

A 3D puzzle map of Europe is shown in the background, with a line graph overlaying it. The graph has a red line that trends upwards, ending at a blue sphere. The puzzle pieces are in shades of blue and grey.

Report
**Financial instruments for the
promotion of return
entrepreneurship: the feasibility
of a transnational guarantee fund
Romania-Italy**

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WORKING PAPER**

Financial instruments for the promotion of return entrepreneurship: the feasibility of a transnational guarantee fund Romania-Italy

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Introduction

The aim of this work is to provide a contribution to the analysis of Guarantee Funds (GF hereinafter) to support micro and small-sized enterprises in Romania.

Functions and purposes of a Guarantee Fund will be analysed to understand how it is possible to create a service network to support Romanian migrants residing in Italy who want to return and start a business in their country of origin, in addition to a network of Romanian entrepreneurs already back to their country after a period spent abroad.

In particular, the analysis will focus on issues of context and on the relevance of the tools developed before and after the activation of the GF, so to achieve the creation of a model that describes both the process and the actions to be undertaken.

Emphasis will be given to remittances and savings, and to the innovative role that they can play in the establishment of the GF as well as in the analysis of existing initiatives in Italy and Romania that could be identified as potential elements to support the implementation of the proposed model.

This analysis and the subsequent modelling of the fund are embedded in the framework of Romanian immigration (or, more precisely - since Romania is part of the EU- Romanian geographical mobility) to Italy and the opportunity to encourage the return of migrants/mobile workers to their country of origin to start entrepreneurial activities.

Operations of business start-up are not a common phenomenon among migrants from Romania (at least not in the most advanced sectors of the economy); however an increasing trend in this direction can be seen, particularly in the building sector, or even more specifically in the services to the building sector. In fact, building, transport and portage¹ are listed among the categories of particular importance for Romanian entrepreneurship in Italy.

Migrants who want to create and start a company in Italy, even if small-sized, encounter major difficulties. When they choose to open their own businesses in their origin country they

¹ See ISTAT data 2010

are confronted with a series of even larger obstacles, ranging from regulatory aspects to administrative, tax, organizational and, of course, financial ones.

In this regard, the barriers to access to credit for starting a business seem to be among the hardest to overcome by potential entrepreneurs, not only for those coming from Romania but also from other countries². Specifically, these obstacles range from the lack of knowledge of the banking system, to lack of significant collateral to offer and to the little knowledge that the banking system generally has of migration phenomena. In such a context, the opportunity of a tool such as a GF can surely help the Romanians to return to their country of origin and to be considered more trustworthy and creditworthy by the financial system.

The main purpose of any fund or guarantee instrument is indeed to support an individual applying for credit to be considered trustworthy, and to provide him/her with a greater opportunity to access and relate to the banking system.

The opportunity to develop such a tool represents the basis for a serious plan for both development aid in countries of origin, and for starting a process of transnational labour mobility that could overcome the problems posed by a more traditional approach to human mobility.

² See questionnaires and interviews of the SU.PA. project (Project co-funded by the Thematic Programme of Cooperation with Third Country on Migration and Asylum)

1 Definition of small sized business and Guarantee Fund (GF)

1.1 Micro-enterprise: elements of identification

For the purposes of this analysis it is important to share a common understanding of what we mean by micro-enterprise and small sized business, and how one should define a GF that can assist their development at a transnational level.

It is not easy to find a standard definition of microenterprise in the Italian and in the wider European market, even though many micro-credit programs have been developed.

The distinctive features and the parameters for the definition of micro enterprise are summarized as follows:

- Specificity of the socio-economic needs.
- Access to small loans/credit despite the shortage / lack of collateral.
- Involvement in development programs for depressed areas.
- Peculiarities of the social and economic inclusion.
- Legal nature (sole ownership ,_Cooperatives_ Limited liability companies etc).
- Number of employees < 10.

The European Commission regards loans of less than 25,000 € as micro-credit, however it would be shortsighted to believe that microcredit is only a purely financial measure. A complete definition of microcredit includes elements that are independent of the amount awarded, and they can be identified as follows:

- The type of credit;
- The purpose of credit;
- The presence of a mentoring/coaching activity.

1.2 Credit Guarantee Organizations: historical aspects and definition

In order to share a common definition of GF, it is now necessary to clarify a few issues that mainly concern the purposes for which such funds were created in the past.

In fact, the GF appears to be a specific option within a broader categorization that includes any institution, association, cooperative or dedicated fund that could facilitate the granting of loans to entrepreneurs starting small-scale undertakings. In this regard, it is more appropriate to use the term Credit Guarantee Organizations (CGO henceforth), which include a variety of shapes and solutions that support business development in a more comprehensive way than a GF. In this report, the two options of GF and CGO will be treated interchangeably.

In historical terms, CGOs have existed in Europe since 1848. Since their inception, these mutual guarantee associations were made up of groups of entrepreneurs who contributed with their own funds to provide credit guarantees to a set of companies, sometimes belonging to the same sector or sharing specific needs (such as farmers, etc.). These associations of mutual guarantee still continue to be an important vehicle for the financing of small sized enterprises in Europe. In some cases, they have evolved to become full-fledged financial institutions such as in the case of Cooperative Credit Banks (hereinafter CCB). The development of different tools also shows that there is not a standard type of CGO, which is “better” than the others. Nevertheless, the aspect that links these experiences is that their success depends on the accuracy and precision with which each CGO is designed in the national context, that is to say, the specific financial institutional framework of a given country. The table below summarizes the different kinds of GFs and CGOs over time:

Table 1 - Different types of CGOs in different historical periods

Period of Establishment	Main Purpose	Prevalent type of CGO
Europe, 19 th century	Mutual assistance among entrepreneurs	Mutual guarantee associations
Europe and North America, 1950-1960	Reconstruction of the sector of small and medium size enterprises	Guaranteed schemes at state level
Developing countries, 1970-1990	Development of micro and small size enterprises, agricultural development	Programs based on the support of the State
Transition economies, 1990-2000	Reconstruction or reactivation of the system for small size businesses	Government programs or supported by NGOs

Source: Guarantee Fund for Small Enterprises, Linda Deleen and Klaas Molenaar, 2004

1.3 The experience of small sized businesses in Italy

In the 1950s, the Italian SMEs often operated in old buildings with very old equipment: the purchase of new technology was a necessity that went beyond their traditional cash flow possibilities, and at that time the financial sector did not have the conditions, in terms of quantity or quality, to ensure such loans. In order to overcome this problem, the Italian government created a structure for financing micro-enterprises called “Artigiancassa” with the aim of providing small loans through the savings of sole proprietors and SMEs that wanted to buy and modernize their plants, purchase equipment and increase the levels of working capital. The establishment of Artigiancassa solved some problems in the short and medium term, but left some unsolved issues on the table in the long run.

