financed by ESIF funding for a certain share (50% for instance) and by the selected financial intermediary for the remaining share (the remaining 50% for instance) • Each micro-loan provided via the financial intermediary will have an interest rate that follows the market conditions (basic rate plus margin related to the risk taken) • As already mentioned, the personal micro-loan instrument may also be supported by the micro-guarantee instrument to reduce the interest rates of the loans provided • In line with the EU regulation, the types of financing that could be covered by the personal micro-loan are the small investments needed by the final recipients (such as transportation and training expenses) • Steps relative to the reception, analysis, and provision of the micro-loan to the final recipient will have to be handled by the financial intermediary, according to the existing and required market procedures. The financial intermediary will also follow its own standards and procedures. Following this, the financial intermediary will have a direct credit relation with the final recipient
Initial amount provided by ESIF funds (m EUR)	EUR 5m
Expected leverage effect	From 1.5 to 2.5
Expected amount available to the target groups	From EUR 7.5m to EUR 12.5m
Socio-economic benefits	• Job creation • Reduction of unemployment • Employability of employees and job flexibility

	• Reduction of the urban exodus and promotion of the polycentric model through local financing support • Reduction of poverty • Improved quality of life
Consistency with the Common Strategic Framework	The personal micro-loan instrument would be consistent with the following thematic objectives (non-exhaustive list of Thematic Objectives): • TO 8 - promoting sustainable and quality employment and supporting labour mobility • TO 9 - promoting social inclusion, combating poverty and any discrimination • TO 10 - investing in education, training and vocational training for skills and lifelong learning
Potential partners	• Potential managers: JOBS MFI, the future specific microfinance fund under the future ERDF Fund-of-Funds for the 2014-2020 programming period, and private fund managers • Potential contributors: JOBS MFI, future ERDF funds-of-fund, and private financial institutions • Potential members of the investment committee: JOBS MFI, impacted ministries like the Ministry of Finance, the Ministry of Labour, the Ministry of Economy, the future ERDF funds-of-fund, and private financial institutions

Source: PwC, 2014.

As illustrated in the analysis, it may be useful to complement the provision of personal microfinance instrument with technical support to the individuals looking for financing. This support may include training, coaching and mentoring. This may require increasing and developing the internal capacity of the MFIs. Such development of the MFIs may call upon a public support that could include measures related to technical assistance under the HRD OP.

While it is recommended that Financial Instruments capitalise on any built-up experience in their use (as with the National Guarantee Fund and the existing JEREMIE Holding Fund), there have been no FIs used to support personal micro-loans, which constitutes to date a market failure. As such, it would be advised to provide support through FIs via MFIs and commercial banks that have experience with Financial Instruments under the Progress initiative or other MFIs and commercial banks that would need to learn the management of Financial Instruments and the use of the ESIF funds. As already detailed in the analysis, this Financial Instruments could also be complemented with grant support to have greater impact.

8.2.3. The Business Microfinance Instrument

The table below synthesises the characteristics of the business microfinance instrument that is proposed under the HRD OP for 2014-2020. It is the third proposed Financial Instrument.

Table 24: Characteristics of the business micro-loan instrument

	Characteristics of the business microfinance instrument
Nature / type of product	Microfinance instrument below EUR 25,000
Objectives	• Reduce the specific difficulties of the target groups and final recipients when accessing finance because the financial institutions consider their project as too risky and/or not bankable • Establish a risk-sharing financing scheme with financial intermediaries in view of providing loans of very small amount to non-bankable individuals willing to create their company and micro-enterprises needing financing to cover their working capital needs and/or invest
Scope of intervention	The FI is meant to over the whole country

Target groups	• Individuals needing financing for a training in view of creating a company • Individuals needing financing to create a company • Micro-enterprises that need financing to keep their business alive • Micro-enterprises that want to expand their business activities • Micro-enterprises needing financing to finance a training for their employees • Training centres • Social enterprises (existing social enterprises and social-entrepreneurs)
Expected advantages	• Provision of micro-loans, potentially with no collateral requirement • Since the micro-loan will be on interest, the interest rate could be decreased thanks to the use of the micro-guarantee instrument proposed previously (the new interest rate would be lower in comparison to the one from a loan that does not benefit from the micro-guarantee)
Details	• Once selected, the financial intermediary will define a portfolio of predetermined micro-loans (this definition will be made with a predetermined volume and amount) • This portfolio will be financed by ESIF funding for a certain share (50% for instance) and by the selected financial intermediary for the remaining share (the remaining 50% for instance) • Each micro-loan provided via the financial intermediary will have an interest rate that follows the market conditions (basic rate plus margin related to the risk taken) • As already mentioned, the business micro-loan instrument may also be supported by the micro-guarantee instrument to reduce the interest rates of the loans provided • In line with the EU regulation, the types of financing that could be covered by the business micro-loan are investment financing (fixed assets) and working capital financing • Steps relative to the reception, analysis, and provision of the micro-loan to the final recipient will have to be handled by the financial intermediary, according to the existing and required market procedures. The financial intermediary will also follow its own standards and procedures. Following this, the financial intermediary will have a direct credit relation with the final recipient
Initial amount provided by ESIF funds (mEUR)	EUR 5m
Expected leverage effect	From 1.5 to 2.5
Expected amount available to the target groups	From EUR 7.5m to EUR 12.5m
Socio-economic benefits	• Promotion of entrepreneurship • Job creation • Creation of new enterprises • Reduction of unemployment • Employability of employees and job flexibility • Reduction of the urban exodus and promotion of the polycentric model through local financing support • Support and structuring of the social economy sector • Reduction of poverty • Improved quality of life
Consistency with the Common Strategic Framework	The personal micro-loan instrument would be consistent with the following thematic objectives (non-exhaustive list of Thematic Objectives): • TO 8 - promoting sustainable and quality employment and supporting labour mobility • TO 9 - promoting social inclusion, combating poverty and any discrimination

	• TO 10 - investing in education, training and vocational training for skills and lifelong learning
Potential partners	• Potential managers: JOBS MFI, the future specific microfinance fund under the future ERDF Fund-of-Funds for the 2014-2020 programming period, and private fund managers • Potential contributors: JOBS MFI, future ERDF funds-of-fund, and private financial institutions • Potential members of the investment committee: JOBS MFI, impacted ministries like the Ministry of Finance, the Ministry of Labour, the Ministry of Economy, the future ERDF funds-of-fund, and private financial institutions

Source: PwC, 2014.

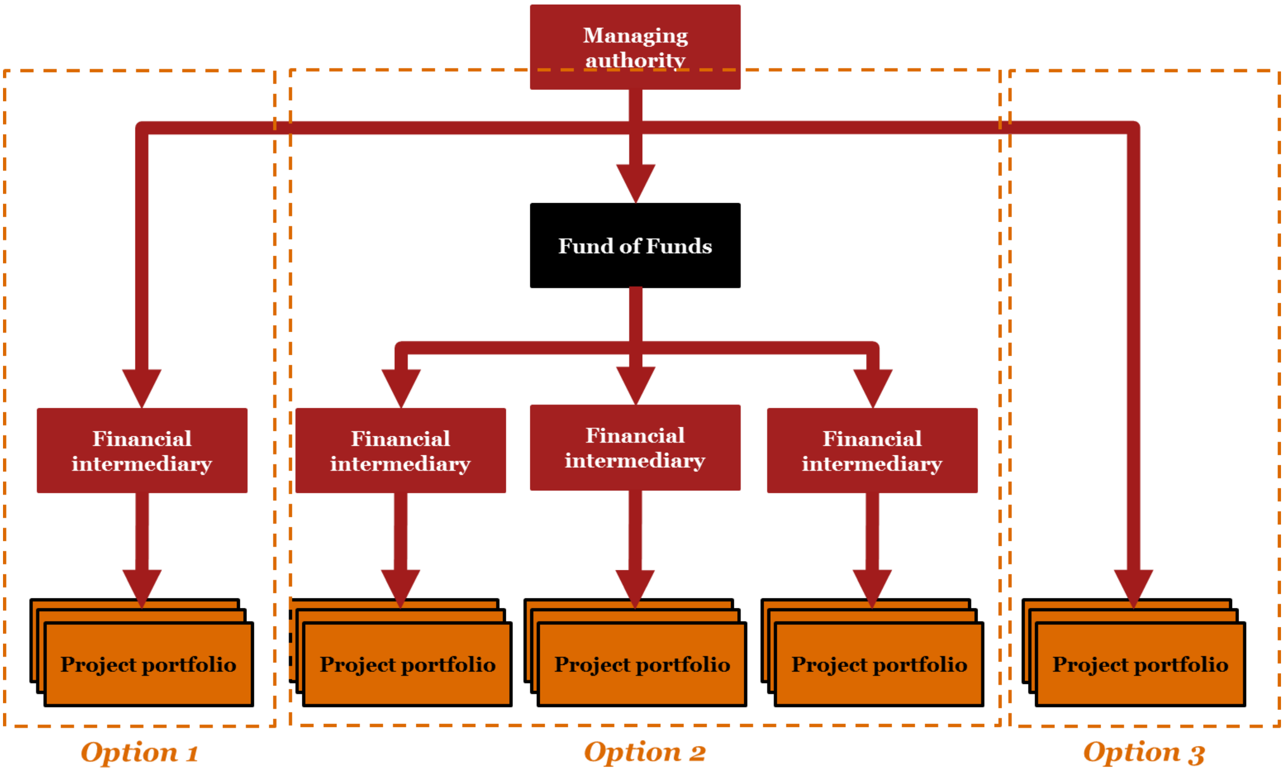
As already mentioned for the personal micro-loans, it may be also useful to complement the provision of business micro-loans with technical support to the individuals willing to create their company and existing micro-enterprises willing to develop. As already said, this support may include training, coaching and mentoring. This may require more developed internal capacity of the MFIs which could benefit from a public support, and more specifically measures related to technical assistance under the HRD OP.

