The Poznan School of Banking
Research Journal
2015, Vol. 58, No. 1

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The involvement of banks and microfinance institutions in options of EU fund absorption between 2014-2020*

Abstract. *This article focuses on the problems of EU spending in the new perspective of 2014-2020, within the framework of the cohesion policy, and with regard to the Europe 2020 strategy. It is a strategy for smart, sustainable, and socio-economic development of favorable social inclusion and aligning development disparities. The article stresses that one of the essential elements in the whole process of the absorption of EU funds in the new perspective of funding is the involvement of financial institutions. Therefore, the main objective of the article was to identify areas and financial instruments, which are at the disposal of the financial institutions, such as banks and microfinance institutions, which are possible to use in order to improve the efficiency of absorption of EU funds in the years 2014-2020.*

Keywords: *European funds, financial institutions, new perspective 2014-2020*

Introduction

Smooth and effective application of financial funds designated for Poland within European Union program on years 2014-2020 requires coordination of many preparation initiatives and application actions, involvement of public and private institutions and accepting priorities and targets set in programs and types of investment activities.

* The project was financed by the National Science Centre granted pursuant to Decision No DEC-2013/09/B/HS4/03610.

Actions undertaken on country level should be coherent with requirements and objectives defined on European Union level. In perspective 2014-2020 usage of funds in frames of coherence policy began subordinated towards objectives achievements within strategy Europe 2020. It is the strategy of intelligent and balanced socio-economic development serving social inclusion and compensation of development disproportion.

One of fundamental element in whole realization of absorption EU funds in new perspective of EU financing is participation and involvement of possibly the largest number of institutions, businesses and people undertaking initiatives on development of Poland. Among theses institutions significant function and importance belongs to financial institutions. Most of them are banks and non-banking financial institutions that could and should play important role in absorption of EU funds on coming years.

The objective of this paper is to point out areas and financial instruments, being under disposal of financial institutions like banks and microfinance institutions, possible to be used in order to enhance effectiveness of absorption of EU funds in 2014-2020. Among the main areas of financial institutions involvement one could distinguish following:

– co-financing of infrastructural projects in terms of credit, loans and bonds issue,
– financial advisory and consulting,
– warranties and guarantees.

Every possibility of involvement area of financial institutions in absorption of EU funds requires individual analysis and risk calculation, which is, from the point of view of financial institution, the most important element of effective and result driven co-operation with beneficiaries of EU funds.

1. General characteristics of EU supportive programs in years 2014-2020

In years 2014-2020 around 94% of the whole EU budget, that is 955.7 billion EUR will be scheduled on realization of particular EU policies. For majority of EU countries membership contribution come back in forms of approved operational programs. Remaining 6% that is 61 billion EUR will be allocated on EU current cost that is administration costs, payroll, IT services. Approved budget on year 2014-2020 proves, that Poland will be one of the biggest beneficiary of EU funds and collect within seven coming years 106 billion EUR. Financial funds of EU will be allocated on scientific researches and its commercialization, key road connections, business development, green transportation (railway, public transport), digitalization of the country, social inclusion, vocational activation.

Table 1. Allocation of EU funds among regions in Poland in 2014-2020 (EFRR)

Regions/Voivodeship	Total allocation on RPO (current prices in EUR)
Lower Silesian	2 252 546 589
Kuyavian-Pomeranian	1 903 540 287
Lublin	2 230 958 174
Lubusz	906 929 693
Łódź	2 256 049 115
Lesser Poland	2 878 215 972
Masovian	2 089 840 138
Opole	944 967 792
Subcarpathian	2 114 243 760
Podlasie	1 213 595 877
Pomerania	1 864 811 698
Silesian	3 476 937 134
Świętokrzyskie	1 364 543 593
Warmian-Masurian	1 728 272 095
Greater Poland	2 450 206 417
West Pomerania	1 601 239 216
Total	31 276 897 550

Source: Programowanie perspektywy finansowej 2014-2020 – umowa partnerstwa [Programming the financial perspective 2014-2020 – The Partnership Agreement], Ministerstwo Rozwoju i Infrastruktury, Warszawa 2014, p. 165.

