PERSPECTIVES

50

March 2006

MICROCREDIT IN EUROPE: THE EXPERIENCE OF THE SAVINGS BANKS

WORLD SAVINGS BANKS INSTITUTE

EUROPEAN SAVINGS BANKS GROUP

MICROCREDIT IN EUROPE: THE EXPERIENCE OF THE SAVINGS BANKS

Table of Contents

This paper was written by Malcolm McDowell, Economic Adviser, with input from Hector Calvo Andres, Adviser, Hughes Kamewe, Financial Sector Development Adviser and the help and contributions of WSBI/ESBG members, notably from the Economic Affairs Committee.

FOREWORD

The concept of microcredit has become familiar to more and more people, the initiative of the United Nations to make the year 2005 International Year of Microcredit having greatly contributed to this.

This paper points to the role of microcredit as an economically viable solution to fight against financial exclusion in Europe, the focus of this study.

Europe's savings banks, united in the European Savings Banks Group, are intimately connected with the provision of savings and other basic financial services to the largest number. Indeed, the original objective of the savings banks was to allow the social advancement of the lower classes by giving them the opportunity to be an active part of the financial system. The savings banks have gone a long way since, and have become modern and profitable financial institutions. But today as at the beginning of their history, savings banks believe that empowerment of the financially excluded is a means not only of alleviating poverty, but also of contributing to job creation and sustainable economic growth.

The current paper "*Microcredit in Europe, the experience of the savings banks*" will provide valuable information on the activities, as well as the views, of European savings banks in the field of microcredit.

Chris De Noose
Chairman of the Management Committee, ESBG

INTRODUCTION

The decision by the United Nations to make 2005 the year of microcredit has very much helped to bring the topic in the spotlight. The result has been clearly favourable at the level of the media: features on microcredit schemes, both in the developing and the developed world, currently appear regularly in the pages of national newspapers.

In the European Union (EU), the importance of microcredit was officially recognised in 2000, when the Council adopted the *European Multiannual Programme (MAP) for Enterprise and Entrepreneurship, in particular SMEs (2001-2005)*, which included the creation of a microcredit window. This was further emphasised in 2003, when the European Council urged Member States to pay special attention to microcredit to encourage the creation of small enterprises.

In this context, Enterprise Directorate General of the European Commission (EC) published a report entitled "*Microcredit for small businesses and business creation: bridging a market gap*" in late 2003, following which it organised a conference on microcredit in Europe in 2004. Practitioners of microloans and policy-makers were invited to the conference to discuss means of facilitating microcredit in Europe.

The Commission's efforts have served to highlight the importance of and need for microcredit not only in developing countries but also in the developed world. By focussing the definition of microcredit as small loans to micro-enterprises, moreover, the Commission has linked the issue closely to SME finance, and the need to improve the access to finance of the 90% of EU enterprises that are either small or medium-sized enterprises, and therefore represent the backbone of the European economy.

While the main emphasis of the Commission study is on the provision of small loans to SMEs, it also highlights microcredit as a means to reduce unemployment as well as tackle the problem of financial exclusion in Europe, which affects 10% of Europeans.

The aim of this paper is to clarify the important work of Europe's savings banks in microcredit via a number of key case-studies, as well as to respond to the Commission in its efforts to facilitate the provision of microcredit in Europe.

It first underlines the importance of seeing microcredit as a means of facilitating access to finance and fighting financial exclusion and then explains the similarities behind the concept of microcredit and the origins of the savings banks.

It then highlights the work of the savings banks in the provision of microcredit as well as microfinance[1] support activities. This adds some detail to the Commission's paper, which recognised the importance of the work of savings banks in these areas.

The final section then responds directly to a number of questions and suggestions put forward by the Commission in its publication on microcredit and at its conference, putting forward a number of recommendations for its attention.

1 Microfinance, as defined jointly by the International Monetary Fund, the World Bank and the United Nations, is the provision of financial services such as credit, savings, and insurance to poorer individuals or communities which are often unserved or under served by traditional financing institutions.

1. THE NEED FOR AND IMPORTANCE OF MICROCREDIT IN EUROPE

A. Microcredit as an economic enabler

Stories abound in the news today on the many successful microcredit schemes in place in the world's developing countries.

