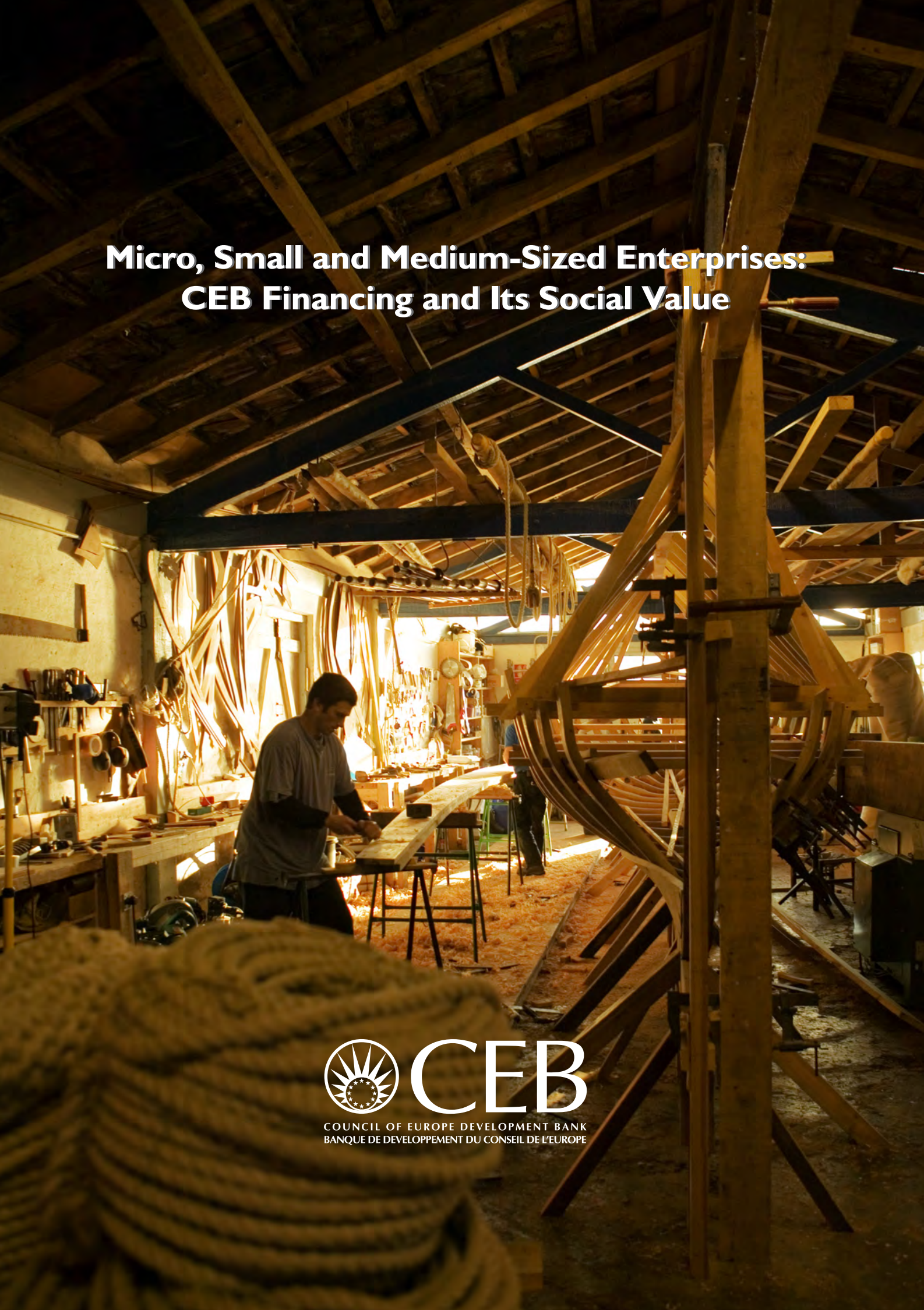
Micro, Small and Medium-Sized Enterprises: CEB Financing and Its Social Value



CEB

COUNCIL OF EUROPE DEVELOPMENT BANK
BANQUE DE DEVELOPPEMENT DU CONSEIL DE L'EUROPE



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FOREWORD

Employment has long been identified as a significant pillar of social inclusion. It helps lift people out of poverty, (re-)integrates marginalised or socially excluded populations, and contributes to the development of social identities of individuals and to social cohesion of communities.

Net job creation and economic growth have increasingly been linked, especially in the past decades, to the growth of micro, small and medium-sized enterprises (MSMEs). Nevertheless, it is smaller companies, as opposed to large firms, that report higher financing obstacles which impede their growth.

The Council of Europe Development Bank (CEB) works with governments and financial institutions to promote the creation and preservation of viable jobs in its Member States. It provides small companies with medium- and long-term financing through intermediaries. The primary financing instrument for this is the "programme loan", a lending instrument widely used in the development community.

From 1956 to end-2012, the Bank approved close to € 9 billion in loans to this effect. This activity has gradually evolved, becoming a major expression of the CEB's social mandate since 1995. From 1995 to 2012, the CEB's financing in favour of job creation and preservation amounted close to € 8 billion, representing a fifth of its total lending activities.

The purpose of this study, entitled "Micro, Small and Medium-Sized Enterprises: CEB Financing and Its Social Value", is to establish a historical overview of the Bank's activities in favour of creation and preservation of jobs from the CEB's establishment to 2012. The study also analyses the socio-economic rationale for the CEB's support to MSMEs.

The key references are additionality, i.e. value beyond the contributions of the private sector, and social added value of the CEB's support in this sector: creation and preservation of viable jobs. The report explains that this final social objective has been achieved through the role of the CEB: *(i)* in promoting financial inclusion of disadvantaged and socially marginalised populations and regions in the Bank's Member States and *(ii)* in providing a particular degree of additionality and producing catalytic effects in the financial sectors of the Bank's so called "target countries" in Central, Eastern and South-Eastern Europe.

I believe that the report is especially pertinent in the context of the socio-economic consequences of the crisis which erupted in 2007. I would also like to underline the Bank's effort to present options to be further explored in order to enhance its existing operating model of MSME financing and to increase the social added value of its operations in this sector.

This study comes as a natural reflection following over four decades of activities in favour of job creation and preservation and is largely based on the input from the operations, technical assistance and monitoring, and evaluation departments. It makes reference, inter alia, to the findings of the recent Evaluation Synthesis Report on the activities of the Bank in favour of MSME financing.

I would hope that this publication will raise awareness of this major sector of the CEB's lending as an integral part of the Bank's contribution to fostering social cohesion in its Member States.



Rolf Wenzel
Governor
Council of Europe Development Bank

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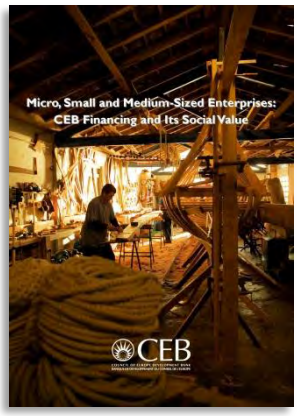
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ABBREVIATIONS AND ACRONYMS

AC	Administrative Council
CDS	Credit Default Swap
CEB	Council of Europe Development Bank
CEE	Central, Eastern and South Eastern Europe (18 countries): Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Czech Republic, Estonia, Georgia, Hungary, Latvia, Lithuania, Republic of Moldova, Montenegro, Poland, Romania, Serbia, Slovak Republic, Slovenia and "the former Yugoslav Republic of Macedonia"
DFIs	Development Finance Institutions
EBRD	European Bank for Reconstruction and Development
EC	European Commission
ECB	European Central Bank
EFL	Europejski Fundusz Leasingowy
EIB	European Investment Bank
EIF	European Investment Fund
EU	European Union
EU-12	Belgium, Greece, Luxembourg, Denmark, Spain, Netherlands, Germany, France, Portugal, Ireland, Italy, United Kingdom
EU-15	EU-12 plus Austria, Finland, Sweden
EU-25	EU-15 plus Poland, Czech Republic, Cyprus, Latvia, Lithuania, Slovenia, Estonia, Slovak Republic, Hungary, Malta (2004)
EU-27	EU-25 plus Bulgaria, Romania (2007)
EVD	Evaluation Department
Findex	Financial Inclusion Index
GDP	Gross Domestic Product
IFC	International Finance Corporation
IFI(s)	International Financial Institution(s)
ILO	International Labour Organization
IMF	International Monetary Fund
IOM	International Organisation for Migration
KfW	Kreditanstalt für Wiederaufbau
L&D	Loans and Social Development Directorate
MFIs	Microfinance Institutions
MSMEs	Micro, small and medium-sized enterprises
NIB	Nordic Investment Bank
NGOs	Non-Governmental Organisations
OECD	Organisation for Economic Co-operation and Development
PACE	Parliamentary Assembly of the Council of Europe
SMEs	Small and medium-sized enterprises
TAM	Technical Assessment and Monitoring Directorate
TSKB	Turkiye Sinai Kalkinma Bankasi A.S.



EXECUTIVE SUMMARY

1. The Council of Europe Development Bank (CEB) is a multilateral bank with an exclusively social mandate. Since its establishment in 1956, the CEB has been committed to supporting social investment projects while giving priority to its historical mission to help in solving social problems of refugees, displaced persons and migrants.

2. In the mid-1960s, the CEB started to support the creation and preservation of jobs in its Member States. To this effect, as of end-2012, it approved € 8.7 billion in loans. Activity in this sector has gradually evolved, becoming a significant pillar of the CEB's lending since 1995. From 1995 to 2012, the CEB approved € 7.6 billion and disbursed € 5.5 billion in loans in favour of job creation and preservation. During this period, this sector represented on average one-fifth of the total CEB lending, with peaks of more than 40% in 2008 and 2012 in the context of the socio-economic consequences of the crisis.

3. In the CEB's so-called "target countries" in Central, Eastern and South-Eastern Europe[i], job creation and preservation was the most significant sector of CEB activities between 1995 and 2012, accounting for 31% of approvals or € 5.0 billion. In the Bank's Western European Member States during the same period, it was the second most important sector, representing 13% of approvals or € 2.6 billion.

4. CEB loans in favour of job creation and preservation have consistently targeted micro, small, and medium-sized enterprises (MSMEs)[ii]. Responding directly to the pressing concern of smaller companies, limited access to finance, the Bank provides them with medium- and long-term financing. The rationale for supporting MSMEs is the recognition of their potential as drivers of economic growth, net employment generators, and promoters of social cohesion.

5. The typical CEB's lending instrument in favour of job creation and preservation is the "programme loan", i.e. a loan financed by the CEB through intermediaries disbursed according to their absorption capacity, and, consequently, demand from beneficiary MSMEs. The CEB has partnered with sovereigns as well as with public and private financial institutions to reach MSMEs in its Member States. In its target countries, where leasing tends to be a source of medium- and long-term financing, the CEB has worked with leasing companies in addition to traditional banks.

6. The CEB's activities, including those in favour of job creation and preservation, involve additionality i.e. value beyond the contributions of the private sector, and social added value. The CEB promotes financial inclusion of MSMEs in all Member States and contributes to deepening local financial systems and strengthening MSME lending markets in its target countries[iii]. The final objective of the CEB's MSME financing is to create and preserve viable jobs. In 1995-2011, following the projections obtained for 60% of loans in favour of MSME financing, the CEB's social impact could be estimated at around 137 000 of jobs created and another 1.6 million of jobs preserved.[iv]

7. Financial inclusion reflects widespread access to financial systems and use of financial products. It equalises opportunities for all populations and thus fosters social cohesion. In its target countries, characterised by generally less inclusive banking systems, the CEB aims to reach a broad spectrum of MSMEs that tend to be underserved and/or credit rationed. In its non-target countries, the CEB addresses disadvantaged regions at the sub-national level, registering unemployment rates above the EU average[v], micro-firms, and socially excluded or marginalised populations, such as immigrants and women.[vi]

8. The depth of financial sectors is characterised by the level of availability of credit. In shallow financial systems, credit to the private sector is limited, medium- and long-term financing is scarce, and MSME lending sectors are usually "embryonic". In its target countries, where the financial sectors, in addition to being less inclusive, are relatively shallow than in Western European countries, the CEB provides a particular degree of additionality. It also produces more pronounced catalytic effects, i.e. working with local financial intermediaries and contributing to mobilising resources from other IFIs for MSMEs.

9. Based on the Bank's experience following over four decades of operations, monitoring, and evaluations, the study presents several options to be explored by the CEB. The non-exhaustive list of alternatives is considered to further enhance the existing operating model of MSME financing and to increase the social added value of the Bank's operations in this sector. These options include: (i) targeting the lower-end of the MSME size spectrum, (ii) complementing the financing instrument (programme loan) with other instruments (e.g. technical assistance), (iii) adding to or replacing the headcount-based approach to impact assessment with more relevant and suitable indicators (e.g. financial inclusion), and (iv) adapting the eligibility criteria to take into account the role and needs of MSMEs.

Executive Summary Endnotes:

[i] Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Cyprus, Czech Republic, Estonia, Georgia, Hungary, Latvia, Lithuania, "the former Yugoslav Republic of Macedonia", Malta, Republic of Moldova, Montenegro, Poland, Romania, Serbia, Slovak Republic, Slovenia, Turkey.

[ii] Throughout the study, the acronym "MSMEs" refers to micro, small, and medium-sized enterprises. In the context of CEB MSME financing, support to micro-firms has not been normally identical to micro-crediting. While both activities refer to supporting individuals or enterprises with fewer than ten employees, micro-crediting is a particular support to the most socially excluded, e.g. low-income individuals, usually with small-value loans, although the array of products has increasingly broadened (see **Chapter 3**, **Box 3.2**). The CEB has only occasionally channelled its lending to microfinance providers with the objective to support marginalised populations, such as immigrants and women (see **Chapter 13**).

[iii] Although CEB MSME financing may have such potential effects, they are not specified as objectives in the design documents, and there are no appropriate monitoring indicators on which final performance could be evaluated.

[iv] The headcount reflects projected figures provided by implementing partners, which are based on self-declarations by the financed MSMEs. At the time of writing, projections were available for 60% of loans in favour of job creation and preservation. The CEB's Evaluation Department (EVD) has highlighted the low information content of, and methodological difficulties associated with the headcount-based approach focused exclusively on number of jobs created and/or preserved. The issues regarding this development impact indicator are a matter of debate, specific not only to the CEB, but also to the IFI community as a whole.

[v] "Disadvantaged regions" in non-target countries were referenced to the EU average in the CEB's Overall Policy Framework for Loan and Project Financing following CEB Administrative Council Resolution 1495 in 2006.

[vi] Conclusions based on the Case Studies presented in Part VI (**Chapter 13**), selected by purposive sampling to cover a range of financing modalities, countries, and final beneficiaries.

INTRODUCTION

The purpose of this study is to provide an overview of the historical commitment, rationale, and social added value of the Council of Europe Development Bank's (CEB) activities in favour of job[1] creation and preservation in its Member States. The publication builds upon over four decades of operations, monitoring, and evaluations in this sector.

From its establishment to end-2012, the CEB approved € 8.7 billion and disbursed € 6.2 billion in loans to this effect. The scope and nature of CEB financing in favour of micro, small and medium-sized enterprises (MSMEs)[2] has evolved in tandem with the overall strategy of the Council of Europe. The first loan was approved in 1968 and operations in this field were officially established as a sector of action in 1979. As of the mid-1990s, CEB support to this sector became a major pillar in the Bank's activities:

- Between 1956 and 1994 the CEB approved loans in value of € 1.1 billion and disbursed € 0.6 billion.
- Between1995 and 2012 the CEB approved loans is value of € 7.6 billion and disbursed € 5.5 billion.

The increase in activities is related to the evolution of the role of the Bank in job creation and preservation as part of the social mandate of fostering social cohesion; the geographical expansion starting in 1994 in Central, Eastern and South-Eastern Europe (CEE); progressive development of the banking sectors in the new member countries; operations under "transit loans"[3] since 2000; and a gradual increase in demand for CEB lending.

Market imperfections limit the willingness of financial institutions to engage in MSME financing and further increase the cost of financing. These market imperfections are aggravated in the context of relatively shallow financial markets, such as in the CEB's target countries. To assist MSMEs to fulfil their potential as drivers of economic growth, net employment generators, and promoters of social cohesion, the CEB responds to the pressing concern of MSMEs, limited access to finance, and provides them with medium- and long-term financing.

The CEB channels its financing through sovereigns and public or private financial institutions, which have the necessary coverage, expertise and institutional willingness and capacities to target beneficiary MSMEs in a sustainable manner. The CEB's activities in favour of job creation and preservation entail additionality, i.e. value beyond the contributions of the private sector, and social impact associated with the creation and preservation of jobs. The degree of additionality depends on the economic cycle and/or the choice of implementing partners.

- In its Member States, the CEB promotes financial inclusion and makes medium- and long-term financing, bank or leasing, available and affordable to MSMEs that tend to be underserved and/or credit-rationed.[4]

[1] "Jobs and employment are not the same. For example, a worker can switch jobs, but remain employed at the same time during a certain period. At the aggregate levels of enterprises and size classes, differences in (changes in) the number of jobs and (changes in) employment levels are, however, very small. The terms "employment" and "jobs" are therefore used interchangeably in this study". EIM Business & Policy Research (2011), Do SMEs Create More and Better Jobs?, European Commission (2012).

[2] Throughout the study, the acronym "MSMEs" refers to micro, small, and medium-sized enterprises. In the context of CEB MSME financing, support to micro-firms has not been typically identical to micro-crediting. While, both activities refer to supporting individuals or enterprises with fewer than ten employees, micro-crediting is a particular support to the most socially excluded, e.g. low-income individuals, usually with small-value loans, although the array of products has increasingly broadened (see **Chapter 3, Box 3.2**). The CEB has only occasionally channelled its lending to microfinance providers with the objective to support marginalised populations, such as immigrants and women (see **Chapter 13**).

[3] Loans granted to intermediaries in non-target countries to finance loans in target countries.

[4] Although financial inclusion may be another potential effect of CEB MSME financing, it is not specified as an objective in the design documents, and there are no appropriate monitoring indicators on which final performance could be evaluated.

- In its target countries, the Bank fosters social cohesion through job creation and preservation not only by promoting financial inclusion of MSMEs, but also by contributing to deepening the financial sectors and strengthening the MSME lending markets[5]. CEB activities in its target countries have a particular degree of additionality and produce catalytic effects, i.e. mobilising IFIs and other local banks to increase their lending to MSMEs. Nevertheless, effective absorption of the MSME support provided by the international community, including the CEB, in the region requires, inter alia, the presence of a national commitment to developing a conducive MSME operating environment. In most of the CEB's non-EU target countries[6] the MSME policy framework is generally advancing towards EU standards in the pre-accession countries, and there is a national pro-active approach to developing the operational environment in the Republic of Moldova and Georgia.

The economic and financial crisis that began in 2007 renewed the role of IFIs in the private sector, including in the MSME sector, in particular in CEE target countries. Given the potential of MSMEs to re-integrate the populations affected by the crisis (such as unemployed, long-term unemployed, and migrant workers), to generate employment and to promote economic growth and social cohesion, the CEB has shown continued support to MSMEs with the final objective of creating and maintaining viable jobs and thus fostering, social cohesion in its Member States. In order to enhance the Bank's operating model of MSME financing to better respond to the needs final beneficiaries and capacities of implementing partners and thus to improve the social added value of operations in this sector, the study presents several options to be further explored. These non-exhaustive alternatives represent a common effort on behalf of the Bank's operations, technical assistance and monitoring, and evaluation departments.

The study is divided into the following six parts:

PART I. CEB Activities in Job Creation and Preservation (1956-2012) illustrates, from the establishment of the Bank in 1956 to end-2012, the historical commitment, evolution and the € 8.7 billion portfolio of the CEB's financing in favour of job creation and preservation.

PART II. MSME Sector: Driver of Social Cohesion describes the socio-economic potential of MSMEs as drivers of economic growth, net employment generators, and promoters of social cohesion, with a focus on CEB Member States.

PART III. Obstacles Facing MSMEs in Fulfilling their Socio-Economic Potential mentions the key concerns cited by MSMEs and concentrates on "access to finance", a pressing problem across MSMEs. It also lists market imperfections as explanations of supply side constraints in MSME external financing and analyses leasing and factoring as preferred alternatives of MSMEs to traditional bank financing, particularly in the Bank's target countries.

PART IV. Shallow Financial Sectors in CEB "Target Countries". In addition to describing financial sectors in the CEB's target countries, this part introduces the Bank's operations under "transit loans" between 2000 and 2009 to reach MSMEs beneficiaries in those Member States.

PART V. Responding to the Consequences of the Crisis: CEB Continued Support to MSMEs provides an overview of the impact of the financial and economic crisis, focusing on the financial and social consequences pertinent to the CEB's MSME activities.

PART VI. Social Added Value of CEB MSME Financing: Lessons Learned and Options Ahead elaborates on additionality and social added value of the CEB's MSME financing based on five Case Studies selected by purposive sampling to cover a range of financing modalities, countries and final beneficiaries. This part also summarises the key lessons learned and several options to be explored by the Bank to enhance its operating model in MSME financing.

[5] Although CEB MSME financing may have such potential effects, they are not specified as objectives in the design documents, and there are no appropriate monitoring indicators on which final performance could be evaluated.
[6] Albania, Bosnia and Herzegovina, Croatia, "the former Yugoslav Republic of Macedonia", Montenegro, Serbia and Turkey

PART I. CEB ACTIVITIES IN JOB CREATION AND PRESERVATION (1956-2012)

Part I illustrates the historical commitment and evolution of the CEB's activities in job creation and preservation (Chapter 1) and the profile of the CEB's loan portfolio in MSME support from the establishment of the Bank in 1956 to 2012 (Chapter 2).

Chapter 2 also presents the strategic commitment of the CEB in Central, Eastern and South-Eastern Europe (CEE) starting with mid-1990s, officially instated under the concept of "target countries" in the Development Plan 2005-2009, which comprises 21 countries (see Table 2.1). It also elaborates on the importance of intermediaries to reach final beneficiaries under the CEB's operating model and the use of "transit loans" in target countries, i.e. loans granted to borrowers in non-target countries with the final objective of benefiting MSMEs in target countries.

Chapter 1. Historical Commitment of the CEB to Job Creation and Preservation

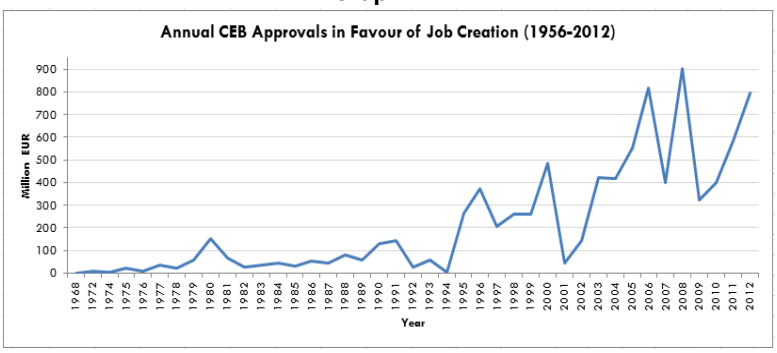
Since its establishment in **1956** by the Committee of Ministers of the Council of Europe[7], the CEB has devoted itself to its social mandate in Europe, i.e. to supporting social investment projects and responding to emergency situations in the least advantaged regions in Europe. Article II of the Articles of Agreement, last amended in 1999, declares the statutory social purpose of the Bank:

- "The primary purpose of the Bank is to help in solving social problems with which European countries are or may be faced as a result of the presence of refugees, displaced persons or migrants consequent upon movements of refugees or other forced movements in the populations and as a result of the presence of victims of natural or ecological disasters.

- The Bank may also contribute to the realisation of investment projects by a Member of the Bank which enable jobs to be created in disadvantaged regions, people in low income groups to be housed or social infrastructure to be created."

The Bank, while giving priority to its historical objectives, has progressively "adapt[ed] its modes and methods of operation to changing socio-economic circumstances in order to achieve an overall result consistent[...] …with its fundamental [social] purpose"[8]. The scope of the Bank's operations has thus gradually broadened to other sectors: education and vocational training, health, housing for low-income persons, improving living conditions in urban and rural areas, protection of the environment, protection and rehabilitation of the historic and cultural heritage, infrastructure of administrative and judicial public services, and creation and preservation of viable jobs.

Graph 1.1



The Bank's activities in employment creation have their origin in the **mid-1960s** (see **Graph 1.1**), when it financed vocational training[9], in line with the changing needs of migrants, aimed at preserving jobs in regions that suffered from depopulation as a result of exodus,

[7] The CEB is based on a Partial Agreement between Member States of the Council of Europe and, as provided for in its Articles of Agreement, comes under the "supreme authority" of the Council. It therefore operates within the framework of the Council of Europe and supports its priorities. On 1 November 1999 the Bank changed its name to "Council of Europe Development Bank" (CEB), having been known first as the "Council of Europe Resettlement Fund for National Refugees and Over-Population in Europe" and then as the "Council of Europe Social Development Fund". For the purposes of consistency and clarity, the name CEB will be used throughout the report to refer to the institution.

[8] Report of the Governor for the Financial Year 1974

[9] Report of the Governor for the Financial Year 1967

and supported migrant workers "who, on their return to their home countries, wish to use the money they have saved and the occupational skills they have acquired abroad to set up their own undertakings"[10].

In **1973** the Bank started to "investigate, in conjunction both with governments and with the specialised Council of Europe committees (in particular the Committee on Co-Operation in Municipal and Regional Matters), new ways [of providing support to its Member States] … by creating new jobs, or through individual or group projects designed to stabilise migratory movements …"[11]. The socio-economic environment following the 1974 crisis portrayed by high unemployment has created a greater need for the Bank's activities in "the creation or continuation of jobs"[11]. Employment officially became an area of the CEB's activity in **1979** and the Bank's activities in this sector have evolved since then, always in line with the overall strategy of the Council of Europe (see **Table 1.1**):

Table 1.1 Snapshot of the Evolution of CEB Activities in Job Creation and Preservation

Year	1979	1987	1993	1995	1997	2006	2009
AC Resolutions	354	934	1313	1313 Revised 2	1424	1495	1522
Sector of Action	"Reduction of Unemployment"			"Job Creation"		"Creation and Preservation of Viable Jobs"	
Objective of CEB Lending under the said Sector of Action	Creation of new jobs or preservation of existing ones	Creation of permanent jobs, including seasonal jobs, at comparatively lower cost per job, without excluding preservation of jobs by introducing automation, especially in less developed regions.	The field of action includes vocational training programmes and job creation projects in disadvantaged regions.	The "other field of action" "reduction of unemployment" is renamed "**job creation**".	First reference to SMEs in the objective: "creation of new permanent and seasonal jobs, not excluding the preservation of important existing ones in viable projects **in small and medium-sized companies** in disadvantaged areas, with the exclusion of agriculture".	Fixed investments or investments in productive equipment, including leasing, aimed at creation and/or preservation of permanent and/or seasonal jobs. The financing of working capital is permitted, limited to certain conditions. Eligibility criteria for MSMEs.	

- **CEB Administrative Council (AC) Resolution[12] 354 (1979)** approved "reduction of unemployment" as the main priority for loan applications other than those related to the Bank's historical priority. "Creation of new jobs or preservation of existing ones, and house-building projects form[ed] an integral part … designed to reduce unemployment". "Vocational training" was identified as the second priority (out of a total of six, including "schemes aimed at stabilising population", "rehousing for migrants", "low-cost housing", and "infrastructure projects").

- In 1980, the **Parliamentary Assembly of the Council of Europe (PACE)** under **Recommendation 895** encouraged the Member States of the Council of Europe "to examine with great attention ways and means to facilitate the access of SMBs[13] to private or public capital and credit resources (for example, through government-guaranteed loan systems, easier access to the stock exchange, temporary direct participation)"[14]. Under **PACE Resolution 798 (1983)**, Member States were called on "to co-operate in the financing of employment creation by SMEs in those countries faced with the problem of returning migrant workers"[15].

- **AC Resolution 934 (1987)** identified "reduction of unemployment" as one "other specific field of action" of the institution, in addition to its statutory priorities. The focus was on creating "permanent jobs, including seasonal jobs, at comparatively lower cost per job, without excluding preservation of jobs by introducing automation, especially in less developed regions". "Vocational training" was also identified as one "other specific field of action", along with "creation of infrastructures", and "development of

[10] Report of the Governor for the Financial Year 1969
[11] Report of the Governor for the Financial Year 1973
[12] Resolutions are approved by the CEB Administrative Council (AC), which is vested with all powers delegated to it by the Governing Board in pursuance of Article IX under the Articles of Agreement of the CEB.
[13] Small and Medium-Sized Businesses
[14] Parliamentary Assembly. Recommendation 895 (1980). http://assembly.coe.int/Mainf.asp?link=/Documents/AdoptedText/ta80/EREC895.htm
[15] Parliamentary Assembly. Resolution 798 (1983). http://assembly.coe.int/Main.asp?link=/Documents/AdoptedText/ta83/ERES798.htm

regions or areas which are declining or which are economically or socially disadvantaged". Preference was given to "developing, underprivileged or declining zone[s] or region[s]".

- Under **AC Resolution 1313 (1993)** "the other field of action", "reduction of unemployment", included "vocational training programmes and job creation projects in disadvantaged regions". Disadvantaged regions were defined as "regions eligible under Objective 1 of the Structural Funds of the European Communities … . Regions outside the Union … [were] eligible if they fulfil[led] the conditions for this objective".

- **AC Resolution 1313 (1993) Revised 2 in 1995:** the "other field of action" "reduction of unemployment" was renamed "**job creation**" and the definition of disadvantaged regions was amended to refer to Objectives 1,2, 5.b and 6 of the Structural Funds of the EU.

- Under the 1997 Final Declaration and Action Plan of the **Strasbourg Summit**, social cohesion was recognised as "one of the foremost needs of the wider Europe". The Bank was "invite[d] … to participate actively in the Council of Europe's action for social cohesion, and urge[d] … to increase its investment effort in the social field and in job creation."[16] **AC Resolution 1424 (1997)** declared the focus of "job creation" to be creating "new permanent and seasonal jobs, not excluding the preservation of important existing ones in viable projects in **small and medium-sized companies in disadvantaged areas**, with the exclusion of agriculture". The disadvantaged regions were considered "EU regions where over 5% of the working population is unemployed. Norway, Switzerland, Liechtenstein and San Marino … [were] treated as EU regions. Other non-EU members … [were] fully eligible".

- Under **PACE Resolution 1365 (2004)** Member States were encouraged "to devise policies favouring the expansion of long-term micro-loan financing, particularly for small and medium-sized businesses"[17]. On 31 March 2004, the **Committee of Ministers** approved the 2004 revised version of the Council of Europe's Strategy for Social Cohesion with particular reference to the right to work, access to employment and economic development: "Access to employment for all and the promotion of decent employment are important factors in combating poverty and exclusion"[18].

- Under the 2005 Action Plan of the **Warsaw Summit**, the Bank was requested "to facilitate, through its own means of action, the implementation of policies which aim at the consolidation of democracy, the promotion of the rule of law and respect for human rights". It was identified that "the central task is to … define remedies and solutions which could be effective in fighting poverty and exclusion, ensuring equitable access to social rights and protecting vulnerable groups".[19]

- **Resolution 1495 (2006):** brought approval of the CEB's Overall Policy Framework for Loan and Project Financing, which officially established the term "sectoral lines of action" and identified the following three sectoral lines of action: "strengthening social integration", "managing the environment", and "developing human capital". Each of these lines comprises a number of sectors of action. "Creation and preservation of jobs" was identified as a sector of action under the line "strengthening social integration".

[16] Council of Europe (1997), *Final Declaration and Action Plan*, Second Summit of the Heads of State and Government of the Member States of the Council of Europe, 10 and11 October 1997, Strasbourg.
[17] Parliamentary Assembly. Resolution 1365 (2004).
http://assembly.coe.int/Documents/AdoptedText/ta04/ERES1365.htm
[18] Council of Europe (2004), *A New Strategy for Social Cohesion*. Revised Strategy for Social Cohesion Approved by the Committee of Ministers of the Council of Europe on 31 March 2004
[19] Council of Europe (2005), *Action Plan CM(2005)80 Final 17 May 2005*, Third Summit of the Heads of State and Government of the Member States of the Council of Europe, 16-17 May 2005, Warsaw.

- **Resolution 1522 (2009)** amended the CEB's Overall Policy Framework for Loan and Project Financing and modified the "sectoral lines of action" to "strengthening social integration", "managing the environment", and "supporting public infrastructure with a social vocation" (see **Box 1.1**).

Box 1.1 CEB Sectoral Lines of Action

Sectoral lines of action	Sectors of action
Strengthening social integration	• Aid to refugees, migrants and displaced persons • Housing for low-income persons • Creation and preservation of viable jobs • Improvement of living conditions in urban and rural areas
Managing the environment	• Natural or ecological disasters • Protection of the environment • Protection and rehabilitation of historic and cultural heritage
Supporting public infrastructure with a social vocation	• Health • Education and vocational training • Infrastructure of administrative and judicial public services

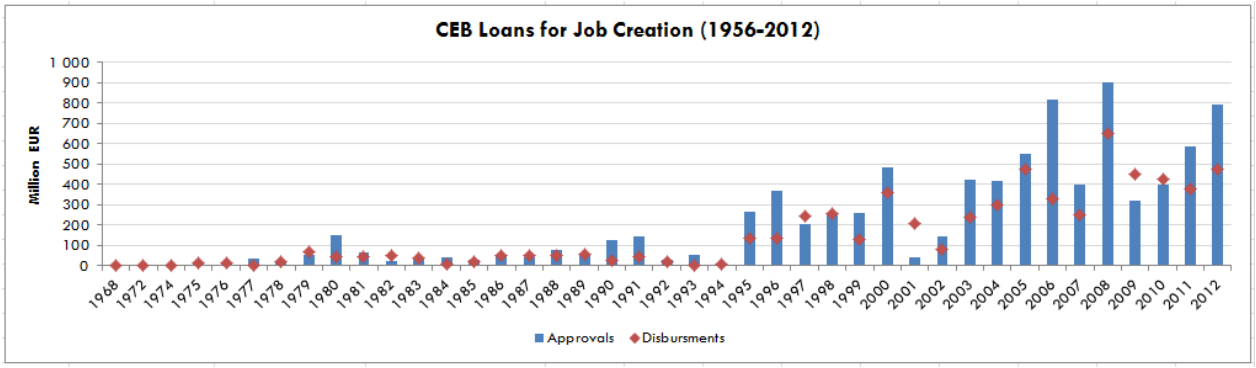
Chapter 2.
CEB Portfolio Profile in Job Creation and Preservation since its Establishment in 1956

Even though the roots of the Bank's financing in favour of job creation date back the mid-1960s, this sector of action became a significant activity from the mid-1990s (see **Graph 2.1**):

- Between 1956 and 1994 the CEB approved loans in value of € 1.1 billion and disbursed € 0.6 billion.
- Between 1995 and 2012 the CEB approved loans in value of € 7.6 billion and disbursed € 5.5 billion.