Additionally Poland can apply for 252 billion EUR for supporting unemployed youth. Apart Coherence Fund, there were financial funds scheduled on Common Agricultural Policy on 32.1 billion EUR. For comparison EU funds allocated for Poland in frames of direct payments and development of rural areas in year 2007-2013 were amounted to 28.6 billion EUR.[1] European Union approved for Poland significant part of funds allocated on supporting agriculture.

In financial perspective 2014-2020 within funds allocated for Poland, 60% of funds will be transferred on 6 country operational programs, including one inter-regional fund for regions of Eastern Poland. These are following programs:

- Infrastructure and environment – 115 billion PLN (27.4 bln EUR),
- Inteligent development – 36 billion PLN (8,6 bln EUR),
- Knowledge, Education, Development – 18 billion PLN (4,7 bln EUR),
- Digital Poland – 9.4 billion PLN (2 bln EUR),
- Eastern Poland – 8.8 billion PLN (2.2 bln EUR)
- Technical Support – 2.9 billion PLN (0.7 bln EUR),

[1] Council Regulation 1782/2003 and 73/2009; Funds on rural areas development – decision of European Commission on 27 of April 2010, 2010/236/EU.

– Regional Operational Program (RPO) – 31.3 billion EUR.

Due to entries in the Partnership Agreement there were 31 247 billion EUR allocated on Regional Operational Program in year 2014-2020, split into 22 571.6 billion EUR on EFRR (72,2%) and 8675.4 billion EUR (27,8%) on EFS. The biggest amounts of funds from both parts EFRR and EFS had been allocated on following regions:

– Silesian (3473.7 million EUR),
– Lesser Poland (2875.4 million EUR),
– Greater Poland (2447.9 million EUR),

From the other hand the least funds had been allocated to following regions: Lubusz (906.1 million EUR) and Opole (944.10 million EUR).

Apart funds from EU designated on regional operational programs, Regions can apply for financial funds coming from national programs. Moreover, European Commission additionally allocate app. 5% of EFRR funds on urban development of every member country. It will be no separated program on urban revitalization, so one can apply for financial funds on that activity from different approved programs.

2. Peculiarity of financing the infrastructural investment – financial assembly of investment ventures

Capital raising on certain investment is one of the essential challenges, appearing in front of the management board of the company. In order to make the correct choice it is necessary to consider various factors and make consolidated balancing. Currently financial market offers many possibilities of obtaining financial funds. One can consider bank credit or bonds issue. Investments, co-financed from European Union due to concept of regional specialization triggered by European Commission, are to stimulate the regional growth, originated from inside, resulted on funds concentration on selected priorities. General legal regulation, concerning instruments of financial engineering are enclosed in the decree 1083/2006. Only paragraph 44 describes the instruments of financial engineering. Legislation is quite well detailed in the regulation 1828/200623 in section 8, focused exclusively on instruments of financial engineering (Art. 43-46).[2] Current legislation regulates first of all:

– minimal scope of concluded agreement on financing (necessity of submitting investment strategy, rules of monitoring, policy of exiting from instrument of financial engineering and also rules of its potential liquidation),

[2] *Rola instrumentów inżynierii finansowej w zaspokajaniu potrzeb przedsiębiorstw w województwie podkarpackim,* PAG Uniconsult, Warszawa 2011, p. 41.

– maximal thresholds of management cost, that could be covered by funds handed over within operational program, according to funds type (from 2% in surety funds to 4% in microloan funds),

– financing principles in so called trust funds (ex. within initiative JEREMIE), offering different types of support,

– limitation of support by instruments of financial engineering exclusively for companies on their start up phase, early stage and development phase.

Peculiarity of conducting investment activity includes preparation of appropriate financial assembly. In a group of financial engineering instruments, special attention is focused on instruments, activated by external financing with debt character. That is the group of instruments, creating the surety funds and non-banking loan funds. First of these instruments acts indirectly, enabling access to existing surety sources, that is first of all credits, offered by banks and loans, offered by non-banking loan funds.