As for the proposed personal micro-loan instrument, there is little experience with business micro-loan using Financial Instruments in Bulgaria. The only experience is the Progress initiative supported by the European Investment Fund, which has not had noticeable results on the microfinance market in the country. Following this and as for the personal micro-loans, it would advised to develop the business micro-loan instrument via MFIs and commercial banks that have experience under the Progress initiative or other MFIs and commercial banks that would need to learn the management of Financial Instruments and the use of the ESIF funds. Finally, the instrument could be complemented with grants.

8.3. Options for structuring Financial Instruments

Three possible options exist for the structuring of the Financial Instruments under the Common Provisions Regulation for the 2014-2020 programming period. They are presented in this sub-section of the study and are subject to the requirements of future regulations. These are exemplified in Figure 26 below.

Figure 26: The different possible structuring options for FIs

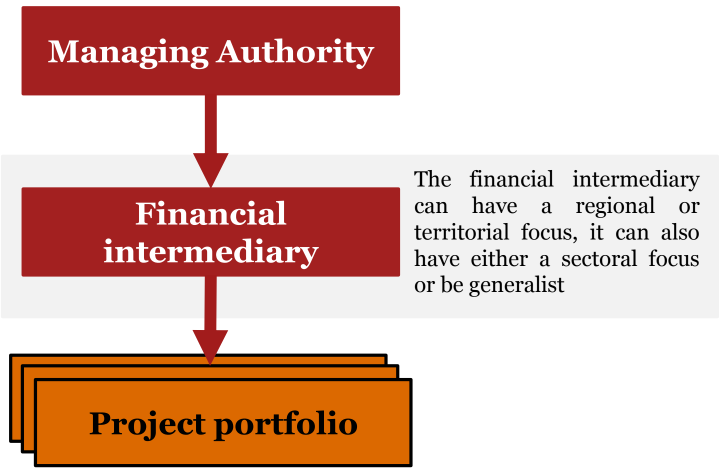


Source: PwC, 2014.

8.3.1. Option 1: Structuring a Financial Instrument without a Fund of Funds

If a single FI is established, a simple financial structure is the most suitable strategy. As shown in Figure 27, the MA would directly feed investment into the financial intermediary, which would then transfer this into the different projects, either individuals or micro-enterprises eligible under the HRD OP.

Figure 27: Functional diagram of the structuring of a Financial Instrument without a Fund-of-Funds



Source: CRP, PwC, 2014.

If the MA lacks the internal capacity and expertise about the operation of FIs, the management of EU funds, or financial competencies; it is recommended that the MA secure technical assistance to develop the necessary capacity to manage the financial intermediary. Advantages and weaknesses of this option are detailed in the table below.

Table 25: Advantages and weaknesses of a governance structure without using a Fund of Funds

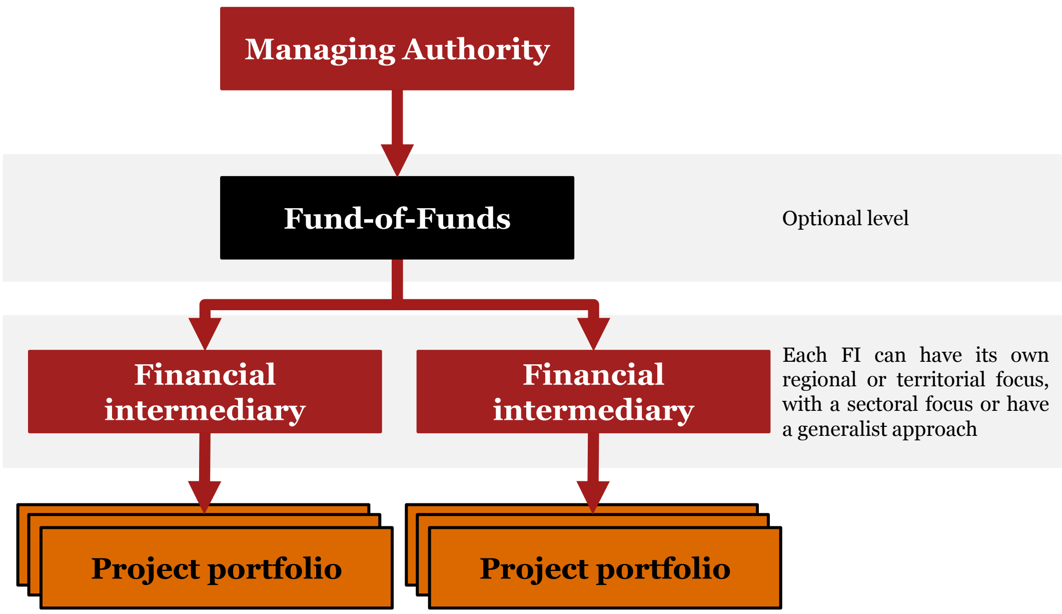
Advantages	Weaknesses
• When the financial intermediary is an already existing entity; then implementation and operation can be achieved rapidly. • Control over the implementation conditions.	• Difficult to operate and remain in line with Article 38 of the CPR. • Spread of Financial Instruments in line with the specialisation of existing entities and with it a loss of strategic vision as to the purpose of the instruments as a whole. Resulting in a lack of flexibility, and a fragmented monitoring and reporting process. • Limited synergy between the different instruments. • Risk of conflict of interest, political influence, and limited deployment possibilities. • Elevated audit risks, and of ineligible expenses.

Source: CPR, EIF, PwC, 2014.

8.3.2. Option 2: Structuring a Financial Instrument with a Fund of Funds

The second possible option is structuring several Financial Instruments under a Fund-of-Funds. Based on past experience, this is the recommended option when dealing with Financial Instruments. The added benefit being that the Fund of Funds can be a beneficiary of both EU funds, national and regional co-financing. Figure 28 below provides an illustration of such a structure.

Figure 28: Functional diagram of the structuring of a Financial Instrument with a Fund of Funds



Source: CRP, PwC, 2014.

The Fund-of-Funds would have for purpose the supply of funding to support projects, individuals and micro-enterprises within a sectorial theme or be generalist in nature. Under current regulations, there are several ways to manage such a fund, the CPR states that this management can be entrusted to the European Investment Bank, the European Investment Fund or another similar organisation, at national or regional level.

It is also possible to allow a pre-selected fund manager to handle the Fund-of-Funds, as well as to transfer the management of this Fund-of-Funds to a national entity after a period of adjustment following the launch and implementation of the instrument, if needed. Advantages and weaknesses of this second option are detailed in the table below.

Table 26: Advantages and weaknesses of a governance structure using a Fund-of-Funds

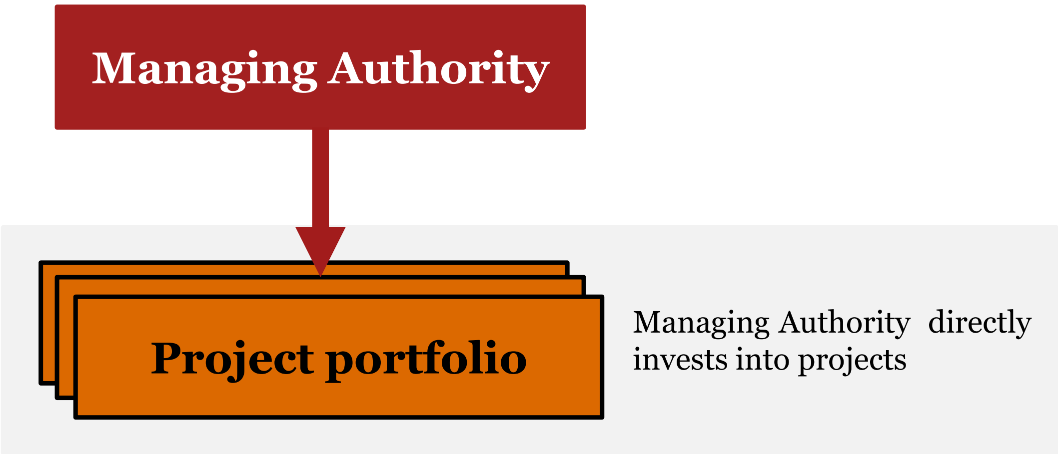
Advantages	Weaknesses
• Allows for the grouping of several Financial Instruments underneath a Fund of Funds structure. This would provide the Fund of Funds manager with a strategic overview of the instruments as a collective, allow for greater flexibility between these, as well as the consolidation of reporting • Delegation of tasks to a financial entity with experience in the management of structural funds (now ESIF funds) and potentially in microfinance • Potential synergies between different Financial Instruments • Allows for the possibility of financial contribution from the entity managing the Fund of Funds • Reduced risk of conflict of interest between experienced fund managers and financial intermediaries • Reduced risk of political influence • Increased deployment options	• No direct control as to the implementation of the instruments • Terms and conditions for the management of the fund need to be negotiated • Dependant on conditions proposed by the fund manager

Source: CRP, EIF, PwC, 2014.

