

- ESF
- EUR 7.32 million
- Loan + soft support
- Employment and social inclusion
- Poland

*... providing loans
combined with soft
support for social
economy ...*

Financing the social economy

Case Study



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Abbreviations

BGK	Bank Gospodarstwa Krajowego – State Development Bank
ERDF	European Regional Development Fund
ESF	European Social Fund
ESIF	European Structural and Investment Funds
OP	Operational programme
MID	Ministry of Infrastructure and Development (managing authority)
MLSP	Ministry of Labour and Social Policy (intermediate body)
PLN	Polish zloty, the national currency
SEE	Social Economy Enterprise
TISE	Towarzystwo Inwestycji Społeczno-Ekonomicznych S.A. – Society for Social and Economic Investments



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1 Summary

This case study reviews the ‘Financial Engineering Support for Social Economy Development’, a project co-financed by the European Social Fund (ESF) that provides loans and ‘soft’ support such as free advice, to socially-oriented enterprises (referred to as ‘social economy enterprises’ or SEEs) across Poland. It was created under Poland’s Human Capital Operational Programme 2007-2013 (OP) as a pilot project to improve SEE access to finance and to tackle unemployment and social exclusion. Final recipients, like the Christian social cooperative ‘Our House’, could access loans coupled with up to 30 hours of free advice. With this loan, this social cooperative could offer a new service, add more jobs and create better working conditions.

The instrument’s design fits the needs of its target group. Low-interest loans are combined with free advice to improve final recipient business skills. Products are delivered through a holding fund and a single financial intermediary manages five loan funds that cover all of Poland. This structure ensures efficiency gains and economies of scale. At June 2015, EUR 6.88 million were disbursed to 288 SEEs through 357 loans, creating 250 jobs and safeguarding an additional 1 000. This is the combined result of two rounds of investment – the instrument finished its first turnover of funds and is currently re-investing in a second round. At the moment of drafting, these figures may not grasp the broader social impacts that would materialise over time and become available for future evaluations.

This project shows that, to improve social entrepreneurship, a scheme should simultaneously address several SEE needs. These include limited collateral or financing possibilities, financing difficulties due to limited profitability and considerable risk, limited experience with external finance or administrative needs and cooperation with other social economy actors such as support centres.

The instrument should continue beyond 2015, with a significantly increased budget. Its impact will be increased by supplementary instruments such as guarantees and venture capital aimed at the social sector.



Financial Engineering Support for Social Economy Development, Poland

THE FINANCIAL INSTRUMENT

Funding source

European Social Fund (ESF), National Operational Programme Human Capital 2007-2013

Type of financial products

Loans combined with additional advisory services

Financial size

EUR 7.32 million operational programme resources (EUR 6.22 million from ESF and EUR 1.1 million from national public funding)

Thematic focus

Promoting sustainable, quality employment and supporting labour mobility

Promoting social inclusion, combating poverty and any discrimination

Timing

July 2012 to December 2015 – Project implementation

Project monitoring until December 2020

Partners involved

Ministry of Infrastructure and Development (MID) (managing authority)

Ministry of Labour and Social Policy (MLSP) (intermediate body)

Bank Gospodarstwa Krajowego (BGK) – State Development Bank (holding fund manager)

Towarzystwo Inwestycji Społeczno-Ekonomicznych S.A. (TISE) – Society for Social and Economic Investments (financial intermediary operating five separate loan funds)



ACHIEVEMENTS

Absorption rate

99.34%¹ of OP resources: ESF and national funding (at June 2015)

EU leverage

1.18 times²

Leverage of public resources

1 time³

Re-investment

22.26%

Main outputs

288 SEEs assisted, EUR 6.88 million disbursed through 357 loans, creating 250 jobs at June 2015. This includes both rounds of turnover:

- first turnover: EUR 6.14 million disbursed through 312 loans to 258 SEEs, creating 240 jobs
- second turnover: EUR 0.74 million disbursed through 45 loans to 30 SEEs, creating 10 jobs

Exchange rate: PLN 1 = EUR 0.23

1 The absorbed amount of EUR 7.27 million includes the lending and 'soft' support budget as well as management costs and fees. This is made of about EUR 7.2 million in investment budget including costs for fund management and fees, and about EUR 0.1 million for 'soft' support. This is further elaborated in section 3.1.