In the following years, a new legislative framework was created to develop consortia of SMEs and to establish business associations such as the “Guarantee Craftsmanship Cooperatives”. These institutions, founded and operated by entrepreneurs, managed to improve the quality of craftsmanship by providing guarantees on bank loans to members of the cooperative. Today, cooperatives usually cover up to 50% of a loan while the matching collateral is provided by the entrepreneur. Consequently, these consortia have a "risk-sharing" approach, where the success or failure of a company is related to the entrepreneur, the consortium and the bank. Over time, such groups were able to provide new financial products to their members, such as savings funds, pension funds and the provision of increasingly sophisticated consultancy services.

The partners of the IFAD co-funded SME project believe that in a long-term perspective an approach adapted from this experience can be successfully transferred to the economies of CEEC in general, and to Romania in particular. Clearly, the commitment to forms of credit guarantee for entrepreneurs returning home poses major challenges at two different levels: first, the increased risk normally associated with start-up operations; and second, the transfer of knowledge of the mechanisms already tested in Western economies requires time, commitment and efforts in order to be understood and adapted to the peculiarities of the countries of origin of migrants.

2 The creation of the Guarantee Fund

2.1 The Guarantee Fund: what premise?

The role of the GF has traditionally been to assist the development of an already established business through an intervention that promotes access to finance for development activities.

However, in the case of return entrepreneurs, the situation is different because this kind of GF should also provide assistance for the creation of new start-ups in Romania and it should achieve a good level of efficiency with a minimum level of default. The creation of the institutional network that selects business projects to be funded is therefore of great importance to ensure that such operations have a positive outcome and development impact.

Clear and specific rules must also be established: they have to foresee "collateral contributions" also by the returnee, such as real estate, guarantees from family and colleagues, purchase of capital goods, matching through the system of remittances and savings, etc.

The main steps that could lead to the creation of the GF can be summarized as follows:

- Activation of information sessions and promotion of the initiative, such as meetings with associations, diasporas, etc.;
- Administration of test/quizzes for the selection of would-be entrepreneurs through the creation of custom-made forms and individual interviews;
- Collection of data and guidance to the business plan with group training sessions;
- Elaboration of market research and business planning with a customized approach and training;
- External evaluation of the GF on the provision of collateral;
- Activation of ongoing support and monitoring of the development of the business plan³.

³ Su.pa The Guarantee Fund *Modular approach and accession criteria*, Veneto Lavoro, 2011

The functional and managerial criticalities of the proposal for the creation of a GF can be detected in two different areas: the institutional network that is key to the success of the Fund (involving local institutions to share risk or counter-guarantee) and an appropriate selection of migrant entrepreneurs to minimize the instability/volatility of the Fund.

In other words this means that it is paramount for the Fund to profile potential users, whereas the protection and preservation of the Fund from insolvency risk necessarily passes through sharing the risk with migrants themselves.

This new GF should be flexible and adaptable to a different set of local finance, identifying different kinds of security depending on the size of the investment. It should also provide selection criteria according to the territoriality of the investment and extended (guarantee) for family activities, and according to a transnational perspective.

The financial dimension of the GF and its financial leverage can also be obtained with the help of other funds that have already been accredited, and provide for the inclusion or connection with projects of cooperation and development.

In this regard, because there are no competition issues with other funds, the attempt to connect the GF to other existing CGOs, such for example those available to IntEnt⁴, is a highly recommended option. In terms of optimal characteristics of the GF, it is also recommended that the financing will be matched with a mechanism designed to collect remittances/savings and in connection with mutual forms of credit.

Being a pilot action, at least at an initial stage, the transnational GF should select applicants following their nationality (i.e. Romanian citizenship), rather than following a criterion of territoriality (GF for Romania). However, if during the testing phase with returnees it is recommended to establish a fund dedicated to the citizens of Romania, at a later stage it may be extended to all those who want to invest in the country, regardless of their nationality.

⁴ Su.pa The Guarantee Fund *Modular approach and accession criteria*, Veneto Lavoro, 2011

2.2 The Development of the Guarantee Fund: actions and methodological aspects

The concrete possibility of the GF to support activities and paths aimed at the creation of and assistance to micro and small-sized enterprises with the support of cooperation projects (which would lead to a truly sustainable development of such enterprises) starts from a few basic elements that can be summarized as follows:

2.2.1 ex-ante (preliminary) actions

The identification of actual needs and requirements that the micro and small-sized business effectively and feasibly respond to. Simply put, identifying the existence of a genuine "market" where the company sells a product / service in demand that can be purchased by the targeted consumers, as a supply available to satisfy such needs and demand. A market research on the site to assess the real opportunities of a particular investment should be carried out to this purpose.

2.2.2 Actions in progress

The capability to involve local actors in the market where the micro and small-sized enterprise will operate. In particular, it will be the entrepreneur who liaises with the local financial system to obtain the necessary resources for the start-up.

The GF will provide its expertise and its support, but it is the company or the single entrepreneur who will have to demonstrate the feasibility of the business idea, validated by the market research, the development of a business plan and the provision of adequate collateral to activate the GF.

2.2.3 ex-post actions (follow up)

The ability to ensure continuity over time, thus avoiding to guarantee businesses with a possible initial success but lacking proper planning, organizational capacity and clear operational strategies to stay in the market. All actions / processes that deal with the follow-up of the initial phase. This means that everything needed in terms of technical and financial

assistance to gradually shift the focus from financial instruments for investment to those dedicated to the working capital financing and the expansion of the initial investment.