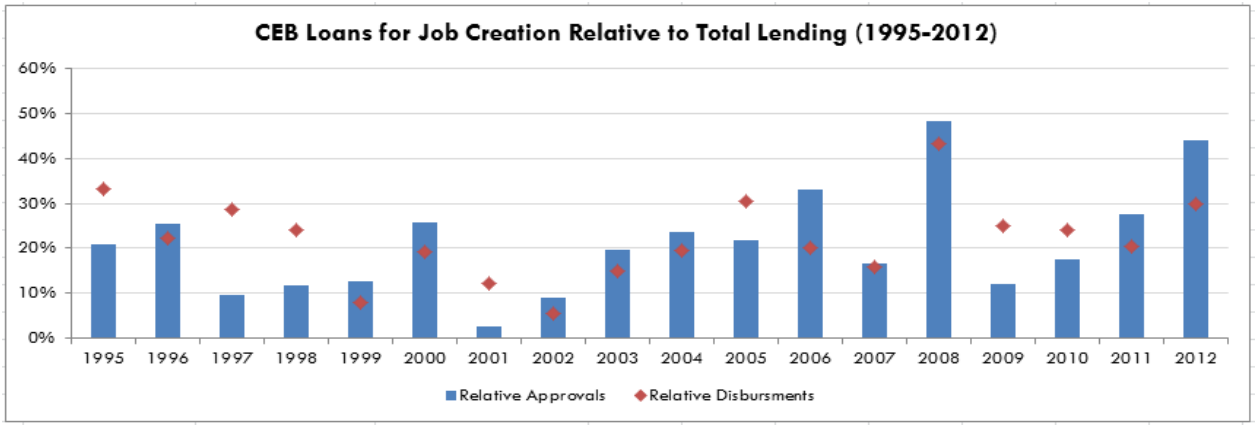
The increase in activities is related to the evolution of the role of the Bank in job creation as part of the social mandate of fostering social cohesion (see **Table 1.1**); geographic expansion as of 1994 into Central, Eastern and South-Eastern Europe (CEE) (see **Table 2.1**); progressive development of the banking sectors in the new member countries (see **Chapters 8** and **9**); use of "transit loans" (see **Chapter 9**); and a gradual increase in demand for CEB lending.

Graph 2.1



Relative to its total lending, between 1995 and 2012, the allocation of CEB loans to job creation averaged 21%. This ratio also holds when excluding the years of lowest (2001 and 2002) and highest activity (2008 and 2012) in this sector (see **Graph 2.2**). The largest share was in 2008 and 2012, when 48% and 44% of total approvals, respectively, were allocated to job creation, given the increased demand for CEB MSME financing as a result of the financial and economic crisis that started in 2007.

Graph 2.2



The geographic commitment of the Bank to the CEE transition countries, the CEB new Member States, was called by PACE under **PACE Resolution 1138 (1997)** on "Promoting Small and Medium-Sized Enterprises in Central and Eastern Europe". PACE "encourage[d] … [the CEB] to enhance its support for SMEs in central and eastern Europe, notably through intermediary credit institutions and micro-credit

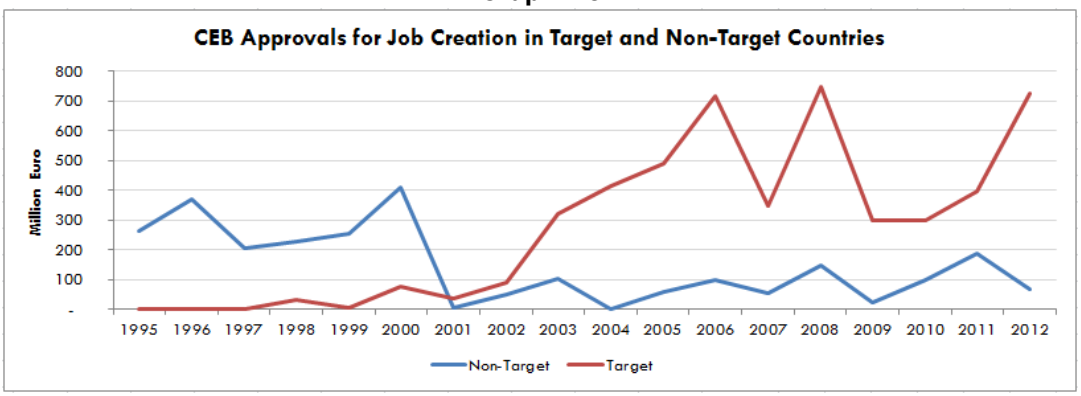
programmes ..."[20]. The institutional strategic commitment to the region was officially declared in The Medium-Term Development Plans 1997-2001 and 1999-2004. The Development Plan 2005-2009 introduced the concept of "target countries", which comprises 21 countries (see **Table 2.1**):

- In addition to the 18 former socialist countries of CEE, it was felt that the development process in Turkey deserved a similar degree of support. Malta and Cyprus were also included in the group as they joined the EU at the same time as some of the CEE countries.
- The Development Plan 2005-2009 had the objective of breaking down equally (50:50) the annual amount of loans disbursed between target and non-target countries.
- The Development Plan 2010-2014 states that the Bank should enhance its support in favour of target countries and increase the share of loans outstanding to these countries to up to 60% by 2014.

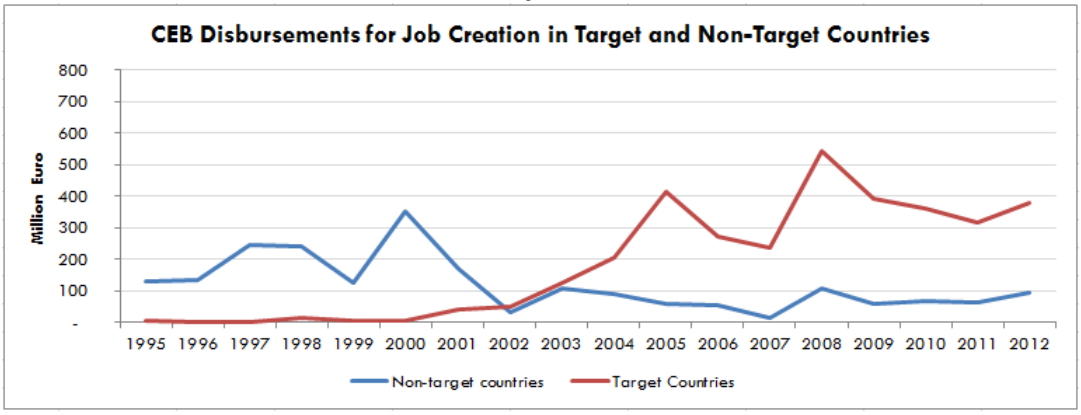
In target countries, job creation and preservation was the most significant sector of CEB activities between 1995 and 2012, accounting for 31% of approvals or € 5 billion, and 30% of disbursements or € 3.4 billion. In the CEB's non-target countries in Western Europe during the same period, it was the second most important sector, representing 13% of approvals or € 2.6 billion, and 14% of disbursements or € 2.2 billion.

Since 2001, the annual loans approved in favour of job creation and preservation in target countries have consistently been higher than those in non-target countries (see **Graph 2.3**). Since 2002, a similar trend can be observed for annual loans disbursed (see **Graph 2.4**). This mostly relates to the use of "transit loans", i.e. loans granted to borrowers in non-target countries[21] with the final objective of benefiting MSMEs in target countries (see **Chapter 9**).

Graph 2.3



Graph 2.4



[20] Parliamentary Assembly. Resolution 1138 (1997).
http://assembly.coe.int/Main.asp?link=/Documents/AdoptedText/ta97/ERES1138.htm

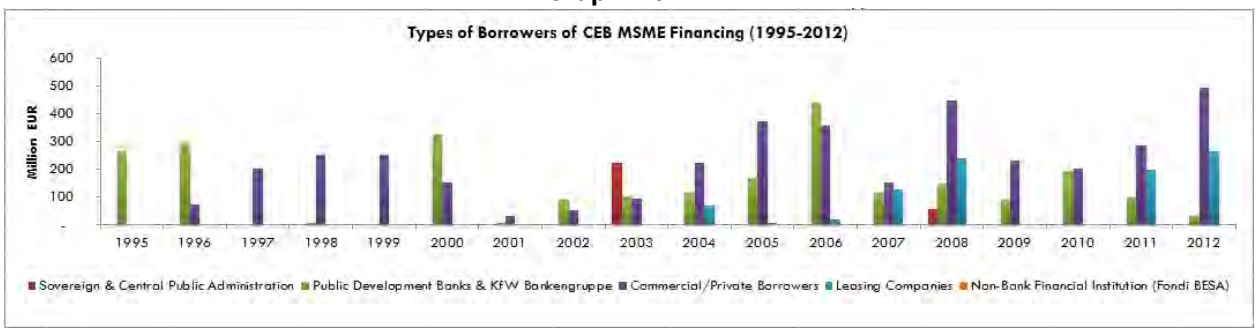
[21] According to the CEB's Policy for Loan and Project Financing, the borrower may be the Member State itself, a central or local government entity, a financial institution or any other public or private entity.

The Bank started to operate via "transit loans" in 2000. This channelling mechanism was necessary given the presence of shallower and less inclusive banking sectors in target countries (see **Chapter 8),** and it was effective given the increasing foreign presence and gradual integration of the financial sectors in those countries since the mid-1990s (see **Chapter 9**). It also represents the gradual process of diversification of distribution channels from sovereign and public financing to commercial and other lending (see **Graph 2.5**).

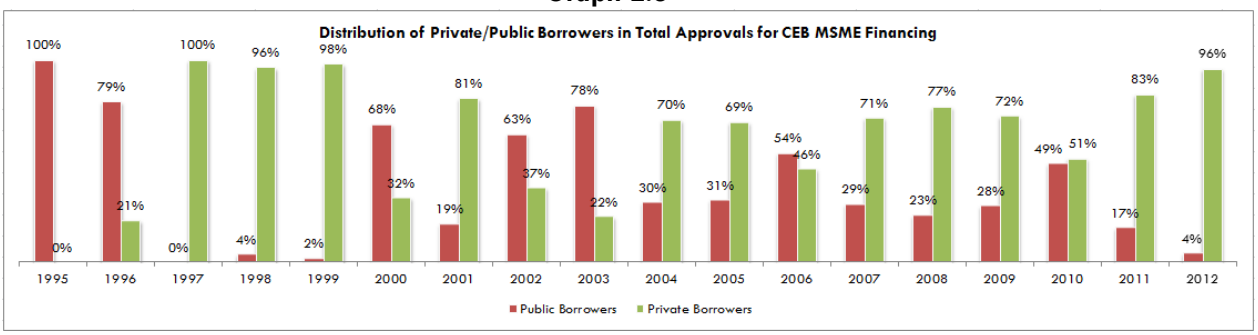
When differentiating between "transit loans" and other loans over the period 1995-2012, the geographic distribution of CEB loans allocated to job creation was slightly more biased towards non-target countries in terms of loans approved (see **Table 2.2**). However, "transit loans" are tools used specifically to reach and provide social added value to final beneficiaries located in target countries. A total of € 1.4 billion of "transit loans" were approved in favour of job creation and preservation during 2000-2009, via banks in Italy (€ 777 million), Germany (€ 493 million) and Sweden (€ 100 million)[22]. This represents slightly more than two-thirds (69%) of the value of "transit loans" approved for all CEB sectors of actions. In 2010-2012, "transit loans" were not approved in favour of MSME financing. This phenomenon could be explained, inter alia, by the deleveraging process undertaken by Western European banks as a consequence of the crisis (see **Chapters 8** and **9**). It also reflects the increased demand for CEB lending from state development banks in target countries.

The CEB does not have branches in its Member States and operates via intermediaries – sovereigns and public or private financial institutions – to reach the intended MSME beneficiaries. **Graphs 2.5** and **2.6** present the diversification of the distribution channels for CEB MSME financing during 1995-2012. During this period, 37% of borrowers of the CEB MSME financing were public (sovereigns, central or local public administration, and public development banks), while the remaining 63% were private borrowers (commercial borrowers, leasing companies, and non-bank financial institutions). The selection of borrowers, including those for "transit loans", implies a screening process of the intermediaries' risk profile, financial solidity, mandate and strategy, governance and management, convergence with the CEB's Environmental Policy, institutional capacity and willingness to reach final beneficiaries, sustainability of the financial mechanisms to reach final beneficiaries, readiness to put in place monitoring modalities to allow the CEB to evaluate social outcomes of the programme and other pertinent criteria.

Graph 2.5



Graph 2.6



Note: The category "Public Borrowers" includes sovereign & public administration (central and regional), and public development banks such as KfW Bankengruppe. The category "Private Borrowers" consists of commercial borrowers, leasing companies, and non-bank financial institution (Fondi BESA).

[22] "Transit loans" were granted to (1) IKB Deutsche Industriebank AG and KfW Bankengruppe in **Germany,** (2) Intesa Sanpaolo S.p.A., Società Italiana per le Imprese all'Estero (SIMEST), and UniCredito Italiano in **Italy,** and (3) Skandinaviska Enskilda Banken (SEB) in **Sweden.**

During 1995-2012, the distribution channels were concentrated around eight intermediaries, which comprised 44% of loans approved and 53% of loans disbursed (see **Table 2.3**):

Table 2.3 CEB Major Partner Institutions 1995-2012

	1995-2012			
Intermediaries	**Loans Approved, MEUR**	**Share in Total Loans Approved****	**Loans Disbursed, MEUR**	**Share in Total Loans Disbursed****
Public Borrowers*	**2 093**	**27%**	**1 860**	**34%**
Finnvera plc, Kuopio	284	4%	159	3%
KfW Bankengruppe	1 239	16%	1 181	21%
Magyar Fejlesztési Bank (MFB)	320	4%	320	6%
OSEO S.A.	250	3%	200	4%
Private Borrowers	**1 260**	**16%**	**1 081**	**20%**
Europejski Fundusz Leasingowy SA (EFL)	310	4%	208	4%
PKO Bank Polski S.A.	250	3%	176	3%
Turkish Industrial Development Bank (TSKB)	200	3%	197	4%
UniCredito Italiano	500	7%	500	9%
TOTAL	**3 353**	**44%**	**2 941**	**53%**

**The category "Public Borrowers" includes sovereign & public administration (central and regional), and public development banks such as KfW Bankengruppe.*

***To present the shares as whole numbers, the percentages have been rounded and their sums may therefore not correspond to the figures in row "Total".*

The largest borrower is KfW Bankengruppe with € 1.24 billion in loans approved and € 1.18 billion in loans disbursed during 1995-2012. It is followed by UniCredito Italiano (€ 500M approved and disbursed) and Magyar Fejlesztési Bank (€ 320M approved and disbursed).

The CEB's financing instrument in favour of MSMEs is the loan passed on through intermediaries: during 1995-2012, 63% of MSME lending was done through programme loans and 37% via project loans (see **Box 2.1**). During the same period, the average size of a loan in favour of MSMEs approved was € 40 million (189 loans). The lowest size was € 500,000 (two loans) and the highest was ≈ € 260 million (three loans). CEB lending is generally characterised by its favourable terms regarding interest rates, tenors and grace periods (see **Chapter 13**).

Box. 2.1 CEB Lending Instruments: Programme Loans and Project Loans

The traditional lending instruments, which are also the main tools for the CEB's activities in its Member States, are project loans and programme loans:

- **Project loans** refer to individual projects directly financed by the CEB, which usually relate to financing capital goods representing the "hardware" foundation of a community, such as rural and urban infrastructure, housing for low-income people or administrative and judicial infrastructure. Project loans are disbursed based on work progress.

- **Programme loans** refer to loans financed by the CEB through intermediaries, disbursed based on the absorption capacity of the borrower.

The typical CEB MSME financing loan is a programme loan, and is referred to as such throughout this study.

Table 2.1 CEB Member States (Year of Accession & Target/Non-target Countries)

CEB TARGET COUNTRIES	YEAR OF ACCESSION	CEB NON-TARGET COUNTRIES	YEAR OF ACCESSION
Turkey	1956	Belgium	1956
Cyprus	1962	France	1956
Malta	1973	Germany	1956
Bulgaria	1994	Greece	1956
Slovenia	1994	Iceland	1956
Lithuania	1996	Italy	1956
Romania	1996	Luxembourg	1956
Croatia	1997	Holy See	1973
"The former Yugoslav Republic of Macedonia"	1997	Switzerland	1974
Estonia	1998	Liechtenstein	1976
Hungary	1998	Portugal	1976
Latvia	1998	Sweden	1977
Republic of Moldova	1998	Denmark	1978
Poland	1998	Netherlands	1978
Slovak Republic	1998	Norway	1978
Albania	1999	Spain	1978
Czech Republic	1999	San Marino	1989
Bosnia and Herzegovina	2003	Finland	1991
Serbia	2004	Ireland	2004
Georgia	2007		
Montenegro	2007		

Table 2.2 Geographic Distribution of CEB Loans for Job Creation (1995-2012)

1995-2012	Approvals			Disbursements	
	MEUR	%		MEUR	%
CEB Target Countries	**3 642**	**48%**		**2 287**	**41%**
BOSNIA HERZEGOVINA	150	2%		75	1%
BULGARIA	200	3%		132	2%
CROATIA	155	2%		126	2%
CZECH REPUBLIC	65	1%		35	1%
HUNGARY	569	7%		467	8%
LATVIA	59	1%		19	0%
POLAND	998	13%		597	11%
ROMANIA	182	2%		2	0%
SERBIA	70	1%		44	1%
SLOVAK REPUBLIC	82	1%		-	0%
SLOVENIA	120	2%		119	2%
TURKEY	900	12%		618	11%
OTHERS	93	1%		55	1%
CEB Non-Target Countries	**2 637**	**34%**		**2 262**	**41%**
BELGIUM	96	1%		92	2%
FINLAND	324	4%		199	4%
FRANCE	496	6%		447	8%
GERMANY	998	13%		929	17%
ITALY	203	3%		157	3%
PORTUGAL	102	1%		92	2%
SPAIN	402	5%		333	6%
OTHERS	16	0%		13	0%
Transit loans (1)	**1 370**	**18%**		**987**	**18%**
Total	**7 648**	**100%**		**5 536**	**100%**

(1) "Transit loans" for MSME Financing benefit the final beneficiaries in target countries
(2) To present the shares as whole numbers, the percentages have been rounded and their sums may therefore not correspond to the total.

Part II. MSME SECTOR – DRIVER OF SOCIAL COHESION

Part II provides an overview of the MSME sector and its socio-economic role, with a focus on CEB Member States. Chapter 3 begins with an analysis of the MSME definition and its variations across CEB member countries. It also illustrates MSME eligibility criteria as stated in the CEB's Policy for Loan and Project Financing, and describes the differences between support to the lower-end of the MSME size spectrum and micro-financing or micro-crediting.

Chapter 4 demonstrates that the expansion of the MSME sector is closely linked to economic growth and net employment generation, which, in their turn, contribute to social cohesion. A typical EU firm is a micro-company, and it is micro-enterprises who contribute the most to total net employment growth in the EU non-financial business economy. The chapter is based both on a literature overview and empirical evidence.

Chapter 3. MSME Definitions across CEB Member Countries

Technical definitions of MSMEs vary from country to country, reflecting variations not only in the size and performance of the economy, but also in cultural and social dimensions. Generally, MSMEs are firms that are relatively small in size in terms of employment, turnover and total assets.

The number of employees is the key criterion employed in all CEB Member States. This classification is generally in line with the EU definition in all CEB member countries[23], except for Georgia (see **Table 3.1**).

In addition to the employment criterion, the turnover and/or balance sheet characteristics are applied in all CEB member countries to define MSMEs according to their size class:

- In the non-EU member countries, the turnover and/or balance sheet criteria are not harmonised and are not comparable with the EU recommendations, with the exception of Iceland (see **Table 3.1**).
- For EU member countries, the implementation of the EU definition is voluntary, but the European Commission (EC), together with the EIB and the EIF, promotes its wide application.

There is a clear distinction between the legal and statistical definitions of MSMEs in EU law. Legally, MSMEs are recognised by size, turnover, balance sheet and independence criteria (EU recommendation 2003/361 as of 6 May 2003, which entered into force in 2005).

Box 3.1 MSME Definition in the EU Law

- For legal and administrative purposes:

Enterprises	Employees	Annual Turnover	Annual Balance sheet	Autonomous
Micro enterprise	1 to 9	< 2 million euro	< 2 million euro	25% or more of the capital or voting rights of another enterprise
Small enterprise	10 to 49	< 10 million euro	< 10 million euro	
Medium enterprise	50 to 249	< 50 million euro	< 43 million euro	
Large enterprise	More than 250	> 50 million euro	> 43 million euro	

- For statistical purposes:

The main criteria of SME statistics for statistical purposes are the number of persons employed.

Source: European Commission (2004), *Recommendation 2003/361 and OECD SME Statistics: Towards a more Systematic Statistical Measurement of SME Behaviour*.

[23] MSME size definitions in Turkey and Albania were harmonised to the EU classification in 2006 and 2008, respectively. Source: IFC MSME Country Indicators 2010 Update.

In the case of the CEB, the first reference to smaller size enterprises was under **Resolution 1424 (1997)**, specifying the beneficiaries of CEB financing for job creation as **"small and medium-sized companies** in disadvantaged areas" (see **Table 1.1**). The eligibility criteria for MSMEs were formalised in the CEB's Overall Policy Framework for Loan and Project Financing in 2006, subsequently revised in 2009[24]:

- The CEB adopts the EU definition of MSMEs.
- In the case of CEB non-target countries (see **Table 2.1**), SMEs must also be situated in regions with an unemployment rate equal to or higher than the average unemployment rate within the EU. Non-target countries not members of the EU are assimilated to the EU regions.
- The unemployment rate criterion for SMEs is not applicable to target countries.
- Micro-credit programmes (see **Box 3.2**) in favour of micro-enterprises are considered for financing irrespective of the location.

Box 3.2 Micro-Financing/Micro-Crediting

CEB support to the lower-end of the MSME size spectrum has generally had a broader scope than micro-financing or micro-crediting. While both activities refer to providing assistance to individuals or firms of up to ten employees, micro-financing has its particularities:

- "Micro-finance clients are often described according to their poverty level: vulnerable non-poor, upper poor, poor, [and] very poor". [25] The term "micro-finance" is often used interchangeably with micro-credit. Micro-credit, as defined by the European Commission, is "a loan [or lease] of up to € 25 000 to support the development of self-employment and microenterprises. It has a double impact: an economic impact as it allows the creation of income generating activities and a social impact as it contributes to the social inclusion and therefore to the financial inclusion of individuals".[26]
- "The term "micro-finance", once associated almost exclusively with small-value loans to the poor, is now increasingly used to refer to a broad array of products (including payments, savings, and insurance) tailored to meet the particular needs of low-income individuals.[25]

In Europe, "in 1992, following the experience in many developing countries, microcredits began to be offered in eastern countries such as Poland, Romania, Bulgaria and the Slovak Republic. In western Europe microcredits are a much more recent development, apart from the United Kingdom and France where they are already quite established".[27]

The landscape of microfinance providers includes credit unions/financial cooperatives (e.g. Romania, Poland), NGOs (e.g. Bosnia and Herzegovina, "the former Yugoslav Republic of Macedonia", Serbia and Turkey), microfinance banks, specialised divisions of traditional banks, support schemes started by existing entities and development banks. The CEB has occasionally channelled its lending through microfinance providers, such as MicroBank[28] in Spain (see **Chapter 13**) with the objective of supporting marginalised populations such as immigrants and women.

The catalytic role of development finance institutions (DFIs) in funding micro-finance institutions (MFIs) is a matter of debate in certain markets. A MicroRate report refers to DFI overfunding in the Bosnian micro-finance sector: "As the topmost recipient of private microfinance funding, Bosnia [and Herzegovina] still constituted the largest recipient of DFI lending during 2007-08. There is little evidence that this level of DFI funding was needed."[29] In 2011, MFIs in Bosnia and Herzegovina experienced difficulties in recovering following over $ 100M of write-offs during 2007-10.[30]

[24] The CEB's Policy for Loan and Project Financing 2009. http://www.coebank.org/Upload/legal/en/ppfp_english.pdf
[25] CGAP, *Microfinance Frequently Asked Questions*, http://www.cgap.org/about/faq. Accessed on 17 January 2013.
[26] European Microfinance Network, *Microfinance in Europe*, *http://www.european-microfinance.org/europe-microfinance_en.php*. Accessed on 17 January 2013.
[27] ESADE Institute for Social Innovation (2011), *The Impact of Microcredits Report*, MicroBank
[28] The entity was renamed "Nuevo Micro Bank, S.A.U" following the re-organisation of the La Caixa Group in 2011. As the name "MicroBank" is used for commercial purposes, it will be referred to as such throughout the study for the purpose of simplicity.
[29] Von Stauffenberg, D., *et al* (2011), *Role Reversal Revisited: Are Public Development Institutions Still Crowding Out Private Investment in Microfinance?*, MicroRate
[30] Mix and CGAP (2012), 2011 Eastern Europe and Central Asia Regional Snapshot, A Mix and CGAP Presentation

Table 3.1 MSME Definitions in CEB Member Countries
Non-EU Member States

Country		Micro	Small	Medium	Source
CEB Target Countries (non-EU Member States only)					
Albania		Up to 9 employees and turnover or balance sheet up to ALL 10M (≈EUR 71k)	Up to 50 employees and turnover up to ALL 50M (≈EUR 356k)	Up to 250 employees and turnover up to ALL 250M (≈EUR 1,8M)	Law No. 1042 (2008) "On some changes and supplements in law No. 8957 (2002) on SMEs"
Bosnia and Herzegovina	Republika Srpska	Up to 10 employees	Up to 50 employees and income up to KM 4M or balance sheet up to KM 2M (≈EUR 1M)	Up to 250 employees and income up to KM 20M (≈EUR 10M) or balance sheet up to KM 10M (≈ EUR 5M)	No official definition of SMEs. The classification is based on entity laws. SMEs in Republika Srpska are defined in the "Law on support to Development of SMEs" (Official Gazette of RS; No. 119/2008. SMEs in FBiH are classified in the "Law on development of small enterprises of the FBiH" (Official Gazette of Federation B&H, No. 19/06 and 25/09). SME Development Strategy in Bosnia and Herzegovina 2009-2011. http://www.mvteo.gov.ba/vijesti/posljednje_vijesti/Default.aspx?id=1204
	Federation of BiH	Up to 10 employees and sales and/or balance sheet up to KM 40k	Up to 50 employees and sales and/or balance sheet up to KM 4M (≈ EUR 2M)	Up to 250 employees and sales up to KM 40M (≈EUR 20M), and/or balance sheet up to KM 30M (≈EUR 15M)	
Croatia		Up to 10 employees, and turnover up to HRK 14M (≈EUR 1.92M) or balance sheet up to HRK 7M (≈EUR 0.96M)	Up to 50 employees, and turnover up to HRK 54M (≈EUR 7.4M) or balance sheet up to HRK 27M (≈EUR 3.7M)	Up to 250 employees, and turnover up to HRK 216M (≈EUR 29,59M) or balance sheet up to HRK 108M (≈EUR 14,79M)	Law of Promotion of Small Business Act (NN 29/02 and NN 63/07) http://www.hbor.hr/Default.aspx?art=1088&sec=1606
Georgia		Up to 20 employees and up to GEL 500k turnover (≈EUR 0.23M)		Up to 100 employees and up to GEL 1.5M turnover (≈EUR 0,68M)	Law of Georgia "Georgian National Investment Agency"
		Annual turnover less than GEL 30k (≈EUR 13.5K)	Annual turnover less than GEL 100k (≈EUR 45K)	–	Georgian Tax Code, in force since 1 January 2011
Republic of Moldova		Up to 10 employees, MDL 3M (≈EUR 0.2M) turnover and total assets	Up to 50 employees, MDL 25M (≈EUR 1.6M) turnover and total assets	Up to 250 employees, MDL 50M (≈EUR 3,2M) turnover and total assets	Law 206-XVI (2006) on Support of SMEs; National Statistical Bureau of the Republic of Moldova
Montenegro		Up to 10 employees	Up to 50 employees and revenue or assets up to EUR 10M	Up to 250 employees, and revenue up to EUR 50M or assets up to EUR 43M	Law on Amendments and Supplements to the Law on Accounting and Auditing (Article 3a), Official Journal of Montenegro No. 80/08. www.gov.me/files/1269946125.doc
Serbia		No definition for micro enterprises	Up to 50 employees, turnover up to EUR 2.5M and/or average property value up to EUR 1M	Up to 250 employees, turnover up to EUR 10M, and average property value up to EUR 5M	Law on Accounting and Auditing. http://siteresources.worldbank.org/EXTLACOFFICEOFCE/Resources/870892-1206537144004/SerbiaSMEFinanceReportFNL.pdf

Country	Micro	Small	Medium	Source
"The former Yugoslav Republic of Macedonia"	Up to 10 employees, turnover up to EUR 50k, and not more than 80% of the gross income should come from one client	Up to 50 employees, turnover and average value of assets in the last two years up to EUR 2M	Up to 250 employees, turnover up to EUR 10M, and average value of assets in the last two years up to EUR 11M	Law on Trade Companies, Official Gazette 28/04 Article 470. http://www.apprm.gov.mk/webdata/dokumenti/SME%20Observatory%202007.pdf
Turkey	Up to 10 employees and turnover/total assets up to TL 1M (≈EUR 408K)	Up to 50 employees and turnover/total assets up to TL 5M (≈EUR 2M)	Up to 250 employees and turnover/total assets up to TL 25M (≈ EUR 10M)	The Small and Medium Enterprises Development Organization (KOSGEB). SME Strategy and Action Plan 2011–2013.
CEB Non-Target Countries (non-EU Member States only)				
Iceland	No definition for micro enterprises	Up to 50 employees, turnover up to EUR 2M and/or balance sheet up to EUR 2M	Up to 250 employees, turnover up to EUR 50M, and/or balance sheet up to EUR 43M	Law Gazette (Act No. 152/2009) http://eng.fjarmalaraduneyti.is/media/log-reglur/Act_No_152_2009.pdf EC Iceland Screening Report (2011): Icelandic SME policy is regularly evaluated in the SME performance review of the European Commission.
Norway	No definition for micro enterprises	Up to 50 employees, turnover up to NOK 60M (≈EUR 8M) and/or balance sheet up to NOK 30M (≈EUR 4M)	No definition for medium enterprises	Accounting Act July 17 1998 No. 56 (Sections 1-6). http://ec.europa.eu/enterprise/policies/sme/business-environment/files/annexes_accounting_report_2011/norway_en.pdf. No official definition. The statistical standard classifies enterprises into eight groups (0 employees, 1-4 employees, 5-9 employees, 10-19 employees, 20-49 employees, 50-99 employees, 100-249 employees, 250+ employees). These groups can be aggregated to the EU's official classification following the number of employees. http://www4.ssb.no/stabas/ItemsFrames.asp?ID=4536002&Language=en
Switzerland	Up to 10 employees, and turnover up to CHF 2M (≈EUR 1.7M)	No definition for small enterprises	Up to 200 employees, turnover up to CHF 40M (≈EUR 33M) and/or balance sheet up to CHF 20M (≈EUR 16M)	Swiss Code of Obligations (CO). Micro enterprises are defined by the Competition Commission (COMCO, 2005). Medium enterprises defined in the Merger Law (art. 2e). http://www.kmu.admin.ch/politik/00100/00102/index.html?lang=fr http://www.weko.admin.ch/org/index.html?lang=en For statistical purposes, the size definition is similar to the EU definition. http://www.bfs.admin.ch/bfs/portal/en/index/themen/06/02/blank/key/01/groesse.html

Sources:
OECD *et al.* (2012), *SME Policy Index: Eastern Partner Countries 2012. Progress in the Implementation of the Small Business Act for Europe*, OECD Publishing.
OECD *et al.* (2012), *SME Policy Index: Western Balkans and Turkey 2012. Progress in the Implementation of the Small Business Act for Europe*, OECD Publishing.

Chapter 4. The Socio-Economic Role of MSMEs

In recent decades, the relation between the average enterprise size and economic development has been shifting towards smallness. In the first three quarters of the twentieth century, economic development signified economies of scale. However from the 1970s onwards, MSMEs have played an increasingly important role in global economies, including European countries:

"Despite ever-larger and noisier mergers, the bigger change coming over the world of business is that firms are getting smaller. The trend of a century is being reversed. Until the mid-1970s, the size of firms everywhere grew; the number of self-employed fell… No longer. Now it is the big firms that are shrinking and small ones that are on the rise."[31]

Beck et al (2005) find a robust, positive relationship between the relative size of the MSME sector and **economic growth**.[32] Ayyagari et al (2005) revealed a significant variation in the size and economic activity of the MSME sector across income groups – countries with a higher level of GDP/capita have larger MSME sectors. These findings are also valid for CEB member countries – in CEB higher income countries, formal MSMEs are not only denser in the business structure, but also employ a higher percentage of the workforce (see **Graph 4.1** and **Graph 4.2**). If the contribution of both formal and informal MSMEs was taken into consideration, the income group differences would level out. This is of particular importance in Central and Eastern European countries, where the size of the informal economy[33], which consists of mostly micro and small enterprises, is substantial in comparison with the rest of CEB member countries (see **Figure 4.1**). As income increases, the share of the informal MSME sector decreases and that of the formal MSME sector increases. According to the Vienna Institute for International Economic Studies, "self-employment is the most common type of informal sector employment, attracting for the most part women, young people and the ill-educated."[34]

The positive relationship between the size of the SME sector and economic growth does not translate automatically into a causal relationship. Overall, there is a lack of empirical research that would prove that MSMEs are the cause of growth, or that they alleviate poverty or decrease income inequality. Nevertheless, Dalberg's "Report on Support to SMEs in Developing Countries Through Financial Intermediaries" (2011), which summarises key economic studies on MSMEs, points out that "with lack of empirical research, it is often hard to distinguish between an absence of evidence and evidence of absence."

Globally, the evidence regarding the argument that MSMEs create more jobs than large firms is fundamentally mixed. While Ayyagari et al (2011) identify highest job growth in small and medium entities and firms up to 2 years old in a panel of 99 developing economies, studies for the US show little evidence that small firms create more jobs (Davis et al, 1996; Neumark et al, 2011), and find the importance of a firm's age, rather than size, in both gross and net job creation, notably through the contribution of start-ups and surviving businesses up to 5 years old (Haltiwanger et al, 2010). Research on European countries, however, identifies MSMEs as the key engine of **job growth in the private sector** (see **Box 4.1**), often citing entrepreneurship and high growth MSMEs as key drivers of employment creation.