2 EU leverage is calculated as the total amount of finance to eligible final recipients, i.e. EUR 7.32 million divided by the total amount of ESF allocation to this financial instrument, i.e. EUR 6.22 million. It does not include the reuse of resources returned to the instrument.

3 Leverage of public resources is calculated as the total amount of finance to eligible final recipients, i.e. EUR 7.32 million divided by the total amount of public resources allocated to this financial instrument, i.e. EUR 7.32 million. It does not include the reuse of resources returned to the instrument.



2 Description of the financial instrument

This scheme tackles the social economy financing gap highlighted by a special ministerial task force and stakeholder consultations. It involves a holding fund that exploits the manager's vast experience, and a single financial intermediary for all of Poland, responsible for managing five loan funds.

2.1 Rationale

Poland's economic transformation since the early 1990s saw some groups experience high unemployment, lower social standing and reduced living standards. The state's response favoured employment rather than expanded social support. However, the disabled, the socially excluded, the long-term unemployed and others were disadvantaged in the labour market. The social economy can play an important role in engaging them. SEEs offer them a chance not only by creating jobs, but by stimulating the integration and development of local communities and unlocking overlooked human potential.

SEEs value social goals above economic ones. For financial institutions non-profit enterprises have high credit risks, normally with a limited credit history or no collateral. Thus, financial institutions often avoid meeting SEE needs. Insufficient attention from banks and limited access to finance are among the major barriers to growth that Polish social entrepreneurs face. Some 37% of SEEs surveyed in 2008 by the Foundation for Socio-Economic Initiatives pointed to difficulties in obtaining external finance as the main barrier to their economic activity.

A pilot project within measure 1.4 ('Financial Engineering Support for Social Economy Development') of the OP supports SEE development through loans. Its objective is to tackle unemployment and social exclusion. It aimed to cover 250 SEEs and create 50 jobs between 2012 and 2015, during its first round of investments. At June 2015 it exceeded these targets by assisting 288 SEEs in both the first and second investment rounds and by creating 250 new jobs. It directly contributed to ESF and the OP's core objectives in employment promotion and social inclusion. Its status of system-project means it provides a major contribution to delivering policy aims of the relevant institutions in labour market and social policies.

When designing the instrument, consultations involved various institutions and a special task force led by the intermediate body (MLSP) on solutions for the social economy. Their conclusions, also based on reports about social entrepreneurship, were that the country's social economy sector was underdeveloped and there was potential for SEE activity. No other market assessment was commissioned.



Neither managing authority nor intermediate body had any substantial experience with financial instruments for labour market and social policies. Therefore the project received 'pilot' status and its aim was to provide experience and verify SEE demand for revolving finance. The holding fund manager's experience with such schemes, both funded nationally and by the European Union, contributed to the financial instrument's design and management.

