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ESF+ financial instruments

Handbook

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ESF+ financial instruments

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Abbreviations

Abbreviation	Full name
ANPAL	National Agency for Labour Active Policies
BGK	Bank Gospodarstwa Krajowego
BOV	Bank of Valletta plc
CEB	Council of Europe Development Bank
CPR	Common Provisions Regulation
EBRD	European Bank for Reconstruction and Development
EIB	European Investment Bank
EIF	European Investment Fund
ENM	Ente Nazionale per il Microcredito
EQF	European Qualifications Framework
EPRS	European Pillar of Social Rights
ERDF	European Regional Development Fund
ESF	European Social Fund
ESF+	European Social Fund Plus
ESIF	European Structural and Investment Funds
EU	European Union
FOF	Fund of Funds
FSMA	Further Studies Made Available
FSMA+	Further Studies Made Affordable Plus
MDB	Malta Development Bank
MQF	Malta Qualifications Framework

NEET	Not in Education, Employment or Training
NESTA	National Endowment for Science, Technology and the Arts
NFSE	National Fund for Social Entrepreneurship
NGO	Non-governmental organisation
NOP	National Operational Programme
OP	Operational Programme
PbR	Pay By Results
SEE	Social Economy Entity
SESC	Social Economy Support Centre
SIB	Social Impact Bond
SIF	Social Innovation Fund
SIFTA	Social Inclusive Finance Technical Assistance
SIS window	Social Investment and Skills window
SO	Specific Objective
SOC	Social Outcome Contracting
SPAO	Active Policy Systems for Employment
TO	Thematic Objective
YEI	Youth Employment Initiative

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Introduction

This handbook provides information on designing and implementing financial instruments within the European Social Fund Plus (ESF+) framework. It is primarily intended for ESF+ managing authorities and other stakeholders in order to raise awareness and facilitate a deeper understanding of the potential role of financial instruments in contributing to the key ESF+ policy areas:

- Employment;
- Education and training;
- Social inclusion.

With a budget of almost EUR 99.3 billion for the 2021-2027 programming period, the ESF+ is the main instrument for investing in people, contributing to the EU's employment, social, education and skills policies, including structural reforms in these areas. Moreover, as the COVID-19 pandemic has impacted EU policy priorities, the ESF+ plays a stronger role in addressing new challenges in terms of labour participation, the need for new social services, updating the educational and health systems, and combating increased inequalities.

Addressing new and increased social challenges through financial instruments provides a sustainable alternative to traditional grant-based financing. Financial instruments have several advantages:

- As they are expected to be repaid, the revolving resources can be further used to support additional final recipients;
- They can attract co-investment from other resources, including the private sector, and therefore, provide more financial support for final recipients;
- Reflows and co-investment increase the available resources, easing the burden on the public budget;
- They can support supply-side development, stimulating the bodies implementing the financial instrument, financial intermediaries and other stakeholders to participate in the improvement of the social economy;
- They contribute to selecting viable projects and investments, increasing the social impact on communities;
- As resources should be repaid, final recipients are more responsible for managing their projects and investments.

This handbook explains how to make the most of these advantages, having been based on practical examples from ESF+ managing authorities that have implemented or are implementing financial instruments.

It is structured in four chapters:

- **Chapter 1** describes the added value of using financial instruments within the ESF+ and their benefits in achieving social goals. It then outlines the typical final recipients and key needs by policy area. This chapter also provides figures and numbers regarding the resources allocated to financial instruments across the policy areas during the 2021-2027 programming period;
- **Chapter 2** the core of the handbook, describes the life cycle and governance options of ESF+ financial instruments as well as the financial products that can be provided to ESF+ final recipients, including the possibilities for their use in combination with grants. It also describes how to use the InvestEU programme through the Member State Compartment;
- **Chapter 3** illustrates how the different financial products can be used across the ESF+ policy areas (employment, education, and social inclusion). It also provides practical examples for inspiration;
- **Chapter 4** concludes the handbook by providing key recommendations for efficient and effective use of ESF+ financial instruments;
- **Annex I** lists relevant resources and publications that can be consulted for further advice and information on financial instruments;
- **Annex II** lists the financial instruments planned under ESF+ by EU Member State and policy area.

01 Why use financial instruments in ESF+ programmes?

1.1 The added value of financial instruments within the ESF+

In recent years, EU Member States have faced a series of interdependent and interrelated crises, significantly expanding the demands and expectations on public policies and budgets, increasing the pressure on them and underscoring the need for improvements in efficiency and effectiveness.

Social policy is one of the areas noticeably impacted by these crises. Faced with both long-standing tasks and emerging challenges, such as the social inclusion of migrants, access to employment in structurally affected regions, and reskilling/upskilling in response to new labour market requirements, social policy is feeling the pinch of budgetary constraints more now than ever. Traditional forms of financing based on non-repayable support are no longer sufficient, necessitating the exploration and utilisation of less conventional methods.

Financial instruments can present a valuable opportunity for public institutions and decision-makers to enhance available resources and strengthen the capacity to address both long-term and emerging social challenges. Financial instruments offer a range of benefits:

Table 1.1: Financial instruments' benefits

Financial instruments' benefit	Description
Revolving effect	Given their repayable nature, financial instruments present continuous flows of money generated through repayments or cost savings as well as the realisation of investments. Such revolved resources can lower the pressure on public budgets as they can be reused for further investments to achieve policy goals.
Leverage effect	The use of public funds in the form of financial instruments has the potential to attract additional public and private resources. This not only multiplies the total resources available to address social needs but also boosts the efficiency of public spending and aligns public and private interests. This alignment can be mutually beneficial. The public sector can alleviate part of both the budgetary burden and risk, while private financial intermediaries can expand their clientele and explore new markets by contributing their own resources to the financial instrument's allocation.
Enhanced quality of supported projects	Given that financial instruments are closely linked to the market and implemented by financial intermediaries with sector-specific expertise and standardised procedures (e.g. for creditworthiness assessment), they support economically viable projects with higher impacts on communities and a better probability of seeing a return on the investment.
Changing the grant-oriented mindset	The use of financial instruments has considerable potential to decrease grant dependency and develop the necessary skill sets for improving financial planning and project management for final recipients.

Combining financial instruments with grants	Combining financial instruments with grants allows and incentivises entry to new or riskier markets. It can close the financial gap to meet the investment needs of crucial projects that may have a high social impact but lower financial return or higher risk.
Earlier availability of financial resources	Resources provided through financial instruments are made available to the final recipients earlier than grants since they are allocated before the project's launch. This can be advantageous for final recipients who have few or no resources for pre-financing or co-financing.
Minimal market distortion	Designing financial instruments requires an understanding of the market, supply-side actors, and demand-side needs and expectations, which improves the public sector's knowledge of current challenges and financing gaps, and the potential solutions for addressing these. Setting up and implementing financial instruments requires structured governance mechanisms regulated by specific selection procedures, as well as contractual agreements. When these procedures are properly carried out in coordination with the private sector, they result in minimal market distortion from a macroeconomic perspective. Unlike grants, financial instruments contribute to the complementarity between the public and private sectors and help better target various market failures.
Collaborating with financial institutions	Implementing financial instruments offers an opportunity to establish stronger ties with financial institutions both for the public sector as well as for final recipients, facilitating the transfer of valuable know-how. Through financial instruments, the public sector can involve experienced non-bank financial intermediaries who know how to select viable projects. Final recipients can gain access to a wider spectrum of financial resources for their projects as well as to private sector expertise, advice and non-financial support. Moreover, refunding the resources improves the final recipients' credit history and, therefore, their bankability.

Source: Own elaboration.

Numerous examples of the implementation of financial instruments across the EU highlight the above-mentioned benefits of financial instruments, demonstrating stimulating strategic and integrated approaches to social interventions at all levels, which enhance the overall effectiveness and advance social policy in the EU. ESF+ financial instruments can play a vital role in achieving several social goals, such as:

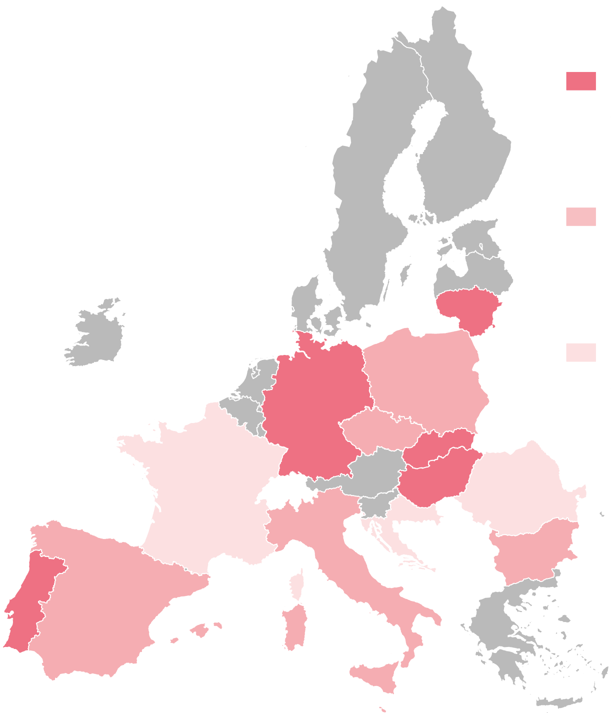
- **Empowering Vulnerable Groups:** Financial instruments can provide financing solutions to marginalised individuals, like the long-term unemployed or migrants, improving their economic circumstances and promoting social inclusion;
- **Skill-building & Education:** Financial instruments can promote skill-building and education by bolstering human resource development through financial support for individual training and lifelong learning programmes;
- **Mitigating Social Exclusion:** Financial instruments can play a critical role in mitigating social exclusion and discrimination by providing financing options that enable wider participation in economic activities and create inclusive labour markets;
- **Promoting Social Entrepreneurship:** Financial instruments can stimulate social entrepreneurship by supplying financing to social enterprises that tackle societal, ethical, or environmental challenges, fostering an environment of innovation and shared prosperity;

- **Enhancing Gender Equality:** By offering financing options, financial instruments can help to enable female entrepreneurship, balance work and life commitments, and fight against gender-based discrimination, furthering gender equality;
- **Facilitating Poverty Alleviation:** By offering financial support to low-income individuals and families, financial instruments can play a pivotal role in poverty reduction endeavours.

The benefits of financial instruments are increasingly recognised by managing authorities and other stakeholders, reflecting a positive long-term trend. In the 2014-2020 programming period as of 31 December 2022, EUR 629.1 million of ESF funds had been committed to financial instruments[1], with EUR 347.1 million already paid out. Among the 11 EU Member States that have implemented financial instruments under ESF, Germany (with a committed amount of EUR 221.9 million), Italy (EUR 188.3 million), and Poland (EUR 61.6 million) have made the largest commitments so far. In total, by the end of 2022, it was reported that 94 financial instruments were being set up or were already operational, with more than 17 000 final recipients already supported by these financial instruments[2].

Compared to the 2014-2020 programming period, the 2021-2027 programming period has seen a change in the composition of EU Member States planning to implement financial instruments under the ESF+. This change is illustrated in the figure below.

Figure 1.1: ESF/ESF+ financial instruments by EU Member State



Source: Elaboration based on Cohesion Data as of 10 April 2024, available here.

1 This figure includes ESF committed to financial instruments for sustainable and quality employment (approx. EUR 354 million), for social inclusion (approx. EUR 65 million), for education and training (approx. EUR 91 million), and for REACT-EU (approx. EUR 118 million). Thus, if considering only the first three items, which correspond to the technical objectives defined in the ESF Regulation and the ESF+ policy areas (please see below), the ESF amount committed to financial instruments would amount to ca. EUR 510 million.

2 European Commission (2023), *Financial instruments under the European Structural and Investment Funds. Summaries of the data on the progress made in financing and implementing the financial instruments for the programming period 2014-2020 in accordance with Article 46 of Regulation (EU) No 1303/2013 of the European Parliament and of the Council – Situation as of 31 December 2022.*

In the current 2021-2027 programming period, managing authorities in a third of EU Member States plan to allocate a total of EUR 682.1 million (0.79% of the total ESF+ allocation) to financial instruments under the ESF+. In absolute terms, the highest amounts for financial instruments are planned in Italy, which, thanks to its supportive and well-functioning banking system, has historically been the top contributor of financial instruments, and in Poland, which is characterised by the long experience and leadership of the national promotional institution. In relative terms, Malta and Croatia are planning the highest share of financial instruments from the entire ESF+ allocation. Detailed information on the extent of the planned financial instruments under the ESF+ in individual EU Member States is provided in the table below.

Table 1.2: 2021-2027 ESF+ allocation to financial instruments by EU Member State

EU Member State	ESF+ allocation (EUR million)	ESF+ financial instruments (EUR million)	Share of ESF+ financial instruments (%)
Italy	13 516	283.9	2.10
Poland	11 890	228.7	1.92
Romania	6 152	80.0	1.30
Croatia	1 794	42.5	2.37
France	5 825	15.0	0.26
Bulgaria	2 340	13.3	0.57
Czechia	2 261	11.7	0.52
Spain	10 314	4.0	0.04
Malta	112	3.0	2.67
Total	**54 205**	**682.1**	**1.26**

Source: Elaboration based on Cohesion Data as of 10 April 2024, available here.

In terms of the types of financial instruments planned for the 2021-2027 programming period, loans[3] are the most common, accounting for 68.2% of the total ESF+ financial instrument allocation. These are followed by grants within a financial instrument operation[4] (19.8%), guarantees[5] (7.9%), and equity/quasi-equity[6] (4.1%). The specific situation in the individual EU Member States is shown in the figure below.

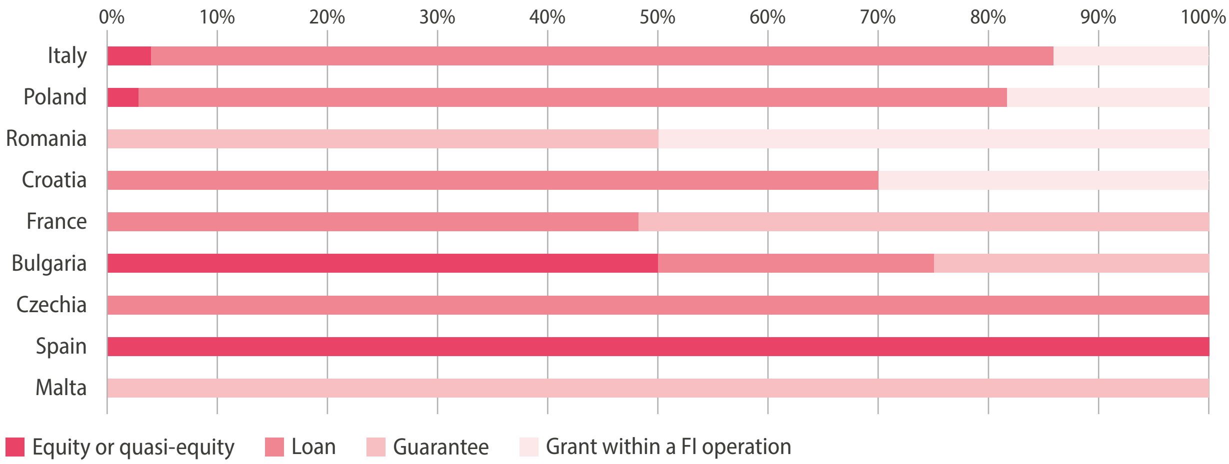
3 According to Regulation 2018/1046, Art.2(40) 'Loan means an agreement which obliges the lender to make available to the borrower an agreed amount of money for an agreed period and under which the borrower is obliged to repay that amount within the agreed period'. See section 2.3.1 for details.

4 Grants within a financial instrument operation are provided together with financial instruments by the body implementing the financial instrument within a single funding agreement. These grants are directly linked and necessary for the financial instrument and do not exceed the value of the investments supported by the financial product (see section 2.4 for details).

5 According to Regulation 2018/1046, Art.2(34) 'Guarantee means a written commitment to assume responsibility for all or part of a third party's debt or obligation or for the successful performance by that third party of its obligations if an event occurs which triggers such guarantee, such as a loan default'. See section 2.3.2 for details.

6 According to Regulation 2018/1046, Art.2(25) 'Equity investment means the provision of capital to a company, invested directly or indirectly in return for total or partial ownership of that company and where the equity investor may assume some management control of the firm and may share the firm's profits'. According to Regulation 2018/1046, Art.2(52) 'Quasi-equity investment means a type of financing that ranks between equity and debt, having a higher risk than senior debt and a lower risk than common equity and which can be structured as debt, typically unsecured and subordinated and in some cases convertible into equity, or as preferred equity. See section 2.3.3 for details.

Figure 1.2: 2021-2027 type of financial instruments planned under ESF+ by EU Member State[7]

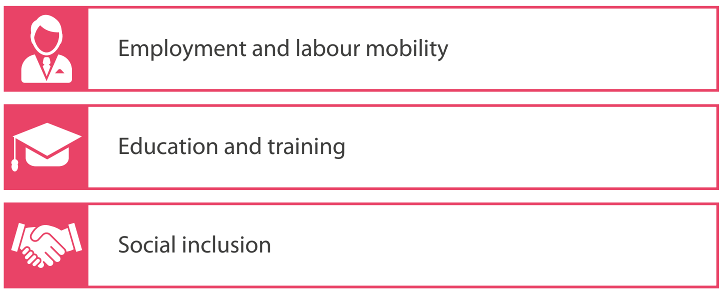


Source: Elaboration based on Cohesion Data as of 10 April 2024, available here.

1.2 Financial instruments and the ESF+ objectives

Financial instruments are highly relevant to the ESF+, the EU's main tool for investing in people, and align well with the ESF+ objectives set out in the ESF+ Regulation[8]. This outlines thirteen specific objectives aimed at bolstering the EU's social dimension and putting the principles of the European Pillar of Social Rights (EPSR)[9] into practice. For clarity, these specific objectives can be organised into the following three policy areas:

Figure 1.3: ESF+ policy areas



Source: Own elaboration.

For the 2021-2027 programming period, the policy area of Employment and labour mobility is the most significant, with a planned financial instrument allocation of EUR 538.8 million (79.0% of the total ESF+ financial instrument allocation). The other two policy areas are set to receive significantly less, with Education and training planned for EUR 76.6 million (11.2%) and Social inclusion for EUR 66.6 million (9.8%). The specific situation in the individual EU Member States is shown in the table below.

7 The information provided, sourced from the Cohesion Data portal, shows how EU Member States have indicated their planned use of financial instruments. It should be noted that this information may be subject to potential adjustments.
8 Regulation (EU) 2021/1057 of the European Parliament and of the Council of 24 June 2021 establishing the European Social Fund Plus (ESF+) and repealing Regulation (EU) No 1296/2013. Available here.
9 EPSR is a set of 20 key principles and rights established by the EU to support fair and well-functioning labour markets and welfare systems. Introduced in 2017, it serves as a framework to guide policies and legislation at both the European and national levels. The principles and rights outlined in the EPSR are centered around three main categories: 1) equal opportunities and access to the labour market; 2) fair working conditions; 3) social protection and inclusion. For more information, please see here.

Table 1.3: 2021-2027 financial instruments planned under ESF+ by EU Member State and policy areas

EU Member State	Employment and labour mobility (EUR million)	Education and training (EUR million)	Social inclusion (EUR million)
Italy	276.3	-	7.6
Poland	125.0	56.3	47.4
Romania	80.0	-	-
Croatia	42.5	-	-
France	15.0	-	-
Bulgaria	-	13.3	-
Czechia	-	-	11.7
Spain	-	4.0	-
Malta	-	3.0	-
Total	**538.8**	**76.6**	**66.7**

Source: Elaboration based on Cohesion Data as of 10 April 2024, available here.

1.2.1 Employment and labour mobility

The specific objectives within the Employment and labour mobility policy area generally aim to ensure equal and fair access to employment for all jobseekers, particularly the disadvantaged. They also strive to modernise the labour market and related services, enabling a flexible response to new conditions and societal needs. The four specific objectives falling within this policy area are shown in the figure below.

Figure 1.4: Specific objectives under the Employment and labour mobility policy area

Policy area Employment and labour mobility

Specific objectives

SO 4.1	Improving access to employment and activation measures for all jobseekers
SO 4.2	Modernising labour market institutions and services to support for labour market matching, transitions and mobility
SO 4.3	Promoting a gender-balanced labour market participation, equal working conditions, and a better work-life balance
SO 4.4	Promoting the adaptation of workers, enterprises and entrepreneurs to change, active and healthy ageing

Source: Own elaboration.

These specific objectives under the Employment and labour mobility policy area cover various aspects and overlap with a number of related themes such as education and training, social services, etc. As a result, the financial instruments implemented in this policy area can have diverse areas of focus. The table below provides an indicative overview of potential financial recipients, along with their respective needs.

Table 1.4: Typical final recipients and key needs under the Employment and labour mobility policy area

Typical final recipients	• Job seekers and inactive people; • The Long-term unemployed; • Young people from marginalised communities at risk of social exclusion; • Entrepreneurs and business creators; • Public institutions/bodies or NGOs providing labour and social services.
Key social goals	• Bridging the information gap/asymmetry between job seekers and employers to alleviate mismatches and inefficiencies in the labour market; • Addressing skills gaps/shortages through increased availability of educational and vocational training programmes to meet the evolving needs of the labour market; • Enhancing labour mobility and related support services to effectively tackle geographical mismatches; • Promoting equal opportunities and combating discrimination to optimise the utilisation/development of human capital; • Strengthening support services for disadvantaged people, contributing to their social inclusion; • Creating pathways to work for individuals (especially the long-term unemployed or inactive) to help them return to gainful employment; • Creating opportunities for youth through supportive services that align with education and training systems; • Creating opportunities for youth through strengthening supportive services and better interconnection of the education system and the labour market; • Encouraging business growth to improve conditions on the supply side of the labour market; • Strengthening care for careers through focusing on work-life balance, continuous training and learning requirements, and the specificities of older workers.

Source: Own elaboration.

A specific description of the needs of disadvantaged groups seeking self-employment and entrepreneurship that can be effectively addressed through the implementation of financial instruments is provided in the box below based on data taken from real a practical example of an ESF financial instrument implemented in Italy (see section 3.1.4 for additional information on this case)[10].

10 Additional examples on how to implement financial instruments for employment and labour mobility are provided in section 3.1.

Box 1.1: Self-employment and entrepreneurship by the disadvantaged groups, Italy

In the context of the Italian labour market, 'Not in Education, Employment, or Training' individuals (NEETs), inactive women, and the long-term unemployed can be categorised as disadvantaged groups. One possible way of increasing their long-term participation in the labour market is through self-employment and entrepreneurship. The ex-ante assessment[11] identified two primary needs of these disadvantaged groups. The first need is access to microcredits and small loans on sufficiently favourable terms, which may include: 1) low interest rates; 2) no collateral or guarantee requirements; 3) longer repayment periods; 4) the possibility of using a grace period for at least the period shortly after the establishment of the respective enterprise. In addition to this financial need, another need identified is mentoring and skills development. Disadvantaged groups, in particular, often lack the entrepreneurial and management skills needed during both the project preparation phase and the implementation phase. Addressing these needs is essential for the long-term development of entrepreneurs and the sustainability of the supported initiatives.

Source: Own elaboration.

1.2.2 Education and training

This policy area encompasses specific objectives that generally aim to contribute to high-quality, accessible, and flexible labour market-relevant education, training, and learning systems. These systems should be equipped to swiftly respond to rapidly evolving societal needs and labour market requirements. The three specific objectives that fall under this policy area are illustrated in the figure below.

Figure 1.5: Specific objectives under the Education and training policy area

Policy area	Specific objectives	
Education and training	SO 4.5	Improving the quality, inclusiveness, effectiveness and labour market relevance of education and training systems
	SO 4.6	Promoting equal access to and completion of quality and inclusive education and training
	SO 4.7	Promoting lifelong learning, in particular flexible upskilling and reskilling opportunities for all anticipating change and new skills requirements

Source: Own elaboration.

As education and training have evolved into a lifelong process not strictly tied to formal educational institutions, financial instruments can adopt a correspondingly diverse character and focus. The table below provides an indicative overview of potential financial recipients and their respective needs.