2.2.4 Types of actions and procedures

Consistently with the above-mentioned principles, the GF should define the specific elements that, without a field analysis, appear difficult to determine beforehand. In particular, the following recommendations are aimed at defining:

The types of micro and small sized enterprises that will be supported, with reference to minimum requirements of a patrimonial, economic, financial and organizational nature. Clearly, at this stage - since the GF should be protected by a collateral provided by the entrepreneur - some types of investment will be preferred over others: for example, a company that foresees the purchase of a certain quantity of capital and easy-to-sell goods will have more chances to obtain credit (and credit guarantees) compared to one investing in so-called "intangible" assets and therefore not really suitable to ensure collateral;

The type of business projects that the GF will support, with respect to the sectors, minimum and maximum duration, covered geographical area (market). To this purpose, it will be necessary for the GF to define a number of priority intervention areas . They may be, on one hand, some traditional sectors where the contribution of traditional knowledge is, in itself, an important qualification (such as in the construction services sector) and, on the other hand, more innovative sectors (such as green economy or jobs) pertaining to more advanced developmental goals of the Regional Operational Plans (ROPs) of the country;

The conditions to get access to dedicated funds and grants. The interest and availability of local banks are essential factors in order to operate in the local market. This is a rather technical phase of the GF set up;

The definition of procedures for the assessment and approval of projects, and monitoring and verification thereof. The responsibilities of would-be entrepreneurs are to be assessed so that the sustainability of their business project is ensured: entrepreneurs must demonstrate a sufficient knowledge of the market where they want to start the business, the economic viability of the project, local market conditions, a realistic and detailed business plan, etc..;

Procedures to initiate actions/countermeasures to overcome the potential difficulties that the different business projects are likely to encounter. In this case, technical assistance must be included as part of the business needs and the business plan must contain a SWOT analysis that clearly identifies potential threats to the success of the business. This allows to plan all the necessary countermeasures that need to be taken, should the threats become real.

Consistently with the above-mentioned recommendations, the following inputs should be taken into consideration:

- Rely on procedures for project proposal evaluation in shared and clear terms;
- Define guidelines to facilitate the initial selection without compromising the entrepreneurship potential of migrants;
- Present the proposal for the operations of the GF to the involved banks and get a feedback;
- Develop feasibility plans based on submitted business plans and establish a set of criteria to determine the expected default rate;
- Make a check up /evaluation of the first received cases;
- Limit the GF's scope to beneficiaries that provide sufficient collateral to protect the fund from the risk of default;
- Assess possible synergies with international cooperation projects;
- Use a cross-sector approach and involve different and relevant stakeholders in the scheme.

A realistic approach to determine the characteristics of the GF entails the initial management of the GF by a public (or public equivalent) body, establishing the possibility to broaden its scope with a gradual inclusion of private sector-driven interventions, including diaspora-led initiatives, individual or collective savings.

3. Business financing

3.1 Business start-up issues

Most entrepreneurs start their business relying on their own financial resources, technical knowledge and vision of business. During the start-up phase, they tend to rely on loans from relatives or friends, the support of other partners, credit from suppliers, while they seldom involve banks, especially when they cannot provide collateral. Some entrepreneurs may renegotiate mortgage-supported loans to get cash for the start-up of their business. However, these dynamics are difficult to quantify, at least from a statistical point of view.

Specific start-up programs of the past have shown that credit guarantees can be useful to stimulate entrepreneurship in a specific area. However, in general the amount of the required guarantees are very high (sometimes up to 100%) and credit conditions (interest on loans) are particularly burdensome. At any rate, if the start-up phase is successful, entrepreneurs generally feel motivated to increase their investment, in addition to maintaining sufficient liquidity to provide a sufficient flow of income.

Nevertheless, when one entrepreneur is applying for a bank loan, this does not mean that he/she necessarily meets all requirements. Normally, the GF comes into play in this phase, because this instrument has been specifically designed to help entrepreneurs gain access to lines of credit that are difficult to obtain in the early stages of business expansion. When the guarantee is aimed to finance start-up operations, in addition to difficulties in obtaining credit based on existing collateral, the assessment of the entrepreneur's historical track record – when available - also becomes an issue.

As part of its rationale, the GF should provide a time-limited support: the entrepreneur pays back the first loan and can apply for another one, in a virtuous cycle.

3.1.1 Start-up guarantee

When designing a sustainable model, a portfolio primarily developed to meet the needs of start-up operations will be subject to a higher level of risk and / or more exposed to

imbalances that may affect its overall sustainability. If the GF is committed to providing guarantees to start new undertakings to individuals who have never had experience in business activities, the focus must necessarily be shifted to the mechanisms of inclusion in the fund and guarantees, and to an increased attention to the owned goods. In general, this means to create an effective selection process in order to identify the business projects with the best potential. In this scenario, the GF will have to refer to other similar bodies/entities as co-guarantors and/or counter-guarantors in order to share risks and reduce its inevitable exposure rate. Therefore, when considering to issue guarantees for the start-up of new businesses, specific requirements must be taken into account for the modeling of a feasible GF that complies with principles of efficiency and effectiveness.

In brief they are:

- Straightforward evaluation of investment feasibility;
- Adequate level of collateral provided by the entrepreneur;
- Adequate interest rates and initial vacancy period (at least 6 months) before the first payment of the loan;
- Presence of co-guarantors or counter-guarantors (preferably public or semi-public bodies);
- Involvement of the diaspora and migrant associations as a vehicle of inclusion in the Fund and to channel remittances and savings for investment purposes.

3.1.2 Planning the development of the GF

In practical terms, the design process of the GF could be broken down into the following phases/components:

1. Establishment of the fund with public or semi-public, and / or with the diaspora financial resources (collective or individual savings/remittances);
2. Deposit of the fund in an Italian bank (preferably with a wide network of branches in Romania) and signature of an agreement for the test of the GF;
3. Definition and development of required skills and tasks to ensure the proper functioning of the GF (who does what);

4. Definition of a strategic plan for the development of the GF with a view to increasing the resources allocated to it, and the players involved in credit award (negotiations with potential partners should start immediately and be based on first-hand experience);
5. Definition of a business plan for the development of guarantee instruments and continuous monitoring of actual results compared to expected results (indicators).

It goes without saying that the GF should award its guarantee only to the business projects that receive a positive assessment, a “quality mark”, by the GF network. This means that a strong connection between the recipients of the credit, migrant associations, GF and CGOs, and the banking system needs to be created. Each of these stakeholders will have a specific interest in participating in the scheme, and the GF must ensure to meet each party’s expectations and interests.

3.1.3 Establishment of the GF

The establishment of the GF should start with a pilot action or a time-limited test phase to assess its usefulness. Thus, in the initial stage, limited funds will be made available: the actual creation of the GF can simply consist of depositing a decided amount in a dedicated bank account. This deposit will be available only in case of payment enforcement (seizure of goods), that is, when the GF management is liable because one or more entrepreneurs that have been awarded credit with the assistance of the GF cannot provide the loan repayments to the lending bank.

In the hypothesis of an initial limited amount available in the GF, it is expected that during the start-up phase:

- Only one bank is chosen to grant credit;
- The maximum amounts of credit/financing awarded do not exceed 25-30% of the initial value of the fund;
- The leverage remains at a fairly low level (it may be 1:3 or even lower).