3. Role of banks and microfinance institutions in providing servicing of financial funds from EU programs

Banking sektor fulfil important role in financing EU programs (in 2007-2013 value of programs 200 billion PLN). Due to estimation, until year 2020 the role of banks in absorption EU funds will be enhanced by significant function of providing financial instruments having repayable character to beneficiaries. According to results of researches conducted in Poland almost half of financial agents, involved in process of co-financing of projects carried out with EU funds, are private owners of non-banking financial institutions.[3]

As far as distribution of instruments supporting credit quality is obvious source of benefis for agent, in case of surety instruments it is difficult to make an assumption that market players (in smaller range it concerns public players as well) work as non-profit, accepting on their own the risk, related to certain incorrectness. Assumption can be made that in case of loan instruments, they can generate profits in another way, for example by cross-selling or incentive system within initiative JEREMIE.[4] Agents can also expect similar solution already approved in SPO WKP after completion of Project, that funds will be used to increase capitals of these players, what would be significant encouragement into

[3] A. Alińska, M. Wajda, *Absorbcja funduszy strukturalnych przez niebankowe instytucje mikrofinansowe*, in: *Fundusze europejskie w polityce spójności*, red. A. Augustyn, H. Ostapowicz, Wyd. Uniwersytetu w Białymstoku, Białystok 2013, p. 174.

[4] P. Tamowicz, B. Lepczyński, M. Liszewska, *Inicjatywa JEREMIE w Polsce. Nowy mechanizm interwencji publicznej. Pierwsze doświadczenia z wdrażania Inicjatywy JEREMIE w województwie pomorskim i pozostałych regionach Polski*, Pomorskie Studia Regionalne, Gdańsk 2013, p. 95.

implementation of surety instruments. Important instrument of support seems to be guarantee or warranty. In practice, guarantees focus, first of all on stimulation of crediting actions of banking sector. This is due to the fact that bank credit still remain the predominant source of financing the economic needs.

Issues related to the financing of investment activity is particularly important in the case of evaluating the activities of loan and surety funds, providing its support in the areas where there is limited ability to use any other external financing sources and applied security of the credit. For these financial institutions unacceptable barrier may prove to be a difficulty in estimating the risk associated with the activities of business entities present on the market as the beneficiaries of EU aid.

According to the research results in the field, the value of guarantees for circulatory loans/credits in the portfolio of guarantee funds in Poland, in volume and value terms is running at the level of 70-80%.[5]

Initial delays in implementation might have been rooted then in problems arising from qualification of circulatory loans/credits. It does not however concern only the past situation as potential exclusion of part of circulatory guarantees with qualification of expenditure at projects clearing stage may bring serious consequences for the stability and expansions of guarantee funds.

In case of active guarantees it would become necessary to move them to own funds account line. Despite relatively small scale of guarantee initiative (ca 1 billion PLN) is not in the position to destabilize banking system, it is important to underline weaknesses of this system, which was used by more than 10^{th} business entities until year end 2013 (only thanks to RPO funds). Future increase of utilization of financial instruments, will analogically bring, as in previous years, the increase of resources being managed by funds. Absence of security norms, risk diversification or funds management supervision requires the implementation of changes, which will secure the stability of this unregulated sector in Poland.[6] The assumption that lack of need for funds supervision results from relatively small share of this sector's assets in all financial sector assets seems to be the wrong standpoint. Dynamic assets increase over recent years and large amount of businesses using them, as well as plans for further increase of guarantee and loan fund capitalization in 2014-2020 perspective, justify implementation of appropriate regulations securing the stability of this system. However, the analysis of guarantee funds system in Poland indicates weaknesses of current system in Poland: fragmented capital, lack of re-guarantees system, lack of adjustment of funds' offer to specifics of banks' activity (each fund offers different terms, banks are

[5] *Analiza stanu rynku funduszy poręczeń kredytowych w Polsce. Ocena i perspektywy rozwoju*, PAG Uniconsult, Związek Banków Polskich, Warszawa 2014, p. 68.

[6] Recent rating of Polish guarantee funds cannot be synonymous with fulfillment of this requirement, because of the necessity to focus on the risk generated as the result of EU funds implementation.

forced into individual evaluation of each case and are not in the position to offer the credit with fund guarantee as the standard banking product).

