

MICROFINANCE – A POSSIBLE ANTICRISIS MEASURE?

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1. Introduction

The increase of economic competitiveness depends mostly on the development capacity of the small and medium enterprises (SMEs) taking into consideration that small business are those that create new jobs and they represent the main promoter for entrepreneurship.

But initiating and developing a business requires the existence of financial resources and, often, finding appropriate sources of finance is a major difficulty for small and medium enterprises, especially for start-ups and micro enterprises.

In general, the banks offer loans to existing businesses, being reluctant to give credits to the companies that do not offer guarantees or to the start-ups. As well, the banks consider that some credits required by SMEs are too small and the costs for administration and monitoring are not justified. In addition, the serious liquidity problems caused by the current financial crisis have restricted lending activity of banks and increased the cost of credit. Therefore, small businesses are forced to seek other credit sources and the microfinance represents a viable alternative.

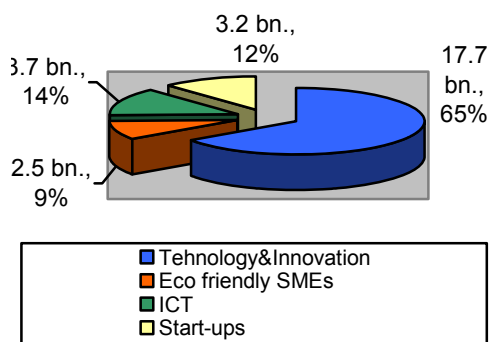
2. Microcredit in the European Union: opportunities vs challenges

The microfinance services have spread rapidly in recent years and it is considered an important source of funding for entities that can not access traditional financial services institutions.

Micro-credit is often used in EU member states and regions as a means to encourage the growth of independent activities and the creation and development of micro-enterprises.

In fact, small business represent a priority for cohesion policy in European Union (2007-2013), financial support offered is 55 billion euros, of which 50% are intended to support small businesses, including micro-enterprises (figure 1).

Figure 1. Financial support for small business - EU cohesion policy (billion)



Source: Delvaux, Ph., *A European initiative for the development of micro-credit*, Directorate General for Regional Policy, European Commission, October 2008

European Commission (in the recent Communication „*A European initiative for the development of micro-credit in support of growth and employment*”¹) defines microcredit as an

¹ European Commission (2007). Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee Of the Regions: A

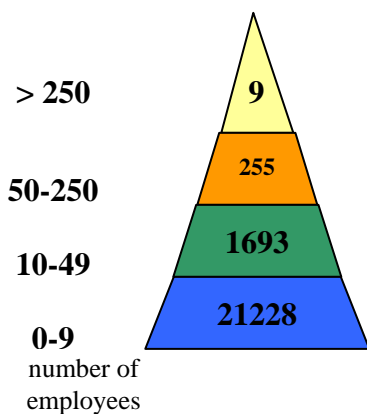
extension of small loans to entrepreneurs for socio-economic enterprises, for the employees to start their own business, for people working in the informal economy and unemployed or others who do not qualify for contacting a banking credit.

The micro-credit is any loan of up to 25,000 euros; the average is generally \$ 10,000 for the old Member States and 3,800 euros for the 12 new Member States

In Europe, microcredit activities aimed at two groups: micro-businesses (with fewer than 10 employees) and disadvantaged people (unemployed or inactive persons receiving social assistance, immigrants, etc.) that intend to start independent activities but do not access to traditional banking services.

At present, in European Union there are 23.2 million enterprises, of which 21.2 million (92%) are micro enterprises and the working population under the poverty line is 28 million (figure 2).

Figure 2. Number of enterprises in Europe (x 1000)



Source: European Commission, *A European initiative for the development of micro-credit in support of growth and employment*, Brussels, 2007.

Micro-credit is important for the rural areas, plays an important role for

integration of the ethnic minorities and immigrants, both economically and socially. Microcredit is seen as a financing tool used to reduce unemployment and to develop areas or disadvantaged groups by providing financial support to SMEs.