11 Ministero del Lavoro e delle Politiche Sociali (2015), *Valutazione ex ante degli strumenti finanziari da attivare nell'ambito del PON IOG 2014-2015 e PON SPAO 2014-2020 Rapporto Finale*. Available here.

Table 1.5: Typical final recipients and key needs under the Education and training policy area

Typical final recipients	• Students • Workers seeking higher qualifications; • Public institutions/bodies providing vocational training; • NGOs providing vocational training; • Enterprises providing training programmes directly for their employees; • Public and private institutions involved in primary and secondary education; • Universities or Higher Education Research Centres.
Key social goals	• Improving access to education and training by overcoming barriers such as poverty, discrimination, and geographical isolation; • Improving access to funding for education and training on favourable terms, independent of socio-economic status and family support; • Enhancing access to funding for companies implementing training systems for their employees; • Improving conditions for educational institutions, including minimising barriers to providing various forms of support to prospective or actual students; • Enhancing the flexibility of the education system to swiftly adapt to the evolving needs and requirements of the labour market; • Improving the quality of education and training and intensifying cooperation with practitioners; • Promoting better/highly qualified jobs requiring and rewarding an educated and skilled workforce; • Ensuring greater coordination among educational and training providers, leading to greater value for public money.

Source: Own elaboration.

A concrete description of the needs of prospective students, which can be efficiently met through the implementation of financial instruments, is presented in the box below based on data taken from a real practical example of an ESF financial instrument implemented in Malta (see section 3.2.4 for additional information on this case)[12].

12 Additional examples on how to implement financial instruments for education are provided in section 3.2.

Box 1.2: Post-secondary education, Malta

In Malta, not all post-secondary specialised courses are provided free of charge. Some are not available in Malta at all, necessitating study abroad, while others are offered by private institutions at a substantial fee. The ex-ante assessment[13] revealed that those seeking further studies primarily need access to funding on favourable terms and conditions. Without such terms and conditions, prospective students would be dependent on their socio-economic background and family support, without which further studies would be unaffordable. Prospective students particularly need: 1) the elimination of collateral or life insurance requirements; 2) a reduction in the interest rates, leading to lower monthly repayments; 3) an extended repayment period; 4) a grace period, possibly lasting for the duration of the studies; and 5) flexible use of funding to cover not only tuition fees but also other study-related expenses, such as accommodation and transport.

Source: Own elaboration.

1.2.3 Social inclusion

The specific objectives within the Social Inclusion policy area have a common aim to facilitate the social and economic integration of individuals from disadvantaged groups. These may include third-country nationals, members of marginalised communities, those in socio-economic difficulties, or those with health issues. The typical methods for achieving social inclusion encompass ensuring equal opportunities and access to both the labour market and social and health services. The six specific objectives that fall under this policy area are illustrated in the figure below.

Figure 1.6: Specific objectives under the Social inclusion policy area

Policy area	Specific objectives	
Social inclusion	SO 4.8	Fostering active inclusion with a view to promoting equal opportunities and improving employabilit
	SO 4.9	Promoting socio-economic integration of third-country nationals, including migrants
	SO 4.10	Promoting the socio-economic integration of marginalised communities, such as Roma people
	SO 4.11	Enhancing equal and timely access to quality, sustainable and affordable social, healthcare and long-term care services
	SO 4.12	Promoting social integration of people at risk of poverty or social exclusion
	SO 4.13	Addressing material deprivation through food and/or basic material assistance to the most deprived persons

Source: Own elaboration.

13 Ministry of Education (2015), *Ex-Ante Assessment of Financial instrument in Operational Programme II 2014-2020 financed through ESF.* Available here.

This relatively broad range of specific objectives under the Social inclusion policy area opens the door for a variety of financial instruments. These can target different final recipients and address diverse needs. The table below provides an indicative overview of potential final recipients and their respective needs.

Table 1.6: Typical final recipients and key needs under the Social inclusion policy area

Typical final recipients	• Social entrepreneurs and enterprises; • Public institutions/bodies or NGOs providing services of general interest (e.g. labour and social services); • Social (public and private) innovators; • Members of disadvantaged, marginalised and discriminated communities; • Female entrepreneurs; • Migrant entrepreneurs; • Roma entrepreneurs.
Key social goals	• Combating marginalisation through accessible and well-funded support services; • Advancing inclusive approaches across all levels of the public and private sector; • Promoting social entrepreneurship by improving access to funding under favourable terms and establishing a convenient legal framework; • Enhancing coordination among multiple stakeholders at different levels to efficiently allocate resources and foster synergies; • Encouraging local partnerships to enhance communication and collaboration among stakeholders with intricate knowledge of the local environment.

Source: Own elaboration.

A specific description of the needs of social enterprises seeking to encourage the social inclusion of disadvantaged people that can be effectively addressed through the implementation of financial instruments is provided in the box below based on data taken from a real practical example of an ESF financial instrument implemented in Czechia[14].

14 Additional examples on how to implement financial instruments for social inclusion are provided in section 3.3.

Box 1.3: Social entrepreneurship, Czechia

Social entrepreneurship in Czechia focuses mainly on social inclusion and the employment of disadvantaged people. As revealed by the ex-ante assessment[15] and other analyses of the Czech environment and foreign experiences, two fundamental needs of social enterprises striving for social inclusion have been identified. The first need is an increase in the availability of funding. This particular need stems from the fact that funding for social enterprises is severely limited due to market failure caused by a number of factors, such as regulatory uncertainty, limitations on profits, low returns on soft investments typical for social enterprises, as well as information asymmetry. Furthermore, presumed lower productivity per worker reduces creditworthiness and exacerbates problems with predicting future cash flows for social enterprises. This is because their profitability is very closely linked to the social entrepreneurs involved. There are also relatively high transaction costs for banks with the smaller investments demanded by social enterprises. The second need is driven by the finding of relatively weak entrepreneurial skills resulting in inadequate business plans, inefficient marketing, and the limited sustainability of projects. This situation can be partly attributed to a long-standing orientation towards non-repayable financing support, especially grants, and a lack of exposure and experience in a purely market-driven environment. Addressing this need is critical for long-term efficiency in social enterprises and for enhancing their capacity to create high-quality projects.

Source: Own elaboration.

15 Ministry of Labour and Social Affairs (2017), *Ex-ante assessment of the use of financial instruments in the Operational Programme Employment 2014-2020*. Available here.

How to use financial instruments?

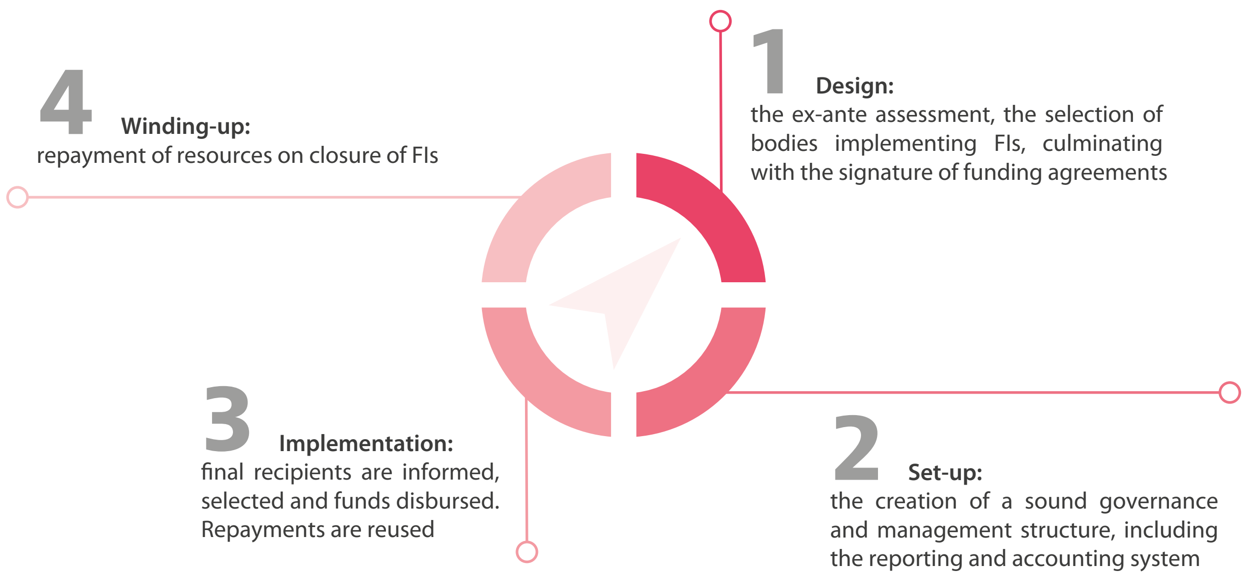
This chapter describes the principal technical aspects to consider when using financial instruments within the ESF+:

- The first section describes the life cycle of financial instruments, detailing its four main phases considering the main regulatory aspects included in the 2021-2027 Common Provisions Regulation (CPR) Regulation[16];
- The second section is more specific on the governance options that an ESF+ managing authority can consider, according to the CPR regulation, when setting up a financial instrument;
- The third section focuses on the key financial products that can be activated to provide finance to ESF+ final recipients;
- The fourth section focuses on the combination of financial instruments with grants;
- The fifth section describes the possibilities that managing authorities can exploit in using the InvestEU programme through the Member State's compartment.

2.1 The financial instrument life cycle

The life cycle of a financial instrument is composed of four main phases: design, set-up, implementation and winding-up.

Figure 2.1: The financial instrument life cycle



Source: Reproduced from fi-compass (2015), Developing an action plan, available here.

16 Regulation (EU) 2021/1060 of the European Parliament and of the Council of 24 June 2021 laying down common provisions on the European Regional Development Fund, the European Social Fund Plus, the Cohesion Fund, the Just Transition Fund and the European Maritime, Fisheries and Aquaculture Fund and financial rules for those and for the Asylum, Migration and Integration Fund, the Internal Security Fund and the Instrument for Financial Support for Border Management and Visa Policy. Available here.

The **design** phase begins with the *programme indications* regarding the planned use of financial instruments (Art.22.3.d.vii of the CPR) for each specific objective and any related justifications . It should also consider market failures, investment needs and complementarities with other forms of support (Art.22.3.a), as well as the planned allocations to financial instruments (Art.22.3.d.viii).

The next step is to conduct *the ex-ante assessment* to identify any market gaps and assess the final recipients' financial needs that can be addressed through financial instruments. This ex-ante assessment must include (Art. 58.3): the proposed value of the programme contribution to a financial instrument; the estimated leverage effect accompanied by a short justification; the proposed financial products[17] to be offered; the proposed target group of final recipients; and the expected contribution of the financial instrument to achieving the specific objectives. New flexibility introduced in the 2021-2027 programming period allows managing authorities to use, and update, when necessary, the 2014-2020 ex-ante assessment.

The last step is to decide the *governance structure* (Art.59). The managing authority may decide to implement the financial instrument in one level through a body implementing the financial instrument or in two levels through a holding fund and bodies implementing the financial instrument (see next section for details). The selection of the body implementing the financial instrument should comply with the applicable public procurement laws and criteria. These criteria include economic and financial viability, the capacity to implement the financial instrument, effective and efficient internal control and accounting systems, robust methodology for selecting final recipients and the ability to add financial resources[18]. However, as working with ESF+ final recipients may be riskier and requires a proper balance between social and financial returns, managing authorities should consider additional aspects in selecting the most appropriate bodies to manage the financial instrument, as outlined in box 2.1 below.

The selection of the body implementing the financial instrument concludes with the *signature of the funding agreement,* a legal commitment between the managing authority and the body managing the holding fund[19] or between the managing authority and the body implementing the financial instrument, or where applicable, between the holding fund and body implementing the financial instrument[20]. Key elements to be included in the funding agreement (according to Annex X of the 2021-2027 CPR) are the investment strategy, the business plan (including the estimated leverage effect), provisions for monitoring and audit requirements, requirements and procedures for managing interest and other gains generated, provisions regarding the calculation and payment of the management costs incurred or of the management fees, provisions regarding the re-use of resources and the winding-up of the financial instrument.

17 For more information on financial products, please see section 2.3 and chapter 3.

18 According to Art. 7 of the Regulation (EU) No 480/2014. For additional information on the selection process of the bodies implementing financial instruments see fi-compass (2021), *fi-compass Knowledge Hub - Selection of financial intermediaries*, available here.

19 According to the 2021-2027 CPR (Art.2.(20)) "holding fund' means a fund set up under the responsibility of a managing authority under one or more programmes, to implement one or more specific funds". In the previous programming period this was labelled as 'fund of funds'.

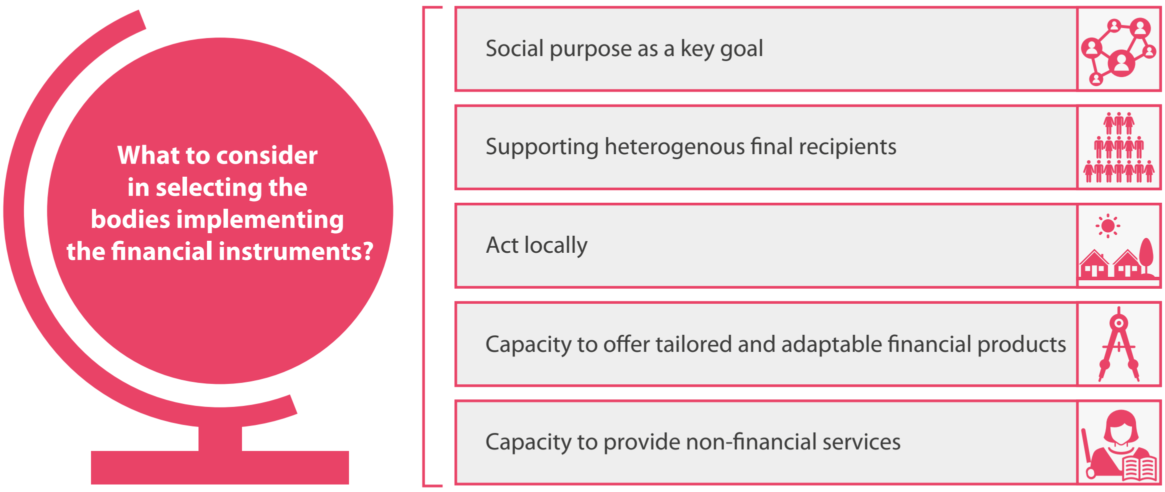
20 Next section 2.2 provides more information on the governance structure implemented through a holding fund. Moreover, examples on this governance option are described under sections 3.1.2, 3.2.1, and 3.3.1.

Box 2.1: What to consider in selecting the bodies implementing the financial instrument?

Moving from financial products for commercial purposes to social purposes implies bodies implementing the financial instrument accepting a higher degree of risk and lower returns, and sustaining long-term projects, typical of those related to social issues, by minimising the costs of running them. Therefore, when selecting the body implementing the financial instrument, various important aspects should be taken into consideration by ESF+ managing authorities:

- **Social purpose as a key goal.** The selected body implementing the financial instrument to operate under the ESF+ framework should promote investments that generate positive social outcomes and contribute to the social inclusion of the most disadvantaged groups. Therefore, bodies implementing the financial instruments should have the capacity to understand and share the social mission of the interventions financed by the ESF+ through financial instruments;
- **Supporting heterogenous final recipients.** Addressing the needs of ESF+ final recipients necessitates an understanding of their social needs, in addition to their financial needs. These social needs can vary substantially both across and within disadvantaged groups and are subject to a changing social environment and external factors;

Figure 2.2: The characteristics of the bodies implementing the financial instruments



Source: Own elaboration.

- **Act locally.** Transparency and mutual trust are key elements to achieve social goals, so local bodies implementing financial instruments are more likely to establish closer relationships with final recipients, which is a key aspect when working with disadvantaged individuals or social enterprises that generally provide social services at a local level. The bodies implementing financial instruments who act locally, know the clients and understand their needs better, while final recipients are expected to be more receptive to initiatives coming from a local institution. With greater knowledge of the local social environment, personal contact with the applicant and familiarity with individual situations and possibilities, they can increase the chance of funds being repaid;

- **Tailored and adaptable financial products.** The bodies implementing financial instruments should ensure a variety of financial products[21] adapted to different specific needs and the expectations of disadvantaged groups, including medium and long term finance for projects that may carry higher risks. When dealing with social enterprises, adaptability also implies that the bodies implementing financial instruments should not limit their focus to a specific investment stage (for instance, start-up phase) and should be ready to invest when the social enterprise is at a different stage (for instance, scaling-up phase);
- **Capacity to provide non-financial services.** Combining financial instruments with grants for financing, such as technical support or advisory services, can be particularly effective in achieving social goals. The bodies implementing financial instruments can therefore be called upon to provide supplementary technical, financial and managerial advice. Qualified expertise within the bodies implementing financial instruments may be needed for providing non-financial services tailored to the specific needs of supported disadvantaged groups.

The bodies implementing financial instruments can be banks and non-bank intermediaries. Banks include, for instance, commercial banks, credit unions, cooperative banks and savings banks. Normally, these do not provide finance to non-bankable or socially excluded targets as part of their usual commercial activities. Non-banks operate prevalently in markets with low financial service penetration and limited public support. They not only aim at developing commercial activities but also at providing finance to socially excluded targets. Non-bank intermediaries can include NGOs or foundations, specialised microfinance intermediaries (non-bank financial institutions) government bodies or agencies, and community development financial institutions.

The **set-up** phase starts by making the *governance structure operational,* by activating the decision-making process according to the roles and responsibilities of the different parties established in the funding agreement. A separate account for the financial instrument, or fiduciary accounts on behalf of the managing authority should be opened by the body implementing the financial instrument (or the body managing the holding fund), to ensure proper accounting and an audit trail (Art.59.9). After transferring the resources to the financial instrument as agreed upon under the funding agreement, the managing authority applies for the first interim payment (request of payment) for a maximum of 30% of the total amount of programme contributions committed to the financial instrument (Art. 92.2.a).

Moreover, under this phase, the *system for documentation, management and control,* as designated in the funding agreement is also made operational.

Under the **implementation** phase, final recipients, informed by body implementing financial instrument or the managing authority about the availability of the financial instrument and the requirements for accessing it, can submit their *application for financing*. Eligibility, risk and the returns of potential investments need to be assessed by the body implementing the financial instrument, together with their capacity to deliver positive impacts in line with the investment strategy. Once the application is approved, the body implementing the financial instrument and the final recipients enter into a contract governing the obligations of the parties, including, for example, the terms and conditions of the transaction, availability of documents proving the investments, and specific separate accounting. The *disbursement* of the financial instrument to the final recipients will take place after the stipulation of the contract.

21 More information on financial products is available in section 2.3 and in chapter 3.

During the implementation phase, the body implementing the financial instrument or the holding fund prepares the *request for each payment* by the managing authority as stipulated in the funding agreement (Art. 92(b)). This request includes declarations of the resources disbursed (or committed in the case of guarantees) and the management costs and fees (Art.68). Moreover, the phase encompasses the monitoring and reporting activities, as established in the funding agreement. The body implementing the financial instrument regularly reports to the managing authority (or to the holding fund, who in turn reports to the managing authority) on the support paid to final recipients (or resources committed as guarantees), management costs and fees, the value of investments and the results of internal controls and monitoring. On-the-spot management verifications (by the managing authority) and audits (by the audit authority) are limited to the level of bodies implementing the financial instrument and, in the context of guarantee funds, to the level of bodies delivering the underlying new loans (Art.81).

Finally, during this phase, *revolving resources* can be re-used to finance additional final recipients (Art. 62). Moreover, if conditions change (for instance, the economic situation, the market, or legislation) the ex-ante assessment and/ or the funding agreement, may need to be revised.

The fourth phase, the **winding-up**, concludes the financial instrument life cycle. It includes the execution of the *exit strategy* (i.e. recovery of the resources invested in final recipients) and the re-use of resources paid back before the end of the eligibility period. Financial instruments may remain operational after the withdrawal of resources attributable to the ESF+ or they can complete their life cycle and be terminated.

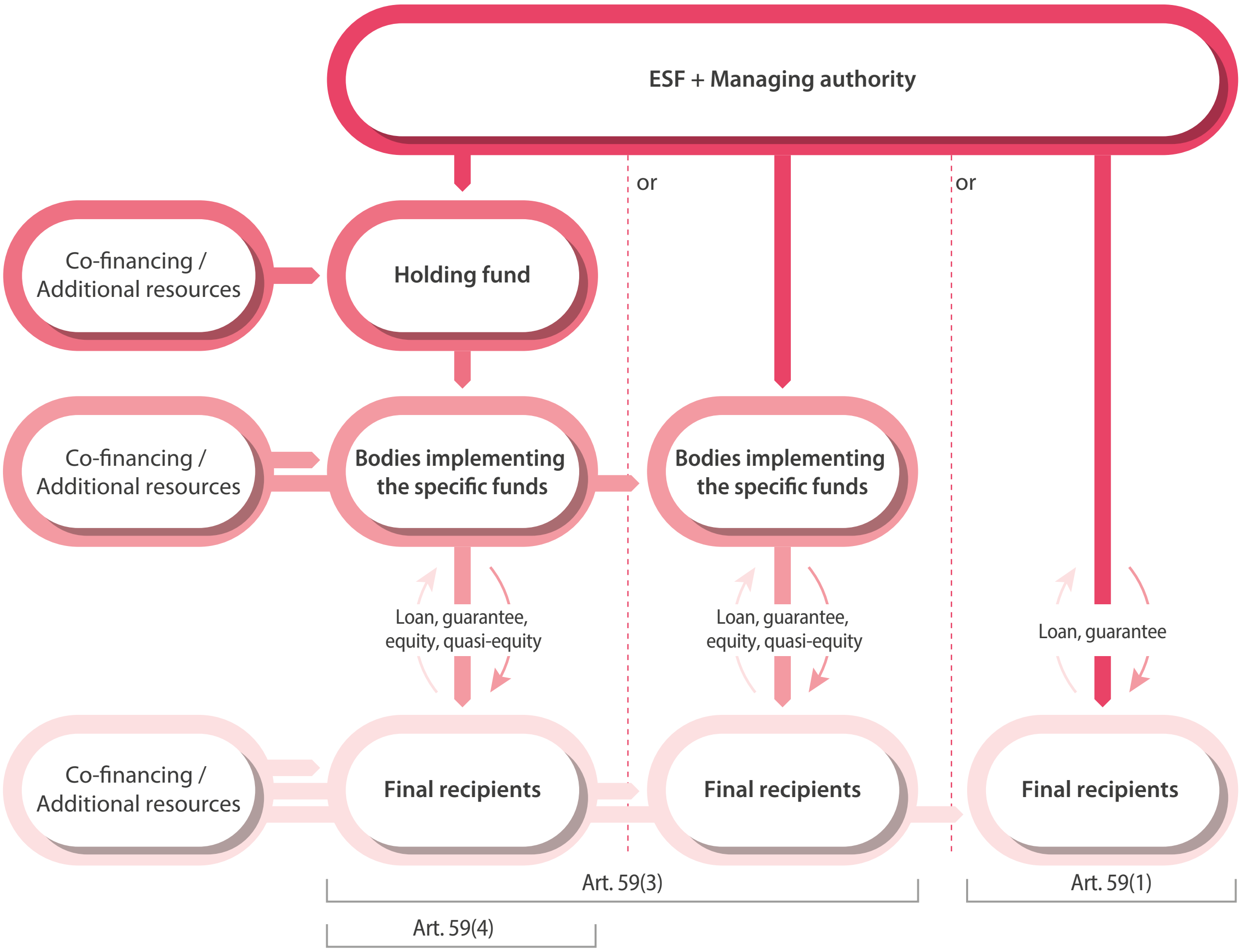
2.2 What governance option to apply?

To implement a financial instrument, the managing authority can choose from different options as per Art. 59 of the 2021-2027 CPR. The managing authority can:

- directly implement the financial instrument, but only providing guarantees or loans (Art. 59.1);
- directly award a contract for the implementation of the financial instrument to (Art. 59.3): the EIB; and international financial institutions in which a Member State is a shareholder; a publicly-owned bank or institution; other bodies falling under the scope of Article 12 of Directive 2014/24/EU22. Under this option, the managing authority has two alternatives:
  - the selected body directly manages and implements the specific funds;
  - the selected body manages and implements a holding fund and in turn may select further bodies to implement specific funds (Art. 59.4).