The success of banks and other financial institutions in extending small loans to the poor with no collateral has not been a result of making available innovative financial products tailor-designed for such people, but rather because the activity represents an economically viable solution to providing the enterprising poor a means to a self-dependent, sustainable livelihood.

In theory, the drawback to the credit institution of providing credit to the poor is that the risk and the cost of lending are too large to make it worthwhile. With no collateral to fall back on, and, in very underdeveloped countries, no formal legal means of securing pay-back, the risk of default would normally be too high to make it profitable for financial institutions to provide loans to such individuals.

In practice, as the various successful schemes in developing countries have proved, things work out very differently. Even the very poor can be relied upon to pay back their loans. In fact, and not surprisingly, the success of microcredit in developing countries has proved that it is not the lack of will that explains why the poor remain poor, it is the lack of opportunity. Once they are given the opportunity, or the economic enablement, the poor can be counted upon to participate sustainably in the economy in which they have become active.

B. Microcredit as one of the solutions to the problem of access to finance in both the developing and the developed world

One way of explaining the lack of economic enablement or opportunity in both developing and developed countries is in terms of lack of access to finance. In turn, microcredit is one solution to the problem of access to finance.

The problem of access to finance in developing countries can be viewed as quite a different problem to that in the developed world. This is true if we compare the developed world to very underdeveloped countries. In the latter, the structures are often not in place i.e: financial institutions may not exist, or only exist in urban areas in countries where the majority of the population is rurally based. Formal legal structures may not even exist as a means of enforcing repayment. In this sense therefore we are talking about lack of access to finance at the most basic level.

The problem of access to finance in more advanced developing countries and developed countries is however not that different. In such countries where the institutions are in place, where geographical proximity exists between banks and customers and where the formal legal structures are in place, another kind of problem of access to finance exists. It is that of financial exclusion.

Financial exclusion exists in both advanced developing countries and in developed countries because of the perceptions by certain financial institutions that the poor are not economically viable. Credit is not extended to such people because the risks to the institution are deemed to be too high due to the lack of collateral and the perceived large rates of default.

Also, given that transacting loans involves a certain amount of fixed costs, the lower the amount of the loan, the less profitable the loan to the lender. Given that loans to the poor are small loans, this acts as an extra deterrent to accept them as clients.

C. Improving access to remedy financial exclusion by extending microcredits

Thus, if microcredit, or the extension of small loans, is a means of giving the poor economic enablement, it is also a solution to the problem of access to finance and a means of tackling financial exclusion. Realising that all these issues are inextricably linked is to appreciate the significance of the impact that the provision of small loans can have on a society and its economy.

In modern, market based economies, financial exclusion amounts to the prevention of economic empowerment.

At a time when discussions in Europe are focussed on ways to promote economic growth, and paying heed to the Commission's announcement of focussing the next five years on the dual goals of economic growth and job creation, the Commission should see the extension and popularisation of microcredit schemes in Europe as a means of bringing the 10% or so of the European population that are financially excluded 'closer to finance' in order to give such people economic empowerment and thereby contribute both to economic growth and job creation.

Seeing the problem of microcredit in Europe in such a light also helps to highlight the potential behind the provision of microloans: **in a dynamic world of growing economic opportunities, the excluded of today are the economically enabled (and the customers) of tomorrow.**

The link of microcredit to the issue of financial exclusion is also a means of putting the spotlight on another aspect of the problem which it represents. The greater the number of people that are kept out of the financial system, the greater the growth of illegal, unregulated, informal credit providers contributing to the development of a black market for financial products which ultimately risks threatening the development of the European economy. Much has been said lately about how such illegal providers are contributing to the problem of over-indebtedness in Europe.

D. Microcredit and savings banks

The core belief behind the activities of specialist microcredit institutions, that the poor could be counted upon to contribute economically in a sustainable and independent manner once they are given the opportunity to do so, is not new, and nor was the application of microcredit schemes in developing countries the first substantiation of that belief. Indeed the original '*raison d'être*' of the savings banks was to allow the social advancement of the lower classes by giving them the opportunity to be an active part of the financial system.

And the provision of microloans to the socially disadvantaged is also something which the savings banks have been intimately connected with for a number of years, along with the provision of savings and other basic financial services (activities which, along with loans are popularly known as 'microfinance' activities when they are targeted at the poor). As **the European Commission itself notes, savings banks, along with co-operative banks, remain the main traditional operators in the field of microcredit**[2].

