



EUROPEAN COMMISSION
Directorate General for Regional Policy

Guide to Risk Capital Financing in Regional Policy

October 2002

Appendix G :

Good Practice Case Studies

(23.06.03)



Centre for
**Strategy & Evaluation
Services**

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LEGAL DISCLAIMER

The following case studies are analysed for illustrative purposes only. They may not have been object of an investigation or of a formal decision by the European Commission on the basis of the relevant rules on State aid laid down in Articles 87-88 of the EC Treaty. The information contained in the write-ups of the case studies has been provided by the managing authority of the schemes and in no way binds the Commission as to the investigation and approval of schemes similar to the ones analysed below. No part of the following analysis may constitute the basis for legitimate expectations by any interested parties. Each scheme potentially involving State aid must be object of a specific approval procedure carried out by the Commission in conformity with Article 88 of the Treaty and with Regulation No. 659/99 (published in OJ L 10 of 13/01/1999).

As concerns case studies regarding candidate countries, under the Europe Agreement they are already subject to the Treaty rules on State aid during the pre-accession phase. The compliance with the State aid rules in this phase is ensured by the competent national Competition Offices, with additional supervisory control entrusted on the Commission.

Introduction

The following table sets out case studies undertaken during the course of the preparation of the Guide. In the Guide, a number of best practice examples from the case studies are referred to. The full case study write-ups in template format are available online from the European Commission's REGIO website:

http://europa.eu.int/comm/regional_policy/sources/docgener/guides/guide_en.htm

Interested bodies are requested to provide new case studies or to update existing case studies. To do so, please follow the layout shown in the template on the next page and send the case study electronically, in its original language, to the European Commission, DG Regional Policy, Coordination Unit regio-coordination@cec.eu.int who will check case studies and decide which ones merit publication.

Case Study No.	Type of Instrument	Name of Scheme	Website Address of Institution
1	Venture Capital, Loans, Micro Loans	Merseyside Special Investment Fund - UK	www.msif.co.uk
2	Seed and Venture Capital	Enterprise Ireland	www.enterprise-ireland.ie
3	Guarantees	Finnvera- Finland	www.finnvera.fi
4	Loans	Finnvera-Finland	www.finnvera.fi
5	Equity and Loans	Finance Wales-UK	www.financewales.co.uk/
6	Loans	Bank für Sozialwirtschaft AG Germany	www.sozialbank.de
7	Guarantees	Portuguese Mutual Guarantee System (SPGM)	www.spgm.pt
8	Guarantees	Eurofidi -Italy	www.eurocons.it
9	Micro-credits and seed capital	Brussel /Bruxelles micro-credits and seed capital fund -Belgium	www.srib.be
10	Guarantees	Hitelgarancia -Hungary	www.hitelgarancia.hu
11	Micro-credits	Fundusz Mikro -Poland	http://www.funduszmikro.home.pl/
12	Business angels	LINC Scotland	http://www.go.uk.com/business_angels.html

Other good practice case studies notified and approved by the Commission in the framework of State aid regime can be found in the European Commission's REGIO website :

- Risk capital aid:

http://europa.eu.int/comm/competition/state_aid/register/ii/by_primary_obj_risk_capital_aid.html, and

-Equity capital :

http://europa.eu.int/comm/competition/state_aid/register/ii/by_instrument_equity_capital.html

Case Study Template

The following template should be used by regional authorities / others operating innovative risk financing schemes with a regional policy orientation wishing to submit a good practice exemplar. Completed templates should be sent to the regional co-ordination unit at DG REGIO (see previous page).

Name of Case Study	
Region/country	Organisation and address
Date of set up	
Duration	Web site
Total resources (€m)	Telephone
1. Outline description of scheme	
2. Sources of finance for scheme (Community, national, private)	
3. Private capital return	
4. Overall targets (for current period)	
5. Target groups	
6. Terms of assistance (typical amount, time, terms of financing)	
7. Management arrangements	
8. Key advantages of scheme	
9. Results of any appraisals or evaluations	

10. Any other comments	
11. Competition Issues	
The scheme is located in :	
Obj 1 area (Treaty art. 87,3,a)	Please tick as appropriate
Obj 2 area (Treaty art. 87,3,c)	Please tick as appropriate
Not located in an Obj area (Treaty art 87,1)	Please tick as appropriate
Does the scheme involve state aid?	Yes /No (If yes, fill in response below)
If the scheme does constitute a state aid, how does it comply with the rules on state aid in the view of the Member State concerned?	
Compatible with state aid rules on (venture capital schemes)	Yes /No
Compatible with <i>De minimis</i> rules (state aid under €100,000 in 3 years)	Yes /No

Case study No. 1	
Merseyside Special Investment Fund - UK	
<p>Region/country Merseyside, UK</p> <p>Date of set up Operational from 1996</p> <p>Duration 10 years for each fund</p> <p>Total resources (€m) First scheme £32m (€53m). Second scheme £80m (€133m)</p>	<p>Organisation and address Merseyside Special Investment Fund Ltd Cunard Building Liverpool L3 1DS</p> <p>Web site www.msif.co.uk</p> <p>Telephone +44 151 243 3727</p>
1. Outline description of scheme	
Provides venture capital to SMEs in an Objective 1 area. Venture capital provided includes equity and loan finance. Some funds also allocated to community/social enterprises. First established under the 1994-99 Objective 1 programme. Remaining funds from the earlier programme will be recycled for new investment from 2005 onwards. New funding under 2000-06 Objective 1 scheme	
2. Sources of finance for scheme (Community, national, private)	
Second scheme established in 2001/02 has a total of £80m (€133m). The largest fund, a venture fund described below is financed from ERDF (£18m), local institutional equity funding (£2m), local institutional debt facility (£20m). The debt is supported by an EIF guarantee. There are two other funds of £20m each, both financed by £9m of ERDF funding and £11m of bank finance.	
3. Private capital return	
<i>Pari passu</i> with public capital (or explain the preference given to private capital)	
4. Overall targets (for current period)	
There are a series of quantified targets. Amongst these are:	
<ul style="list-style-type: none"> • Over 1000 companies to receive funding • 7,170 additional gross jobs • 3,190 jobs safeguarded <p>On the basis of an ERDF investment of €60m, the cost per gross job is likely to be of the order of €5,500. But funds will be recycled, so the cost per job will be reduced as more jobs are created using recycled funding.</p>	
5. Target groups	
Target groups are mainly SMEs in the Merseyside area. The scheme aims to fill a financing gap where there is a market failure in providing finance for SMEs – SMEs are required to seek other sources of commercial finance first before MSIF will consider them. Companies must have their head office and/or a material proportion of their activities in Merseyside.	
Targets are defined in more detail in a series of investment and operational guidelines set out for each fund.	
6. Terms of assistance (typical amount, time, terms of financing)	
There have been two series of funds set up by MSIF, under the 1994-99 and 2000-06 Objective 1 programme. Both have similar structures and are divided into three funds aiming at different sizes of	

organisation and were initially under separate fund management. The target of the new series (2000-06) funds are:

Venture fund. A £40m (€67m) fund to provide equity based finance (equity, loans and loan stock instruments such as convertibles) to SMEs. Terms are similar for loans to the mezzanine fund below. In respect of equities, any remaining investments at the end of the fund are to be transferred to a limited partnership or trust.

Mezzanine fund – a £20m (€33m) fund to provide loan finance to SMEs. Loan limits are from £75K (€125K) to £600K (€1m), typically with a term of 3 to 7 years at a rate of interest of LIBOR plus 4% to 6%. An interest rate rebate of 33% may be available if certain targets are met.

Small firms fund – a £20m (€33m) fund to provide loan finance to small firms. Of this fund, £2m (€3m) has been allocated to community/social enterprises in association with another local organisation. The remaining fund is available for loans from £3K (€5K) to £75K (€125K), typically with a term of 3 to 7 years at a rate of interest of LIBOR plus 4% to 6%. An interest rate rebate of 33% may be available if certain targets are met.

7. Management arrangements

A separate company (MSIF) has been established to take responsibility for the use of the ERDF grant. A special form of company (Company limited by Guarantee) has been used with the requirement that any surplus funds be reinvested in Merseyside. The company is controlled by a mix of public and private sector partners.

To operate the funds, MSIF has set up a series of partnerships using a type of organisation called a ‘limited partnership’. This organisation provides for a separate legal identity for each fund and limits the liability of partners to the capital they have committed to invest. Funds are obtained from the ERDF, local investors and banks under arrangements that surplus funds (after repaying loans and local investors) are returned to MSIF at the end of the period. For example, it is expected that approximately £11m (€18m) will be recycled from the 1994/99 period.

Each investment fund is managed by specialist fund managers, working to investment objectives set out in operational guidelines for each fund. The fund managers invest on a commercial basis. Their remuneration is partly based on success. Initially, all funds had private sector managers appointed following a public tender and this was seen as a key attribute of the success of MSIF. More recently, to ensure continuity, MSIF has acquired one of these Fund Management companies (now named Alliance Fund Managers Ltd) in order to employ all the staff directly. By paying competitive rates, AFM has also employed other experienced individuals.

8. Key advantages of scheme

Amongst the key attributes of the scheme are:

- The ability to recycle funding after loans have been repaid or equity sold
- A fund structure that allows ERDF funding to be leveraged using private sector funding
- A portfolio of different funds aiming at the needs of different sizes of companies
- Professional and independent fund management operating on a commercial basis
- Management incentivisation scheme linking remuneration to fund management performance over fixed time period
- Clear investment guidelines designed to target investment to the area being helped, and concentration of assistance on companies who would not otherwise obtain finance i.e. on market failure
- The dedication of funds to community/social enterprises targeted at deprived areas, which encourages entrepreneurship as a regeneration and social inclusion catalyst

9. Results of any appraisals or evaluations

MSIF was one of the organisations appraised in the Commission’s 1998 evaluation of financial engineering schemes. It has also been assessed in the context of wider Objective 1 interim and ex-post evaluations for

the 1994-99 period. These assessments have generally been very positive.

10. Any other comments

In setting up the fund a key role was played by professional advisers, including accountants and lawyers. The new fund took some two years to set up, including time for a review of the scheme by national government agencies and departments. To some extent, it has been possible to employ professional advisers on a contingency fee basis (all or part of the fees are paid only if the scheme goes ahead)

In setting up the scheme, it must be recognised that a complex structure will need clearance and agreement from a number of agencies. At the EU level this will include both DG REGIO and DG COMP. At national level, this might include regional agencies as well as relevant central government departments. The complexity of the scheme, and the number of agencies involved, can lead to an extended set up time.

