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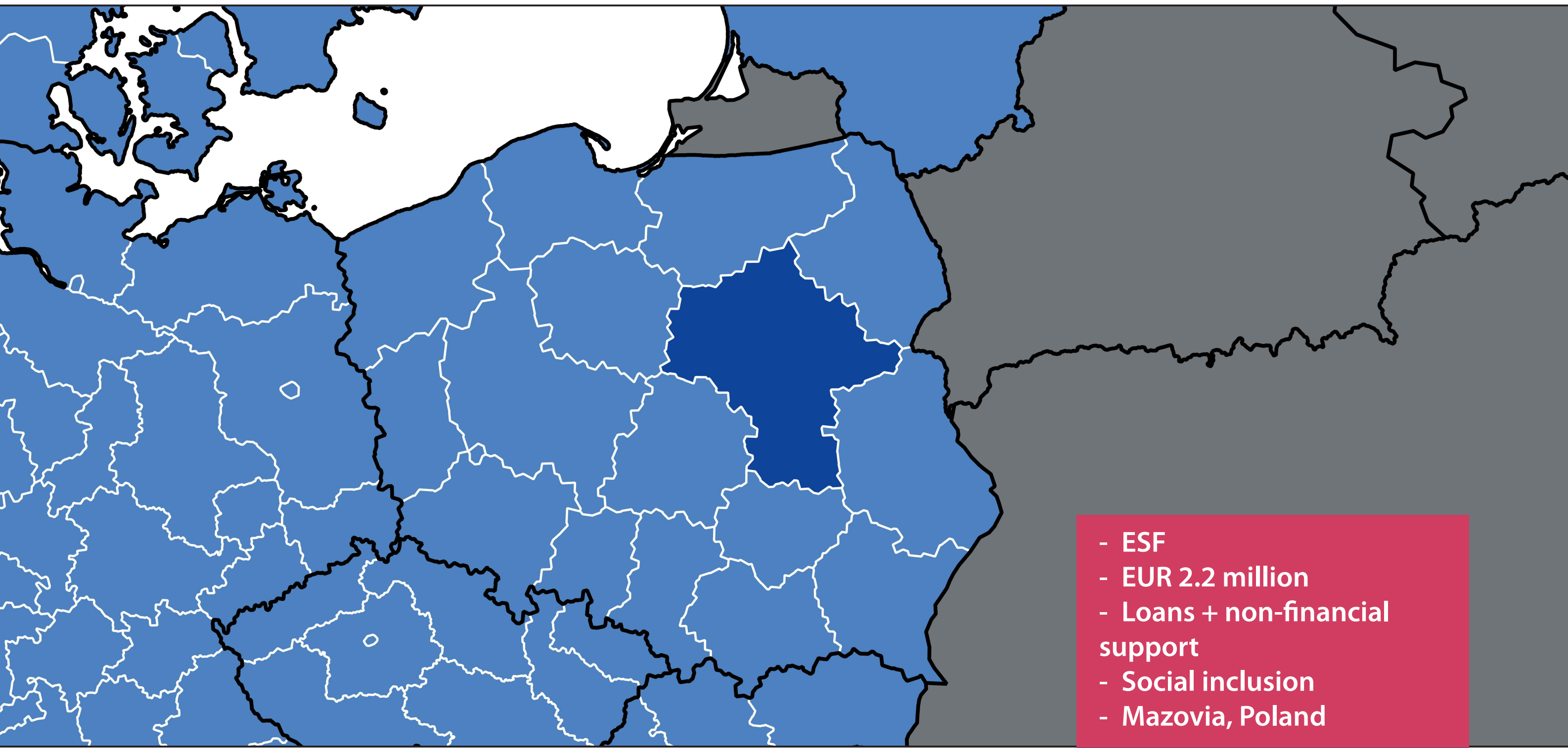
ESF



- ESF
- EUR 2.2 million
- Loans + non-financial support
- Social inclusion
- Mazovia, Poland

…financial instruments help people turn their ideas and skills into a new business and sustainable employment…

Creating new jobs and entrepreneurship through financial instruments

Mazovia, Poland

Case Study

European Commission

European Investment Bank
The EU bank

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The authors of this study are a consortium of five companies: Sweco (lead), t33, University of Strathclyde – EPRC, infeurope and Spatial Foresight.