8.3.3. Option 3: The Managing Authority providing Financial Instrument support directly to final recipients

The third option is that the Managing Authority manages the Financial Instruments itself instead of a financial intermediary or via a Fund of Funds (Figure 29). According to the CPR, the MA has the possibility of executing the disbursement of loans and guarantees without the employing a Fund of Funds structure in accordance with Article 38 (4)(c). This option does not require a financing agreement, instead requiring a “strategy paper” as stated in the CPR. Management fees are thus not a consideration, although some fee may be required if the MA is expected to provide technical assistance services.

Figure 29: Functional diagram of the structuring when the Managing Authority provides Financial Instruments directly to projects



Source: CRP, PwC, 2014.

Advantages and weaknesses of this third and last option are detailed in the table below.

Table 27: Advantages and weaknesses of direct funding from the MA

Advantages	Weaknesses
• No need for a financial agreement, only a strategy paper. • Rapid establishment and operation of funding activities if the MA possesses the necessary knowledge and capacity • Reduced effort for reporting and monitoring • Greater direct control on operations	• If the MA does not possess the necessary knowledge, capacity and expertise, the establishment and operation of the Financial Instrument would be problematic • Limited synergies with other Financial Instruments • No advances possible • Greater audit risks, and risks from ineligible expenses • Greater risk of conflict of interest, political influence and limited deployment options • Not eligible for management fees, with the exception of technical assistance services

Source: CRP, EIF, PwC, 2014.

This option is preferable when the Managing Authority has sufficient experience and technical knowledge in the matter of loans or in guarantees. It should be noted that this option is not possible in all Member States, as it is subject to national law.

Based on these three options, the following section indicates the proposed management structure of the proposed Financial Instruments under the HRD OP for 2014-2020.

8.4. Proposal for the structuring of a Financial Instrument dedicated to Human Resources Development

The analysis of supply and of demand for financial products to finance target groups and final recipients in the upcoming HRD OP, the exposition of the indicative financing gap, along with the identification of the market failures, allows for the identification of the potential for the establishment of dedicated Financial Instruments for the provision of micro-guarantees, personal micro-loans and business micro-loans.

The analysis of the different aspects of the market shows that there is an important demand for financial solutions. These are however unlikely to be met through financing from commercial banks and MFIs without any public intervention as the Bulgarian macroeconomic environment is not conducive to investments in highly risky projects at present, the private sector often perceives the final recipients as being non-bankable, interest rates are high, the amount of micro-credit products offered is limited or even scarce, the microfinance sector is currently not developed and structured enough to cover the potential demand; and the social economy sector is not sufficiently defined to permit financing different from grants.

Three Financial Instruments have been identified as necessary for improving the access to finance of the people at risk of poverty or socially excluded in the country. These FIs are: micro-guarantees, personal micro-loans and business micro-loans.

Taking into consideration the elements analysed throughout the present study, two structures are proposed for the management and governance of the proposed Financial Instruments. Their main characteristics are:

- For the **Proposed Structure 1**, the leverage of the future ESIF Fund-of-Funds[89] to be developed for the ESIF funds under the Innovation and Competitiveness Operational Programme (IC OP). This is close to the Option 2 detailed previously and leverages the experience acquired by the JEREMIE Holding Fund over the 2007-2013 programming period; and
- For the **Proposed Structure 2**, the leverage of the National Guarantee Fund for the micro-guarantee instrument on the one hand and the set-up of personal micro-loan and business micro-loan instruments via commercial banks and Microfinance Instruments on the other hand. In this structure, no Fund-of-Funds would be set up. This is close to the Option 1 detailed previously and leverages the experience acquired by the National Guarantee Fund as well as the experience of commercial banks and MFIs with previous Financial Instruments, which may have not been related to micro-loans.

The two proposed structures are detailed in the following sub-sections.

In both structures, the Managing Authority would oversee the disbursements of the envelopes of each Financial Instrument that need to be defined and need to be in line with the Priority Axes 1 and 2 of the HRD OP. As already mentioned, the Managing Authority may also complement these Financial Instruments with grants and technical assistance services.

8.4.1. Proposed Structure 1 – Leverage of the future ESIF Fund of Funds

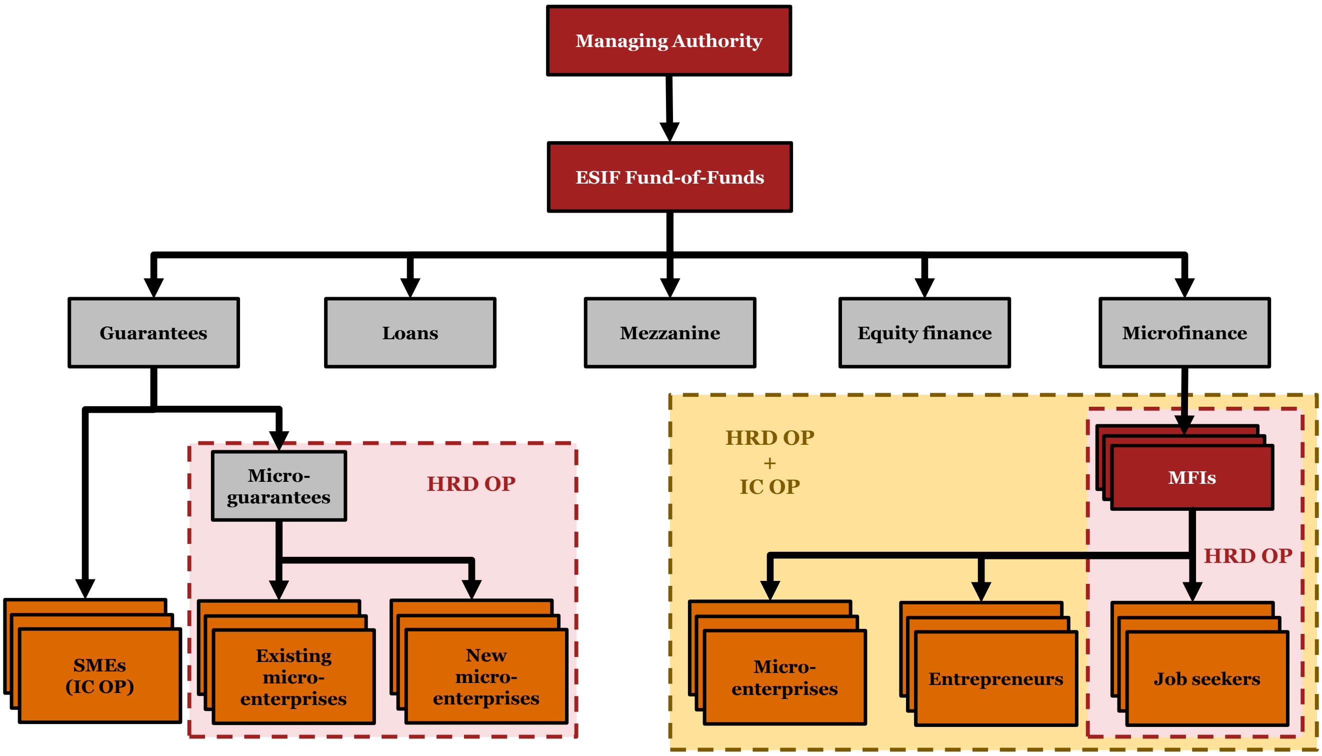
The first proposed structure consists in using the future ESIF Fund-of-Funds to be set up under the IC OP for the 2014-2020 programming period. In this situation, the Managing Authority would invest its funding into the Fund-of-Funds and would pinpoint and orient this funding towards the target groups identified in the HRD OP. Following that:

- The guarantee fund could include a micro-guarantee fund that would provide such instruments to the existing and newly created micro-enterprises to be targeted under the HRD OP.
- The microfinance fund could:
  - Include a specific sub-fund to provide personal micro-loans to job-seekers; while
  - Business micro-loans could be provided to micro-enterprises and entrepreneurs, and focus on the specific target groups and final recipient identified in the HRD OP (i.e. micro-enterprises with temporary difficulties, training centres, social enterprises, socially excluded entrepreneurs and social entrepreneurs) while ESIF funding under the IC OP would focus on innovative micro-enterprises and entrepreneurs who are not at risk of poverty.

[89] The name of the Fund of Funds has not been defined yet. That is why a generic name has been preferred to define it.

Figure 30 below illustrates this Proposed Structure 1.

Figure 30: Proposed Structure 1 for the Financial Instruments under the HRD OP for 2014-2020



Source: PwC, 2014.