Case Study No. 2	
Enterprise Ireland -	
Region/country: Ireland	Organisation and address Enterprise Ireland Investment Services Directorate Wilton Park House Wilton Place Dublin 2
Contact name Denis Marnane Director, Investment Services	E mail and web site www.enterprise-ireland.ie
Date of set up 1994	Telephone + 353 1 808 2000
Total resources (€m) 1994-1999: €90m 2001-2006: €500m (expected)	
1. Outline description of scheme	
<p>The Seed and Venture Capital Measure under the Operational Programme 1994-1999 was targeted at Venture Capital funds and promoters with the overall objective of stimulating the growth and employment potential of growth oriented enterprises, through the provision of additional equity funding at the lower end of the seed/venture capital market.</p> <p>The aim was to stimulate investment of Venture Capital funding by the private sector in a partnership process of through matching EU (public funds) and private finance. This funding was to fill the gap left by existing Venture Capital funds in providing start-ups access to finance that was typically aimed at established companies with considerable assets. The measure is managed by Enterprise Ireland but implemented by fund managers on a commercial basis.</p> <ul style="list-style-type: none"> ▪ 15 funds currently fully operational ▪ Over 210 investments to the end of 2000 in 125 companies 	
2. Sources of finance for scheme (Community, national, private)	
<p>1994-1999: public funding of €40m (EU/national) matched by €40m private investment. The full value of the fund was invested within this period. By 2000 the funds had returned €30m which has been redistributed for further investments in Venture Capital.</p> <p>2001-2006: public funding of €95m (national) with an objective of leveraging €400m in private funding. Almost €300m has already been leveraged. The proven success of the first programme has resulted in private investors being more inclined to participate in venture capital for start-up businesses.</p>	
3. Private Capital Return	
<i>Pari passu</i> with public capital.	
4. Overall targets	
No information available	
5. Target groups	
<p>The aim is to specifically assist start-up and early stage development companies.</p> <p>The 2001-2006 programme has a distinct focus on developing the regions and no more than 25% of the funds can be invested in the Dublin region.</p> <p>Certain sectors have been identified by Enterprise Ireland as growth sectors and as such require investment: phototonics, obtronics, bio-technology and knowledge based industries. Other sectors that</p>	

have received funding are multimedia, communications, software and food processing.
6. Terms of assistance (typical amount, time, terms of financing)
Typical commercial terms of assistance as would be expected from the private sector. Terms vary according to each fund.
7. Management/operational arrangements
Enterprise Ireland considers the management of the funds by the private sector on a purely commercial basis as a critical success factor. The individual fund managers with private sector management resources and expertise, together with their investment committees manage the funds. An entrepreneur will submit a business plan which is assessed by the Fund Manager on the basis of potential return on investment. Post investment policy allows active investment e.g. board representation. The investment policy is to make commercial investments in growth companies. Unlike other Irish venture financing instruments (ordinary and preference shares), Enterprise Ireland is looking for a financial return on investment. The only involvement Enterprise Ireland has is the provision of funds and identification of key sectors that should be focused on.
8. Key advantages of scheme
<ul style="list-style-type: none"> ▪ Venture Capital in Ireland has significantly evolved and private investment for SMEs is stimulated through a partnership approach. ▪ Fills a gap left by previously existing venture capital funds. ▪ The scheme is run on a purely commercial basis. ▪ Clear focus on very specific sectors and regions requiring additional financing.
9. Results of any appraisals or evaluations/benchmarks/performance
<ul style="list-style-type: none"> ▪ 80% of investments are in start-up and early stage companies. ▪ 60% of invested funds are in software projects. ▪ Investments made in 2000 represented a 40% growth rate over the previous year with the significant change that 47% of the total was in follow-on investments compared to 24% in 1999. This is a measure of the continuing need of companies to have access to Venture Capital at various stages of their lifecycle.
10. Any other comments
Initial difficulties in getting the private sector involved but success of the first programme has resulted in significant leveraging of private finance in the current operational programme. Funds need to be as large as possible. Below a certain level it is not feasible e.g. management fees are prohibitive. As few conditions as possible should be applied by the state. The market will find its own level e.g. a good project will get the funding it requires. Other sources of venture financing for SME's in Ireland are: <ul style="list-style-type: none"> ▪ Enterprise Ireland: Ordinary Shares, Preference Shares ▪ Venture Capital Funds: seed capital, early stage, development, specialist, regional and overseas funds ▪ Private: individuals, BES, Business Angels ▪ Institutions: corporate finance houses, brokers ▪ Corporate Venturing/joint ventures ▪ Capital Markets
11. Competition Issues

Case Study 2
Seed and Venture Capital Measure
Ireland

Object of Commission procedure, State aid N 172/2000. The authorisation letter of 17/10/2000 sent to the Irish authorities is available on the Internet site: http://europa.eu.int/comm/sg/sgb/state_aids/.

The Commission decided that the scheme does not constitute State aid. The main ground for its authorisation was the compliance with the 'market economy investor principle', namely:

- (i) Ireland invests public funds *pari passu* with private venture capitalists, with a maximum level of 30-50% of public funds for each investment/vc fund,
- (ii) there is a proportional sharing of management and administrative fees, no liability on the State;
- (iii) funds are invested into SMEs exclusively through equity-related instruments due to shortage of availability of financing; no funding provided for SMEs in difficulty;
- (iv) public funds are allocated through public call tenders;
- (v) investment decisions are profit-driven, private management is remunerated under commercial criteria;
- (vi) close monitoring of investments and regular submission of information to the Commission is ensured.

Is the scheme located in an Objective area?	
Yes, Obj 1 area (Treaty art. 87,3,a)	(phasing out)
Yes, Obj 2 area (Treaty art. 87,3,c)	
No, not located in an Obj area (Treaty art 87,1)	
Does the scheme involve state aid?	No
If the scheme does constitute a state aid, how does it comply with the rules on state aid in the view of the Member State concerned?	
Compatible with state aid rules on venture capital schemes	Note: Risk capital communication still not in force at that time
De minimis rules (state aid under €100,000)	

Case Study No. 3	
Finnvera Guarantee Fund - Finland	
Region/country	Organisation, address and email
Helsinki (Uusimaa)/Finland	Helsinki
Contact name	Visiting address: Vuorimiehenkatu 1
Anneli Soppi	PO Box 1010
Martin Ingman	FIN - 00101 Helsinki
	Fax +358 204 60 7220
Date set up	Web site and email
Finnvera was brought about by the merger of Kera Corporation and the Finnish Guarantee Board in 1999.	www.finnvera.fi
	Martin.Ingman@finnvera.fi
	Anneli.Soppi@finnvera.fi
Total resources (€m)	Telephone
1,410.8m euros. In 2001, Finnvera had outstanding commitments of €4,908.7m and issued guarantees totalling €376m.	Anneli Soppi + 358 204603709 (Tampere)
	Martin Ingman +358 204 6011 (Helsinki)
1. Outline description of scheme	
<p>Finnvera offers SMEs three main categories of financial instrument; loans, guarantees and export credit guarantees. This case study focuses on Finnvera's portfolio of guarantee products, which are tailored according to the needs of SMEs depending on the business sector in which they operate and on their developmental needs and objectives.</p> <p>Finnvera is 100% owned by the Finnish State. Its main objectives are to provide risk finance to SMEs in cases of identifiable market failure and to support SME promotion and development of indigenous SMEs. It also seeks to promote national industrial and national and EU regional policy objectives.</p>	
2. Sources of finance for scheme (Community, national, private)	
<p><i>Finnvera funds its activities mainly by issuing bonds in the domestic market. Its long-term objective is to achieve financial self-sustainability.</i></p> <p>In terms of Community financing to support Finnvera's guarantee products, the European Investment Fund (EIF) provides assistance in the form of a counter-guarantee available through the Growth and Employment Guarantee scheme. In 2001, guarantees granted under this scheme amounted to €177.1m.</p> <p>In terms of raising capital from the private sector to fund its activities, Finnvera takes advantage of its high credit rating to raise money directly on the capital markets, predominantly through the issuing of bonds.</p>	
3. Private capital return	
<p>The guarantee schemes operated by Finnvera are 100% supported by the Finnish state. Private capital return therefore not relevant.</p>	
4. Overall Targets	
<p>The EIF requires Finnvera to keep monitoring data on the impact of loan guarantees on beneficiary companies such as employment and new business creation. Regular feedback is provided to the EIF, usually on a quarterly basis.</p> <p>In 2001, Finnvera contributed to the creation of more than 2,300 new businesses and 10,600 jobs. Currently, Finnvera is assisting over 27,000 clients.</p>	
5. Target groups	
<p>Finnvera is a tool for the Finnish government to achieve industrial and regional policy objectives. One of its goals is to promote SME development. Target groups therefore include all SMEs and micro-firms.</p> <p>Finnvera has developed tailored guarantee products for SMEs operating in particular sectors e.g. an environmental guarantee is available to Finnish companies in the industrial sector to finance investment in environmental protection measures. The micro-enterprise guarantee targets SMEs with less than 5 employees and in particular, those with little or no collateral who would not otherwise obtain loan financing.</p> <p>Finnvera's investment decisions are based on commercial profit-driven criteria, but the attainment of social</p>	

and regional objectives such as job creation is also emphasised.

6. Terms of assistance (typical amount, time, terms of financing)

Finnvera offers a range of innovative guarantee products including the Small Enterprise Guarantee, a micro-finance guarantee, growth guarantee, internationalisation guarantee, venture capital guarantee, an environmental guarantee, a guarantee specific to the shipping industry and a guarantee to fund growth or expansion projects. Guarantee products are tailored according to business developmental needs.

Some of Finnvera's guarantee products receive EU support through the European Investment Fund (EIF). The Finnish national guarantee fund also provides a counter-guarantee amounting to 55% of the capital guaranteed by Finnvera. This considerably reduces Finnvera's overall level of operational risk and frees up capital to provide more guarantees to companies, which in turn leverages additional loans from the private sector.

SMEs pay a small handling fee to Finnvera if the application is approved. In addition, the firm then pays a fixed percentage fee to cover the risk premium. The percentage fee paid by the SME varies depending on the risk classification, which is determined by means of a comprehensive qualitative and quantitative risk assessment.

The Growth Guarantee scheme is eligible for EU support under the EIF's Guarantee Facility Growth and Employment fund.

7. Management arrangements

Finnvera's guarantee portfolio is managed in-house. Finnvera's headquarters are split between Helsinki and Kuopio. It has 16 regional offices and 4 business support units.

Guarantee applications are assessed in two stages a) rigorous quantitative risk assessment using a computerised Customer Risk Management classification system and b) qualitative assessment carried out by one of Finnvera's 100 business analysts, who are divided into sectoral units.

In 2002, a profit sharing scheme, specific to each business unit and evaluated over a three year reference period commencing 2002, was adopted.

8. Key advantages of scheme

- Sophisticated customer risk management system based on seven levels of lending risk is used to assess guarantee applications. The 'CRM' system was developed in-house and provides a computer-generated risk analysis. This is supplemented by qualitative analysis carried out by business analysts with sectoral expertise.
- The use of commercial investment criteria and the carrying out of a detailed risk assessment and analysis of the business plan etc. help to ensure a minimal level of default. Rigorous quantitative and qualitative pre-screening procedures helps reduce level of risk for lending institutions
- Annual monitoring of the financial statements of client companies following granting of guarantee further minimises the default rate and acts as an early warning system in respect of companies experiencing difficulties. Companies are provided with a free benchmarking analysis of their financial position compared with others in their sector
- Improves SME access to finance and addresses market failure where lack of collateral, credit history and/ or track record constitute major obstacles to obtaining credit on reasonable terms
- Targeting of particular sectors/ groups allows Finnvera to fulfil its social, industrial and regional policy objectives, such as promoting SME development, creating employment and encouraging investment in environmental businesses
- Sectoral specialisation of Finnvera business analysts at regional level helps ensure low rate of default and contributes to banks better understanding of the industries in which clients operate
- Good vertical linkage with business support organisations such as the employment and economic development centres helps bolster SME survival rates and minimise rate of default
- Strong regional presence through Finnvera's 16 regional offices means close relationships with and understanding of client base
- Innovative fund-raising mechanism (the issuing of bonds on the domestic market) enables Finnvera to access comparatively cheap sources of capital direct from capital markets rather than via a financial intermediary

- | |
|--|
| <ul style="list-style-type: none">• Substantial private sector leverage effect of guarantee instruments. There is a high multiplier effect between the capitalisation of a fund and the total amount of loans it is able to leverage through utilisation of guarantees and counter-guarantees. |
|--|

9. Results of any appraisals or evaluations
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An evaluation of the efficiency and effectiveness of Finnvera's operations will be carried out next year.