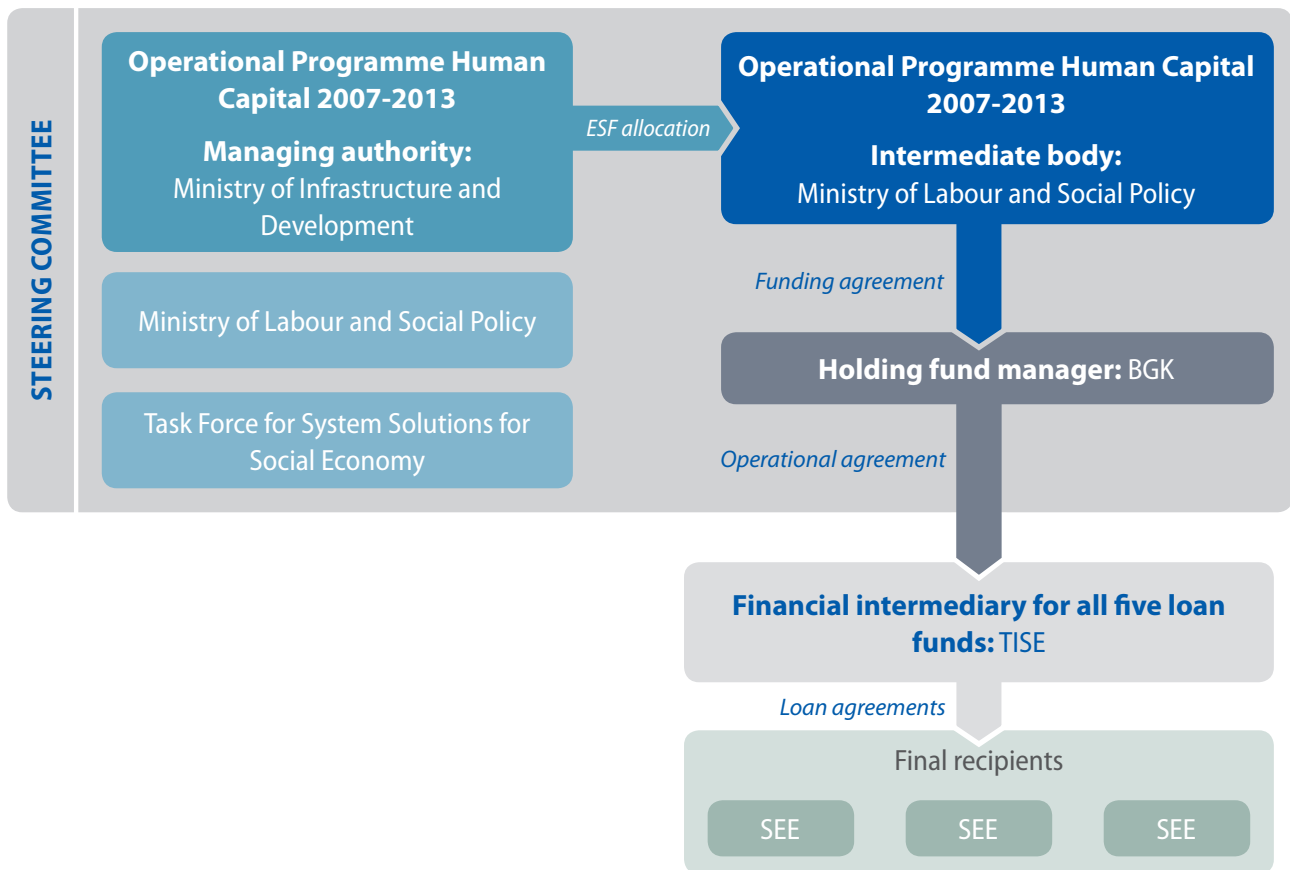
The instrument works in the wider framework of public support for social economy. Within the OP, a supplementary project prepares business advisors in a country-wide network of Social Economy Support Centres. The advisors' role is to help SEEs access finance. Additional synergies may arise with regional ESF grant support to combat exclusion and for strengthening the social economy.

2.2 Organisational structure

The scheme's structure is based on a holding fund and five loan funds covering the whole country, divided into five macro-regions. It consists of a managing authority, an intermediate body, a holding fund manager and a financial intermediary. The intermediate body (MLSP) is the government body responsible for labour and social integration policies, and thus in charge of the OP priority under which this instrument falls.

Under the funding agreement, the intermediate body entrusted BGK with the role of holding fund manager. TISE was selected as financial intermediary for all five funds through an open procurement procedure. The project is supervised by a steering committee including the managing authority, the intermediate body and the MLSP's other relevant units, the holding fund manager and the Task Force for System Solutions for Social Economy. The financial intermediary may be invited on an ad hoc basis as observer.

Figure 1: The financial instrument's organisational structure⁴



4 The term 'operational agreement', defining the contract between the holding fund manager and the financial intermediary, is not related to Structural Funds regulation. In the 2014-2020 programming period, only funding agreements are foreseen.



Christian social cooperative 'Our House': Objectives

The Christian social cooperative 'Our House' operates an integration kindergarten, an integration nursery and a music nursery in Warsaw. Its aim is to create modern, thriving places where children can freely play, develop, grow and learn. All locations are open to communication and cooperation with parents and the local community. The Cooperative took a 5-year loan of PLN 100 000 (EUR 25 000) to build and equip a hall for sensory integration therapy, to equip playgrounds in the integration nursery and kindergarten, as well as for advertising. Sensory integration therapy is based on movement and requires properly arranged space.

External capital was necessary because the cooperative did not have sufficient funds to finance the investment. Even though the recipient was not required to contribute funds, it did so to a small extent.



2.3 Financial products and financial terms

The instrument offers low-interest loans to SEEs, distributed by a financial intermediary, who also reaches out to potential final recipients through information and promotion activities. Promotional activities involve cooperation with Social Economy Support Centres.