Therefore, the use of microcredit is not aimed solely at stimulating entrepreneurship and economic growth but also social aspects. In fact, the European Union considers the micro-credit schemes as a vital tool to boost competitiveness and entrepreneurship, particularly for women and minorities.

Thus, the micro-credit activity plays an important role in achieving the Lisbon Strategy regarding the economic development and jobs' creation and promoting social inclusion in accordance with the modern meaning „flexicurity” (a combination of flexibility and social security).

European Commission underlines the cost effectiveness for the micro-credit schemes as an instrument of public policy given that the environment cost to support microcredit schemes in Europe is under 5000 Euros for a new job created, with a survival rate of over 60% after two years, for a a started business based on microcredit (EC, 2007b).

Over the past decades, the European economy has evolved from the dominance of large industrial enterprises to a greater reliance on small businesses, mostly in the services field, leading to an increased demand for microcredit.

In the current context, while microcredit is commonly associated with small loans for entrepreneurs from poor countries, in the context of international financial crisis, it becomes a tempting tool for developed economies, too.

Thus, on short-term, the potential demand for microcredit in the EU could rise, according to Eurostat estimates, to more than 700,000 new loans, with a value of about 6.1 billion euros. The

average size of a micro-credit is estimated at 7,000-8,000 euros.

The demand for microcredit can be classified in the following trends: demand for microcredit which has a positive impact on small firms, the demand for creation of new jobs that lead to a lower unemployment and social exclusion, demand for funds to maximize the contribution of informal sector and demand for loans to minimize the effects of immigration.

3. Initiatives at the European level regarding the microcredit

Microfinance is an effective tool to stimulate entrepreneurship but ensurance of a micro-credit offer for the member states is a very difficult task.

Although there is an active microfinance sector in many member states and regions, however, there is not a uniform legislation regarding microfinance activities in the European Union as part of the *acquis communautaire*.

In Europe, only two countries, France and Romania, have specific legislation on micro-credit. In the other countries, the microcredit activity is regulated by laws that govern the institutions that provide micro-loans: banks and non banking institutions. While legislation covering the banking sector is harmonized to a great extent with European banking laws, regulations on micro-credit granted by non-banking institutions differ from country to country (table no. 1).

Table1. Characteristics of the regulatory system for the microcredit activities in the European countries

Country	Non bank Institution	Interest rate cap	Tax incentives	Special regulation	Guarante schemes
Austria	x				x
Belgium	x	x			x
Bulgaria	x				x
Cyprus					x
Czech Rep.	x				x

Finland	x				x
France	x			x	x
Germany	x	x			x
Hungary	x				x
Ireland	x		x		
Italy	x	x			x
Latvia	x				x
Lithuania	x				x
Luxem.	x				x
Poland	x	x			x
Portugal					x
Romania	x			x	x
Slovak Rep.	x				x
Sweden	x				x
Turkey	x				x
United Kingdom	x	x	x		x

Sursa: European Commission, *The Regulation of Microcredit in Europe*, Expert Group Report, Brussels, April 2007

The EU and its member states have taken some actions to support micro-credit (CIP, EQUAL, PHARE, etc.) but these have not proved sufficient in order to allow sustainable development for micro-credit activities in Europe.

Therefore, the European Commission proposed new initiatives to stimulate microcredit such as:

- to improve legal and institutional environment of the member states;
- fostering entrepreneurship,
- promoting best practices, including training activities and provide additional financial capital for microfinance institutions.

The micro-credit operations must be integrated into a broader framework in accordance with the subsidiarity principle, being necessary to be created a more favorable environment for the sector.

The community initiatives to develop micro-credit activities have resulted in JEREMIE (Joint European Resources for Micro, Small and medium - Joint European Resources for Micro and Medium Enterprises) with the support of the European Investment Fund in order to improve the access to finance, including the micro-credits to SMEs.

The program facilitates the use of financial products such as micro-credit,

loan guarantees, venture capital funds, seed capital, etc.. Also, a special attention is given to the start-ups, technology transfer and innovation funding.