10. Any other comments

NA

Case Study No. 4	
Finnvera Loan Fund - Finland	
Region/country	Organization and address
Helsinki (Uusimaa)/Finland	Helsinki
Contact names	Visiting address: Vuorimiehenkatu 1
Mr Martin Ingman	PO Box 1010
Ms Anneli Soppi	FIN - 00101 Helsinki
	Fax +358 204 60 7220
Date of set up	Web site and email
Finnvera was brought about by the merger of Kera Corporation and the Finnish Guarantee Board in 1999.	www.finnvera.fi
	Martin.Ingman@finnvera.fi
	Anneli.Soppi@finnvera.fi
Total resources (€m)	Telephone
1,410.8m euros, with €4,908.7m in committed loans. In 2001, Finnvera made loans of €332m.	Anneli Soppi + 358 204603709 (Tampere)
	Martin Ingman +358 204607205 (Helsinki)
1. Outline description of scheme	
<p>The type of loans offered by Finnvera include capital loans (in the form of a convertible bond), development loans, entrepreneur loans, internationalisation loans, investment and working capital loans, loans for women, micro loans and the Joint European Venture loan scheme. Finnvera also offers interest rate subsidies on loans to SMEs in eligible areas that receive support from ERDF Objective 2 and from Finnish domestic industrial support programmes.</p> <p>Finnvera is 100% owned by the Finnish State. Its main objectives are to provide risk finance to SMEs in cases of identifiable market failure and to support SME promotion and development and the internationalisation of indigenous SMEs. It also seeks to promote national and EU regional policy objectives.</p>	
2. Sources of finance for scheme (Community, national, private)	
<p>Finnvera funds its activities mainly by issuing bonds in the domestic market. Its long-term objective is to achieve financial self-sustainability.</p> <p>Companies located in Structural Fund supported regions (Objectives 1 & 2) in Finland are eligible to apply for an ERDF-backed interest rate subsidy, which is complemented by an additional interest rate subsidy from the Finnish government. ERDF is utilised for Micro-loans, Small loans and a special loan to Women Entrepreneurs, Entrepreneur loans (start-ups and business transfers) and Investment loans in Objective Areas 1 and 2.</p> <p>In addition, Finnvera receives EU support for other types of schemes including the Joint European Venture scheme (JEV), which seeks to promote the creation of joint ventures and to increase the number of jobs within the European Economic Area (EEA). Businesses can get financial support for setting up joint ventures that have partners from at least two EEA countries.</p> <p>Finnvera has a long-term loan facility from the European Investment Bank (EIB). Finnvera has also obtained financial support from the EIF through the Growth and Employment Guarantee and Small Enterprise Guarantee Portfolio. Finnvera also receives European Investment Fund financial support through the Environmental Loan scheme. In 2001, EIF-supported loans made under the Environmental Loan scheme amounted to €38.0m.</p> <p>Finnvera takes advantage of its high credit rating to raise money directly on the capital markets, predominantly through the issuing of bonds.</p>	
3. Private capital return	
Loan schemes operated by Finnvera are 100% supported by the Finnish state – private capital return therefore not relevant.	
4. Overall Targets / Impacts	
In order to meet requirements under ERDF funding, Finnvera keeps monitoring data on the impact of interest rate subsidy schemes such as the women's loan and SME loan scheme on beneficiary companies in	

terms of key output indicators such as direct jobs created and the amount of new investment leveraged.

Between January 1997 and December 2001, 6450 women entrepreneurs were granted loans, leading to the creation of 6,970 jobs and 14,781 SME loans were granted contributing to the creation of 16,492 direct jobs.

5. Target groups

Finnvera is a financial investment tool for the Finnish government to achieve industrial and regional policy objectives. One of its goals is to promote SME development. Target groups therefore include all SMEs – with a particular focus on micro-firms.

In addition, Finnvera has developed specialist financial investment products for SMEs operating in particular sectors. Finnvera’s investment decisions are based on commercial profit-driven criteria, but the achievement of social and regional aims such as improving access to finance for SMEs and new job creation are seen as parallel objectives.

6. Terms of assistance (typical amount, time, terms of financing)

Loans: Of the €332m granted in loans in 2001, approximately €98m was granted in the form of interest-rate subsidised loans in keeping with the Finnish government’s industrial policy goals of encouraging SME start-ups and facilitating their growth and development. Of the €98m in loans benefiting from an interest-rate subsidy, approximately €29m was devoted to micro loans and €16m to women entrepreneurs. A further €26m was granted in the form of environmental loans.

A ‘special interest’ subsidy from the Finnish State is available for specific types of loans e.g. developmental loans, environmental loans, start-up loans, environmental loans and micro-lending. The level of subsidy i.e. national plus EU funding on interest rate subsidy schemes is 3%. The interest rate subsidy is transferred to the borrower – a type of instrument known as a “soft loan”.

In terms of the proportion of loan financing Finnvera will lend relative to total capital required, typically, Finnvera will lend around a third of the SME’s capital requirement (with the other two thirds coming from traditional bank finance and the SME’s own capital resources). However, the maximum percentage it can lend to small firms is 75%. In the case of micro lending, the proportion of financing Finnvera can provide is up to 100%.

The level of default on loans made by Finnvera is very low and compares very favourably with banking institutions. Overall, the level of default on loans is 3%. The survival rate of companies assisted is also significantly above average, at 88% for the women’s entrepreneurs scheme and 82% for the small loans scheme.

Special loans: For certain types of loan known as ‘special loans’ (micro loans, development loans and entrepreneur loans) the Finnish state provides a credit loss compensation scheme: for every 1€ lost through loan defaults, 55% is compensated by the State. Finnvera bears the cost of the remaining 45%.

As far as other loans and guarantees are concerned, there is a credit and guarantee loss compensation from the Finnish State. The scheme operates on the following basis:

<i>Region type</i>	<i>Percentage of losses guaranteed</i>
Region I	65%
Region II	50%
Region III (regions not eligible for regional subsidies)	40%

Micro-lending: Under the micro loan scheme, firms can borrow between €3,500 and €35,000. Typical lead times for an investment decision are around 2 weeks. The duration of the loans is 5 years of which 1 year is redemption-free. The interest rate subsidy scheme for women entrepreneurs is charged at the rate of Euribor¹ plus 1% whilst the interest rate on the SME loan scheme is Euribor plus 1.5%.

The Finnish state provides a credit loss compensation scheme whereby every 1€ that Finnvera loses as a

¹ Euribor is a basket of wholesale interest rates charged by Eurozone banks.

result of loan defaults, 55% of the loss is compensated. For certain types of loan scheme, such as the micro loan scheme, the risk is further reduced because the loans are counter-guaranteed by the European Investment Fund (EIF).

Joint European Venture: The maximum level of support available under the JEV Initiative is €100,000 per project. The maximum sum available for feasibility studies is €50,000, which cannot account to more than 50% of the total cost of the feasibility study. Financing is provided via an interest-free loan, which is converted into a grant upon application if the joint venture is established. Assistance towards investment costs is granted upon application after the investment has been completed.

7. Management arrangements

Finnvera's loan portfolio is managed in-house. With a joint Headquarters in Helsinki and Kuopio, Finnvera has 16 regional offices and 4 business support units.

Loan applications are assessed in two stages a) rigorous quantitative risk assessment using a computerised Customer Risk Management classification system and b) qualitative assessment carried out by one of Finnvera's 100 business analysts, which are divided into sectoral units.

In 2002, a profit sharing scheme, specific to each business unit and evaluated over a three year reference period commencing 2002, was adopted.

8. Key advantages of schemes

- Sophisticated customer risk management system (developed in-house) based on seven levels of lending risk is used to screen and assess loan applications. The 'CRM' system provides a computer-generated risk analysis based on a broad range of risk factors (in order to help minimise risk levels). This is supplemented by qualitative analysis carried out by sectorally trained business analysts
 - Annual monitoring of the financial statements of client companies following the granting of a loan further minimises the default rate and acts as an early warning system in respect of companies experiencing difficulties. Companies are provided with a free benchmarking analysis of their financial position compared with others in their sector
 - Lending decisions based on commercial lending criteria i.e. detailed risk assessment, analysis of the business plan etc. to ensure minimal level of default
 - Rigorous quantitative and qualitative pre-screening procedures helps reduce level of risk for lending institutions
- Improves SME access to finance and addresses market failure, particularly in respect of disadvantaged social groups such as women entrepreneurs, ethnic minority groups, young entrepreneurs etc. where lack of collateral, credit history and/ or track record constitute major obstacles to obtaining credit on reasonable terms
 - Targeting of particular sectors/ groups allows Finnvera to fulfil its social, industrial and regional policy objectives, such as promoting SME development, creating employment and encouraging investment in environmentally sustainable businesses
 - Sectoral specialisation of Finnvera business analysts at regional level helps ensure low rate of default and contributes to banks better understanding of the industries in which their clients operate
 - Strong regional presence through Finnvera's 16 regional offices enables close proximity with and understanding of client base
- Good vertical linkage with business support organisations such as the employment and economic development centres further minimises the rate of default
 - Innovative fund-raising mechanism (the issuing of bonds on the domestic market) enables Finnvera to access comparatively cheap sources of capital direct from capital markets rather than via a financial intermediary
 - Relatively short lead times between applications being made and investment decisions being taken

9. Results of any appraisals or evaluations

An evaluation of the efficiency and effectiveness of Finnvera's operations will be carried out next year.

10. Any other comments

No	
11. Competition Issues	
<p>The loan scheme administered by Finnvera was object of a Commission procedure, State aid N 465/2000. The decision is set out in the Commission letter to the Finnish authorities, available on the Internet site: http://europa.eu.int/comm/sg/sgb/state_aids/.</p> <p>The Commission decided that the scheme constitutes State aid within the meaning of Article 87 (1) of the Treaty, but authorised it under Article 87 (3) of the Treaty and the Block Exemption Regulation for SMEs (“SME BER”). The main grounds for this authorisation were:</p> <p>(i) the beneficiaries are SMEs within the meaning of the SME BER, whose activities and aided eligible costs are exclusively those covered by the SME BER and comply with the ceilings set therein;</p> <p>(ii) the Finnish authorities committed to complying with the State aid rules in specific sectors (e.g. the Community Guidelines on State aid for rescue and restructuring firms in difficulty) and respecting the BER rules on the cumulation of aid;</p> <p>(iii) the Finnish authorities committed to notifying the Commission for approval any large individual cases as provided for by the SME BER.</p>	
Is the scheme located in an Objective area?	
Yes, Obj 1 area (Treaty art. 87,3,a)	
Yes, Obj 2 area (Treaty art. 87,3,c)	(in case of interest rate subsidy loan scheme)
No, not located in an Obj area (Treaty art 87,1)	
Does the scheme involve state aid?	Yes
If the scheme does constitute a state aid, how does it comply with the rules on state aid?	
Compatible (with state aid rules)	Compliance with the Exemption Regulation for SMEs
De minimis rules (state aid under €100,000)	

Case Study No. 5	
Venture Capital, the Wales Innovation Fund (WIFL) - Wales, UK	
Region/country	Organisation and address
Wales, UK	Finance Wales plc
Contact name	Oakleigh House
Enquiries	Park Place
	Cardiff
	CF10 3DQ
	Great Britain
Date of set up	Web site and email
Operational from November 1999. It was intended originally to establish a ten-year limit on the life of the scheme. However, the fund was invested fully by the end of 2001 and investments are made for a 3-5 year period.	http://www.financewales.co.uk/
Total resources (€m)	Telephone
Total resources £5.0m (€8m)	+44 29 2033 8100
1. Outline description of scheme	
<p>One of a range of integrated business support and financing programmes for SMEs provided by Finance Wales, WIFL invests venture capital in smaller technology-based businesses in Wales.</p> <p>An independently and commercially-managed subsidiary of the Welsh Development Agency, Finance Wales exists to help small and medium-sized businesses in Wales to realise their true potential for innovation and growth. Programmes include:</p> <ul style="list-style-type: none"> • Loan, equity, and mezzanine funding for companies; • Financial support for specific investments, such as university spin-outs; • Xenos – a network of business angels in Wales; and, • Management support programmes, such as “Access to Capital”, and “Mentor Wales”, <p>Venture capital provided by WIFL includes equity, loans, and mezzanine finance (such as convertibles and loan stock with an equity option attached). Overall fund supports businesses throughout Wales but use of EU resources is confined to businesses based in the Objective 2 area of Industrial South Wales. First established under Priority 3, Measure 2 (increased direct investment in SMEs) of the 1997-1999 Industrial South Wales Objective 2 programme.</p> <p>Funds from the realisation of WIFL’s investments will be recycled to secure the sustainability of the fund.</p>	
2. Sources of finance for scheme (Community, national, private)	
WIFL is financed from three sources: private equity capital from the Royal Bank of Scotland (£3m); equity capital from the Welsh Development Agency (WDA), provided by HM Treasury (£0.5m); and ERDF funds (£1.5m). No financial guarantees support the fund.	
3. Private Capital Return	
<i>Pari passu</i> with public capital	
4. Overall targets (for current period)	
Original target was full investment of WIFL funds by the end of 2001. This was achieved by mid-2002.	
Original expectation was that this would constitute up to 20 investments in equity and loans. The Fund has invested in 14 companies to date in a mixture of equity and loans.	
5. Target groups	
Technology-based businesses with a good management team, growth potential, products protected by intellectual property, and, ideally, a solid balance sheet are the fund’s primary targets. In general, the fund looks to support businesses with proven product or service concepts. The fund will also consider good quality investments from more traditional sectors, including small MBOs.	