22 Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Directive 2004/18/EC Text with EEA relevance, available here.

Figure 2.3: Financial instrument governance options according to the 2021-2027 CPR



Source: Own elaboration based on Zalite Leva (2021), The regulatory framework for financial instruments – The new CPR, in fi-compass 'ESF+ financial instruments responding to social challenges in Europe', on-line event 2 December 2021, available here.

National co-financing of a programme may be provided in accordance with the fund-specific rules (Art. 59.8) either by the managing authority or at the level of the holding fund, at the level of specific funds, or at the level of investments in final recipients. When the national co-financing is provided at the level of investments in final recipients, the body implementing financial instruments shall keep documentary evidence demonstrating the eligibility of the underlying expenditure.

Finally, the managing authority directly implementing the financial instrument, or the body implementing the financial instrument, shall either keep separate accounts or maintain an accounting code for each priority.

Each governance option has different advantages:

- Setting up a holding fund can provide significant added value when there is no considerable in-house financial or fund management expertise within public sector organisations. However, because of the multi-level implementation structure, it also entails longer setup times and higher management costs and fees;
- Entrusting a financial intermediary with the implementation of the financial instrument provides the managing authority with a structure that is well-equipped and experienced in professionally managing funds and investments. It leverages the knowhow and expertise that public and private bodies possess of the local financial and legal environment;
- Direct management of the financial instrument allows for a simplified structure and procedures, including less burdensome monitoring and reporting activities, no requirement for a funding agreement, and quicker implementation. However, this option demands a high level of experience and expertise in managing the financial products that managing authorities may lack.

2.3 What financial product?

To support ESF+ final recipients, managing authorities have various options, with some being more suitable for specific final recipients and/or objectives, as discussed in more detail in the next section.

Financial instruments can support social projects/investments by providing the following financial products[23]:

- **Loans** are agreements that oblige the lender to make available to the borrower an agreed sum of money for an agreed period of time and under which the borrower is obliged to repay that amount within the agreed time. A sub-category of loan products is represented by **microcredits**[24] (i.e. up to EUR 25 000[25]), under which a further distinction includes **personal loans**, which only target individuals[26];
- Guarantees are written commitments to assume responsibility for all or part of a third party's debt or obligation or for the successful performance by that third party of its obligations if an event occurs which triggers said guarantee, such as a loan default;
- Equity is the provision of capital to a firm, invested directly or indirectly in return for total or partial ownership of that firm where the equity investor may assume some management control of the firm and may share in the firm's profits within the equity products. Quasi-equity is a type of financing that ranks between equity and debt, having a higher risk than senior debt and a lower risk than common equity. Quasi-equity investments can be structured as debt, which is typically unsecured and subordinated[27] and in some cases convertible into equity, or as preferred equity.

Moreover, managing authorities can also opt to **combine financial products with grants**[28]. Grants can enable financial instruments to support riskier components of ESF+ projects or cover the part of the investment cost that is unlikely to be repaid from project revenues or cost savings. Combining financial instruments with grants can also increase interest in the use of financial instruments, both for final recipients (for instance, when grants decrease the costs of accessing finance) and the bodies implementing the financial instrument (allowing them to enter new markets and attract new clients).

23 Definitions according to the 2021-2027 CPR (Art. 2(17)), according to which "'financial product' means equity or quasi-equity investments, loans and guarantees as defined in Article 2 of the Financial Regulation'. The Financial Regulation (Regulation 2018/1046) includes the definition of a loan under Art.2(40), guarantee under Art.2(34), equity under Art. 2(25) and quasi-equity under Art. 2(52). See also European Commission (2015), *Guidance for Member States on financial instruments – Glossary*, available here, and fi-compass (2015), *Financial instruments products – Loans, guarantees, equity and quasi-equity*, available here.

24 See also fi-compass (2016), *Financial instruments working with microfinance*, available here.

25 In the InvestEU programme, under the Social Investment and Skills window, the microcredit threshold has been doubled (EUR 50 000). See Commission Delegated Regulation (EU) 2021/1078 of 14 April 2021 supplementing Regulation (EU) 2021/523 of the European Parliament and of the Council by setting out the investment guidelines for the InvestEU Fund, available here.

26 See also fi-compass (2016), *Financial instruments working with personal loans*, available here.

27 See sections 2.3.1 and 2.3.3 for more information on unsecured loan and subordinated loan respectively.

28 More information on the combination of financial products with grants is provided in section 2.4. Moreover, practical examples are reported in sections 3.1.4, 3.2.4, and 3.3.4.

2.3.1 Loans

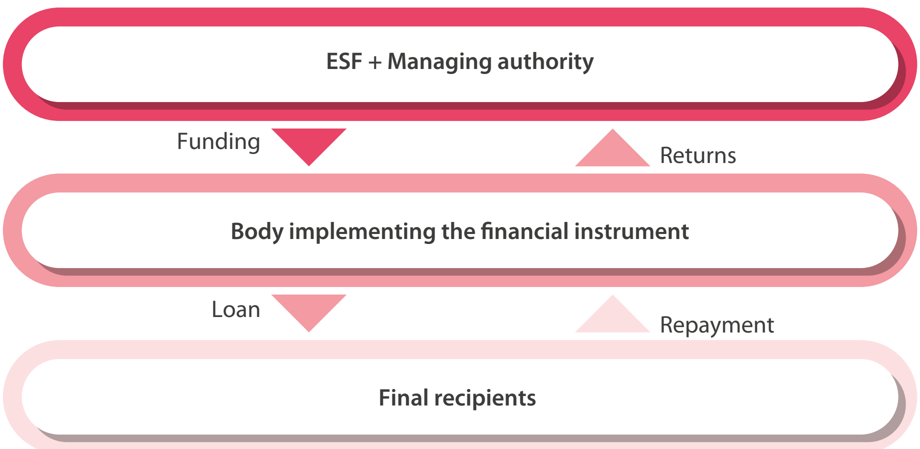
Loans are agreements that oblige the lender to give a sum of money (the principal) to the borrower in exchange for future repayment of the principal along with interest, within an agreed time frame. In general, the interest charged consists of the market rate plus a risk premium reflecting the likelihood of the lender receiving their money back. This risk premium encompasses credit risk which varies with the borrower's credit history and expected cash flow. The interest rate can be lowered by using interest rate subsidies financed by grants (see section 3.2.5). Risk completely ceases only once the loan is fully repaid, the maturity date. Therefore, the later the maturity date, the higher the risk premium.

The **leverage effect** for loans arises from the resources co-invested in addition to the ESF+. These can be public, such as those from a national or regional programme, and /or private, when, for instance, the body implementing the financial instrument contributes its own resources to provide additional loans. One way to encourage bodies implementing the financial instruments to contribute with their private finance to the ESF+ resources is to subsidise the interest rate applied by the body implementing the financial instrument with grants in order to lower it to the level of the interest rate applied on the loans covered by ESF+ resources (see section 3.2.5).

A loan can be **secured** when the borrower offers assets such as property, receivables, or investments as collateral to decrease the risk premium. These assets become the property of the lender if the borrower defaults (fails to repay the loan). The quality of the collateral backing the loan determines the risk of loss. Secured loans typically have lower interest rates than unsecured loans, which do not require collateral and are used for borrowers who do not own property or assets. For unsecured loans, the risk of loss is determined by the certainty of cash flow from the borrower. Lenders focus primarily on the credit rating, history and debt ratio of the borrowers.

Microcredits are loans up to EUR 25 000 designed to support enterprises, mainly microenterprises (businesses employing fewer than 10 people and with an annual turnover and balance sheet of less than EUR 2 million) or individuals (**personal loans**). These loans can be used to support a personal need, for instance, to improve job opportunities or living conditions. Typically, microcredits have relatively higher management costs and risks, resulting in higher interest rates. Consequently, not all financial intermediaries are willing to operate in microfinance markets.

Figure 2.4: Loan mechanism



Source: Own elaboration based on fi-compass (2015), Financial Instrument products – Loans, guarantees, equity and quasi-equity, available here.

Box 2.2: Pros and cons of loans[29]

The key advantage of loans is that they are **not particularly difficult to administer** (resulting in limited management costs/fees), and, since the lending mechanism is well understood, **the need for capacity building and the risk of misunderstanding is reduced**. Moreover, a defined repayment schedule makes **budgeting easier**. Finally, when loans support social enterprises or self-employment initiatives, the equity of the final recipient is preserved as there is **no claim on the ownership of the enterprise**.

However, funded products such as loans require more initial resources than unfunded products such as guarantees. Moreover, it can be difficult to establish the probability of default, especially when dealing with final recipients lacking any history, which is a typical characteristic of several ESF+ final recipients, such as migrants, unemployed individuals or young people. Finally, the benefit for the final recipient is almost entirely financial, as knowhow is not transferred.

2.3.2 Guarantees

The guarantee acts as a type of 'insurance policy' against non-payment. It supports access to finance by transferring or mitigating risks and therefore reducing the costs that final recipients may not be able or willing to pay. Under a guarantee scheme, the guarantor issues a guarantee for an agreed amount of debt in the event that the final recipient fails to repay the lender.

The guarantee is therefore particularly appropriate for individuals with no credit history or lack of collateral or for enterprises, such as social enterprises, with low expected financial returns.

Typically, the borrower pays the guarantor a premium as a fee, in addition to repaying the loan. These fees are contingent on the guarantee period, the risk factor, and the amount of the loan to be guaranteed. In the event of default by the borrower – in accordance with terms clearly defined in the contract – the guarantee fund will reimburse the lender. If there is no loan default, there is no cash outflow from the guarantee fund.

Each guarantee scheme should specify the risk-sharing formula, the timing and calculation of guarantee claim payments, responsibilities for collection against defaulting borrowers, what happens to funds recovered, the maximum exposure for individual loans, guarantee approval and issuance procedures as well as the fees.

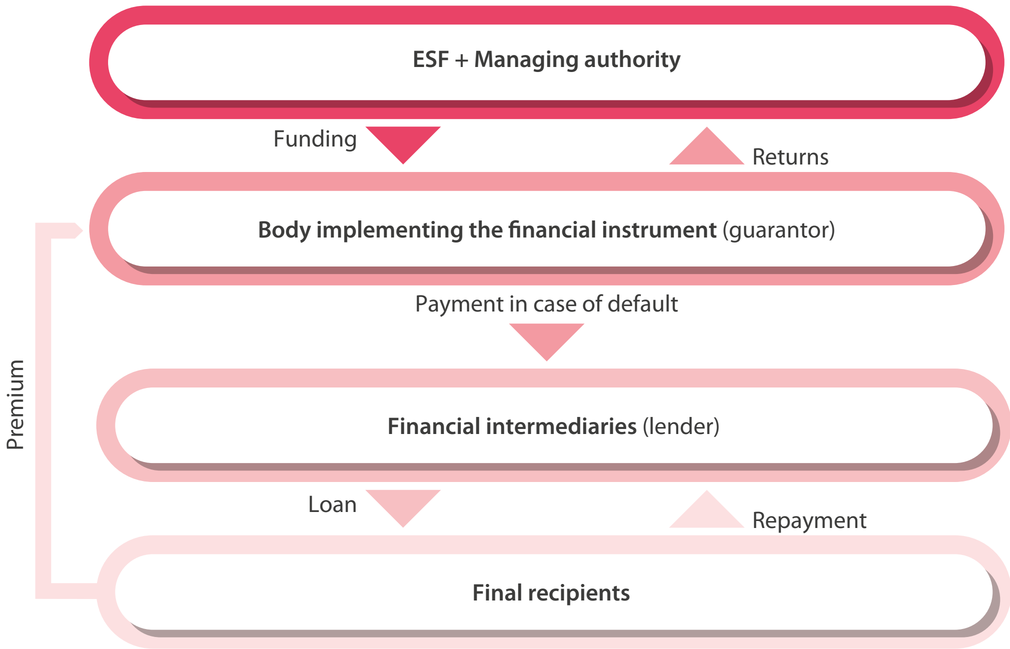
29 See sections 3.1.1, 3.2.1 and 3.3.1 for practical examples on how to implement a loan scheme.

A guarantee can be **uncapped** or **capped**. In the first case, it provides protection against losses and full reimbursement of each loan in a new portfolio, within a pre-determined guarantee rate. Although the lender bears some risk, the uncapped guarantee reduces the capital required for a lender. In the second case, it indemnifies the lender up to a pre-defined percentage or amount of the loan and for the portfolio in default. The capped guarantee, therefore, requires more capital for a lender. A specific guarantee scheme is the **first loss default/ portfolio guarantee** where the guarantor covers the losses of a loan portfolio until the cap is reached. Therefore, the lender is exposed to losses over and above the capped amount of the guarantee, rather than both the lender and the guarantor sharing the risks of every default in proportion.

Finally, a guarantee scheme can also include a **counter-guarantee**, which allows a guarantor to seek reimbursement if it has to pay a claim under a guarantee they issued for a loan in default.

The **leverage effect** in a guarantee scheme is the ratio between the resources allocated by the lender for the loans and the amount of ESF+ resources allocated to cover the expected losses through the guarantee.

Figure 2.5: Guarantee mechanism



Source: Own elaboration based on fi-compass (2015), Financial Instrument products – Loans, guarantees, equity and quasi-equity, available here.

Box 2.3: Pros and cons of guarantees[30]

Guarantees have two main advantages:

- by mitigating losses for the lender in the event of default, they decrease the investment risk and subsequently **increase the willingness of the lender to finance riskier projects or more final recipients**;
- by lowering the cost of financing (lower or no guarantee fees, lower or no collateral requirements as well as lower risk premiums), **the financial sustainability of final recipients' projects increases**.

Moreover, unfunded products such as guarantees require **fewer initial ESF+ financial resources** than funded products such as loans. As a consequence, since ESF+ contributions cover only the defaulted loans, there is **a high leverage effect**. Finally, as in the case of loans, guarantees can **preserve the equity of final recipients** as there is normally no claim on the ownership of the enterprise.

However, being a risk reserve for the lender, the guarantee does not directly provide liquidity to final recipients. Moreover, there is no transfer of business expertise to final recipients. Finally, estimating the appropriate cap, or maximum limit, can be challenging.

2.3.3 Equity and quasi-equity

In the equity mechanism, resources are committed by a managing authority to an equity fund managed by an investor, i.e. a body implementing the financial instrument (or equity fund manager) who in turn identifies and invests the resources, alongside funds committed by other investors, in target final recipients. In return for the investment, the equity fund receives a share of the ownership of the company. Depending on the size of the investment, the investor can play a hands-on role in running the enterprise (active investor) or take little part in the management of the enterprise (passive investor). After a period of growth and development (typically four to ten years), the investor will seek to exit the company by selling its shares, securing a financial return on the equity investment and enabling the company to further develop its economic and financial viability.

Equity instruments are typically used under the ERDF[31] generally by enterprises in high-tech industries (such as biotech, ICT, high-tech energy, nanotechnology, applied mechanics and robotics) or for innovative products or services with expensive R&D projects. However, within the ESF+, equity instruments can be used to support social enterprises helping to deliver high-quality services of general interest to disadvantaged people.

The types of equity investment are often described by the relevant development stages of an enterprise, starting with pre-seed, then the early stage which includes seed and startup, followed by growth and expansion. Investment in newly established enterprises can finance the study and development of a concept or prototype. Mature enterprises with proven business models may need equity investment to fund new projects, including the penetration of new markets.

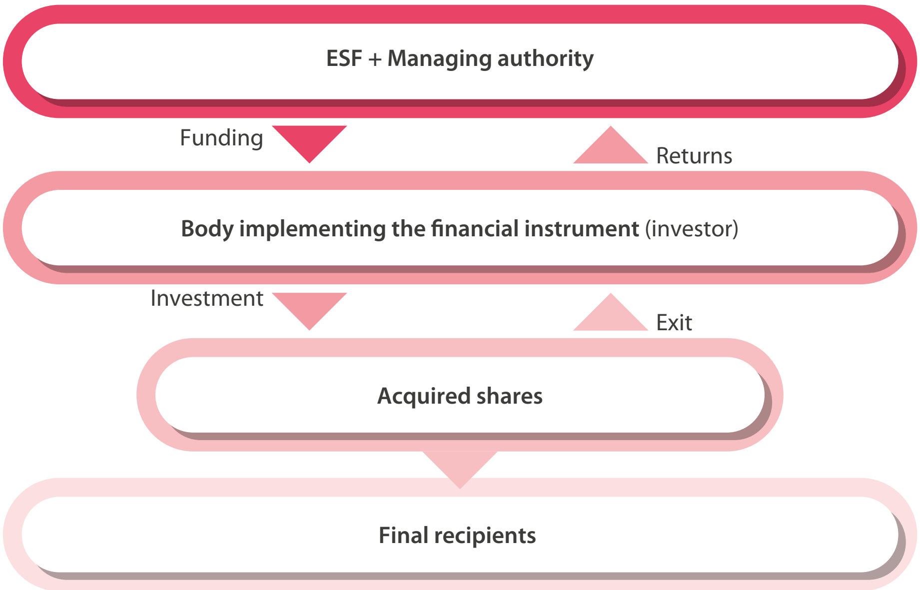
A particular category of equity instruments is represented by **quasi-equity** (also known as mezzanine capital or mezzanine finance), which combines features of both equity and debt products. Quasi-equity instruments are classified as closer to equity or debt capital according to the level of ownership acquired and the exposure to loss in the event of insolvency[32]. The risk profile changes with the duration of capital commitment and the remuneration conditions.

30 See sections 3.1.2, 3.2.2 and 3.3.2 for practical examples on how to implement a guarantee scheme.
31 See fi-compass (2022), ERDF Equity financial instruments, available here.
32 Additional detail available in fi-compass (2022), *Quasi-equity finance for SMEs A fi-compass model financial instrument*, available here. Please see section 3.1.3 for an example of a quasi-equity financial instrument.

Different examples of quasi-equity include:

- **Subordinated loans**, which have a lower repayment priority than normal (senior) loans. In the event of the company's default or liquidation, subordinated loans are repaid only after senior loans are fully settled. Due to the higher risk involved, subordinated loans usually have higher interest rates and often do not require collateral;
- **Convertible bonds** are debt where the initial investment is structured as a debt claim, earning interest. At the investor's discretion, the debt can be converted into equity at a predetermined conversion rate. A convertible bond is essentially a bond combined with a share option where the holder may exchange the bond for a predetermined number of shares at a predetermined price. Because convertibles can be changed into shares they have lower interest rates[33];
- **Preferred stocks** are stocks that entitle the holder to a fixedrate dividend, paid before any dividend is distributed to holders of ordinary shares. Holders of preferred stock also rank higher than ordinary shareholders in receiving proceeds from the liquidation of assets if a company is wound up[34].

Figure 2.6: Equity mechanism



Source: Own elaboration based on fi-compass (2015), Financial Instrument products – Loans, guarantees, equity and quasi-equity, available here.

33 Example: An investor provides a loan to a company by purchasing a convertible bond. Over time, the investor has the option to exchange the loan for shares in the company. If the company's performance improves, the investor may choose to convert the bond into shares, becoming a shareholder instead of simply collecting interest and the repayment of the principal.

34 Example: A shareholder owns preferred stock in a company and receives regular dividends at a fixed rate, even if common shareholders receive none. If the company is liquidated, preferred shareholders will be paid from any remaining assets after the company's debts are settled, but before any payments are made to common shareholders.

Box 2.4: Pros and cons of equity[35]

Equity instruments have **higher potential returns** compared to debt instruments. Moreover, as the investors enter into enterprise ownership, they play an **active role in project management** and can influence the configuration and mission of the company. As a consequence, the final recipient may benefit from the investor's **management expertise**. Moreover, equity instruments can also stimulate equity investment from the private sector in riskier areas not previously serviced.

On the other hand, equity can be a time-consuming and cost-intensive investment, more difficult to administer compared to debt instruments (high set-up and operational costs). From the investors' side, there is also a higher potential insolvency risk for the entire invested capital, if the enterprise is unable to repay the investment due to lower profits or lower asset appreciation than expected. Moreover, since equity is repaid through an enterprise's ongoing profits and asset appreciation, it can take a long time for investors to recover their investment. Therefore, equity is not suitable for short-term financial needs, as an enterprise usually cannot repay the investment in the short term. Finally, compared to debt instruments, equity can be less attractive to final recipients due to the obligation to yield control.

2.4 Combination with grants

Within the ESF+ framework, combination is particularly useful as it contributes to the social benefit for final recipients excluded from financial support[36]. In particular, as social challenges can vary considerably among the typical target groups of the ESF+ support, the combination of grants and financial instruments allows for the design of flexible financial solutions tailored to final recipients' needs and expectations. This approach also allows for the calibration of repayable forms of support in line with expected revenues or savings. Moreover, in the 2021-2027 programming period, ESF+ managing authorities can exploit new flexibilities introduced in the CPR (see box below for details).

Financial instruments and grants can be combined into one or two operations. When combined into **one single operation**, the managing authority entrusts directly or selects one or more body implementing the combined financial instrument who is able and willing to manage the financial instruments combined with grants. A single funding agreement is then signed with each body implementing the combined financial instrument covering both the financial instrument and the grant component. Final recipients submit a single application for financing to the body implementing the combined financial instrument.

35 See sections 3.1.3, 3.2.3 and 3.3.3 for practical examples on how to implement an equity scheme.

36 fi-compass (2021), *Combination of financial instruments and grants under shared management funds in the 2021-2027 programming period*, available here. See also fi-compass (2021), *fi-compass Knowledge Hub – Combination of financial instruments with grants – Notes of workshop*, available here.

The combination in **two separate operations** can be at the final recipient level but not at the financial instrument level. The key characteristic of the combination in two separate operations is that eligibility and payment rules for the financial product component and the grant component remain distinct. Combinations where the vast majority of the projects require an amount of grants higher than the investments supported by the financial product will only be possible in two operations. Separate operations do not prevent both forms of support from being delivered through the same body. Finally, some of the 2014-2020 combinations under two sets of rules can be implemented under one financial instrument in the 2021-2027 period. This can continue for investments where the grant does not fulfil conditions for one operation such as where the grants are delivered by the managing authority. Also, any combination with other Union forms of support at the level of the investment must be undertaken in two separate operations, particularly in the case of support through a loan guaranteed under InvestEU and a grant from shared management funds.

Box 2.5: The new flexibilities for combination under the 2021-2027 CPR

The new flexibilities introduced in the 2021-2027 CPR extend the 2014-2020 combination options. First, **the body implementing the financial instrument can now disburse the combined support directly to the final recipients**, rather than solely on behalf of the final recipients, which is a key advantage. Moreover, the **new CPR also simplifies and expands options to combine financial instruments and grants into a single operation**. For instance, a combination can support projects that do not generate sufficient returns or savings to be economically viable. The new CPR also retains the option to combine financial instruments and grants under two separate operations.

Furthermore, under the 2021-2027 CPR, **combined financial instruments and grants in one operation are implemented solely under the regulatory framework for financial instruments**. This provides a number of advantages in terms of simpler and faster management as well as reducing the burden on managing authorities[37]. Firstly, **payment to final recipients is possible 'up front'**, in advance of expenditure, if the managing authority so chooses. Secondly, **national co-financing of a programme must be demonstrated at the level of the combined instrument**, without distinguishing between the grant and financial instrument. This gives managing authorities greater flexibility to deploy resources across a programme, as they can take advantage of flexibilities under article 59(8) of the CPR. For example, national co-financing could be provided at the level of specific funds or at the level of investments in final recipients. Moreover, audit, management verifications and controls and reporting are at the level of the combined operation. Therefore, **audit requirements focus on the beneficiary level** - i.e. the body implementing the fund, the fund of funds, or the managing authority with direct implementation - and exclude the final recipient level. For a guarantee instrument, this scrutiny extends to the bodies responsible for granting the underlying loans. In general, final recipients should not be audited in relation to the financial instrument.

37 fi-compass (2021), *fi-compass Knowledge Hub – Combination of financial instruments with grants – Notes of workshop*, available here.

