



PROGRAM
REGIONALNY
NARODOWA STRATEGIA SPÓJNOŚCI



Pomorze
Zachodnie

UNIA EUROPEJSKA
EUROPEJSKI FUNDUSZ
ROZWOJU REGIONALNEGO



Ex-ante assessment methodology for financial instruments in the West-Pomeranian Voivodeship in the 2014-2020 programming period

SUMMARY

imapp

PAG  Uniconsult

Warszawa, December 2014

The evaluation is financed by the European Union with European Regional Development Fund under Regional Operational Programme Zachodniopomorskie Voivodeship for years 2007-2013

The project "Ex-ante assessment methodology for financial instruments in the West-Pomeranian Voivodeship in the 2014-2020 programming period" was implemented from February to December 2014 and two reports concerning different aspects of financial instruments planned under the Regional Operational Programme were created within the framework of the project.

Following the theory of economics and specialised literature, the analysis is commenced with the indication that the public intervention using financial instruments may take place in case of market projects (profitable), with respect to which the difference between a level of funding optimal in view of policy objectives and an actual level currently observed occurs. The reasons for discrepancies between potential and actual investments may be different, however, in principle, the most important reason is limited access to debt financing of economically justified projects due to the failure of the financial market as well as too low profitability (relatively very long period of return) of the projects. The public intervention using financial instruments should be aimed at eliminating the financing gap (providing better access to finance) or creating incentives for undertaking certain actions (improving conditions of making funding available). These two measures may, yet do not have to occur together, and for each proposed intervention area, it is crucial to answer the question about the effects of introducing financial instruments, i.e. to what extent the objective of the intervention is to make debt financing more accessible and to what extent is to reduce its price.

The West-Pomeranian voivodeship has broad experience in implementing financial engineering instruments and a large network of strong financial intermediaries, partially running business outside their regions. In the field of supporting debt and guarantee financial instruments, the key role in the past few years was the support under the so-called JEREMIE initiative implemented by Bank Gospodarstwa Krajowego, which acted as the Manager of the West-Pomeranian JEREMIE Holding Fund. PLN 280 million were allocated for the project. BGK in collaboration with the Managing Authority was responsible for the selection of the financial intermediates (e.g. banks, loan or holding funds), which receive support from the JEREMIE Holding Fund and on the basis thereof provide financial support to companies on preferential terms (loans, credits and guarantees). The projects implemented by the financial intermediaries under the JEREMIE initiative allowed to grant by the end of March 2014 1,840 loans and credits to West-Pomeranian SMEs of the total value of PLN 199 million. The value of 1,859 granted guarantees is PLN 171 million - which allowed entrepreneurs to obtain financing in the amount of PLN 323 million. Among the entrepreneurs who received support under the JEREMIE initiative, as much as 86% were micro-enterprises (which constituted nearly 100% in a group of those that signed the Loan Portfolio Guarantee) and every fifth company involved in JEREMIE at the time of signing a loan/credit or guarantee agreement operated on the market for a period shorter than 24 months (as much as 36% of the companies were those that benefited from the Loan Portfolio Guarantee).

The so-called JESSICA initiative was also implemented in the West-Pomeranian voivodeship, which supports urban regeneration. The JESSICA Holding Fund of PLN 148,7 million was established on 30 July 2009, whereas the support was channelled through two Urban Development Funds (UDF): BZ WBK SA - UDF for the Szczecin's Metropolitan Area (SMA) and BOŚ SA – UDF for the areas outside the

Szczecin's Metropolitan Area (SMA). The value of agreements signed by the two urban funds with the final recipients is PLN 147 million, therefore 101% of the funds entrusted to the UDF. All agreements were signed by the end of 2013.

Additionally, the lending support project for persons setting up businesses (financed under measure 6.2 OP HC) was also implemented. The research on the project's beneficiaries shows relatively high efficiency of support (more than half of the subjects declared that they would not start business without any loan granted under the project), however, the supported persons are over-represented by those with a university degree aged below 50.

As far as equity instruments are concerned, only one investment incubator is located within the area of the voivodeship, financed under Measure 3.1 IE OP, i.e. Pomeranus Seed capital fund - operating as of 2009 within the structures of the Polish Entrepreneurs Foundation (PFP) in Szczecin.