The scheme aims to fill a financing gap because of a well-established lack of risk capital for small-scale investments (below £3m) in technology-based businesses in Wales. Companies need not have exhausted other sources of commercial finance before they approach the fund.

Targets are defined in more detail in a series of investment and operational guidelines.

6. Terms of assistance (typical amount, time, terms of financing)

Average investments are £150k (€240k), typically for 3 to 5 years. Fund limits are from £50k (€80k) to £500k (€800k) per company. A range of different forms of finance is available: ordinary equity; preferred equity; convertibles; loan stock with an equity option; and variable interest rate term loans. In situations where ordinary, voting equity shares are purchased, the fund limits its participation to a minority stake of between 20% and 50% of the voting shares.

The fund establishes a bespoke financing package for each participating company on a case-by-case basis. Financing structures take into account factors such as the cash flow and asset structure of the company, the nature of the new investment (fixed assets, intangibles, working capital), and the preferences of other investors.

Measures are also taken to establish clear governance and performance monitoring systems, and, where necessary, to strengthen the management team of companies supported by the fund. Additional or replacement managers are provided by the fund on a case-by-case basis. A non-executive director is appointed to represent the fund's interests in all cases. And, the fund monitors progress of all companies against objectives on a monthly basis or quarterly basis. An independent "Performance Monitor" carries out this process.

7. Management arrangements

A separate, private limited company (The Wales Innovation Fund Limited) has been set up to run the fund. Finance Wales plc own 40% of the shares and the Royal Bank of Scotland own 60%. Voting rights (each of the two investors has 50%), and the treatment of losses, gains, recycling of realised investments, and unrealised investments are defined by a shareholder agreement. ERDF funds are provided to WIFL as grants and drawn down on a case-by-case basis.

The fund was initially managed by a procured fund management team working to investment objectives set out in the operational guide, but in the latter stages of the investment period, was managed by an in-house team of Finance Wales employees, working to the same guidelines.

All investments are made on a commercial basis although the support of Finance Wales and the ERDF enables investments to be made in situations with higher risk profiles.

8. Key advantages of scheme

Amongst the key advantages of the scheme are:

- Ability to overcome a financing gap. The fund is willing to do smaller deals and consider higher risk profiles with longer realisation periods than those generally handled by venture capital firms. Although the UK has Europe's most advanced and sophisticated venture capital market, major funds are, in general, not interested in supporting investments of less than £3m (€4.8m), especially in technology companies located away from the major 'clusters' of innovative activity in SE England. Administrative costs of individual deals and the difficulty of finding enough good quality investments to diversify risk, limit the attractiveness of investments in small, growing, technology-based companies in Wales;
- Access to different forms of risk capital within the same fund and from other, complementary funds run by Finance Wales. This enables the financing structure of each participating company to be 'designed' on a bespoke basis. A better match between sources and uses of funds; greater liquidity, and a reduced risk of insolvency are some of the benefits;
- The provision by Finance Wales of complementary services, such as the Access to Capital and Mentoring programmes. These help make firms more "investor ready" and improve management capacity;
- The ability to recycle funding after investments have been realised. This reduces the cost of achieving public policy objectives, such as job creation;
- A funding structure that allows ERDF and WDA funding to be leveraged using private sector finance;
- Involvement of the private sector in the governance of the fund. This helps impose commercial disciplines in investment decision-making and raises the profile of Wales as a place for other private fund managers to invest. Private sector involvement also helps the fund to 'syndicate' deals with

other public and private sector funds. This increases still further the leverage gained from ERDF and WDA resources;

- Links with Xenos, the Welsh Business Angels network. Close access provides fund managers with a flow of potential deals and the opportunity to involve angels in further financing rounds;
- Public policy objectives that combine the stimulation of innovation with job and wealth creation;
- Clear investment guidelines designed to target investment to the area being helped, and to concentrate assistance on companies who would not otherwise obtain finance; and,
- Role of Finance Wales in educating the wider business community about the benefits of risk capital, especially equity. Involvement of intermediaries (such as lawyers and accountants) is critical to the success of a venture capital programme. They provide a network of links to established companies with good ideas and a lack of capital to exploit them. Many of the firms supported by the scheme are established organisations rather than start-ups.

9. Results of any appraisals or evaluations

This is a small-scale fund and has yet to be formally evaluated. In general, Finance Wales are very pleased with the progress of the fund and 14 companies have received support. The scheme has, however, been an important learning experience for Finance Wales. It has enabled them to set up and manage a complex venture capital fund that provides management services, corporate finance expertise and multiple sources of finance to technology-based companies. It has also strengthened the relationship between Finance Wales and the private sector.

Experience gained from the operation of WIFL has informed the development of the new Welsh Objective 1 equity programme set up by Finance Wales. This ten-year fund has committed resources of £20.5m of which 45% will come from ERDF. Barclays Bank is the private sector partner.

10. Any other comments

The idea for the fund was outlined in the 1998 Mapping Study that identified the benefit of setting up a single provider of risk capital and business advice for SMEs. Setting up the fund took a further eighteen months because of the complex structure and the need to negotiate with Royal Bank of Scotland, the UK Government, DG COMP, and DG REGIO. Complex venture financing schemes have extended set-up periods because of the need for clearance from the EU and a range of regional and central government departments.

Case Study No. 6	
Revolving Loan Fund, Bank für Sozialwirtschaft - Germany	
Region/country	Organisation and address
New German Länder (<i>Berlin-Ost, Brandenburg, Mecklenburg-Vorpommern, Sachsen, Sachsen-Anhalt, Thüringen</i>) = German Objective 1 areas	Bank für Sozialwirtschaft AG (BfS) Wörthstr. 15-17 D-50668 Köln Germany
Date of set up	Web site
12.12.1974	www.sozialbank.de
Duration	Telephone
Usual loan term: 25 years	+49 221 97356 0
Total resources (€)	
175 Mio. Euro	
1. Outline description of scheme	
<p>Revolving loan fund dedicated to private sector organisations specialising in social welfare-related work in Germany (in order to be eligible for a loan, applicants must be members of one of the top six German associations dealing with private sector welfare work).</p> <p>The scheme seeks to promote private sector welfare work and to improve the social infrastructure in Germany. Since 1991, the objective of the fund has been to promote the new “Länder” mentioned in the German Unification Treaty.</p> <p>Funding is available for the following types of projects;</p> <ul style="list-style-type: none"> ▪ Project funding ▪ Investment projects ▪ Structural development projects 	
2. Sources of finance for scheme (Community, national, private)	
<p>The <i>Bank für Sozialwirtschaft</i> (BfS) revolving loan fund is funded by national government. BfS manages the fund on behalf of the German Federal Ministry of the Family, the Elderly, Women and Youth. Up to 50% of the loan principal comes from the BfS revolving fund. The remaining 50% is derived from the following sources:</p> <ol style="list-style-type: none"> 1) Other public capital (from regional or local authorities) 2) Private capital from banks (in the form of loans) 3) Private capital (mainly from private foundations) 4) Loan applicant’s own capital 	
3. Private capital return	
<i>Pari passu</i> with public capital	
4. Overall targets (for current period)	
No information available	
5. Target groups	
The revolving loan fund targets facilities and organisations (SMEs) specialising in private sector welfare work (members of the six top German associations).	

In the context of the reorganisation of services and the up-coming Basel II conference, companies active in the social welfare field are facing a number of significant new challenges. Approximately half of all facilities and organisations in the social sector will have to change their internal structures in order to cope with changes currently taking place within the social welfare sector. There is an increasing need for finance and innovation in order to fund necessary changes – financing is needed, for example, to help implement the introduction of more effective management instruments, facilitate changes in organisational structures as well to fund investment in physical infrastructure.

Companies in the social sector find it difficult to get loans. There is often a market failure in respect of access to capital, with banks withdrawing continuously from sectors where little growth is expected.

The provision of loans from the BfS loan scheme helps companies operating in the social sector to maintain their competitiveness and helps to create and safeguard jobs by enabling companies to keep pace with industry-changes and regulatory requirements.

There are four typical areas of financing:

- 1) Organisations/ institutions operating at national level
 - Central administration of federal and specialised associations
 - Schools and qualification centres of the top associations on national and regional level
- 2) Regional organisations with activities involving several regions
 - Administration and education/qualification facilities of regional associations
- 3) Organisations/ associations involved in the following types of activities;
 - Health clinics and recreation centres
 - Holiday homes for families
 - Homes for people with disabilities
 - Youth hostels
 - Self-help facilities
 - Integration facilities for migrants and refugees
- 4) Pilot projects
 - e.g. initiatives aimed at promoting the social inclusion of marginal groups

6. Terms of assistance (typical amount, time, terms of financing)

The BfS revolving fund offers interest-free loans usually over a term of 25 years. An administration fee of 2% of the loan principal has to be paid at the commencement of the loan contract. The creditor pays an annual administration fee of 0.03% of the original loan sum. The loan is repaid quarterly - the first repayment is only payable however after the first six months. Each year at least 4 % of the loan sum has to be paid back. Repayments are re-added to the funds and used for new loans (revolving loan fund).

7. Management arrangements

The loan-seeking organisation applies for a BfS loan through a regional association which promotes private sector welfare work. The regional association transfers the application to the association's national headquarters for assessment. The association defines its special funding aims. The application and the project's content are then discussed in a loan committee composed of representatives from the six top associations. The applications fitting into the funding objectives that are accepted by the loan committee are transferred to the grant committee composed of representatives of the top associations and Bank für Sozialwirtschaft AG. The grant committee checks the general eligibility of the application according to the loan fund's guidelines. If the application is accepted as eligible, Bank für Sozialwirtschaft AG examines the security of the loan application. This procedure is managed by the trust department of Bank für Sozialwirtschaft AG.

8. Key advantages of scheme

- Interest-free, long-term loans meet the financial needs of social-orientated organisations willing to invest.
- The use of revolving finance - reinvestment of loan repayments enables the fund to use all available capital in order to maximise investment opportunities.
- The funding institute can influence the purpose for which funds are used through the fund's legal

framework and operational guidelines.

- Experience has proved that there is no significant risk for the lending institute.
- The success of such a revolving loan scheme depends on the knowledge of the market and the client's needs. These conditions are fulfilled as Bank für Sozialwirtschaft AG's financial expertise – the loan product has been developed on as close to commercial criteria as possible.

9. Results of any appraisals or evaluations

The German Federal Court of Auditors has unlimited audit rights for the BfS revolving fund. It audits the funding guidelines set out by the Federal Ministry of Family, the Elderly, Women and Youth.

Bank für Sozialwirtschaft AG submits the application proofs to the Federal Ministry of Family, the Elderly, Women and Youth. This contains both the balance of the fund and the list of funded projects.