E. Towards the savings banks' views on a definition of microcredit

While no formal definition of 'microcredit' exists, there are many interpretations, each dependent on what the interlocutor is wishing to focus on. At its most basic, the provision of microcredit is, as we have implied so far, the extension of micro sized loans to the poor.

In a European context, a more formal and specific definition of microcredit has been provided by the European Commission as being a loan not exceeding 25,000 Euro. The Commission has also focussed the context of the provision of such loans (as well as associated guarantee schemes) to new and existing micro-enterprises (between 0 to 9 employees), which could equally be small businesses or entrepreneurs[3]. These requirements form part of the eligibility criteria of the Microcredit Guarantee window operated by the European Investment Fund (EIF) on behalf of the European Commission, in the framework of the Multiannual Programme for Enterprise and Entrepreneurship (2001-2005).

2, 3 "Microcredit for small business and business creation: bridging a market gap", November 2003, European Commission

The focus of the European Commission is in line with the specific requests by the European Council in 2003 to make entrepreneurship a priority, and in particular for special attention to be paid to microcredit. The Council's request was driven by the expressed belief that Europe does not have enough entrepreneurs and that the founders of small businesses often have no adequate access to external finance.

Besides the specific eligibility criteria for the Microcredit Guarantee Window stated above, the European Commission opted to look in its 2003 report at a broader perspective, and to "take into account all business creators, including unemployed persons, as well as to partly cover, on the one hand, some substantial activities carried out by non-banks, in particular, by limited liability companies, and, on the other hand, to analyse the NGOs which deliver microcredit programmes primarily from a social inclusion perspective"[4].

The EC has very much in mind the plight of the unemployed for self-financing and says as much, identifying "a growing trend towards the creation of one-person self-employed businesses, particularly by unemployed persons", and seeing microloans as being "particularly useful to promote self-employment and the creation of small businesses in the services sector, where access to credit is often difficult".

In the EC paper on microcredit, the following technical distinction between micro-lending and conventional bank lending is offered, thereby offering further insight on the EC's understanding of the concept of microcredit:

- Credit assessment methods used in microfinance focus more on the borrower and the likely impact of their business on their community than on the business plan.
- Microfinance providers generally attempt to reduce or avoid the need for collateral.
- Step lending techniques, in which larger follow-up loans are provided if the initial loan is successfully repaid, reduce risk and transaction costs.
- The maturity period is normally short and the interest rate often relatively high compared to traditional bank loans.

4 "Microcredit for small business and business creation: bridging a market gap", November 2003, European Commission

Further, it adds that it does not include personal or consumer loans, despite the fact that often operations registered as personal loans are in fact microloans to micro-enterprises and self-employed entrepreneurs, adding that in general, as the majority of microcredit borrowers are self-employed entrepreneurs, it remains difficult to distinguish whether the loan awarded qualifies as a microloan to the micro-enterprise or a personal loan.

The European Savings Banks Group welcomes the European Commission approach in using a broad definition for microcredit. Given the diversity of microcredit practices across countries, trying to establish a more specific definition may not contribute to the ultimate goal of the debate, which is to foster and facilitate the provision of small loans. A broad definition further allows a number of support activities provided by European savings banks within the context of their efforts to improve access to finance to be taken into consideration. We report on a number of these activities in the next section of this report.

ESBG members are however less supportive of the choice of the Commission's threshold of 25,000 Euro and below used to categorise loans as microcredits. While the ESBG acknowledges the need to establish clear criteria for the European Investment Fund to operate the Microcredit Guarantee window, with regards to defining microcredits, the experience of the ESBG members is that a number of loans which they provide and themselves consider to be small loans are in fact superior to 25,000 Euro in value. For this reason, ESBG reserves judgment on what the exact threshold should be for a loan to be regarded as a microcredit, believing, as expressed in the previous paragraph, that preciseness in definition is perhaps less important than practice. For this reason too, the activities of ESBG members reported in the next section within the context of what they themselves regard as relevant to the topic of microcredit, is not limited in terms of value.

However in the context of the EIF's criteria, ESBG members would urge the Commission to assess whether the 25,000 Euro threshold of the microcredit guarantee facility is adequate.