3.2 Management of the test phase

The test phase involves a formal agreement with a bank or another credit provider. This agreement regulates the relationship between the manager of the GF and the credit institution. Importantly, regulations for the fund management and its design should be integral part of the agreement. Such regulations should define and clearly explain the criteria and procedures to:

Identify and select beneficiaries: target beneficiaries and types of operations that can be guaranteed are defined. In our case, it could be Romanian entrepreneurs from a specific area or industrial sector;

Identify eligible projects: the regulations should determine for what kind of operations one can request the services and credit guarantee of the GF: E.G, commercial credit (supply of raw materials, inventories, stockings etc...), or investments in technology (equipment, vans or transportation means, etc.). It may be appropriate to fund operations that provide easily tradable goods as collateral, in order to reduce the risk of exposure to insolvencies, especially by the GF;

Define procedures and tools in order to intake requests of access to the guarantee, and forward such requests to the bank. In this case, the institutional network will select and promote the best business projects and define the criteria for identifying them;

Creation of a selection and assessment committee: this is a particularly important body in the development of the guarantee tool, as it has the responsibility for deciding on the eligibility or ineligibility of the requests received by the GF. Such a committee is also crucial to ensure the good outcome of the process with regard to the identified lending bank. It is advisable that representatives of the bank participate in the committee, thus involving the bank early in the assessment of the credit requests;

Verification and monitoring of the management of GF: this is also an important activity that allows for the ongoing monitoring of the progress of the loans, their regular return in order to take appropriate measures in a timely manner, understand what difficulties may arise and how to manage them; in this respect, the important role of the partner institutions that carry out support activities directly or through the mobilized network is also highlighted;

Defining the criteria for payment enforcement of the GF: in general, this defines the number of unpaid installments that will trigger the insolvency and the conditions to declare the credit unrecoverable, after which the process of using the deposit as a guarantee is activated. In this procedure, it is recommended a minimum level of mediation with the entrepreneur who may be assisted and supported in re-negotiating the loan from the bank;

Definition of the technical features of the operations which can be guaranteed: type of transaction (mortgage, credit on current account, down-payment, etc..), minimum and maximum duration and amount, conditions (in particular, how to calculate interest rates), frequency of installments for repayment;

Definition of the coverage rate of the GF with regard to the single form of credit; during the test phase it is likely that the financial intermediary - especially if it is a bank – requests a 100% coverage, that is, that the agreements foresee that each credit awarded with the assistance of the GF is entirely covered by the guarantee. Such a percentage can be certainly reduced over time (up to 50%), according to the performance of the GF and awarded businesses during the test phase, which will allow to measure the degree of risk of the credit operations managed or to be managed;

Definition of the amount of credit line that can be awarded by creating a leverage of the GF. An indication of the multiplier is connected with the definition of the percentage of guarantees on individual positions (situations). In the test phase it is reasonable to start with a low leverage - 2 or 3 – and, following the results of the test, to increase the leverage on a consolidation phase of the GF. Obviously, in the presence of a high percentage of guarantees on individual credit transactions, the option will be a small leverage, therefore the multiplier will be minimal;

Definition of the assessment process for each application: "who does what" must be clearly outlined with respect to the assessment of each request for guarantee and credit award. This can be done by identifying effective but not overly-complex procedures. It may also be appropriate to give an indication on the timing of the process and identify who - structures and / or individuals - will be in charge of preliminary actions ie. the collection of documents, the pre-selection, and the preliminary analysis and evaluation of the applications;

Identification of structures and / or professionals who will provide the technical assistance, support and follow-up to the recipients: again, it is important to combine the management of credit guarantee with counseling activities offered by diverse actors not necessarily with expertise in the financial sector, such as migrant associations, specialized NGOs, etc., and who may add value to the entrepreneur’s personal and professional development.

It is useful to use the test phase to verify the applicability and feasibility of this working method, also in order to early identify appropriate improvements and to engage - with the utmost transparency and clarity - all involved parties in the operations and specific support actions.

It is worthwhile to recall and emphasize that the establishment and the operations of a guarantee tool is only a part of a broader process that brings together all the actions aiming to promote growth and development of enterprises and entrepreneurs. It is true that access to credit often becomes a determining factor in whether or not to start a business path, but it remains a tool that cannot – just by itself – give an answer to all the problems of the entrepreneur unless he/she proves to have all the different “assets” to run a business.

4 The model of the Guarantee Fund

4.1 Preliminary actions of the GF modelling

Two basic options can be taken into consideration, depending on the available resources and on the involvement degree of the stakeholders at local level. These options may be: financing start-up businesses of aspiring entrepreneurs in the process of returning to their country of origin (**Option A**); and financing and guarantee for return entrepreneurs already operating in the country of origin (**Option B**). Both options foresee interventions that follow some common rules as summarized below. The homogeneous, standardized and replicable system should ensure:

- Support to professionals /practitioners who will perform selection, preliminary analysis, and assistance to business start-up and development;
- Easier access to credit by establishing procedures with methods of analysis and evaluation shared by the local network and lending institutions;
- The creation and maintenance of a system of guarantees that allows for a significant extension of the results in terms of funding (and possibly disbursed micro-credit) by increasing the leverage ratio;
- Higher accessibility to benefits, grants, community or public resources allocated to support the development and financing of actions in a broad sense;
- More effectiveness in developing proposals that will help identify specific and acknowledged categories of credit/ loans for the design of the Fund's objectives and structure;
- Support of the socio-economic growth of marginal and rural areas and people at risk of poverty and exclusion through micro-credit tools;
- Socio-economic reintegration of people excluded or at the margins of the labour market;
- The creation of the conditions for overall regeneration of economically depressed areas;

- The promotion of local development strategies and support to supply chain projects;
- The protection of the identity of particular economic and cultural areas at risk of depopulation;
- The safeguard of peculiar elements of a territory based on its natural vocation and environment.

In short, the beneficiaries of the programs of the GF may be:

1. Small sized businesses and micro-enterprises in economically weak or depressed areas, active in agriculture, crafts, trade and services;
2. Small sized and micro-enterprises running operations with the use of secured capital goods;
3. Business projects aimed at specific economic categories (for example companies operating in the environmental / energy sector, tourist and hospitality sectors, and working in the social economy).

- **Option A: Start up of companies in the country of origin** Identification of some business projects of migrants returning to their country of origin (namely Romania): this option is an effective way to identify the business projects, the financial and entrepreneurial characteristics and needs. On the one hand this option requires a major effort in terms of business analysis and support, on the other hand it makes it possible to understand - while following through all the steps of the business start-up - the critical issues and needs that arise in the different phases of start-ups. For this option it is also necessary to identify one or more financial bodies willing to give financial support to business start-ups. The financial partners should also be willing to explore specific and tailored solutions to the needs emerging from the preliminary inquiry.