10. Any other comments

No

Case Study No. 7	
SPGM Mutual guarantee scheme - Portugal	
Region/country: Portugal	Organisation and address SPGM - Sociedade de Investimento, S. A. Rua Prof Mota Pinto 42 F, sala 206 P – 4100-353 Porto Portugal
Contact name Miguel Sousa Branca	E mail and web site spgm@spgm.pt www.spgm.pt
Date of set up System (and SPGM) set up in 1994	Telephone + 351 22 616 52 80 + 351 22 616 52 89 (Fax)
Total resources (€m) SPGM share capital €12.5m (€ 100m live guarantees) Counter Guarantee Fund €57m	
1. Outline description of scheme	
<p>The Portuguese Mutual Guarantee System was set up in 1994, initiated by IAPMEI (SME national agency). Later, IFT (tourism national agency) also joined it. The system comprises:</p> <ul style="list-style-type: none"> - SPGM, created in 1994 as an investment bank structure (<i>sociedade de investimento</i>) - Counter Guarantee Fund, created in 1999 (funds valued at €57m) - 3-4 new Mutual Guarantee Societies (to be created during 2002). <p>The objective of SPGM when set up, was to test the need for and develop a mutual guarantee system in Portugal which would assist SMEs in accessing finance that was more readily available to larger companies. SPGMs current role includes liaison with banks and SMEs, carrying out administrative work and managing the Counter Guarantee Fund on behalf of the state.</p> <p>A third level counter guarantee is provided by the EIF in certain circumstances e.g. for SMEs and banking operations within the European Initiative for Growth and Employment.</p> <p>As a result of the successful development of the mutual guarantee system and the expansion of activities which SPGM is responsible for, the system is now in the process of creating three separate Mutual Guarantee Societies (MGS) which will become the commercial entities of the system:</p> <ul style="list-style-type: none"> • Norgarante - located in Oporto, splitting off from current SPGM. • Lisgarante – located in Lisbon, splitting off from the current SPGM. • Garval – located in Santarém, an area that has always had particular interest and motivation to work with mutual guarantees. • A fourth MGS is likely to be established in the Algarve with a focus on tourism. <p>SPGM will thereafter function as a holding company focusing its activities to continued management of the Counter Guarantee Fund and back office/support functions of the system, such as legal and administrative work and implementing IT solutions for the MGSs.</p>	
2. Sources of finance for scheme (Community, national, private)	
<p>Current Shareholders:</p> <p>50% state/public funded (IAPMEI/IFT) with EU support</p> <p>50% private sector funding from</p> <ul style="list-style-type: none"> • The 4 largest banks (BCP, BPI, BTA, BES) (35%) 	

<ul style="list-style-type: none"> • 400 SMEs (15%) through share capital. <p>The objective is to achieve 50% of funding from SMEs within the next 3 years. The system is comfortably within the EU recommended solvency ratio of 8%. The Portuguese currently have a solvency ratio closer to 14-15%.</p>
<p>3. Private capital return</p>
<p><i>Pari passu</i> with public capital.</p>
<p>4. Overall targets</p>
<p>No information available.</p>
<p>5. Target groups</p>
<p>Target sectors have traditionally been manufacturing, commerce, and tourism but will expand to include services and real estate/construction from the 2002 fourth quarter, as soon as the new Mutual Guarantee Societies are established. Agriculture is the only sector completely excluded from funding.</p> <p>Initially SPGM focused on providing funding to medium sized companies, in particular manufacturing around the Oporto region. The focus is now shifting towards smaller companies, in part due to the effects of globalisation e.g. textile industry relocating elsewhere in the world which has resulted in the need to develop alternative local industry.</p> <p>There are no particular eligibility criteria at the moment with all companies given an equal right to apply for a guarantee. However it is expected that in the future some sort of prioritisation might be introduced in favour of SME's already participating in the share capital of the new Mutual Guarantee Societies.</p>
<p>6. Terms of assistance (typical amount, time, terms of financing)</p>
<p>Level of cover provided: typically 50% with a maximum of 80%. 100% is available to smaller operations on a limited basis.</p> <p>Costs to the SME:</p> <ul style="list-style-type: none"> ▪ Administrative cost ▪ Annual commission based on the value of the guarantee – between 0.5% and 3% (normally not above 2.0%) depending on the risk perceived in the SME and type of operation <p>Participation in the system requires the SME to hold shares valuing a minimum of 2% of the guaranteed amount (increasing to 3% or more as the value of the system proves itself and aim is to increase SMEs share capital). Minimum amount €500.</p>
<p>No other collateral is required from the business e.g. secured assets but there are certain contractual agreements which must be adhered to which include:</p> <ul style="list-style-type: none"> ▪ Company owners are not allowed to sell the company or a part of the company. ▪ Entrepreneur must not leave the company. ▪ Cross-default – all parties owed share in any income paid if defaulted. ▪ Credit document is often required from the entrepreneur and his/her company which would assist in reclaim of funds in case of default. <p>The default rate currently very low (1.7%). However this is expected to increase as loans get closer to maturity date.</p> <p><i>The Counter Guarantee Fund provides 50% cover for the guaranteed value of the MGS.</i></p>
<p>7. Management/operational arrangements</p>

<p>SPGM is currently responsible for all management and operational aspects of the scheme. Typical operations include:</p> <ul style="list-style-type: none"> ▪ Medium and long term bank loan guarantees ▪ Short term bank loan guarantees ▪ Guarantees covering the anticipation of public grants ▪ Guarantees in favour of tax authorities ▪ Medium and long term leasing contract guarantees ▪ Bond principal guarantees ▪ In general any guarantees covering any other contractual business duties of SMEs ▪ SPGM also provides informal financial advice to SMEs requiring assistance
<p>8. Key advantages of scheme</p>
<p>For SMEs</p> <ul style="list-style-type: none"> ▪ Ability to negotiate on a trilateral basis with the bank within the MGS. ▪ Less security is required by the bank if backed by SPGM. ▪ Lower interest rates. ▪ Improved financial structure and credibility. ▪ Should be at least better off by going with SPGM. ▪ Offers competitive advantage to SMEs. ▪ Reduces constraints related to company size. <p>For the state</p> <ul style="list-style-type: none"> ▪ Even though progress has been slower than planned the creation of the system is considered a success as over 7 years SPGM has established a successful Mutual Guarantee System in Portugal. ▪ Still relatively small but already have €100m worth of guarantees and has been assisting 400 companies. ▪ Provides competitive advantage to the economy where SMEs account for 75% of jobs. ▪ Encourages repeat business with companies which is the preferred outcome as a company can maintain guaranteed funds to the value of the 2% share taken.
<p>9. Results of any appraisals or evaluations/benchmarks</p> <ul style="list-style-type: none"> ▪ Default rate less than 2% over the first 7 years. ▪ Accumulative value guaranteed has risen from €3m in 1995 to €167m in 2001. ▪ From 1994 – 2001: 23,000 jobs created for €500m invested.
<p>10. Any other comments</p>

The development of the Portuguese Mutual Guarantee System has clearly been a success over the last 7 years and some recognition must go to the President of SPGM (Mr. José António Barros), who has been involved since the set up in 1994 and who is a dynamic entrepreneur himself and very close to the requirements of small business. Other state assistance for SMEs provided by IAPMEI includes:

- 0% loans
- grants
- interest rate subsidies

Legal and fiscal constraints provided the greatest challenge to setting up the system e.g. absence of a counter guarantee fund until 1999. Creation of the Mutual Guarantee Societies was constrained by some facts such as the need to change the existing law which took a long time to adapt.

Difficulties in convincing SMEs that there is a real benefit from a Mutual Guarantee Fund. In Santarém, this message was more easily transmitted, probably due to a very dynamic Entrepreneur Association that worked with local business to invest in the new Society share capital. Other areas have been less interested in the concept. Key messages that have been emphasised to such SMEs are:

- The system exists to assist SMEs in accessing finance.
- Public funds (national and indirectly EU) have been invested in the system.

In the future, SMEs will eventually own 50% of the Mutual Guarantee Societies share capital.

Case Study No. 8	
Eurofidi mutual guarantee scheme - Italy	
Region/country	Organisation and address
Piedmont/Italy	Eurofidi 1. Via Perugia, 56 10152 Turin 2. Fincredit Confapi Via della Colonna Antonina, 52 00186 Rome
Contact name	
Mr Andrea Muti (Rome) Miss Alessandra Romano (Turin) Mr Andrea Giotti, Chief Executive Eurofidi Guarantee Consortium	
Date of set up	Web site and email
Forerunner to Eurofidi (Artigianfidi and Fidi piemonte) was set up in 1980. Fund has been operating as Eurofidi since 1999.	fincredit@confapi.it a.romano@eurocons.it www.eurocons.it
Total resources (€m)	Telephone
1.675 million euros of guaranteed loans at end of 2000	+39 06 69 015 312 (Rome) +39 011 24 19 234 (Turin)
1. Outline description of scheme	
<p>Eurofidi is a mutual guarantee fund providing loan guarantees to small and medium sized enterprises. With headquarters in Turin and 8 regional offices, it is the largest guarantee consortium in Italy, and the third largest in Europe. Its primary objective is to facilitate access to finance for SMEs in the Piedmont Region. It also assists financial institutions in screening loan applications and in risk management.</p> <p>Eurofidi has 16,000 SME members whose financial needs are served by 32 banks and 2 leasing associations which have underwriting agreements with the consortium. Eurofidi provides guarantees on short, medium and long-term loans, commercial paper and investment certificates. At the end of 2000, the guarantee consortium had issued guarantees on loans amounting to 1.675 million euros.</p>	
2. Sources of finance for scheme (Community, national, private)	
<p>Eurofidi provides guarantees to new SME start-ups under the European Investment Fund (EIF) backed SME Guarantee Facility. The EIF counter-guarantees up to 50% of the value of guarantees issued by Eurofidi.</p> <p>Eurofidi also collaborates with Mediocredito Centrale, the National Guarantee Fund for SMEs set up by the Italian Ministry of Industry. In common with the EIF, the National Guarantee Fund also provides counter-guarantees on guarantees issued by Eurofidi, further reducing the risk burden. Eurofidi receives some grant finance from the Piedmont Region.</p> <p>In terms of private sector contributions, half of the equity for the risk capital fund is provided through Eurofidi's mutual structure, i.e. through its 16,000 SME members. The remaining finance comes through public sector sources. Overall, the split between public and private sector financing is approximately 50-50.</p>	
3. Private capital return	
<i>Pari passu</i> with public capital	
4. Overall Targets	
No information available	
5. Target groups	
<p>Target groups include SMEs and micro-firms in the industrial, commercial, services, craft and tourism sectors. In terms of the sectoral split between different types of SMEs by loan guarantee size, the industrial sector (35%) accounted for the largest share of guarantees, followed by commerce (34%), small industry (22%), services (8%) and agriculture (1%).</p> <p>In terms of loan duration, 70% of guarantees issued by Eurofidi were medium to long term, whilst 30% were short-term.</p> <p>In terms of targeting in the micro-finance field, Eurofidi targets firms in the craft sector, which have particular credit needs and have historically found it difficult to access finance.</p>	

6. Terms of assistance (typical amount, time, terms of financing)

Eurofidi provides guarantees of up to 50% on total loan size. The Italian national guarantee fund provides a counter-guarantee that considerably reduces Eurofidi's overall level of risk. For example, if Eurofidi guarantees 50% of the loan value, the National Guarantee Fund for SMEs counter-guarantees 90% of the Eurofidi guarantee i.e. 45% of total loan value. This enables Eurofidi to significantly leverage its capital.

The maximum amount covered by loan guarantee depends on the duration of the loan. For short-term loans, the maximum is 250.000 euros, whereas for medium-long term loans, the maximum is 750.000 euros.

SMEs pay a small handling fee to Eurofidi when making a guarantee application. If this is approved, the firm then pays a fixed percentage to Eurofidi as a risk premium. For short-term loans, SMEs typically pay a 1.5% risk premium to Eurofidi in return for the guarantee. In the case of medium-long term loans, the premium is 3%. The risk factor doesn't influence the percentage fee paid by SMEs in exchange for the guarantee product but determines the amount of the loan Eurofidi is willing to guarantee. This normally amounts to 50% but could be reduced where the loan risk is particularly high.

The interest rate differential between the rate an SME would pay on the open market and that paid on a guarantee-backed loan is dependent on the risk of default, which is assessed by the financial lending institution. Standard parameters are applied across sectors and regions. In Piedmont, the interest rate differential is typically between 1-2%.

If an SME defaults on the loan, the guarantee fund immediately pays the creditor. The bank then pursues the SME for reimbursement on Eurofidi's behalf. When the new Basel Agreement on Capital Adequacy is implemented by banks, Eurofidi will have the right to pursue SMEs directly for payment.