The maximum loan amount is PLN 100 000 (EUR 25 000) with interest rates of up to half of the central bank rate, i.e. 0.88% at June 2015. This may be reduced to a quarter of the rate, or 0.44% at June 2015 for eligible entities. The maximum repayment period is 60 months and there is a six-month grace period. No contribution from borrower or loan guarantor is required. The primary form of collateral is a signed blank promissory note⁵. Loans and repayments are free from fees or commissions.

⁵ This instrument is used as legal collateral in Poland, where a note is given to the lender 'in blank', i.e. there is no sum filled in. In case of loan default, the lender calculates the amount due, made up of the borrowed amount plus the interest accrued until that date, and fills in the note.

Loans finance SEE investments to expand business activity by increasing revenue or employment. Applicants prepare a business plan and prove the investment's viability. Any eligible SEE must also demonstrate they are micro or small enterprises conducting an economic activity for at least 12 months before applying for the loan.

Loans are offered jointly with ESF-funded consulting to facilitate the use of funds. Borrowers receive up to 30 hours of free advice on issues such as accounting, taxes, management of human resources, information and promotion. The average is 20 hours and it is highly appreciated, especially by SEEs with insufficient experience in finance.

Figure 2: Composition of the support package



The support complies with *de minimis* aid rules. The holding fund allows the financial intermediary, through an operational agreement, to grant both the loan and 'soft' support on their behalf.

Christian social cooperative 'Our House': Financing gap

The Cooperative does not consider its investment needs as too specific to distinguish them from ordinary, i.e. non-social enterprises. However, there was no market alternative for the cooperative to acquire the necessary funds, other than the loan through this financial instrument. No financial institution offered any competitive lending option.





3 Main strategies to support social entrepreneurship

The instrument combines loans and free advisory support to cover all the needs of social enterprises. Its design involved the managing authority and the intermediate body as well as the holding fund manager, while the latter along with the financial intermediary mainly handled implementation. The steering committee facilitates information exchange. Regular reporting ensures the proper deployment of funds.

3.1 Design phase

The financial instrument's design is based on recommendations from the Task Force on System Solutions for Social Economy, appointed in 2008 by Poland's Prime Minister and chaired by the Minister of Labour and Social Policy. It operates under another ESF-funded project within the OP, supervised by the intermediate body. The group created the concept of an ESF-funded SEE support scheme based on preferential loans distributed regionally. The scheme was designed to function as a financial instrument with a holding fund structure. It was a way to test this method of financing SEEs, to verify demand and provide experience for the design of financial instruments.

To ensure critical mass, the budget was set at PLN 30 million (EUR 7.3 million), made up of ESF (85%) and state funding (15%). No private investors or contributions from final recipients were envisaged. The investment fund had PLN 29.6 million (EUR 7.2 million), including management costs and fees, and 'soft' support services were allocated PLN 400 000 (EUR 100 000). At the design stage no arrangements were made to share costs between stakeholders. The holding fund pays the financial intermediary based on the volume of loans distributed.

An important aspect of the project was the territorial deployment of funds. To answer regional specific needs, the project divided Poland into five macro-regions with similar socio-economic conditions within each one. There was a separate lot for each region in the call for tenders for financial intermediaries.

The target group was specified as economically active SEEs. They had to comply with additional formal, economic and social criteria. Although leveraging private resources was not anticipated, some final recipients stated that additional private resources were involved in their investments, but these were not monitored.



The use of a holding fund structure exploited the fund manager's expertise in delivery and administration. The managing authority and intermediate body could delegate tasks including ensuring the specific implementation requirements are met, coordinating the scheme's territorial deployment, selecting and managing financial intermediaries, monitoring investments and handling all internal financial settlements and payments.

The administrative constraints on the design of this instrument were not very different from any similar scheme in any other economic sector for different types of final recipients.

3.2 Set up phase

Based on the selection criteria adopted by the monitoring committee, the managing authority and intermediate body appointed BGK as beneficiary for the project and as holding fund manager. The funding agreement was concluded in July 2012. Detailed rules for financial instruments were developed through the Steering Committee and between the managing authority (at that time the Ministry of Regional Development, later replaced by the Ministry of Infrastructure and Development), the intermediate body (Ministry of Labour and Social Policy) and the financial group of the Task Force for System Solutions for Social Economy and the holding fund manager (BGK).