The four main types of combinations that can be used under the ESF+ include:

- The combination of financial instruments and **grants for interest rate and guarantee fee subsidies**. In this case, grants can reduce the cost of accessing finance while ensuring that the bodies implementing the financial instrument receive acceptable interest remuneration. Reducing the cost of finance through interest rate subsidies can be particularly effective in the area of education;
- The combination of financial instruments and grants for **technical support**. Technical support can support self-employment initiatives. It can, for instance, increase the skills to start and manage a business, by providing, for instance, ad-hoc training, guidance, and advisory services, which contribute to an improvement in the final recipients' managerial capacities;
- The combination of financial instruments and **performance-based grants**. This type of combination is used to incentivise more project promoters to submit investment projects with a higher policy impact. Performance-based grants can be particularly suitable for supporting social enterprises in achieving social goals and increasing the social impact of their activities. Performance-based grants can take different forms when performance objectives are met, including: capital rebates, when part of the loan is converted into a grant, so the final recipient benefits from a reduction in capital due and repays the outstanding loan following a revised amortisation plan[38]; recoverable grants, when part of a grant is converted into a loan; and convertible grants, when part of the grant is converted into equity, thus increasing the shares held by the financial instrument;
- The combination of financial instruments and **capital grants**. In this type of combination, a capital grant can cover the non-revenue generating/ cost-saving part of the investment. This combination can finance investments with financial viability gaps. Capital grants could be also used to lower the burden of the repayable part on the project cash flows or to decrease the final costs of the supported investment to be financed by users. For instance, to support self-employment and entrepreneurship, the capital grant can be used to purchase equipment and vehicles, although ESF can only be used in case where such purchase is necessary for achieving the objective of the operation, or those items are fully depreciated during the project lifetime, or the purchase of those items is the most economic option[39].

38 On this type of combination, see the example under section 3.3.4.
39 As per eligibility rules outlined in Article 16(1.b) of the Regulation 2021/1057 establishing the European Social Fund Plus.

Box 2.6: Pros and cons of combining financial instruments with grants[40]

Other than allowing for more **flexible financial solutions tailored to final recipients' needs**, combining financial instruments with grants can also contribute to:

- **higher viability and sustainability of projects**, essential for the effective use and reimbursement of financial resources;
- **the social impact** of projects, stimulating, for instance, social enterprises and self-employment initiatives to be more impact-driven and improve their capacity to monitor and measure their contributions to social benefits;
- better-structured projects and thus **improved attractiveness to private investors**;
- incentivising **financial intermediaries to enter new or riskier markets**.

However, there are also challenging aspects when the combination is implemented within the ESF+ framework, including technical difficulties encountered by managing authorities or implementing bodies or a lack of capacity and experience in managing the grant component by financial intermediaries. Generally, the combination appears to pose less of a burden during implementation, as the major issues are tackled in the design phase[41]. To limit these challenges, ESF+ managing authorities should:

- **Carefully assess, in the ex-ante assessment, the need and the scope for a grant component** directly linked and necessary for the financial instrument. The ex-ante assessment should analyse why a combination is needed, the possible type of combination, and the related grant intensity;
- **Ensure flexibility to adapt the combination to market conditions and final recipients' needs and expectations**, while at the same time, better developing and tailoring the design of the financial product;
- **Carefully select the bodies implementing the combined support.** Additionally, managing authorities might consider training and awareness-raising amongst potential bodies implementing the combined support to address any concerns regarding the implementation of grants. Moreover, the selection process of the bodies implementing the combined support and the funding agreement should ensure that the benefit of the financial instrument and its grant component is transferred to the final recipient;
- **Keep administration of the grant as simple as possible**, specifying, for example, that the grant shall be given as a fixed lump sum or percentage of the investment/financing (as for capital grants or rebates), or to reduce the interest rate to a specific level (as in case of interest rate subsidies). Any calculation methodology of the grant elements should be clearly determined and described in the funding agreement;
- **Combine grants and financial instruments in one operation**, if possible, as this allows for simpler procedures. The bodies implementing a combined financial instrument in one operation shall be selected based on a single procedure, simultaneously covering both the grant and the financial product components. This is a significant difference with the option of combining financial instruments and grants in two separate operations, which requires two distinct selection procedures.

40 See sections 3.1.4, 3.2.4 and 3.3.4 for practical examples on how to combine financial instruments with grants.

41 According to the *fi-compass survey on ESF financial instruments for 2014-2020, see fi-compass (2019), Survey on financial instruments under the European Social Fund (ESF) – Reflections at present and ideas for future*, available here.

2.5 The InvestEU programme and the Member State compartment

ESF+ managing authorities can also exploit opportunities offered by financial instruments managed at the EU level under the **InvestEU programme**[42]. The InvestEU programme in the 2021-2027 programming period brings many different forms of EU financing under one umbrella, making funding for investment projects simpler, more efficient and more flexible. It comprises three building blocks:

- the **InvestEU Fund**, providing an EU guarantee to support the financing of and investment in internal EU policies grouped in 4 main policy areas – sustainable infrastructure, research innovation and digitalisation, SMEs and social investment and skills;
- the **InvestEU Advisory Hub**, supporting project development, access to finance and capacity-building assistance;
- the **InvestEU Portal**, giving visibility to projects seeking finance and information on investment opportunities.

The InvestEU Fund provides a guarantee to leverage substantial private and public long-term funds to contribute to Europe's economic and social recovery by aligning investors with the EU policy priorities. The EU provides a EUR 26.2 billion guarantee to cover the risk of investments which is expected to attract private and public investments and mobilise an additional EUR 372 billion. The guarantee is governed by indirect management with specific financial institutions, such as national promotional banks, the European Investment Fund (EIF), and the European Investment Bank (EIB), which have concluded agreements with the European Commission and are referred to as implementing partners. The implementing partners of the InvestEU Fund are among others, the European Bank for Reconstruction and Development (EBRD), the Council of Europe Development Bank (CEB) or the Nordic Investment Bank (NIB), together with the European Investment Bank (EIB) and the European Investment Fund (EIF). The EIB and EIF are active in each member state and manage about 75% of the InvestEU guarantee.

2.5.1 Setting-up a Member State compartment

The InvestEU programme supports investments under two compartments:

- An **EU compartment**, focussing mainly on EU policy priorities and investments with EU added value;
- A **Member State compartment**, focussing mainly on specific national priorities. The InvestEU programme also provides for an opportunity to Member States to add funds to the EU guarantee's provisioning by voluntarily channelling a part of their Cohesion Policy Funds or of their RRF funds to the Member States compartment for each of the policy areas mentioned above. For example, an interested ESF+ managing authority in a given Member State have the opportunity **to contribute a portion of their ESF+ funds to the InvestEU Fund** by setting up a "Member State compartment" to support social investment and skills in line with their policy objectives identified under shared management;

  For the Member State compartment to be activated, the EU country needs first to indicate their intention in a programming document (a partnership agreement and/or a programme amendment). At the beginning of the programming period, the Member States can choose to contribute up to 2% of their shared management fund allocation via their Partnership Agreements (Art. 14 of the CPR[43] and Art. 9-10 in the InvestEU regulation[44]).

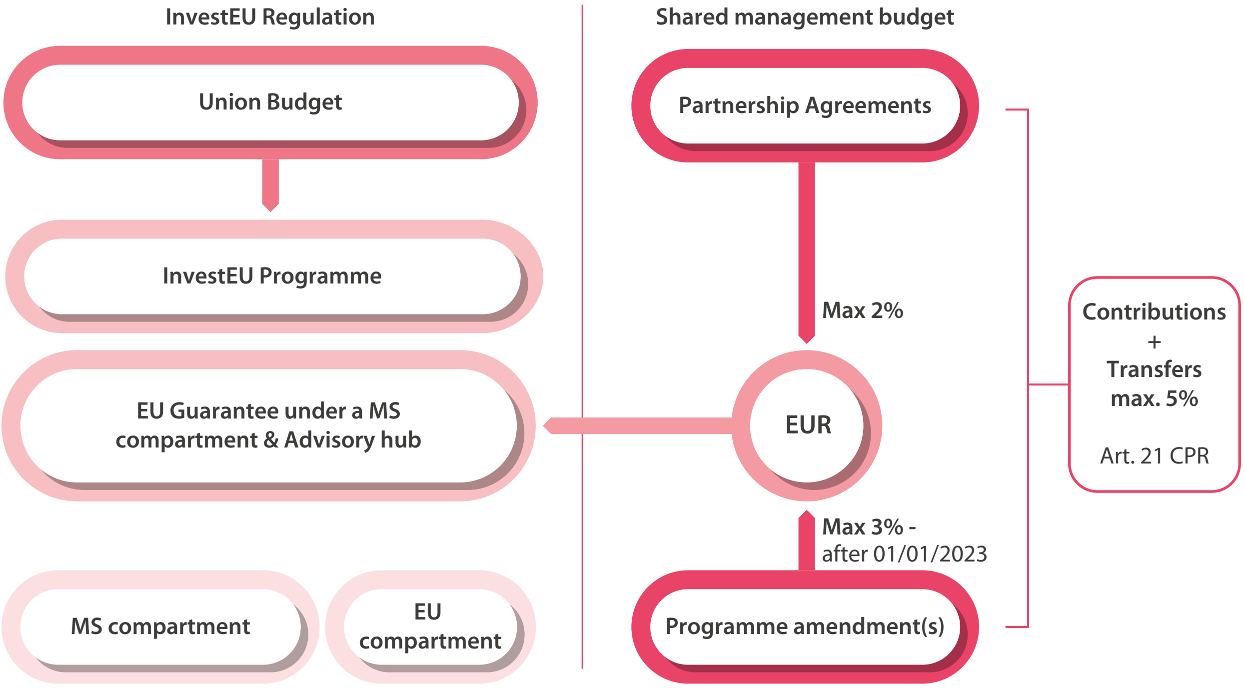
42 Summary of the InvestEU programme, including regulation, available here. Additional information on budget and performance available here.

43 Regulation (EU) 2021/1060 of the European Parliament and of the Council of 24 June 2021 laying down common provisions on the European Regional Development Fund, the European Social Fund Plus, the Cohesion Fund, the Just Transition Fund and the European Maritime, Fisheries and Aquaculture Fund and financial rules for those and for the Asylum, Migration and Integration Fund, the Internal Security Fund and the Instrument for Financial Support for Border Management and Visa Policy.

44 Regulation (EU) 2021/523 of the European Parliament and of the Council of 24 March 2021 establishing the InvestEU Programme and amending Regulation (EU) 2015/1017.

After 1 January 2023, Member States may further allocate an amount of up to 3% of the initial national allocation through one or more programme amendment requests. The Commission must then sign a 'contribution agreement' with the EU country concerned. This document sets out details of the financing and implementation, including the Member State strategy (products used, the targeted multiplier, etc.), the implementing partners proposed by the national authorities and possible combinations with the EU compartment. **With this voluntary contribution, EU countries can leverage the high credit rating of the EU guarantee, providing national and regional investments with greater firepower while cutting red tape.**

Figure 2.7: The Member State compartment under the InvestEU programme



Source: Lagarre V. and Kerpel-Fronius A. (2021), InvestEU: Social Investment Skills Window and Member State Component, fi-compass, presented at the 'ESF+ financial instruments responding to social challenges in Europe' event, 2 December 2021, available here.

Under the Member State compartment, loans, guarantees or equity investments can be offered as a complement to other public and private investments. More specifically, managing authorities can implement[45]:

- **An existing financial product or an advisory initiative designed for the EU compartment**, ring-fenced for the contributing Member State(s) or region(s). In practice, products for the EU Compartment are designed by the EIB Group and other Implementing partners and regularly discussed with Commission services. Examples of existing InvestEU products that might be of interest to ESF+ managing authorities are provided in the following section;
- **A product combining InvestEU support from the Member State Compartment and the EU Compartment.** This means that the EU guarantee backing the operations will include financing from the EU and the Member State Compartment;
- **A tailor-made financial product** to address specific needs and specific final recipients of the originating Member State or region.

2.5.2 Examples of InvestEU products under the Social Investment and Skills window

Among the four 'windows' of the InvestEU programme, **the "Social Investment and Skills window" (SIS window)** is of particular importance for ESF+ managing authorities[46]. The SIS window has a budget of EUR 2.8 billion of the EU guarantee and aims to deliver on the principles of the European Pillar of Social Rights by supporting: microfinance and social enterprises; social impact and innovation; education, training and skills; social infrastructure and services (including health and educational infrastructure, and social and student housing).

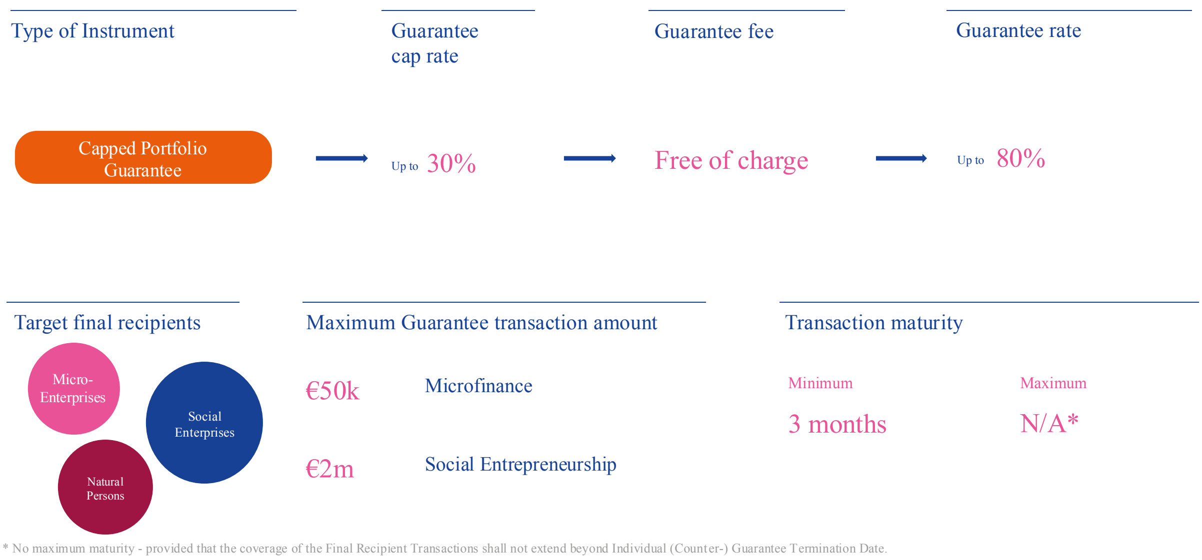
In particular, actions under the SIS window aim to reduce inequalities (including gender disparities) and enhance resilience and inclusiveness through the promotion of employment including entrepreneurship and self-employment, social enterprises and social economy as well as innovation, social inclusion, improving citizens' health, well-being and overall quality of life, and supporting a just transition to a low carbon economy. The SIS window targets investments in social enterprises, microfinance, training, social housing, social innovation, integration of migrants, and other sectors within the social sphere. Projects may also target education, training, and health and long-term care, amongst other related themes.

Examples of SIS window InvestEU financial products that could be of interest to ESF+ managing authorities in the context of a potential contribution to the Member State compartment include the following products implemented by the EIF:

- The **Microfinance and Social Entrepreneurship Portfolio Guarantee Product** aims to enhance access to finance for micro- and social enterprises (including the self-employed), thus supporting the development of a nascent market for inclusive and social finance. It is offered to financial intermediaries by the EIF only in the form of a capped (counter-) guarantee. The rate is up to 80% with respect to each loan transaction and the cap is set at the level of the expected loss, but not exceeding 30% of the loan portfolio. Eligible financial intermediaries are banks, non-banks, credit cooperatives, and leasing companies;

45 Lagarre V. and Kerpel-Fronius A. (2021), *InvestEU: Social Investment Skills Window and Member State Component*, fi-compass, presented at the 'ESF+ financial instruments responding to social challenges in Europe' event, 2 December 2021, available here.
46 The other 'windows' are: SMEs; Sustainable infrastructure; and Research, innovation and digitalisation.

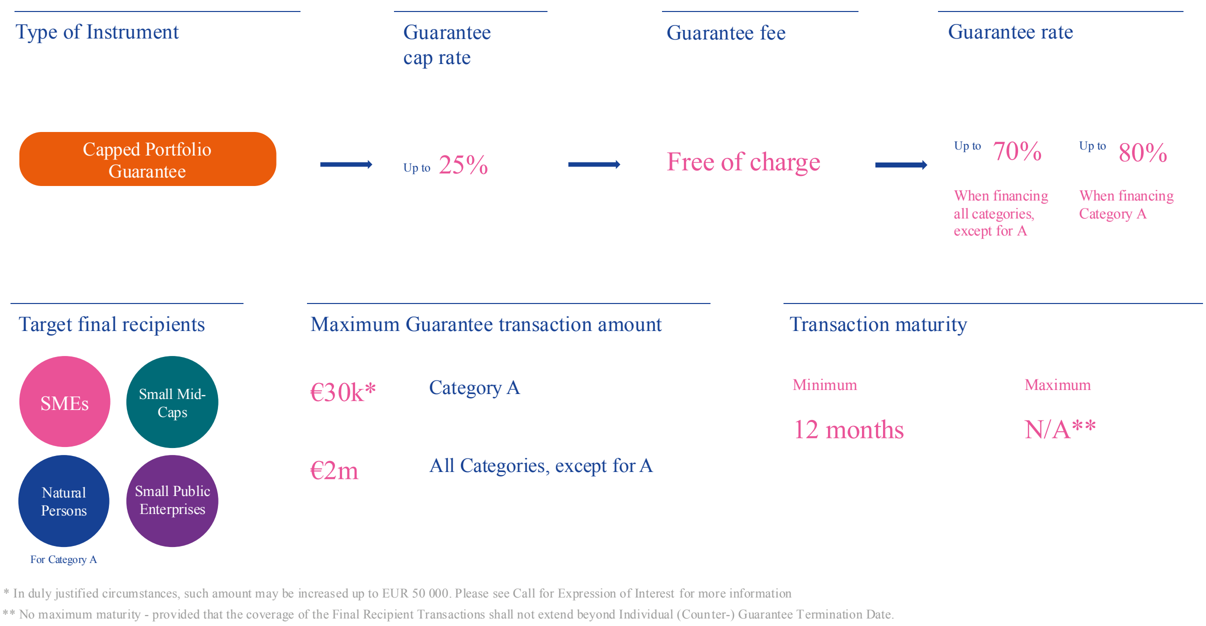
Figure 2.8: The Microfinance and Social Entrepreneurship Portfolio Guarantee Product



Source: EIF's InvestEU Portfolio Guarantee Products, available here.

- **The Skills and Education Portfolio Guarantee Product** supports investments in skills, education and training. Eligible financial intermediaries are those providing financing to students and learners, entities investing in upskilling their workforce, entities supplying education and training and entities supplying services ancillary to education. The product has a cap rate of up to 25% of the loan portfolio and 80% with respect to each loan transaction for individuals (students and learners, i.e. category A) and 70% with respect to each loan transaction for SMEs, small mid-caps or small public enterprises (i.e. categories B, C and D);

Figure 2.9: The Skills and Education Portfolio Guarantee Product



Source: EIF's InvestEU Portfolio Guarantee Products, available here.

- The **Capacity Building Investment Product** aims to enhance the institutional capacity of financial intermediaries that are not yet sustainable or that require risk capital to sustain their growth and development within the spheres of microfinance, social entrepreneurship or skills and education. Under the Capacity Building Investment Product, the EIF supports dedicated investments in selected financial intermediaries primarily through subordinated loans for the following purposes: organisational development and expansion of the financial Intermediary, including branch expansion, scaling-up or investment in IT infrastructure (e.g. mobile banking, etc.); investment in human resources such as recruitment and staff training; operational and institutional capabilities contributing to the sustainability of the financial intermediary (including greenfield institutions), including, inter alia, investments in working capital and in improving the strategic/governance capabilities of the financial intermediary in order to maintain a sustainable business with a social performance focus; institutional capacity building to increase the debt capacity of financial intermediaries while maintaining a balanced socio-commercial profile;
- Under InvestEU, the EIF is in charge of deploying EUR 6.5 billion in equity across various policy areas, grouped into Thematic Strategies and Horizontal Priorities. Under Thematic Strategies, the most relevant for social purposes is the **equity product for "Social Impact"**[47]. EIF provides equity investments and co-investments to, or alongside, funds in the areas of venture capital, private equity, and private credit. This includes fund-of-funds, cross-over funds, (co-) investment schemes, special purpose vehicles in various forms that undertake long-term risk capital investments in the form of equity, preferred equity, hybrid debt-equity instruments, tailor-made debt financing, other types of mezzanine financing, Social Outcomes Contracting (SOC) investment schemes. Supported financial intermediaries may pursue generalist, specialised or mixed investment strategies, but must invest in a least one of the following areas: social entrepreneurship; impact-driven enterprises and investments in SOCs supporting social sector organisations; skills and education. Regarding horizontal policy priorities, the EIF aims to foster the economic **empowerment of women** and increase their participation in the fields of venture capital and private equity. Financial intermediaries contribute to this policy priority if they comply with at least one of the InvestEU's gender criteria[48].

In addition to the possibility of contributing shared management funds to the implementation of existing InvestEU financial products, Member States may also contribute resources to the implementation of the existing InvestEU **advisory initiatives**. An example of a successful advisory initiative under the SIS window of InvestEU is the **Social Inclusive Finance Technical Assistance (SIFTA)**, implemented by the EIB. SIFTA provides targeted capacity-building services for microfinance and social enterprise finance providers in the form of tailored training, workshops, peer-to-peer exchanges and study visits on a wide range of topics related to financing micro and social enterprises. It also offers rating, assessment and evaluation services to such providers[49].

Overall, contributing to a Member State Compartment of InvestEU offers **several benefits** for the managing authorities. These include the ability to tackle national priorities **using ready-made InvestEU products, ring-fenced** for the contributing Member State(s) or region(s), **cutting the administrative burden**, gaining **significant leverage, avoiding the need for national co-financing**, and benefiting from **simplified State Aid rules**[50].

47 Additional information on the InvestEU equity product "Social Impact" is available here. Please also see section 2.5.1 for detail on how a managing authority can set-up the Member State compartment to access and use InvestEU financial products.

48 A financial intermediary is considered to adhere to the gender criteria if it satisfies at least one of the following: its management team is composed of at least one-third female partners; or its senior investment team provides for at least 40% female representation; or at least 40% female representation is provided in its investment committee.

49 More information on SIFTA is available here. Please also see section 2.5.1 for detail on how a managing authority can set-up the Member State compartment to access and use InvestEU financial products.

50 More information on the InvestEU Member State compartment is available here.

03 The specificity of ESF+ financial instruments

This chapter provides an overview of the most appropriate financial instruments by policy area (employment, education, and social inclusion). It also offers an indication of the current resources allocated by ESF+ managing authorities for the 2021-2027 programming period, both by SO and financial product. Moreover, specific examples (mainly from the 2014-2020 programming period) per each policy area and financial product are proposed to guide and inspire ESF+ managing authorities who intend to set up and implement financial instruments to address social challenges.

3.1 Financial instruments for employment

Financial instruments are particularly appropriate for improving job opportunities and contributing to self-employment in specific target groups such as the long-term unemployed, migrants, women, people over 50, and young people, who have a hard time finding a job, but are willing to run an entrepreneurial activity.

In the 2014-2020 programming period, most of the financial instruments supported by the ESF addressed employment. Approximately EUR 354 million, accounting for more than half of the overall ESF amount for financial instruments (EUR 629 million), was committed to the Thematic Objective (TO) 8 'Promoting sustainable and quality employment and supporting labour mobility'[51].

In the 2021-2027 programming period, the proportion of resources allocated to financial instruments for employment purposes is significant too. Out of the ESF+ EUR 682 million allocated to financial instruments, 79% (EUR 539 million) is dedicated to employment[52]. Out of this EUR 539 million (see table below):

- 94% is for SO 4.1 'Access to employment and activation measures for all jobseekers';
- Nearly 2.4% for SO 4.3 'Promote gender-balanced labour market participation';
- Nearly 3.7% for SO 4.4 'Promote the adaptation to change by workers';
- No allocation is foreseen for SO 4.2 'Modernise labour market institutions and services', as this SO mainly targets public employment services by promoting actions such as training staff in institutions operating on the labour market at national, regional and local levels, fostering cooperation and partnership between public bodies, or developing better information and communication systems at national level;
- Most of the allocated resources (nearly 69%) are for loan products, 8.9% for guarantees (foreseen only under SO 4.1), and 2% for equity and quasi-equity (foreseen only under SO 4.4); around 20.5% is for grants combined within a financial instrument operation.

