European Network for Rural Development

This series of informative fiches aim to present, in summary, examples of practices and approaches that EU Member States and Regions have put in place in order to implement their Rural Development Programmes in the current period. These examples want to contribute to the understanding of what has worked well and less well in the delivery of the 2007-2013 RDPs and as far as possible, draw lessons in the view of future improvement of the programmes.

The Latvian Credit Fund under the 2007-2013 Rural Development Programme

Keywords: Financial instruments, Credit Fund

EU Member State: Latvia

Specific Location: The approach was applied nationwide

Implementing entities: Ministry of Agriculture; Rural Support Service (Paying Agency); State Joint Stock Company "Rural Development Fund" (Fund Manager); Financial intermediaries (commercial banks)

RDP Measure and budget: M121 - Modernization of agricultural holdings; M123 - Adding value to agricultural products; M312 - Business creation and development; M313 - Development of tourism activities.

Available financing for the Credit Fund: EUR 37.60 million

Implementation Period: From July 2010 until the end of the 2007-2013 EAFRD programming period

Needs addressed

During the 2008-2009 economic crisis, Latvian enterprises had a very limited ability to invest their own financial resources or to take loans that would give them the possibility to match EAFRD funds for the modernisation of agricultural holdings, adding value to agricultural products and economic diversification of rural businesses.

To support farmers, providers of rural tourism services and other rural entrepreneurs, the Ministry of Agriculture proposed to implement a new financial instrument – the ***Credit Fund*** – to give loans with reduced interest rates to implement EAFRD projects.

It was decided to provide all commercial banks with financial resources in order to give the beneficiary the flexibility to choose the most convenient credit institute based on past cooperation records. The State Joint Stock Company "Rural Support Fund" - dealing with different kinds of support programmes for rural entrepreneurs - was chosen as a manager of the Credit Fund.

Key elements of the approach

When a call for projects under RDP measures 121, 123, 312 (311) or 313 is announced by the Paying Agency (PA), those beneficiaries that: i) receive approval of their application and; ii) are not considered as being in difficulty, according to the Community Guidelines on State Aid for Rescuing and Restructuring Firms in Difficulty (2004/C244/02), have the possibility to get a loan with reduced interest rate with respect to what is available on the market.

The interest rate is calculated by summing up 20% of the 12 month EURIBOR or RIGIBOR rate with 70% of the average interest rate given to domestic enterprises and private persons according to the conditions applied by the Bank of Latvia. The interest rate is fixed for the whole duration of the loan up to a period of 15 years.

After receiving the application approval from the PA, the beneficiary approaches the credit institution that has a cooperation agreement with the Rural Development Fund – the manager of the Credit Fund. The bank assesses the financial viability of the project and makes a preliminary decision on the provision of the loan. Once the project is approved, the loan is issued to the beneficiary via the intermediary.

Objective

The Latvia Credit Fund aimed to promote the implementation of EAFRD projects while addressing the lack of sufficient private funding or from market sources.

Main steps and features of the initiative or approach

The functioning of the new financial instrument can be described in two phases: i) programming and establishment and; ii) implementation.

During the **programming and establishment phase**, the Ministry of Agriculture observed and analysed similar financial instruments that were planned to be introduced in other EU Member States, such as Lithuania, Romania and Germany. There were discussions between the Ministry of Agriculture and other potential stakeholders and beneficiaries in order to design adequate financial instruments that be used in the most effective ways in order to respond to the financial crisis and help beneficiaries to get the necessary resources to develop projects. The EC was also involved in the consultation process in order to avoid the misuse of EAFRD funds. The Ministry of Agriculture decided that instead of having one financial institution providing loans at reduced interest rate, this could possibly be offered to all financial intermediaries - commercial banks. The State Joint Stock Company "Rural Development Fund", which is already dealing with other support programmes for rural entrepreneurs, would be responsible for the overall management of the Credit Fund.