The ESBG would also like to express some reservation on the above outlined distinction between conventional and microcredit loan methods, believing it to be too strict and in any case not relevant to an important proportion of the small loans granted by ESBG members. It should be furthermore noted that this distinction between conventional and microcredit loans is much stricter than the broad definition of microcredit provided by the European Commission, and as such, not fully compatible with it.

The ESBG fully shares the view that the provision of consumer loans should not be regarded as microcredit. Notwithstanding this, the small loans which are granted to persons under the risk of social exclusion for them to satisfy basic needs should be regarded as microcredit. Such loans are not merely consumer loans since they are crucial in allowing persons which are under the risk of social exclusion to engage in an economic activity.

2. MICROCREDIT SCHEMES OF THE EUROPEAN SAVINGS BANKS

This section describes the involvement of European savings banks in microcredit operations with a number of case studies (Bulgarian Post Bank, German savings banks group, French savings banks group, Spanish savings banks, Lloyds TSB in the UK and Romania Banc Post). These experiences vary in size, targets and maturity. The descriptions are grouped in three main business models (the balance sheet-based model, the off balance sheet-based or foundation-based model and the agency-based model).

A. Balance sheet-based model

This model is characterised by the existence of a typical commercial relationship between the savings bank and the beneficiaries of micro-credit. Regardless of possible special features (e.g., a subsidised component) the scheme is operated by the savings bank as part of its regular lending activities. Profits or losses that result from micro lending activities are consolidated within financial statements in this model.

Among European savings banks, there are several examples of significant scale balance sheet-based micro lending programmes. An example is found in small loans released under the small businesses lending window at Post Bank (Bulgaria). Other examples are some small-scale activities carried out by the German savings banks (in partnership with the KFW[5] and the EIF), the Bank of Valletta in Malta (in partnership with the EIF), BBK Solidario (Spain) an affiliate of Bilbao Bizkaia Kutxa and Lloyds TSB in the UK (in the framework of the Small Firms Loans Guarantee Scheme).

5 Founded in 1948, KfW is today the promotional bank of the Federal Republic of Germany dedicated to SME financing. KfW is owned by the Federal Republic of Germany (80%) and by the federal states (*Länder*) (20%).

Case study 1: small business loans at Bulgaria Post Bank

Post Bank provides tailored financial solutions to small and medium sized enterprises. The bank has developed a "Small Business Lending Department" which offers different credit products for trade, services and manufacture business. Following this approach Post Bank supports 'credit-worthiness' activities with a minimum six months business history, annual sales turnover lower than 513,000 Euro (1 million Bulgarian Lev - BGN) and registered under the commercial code of the country. It offers products with flexible maturities, options for different collaterals, appropriate interest rates and various credit schemes such as the following:

"Practice Scheme"

Specially designed to address working capital needs "Practice" was developed for those small companies whose business usually is not routed through bank accounts. The loan amount offered ranges between 7,700 Euro and 128,000 Euro (15,000 – 250,000 BGN) for a repayment period up to 24 months and interest rates of 11.5% to 12.5%.

"Discounting Scheme"

The "Discounting loan" has been developed for small companies which run their activity as distributors of bigger companies. Conditions are almost the same as the "Practice Scheme", the loan amount offered ranges from 7,700 Euro to 128,000 Euro, but the repayment rate is shorter, 12 months only.

"Progress Scheme"

This credit line is designed to finance long-term investments, namely the purchase of equipments and installations (offices, storehouses, etc.) by small companies but also to micro-companies with a maximum of ten employees. This scheme allows a maximum loan amount of 20,500 Euro (40,000 BGN) for interest rates of 12.5% to13.5%.

Besides these credit schemes, the Bulgarian Post Bank offers other advantages for small companies:

- Automatic revolving of the existing credit schemes
- Automatic pre-approval of the Practice Scheme for existing customers of Post Bank
- Grace periods of up to 8 months for investment and equipment loans
- Flexible combined collateral

Post Bank has been successful in helping many small firms to develop their activities and increasing the bank's small business loan portfolio. It has a broad network of 29 branches and 89 offices and is present in 2,300 post offices.

Case-study 2: the micro-lending experiences of the German savings banks

In Germany, savings banks have strong connections with the SME sector broadly and the craft industry in particular. According to estimates, savings banks in Germany account for nearly 43% of loans to SMEs (2005) and this market share is as high as 70% for small businesses with a turnover below 500,000 Euro.

