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CIP □ EU FINANCIAL INSTRUMENT FOR SMALL AND MEDIUM SIZE ENTERPRISES

Abstract

This paper presents CIP (Competitiveness and Innovation Programe) as a framework for gurantie facilitiy for SMEs (Small and Medium Sized Enterprises) founded by European Community and European Investment Found. Small and Medium Sized Enterprises constitute the basis of the European economy. They play a remarkable role for regional adjustment to the economic globalisation for innovation, economic growth and employment within the EU. National and regional authorities have to ensure a favourable environment for SMEs, including innovative ones, by developing SMEs support programes and facilitating their access to finance. It can be a great opportunity for financing Serbian Small and Medium sized Companies in the future if the Government established appropriate intermediar institution. In that way Serbian SMEs will increasing their access to finance and risk capital which enables them to tap their growth and innovation potential and achieve competitiveness.

Key words: CIP, SMEs, Competitiveness, Economic Growth

INTRODUCTION

Small and Medium Sized enterprises (SMEs) are the backbone of all economies and are a key source of economic growth, dynamism and flexibility in advanced industrialized countries, as well as in emerging and developing economies.[1] SMEs constitute the dominant form of business organization, accounting for over 95% and up to 99% of enterprises depending on the country. They are responsible for between 60-70% net job creations in OECD countries. Small businesses are particularly important for bringing innovative products or techniques to the market. Fostering the competitiveness of SMEs is a general goal of the CIP. Moreover, SMEs are a particular target group in the entrepreneurship and innovation program which includes high-tech SMEs and traditional micro-and family firms, covering the industrial and services sector. The program consists of two SME related actions: firstly, providing access to finance and secondly encouraging SME cooperation.

1. IMPORTANCE OF FINANCING SMALL AND MEDIUM SIZED ENTERPRISES

SMEs are vital for economic growth and development in both industrialized and developing countries, by playing a key role in creating new jobs. Financing is necessary to help them set up and expand their operations, develop new products, and invest in new staff or production facilities. Many small businesses start out as an idea from one or two people, who invest their own money and probably turn to family and friends for financial help in return for a share in the business. But if they are successful, there comes a time for all developing SMEs when they need new investment to expand or innovate further.

In some OECD countries such as in Belgium, Ireland, Italy, Portugal and the United Kingdom, small manufacturing firms are almost as innovative as large firms. [2] Similarly in services, small firms in some OECD countries, for example in Portugal, Switzerland and the United Kingdom are equally innovative as large firms.

That is where they often run into problems, because they find it much harder than larger businesses to obtain financing from banks, capital markets or other suppliers of credit. This “financing gap” is all the more important in a fast-changing knowledge-based economy because of the speed of innovation. Innovative SMEs with high growth potential, many of them in high-technology sectors,

have played a vital role in raising productivity and maintaining competitiveness in recent years, but innovative products and services, however great their potential, need investment to flourish. If SMEs cannot find the financing they need, brilliant ideas may fall by the wayside and this represents a loss in potential growth for the economy.

In most countries, commercial banks are the main source of finance for SMEs, so if the SME sector is to flourish it must have access to bank credit. The characteristics of the banking system in emerging markets frequently inhibit SME lending. Many banks are state-owned; their credit may be allocated on the basis of government guarantees or in line with government targeting to develop specific sectors. Often banks are subject to ceilings on the interest rates they can charge, which make it difficult to price credit in a way that reflects the risk of lending to SMEs. Many banks may have ownership and other ties to industrial interests and will tend to favor affiliated companies. In a market where banks can earn acceptable returns on other lending, it will not develop the skills needed to deal with SMEs.

2. THE COMPETITIVENESS AND INNOVATION PROGRAM (CIP) AS A CHANCE FOR FINANCING SMES

As alluded to earlier, innovative SMEs find it difficult to obtain access to various sources of financing. However, each growth phase has different financing requirements. The CIP (Competitiveness and Innovation Program) is a bundle of measures to support the Lisbon agenda, with the goals to increased competitiveness and growth.