- **Option B: Starting a pilot project with small-sized or micro-enterprises with previous experience** This option aims at obtaining a detailed analysis of the needs of target companies and provides for the identification of some small sized or micro-enterprises (at least 3, max 10), to ascertain the financial needs and their nature (financing fluid assets rather than new investments). In this context a local financial partner (a bank in Romania) willing to be involved in pathways of credit award should be identified with the aim to assess how its services and products can be adapted to the needs identified by the involved companies. The duration of the testing phase could be 3 years depending on the circumstances. Clearly, the presence of returned migrants is fundamental.

In parallel with these paths, it is important to constantly update the in-depth analysis of the local context, gathering the necessary information, involving actors on the ground that can be sensitized on this issue. Continuing analysis and information are important to early identify the socio-economic trends of the area, and to adjust/adapt the development of business to the detected local trends or changes.

The methodology for being constantly updated on the local dynamics must necessarily include:

- Meetings with public authorities that regulate and control both the development of small sized and micro enterprises and the banking and financial sector;
- Meetings with the directors / heads of local banks, and possibly of Microfinance Institutions in Romania, to understand the functioning of organizations, areas where they operate, the target of financing, credit methodologies, the types of sources of financing received, etc.;
- Visits to local branches of the banks / microfinance institutions to request further information on their functions and their actual operations, on the local financial environment, the methodology used to deliver credit, the beneficiaries, etc..;

- Visits to entrepreneurs' organizations interested in the development of the local economy, interviews with staff on the offered services and the target beneficiaries of the services, etc..;
- Field visits and interviews, direct observation of the reality of local micro-enterprises, with particular attention to their financial needs;
- Collection of desk information to track the macroeconomic situation.

The good outcome of the creation of a GF in the countries of origin of migrants depends on the ability to initiate pathways that are strongly oriented to the territory, which actively involve local actors and that stem from the willingness of Local Authorities to create a favorable environment for the implementation of measures aimed at strengthening the economic and social development.

4.2 Migrant Banking

The so-called migrant banking activities are well suited to respond to changes in Italian society, which is increasingly becoming more multiethnic due to immigration. Banks and financial institutions are increasingly developing financial services dedicated to the new legal residents in the country.

In addition to increased remittances flows from Italy to other European and non-EU countries, banks are now focusing on attracting new customers by opening more traditional bank accounts, rather than capitalizing on transaction costs related to remittances and transfers.

Importantly, savings are as important as remittances, because they represent a value of the investment project of migrants. This aspect should be carefully monitored for the purposes of productive return and entrepreneurship.

4.2.1 Foreign entrepreneurs in Italy

Romania is among those communities with a strong presence of entrepreneurs in the total population of foreigners residing in Italy, with a 5.3% of the total foreign enterprises. The entrepreneurship degree shows that Italy is considered an ideal target for policies focused on

the international mobility of workers. It is realistic to assume that entrepreneurs who have been successfully running their own enterprises in Italy for a period of time may be those with a higher potential of success once they decide to return home and open their own firms there. The technical and operational know-how that many of these foreign entrepreneurs have accumulated during their stay in Italy is an important resource for the dissemination of new knowledge, once they return home to run activities identical or similar to those undertaken in Italy.

4.2.2 The needs of migrants and the financial offer

Regardless of the problems associated with different ethnic, cultural, individual and social factors, the needs of migrants can be broken down according to the migration phase that they are living. This approach constitutes a good basis for understanding the different financial needs related to the different stages of their migration project.⁵ The migration process can be divided into several stages, each of them representing specific financial products that banks can offer.

4.2.3 Trends and strategies in the mainstream banking system

The trends of Italian banks with regard to migrant banking activities highlight two main approaches, namely:

Universal approach: the migrant is no different from other targeted national customers and the services offered are based on the assumptions of the so-called "social bank", aimed to increase access to the banking system of those categories of customers belonging to the most vulnerable or marginalized groups. Banks that adopt this approach do not offer specific services for migrants, but ordinary services in order to simplify the bureaucratic process to include migrant customers in the system and offer them the most reliable products from a wider range of services.

Migrant-oriented approach: the banks that adopt this approach offer financial products to migrants with *ad hoc* service packages, specifically designed according to different standards

⁵ "Migranti istituzioni bancarie e nuove forme della cittadinanza", in L. Anderloni (a cura di) *Il social banking in Italia. Un fenomeno da esplorare*, Fondazione Giordano dell'Amore, Giuffr  Editore, Milano, 2005

such as ethnicity, the demands of family, etc. This group of banks is considered as one of the main targets for the present model. The services offered in this case, range from money transfer, the creation of transnational twin accounts, credit cards and debit cards among others. In addition to these products, other services are aimed at savings management, access to loans in the country of origin, and different kinds of insurance.

A list of the main types of migrant banking services includes⁶: Twin saving/checking accounts, Certificates of Deposit (in Italy), Products for accumulating savings (in Italy); Sharings of investment trust; Bonds; Mortgages; Personal Loans (in Italy); Consumer credit (in Italy); Microcredit (in Italy and the country of origin), Business Loans (in Italy and the country of origin), Investment funds, Life insurance, Health insurance, Insurance on remittances, services on Remittances and Rechargeable cards.

This list shows the wide range of possibilities to use specific financial instruments, however, new trends of the banks are evolving as a mix of the two approaches which are "universal" and "migrant-oriented" as mentioned above, in order not to discriminate against migrant customers, but consider them a specific target of tailored marketing strategies.

The most interesting activities in the field of migrant banking are built upon a two-fold approach and take into account two different time perspectives:

1. **Short-term vision:** match between supply and demand of new services in Italy aiming at the integration of immigrants into the banking system;
2. **Medium to long term vision:** focus on the mobility and transfer of migrants' savings, linked to specific cash flows that can improve the circulation of money according to a transnational perspective.

The actions aimed at the economic and social development in countries of origin of migrants as a main topic of the SME project fall into the second category: a medium-long term vision.

⁶ See report of SME for WP4: "Activity Report: Structuring innovative financial tools for migrants" by Veneto Banca - 2010

4.3 Initiatives in the field of remittances and their role in development

Remittances are often compared to other types of capital flows, as the flows of foreign direct investment or development aid. However, we must take into consideration the basic differences between different financial flows, namely that they are characterized by different functions and by the diverse economic and social effects that they aim at.