Close to 75% of SMEs have a banking relationship with a member institution of the "*Sparkassen Finanzgruppe*" and almost 60% of SMEs have their local savings bank as main banking partner or "*Hausbank*".

Nearly 50% of DtA[6] loans were dispatched through the savings bank group for a cumulative amount of 2.4 billion Euro (2002). "*Startgeld*" is a seed money programme launched in 1998 by DtA and now operated by the KFW Group. It allows lending of up to 50,000 Euro with the risk being shared between the DtA/KFW (40%), the European Investment Fund (40%) and the lending bank (20%). According to a report released by the European Commission "*In 2002,….. between the Hausbanken involved in DtA programmes targeting start-ups, 60% are savings banks (+ 8.3% over the last five years)*"[7]. Evidence from this DtA programme substantiates the involvement of German savings banks in microcredit activities. The risk incurred by a savings bank under this programme may reach 10,000 Euro per loan. Although all business start-ups are eligible to "*Startgeld*" a particular development has been the larger proportion of women entrepreneurs (60%) who received a loan.

"*Micro-Darlehen*" is also a microloan scheme launched by DtA in 1999 and since the merger administered by the KFW and co-guarantee by the EIF in the framework of the Multiannual Programme. KFW operates through partner banks, savings banks inclusive. Eligibility for this scheme includes individuals, especially unemployed people, people from minority groups (foreigners and migrants), micro-enterprises and independent professionals with less than 10 employees. The money can cover up to 100% of the total costs of the projects. The scheme allows borrowing up to 25,000 Euro but KFW releases the on-lending credit institution from 80% of its liability (of which 40% is co-guaranteed by the EIF).

6 The Deutsche Ausgleichsbank (DtA) – which previously existed as a separate state owned banking organisation to provide SME and start up finance - has now been absorbed into the KfW banking group.

7 "Microcredit for small business and business creation: bridging a market gap", November 2003, European Commission.

In addition to their involvement in DtA/KFW programmes, a number of German savings banks engage in micro lending activities. Given the decentralised structure of German savings banks (460 local institutions and 11 regional banks), these are in general local initiatives.

"*S-Startkapital*" is an example of a microcredit scheme developed by the savings bank of Bonn to provide start-up loans in support of the creation of innovative companies. The scheme was introduced in October 1996 to promote the structural development of the city of Bonn following the decision to transfer the activities of the Federal Government to Berlin. "*S-Startkapital*" aims at closing the gap between DtA/KFW programmes and other start-up loans offered at that time by the savings bank of Bonn. The scheme allowed any innovative start-up promoter to borrow up to a minimum of 10,000 Deutsche Mark (around 5,000 Euro) and a maximum of 100,000 Deutsche Mark (around 50,000 Euro), with the condition that the loan should not exceed 25% of the project costs. Under this scheme, money is repayable over 12 years, no collateral is required and no interest is due over the first four years.

Case-study 3: the microcredit experiences of the French savings banks

In 1999, the French savings banks reform Act passed in France recognised and included in the new statutes the long-standing initiatives of the French savings banks to promote self-reliance by allowing them to develop activities in the field of commitment to society. French savings banks now finance specific initiatives, known as "PELS" (or LSEP in English: Local and Social Economy Projects) which are local social projects to combat social exclusion. In the framework of the PELS projects, the French savings banks allocate microcredits to people that encounter difficulties in setting-up their own businesses (such as the long-term unemployed and the disabled). Evidence reveals that allocated funds have allowed many unemployed people to set-up their own micro-enterprises.

The French Savings Banks Group has also developed partnerships with mentoring networks (such as France Active, Adie, France Initiative Réseau, Boutiques de Gestion). While the mentoring entities provide business support services in order to further assist micro-entrepreneurs get their projects off the ground, the French savings banks grant these entrepreneurs (helped by the mentoring networks), microcredits (on average 5,000 Euro per loan) and offer them a current account with a means of payment, thereby putting in place a basis to develop a long-term banking relationship.

Since 2001, over 50 million Euro of available funds went directly or indirectly to jobless people willing to set-up their own business (28 million Euro in terms of loans to micro-entrepreneurs and 22 million Euro to support microcredit institutions/business support services) and 6,000 (former financially excluded) entrepreneurs had access to microcredit.