The holding fund manager is responsible for implementing the scheme, including financial intermediary selection and supervision, OP resource management, settlements and payments, as well as accountability to the managing authority and intermediate body. The financial intermediary was selected through a public procurement procedure. The criteria included an indicative cost for granting a loan and for providing 'soft' support, as well as methods for reaching and appealing to SEEs. The open call for tenders was announced in September 2012, with one lot for each macro-region.

The financial intermediary (Towarzystwo Inwestycji Społeczno-Ekonomicznych S.A. or TISE) was selected for all five lots and an operational agreement was concluded in January 2013. TISE's role is to provide loans and consulting services to SEEs. It is also responsible for monitoring the use of loan funds, repayments and the recovery of any non-performing loans.

The financial intermediary reports to the holding fund manager on implementation of the funding agreement. It also monitors the status of loans with final recipients and evaluates investments at various stages. The holding fund manager reports on the instrument's performance quarterly to the intermediate body and every half a



year to the managing authority. There is an exchange of information between all institutional stakeholders also at steering committee meetings.

The funding agreement envisages periodic performance reports from the financial intermediary to the holding fund manager, along with monthly statements of loans granted and quarterly reports on *de minimis* aid granted. TISE should immediately inform the holding fund manager of any implementation problems, irregularities or intentions to discontinue loan contracts.

Final recipients complete investment evaluation questionnaires when signing the loan agreement, mid-term and in the late repayment phase. The results are forwarded to the holding fund manager. To ensure effective loan distribution in compliance with the instrument's framework, TISE monitors repayments and controls borrowers with the help of a network of representatives acting in each macro-region. Samples of borrowers from each of the macro-regions are also visited by BGK to verify compliance, the quality of service and loan impact on the SEE business.

Christian social cooperative 'Our House': Application and administration

The decision to apply for a loan was made at a meeting of the cooperative's members. The application process was short and, as with subsequent processes during the investment, did not involve any excessive administrative burden. Procedures were clear and user-friendly, which was largely thanks to the high commitment and professional approach of the TISE staff.



