

Opinion of the European Economic and Social Committee on the 'Proposal for a Decision of the European Parliament and of the Council establishing a European Microfinance Facility for Employment and Social Inclusion (Progress Microfinance Facility)'

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Rapporteur-general: **Ms Gabriele BISCHOFF**

On 17 July 2009 the Council of the European Union decided to consult the European Economic and Social Committee, under Article 152 of the Treaty establishing the European Community, on the

'Proposal for a Decision of the European Parliament and of the Council establishing a European Microfinance Facility for Employment and Social Inclusion (Progress Microfinance Facility)'

On 14 July 2009 the Committee Bureau instructed the Section for the Single Market, Production and Consumption to prepare the Committee's work on the subject.

In accordance with Rule 20 of the Rules of Procedure, the European Economic and Social Committee appointed Ms Gabriele BISCHOFF as rapporteur-general at its 456th plenary session, held on 30 September and 1 October 2009 (meeting of 1 October 2009), and adopted the following opinion by 171 votes to none, with 2 abstentions.

1. Summary of the EESC's conclusions and recommendations

1.1 Appropriate finance facilities for businesses are a key prerequisite for economic growth, not least for micro-enterprises in the social economy. The development of micro-credit is therefore to be welcomed, given that it could represent a new way of fostering the entrepreneurial spirit and of creating new jobs in micro-enterprises (enterprises employed less than ten people, with an annual turnover or balance sheet total not exceeding EUR 2 million). This takes account of the fact that there are, to date, only limited microfinance facilities available in Europe.

1.2 Providing micro-credit to micro-enterprises in the social economy and to disadvantaged groups is much more complex and expensive than providing conventional credit, but this additional expense can be reduced, firstly, by developing standardised high-tech services, marketing micro-finance services more effectively and making them generally more professional, and secondly by means of guarantees and co-financing. One of the key purposes of the proposed microfinance facility will thus be to develop the tools for microfinance services, including in cooperation with existing financial service providers. This will involve developing organisational structures that allow the standardised processing of large numbers of applications; without appropriate software and the use of web-based technologies, it will not be possible to achieve the highest possible level of professionalism.1.2.1 In addition, previous experience in Europe with the issuing of micro-credit has demonstrated that market incentives also need to be provided in order to ensure that the financial sector does actually carry out the duty assigned to it: that of providing micro-credit to the two specific target groups.

1.3 Disadvantaged persons setting up businesses should be given greater access to microfinance services not only when first starting up, but also for the first few years of operation.

1.4 Approximately 1 % of the funds in the Progress microfinance facility are earmarked for administrative expenditure, not including the funds provided to pass-through banks and microfinance institutions for them to pass on to the target groups. The Committee is keen to find out what proportion of the funds are granted to pass-through banks and microfinance institutions so that they can provide this credit. Steps must also be taken, for example by means of regular monitoring at European level and by publishing the credit conditions on the website of the competent supervisory authority, to ensure that the banks are in fact passing the favourable interest rates on to the target groups.

1.5 The impact on employment and social policy that the establishment of a European microfinance facility aims to achieve should be evaluated precisely, differentiating between the target groups. The two target groups – micro-enterprises in the social economy and individual applicants (unemployed, young or socially disadvantaged people) – need different consultancy and support capacities, which also need to be taken into consideration in organisational terms, bearing in mind the intersections with other relevant programmes.

1.6 Finally, the EESC recommends looking into what other sources of financing – apart from Progress – are available and could fund the new microfinance facility.

2. Introduction and summary of the Commission proposal

2.1 In its communication of 13 November 2007 on a European initiative for the development of micro-credit in support of growth and employment [COM(2007) 708], the Commission suggests, firstly, improving the legal and institutional frameworks in the Member States and, secondly, establishing a new facility to support the creation and development of micro-credit institutions in the Community⁽¹⁾. Additional funding should also be provided for new non-bank microfinance institutions⁽²⁾. The Commission communication states that the development of a structure for issuing micro-credit could play an important role in the realisation of the Lisbon strategy for growth and jobs⁽³⁾.

2.2 Commission Recommendation 2003/361/EC of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises⁽⁴⁾ defines 'micro-credit' as loans under EUR 25 000 and 'micro-enterprise' as an enterprise which employs fewer than 10 persons (including self-employment) and whose annual turnover and/or annual balance sheet does not exceed EUR 2 million.

2.3 The expert group report on the regulation of micro-credit in Europe highlights the extent of the differences between the Member States in the provision of micro-credit and in their legal frameworks.

2.4 The Commission has already, in its communication of 3 June 2009⁽⁵⁾, announced a new EU microfinance facility for employment (Progress Microfinance Facility).