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[31] A 1989 quotation from The Economist contained in Acs, Zoltan J., *et al.* (1996), *Small Business in the Modern Economy,* Cambridge, MA

[32] Ardic, Oya P., *et al.* (2011), *Small and Medium Enterprises. A Cross-Country Analysis with a New Data Set*, The World Bank

[33] "**The shadow economy** includes all market-based legal production of goods and services that are deliberately concealed from public authorities for any of the following reasons: (1) to avoid payment of income, value added or other taxes, (2) to avoid payment of social security contributions, (3) to avoid having to meet certain legal labour market standards, such as minimum wages, maximum working hours, safety standards, etc., and (4) to avoid complying with certain administrative procedures, such as completing statistical questionnaires or other administrative forms." Source: Schneider, F., *et al.* (2010), *Shadow Economies All over the World. New Estimates for 162 Countries from 1999 to 2007,* The World Bank

[34] Vidovic, H. (2012), *Labour Market Issues in Europe's Eastern and Western Balkan Neighbours*, the Vienna Institute for International Economic Studies, Monthly Report.

Box 4.1: Do MSMEs generate more jobs?[35]

The study entitled "Do SMEs Create More and Better Jobs?" published by the European Commission in 2012 provides statistical evidence supporting the vital contribution of MSMEs in European economies, accounting for 85% of the net new jobs created during 2002-2010 and more than two-thirds of the total employment in the non-financial business economy (2010). The study shows that in the EU, MSMEs create more jobs than large enterprises. In most of the EU countries, job creation by the MSME sector has been more than proportionate relative to its share in employment.

Enterprise size class

During 2002-2010, the total number of jobs in the EU-27 non-financial business economy increased by 1.1M annually, equivalent to an annual growth of 0.9% corrected for the population effect[36] – see **Table 4.2 in Statistical Annex**:

- 0.9M of these newly created jobs (85%) can be attributed to MSMEs.
- Only 0.2M (15%) to large companies.

MSMEs also had a significantly higher net employment growth rate (1% annually) than large enterprises (0.4%) – see **Table 4.3 in Statistical Annex.**

Within the MSME size class, micro-enterprises contributed the most to total net employment growth in the non-financial business economy. They accounted for 58% (see **Table 4.2 in Statistical Annex**) of total net employment growth and registered an annual net employment growth rate of 1.7% (see **Table 4.3 in Statistical Annex**) – the highest rates among all enterprise size classes.

MSME age class[37]

Within the MSME age class, in 2008 most employment was found in established enterprises, i.e. 10 years or older (see **Figure 4.2 in Statistical Annex**), while employment creation was negatively correlated with the age of firms, being mainly attributed to surviving newly born enterprises during 2005/2008 (see **Figure 4.3 in Statistical Annex**). This finding is in line with the study undertaken by Haltiwanger et al (2010) mentioned at the beginning of the Chapter 4.

Surviving newly born MSMEs accounted for the major part of employment growth during 2005-2008, which more than compensated for the employment destruction caused by enterprise deaths in all age groups and size classes (but of which a majority can be attributed also to new born enterprises).

A further increase in the number of newly born enterprises does not automatically translate into a total employment increase:

- The group of newly born SMEs does not consist only of start-ups – the initial size of start-ups and their further growth during the first years create new jobs, but spin-offs, mergers, and acquisitions are less likely to create new employment.
- Fewer than half of start-ups survive for more than five years and only a fraction develop into high-growth firms which make significant contributions to job creation.
- One half of newly created firms have disappeared after five years.

Generally, more empirical evidence is needed to understand the importance of age as opposed to size of firm in European countries.

[35] This text box is based on: (i) EIM Business & Policy Research (2011), *Do SMEs Create More and Better Jobs?,* European Commission (2012), (ii) OECD, *Small Business, Job creation and Growth: Facts, Obstacles and Best Practices*, and (iii) Kraemer-Eis, H., *et al.* (2012), *European Small Business Finance Outlook, May/2012*, European Investment Fund

[36] "**The population effect** – changes in the classification of enterprises in size classes due to growth or shrinkage. If an individual SME grows from 200 to 300 employees, it is clear that SMEs have made a positive contribution to employment growth. However, as captured by statistics on employment levels by size class, the employment level of SMEs actually decreases, because this firm no longer belongs to the SME size class. Thus, the number of jobs in the SME size class actually drops by 200 employees, while the employment level in the size class of large enterprises increases by 300 jobs. Because of this population effect, changes in the employment levels of size classes do not give information on which part of the overall employment changes can be attributed to the different size classes." Source: EIM Business & Policy Research (2011), *Do SMEs Create More and Better Jobs?,* European Commission (2012)

[37] **MSME age class**: newly born enterprises (up to five years old); young enterprises (from five to ten years old); and established enterprises (ten years and older).

In 2008[39] a total of ≈20.9M MSMEs, including zero size class enterprises, i.e. enterprises with no paid employees, were registered in the EU-27. They accounted for 58.6% of GDP and 66.7% of jobs (see **Table 4.1**). The typical European firm is a micro firm. Particular attention is paid to the potential for employment growth of zero size class enterprises. While the average enterprise employs six persons, about half of all EU enterprises in industry, construction and services, and two-thirds of all newly born enterprises, i.e. up to five years old, were registered as zero size class in the EU-27 non-financial economy in 2007. However, many of them did not register growth.

Table 4.1. MSME Sector in the EU-27

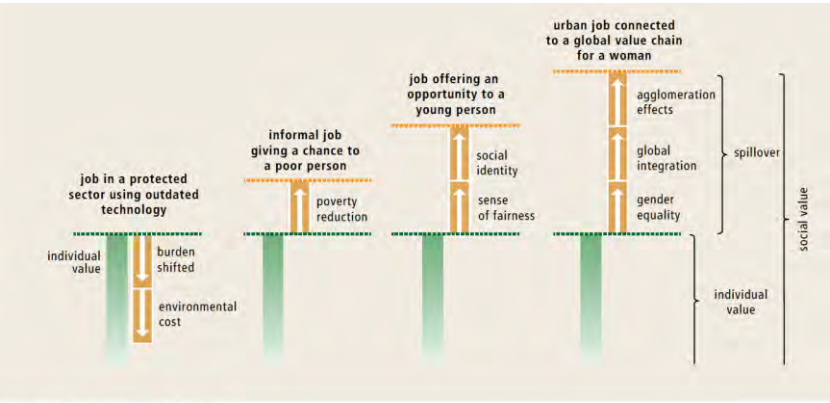
2008	Number of enterprises	Persons employed	Value added[38]
	Share in total (%)		
All enterprises	100.0	100.0	100.0
All SMEs	99.8	66.7	58.6
Micro	92.0	29.0	21.8
Small	6.7	20.5	18.6
Medium-sized	1.1	17.2	18.2
Large	0.2	33.3	41.4

Source: Eurostat Pocketbooks (2011), *Key figures on European business with a special feature on SMEs,* Eurostat and European Commission

In the EU-27, the contribution of MSMEs to total value added was lower than their contribution to employment (see **Table 4.1**). This is mostly due to the inherent characteristics of MSMEs, such as inability to benefit from economies of scale and/or to adopt or develop innovations, and low level of capital intensity. This could also be explained by MSMEs engaging in sectors of industry with low productivity, such as construction and the retail trade. Thus, while MSMEs employ a large portion of employees and create most jobs, their contribution to productivity is lower than that of large enterprises (see **Figure 4.4 in Statistical Annex**).

Nevertheless, it is generally agreed that the expansion of the MSME sector is closely linked to economic growth and job creation, which, in their turn, contribute to **social cohesion** by reducing poverty, increasing productivity, and raising the standard of living of poor people (see **Figure 4.5**)[40].

Figure 4.5 Social Value of Jobs



Source: The World Bank (2012), *World Development Report 2013: Jobs,* International Bank for Reconstruction and Development/The World Bank

[38] **Value added** per occupied person – a measure for the efficiency with which enterprises contribute to GDP – is found to be positively correlated with enterprise size.

[39] Latest available data at the time of writing

[40] Joint Report of 31 Multilateral and Bilateral Development Finance Institutions (2011), *International Finance Institutions and Development Through the Private Sector*, International Finance Corporation

The MSME sector directly reaches local populations, including the informal sector and disadvantaged populations, and contributes to their well-being:

- Poor people identify employment – whether through self-employment or from receiving a salary – as "their best prospect for escaping poverty"[41].
- "A successful private sector, [notably MSME sector], expands the variety and reduces the costs of goods and services, including those consumed by poor people".
- Supporting MSMEs by addressing difficulties, such as "insecure property rights, corruption, policy unpredictability, and limited access to finance and public services, increases [their] incentives to join the formal economy."[42] The shift to formal production supports the creation of a strong middle class and contributes to strengthening democratisation and the rule of law (Africa Commission, 2009).
- Micro-enterprises play an important social role in re-integrating long-term unemployed and the elderly into the labour market, engaging the highest percentage of long-term unemployed and people aged 50+. This is of particular importance in the European context of demographic contraction, ageing population and economic crisis: in 2010, 28.5% of the EU working age population (aged 15-64) was 50+ years old and 43% of the unemployed were long-term unemployed (see **Chapter 12**).
- The overall job quality (see **Box 4.2**) in the EU, based on reported job satisfaction, is highest among MSMEs. Employees in MSMEs report higher job satisfaction in terms of the "soft" side of work relationships, such as work climate, working time arrangement, or work-life balance. Nevertheless, when it comes to "hard" dimensions or "employment quality" (training and career opportunities, remuneration levels) large firms are best positioned, followed by small and medium-sized enterprises. Small firms tend to invest less in training and rely more on external recruitment for raising competence. High job turnover poses problems for employment security, and small establishments are often exempt from giving notice to their employees. In addition, "the average wage in large enterprises was 2.6 times higher than in micro-firms in 2010"[43].

Box 4.2 Job Quality[44]

Generally, job quality refers to two dimensions:

- Employment quality – which refers to contractual aspects of the job, such as employment agreement, working hours, remuneration etc.; and
- Work quality – which denotes material characteristics of the job, such as work autonomy, intensity of work, physical working conditions etc.

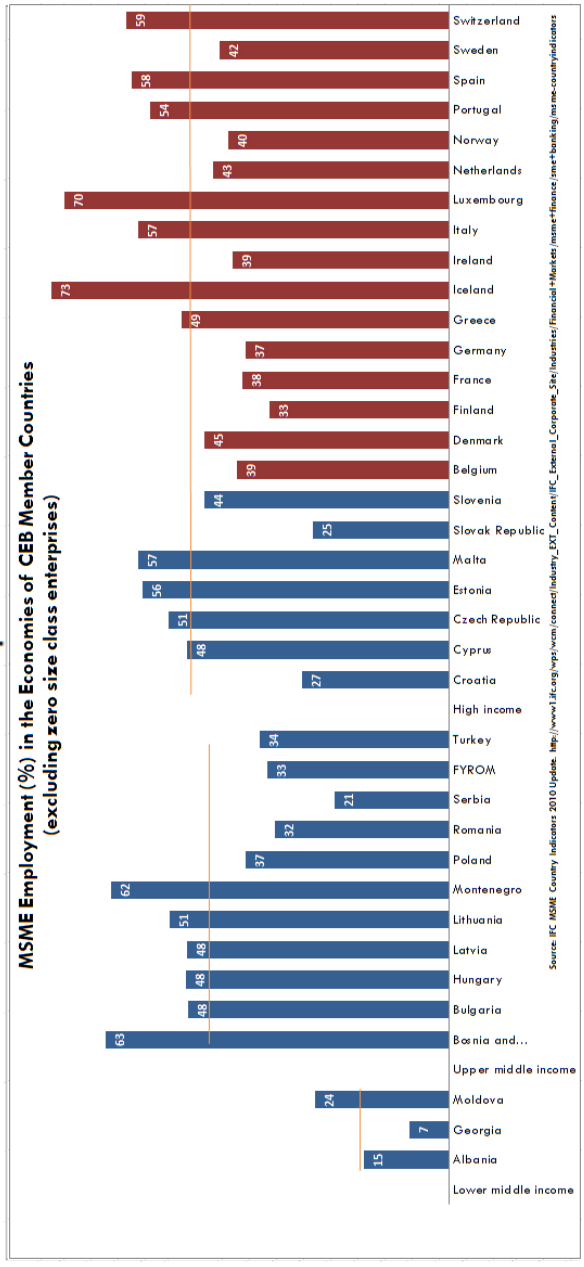
[41] Joint Report of 31 Multilateral and Bilateral Development Finance Institutions (2011), *International Finance Institutions and Development Through the Private Sector*, International Finance Corporation

[42] Development and Cooperation – EUROPEAID (2012), *Private Sector Development*, European Commission. http://ec.europa.eu/europeaid/what/economic-support/private-sector/private_sector_en.htm

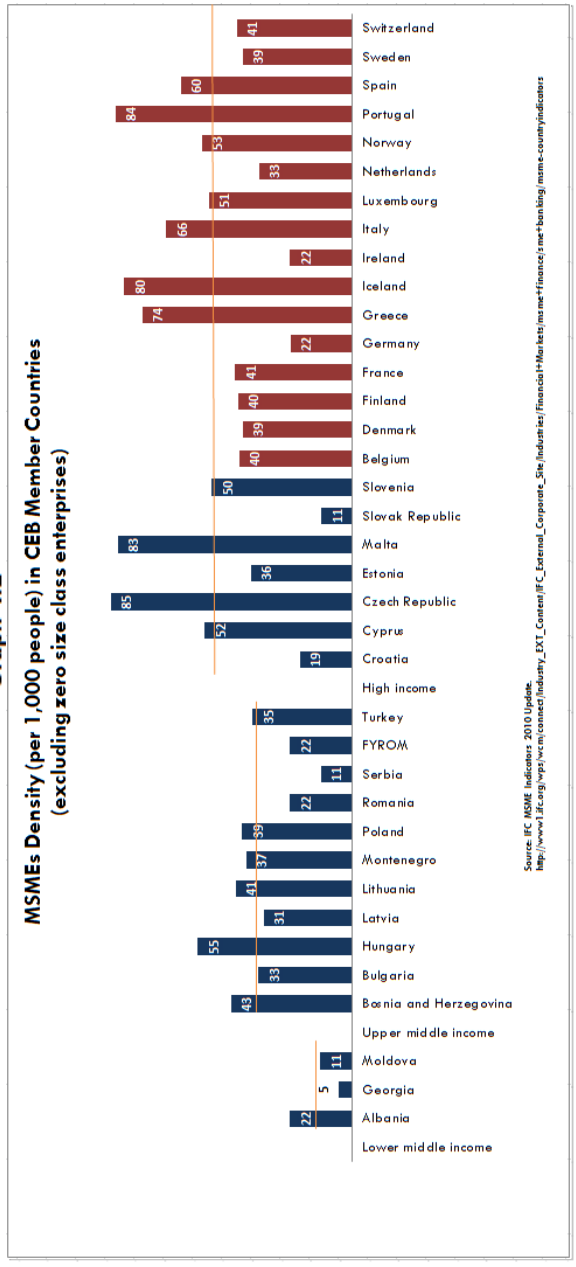
[43] Wymenga, P *et al.* (2011), *Are EU SMEs Recovering from the Crisis? Annual Report on EU Small and Medium sized Enterprises 2010/2011*, European Commission, DG-Enterprise.

[44] The text in this section is based on: EIM Business & Policy Research (2011), *Do SMEs Create More and Better Jobs?*, European Commission (2012)

Graph 4.1

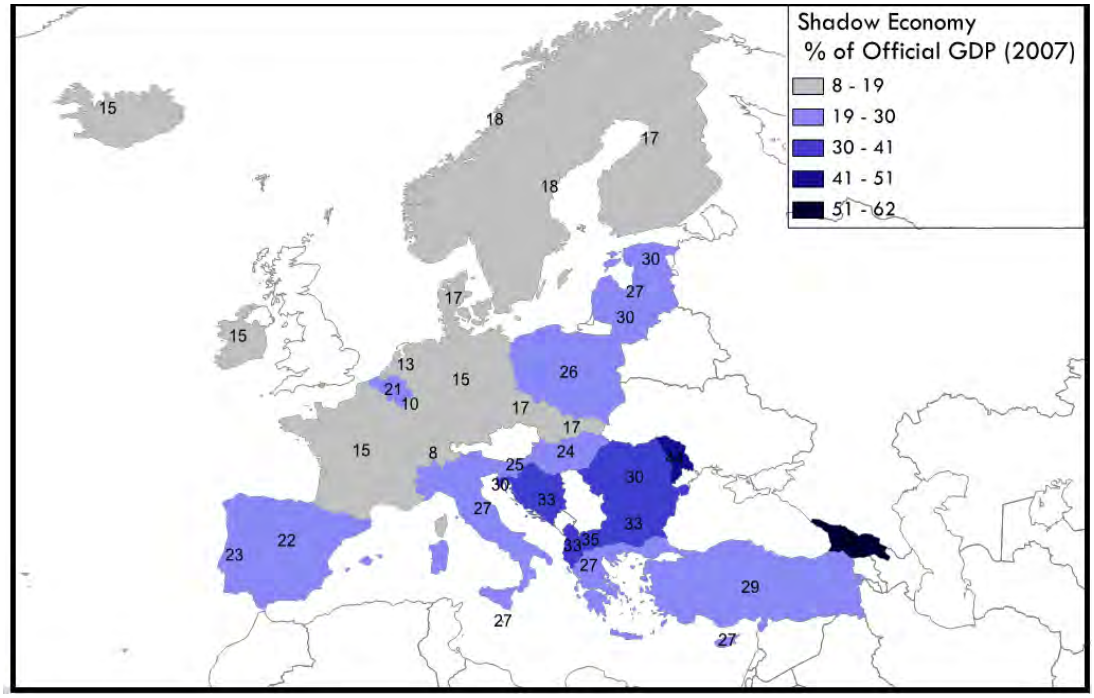


Graph 4.2



Available data for all CEB member countries from single and/or comparable sources excludes zero size class enterprises: These own graphs are based on the IFC MSME Country Indicators 2010 Database, which contains indicators for all CEB member countries but does not include data on zero size class enterprises. The line represents the average figures per income groups of countries reflected in the graphs. The classification follows the World Bank Atlas Method as of 2012 (lower middle income, upper middle income, and high income).
Source: Kushnir, K. *et al.* (2010), *Counting MSMEs across the World*, International Finance Corporation/The World Bank.

Figure 4.1. Size of the Informal Economy in CEB Member Countries (2007)



Source: The data in this own map is taken from: Gill, I., *et al.* (2012), *"Golden Growth. Restoring the Lustre of the European Economic Model"*, International Bank for Reconstruction and Development/International Development Association/The World Bank.
No data available for Montenegro and Serbia

PART III. OBSTACLES FACING MSMEs IN FULFILLING THEIR SOCIO-ECONOMIC POTENTIAL

Part III describes the key concerns cited by MSMEs in the EU and analyses the variations of "access to finance" as a pressing problem of MSMEs across CEB member countries (Chapter 5).

Chapter 6 shows that across CEB member countries MSMEs tend to be underserved and face difficulties in accessing external financing, namely bank financing, and it is the larger and more mature enterprises that are more likely to obtain the requested external financing. The evidence is based on the EC/ECB Survey on SMEs' Access to Finance (SAFE) conducted in 2011.

The rejection for external financing is mostly associated with supply side constraints, rather than weak demand. Chapter 7 lists market imperfections as explanations of these supply side constraints, and identifies leasing and factoring as preferred alternative sources of external financing to traditional bank financing, especially in CEB target countries. In this context, Chapter 7 also provides an overview of the Bank's operations, as of 2004, with leasing companies as an MSME financing instrument in its target countries.

Chapter 5. Key Obstacles Perceived by MSMEs

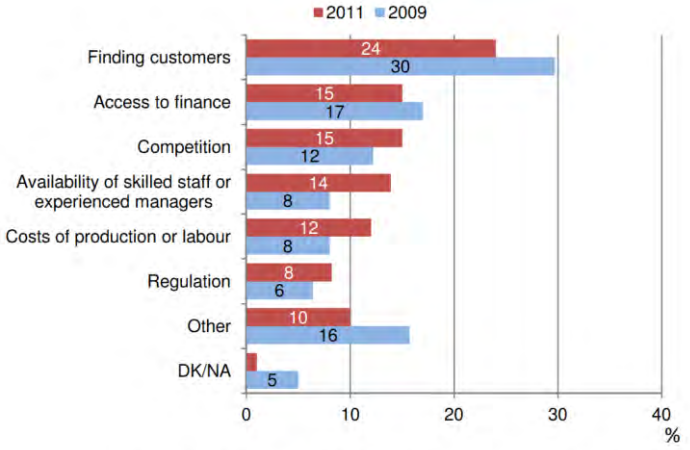
The dominant concern for MSMEs remains "finding customers" both during recession and the recovery, being cited by 30% of MSMEs in 2009 and 24% in 2011 (see **Figure 5.1**). These responses reflect the cyclical nature of demand for the MSME output.

MSMEs in the EU-27 perceive "access to finance" as their second most pressing problem, along with "competition". In 2011, 15% of MSMEs reported "access to finance" among the top concerns, a slight drop from the 2009 level of 17%.

In the EU-27, newly born MSMEs listed "Finding Customers" and "Access to Finance" as their most pressing difficulties, both at ≈20%.

One fundamental problem in dealing with the MSME financing gap[45] is lack of basic information about the size of the gap[46].

Figure 5.1 The Most Pressing Problems of MSMEs in the EU-27



Q0. What is currently the most pressing problem your firm is facing?: All SMEs, % EU-27

Source: Ipsos Mori (2011), SMEs' Access to Finance Survey. Analytical Report, European Commission, Enterprise and Industry.

According to the OECD, most of the indicators are based on supply-side data from financial institutions or government agencies. In order to get a complete picture, quantitative demand-side data, as collected by MSME surveys, should be integrated in the analysis.[47] However, quantitative demand-side surveys are rare, and the only evidence is often in the form of complaints from MSMEs themselves

[45] "There is no commonly agreed definition of the **SME financing gap**, but the term is basically used to mean that a sizeable share of economically significant SMEs cannot obtain financing from banks, capital markets or other suppliers of finance. Furthermore, it is often alleged that i) many entrepreneurs or SMEs that do not currently have access to funds would have the capability to use those funds productively if they were available; ii) but due to structural characteristics, the formal financial system does not provide finance to such entities." Source: OECD (2006), *The SME Financing Gap: Theory and Evidence.*

[46] OECD Policy Brief (2006), *Financing SMEs and Entrepreneurs.*

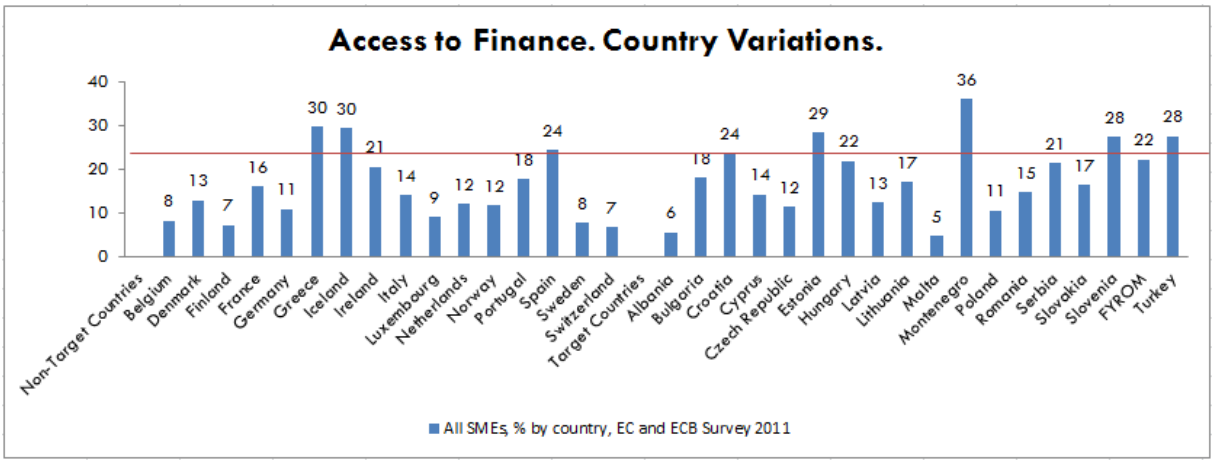
[47] OECD (2012). *Financing SMEs and Entrepreneurs 2012: An OECD Scoreboard.*

reflected in various qualitative opinion surveys. In Europe, one such example is the Survey on SMEs' Access to Finance (SAFE) [48] conducted every two years by the EC and the ECB (see **Graph 5.1**):

- In CEB target countries, "access to finance" is the most pressing problem in Montenegro, Estonia, Slovenia, Croatia and Serbia mentioned by over more than one in five MSMEs, and is ranked the second most dominant issue in Turkey, "The former Yugoslav Republic of Macedonia", and Lithuania.

- In CEB non-target countries, MSMEs cited "access to finance" as the most pressing problem in Greece, Iceland and Spain, and as the second most important issue in Ireland and Portugal.[49]

Graph 5.1. Access to Finance. Variations across CEB Member Countries*.



*Own graph based on the 2011 Survey on SMEs' Access to Finance conducted by EC and ECB across 38 countries. The red line indicates the EU average. *Data is not available for Bosnia and Herzegovina, Georgia and the Republic of Moldova.*

Source: Ipsos Mori (2011), SMEs' Access to Finance Survey. Analytical Report, European Commission, Enterprise and Industry.

[48] The survey on SMEs' Access to Finance (SAFE), conducted by the EC and the ECB every two years, shows results at an aggregated EU-27 level. SAFE surveys were undertaken in June-July 2009 and August-October 2011. This Part III of the study details the conclusions of the 2011 survey and focuses on findings related to the EU-27.

[49] Ipsos Mori (2011), *SMEs' Access to Finance Survey. Analytical Report,* European Commission, Enterprise and Industry.

Chapter 6. MSMEs' Limited Access to External Financing

Across Europe, MSMEs usually rely on the following sources of external financing (see **Figure 6.1 in Statistical Annex**):

- Overdrafts and credit lines;
- Leasing, hire-purchase and factoring;
- Trade credit; and
- Bank loans.

According to the 2011 Survey on SMEs' Access to Finance (SAFE), banks are the most common provider of loans to MSMEs in the EU, with 87% of MSMEs that got a loan obtaining the loans from banks. Bank loans are also the most favoured source of external financing, cited by 63% of MSMEs that expect to grow in the coming years. [50]

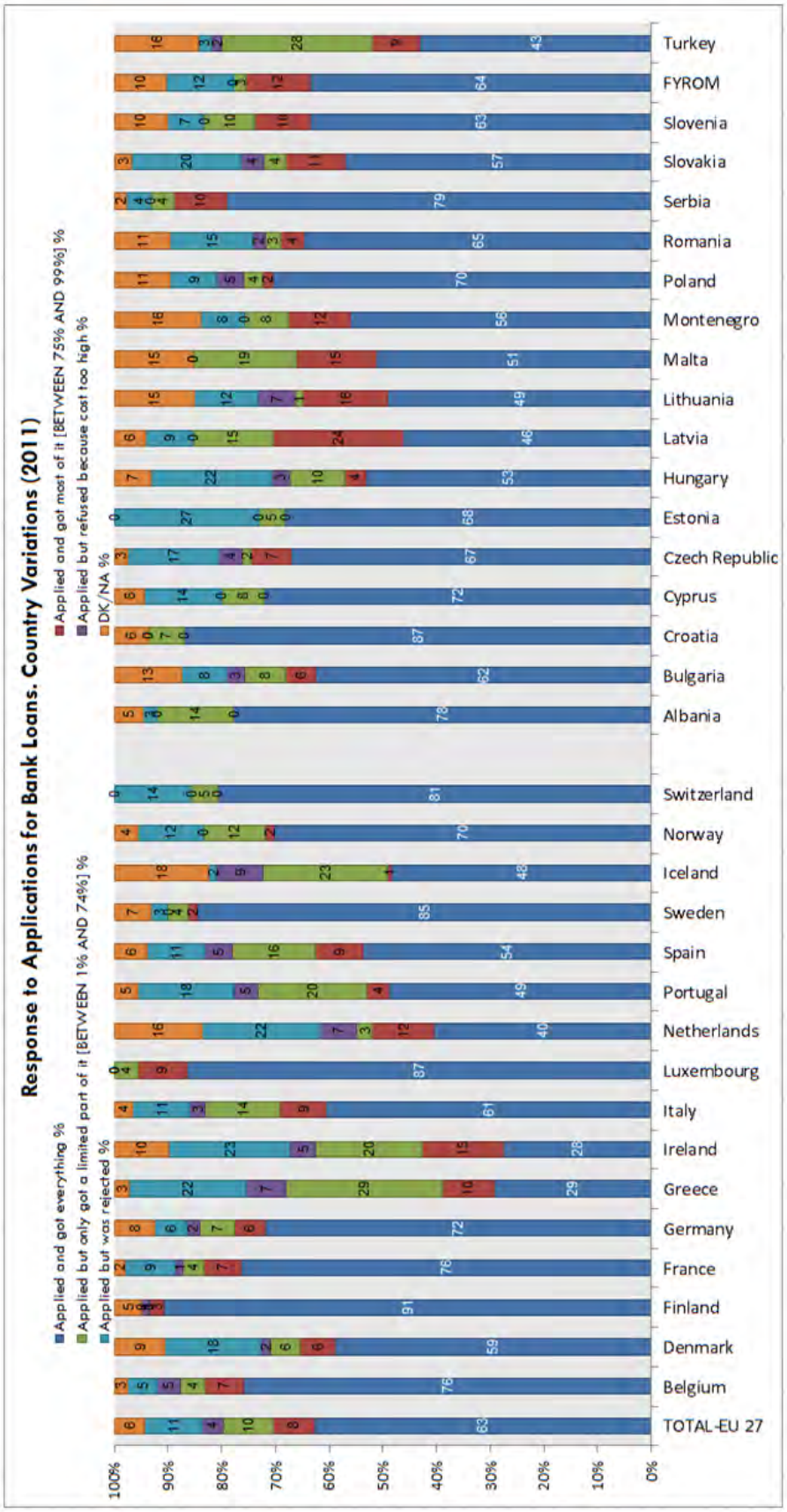
Nevertheless, MSMEs are underserved and it is the larger and mature enterprises that are more likely to obtain the requested external financing. About one third of MSMEs did not obtain the finance they had planned for – only 63% of MSMEs that applied for a bank loan obtained the full loan (see **Figure 6.2 in Statistical Annex**), as opposed to 77% of large enterprises. According to SAFE, younger and smaller enterprises are generally more likely to receive only partial financing, and to be immediately rejected. The highest rejection rate is among micro enterprises and MSMEs active between 2 and 5 years[52]. At the CEB country level, countries where MSMEs were less likely to obtain everything they requested when applying for a bank loan were Ireland, with only 28% of MSMEs citing that they got everything and 23% were rejected outright, and Greece, with 29% of MSMEs got everything and 22% were rejected. As a comparison, at the EU level 63% of MSMEs got everything and 11% were rejected (see **Graph 6.1a**). When applying for bank overdraft, only 7% of MSMEs in Greece, 22% in Turkey, 24% in Albania, 31% in "the former Yugoslav Republic of Macedonia", 34% in Ireland, and 40% in Montenegro got everything as opposed to the EU average of 61% (see **Graph 6.1b**).

The most cited limiting factors to get bank financing are "insufficient collateral or guarantee" and "interest rates or prices that are too high", with one in five MSMEs citing them as limitations to their ability to attract potential financing. The proportion of MSMEs perceiving interest rates to be too high marginally reduced from 24% in 2009 to 20% in 2011 (see **Figure 6.3 in Statistical Annex**). However, over a half of MSMEs that applied for a bank loan reported that interest rates have been increased by the bank over the last six months[52].

The rejection for external financing is mostly associated with supply side constraints, rather than weak demand. According to the IFC, microeconomic studies of MSME behaviours indicate that the finance gap is on the supply side[51]. According to SAFE, in 2011 twice as many MSMEs in the EU perceived that banks have become less willing to provide a loan (27%) rather than more willing (13%). In 2009 the perception was more negative with approximately 4 times as many MSMEs citing that banks willingness has deteriorated (32%) rather than improved (7%). In CEB target countries, the highest level of deteriorations was cited in Romania (41%), Slovenia (38%) and Montenegro (33%). In CEB non-target countries, the highest levels of deteriorations were perceived in Spain (50%), Greece (46%), Ireland (38%), and Portugal (36%)[52].

[50] Ipsos Mori (2011), *SMEs' Access to Finance Survey. Analytical Report,* European Commission, Enterprise and Industry.
[51] International Finance Corporation (2010), *The SME Banking Knowledge Guide. IFC Advisory Services. Access to Finance.*

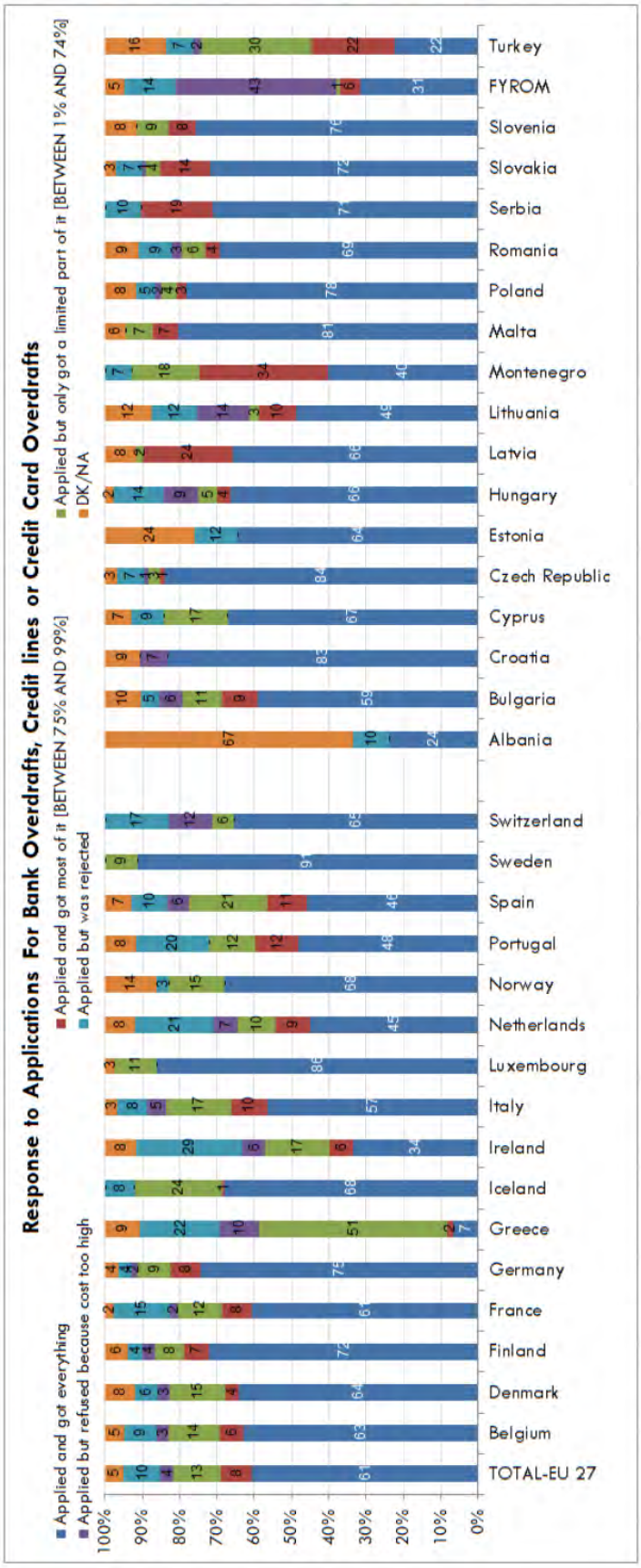
Graph 6.1b. Response to MSME Applications for External Bank Financing. Variations across CEB Member Countries*.