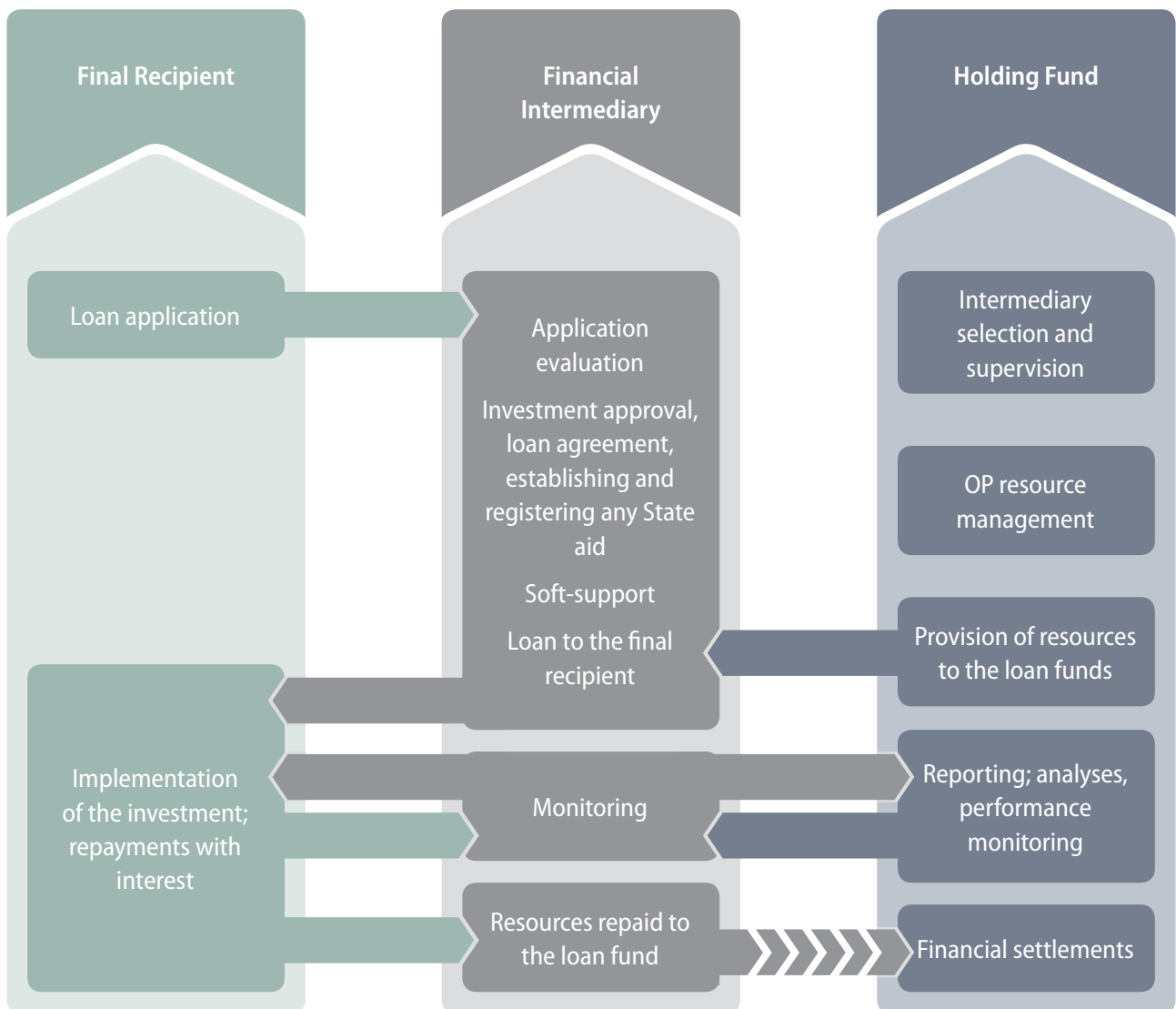
3.3 Implementation phase

The holding fund manager and the financial intermediary marketed the financial instrument. The holding fund manager assured general marketing communication channels such as websites, press material, meetings and interviews with journalists, sponsored articles in the national press, three conferences and promotional material like leaflets and web banners. The financial intermediary distributed information about loan applications in all macro-regions via the web, advertisements in local newspapers and cooperation with Social Economy Support Centres. The marketing strategy was fully adjusted to the financial instrument life cycle and has not required modifications. Emphasis was put on the timing of calls for applications to attract the largest group of SEEs.

SEEs access the scheme by submitting a loan application with a business plan, which is evaluated by the financial intermediary in accordance with a dedicated uniform Assessment Methodology, Lending Regulation and the operational agreement.

The financial instrument investment strategy had only one significant change. Initially the strategy envisaged a single turnover of funds, but at the beginning of 2014 a second turnover round was initiated. Based on demand and project outputs, the financial product was tailored to target group needs.

Figure 3: Process of accessing the financial products



3.4 Winding-up phase

The financial instrument's investment period is expected to continue until the end of 2015. Monitoring will continue until the end of 2020. With regard to the exit strategy, it is assumed that any future decision on continued fund turnovers



will be based on a prior assessment of the scheme's outputs and outcomes in 2016 or 2018 against criteria set by the managing authority and intermediate body. Formally, the exit strategy will be included in an annex to the operational agreement between holding fund manager and financial intermediary.

The scheme's final results and their comparison with initial expectations will be available after the end of the monitoring period.

Christian social cooperative 'Our House': Advantages and challenges of the financial instrument

The main benefit of using the financial instrument was that it enabled the hall to be built and equipped, with tools that offered sensory integration therapy for children. This also considerably improved the cooperative's position in the market for care and educational services in Warsaw. The investment also provided experience in the administrative requirements and procedures of accessing a financial instrument. Such experience will help when applying for resources for further development.

The cooperative's opinion of the scheme is unambiguously positive with no significant problems or challenges to date. Advice to potential final recipients is to carefully consider the purposes of the loan. They must guarantee future revenues that allow repayment. Another important element is employing proper personnel, since this determines the success or failure of an investment.





4 Achievements and challenges

The financial instrument, although still in operation, has already exceeded its targets, creating 250 jobs and supporting 288 SEEs at June 2015. Its main advantages are combining loans with 'soft' support, an effective organisational structure and the financial intermediary's vast experience. Challenges, such as regulatory constraints on intermediary selection, or the numerous eligibility criteria imposed on final recipients, were eventually overcome.