Abbreviations

Abbreviation	Full name
ESF	European Social Fund
ESIF	European Structural and Investment Funds
EU	European Union
MID	Ministry of Infrastructure and Development[1]
MLSP	Ministry of Labour and Social Policy[2]
OP	Operational Programme
PAED	Polish Agency for Enterprise Development
PLN	Polish zloty, the national currency
SRCP	Stowarzyszenie 'Radomskie Centrum Przedsiębiorczości' - 'Radom Entrepreneurship Centre' Association

1 As of November 2015, the Ministry of Infrastructure and Development changed to the Ministry of Economic Development. The case study concerns the financial instrument's delivery period of 2012-2015 and therefore the ministry's name corresponds to the respective one of that time in the programming period 2007-2013.

2 As of November 2015, the Ministry of Labour and Social Policy changed to the Ministry of Family Labour and Social Affairs. The case study concerns the financial instrument's delivery period of 2012-2015 and therefore the ministry's name corresponds to the respective one of that time in the programming period 2007-2013.

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1 Summary

This case study reviews the financial instrument 'Creating new jobs and entrepreneurship in Poland's Mazovia region', a pilot scheme implemented under Poland's European Social Fund (ESF) co-funded Human Capital Operational Programme (OP). The financial instrument provides loans of up to EUR 12 500 as well as training and business advice to Mazovian residents who intend to start a business but have limited access to capital. Loans are provided at below market interest rates and have reasonable collateral requirements. The financial instrument's objective is to tackle intra-regional disparities in unemployment as well as underemployment and to promote entrepreneurship. The financial instrument helped people like Mr. Andrzej Snopek, who used a loan to open a restaurant.

This financial instrument shows how ESF co-funded loans can help people with insufficient capital but with ideas and skills, to start a new business. This is especially important in areas with a general lack of job opportunities that need to improve the local socio-economic situation. It is also an example of cooperation between national and regional OP institutions for the implementation of financial instruments. To the end of 2015, the financial instrument helped to create 151 jobs, through personal loans worth EUR 1.6 million. By encouraging individuals to take responsibility for their financial future and increasing their business capabilities, the financial instrument also promoted an entrepreneurial culture in the region.

The financial instrument's budget of EUR 2.24 million came entirely from the OP, with 85% from the ESF and 15% from state funding. Loans are combined with non-financial support such as training and business advice to increase business sustainability. The financial instrument, managed by a non-governmental organisation supporting local businesses, highlights the importance of selecting capable and specialised financial intermediaries to reach the disadvantaged. It also shows the challenges of coordinating different forms of public support that promote self-employment in a specific territory.

The scheme is expected to continue in the 2014-2020 programming period, possibly combined with an interest rate subsidy. Its positive results led the authorities to consider the possibility of delivering other financial products like ESF-funded guarantees and social venture capital.

Creating new jobs and entrepreneurship through financial instruments, Mazovia, Poland

THE FINANCIAL INSTRUMENT

Funding source

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

Type of financial products

Loans combined with non-financial support

Financial size

EUR 2.24 million operational programme resources (EUR 1.9 million from ESF and EUR 0.34 million from national public funding)

Thematic focus

Social inclusion, employment

Timing

December 2012 to December 2016 – Project implementation
Project monitoring until December 2020

Partners involved

Ministry of Infrastructure and Development (MID) (managing authority)
Mazovia Marshall Office (intermediate body 1st level)
Mazovian Unit for EU Funds Implementation (intermediate body 2nd level)
'Radom Entrepreneurship Centre' Association (financial intermediary)

ACHIEVEMENTS

Absorption rate

75.9[3] % of OP resources: ESF and national funding (as at end of 2015)

EU leverage

1.18 times[4]

Leverage of public resources

1 time[5]

Re-investment

Re-investment has not yet started

Main results

151 personal loans/final recipients, a total of EUR 1.6 million in loans, 151 jobs created (of which 76 for women and 75 for men), 183 participants in the project (of which 94 were women and 89 men) at the end of 2015.

Exchange rate: PLN 1 = EUR 0.25 (Q2 2015)

3 The absorbed amount of about EUR 1.7 million includes the lending and non-financial support budget as well as management costs and fees. This includes about EUR 1.6 million in investment budget including costs for fund management and fees, and about EUR 0.08 million for non-financial support. This is further elaborated in sections 3.2 and 4.1.