*This own graph is based on the 2011 Survey on SMEs' Access to Finance conducted by EC and ECB across 38 countries. *Data is not available for Bosnia and Herzegovina, Georgia and the Republic of Moldova.*

Source: Ipsos Mori (2011), SMEs' Access to Finance Survey. Analytical Report, European Commission, Enterprise and Industry.

Graph 6.1b. Response to MSME Applications for External Bank Financing. Variations across CEB Member Countries*.



*This own graph is based on the 2011 Survey on SMEs' Access to Finance conducted by EC and ECB across 38 countries. *Data is not available for Bosnia and Herzegovina, Georgia and the Republic of Moldova.*

Source: Ipsos Mori (2011), *SMEs' Access to Finance Survey. Analytical Report*, European Commission, Enterprise and Industry.

Chapter 7. Imperfections in the MSME Lending Market. CEB Support under Leasing.

In a perfect financial market, the differences between large and smaller enterprises such as profitability, growth, and probability of survival would be reflected in higher interest rates or less favourable terms of debt financing for smaller entities. In reality, there are market imperfections that limit the willingness of banks to engage in MSME financing and/or increase further the cost of financing:

- Asymmetric information: MSMEs tend to be opaque with "outsiders", namely with traditional banks or tax authorities, and it is usually the "insiders" who have more and better information about the expected profits, strategic goals, and/or ownership structure. This phenomenon leads to higher transaction costs relative to the small size of MSMEs operations and their greater risk of failure, reflected in higher interest rates.

  Higher interest rates lead to adverse selection by deterring "good borrowers" and attracting "bad borrowers", which increase the overall risk profile of borrowers. To counter this effect, banks may consider instead "deny[ing] credit to a random set of borrowers, (i.e. credit rationing)"[52].

  Theoretically, there are two solutions to manage the asymmetry of information: the provision of collateral, i.e. signalling of creditworthiness, and the pursuit of long-term relationships with clients[52], i.e. screening:

  - Provision of collateral – applied by traditional banks as reflected in the credit constraints perceived by MSMEs (see **Figure 6.3 in Statistical Annex**). The collateral requirement "may [however] lead to situations in which lending is not based on expected return but rather on access to collateral[53]".

  - Pursuit of long-term relationship with clients – practised mainly by micro-finance providers.

- Immature financial markets, such is the case in most of CEB target countries where financial sectors are shallower and less inclusive in comparison to the Western European countries, as referenced to the EU average (see **Chapter 8**):

  - Banks in countries with immature (shallow) financial systems usually face little competition, and thus little incentives, to take additional risks and to operate actively in the MSME market, as their core markets are sufficiently profitable. The core markets are usually related to ownership or ties to industrial interests or government targeting to develop specific sectors. According to the IFC, in mature financial systems competition in existing markets is one of the reasons cited by commercial banks for focusing "downstream" and serving MSMEs[54].

  - Banks in developing countries are often reliant on short-term liabilities, such as deposits. They are thus challenged to avoid the mismatch in the maturities of assets and liabilities and tend not to provide longer term financing, terms most preferred by MSMEs.

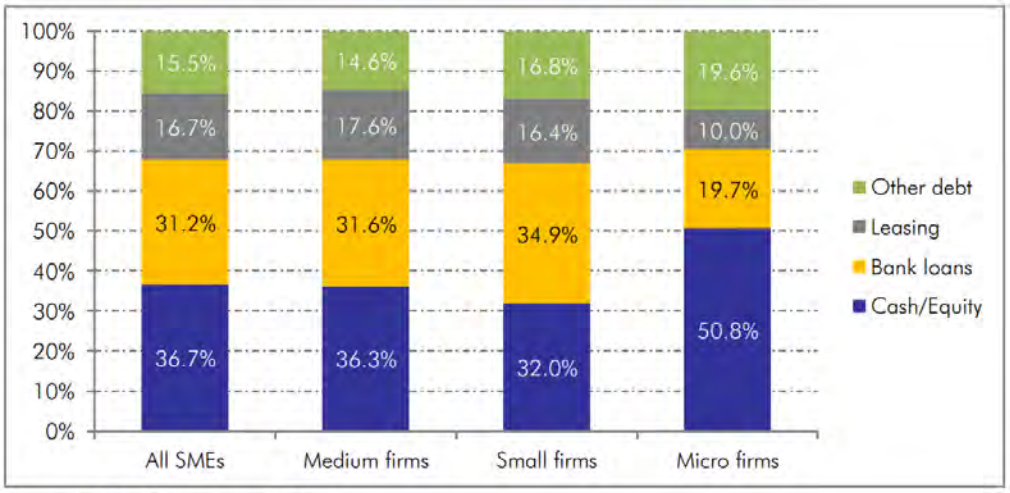
These market imperfections and the inherent characteristics of smaller entities create an environment in which MSMEs are more likely to be either (i) credit rationed/unserved, or (ii) underserved, i.e. have a certain access to external financing, but not sufficient, because of credit constraints for example.

In this context, leasing and factoring have become important alternative sources of MSME financing to bank loans and overdrafts (see **Figure 6.1 in Statistical Annex**). Compared to traditional lending, which makes cash available to MSMEs, leasing provides with tangible asset with no additional collateral required, as the asset itself is the collateral for the transaction.[55] It is often seen as a source of medium- and long-term financing and it is considered "last financing resort"[55]. It has been gaining a high relevance

[52] Canton, E., *et al.* (2011), *Investigating the Perceptions of Credit Constraints in the European Union.*
[53] OECD, SMEs and Entrepreneurship, "*Small Businesses, Job Creation and Growth: Facts, Obstacles and Best Practices*".
[54] International Finance Corporation (2010), *The SME Banking Knowledge Guide. IFC Advisory Services. Access to Finance*
[55] Kraemer-Eis, H., *et al.* (2012), *The Importance of Leasing for SME Finance,* European Investment Fund (EIF), Research and Market Analysis.

as a result of the consequences of the crisis, such as Basel III regulations and deleveraging of Western European banks (see **Chapters 9** and **11).** The advantage is also shown by relatively lower rejection rates (see **Graph 7.1**) compared to applications for bank loans or overdrafts (see **Graph 6.1a** and **Graph 6.1b**). At the EU-level, 71% of MSMEs that applied for leasing or factoring or other source of external financing except for overdraft, bank loan or trade credit, got everything, as opposed to 63% of MSMEs that applied for bank loan and 61% that applied for bank overdraft, credit line or credit card overdraft. Nevertheless, the share of investments financed by leasing is smaller than that financed by bank loans or "other debt" (see **Figure 7.1**).

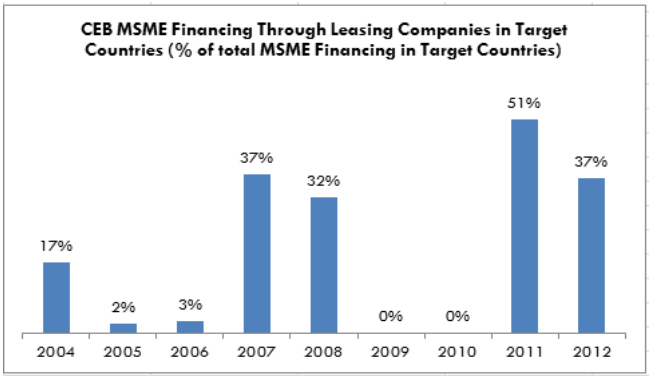
Figure 7.1. SMEs' Fixed Asset Investment Financed by Different Sources (2010)



Source: Kraemer-Eis, H., *et al.* (2012), *The Importance of Leasing for SME Finance,* European Investment Fund (EIF), Research and Market Analysis. *The graph, based on 8 EU member states and nine industrial sectors, was prepared by Oxford Economics. The authors consider the findings representative for the Europe as a whole.*

From 2004, the CEB started to use leasing as an MSME financing instrument in its target countries by providing medium- to long-term financing to leasing companies. During 2004-2012, 21% of CEB MSME financing in target countries, or € 1 billion, was done through leasing. 2011 was the year which registered the highest share of leasing operations of 51%, 2005 and 2006 had low shares of 2% and 3%, respectively, and 2009 and 2010 being the years when leasing was not used (see **Graph 7.2.**). The CEB's 2011 Annual Report on Project Preparation and Follow-Up concluded that leasing was a particularly effective way to reach small firms. The Bank's on-site visits to sub-projects financed by leasing companies systematically reported that the lease instrument allowed small firms to obtain needed capital equipment even when they had limited or no access to bank funding.[56]

Graph 7.2.



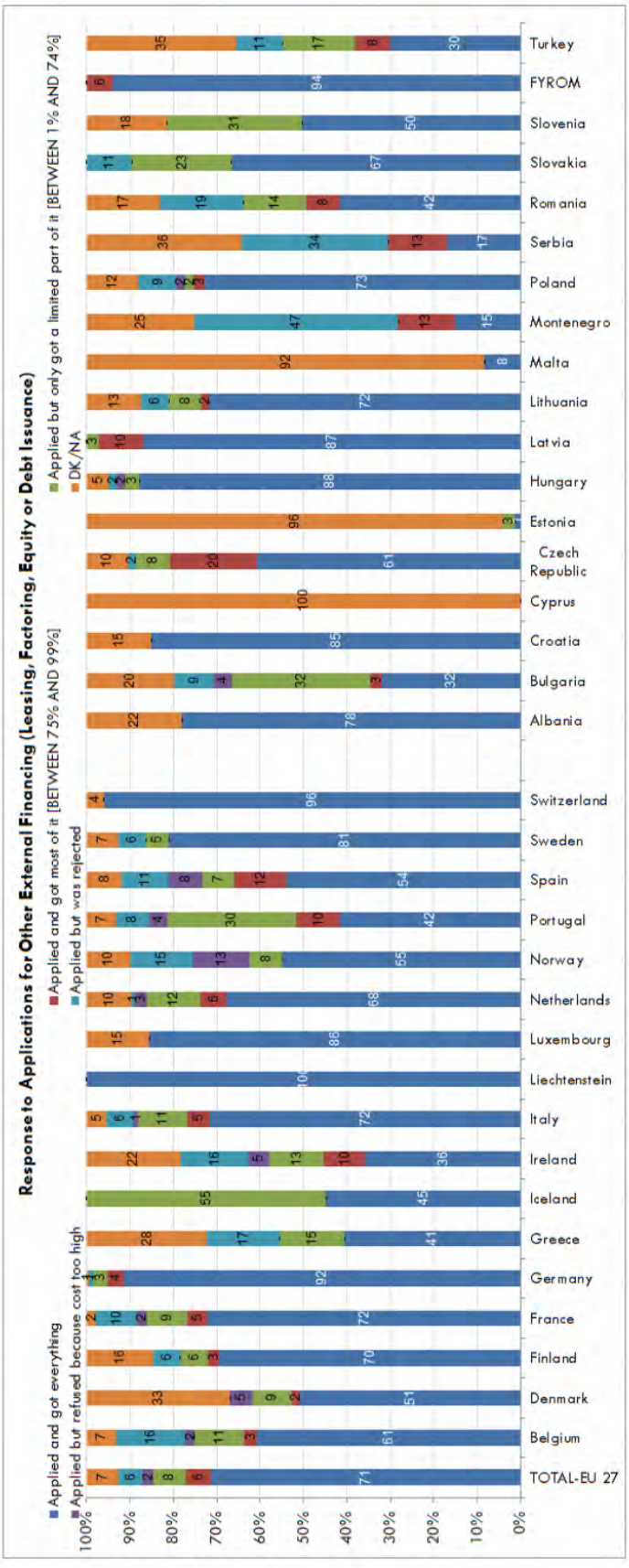
[56] The CEB's Annual Report on Project Preparation and Follow-Up 2011.

Generally, the structural market weaknesses in MSME lending create an unequal playing field with large enterprises, which in turn undermines their socio-economic potential and disrupt social cohesion. In this sense, the CEB acts directly upon these market imperfections and:

- Supports with medium- and long-term financing not only traditional banks, but also micro-finance institutions (see **Chapter 13, Case 2. MicroBank, Spain**) and leasing companies (see **Chapter 13, Case 3. EFL Poland** and **Case 4. TSKB Turkey**).

- Increases the availability and affordability of external financing for MSMEs and thus fosters the development of deeper and more inclusive financial sectors, most needed in CEB target countries (see **Chapters 8** and **9**, and **Chapter 13: Cases 3-5, EFL, TSKB** and **ProCredit**). The geographic focus on target countries is also in line with the Bank's strategic commitment to increase its lending activities in the CEE countries (see **Chapter 2**).

Graph 7.1. Response to MSME Applications for Other External Financing. Variations across CEB Member Countries*.



*Data in this own graph is based on the 2011 Survey on SMEs' Access to Finance conducted by EC and ECB across 38 countries. *Data is not available for Bosnia and Herzegovina, Georgia and the Republic of Moldova. Data excludes overdrafts, credit lines, bank loans and trade credit.*

Source: Ipsos Mori (2011), *SMEs' Access to Finance Survey. Analytical Report*, European Commission, Enterprise and Industry.

PART IV. SHALLOW FINANCIAL SECTORS IN CEB "TARGET COUNTRIES"

Part IV describes the financial sectors in CEB target countries (see Table 2.1), which represent a priority region for the Bank's activities. Despite the gradual financial integration and increased foreign presence in their financial sectors since mid-1990s, CEB target countries have relatively shallow and less inclusive financial systems than non-target countries (Chapter 8). In shallow financial systems credit to the private sector is limited, the capacity for term transformation is constrained, and MSME lending sectors are usually "embryonic" (see Chapter 7).

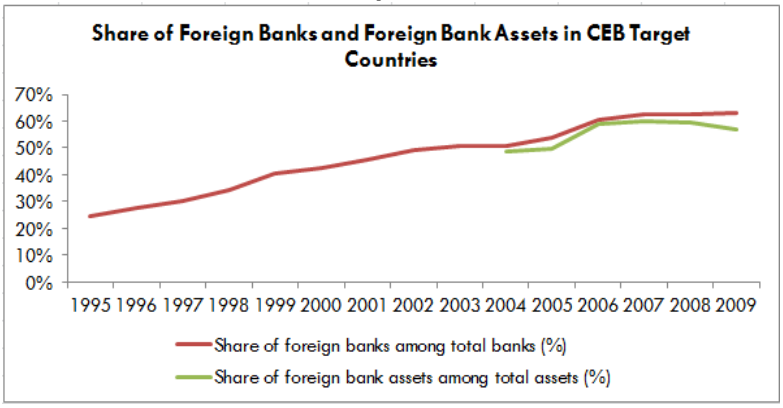
Nevertheless, the foreign presence in the region has allowed the international community, including the CEB, to reach more effectively local beneficiaries. For example, from 2000 to 2009, the Bank also operated through "transit loans" to reach MSMEs in its target countries, i.e. loans granted to financial intermediaries in non-target countries to finance projects in target countries (Chapter 9).

Chapter 10 points out an important prerequisite for effective absorption of the MSME support provided by the international community, a conducive MSME operating environment. It also concludes that in most of the CEB non-EU target countries, the MSME policy practices and standards are generally advancing towards EU standards.

Chapter 8. Financial Intermediation in CEB Target Countries

Since the mid-1990s, financial sectors of almost all CEB target countries have been characterised by an increasing presence of foreign banks (see **Graph 8.1**), almost exclusively from the EU. This cross-border banking phenomenon was facilitated by a certain progress in political integration, the removal of nationality restrictions, the liberalisation of market access, and privatisation of state-owned banks.

Graph 8.1



Source: Own graph based on data from: Claessens, S. *et al.* (2012), *Foreign Banks: Trends, Impact and Financial Stability,* International Monetary Fund.
Data is not available for Cyprus, Malta and Slovenia. Data was aggregated based on a weighted average using GDP (GDP, PPP, USD) from the IMF WEO April 2012 Database. GDP data was not available for BiH 1995/1997, and for Serbia and Montenegro 1995/1999.

This financial integration contributed to the gradual development of the financial sector in CEB target countries.[57] Financial development is traditionally described by the **depth of financial markets**. The depth of financial intermediation in CEB target countries, measured by domestic credit to the private sector as a percentage of GDP, although gradually progressing, is significantly below the EU and euro area levels, with the exception of Cyprus and Malta (see **Graph 8.2**). Also, in the Western Balkans, and some other CEB target countries, financial sectors are characterised by the dominance of the banking system, with a weaker role of underdeveloped ("embryonic") capital markets and insurance sub-sectors.

[57] Financial integration followed a certain progress in political integration, especially with the EU, which allowed multinational banks to initiate "long-term strategies in the region (even ahead of actual institutional improvements). Source: Friedrich, C., *et al.* (2010), *Financial Integration and Growth – Is Emerging Europe Different?*, European Bank for Reconstruction and Development (EBRD).

The depth of the financial sector is not the unique indicator of the level of financial development. The amounts of credit in a financial system do not reflect the actual use of financial services by the wide population, as credit could "be concentrated among the largest firms and wealthiest individuals … [F]inancial systems can become deep without delivering access to all"[58]. **Financial inclusion** is thus another element that demonstrates the level of maturity of financial markets. Financial inclusion determines "the extent to which households and firms can access and use formal financial services"[59], "without price or non-price barriers to their use"[60]. In this sense, inclusive financial systems equalize opportunities, and create a levelled playing field for all participants. Generally, the financial sector tends to be less inclusive in CEB target countries compared to the euro area:

- The World Bank defines a common proxy variable of access to financial institutions the number of bank accounts per 1 000 adults[61]. According to the Global Financial Inclusion Index (Global Findex)[62] in 2011 the share of the population aged 15+ with an account at a formal institution was consistently lower than the euro area average in all CEB target countries, with the exception of Slovenia, Estonia and Malta (see **Table 8.1**).

- Although the expansion of branch networks has improved the geographic access to financial services, many rural areas still remain poorly served. According to the Global Findex Database, the use of bank accounts in rural areas in CEB target countries is consistently lower than the usage in urban areas, which is an opposite tendency compared to the euro area (see **Table 8.1**). Also, the use of bank accounts in rural areas is generally lower than the euro area average of 89%, reaching as low as 15% of the rural population aged 15+ in the Republic of Moldova.

- Given the limited capacity for term transformation imposed by the maturity mismatch between deposits and loan portfolio, and the little competition in the financial systems (see **Chapter 7**), MSMEs remain an underserved population.

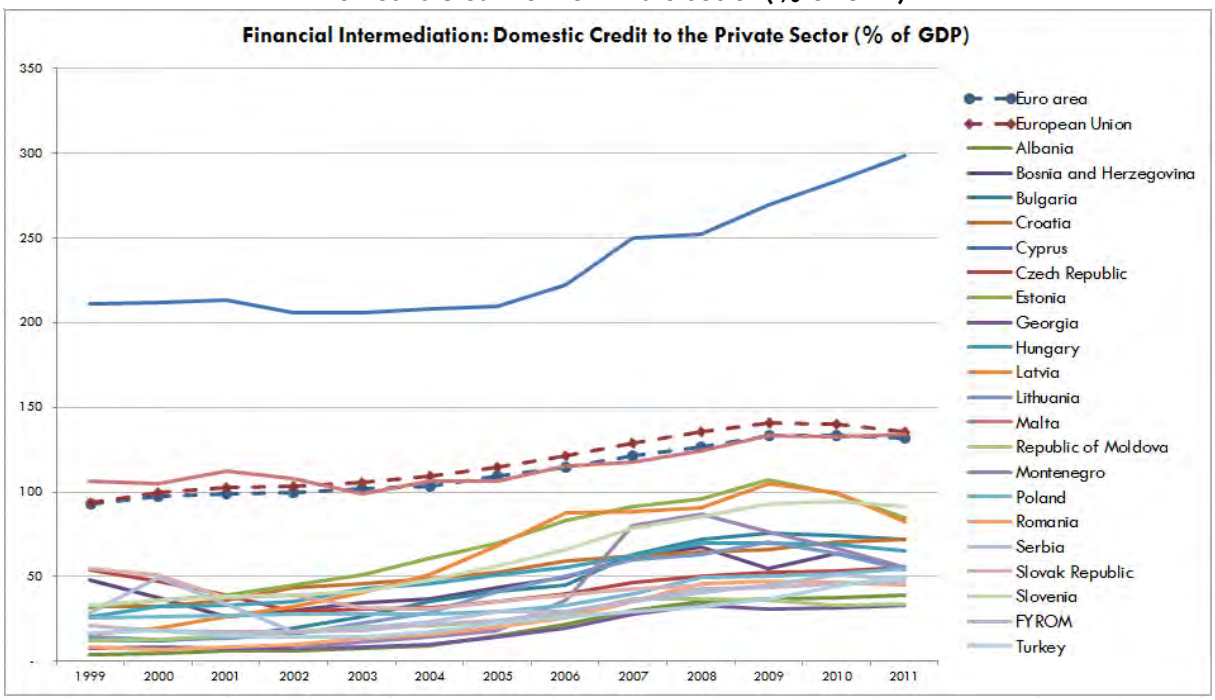
[58] Demirguc-Kunt, A., *et al.* (2012), *Measuring Financial Inclusion: The Global Findex Database*, The World Bank.
[59] Beck, T., *et al.* (2008), *Access to Finance: An Unfinished Agenda,* The World Bank Economic Review, Vol 22, No. 3, pp. 383-396.
[60] Demirguc-Kunt, A., *et al.* (2012), *Measuring Financial Inclusion: The Global Findex Database*, The World Bank.
[61] Cihak, M., *et al.* (2012), *Benchmarking Financial Systems around the World*, The World Bank.
[62] The Global Financial Inclusion Index (Global Findex) is a World Bank database that identifies the demand side data on financial inclusion.

Table 8.1 Financial Inclusion Indicators in CEB Target Countries and the Euro Area (2011)

Global Findex (2011)	Account at a formal financial institution (% age 15+)		
	Total	Rural	Urban
Albania	28.26	24.23	32.87
Bosnia and Herzegovina	56.21	54.68	59.74
Bulgaria	52.82	45.36	62.01
Croatia	88.39	88.03	89.34
Cyprus	85.23	83.22	87.40
Czech Republic	80.65	79.44	82.40
Estonia	96.82	96.77	96.87
Georgia	32.98	29.20	40.70
Hungary	72.67	69.67	78.39
Latvia	89.65	86.41	92.64
Lithuania	73.75	73.06	74.83
Malta	95.27	94.96	95.71
Republic of Moldova	18.06	14.88	30.03
Montenegro	50.43	48.78	54.22
Poland	70.19	69.00	72.38
Romania	44.59	37.40	56.00
Serbia	62.21	55.65	72.27
Slovak Republic	79.58	78.54	82.52
Slovenia	97.14	97.07	97.27
FYROM	73.69	72.62	74.74
Turkey	57.60	55.98	58.49
Euro area	**90.52**	**88.98**	**86.78**

Source: World Bank Global Financial Inclusion Index. 2011.

Graph 8.2. Financial Intermediation in CEB Target Countries, the EU and the Eurozone Domestic Credit to the Private Sector (% of GDP)



Source: Own graph based on the World Bank Indicator "Domestic Credit to the Private Sector as a % of GDP". Domestic credit to private sector refers to financial resources provided to the private sector, such as through loans, purchases of non-equity securities, and trade credits and other accounts receivable, that establish a claim for repayment. For some countries these claims include credit to public enterprises.

Chapter 9.
Foreign Presence in the Banking Sectors. CEB Support under "Transit Loans".

The presence of foreign banks in CEB target countries has facilitated the absorption of local shocks, such as credit and demand booms and provided a stable loan-to-deposit ratio: the credit growth during 1999-2007 in CEB target countries was mostly attributed to the presence of foreign banks (see **Figure 9.1 in Statistical Annex**).

Given the strong presence and profiles of Western European banks in target countries, the CEB has started since 2000 to support these banks via a CEB mechanism labelled "**transit loans**", i.e. loans granted to financial intermediaries in non-target countries to finance projects in target countries (see **Box 9.1** and **Chapter 2**). This mechanism contributed to mitigating the CEB's credit risk, as the risk borne by the CEB is that related to financial intermediaries, which have stronger risk management and financial solidity, and not that of final beneficiaries.

Box 9.1. "Transit Loans"

CEB loans are said to be "intermediated" when borrowers from the CEB provide funding for legally separate third parties responsible for implementing one or more projects. The relevant intermediaries must:

- Assume operational responsibility for identifying final beneficiaries;
- Transfer the funds to the final beneficiaries;
- Effect the repayment to the CEB of the loans granted to the final beneficiaries, the CEB's credit risk being that of the intermediaries;
- Assume responsibility for reporting to the CEB on the operations carried out.

Source: Excerpt from the CEB (2012), *Financing Social Projects in CEB Target Countries: Achievements and Challenges.*

Furthermore, "transit loans" allowed the CEB to reach local beneficiaries it otherwise would not have access to. The financial intermediaries through which the Bank has operated, supported the CEB's mission given the alignment in their mandates and incentives: more transparent governance and management, institutional capacity and willingness to reach final beneficiaries, sustainability of the financial mechanisms to reach final beneficiaries, convergence with the CEB's Environmental Policy, and readiness to put in place monitoring modalities to allow the CEB to evaluate social outcomes of the programme.

In terms of the overall CEB activities, "transit loans" have mainly been used to reach MSMEs for preservation and creation of viable jobs; fund housing for lower income groups; and invest in small municipal infrastructure projects, sectors that are naturally suited to the use of intermediaries. During 2000-2009, a total of € 1.4 billion of "transit loans" were approved in favour of job creation and preservation, via financial institutions in Italy (€ 777 million), Germany (€ 493 million) and Sweden (€ 100 million) (see **Table 9.1**). This represents slightly more than two-thirds (69%) of the value of "transit loans" approved for all CEB sectors of actions during the period 2000/2009.

Table 9.1. CEB MSME Financing through "Transit Loans". Amounts Approved (2000-2009).

Million EUR	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	Grand Total
"Transit Loans" / GERMANY	**60**	**30**	**75**	**50**	**48**	**50**	**80**	**100**			**493**
IKB Deutsche Industriebank AG		30									
KfW Bankengruppe	60		75	50	48	50	80	100			
"Transit Loans" / ITALY				**20**	**30**	**120**	**405**	**2**	**200**		***777***
Intesa Sanpaolo S.p.A.				20	30	20	55	2			
Società Italiana per le Imprese all'Estero (SIMEST)							150				
UniCredito Italiano						100	200		200		
"Transit Loans" / SWEDEN							**40**			**60**	**100**
Skandinaviska Enskilda Banken (SEB)							40			60	
Grand Total	**60**	**30**	**75**	**70**	**78**	**170**	**525**	**102**	**200**	**60**	**1 370**

In 2010-2012, "transit loans" were not approved in favour of MSME financing. This phenomenon could be explained, inter alia, by the deleveraging process of Western European Banks as a consequence of the crisis. It also reflects the increased demand for CEB lending from state development banks in target countries.

The foreign presence in CEB target countries has also made the region more vulnerable to external shocks. The financial crisis that began to affect Western European markets in H2 2007 started to impact the lending in CEE, Baltic States and Turkey in September 2008. Although it is difficult to disaggregate supply- and demand-side effects, the reduction in lending was a direct consequence of the presence of multinational banks and the transmission mechanisms of home-country shocks[64]. "Popov and Udell (2012) show[ed] how foreign banks transmitted the crisis to emerging Europe and that the severity of shocks depended on the parent bank's balance sheet … In absolute terms, [the annual] credit growth of [private] domestic and foreign banks in Central and Eastern Europe, the Baltic states and South-Eastern Europe converged in 2008 and 2009", implying that foreign banks decelerated more (see **Figure 9.1 in Statistical Annex**).

Nevertheless, the international community has contributed to preventing uncoordinated withdrawals by multinational banks that would have caused not only a reduction in lending and asset prices, but also macroeconomic destabilisation in the region. The European Bank Coordination ("Vienna") Initiative[65] was launched on 23 January 2009. This public-private platform aimed to coordinate the efforts of multinational banks, home and host country supervisors, fiscal authorities, the IMF, and development institutions (see **Figure 9.2 in Statistical Annex** and **Box 9.1**).

Box 9.2 The "Vienna Initiative"

Vienna Initiative 1.0 (2009)

The European Bank Coordination ("Vienna") Initiative[63] was launched on 23 January 2009 "at the height of the financial crisis". It provided a platform for decision making and coordination of efforts of all "key stakeholders in the EU-based cross-border bank groups that [we]re active in emerging Europe." The Initiative brought together public and private sector stakeholders, including IFIs (IMF, EBRD, EIB, and the World Bank); European Institutions (European Commission, ECB as observer); home and host country regulatory and fiscal authorities of large cross–border bank groups.

According to the IMF, state-owned banks in Central and Eastern Europe and the banks participating in the Vienna Initiative were relatively more stable lenders during 2008-2010 than non-participating banks (**Figure 9.2 in Statistical Annex** lists countries and parent banks of subsidiaries part of the Vienna Initiative). The participation in the Vienna Initiative was also found to have positive spill-over effects to the rest of the region. In this sense, the Vienna Initiative is described as a "relatively successful example of catalytic funding where public funds provided by the IMF, EU, and various development institutions were complemented by a coordinated (but non-coercive) bail-in of private-sector lenders".

Vienna Initiative 2.0 (2012)

In 2011, Western European Banks were again under pressure of deleveraging, including selling local subsidiaries. The Vienna Initiative was re-launched in January 2012 "to foster home and host authority coordination in support of stable cross-border banking and guarding against disorderly deleveraging [in CESEE]". In addition to prevent excessive uncoordinated decline in bank lending, the objective of the initiative is to advance a banking model that relies more on local sources of funding.

Sources: The text in this box is based on (i) De Haas, R. *et al.* (2012), *Foreign Banks and the Vienna Initiative: Turning Sinners into Saints?*, International Monetary Fund and (ii) the Official Mission Statement of the Vienna Initiative.

[63] Source: http://www.ebrd.com/pages/about/workwith/ifi.shtml

[64] EBRD Working Paper on "South-Eastern Europe: Lessons from the Global Economic Crisis" lists three channels of contagion: 1. External demand dropped sharply; 2. Access to finance became much more difficult or expensive; 3. Volume of remittances fell, which in turn depressed domestic demand. Source: Sanfey, P. (2010), *South-eastern Europe: Lessons from the Global Economic Crisis*, European Bank for Reconstruction and Development (EBRD)

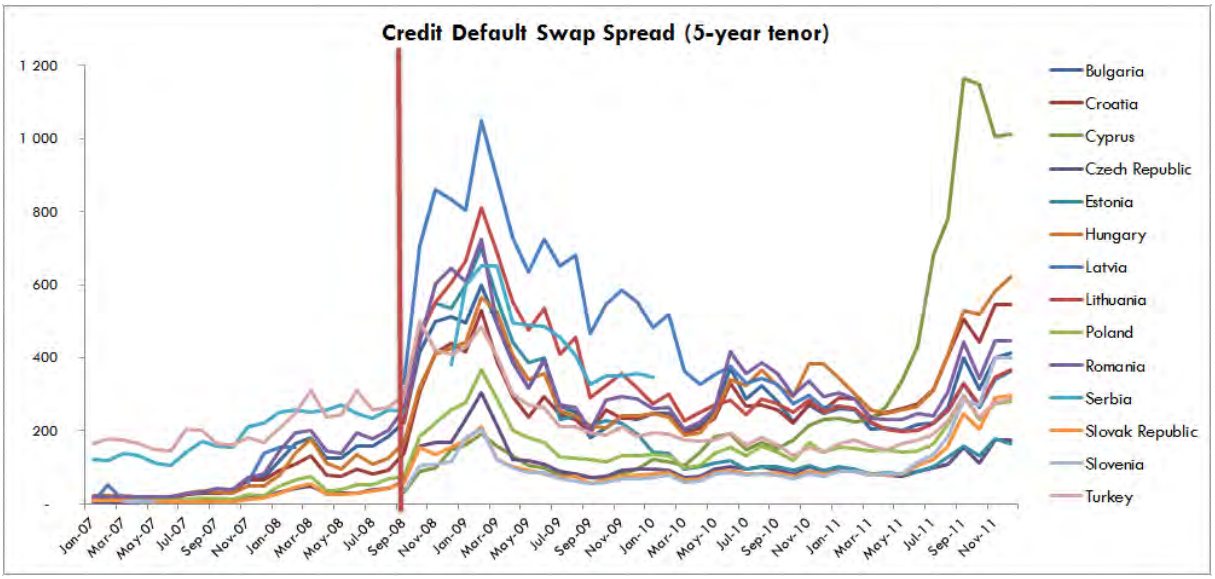
[65] Source: http://www.ebrd.com/pages/about/workwith/ifi.shtml

Additionally, the renewed presence of IFIs starting with 2009 provided strong support for the banking sector in the transition region.

According to the EBRD, "the overall effect of support can in principle be quantified by computing amounts pledged and disbursed, but such a calculation would miss an important part of the story, namely, the return of some level of confidence to the region. One way to see this is to look at … [the evolution of] credit default swap (CDS) spreads …".[66] The first peak in most CEB target countries was in February or March 2009, "when the sense of panic about the region's prospects was at height" [66]. The international community contributed to the reduction of CDS spreads[67] to a relatively stable level (see **Graph 9.1**).

In the light of the second wave of deleveraging of Western European banks in 2011-2012, the Vienna Initiative was re-launched in January 2012 (see **Box 9.2**). Overall, the international support allowed containing the deleveraging process in CESEE countries in comparison with Greece, Ireland, Italy, Portugal, and Spain: countries that were affected the most by the banking crisis (see **Chapter 11**).