51 European Commission (2023), *Financial instruments under the European Structural and Investment Funds - Summaries of the data on the progress made in financing and implementing the financial instruments for the programming period 2014-2020 in accordance with Article 46 of Regulation (EU) No 1303/2013 of the European Parliament and of the Council - Situation as of 31 December 2022*, available here.

52 Based on Cohesion Data portal, available here.

Table 3.1: 2021-2027 allocation to financial instruments for employment by SO and financial product

SO	Allocation (EUR million)				
	Total	Loan	Guarantee	Equity or quasi-equity	Grants within a financial instrument operation
SO 4.1 Access to employment and activation measures for all jobseekers'	506.3	360.4	47.8	-	98.1
SO 4.3 Promote a gender-balanced labour market participation	12.7	4.8	-	-	7.9
SO 4.4 Promote the adaptation to change by workers	19.9	4.5	-	10.9	4.5
Total	**538.9**	**369.7**	**47.8**	**10.9**	**110.5**

Source: Elaboration based on Cohesion Data, available here. Data extracted in April 2024. See Annex II for further details regarding planned financial instruments for employment.

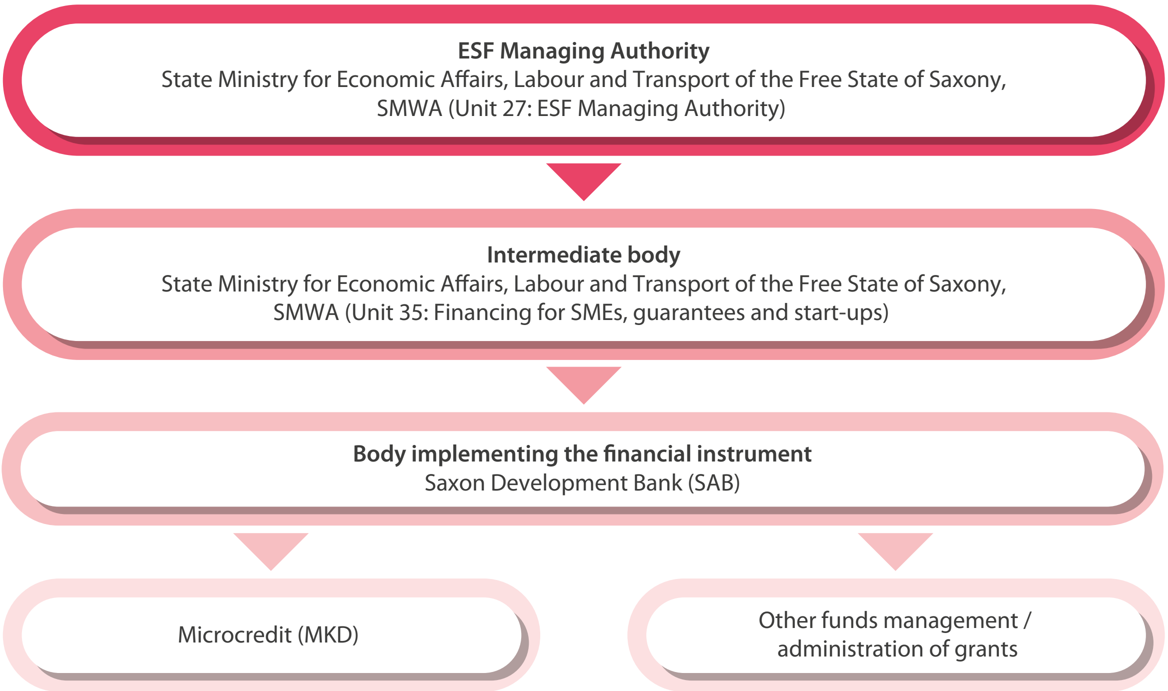
3.1.1 Loan products

As evident from the allocations foreseen for the 2021-2027 programming period as well as from past programming periods, **loan products** are particularly appropriate to support employment, especially to improve access to employment for job seekers and promote self-employment (So 4.1). Loan products can be used, for instance, to favour small business creation, especially when they include longer repayment periods, lower interest rates and reduced collateral requirements to mitigate the risk of failure and encourage individuals to start new businesses. Experience also suggests that even a small amount of financial support, such as **microcredit**, can provide an effective means to start a business, such as a microenterprise. Microcredits can in fact address the financial needs of some of the most disadvantaged ESF+ target groups, such as individuals Not [engaged] in Education, Employment or Training (NEETs), who typically face significant barriers in accessing finance to start a business. Microcredits in the form of **personal loans** are also suitable products for promoting a better work-life balance under SO 4.3.

Box 3.1: Mikrodarlehen, Saxony (Germany)[53]

Type of instrument: Microloan
Financial size / Funding sources: EUR 17 million / OP resources for transition regions in Saxony; more developed regions in Saxony are supported by a state fund under the same financial instrument
Final recipients: Enterprises and micro enterprises
Timing: from March 2016 to September 2023
Governance: Saxon State Ministry of Economic Affairs, Labour and Transport (managing authority); Saxon Development Bank (SAB) (financial intermediary acting as fund manager, i.e. the body implementing the financial instrument)
Description: The Mikrodarlhen is a financial instrument implemented in Saxony, Germany. It was introduced across all the NUTS-2 regions within Saxony, utilizing 2014-2020 ESF resources solely in transition areas. The management of the fund is entrusted to SAB, the Development Bank of Saxony.

Figure 3.1: Mikrodarlehen governance structure



Source: Own elaboration.

53 Based on the fi-compass (2022), *Mikrodarlehen - Microloans for entrepreneurs and start-ups in Saxony, Germany'*, available here.

The aim of the instrument is to enhance access to financing for business founders and micro-enterprises. It mainly targets businesses that intend to employ the founder(s) full-time, although it can also support businesses with part-time employment if they plan to transition to full-time.

The instrument offers final recipients up to 80% of the project cost or a maximum loan of EUR 20,000, with a maturity of up to 6 years. It features notably low interest rates and requires no fees or collateral, providing a significant advantage for those who are unable to secure commercial loans due to their history or the perceived riskiness of their start-up.

Final recipients may also avail of supplementary advisory services provided under the ESF OP to prepare their applications for the instrument.

This case exemplifies the effective implementation of a financial instrument under the ESF to assist businesses. Not only has the instrument demonstrated sound management by the NPB, but it has also led to the establishment of a state fund that can be reused over time.

The instrument had contributed to the realization of almost 1 000 start-up projects by the end of 2023[54]. By 2020, nearly half of the final recipients were women, exceeding the instrument 's target of 35%. The instrument will continue into the 2021-2027 programming period[55].

Additionally, loan instruments can also contribute to the challenges of transforming enterprises (SO 4.4), for instance through Workers Buyout Operations (WBO). WBO refers to a restructuring process in which employees buy a majority or total ownership stake in their own company and, in effect, become the owners. WBO generally serve to avoid the loss of jobs arising from financial crises. WBO can also be financed through equity instruments.

3.1.2 Guarantee products

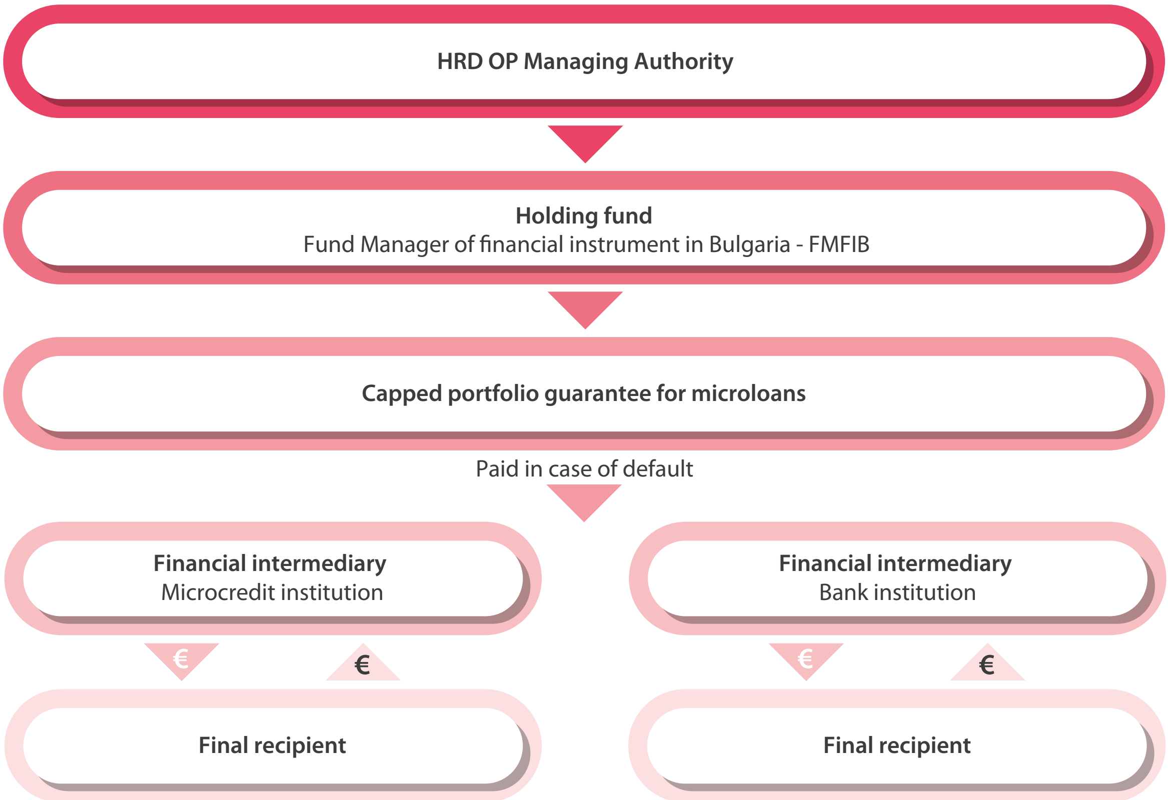
Guarantee products can support disadvantaged individuals lacking the necessary financial backing and collateral to start a business (SO 4.1). They provide credit risk protection and can also attract additional funds for business creation and expansion, by increasing the incentives of financial intermediaries to lend and serve a broader segment of clients. Guarantees may be particularly appropriate for young people, migrants or long-term unemployed individuals, who lack credit history and are therefore perceived as unbankable by financial intermediaries/bodies implementing the financial instrument.

54 Further detail available here.
55 Further detail available here.

Box 3.2: Guarantee for microloans, Bulgaria[56]

Type of instrument: Capped portfolio guarantee for microloans[57]
Financial size / Funding sources: ESF, Operational Programme Human Resource Developmen t: EUR 3.1 million programme resources (of which 15% national resources)
Final recipients: Start-ups, owned and managed by unemployed people; youths under 29; people with disabilities; social enterprises; start-ups owned and managed by people starting their first enterprise or self-employment
Timing: from May 2016 to December 2023
Governance: Ministry of Labour and Social Policy (Managing Authority); FMFIB (Holding fund); Unicredit and BDB Microfiancning (financial intermediaries)
Description: The primary objective of the instrument is to facilitate easier access to finance for the creation of new jobs, including those in social enterprises and self-employment opportunities. This is particularly crucial as the instrument addresses the financing gap for target recipients deemed too risky by the market. The instrument is designed to provide preferential conditions compared to market offerings considering rates and costs.

Figure 3.2: Guarantee for microloans governance structure



Source: Own elaboration.

56 Based on the fi-compass (2022), *ESF Financial instruments for microfinance in Bulgaria*, available here.
57 In addition to the guarantee financial instrument, also a risk sharing micro-finance facility was implemented in Bulgaria. For more info on both instruments, please see fi-compass (2022), ESF Financial instruments for microfinance in Bulgaria, available here.

The government opted to establish h a 100% government-owned company, formally named the "Fund Manager of Financial Instruments in Bulgaria" (FMFIB), in the form of a holding fund to manage financial instruments under various ESIF-funded OPs, including the Human Resource Development OP for the 2014–2020 period. The holding fund manager selected one microfinance institution (BDB Microfinancing) and a bank (Unicredit) as financial intermediaries for the capped portfolio guarantee for microloans[58]. Agreements with these intermediaries were signed in June 2020 and July 2021. Therefore, the two financial intermediaries were the exclusive entities authorized to provide microcredit using the guarantee. This arrangement encompasses a maximum loan amount of EUR 50 000, featuring an 80% guarantee rate per individual loan and a capped rate of 25% for losses on the guaranteed portfolio.

The deployment of the instrument coincided with the Covid-19 pandemic, impacting both active promotion in the target population and a longer than anticipated implementation phase. Additionally, considering it was the first experience for the managing authority of HRDOP, the uptake was lower than planned, with nine loans allocated under the capped guarantee instrument as of January 31, 2022. Various challenges have been encountered during the set up and the implementation of the instrument.As expected, vulnerable groups were viewed by potential financial intermediaries (especially banks) as high-risk clients, making the process for the selection of financial intermediaries very difficult. Nevertheless, this perception has been changing. An entrepreneurial ecosystem cannot be created overnight. While grants were the most common option in the past, testimonies from the target group of vulnerable micro entrepreneurs point out that many prefer to obtain debt financing with much shorter notice and less bureaucratic reporting requirements. Thus, there has been a shift away from relying on grants only. However, it is worth mentioning that grants are still necessary for most of the final recipients targeted by the ESF financial instruments in Bulgaria, as they do not show fully viable business models according to financial intermediaries' appraisal. Therefore, a combination of a financial instrument with grants could be a suitable solution, where the grant element could be used to provide coaching and guidance to entrepreneurs and to improve sustainability and viability of their projects.

3.1.3 Equity and quasi-equity products

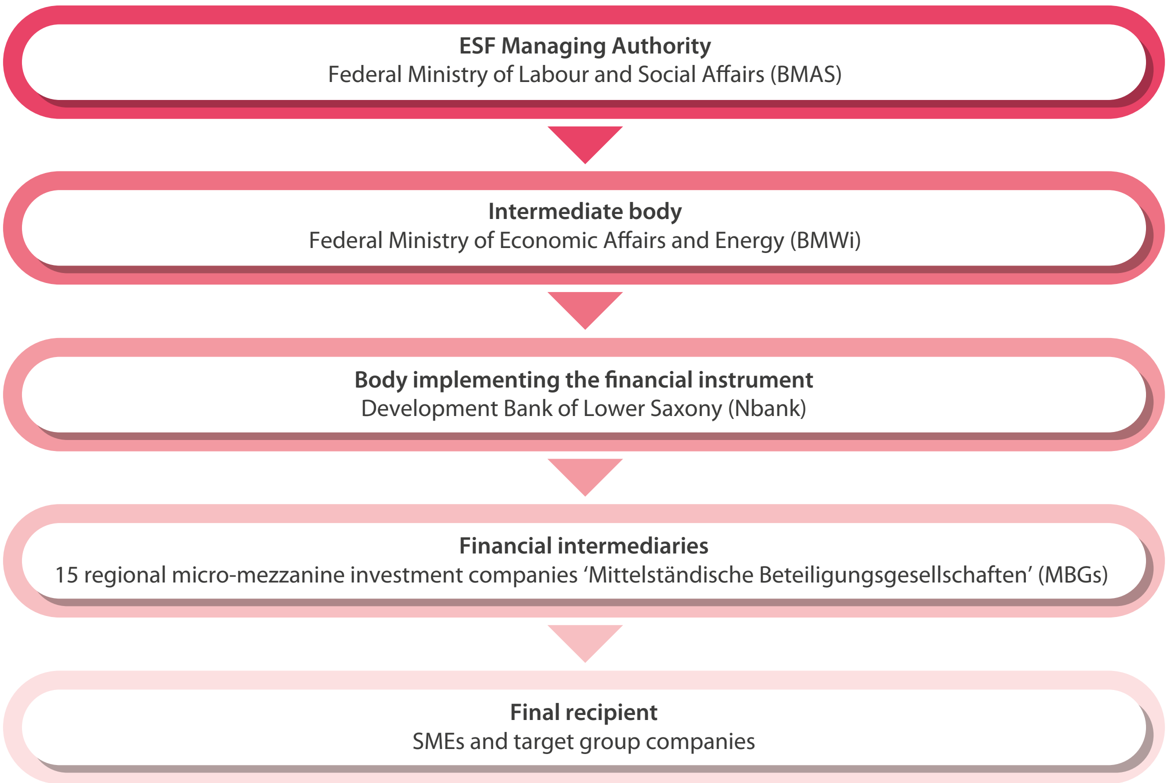
Equity and **quasi-equity** products can improve the creditworthiness of final recipients through an increased capital base, making financial intermediary banks more willing to provide additional capital for enterprises established or led by women, migrants, or unemployed individuals (SO 4.1). Support from equity and quasi-equity instruments can help enterprises to better focus on financial sustainability, increasing their ability to obtain additional finance and leading to a general improvement of their business capacity, as well as the capacity to hire new people from disadvantaged groups.

58 In addition to the guarantee financial instrument, also a risk sharing micro-finance facility was implemented in Bulgaria. For more info on both instruments, please see fi-compass (2022), *ESF Financial instruments for microfinance in Bulgaria*, available here.

Box 3.3: Mikromezzaninfonds, Germany[59]

Type of instrument: Mezzanine capital (quasi-equity
Financial size / Funding sources: 2007-2013: EUR 83.33 million from OP (EUR 50 million from ESF and EUR 33.33 million from the national ERP Special Fund); 2014-2020: EUR 152 million from Federal ESF OP (from ESF resources and national ERP Special Fund)
Final recipients: SMEs and enterprises led by disadvantaged people
Timing: from September 2013 to December 2023
Governance: Federal Ministry of Labour and Social Affairs (BMAS) (managing authority of the national ESF OP); Federal Ministry for Economic Affairs and Energy (BMWi) (intermediate body responsible for management and implementation of the Mikromezzaninfonds); The Investment and Development Bank of Lower Saxony (NBank) (fund manager); 15 regional investment companies for SMEs (financial intermediaries)
Description: Mikromezzaninfonds Deutschland is a financial instrument co-funded by the ESF within the ESF OP at the federal level in Germany. This initiative demonstrates the potential for promoting social inclusion through mezzanine capital, targeting specific SME groups using local financial partners and, collectively, widespread financial intermediaries.

Figure 3.3: Mikromezzaninfonds governance structure



Source: Own elaboration.

59 Based on fi-compass (2016), *Mikromezzaninfonds, Germany*, available here.

From a legal and economic standpoint, Mezzanine capital combines aspects of equity and debt capital. A micro-mezzanine investment provides the final recipient with economic equity without the investor having any right to vote or influence. The injected capital improves final recipients' capital base and, consequently, their credit rating and the terms and conditions for bank finance.

Funding, provided as dormant investment, is provided by 15 regional investment companies ('Mittelständische Beteiligungsgesellschaften', or MBGs) which have suitable local knowledge and networks in the respective Federal States, where the investment is made. Mikromezzaninfonds provides silent partnership investments of up to EUR 50 000 with a term of ten years. Final recipients belonging to specific target groups (i.e. enterprises providing vocational training, founded out of unemployment or run by women or people from migrant backgrounds, as well as social enterprises), could benefit from a participation of up to EUR 150 000. The dormant investment may be used for all corporate management purposes.

In return for the financing, final recipients have to pay a profit-based remuneration of up to 1.5% of the deposit. In addition, non-profit-based remuneration of generally 8% per annum in relation to the nominal amount of the deposit has to be paid to financial intermediaries on quarterly basis.

Funded entrepreneurship initiatives include those founded by unemployed individuals, businesses led by women or individuals with a migration background, commercially oriented social enterprises, and those with an environmental focus. Additionally, companies offering training and working in the health and care sector are part of the target group. Companies in need of restructuring or a bailout are ineligible, and all applying companies must demonstrate sufficient economic viability.

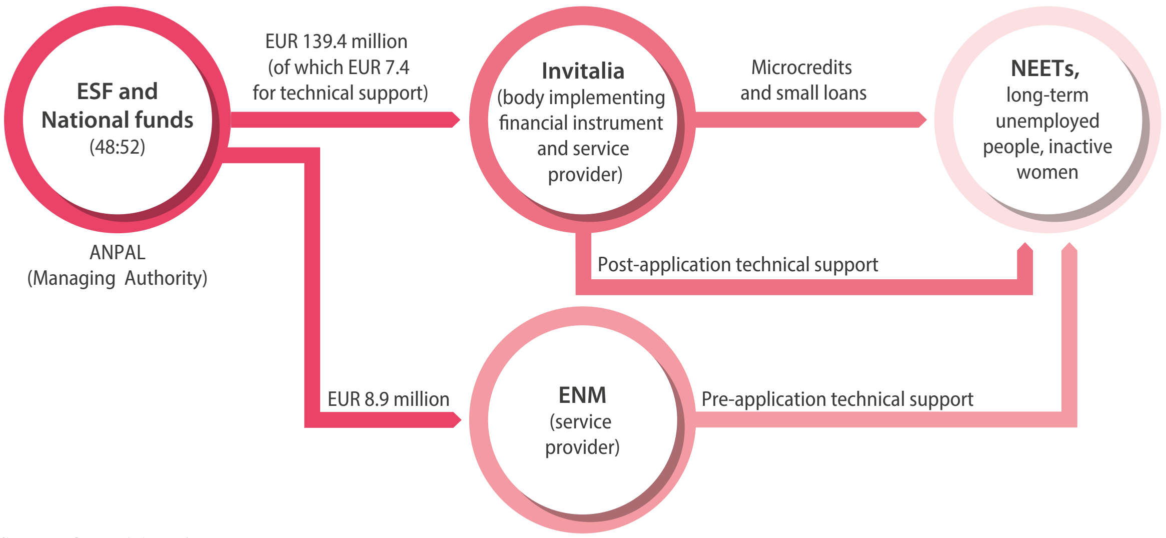
3.1.4 Combination with grants

To make the financial support more effective and efficient and increase the sustainability of the projects financed, providing loan products in **combination with grants** financing business development services is often a necessary option within the ESF+ framework. Business development services could include, for instance, technical support (including for loan applications), business skill development, training activities for enterprise management, professional assistance, financial education, and debt advisory services. The aims and type of business development services vary with the needs and expectations of final recipients. Business development services can be both before the loan application and after the loan contract. By increasing the human capital of the final recipients, job qualifications and opportunities can improve as well as their capacity to create and manage income-generating activities.

Box 3.4: SELFIEmployment, Italy

Type of instrument: Microloan products combined with grants
Financial size / Funding sources: EUR 132 million for the financial instrument financed by two ESF 2014-2020 national operational programmes (NOPs), with EUR 62 million from YEI NOP and EUR 70 million from SPAO NOP. The two NOPs also contribute EUR 16.3 million for the grant component (EUR 3.1 million from YEI NOP and EUR 13.2 million from SPAO NOP)
Final recipients: NEETs, inactive women and long-term unemployment individuals
Timing: from 2015 to 2023
Governance: ANPAL (managing authority); Invitalia (fund manager; non-financial services provider); ENM (non-financial services and communication services)
Description: The SELFIEmployment initiative, established in 2015, combines different types of loans (microcredits, extended microcredits and small loans[60]), with grants in two operations. The grants can finance training and coaching – both before and after the loan application - to equip individuals with the knowledge to launch and sustain businesses as well as enhance their self-employment and entrepreneurial opportunities. It targets individuals Not [engaged] in Education, Employment or Training (NEETs), inactive women and the long-term unemployed.

Figure 3.4: SELFIEmployment combination structure



Source: Own elaboration.

60 Microcredit, from EUR 5 000 to 25 000; extended microcredit, from EUR 25 001 to 35 000; small loans, from EUR 35 001 to 50 000.

Invitalia S.p.A. (the National Agency for Investment Attraction and Business Development) acts both as the fund manager and the provider of post-application technical support. ENM (National Entity for Microcredit) is the provider of pre-application technical support and it is also in charge of communication activities. Both types of support are provided in two operations.