The partnership in France between these mentoring networks and the savings banks has been a positive factor for the success of PELS. Evidence indicates that 75% of micro-enterprises financed within these schemes are still operational after three years. This compares favourably against statistics for the EU as a whole which reveal that some 30% of new enterprises do not survive more than 3 years after their creation and some 50% less than 5 years[8].

It is furthermore important to note that losses generated by microcredits granted by the French savings banks represent on average only 5% of outstanding loans. This is due not only to the lower rate of business failure (these rates are much lower when entrepreneurs are helped by mentoring organisations), but also to the guarantee facilities.

According to recent evaluations, out of the 6,000 entrepreneurs who had access to microcredit and business support services by the French Savings Banks Group, 5,000 permanent jobs were created. The long term implications of this activity should be also taken into account, since the objective is to have former financially excluded people become "included" and for these people to develop a normal commercial banking relationship with their savings bank.

Another commitment of the French savings banks to microcredit is in terms of the distribution of European Investment Bank funds as loans to small and micro enterprises. In September 2005, the French savings banks agreed to have 250 million Euro in funds made available as loans to such firms on attractive terms via their network.

8 "Microcredit for small business and business creation: bridging a market gap", November 2003, European Commission.

Case-study 4: the micro lending activities of Lloyds TSB

Lloyds TSB has undertaken various initiatives in the field of microfinance either as a direct provider of small loans to businesses start-ups or as a provider of capital on-lent to micro-enterprises. Beyond a philanthropic aim, this involvement in microfinance is commercially driven with the objective to develop business opportunities.

Lloyds TSB takes part in the "Small Firms Loans Guarantee Scheme". Backed by the British government and provided through the bank, it offers loans for start-ups or for small enterprises wishing to expand. The scheme is specially designed for those enterprises that cannot take advantage of conventional financial services due to their lack of guarantees or credit history. The loans are from £5,000 to £100,000 (7,500 Euro to 150,000 Euro).

The bank has over 575,000 small business customers and helps 100,000 business start ups every year, 60% of whom are one-person self-employed businesses. Most of its borrowing customers borrow less than 25,000 Euro and security is not in general required for amounts less than 15,000 Euro.

Lloyds TSB has also been involved in a wide range of projects on both a commercial and semi-commercial basis, providing capital for loan funds to business start-ups, micro-businesses and social enterprises. The creation of Community Development Venture Funds is one initiative sponsored by the government's Social Investment Taskforce to meet the needs of growth businesses unable to attract traditional capital to fund that growth. Since the creation of this task force Lloyds TSB has contributed to a wide range of programmes aiming at creating a favourable environment for the under-served community.

Recently Lloyds TSB provided a £1 million Loan Fund with the support of the Department of Trade and Industry's (DTI) Phoenix Fund[9]. The fund acts as lender of last resort, allowing people over 50 who are not in work and cannot raise finance from conventional sources, to set up a business.

9 The Phoenix Fund supports a number of activities designed to encourage entrepreneurship among disadvantaged communities by working through specialist intermediary organisations, including providing support to Community Development Finance Institutions (CDFIs). CDFIs provide finance and associated business support to enterprises from disadvantaged communities that are unable to access part or all of the finance they require from conventional sources but nevertheless have viable business propositions which, if supported, are likely to have a positive impact on the community in which they are based.

The Bridges Fund is another initiative where Lloyds TSB contributed. Initiated by the DTI's Phoenix Fund, it aims at raising £20 million (30 million Euro) from the private sector, including banks, pension funds and social entrepreneurs, to invest in established businesses run by entrepreneurs in under-invested communities in England. Lloyds TSB Scotland has committed £3 million (4.5 million Euro).

Finally, in the north of the UK, Social Investment Scotland (SIS) was launched in September 2001 as a £5 million (7.5 million Euro) partnership between Scotland's four biggest banks including Lloyds TSB Scotland, each providing £750,000 (1.19 million Euro) and the public sector giving the remaining £2 million (3 million Euro). SIS provides competitive loans to more-than-profit social enterprises and voluntary organisations, along with business support and advice.

B. Off balance sheet-based model

The second model applied by savings banks can be characterised as "off balance sheet-based", as profit and losses resulting from the microcredit operations are not consolidated in the bank's financial statements. Microcredit initiatives from various foundations belonging to Spanish savings banks can be grouped under this model.