This proposed Structure 1 is the option that presents the greatest potential for added value, maximising the potential for leverage generation as well as being most-suited to the circumstances of the Bulgarian market. Nevertheless, in order to propose to the Managing Authority another viable option for the structuring of the Financial Instruments under the HRD OP for 2014-2020, a second structure is proposed in the next sub-section.

8.4.2. Proposed Structure 2 – Financial Instruments without a Fund-of-Fund

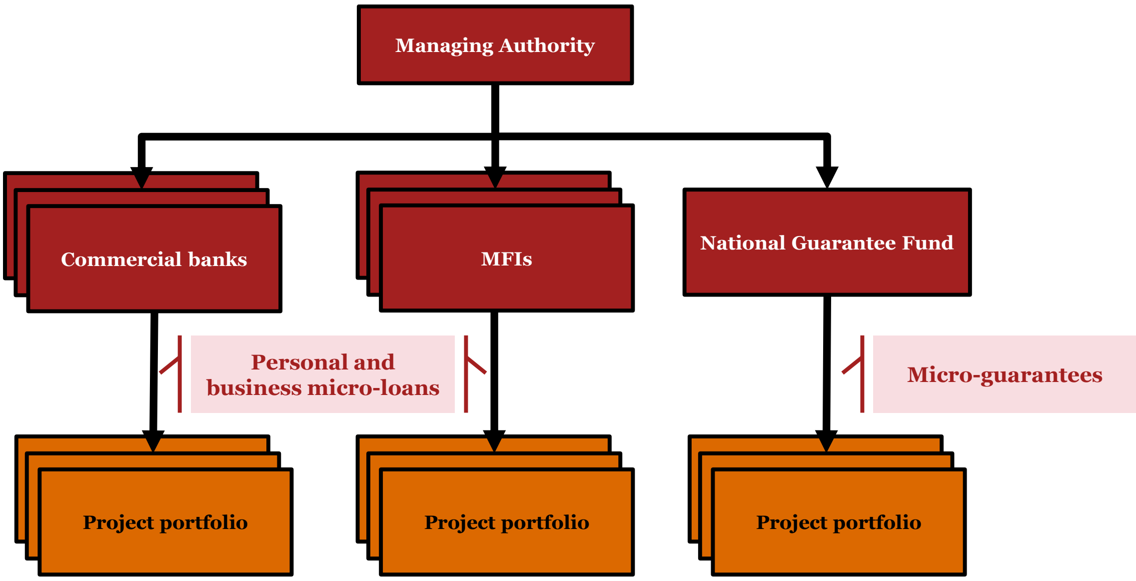
The second proposed structure consists in developing the Financial Instruments without a Fund-of-Funds but via financial intermediaries, as previously detailed in Option 1. In this situation, the Managing Authority would invest its funding into different financial intermediaries, depending on the instrument to design and implement. For instance:

- The National Guarantee Fund could include a micro-guarantee fund that would be funded by funding from the HRD OP to provide micro-guarantees to existing and new micro-enterprises; while
- Personal and business micro-loans would be provided to existing micro-enterprises, new micro-enterprises and entrepreneurs via commercial banks and/or Microfinance Institutions.

All financial intermediaries would have to focus on the specific target groups and final recipient identified in the HRD OP, namely micro-enterprises with temporary difficulties, training centres, social enterprises, socially excluded entrepreneurs and social entrepreneurs. With regards to the products, the personal micro-loans would be exclusively devoted to the unemployed people (also socially excluded or at risk of poverty) willing to finance training or needing financing to cover mobility costs and have better access to the labour market.

Figure 31 below illustrates this Proposed Structure 2.

Figure 31: Proposed Structure 2 for the Financial Instruments under the HRD OP for 2014-2020



Source: PwC, 2014.

For both Proposed Structures, it should be stressed that the characteristics of funds and sub-funds need to be thoroughly analysed and validated prior to the creation and inception of the funds.

8.5. Assessment of the proportionality of financial allocations for investments through FIs

In the present chapter, indicative amounts were provided as estimates of the potential allocation of funds to 3 potential FIs that were identified by the analysis. These amounts are the following:

- Micro-guarantee instrument: EUR 10m
- Personal Microfinance instrument: EUR 5m
- Business Microfinance instrument: EUR 5m

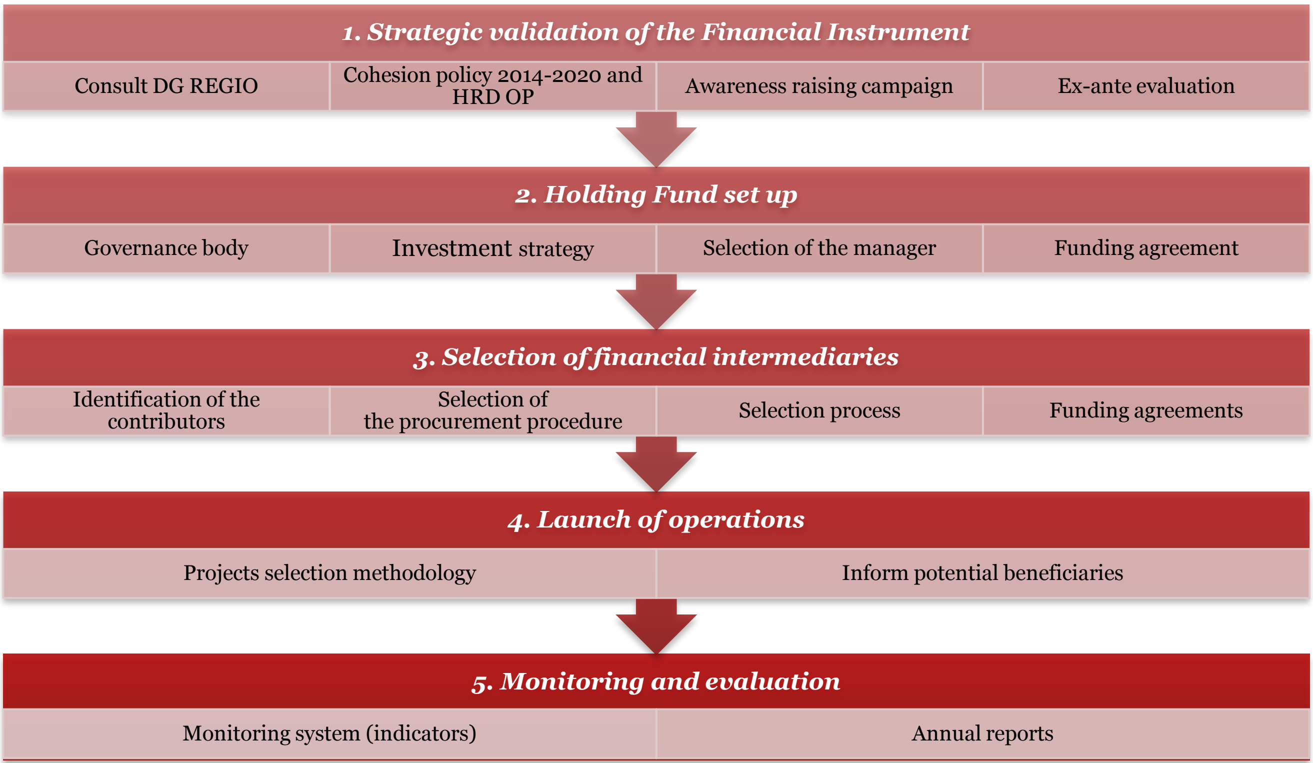
These suggestions are based on estimates deriving from the analysis presented in the present report. However the following points have to be taken into account:

- The demand that was quantified in the relevant section illustrated a very large need for financing. This estimate was however provided as an indication of the needs for financing from the suppliers of financing and not necessarily from an FI.
- The main market failure that is relevant to the potential beneficiaries remains the lack of specialized institutions that could successfully implement relevant FIs is an important barrier. The amounts provided are taking this limitation into account and therefore the amounts remain conservative.
- The amounts provided are considered realistic according to the market reality and would be able to generate the added value presented in Chapter 7, stimulate the development of an intermediary market and specifically MFIs with a more social orientation.

9. Action plan for the implementation, monitoring and evaluation of the Financial Instruments

This section of the study will present the plan of necessary actions in order to set up the FIs as proposed in Section 8, if the MA decides to create a Fund of Funds to manage the investment of ES Funds via FIs. In the event that the MA opts to invest into the JEREMIE Holding Fund, the necessary stages will also be presented. They are presented in chronological order, from their strategic valuation all the way to the monitoring and evaluation process once they are implemented (Figure 32).

Figure 32: Action plan for the implementation of FIs



9.1. Validation of the Financial Instrument

The implementation of a dedicated Financial Instruments for Human Resources Development must be linked to the strategies set out in national policy and must be consistent with the regulatory framework for Cohesion Policy 2014-2020 to receive a portion of the funds allocated through operational programs.