Grants are used to finance training for entrepreneurial self-employment skills, managed by ENM through the YES I START UP programme, implemented before the loan application, with a budget of EUR 8.9 million. It offers 60 hours of foundational training, and in-class or synchronous online sessions accommodating various group sizes. There is also an additional 20-hour module with specialised guidance, tailored for individual learners or small groups, delivered in-person or online. However, the technical support provided by ENM is not exclusively used for potential final recipients of the SELFIEmployment revolving fund (i.e. NEETs, inactive women, and the long-term unemployed are not obliged to apply for the SELFIEmployment financial support). Technical support is also provided by Invitalia (the fund manager and beneficiary of the grant) for business design and implementation, with a budget of EUR 7.4 million. The Invitalia tutoring service is delivered after the loan is disbursed and, unlike participation in the YES I START UP programme, it is mandatory. It starts before the new firm begins operations and lasts for 24 months providing continuous individual online support through webinars and digital consultations.

From its establishment to 1 November 2023, the instrument contributed to the creation of 3 620 new jobs and financed 2 047 projects with EUR 67.1 million. Less developed regions located in Southern Italy, which have the highest rates of NEETs, inactive women, and long-term unemployed, had the highest demand. The most common loan type was microcredit, while the predominant economic activity financed was wholesale and retail trade, followed by accommodation and food services.

3.2 Financial instruments for education

Using financial instruments for education[61] is a way to support individuals from socially disadvantaged backgrounds to improve their human capital and, therefore, to increase their job opportunities. In particular, financial instruments financed by the ESF+ with more flexible and appropriate conditions can contribute to increased access to finance for young people, who are likely to have lower personal savings and less collateral, less credit history, and less past business experience. Moreover, ESF+ financial instruments can develop entrepreneurial mindsets and skills to make young people aware of self-employment as a career option and equip them with the entrepreneurial knowledge, technical skills and competencies required to establish and run a successful business.

In the 2014-2020 programming period, EUR 91 million, accounting for around 14.5% of the total ESF amount committed to financial instruments, was allocated to TO10 'Enhancing equal access to education and lifelong learning'[62].

61 See also fi-compass (2022), Financial Instruments for education and learning, available here.

62 European Commission (2023), *Financial instruments under the European Structural and Investment Funds - Summaries of the data on the progress made in financing and implementing the financial instruments for the programming period 2014-2020 in accordance with Article 46 of Regulation (EU) No 1303/2013 of the European Parliament and of the Council - Situation as of 31 December 2022*, available here.

In the 2021-2027 programming period, the proportion of resources allocated to financial instruments for education is 11% of the total ESF+ resources allocated to financial instruments63. Out of this EUR 76.6 million (see table below):

- 17.4% is for SO 4.5 'Improving education and training systems;
- 9.1% for SO 4.6 'Quality and inclusive education and training systems';
- 73.5% for SO 4.7 'Lifelong learning and career transitions';
- Most of the allocated resources (60%) are for loan products, especially for SO 4.7, 8.1% for guarantees, and 14% for equity and quasi-equity; around 13.6% is for grants combined within a financial instrument operation, only foreseen under SO 4.7.

Table 3.2: 2021-2027 allocation to financial instruments for education by SO and financial product

SO	Allocation (EUR million)				
	Total	Loan	Guarantee	Equity or quasi-equity	Grants within a financial instrument operation
SO 4.5 Improving education and training systems	13.3	3.3	3.2	6.7	-
SO 4.6 Quality and inclusive education and training systems	7	-	3	4	-
SO 4.7 Lifelong learning and career transitions	56.3	42.7			13.6
Total	**76.6**	**46**	**6.2**	**10.7**	**13.6**

Source: Elaboration based on Cohesion Data, available here. Data extracted in April 2024. See Annex II for further details regarding planned financial instruments for education.

3.2.1 Loan products

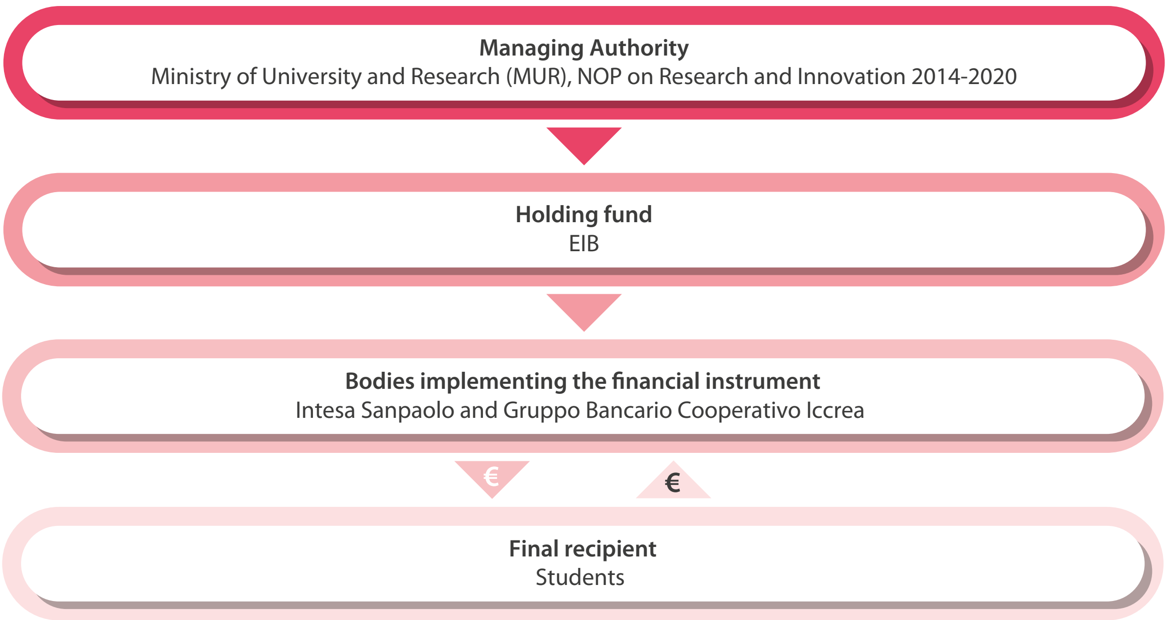
Loans, and, in particular, personal loans, are particularly suitable for education, as in the case of student loans, to acquire new skills (SO 4.5) and for life-long learning, improving job qualifications (SO 4.7). Removing collateral requirements from financial intermediaries and offering long term repayment with an appropriate period of grace for the students is a key element to keep in mind when designing financial instruments.

63 Based on Cohesion Data portal, available here.

Box 3.5: StudioSì, Italy[64]

Type of instrument: Loans
Financial size / Funding sources: EUR 100 million from ESF resources (NOP Research and Innovation 2014–2020)
Final recipients: Students
Timing: From 2019 to December 2023
Governance: Ministry of University and Research (managing authority); EIB (Holding fund manager); Intesa Sanpaolo and Gruppo BCC Iccrea (financial intermediaries, i.e. bodies implementing the financial instrument)
Description: The financial instrument focuses on students in Southern Italy (Campania, Calabria, Puglia, Sicilia, Basilicata, Sardegna, Abruzzo, and Molise) in subjects consistent with the thematic areas identified by the National Smart Specialization Strategy. The instrument is a good example of a financial instrument aiming to improve access to higher education and training. The priority of the product is to reduce the existing financial gap for students in the regions of Southern Italy and improve student access to university degrees.

Figure 3.5: StudioSì governance structure



Source: Own elaboration.

64 Based on fi-compass (2022), *Financial instruments for education and learning',* available here.

The product provides funds up to EUR 50 000, interest-free, and without any personal or third-party guarantee obligation. In addition to tuition fees, the funding can cover study-related costs. The financial instrument is managed through a holding fund established as a separate block of finance within the EIB. The managing authority is the Ministry of University and Research (MUR), and two financial intermediaries (Intesa Sanpaolo and Gruppo BCC Iccrea) were selected as the bodies implementing the financial instrument. They are each responsible for managing EUR 46.5 million, resulting in a total provision of loans to final recipients amounting to EUR 93 million (EUR 7 million was for fees and management costs).

As holding fund manager, the EIB was in charge of the implementation of the investment strategy. It prepared the tender for the selection of the bodies implementing the financial instrument and managed the evaluation. It then negotiated the operational agreements with the bodies implementing the financial instrument. Moreover, it monitored and controlled the activities of the bodies implementing the financial instrument on the basis of the terms and conditions set up in the operational agreements. It manages the treasury of the financial instruments and is in charge of reporting the progress of operations and the costs for the management of the financial instrument to the investment committee.

By 31 December 2023 the instrument funded 3 737 personal loans, for an overall amount of about EUR 75.5 million and an average of about EUR 20 000 per loan. Women accounted for 47% of the loan recipients.

3.2.2 Guarantee products

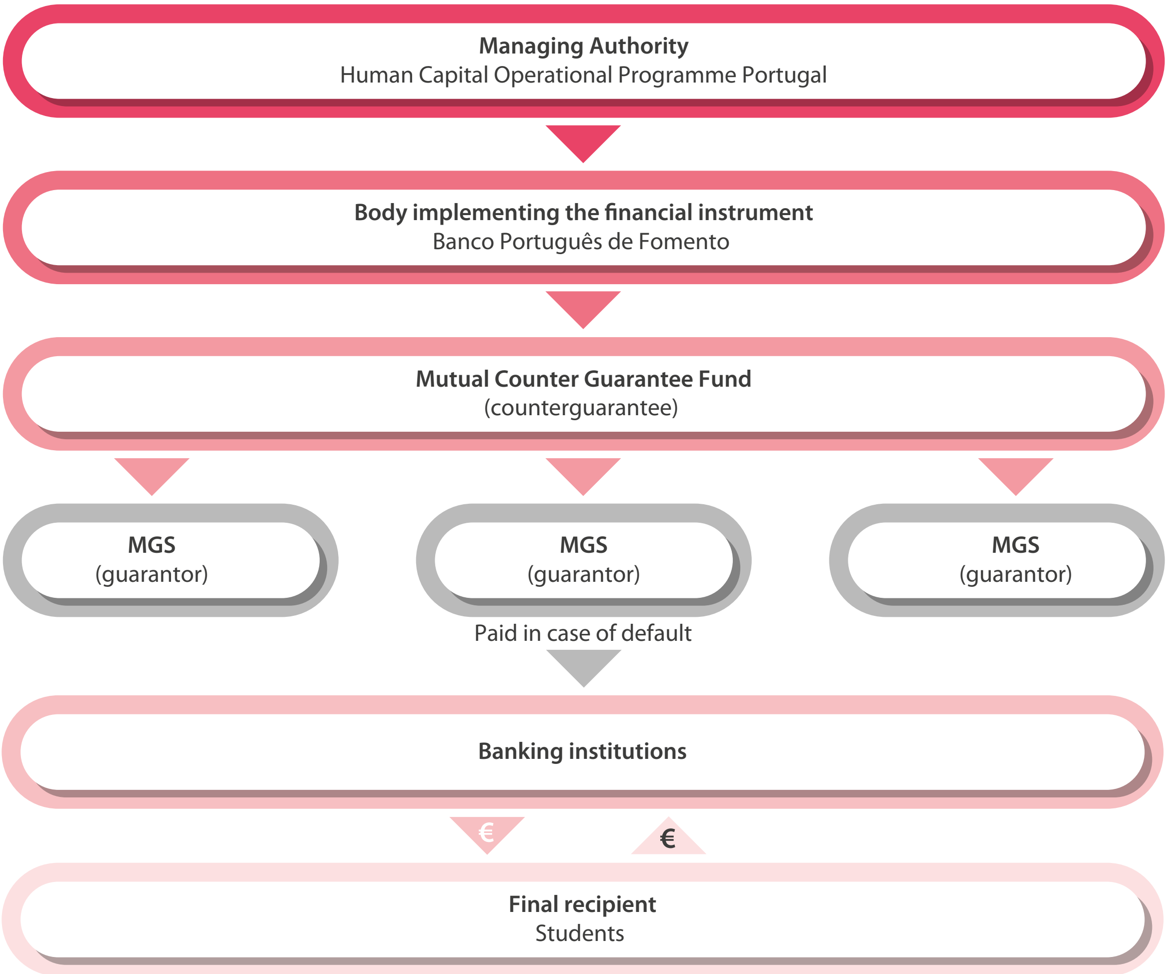
Generally, loans for education, especially those targeting students, are relatively risky because of the uncertainty of future graduate incomes or employment status. Therefore, having a **guarantee** reduces payment default risks on the financial intermediaries which allocate the loans.

Box 3.6: Student Loans with Mutual Guarantee, Portugal[65]

Type of instrument: Mutual guarantee
Financial size / Funding sources: EUR 10.3 million from ESF and EUR 3.8 million from national public sources (EUR 14.1 million in total) leveraging to EUR 85 million
Final recipients: Students in public and private higher education institutions[66]
Timing: 2015 to 2023
Governance: Human Capital Operational Programme Portugal (managing authority); Banco Português de Fomento (body implementing the financial instrument); MCGF (counter-guarantor); Mutual Guarantee System (guarantor)
Description: The scheme is financed by the Human Capital Operational Programme Portugal and has been coordinated by Banco Português de Fomento since 2020 as the implementing body. The main objective is to improve accessibility to higher education, specifically targeting students frequently marginalized due to their socio-economic status. It was selected as a key instrument in working towards this goal. Additionally, the program actively contributes to achieving the EU-level target of having 40% of individuals aged 30–34 enrolled in higher education.

65 Based on fi-compass (2022), Financial instruments for education and learning', available here.
66 The student must be enrolled in the following ISCED levels: Professional superior technical specialisation courses (ISCED 5); Undergraduate courses (ISCED 6); Master level courses (ISCED 7); Doctoral level courses (ISCED 8).

Figure 3.6: Student Loans with Mutual Guarantee governance structure



Source: Own elaboration.

To reach this goal, the managing authority has designed the instrument as a counter-guarantee. The instrument aims to provide a counter-guarantee to the guarantor, the Mutual Guarantee System (MGS), which provides guarantees to bank institutions offering special credit lines, specifically university student loans. The MGS is a public-private partnership and consists of institutions with a regional and/or multisectoral focus. Their activities include providing portfolio guarantees for special credit lines, particularly university student loans.

The final beneficiaries of the instrument are students enrolled in higher education institutions in the less developed regions of mainland Portugal. The loan amount varies between EUR 1 000 and EUR 5 000 per year, with a maximum amount of EUR 30 000 per student. Each awarded loan is counter-guaranteed by the Mutual Counter Guarantee Fund (MCGF) of Portugal. The interest rate is market-related, with further discounts for socio-economically disadvantaged students. There is an 80% guarantee limit on each loan, along with a cap rate of 15% of the total loan amount. Students are not required to provide any additional endorsements or warranties, except for loans exceeding EUR 15 000, for which a promissory note may be required.

The estimated ESF leverage was, in fact, 8.5x times. As of December 31, 2020, the loan scheme had supported 1 193 students.

A number of challenges was encountered when setting up and implementing this financial instrument. For example, there were significant difficulties in finding appropriate intermediaries at national level. Financial intermediaries perceived the loan scheme as riskier, compared to their own commercial products. Commercial banks required the option to demand additional collateral from students to cover the part of the loan that is not guaranteed by the financial instrument. However, this was not allowed, therefore there was a sub-optimal number of intermediaries offering these student loans. In the future, when designing similar instruments, a combination of the financial instrument with grants could be considered as a way to decrease the perceived level of risks of student loans and to incentivise policy impact.

3.2.3 Equity and quasi-equity products

Equity and **quasi-equity** instruments can be used to invest in enterprises that offer services ancillary to education (suppliers of education and lifelong training), enterprises investing in skills, or funds investing in education technologies or education more broadly.

3.2.4 Combination with grants

Providing financial instruments for education can be particularly effective when **combined with grants**. These can be, for instance, in the form of interest rate subsidies during the grace period on eligible loans for students. Other than making the loan more affordable for final recipients, interest rate subsidies can improve the willingness of financial intermediaries to provide finance, contributing to the multiplier effect of the ESF+ resources allocated to the financial instrument.

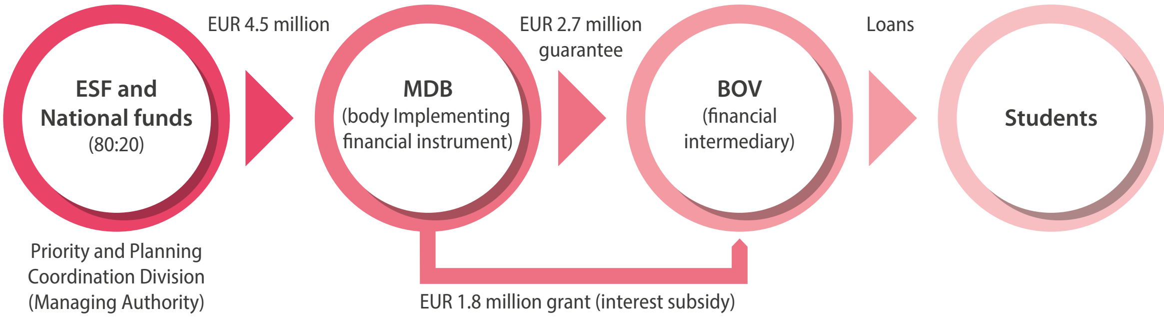
Box 3.7: Further Studies Made Available (FSMA) and Further Studies Made Affordable Plus (FSMA+), Malta[67]

Type of instrument: Loan and guarantee combined with grants
Financial size / Funding sources: EUR 2.7 million for the guarantee and EUR 1.8 million for the grant element (FSMA 2014-2020); EUR 3 million for the guarantee and EUR 2 million for the grant element (FSMA+ 2021-2027). FSMA and FSMA+ are 80% funded through ESF/ESF+ and 20% through national funds
Final recipients: Students attending courses in Malta Qualifications Framework (MQF) levels 5, 6, 7 and 868
Timing: FSMA from October 2019 to December 2021; FSMA+ from January 2022, ongoing
Governance: Priority and Planning Coordination Division (managing authority); the Malta Development Bank (body implementing the financial instrument); Bank of Valletta plc (financial intermediary)
Description: Further Studies Made Affordable (FSMA) is a financial instrument developed in Malta during the 2014-2020 programming period and continued in the 2021-2027 programming period as FSMA+ (Further Studies Made Affordable Plus). It combines loans covered by a guarantee with an interest rate subsidy financed by grants in one operation.

67 Based on fi-compass (2022), *Financial instruments for education and learning',* available here.
68 Level 5 refers to an Undergraduate Certificate/Diploma and a VET Higher Diploma/ Foundation Degree; level 6 refers to Bachelor's Degree; level 7 refers to Master's Degree and Post-Graduate Diploma/Certificate; level 8 refers to Doctoral Degree.

Designed for students, the financial instrument is a portfolio-capped financial guarantee with loan-by-loan credit risk coverage (80% of each loan capped at 25% of the portfolio) combined with an interest rate subsidy for all interest incurred during the moratorium period plus one year for each eligible loan.

Figure 3.7: FSMA combination structure



Source: Own elaboration.

The instrument provides a grace period with zero repayment during the students' studies, with a full subsidy of the 2.75% interest rate for up to 5 years. Combining the financial instrument with the interest rate subsidy in one operation significantly reduces the cost of finance for students. It eliminates the need to provide collateral or life insurance cover, significantly reduces the interest rate and makes the loan more affordable for students through lower monthly repayments. Also, the Malta Development Bank is positive about the combined support mechanism of FSMA, reducing its risk of financing students. In total, 268 loans corresponding to EUR 8.6 million had been issued to students under FSMA from October 2019 to December 2021 (with 100% of programme resources committed) and 219 loans corresponding to EUR 9.6 million under FSMA+ by August 2023 (64% of programme resources committed). The average value of the loans was EUR 32 700 and EUR 43 800 under FSMA and FSMA+ respectively.

Both FSMA and FSMA+ are considered a success by stakeholders in Malta and across Europe. Despite the fact that it was the first financial instrument in Malta managed by MDB, the ability to combine different forms of support into one product made the offering to students more attractive. The instruments also remained successful during and after the pandemic, which led to the expanded budget for the FSMA+. Without combining the different forms of support, FSMA and FSMA+ would not be able to offer such appealing criteria and conditions for target users. Similarly, no commercial bank could provide a financial instrument with the same conditions as the FSMA and FSMA+. The combined support has enabled the financial intermediary to lower its risk rating and become more open to supporting students.

3.3 Financial instruments for social inclusion

Financial instruments can be used to address social inclusion in specific disadvantaged individuals prevented from economic and financial opportunities due to their poverty, lack of basic competence and lifelong learning opportunities, or as a result of discrimination.

Financial support for the social economy and, in particular, social enterprises aimed at giving vulnerable groups access to economic opportunities and social services, is key to solving the issue of social exclusion[69].

69 See also fi-compass (2016), Financial instruments working with social entrepreneurship, available here.

Social enterprises are typically considered to have the capacity to design innovative and effective initiatives for social inclusion resulting from their close connection with the communities where they operate. They can provide innovative social solutions to address social challenges, such as combating the unemployment of disadvantaged individuals (SO 4.8) or their difficulties in accessing social services (SO 4.11). Social enterprises can also employ or provide services to unemployed people over 50 years of age, long-term unemployed people, people with disabilities and with mental illness, migrants, homeless people and low-income persons.

In the 2014-2020 programming period, EUR 65 million, accounting for around 12.7% of the total ESF amount committed to financial instruments, was allocated to TO9 'Social inclusion'[70].

In the 2021-2027 programming period, the proportion of resources allocated to financial instruments for social inclusion is 9.8% of the total ESF+ resources allocated to financial instruments[71]. Out of this EUR 66.7 million (see table below):

- 79% is for SO 4.8 'Active inclusion and employability;
- 21% for SO 4.11 'Equal access to quality social and healthcare services;
- Most of the allocated resources (nearly 75%) are for loan products, especially for SO 4.8 and 9.2% for equity and quasi-equity (only under SO 4.8); 16% is for grants combined within a financial instrument operation.

Table 3.3: 2021-2027 allocation to financial instruments for social inclusion by SO and financial product

SO	Allocation (EUR million)				
	Total	Loan	Guarantee	Equity or quasi-equity	Grants within a financial instrument operation
SO 4.8 Active inclusion and employability	52.7	39.1	-	6.1	7.5
SO 4.11 Equal access to quality social and healthcare services	13.9	10.8	-	-	3.2
Total	**66.7**	**49.9**	**-**	**6.1**	**10.7**

Source: Elaboration based on Cohesion Data, available here. Data extracted in April 2024. See Annex II for further details regarding planned financial instruments for social inclusion.

3.3.1 Loan products

Loan products are suitable for promoting social entrepreneurship and contributing to social economic growth. They help improve or create new capacities for social enterprise investments and promote start-ups and new social business initiatives within the social economy, even through microfinance. Loan products can also contribute to covering the unmet demand that social enterprises typically have for external financing, and encourage them to use repayable funding.