4 EU leverage is calculated as the total amount of finance to eligible final recipients, i.e. EUR 2.24 million, divided by the total amount of ESF allocation to this financial instrument, i.e. EUR 1.9 million. It does not include the reuse of resources returned to the instrument.

5 Leverage of public resources is calculated as the total amount of finance to eligible final recipients, i.e. EUR 2.24 million divided by the total amount of programme resources allocated to the financial instrument, i.e. 2.24 million. It does not include the reuse of resources returned to the instrument.

2 Description of the financial instrument

The financial instrument was established to address the worsening economic situation in Mazovia, where large intra-regional disparities in unemployment prevented disadvantaged people and notably women from improving their situation. Set up in one of the worst crisis-affected areas, the financial instrument, managed by a local non-governmental organisation, provides loans and free advisory services to the disadvantaged.

2.1 Rationale

The financial instrument promotes entrepreneurship and job creation in Mazovia, especially among women. In the years before its launch in 2012, the regional economic situation had deteriorated as a consequence of the global economic crisis and the slowdown it caused in Poland. The regional unemployment rate had risen since mid-2008, reaching 8.5% in 2012. Although overall this was still better than the national average of 9.9%, intra-regional disparities were large – unemployment rates ranged from around 5% in Warsaw to over 30% around the city of Radom. A total of 52% of unemployed people were long-term unemployed, 25% were over 50 and 18% were under 25 years-old, and over 43% lived in rural areas. There were also significant numbers of underemployed people – up to a third of all those working, among whom 63% were women. In addition, women were less often self-employed (8% of women were professionally active versus 13% of men).

Available statistics and studies showed access to finance as a major problem for individuals willing to start a business, with disadvantaged individuals, including the unemployed, being particularly impacted. Banks did not offer personal loans for starting a business for more than PLN 10 000 (EUR 2 500), which was a barrier to self-employment. A regional survey carried out by the Stowarzyszenie 'Radomskie Centrum Przedsiębiorczości' (or 'Radom Entrepreneurship Centre' Association – SRCP)[6] found that 61 women out of the 65 surveyed were interested in starting a business, and 57 women could be interested in applying for a loan. This was higher than a 2011 nationwide study, where 63% of employed and 51% of unemployed/inactive women were potentially interested in starting a business.

Against this backdrop, the managing authority decided in 2012 to set up financial instruments in various Polish regions, including 'Creating new jobs and entrepreneurship in the Mazovia region through financial instruments', which is one of the two loan schemes established in the region. The managing authority and intermediate bodies had no substantial experience with the use of financial instruments for the labour market or social policies. Thus, the financial instrument was intended as a pilot to gain experience. However, the regional-level intermediate bodies were familiar with enterprise support schemes through financial instruments under the regional Mazovia OP 2007-2013. Additionally, the financial intermediary, SRCP, had a track record of implementing projects funded by the World Bank, the Polish Agency for Enterprise Development (PAED) and the Ministry of Labour and Social Policy (MLSP), under which it provided loans as well as training and advisory services to individuals and social enterprises.

The financial instrument was to function within a wider framework of public support to promote self-employment, mostly funded from the ESF or the national budget. For instance, start-ups can access loans through another financial instrument with a different financial intermediary under the same Human Capital OP. In addition, there is another start-up financial instrument initiative under the regional OP, a government programme called 'First Business – Support for the Start',

6 With a sample of 100 individuals (65 women and 35 men) who were unemployed, inactive or employed.

a Mazovian regional loan fund and a PAED loan fund for women entrepreneurs. Moreover, grant support is available under the Human Capital OP and the domestic Labour Fund deployed by local labour offices. Finally, there is a range of training and business counselling services available under the same OP.