7. Management arrangements

In order to operate loan guarantee schemes across the Piedmont region, Eurofidi management has established agreements with 32 banks and 2 leasing companies that provide access to credit to SME members.

Eurofidi is part of the Eurogroup and is a limited company. The *Eurogroup* is divided into three sub-branches, *Eurofidi*, which offers loan guarantees, *Eurocons*, which provides business support and consultancy services and *Eurobroker*, which provides consultancy on the insurance needs of SMEs.

Most of Eurofidi's employees (200 plus people) are engaged in marketing and promotional activities to affiliated banks and to potential and existing SME clients.

8. Key advantages of scheme

- Rigorous quantitative and qualitative pre-screening procedures and Eurofidi's in-depth knowledge of the business sectors in which clients operate helps reduce the level of risk for lending institutions
- The principal of risk sharing between the lending institution and Eurofidi significantly reduces the level of risk to financial institutions
- Improves SME access to finance where lack of collateral and track record are major obstacles to obtaining credit. Enables SMEs to access finance at preferential rates and to borrow more credit thus helping to level the playing field between SMEs and their larger counterparts
- Enables financial institutions to pool risk across a broad portfolio of loans with a significant percentage of loan value backed by guarantee
- The ability to revolve resources through reinvestment of part of the guarantee premium paid by SMEs into a risk capital fund
- Substantial private sector leverage effect of guarantee instruments. There is a high multiplier effect between the capitalisation of a fund and the total amount of loans it is able to leverage through utilisation of guarantees and counter-guarantees.
- The use of peer monitoring to assess potential risk of SME guarantee applications helps minimise rate of default. SME beneficiaries are both clients and members of the Eurofidi Consortium.
- Diversification into complimentary product areas benefits wider regional development objectives. For example, other business units within the umbrella organisation 'Eurogroup' can offer consultancy

services to SMEs on financial matters, the attainment of recognised quality standards (Eurocons), and on insurance-related matters (Eurobroker)

- Addresses market failure in banking system. Consolidation process in banking sector means that banks are less interested in maintaining and developing local and regional relationship banking. Eurofidi fills the gap
- Guarantee fund provides advisory assistance and help in dealing with the lending institution throughout the duration of the loan guarantee. For example, prior to an SME going to the bank to ask for a loan, Eurofidi carries out a critical assessment of the business plan. Similarly, if an SME encounters difficulty making loan repayments, Eurofidi deals directly with financial institutions on the SME's behalf in an intermediary capacity.

9. Results of any appraisals or evaluations

Comparatively low rate of default on loans backed by guarantees (1-3%) depending on business sector compared with traditional bank loans (7%)

10. Any other comments

In order for Guarantee funds to operate effectively, they need to be highly capitalised.

Once the cost of the loan plus the cost of the risk premium for the guarantee are added together, guarantee-backed loan finance is often as expensive as normal loan finance. The main benefit, however, is that an application made through a guarantee fund is seen as more credible than an application from an individual SME, partly because of rigorous risk assessment procedures, but equally because the SME may have little, if any collateral, and would not be able to access finance without the guarantee.

Case Study No. 9	
Brusoc micro-credits scheme - Belgium	
Region/country	Organisation and address
Bruxelles Capitale / Belgium	BRUSOC S.A 32, Rue de Stassart 1050 Bruxelles Belgium.
Contact name	
Ms Sophie Fétu	
Date of set up	Web site and email
April 2001 (micro credits), September 2001 (seed capital).	www.srib.be s.fetu@srib.be
Total resources (€m)	Telephone
€5m total budget (micro credits) for the 2000-06 period – support from Objective 2 Structural Funds €4m total budget (seed capital) for the 2000-06 period – support from Objective 2 Structural Funds	+33 (0)2 5482211
1. Outline description of scheme	
<p>BRUSOC ('Bruxelles sociale') provides micro credits to individuals looking to set up their own business and provides seed capital in the form of both equity and loans to micro-enterprises. BRUSOC targets the financially and socially excluded i.e. disadvantaged social groups such as refugees, ethnic minorities, the long-term unemployed and those on very low incomes. The primary objectives of the micro credit scheme are to encourage entrepreneurship and endogenous economic development, to regenerate deprived urban areas and to combat social and financial exclusion. The two ERDF-funded schemes support new and existing businesses located within the Objective 2 area of Bruxelles Capitale (population within eligible area - 350,000). Financial support is closely linked to the provision of business support and advisory services.</p> <p>An additional scheme is in operation with funding from national sources that provides assistance to companies pursuing social objectives such as placing the long-term unemployed on company training schemes.</p>	
2. Sources of finance for scheme (Community, national, private)	
Both the micro credits and the seed capital schemes operated by BRUSOC are eligible for ERDF funding. European funds are co-financed by the Belgian government and municipal authorities in Bruxelles Capitale.	
3. Private capital return	
Not applicable, the scheme is entirely funded by the public sector	
4. Overall targets (for current period)	
<p>There are no specific targets to be attained in terms of the number of individuals assisted etc. However, data is kept in respect of the following indicators;</p> <ul style="list-style-type: none"> - How many dossiers (potential applicants) have been dealt with - Number of successful applications compared with the total number of applications - Number of jobs created - Age and educational level of applicants 	

<ul style="list-style-type: none"> - For unemployed applicants, the length of unemployment - Gender of applicants (in support of principle of gender mainstreaming) <p>Currently, about one-third of enquiries regarding loans to micro-entrepreneurs or the self-employed lead to actual loans being made – the relatively low ratio is explained by the fact that many of those enquiring about the schemes are ineligible (either because they are not located within the Objective 2 eligible area or because they do not meet Belgium’s legislative requirements for new business start-ups (minimum of €6,200 capital plus requirement to have a <i>carte professionnelle</i>, which is only obtainable by Belgian nationals).</p>
<p>5. Target groups</p> <p>BRUSOC targets all disadvantaged social groups located within or willing to set up a business in the Objective 2 area of Brussels, Bruxelles-Capitale. Examples of the types of social groups targeted by BRUSOC includes refugees, ethnic minorities, the long-term unemployed and those on very low incomes.</p> <p>BRUSOC uses promotional literature to target individuals and micro-enterprises – leaflets are displayed in appropriate venues where target groups are likely to come across them. Examples include employment and unemployment offices, business centres and business incubators, NGOs, the municipal buildings and guichets de l’économie locale.</p>
<p>6. Terms of assistance (typical amount, time, terms of financing)</p> <p><i>Eligibility Criteria:</i> Applicants must be located in the Objective 2 eligible area or willing to locate their business within the area. They must not be able to obtain the loan from other sources such as a commercial bank loan and they must invest a symbolic fixed sum of money in the business in order to be eligible to apply.</p> <p><i>Micro-credits scheme:</i> BRUSOC typically lends over a three year period. Micro loans are made to individuals to set up their own business as a self-employed person – the amount lent ranges from €1,240 to €12,400 whilst the typical amount lent is between €8,000-10,000. Micro loans are lent at a flat rate of 4% - reflecting the subsidy from national and ERDF sources. As a symbolic gesture towards the principal of risk sharing and in order to demonstrate the degree of commitment of micro-credit applicants to their entrepreneurial idea, individual applicants must demonstrate that they are willing to invest a minimum of €620 of their own funds.</p> <p><i>Investment capital:</i> Investment capital in the form of either a loan or equity is available to both start-ups and existing companies – the amount lent ranges from €5,000 to €50,000. The typical amount lent is between €10,000 and €15,000. As a symbolic gesture towards the principal of risk sharing, SME applicants for loan or equity financing must demonstrate that they will be investing a minimum of €6200 of company funds</p> <p><i>Selection criteria / application procedure:</i> BRUSOC operates a four stage application process. Applicants are first vetted to determine whether they meet the geographic requirements of the schemes (i.e. are located or are willing to locate their business in an area qualifying for Objective 2 status) and whether they meet the necessary legal requirements (in Belgium, firms are required to have a minimum of €6,200 of capital in order to create an enterprise and all individuals must hold a <i>carte professionnelle</i> before they are allowed to trade). Assuming that applicants meet both the necessary eligibility criteria, a face to face consultation session is then organised. This focuses on an assessment of the project, its commercial viability and the personal circumstances of the applicant. Applications then go before a Management Board (<i>Conseil d’administration</i>) for consideration and approval. If the application is successful at Management Board stage, BRUSOC then draws up a formal business plan and carries out a small-scale market analysis on behalf of the applicant.</p>
<p>7. Management arrangements</p> <p>The Objective 2 Single Programming Document included a provision for the use of financial engineering instruments relating to ‘social finance’. The SPD was signed in July 2000 and applies to the 2000-06 programming period.</p> <p>BRUSOC is part of the umbrella SRIB group (<i>Société Régionale des Investissements de Bruxelles</i>), a quasi-public sector body that promotes start-ups and SME growth and development. The Belgian municipal government has delegated the management and implementation function of the micro-credits and investment capital scheme (social finance) envisaged in the Bruxelles-Capitale SPD under the ‘financial</p>

engineering for social capital' budget line to SRIB.
8. Key advantages of scheme
<p>Amongst the key attributes of the scheme are:</p> <ul style="list-style-type: none"> • Facilitates access to finance amongst disadvantaged social groups and redresses market failure through the targeting of the financially and socially excluded • Promotes a culture of entrepreneurship in a deprived area and amongst the socially excluded • Promotes sustainable local economic development. Makes an important contribution to urban regeneration i.e. the improvement and renaissance of run-down and socially and economically deprived areas; • Enhances the local community and encourages further investment (catalytic effect of micro-credits) e.g. by encouraging new shops to be set up which lead to physical improvements to buildings and in turn, contributes directly to improved quality of life for local people;
<ul style="list-style-type: none"> • Financial support to micro-entrepreneurs from BRUSOC is closely linked to the provision of ongoing advisory support and assistance (l'accompagnement) throughout the 3 year duration of the financing. Assistance is provided free of charge, reflective of the social aims of the scheme. Many of BRUSOC's clients have not received formal education or training - advisory support is therefore particularly beneficial when dealing with marketing/ administrative/ taxation/ accounting and legal issues. Whilst many applicants are highly creative, imaginative and entrepreneurial, they lack the formal know-how in terms of how to set up, develop and grow their own businesses; • Rather than setting up a new institution to manage and implement the micro-credits and investment capital schemes, the municipal government tapped into the expertise of a pre-existing institution with the necessary financial expertise and knowledge of the SME sector to administer the ERDF-supported scheme; • BRUSOC has established a network of public and private sector partner organisations that can provide specialist help when needed e.g. on accountancy and legal issues etc. BRUSOC provides generalist advice and some specialist support in-house
9. Results of any appraisals or evaluations
None
10. Any other comments
<p>Anecdotal evidence suggests that one of the difficulties with micro-credit schemes is that it is difficult to reach those most in need. Micro loan applicants have to be entrepreneurial, resilient and determined in order to succeed. Applicants have to undergo what can be a lengthy application process, particularly for those without Belgian or EU national status, as they are required by law to apply for a <i>carte professionnelle</i>, a process that can take several months. The regulatory environment for becoming self-employed and/ or setting up a company is quite complex and time – consuming in Belgium. This therefore puts off some of the target market from applying.</p>