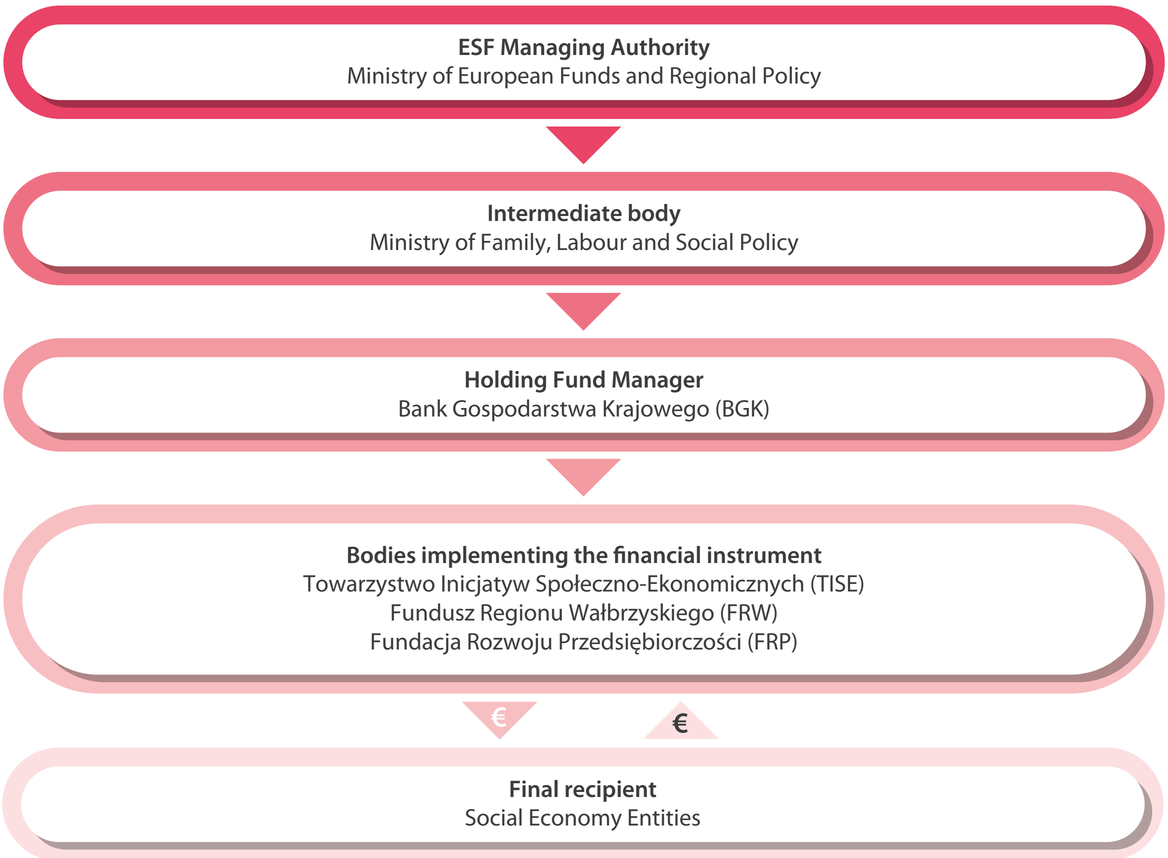
70 European Commission (2023), *Financial instruments under the European Structural and Investment Funds - Summaries of the data on the progress made in financing and implementing the financial instruments for the programming period 2014-2020 in accordance with Article 46 of Regulation (EU) No 1303/2013 of the European Parliament and of the Council - Situation as of 31 December 2022*, available here.

71 Based on Cohesion Data portal, available here.

Box 3.8: The National Fund for Social Entrepreneurship, Poland[72]

Type of instrument: Loans
Financial size / Funding sources: 37 million from ESF National OP Knowledge, Education, Development' (OP KED)
Final recipients: Social economy entities
Timing: 2014-2020
Governance: Ministry of European Funds and Regional Policy (managing authority); Ministry of Family, Labour and Social Policy (intermediate body); BGK (holding fund manager); TISE, FRW and FRP (bodies implementing the financial instruments)
Description: The National Fund for Social Entrepreneurship (NFSE) is a financial instrument available in all of Poland set up in the 2014-2020 programming period, within the framework of the ESF National OP 'Knowledge, Education, Development' (OP KED)', that builds on the success of the 2007-2013 pilot financial instrument.

Figure 3.8: NFSE governance structure



Source: Own elaboration.

72 Based on fi-compass (2021), *Financing the Social Economy in Poland*, available here.

The Polish National Promotional Bank, BGK, was appointed as the holding fund manager, and selected three financial intermediaries as the bodies implementing the financial instruments to ensure a minimum leverage of 1.15x times the OP resources. The financial instrument provides first-loss protection for loan portfolios, thereby partially mitigating the risks faced by financial intermediaries and, as a result, enabling expanded outreach and improved borrowing terms for the ultimate recipients.

The instrument aims to provide long-term, affordable loans to Social Economy Entities[73] (SEEs) while also offering business development services to final recipients through the Social Economy Support Unit network[74]. The NFSE's financial products include start-up loans (microloans below EUR 25 000) and development loans for more established entities (up to EUR 117,900 per loan, and up to EUR 235 800 per SEE). Each product is tailored to the development stage of the respective final recipients. Notable features of the NFSE include the opportunity to reapply for a second loan after the first is repaid, a 6-month grace period, and interest rate subsidies under certain conditions.

Due to the COVID-19 pandemic, the instrument was adjusted to enhance the financial intermediaries' capacity to offer affordable finance. Changes to NFSE loan parameters, such as reduced interest rates, payment holidays, and extended maturities, helped SEEs stay afloat during the pandemic. In parallel, a liquidity line was established using resource reflow from OP Human Capital 2007-2013 to support SEEs.

By the end of July 2023, almost EUR 33 million (92% of the allocated resources, including EUR 4.5 million from financial intermediaries) had been disbursed. 1 171 SEEs (almost 98% of the target) had been financed and around 115% of the new job creation target had been reached.

3.3.2 Guarantee products

When supporting social enterprises, loan products can be complemented with **guarantees** in order to increase the incentives for financial intermediaries to lend and boost the development of finance markets for social enterprises. Access to financial resources for social enterprises can, in fact, be more complex than for other enterprises[75]. Financial intermediaries may perceive it as riskier to finance social enterprises, therefore the guarantee can contribute to decreasing the lending risk.

73 Those include social enterprises; NGOs; business entities created to achieve social goals; reintegration agents, providing social and occupational reintegration services for people at risk of social exclusion.

74 The non-financial support is delivered outside the financial instrument framework. The Social Economy Support Units are a network of entities, mostly operated by NGOs financed through ESF resources from 2014-2020 OP Knowledge, Education, Development and 2014-2020 Regional OPs.

75 European Commission (2020), *Social enterprises and their ecosystems in Europe - Comparative synthesis report*, available here.

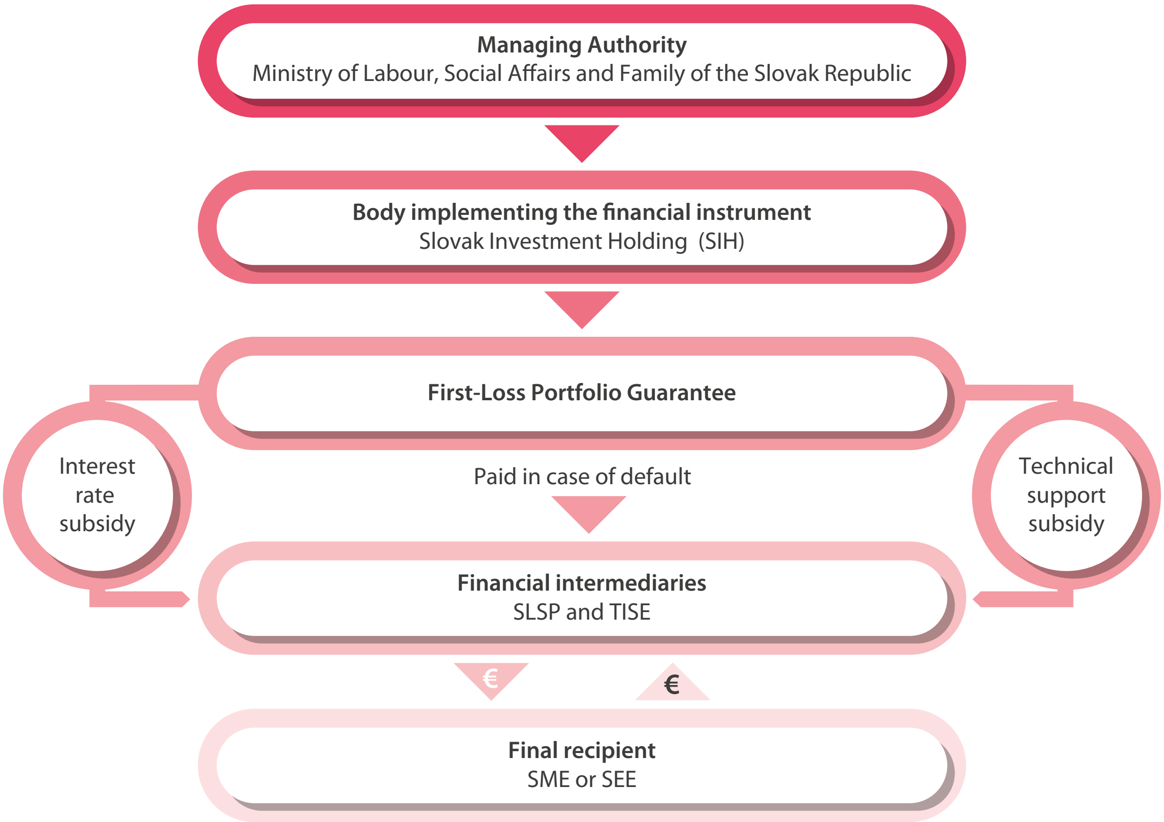
Box 3.9: First-Loss Portfolio Guarantee, Slovakia[76]

Type of instrument: First-Loss Portfolio Guarantee (in combination with Technical Support and Interest Rate Subsidy)
Financial size / Funding sources: EUR 7.31 million (ESF 4.97 million + national co-financing EUR 0.88 million; ERDF 1.24 million + national co-financing EUR 0.22 million). Out of the ESF + national co-financing: EUR 3.00 million allocated to the guarantee; EUR 2.55 million allocated to the Interest Rate Subsidy; EUR 0.30 million allocated to Technical Support[77]
Final recipients: Social economy enterprises
Timing: from 2019 to 2023
Governance: MPSVR (managing authority), Ministry of Interior (MINV) (intermediate body), SIH (body implementing the financial instrument), Ministry of Finance (MoF) (supervisory body), SLSP and TISE (financial intermediaries)
Description: The Guarantee Instrument enhances the provision of preferential loans to social economy enterprises. The aim is to improve access to finance for social economy entities that are considered too high-risk for banks, due to their non-profit focus and lack of collateral. SIH provides EUR 3.75 million as a guarantee to two financial intermediaries to cover new loans up to a volume of EUR 18.75 million, creating new opportunities for accessible financing by the end of 2023.

The guarantee provides the financial intermediaries with individual credit risk cover up to a maximum of 80% per loan, meaning the financial intermediary is entitled to a reimbursement of 80% of the defaulted loan principal and a specified portion of the interest, up to 25% of the portfolio is covered (guaranteed cap rate). Moreover, the Guarantee Instrument allows for substantially better lending conditions and is strengthened by an additional EUR 3.6 million in support in the form of interest rate subsidies and technical support. This package enables the intermediaries to lower the interest rates on loans by 2% on average, including the possibility of offering loans with 0% interest rates to social economy enterprises whose social contribution would be very valuable, but who are unable to break even under commercial financing. The guarantee, which SIH provides free of charge to the financial intermediary, is combined in a single operation with an interest rate subsidy (up to 2% of the loan value) paid by SIH to the financial intermediary, and a grant for technical support (up to 10% of the loan value).

76 Based on fi-compass (2022), *ESF financial instruments in the Slovak Republic*, available here.
77 Based on the information provided by SIH, the agreement with the financial intermediary TISE was terminated by mutual agreement in July 2022. In the case of the financial intermediary SLSE, the implementation of the financial instrument took place only under PO 3, not under PO 6. As of 31 December 2023, eligible expenditures in the case of SLSP were as follows: EUR 1.644 (ESF 1.397 million + national co-financing 0.247 million). Out of the ESF + national co-financing: EUR 1.572 million allocated to the guarantee; EUR 0.059 million allocated to the Interest Rate Subsidy; EUR 0.013 million allocated to Technical Support.

Figure 3.9: First-Loss Portfolio Guarantee governance structure



Source: Own elaboration.

As of May 2021, the total volume of loans granted had amounted to EUR 7.6 million, representing EUR 1.5 million in guarantees. Approved loans ranged between a minimum of EUR 0.08 million and a maximum of EUR 4.5 million, targeting social enterprises focused on employment and job creation.

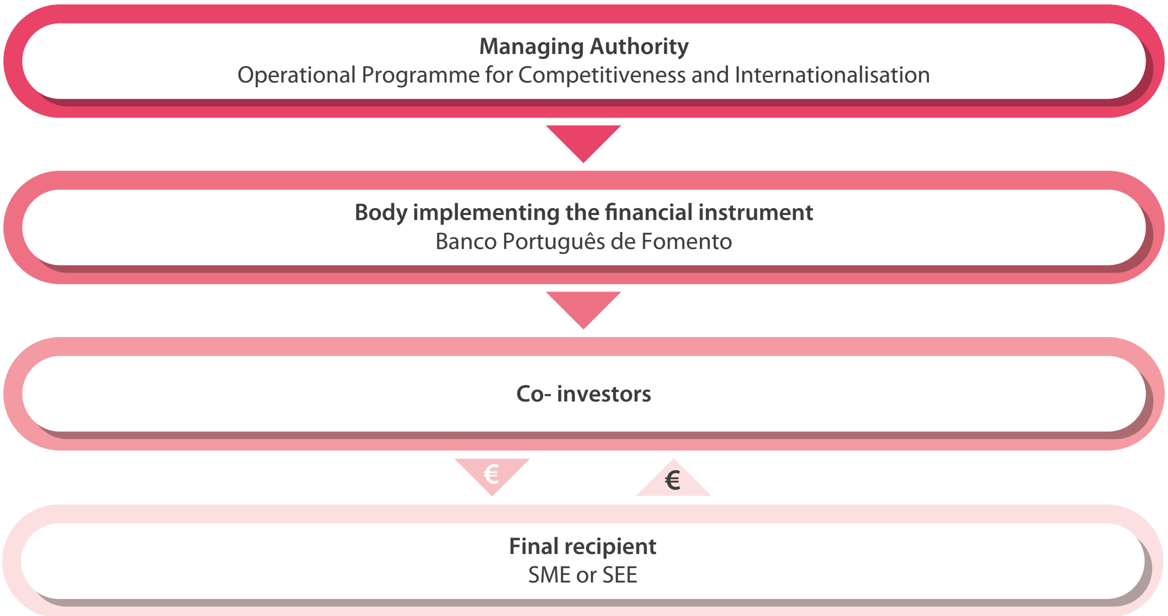
3.3.3 Equity and quasi-equity products

Equity and **quasi-equity** may be suitable for increasing social enterprises' capital, by stimulating local private equity industry investment and social investors in riskier areas not previously serviced. As with equity products, there is an active role in project management by investors, social enterprises can therefore benefit from the investor's management expertise and increase their knowledge and skills in project management.

Box 3.10: Social Innovation Fund, Portugal[78]

Type of instrument: Equity and guarantee
Financial size / Funding sources: EUR 82.4 million, 85% from 2014-2020 ESIF (different OPs) and 15% from the Portuguese state budget
Final recipients: Social enterprises
Timing: 2018-2023
Governance: OP for Competitiveness and Internationalisation (managing authority); Banco Português de Fomento (fund manager/guarantor, i.e. body implementing the financial instrument)
Description: The Portugal Social Innovative Initiative incorporates the Social Innovation Fund (SIF) into its framework, which includes four different phases[79].

Figure 3.10: Social Innovation Fund governance structure (debt instrument)



Source: Own elaboration.

78 Based on fi-compass (2020), *Supporting the development of Social Finance Ecosystems in Member States under ESF*, available here.
79 A capacity-building grant scheme aiming to improve the organisational and management competencies of organisations and teams directly involved in social innovation and social entrepreneurship projects; a venture philanthropy matching-fund scheme, a grant, to support the early growth of social innovation or social entrepreneurship projects; the Social Outcomes Contracting Programme, a financing instrument that uses an outcome payment mechanism to support innovative projects addressing societal problems in specific public policy areas; and the SIF.

The SIF is designed to support the final phase of social innovation and social entrepreneurship projects, aiding in the growth and consolidation of financially sustainable initiatives that yield significant social impact. These projects span various sectors, including: employment, training and education; social, financial and digital inclusion; active ageing; and health and well-being.

Originally part of the Operational Programme for Social Inclusion and Employment (OP SIE), SIF was later transferred to the Operational Programme for Competitiveness and Internationalisation (OP CI). In December 2018, PME Investimentos, then substituted by the Banco Português de Fomento, a wholly public financial entity, was officially appointed as the Fund Manager for SIF.

The SIF is structured as a hybrid model of fund with two distinct financial instruments: a debt financial instrument (guarantee), designed to ease access to finance for social economy entities; and an equity financial instrument to foster the social investment market.

The debt instrument entails providing guarantees to financial institutions, enabling them to offer loans to social economy entities under favourable conditions. This involves an 80% (fixed rate) deal-by-deal guarantee and counter-guarantee for loans with subsidised interest rates, covering up to 100% of costs related to social innovation or social entrepreneurship projects, capped at EUR 2.5 million. The loan has extended maturities, up to 10 years, with a 3-year grace period. Approval of loan requests is contingent on the financial intermediary's assessment.

On the other hand, the equity instrument entails partnering with private investors to co-invest in SMEs carrying out social innovation initiatives. Using a venture capital approach, SIF can provide up to 70% of the total co-investment, ranging from EUR 25 000 to EUR 2.5 million, for SMEs looking to enter the market. SIF offers up to 60% co-investment under comparable financial criteria for SMEs that have been in the market for fewer than seven years. The maturity is ten years, and co-investors have a call option that can be exercised within the first six years under different IRR circumstances.

The SIF is a compelling project as its loan and equity arms enable it to focus on projects and final recipients with strong financial foundations. This distinguishes it from other forms of support for social initiatives under ESF, ultimately promoting larger social projects and the social investment market.

In terms of accomplishments, at the end of 2023, the equity instrument had backed 17 investments totalling EUR 19.9 million[80].

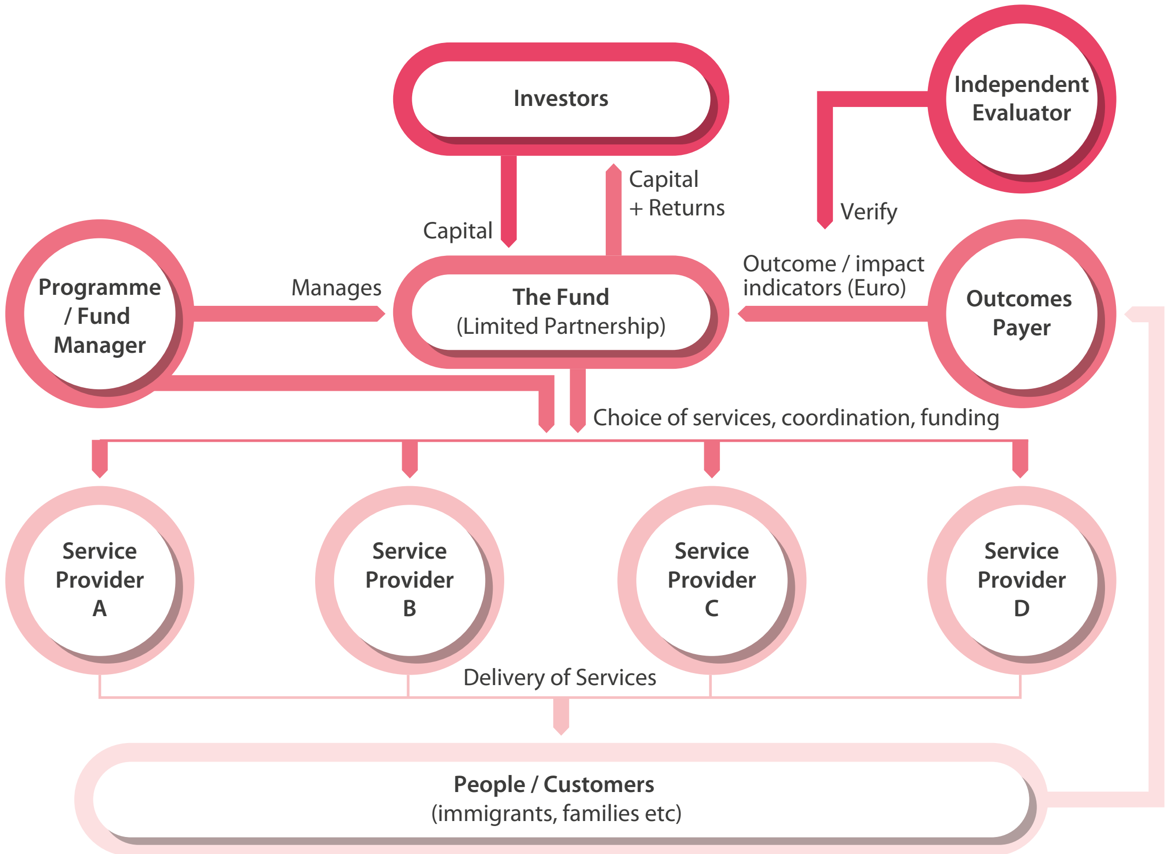
Social Outcomes Contracting (SOC), where a social service provider is remunerated through a 'payment by results' type of contract can also be supported through an **equity financial instrument**. In a SOC, the social service provider's compensation is linked to outcomes rather than specified tasks. An outcomes payer only pays the service provider if the outcomes are achieved. An equity financial instrument may invest in the company being set up to take on a SOC project, providing it with the liquidity it needs to set up and operate the service pending the commencement of outcome payments.

80 Information retrieved from the last report available from BP Fomento, available here.

Box 3.11: The KOTO SIB Programme, Finland[81]

Type of instrument: SOC
Financial size / Funding sources: 10 million from the EIF through the EFSI SME Window[82]
Final recipients: Service providers
Timing: 2018-2023
Governance: Ministry of Economic Affairs and Employment (managing authority)M Epiqus Oy (programme manager); Sitra, SOK Corporation, City of Espoo, Tradeka, Orthodox Church of Finland, Epiqus Oy, Tom Tukiainen (investors)
Description: The KOTO-SIB programme[83] was launched in 2017 for a period of three years by the Finnish Ministry of Economic Affairs and Employment. It supports migrants in finding employment by linking tailored vocational and language training to shortages in the Finnish labour market. It was designed to encompass language training, general career coaching, as well as more specific work skills.

Figure 3.11: The KOTO SIB governance structure



Source: Mika Pyykkö (2022), About SIBs and especially Koto SIB, Public Private Partnerships in Social Finance, June 21, 2022, Stockholm.

81 Based on EIB (2021), KOTO-SIB structure: fast integration and employment programme for immigrants in Finland, available here.
82 EFSI (European Fund for Strategic Investments) was the predecessor of InvestEU programme.
83 See also the website of the Finnish Ministry of Economic Affairs and Employment here.

The fund was set up as a limited partnership qualified as a social entrepreneurship fund under the EuSEF regulation[84] and received investors' commitments for EUR 14.2 million, with another EUR 10 million from the EIF, using EFSI SME Windows resources[85]. The fund manager has identified several social services providers from the training and recruitment sector[86] to provide migrants with work-life-oriented training to help them access the labour market and support them in their interactions with potential employers. Finally, an independent evaluator is expected to assess the impact of the programme and the amount of government savings[87].

The Ministry acts as the outcomes payer, i.e. it pays back investors for achieved outcomes and bears only the cost of proven impacts. As the achieved outcomes lead to cost savings (for the community and therefore for the government), investors are paid back through a portion of these savings. The government's budget savings are intended as the combined effect of the reduction in the provision of unemployment benefits and of an increase in income taxes collected from the salaries of employed migrants.

As of June 2022[88], nearly 2,200 migrants were involved, about 77% of whom had received training for at least 70 days. 1,219 in training had secured employment (71% of all the migrants involved in the programme). The savings to the government were estimated to be at least about EUR 15 20 million as of the end-2020.

3.3.4 Combination with grants

Financial instruments in **combination with grants** can be particularly appropriate for social enterprises. Grants, for instance, can finance technical support and business development and advisory services for persons managing or operating a social enterprise, to improve their managerial, financial and marketing skills and increase the quality of social services provided by the enterprise. Grants can also be in the form of interest rate subsidies, for instance only for loans financed by financial intermediaries using their own resources, to cover the difference between the market interest rate indicated by the intermediary and that applied to a loan from ESF+ resources. Finally, grants can be performance-based, for instance in terms of capital rebates, in which part of the loan is converted into a grant if a pre-agreed social outcome is achieved by the social enterprise. The social enterprise benefits from a reduction in capital due and repays the outstanding loan following a revised amortisation plan.