2.5 The Commission proposal of 2 July 2009 on establishing a European Microfinance Facility for Employment and Social Inclusion⁽⁶⁾ aims, in view of the economic and financial crisis and the ensuing impact on employment levels and the availability of credit, to create a new EU microfinance facility to assist (potentially) unemployed people and disadvantaged groups to establish micro-enterprises or become self-employed by providing micro-credit of up to EUR 25 000, along with guarantees, equity instruments, debt instruments, and other measures such as communication activities, monitoring, control, audit and evaluation. Support can also be provided for micro-enterprises in the social economy that provide work for unemployed and disadvantaged people. The aim of this is to pave the way for the unemployed and other disadvantaged groups to become entrepreneurs. The reallocation of EUR 100 million from the current Progress budget, which could leverage more than EUR 500 million in total, could benefit up to 45 000 people and businesses over the four years from 2010 to 2013, with an estimated average loan of EUR 11 000. This will be administered by the Commission in cooperation with international financial institutions such as the European

Investment Bank (EIB) and the European Investment Fund (EIF); there will be no additional administrative burden for the Member States.

3. General comments

3.1 The EESC welcomes the fact that the Commission's proposals concerning the establishment of a microfinance facility show that it is committed to job creation and that it wants to help to promote entrepreneurship among disadvantaged groups. Nonetheless, it should be noted that there has, to date, been comparatively little experience in the use of microfinance facilities in Europe and that an extraordinary amount of imagination will be required in order both to safeguard the administrative management of micro-credit and other resources and to ensure that this facility remains practicable in the long term. In view of the impressive successes achieved by microfinance services in the field of development cooperation (for which Grameen Bank and its founder, Muhammad Yunus, were awarded the Nobel Peace Prize in 2006), it is worth emphasising both the opportunities and the challenges involved in translating this experience to the European context, not least because some of the essential advantages of the original concept (such as integration in a local, professional or ethnic community, which engenders trust and thus reduces monitoring costs and defaulting) are lost in the process of this translation. The extent to which this experience can be applied to more developed countries is therefore disputed.

3.2 In Europe, too, there is a real need for microfinance services: only around half of smaller enterprises have a generally positive attitude towards the role of banks in terms of access to credit⁽⁷⁾. The Jeremie programme (Joint European Resources for Micro to Medium Enterprises), which is primarily funded from the Structural Fund, is a joint initiative of the DG Regio and the EIB Group to support and improve financing for micro-enterprises and SMEs⁽⁸⁾.

3.2.1 In addition, the European Commission has launched significant initiatives – in the form of the CIP framework programme (Competitiveness and Innovation Framework Programme)⁽⁹⁾ and the Jasmine (Joint Action to Support Microfinance Institutions in Europe) pilot initiative, which is intended, *inter alia*, to support the consolidation and development of non-bank microfinance institutions⁽¹⁰⁾ – to improve the capital position of SMEs and micro-enterprises. The Committee recommends that these various measures should be better coordinated with each other. In its opinion⁽¹¹⁾ on Jeremie back in 2006, the Committee made it clear that it had always supported Commission initiatives to facilitate access to credit for micro-enterprises and SMEs and therefore called for the broad-based involvement of the social partners.

⁽¹⁾ See COM(2007) 708, p. 2

⁽²⁾ See *ibid.*, p. 11

⁽³⁾ See *ibid.*, p. 2

⁽⁴⁾ OJ L 124 of 20.5.2003, p. 36.

⁽⁵⁾ COM(2009) 257, 3.6.2009

⁽⁶⁾ COM(2009) 333.

⁽⁷⁾ See Eurobarometer (2005): SME Access to Finance, Flash Eurobarometer 174.

⁽⁸⁾ See COM(2006) 349, p. 9

⁽⁹⁾ See COM(2005) 121, p. 6

⁽¹⁰⁾ See COM(2007) 708, p. 3

⁽¹¹⁾ OJ C 110, 9.5.2006

3.2.2 The Committee also stated that EIB funds, where they had been used, had proved to be a useful tool in facilitating access to credit for micro and small businesses.

3.2.3 In that opinion, the Committee also noted that access to micro-credit should be facilitated particularly for SMEs and that there must also be outreach to specific groups such as young or female entrepreneurs, or those from disadvantaged groups, including ethnic minorities.

3.3 The opportunities presented by the use of microfinance services arise from the key importance to, for example, business start-ups of forms of financing that are as informal and quick as possible. The great majority of the funding needed for business start-ups is provided by the founder of the business or by relatives, friends and neighbours⁽¹⁾, which points to the limitations of normal bank loans: the smaller the amount requested, the higher the rejection rate, because it is too time-consuming to assess the applications carefully. Microfinance services can bridge the gap between informal funding streams (which are limited in their efficiency) and bank financing. If micro-credit and other microfinance services can be judged to be as quick, straightforward and flexible as informal funding sources can be, micro-credit will be able to make a key contribution to a dynamic economy and entrepreneurship.

3.4 People in the target groups setting up businesses need to have access to microfinance services not only when they are first starting up but also for the first few years afterwards, because they are to a large extent dependent on small lump-sums to fund their projects.