The above-mentioned activities, even though significant, did not eliminate the problems of companies with the availability of funds. Thanks to the analyses performed, the financing gap in micro, small and medium enterprises was estimated. It was nearly PLN 2,4 milliard according to the measure of unallocated funds (i.e. loans and credits, for which the West-Pomeranian companies applied, but did not receive in 2013) and almost four times as much if the companies' own assessment of unsatisfied investments is to be taken into account. It is also worth mentioning that the financing gap more in terms of the number of enterprises rather than in terms of its value concentrates among micro-enterprises and individually refers to insignificant amounts. Additionally, it must be stressed that the research was conducted in the circumstances of availability of financial instruments under JEREMI as well as other national instruments, in particular BGK de minimis guarantees - in case of lack thereof, the unsatisfied needs would probably be even higher. As part of the research, the guarantee risk was also assessed. In case of standard guarantees to be granted under the regional operational programmes, the risk was assessed at 25% and in case of guarantee products for start-up enterprises it would be 35%.

Within the framework of particular investment priorities, we suggest considering the application of the following instruments - however, it must be noted that the basic scope of the analysis concerned financial instruments only, but in the second report it was supplemented with some considerations on the application of the so-called mixed instruments (new type of instruments offered by structural funds, combining non-refundable financing and financial instruments, also offered by EU funds; the examples thereof are the subsidies for the capital entry or for guarantee commissions). Additionally, the report also contained the analysed possibility and grounds for applying the non-refundable instruments related to commercially oriented reimbursable financing, such as the subsidisation of the interest on commercial credits or subsidies for the payment of the principal value of the commercial credit.

Under investment priority 1b¹ (1.2)² we propose capital entries at the early (seed) stage of development of an enterprise in the amounts from PLN 200,000 up to PLN 2 million, we propose that

¹ To avoid any doubt, we use both current and previously used designations of investment priorities.

the allocation for such instrument was PLN 15 million and the entries were allocated for innovative start-ups. We also suggest applying the quasi equity (*mezzanine*) loan instruments in the amounts from PLN 200,000 up to PLN 2 million for the period of 10 years, addressed to the existing micro, small or medium developing enterprises, based on R&D research results; the allocation for such instrument should be also PLN 15 million.

Under investment priority 3a (3.1), we additionally suggest considering the use of soft support in the form of advisory services and training courses preparing the capital entry.

Investment priority 3c (3.3) is the area, where the intervention addressed to enterprises should be concentrated. Based on the general concept of using financial instruments as well as on the results of the financing gap analysis, we have proposed:

- the instruments to bridge the financing gap: guarantees (basically up to PLN 300,000), micro loans (up to PLN 100,000), investment working capital loans (from PLN 100,000 to PLN 500,000) - with the total allocation of PLN 131 million;
- the instruments to bridge the financing gap and to create the incentive effect: investment loan (from PLN 0.5 million to PLN 1 million) - with the total allocation of PLN 50 million;
- the instruments to create the incentive effect: large investment loan (from PLN 1 million) - with the total allocation of PLN 30 million;

In case of investment priority 3c (3.3), we also suggest considering the grant of subsidies for the *mezzanine* loan transactions. The subsidy should be from PLN 5,000 to PLN 20,000 of de minimis value and cover the advisory fees, in particular the attorney's fees related to the preparation of the loan transaction.

Furthermore, as part of this investment priority, we suggest considering the subsidisation of the interest on commercial credits, potentially supported by guarantee. Such mechanism seems worth considering in case of some industries or groups of enterprises, which have no serious problems with obtaining refundable financing and whose financing risk is at a limited and average level, but also those whose development and investments should be supported as part of the regional policy (thus, these could be the companies representing industries related to intelligent specialisations).

The intervention under IP 4a (4.1) should be coordinated with the intervention under IP 4e (4.7) - we recommend creating one mechanism of preferential loans for both IPs intended for the construction of engine-driven cogeneration plants and producing electricity from renewable resources, with the total allocation of PLN 146 million and concentration on biogas plants and photovoltaic farms.