With a total budget of over € 1.1 billion, the CIP Financial Instruments should enable financial institutions to provide about € 30 billion of new finance for up to 400 000 small businesses in Europe. Predecessor program have benefited more than 360 000 SMEs.

In the table below are represented the major themes of the CIP and their budget. [3]

Table 1: Some major CIP themes and their budgets

Facilitate access to finance for SMEs	€ 1129 million
Support services for enterprises (especially SMEs)	€ 338 million
Promotion of Innovation and particularly eco- innovation	€ 585 million
ICT interoperability and up- take	€ 728 million
Energy issues (e.g. efficiency, renewable)	€ 727 million

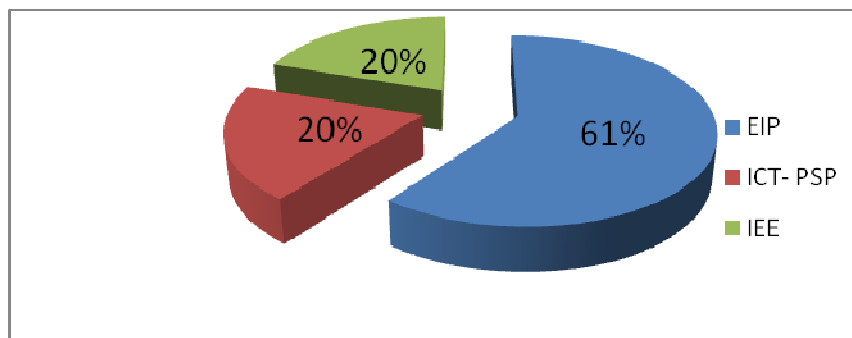
Financial instruments address SMEs' needs for financing at various stages of development. They cover areas of the market where there are few private investors, mainly the seed, start-up, expansion and business transfer phases. These instruments increase the investment volumes of risk capital funds and provide guarantees for lending to SMEs. [5]

The three specific programs in the CIP framework are [4]:

- Entrepreneurship and Innovation Program
- ICT Policy Support Program
- Intelligent Energy-Europe Program

A breakdown of the CIP budget is shown in the figure below:

Figure: Breakdown of the CIP Budget



Source: CIP Fact Sheet

The program consists of two SME related actions: firstly, providing access to finance and secondly encouraging SME co-operation. The financial instruments consist of:

- *The High Growth and Innovative SME Facility (GIF)* contributes to the establishment and financing of SMEs and the reduction of the equity and risk capital market gap
- *The SME Guarantee (SME G) Facility* provides counter- or co-guarantees for guarantee schemes as well as direct guarantees (including debt financing, micro credits etc)
- *The Capacity Building Scheme (CBS)* improves the investment and technology expertise of funds investing in SMEs, enhancing the credit appraisal procedure for SME lending.

Concerning research, the CIP will focus on downstream aspects (closer to market) and the innovation process, promoting innovation support services for technology transfer and use, projects for the implementation and market take-up of technologies, including ICT. One concrete example is the Galileo Project, where innovative SMEs could develop applications for the Galileo satellite positioning system for logistics, transport, safety or security services.

The main difference between CIP and FP7 (The Seventh Framework Program for Research and Development) is presented in table below:

Table 2: The main difference CIP versus FP7 [5]

PROGRAMME	SUB PROGRAMME	SME OPPORTUNITY
FP7	Cooperation	SMEs can participate in projects in 9 area, higher co-financing, simplification of procedures, 15 % of the total budget is reserved for SMEs
	Ideas (basic research)	SMEs can participate in basic research
	People (mobility)	Industry-academia, partnerships
	Capacities (infrastructure, clustering and others)	Funds for SMEs to outsource research
CIP	ICT Policy Support	SME can participate
	Entrepreneurship and Innovation	Funding instruments for SMEs

3. INTERMEDIARIES AND SELECTION PROCESS AS BASIC CONDITIONS FOR CIP

The CIP financial instruments are not directly available to SMEs but implemented by the European Investment Fund (EIF) and selected financial institutions. EIF manages the program on behalf of the

Commission with the aim reaching as many growing SMEs as possible. Small businesses can contact selected national financial institutions to get access to investments or guaranteed lending.