Case-study 5: the microcredit initiatives of Spanish savings banks

Spain has a great tradition of social banking targeting under-served financially excluded communities. In addition to providing funds to promote social community development and cultural activities, some Spanish savings banks have undertaken micro lending activities through their foundations. This is the case for Caja de Granada, Caixa Galicia and Caixa Catalunya amongst others. These foundations are currently specialising in supporting local micro-entrepreneurs.

"*Fundación Un Sol Mon*" from Caixa Catalunya operates a microcredit programme, mainly in Catalonia. It gives support to income-generating activities for individuals and cooperatives that due to a lack of guarantee/ collateral do not have access to conventional finance. Applicants for a microcredit must have a business project or own a small company.

The projects presented must be economically feasible and respect the environment. The loans are aimed at financing the purchase of merchandise and new plant machineries or premises in order to help enterprises grow. From the beginning, almost 1,900,000 Euro has been released. For 2003, Fundación Un Sol Mon estimated that more than 550 jobs have been created through both individual and group microcredits.

Other foundations belonging to Caja de Granada and Caixa Galicia have similar microcredit programmes. Since 2002, Caixa Galicia started its micro-credit programme conceived to provide access to finance to self-employed people and those without guarantees unable to access conventional loans. The maximum loan amount is 12,000 Euro with an interest rate of 4% (lower than the market rate).

The three foundations mentioned above work with “support entities”, which manage microcredit applications. They are responsible for assisting potential entrepreneurs to define their activity, assess the viability of projects and, once the microcredit has been granted, provide technical advice and monitor the funded actions throughout the lifetime of the microcredit. They provide an accompanying role to the micro-entrepreneurs and are the intermediaries between the foundation and the final beneficiary.

C. Agency-based model

The third model operated by savings banks is based on an agency relationship with national or international financial institutions (e.g. European Bank for Reconstruction and Development (EBRD), the European Investment Bank, the European Investment Fund, KFW). These intermediaries work through local financial institutions, but the major difference here is that these intermediaries are 100% risk exempted. The credit policy is defined by fund providers and applied by the lending institution. However, in some cases like with the European Investment Fund, the lending institution is empowered with full responsibility for credit decisions.

Case-study 6: the microcredit experience of Banc Post in Romania[10]
Banc Post provides service to a wide range of customers through its 163 agencies operating in all districts in Romania. Moreover, a commercial agreement with the Romanian National Postal Service Company allows Banc Post to offer its products and services through more than 2,650 post offices enabling the access of a larger number of clients to the wide range of Banc Post products.

As a partner of small businesses, Banc Post is part of the EU/EBRD SME Programme dedicated to the candidate states for the European Union. Signed in May 2002 and amounting to 10 million Euro, EU/EBRD Facility for SME Financing aims to promote the development of small businesses by providing them access to finance. This scheme is targeted at new, rather than existing, customers of Banc Post. Main sectors covered are the manufacturing industry, the hotel industry, tourism, resources and environmental, construction and commerce. Part of the funds is devoted to micro and small-sized enterprises with no more than 20 employees in order to develop a microcredit window giving up to 30,000 Euro per credit line. The repayment period and the annual interest rate do not exceed respectively 4 years and 9%.

In the framework of an International Seminar in Bratislava (Slovakia), Banc Post has recently been granted the Award for "Best performance of a large bank taking part in the EU/EBRD programme for financing SMEs in EU candidate states" by the EBRD and the European Commission.

10 www.bancpost.ro/bpsite/produsul.jsp

3. POLICY RECOMMENDATIONS

The ESBG welcomes the focus of the Commission on microcredit, as it is a means to facilitate access to finance and therefore help in fighting financial exclusion. Furthermore, a number of microcredit schemes, including those of the savings banks, are focussed on giving unemployed entrepreneurs the means to establish their own business. In so doing, microcredit also contributes to reducing unemployment.

Savings and retail banks have a long standing tradition of providing finance to all parts of society. The types of products and services offered by ESBG members vary across Europe according to the needs and characteristics of the communities in which they operate, ranging from small loans to individuals without collateral to the most sophisticated support services designed to accompany SMEs in their growth.