Graph 9.1 Credit Default Swap (CDS) Spreads for CEB Target Countries (2007-2011)



Source: Own graph based on data from Bloomberg 10 September 2012. Data not available for Albania, Bosnia and Herzegovina, Georgia, "the former Yugoslav Republic of Macedonia", Malta, the Republic of Moldova, and Montenegro

[66] Sanfey, P. (2010), *South-eastern Europe: Lessons from the Global Economic Crisis*, European Bank for Reconstruction and Development (EBRD)

[67] **Credit Default Swap (CDS)** is a popular credit derivative that provides insurance against a default by a particular company or sovereign entity. The buyer of the insurance makes periodic payments to the seller, known as CDS spread, and in return it obtains the right to sell a bond issued by the reference entity for its face value if a credit event occurs, i.e. in case of default of the entity. Definition taken from: Hull, J., *et al.* (2004), *The Relationship between Credit Default Swap Spreads, Bond Yields, and Credit Rating Announcements*, Joseph L. Rotman School of Management.

Chapter 10.
MSME Operating Environment in Target Countries (Non-EU Member States Only)

Relatively shallow and less inclusive financial systems inherently lead to more pervasive MSME financing gaps in CEB target countries. In this context, the support of the international community, including that of the CEB, to the region carries a particular degree of additionality, i.e. value beyond the contributions of the private sector. The commitment of publicly-owned international organisations and privately-owned foreign companies is essential for deepening the infrastructure of financial institutions and of the lending market:

- Financial institution infrastructure relates to the "market presence of different types of financial institutions that provide credit, as well as the competition among these institutions."
- Lending infrastructure refers to "the rules and conditions set up mostly by governments that affect financial institutions and their abilities to lend to different potential borrowers"[68].

At the same time, effective absorption of the MSME support provided by the international community requires, inter alia, the presence of a national commitment to developing a conducive MSME operating environment. In the context of CEB target countries that are not EU-27 members, the MSME policy framework is generally advancing towards EU standards in most of the pre-accession countries[69] (see **Box 10.1**). Also, there is a national pro-active approach to develop an effective operating environment and SME policies and mechanisms in the Republic of Moldova and Georgia (see **Box 10.1**).

Box 10.1 SME Policy in CEB Target Countries (Non-EU Member States Only)

Under the Small Business Act for Europe (SBA), the EC, EBRD, ETF and OECD assess the SME policy in pre-accession countries of the Western Balkans (**Albania**, **Bosnia and Herzegovina**, **Croatia**, Kosovo*, **"the former Yugoslav Republic of Macedonia"**, **Montenegro**, **Serbia**) and **Turkey**, and in the Eastern Partner countries (Armenia, Azerbaijan, Belarus, **Georgia**, **Republic of Moldova**, and Ukraine).

The 2012 assessment concluded that Western Balkans economies have converged closer to EU standards in terms of the SME policy practices and standards since 2009, the date of the last SBA assessment, however at a slower and uneven pace reflecting various degrees of "economic development and advancement in the EU accession process".

- "While progress has been made in the improvement of the operational climate, [e.g. company registration and administrative simplification], particularly in some of the Western Balkan economies such as Croatia, Serbia and "the former Yugoslav Republic of Macedonia", further efforts are required to reduce administrative barriers, eliminate unfair competition from informal enterprises, upgrade the regulatory and legislative framework for access to finance and improve the responsiveness of the public administration to SMEs needs."
- Bosnia and Herzegovina registered "below regional average performance in most of the policy dimensions, indicating a limited level of policy convergence and the persistence of significant gaps in policy implementation."

In the case of the Republic of Moldova and Georgia, assessed under the Eastern Partner Countries, the 2012 assessment concluded that "countries are taking a pro-active approach to streamline the operational environment, … [and that they] started developing institutions and mechanisms for SME policy making".

Source: (i) OECD, *et al.* (2012), *SME Policy Index: Eastern Partner Countries 2012. Progress in the Implementation of the Small Business Act for Europe,* OECD Publishing and (ii) OECD, *et al.* (2012), *SME Policy Index: Western Balkans and Turkey 2012. Progress in the Implementation of the Small Business Act for Europe,* OECD Publishing.

** All reference to Kosovo, whether to the territory, institutions or population, in this text shall be understood in full compliance with United Nations Security Council Resolution 1244 and without prejudice to the status of Kosovo.*

[68] Berger, A., et al. (2004), *A More Complete Conceptual Framework for SME Finance*", for presentation at the World Bank Conference on SME: Overcoming Growth Constraints

[69] Albania, Bosnia and Herzegovina, Croatia, "the former Yugoslav Republic of Macedonia", Montenegro, Serbia and Turkey

PART V. RESPONDING TO THE CRISIS CONSEQUENCES: CEB CONTINUED SUPPORT TO MSMEs

Part V focuses on financial (Chapter 11) and social consequences (Chapter 12) of the financial and economic crisis that started in 2007 relevant to the CEB's MSME activities in its Member States.

Chapter 11 emphasises on the renewed role of IFIs in the private sector, namely the MSME sector, particularly in CEE countries since 2009. It also points out that the CEB's long-standing financial soundness and strong commitment to fostering social cohesion in its Member States, allow the Bank to remain a partner of choice for sovereigns and financial institutions in its member countries. This role is particularly strengthened in MSME financing in the context of more fragile borrowers, tightened credit supply and credit standards in financial sectors, subdued growth, and reduced employment opportunities.

Chapter 12 lists common social issues pertinent to most CEB countries, such as rise in unemployment; increase in long-term unemployment; introduction of flexibility enhancing schemes (e.g. part-time or fixed contracts); and increase in unemployment rates of migrants. The socio-economic environment risks marginalising or socially excluding these disadvantaged populations. Given the potential of MSMEs to re-integrate these populations, to generate employment and to promote economic growth and social cohesion (see Chapter 4), the CEB has provided continued support to MSMEs to create and/or maintain viable jobs and thus, to foster social cohesion in its Member States.

Chapter 11. Financial Consequences of the Crisis: Impact on CEB Borrowers

Fragile Sovereigns

The banking crisis exposed underlying structural problems of public debt, which caused sovereigns to lose their risk free status (**Table 11.1** compares the sovereign ratings of CEB member countries before the crisis and in August 2012). The materialisation of the European sovereign debt crisis starting with 2010 further undermined the capital positions of financial institutions and destabilised the financial system in the euro area. The ECB has undertaken non-conventional measures, such as long-term repurchasing operations, in numerous attempts to restore the confidence in the solvency of governments in the euro area.

Theoretically, fiscal monetisation through central bank measures could help stabilise financial markets temporarily. However, a major downside is that monetisation implies trading off price stability, which is an important pillar in sustainable growth and social stability. A fundamental solution to a sovereign debt crisis is fiscal consolidation. [70] But, fiscal consolidation could create social discontent as it often relies on reducing current expenditures, including social spending.

Across CEB members, countries have been affected at various degrees, with the severity of the impact depending on factors, such as housing market conditions, the export dependency, the budgetary position and the size of the financial sector and its exposure to high risk assets.

- Generally, CEB non-target countries have been affected the most by the banking crisis, namely Greece, Ireland, Italy, Portugal and Spain (GIIPS).

- CEB target countries have generally been more resilient to subprime or subprime-related assets issue given the low degree of sophistication of the financial products. However, the domination of foreign banks, as described in **Chapters 8** and **9**, means that target countries are not immune to shocks from CEB non-target countries. The BIS Consolidated Banking Statistics Database on an

[70] Shirakawa, M. (2012), *Sustainability of Government Debt: Preconditions for Stability in the Financial System and Prices*, Banque de France, Financial Stability Review, No 16. April 2012.

ultimate risk basis[71] shows that foreign claims of European banks in CEB target countries have generally declined. However, this reduction was largely on a small-scale, except for Hungary, where the reduction was mostly caused by domestic shortcomings rather than euro area contagion (see **Graph 11.1**). According to the Vienna Institute for International Economic Studies, the relatively small decline in foreign claims was possible given: (i) the steady presence of creditor countries, namely Austria, Italy and France, and (ii) coordinated efforts of the international community, such as the Vienna Initiative (see **Chapter 9**).[72]

- Between June 2008 and December 2011, the banking sector in CESEE countries suffered a deleveraging on average of 14%, while in the GIIPS countries – of 40%.[74] The GIIPS countries have also witnessed the most severe sovereign rating downgrades, when comparing the ratings from the pre-crisis year with the one in August 2012 (see **Table 11.1**).

Financial Institutions under Regulatory Pressures

As a response to the crisis, banks and financial authorities have been challenged to ensure financial stability. In September 2010 Basel III was signed to strengthen global capacity and liquidity regulations (see **Box 11.1**). The proposed measures aim to strengthen banks' capital and liquidity positions, improve the banking sector's ability to absorb shocks, and thus reduce the risk of spill-over from the financial sector to the real economy, i.e. to ensure financial stability.

Box 11.1 Basel III

The Group of Governors and Heads of Supervision (GHOS), the oversight body of the Basel Committee, reached an agreement in September 2010 to strengthen global capacity and liquidity regulations, commonly referred to as Basel III (**Figure 11.1 in Statistical Annex** summarises the main changes to the definition of regulatory capital under Basel III). The agreement resulted in a significant increase in minimum requirements for common equity and Tier One capital and an extensive prudent valuation framework to come into effect on 1 January 2013 through Capital Requirements Directive IV (CRD IV). A countercyclical capital buffer and a leverage ratio requirement are also to be introduced. The transition period is estimated to last until 2021.

The Capital Requirements Directive III (CRD III)[73], which implements "Basel 2.5" regulatory framework, became effective as of 31 December 2011.

To counter the funding and capital-related pressures, banks have the option to adjust their capital and liabilities, and reduce assets (**Figure 11.2 in Statistical Annex** lists deleveraging processes and means to accommodate them). The latter is considered the more viable option given the sovereign strains hampering access to capital markets. Asset reduction could entail "selling off (non-core) business lines, shedding liquid assets (e.g. securities holdings) and scaling down the loan portfolio (e.g. non-renewal of maturing loans and restricting new lending)"[75].

[71] The ultimate risk country is defined as the country in which the guarantor of a financial claim resides and/or the country in which the head office of a legally dependent branch is located.
[72] Gligorov, V., *et al.* (2012), *New Divide(s) in Europe?*, Vienna Institute for International Economic Studies, Current Analyses and Forecasts, March 2012
[73] The Basel Accord is implemented in the EU via the Capital Requirements Directive, designed to ensure the financial soundness of credit institutions (banks and building societies) and certain investment firms. The CRD I came into force on 1 January 2007, with firms applying the advanced approaches from 1 January 2008. Source: Financial Services Authority
[74] Al Obaidi, L., *et al.* (2012), *The European Banking Crisis and Spillover Effects in the countries of CESEE Revisited*, Vienna Institute for International Economic Studies, Monthly Report, July 2012. CESEE countries are defined as AL, BA, BG, HR, CZ, EE, HU, LV, LT, MK, ME, PL, RO, RS, SK, SI.
[75] European Central Bank (2010), *Financial Stability Review. June 2012,* European Central Bank.

Generally, externalities associated with an orderly deleveraging are positive, and they focus on the resilience of the financial system and sustainable economic growth:

- More efficient allocation of financial resources;
- Correction of over-inflated asset prices;
- Reduction in debt overhangs.

However, while deleveraging processes are intended to develop more robust banking models, they could be "long and painful, especially in cases where they occur simultaneously with shocks to the financial sector"[76]. The evidence suggests that deleveraging has contributed to tighter credit supply (see **Figure 11.3 in Statistical Annex**). The IMF (2012b) projected that the need of deleveraging could reduce the outstanding credit supply in the euro area by 1.7% in 2012[77]. This tightening in credit supply and standards has brought MSMEs' needs to attention.

Response to the Crisis: IFIs' Renewed Support to the Private Sector

In this context of more fragile European sovereigns, unresolved structural problems in the financial sectors, and tighter credit supply and standards, the role of IFIs support to the private sector, including MSMEs, has strengthened:

- The renewed presence of IFIs in most of the CEB target countries starting with 2009, inter alia, prevented a chaotic withdrawal of foreign banks from the region (see **Chapter 9**). Within the context of the Vienna Initiative 1.0, on 27 February 2009, the EBRD, the EIB Group, and the World Bank Group launched a two-year "Joint IFI Action Plan" which resulted in the provision of € 33 billion for the CEE economies during 2010/11. One of the priority areas was " … financial assistance to strengthen banks and support lending to the real economy, particularly to small and medium enterprises (SMEs) …"[78].

- In the light of the second wave of deleveraging of Western European Banks in 2011-2012, the Vienna Initiative 2.0 was re-launched in January 2012 (see **Chapter 9**). In this context, on 8 November 2012, a renewed "Join Action Plan" of the EBRD, the EIB Group, and the World Bank Group was initiated aiming to assist the CEE economies with over € 30 billion during 2013/14[79]. The EIB support, committed at € 20 billion, will address priority areas such as SMEs and energy efficiency[80].

The CEB has also continued its support to the MSME sector affected by the crisis, with a focus on its target countries:

- In 2008, the CEB provided the largest shares of MSME financing in both absolute, € 0.9 billion, and relative terms since its establishment in 1956. As a share of the CEB total lending, 48% of approvals and 43% of disbursements were aimed at assisting MSMEs with the objective of viable job creation and/or preservation (see **Graph 2.2**). 83% of the loans in favour of MSMEs benefited CEB target countries.

- In 2012, the second largest share of financing, 44% of total approvals or € 0.8 billion, was in favour of job creation and preservation. 92% of the loans in favour of MSMEs benefited CEB target countries.

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[76] European Central Bank (2010), *Financial Stability Review. June 2012,* European Central Bank.
[77] Kraemer-Eis, H., *et al.* (2012), *European Small Business Finance Outlook, May/2012*, European Investment Fund
[78] European Investment Bank (2009), *Joint IFI Action Plan in Support of Banking Systems and Lending to the Real Economy in Central and Eastern Europe,* http://www.eib.org/about/news/joint-support-for-central-eastern-and-southern-europe.htm
[79] The financial support is intended for the following economies: Albania, Bosnia Herzegovina, Bulgaria, Czech Republic, Croatia, Estonia, "the former Yugoslav Republic of Macedonia", Hungary, Kosovo*, Latvia, Lithuania, Montenegro, Poland, Romania, Serbia, Slovak Republic and Slovenia.
[80] European Bank for Reconstruction and Development (2012), *New Joint IFI Action Plan for Growth in Central and South Eastern Europe*, http://www.ebrd.com/pages/news/features/joint-ifi-action-plan.shtml.

- From 2008 to 2012, more than three-quarters of CEB loans in favour of MSMEs were channelled through private borrowers (see **Graph 2.6**), and 82% of the loans to MSMEs focused on CEB target countries (see **Graph 2.3**). During this period, 18% of loans approved benefitted non-target countries[81] (France, Spain, Finland, and Portugal), as opposed to 24% during 2000-2007.

The CEB's financial soundness and strong commitment to fostering social cohesion in its Member States have allowed the Bank to remain a partner of choice for sovereigns and financial institutions in target and non-target countries, especially in the context of a socio-economic environment worsened by the crisis (see **Chapter 12**). The CEB's financial solidity was reaffirmed by the Bank's high credit rating: as at end-2012, the CEB was rated AA+, Aaa, and AA+ by Fitch Ratings, Moody's Investors Service and Standard & Poor's, respectively[82].

Table 11.1 Historical Sovereign Ratings according to Fitch Ratings

Target Countries	Date	Foreign currency rating		Local currency rating	
		Long-Term	Outlook/Watch	Long-Term	Outlook/Watch
Croatia	21-May-2009	BBB-	negative	BBB	negative
Croatia	6-Jul-2005	BBB-	stable	BBB+	stable
Cyprus	25-Jun-2012	BB+	negative	BB+	negative
Cyprus	12-Jul-2007	AA-	Rating Watch negative	AA-	Rating Watch negative
Czech Republic	13-Dec-2011	A+	stable	AA-	stable
Czech Republic	4-Mar-2008	A+	stable	AA-	stable
Estonia	5-Jul-2011	A+	stable	A+	stable
Estonia	31-Aug-2006	A	stable	A+	stable
Georgia	15-Dec-2011	BB-	stable	BB-	stable
Georgia	18-Jul-2007	BB-	stable	BB-	stable
Hungary	6-Jan-2012	BB+	negative	BBB-	negative
Hungary	5-Nov-2007	BBB+	stable	A-	stable
Latvia	13-Dec-2011	BBB-	stable	BBB	stable
Latvia	17-Aug-2007	BBB+	stable	A-	stable
Lithuania	13-Dec-2011	BBB	stable	BBB+	stable
Lithuania	7-Dec-2007	A	negative	A+	negative
Malta	12-Jul-2007	A+	stable	A+	stable
Republic of Moldova	17-Dec-2009	-	-	-	-
Republic of Moldova	18-Jun-2007	B-	positive	B	positive
Poland	18-Jan-2007	A-	stable	A	stable
Romania	4-Jul-2011	BBB-	stable	BBB	stable
Romania	31-Aug-2006	BBB	stable	BBB+	stable
Serbia	16-Aug-2012	BB-	negative	BB-	negative
Serbia	19-May-2005	BB-	stable	BB-	stable
Slovakia	8-Jul-2008	A+	stable	A+	stable
Slovakia	23-Jul-2007	A	positive	A+	stable
Slovenia	8-Aug-2012	A-	negative	A-	negative
Slovenia	12-Jul-2006	AA	stable	AA	stable
FYROM	27-Oct-2010	BB+	stable	BB+	stable
FYROM	14-Aug-2007	BB+	positive	BB+	positive
Turkey	23-Nov-2011	BB+	stable	BB+	stable
Turkey	12-Dec-2007	BB-	stable	BB	stable

Non-Target Countries	Date	Foreign currency rating		Local currency rating	
		Long-Term	Outlook/Watch	Long-Term	Outlook/Watch
Belgium	27-Jan-2012	AA	negative	AA	negative
Belgium	2-May-2006	AA+	stable	AA+	stable
Denmark	10-Nov-2003	AAA	stable	AAA	stable
Finland	21-Sep-2000	AAA	stable	AAA	stable
Finland	5-Aug-1998	AAA	-	AAA	-
France	16-Dec-2011	AAA	negative	AAA	negative
France	21-Sep-2000	AAA	stable	AAA	stable
Germany	21-Sep-2000	AAA	stable	AAA	stable
Greece	17-May-2012	CCC	-	CCC	-
Greece	5-Mar-2007	A	positive	A	positive
Iceland	17-Feb-2012	BBB-	stable	BBB+	stable
Iceland	15-Mar-2007	A+	stable	AA+	stable
Ireland	27-Jan-2012	BBB+	negative	BBB+	negative
Ireland	21-Sep-2000	AAA	stable	AAA	stable
Italy	27-Jan-2012	A-	negative	A-	negative
Italy	19-Oct-2006	AA-	stable	AA-	stable
Luxembourg	21-Sep-2000	AAA	stable	AAA	stable
Netherlands	21 sept 2000	AAA	stable	AAA	stable
Norway	21-Sep-2000	AAA	stable	AAA	stable
Portugal	24-Nov-2011	BB+	negative	BB+	negative
Portugal	1-May-2007	AA	stable	AA	stable
San Marino	23-Jul-2012	BBB+	negative	-	-
San Marino	10-Jan-2001	AA	stable	-	-
Spain	7-Jun-2012	BBB	negative	BBB	negative
Spain	10-Dec-2003	AAA	stable	AAA	stable
Sweden	8-Mar-2004	AAA	stable	AAA	stable
Switzerland	21-Sep-2000	AAA	stable	AAA	stable

Source: Fitch Ratings, *Complete Sovereign Rating History,* Update as of 24 August 2012

Highlighted In red: to signal reduction from the previous presented rating for the relevant country

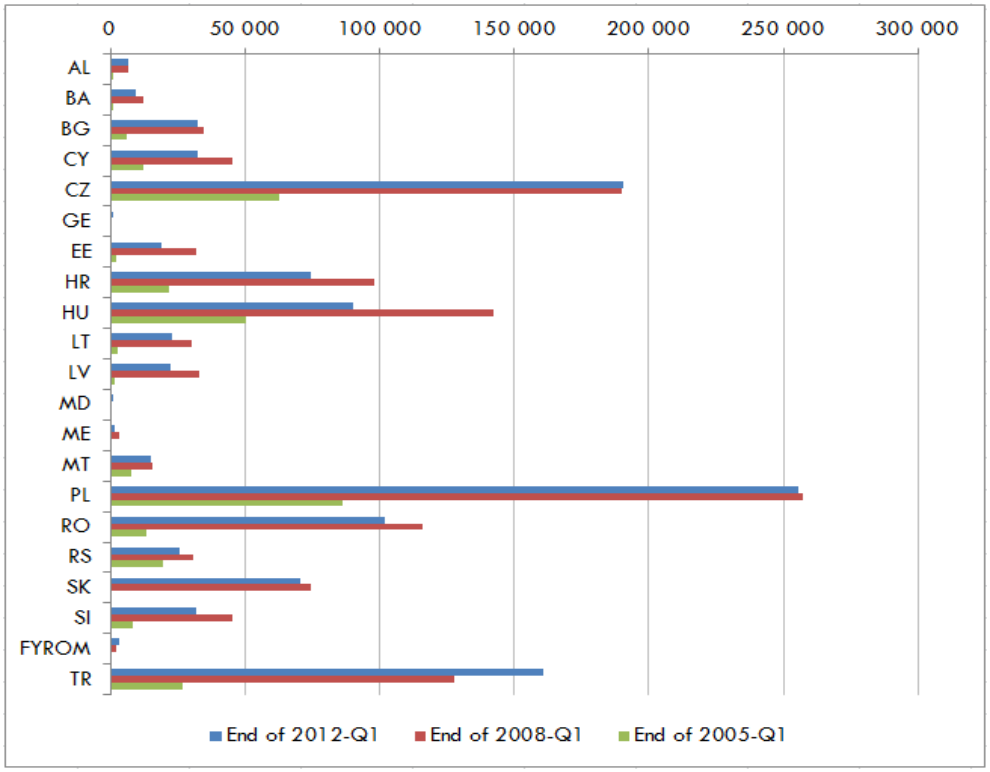
The table shows the latest rating as of August 2012, and the first available rating as of 2007, as reference to the pre-crisis year.

Note: Data not available for Albania, Bosnia and Herzegovina, Bulgaria, and Montenegro

[81] The figure does not include "transit loans" used to reach MSMEs in target countries (see **Chapters 1** and **9**).

[82] On 12 December 2012, Moody's confirmed its Aaa rating with a stable outlook. On 25 September 2012, Fitch Ratings downgraded the CEB's long term Issuer Default Rating (IDR) from AAA to AA+; outlook stable. The rating of CEB's short term debt was affirmed at F1+, which is the highest grade of the rating scale. On 27 December 2012, Standard & Poor's lowered the CEB's long term issuer credit rating from AAA to AA+; outlook stable. Source: CEB Website.

Graph 11.1 Consolidated Foreign Claims in CEB Target Countries, USD Million



Source: Own graph based on BIS Consolidated Banking Database. Foreign claims of the European reporting countries include (i) cross-border and local claims and (ii) claims on banks, non-bank private sector and public sector. The counterparty is the country of residence of the ultimate obligor of the exposure.

Chapter 12. Social Consequences of the Crisis in CEB Member Countries

In the context of poor financial regulation and supervision systems, the financial crisis has also revealed imprudent behaviour on behalf of financial institutions. In conditions of macroeconomic growth, increasing asset prices and high liquidity, this behaviour generated profits. But, in periods of bust, it transferred the financial shocks into the real economy, expressed in significant drops in GDP.

Although countries have been affected differently by the crisis, there are common social issues pertinent to most CEB countries, such as rise in unemployment; increase in long-term unemployment; introduction of flexibility enhancing schemes, such as part-time or fixed contracts; and increase in unemployment rates of migrants. This socio-economic environment risks marginalising or socially excluding these disadvantaged populations. Given the potential of MSMEs to generate employment and promote economic growth and social cohesion (see **Chapter 4**), the CEB has provided continued support to MSMEs to create and/or maintain viable jobs and thus, foster social cohesion across its Member States.

Labour Market: High Unemployment and Low Capacity to Generate Employment

Across CEB member countries, labour markets started to deteriorate from mid-2008 onwards following the financial shocks which transferred into the real economy:

- In 2009, GDP suffered the strongest drop in all CEB countries except for Poland and unemployment rates increased in all CEB member countries, except for "the former Yugoslav Republic of Macedonia". The Baltic States experienced the largest drop in real GDP growth and the highest increase in unemployment (see **Graphs 12.1** and **12.2 in Statistical Annex**). In the CEB non-target countries, the unemployment rates in Greece, Ireland, Portugal, and Spain, exceeded the EU-average of 9.7% for 2011, thus qualifying as "disadvantaged regions"[83] under the CEB's MSME financing. The estimates for 2012 indicate that these countries continued to register a higher unemployment rate than the EU-average of 10.5%. In 2012, the unemployment rate for Italy is also estimated to have reached a slightly higher level than the EU-average, of 10.6%.
- The contraction in GDP in the crisis year of 2009 exceeded the drop in employment in the majority of the CEB member countries. However, in 2010 the recovery in GDP was accompanied only by a slow recovery in employment (see **Graph 12.2 in Statistical Annex**). This evidences the low capacity of the economy to generate jobs, and labour hoarding tendencies during recession years, which imply accepting a decrease in productivity. Labour hoarding refers to the practice in which companies retain employees that would otherwise be laid-off during recession years, i.e. "overstaffing". This practice is based on the expectation that this workforce would be needed during the imminent recovery period.

In addition to labour hoarding approaches, countries also responded to the crisis by reducing the hours worked via flexibility-enhancing schemes or by applying a combination of both measures (see **Figure 12.1 in Statistical Annex**)[84]. But, flexibility-enhancing policies, such as fixed-term contracts or part-time working schemes, have been introduced in the context of hitherto employment protection regulations. This caused a de facto implementation "at margin" that created two labour markets:

- Permanently protected employees (insiders); and
- Temporary employees (outsiders)[85], mostly comprising of the young workforce, that have to accept job insecurity and lower job quality, as it is less costly not to renew fixed term contracts than to make permanent employees redundant.

[83] "Disadvantaged regions" in non-target countries were referenced to the EU average in the CEB Overall Policy Framework for Loan and Project Financing following the CEB Administrative Council Resolution 1495 in 2006.
[84] Stehrer, R., *et al.* (2012), *Sectoral Employment Effects of Economic Downturns*, Vienna Institute for International Economic Studies, Research Reports, August 2012.
[85] Vidovic, H. (2012), "*Special Section III: Labour Market Developments and Prospects*", Vienna Institute for International Economic Studies, Current Analyses and Forecasts, Fasting or Feasting - Europe - Old and New - at the Crossroads, July 2012

Generally, the crisis has created widespread anxiety about job instability and job quality. According to the ILO 2012 Global Employment Trends, there is a great risk of entering "a second dip in growth and employment … exacerbating the severe labour market distress that has emerged since the onset of the crisis" with fiscal policy space dramatically limited[86].

A natural response to this social environment is the Bank's continued activities under the sector of action "creation and preservation of viable jobs" given the socio-economic potential of MSMEs. Under the circumstances of tightened credit supply and credit standards that aggravate the SME financing gap, the CEB continues to provide its support to MSMEs to assist them in fulfilling their capacity to generate jobs and promote economic growth and social cohesion (see **Chapter 4**). Additionally, by assisting MSMEs, the CEB continues to support national social agendas that have increasingly become focused on addressing social issues in the context of austerity measures and limited fiscal space.

Affected Populations by the Crisis: Long-term Unemployed and Migrant Workers

In 2011, long-term unemployment rates, i.e. unemployed more than 12 months, were higher than the EU-average of 42.9% in most of the CEB member countries. Nevertheless, the incidence of long-term unemployment differed across CEB member countries. Compared with the pre-crisis period, major increases in long-term unemployment as a share of total unemployment were registered in Lithuania, Spain, Latvia, and Ireland with an increase of 20 pps to 30 pps (see **Graph 12.3 in Statistical Annex**).

Long-term unemployment has negative social implications, as it directly affects people's lives and incomes, and can impede economic growth. It could lead to the "degradation of skills and thus decrease [in] employability …". "… [U]ltimately[,] [it could cause] discouragement and exit from the labour market [and thus,] risk … increasing poverty and social failure" [87] It is thus important to support long-term unemployed and re-integrate them in the labour market. Micro-enterprises have been found to engage the highest percentage of long-term unemployed (see **Chapter 4**). In this sense, the CEB's typical financing of micro-enterprises could contribute to assisting these disadvantaged populations, and promote their social inclusion.

Another population group strongly affected by the crisis is constituted of migrant workers, which was already at a disadvantage even before the crisis. Unemployment rates of migrant workers have predominantly been higher than those of natives in the EU-27 (see **Figure 12.2 in Statistical Annex**). And as the economic demand reduced as a result of the crisis, the demand for migrant labour has also decreased.

- The International Organisation for Migration[88] recognises that "not all immigrants can or will return home, especially those coming from countries where prospects for employment are worse, those with strong social protection in the country of destination, those who have resided in the destination country for a long period of time, and those with strong social networks. In addition, unemployed migrants may adopt a **"wait-and-see" approach**, preferring to overstay on their current visa while waiting for an economic upturn"[88].

- When deciding to return to their countries of origin, the migrants are usually faced with stringent local labour markets.

[86] International Labour Office (2012), *Global Employment Trends 2012. Preventing a Deeper Jobs Crisis,* International Labour Organization.
[87] Gligorov, V., *et al.* (2012), *New Divide(s) in Europe?*, Vienna Institute for International Economic Studies, Current Analyses and Forecasts, March 2012
[88] Koehler, J., *et al.* (2010), *IOM Thematic Study: Migration and the Economic Crisis in the European Union: Implications for Policy,* International Organization for Migration

In both situations, the issue of unemployed migrants and their inclusion into the labour force and local communities is of importance to fostering social cohesion in the CEB member countries. The CEB has given absolute priority to migrants since its establishment in 1956 (see **Chapter 1**). The areas of support evolved in line with the changing needs of migrants. In the socio-economic environment engendered by the crisis, the CEB's focus on migrants under the sector of action "creation and preservation of viable jobs" is pertinent to the needs of this disadvantaged group, and would thus contribute to fostering social cohesion in its Member States. For example, this study presents the CEB support to migrants under MSME financing through its partnership with MicroBank in Spain (see **Chapter 13, Case 2**).

These populations – unemployed, long-term unemployed and migrant workers – represent several social groups badly affected by the crisis in most of the CEB Member States. The financial and economic environment risks marginalising or socially excluding these groups. Given the potential of MSMEs to (re-)integrate these populations, to generate employment and to promote economic growth and social cohesion, the CEB has continued to provide support in favour of MSME financing responding to the consequences of the crisis that started in 2007. To this effect, at end-2012 "creation and preservation of viable jobs" has remained one of the major pillars of the CEB's activities in its Member States.

PART VI. SOCIAL ADDED VALUE OF CEB MSME FINANCING: LESSONS LEARNED AND OPTIONS AHEAD

Part VI elaborates on additionality, i.e. value beyond the contributions of the private sector, and social added value of the CEB's activities in job creation and preservation based on five Case Studies selected by purposive sampling (Chapter 13). The key message is that all CEB loans in this sector have the final objective of creating and preserving viable jobs by providing MSMEs with medium- and long-term financing. To this aim, the Bank contributes to promoting financial inclusion of MSMEs in its member countries and also, to deepening financial sectors and strengthening MSME lending markets in its target countries, although these are not stated as explicit objectives at the design stage.

Chapter 14 builds upon the main lessons learned following over four decades of operations, monitoring, and evaluations of the CEB's activities in favour of job creation and preservation. It also provides options to be explored by the Bank to enhance its operating model of MSME financing and thus, the social added value of its operations.

Chapter 13. Case Studies

Small firms not only report higher financing obstacles as opposed to large firms (see **Chapters 5** and **6**), but also they are more adversely affected by financial constraints, along with legal constraints and corruption[89]. This phenomenon could be attributed to the limited availability of alternative financing sources, and the inability to take advantage of economies of scale.

Thus, MSMEs face disproportionate barriers to accessing finance that create an unequal playing field with large enterprises. This inequality, in its turn, undermines the socio-economic potential of MSMEs as drivers of economic growth and net employment generators, and thus disrupts social cohesion. In line with the practice of the international community (see **Table 14.1**), the CEB assists MSMEs in its member countries and provides them with medium- and long-term financing.

The social added value of CEB MSME financing, based on established in-house methods, is creation and preservation of viable jobs. In 1995-2011, following the projections obtained for 60% of loans in favour of MSME financing, the CEB's social impact could be estimated at around 137 000 of jobs created and another 1.6 million of jobs preserved[90].

In order to analyse the CEB's additionality and social added value, the study presents five case studies as at 31.12.2011. The selection of the case studies is based on purposive sampling to cover a range of financing modalities (loans and leasing), countries (target: **Cases 3-5**, **Poland**, **Turkey**, **Bulgaria**, and **"the former Yugoslav Republic of Macedonia"**; and non-target**: Cases 1-2**, **Finland** and **Spain**), and final beneficiaries.

Intermediaries: Strong Profiles and Alignment of Mandates/Incentives

MSMEs benefitting from CEB-financed programmes are generally those within the existing pipeline of intermediaries. Under this operating model, the social added value of the CEB's operations is highly correlated with the choice of the intermediaries.

[89] Beck, T., *et al.* (2002), *Financial and Legal Constraints to Firm Growth: Does Size Matter?*, The Journal of Finance, Vol. LX, No. 1, 2005.

[90] The headcount reflects projected figures provided by implementing partners, based on self-declarations by the financed MSMEs. At the time of writing, estimations were available for 60% of loans in favour of MSME financing. The CEB's Evaluation Department (EVD) has highlighted the low information content of, and methodological difficulties associated with the headcount-based approach focused exclusively on number of jobs created and/or preserved. The issues regarding this development impact indicator are a matter of debate, specific not only to the CEB, but also to the IFI community as a whole.

"When a potential borrower shows interest in the CEB contributing to part-financing a project, the CEB first of all proceeds with the identification of the project in order to define in principle its social purpose and its eligibility as well as the financial quality of the borrower and/or, where applicable, of the guarantor"[91]. Borrowers are evaluated for criteria such as the clarity and sustainability of the financial mechanisms to reach final beneficiaries, affinity of the intermediary's strategy and mandate with the CEB's objectives, governance and management, convergence with the CEB Environmental Policy, and readiness to put in place monitoring modalities to allow CEB to evaluate social outcomes of the programme. The quality of their risk management and the degree of financial soundness are also carefully analysed. "Borrowers must provide monitoring reports at least once a year and prior to any disbursement, with the exception of the first tranche"[92]. Disbursements may be suspended if the general conditions relative to the loan are not complied with, in particular the contractual provisions for project monitoring.

The CEB has worked with sovereigns and private and public financial institutions, including banks and leasing companies (see **Graphs 2.5** and **2.6**). In its target countries, the CEB has also operated through subsidiaries of foreign banks given their stronger risk and financial profiles and institutional capacity and willingness to monitor disbursements to MSME beneficiaries.

Cases 1 to **5** evidence that the implementing partners of the CEB-financed programmes were important players in the local markets; and had the relevant mandate, expertise, willingness and institutional capacity to reach effectively MSME beneficiaries at the moment of loan approval and subsequent disbursements.