After the consultation phase and negotiations with the EC, the Ministry of Agriculture elaborated national regulatory acts that defined the implementation system, tasks and responsibilities for the establishment and functioning of the Credit Fund (Regulation No 664 'Order for administrating state and EU support for agriculture, rural and fisheries development for establishing the Credit Fund')

The **implementation phase of the Credit Fund** involves the following actors with the respective functions:

- Rural Support Service (PA): evaluation of business plans submitted by the Credit Fund (Rural Development Fund), transfer of finances to the Credit Fund, evaluation of project applications submitted by beneficiaries in compliance with EU and national regulatory acts, control of the use of money within the Credit Fund.
- State Joint Stock Company "Rural Development Fund" (Fund Manager): evaluation of financial intermediaries (credit institutions), transfer of money to financial intermediaries, budgeting and record keeping of the Credit Fund.
- Financial intermediaries (commercial banks): approval of loan applications, reporting to the Credit Fund and the Rural Support Service.

The procedure for project applications and issuing loans consists of the following steps:

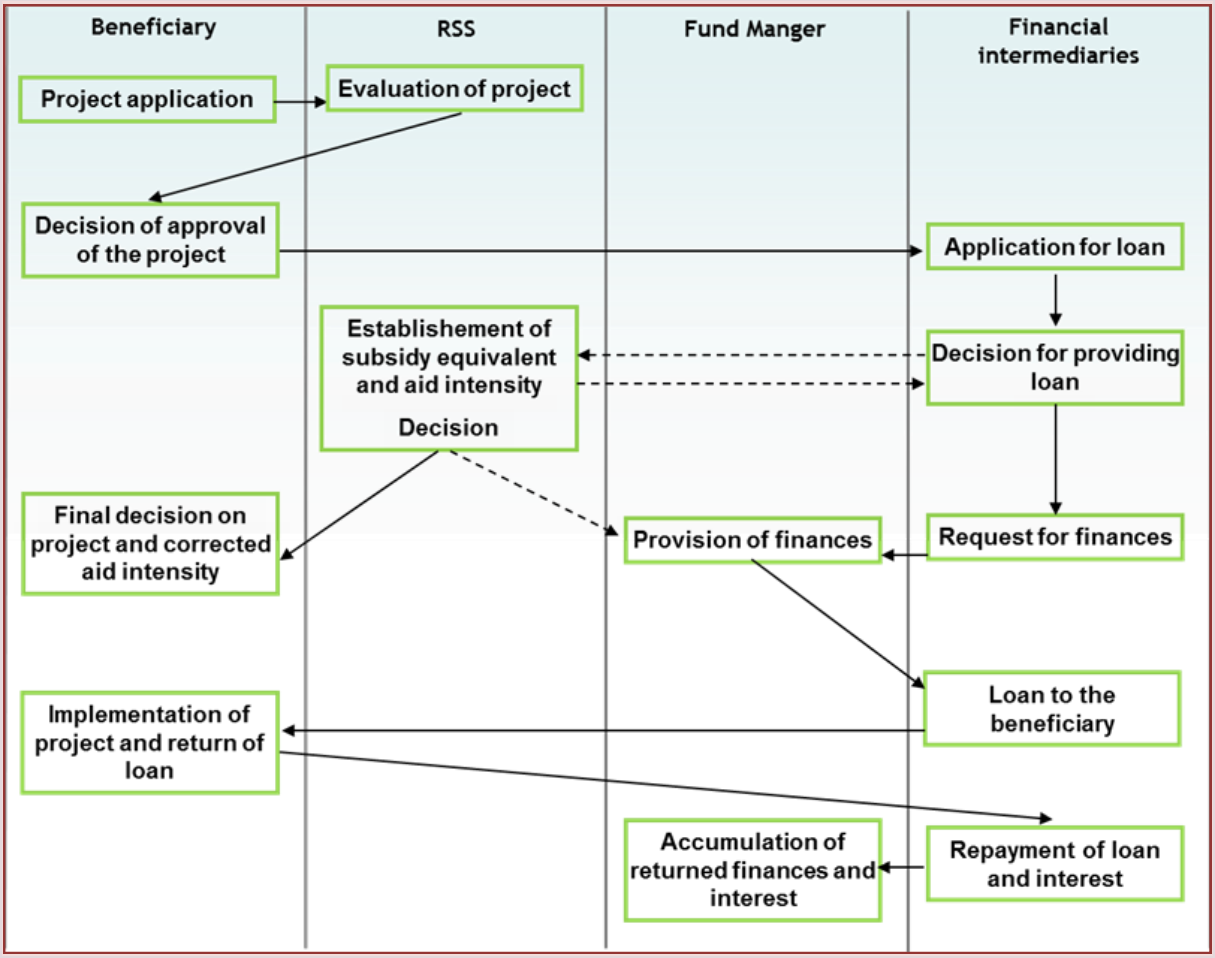
1. For each relevant RDP measure, the potential beneficiary applies for RDP support via a project application form completed with a business plan to the Rural Support Service (PA).
2. The Rural Support Service evaluates the project and, if it meets all the requirements and criteria, approves it.
3. The beneficiary applies for a loan with the financial intermediary (commercial bank that has a cooperation agreement with SJSC Rural Development Fund - the fund manager). The financial intermediary evaluates the financial viability of the business plan and makes a preliminary decision.
4. The financial intermediary submits the decision with the risk assessment of the borrower to the Rural Support Service. On the basis of the information received by the intermediary about the amount of loan requested and the interest rate, the Rural Support Service calculates the equivalent subsidy and corrects the aid intensity. The Rural Support Service makes the final decision on the project.