Remittances are mainly private and/or personal transfers and have not a commercial or public nature, since migrants are often engaged simultaneously in multiple jobs (they accept multiple tasks) and they tend to limit spending in the country of the destination in order to send money home. The channeling of remittances through formal mechanisms that are accessible and attractive to consumers increases financial transparency and promotes the inclusion of a target population largely “non- bankarized” within the financial system.

Remittances (and savings) represent a business opportunity, especially for those financial institutions that are capable of providing remittance- related services. In the framework of development, the main issue on remittances focuses on the ways to promote a healthy competition that creates better services especially for the most marginalized customers, especially those living in rural or under-developed areas.

This multifold approach to remittances is consistent with the IFAD project - SME and is particularly important because an exclusive focus on the reduction of transfer costs may lead to disregarding or downsizing a potential in terms of additional financial services that can be activated by remittances /savings and can be conducive to a long-term development which is precisely the theme of this report. At the same time, it is necessary to assess whether these approaches to remittances do not create market distortions, as it may happen if an initiative, funded by donors or subsidies, leads to the creation of unfair competition in the market.

A large number of international organizations, bilateral and multilateral donors and governments of developing countries that attract significant levels of remittances are considering how to promote remittances at lower costs, and how to channel these transfers of money to activities that are not limited to improving consumption but also have implications for productive and development-oriented activities.

4.4 The National Guarantee Fund in Romania

The National Guarantee Fund for Small and Medium sized Enterprises (FNGCIMM hereinafter) was established in December 2001, pursuant to Law 133/1999 to promote the development of small sized local businesses. Although in its mission the FNGCIMM does not foresee the provision of assistance and guarantees to micro entrepreneurs (and micro-credit), these categories are explicitly listed among the potential beneficiaries, and therefore may be beneficiaries of a possible experiment to be proposed to the Fund managers.

In essence, the FNGCIMM is addressed both to small sized and large companies, although the average size of the guarantees provided seems to be quite high (around € 75,000) and it addresses bigger companies than those targeted by the GF proposed in the framework of this project.

In operational terms, the FNGCIMM provides two basic types of guarantees, the first is called a "standard guarantee" and the second "plafond guarantee."

4.4.1 Standard Guarantee

The FNGCIMM warranty covers the risk of credit default by a percentage equal to 80% of the amount up to a figure of 2.5 million euro.

The types of loans that are guaranteed by the Fund include loans for medium and long term financing of capital goods, expansion of production capacity, purchase of equipment, machinery, buildings, etc. The Guarantee Fund covers short-term loans, such as credit lines for fluid assets, loans for the costs of trading, the financing of customer invoices, export credit, etc. Security is activated through some compulsory steps well described in the Fund's internet site (<http://www.fngcimm.ro>).

4.4.2 Plafond Guarantee

The so-called "plafond guarantee" sets a ceiling or maximum threshold to guarantees for loans granted to development projects and to finance the fluid assets of the company. The guarantee covers a maximum value of 700,000 lei (about 170,000 €), at an exchange rate established by the Romanian Central Bank and in force at the date of the guarantee issuance

The advantages of using the guarantee for SMEs can be: the elimination of the main causes of rejection of the credit demand (no guarantees) by using the GF in addition to applicants' collaterals; the reduction of uncertainty about issuance of credit / letter of guarantee; the reduction of additional costs of credit by eliminating the need to guarantee with real estate or similar collateral; the optimization in terms of flexibility of bank loans with regard to required collateral, without additional guarantees and time saving thanks to the use of mortgage loans.

Some critical remarks: the FNGCIMM is aimed at companies that already have a solid structure, that have been running operations for least two years and are considered creditworthy on the basis of identified collateral. In our case, and bearing in mind the two options identified above, the FNGCIMM expressly excludes the possibility of financing start-up companies (option A) while nothing seems to prevent it from financing small sized businesses or micro-businesses that already exist and have been established by return migrants (option B). It must be said that the condition of returnees has no relevance to the FNGCIMM as the only variable in this respect is the requirement of at least two statements of account (balances).

Basically, two proposals could be addressed by the SME - IFAD project-to the FNGCIMM assuming to carry out a pilot project:

- **Option A (company start-up)** the SME's GF could consider the provision of a counter-guarantee that protects the FNGCIMM (and therefore the Bank) against the risk of potential default.
- **Option B (return entrepreneurs with an existing business)** SMEs could propose a co-guarantee for a financial product, specifically designed for returnees with a satisfactory banking history, that might also allow to extend the warranty to businesses that have been running for less than two years (that is to say, with only one certificated balance).

The transnational GF should therefore work both as a **co-guarantor** and **counter-guarantor** according to the type of projects to be funded. It is also obvious that, in the case of option A (start-up), funds (and therefore the guarantee) will cover the acquisition of investment capital, while in option B (existing businesses) the funds will be addressed to fluid capital or up-scale /expansion projects.

4.5 The institutional network in Romania

A desk research, which needs to be integrated by field research in the future, had the specific purpose of highlighting the potential interest of institutions in taking part in the model to be designed. Amongst the most relevant:

National Agency for Employment (ANOFM hereinafter): is the Romanian institution that focuses on the possibilities of employment for the population residing in the country and abroad.

Obiettivo Lavoro (OL Romania) is the biggest Italian company for the management of human resources. OL operates in the management of migration flows and as a recruitment agency in countries such as Romania, where its presence is considered significant. The potential role of OL could be to become an actor of the GF and to channel a portion of the financial flows of migrants to the model and to banking institutions.

Ministry of Labour and Social Policy (MLSP hereinafter): The MLSP of Romania has shown that while migration maintains a relatively low unemployment rate and high remittances inflows (both phenomenon affected by the global economic crisis), the labor shortage in the market due to financial losses create strong wage pressures on businesses. The MLSP together with the Government of Romania has taken a series of initiatives to address the labor crisis and to encourage Romanians to stay in or return to the country.

Ministry for Small and Medium sized Enterprises and Cooperatives (MMIC hereinafter) as a governmental agency responsible for SMEs, the MMIC focuses its efforts on the promotion of an adequate regulatory framework, public policy, transport and financial support for SMEs. The Directorate General for SMEs, plays a key role on the actual implementation of the government program and determines the overall strategies to be adopted.

4.6 The model of the Guarantee Fund

The GF model works in two separate operating modes depending on whether it acts as co-guarantor or counter-guarantor of the corresponding Romanian Fund (the assumption is to involve the Romanian FNGCIMM). However, participation of a number of other players and stakeholders and qualified representatives of particular interests is paramount. They are partners of an institutional network consisting of public, semi-or quasi-public institutions, together with the diaspora of Romania, the migrant associations and other organizations such as Obiettivo Lavoro, NGOs, etc. Each player should participate in the test pursuing its interests, which are complementary and supplementary to those of other project players.