Favourable Lending Conditions: Additionality of CEB Financing

"CEB raises funds on the best terms available on capital markets, and passes these terms to the borrower, applying the lowest possible margin which takes into account the need to cover its operating costs" [92]. CEB lending is generally distinguished with its favourable terms, regarding interest rates, tenor and grace periods:

- The level of interest rates is established for each disbursed tranche of a loan. The interest rates are generally more competitive than those provided by commercial loans, without distorting the local markets. In **Cases 1-5**, the borrowers received an interest rate advantage ranging roughly between 0.05% and 2% compared to the levels they would have otherwise been charged on the market (pertinent for borrowers that had direct access to the market)[92]. The borrowers have a choice between fixed and variable interest rates, but the customary CEB financing is through floating rates. The CEB's reference currency is EURO, which does not exclude recourse to other currencies.
- The tenor is medium- to long-term. During 1995-2011 the customary tenor for MSME lending was 10 years applied to more than two-fifths, or € 2.1 billion, of disbursements under MSME financing, with the shortest tenor being 3 years (€ 0.3 billion) and the longest, 15 years (€ 0.3 billion).
- Grace period may be granted, if estimated appropriate, for loan repayments, not for interest repayments. Almost 30% of disbursements during 1995-2011 contained a grace period. For those loans the customary grace period was 5 years applied to almost two-fifths, or € 0.5 billion, of loans disbursed with grace period. The tenor and grace periods reflect the nature of the underlying investment.

The CEB, similar to other IFIs, strives not to crowd-out private sector players: it aims at providing lending to final beneficiaries that tend to be underserved and/or credit rationed by the private sector.

[91] CEB Policy for Loan and Project Financing 2009. http://www.coebank.org/Upload/legal/en/ppfp_english.pdf
[92] Approximations are provided by the CEB's General Directorate for Loans and Social Development for borrowers which had direct access to market financing at the moment of tranche disbursement.

Eligible Costs

The CEB's share of financing may represent up to 50% of the total eligible cost of the sub-project[93]. During 1995-2012, the average size of an MSME programme loan approved for intermediaries was € 40 million (189 loans). The lowest size was € 500,000 (two loans) and the highest was ≈ € 260 million (three loans).

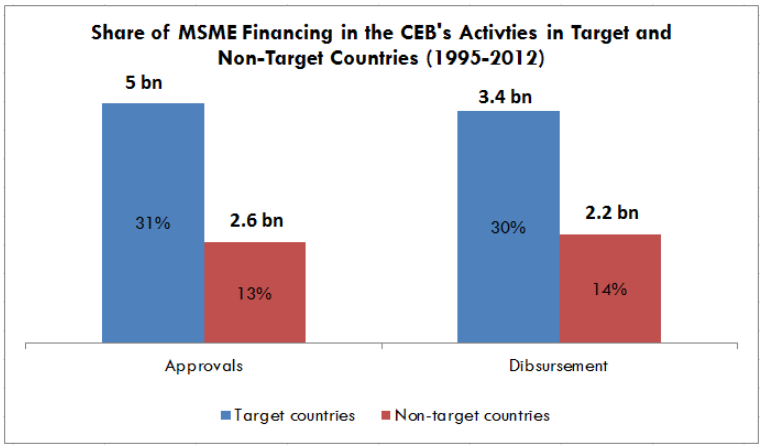
CEB MSME financing must involve fixed investments or investments in productive equipment[94], including in the form of leasing, aimed to create and/or preserve permanent and/or seasonal jobs.

CEB can also cover working capital financing when it de facto fulfils the criteria of an investment financing, rather than ordinary working capital financing (e.g. see **Case 1**, **Finnvera**). The financing of working capital is limited to the level of small enterprises as defined by the EU and up to € 50 000 by sub-project[95].

CEB Social Value: Promoting Financial Inclusion in CEB Target and Non-Target Countries[96]

Given the judicious choice of intermediaries, the CEB is able to reach MSMEs that tend to be underserved and/or credit rationed, disadvantaged regions and socially excluded populations in its target and non-target countries (**Table 13.1** presents the CEB MSMSE financing as a share of total CEB financing during 1995/2011).

Table 13.1



Note: The percentages are calculated based on the MSME financing as a share of total CEB financing during 1995/2012 for target and non-target countries, separately.

From the Bank's establishment to end-2012, job creation and preservation in target countries accounted for 61% of CEB MSME lending or € 5.3 billion. From 1995 to 2012, it was the most significant sector of CEB activities in target countries. During this period, as a share of CEB lending in target countries for all sectoral lines of action, it represented 31% of approvals or € 5 billion, and 30% of disbursements or € 3.4 billion.

[93] The share may be higher, but not exceeding 90%, in case of (1) projects in favour of refugee populations, migrants and displaced persons; (2) reconstruction and or/rehabilitation of destroyed or damaged infrastructure in the wake of a natural or ecological disaster; and (3) projects implemented in the CEB target countries. Source: CEB Policy for Loan and Project Financing 2009.

[94] Eligibility is excluded for investments in the primary agricultural sector, weapons, nuclear energy, tobacco, production of spirits, gambling, pornography, and products considered by EU regulations to be harmful to health and to the environment

[95] The CEB's Policy for Loan and Project Financing 2009. http://www.coebank.org/Upload/legal/en/ppfp_english.pdf

[96] Although financial inclusion may be another potential effect of CEB MSME financing, it is not specified as an objective in the design documents, and there are no appropriate monitoring indicators on which final performance could be evaluated.

- The CEB MSME support in target countries in **Cases 3-5 (Poland, Turkey, Bulgaria,** and **"the former Yugoslav Republic of Macedonia")** reached a broad spectrum of MSMEs that tended to be underserved and/or credit rationed in the context of generally less inclusive banking systems (see **Chapter 8**). It also supported specialised leasing companies, which are often the preferred alternative to external banking financing (see **Chapter 7**), such as EFL, the leader in the Polish leasing market (see **Case V.3**).

From the Bank's establishment to end-2012, job creation and preservation in non-target countries in Western Europe accounted for 39% of CEB MSME lending or € 3.4 billion. From 1995 to 2012, it was the second most significant sector of CEB activities in non-target countries. During this period, as a share of CEB lending in non-target countries for all sectoral lines of action, it represented 13% of approvals or € 2.6 billion, and 14% of disbursements or € 2.2 billion.

- The Bank's MSME support in non-target countries addresses disadvantaged regions at the sub-national level, registering unemployment rates higher than the EU average[97][98], socially excluded or marginalised populations, such as immigrants and women, and micro-firms. Under **Case 1 (Finland)** the programme loans to Finnvera, the only full state-owned financial institution in Finland, targeted MSMEs located in pre-defined disadvantaged regions with predominantly high unemployment rates. Under **Case 2 (Spain)**, the support to MicroBank, the MFI of La Caixa, aimed at reaching socially disadvantaged populations that risked marginalisation and/or social exclusion, such as women and immigrants.

CEB support to the lower-end of the MSME size spectrum has generally had a broader scope than micro-financing or micro-crediting (see **Box 3.2**). Nevertheless, the CEB has occasionally channelled its lending through microfinance providers, such as MicroBank[99] in Spain (see **Case 2**) with the objective to support marginalised populations, such as immigrants and women.

CEB Social Value: Contributing to Deepening Financial sectors in CEB Target Countries

In its target countries in CEE, the CEB fosters social cohesion through creation and preservation of employment not only by promoting financial inclusion of MSMEs, but also by contributing to deepening the financial sectors and strengthening the MSME lending market [100].

CEB activities provide a particular degree of additionality, as the private sector tends not to provide medium- and long-term financing in shallow banking sectors. The CEB also plays a catalytic role, i.e. working with local financial intermediaries and contributing to mobilising resources from other IFIs to increase their lending to MSMEs. Also, since the CEB supports both local and foreign intermediaries, it may contribute to introducing competition and expertise and to increasing efficiency in the local financial sectors.

- For example, **Case 5** presents CEB MSME financing in "the former Yugoslav Republic of Macedonia", where the banking sector is highly concentrated. The CEB partnered with ProCredit Bank, established as a local reference bank for micro-credits, to increase the availability of medium to long-term financing and to potentially contribute to mobilising other IFIs to increase their lending to MSMEs.

[97] "Disadvantaged regions" in non-target countries were referenced to the EU average in the CEB Overall Policy Framework for Loan and Project Financing following the CEB Administrative Council (AC) Resolution 1495 in 2006. The previous CEB definitions can be found in **Chapter 1** under AC Resolution 1313 (1993), 1313 Revised 2 (1995), and 1424 (1997).

[98] Non-target countries not members of the EU are assimilated to the EU regions. Source: The CEB's Overall Policy Framework for Loan and Project Financing.

[99] The entity was renamed "Nuevo Micro Bank, S.A.U" following the re-organisation of the La Caixa Group in 2011. As the name "MicroBank" is used for commercial purposes, it will be referred to as such throughout the study for the purpose of simplicity.

[100] Although deepening financial sectors and/or strengthening the MSME lending markets may be other potential effects of CEB MSME financing, they are not specified as objectives in the design documents, and there are no appropriate monitoring indicators on which final performance could be evaluated.

Nevertheless, effective absorption of the MSME support provided by the international community, including the CEB, in the region requires, inter alia, the presence of a national commitment to developing a conducive MSME operating environment. In most of the CEB non-EU target countries[101] the MSME policy framework generally advances towards EU standards in the pre-accession countries, and there is a national pro-active approach in developing the operational environment in the Republic of Moldova and Georgia (see **Chapter 10**).

Sustainability of CEB Activities

The Bank aims to achieve sustainability of its activities over the medium- and long-term. Its operating model allows addressing the viability of operations by maximising the quality of projects/programmes (see **Chapter 14**). To this end, the CEB is closely involved in the design, preparation and monitoring of projects/programmes. It appraises the financial and institutional capacity of implementing partners, and the adequacy of the financing package.

- For example, the CEB's technical mission deemed the sustainability of the programme with ProCredit in Bulgaria (see **Case 5**) as high. This opinion was expressed given the institutional capacity of the implementing partner: "ProCredit is a sound micro-finance institution operating on a best-practice basis, with an ownership that is committed to its development and mission. Its business strategy is sound and it has in place an active business development plan and resource mobilization strategy"[102].

The sustainability of CEB activities also relies on external factors, such as the effectiveness of national and/or sub-national business and economic policies. In this sense, CEB loans tend to address the macroeconomic environment and imbalances at the sub-national level and thus complement national or regional policies and priorities.

- For example, the already mentioned CEB cooperation with Finnvera (see **Case 1**) targeted Finnish SMEs located in disadvantaged regions. These regions were also defined as Objective Areas in the context of the EU Structural Funds, which matched with high unemployment regions of Finland (see **Box 13.1**).

[101] Albania, Bosnia and Herzegovina, Croatia, "the former Yugoslav Republic of Macedonia", Montenegro, Serbia and Turkey

[102] Excerpt from the mission report of the CEB's Technical Assessment and Monitoring Directorate.

Case 1. FINNVERA (FINLAND)

PURPOSE	Creation and preservation of viable jobs by SMEs
BENEFICIARIES	Finnish SMEs located in disadvantaged regions of Finland (see **Box 13.1**)[103]
CEB ADDED VALUE	Strengthening social cohesion through creation and/or preservation of jobs, namely in the regions registering particularly high unemployment rates (see **Box 13.1**), by supporting the only fully state-owned financial institution mandated to supplement the financial markets with loans to enterprises that have difficult access to commercial bank loans. Promoting financial inclusion (1) of underserved small scale enterprises, specifically in vulnerable regions. Enhancing the catalytic role (1) of Finnvera. Fostering programme sustainability: The programme loans supported the core activities of Finnvera, the only fully state-owned financial institution and an industrial policy actor. Finnvera's well-thought policies ensured that its activities carried high value added and that its investments complied with all appropriate policies. Supporting the country's regional policy objectives. Demonstration effects/Replicability: Finnvera's sound governance and financial management, robust operating procedures and well-thought criteria for allocating interest rate subsidies set it out as an exemplary institution that provided with useful reference for similar CEB projects in transition countries. *(1) Although CEB MSME financing may have such potential effects, they are not specified as objectives in the design documents, and there are no appropriate monitoring indicators on which final performance could be evaluated.*

Finnvera Coverage

Finnvera plc is a state-owned specialised financial institution mandated to complement the financial market in the area of enhancing SMEs' access to finance, particularly in the disadvantaged regions. It aims at promoting the Finnish SMEs and facilitating their exports and internationalisation. The State of Finland owns the entire stock of Finnvera, which was formed by merging KERA and the Finnish Guarantee Board at end-1998. The State also pays interest rate subsidies for loans to the disadvantaged regions of the country. Finnvera's financing is in the form of loans, guarantees, equity investments and export credit guarantees. Its loan categories include investment loans, development loans, micro-loans, working capital loans, loans for women entrepreneurs, environmental loans, entrepreneur loans and internationalization loans. It operates out of 16 regional offices in Finland and also has a representative office in St. Petersburg.

The CEB has approved a total of 280M for Finnvera for four programme loans since 1996, out of which € 159M were disbursed for three programme loans as at 31.12.2011. The CEB financing also covered working capital limited to certain conditions. For example, under **loan programme 2** the working capital financing could not exceed 30% of the investment cost; and under **loan programme 3** a maximum of 20% of the total loan amount of € 100M could be directed for working capital financing. Also, the working capital financing was only accepted in the context of fixed investments.

[103] Disadvantaged regions were defined as (i) the regions of Finland that were eligible under Objectives 2, 5b, and 6 of the EU Structural Funds and, from 1997, with unemployment rate superior or equal to 5% following AC Resolution 1424 (**under programme loan 1**), and (ii) regions specified in 2000-2006 EU Objective Areas 1 and 2 and having difficult access to commercial loans due to lack of suitable collateral (under **programme loans 2** and **3**).

The three disbursed programme loans have resulted in part-funding of 1 496 beneficiaries, mostly micro and small companies located in disadvantaged regions, creating 3 277 jobs and preserving 9 963 jobs (as at 31.12.2011):

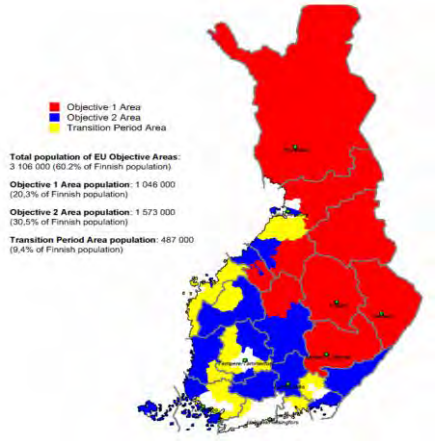
Table 13.2 Distribution of Final Beneficiaries according to Enterprise Size Class

Size Class	Number of Enterprises	%
Micro (< 10 employees)	964	65%
Small (<50 ecmployees)	379	26%
Medium (<250 employees)	129	9%
Large	0	0%
Total	**1 472**	**100%**

*Note: Due to data limitations, the table does not include the social added value of **programme loan 1** of € 9 million, which benefitted 24 enterprises.*

Box 13.1 Finnish Disadvantaged Areas

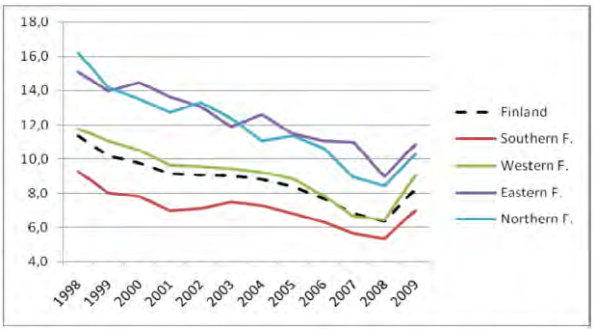
Finnish Disadvantaged Areas
EU Objectives 2000/06



Under **programme loans 2** and **3,** Disadvantaged regions have been qualified as those specified in the EU Objective Areas, which matched with high unemployment regions of Finland:

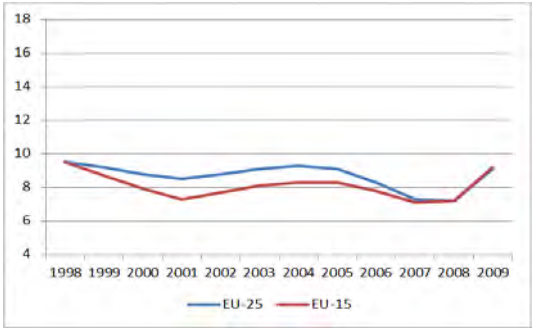
- EU Objective 1 Area covered Northern and Eastern Finland, which registered unemployment rates higher than the EU averages.
- EU Objective 2 Areas covered rural and industrial regions that faced structural difficulties.

Unemployment Rates (%) Across Regions in Mainland Finland



Source: Laakso, S., *et al.* (2010), *Expert Evaluation Network Delivering Policy Analysis on the Performance of Cohesion Policy 2007-2013. Task 2: Country Report on Achievements of Cohesion Policy. Finland*, Urban Research TA.

Unemployment Rates (%) in EU-15 & EU-25



Source: EUROSTAT, October 2012 Update

Case 2. MICROBANK[104] (SPAIN)

PURPOSE	Creation and preservation of viable jobs by supporting self-employment and micro-businesses.
BENEFICIARIES	Micro-firms and individuals, such as immigrants and women, with limited access to credit.
CEB ADDED VALUE	Strengthening social integration and creating and/or preserving jobs, in particular for disadvantaged populations that risked social exclusion or marginalisation, by supporting a well-run micro-finance institution with a social vocation that is clearly and effectively reaching beneficiaries with which formal institutions rarely operate. Promoting financial inclusion (1) of underserved, socially excluded, or marginalised populations. Fostering programme sustainability: MicroBank has the requisite personnel, administrative and monitoring capacity to carry out the programmes loans given its close organic and institutional ties with the parent La Caixa, which has experience in the micro-credit field since 2000. Demonstration effects/Replicability: MicroBank's sound governance, effective operating modalities, and clarity of the social targeting mechanism set it out as an exemplary institution that provided a useful reference for similar CEB projects in CEE countries. *(1) Although CEB MSME financing may have such potential effects, they are not specified as objectives in the design documents, and there are no appropriate monitoring indicators on which final performance could be evaluated.*

MicroBank Coverage

The **Caja de Ahorros y Pensiones de Barcelona, La Caixa,** is the result of the merger, in 1990, of the Caja de Pensiones, founded in 1904, and the Caja de Barcelona, founded in 1844. The mission of La Caixa is "*[t]o encourage saving and investment by offering the best and most comprehensive range of financial services to the greatest number of customers and make a decisive contribution to society to provide flexible tailored coverage of basic financial and social needs*"[105]. In response to the needs expressed on the market, La Caixa began to develop a program of Social Micro-Credit in July 2000. Since then, the lending activity has grown considerably, and La Caixa has become the private sector entity with the largest share of micro-credit lending.

In June 2007, La Caixa decided to create **MicroBank – Banco Social De La Caixa**, 100% held by La Caixa, aimed at fully assuming management of the micro-credit portfolio developed and managed by La Caixa itself. As at end-2011, "*since it was set up, MicroBank has granted 128 203 loans, lending € 806.8 million to finance various projects.*" [106]

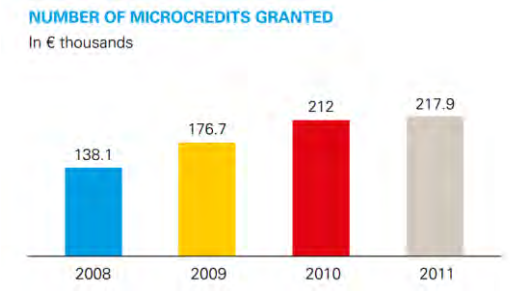
In January, the Board of Directors of La Caixa announced a re-organisation process, under which La Caixa passed on its banking business to **Criteria CaixaCorp**, which subsequently became a banking group under the name **CaixaBank, S.A.** On 30 June 2011, all the banking business of La Caixa, including consumer banking, private banking and asset management, was transferred to **CaixaBank**.

[104] The entity was renamed "Nuevo Micro Bank, S.A.U" following the re-organisation of the La Caixa Group in 2011. As the name "MicroBank" is used for commercial purposes, it is referred to as such throughout the study for the purpose of simplicity.

[105] http://www.lacaixa.com/informacioncorporativa/misionvisionyvalores_en.html

[106] http://www.microbanklacaixa.com/deployedfiles/microbank/Estaticos/PDFs/Informe_Anual_2011_ANG.pdf

Box 13.2 MicroBank. Annual Report 2011[108]

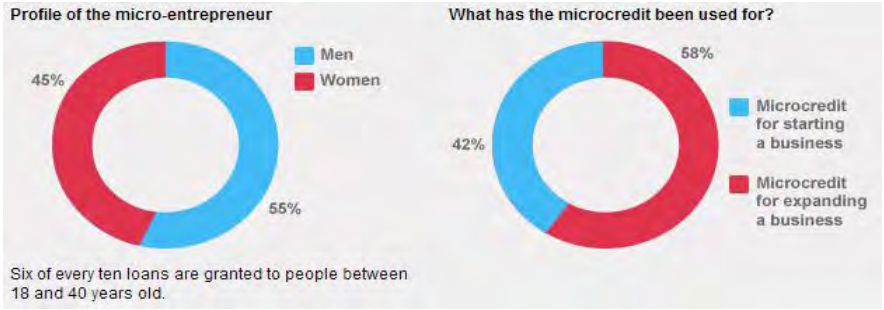


MicroBank' strategy and mandate have strong affinities with the CEB's objectives:

"MicroBank offers financial products and services especially adapted to the needs of entrepreneurs, micro-entrepreneurs and families in order to contribute to:

- *The promotion of productive activity and job creation through financial support for self-employed professionals and microenterprises.*
- *Self-employment through the setting up of small businesses supported by the granting of microcredits to new entrepreneurs.*
- *Personal and family development, responding to specific needs and enabling people to overcome temporary difficulties.*
- *Financial inclusion, promoting the use of banks among new clients through the entity's wide commercial network."*[107]

Box 13.3 MicroBank. Profile of the Micro Client Since June 2007. Annual Report 2011.[107]



Prudently managed and adequately capitalised, MicroBank targets predominantly vulnerable populations (e.g. immigrants and women). MicroBank's activity is spread over the entire territory of Spain. But, the geographical distribution of its operations is most concentrated in Andalucia, Catalonia, Madrid and Valencia. This makes MicroBank a natural collaborating partner of the CEB in promoting social cohesion and integrating disadvantaged populations in Spain. Initial co-operation between the CEB and MicroBank was also the first programme loan that MicroBank has contracted with an IFI since its creation in June 2007.

In total CEB approved € 143M for three projects, out of which € 130M were disbursed as of 31.12.2011. The CEB programme loans were distributed through three types of loans: (1) social micro-credits targeting persons with self-employment projects; (2) financial micro-credits for small entrepreneurs and micro companies, and (3) family micro-credits to assist in family entry and settlement, female victims of violence, people with disabilities etc.

[107] http://www.microbanklacaixa.com/informacioncorporativa/misionvisionyvalores_en.html
[108] http://www.microbanklacaixa.com/deployedfiles/microbank/Estaticos/PDFs/Informe_Anual_2011_ANG.pdf

Social micro-credits were channelled and managed through 407 social entities with which MicroBank signed Cooperation Agreements for counselling services to potential beneficiaries and for follow-up of projects thus financed. Financial micro-credits were solicited directly by the beneficiaries at one of the 5 129 La Caixa local offices.

The three disbursed programme loans have resulted in part-funding of 29 752 beneficiaries (see **Table 13.3** for the distribution of final beneficiaries according to vulnerable groups), mostly individuals of micro-enterprises, creating 9 467 jobs and preserving 14 140 jobs (as at 31.12.2011):

Table 13.3 Distribution on Final Beneficiaries according to Vulnerable Groups

Final Beneficiary	Number of Beneficiaries	%
Women	11 032	40%
Immigrants	3 531	13%
Families	16 158	59%
Others	6 994	26%
Total		

Notes:
*1. Due to data limitations, the table does not include the social added value of **programme loan 1** of € 30M.*
*2. Under **programme loan 3** of 100M EUR, the table includes the data only for the tranche disbursed of € 50M.*

Case 3.EUROPEJSKI FUNDUSZ LEASINGOWY (EFL) (POLAND)

PURPOSE	Creation and preservation of viable jobs in Polish SMEs
BENEFICIARIES	Polish SMEs according to the Polish MSME definition under **programme loan 1**, Polish SMEs according to CEB's eligibility criteria under **programme loan 2**.
CEB ADDED VALUE	Strengthening social cohesion through investment in job creation and/or preservation in SMEs, by providing support to the leader in the Polish leasing market to better respond to the needs of SMEs. Supporting emerging firms that tend to present high risk, but have a very high job creation potential and promote entrepreneurship. Promoting financial inclusion (1) of SMEs who tend to be constrained in accessing external banking financing, and for which leasing may be an alternative source of investment financing. Fostering programme sustainability: The programme loans supported the core activities of EFL, the leader on the Polish leasing market since its establishment in 1991. EFL has the institutional capacity and willingness to reach final beneficiaries following clear and sustainable mechanisms. As such the programme loans have been deemed sustainable at all levels. Supporting the country's socio-economic strategy. Demonstration effects/Replicability to other CEE countries. *(1) Although CEB MSME financing may have such potential effects, they are not specified as objectives in the design documents, and there are no appropriate monitoring indicators on which final performance could be evaluated.*

EFL Outreach

The Crédit Agricole Group is market leader in Universal Customer-Focused Banking in France and one of the largest banks in Europe. The Crédit Agricole Group consists of Crédit Agricole S.A. along with all of the Regional Banks and Local Banks. In leasing, Crédit Agricole Leasing & Factoring (CAL&F) offers a full range of leasing solutions for investment in equipment and real estate, as well as financing for sustainable development projects, public-private partnerships.[109] CAL&F has a presence in 6 countries (Europe and the Maghreb) and is *7th* in Europe in leasing as of 31.12.2011 (see Box **13.4**).

The EFL, the leading leasing company in Poland, is part of CAL&F. The EFL has been a market leader in Poland since its incorporation in 1991, and joined the Crédit Agricole Group in 2001. It was created in 1991 as a private leasing company focused on meeting the needs of small firms. EFL's fields of expertise are: leasing of cars and trucks, leasing of machinery and equipment, IT equipment, leasing of property. Since 2008, the EFL has operated under two business lines:

- Retail Leasing - business line dedicated to the provision of services to customers from the SME sector, and
- Corporate Leasing - business line dealing with capital groups, institutions and large enterprises.

The Retail Leasing line has the mission to: "*support the development of small and medium enterprises by creating a safe, efficient and accessible investment financing system*"[110]. Thus, EFL's mandate is in line with the CEB mission of fostering social cohesion.

[109] Credit Agricole Leasing and Factoring. Activity Report 2011.
http://www.ca-leasingfactoring.com/upload/file/rapport_activite/CAL&F_RA_anglais_planches.pdf
[110] http://www.inochlod.pl/media/pub/nasz_partner_EFL_en.pdf

As at end-2011, the EFL had 904 employees, a portfolio of about 230 000 clients, and € 1.1 billion in outstandings.

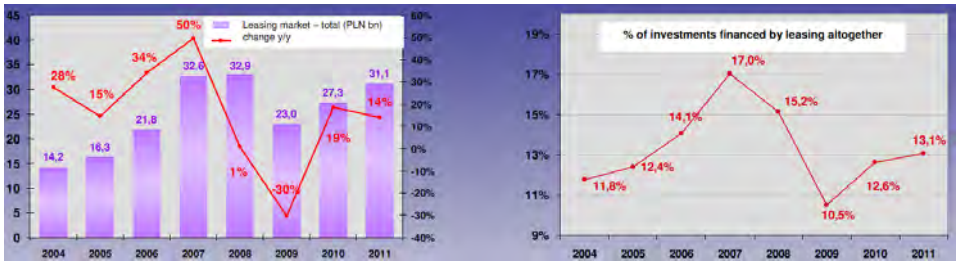
For most MSMEs in Poland, leasing is the only formal form of investment finance to which they have access. In 2004-2007 the average annual Polish leasing market increase amounted to 32%, significantly exceeding the investment dynamics in the economy at 11%. In 2008, the leasing market in Poland reacted to the economic slowdown, but it revived in 2009-10 given the public investments in infrastructure co-financed from the EU funds (see **Box 13.5**).

Box 13.4 Crédit Agricole Leasing and Factoring. Data as of end 2011



Source: http://www.ca-leasingfactoring.com/en/our-company/key-figures

Box 13.5 Polish Leasing Market 2004-2011



Source: Polish Leasing Association (2011), *Leasing Industry 2011 Results*, Polish Leasing Association

As the EFL has been the leader in the leasing market since its establishment and has a strong national coverage (see **Box 13.6**), the CEB appreciated the collaboration with the EFL as one of high social added value: this partnership allowed the CEB effectively reaching and supporting Polish micro- and small enterprises.

The collaboration between the CEB and EFL started in 2004. The CEB has previously approved ≈€ 504 million for Crédit Agricole S.A. France. For the EFL, the CEB approved € 180M for two programme loans, out of which € 176M were disbursed as at 31.12.2011.

Box 13.6 EFL National Distribution Network. 2011.



Source:
http://www.inochlod.pl/media/pub/nasz_partner_EFL_en.pdf

The major drivers of growth in the Polish leasing market are transport vehicles and machinery. Most Polish SMEs operate in trade and services sectors, and cars are generally their single most expensive and indispensable, capital investment. Leasing is the practical way of financing such lumpy purchases as it allows SMEs to match cash flows. Vehicle leasing has thus been also considered eligible for the CEB financing.

Generally, the sub-projects co-financed by the CEB resembled micro-credit schemes given the EFL's close knowledge of and relationship with the client and its business, monitoring of the lessee with monthly repayments, a high level of repeat business, strict follow-up and well-developed back-office and administrative systems.

The two disbursed programme loans have resulted in part-funding of 16 288 beneficiaries (see **Table 13.4**), creating 16 413 jobs, and preserving 243 721 jobs (as at 31.12.2011):

Table 13.4 Distribution of Final Beneficiaries according to Enterprise Size Class

Size Class	Number of Enterprises	%
Micro (< 10 employees)	8 820	54%
Small and Medium (<250 employees)	7 408	46%
Total	**16 228**	**100%**

Case 4. TURKIYE SINAI KALKINMA BANKASI A.S. (TSKB) (TURKEY)

PURPOSE	Creation and preservation of viable jobs in SMEs
BENEFICIARIES	SMEs located throughout Turkey
CEB ADDED VALUE	Strengthening social cohesion through investment in job creation and/or preservation, by providing support to Turkey's industrial development bank to better respond to the needs of SMEs. Promoting financial inclusion (1) by making available medium- and long-term financing terms, on-lent by TSKB, to the final beneficiary SMEs. Deepening the financial system (1): by supplementing the Turkish banking sector with medium- and long-term financing opportunities for SMEs, IFIs, such as the CEB, provide crucial additionality and produce catalytic effect in the banking sector. Fostering programme sustainability: The programme loans supported the core activities of TSKB, as such they are deemed sustainable. Supporting the country's socio-economic strategy. Demonstration effects/Replicability to other CEE countries. *(1) Although CEB MSME financing may have such potential effects, they are not specified as objectives in the design documents, and there are no appropriate monitoring indicators on which final performance could be evaluated.*

TSKB Outreach

Established in 1950, TSKB is the first privately owned investment development bank of Turkey. It was founded with the support of the World Bank and with the cooperation of the Government of the Turkish Republic, the Central Bank of the Turkish Republic and the commercial banks in Turkey. TSKB, the "Industrial Development Bank of Turkey" was established for the purpose of meeting the following objectives:

- To provide assistance to private sector enterprises in all economic sectors in Turkey, especially the industry sector,
- To promote the participation of private and foreign capital incorporations founded or to be founded in Turkey, and
- To contribute to the development of the capital markets in Turkey.

TSKB provides financial support, and consultancy, technical assistance and financial intermediation services. The majority of loans extended to the private sector are medium- and long term. Through its *Corporate Lending and Project Finance* services, TSKB acts as an intermediary for the funds provided by IFIs, such as the World Bank (IBRD), EIB and KfW, in order to finance SMEs investments in any region of Turkey. TSKB has built up a strong relationship with IFIs and is the borrower of choice for multi-lateral credit lines. For example, TSKB is preferred by the World Bank within the framework of Export Finance Intermediary Loans.

The cooperation between the CEB and TSKB started in 2003. TSKB was one of the four Turkish banks participating in the first CEB programme loan approved in favour of Turkish SMEs for which the borrower was the Republic of Turkey. Out of the € 200 million CEB loan made available under the previous programme loan, about € 65 million were allocated and disbursed to TSKB. The first programme loan approved for TSKB was in 2005, and since then, the CEB has approved a total of € 200M under two programme loans, out of which € 197M were disbursed as at 31.12.2011.

In addition to direct lending to private companies, TSKB also acts as an intermediary, lending to leading Turkish commercial banks and leasing companies which, in turn, on-lend to SMEs, through the so-called APEX (wholesale) banking in support of SMEs. TSKB is the leader and model implementer of APEX banking in Turkey. APEX banking allows TSKB to have a national coverage of Turkish SMEs. This structure was used to on-lend 50% of the CEB funds under **programme loan 2**. This allowed the disbursement of the CEB funds through mainly leasing companies, and thus, responding to the SME needs which have regular recourse to leasing as it is usually the most feasible investment financing alternative, in the presence of limited access to finance.

The programmes loans co-financed by the CEB contributed to the implementation of capital investments projects in SMEs, primarily in newly established companies or modernization of existing companies, with the aim to create and/or preserve jobs.