Drawing from their experience in this area, ESBG members would like to propose the following recommendations for future policy measures:

A. Strengthening European and national partnership

The ESBG welcomes the microcredit guarantee facility under the *Multiannual Programme for enterprises and entrepreneurship (MAP)*, managed by the European Investment Fund on behalf of the European Commission, and supports its inclusion in the new *Competitiveness and Innovation Framework Programme (CIP) 2007-2013*. In line with the recommendation in the report on "*Microcredit for small businesses and business creation: bridging the market gap*", the ESBG agrees that the budget allocated to the SME guarantee facility should be increased.

However in the context of the EIF's criteria, ESBG members would urge the Commission to assess whether the 25,000 Euro threshold of the microcredit guarantee facility is adequate. It should be recalled in this context that despite the fact that the PHARE programme[11] sets a threshold for individual loans of 125,000 Euro (well in excess of 25,000 Euro) the average loan amounts to 22,000 Euro[12].

In addition, the ESBG strongly encourages the Commission to update best practices regarding microcredit and undertake a comprehensive and in-depth analysis of microcredit in Europe.

B. Improving regulation

The ESBG would like to highlight the crucial role of DG Enterprise in monitoring all legislation which may impact on the provision of microcredit. In this context, it is of the utmost importance that DG Enterprise has the capacity of influencing proposals by other Directorate Generals if these are seen to create additional barriers to the facilitation of microcredits. The recent commitment by the Commission to better regulation is a good step in this direction and progress in that area should be closely monitored.

Ensuring that regulatory proposals do not create additional barriers to the facilitation of microcredits is particularly important in the context of anti-money laundering and anti-terrorism legislation. It should be kept in mind that overly strict legislation aimed at combating financial crime may exclude persons who have no permanent address or identification documents from accessing all types of financial services.

On another note, the Commission should be aware of the impact of prudential legislation on the ability of banks to provide microcredit. Specifically, the new Capital Requirements Directive (CRD) requires banks to adjust their capital basis on the actual risks taken. Against this background, the EBSG would like to reiterate the importance of the microcredit windows managed by the European Investment Fund which limits the risk by borrowers with insufficient collateral.

11 The Phare programme is one of the three pre-accession instruments financed by the European Union to assist the applicant countries of Central and Eastern Europe in their preparations for joining the European Union.

12 "Microcredit for small business and business creation: bridging a market gap", November 2003, European Commission

Furthermore, the ESBG would like to encourage the Commission to undertake a broad consultation on some critical and sensitive thoughts such as charging above market interest rate to cover high risk and high administrative costs associated with the provision of microcredit and the enforcement of legislation on late payments.

C. Fighting financial exclusion via microcredits

While microcredit is one way to contribute to the fight against financial exclusion, the European Commission should assess the nature of the problem and the available means to tackle it. The ESBG would therefore like to encourage the European Commission to carry out an in-depth study of financial exclusion in European banking markets in order to assess the nature of the problem, with a view to drawing up recommendations on means to tackle it. The Commission is also encouraged to carry out an analysis of the existence of illegal money lenders which prey on the financially excluded, and develop recommendations on ways to tackle their existence as well as to protect consumers from them.

About WSBI (World Savings Banks Institute) and ESBG (European Savings Banks Group)

WSBI (World Savings Banks Institute) is one of the largest international banking associations and the only global representative of savings and retail banks. Founded in 1924, it represents savings and retail banks and associations thereof in 86 countries of the world (Asia-Pacific, the Americas, Africa and Europe – via the European Savings Banks Group). It works closely with international financial institutions and donor agencies and facilitates the provision of access to financial sectors worldwide – be it in developing or developed regions.

ESBG (European Savings Banks Group) is an international banking association that represents one of the largest European retail banking networks, comprising about one third of the retail banking market in Europe. It represents the interests of its members vis-à-vis the EU Institutions and generates, facilitates and manages high quality cross-border banking projects.

WSBI-ESBG members are typically savings and retail banks or associations thereof. They are often organised in decentralised networks and offer their services throughout their region. WSBI and ESBG member banks have reinvested responsibly in their region for many decades and are one distinct benchmark for corporatesocial responsibility activities throughout Europe and the world.

Rue Marie-Thérèse, 11 ■ B-1000 Brussels ■ Tel: +32 2 211 11 11 ■ Fax: +32 2 211 11 99
info@savings-banks.com ■ www.savings-banks.com

ISSN 1782-396X