

# POSITION PAPER



ESBG's views on the European Commission  
Communication: "*A European initiative for the  
development of micro-credit in support of growth and  
employment*"

14 February 2008





## Introduction

As the representative of one of the largest networks of microfinance providers in Europe, with members in 26 European countries, active in this field, sometimes for more than a century<sup>1</sup>, the ESBG has with great interest followed to the EU debate regarding the development of microcredit in Europe. This ESBG document provides comments on the recent EC Communication “*A European initiative for the development of micro-credit in support of growth and employment*”<sup>2</sup>. It first provides general views on the ESBG position, followed by comments on some specific issues addressed in the Communication. The ESBG would also like to express its willingness to further contribute to the initiatives of the Commission in this field and to the work of the envisaged central body including to monitor and coordinate action in support of microcredit in Europe.

### 1. ESBG’s general approach towards microcredit

- The ESBG embraces and would like to call for a more **comprehensive approach towards microcredit**. It is important to acknowledge that there is a wide-ranging variety of institutions offering microcredit in Europe, all with diverse aims and targets, but all actively contributing to reach a higher level of financial inclusion in Europe, whether they are banks, non-banks or other types of institutions. In this respect, the development of a clear definition of Microfinance Institution (MFI) would be necessary, to clarify the scope of the planned EU actions.
- The ESBG acknowledges that the Commission’s initiative is part of the EU measures aimed at the achievement of the goals of the Lisbon agenda. As such, the Communication focuses on microcredit serving entrepreneurs and micro-businesses with limited access to conventional banking channels. The ESBG however perceives a potential lack of coherence between the initiatives at EU level as regards the target groups for the support envisaged (start-ups or small enterprises vs. financial excluded entities and individuals). In this context, the ESBG would recommend that an integrated approach should be more clearly communicated and developed, incorporating and facilitating microcredit schemes aiming at **supporting both small businesses and socially and financially excluded individuals with the aim of self-employment**.
- Against this background, and in order to reap the full benefits of microcredit in the form of growth and job creation, the policy measures in favour of microcredit, developed at EU or national level, should be targeted at all intermediaries providing micro-credit. This would particularly be required to ensure that:
  - all microcredit services initiatives throughout the EU, whatever the status or the legal structure of the provider involved are able to develop optimally, and with a view to optimise the advantages brought to the beneficiaries. In this regard, specific attention will need to be given to the scope and focus of follow-up actions or recommendations eventually launched

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<sup>1</sup> For more information on microcredit initiatives within ESBG member institutions, see:  
[http://www.esbg.eu/uploadedFiles/Publications\\_and\\_Research\\_\(ESBG\\_only\)/brochure%20screen%20view.pdf](http://www.esbg.eu/uploadedFiles/Publications_and_Research_(ESBG_only)/brochure%20screen%20view.pdf)

<sup>2</sup> [http://eur-lex.europa.eu/LexUriServ/site/en/com/2007/com2007\\_0708en01.pdf](http://eur-lex.europa.eu/LexUriServ/site/en/com/2007/com2007_0708en01.pdf)



- by the Commission and/or the Member States. In any case, **all interested actors**, including savings and socially committed retail banks, should be part of the preparatory reflections and discussions especially on the Code of conduct that the Commission could decide to develop;
- the central body envisaged by the Commission to monitor and coordinate action in support of microcredit gets a **comprehensive overview and covers all initiatives** developed in this field, **irrespective of the supporting institution**. This will be all the more important for promoting the exchange of best practices, especially between banks and non banks, as suggested by the Commission.
  - Tradition and longstanding **experience** of the local market is crucial for evaluating the viability of a business concept whatever its scope and size, and including small-scale projects. The ESBG Members welcome, and are open to cooperate with other micro-finance providers in this context, by contributing to the development of microcredit not only through their expertise in banking but also with their thorough knowledge of their local markets.
  - Given this local dimension of microcredit, ESBG believes that the EU focus should primarily be on **facilitating microcredit at national, regional or local level**, before looking at the creation of a single market for microcredit per se.
  - We welcome that the Commission acknowledges that **accompaniment and follow-up of micro-borrowers** is crucial for the development of microcredit in Europe. Savings banks across Europe have operated in this spirit at local level for more than a century and used microcredit as a means to help entrepreneurs to integrate, or re-integrate, into social and economic life. In this context, **the use of the term “non-bankable”** seems inappropriate, as it reflects a vision of irrevocable exclusion of citizens from the formal financial system, whereas microcredit has to be read as one of the solutions offered to individuals or entrepreneurs in need to access or re-incorporate conventional banking channels.