3.5 Regardless of the current economic and financial crisis, providing micro-credit is much more complex and expensive than providing conventional credit, because the sums lent are comparatively small, the collateral customary to banks is usually not provided and the handling costs are very high. A high caseload, an appropriate organisational structure and suitable technology, and in general the highest possible degree of professionalism, are therefore vital to the success of microfinance initiatives. It is essential that any experience gained with similar initiatives and programmes (CIP, Jeremie, EIB pilot, Jasmine) should be taken into consideration right from the start.

3.6 In view of the level of professionalism required, it will be necessary, first of all, to operate micro-credit as far as possible on a standardised retail banking model, in order to benefit from economies of scale and advantages in the distribution of risks. Such high customer numbers are an ambitious target, as experience in the UK and Canada has shown⁽²⁾. This demonstrates the importance of a high level of awareness (due, for example, to advertising campaigns such as the French organisation ADIE's 'micro-credit weeks') and the need for easy access

(e.g. on the Internet). We need to establish whether, and if so how, this can be achieved, and what role other programmes (such as the ESF) can play (technical support); the intersections with these programmes and initiatives also need to be set out, for the sake of consistency.

3.7 With regard to the set-up of the business processes, it is also important to establish the organisational structure for the envisaged retail banking system so that applications can be dealt with quickly and flexibly, with appropriate forms of security, and in order to use standardised penalties and forms of risk distribution in the case of breaches of contract (delayed payments). There is thus also the issue, as with consumer credit, of how to assess customers' credit ratings as easily, quickly and reliably as possible.

3.8 Thirdly, one of the technical requirements for this kind of retail banking system is a fully developed software system for initiating, concluding and monitoring loan agreements, which could deal with the balancing act between standardised retail banking and the individual handling of applications, and help to open up the microfinance market segment.

3.9 Both micro-enterprises in the social economy and individuals in Member States and regions where separate micro-credit institutions have already been set up may find it quicker and easier to get access to funds than applicants in countries and regions where such institutions do not exist or are still being developed. The EESC recommends that the programme should ensure that this does not lead, in general, to inequalities in access.

3.10 One key question is whether loans should be provided by conventional credit institutions or by separate microfinance institutions that may need to be set up specially, and which are usually very small and not run for profit. On the one hand, a network of microfinance service providers has been developing in Europe over the past few years, with support from the Commission, although only a fifth of these service providers (less than 20) issue more than 400 micro-loans a year⁽³⁾. On the other hand, it will be almost impossible to extend microfinance services without high-quality, professional, profit-oriented management – and in this respect the banks (which already issue the majority of micro-credit) have a big advantage. It does not seem wise to distribute resources solely through small microfinance service providers operating in the public interest that concentrate on people without a fixed income, women, young people, the elderly and migrants: this kind of 'niche' banking system would institutionalise the marginalisation of these groups in yet another field. Therefore, in order to ensure that the banking sector does take on micro-credit despite the fact that the returns are expected to be small, there will probably be a need for additional market incentives or subsidies for the development of the necessary infrastructure.

⁽¹⁾ See <http://www.gemconsortium.org/download.asp?fid=608>

⁽²⁾ See <http://ssrn.com/abstract=976211>

⁽³⁾ With regard to microfinance in the EU, see www.nantiklum.org/Overview_final_web.pdf and www.european-microfinance.org/data/file/Librairy/ISSUE%20PAPER.pdf

3.11 As the microfinance initiative quite explicitly aims to have an impact on employment and social policy, it is crucial for the programme's effectiveness also to be evaluated in this respect, with a distinction being drawn between the two target groups (micro-enterprises in the social economy and disadvantaged individuals). To date, the only criteria to be taken into consideration have been credit volume and the number of beneficiaries, but the EESC recommends also quantifying integration in the mainstream labour market, the income achieved, and indirect additional employment effects for the various groups mentioned in the Commission communication. This is the only way of showing the success of the initiative from these perspectives ⁽¹⁾.

3.12 One positive point worth emphasising is that the Commission's proposal also envisages support measures, such as communication activities, monitoring, control, audit and evaluation (Article 4(1)); however, it remains uncertain whether this would primarily involve support for the people

starting businesses or for the microfinance institutions, how this would be organised and how the overall funding pot would be distributed between guarantees, equity instruments, debt instruments and support measures.

3.13 The EESC recommends ensuring that the reduced interest rates are passed on to borrowers. It would also be worth establishing what proportion of the resources should flow through to pass-through banks and microfinance institutions to pay for administration.

3.14 As stated in opinion INT/495, the EESC supports the initiative to create a new microfinance facility for the target groups, but has some doubts as to whether it is sensible or practical to fund that new microfinance facility by cutting funding for Progress. It therefore recommends looking into what other sources of financing – apart from Progress – are available and could fund the programme.

Brussels, 1 October 2009.

The President
of the European Economic and Social Committee
Mario SEPI

⁽¹⁾ For a procedure of this kind, see <ftp://repec.iza.org/RePEc/Discussionpaper/dp3220.pdf>