5. Upon approval of the project, the financial intermediary submits a request to the Fund Manager which assesses the request and provides the finances to the intermediary on the base of the cooperation agreement.

The intermediary issues the loan to the beneficiary.

As the project beneficiary implements the project and returns the loan to the financial intermediary, the latter repays the loan and interest rate to the Fund Manager, which accumulates returned finances and interest (see graph on Operation of Credit Fund below).

Graph 1: Operation of Credit Fund



Main results and benefits

By December 2013, all loans were paid for a total amount of EUR 26.54 million and 56 projects were implemented, namely:

- M121 - Modernization of agricultural holdings: 51 projects
- M123 - Adding value to agricultural products: 4 projects
- M313 - Development of tourism activities: 1 project

The Credit Fund proved to be an efficient instrument in time of economic crisis allowing banks and rural businesses to face the constraint of limited financial capacity. With such instrument already established and considering the experience accumulated, responding to possible future market failures would be quicker and easier. The Ministry of Agriculture is satisfied with the results and will continue its implementation in the next programming period, particularly targeting agricultural holdings and entrepreneurs with a turnover of less than EUR 70 000.

Lessons learnt

The Ministry of Agriculture highlights some of the lessons learned derived from the establishment and implementation of the Credit Fund instrument during the 2007-2013 programming period:

The preparatory phase involved too many consultations with stakeholders and the EC and therefore the Credit Fund was not used as originally planned. By the time the fund was established (2010), the commercial banks partially recovered their lending capacity and regular loans were again available on the market.

Typically, as all the risks are undertaken by credit institutions, loans were provided only to clients who already showed a solid credit history. Also, preference was given to large projects. However, small and medium sized enterprises and agricultural holdings were the ones with the highest financing needs. The criteria used for the risk assessment of the borrower were too strict and excluded many small and medium sized farmers and enterprises from the possibility to receive loans. The Ministry of Agriculture is planning to better support small farmers or business start-ups in rural areas during the next planning period.

The current implementation mechanism of the Credit Fund envisages a quite complicated system of decision making and assessment of the projects (business plan), taking place in different institutions. This creates some administrative burdens and delays. In the future, the Ministry of Agriculture would like to introduce streamlined procedures and reduce crosschecking by following a "one stop-shop" principle.

Additional sources of information

Additional Sources of Information: Information about the Latvian Credit Fund: http://www.laf.gov.lv/index.php/kreditufonds (in Latvian)

The Cabinet regulation of July 20th, 2010 No 664 “Order for administrating state and EU support for agriculture, rural and fisheries development for establishing the Credit Fund“ http://likumi.lv/doc.php?id=214319 (in Latvian)

Presentation of the Latvian Credit fund and other relevant documents from the ENRD workshop on Financial instruments: http://enrd.ec.europa.eu/en-rd-events-and-meetings/seminars-and-conferences/cc-workshop-on-financial-instruments/en/cc-workshop-on-financial-instruments_en.cfm