Case study No. 10	
Hitelgarancia guarantee scheme – Hungary	
Region/country	Organisation and address
Budapest, Hungary	Hitelgarancia Rt. (Creditguarantee Co. Ltd.) Headquarters H-1053 Budapest, 2, Szép Street, Hungary
Contact name	
na	
Date of set up	Web site and email
Established in 1992 as joint undertaking between the Hungarian State, the Hungarian Venture Capital Fund, commercial banks, business federations and industry Guilds. The scheme has the strong backing and support of commercial banks in Hungary	www.hitelgarancia.hu http://www.hitelgarancia.hu/index_en.html (website in English) hgrt@hitelgarancia.hu
Total resources (€m)	Telephone
In 2001, Hitelgarancia Rt. issued over 6,800 new guarantee contracts worth in excess of EUR 354M of loan guarantee cover, which helped SMEs to secure total financing from new loans and bank guarantees of EUR 442M. The average guarantee issued by Hitelgarancia was approximately 68% of total loan size	Phone: + (36-1) 485 8300 Fax: + (36-1) 485 8320
1. Outline description of scheme	
<p>The primary objective of Hitelgarancia is to facilitate and improve access to finance for indigenous Hungarian small and medium sized enterprises (SMEs). Hitelgarancia makes unconditional guarantees on SME loans to banks. The scheme seeks to address market failure and is targeted at firms lacking the necessary collateral requirement to obtain credit and satisfy the risk assessment criteria of financial institutions such as banks and savings institutions.</p> <p>The objectives of the Hitelgarancia guarantee scheme can be summarised as;</p> <ul style="list-style-type: none"> ⇒ Improving SME access to finance, particularly where the entrepreneur has little in the way of capital/collateral ⇒ At a strategic level, fostering the development of the SME sector in line with Hungarian governmental economic development policy ⇒ Encouraging the financial sector to increase their propensity to lend to SMEs in general and micro-firms in particular ⇒ Assisting in the continuing development and expansion of the Hungarian banking sector by encouraging SME-led economic growth 	
2. Sources of finance for scheme (Community, national, private)	
<p>The scheme is financed by the central budget and by Hitelgarancia itself. In terms of the corporate structure, 50% of the shares in Hitelgarancia plus one vote are owned by the Hungarian State with the remaining part of the share capital owned by commercial banks, the Hungarian Venture Capital Fund, Business Federations and various industry guilds. The private sector, whilst making an important contribution through their continuing support for the Hitelgarancia guarantee scheme and the screening of applications, does not contribute directly financially.</p> <p>No Community funding is currently available although if Hungary were to join the EU as part of a first wave of countries in 2004, it is possible that Objective 1 funding may be available throughout most of Hungary as well as the possibility of eligibility for EIF counter-guarantees, which takes liabilities off the balance sheet and improves leverage ratios.</p>	

3. Private capital return

Hitelgarancia can guarantee up to 80% of the loan total. In case of loans guaranteed by Hitelgarancia banks / savings co-operatives must assume the risk for at least 20% of the total investment.

4. Overall targets (for current period)

- 2003: €478m (traditional loans) plus guarantee volume related to Szechenyi Card €113m
- 2004: €531m (traditional loans) plus guarantee volume related to Szechenyi Card €202m
- 2005: €598m (traditional loans) plus guarantee volume related to Szechenyi Card €236m

NB: The Szechenyi Card is a brand new product offered by Hitelgarancia and commercial banks to SMEs. The Szechenyi Card is a credit card (overdraft facility) that is aimed at quick settlement of the temporary liquidity problems of individual entrepreneurs and micro, small and medium-sized enterprises. The credit card facility is backed by Hitelgarancia Rt.'s guarantee.

Targeted number of guarantee contracts in the next three years:

- 2003: 8,000 pcs (traditional) + 25,000 pcs (Szechenyi Card)= 33,000
- 2004: 8,600 pcs (traditional) + 30,000 pcs (Szechenyi Card)= 38,500
- 2005: 9,300 pcs (traditional) + 35,000 pcs (Szechenyi Card)= 44,300

Estimated default rate in the next three years (2003-2005): approx. 4%

Estimated leverage effect: 2003: 1:1.47 2004: 1:1.51 2005: 1:1.59

5. Target groups

In terms of targeting, the scheme seeks to address market failure and is aimed at those SMEs and micro-firms that could not otherwise obtain a loan based on normal commercial lending criteria – due to lack of collateral, poor credit rating or the degree of risk involved. The provision of guarantees to micro-firms seeking loans is particularly encouraged. In 2001, 34% of loan guarantees out of the total number of contracts were made to micro-firms, whilst 36% were made to firms with between 10 and 49 employees.

Hitelgarancia targets its support at those companies seeking guarantees on investment loans – however, guarantees in respect of working capital loans and loans to cover operational costs are also considered.

With regard to eligibility criteria, the following individual or joint undertakings are eligible to apply for assistance a) micro enterprises, b) SMEs c) co-operatives.

Key eligibility criteria are set out below;

- ⇒
- ⇒
- ⇒
- ⇒
- ⇒
- ⇒
- ⇒
- ⇒

There is a conscious sectoral-orientated approach, as Hitelgarancia does not provide guarantees for the companies operating in transportation / forwarding business and the firms involved in direct export business. In practice, there has also been a concentration of loan guarantees made in certain sectors, representative of wider economic trends in Hungary. Most of the guarantees (approximately EUR 122M) were provided to companies in the trade sector. The proportion of guarantees granted to businesses in the food and service sectors (22% and 18% respectively) has also been considerable.

6. Terms of assistance (typical amount, time, terms of financing)

With regard to the terms of the guarantee, Hitelgarancia is able to guarantee up to a maximum 80% of the total loan amount, the amount which Hitelgarancia is able to guarantee is dependent on an assessment of the guarantee risk. There is no minimum amount stipulated. The bank's own risk varies depending on the

percentage of the loan guaranteed but can be as low as 20% on loan in question.

Minimum collateral required:

- ⇒
- ⇒

Hitelgarancia is liable for 30% of total potential losses resulting from guarantee liabilities whilst the remaining 70% is backed by a counter-guarantee from the Hungarian state. One special feature of the Hungarian system is that by law, defaults on loans must be repaid by the guarantor institution within 8 days of receipt of the default notice. The provision by the SME of some form of collateral is a pre-requisite to obtaining the guarantee – however, the exact percentage of the loan demanded as collateral as a pre-condition for the guarantee is determined by the degree of risk involved.

The types of loans which can be covered by a Hitelgarancia-backed guarantee include the following;

- Working capital loans,
- Current account loans,
- Complementary working capital loans,
- Investment and development loans,
- Entrepreneur's credit lines and;
- Bank guarantees.

In terms of the duration of the guarantee, Hitelgarancia issues guarantees on both long and short term bank loans. The loan itself is often procured from the financial institution on more preferential terms than would have otherwise been the case considering the poor credit rating of the typical SME applicant. The maximum duration of a guarantee is 15 years

Hitelgarancia charges a fee in respect of the guarantee issued to the SME to cover inherent risk – there is the possibility of a guarantee fee subsidy of up to 50% for loans not exceeding €165,000.

The table below sets out the risk management scoring system adopted to assess loan applications requiring a guarantee.

Loan Risk management

Up to EUR 124,000	Simple scoring
EUR 124,000 – EUR 413,000	Scoring, simplified risk analysis
Over EUR 413,000	Scoring, risk analysis, on-site survey. No secondary credit assessment

Hitelgarancia charges a fee in return for the issuance of a guarantee to reflect the inherent risk involved and to cover losses from default. The fee rates depend on the duration of the loan and other factors. There is a minimum guarantee fee however of 1,000 HUF.

Fee rates for guarantee applications submitted after 1st January 2003 are as follows:

Guarantee Fee Rates					
Duration of guarantee	Up to 1 year	1 – 3 years	3 – 6 years	6 – 10 years	Over 10 years
Fee applicable for guarantee in % (in case of annual payments)	1.2%	1.2%	1.2%	1.6%	2.0 – 3.0%
In case of lump sum, up-front fee payments		1.8%	3.0%	3.6%	5.0%
7. Management arrangements					
<p>The scheme is operated and administered by Hitelgarancia directly in conjunction with the private sector. The necessity or otherwise of a Hitelgarancia-backed guarantee is determined by the financial institutions (usually banks and savings co-operatives) screening applicants. Financial institutions deal directly with the SME and if deemed necessary will submit applications to Hitelgarancia in instances where the SME has insufficient capital to obtain access to credit based on normal commercial lending criteria.</p>					
8. Key advantages of scheme					
<ul style="list-style-type: none"> • Hitelgarancia plays a role in supporting the Hungarian SME sector more widely and therefore makes a valuable contribution to Hungarian government economic policy • Facilitates SME access to finance • Inter-linkages between the guarantee scheme and government-funded business support organisations help SMEs to derive maximum benefit from the guarantee scheme by ensuring that the provision of finance is tied in to the provision of business support services. The holistic approach to SME development has been proven to be more successful than a disjointed approach • The guarantee scheme embodies the risk sharing principal between the public and private sector which encourages the private sector to lend to SMEs and micro-firms and to generally improve SME access to finance • Provides one of the few alternatives open to SMEs/ micro-firms lacking the necessary capital to secure credit • From the financial sector’s perspective, rapid guaranteed payment (within 8 days of default on a loan) encourages private sector to participate in the scheme • Improved loan terms on preferential rates for SMEs (although this benefit is counter-balanced against the fee for the issuance of the guarantee) • The scheme demonstrates a good leverage effect. In 2001, Hitelgarancia Rt. guaranteed EUR 354M worth of loans, which enabled Hungarian SMEs to borrow a total of EUR 442M from financial institutions, a leverage effect of 1:1.2 					
9. Results of any appraisals or evaluations					
NA					
10. Any other comments					
<p>As banks have become more familiar with Hitelgarancia’s guarantee product, there has been a greater propensity amongst financial institutions towards a) recourse to the guarantee product itself and b) lending money to small and medium-sized enterprises. This trend has been accelerated by speedy decision-making processes and favourable guarantee fees.</p> <p>From time to time the Transport Ministry and the Ministry of Finance invites Hitelgarancia to participate in different SME support programs for SMEs. A good example of this is the 50% state guarantee fee subsidy granted to SMEs by the Ministry of Economy and Transport on loans not exceeding HUF 40 million (approx. EUR 165,000).</p>					

Case study No. 11	
Fundusz Mikro scheme (micro-finance scheme) – Poland	
Region/country Poland	Organisation and address Fundusz Mikro Sp. z o.o. ul. Żurawia 22, 00-515 Warszawa, Poland.
Date of set up 1994	
Duration No time limit	Web site Website: www.funduszmikro.com.pl Email: fm@funduszmikro.com.pl
Total resources (€m) \$20m	Telephone/ Fax tel. +48 (022) 629 00 92, fax +48 (022) 628 88 11
1. Outline description of scheme	
<p>Fundusz Mikro was established in 1994 by the Polish American Enterprise Fund (PAEF) to promote the development of micro-enterprises in Poland. The fund was launched with funding from PAEF of USD 20 million for loan capital supported by a USD 4 million grant from USAID to cover fund set-up costs. The fund disbursed its first micro-loan in February 1995. The fund seeks to provide finance to those micro-firms or individual entrepreneurs that have had difficulties obtaining access to finance from banking institutions.</p> <p>Fundusz Mikro operates through a network of 31 branches located in cities across Poland. Fundusz Mikro also has information points located in surrounding rural areas. To date, upwards of 27,000 Polish micro-enterprises have benefited from loans amounting to more than €96 million.</p> <p>Fundusz Mikro is registered as a limited liability company - the only legal entity that enables institutions in Poland not registered as a bank to grant interest-bearing loans.</p>	
2. Sources of finance for scheme (Community, national, private)	
The scheme is financed by the Polish American Enterprise Fund (PAEF) to promote the development of micro-enterprises in Poland.	
3. Private capital return	
Not applicable	
4. Overall targets (for current period)	
Fundusz Mikro does not set any specific quantifiable targets.	
5. Target groups	

The scheme provides micro-loans to three distinct groups.

- ⇒ Loans for micro-businesses operating in urban and rural areas
- ⇒ Micro loans to start-up companies
- ⇒ Loans for associations set up to make small Community-based investments

Fundusz Mikro keeps statistics in respect of certain key indicators which it uses to monitor its activities. These include the proportion of loans distributed to women (40%) and to men (60%). Fundusz Mikro also keeps data on the breakdown of businesses by industry type: 55% of loan recipients were trade-based, 35% were services-based and the remaining 10% were industrial firms. In terms of the intended purpose of the loan, 31% of loans are used to fund working capital requirements whilst 69% are used for investment purposes.