For venture capital, EIF invests in funds focused in early and expansion stage or specialized sectors, particularly eco-innovation. In these cases, EIF is usually a cornerstone investor. For guarantees, the EIF establishes risk-sharing arrangements with intermediaries that provide finance directly to SMEs, such as banks, or with intermediaries that issue guarantees for the benefit of lending institutions.

An intermediary is an originator or any other party undertaking to establish an Additional Portfolio. Intermediaries shall be established and be operating in one or several Participating Countries and will be selected among banks, leasing companies, guarantee schemes, special purpose entities ("SPEs"), micro finance institutions and any other financial institutions committed to SME financing.

Intermediaries shall be selected in conformity with best business and market practices in a fair manner, avoiding any conflict of interest. On the basis of a call for expression of interest proposals will be examined by the EIF, on a continuous basis, using professional analysis and judgment taking into account these Guarantee Policy and Operational Guidelines. Proposals will be considered for approval by the EIF and the Commission, after satisfactory evaluation and pre-selection by the EIF, within the constraints of the available Community budget allocations.

Intermediaries shall be selected having regard to the following selection criteria, in no particular order of priority:

- The financial standing and operational capability of the Intermediary, and its ability to manage risk, service the Securitized Portfolio (as defined below) and to comply with the terms and conditions of the SME Guarantee Facility;
- The Intermediary's willingness and ability to originate the Additional Portfolio;
- The Intermediary's overall commitment to SME financing;
- The extent to which an EU Guarantee would enhance the Intermediary's access to capital markets;
- The extent to which the Additional Portfolio includes SME Financing granted to finance investments, transfer of business, as well as mezzanine financing and/or other quasi-equity instruments;
- The extent to which the Securitized Portfolio and/or the transaction structure contain, especially in the case of experienced Intermediaries, innovative features, such as:
 - i. less customary underlying assets (e.g. mezzanine financing or other equity-related instruments, bonds issued by SMEs, micro-credit instruments, etc.);
 - ii. underlying assets originated in different countries or in countries where the securitization market is considered relatively less developed;
 - iii. Multi-seller origination.
- the extent to which the Securitized Portfolio includes SME obligors;
- the willingness to accept the criteria for Enhanced Access to Finance

The selection of Intermediaries shall be based on market conditions and practices in the relevant country or region, in particular regarding the credit quality and risk diversification of the Securitized Portfolio.

4. IMPLEMENTATION OF CIP

According to the 2008 Implementation Report of the Competitiveness and Innovation Framework Programme (CIP), the budget committed to the EIP- Financial Instruments was 151.18 million €, to the EIP- Competitiveness of SMEs was 137.69 million €, to the ICT- PSP 44.48 € million and to the IEE was 70.22 € million. Therefore, the total budget committed achieved 403.57 million € [3]

In the framework of the EIP, by the end of 2008, following results had been represented:

Improvement of access to finance for the start- up and growth of SMEs, including investment to innovation activities, was provided mainly by the Community financial instruments. In 2008, more than 153 million € were committed and 28 innovative companies with high- growth potential were supported via *The High growth and Innovative SME Facility (GIF)*. Also, 14 transactions with financial intermediaries from 10 countries had been approved.

By the end 2008, 26.269 loans to 24.551 SMEs were supported and 12 deals with financial intermediaries from 9 countries, committing 110 million € for guarantees (or counter-guarantees), had been approved by the *SME Guarantee Facility (SME G)*. [3]

Third financial instrument the *Capacity Building Scheme (CBS)* had shown no response from the market and the Commissions services currently examining the possibility to re-allocate the budget to technology transfer and eco-innovation.