2.2 Organisational structure

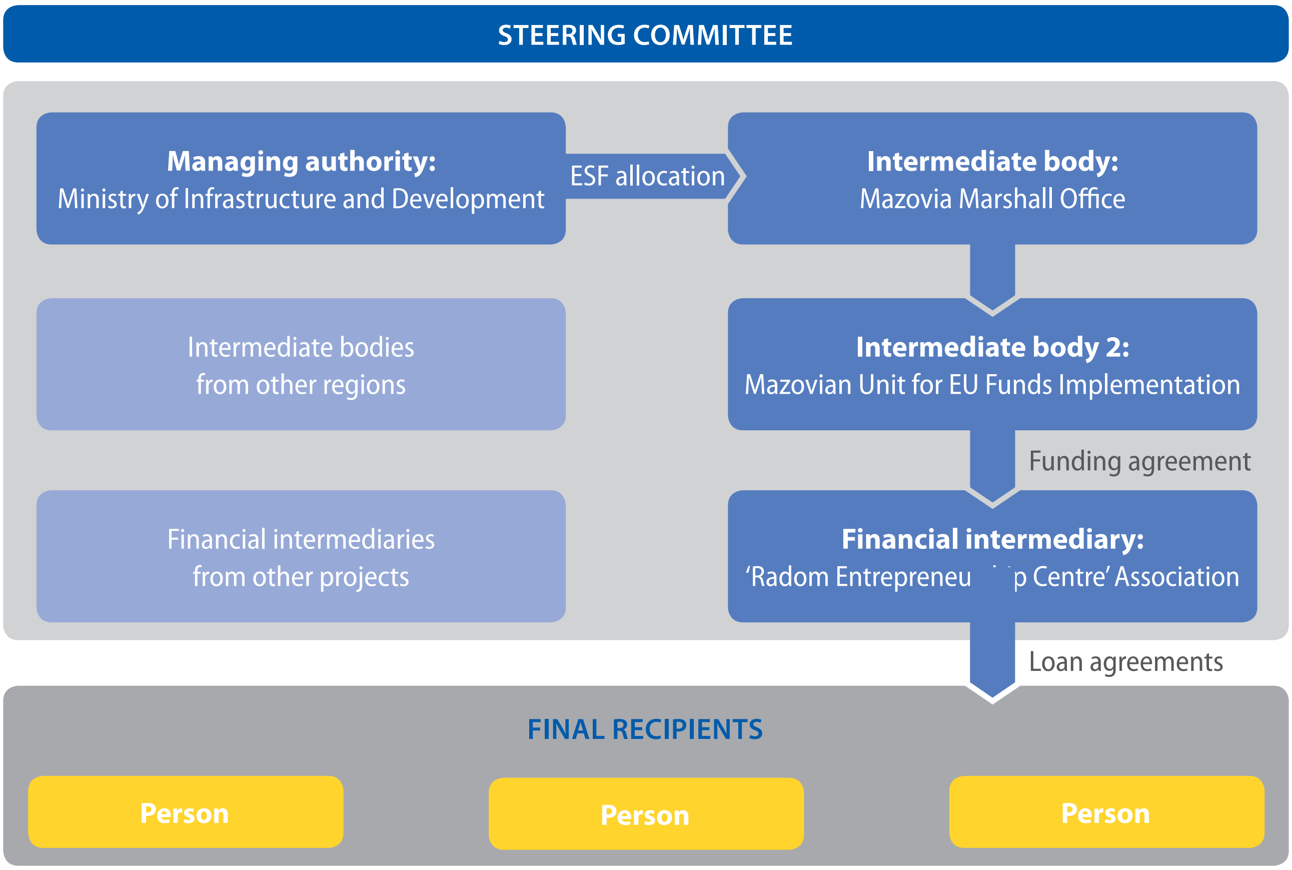
This financial instrument involves several bodies, with different roles and responsibilities.

The **managing authority** (Ministry of Infrastructure and Development – MID) is ultimately responsible for the operation and delegated implementation of the financial instrument to the regional government – the Mazovia Marshall Office, which was appointed as intermediate body.

This **first-level intermediate body** delegated the responsibilities of selecting the financial intermediary, contracting, monitoring, payments and settlements, controls as well as information and promotion under the operation to the Mazovian Unit for EU Funds Implementation (Mazowiecka Jednostka Wdrażania Programów Unijnych, a subsidiary of Mazovia's Marshall Office), which was the **second-level intermediate body**.

The implementation of both ESF financial instruments in the region is overseen by a **steering committee**, chaired by the managing authority, and including all relevant regional intermediate bodies, including the Mazovian Unit for EU Funds Implementation, and financial intermediaries from all financial instruments financed by the OP.