The European Union initiative to provide partial guarantees for micro loans portfolios through the Multiannual program for Enterprises and Entrepreneurship, (2001-2005) was continued and extended under the Program for Entrepreneurship and Innovation (part of Competitiveness and Innovation Framework Program - CIP), managed by the European Investment Fund.

Thus, the SME Guarantee Facility – (SMEG) provides additional guarantees to increase the supply of loan capital to SMEs and covers the following areas: access to credit for SMEs, providing micro-credit and securitization.

There were set up various organizations and networks in this field (European Microfinance Network, created in 2003 in Paris and Microfinance Center for Central and Eastern Europe and NIS established in Warsaw in 1996) that have the common mission of promoting microfinance, encouraging the entrepreneurship and creating new jobs. The attitude of the European Commission regarding the redefining of the micro-credit designed to ensure economic restructuring for disadvantaged groups in the society is supported by the European Savings Banks Group (ESBG), that represented one of the largest networks of microfinance providers in Europe, with members in 26 European countries.

According to this institution, due to the local dimensions of micro-credit activities, the EU should aim primarily at the microcredit at national, regional or local level, before seeking to create a single market for microcredit.

However, the European Commission aims to introduce a pan-European system of microcredit in order to harmonize and integrate all

microfinance initiatives at member states and candidate states.

A recent joint initiative of the European Commission, European Investment Bank and European Investment Fund had as result the JASMINE program (Joint Action to Support Microfinance Institutions in Europe) designed to support the micro-credit activity in Europe for two types of actions:

- ▶ Technical assistance to microfinance institutions in order to make them more reliable and to attract easier the necessary funding

- ▶ Funding the activities of non-banking financial institutions in order to grant more loans.

The purpose of the JASMINE program is to improve the access to finance for small entrepreneurs, the unemployed and people who are unable to access bank loans. This program began in 2009, with a pilot phase of three years and with a capital of 50 million euros.

On July 2, 2009, European Commission has proposed to create a new tool for micro financing – named Progress - which could offer a real help to the small business owners and people who will start new businesses, in particular young people and unemployed. Thus, the new tool of microfinance is to help people who, under the current reduction of credit resources, might face difficulties in accessing funds for starting of new businesses.

Besides access to funds, these people will benefit from additional support measures, such as: training and professional counseling. Disadvantaged people, including young people, who want to develop a small business will also benefit of guarantees and assistance on preparing a business plan.

The initial budget will be 100 million Euro and it is expected that this amount will mobilize over 500 million Euro in a joint initiative with international financial institutions, in particular with the

European Investment Bank Group. The result of this initiative can be materialized in approximately 45,000 loans for a period of up to 8 years. In addition, the possibility of loans to benefit from reduced interest rates through the assistance of the European Social Fund will facilitate the access to funds.

Microcredit will be designed for micro-enterprises with less than 10 employees and unemployed or inactive people who want to start independent activities but have no access to traditional banking services. The Commission estimates that the new tool of microfinance will be operational in 2010.

The service, agriculture and tourism sectors may represent areas with potential to absorb a significant proportion of the workforce available in the labor market, for which Romania and other EU countries should develop the necessary tools for applying this idea, especially in the non-banking market.

4. Conclusions

The recent initiatives of the European Commission and Small Business Act provide an opportunity to

improve the micro-credit in Europe. But development of this sector is a challenge that involves many stakeholders, such as:

- Member States (providing the institutional, legal and commercial activity needed to promote micro-credit)
- European Commission (JEREMIE, JASMINE, SME Guarantee Facility, etc.)
- European Parliament (adoption of measures to strengthen the capacity of micro finance institutions);
- European Investment Bank Group (financial expertise, fundraising, etc.)
- Micro-financing networks (informing, the best practices, etc.);
- public and private investors, banks (financing and expertise).

Improving access to microcredit in order to develop a business by the small entrepreneurs, unemployed and disadvantaged people who lack access to traditional banking instruments is a possible solution provided by the European Union to the Member States in order to overcome the crisis.

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