Consistency with the strategy of the 2014-2020 Cohesion Policy and the HRD OP of Bulgaria

For the Financial Instruments to receive funds under the Common Strategic Framework (CSC), including the ESF in the field of social inclusion & poverty reduction and for the projects it finances to be eligible for these funds, it must be consistent with:

- The Europe 2020 strategy for smart, sustainable and inclusive growth;
- The Common Strategic Framework and the 11 thematic objectives that it provides. The investment strategy of the FI will contribute to the fulfilment of the "thematic concentration[90]" which obliges each Member State to allocate at least 80% of ESF resources to one or more of the following four thematic objectives:
  - TO 8: Promoting employment and supporting labour mobility;
  - TO 9: Promoting social inclusion and combating poverty;
  - TO 10: Investing in education, skills and lifelong learning;
  - TO 11: Enhancing institutional capacity and an efficient public administration.
- The priorities of the ESF Operational Programme 2014-2020 for Bulgaria (Section 3), which is under review by the European Commission and is expected to be finally approved until the end of the year (2014).

The investment of the dedicated FIs should be consistent with the elements presented above. This strategy will be defined in several ways:

- In the Operational Programme Human Resources Development;
- In the investment strategies of the Fund of Funds.

Launching an awareness campaign for the different actors

There is no experience in Bulgaria in the use of Financial Instruments in the field of social inclusion. The use of such a tool requires the ability to analyse the projects, and an understanding of the concept of return on investment and business plan.

As such, it is vital to launch an awareness campaign early in the process. Local and regional actors who are potentially involved in the implementation of the FI need to be familiar with the integrated approach of the project's structures, the principle of return on investment, and the recycling of funds in order to deliver on their "revolving" nature.

Technical assistance could play an important role in raising awareness, which can be complemented with hands-on support to potential beneficiaries.

Conducting an ex-ante evaluation

The Bulgarian Ministry of Finance has initiated an ex-ante assessment of the Financial Instruments as is stated by the CPR in order to identify any market failures, situations of suboptimal investment, determine the respective investment needs, the possible involvement of the private sector and the added value of any implemented FIs. This process helps avoid duplication and inconsistencies between financing tools implemented by different actors at different levels and avoid any possible distortion of the market. Table 28 presents the main component of this study which is element of response to the ex-ante assessment.

During the implementation phase, it will be necessary to deepen the MA's understanding of the legal aspects related to the launch of the operations (Section 3.5 and 7.3).

[90] Article 9 of the ERDF Regulation project

Table 28: Key elements of the ex-ante assessment

Component of the ex ante assessment (Article 32)	Elements of response in this study to document these criteria
a. *An analysis of market failures, suboptimal investment situations, and investment needs for policy areas and thematic objectives or investment priorities to be addressed with a view to contribute to the strategy and results of the relevant programmes and to be supported through financial instruments.*	6.1 Analysis of the current financing situation of human resources development in Bulgaria 6.2. Solicitation for financing urban development in Bulgaria 6.3. Identification of market failures
b. *An assessment of the value added of the financial instruments considered to be supported by the CSF Funds, consistency with other forms of public intervention addressing the same market, possible state aid implications, the proportionality of the envisaged intervention and measures to minimise market distortion.*	7. Evaluation of value added, 8. Recommendations on investment strategies for a dedicated financial instrument for urban development in Bulgaria
c. *An estimate of additional public and private resources to be potentially raised by the financial instrument down to the level of the final recipient (expected leverage effect), including as appropriate an assessment of the need for, and level of, preferential remuneration to attract counterpart resources from private investors and/or a description of the mechanisms which will be used to establish the need for, and extent of, such preferential remuneration, such as a competitive or appropriately independent assessment process.*	8. Recommendations on investment strategies for a dedicated financial instrument for urban development in Bulgaria 8.3. Proposal for structuring dedicated financial instruments in Bulgaria
d. *An assessment of lessons learnt from similar instruments and ex ante assessments carried out by the (region) in the past, and how these lessons will be applied going forward.*	6. Analysis of current financing situation of urban development in Bulgaria 6.2. Analysis of the supply of financial actors for urban development in Bulgaria
e. *The proposed investment strategy, including an examination of options for implementation arrangements within the meaning of Article 33, financial products to be offered, final recipients targeted, envisaged combination with grant support as appropriate.*	8.1 Recommendations on investment strategies for a dedicated financial instrument for urban development in Bulgaria 8.2 Options for structuring a financial instrument 8.3. Proposal for structuring dedicated financial instruments in Bulgaria
f. *A specification of the expected results and how the financial instrument concerned is expected to contribute to the achievement of the specific objectives and results of the relevant priority or measure including indicators for this contribution.*	8. Recommendations on investment strategies for a dedicated financial instrument for urban development in Bulgaria 8.3. Proposal for structuring dedicated financial instruments in Bulgaria
g. *Provisions allowing for the ex-ante assessment to be reviewed and updated as required during the implementation of any financial instrument which has been implemented based upon such assessment, where during the implementation phase, the managing authority considers that the ex-ante assessment may no longer accurately represent the market conditions existing at the time of implementation.*	9.6 Use of the results for corrective actions 9.7 Guidelines to establish and quantify the expected results

9.2. Creation of the Fund of Funds

As explained in Section 8.4, it is possible that the establishment of dedicated Financial Instruments for Human Resources Development in Bulgaria could include a Fund of Funds. This will enable a rapid implementation of the FIs and may, if necessary, be removed after an initial phase of implementation if the MA and regional organisations are able to demonstrate the ability to take over these the duties.

Constitution of the governing body of the Financial Instruments

The governance of the FIs is provided by an investment committee which is the supervisory body of the management of the Fund of Funds. The investment committee would incorporate representatives of the MA and impacted public stakeholders and ministries, as well as other co-investors.

The governing body of the FIs must have a structure that brings the political, administrative, and financial competence in the country. It must at least encompass representatives of the State, the main partners of the priority areas, the National Guarantee Fund and other financial institutions.

Development of the investment strategy

The investment strategy of the Fund of Funds is to set the policy and the investment targets that are in line with the objectives of the Operational Programme Human Resources Development. The goal of the strategy is to define the choice of investment for the programming and the implementation of the dedicated Financial Instruments.

At a minimum, the investment strategy should include[91]:

- Target groups;
- Investment products offered;
- Estimates of the amounts to be invested in the fund;
- Limitations of investments and investment controls;
- General Criteria for the selection and evaluation of funds (e.g., types of appropriate structure for managing a fund);
- Provisions relating to the recycling of funds.

The Fund of Funds' investment strategy is usually part of the investment agreement concluded between the Managing Authority and the manager of the investment fund.

Selection of the Fund of Funds manager

According to Article 33, paragraph 4 b) of the Common Provisions Regulation, the Managing Authority is allowed to entrust the implementation tasks to the:

- European Investment Bank;
- International financial institutions of which Bulgaria is a shareholder, or financial institutions established in Bulgaria that pursue public policy objectives under the control of a public authority, selected in accordance with EU rules and national rules;
- A body governed by public or private law selected in accordance with EU rules and national rules.

At present, there is no Fund of Funds. The EIF could be a temporary partner involved in the launch of the FIs and will aim at transferring the administration of the fund to national authority in a specific body after an initial phase of implementation.

[91] JESSICA – Holding Fund Handbook. EIB-DG Regio, novembre 2010.

Establishing a financing agreement with the managing authority

Once the fund manager is selected, it is then necessary to establish a financing agreement between the MA and the Fund of Funds. If the MA is an entity other than the Ministry of Labour and Social Policy, this financing agreement can be tripartite in the event that the Regional Council would also contribute to the Fund of Funds.

The CPR (Article 33, paragraph 6) states that entities (like Fund of Funds manager) that have been delegated implementation tasks will have to open fiduciary accounts in their name and on behalf of the managing authority. Assets held in the trust accounts must be managed in accordance with the principle of sound financial management, in compliance with the appropriate prudential rules, and must be have sufficient liquidity.

9.3. Selection of Financial Intermediaries

As previously presented in Section 8.4, there are two options to consider:

- Fund of Funds, based on the JEREMIE Holding Fund experience
- Financial Intermediaries

Identification of the contributors

In order to implement the funds, public and private actors should be identified to contribute to their co-financing and co-investment, as well as the nature of these contributions (financial or in kind).

Choice of methods for selecting the financial intermediaries

A transparent and non-discriminatory selection process for the financial intermediaries must be organised. According to Article 33, paragraph 5 of the Regulation on common provisions, the Fund of Funds' manager may entrust part of the implementation to financial intermediaries[92]. The financial intermediaries should be selected through open, transparent, proportionate and non-discriminatory procedures while ensuring that there are no conflicts of interest. As such, the selection of a financial intermediary should be done through a public procurement procedure. The choice of this procedure depends on the target of the financial intermediary and the level of competition among potential candidates. The most commonly used procedures are the open or restricted procedures. The proposed regulations do not provide further details on the selection of the funds.

Selection process

The Fund of Funds launches calls for expressions of interest by publishing the corresponding terms of reference, receives proposals from various candidates and selects the manager. In the case where a prior sensitisation campaign made compatible projects with a dedicated FI for human resources development, the selection of the financial intermediary can be done on the basis of targeted groups.

Although the selection would be done directly by the Fund of Funds' manager, the governing body of the FI (Investment Committee) would also be involved.