Figure 1: The organisational structure



The **financial intermediary**, SRCP, is a non-governmental organisation based in Radom that targets social activities and supports local micro, small and medium-sized businesses. It has offered public loan funds since 1994 using domestic, EU and other funding. SRCP has implemented other initiatives like a guarantee fund, an entrepreneurship incubator, a social economy support centre and employment promotion campaigns. Its organisational structure includes a project coordinator responsible for general management, while financial decisions are taken by a loan committee, based on applications and recommendations from the SCRP's financial experts. Loan officers provide support for completing loan applications and offer general information to potential final recipients.

'Pronto' Restaurant: Objectives

Andrzej Snopek, an experienced chef, wanted to open a small restaurant but he lacked funds. He needed to lease premises, adapt it to the needs of a restaurant, purchase the catering and refrigeration equipment, equip the kitchen and the dining room as well as purchase the food.

© Pronto Restauracja Andrzej Snopek

2.3 Financial products and final recipients

The financial instrument is directed at residents of Mazovia, who want to start a business but who have difficulty in accessing finance. Unemployed or inactive people are the principal target group, but the scheme is also open to employed people. Potential final recipients shall not have had a business activity or obtained public funding for start-ups in the 12 months prior to the application.

The maximum loan is for PLN 50 000 (EUR 12 500) at an annual interest rate of maximum 4%, which is below the market rate, and with no commissions for borrowers. The repayment period is up to 60 months and there can be a 12 month grace period. Borrowers are not required to contribute self-financing. The collateral needed is a signed blank promissory note[7] as well as either a guarantee, a mortgage, a life insurance policy, blocked funds or consent to the seizure of tangible assets. Applicants must present their business plan, justifying the need for investments and working capital, and the viability of the proposed business.

The financial intermediary provides the loans jointly with ESF-funded non-financial support under the *de minimis* aid rules. Before legally registering the business and receiving the loan, borrowers participate in a three-day group training and one-day group advisory service. There are also two individual consulting services, one prior to registering the business activity and one within a year after, both for a minimum of two hours per person. These address business issues that the final recipients face during start up and in the early stage. The non-financial support is free of charge, and participation in at least 80% of the non-financial support activities is obligatory prior to registering the business activity.

7 This instrument is used as legal collateral in Poland, where a note is given to the lender '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.

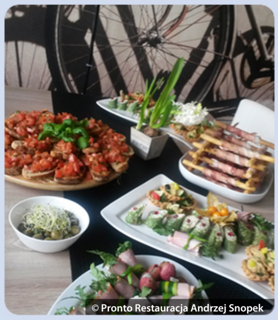
Figure 2: The financial instrument support package

Low-interest ESF loan
(max. EUR 12 500)

ESF-funded non-financial support
(consulting/training)
(group and individual)

‘Pronto’ Restaurant: Financing gap

Other than this financial instrument, there was no viable alternative for Mr. Snopek to obtain the necessary funds. The owner could not fulfil the collateral requirement of a commercial bank loan. At the same time, commercial loans had high interest rates, front-end fees and short funding periods of up to two years. Only the loans offered by the SRCP presented conditions that the borrower felt able to afford.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3 Features of the financial instrument for personal loans

The financial instrument was designed as a pilot to verify the demand of disadvantaged individuals for start-up loans. A regional network of specialists informed the target group about the opportunity, after which word-of-mouth further raised awareness.

3.1 Design phase

After the managing authority defined the target group and framework conditions for the financial instrument, the second-level intermediate body launched a competitive call to select the financial intermediaries. This was based on criteria adopted by the monitoring committee in line with the Structural Funds regulations.

In their applications, financial intermediaries needed to identify an existing financial gap they intended to address, as well as to demonstrate that the project would not make a loss. In addition to operating the loan fund, financial intermediaries were also required to offer non-financial support for setting up and conducting business activities, tailored to final recipients' needs. Potential financial intermediaries included banks, financial institutions and not-for-profit organisations, who could expand their activities while being paid for management.

SRCP's application built on available public statistics and studies as well as on its own research, as described in section 2.1 above, and also focused on creating opportunities for women entrepreneurship. In addition, the need for non-financial services to support aspiring entrepreneurs was emphasised, as a SRCP study in 2011 showed that half of the people surveyed had no knowledge of conducting business activities.[8]

3.2 Set-up phase

SRCP was selected in 2012 and, under the funding agreement, the investment period was between December 2012 and the end of 2016. The financial instrument intended to create new jobs and entrepreneurship for 222 people in Mazovia. This would be achieved by supporting 200 individuals, of whom 106 were women and 94 men, and especially the unemployed, estimated at 55% of all final recipients, and the inactive, an additional 10%.