6. Terms of assistance (typical amount, time, terms of financing)

The amount of the initial micro-loan must not exceed €2,500. On average, the amount of the initial loan is typically approximately €1,500. Following repayment of the first loan, entrepreneurs are entitled to apply for another larger loan (up to 50% more than the initial loan) provided the loan recipient has repaid all installments of the preceding loan on time.

Loans are granted for a period of not longer than 1 year. A grace period or payment suspension of up to 3 months is possible, if, for example, the business is experiencing cash-flow problems. The average interest payment on short-term loans is 22% on an annual basis, but this depends on the duration of the loan and the extent to which Fundusz Mikro has previously had dealings with the company. The 22% average rate charged by Fundusz Mikro compares with a typical interest rate charged by Polish financial institutions of between 16% and 23% per annum – this is usually combined with a set-up fee on the loan of between 1 and 4% of the loan amount. However, whilst traditional bank finance can be considered marginally cheaper than borrowing from Fundusz Mikro, financing from traditional sources is generally not an option to micro-enterprises, due to onerous collateral requirements.

In cases where the firm has a consistent track record of making regular loan repayments, it is more likely that a preferential interest rate will be given. The maximum loan the scheme can offer under normal circumstances is €7,000. Regular customers who have already drawn several loans from Fundusz Mikro and who have maintained regular loan repayments can access loans for higher amounts at special low interest rates. In addition to paying the interest on the principal, borrowers must also pay an administrative fee to Fundusz Mikro amounting to 2% of the sum of the loan at the time of the loan being taken out. This fee is reduced to 1% in the event of subsequent loans if the preceding loan has been repaid on time.

In terms of eligibility criteria for a micro-loan, the main preconditions for obtaining a loan are first that the firm must be conducting a legal business activity and secondly that the applicant must provide cash flow projections that demonstrate the borrower's ability to repay the loan. Loan officers carry out a cash flow projection of the applicant firm based partly on the applicant's own assessment and partly on critical assumptions based on the historical performance of similar firms operating in the same or a related sector. The appraisal process also takes into consideration the firm's future growth and development prospects and the business skills and commercial acumen of the owner.

Fundusz Mikro does not require proof of income from micro-loan applicants and relies instead on income declarations made by applicants and on a credit assessment made by Fundusz Mikro loan officers.

In terms of collateral requirements, the loan is conditional upon a guarantee being signed by a minimum of three individuals. This applies to both individual and group loans. In the case of individual loans, the three guarantors must be able to demonstrate sufficient income making it possible for them to lend assistance to the borrower if the borrower encounters repayment problems. Within the framework of group loans, all guarantors are simultaneously borrowers.

Since the scheme's inauguration in 1994, a total of 27,095 micro-firms have been assisted of which 8,637 are current clients (the remainder having paid off their short-term loans). To date, the scheme has only had a 4% default rate on loans.

7. Management arrangements

Fundusz Mikro operates through a network of 31 branches located in most large cities in Poland.

Branches are managed by branch managers, who in turn are in charge of between 1 and 4 loan officers. The branch manager is responsible for the entire portfolio of loans. Loan officers do not have their own portfolios of customers and each of them may be directed to carry out any loans, depending on current requirements. Individual branches are responsible for:

- Providing information about the micro-credits scheme to as large a number of entrepreneurs as possible
- Establishing long-term co-operation with entrepreneurs wishing to take advantage of the scheme
- Carrying out loan risk analysis
- Taking decisions on loan applications
- Signing loan agreements and sending these to head office
- Taking appropriate steps with regard to borrowers who do not repay their loans.

Branch managers are in turn responsible to the Operations Director and to senior managers at head office. They additionally receive help from 5 operational coordinators, who are also responsible to the Operations Director.

A division composed of 5 individuals handles the administration of loans. Approximately 10,000 repayments are administered each month in respect of existing loans. Several hundred new loans are also disbursed each month. The system conducts all account settlements automatically. The Administration division sends all branches reports on late repayments, which makes it possible for branch managers to take appropriate steps as soon as any delayed payments are identified.

Fundusz Mikro has approximately 100 employees.

8. Key advantages of scheme

- Facilitates access to capital for micro-firms which would otherwise have encountered difficulties in securing borrowing from financial institutions due to lack of collateral.
- The finance package offered by Fundusz Mikro is offered on straight-forward terms which are easy for micro-entrepreneur to understand – there is also minimal administration and bureaucracy for the micro-firm loan applicant.
- Fundusz Mikro applies a decentralized approach to decision-making in terms of the disbursement and granting of loans. This allows managers to build relationships with entrepreneurs over time, many of whom come back for additional loans to fund investment. It also helps minimize risk by ensuring that loan officers and branch managers know their customers, which would be impossible if the scheme were to be administered centrally
- Management Information Systems data is fed directly back to branch level which means that late payment problems are identified quickly. This means that loan officers can contact defaulters quickly and attempt to resolve any problems the micro-entrepreneur might be having. This helps to keep the default level down to an absolute minimum. The default rate on micro-loans disbursed is 4.0%.
- Rigorous screening procedures to minimise the risk of loan default. Loan assessors look at the loan from both the perspective of Fundusz Mikro as a lending institution and from the micro-firm's perspective. A risk assessment is first carried out by Fundusz Mikro of the applicant firm's ability to repay the loan and then a further analysis is carried out which focuses solely on the likely benefits to the entrepreneur of accessing the micro-loan
- Loan assessors at Fundusz Mikro believe it is important to ensure that borrowers benefit from loans as well as simply assessing whether they are able to pay them back. There is an important educational dimension to the loan assessor's role since there is often a lack of business skills amongst potential new entrepreneurs in Poland.

9. Results of any appraisals or evaluations

Fundusz Mikro's accounts have been audited every year by Arthur Andersen. This year they will be audited by Ernst and Young.

10. Any other comments

The objectives of the scheme have been defined by Fundusz Mikro as to:

- ⇒ Create opportunities for the development of entrepreneurship by providing access to capital on the basis of an assessment of the entrepreneurial capabilities of the loan applicant.
- ⇒ Assist as many possible entrepreneurs with growth and development potential as possible.
- ⇒ Minimise financial risk
- ⇒ Minimise the rate of loan default by rigorously screening micro-loan applications from entrepreneurs
- ⇒ Support the education process for entrepreneurs through joint assessment of investment plans and calculation of business returns and risks.
- ⇒ Support social capital by encouraging successful entrepreneurs who benefited from micro-loans to act in a mentoring capacity to other new entrepreneurs and to promote the micro-finance concept more widely

Fundusz Mikro is a member of the Micro Finance Network, an international organization of leading microfinance programs. Fundusz Mikro is also a member of the Micro Finance Centre for Central and Eastern European countries and the International Leaders Forum on Development Finance established by the Ford Foundation.

Case study No. 12	
LINC Scotland, Business Angels – UK	
Region/country	Organisation and address
UK	LINC Scotland Queens House 19, St Vincent Place Glasgow G1 2DT
Contact name	Web site
na	www.lincscot.co.uk/index2.htm
Date of set up	Telephone
1994	+44 141 221 3321
Total resources (€)	
N.A.	
1. Outline description of scheme	
<p>LINC Scotland was set up in 1994 to bring together small companies in search of finance and business expertise with private individuals prepared to invest money, time and business skills in exchange for an equity stake. Such individuals are often called Business Angels and the process is referred to as informal investment. LINC Scotland itself operates a not-for-profit, business introduction network or "marriage bureau" for companies and investors. It also works to support the overall development of the business angel marketplace in Scotland through awareness raising and educational/training activities. Its work is supported by a wide range of public and private sector organisations. The scheme operates nationwide in terms of recruitment to its angel database but individual investment facilitation schemes based on the LINC Scotland model have been set up in each of the eligible Objective areas across Scotland.</p> <p>For a number of years, LINC Scotland has received financial support from ERDF towards its operational costs. The scheme was one of the first in Europe to receive financial support from ERDF. No public money is used to support investments directly – rather, the role of the Angel network is to act as a facilitator between businesses seeking investment and Angel investors.</p>	
2. Sources of finance for scheme (Community, national, private)	
<p>ERDF provides up to 50% of the operational cost of running the Angel network in eligible areas. Local co-funding is made up of both public (Scottish Enterprise) and private sector sponsorship. ERDF is not used to fund investment directly but to support the network – which matches private sector investors and small firms seeking equity.</p>	
3. Private capital return	
N.A.	
4. Overall targets (for current period)	
<p><i>LINC Scotland sets targets and keeps monitoring data in respect of the impacts of matched angel investments where ERDF funding has been used to support LINC Scotland's operational costs. Monitoring data is kept in respect of the number of projects assisted, the number of jobs created (which can only be properly measured over the longer term) and the amount of private sector investment leveraged.</i></p>	

Target January 2002-March 2004					
Area	Advised	Invested in	Jobs	Private Sector Leverage (£)**	ERDF Contribution (£)
East Obj. 2	124	20	345	4,000,000	223,397
East Transition	103	13	234	2,600,000	115,847
Strathclyde Ob. 2	162	27	347	4,150,000	386,883
TOTAL	445	69	1033	12,500,000	783,216
<i>Achieved to 31.12.02</i>	<i>81</i>	<i>22</i>	<i>207</i>	<i>12,279,000</i>	...
<p>** Private Sector Leverage = direct Angel investment + other private investment levered by their intervention as deal leader.</p> <p><u>Notes on variances:</u></p> <ul style="list-style-type: none"> • Number of projects handled is less than projected due to economic downturn but quality has been more consistent, so 'hit rate' (i.e. proportion achieving investment) is better than 1 in 4 as opposed to the projected 1 in 6.5 which was based on previous experience. • Average deal size is much greater than predicted due to the business angel sector having to fill the gap left by formal VCs retreating further up the market to higher value deals. • Jobs impact will not be determined until at least 12 months after end of the project so current pro rata position seems satisfactory. There is inevitably a time lag between making an investment and job impacts materialising. 					
5. Target groups					
<p>SMEs inside eligible Objective areas (although LINC Scotland also provides a limited service outside eligible areas). Three main types of potential recipients of angel financing can be distinguished:</p> <ul style="list-style-type: none"> • Start-up companies requiring equity investment that are too early stage to attract mainstream venture capitalists because product and/or market are not yet proven. • Young companies requiring amounts of equity investment that are too small to interest mainstream venture capitalists because of disproportionate cost for VCs in participating in small deal sizes, i.e. under £500K • Established businesses which recognise the need to strengthen their board or management team, as well as their balance sheet, to sustain successful growth and development. 					
6. Terms of assistance (typical amount, time, terms of financing)					
The Angel network acts as a facilitator of equity investment and therefore does not make investments directly in its own right					
7. Management arrangements					
NA					

8. Key advantages of scheme

- Significant leverage effect of European money – the amount invested by ERDF / other public sources is very small when compared to the level of private sector investment leveraged through the angel network. However, a caution is needed in that Angel introduction networks do not make investments directly so the leverage effect inevitably appears high compared with more direct forms of intervention.
- While failure rates have been relatively high (but comparable with those of formal venture capital) due to the high risk nature of the types of companies invested in, the rewards can be very high both for the angel investor and for the wider community from an employment and wealth creation perspective
- Angels bring business skills and experience to small businesses - since they tend to invest in sectors they understand, angels can be an important source of advice and mentoring for the management of innovative or technology-based businesses. This kind of added value can give the company a real edge over its competitors.
- Credibility and leverage - with their track record of business achievement, having business angels on the Board of an SME increases the likelihood of securing additional funding. Equity finance also has advantages over debt finance in that it helps to strengthen the balance sheet of the business, a key driver for supporting future growth and for leveraging funds from other sources. Quite often the angels have the financial skills and contacts to help bring the whole package together.

9. Results of any appraisals or evaluations

- A review undertaken recently of investments made up to the end of 1998 (i.e. sufficient time has elapsed for outcomes to be known) revealed that of 61 deals matched by LINC Scotland, 24 firms subsequently went out of business – reflecting the high risk nature of investments.
- However, more positively, the remaining firms collectively employ 3,500 people –illustrative of the high risk - high reward nature of Angel investing.

10. Any other comments

No