The GF will use the opportunity to serve as a counter-guarantor of FNGCIMM when it is deemed appropriate or, in a risk-sharing perspective, it will get the burden of the joint guarantee with the corresponding partner in Romania. Similarly, in order to make the test phase more appealing to financial institutions, a good idea is to involve (or at least to get the patronage) of the European Investment Fund.

Numerous actors can participate in the definition of the GF, its rules and procedures for selection and inclusion and they potentially include:

- Banks
- Would be Romanian entrepreneurs living abroad and Romanian return entrepreneurs
- Migrant associations and diasporas
- The FNGCIMM and other local funds (investment cooperatives, etc.).
- The National/Regional Management Authorities of the ERDF and other EU structural funds
- The European Investment Fund (EIF)
- Local Holding Funds such as JEREMIE
- Any other counter-guarantor or co-guarantor interested in participating in the model

The GF will be asked to enter into agreements with banks and to promote, through the institutional network, processes of bankarization of migrants and channeling of remittances / savings that can be used as additional resources to fund the GF.

According to statistics, the total amount of formal remittances sent by Romanians living in the Veneto Region amounted to over € 40 million in 2007. About 50% of remittances have been transferred through informal channels⁷. It is therefore apparent that migrants that are not yet bankarized represent a potential target for banks with figures of around 40 million Euros.

It may be easy to identify the specific interests of the above actors to be included in a mechanism of GF, however, the interest of banks in such a scheme may be less simple to understand. While banks may have an interest in achieving greater warranty coverage for the most hazardous operations (such as start-ups), they can also support a mechanism for migrants' bankarization, which can be an area of interest not just because of the increased level of official remittances, but also for the opportunity to provide private services to migrants (saving-related), as we have seen in the section on migrant banking. A great deal of attention should be given to the choice of the professional management of the Fund, which should be able to build a shared set of rules to assist the process of returnees from the initial stages to the granting of the guarantee and the follow-up to ensure the success of the business.

To summarize, the GF, together with migrant associations, will be the engine of the whole process by establishing relationships with:

- The banks in order to channel migrants in their migrant banking services
- The FNGCMM to share the guarantee risk
- The EIF or alternatively the JEREMIE program in order to share the risk
- Job Brokers as Obiettivo Lavoro, NGOs, regional development agencies (the RDAs) in order to create a network of services for migrants

⁷ Source: CeSPI

A viable scheme for the Option A (start-up) can be summarized in the figure below.

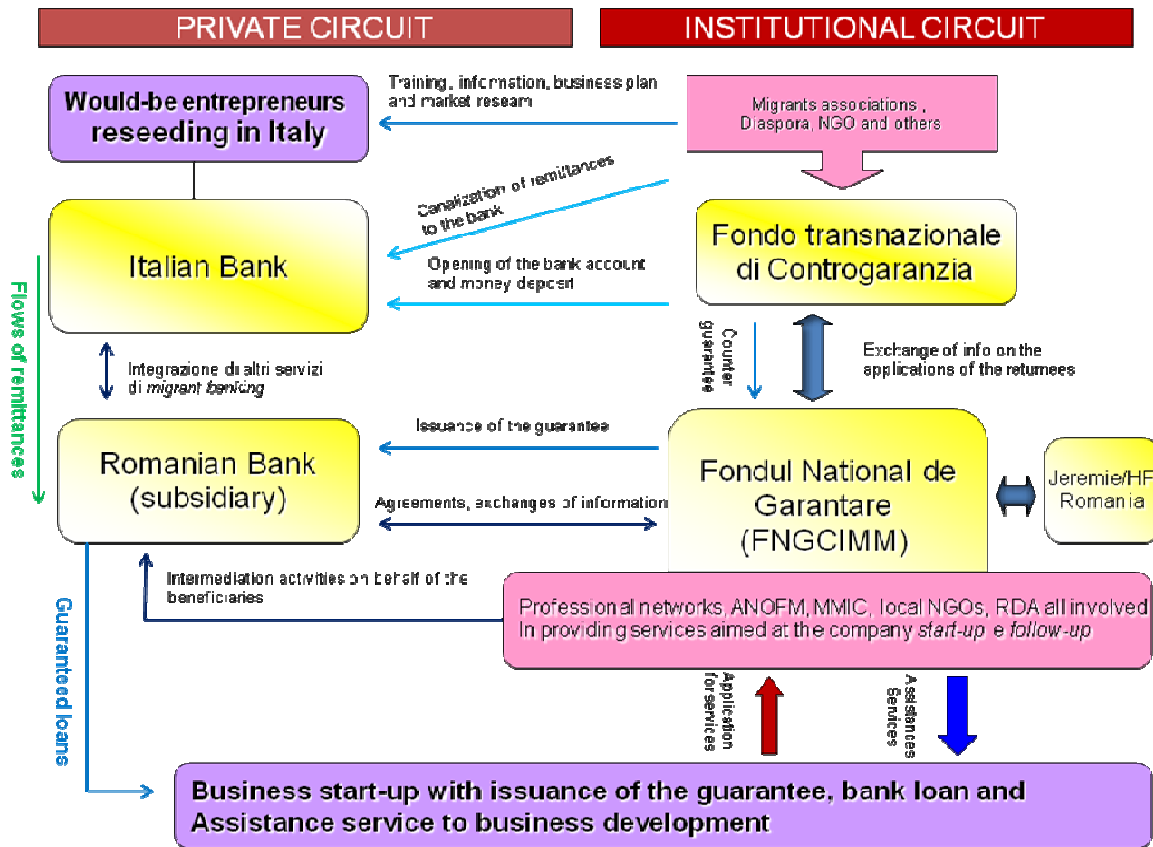


Figure 1 - The model for financing start-up business of return entrepreneurs The counter- guarantee role. Source: Elaboration by IFAD-SME

Would-be entrepreneurs submit a business idea to associations of migrants, diaspora, the Italian NGOs or other institutional bodies that interface with the GF. In turn, the entrepreneurs get a business plan and market research that are the basis for the evaluation for inclusion or exclusion in the mechanism of obtaining the guarantee. In the case of start-up, the selection criteria shall be very strict and aspiring entrepreneurs will likely have to provide personal collateral.

One of the objectives of institutional players such as associations, NGOs, etc... should also be to counsel entrepreneurs on managing their remittances/savings and using migrant banking services. In this way, a greater inclusion and increased use of formal banking channels for remittances may be ensured. Some financial products can be integrated according to single project's requirements, such as creating mechanisms to allocate part of remittances for investment rather than consumption. The banks will have to indicate what types of services

they intend to provide in accordance with the existing best practices.⁸ The choice of the partner bank should be made among those institutions that have offices or partner banks in Romania and can provide "twin services" or other services specifically dedicated to migrants.