The official launch of the Enterprise Europe Network, a network of services in support of business and innovation, received high visibility with more than 1000 participants and covered EU 27 countries, the EEA countries, candidate countries, countries of the Western Balkans (Montenegro, Serbia, Bosnia and Herzegovina) and other third countries (Chile, China, Egypt, Israel, Russia, USA etc.). In 2008, nearly 81 million € was committed to the activities of the Enterprise Europe Network.

In area of policy analyses, development and coordination such actions as the SME performance review, entrepreneurship education actions, Corporate Social Responsibility measures etc. were undertaken, with the 6.7 million budget committed.

The ICT- PSP Programme

The ICT- PSP in 2008 was mainly based on two themes: ICT for user-friendly administration, public services and inclusion and ICT for energy efficiency and sustainability in urban areas.

Twenty retained proposals (from 66 received) for budget of € 40 million, provided a very good coverage of the themes and objectives addressed, involving public authorities, private companies and standardization bodies among the participants. Overall, 40% of participants in the selected proposals of the Call were represented by public bodies, almost 25% were represented by SMEs and 15% were large enterprises and the other entities.

The IEE Programme

The Call for proposals 2007, in the framework of the IEE, attracted 97 SAVE proposals (SAVE is action for fostering of energy efficiency and the rational use of energy resources). Eleven of which were selected for funding with 11 million € budget committed. Under ALTENER (which aimed at promoting new and renewable energy sources and to support energy diversification) 95 proposals were submitted with the 17 million € budget allocated. And under STEER (aimed at promoting of energy efficiency and the use of new and renewable energy sources in transport) 6 proposals were selected for funding, representing more than 8 million €.

It can be concluded that during the second year of operation of the CIP most of the instruments and actions had been established. The financial instruments and the European Enterprise Network were fully operational and supporting European SMEs, pilots and thematic networks were selected through a call for proposals involving a large number of public bodies and SMEs. Also, there was a high proportion of SMEs among private beneficiaries and the calls benefited from the active involvement of applicants from all participating countries.

CONCLUSION





Small and Medium Sized Enterprises (SMEs) face considerable difficulties on the financial market due to the reluctance of the investors to finance them. The European Commission strongly encourages the financing of start-up and growing SMEs. The Community programmes like the 7th Research Framework Programme (FP7) and the Competitiveness and Innovation Programme (CIP) offer many financing opportunities for SMEs. The complexity of these European programmes makes it difficult for entrepreneurs and SME support organizations to choose the most suitable funding for SMEs. Each programme has different objectives and establishes its own rules for funding application. Intermediary shall undertake to create an Additional Portfolio by using a significant part of the resources made available as a result of the securitization transaction to fund financing and/or guarantees to SMEs. For Serbian SMEs constitution of Intermediary will be a chance for financing in the future.

One of the problems which can be solved in the future is CIP delivered. CIP is delivered in partnership with a number of different groups of stakeholders and the involvement is comprehensive from the Parliament to the Member States. It is most often the case that stakeholders are able to relate to one part of CIP and not the overall programme. Therefore the creation of the framework programme can be said to have had little impact on the Member State stakeholders who have heard of component parts but rarely understood the concept of CIP as an entity. This was also the case within the European Commission to a certain extent. Where stakeholders do have views, it is usually stated that CIP is confusing. It does not give out one message about what it does and who it is for. Overcoming these problems would create the possibility for the inclusion of as many shareholders and thus for the implementation of CIP.

5. REFERENCES

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PHOTOS FROM THE WORKSHOP ON □HUNGARIAN SME POLICY□ HELD IN GYŐR

	
<p>Prof. Habil Dr. László Szerb (right) and Tibor Szegő</p>	<p>Dr. Éva Szalka, Deputy Dean of the Kautz Gyula Faculty of Economics, Győr</p>
	
<p>Németné Andrea Gaál</p>	<p>Gyula Kovács (right) and István Kovács</p>

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