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[92] Provided they take responsibility to ensure that these financial intermediaries meet the criteria set out in Article 57 and Article 131, paragraph 1, point 1 a) and paragraph 3 of the Financial Regulation.

Establishing the financing agreements between each financial intermediary and the Fund of Funds

Subject to confirmation by the implementing Regulations of the Regulation with common provisions, a financing agreement will be established between the investment fund and each of the financial intermediaries. It will define the modalities of contribution of the Fund of Funds in each of the selected financial intermediary, the investment plans, and modes of operations of the latter.

Once the financing agreement is established, the managing authority can contribute with ESF to the Fund of Funds, which in turn will invest in the financial intermediaries according to their respective investment plan. The financial intermediaries will then raise additional funds from other public and private contributors. Subject to confirmation by the final regulations for the period 2014-2020, the national public counterpart completing the ESF may be made at different levels (Fund of Funds, financial intermediary or at the targeted groups' level).

9.4. Operations

Procedures for selecting projects

Once created, the financial intermediaries will define the eligibility criteria and the procedures for the selection of the projects, while respecting the eligibility rules and the priorities of the Operational Programme Human Resources Development.

Informing potential beneficiaries

Communication activities targeting potential beneficiaries of the financial intermediaries should be organised to inform them correctly of the functioning of the FI and the eligibility criteria of the different funds. It will be especially necessary to assist them in preparing their project so they can benefit from the mechanism.

Technical assistance for the recipients could well be required in the preparation of the project. Organisations could possibly provide this technical support, while ensuring that they avoid potential conflicts of interest with respect to their role in the FI. Given the lack of experience with FIs in Bulgaria, this role could be provided by an external consultancy or the EIF's advisory services.

9.5. Monitoring and evaluation

9.5.1. Monitoring

The Fund of Funds in collaboration with the financial intermediaries will create a system of monitoring and evaluation of the Financial Instruments dedicated to the priority areas. This system should include:

- Procedures to ensure transparency in the operation of the instruments;
- Indicators of socio-economic benefit arising from projects invested into;
- Indicators of physical monitoring;
- Indicators of financial monitoring. In terms of financial monitoring, the CPR (Article 34, paragraph 1) states that the dedicated funds and Fund of Funds manager should produce regular transactions monitoring reports and transmit them to the management and expenditure control organisation at the beginning of the accredited programme period.

Regular monitoring

With a view to regular monitoring of the Programme and to making any adjustments needed to its policy and funding priorities, the Commission shall draw up an initial qualitative and quantitative monitoring report covering the first year, followed by three reports covering consecutive two-year periods.

The total of the regular reports shall cover:

- The Programme's results and particularly,
- The extent to which the principles of equality between women and men and gender mainstreaming have been applied, as well as
- How anti-discrimination considerations, including accessibility issues, have been addressed through its activities.

The engagement and assistance of local MAs shall be required, whereby the latter may use these reports to evaluate and analyse the achievements and short-comings of the Programme, and initiate change to employment of FIs or introduce other structural and operational alterations in order to facilitate the smooth running and result-oriented nature of the Programme. The chosen operational structure and selected FIs in use will be in focus in earlier reports as well as tangible effects and outcomes of the programme.

Annual Reports

Due to the specific procedures and delivery structures of the FIs, the provision of information control on the use of budgetary resources from the ESI funds are crucial for all stakeholders, as they provide indications about the actual performance of supported instruments and, if necessary, the adjustments required to ensure their effectiveness. As such, the CPR (Article 40) states that the MAs must forward to the Commission a "special report on the activities related to Financial Instruments" in the form of an annex to the annual implementation report of the Operational Programme.

This report will contain the following information:

- The name of the programme and the priority under which support from the ESI Funds are granted;
- A description of the financial arrangements and the implementation methods;
- Identification of the organisations to which the implementation tasks have been entrusted;
- The total disbursement, by programme, priority or measure, of the FI mentioned in the claims submitted to the Commission;
- The total amount of assistance disbursed or committed for guarantee contracts by the FI to the final recipients, by program and priority or measure, included in the requests for payment submitted to the Commission;
- The income of the FI and repayments thereof;
- The multiplier effect of investments made by the FI and the value of investments and participations;
- The contribution of the FI to the achievement of programme indicators and of the concerned priority.

9.5.2. Evaluation

The regulation for the 2014-2020 European Structural and Investment Funds (ESIF)[93] represents a radical change for operational programmes. The Common Provisions Regulation (CPR) emphasises programme objectives, the logic of intervention to achieve the expected results and the evaluation of effectiveness and impacts. Furthermore it requires from Managing Authorities and the Commission annual reporting on outputs and results, including findings of evaluations where available. In previous programming periods, evaluations

[93] Regulation (EU) No 1303/2013 of the European Parliament and the Council of 17 December 2013 laying down common provisions on the ESI Funds, referred to throughout this document as the CPR (Common Provisions Regulation).

have tended to focus more on implementation issues than capturing the impacts. For 2014-2020, the CPR requires Managing Authorities to carry out evaluations which assess the effects of the ESIF programmes.
Evaluations should serve to improve the effectiveness and efficiency of programmes as well as to assess their effects. They are meant to increase knowledge of what works and what does not in order for decision makers to make timely decisions to support the implementation of programmes and to draw conclusions for policy making.

Mid-term evaluation

A mid-term evaluation of the Programme shall be carried out by 1 July 2017 to measure, on a qualitative and quantitative basis:

- Progress made in meeting the Programme's objectives;
- The social environment within the Union and any major changes introduced by Union legislation;
- Whether the resources of the Programme have been used efficiently and to assess its Union added value.

The results of that mid-term evaluation shall be presented to the relevant EU-level institutions, and will incorporate all countries within the Union, where the Programme is active. This will require the input and facilitation of local MA, and will represent the first deeper review of the progress of the Programme. On the basis of the composed report, necessary changes here may be identified and implemented on EU-level as well as on local level by the MA.

End-period evaluation (2020)

Before submitting any proposal for a prolongation of the Programme beyond 2020, the Commission shall present to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions an evaluation of the conceptual strengths and weaknesses of the Programme in the period 2014 to 2020.
By 31 December 2022, the Commission shall evaluate ex-post the impact and Union added value of the Programme and shall forward a report containing that evaluation to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions.

The assistance of MA's shall be sought in the preparation of the report, whereby the focal point will be the end results and achievements of the Programme during the programming period. The overall success of the Programme as well as the business case for extending its use beyond 2012 including the employment of FIs currently in place will be assessed at this stage.

9.6. Use of the results for corrective actions

Following the monitoring and evaluation system, the expected results will be evaluated and corrective actions could be implemented based on the defined indicators measurement.

If any type of evaluation reveals that the Programme has major shortcomings, the Commission shall, if appropriate, submit a proposal to the European Parliament and to the Council, including appropriate amendments to the Programme to take account of the results of the evaluation.

According to article 37 (2), (g) of the Regulation 1303/2013, the MA may consider that the ex-ante assessment is no longer representing accurately the market conditions existing at the time of implementation and may decide to amend its programmes and redesign its investment strategy.

In order to prevent the need of such actions, it is necessary that MAs utilize evaluations for reassessment and implementing change across current FIs schemes. In this process, indicators may be modified; financial intermediaries may be reassessed and reselected as well as the implementation of the Programme itself within the framework and guidelines pre-set by the EC.

The MA should keep flexibility in terms of allocation of funds in the HRD Programme so as to be able to transfer funding initially devoted to grants to FIs within a specific Priority axis.

9.7. Guidelines to establish and quantify the expected results

In order to successfully assess the achievement of Programme objective, it is imperative to conduct evaluations across all instruments of the Programme, especially inclusive of operational solutions and practices. Even though the unbiased assessment of the impact and effects of the Programme activities as a whole in relation to the established IPs and TOs should be the primary goal, in order to obtain an accurate snapshot of the Programme's benefits and short-comings, MAs should first concentrate on the evaluation of the operational framework of FIs in use, whereby monitoring their separate impact through relevant and specific indicators and then, aggregating their cumulative effects to reach a complete assessment of the entire Programme.

Thus, setting-up result targets and a practical monitoring process of the envisaged FIs is essential for MAs to monitor FIs performance and contribution to the corresponding investment priority (ies) under the ESI Funds and to the overall objective(s) of the related Programme(s). MAs must aim at assessing the relevant result, outcome and performance indicators so that a clear and all-encompassing picture of FI suitability and effects may be drawn.

The main methodological steps for the execution of such assessment for any given FI are presented in Figure 33 below; more detailed information is included in Annex 9:

Figure 33: Main methodological steps for the execution of an assessment for any given FI.

Source: PwC Ex-ante assessment methodology for financial instruments for 2014-2020.

9.8. Insights for the monitoring and reporting system of the Financial Instruments

As presented in Figure 33, as a part of Step 1 (Expected Results) of conducting a FI progress evaluation, the MA will need to define series of specific indicators for each FI in use. These should be targeted to measure performance of the particular FIs; they should be clearly measurable and should account for the adherence to the pre-defined TOs and IPs of the Programme.