The GF can open an account with the Italian branch of the partner bank, where it will deposit the amount of money needed for the testing phase, and will enter into a counter-guarantee agreement with the GF in Romania (FNGCIMM) so that - if the funded operation fails - the bank can refer to the FNGCIMM, which in turn will be reimbursed by the transnational GF. It is up to the GF managerial skills to negotiate fees and interest rates.

In this way, the FNGCIMM can extend the range of its operations, namely, to start-ups that are currently excluded from the scope of services (the recipients of the FNGCIMM guarantee must have two mandatory recorded budgets).

A network of professionals (the SME project has already started this process in the other ongoing activities) supported by public or semi-public bodies such as the RDAs, the ANOFM the MMIC, etc. should also be created for the purpose to minimize the risk of default and to support the development of the returnee's company in all its phases. The return entrepreneur must rely on the services provided by these organizations, so that his/her progress is monitored and payments of the loan are as regular as possible. An interesting option for the operations of this mechanism is represented by the possibility to activate the JEREMIE tool in Romania, which could in turn support a similar experiment and create a replicable model in other areas in Europe. To ensure smooth operations as those foreseen in the provided scheme, exchange of information between institutional and private actors needs to be made according to shared procedures and rules. This will allow for the selection of the best projects and thereby significantly reduce the level of risk involved with Option A (financing for start-up).

⁸ Cfr. 9.5 Leveraging remittances and enterprises development in "Molenaar Klaas, Enterprising migrant's in the driver's seat, IntEnt Foundation, 2009"

Option B can be as follows:

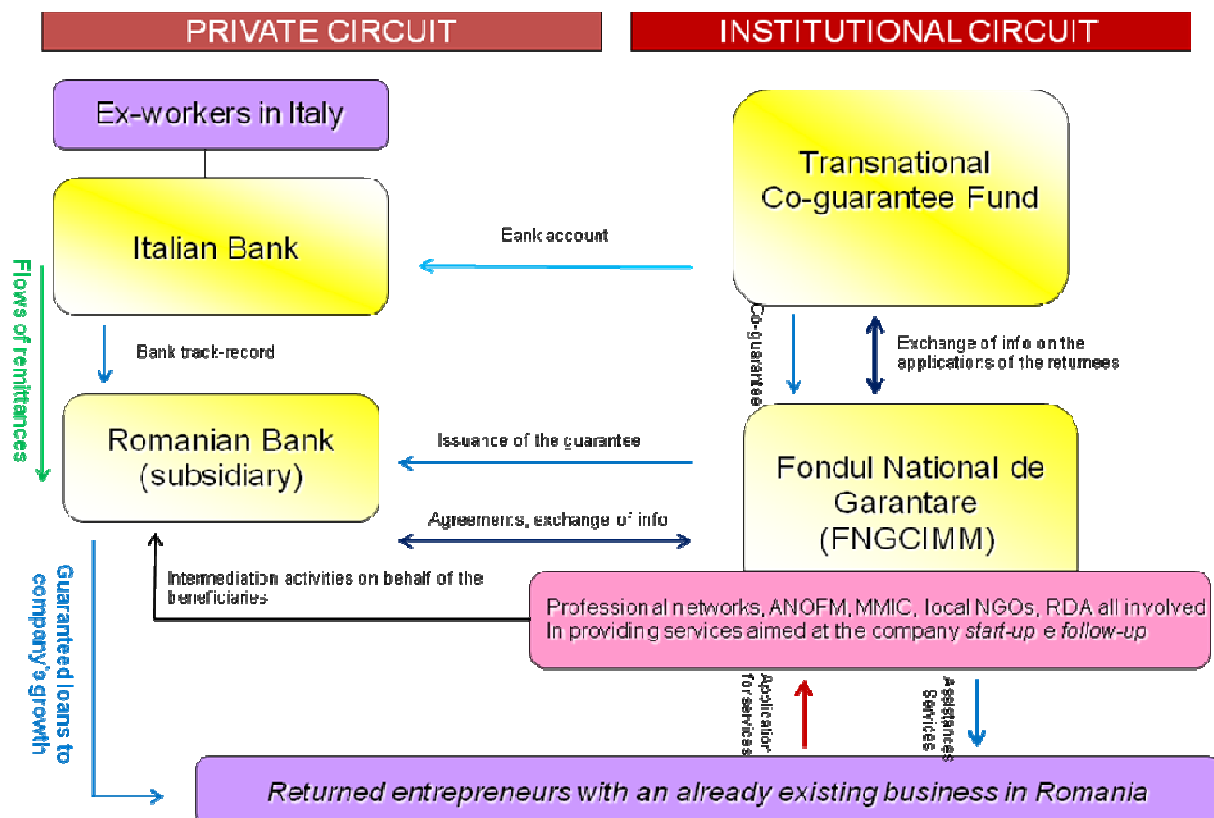


Figure 2 - The financing model for existing businesses of returnees The co-guarantee.
 Source: Elaboration by IFAD-SME

Figure 2 represents the model corresponding to Option B, or the possibility to provide guarantees and loans to return entrepreneurs when they have already started a business in the country. In this case, it is sufficient to provide a co-guarantee that may help to broaden the parameters to grant loans to existing businesses by spreading the risk taken by the FNGCIMM. In fact, in this case, the guarantee could be extended to return entrepreneurs who have consolidated budgets for only one year (instead of two, as required by the actual regulations of the FNGCIMM) or to activities that normally do not have all requirements to represent a collateral /security.

In this regard, the testing phase (pilot project) would represent an additional facilitating factor for those who have decided to leave the country of destination to return and do business in countries of origin. In this case, a Romanian formerly working in Italy could provide his/her banking track record over the period of stay in Italy to the Romanian bank, thus enhancing the possibility of financial credit lines based on his/her behavior. The mechanism is not very different from the one shown in Figure 2, with the FNGCIMM issuing

its guarantee (standard or plafond) to the bank as a result of a greater share of the risk achieved through the co-guarantee agreement with the transnational GF. It is important to rely on a network of serious professionals who can assess the feasibility of operations and to help the bank and the fund make decisions.

Finally, the testing phase will be pivotal for the actual viability of the model. During this phase it is likely that new contributions will be made, and the relationships between the Bank and the GF will become more established, so the parameters for the functioning of the model in both option A and B will become more explicit and effective.



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