The total budget was PLN 8.96 million (EUR 2.24 million), entirely from OP funds, with 85% from ESF and 15% from national funding. Contributions from private investors or final recipients were not envisaged. The total budget was split between the investment fund of PLN 8.5 million (EUR 2.13 million), including fund management costs and fees up to a specified ceiling, and non-financial support services of about PLN 0.45 million (EUR 0.11 million). The initial single loan average value was expected to be about PLN 25 000 (EUR 6 250).

8 With a sample of 60 individuals (23 women and 37 men).

'Pronto' Restaurant: Application and administration

Having taken the decision to apply for a loan, the whole process and the formalities took less than a week, thanks to the professionalism and commitment of the financial intermediary.

Subsequent contacts with the financial intermediary, according to the borrower, did not result in an excessive administrative burden, due to the clear and user-friendly procedures.

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3.3 Implementation phase

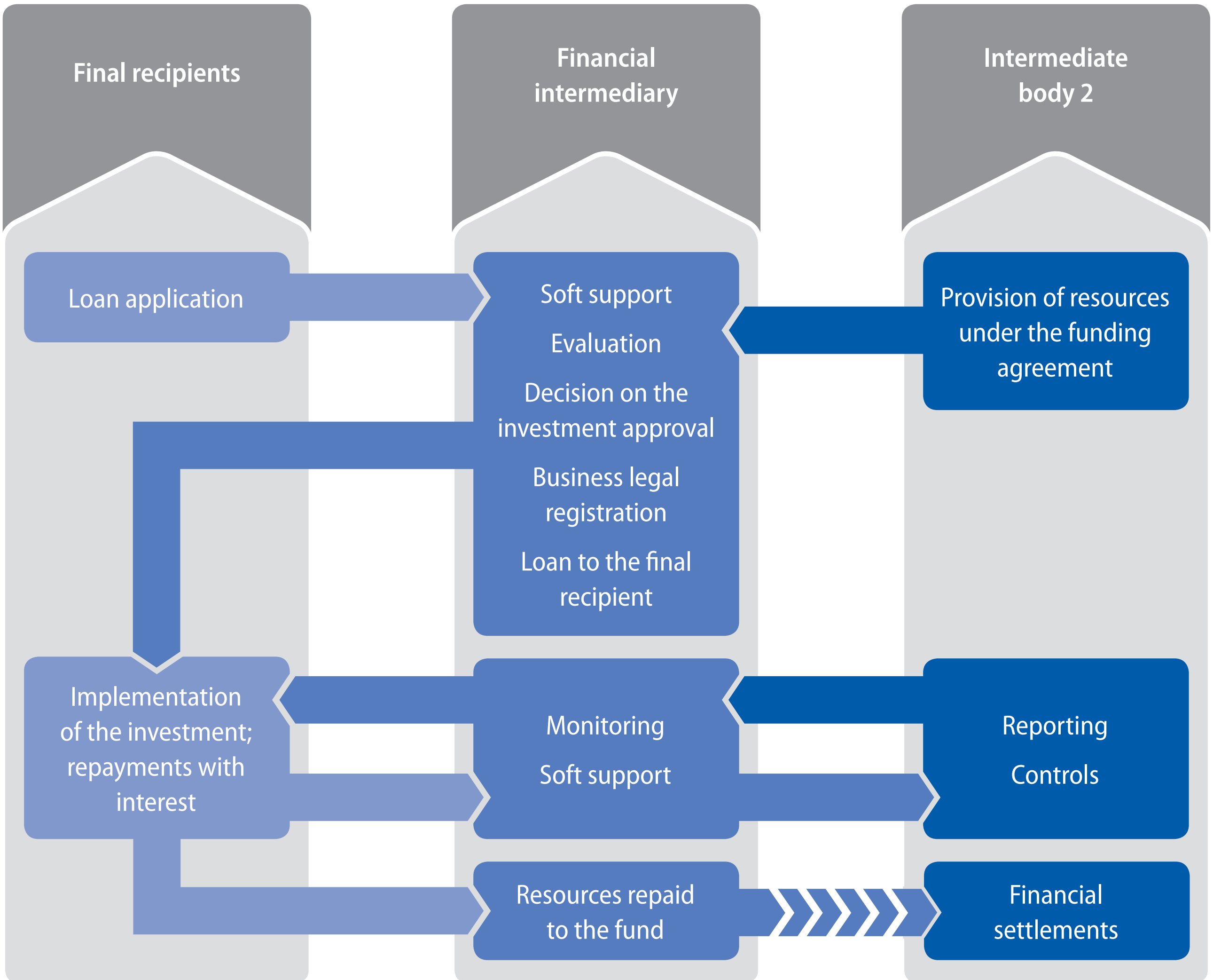
The financial instrument was marketed to potential final recipients by the financial intermediary, who launched a website detailing the scheme's objectives, rules for participation and contact details. Additionally, the financial intermediary held a series of meetings at the territorial Labour Offices with employees who were in direct contact with the target group. The financial instrument was also advertised at job fairs, in local newspapers, through posters, leaflets and on the internet. At a later stage, information about the loans was spread by word-of-mouth, through the positive opinions of the new entrepreneurs and concrete investment examples.