Depending on the needs of the MA and the applicable requirements, 3 types of indicators should be defined:

- **Output indicators**

  MAs should use the set of common indicators already predetermined in the fund-specific Regulations or complementary documents provided by the Commission. Indicators could cover the different forms of support to beneficiaries (including technical support) through FIs.
- **Performance indicators**

  could be defined with regard to measuring the operational efficiency of FI implementation (e.g. management costs, expected credit loss);
- **Result indicators**

  Following the new results-oriented approach, there should be special attention paid to the definition of clear and measurable result indicators. The result indicators must be clearly interpretable, statistically validated, truly responsive and directly linked to the specific objectives of the investment priority or focus area the FI is contributing to.

Below are presented tables of indicators for the chosen FIs for HRD OP 2014-2020, as described in Section 8 of this report. These should be as a specific guidance to the MA regarding the measurement of the effectiveness and progress of each specific FI. That being said, these may need to be revised after the operationalization of the FI itself, and depending on target group modifications or the use and type of chosen intermediaries.

As seen in previous sections, the planned use of FIs under HRD OP 2014-2020 concerns PA1: Improving the access to employment and the quality of jobs and PA 2: Reducing poverty and promoting social inclusion.

9.8.1. General overview of monitoring system and evaluation of expected results

At this stage in the planning process, it is not possible to go too far into detail regarding the results based indicators that must be used to monitor FI performance and inform investment strategy updates as well as in the funding agreements, but a brief presentation of three basic elements is necessary that FIs indicators need to include:

- Indicators defined by the HRD OP to monitor the progress of the FIs
- Standard financial indicators to assess the performance of the funds
- Additional indicators to monitor and assess whether the objectives specific to the target groups are achieved

Because no formal decisions have been made regarding the specific priority axis that will be included in the FI strategy to the elements below are proposals to be considered as a basis for discussion. These indicative points can be adjusted and operationalised during the formulation of the funding agreement that will define the targets and performance criteria for the ESIF FoF and the sub-funds.

Examples of indicators relative to the target groups are presented in Annex A.10. These indicators are relevant to monitor the achievements of the FIs in terms of groups targeted by the HRD OP.

As far as the reporting is concerned, it could be done:

- On a monthly basis for key data such as total amounts disbursed, number of loans approved/signed/disbursed, total number of SMEs supported.
- On a quarterly basis for more fine-tuned information such as split between social enterprises, training centres, newly created company vs existing companies, percentage of increase in the number of new established micro-enterprises, the volume of the loans per final recipients.

If some of the defined indicators are not at the expected level of achievement in relation to the periodicity stated, the MA might consider to either revising the funding agreement, launch another call for proposal to select other financial intermediaries and/or modify the products' offer.

In the following section are presented tables of indicators for the chosen FIs for HRD OP 2014-2020, as described in Section 8 of this report. These should be as a specific guidance to the MA regarding the measurement of the effectiveness and progress of each specific FI. That being said, these may need to be revised during the implementation of each FI, depending on elements of each FI needing to be assessed.

9.8.2. Indicators for the use of Micro-guarantee Instrument

For Priority Axis 1, IP 2 *Sustainable integration into the labour market of young people* and IP 3 *Self-employment, entrepreneurship and business creation up to 29 years of age who are involved in self-employment*, Within Priority Axis 2 IP 4 *Promoting social entrepreneurship and vocational integration in social enterprises and the social and solidarity economy in order to facilitate access to employment:* the Micro-guarantee instrument would be among the preferred option in terms of FI use. The objective of this IPs is reducing the specific difficulties of the target groups and final recipients when accessing the labour market and improving the quality of jobs. Often representatives of the target groups are restricted when seeking financing due to lack of collateral or due to high level of risk of the projects, hence the micro-guarantee instrument is expected to facilitate and promote entrepreneurship, job creation, reduction of unemployment and poverty and improve job and life quality.

Type of FI	*Micro-guarantee Instrument*
Source of financing	*ESF and YEI*
Funds budget	*EUR 10m + co-financing/ leverage*
Specific objective of corresponding IPs/Focus area	Within **Priority Axis 1:** **IP 2**: Sustainable integration into the labour market of young people in particular those not in employment, education or training, including young people at risk of social exclusion and young people from marginalised communities, including through the implementation of the Youth Guarantee. The target groups of this IP are economically inactive young people in the age group of 15 to 29 years old; youth and unemployed people up to 29 years of age, who are not enrolled in the educational system and youth registered as job-seekers up to 29 years of age. **IP 3:** Self-employment, entrepreneurship and business creation, including innovative micro, small and medium-sized enterprises. The target groups for this IP are people willing to start independent business activity; self-employed people; and workers in micro-enterprises, who have benefited from the Operational Programme Human Resources Development. Within **Priority Axis 2** **IP 4:** Promoting social entrepreneurship and vocational integration in social

	enterprises and the social and solidarity economy in order to facilitate access to employment. The target groups for this IP are people with disabilities; disadvantaged people in the labour market and other socially excluded people; representatives of different communities employed in social enterprises, cooperatives and specialised enterprises for people with disabilities; people employed in social entrepreneurship institutions and organisations.				
Result indicator	**Indicator**	**Unit**	**Baseline Year (2013)**	**Target (2023)**	**Source**
	Reduction of unemployed people willing to create a business and unable to access financing	%			MA/ Employment Agency
	Investment in micro-enterprises	mEUR			Financial Intermediary / FoF
Output indicators	**Indicator**	**Unit**	**Baseline Year (2013)**	**Target (2023)**	**Source**
	Number of jobs created	Number			Employment agency
	Number of new enterprises supported	Number			MA
	Number of enterprises receiving loans	Number			Financial Intermediary / FoF
Performance indicators	**Indicator**	**Unit**	**Baseline Year (2013)**	**Target (2023)**	**Source**
	Absorption rate	%			MA
	Volume of loans under guarantee	mEUR			Financial Intermediary / FoF
	Current default rate of the guaranteed loans	%			Financial Intermediary / FoF
	Management cost (% on volume of total loans guaranteed)	%			Financial Intermediary / FoF
	Leverage brought by the instrument	%			Financial Intermediary / FoF + MA

9.8.3. Indicators for the use of Business Microfinance Instrument

Business Microfinance Instrument covers the same IPs as by the Micro-guarantee Instrument.

This instrument will support individuals needing financing for a training in view of creating a company, individuals needing financing to create a company, micro-enterprises which need financing to finance training for their employees, micro-enterprises that need financing to keep their business alive, micro-enterprises that want to expand their business activities, training centres, social enterprises (including existing social enterprises and social entrepreneurs).

Type of FI	*Business Microfinance Instrument*
Source of financing	*ESF and YEI*

Funds budget	*EUR 5m + co-financing/ leverage*				
Specific objective of corresponding IP/Focus area	Within **Priority Axis 1:** **IP 2**: Sustainable integration into the labour market of young people in particular those not in employment, education or training, including young people at risk of social exclusion and young people from marginalised communities, including through the implementation of the Youth Guarantee. The target groups of this IP are economically inactive young people in the age group of 15 to 29 years old; youth and unemployed people up to 29 years of age, who are not enrolled in the educational system and youth registered as job-seekers up to 29 years of age. **IP 3:** Self-employment, entrepreneurship and business creation, including innovative micro, small and medium-sized enterprises. The target groups for this IP are people willing to start independent business activity; self-employed people; and workers in micro-enterprises, who have benefited from the Operational Programme Human Resources Development. Within **Priority Axis 2** **IP 4:** Promoting social entrepreneurship and vocational integration in social enterprises and the social and solidarity economy in order to facilitate access to employment. The target groups for this IP are people with disabilities; disadvantaged people in the labour market and other socially excluded people; representatives of different communities employed in social enterprises, cooperatives and specialised enterprises for people with disabilities; people employed in social entrepreneurship institutions and organisations.				
Result indicator	**Indicator**	**Unit**	**Baseline (2013)**	**Target (2023)**	**Source**
	Reduction of unemployed people willing to create a business and unable to access financing	%			MA/ Employment Agency
	Investment in micro-enterprises	mEUR			Financial Intermediary/ FoF
	Volume of loans for working capital for micro-enterprises	mEUR			Financial Intermediary/ FoF
Output indicators	**Indicator**	**Unit**	**Baseline (2013)**	**Target (2023)**	**Source**
	Number of enterprises receiving micro-financing	Number			MA
	Number of micro-enterprises created	Number			MA
	Number of micro-enterprises supported	Number			MA
	Number of individuals undergone training, who created a micro-enterprise	Number			MA/ Employment Agency/ NAVET
Performance indicators	**Indicator**	**Unit**	**Baseline (2013)**	**Target (2023)**	**Source**
	Credit loss (volume of defaulted loans/volume of total loans outstanding)	%			Intermediary/ FoF
	Management costs (% on volume of total loans outstanding)	%			Intermediary/ FoF
	Leverage (Private investment	%			Intermediary/

	matching public support to micro-enterprises/ total public support)				FoF

9.8.4. Indicators for the use of Personal Microfinance Instrument

The Personal Microfinance Instrument will help reduce the specific difficulties of the target groups and final recipients when accessing finance because the financial institutions consider their project as too risky and/or not bankable. At the same time it will establish a risk-sharing financing scheme with financial intermediaries in view of providing loans of very small amount to non-bankable individuals needing financing to have an improved access to the market labour (this is mostly to finance training or to improve the mobility of unemployed and disadvantaged people by financing bus tickets and/or car expenses).