The first fully disbursed programme loan and the second programme loan which was 50% allocated to SMEs have resulted in part-funding of 154 beneficiaries (see **Table 13.5**), creating 2 898 jobs and preserving 15 832 jobs (as at 31.12.2011):

Table 13.5 Distribution of Final Beneficiaries according to Enterprise Size Class*

Size Class	Number of Enterprises	%
Micro (< 10 employees)	22	14%
Small (<50 employees)	39	25%
Medium (<250 employees)	86	56%
Large	7	5%
Total	**154**	**100%**

** The table does not include the statistics for the € 50M disbursed to TSKB in November 2011 under **programme loan 2** of € 100M. When drafting the study, TSKB was under the process of gradually allocating the tranche to final beneficiaries.*

Case 5.PROCREDIT BANK (BULGARIA AND "THE FORMER YUGOSLAV REPUBLIC OF MACEDONIA")

PURPOSE	Creation and preservation of viable jobs
BENEFICIARIES	SMEs on the micro- or lower end of the market
CEB ADDED VALUE	Strengthening social cohesion through investment in favour of job creation and/or preservation, by providing support to ProCredit Bank, a well-run "niche bank" that serves solely MSMEs. Promoting financial inclusion (*) of MSMEs which have limited access to external banking financing through (i) the provision of medium and long-term lending conditions; and (ii) ProCredit Bank's specialized lending methodology based on cash-flow projections, personnel intensive approach and long-term relationships with clients allowing it to support small entrepreneurs with less burdensome collateral requirements. Contributing to deepening the financial system (*): Savings in target countries are generally concentrated in deposits of fewer than twelve months, and local banks rely on international support for longer term funds. Additionally, local banks follow conservative risk management techniques that inherently increase the cost of transactions with SMEs, translated into higher interest rates and collateral requirements. Thus, IFIs, such as the CEB, provide crucial additionality in the local banking sectors. Fostering programme sustainability: ProCredit Banks are sound micro-finance institutions operating on a best-practice basis, with an ownership committed to its mission. ProCredit Holding is the majority shareholder of ProCredit Banks, and it provides support in the form of refinancing, human resources, management information systems, auditing, controlling, marketing, retail operations, risk management, staff training etc. All these elements guarantee sustainability of sub-projects beyond the duration of the programme loans. Supporting the country's socio-economic strategy. (*) *Although CEB MSME financing may have such potential effects, they are not specified as objectives in the design documents, and there are no appropriate monitoring indicators on which final performance could be evaluated.*

ProCredit Bank Coverage

ProCredit Group consists of 21 banks operating in transition economies and developing countries in South Eastern Europe, Latin America and Africa. In South-Eastern Europe it is present in Albania, Bosnia and Herzegovina, Bulgaria, Kosovo*, "The former Yugoslav Republic of Macedonia", Republic of Moldova, Romania and Serbia. Its mandate is the "*provision of credit and other banking services to very small, small and medium-sized enterprises and lower and middle income savers who have previously had limited access to formal financial services*"[111].

ProCredit Holding is the majority shareholder in the group of 21 banks. The ProCredit Group is led by ProCredit Holding AG & Co. KGaA, a holding company based in Frankfurt am Main, Germany. Legally founded in 1998 as Internationale Micro Investitionen AG (IMI) by the consulting firm IPC, the beginning of the IMI dates back 1980, when "*IPC was founded as a consultancy company focused on bringing MSMEs and other low-income groups into the formal financial sector. Since then, IPC and a core group of international IFIs and donors who today are partners in ProCredit have benefited from a learning process covering three decades, out of which they developed an effective credit technology and approach to institution building*"[112].

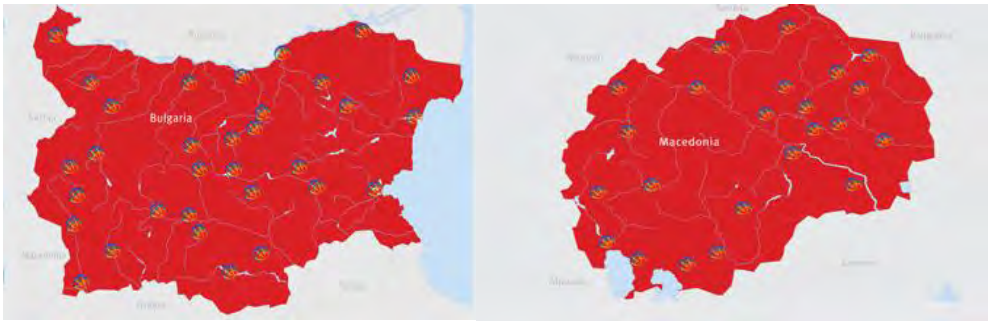
The CEB started to cooperate with ProCredit in 2005. The CEB approved a total of € 31M under four programme loans to ProCredit Bank Bulgaria and ProCredit Bank "the former Yugoslav Republic of Macedonia". As of 31.12.2011, € 17M was disbursed for two programme loans.

[111] http://www.procredit-holding.com/front_content.php?idcat=22
[112] http://www.procredit-holding.com/upload/pdf/AnnualReports/Annual_Report_2011/pch_AR_2011_15-05.pdf

ProCredit Bank (PCB) Bulgaria *was founded in June 2001 to create a reliable financial partner for small businesses. As of the end of 2011, the bank had total assets under management of € 705 million and a country-wide network of 83 branches (see* ***Box 13.7****) In its core market of small business loans of up to € 150 000, ProCredit Bank Bulgaria has strengthened its position through the years and is generally considered to be a market leader*[113]. At end-2011, PCB Bulgaria had 169 131 clients.

ProCredit Bank "The former Yugoslav Republic of Macedonia" started to operate in October 2003 with the aim of serving small businesses and ordinary people, focusing on lower-income families. It has a country-wide coverage of 35 branch offices (see **Box 13.7**). Its main areas of support involve job creation, rural modernization and environmental protection in the least developed regions of "the former Yugoslav Republic of Macedonia". Generally, in "the former Yugoslav Republic of Macedonia" the banking sector is highly concentrated, with the three largest banks accounting for 64% of total assets (as of 31.12.2011). However, most of the banks underserve or credit ration MSMEs. Thus, ProCredit is perceived as the reference bank for micro-credits.

Box 13.7 ProCredit Bulgaria and ProCredit "The former Yugoslav Republic of Macedonia". Coverage, 2011.



Source: http://www.procredit-holding.com/front_content.php?idcat=30

(1) **CEB Loan € 5M for ProCredit Bulgaria approved in July 2005 (disbursed in 2005/06)**

The programme loan benefitted 99 small and medium sized enterprises, preserved 1 485 jobs and created 445 jobs.

(2) CEB Loan for ProCredit Bank "The former Yugoslav Republic of Macedonia" of € 12M approved in 2008 (disbursed in 2008/09)

The programme loan benefited 219 SMEs, mostly the smaller end of the spectrum (see Table **13.6**), preserved 2 647 jobs, and created 439 jobs.

Table 13.6 Distribution of Final Beneficiaries according to Enterprise Size Class

Size Class	Number of Enterprises	%
Micro (< 10 employees)	90	41%
Small (<50 ecmployees)	85	39%
Medium (<250 employees)	44	20%
Large	0	0%
Total	**219**	**100%**

[113] http://www.procredit-holding.com/front_content.php?idcat=30

Chapter 14. Lessons Learned and Options Ahead

The purpose of this final chapter is (i) to summarise the main lessons from the Bank's experience in MSME financing following four decades of operations, monitoring and evaluations, and (ii) to outline several options for further consideration so as to enhance the Bank's existing operating model and the social added value in this sector through common contributions from the in-house directorates.

Lessons Learned

The CEB pays particular attention to the quality of all projects/programmes and strives to optimise their social added value[114]:

- The CEB performs an in-depth appraisal of the financial condition of the borrower and, where necessary, of the guarantor. On the basis of the loan request formulated by the borrower, the Bank assesses the project's/programme's objectives and financing plan by carefully analysing its socio-economic impact, technical aspects and costs, the institutional capacity to manage the project as well as the project's impact on environment. Following on from the Opinion on Admissibility by the Secretary General of the Council of Europe and subsequent project approval by the CEB's Administrative Council, the project/programme financing can start once the framework loan agreement has been negotiated between the Bank and the borrower.
- After the first disbursement, the Bank's services, Directorate General for Loans and Social Development and Directorate for Technical Assessment and Monitoring, carry out regular monitoring and on-site missions to verify the physical progress of works, compliance with costs and procurement procedures, and the achievement of the project's/programme's approved objectives and anticipated social effects. The CEB focuses on assistance and monitoring throughout the entire project cycle.
- Upon completion of the project/programme, a final report drawn up by the borrower details the use of funds and compliance with objectives approved by the Administrative Council and provides information on the material and social results obtained.
- An independent assessment of selected projects and programmes by the Evaluation Department (see **Box 14.1**) enables the CEB to measure their medium-term socio-economic impact and to improve the quality of on-going and forthcoming projects and programmes through organisational learning.

Box 14.1 The CEB's Evaluation Department (EVD)

Created end-2002, the Evaluation Department (EVD) has defined guidelines in accordance with international best practices and OECD-DAC Guidelines. EVD is independent from the Bank's operational services and reports directly to the Governor, who transmits evaluation reports unaltered to the Administrative Council.

Each evaluation follows a rating system based on the criteria of:

- *Relevance* (of objectives with regard to needs),
- *Effectiveness* (achievement of objectives),
- *Efficiency* (conversion of inputs into results),
- *Impact* (broader, notably social or environmental, effects) and
- *Sustainability* (prospects for lasting effects beyond project implementation).

The evaluation cycle in the field of job creation was launched in 2006. From 2006 to 2009, EVD evaluated seven CEB-financed programmes in favour of creation and preservation of viable jobs benefitting MSMEs in CEB target countries. The selection of programmes was based on purposive sampling to cover a range of implementing modalities and countries. The evaluation synthesis was based on evidence collected through a survey of more than 2 000 companies and field visits to over 20 financial intermediaries, including on-lending banks and leasing banks, participating in CEB-financed programmes.

Source: The text box is based on the CEB Website describing the Evaluation at the CEB

[114] CEB Report of the Governor 2011

Following the assistance and monitoring performed by the General Directorate for Loans and Social Development, on-site missions conducted by the Directorate for Technical Assessment and Monitoring, and evaluation findings of the Evaluation Department, several lessons and findings can be summarised regarding the Bank's activities in the sector of action "creation and preservation of viable jobs":

- The CEB has successfully deployed its efforts to prioritise investments in its target countries, including through the use of "transit loans" (see **Chapters 2, 9** and **11**).
- Social impact was mainly associated with the creation and preservation of viable jobs, as explicitly defined in the social objective of CEB financing. Employment generation effects, based on established in-house methods, were generally above expectations, varying with the financial performance of the financed SMEs.
- A multiplier effect was also registered in terms of jobs created in other companies, mainly suppliers. Thus, the indirect job creation impact was also significant.
- Relevance of the Bank's activities depends on the prevailing market conditions, both national and international, and/or on the choice of the implementing partner.
- Relevance is high when access to credit is more difficult. Thus, in the context of the socio-economic consequences of the banking crisis of 2007 (see **Chapters 11** and **12**), CEB financing has a more pronounced financial additionality as opposed to the pre-crisis years. Generally, the CEB's additionality is related to the Bank's provision of medium- and long-term, thus stable, debt to intermediaries and final beneficiaries (see **Chapter 13**).
- The judicious choice of intermediaries at appraisal allows for an effective transfer of the CEB's social development objective to the implementing partners. It also determines the capacity of the Bank to reach its intended final beneficiaries, assuming they are well-defined at the design stage. Preference should be given to partners with broad experience and a business strategy focused on support to MSMEs .
- Very broadly defined SME programmes tend to score lower relevance ratings; while more targeted programmes involving smaller lending volumes and narrower social objectives have higher added value. For example, the Evaluation Report on Women Entrepreneurship in the Baltic States in 2002-04 channelled through 5 intermediary banks in target countries (2 in Lithuania, 2 in Latvia and 1 in Estonia) concluded that the programmes performed well and were highly efficient. The programmes aimed to create and preserve jobs in firms owned or managed by women, or which had a project improving women's situation on the labour market.[115] The focus on small credits to small, successful women-led firms provided the CEB with a specific niche and the cooperation with the Nordic Investment Bank (NIB) was valuable, in particular at the start-up phase of the programmes. All five programmes were complemented by technical assistance provided by NIB.
- Leasing was an effective measure to reach micro- and small businesses in the CEB's target countries. This instrument allowed smaller firms to obtain needed capital equipment even when they had limited or no access to bank funding (see **Chapter 7**).
- Sharing the knowledge gained from prior operations represents another source of the CEB financing's added value. For example, following its cooperation with specialised DFIs, such as Finnvera (see **Chapter 13, Case 1**), which have built the necessary expertise and capacity to reach firms that tend to be underserved and/or credit rationed by commercial banks (e.g. start-ups, firms facing difficulties finding merger partners or selling-out), the CEB brought this experience into the discussions on preparation of activities with other intermediaries that could have benefitted from potential improvement in their targeting mechanisms.

[115] Preparation in Lithuania was supported by a Finnish Trust Account, whereas in Estonia and Latvia existing NIB women entrepreneurship programmes were renewed. The Trust Fund and the cooperation with NIB contributed to an exemplary preparation of the programme. A major added value of the programme was the successful transfer of the CEB social objectives to intermediary banks. Source: EVD Report

Options Ahead

Following the aforementioned findings and four decades of operations, monitoring and evaluation, it would be sensible for the Bank to continue to prioritise MSME financing in its target countries, where the additionality of longer maturities of its loans is most effective and catalytic effects are generally more pronounced given shallow and less inclusive financial systems (see **Chapters 8** and **9**).

At the same time, the Bank could consider enhancing the existing operating model of CEB MSME financing to better respond to the needs of the intermediaries and final MSME beneficiaries. The suggested options represent a common effort by the in-house directorates to contribute to the enhancement of the social added value of the CEB's operations in this sector[116]. The following list is not to be considered exhaustive or limiting:

- Adopting a more targeted approach, such as focusing on the lower-end of the MSME size spectrum.

CEB applies the EU definition of MSMEs as eligibility criterion for MSME financing (see **Chapter 3**), according to which 99.8% of European enterprises (see **Chapter 4**) could be potential participants in CEB-financed operations in favour of job creation and preservation. This general targeting is evidenced in **Cases 1** to **5** presented in **Chapter 13**. For example, when aggregating the final beneficiaries of the CEB support in favour of job creation and preservation to the five borrowers in **Cases 1** to **5**, the main recipients of the CEB financing represent the broad spectrum of MSMEs (see **Table 14.1**). This indicates an absence of specific targeting of the lower-end of the MSME size spectrum.

Table 14.1 Distribution of Final Beneficiaries across Enterprise Size Class (Based on Five Case Studies)

Size Class	Finnvera	MicroBank	EFL	TSKB	ProCredit Bulgaria	ProCredit FYROM	Total	%
Micro (< 10 employees)	964	2249	8 820	22	0	90	**12 145**	**59%**
Small and Medium (<250 employees)	508	117	7 408	125	99	129	**8 386**	**41%**
Large	0	0	0	7	0	0	**7**	**0%**
Total Number of Beneficiaries	**1 472**	**2 366**	**16 228**	**154**	**99**	**219**	**20 538**	**100%**

Notes:

1. *The table presents actual final beneficiaries only of utilised tranches.*
2. *Due to data limitations, the table does not include number of beneficiaries under **the programme loan 2 and 3** of € 150 million for MicroBank, for which the monitoring reports disaggregated the beneficiaries into the following categories: women, migrants, families, and others (see **Case 2**).*
3. *Due to data limitations, the table does not include the final beneficiaries of **programme loan 1** of € 9 million to Finnvera.*

To increase its social added value in terms of job creation and preservation and contribution to the social cohesion of local communities, the Bank could consider setting additional targeting measures to effectively reach the lower-end of the MSME size spectrum. Under the current operating model of MSME financing, these measures would have to be complemented with a judicious screening of implementing partners, a comprehensive understanding of their effectiveness as resource allocators to sub-projects which are economically, socially and environmentally sustainable[117], and close technical co-operation with them in the design, preparation of operations, and monitoring arrangements[118].

To this effect, certain action has already been taken by the Bank in recent years. The CEB's 2011 Annual Report on Project Preparation and Follow-Up concluded that "specific limits on total project size and/or CEB loan amounts have brought down the size of [sub-]projects supported by [the] CEB and increased focus on [smaller] firms that typically have more difficult access to long-term funds"[119].

[116] The suggestions are based on testimonies and reports of the CEB's General Directorate for Loans and Social Development, Directorate for Technical Assessment and Monitoring, and Evaluation Department.
[117] The CEB's Progress [Monitoring] Report on Projects 2009
[118] The CEB's Progress Report on Projects - 2007
[119] The CEB's Annual Report on Project Preparation and Follow-Up 2011

These additional targeting measures could also contribute to differentiating the Bank's activities in this sector from other IFIs active in the CEB's countries of operations, such as the EIB or the EBRD (see **Table 14.2**).

- Complementing the existing financing instrument, programme loans passed on through intermediary banks, with additional instruments, such as technical assistance for programme preparation, to confer a more differentiated and contextualised approach to MSME financing.

This contextualised strategy is followed by other IFIs, such as the EIB and the EBRD. For example, the EIB Group in addition to its general SME support has implemented financial instruments such as JASMINE and JEREMIE and is developing new structures to provide additional funding for SMEs, such as guarantee structures in partnership with the EC. In addition to SME finance through financial intermediaries, the EBRD provides policy dialogue to improve the business climate for MSMEs and non-financial enterprise support under its TurnAround Management (TAM) and Business Advisory Services (BAS) (see **Table 14.2**).

- Complementing or replacing the headcount-based impact indicator with more relevant and suitable indicators.

EVD has highlighted the low information content of, and methodological difficulties associated with, the headcount-based approach focused exclusively on number of jobs created and/or preserved. Such an objective is usually not "transferable" to intermediary banks and/or participating banks.

Complementing or replacing the said development impact indicator with more relevant and suitable indicators would provide more pertinent information on the actual impact of programmes. For example, when programmes entail financial inclusion (see **Cases 1** to **5**) adequate monitoring indicators should be assessed. For these purposes, a clearer operational definition of objectives would have to be defined at the design stage. This would allow for an evidence-based and problem-focused analysis at the design stage, taking into account national and sub-national specificities, such as the depth of the SME lending market and types of services available to SMEs.

This approach would build upon the in-house "two-pronged approach" applied to project/programme screening, which appraises the social added value at two levels: "country" parameters and the intrinsic characteristics of the project/programme itself. For example, under this approach the financial impact of a programme is pre-screened by assessing, inter alia, its "capacity to address market imperfections" and "deepening of the financial system to enhance the availability of long-term funds for social projects" [120].

- Adapting the eligibility criteria[121]

The definition of eligible goods, effectively focusing on hard goods, does not fully take into account the role and needs of MSMEs. For example, MSMEs increasingly require not only machines, but also know-how support for growth. In this sense, the CEB could also consider extending its financing to services, such as consultancy or software development. However, given the nature of the CEB loans, only medium- and long-term investments could be appropriate for financing.

***

Thus, in order to respond to the needs of intermediaries and MSME beneficiaries, the Bank could explore the aforesaid suggestions by enhancing its operating model and offering a more differentiated and contextualised MSME strategy. If pertinent, these options would be considered in a holistic manner taking into account the Bank's overall strategy and available resources, including donors' contributions, and willingness and institutional capacity of its implementing partners.

[120] The in-house "two-pronged approach" approach for screening project loans and programme loans takes into account the country context and the project's social value added. The underlying premise of "the two-pronged approach" is that the social added value of a project loan or programme loan depends on both the intrinsic characteristics of the project/programme and the context in which it is carried out ("country" parameters).
[121] The CEB's Progress [Monitoring] Report on Projects 2009

Table 14.2 Quotes from IFI Policy Statements

	IFC[122]	EIB Group[123]	EBRD
Mission Statement	Purpose: to create opportunity for people to escape poverty and improve their lives by: (i) Mobilising other sources of finance for private enterprise development; (ii) Promoting open and competitive markets in developing countries ; (iii) Supporting companies and other private sector partners where there is a gap; (iv) Helping generate productive jobs and deliver essential services to the poor and the vulnerable.	The EIB is the long-term financing institution of the European Union. Its mission is to help implement the EU's policy objectives by financing sound business projects.	To support projects from central Europe to Central Asia. Investing primarily in private sector clients whose needs cannot be fully met by the market, the Bank fosters transition towards open and democratic market economies.
MSME Strategy	***MSME Finance*** MSME finance includes leasing, microfinance, retail payments, SME banking, and banking on women. ***SME Banking*** IFC works to increase access of SMEs to financial services in developing countries by providing funding for equity, loans, and mezzanine finance to financial intermediaries focusing on SME financing, and by building capacity of financial intermediaries and raising awareness on best SME Banking practices. IFC uses both investments and technical assistance to support financial intermediaries outreach to the SME sector more effectively and efficiently.	SME finance is a joint priority for the EIB Group (EIB and EIF). ***SMEs and Medium-Sized Corporates (MidCaps)[124]*** In the EU and Candidate and Potential Candidate Countries, primarily through Loans for SMEs and Loans for MidCaps. ***EIF*** Equity, guarantees and securitisation activities and deployment of microfinance resources. ***Microfinance since 2000*** In 2011, successful start of microfinance operations under the European Progress Microfinance Facility. ***Specific Initiatives*** JASMINE (Joint action to support micro-finance Institutions in Europe); JEREMIE (Joint European resources for micro to medium enterprises initiative) and equity funds of funds.	Support for MSMEs is central to the Bank's transition mandate in its countries of operation. ***MSME Strategy adopted in 2006 based on three pillars:*** ▪ **Finance** through financial intermediaries ▪ **Policy dialogue** to improve the business climate for MSMEs ▪ **Business support** TurnAround Management (TAM) and Business Advisory Services (BAS) for non-financial enterprise support In April 1999, the EBRD and the European Commission launched the SME Finance Facility for micro, small and medium-sized enterprises operating in the EU Accession countries of central and eastern Europe[125].
MSME Instruments	IFC uses both investments and technical assistance to support financial intermediaries outreach to the SME sector more effectively and efficiently. Investments: equity investments, loans, revolving credit lines, and risk mitigation facilities. Advisory services: strategy, market segmentation, product development, risk management and IT/ MIS facilities.	"Loan for SMEs", intermediated through financial intermediaries, remains the Bank's core SME financing instrument. The EIB requires the intermediary to match the funds provided by its loan with at least the same amount, thus creating a leverage effect. Maximum cost of investment is € 25M. The EIB's contribution can be up to 100% of the investment, with a maximum of € 12.5M. The EIB Group is also developing new structures to provide additional funding for SMEs: (i) guarantee structures in partnership with the European Commission, leveraging on Structural Funds and aimed at meeting the specific demand in countries facing particular liquidity squeezes; (ii) an extension of the Risk Sharing Finance Facility (RSFF) to SME financing to provide sustainable, long-term support for SMEs, including innovative ones.	Credit lines to existing commercial banks (so called "partner banks") focused on MSE and/or SME sub-borrowers, investments in and loans to specialised microfinance banks, SME leasing operations, and loans to non-bank microfinance institutions. In the EU/EBRD SME Facility a micro loan/lease is a loan up to a maximum of € 30k, and a small loan/lease between € 30k and € 125k. In the MSE lending programmes a micro loan is a loan up to $ 10k and a small loan can go up to $200k. Other credit lines targeting SMEs have traditionally exceeded the loan size targets of the two types of programmes mentioned above. Products to be explored: Support to non-bank microfinance institutions (MFIs); Local Currency Financing; Microleasing; Risk Sharing; Credit Scoring; MSME Focussed Equity and Loan Funds; TAM/BAS innovative programmes.[126]

[122] http://www1.ifc.org/wps/wcm/connect/corp_ext_content/ifc_external_corporate_site/what+we+do/whatwedo
[123] http://www.eib.org/attachments/thematic/eib_report_activities_supporting_smes_2011_en.pdf
[124] A "MidCap" is defined by EIB as any autonomous enterprise or group employing < 3 000 people.
[125] This includes Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovak Republic and Slovenia.
[126] http://www.ebrd.com/downloads/policies/sector/msme.pdf

CONCLUDING REMARKS

Since the mid-1960s, the CEB has provided financing in favour of "creation and preservation of viable jobs" in its member countries, recognising the link between employment and social cohesion. From 1995, the CEB's support to this sector became a significant part of the CEB's operations in its Member States.

The final objective of CEB financing in this sector is to create and preserve viable jobs by providing MSMEs with medium- and long-term financing. To this effect, the CEB promotes financial inclusion of MSMEs in its member countries and also contributes to deepening financial sectors and strengthening MSME lending markets in its target countries[127].

The financial and economic crisis that started in 2007 affected all CEB member countries, evidenced in more fragile sovereigns, tightened credit supply and credit standards, subdued growth, and reduced employment opportunities. The unemployed, long-term unemployed and migrant workers are several social groups badly affected by the crisis in most CEB Member States. Given the potential of MSMEs to (re-)integrate the populations, to generate employment and to promote economic growth and social cohesion, the CEB has provided continued support to MSMEs in its member countries, with particular focus on its target countries.

At end 2012, the CEB's support to MSMEs remained a major pillar of its activities. In order to increase the social added value of its operations under this sector, the CEB could further explore several alternatives to enhance its operating model by developing a more differentiated and contextualised approach that would respond to the needs of final beneficiaries and capacities of implementing partners. Following over four decades of operations, monitoring and evaluations, the study presents several non-exhaustive alternatives for consideration, such as targeting the lower-end of the MSME size spectrum; complementing the financing instrument (programme loan) with other instruments (e.g. technical assistance); adding to or replacing the headcount-based approach to impact assessment with more relevant and suitable indicators (e.g. financial inclusion); and last but not least, adapting the eligibility criteria to the role and needs of MSMEs.

[127] Although CEB MSME financing may have such potential effects, they are not specified as objectives in the design documents, and there are no appropriate monitoring indicators on which final performance could be evaluated.

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STATISTICAL ANNEX

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Table 4.2

Total employment growth in the non-financial business economy and contribution of size classes, EU27, 2002-2010

	Micro	*Small*	*Medium-sized*	*SMEs*	*Large*	*All enterprises*
2002-2003	1,804,000	34,000	-205,000	1,633,000	-447,000	1,186,000
2003-2004	637,000	436,000	228,000	1,300,000	315,000	1,616,000
2004-2005	896,000	425,000	262,000	1,583,000	309,000	1,892,000
2005-2006	1,361,000	733,000	518,000	2,612,000	419,000	3,031,000
2006-2007	1,233,000	655,000	690,000	2,578,000	1,214,000	3,792,000
2007-2008	958,000	216,000	252,000	1,426,000	621,000	2,048,000
2008-2009	-1,356,000	-830,000	-647,000	-2,833,000	-948,000	-3,781,000
2009-2010	-488,000	-247,000	-182,000	-917,000	-177,000	-1,094,000
average	631,000	178,000	115,000	923,000	163,000	1,086,000
average, % of all enterprises	58	16	11	85	15	100

Explanation: Enterprsies that were micro enterprsies in 2002, plus newly created enterprises during 2002 -2003 (taking into account exit as well) created 1,804,000 jobs in 1804000; similarly, enterprises that were micro enterprises the previouos year, have on average created 631,000 jobs between 2002 and 2010.

Note: The contribution of size classes to total employment growth is controlled for the population effect.

Source: EIM, based on European Commission: Are EU SMEs recovering from the crisis? Annual Report on EU Small and Medium Sized Enterprises 2010/2011; data 2008-2010 estimates.

Table 4.3

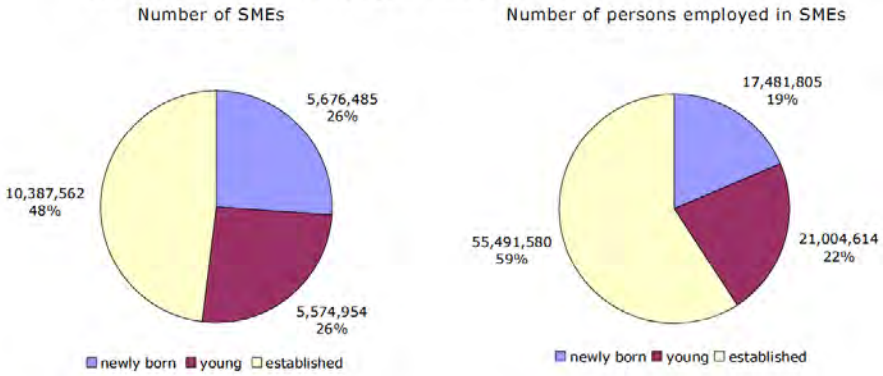
Average annual employment growth rates in the non-financial business economy, 2002-2010

	Micro	*Small*	*Medium*	*SMEs*	*Large*	*All enterprises*
			average annual change in %			
Bulgaria	3.7	5	1.9	3.5	-0.1	2.4
Cyprus	2.2	2.9	3.3	2.7	2	2.5
Czech Republic	-1.8	0.4	0.9	-0.5	-0.3	-0.4
Estonia	2	0.3	1.1	1.1	-0.2	0.8
Hungary	0.5	0.8	-0.3	0.4	-0.1	0.2
Latvia	0.1	0.5	-0.6	0	-1.3	-0.3
Lithuania	6.5	1.7	0.9	2.8	-0.3	2
Malta	-1.8	1.6	1.5	-0.1	-2.9	-0.8
Poland	1.5	2.2	2.5	1.9	2.5	2.1
Romania	12.2	3.9	-0.1	4.9	-3.1	1.6
Slovak Republic	15	-0.7	-0.2	3.2	-1	1.2
Slovenia	2.5	0.5	-1.5	0.7	1.9	1.1
Belgium	1.5	0.3	0.4	0.9	1	0.9
Denmark	1.1	0.5	0.3	0.6	-0.1	0.4
Finland	1.6	0.8	0.5	1	-0.3	0.5
France	1.4	-0.4	-0.4	0.3	0.5	0.4
Germany	2.2	1.3	1.6	1.7	0.2	1.1
Greece	0.9	2.8	0.6	1.2	-1.5	0.6
Ireland	3.4	0.6	0.5	1.5	0.1	1
Italy	1	0.5	0.5	0.8	0.4	0.7
Luxembourg	2.9	1.9	1.7	2.1	-0.5	1.2
Netherlands	7	0.9	-2.7	1.9	0.5	1.4
Portugal	2.6	1.1	0.7	1.7	1.2	1.6
Spain	0.4	-0.4	0.4	0.2	1.8	0.5
Sweden	0.3	3	2.6	1.6	0.9	1.3
EU27	1.7	0.7	0.5	1	0.4	0.9

Source: *EIM Business & Policy Research, based on European Commission: "Are EU SMEs recovering from the crisis? Annual Report on EU Small and Medium Sized Enterprises 2010/2011; data 2008-2010 estimates.*
Note: *the contribution of size classes to total employment growth is controlled for the "population effect"*[128].

Figure 4.2

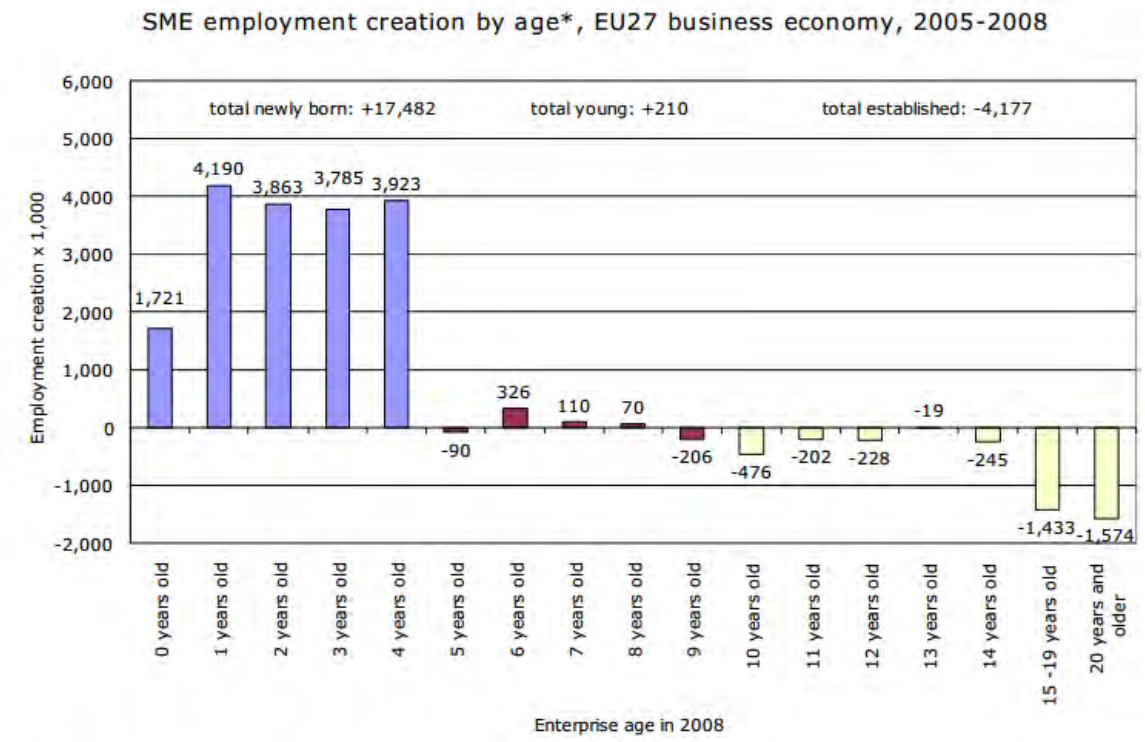
The number of small and medium-sized enterprises and their employment in the EU27 business economy, by age of firm, 2008



Legend: Newly born enterprises: up to five years old in 2008; Young enterprises: 5 up to 10 years old in 2008; Established enterprises: 10 years and older in 2008.
Source: Share of enterprises by age class and share of employment by age class extracted from the Orbis-Amadeus database (n=2,609,300 observations). The total number of enterprises and employment is extracted from Eurostat Structural Business Statistics database for 2008, which is supplemented by the financial industries and other services

[128] For an explanation of the "population effect", please see p. 19

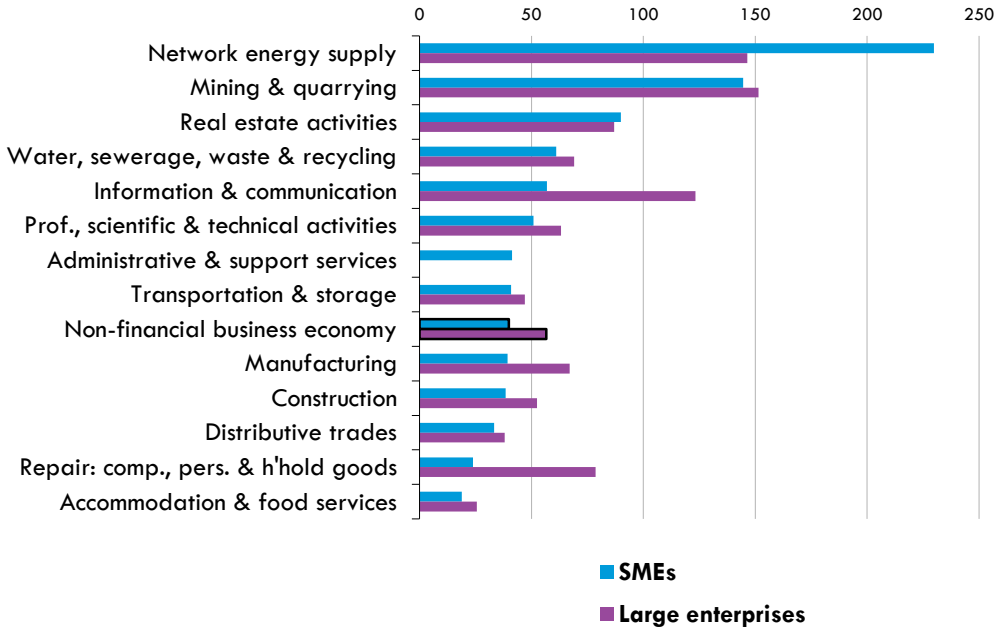
Figure 4.3



** Only enterprises that survived.*

Source: Orbis-Amadeus (n=2,609,300).