Individuals can access the scheme by submitting a loan application to the financial intermediary, where they can consult a loan officer and develop the proposal further if necessary. The proposal is then evaluated by a SRCP financial expert who assesses:

- compliance with the lending procedures adopted by the financial intermediary;
- readiness of the business;
- suitability of other funding sources;
- repayment capacity;
- proposed collateral; and
- probability of commercial success.

The expert forwards the application to the loan committee of the financial intermediary for the final decision. Applications are assessed within 30 days, after which disbursement can be made in full or in tranches.

Figure 3: Implementation process



Monitoring and reporting is on three levels. First, the financial intermediary monitors, on a monthly basis and based on the loan agreement, the borrower's business activity status, loan use and repayments, as well as use of training and advisory services. Second, under their funding agreement the financial intermediary sends quarterly performance reports to the second-level intermediate body. These detail the support granted and the final recipients served, including the number and value of loans, number of borrowers, management costs and any gains from treasury management. The second-level intermediate body controls implementation based on documentation and on-site visits. Thirdly, the second-level intermediate body submits quarterly performance reports to the first-level intermediate body who informs the managing authority. Key issues related to all the schemes under the Human Capital OP are discussed in the steering committee.

3.4 Winding-up phase

After the end of the investment period in December 2016, resources will continue to be paid back to the financial instrument and investments will be monitored up to the end of 2020. Before the end of the monitoring period, the managing authority and intermediate body will assess the achievements of the scheme and decide whether it should be continued. Whatever the outcome of the assessment, the resources still available will be used to support entrepreneurship after the monitoring period.

4 Achievements and challenges

At the end of 2015, the financial instrument had disbursed 76.9% of its investment funds and helped to create 151 new jobs. Funded businesses are more sustainable due to the non-financial support involved, as well as to the thorough loan assessment process. During implementation there were uncertainties with the interpretation of the regulatory provisions, underestimation of the final recipient financing needs, and coordination between some stakeholders needed to be improved, so there was a steep learning curve. The acquired knowledge will help in the 2014-2020 programming period.

4.1 Outcome

At the end of 2015, the financial intermediary provided loans worth over PLN 6.5 million (EUR 1.6 million), or 76.9% of the scheme's total investment budget. The non-financial support implemented was worth PLN 0.32 million (EUR 0.08 million), or 73.7% of its total budget. A total of 183 people benefited from the scheme, all of whom received non-financial support and 151 received loans. This helped create 151 new jobs, of which 76 were for women and 75 for men, 18 jobs for the age group 15-24, 12 jobs for the age group 50-64, 23 jobs were for the long-term unemployed, 4 jobs were for the disabled, and 41 were for people from rural areas. Out of the total of 183 persons that benefited from the scheme 94 were women and 89 were men, 21 people were from the age group 15-24, 16 from the age group 50-64, 29 persons were long-term unemployed, 5 were disabled and 51 were from rural areas. The average loan was for PLN 41 900 (EUR 10 475), compared to the initial estimates of individual final recipient financing needs of PLN 25 000 (EUR 4 250). Over 92% of loans were provided for the maximum repayment period of five years.