Type of FI	*Personal Microfinance Instrument*				
Source of financing	*ESF and YEI*				
Funds budget	*EUR 5m + co-financing/ leverage*				
Specific objective of corresponding IP/Focus area	Within **Priority Axis 1:** **IP 2**: Sustainable integration into the labour market of young people in particular those not in employment, education or training, including young people at risk of social exclusion and young people from marginalised communities, including through the implementation of the Youth Guarantee. The target groups of this IP are economically inactive young people in the age group of 15 to 29 years old; youth and unemployed people up to 29 years of age, who are not enrolled in the educational system and youth registered as job-seekers up to 29 years of age. Within **Priority Axis 2** **IP 4**: Promoting social entrepreneurship and vocational integration in social enterprises and the social and solidarity economy in order to facilitate access to employment. The target groups for this IP are people with disabilities; disadvantaged people in the labour market and other socially excluded people; representatives of different communities employed in social enterprises, cooperatives and specialised enterprises for people with disabilities; people employed in social entrepreneurship institutions and organisations.				
Result indicator	**Indicator**	**Unit**	**Baseline (2013)**	**Target (2023)**	**Source**
	Reduction of the unemployed people that could not find a job due to lack of qualification	%			Employment agency
	Reduction of the unemployed people that could not find a job due to lack of mobility	%			Employment agency
Output indicators	**Indicator**	**Unit**	**Baseline (2013)**	**Target (2023)**	**Source**
	Number unemployed people finding a job after have completed a training	Numb er			Employment agency
	Number of unemployed people finding a job after receiving funding for mobility	Numb er			Employment agency
Performance indicators	**Indicator**	**Unit**	**Baseline (2013)**	**Target (2023)**	**Source**
	Credit loss (volume of	%			Intermediary/

	defaulted loans/volume of total loans outstanding)				FoF
	Management costs (% on volume of total loans outstanding)	%			Intermediary/ FoF
	Leverage (Private investment matching public support to microenterprises/ total public support)	%			Intermediary/ FoF

9.9. Proposed schedule for the evaluation of the expected results

The definition of indicators is the cornerstone of a feedback system that will allow the fund to adapt over time. The next step is to create a mechanism for these data to filter up to the management process, and ultimately to inform changes to the investment strategy, if needed.

The MA may consider the content of the required specific report as listed in Article 46 (2). Fiche No. 4B 'Reporting on financial instruments to the Commission under the annual and final implementation reports' provides, on a provisional basis, much more detailed information concerning the reporting obligations of the MA. This information will be part of the Implementing Act under preparation. However, the requirements for reporting to the Commission do not limit the reporting requirements that the MA may consider necessary to get from the fund of funds or the financial intermediary.

In order to be able to respond to its obligations towards the Commission, MAs have to make sure that all the necessary information is available. For that, the overall data set should be part of the funding agreement between the MA and the financial intermediary. In this context, also the requirements regarding the monitoring system allowing for IT-based data collection and reporting might be specified.

Annex IV of the CPR provides **secondly** another element of the reporting for the MA (via funding agreement). This second element is about the steering of the FI. The MA may pilot the FI to some extent through conditions in the funding agreement about targeted results, leverage, reutilisation of resources and responses of the FI, when things develop differently and deviations occur.

The MA could, therefore, decide to set up a monitoring and reporting system that provides them with information on the performance of the FIs in shorter intervals, e.g. with **quarterly** monitoring reports. A closer monitoring would allow the MA to identify possible hinders and issues in FI implementation and to facilitate its management. As an example, the MA should include the amount of eligible expenditures incurred (in line with Article 42(1) (a)(b)(d) in payment requests. A bottom-up reporting approach could be implemented as defined below.

Figure 34: Steps of the reporting process

Source: PwC Ex-ante assessment methodology for financial instruments for 2014-2020.

For ensuring **data collection** and availability, the overall data set should be part of the funding agreement between the MA and the financial intermediary. In this context, it is advisable to define a standard reporting format, for instance an IT-based system or a common template. This will make data aggregation more efficient.

For the **operational information** reports on items such as like deal flow, addressed target groups, uptake of the FI (to phase inter alia the payments of the contribution) and/or risk profile of the implemented investments might be necessary. More generally, such a reporting is to document the progress made in implementing the FI over the preceding period. Progress reports should include elements such as analyses of progress made in comparison with the established investment strategy as well as the provisions of the funding agreement.

For the **financial reporting** element**,** the information with respect to **accountability** is important. Annex IV states that minimum requirements of such documentation are included in the funding agreement. As there are different regimes to implement FIs, the minimum requirements are expected to be different and adapted to the situation. If the MA has entrusted the implementation of the FI to a financial intermediary, the documentation and the audit of the escrow account (normally a part of the audit of the whole entity where the escrow account is located) will be important. A system to document the current payments for the management and liabilities for present and future fees will be needed as well. If the FI is implemented by a dedicated entity such as a fund with its own legal personality and defined governance for different groups of investors (who may have different non-pari passu arrangements) then a complete set of financial statements will be needed, including:

- Economic out-turn account;
- Balance sheet and P&L;
- Management costs statement;
- Various notes to financial statements.

The funding agreement has to fix appropriate documentation requirements.

Periodicity

The funding agreement is required to contain provisions for the monitoring activities and revision of the investment strategy. Typical practice is to establish a biannual monitoring report and accompanying FoF investment board meeting dedicated to monitor these indicators and their level of results' achievement to further on make potential changes to the investment strategy.

Section 8.4 above proposes 2 structures therefore the schedule to evaluate the expected results could be different:

- Proposed structure 1: In this scenario, an ESIF Fund-of-Funds is established for several Operational Programmes thus the defined indicators for each OP concerned need to have aligned periodicity for accuracy, relevance and practical management. Under this option, the fund will include FIs for micro-enterprises and entrepreneurs, final recipients which are also targeted by OP Innovation & Competitiveness. The monitoring and evaluation system for micro enterprises and entrepreneur has to be aligned with the system to be set-up under OP innovation and competitiveness. The MA might consider to have monthly reports as per previous JEREMIE initiative under the EIF, a quarterly report may be sufficient if the reporting for the new initiative to support SME under IC OP becomes monthly

- Proposed structure 2: In this scenario, the MA has direct contact with financial intermediaries and needs to align the different schedules to monitor the progress and performance of each FI at the same time; in order to facilitate decision-making and overall view of the achievement of all the FIs.

As a general recommendation, the monitoring and evaluation system of the FIs needs to be designed in such a way that it avoids administrative burden for the financial intermediaries and a relevant amount of quantitative data to enable reporting on a monthly basis and quick decision-making.

When considering the reporting schedule that the MA has to adopt vis-à-vis the EC, the MA could envisage performing an evaluation of the performance of each FI after 2 years of existence, corresponding to the mid-term evaluation which shall be carried by 1 July 2017 for the HRD OP. The performance evaluation of all the FIs may be based on the compilation of the monthly or quarterly reports produced (so-called progress reports), according to the funding agreement and the arrangements with the financial intermediaries. These progress reports may substantiate the mid-term evaluation of the FIs to be conducted, if relevant, in parallel with the mid-term evaluation of the HRD OP.

10. Conclusion

In the present report, an analysis was provided in order to provide quantitative and qualitative estimates of financing gaps and market failures, so that recommendations are provided of potential FIs related to the OP Human Resources development. It was estimated that the following amounts could be channelled through FIs in three policy areas as follows:

- Micro-guarantee instrument: EUR 10m
- Personal Microfinance instrument: EUR 5m
- Business Microfinance instrument: EUR 5m

If Bulgaria decides to create and implement Financial Instruments dedicated to support Human Resources Development, it is important to pay particular attention to the following key factors for success, beyond the recommendations and action plans set out in this study.

Build on existing experience with FIs

Experience with FIs is limited in Bulgaria, for that reason it is more logical to build on existing experience such as JEREMIE and the National Guarantee Fund.

Provide technical assistance for setting up projects

Use of FIs requires the development of project evaluation expertise as well as an increased awareness of the concept of return on investment and the forecasted business plan. Technical assistance will be needed to ensure that these tasks of the project preparation are successfully carried out.

Raise awareness

If uptake of financial support is to be maximised, then it is vital that there be an important awareness raising action to make potential beneficiaries aware that the funding exists.

Redefine the scope of the projects

It is essential to have the ability to redefine the scope of projects to ensure that they are *integrated, sustainable and bankable*. An FI requires the involvement of the public sector together with the private sector on larger scope projects, all while ensuring the public sector make a financial return. In the long run, this return will be used to help recycle the funds initially invested.

Separating the economic and political time horizons

The logic of FIs is associated with a multi-year vision; public actors are required to adopt a broader perspective to consider the projects in their entirety in the medium to long term.

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