## **2. Specific comments on matters addressed in the Communication:**

The Communication proposes to **improve the legal and institutional environment for microcredit in the Member States**. It concretely encourages Member States to (cf. page 5 and s. of the Communication):

- Establish a wider provision of **loan guarantees** and, as portfolios develop, the **securitisation** of microcredit portfolios.

The ESBG would recommend an analysis of the feasibility of any measures in favour of securitization of microcredits before proceeding in this direction. The 5<sup>th</sup> Commission Roundtable between Banks and SMEs addressed the issue of securitization of SME loans. The examples presented in that report show that successful securitization of SME loans in many cases depends on public financial support.<sup>3</sup> Moreover, securitization of loan portfolios require an effort with certain fixed costs for structuring the portfolio, which is based on component loans with an accepted rating. Microcredits are normally provided without a formal rating (sometimes with a “scoring”). The requirement of a rating for these credits would entail a heavy

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<sup>3</sup> [http://ec.europa.eu/enterprise/entrepreneurship/financing/docs/roundtable\\_securing\\_2007.pdf](http://ec.europa.eu/enterprise/entrepreneurship/financing/docs/roundtable_securing_2007.pdf)



increase the transaction costs, which as a result could make microcredits more expensive and thus less attractive.

When approaching the issue in relation to microcredits, which are by nature even smaller and at least as heterogeneous as SME loans in general, there may be reason for caution in the promotion of creating Asset Backed Securities.

- Help microcredit become sustainable by **relaxing interest caps** for microcredit operations

The ESBG acknowledges the idea of the Commission to envisage relaxing interest rate caps for microcredit as this might in some cases prove beneficial for the expansion of the provision of microcredit. As microcredit activity involves high risk, small amounts for each credit and high administrative costs, we would generally be in favour of any measures aimed at reducing the costs for the providers in order to expand the outreach and give opportunities to new market entrants. Although microcredit practices in some developing countries have benefited greatly from a relaxation of interest rate caps, the ESBG believes that our European credit culture may call for a different approach. Looking forward, a careful approach must be taken when “translating” microcredit practices which have proven successful in the developing world, into a European context. We would therefore call for an in-depth assessment of the impacts of such measures, before taking any clear steps in this direction. Issues such as “predatory lending” and risks of “overindebtedness” should also be considered in this framework.

- Allow Microfinance institutions (MFIs) **access to borrower databases** and facilitate their **evaluation of the risks**

The ESBG is strongly supportive of the approach to exchange best practises at European level as it would help providers to get a better picture of the profile of micro borrowers. As regards scoring and exchange of data, the ESBG wishes to stress that a quantitative approach is not the only way to assess reimbursement, as microlending has proven to be based on confidence and on a global approach towards the situation of the borrower, rather than statistics.

In addition, the ESBG believes that such a database may prove unrealistic particularly considering the varying structure in place in the different European countries which would need to be streamlined, and that the efforts of gathering the data may not outweigh the benefits it could bring. It would also be important to assess the technical aspects of such a database, particularly if it is expected to interact with databases at national level.

- Reduce MFIs operating costs applying favourable **tax schemes**

The ESBG, as mentioned in its general remarks, would generally advocate against any favourable treatment for certain providers per se. This also applies to investments in microcredit activities, which would have to apply to all activities in this field, regardless of the intermediary institution. Such an approach would not only create distortion but might also impede operations in the field of microcredit among those actors that do not benefit from the advantages. Particularly the microborrowers would be disadvantaged if providers with the greatest operational skills or the greatest capacity to mobilise financial resources would withdraw from this area of credit.

- Incorporate microcredit into **regulation and accounting standards**



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The ESBG considers that a careful cost/benefit analysis of any legislative proposal, such as including microcredit in accounting standards, in order to avoid any unnecessary administrative burden, which would prevent rather than support the development of microcredit. Regulation needs to give flexibility to the development of microcredit in Europe.



## About ESBG (European Savings Banks Group)

ESBG (European Savings Banks Group) is an international banking association that represents one of the largest European retail banking networks, comprising about one third of the retail banking market in Europe, with total assets of € 5215 billion (1 January 2006). It represents the interest of its members vis-à-vis the EU Institutions and generates, facilitates and manages high quality cross-border banking projects.

ESBG Members are typically savings and *retail* banks or associations thereof. They are often organised in decentralised networks and offer their services throughout their *region*. ESBG Member banks have reinvested *responsibly* in their region for many decades and are one distinct benchmark for corporate social responsibility activities throughout Europe and the world.



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