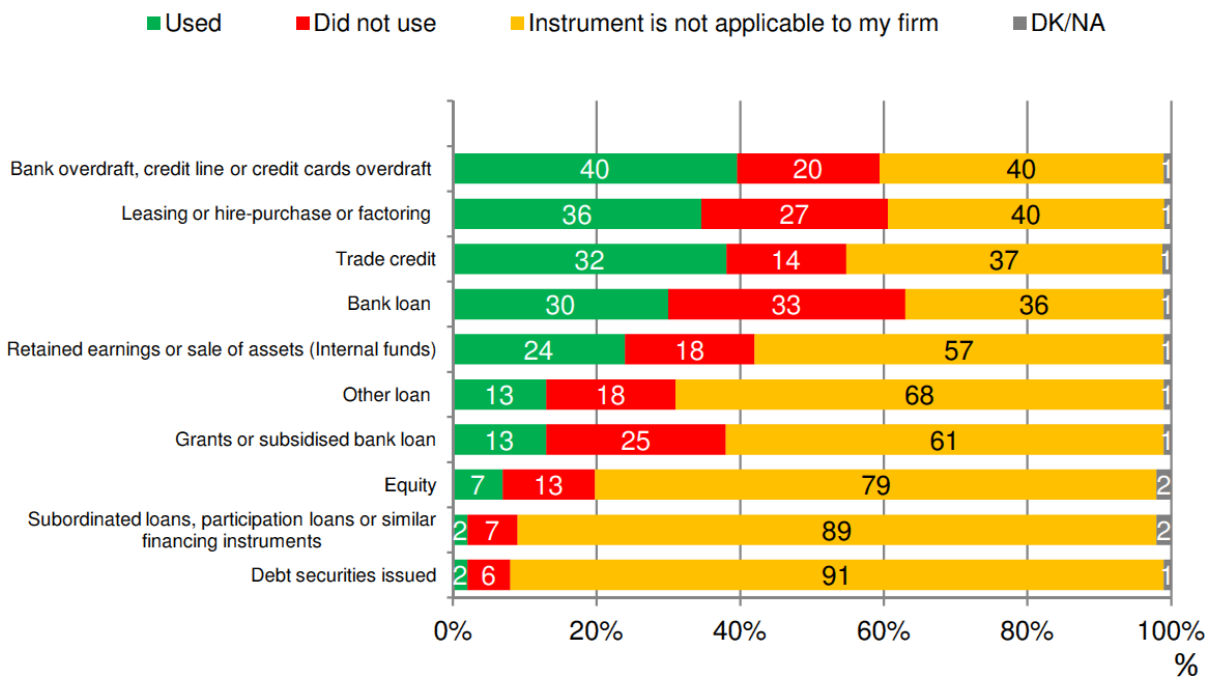
Figure 4.4 Apparent Labour Productivity, EU-27, 2008 (EUR 1 000/person)



Source: Eurostat. Key figures on European business with a special feature on SMEs (2011 edition) ISSN 1830-9720

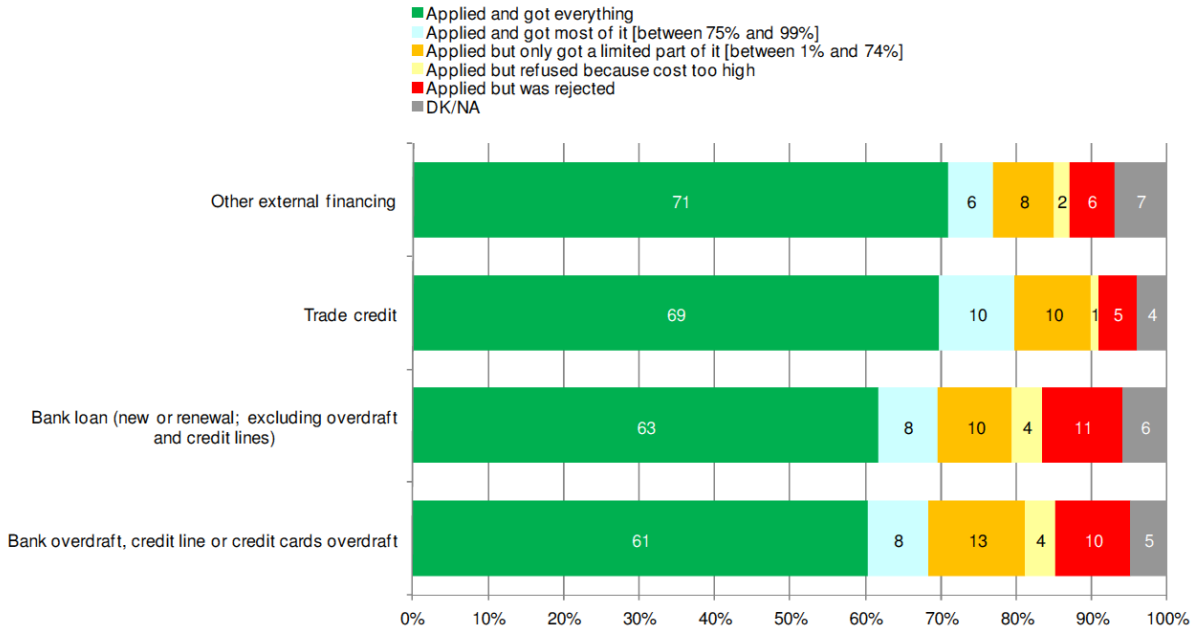
(1) Administrative and support services, not available for large enterprises

Figure 6.1 MSMEs' Use of Internal and External Financing in the Past Six Months
EU-27, 2011



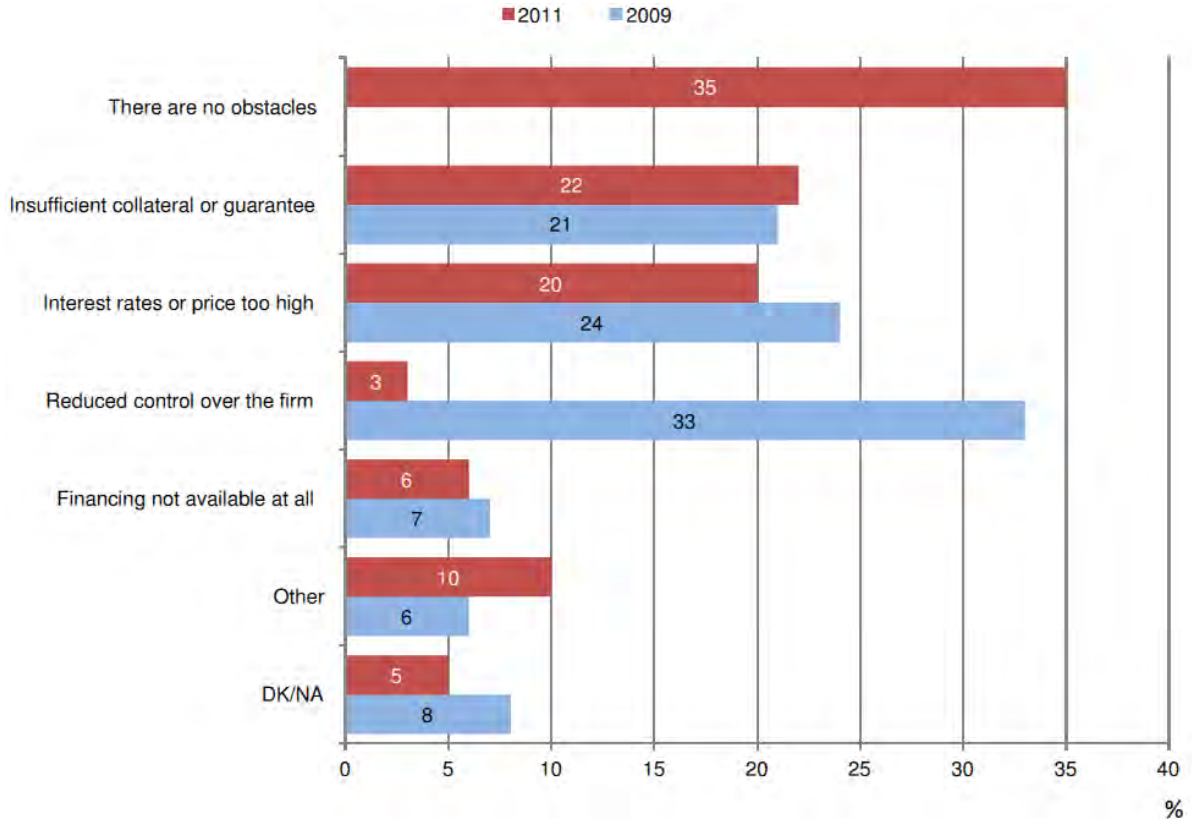
Source: 2011 Survey on SMEs' Access to Finance (SAFE) conducted by EC and ECB across 38 countries.

Figure 6.2. Outcome of the MSME Applications for External Financing
EU-27 (2011)



Source: 2011 Survey on SMEs' Access to Finance (SAFE) conducted by EC and ECB across 38 countries.

Figure 6.3. The Most Important Limiting Factors to Obtaining Bank or Other Loans EU-27, % MSMEs



Source: 2011 Survey on SMEs' Access to Finance (SAFE) conducted by EC and ECB across 38 countries.

Figure 9.1.
Credit Growth across Central, Eastern and South-Eastern Europe, the Baltic States, and Turkey

This table provides information on the presence of VI support and/or government support for the parent banks of subsidiaries in countries that were part of the Vienna Initiative. Source: EBRD and banks' websites. "Y" ("N") indicate that the subsidiary's parent bank received (did not receive) government support in 2008-09.

	BOSNIA-HERZEGOVINA		HUNGARY		LATVIA		ROMANIA		SERBIA	
	Bank name	Support	Bank name	Support	Bank name	Support	Bank name	Support	Bank name	Support
Parent participates in VI	Raiffeisen Bank	Y	UniCredit Bank	Y	DnB Nord Bank	N	Alpha Bank Romania	Y	Société Générale Bank Serbia	Y
	Intesa SanPaolo Bank	Y	Raiffeisen Bank	Y	SEB Bank	N	Banc Post	Y	UniCredit Bank	Y
	UniCredit Bank	Y	Erste Bank Hungary	Y	Swedbank	N	Banca Romaneasca	Y	Piraeus Bank Beograd	Y
	HypoAlpe-Adria-Bank	Y	K&H Bank	Y			Piraeus Bank Romania	Y	Eurobank EFG	Y
	Volksbank BH	Y	CIB Bank	Y			Volksbank Romania	Y	Volksbank Serbia	Y
	NLB Bank	N	Magyar Takarekszövetkezeti Bank	Y			Banca Comerciala Romana	Y	Alpha Bank Serbia	Y
	Turkish Ziraat Bank Bosnia	N					UniCredit Tiriac Bank	Y	Vojvodjanska Bank	Y
	ProCredit Bank	N					BRD - Groupe Societe Generale	Y	Banca Intesa	Y
	Sparkasse Bank	N					Raiffeisen Bank	Y	HypoAple-Adria Bank	Y
									Raiffeisen Bank	Y
Parent does not participate in VI	Bosna Bank International	N	KDB Bank	N	HVB Bank Latvia	Y	Egnatia Bank	N	NLB Bank	N
	ZepterKomercBank BanjaLuka	Y	Volksbank	Y			ProCredit Bank	N	ProCredit Bank	N
			Commerzbank	Y			ABN Amro Bank	Y	Erste Bank	Y
			Banco Popolare	Y			OTP Bank	N	OTP Bank	N
			Deutsche Bank	N			San Paolo IMI Bank	Y	Marfin Bank	N
			Fundamenta-Lakaskassza	N			Banca de Creditsi Dezvoltare Romexterra	N	Moskovska Bank	N
			Allianz Bank	N			Emporiki Bank	N	Credit Agricole	Y
			Budapest Hitel-ésFejleszési Bank	Y					Findomestic Bank	Y
									KBC Bank	Y

Source: De Haas, R. *et al.* (2012), *Foreign Banks and the Vienna Initiative: Turning Sinners into Saints?,* International Monetary Fund. *The dataset comprises 1,294 banks in the ECA region.*

Figure 9.2.
Overview of Government Support to Parent Bank and Participation in the Vienna Initiative

Region	Bank ownership	No. bank-year obs.	No. banks	Average annual credit growth		
		1999-2009	2009	1999-2007	2008	2009
		(1)	(2)	(3)	(4)	(5)
Central & Eastern Europe & Baltic States	Domestic state	94	11	0.27	0.09	0.11
	Domestic private	497	39	0.32	0.17	0.07
	Foreign	748	75	0.39	0.14	0.06
	Vienna	*74*	*8*	*0.45*	*0.13*	*-0.05*
	Non-Vienna	*674*	*67*	*0.38*	*0.15*	*0.07*
	Total	**1,339**	**125**	**0.36**	**0.16**	**0.07**
SEE	Domestic state	79	6	0.36	0.22	0.19
	Domestic private	340	23	0.49	0.21	0.09
	Foreign	527	74	0.67	0.26	0.05
	- Vienna	*165*	*24*	*0.78*	*0.20*	*0.06*
	- Non-Vienna	*362*	*50*	*0.63*	*0.28*	*0.05*
	Total	**946**	**103**	**0.57**	**0.24**	**0.07**
Turkey	Domestic state	25	4	0.19	0.09	0.22
	Domestic private	137	17	0.44	-0.05	0.13
	Foreign	89	12	0.44	0.05	0.18
	Total	**251**	**33**	**0.41**	**0.00**	**0.16**

Source: Bankscope database.

Source: De Haas, R. *et al.* (2012), *Foreign Banks and the Vienna Initiative: Turning Sinners into Saints?,* International Monetary Fund

Figure 11.1. Main Changes to the Definition of Regulatory Capital under Basel III

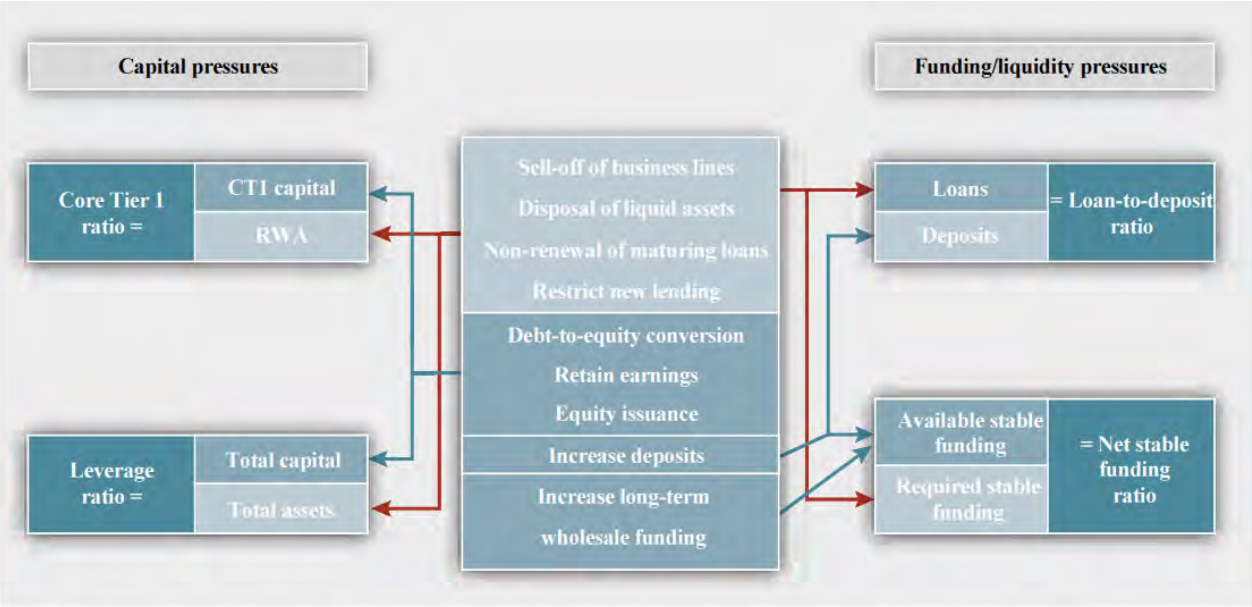
Main changes to the definition of regulatory capital

	Basel II requirements	8%	Basel III requirements	8%
Tier 3			Abolished	
Tier 2	E.g. undisclosed reserves, subordinated debt - Deductions	4%	No substantial alterations	2%
Additional Tier 1	Some preference shares Hybrid capital - Deductions	2%	Some preference shares Portions of minority interests Hybrids with innovative features no longer accepted	1.5%
Core Tier 1	Common equity Retained earnings Minority interests Some preference shares - Deductions	2%	Common equity Retained earnings Portions of minority interests Preference shares generally excluded Silent partnerships generally excluded Portions of minority interests excluded - All existing deductions - Additional deductions (e.g. deferred tax assets)	4.5%

Source: ECB.
Note: GHOS agreement allows for a ten-year phasing-out period for certain instruments issued by non-joint stock companies.

Source: ECB. Financial Stability Review. December 2010

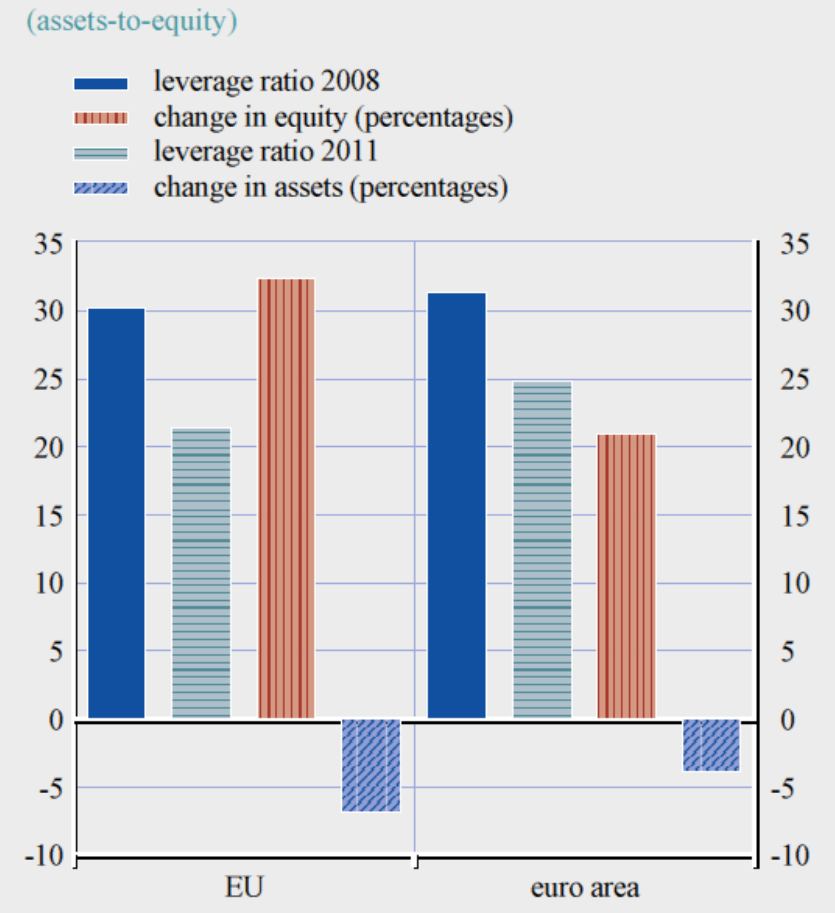
Figure 11.2 Deleveraging Processes and Means to Accommodate Them



Source: ECB.
Notes "CT1 capital" refers to core Tier 1 capital and "RWA" to risk-weighted assets. The "loan-to-deposit ratio" is a proxy for the loan-to-stable funds ratio (owing to measurement problems).

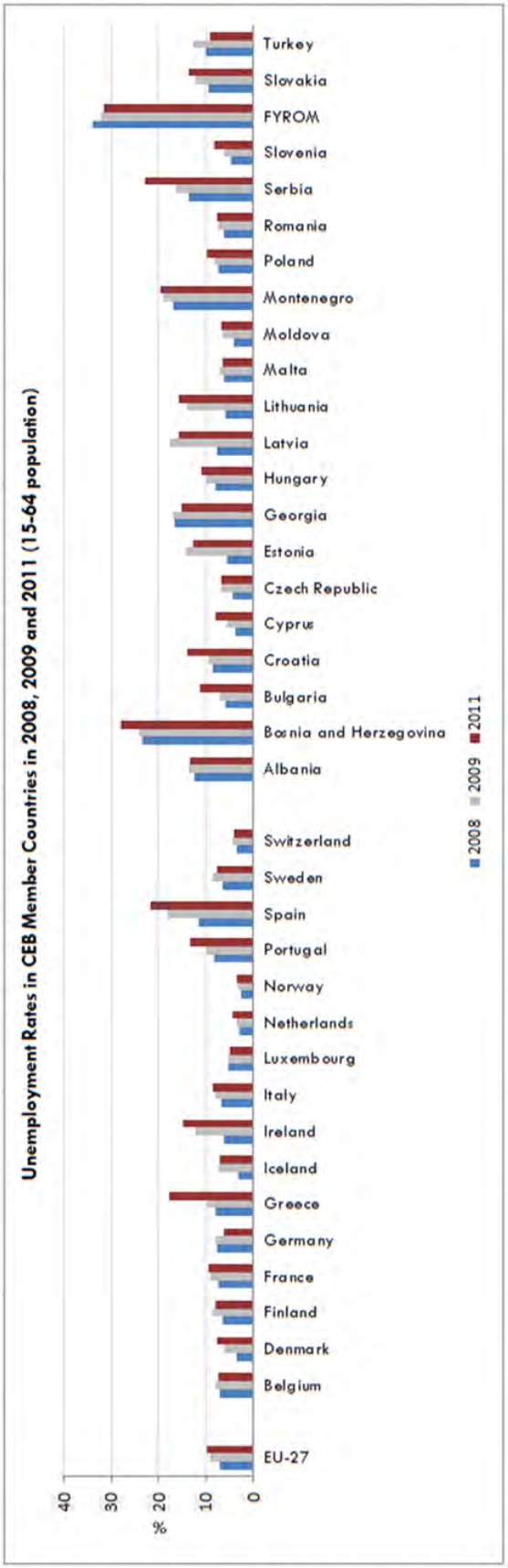
Source: ECB. Financial Stability Review. June 2012.

Figure 11.3. Leverage Ratios of Large EU Banks



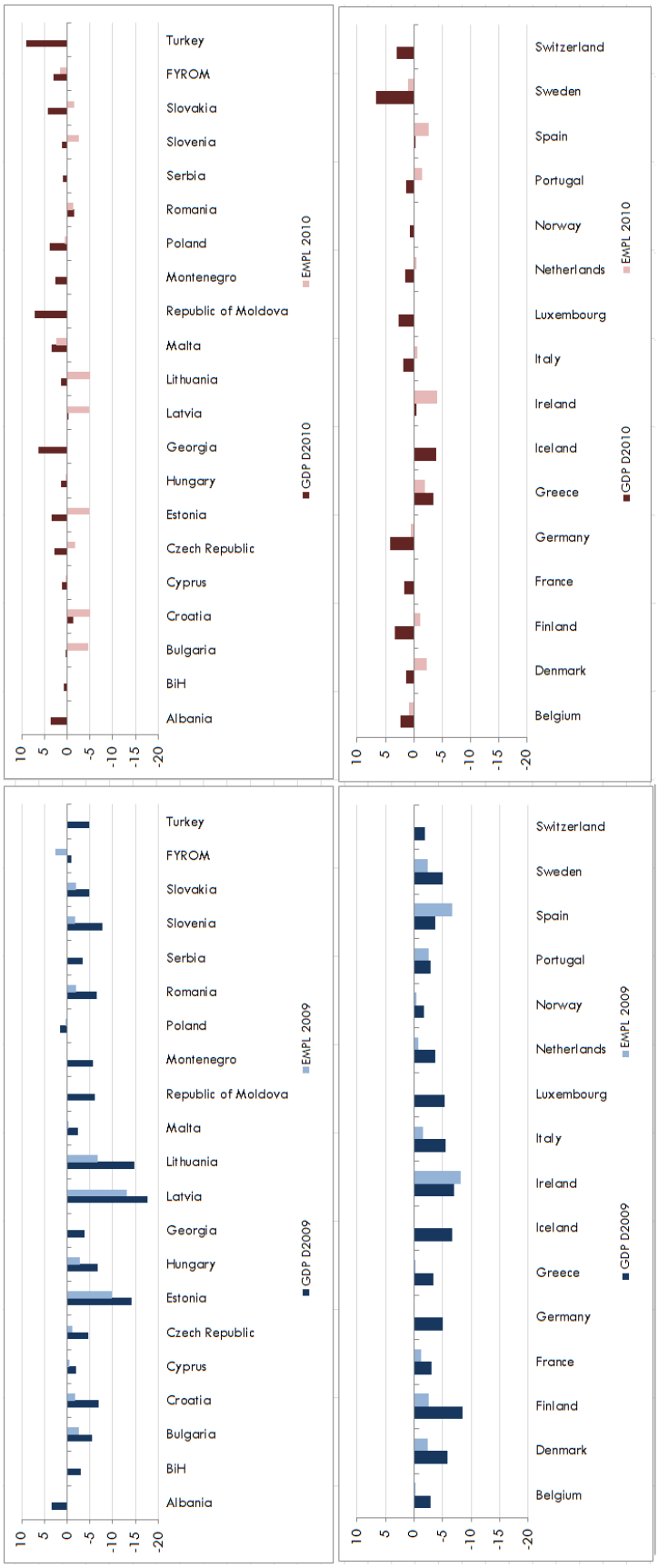
Source: ECB. Financial Stability Review. June 2012.

Graph 12.1 Total Unemployment Rates in CEB Member Countries (15-64 population)



Source: Own graph based on Eurostat September 2012 Update and World Economic Outlook October 2012 Database.

Graph 12.2 Comparisons of Annual Real GDP and Employment Growth Rates in 2009 and 2010 in the CEB Member Countries (%)



Source: Own graph based on Eurostat September 2012 Update and World Economic Outlook 2012 Database. Data not available for Employment Growth Rates for Albania, Bosnia and Herzegovina, Georgia, the Republic of Moldova, Montenegro, and Serbia.

Figure 12.1 Summary of Measures Taken in Countries to Support Jobs during the Recession

Type of measures	Countries concerned
Short-time work or temporary lay-offs schemes	Schemes in place before the crisis: BE, DE, DK, IE, ES, FR, IT, CY, LU, AT, RO, FI, NO, TR, USA Newly introduced schemes: BG, CZ, HU, LT, LV, MT, NL, PT, PL, SI, SK, SE (manufacturing), HR [With compulsory training: CZ, HU, CY, MT, NL, PT, SI]
Employee leasing	FR (Metals), DE (Metals, chemicals)
Extended holidays or career breaks/sabbaticals	LT, BG, NL (Metals), UK, FI, IE
Flexible working arrangements	EE, ES, PL, BG, NL, FR, LT, UK
Pay freezes/cuts	BE, BG, DE (metalworking, textiles and chemicals), EE, IE, EL, ES, FR, HU, IT, LV, LT, NL (Metals), PT, SK, SI, FI (Manufacturing), SE (engineering, architectural consultancies), UK (mainly in the public sector)
Old car buy-back schemes	DE, IE, FR, ES, AT, IT, UK, TR, USA
Access to credit for enterprises	LT, DE, ES, FI, IE, IT, PL, UK
Business start-up incentives	LT, BG, EL, IT, IE, UK, PL, ES, FI, HR, UK
Wage subsidies	LT, BE, NL, BG, UK, AT, EE, CY, PT, SE, FI, UK, FR, EL, IE, ES, HR, PL
Reduction in non-wage labour costs	LT, DE, FI, BE, FR, CZ, PT, UK, HU, IE, PL, SI, NL, IT, TR, UK
Public works for unemployed	LT, IE, LV, HR, TR
Training and work experience programme	CZ, EE, ES, NL, CY, PL, SE, IE, UK, FI, LV, AT, MT, PT, FR, BE, EL, IT, BG, LT, RO, DK, HR, TR, UK
Corporate tax cuts	LT, ES, FR, PL, UK
Job-search assistance	BE (Banking), DK, DE, LT, FR, EE, IT (Chemicals), FI, UK, AT, EL, BG, FR, PL, NL, ES, HR
Reduced statutory minimum wage	PL
Fixed-term employment contracts	LT, DE (Metals), PL
Income support to families	ES, FI
Public investment	DE, ES, UK, USA

Sources: OECD, *Addressing the labour market challenges of the economic downturn*, 2009

Industrial Relations in Europe, 2010

Joint EMCO-COM Paper, *The employment crisis: policy responses, their effectiveness and the way ahead*, 2010

OECD, *The Role of Short-Time Work Schemes during the 2008-09 Recession*, 2011

European Economy, *Short time working arrangements as response to cyclical fluctuation*, 2010

IZA, *Short-Time Work Benefits Revisited: Some Lessons from the Great Recession*, 2011

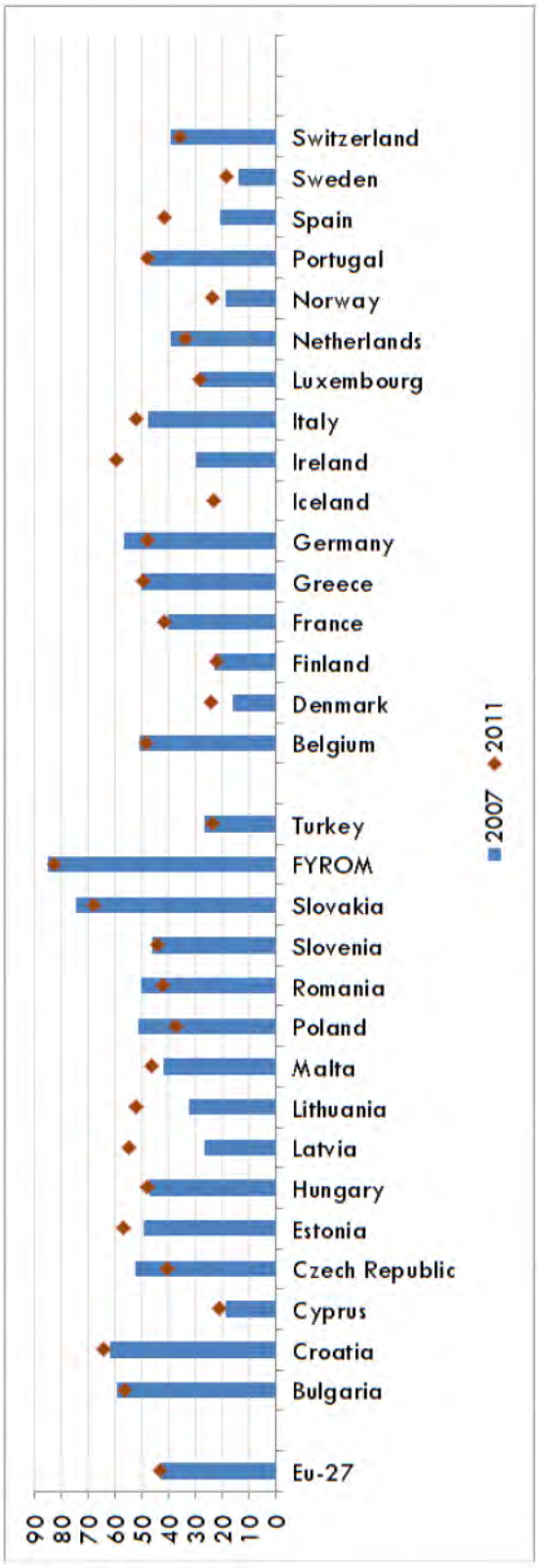
Eurofound, *Extending flexicurity – The potential of short-time working schemes*, 2010

Eurostat, Labour Market Policy Database

Sectoral employment 2010 - 13 case-studies (DE, EE, ES, FI, FR, IE, IT, LT, PL, UK, HR, TR, US)

Source: Vienna Institute for International Economic Studies. Research Reports. "Sectoral Employment Effects of Economic Downturns". Stehrer, R., Ward, T. et al. August 2012.

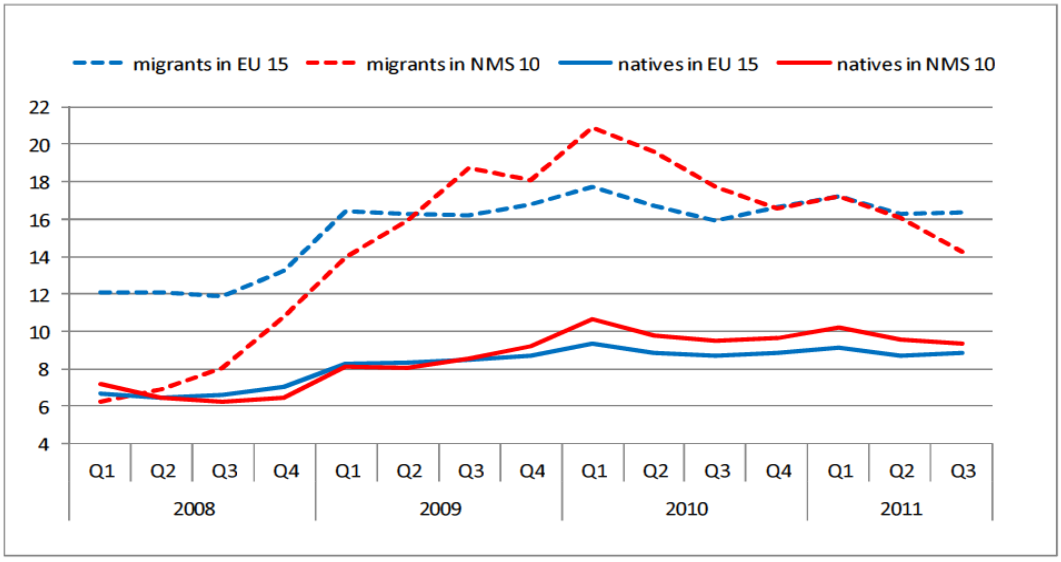
Graph 12.3 Long-Term Unemployment as a Percentage of Total Unemployment (15-64 population) in CEB Member Countries



Source: Own graph. EUROSTAT, Labour Force Survey. September 2012 Update. Data not available for Albania, Bosnia and Herzegovina, Georgia, the Republic of Moldova, Montenegro, Serbia.

Figure 12.2

Unemployment rates of natives and migrant workers in the EU, 2008-2011



Source: Leitner, S. (2012), *Social Consequences of the Crisis and Beyond,* the Vienna Institute for International Economic Studies, Spring Seminar, 23 March 2012.



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