Financial instruments for sustainability and growth of social enterprises – good practices[1]

Case study – Entrepreneurship promotion fund (Lithuania)[2]

The success of the Lithuanian model is due to the provision of both financial and consultative aid to the small and medium enterprises, applicants for a loan from the Entrepreneurship promotion fund .

The main challenges before starting businesses are:

- Lack of sufficient credit history
- High interest rates of the commercial loans which recipients are often unable to pay
- Lack of expertise in sustainable business development and governance

To overcome the abovementioned challenges, a cooperation between multiple public and private partners, including ministries, a state-owned social fund and 57 credit unions, was put into practice in Lithuania. The loans provided had better-than-market conditions (including low interest rates) and were combined with free training of the micro and small enterprises that have been operating for less than one year, as well as individual entrepreneurs and social enterprises. Priority was given to disadvantaged groups – unemployed people, disabled people, young people under age 29 and individuals over 50. The main objective was to stimulate quality employment and social inclusion and to promote an active labour and business market, oriented towards job-creation. Analysis of the current market situation was conducted as part of the consultative program in Lithuania as to ensure that emerging market gaps were addressed immediately.

Lessons learned: The choice of a governing institution was key for the success of the measure. A state-owned institution with the necessary expertise and administrative capacity was chosen as a holding fund manager (INVEGA). Financial intermediaries were selected under a public procurement procedure. A consortium of 57 credit unions, providing 154 locations, was created in order to achieve extensive geographical coverage and inclusion of both rural and urban areas. The initial strategy was amended in the process of distributing the funds as to prolongate the measure for two more years, issuing new loans to answer the high demand. Almost a quarter of the funds were reinvested for the period. The income from interest rates and investments was used to cover the expenses for management of the fund.

Case study – Financing the social economy (Poland)[4]

The Polish practice offers an example for a successful combination of low interest rate loans and free consultations for improvement of the recipients' business skills. The maximum loan amount is EUR 25 000 with repayment period of up to 60 months, including a 6-month grace period. No contribution from the borrower or from a loan guarantor is required. The primary form of collateral is a signed blank promissory note. Additionally, borrowers receive up to 30 hours of free advice on accounting, management of human resources and business control.

The need of implementing the measure was observed in relation to the underdeveloped social economy in Poland, compared to other EU member states. After analysing the market conditions, the authorities concluded that there were several challenges before social enterprises that ought to be cumulatively addressed:

- Limited collateral property
- Limited financing possibilities
- Financing difficulties due to the limited profitability and considerable risk
- Limited experience with external finance or cooperation with other social economy actors such as support centres.

The instrument for social economy promotion works within the wider framework of public support for social economy. Poland's territory was divided into five macro-regions based on their socio-economic characteristics and funds were distributed accordingly. The target group were economically active social enterprises that complied with the additional formal, economic, and social criteria set in the program. Some final recipients managed to co-finance the investments with additional private resources even when it was not required to do so.

Lessons learned: The implementation of the financial instrument demonstrated the strong market demand for such loans. Loans provide a much more adequate promotion of business environment and financial investments compared to grants. The project facilitated job-creation and brought additional intangible benefits to the recipients. Borrowers gained experience in management, business planning, risk-taking, handling external finance and implementation of EU fund projects.

Case study – The Portuguese Social Innovation initiative[6]

Lessons learned:

• Social innovation is not an easy theme, as it is usually assumed as being 'too innovative' and 'nice to have' only after other priorities have been covered. Therefore, it is fundamental to have strong political support at the highest level to move the agenda forward.

• Rather than embedding a social innovation component in all ESIF[7] -financed projects as a transversal priority, the best way to attain critical mass and generate effective impact is by committing a dedicated ESIF budget specifically for financing social innovation projects (even if just a small amount for a proof-of-concept).

• Covering different sectors (Education, Health, Social Protection, Environment, etc.) and levels of intervention (national, regional, local), it is very important to plan and organise well in advance the alignment of social innovation with the ESIF OPs[8] structure concerning the type of fund, geographic coverage and governance, in order to minimise future constraints.

• Focusing the financing instruments on funding projects (regardless of the institutional format of its implementing organisations) rather than on funding specific types of entities (e.g. social economy organisations) allows for a more targeted and effective approach, while avoiding the pitfalls of an evolving legal environment (e.g. related to the legal definition of social enterprises).

• Social innovation projects tend to have different financing needs as they evolve, so it might be relevant to finance the different stages of the life cycle of social innovation and social entrepreneurship projects, thereby setting a comprehensive approach that effectively addresses all relevant needs and builds a sound project pipeline. The key is to adjust the type of financing structures and models to the characteristics of each stage.

• A dedicated structure (either part of pre-existing organisations or newly created for this purpose), with work and inputs of a dedicated technical team that includes both ESIF and social innovation experts, is fundamental for the successful implementation of an integrated social innovation initiative.

• Financing social innovation alone won't work, if not complemented by a strong focus on developing its ecosystem, building networks and engaging with all relevant stakeholders (implementing entities, social investors, intermediaries, evaluators, public sector organisations, etc.)

[1]The present material has been prepared by the Bulgarian Center for Not-for-Profit Law with the assistance of Martina Bogdanova, law graduate from Sofia University "St. Kliment Ohridski", and Polina Dyankova, third year law student at Sofia University "St. Kliment Ohridski"

[2]Based on the material: European Commission DG Regional and Urban Policy, European Investment Bank Advisory Services fi-compass (2015), "Entrepreneurship promotion fund. Case study.", available online: https://www.fi-compass.eu/publication/case-studies/case-study-entrepreneurship-promotion-fund

[3]The Lithuanian Entrepreneurship promotion fund had the European social fund (ESF) as a funding source. The size of the financial aid was of EUR 14.48 million, entirely contributed by the ESF. The absorption rate by the end of 2013 (initial program period) was of 78.32%, while the reinvestment reached 24.2% of the sum.

[4]Based on the material: European Commission DG Employment, Social Affairs and Inclusion, European Investment Bank Advisory Services fi-compass (2016), "Financing the social economy. Case study.", available online: https://www.fi-compass.eu/publication/case-studies/case-study-financing-social-economy

[5]The financial size of the instrument is of EUR 7.32 million (EUR 6.22 million from the European Social Fund + EUR 1.1 million from national public funding). The absorption rate by June 2015 was 99.34% with reinvestment of 22.26% of the sum.

[6]Citation from the material: European Commission DG Employment, Social Affairs and Inclusion, European Investment Bank Advisory Services fi-compass (2020), "Supporting the development of Social Finance Ecosystems in Member States under ESF. Lessons learned from the Portuguese Social Innovation initiative.", p. 17, available online: https://www.fi-compass.eu/publication/factsheets/supporting-development-social-finance-ecosystems-member-states-under-esf

[7]ESIF – European Structural and Investment Funds

[8]OP(s) – Operational Programme(s)

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