4.1 Outcome

Although the financial instrument is still in the investment period at the time of drafting, its outcome is already better than expected. The scheme's loans served more SEEs and created more new jobs than originally anticipated. The second round of investments has already started and, at June 2015, EUR 6.88 million were disbursed through 357 loans, supporting 288 SEEs or 115% of target and creating 250 jobs, which is 480% of initial expectations and project assumptions. Additionally, around 1 000 safeguarded jobs have been reported. The leverage effect of ESF, for the first turnover of funds, is 1.18, as additional private resources were not envisaged and are not reported.

4.2 Main operational achievements

Although there is no detailed evidence-based evaluation yet, an analysis of up-to-date performance shows good results. Evidence of the financial instrument's long-term impact should be available when all the final recipient evaluation surveys have been collected. Additionally, the financial intermediary will also provide an assessment of the scheme's impact on the SEE environment.

The combination of loan and 'soft' support significantly increased the quality of investments as well as the scheme's 'friendliness' to borrowers. 'Soft' support also generated added value for SEE business skills. Importantly, the loan conditions are highly attractive, with low interest rates, no commissions or additional fees, minimum collateral requirements and no contribution required from final recipients.

The organisational structure was highly effective, ensuring cooperation between stakeholders. The framework of the steering committee helped solve issues of strategic relevance. The holding fund manager's financial market experience and professional administrative capacity made sure that management of the instrument was cost-effective.



Finally, the financial intermediary's international background and experience in cooperation and lending to the social economy sector contributed significantly to the operational achievements. Well-developed procedures both efficiently handled borrower requirements and also enabled quick solutions to emerging problems.

4.3 Main challenges

For the managing authority, the delivery of the instrument also involved challenges, especially with the selection of financial intermediaries through a public procurement procedure.

For the financial intermediary, challenges included the multiple eligibility parameters imposed on final recipients, insufficient institutional databases on SEEs and inadequate capacity in some Social Economy Support Centres. These challenges were overcome thanks to TISE's own administration and market penetration in all macro-regions.

Christian social cooperative 'Our House': Achievements

Thanks to the investment it was possible not only to offer a new social service, but also to increase the number of jobs in the cooperative and to improve working conditions for therapists. Revenues from operations have increased, along with the cooperative's position in the Warsaw market. The cooperative is planning to develop further, through more branches in Warsaw. After the positive experience with this financial instrument, the cooperative is open to using financial instruments in the 2014-2020 programming period as well.



With this support, disabled children have benefited from therapy in a fully equipped hall. The cooperative also increased its competitiveness in the market for care and educational services.



5 Lessons learnt and outlook

The social economy sector in Poland is relatively underdeveloped as compared to most EU Member States, and Polish SEEs face a financial market gap that impedes their development. Projects providing easier access to finance for SEEs are valuable from both an economic as well as a social point of view. The experience of this financial instrument shows that there is strong market demand for such loans. These products proved to be better than grants in terms of promoting responsible business decisions and financially viable investments. The project produced significant outputs in job creation and it is likely that future analyses will show growth in the SEEs supported.

The project also brought additional intangible benefits to final recipients. Apart from the funds received, borrowers gained expertise in management, business planning, risk-taking, handling external finance and in implementing EU fund projects. They also received or may receive a positive credit evaluation, which in future would help them obtain commercial finance.

Access to financial instruments is crucial for strengthening Poland's social economy. This was recognised and promoted in national government development strategies and programmes such as the National Programme for the Development of Social Economy. This programme implements medium-term strategies like the National Development Strategy 2020, the Development of Social Capital Strategy, the Human Capital Development Strategy and the National Strategy for Regional Development.

The financial instrument described here is a pilot to test this way of financing social enterprises. The experience will be used in the 2014-2020 programming period, where country-wide ESF co-financing is envisaged under the national operational programme Knowledge Education Development 2014-2020. This programme addresses the need for reform and systemic change in employment, social inclusion, education and good governance. The operational programme aims to strengthen public policies that pursue Europe 2020 objectives in those areas. The shape of the programme and its scope are highly influenced by experience in implementing ESF co-funded OPs.

Due to the good results, this financial instrument is proposed to continue under the 2014-2020 national operational programme with a significantly increased budget. This depends on the outcome of an ex-ante assessment study to justify the instrument's continuation. Moreover, the positive experience spilled over to other potential financial products, and the managing authority has proposed additional ESF co-financed instruments to provide guarantees and venture capital in the social sector.



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