It results in low demand for funds guarantees, smaller access to financing for small and medium enterprises, lower effectiveness of public funds involved in comparison with other EU countries.[7] The consequence of this specific market situation is the necessity to analyze the role of guarantee funds in wider context, which involves at least three basic factors:

– first, real interest presented by financial institutions in making debt financing available (readiness to offer debt products),

– second, debt financing access conditions, which can present positive or negative factor to use this source of financing,

– third, susceptibility of entrepreneurs to fulfill their financial needs based on debt financing.[8]

The issue of under-control or over-control of the market related to EU funds distribution and the definition of financial institutions role as intermediaries and advisors in effective distribution of EU funds becomes ever so important, especially when the analysis of financing sources used by medium/small enterprises and households is done. It is estimated that the portfolio of lending companies amounts to appx. 4 billion PLN. In banking sector, consumer credits sum up to 150 billion PLN, and with mortgages included, it exceeds 500 billion PLN. Comparison of these numbers gives a fraction, but taking into account only low value credits, which are below 4 thousand PLN, it amounts to 30-40% of banks portfolio – and that is not a margin any more.[9]

Another important factor that needs focused attention when evaluating EU funds implementation efficacy in next funding stage (2014-2020) is the perspective of the value of costs, fees, commissions etc. In line with Art. 78 point d European Council (WE) Regulation nr 108/2006, dated: July 11, 2006, setting general regulations regarding European Fund for Regional Development and Cohesion Fund and repealing European Council (WE) Regulation nr 1260/1999, resources from European Fund for Regional Development can cover qualified expenditure for management or management fees.[10] This regulation is being detailed in Art. 43, EU Council Regulation nr 1828/2006, dated: December 8, 2006, setting detailed acceptable means of compliance of EU Council Regulation nr 1083/2006 setting general regulations regarding European Fund for Regional Development, European Social Fund and Cohesion Fund and European Parliament and Council

[7] *Analiza stanu rynku...*

[8] *Rola instrumentów inżynierii finansowej...*, p. 41.

[9] G. Krekora, Blog Alebank: www.alebank.pl/index.php?option=com_content&view=article&id=48490:jablko-nie-gruszka-kredyt-nie-pozyczka&catid=709&Itemid=196 [20.12.2014].

[10] Due to the limited application of management fee in Poland, it will be analyzed only the case of the cost refund for management.

Regulation nr 1080/2006 regarding European Regional Fund, which states that: management costs cannot exceed, yearly average, during the term of funding program, the below stated limits, unless, the bid conducted proves the necessity to increase these limits, according to current rules:

– 2% of the capital provided by the fund program to trust fund or capital provided by fund program or trust fund to guarantee funds;

– 3% of capital provided by the fund program or trust fund to financial engineering instrument in all remaining cases, excluding micro crediting instruments designated for micro enterprises;

– 4% of capital provided by the fund program or trust fund to micro crediting instruments designated for micro enterprises.

Issues relating to the value of fees are especially important from the point of view of EU funds beneficiaries. It is important that these values do not significantly exceed the level of financial investment especially those by financial institutions. IT is to remember that EU funding is aimed at serving beneficiaries and not to multiply financial intermediaries' profits.

Another form of support of financial institutions in EU funds implementation, are guarantees and warranties. It is an example of financial product offered by banks as well as non-banking financial institutions. Popularity of this product results first of all from the intention to decrease risk exposure by banks and micro financing institutions. It constitutes one of basic forms of warranty, eagerly used by consumer clients as well as by micro, small and medium entrepreneurs, who contrary to big corporate clients do not provide appropriate financial indices, confirming their creditworthiness. These instruments constitute the group of products aimed at improvement of credit quality. Because of ease of funds leveraging, this instrument was also used to distribute European funds in 2007-2013 perspective. It was used to pass the capital into management (most often by warranty funds) with aim to provide individual warranties as well as guarantees for guarantee funds and in the form of portfolio guarantees implemented among others by banks.[11]

In case of guarantee funds the indicator of value of active guarantees in relation to capital owned amounted to only 125% in 2013, while in most European countries it is many times higher.