Loans for investment purposes were only 9% of the total disbursed amount, or PLN 0.6 million (EUR 0.15 million), while 90% of all disbursed funds were for loans combining investment and working capital, PLN 5.8 million (EUR 1.45 million). From total investments, 43% of the amount borrowed or PLN 2.83 million (EUR 0.70 million) was for the service sector, 44% for trade, 8% for manufacturing and 5% for construction.

The job creation process under the scheme was a clear achievement not only in terms of its final output but also considering its pattern – a stable delivery of 40-60 jobs annually, i.e. at the end of 2013 there were 60 jobs created, at the end of 2014 – 100, and at the end of 2015 – 151.

The financial instrument's long-term impact should be more extensively evaluated after the end of the project. The success or failure of the start-ups will depend on the attitude, commitment and entrepreneurship skills of the final recipients. However, the revolving support is believed to help unemployed and inactive target groups get acquainted with market mechanisms and develop skills useful in later phases of their activity. By encouraging final recipients to take action and responsibility for their own decisions and their financial future, the scheme is considered to have helped to change the mentality and increase the capacity within the target group. Final recipients also build a credit history, which can improve their access to finance for future business development.

4.2 Achievements

The pilot nature of the instrument means the main achievement is its **effective implementation**. The scheme enjoyed considerable demand from the target group, as shown by the number of final recipients, the loans provided and the jobs created. The commitment and experience of the financial intermediary helped reach a large number of potential final recipients, as well as more generally promote the idea that loans can be a viable form of public support. The managing authority can reuse repaid funds for future labour market and social policy interventions.

An important achievement is the **high sustainability of the investments**. The non-financial support helped final recipients to get acquainted with the principles of entrepreneurship, as well as formalities related to business activity registration and administrative requirements. This was of particular importance as the project is directed at people who often had neither the necessary business knowledge nor any experience. The support package also required thoughtful planning, as loan contracts were signed only if the applicant's business plan did not raise any doubts in terms of viability. Due to the careful assessment process, only five investments have defaulted.

4.3 Challenges

The **legal and procedural framework** of Structural Funds regulations and the related managing authority guidance seemed more appropriate for grants than for financial instruments. Particularly during the early stages of implementation, financial intermediaries were confused with some regulatory provisions that required a different approach than their normal lending activities, and the lack of others. However, many technical issues were solved with the help of the steering committee.

Another challenge involved the **assumptions about the average loan amount**. It turned out that the individual final recipient financing needs were almost twice the initial estimate. Consequently, the fund's budget may be too small to support the number of final recipients expected at the beginning. Still the **maximum loan** of PLN 50 000 (or EUR 12 500) proved not to be suitable for manufacturing activities and limited the potential to the services and trade sectors.

Lastly, **inadequate coordination** created competition between the different funding sources, especially public grants and financial instruments. The different institutions involved tended to only promote the support they could offer. This required more intensive marketing efforts from SRCP.

'Pronto' Restaurant: Achievements

Thanks to the financial instrument's support, it was possible to create two new jobs and a place for eating and gathering for the local community. First job was created instantly after the business set up and the second during the first operational year. The quality of the business is confirmed by positive feedback from customers and the gradual increase in the number of new customers, as well as in sales and profit.

Recently, demand has exceeded the current capacity in terms of space and staff available. Andrzej Snopek is now looking for larger premises and is planning to apply for EU funding to develop the business and introduce new technology. He is also looking for domestic Labour Office financing to create new jobs.

5 Lessons learned and outlook

The experience gained will be used under the 2014-2020 ESIF OPs. Similar financial instruments will be proposed under the new generation of ESF and ERDF funded regional OPs, possibly in combination with interest subsidies. Moreover, the positive implications of this and other schemes have spurred interest in other financial products. Under the country-wide ESF OP Knowledge Education Development 2014-2020, addressing reform and systemic change in employment, social inclusion, education and good governance, the managing authority has proposed additional ESF-funded financial instruments to provide guarantees and venture capital for the social economy.

www.fi-compass.eu
contact@fi-compass.eu

European Commission
DG Employment, Social Affairs & Inclusion
B-1049 Brussels
BELGIUM

European Investment Bank
Advisory Services *fi-compass*
98-100, boulevard Konrad Adenauer
L-2950 Luxembourg