Similarly to IP 4a and 4e, the intervention in IP 4b (4.2) is basically addressed to enterprises - with the objective of improving their power efficiency. These fully market projects may be the subject of support for creating the incentive effect and - to a lesser extent - to eliminate the financing gap. Therefore, we recommend concentrating on preferential loans in IP 4b, with the allocation of PLN 73

² Due to amendments to the projects financed under IP 1b, it may be assumed that the capital entries should be implemented rather under investment priority 3a and the quasi-equity loans under investment priority 3c.

million and the scope of preference broader than in 3c (regardless of the value of the undertaking, solely depending on the increase of power efficiency).

IP 4c (4.3) is another area of high potential of using financial instruments for helping the condominiums and house co-operatives to reduce energy intensity of residential buildings - we recommend applying preferential loans of maximally extended payment period (even to 15 years), with the budget for the instrument in the amount of around PLN 45 million.

In case of investment priorities 4a/4g and 4c, it is worth considering the application of mixed instruments - as an alternative to financial instruments - in the form of subsidies allowing a partial repayment of the commercial credit capital. Such instrument could be taken into account in case of large number of small projects within the range of a few to several thousand Polish zlotys (e.g. installation of renewable energy source by prosumers).

Under investment priority 4e (4.5), we have considered the application of financial instrument for buying urban transport fleet (the allocation of at least PLN 40 million in the amount of PLN 2-15 million for the maximum period of 10-12 years), however, in the end we would rather recommend the application of the interest subsidisation mechanism (however, it is also acceptable to use the low intensity subsidy).

The financial instruments may also be used as a means of support for self-employment under IP 8iii (8.7), where the assumptions from the first report (allocation of PLN 57,4 million with approx. 1,400 of the loans granted) must be however treated carefully due to the requirement of allocating 80% of the priority allocation for supporting persons in difficult situation on the labour market - in case of which the support through financial instruments may not be fully adequate. Under the priority, it is possible to apply mixed instruments in the form similar to the one as proposed for investment priorities 3a and 3c, i.e. advisory services and training courses preparing for the grant of the loan for starting business.

On the other hand, the intervention under IP 9b (9.2) should be, above all, aimed at solving social problems in revitalised areas through infrastructure undertakings on a smaller scale, which supplement the investments necessary for the revitalisation of a given area, implemented under other CTs, which may significantly limit the legitimacy and scope of the application of financial instruments, therefore their form and possibility of application should be still revised. The proposed loan amounts are from PLN 200,000 to PLN 10 million for the period of 20 years, and the minimum allocation should be PLN 60 million. Interest rates on loans should be preferential, from 0% to 2%.

With respect to other investment priorities we do not recommend the application of financial instruments.

The concept of demarcation of the above-mentioned instruments together with the subsidy support was presented in the second report - it is especially significant for the purpose of establishing a cohesive support system for enterprises. The basic criterion of demarcation between the instruments is the volume of support and its purpose - however, the general principle is that the funds for more general goals related to the elimination of the financing group are more widely

available and are granted in the smaller amounts at market terms or similar thereto, whereas the broader scope of support (preferential terms, subsidies) is reserved for larger, specialist projects, where the incentive effect is more important than the elimination of the financing gap.

Additionally, the implementation solutions related to the implementation of financial instruments are also analysed in the first report. These opportunities are quite well described in the General Regulation, however in view of the past experience, we recommend the two most well-founded variants.

The first variant is the implementation of funds using the mechanism of the fund of funds for all the investment priorities, where the implementation of financial instruments is provided for. The sub-variant would be to entrust the implementation of financial instruments under investment priority 8iii (8.7) to the Voivodeship Labour Office.

On the other hand, the second variant of the implementation solutions, which we have recommended for consideration, assumes that two external institutions should be chosen and play the role of the fund of funds. After adopting this solution, one of the aforesaid institutions would be responsible for implementing financial instruments in the field of enterprises, i.e. under investment priorities 1b (1.2), 3a (3.1), 3c (3.3) and revitalisation priorities, i.e. 9b (9ii), whereas the second institution - under priorities 4a and 4c (4.1 and 4.3) related to environmental protection.

According to the evaluators, the second variant has slightly more advantages than the first variant, however, the first variant should be also considered acceptable.