– according to experts, such a situation is the result of three factors, namely,

– absence of instruments forcing guarantee funds to undertake higher risk (in most cases, unfortunately mechanisms the role of which would be to allocate new public funds in those guarantee funds which enjoyed the highest capital usage),

– constant inflow of public funds as the result of subsequent EU programs and resulting from this – constant increase of denominator of the fraction, describ-

[11] M. Wajda, *Analiza wdrażania instrumentów wsparcia jakości kredytowej współfinansowanych ze środków europejskich w latach 2007-2013 na podstawie udzielonej pomocy de minimis*, UwB Optimum, Białystok 2014 (in print).

ing the level of engagement of fund's capital and finally fragmentation of guarantee funds sector and its limited attractiveness to banking sector,

– absence of effective re-warranty mechanisms.

In line with adopted assumption in the area of 2014-2010 planning, there will be an increase of usage of returnable instruments, including guarantee instruments. Aimed value of warranty-guarantee portfolio in the next planning period may exceed even 10 billion PLN. It is necessary then to undertake the effectiveness analysis of used guarantee instruments co-financed by European funds, especially in the new distribution phase 2014-2020. Based on the data regarding *de minimis* aid provided as part of guarantee systems worth noting, inter alia, to analysis on the speed of the implementation and benefits for SME under the extended warranty. The results obtained research shows that it is worthwhile to develop this form of support for the development of entrepreneurship.

It is important to also remember that in 2015 will be the end of government *de minimis* program by Bank Gospodarstwa Krajowego. From the perspective of evaluation of public finance condition and country budget conditions, it is clear that EU funds are the only significant source of financing of the development of new warranty-guarantee system.

Conclusions

Analysis of issues presented in this article illustrates that the system of financial institutions, especially the system of loan - guarantee in Poland was developed when the scale of demand for such external financing sources was limited. However the development of this group of entities and ever increasing demand for this kind of services and products and first of all and inflow of structural funding shows that present solutions might not be sufficient.

It is proved if only by the indicator of average value of funding per one financial intermediary (model without the manager of trust fund) which amounted to ca 15 million PLN.[12]

Additionally the change of system architecture has to include significant increase of loan and guarantee funds capitalization and resulting necessity to implement control regulations and risk management norms, which will assure the stability to its important from the point of view of SME sector.[13] It is necessary then to implement series of institutional and legal changes, new subjects coming

[12] The average size of a financial intermediary funding for implementing the financial instruments without a trust fund manager.

[13] By the end of 2013. financial instruments supported 27 thousand companies. See: Wdrażanie Regionalnych Programów Operacyjnych, 31.01.2014, www.funduszeeuropejskie.gov.pl/Analizy-RaportyPodsumowania/poziom/Strony/RPO_stan_wdrazania_310114.aspx [14.07.2014].

to stage and setting development supporting objectives before the new phase of EU funds distribution in order to secure not only appropriate speed of funds usage but also to improve effectiveness of their usage. It seems that at present, the most significant challenge in front of financial institutions is to actively join and work for the improvement of usage of available EU financial funds.

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Ocena ex ante ryzyka dla gwarancji w ramach finansowania ze środków UE na lata 2014-2020 przedsięwzięć w zakresie realizacji celów tematycznych: wzrost konkurencyjności sektora MŚP oraz wzmacnianie badań naukowych, rozwoju technologicznego i innowacji w przedsiębiorstwach", PAG Uniconsult, Warszawa 2014.

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Możliwości absorpcji funduszy UE w latach 2014-2020 z perspektywy zaangażowania banków i instytucji mikrofinansowych

Streszczenie. *Artykuł koncentruje się na problemach wydatkowania środków UE w nowej perspektywie 2014-2020 w ramach polityki spójności z uwzględnieniem strategii Europa 2020. Jest to strategia na rzecz inteligentnego i zrównoważonego rozwoju społeczno-gospodarczego, sprzyjająca inkluzji społecznej i wyrównywaniu dysproporcji rozwojowych. Jednym z zasadniczych elementów realizacji procesu absorpcji środków UE w nowej perspektywie finansowania UE jest udział i zaangażowanie instytucji finansowych. Dlatego też wskazano obszary i instrumenty finansowe, będące w dyspozycji instytucji finansowych, jakimi są banki i instytucje mikrofinansowe, możliwe do wykorzystania w celu poprawy efektywności absorpcji środków funduszy UE w latach 2014-2020.*

Słowa kluczowe: *fundusze europejskie, instytucje finansowe, nowa perspektywa 2014-2020*