84 EU Regulation 2013/346/EU.

85 The other investors are: Sitra (EUR 1.5 million), SOK Corporation (EUR 1 million), City of Espoo (EUR 0.5 million), Tradeka (EUR o.25 million), Orthodox Church of Finland (EUR 0.2 million), Epiqus Oy (o.14 million) , Tom Tukiainen (EUR 0.1 million). Remaining resources were provided by Sewatek Oy, Erkki Turanlahti, and Arowana Advisors Oy.

86 In Finland social enterprises can adopt a variety of legal forms and ownership structures. The majority of social enterprises are limited companies (as in the case of the KOTO-SIB), but some are also cooperatives, foundations and associations. See European Commission (2019), *Social Enterprises and their Ecosystems in Europe – Country Report*, Finland.

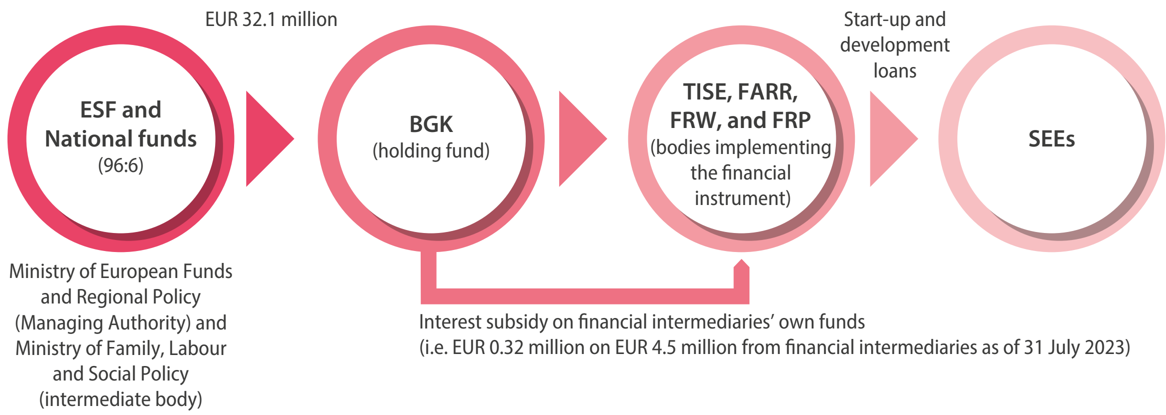
87 The programme ended on 31st December 2019 and foresaw a monitoring period of three years. The evaluation started at the end of 2022.

88 Mika Pyykkö (2022), *About SIBs and especially Koto SIB*, Public Private Partnerships in Social Finance, June 21, 2022, Stockholm. An external evaluation started at the end of 2022.

Box 3.12: The National Fund for Social Entrepreneurship, Poland[89]

The National Fund for Social Entrepreneurship (NFSE), during the 2014-2020 programming period, combined loan products with interest subsidies (see box 3.8 for details on the governance structure). They were paid by BGK to the four selected financial intermediaries (acting as the bodies implementing the financial instrument) who co-invested, providing additional capital of their own. The subsidies covered the difference between the market interest rate applied by the and the interest rate applied to a loan granted from ESF funds[90]. In this way, the preferential interest rate for each SEE loan was equalised regardless of the source of financing (i.e. whether the loan is funded by ESF, the state budget or the financial intermediary directly). Moreover, the interest rate could be further reduced for high social impact in terms of job creation. The interest rate subsidy contributed to reducing the cost of the loans for SEEs and attracting additional resources from the selected financial intermediaries.

Figure 3.12: NFSE combination structure



Source: Own elaboration.

For the 2021-2027 programming period, the managing authority is planning to implement a combination of loans and capital rebates using ESF+ resources[91]. This is in place of the interest rate subsidies used in the 2014-2020 programming period, which were perceived to be overly burdensome during the interviews. The NFSE will continue to finance both the start-up and development loans, and capital rebates will apply to both with the same conditions.

89 Based on fi-compass (2021), *Financing the Social Economy in Poland*, available here.
90 For the start-up loans, the interest rate is 1.06% per annum. If there is a commitment to create at least one new job as part of the project financed by the loan, the interest rate is reduced to 0.53% per annum- For the development loans, when the loan does not exceed EUR 22 500 or PLN 100 000, the interest rate is 1.14% per annum. If there is a commitment to create at least one new job as part of the project financed by the loan, the interest rate is reduced to 0.57% per annum. When the loan exceeds EUR 22 500 or PLN 100 000, the interest rate is 1.60% per annum. If there is a commitment to create at least one new job for every EUR 22 500 or PLN 100 000, the interest rate is reduced by 0.15% for each job.
91 See section 2.4 for the definition of a capital rebate.

A capital rebate of 25% will be applied when an SEE achieves measurable social effects, such as: 1) new job creation for people with disabilities or mental disorders; 2) new health or social services in the local community; 3) special access services; 4) green economy results. The rebate will be due if the following criteria are met:

- the borrower submitted a request for the rebate as part of the loan application;
- the borrower has achieved one of the social benefits listed under conditions 1-4 above: specifically, for condition 1, it has maintained the job/activity for at least 12 months, while for conditions 2-4, the entire loan is used for these purposes;
- the borrower has not experienced any delays in repaying the loan or any delays have not exceeded 30 days.

The rebate value may not exceed the total limit of 25% of the loan amount even if several types of social benefits are achieved simultaneously. The maximum rebate of 25% can be granted provided that at least one condition is met. The rebate is implemented to reduce the outstanding capital 12 months into the loan. If the outstanding capital falls below 25% of the initial loan (i.e. the eligible capital rebate), only the outstanding capital will be written off meaning the rebate will be less than 25%.

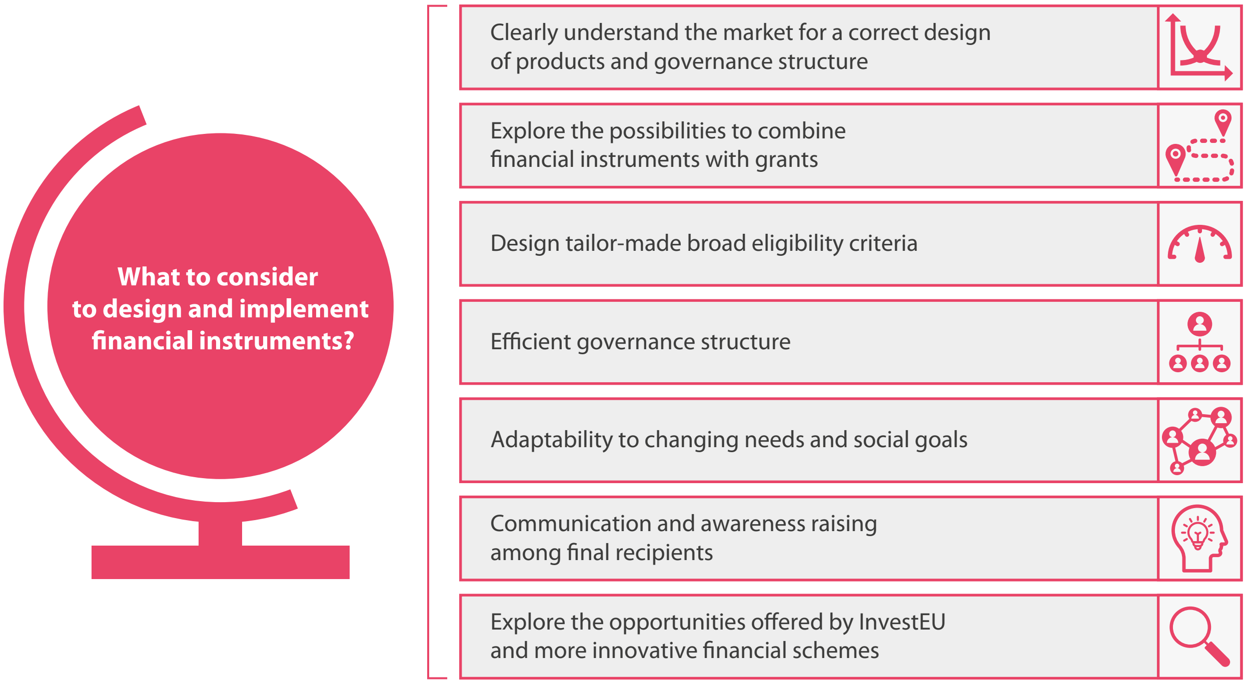
04 What to consider for efficient and effective use of financial instruments?

In times of public budget constraints and continuing crises (health emergencies, migration flows, war), using repayable forms of financial support to address social challenges is a more sustainable option as it allows for both the attraction of additional funding from the private sector and the re-use of resources for the benefit of additional final recipients. Designing and implementing financial instruments within the ESF+ necessitates a context-driven approach. These instruments should, in fact, address specific social needs which may vary across different disadvantaged groups and contexts. This requires identifying and adopting tailored financial solutions and establishing a governance structure involving financial intermediaries and bodies implementing the financial instruments experienced in addressing specific social challenges. Moreover, financial instruments can only support income-generating or cost-saving investments that enable the initial support to be repaid. This may be more challenging when the investment is led by typical ESF+ target groups.

It is fundamental that financial instrument design and implementation build on an **accurate assessment of the market situation** in order to provide clear evidence of the need for public intervention. Achieving social goals may require a long-term perspective, so predictability is key. Attention, therefore, should be paid to the ex-ante assessment and the investment strategy by identifying the final recipients' needs and expectations, the financial gap, and the most appropriate financial product tailored to the final recipients' repayment capacity. Stakeholder consultation and the involvement of relevant actors within the social economy in analysing the market could help managing authorities better design financial solutions. Capacity-building activities and awareness-raising may also be needed to increase knowledge about the potential of supporting ESF+ target groups through financial instruments. For instance, the capacity-building services offered by fi-compass could support managing authorities interested in advancing the design and set-up of financial instruments. These services address the specific needs of managing authorities related to preparing and implementing financial instruments and aim to strengthen their skills via specific initial and advanced capacity-building learning modules[92].

92 For additional information, see the brochure fi-compass (2017), *Capacity building services on financial instruments in support of ESF managing authorities*, available here.

Figure 4.1: Key aspects to consider for an efficient and effective use of financial instruments



Source: Own elaboration.

In designing the most appropriate form of financial support, the managing authorities should **consider a combination of financial instruments and grants**. Complementary support with grants can be crucial for implementing financial instruments within the ESF+. Moreover, the new flexibilities introduced in the 2021-2027 CPR allow managing authorities to exploit different solutions in terms of combination. Grants can decrease the cost of finance, equip final recipients with new skills and knowledge, and orientate financial resources towards impact-driven projects and investments. Even so, the need for a grant component should be clearly assessed in the ex-ante assessment.

In the design phase, managing authorities should consider **the importance of tailor-made, broad eligibility criteria** (for selecting intermediaries, final recipients and eligible expenditures) when designing a financial instrument to achieve social goals. Eligible criteria that are too restrictive may have a counter-productive effect on the final recipients (exclusion) and be less attractive to traditional financial intermediaries that already perceive the ESF+ key policy areas as being risky.

The implementation of financial instruments requires **institutional and administrative capacity and an efficient governance structure**. This step involves identifying and selecting the most appropriate financial intermediaries as the bodies implementing the financial instrument willing to engage in riskier projects and investments. Managing authorities should also be aware of the constraints that traditional financial intermediaries, such as banks, face when addressing social issues. Providing financial support to the typical ESF+ target groups may, in fact, require a large number of applicants to be dealt with for a small volume of individual finance, which may not appeal to traditional bank intermediaries. Therefore, managing authorities may also need to consider different or alternative types of financial intermediaries as the bodies implementing the financial instrument, such as non-bank entities that have experience and are better equipped to work in the social economy. Additionally, training and awareness initiatives might be considered to enhance the capacity of entities tasked with implementing financial instruments.

In choosing the implementation option and structure, **flexibility should be ensured to reflect changing needs or circumstances or to deal with unintended outcomes**. Feedback loops resulting from monitoring and evaluation and revisiting the financing gap are essential components of the capacity to adapt to changing requirements and conditions. Given the need to adapt to the changing environment and the potentially evolving social needs of final recipients, adjustments to the financial instrument investment strategy may also become necessary.

Communication and publicity measures are crucial for raising awareness among potential final recipients. Inadequate information flow may result in fewer final recipients applying to the financial instrument, especially among typical ESF+ target groups, who may have no means or knowledge to access such information. Activities such as seminars and networking can effectively inform and educate final recipients on the potential use of financial instruments. Additionally, using grants to finance pre-application training and advice, as well as project/ investment design, could equip potential final recipients with the necessary skills to fully exploit the opportunities offered by financial instruments.

Managing authorities should also explore **the possibilities offered by the EU indirect management instruments, such as InvestEU**. Financial resources from the ESF+ contributed to the InvestEU Fund, the Member State compartment, can increase the amount of funding available to financial recipients. The EU-level guarantee is, in fact, specifically designed to increase the participation of private resources co-investing in financial instruments, including contributions from social investors. These investors can foster social entrepreneurship and support the scaling of successful social innovations.

Finally, when the analysis reveals the presence of an advanced social economy, with experienced social providers and social investors, but highlights a mismatch between the demand and supply of finance, managing authorities **can explore more innovative solutions such as those offered by SOC schemes**. While these instruments may be more complex to design and set up, they can provide significant added value in addressing social needs and reducing barriers for social organisations to access finance and scale up. Moreover, they can contribute to changing the mindset of public bodies, called to make more efficient use of public resources and urge final recipients to identify innovative approaches to achieve social goals.

ANNEX I: Additional resources and publications on financial instruments

ESF/ESF+ documents

Document / Resource	Theme
fi-compass (2015), *Developing an action plan*, available here.	Action plan
fi-compass (2016), *Financial instruments working with microfinance*, available here.	Microloans
fi-compass (2016), *Financial instruments working with personal loans*, available here.	Personal loans
fi-compass (2016), *Financial instruments working with social entrepreneurships*, available here.	Financial instruments for social enterprises
fi-compass (2016), *Introducing financial instruments for the European Social Fund*, available here.	Financial instruments in ESF
fi-compass (2017), *Capacity building services on financial instruments in support of ESF managing authorities*, available here.	Capacity building services for ESF
fi-compass (2019), *Survey on financial instruments under the European Social Fund (ESF) – Reflections at present and ideas for future*, available here.	Financial instruments in ESF
fi-compass (2020), *Crowdfunding and ESF opportunities: future perspectives for managing authorities*, available here.	Crowdfunding financial products
fi-compass (2020), *Supporting the development of Social Finance Ecosystems in Member States under ESF*, available here. here.	Financial instruments in ESF
fi-compass (2021), presented at the 'ESF+ financial instruments responding to social challenges in Europe' event, 2 December 2021, available here.	Financial instruments in ESF+
Lagarre V. and Kerpel-Fronius A. (2021), *InvestEU: Social Investment Skills Window and Member State Component*, fi-compass, presented at the 'ESF+ financial instruments responding to social challenges in Europe' event, 2 December 2021, available here.	InvestEU
EIF's InvestEU Portfolio Guarantee Products, available here.	EIF's financial products under InvestEU
Zalite Leva (2021), *The regulatory framework for financial instruments – The new CPR, in fi-compass 'ESF+ financial instruments responding to social challenges in Europe'*, on-line event 2 December 2021, available here.	Regulatory framework for 2021-2027 financial instruments
fi-compass (2022), *Financial instruments for education and learning*, available here.	Financial instruments for education

Case studies

Document / Resource	Theme
fi-compass (2016), *Mikromezzaninfonds, Germany*, available here.	Quasi-equity
fi-compass (2021), *Financing the Social Economy in Poland*, available here.	Loans
EIB (2021), *KOTO-SIB structure: fast integration and employment programme for immigrants in Finland*, available here.	SOC
fi-compass (2021), *Financing the Social Economy in Poland*, available here.	Loans
fi-compass (2022), *ESF financial instruments in the Slovak Republic*, available here.	Guarantees and equity
f-compass (2022), *Mikrodarlehen - Microloans for entrepreneurs and start-ups in Saxony, Germany*, available here.	Loans
fi-compass (2022), *ESF Financial instruments for microfinance in Bulgaria*, available here.	Loans and guarantees

General documents

Document / Resource	Theme
Cohesion Data Portal, available here.	Cohesion policy database
European Commission (2015), *Guidance for Member States on financial instruments – Glossary*, available here.	EC's guidance on financial instruments
fi-compass (2015), *Financial instruments products – Loans, guarantees, equity and quasi-equity*, available here.	Financial products
European Commission (2020), *Social enterprises and their ecosystems in Europe - Comparative synthesis report*, available here.	Social economy
fi-compass (2021), *Combination of financial instruments and grants under shared management funds in the 2021-2027 programming period*, available here.	Combination of financial instruments with grants
fi-compass (2021), *fi-compass Knowledge Hub – Combination of financial instruments with grants – Notes of workshop*, available here.	Combination of financial instruments with grants

European Commission (2023), *Financial instruments under the European Structural and Investment Funds - Summaries of the data on the progress made in financing and implementing the financial instruments for the programming period 2014-2020 in accordance with Article 46 of Regulation (EU) No 1303/2013 of the European Parliament and of the Council - Situation as of 31 December 2022*, available here.	Data on financial instruments in ESIF
European Investment Bank (2021), *Social Outcomes Contracting in Europe*, available here.	Social outcomes contracting
European Commission (2021), *Study on the benefits of using social outcome contracting in the provision of social services and interventions – a cross-country comparative assessment of evolving good practice in cross-sectoral partnerships for public value creation*, available here.	Social outcomes contracting
EVPA (2022), *Accelerating Impact - Main takeaways from the first harmonised European impact investment market sizing exercise*.	Impact investment
fi-compass (2022), *ERDF Equity financial instruments*, available here.	Equity products
Regulation (EU) 2021/1057 of the European Parliament and of the Council of 24 June 2021 establishing the European Social Fund Plus (ESF+) and repealing Regulation (EU) No 1296/2013, available here.	ESF+ legislative framework
Regulation (EU) 2021/1060 of the European Parliament and of the Council of 24 June 2021 laying down common provisions on the European Regional Development Fund, the European Social Fund Plus, the Cohesion Fund, the Just Transition Fund and the European Maritime, Fisheries and Aquaculture Fund and financial rules for those and for the Asylum, Migration and Integration Fund, the Internal Security Fund and the Instrument for Financial Support for Border Management and Visa Policy, available here.	CPR legislative framework
Delegated Regulation (EU) 2021/1078 of 14 April 2021 supplementing Regulation (EU) 2021/523 of the European Parliament and of the Council by setting out the investment guidelines for the InvestEU Fund, available here.	InvestEU legislative framework

ANNEX II: Financial instruments planned under ESF+ by EU Member State and policy area

Table A.1: 2021-2027 planned financial instruments for employment

Member State	Programme name	SO	Type of financial instrument	EU amount	Total amount	Short description
Croatia	Efficient Human Resources - HR - ESF+ (2021HR05SFPR001) Link	4.1	Grants within a FI operation	12 750 000	15 000 000	The financial instrument combines micro-loans and grants to stimulate investments in projects led by micro and small entrepreneurs as well as entrepreneurs aligned with socio-entrepreneurial principles. It will further support investments in **socially innovative forms of business** financing projects with an emphasis on developing new models, products and/or services and scaling existing social innovations and networking activities.
			Loan	29 750 000	35 000 000	
France	Occitanie ERDF-ESF+ (2021FR16FFPR004) Link	4.1	Guarantee	2 800 000	4 666 667	The financial instrument aims at supporting **social economy entities** (SEEs) and the development of projects led by them by facilitating financing from private financial organizations (such as bank intermediaries and business loan associations). It may include bank loan guarantees. Following the ex-ante study, additional financial instruments, dedicated to SEEs and/or individual entrepreneurship, may also be explored.
			Loan	7 200 000	12 000 000	
France	Île-de-France et bassin de la Seine - ERDF/ESF+ (2021FR05FFPR001) Link	4.1	Guarantee	5 000 000	12 500 000	The financial instrument will offer a guarantee to companies to facilitate their access to bank loans and to support the creation and development of small and medium-sized businesses, particularly in the field of **social economy**. The instrument is also expected to support employment and social innovation, in particular via social economy companies. Indeed, Île-de-France has a network of social economy companies that are among the most innovative in France but which sometimes lack resources.
Italy	Youth, Women and Jobs - IT - ESF+ (2021IT05SFPR001) Link	4.1	Loan*	106 848 044	178 080 073	The financial instrument supports **self-employment and entrepreneurship** by offering subsidised loans. Its primary target groups include NEETs, young people who have just completed their education and are seeking work; young people who are able to work but are not actively seeking employment; and young people who are unable to actively participate due to family responsibilities or health issues.
			Loan**	6 128 075	15 320 188	
			Loan***	34 676 627	86 691 568	

Italy	Abruzzo - ESF+ (2021IT05SFPR002) Link	4.1	Grants within a FI operation	8 000 000	20 097 561	The financial instrument, in the form of microcredit, will support applicants in creating and developing new businesses. The tool is intended to help **young people** access credit and support new youth entrepreneurship.
			Grants within a FI operation	7 400 000	18 822 968	The financial instrument will take the form of a guarantee for the creation of **new businesses in internal areas**. To support newly established micro- and small businesses, the initiative also offers post-business start-up services financed by grants.
			Grants within a FI operation	7 400 000	18 822 968	The financial instrument is intended for the creation of new businesses owned by **women**. Additionally, to support newly established micro- and small female-owned businesses, post-business start-up services will also offered with particular attention to the specific needs of new businesses.
	Basilicata - ERDF/ESF+ (2021IT16FFPR004) Link	4.1	Loan	1 750 000	2 500 000	The financial instrument, in the form of microcredit, will extend the approach from the 2014-2020 programming period. It will target the **unemployed or inactive young people**, as well as **NEETs**, along with young adults **up to the age of 35**.
			Loan	3 714 273	5 306 104	The financial instrument, in the form of microcredit, aims to support micro-enterprises with a focus on those initiated by **individuals in vulnerable situations** or those who employ them during their start-up and development phases.
		4.3	Loan	1 400 000	2 000 000	The financial instrument, in the form of microcredit, aims to support micro-enterprises during their start-up and development phases, with a focus on enterprises initiated by **women** in vulnerable situations or those who employ them.
	Calabria - ERDF/ESF+ (2021IT16FFPR003) Link	4.1	Loan	769 785	1 099 693	The initiative will set up funds aimed at providing small loans to support **business creation and self-employment** for young people, long-term unemployed people and other disadvantaged groups.
			Grants within a FI operation	769 784	1 099 691	
		4.3	Loan	549 847	785 496	The financial instrument will provide small loans to support business creation and self-employment. The primary focus is on **women** who are unemployed or inactive, including those involved in caregiving and activities providing assistance for family members.
			Grants within a FI operation	549 845	785 493	

Italy	Campania - ESF+ (2021IT05SFPR003) Link	4.1	Loan	20 000 000	28 571 429	Financial instruments (such as microcredit) are expected to be used within the priorities for **youth employment** for the start-up and development of businesses, including freelance activities or self-employment. The financial instruments may be supplemented with grants.
			Grants within a FI operation	10 000 000	14 285 714	
			Loan	25 000 000	35 714 286	Financial instruments are expected to be used within the employment priorities for the start-up and development of businesses, including freelance or self-employment. The target recipients are **unemployed or inactive individuals**, as well as those facing the **risk of job loss**. The financial instruments may be supplemented with grants.
		4.4	Loan	4 500 000	6 428 571	Financial instruments may be used within the employment priority to fund **worker buyouts**. The primary recipients could include workers experiencing ordinary and extraordinary layoffs, those involved in company restructuring processes and workers in precarious situations. The financial instrument may be supplemented with grants.
			Grants within a FI operation	4 500 000	6 428 571	
	Lazio - ESF+ (2021IT05SFPR006) Link	.4.1	Loan	1 400 000	3 500 000	The financial instrument 'Microcredito Fondo Futuro' provides subsidised loans for the creation of self-employment projects through the start-up of new businesses (micro and small businesses) or professional activities. These small loans are offered at a subsidized rate to individuals facing difficulties in accessing bank credit, with **women** being a primary focus.
			Loan	3 200 000	8 000 000	The financial instrument the 'Microcredito Fondo Futuro' primarily targets **individuals over the age of 35**.
			Loan	1 400 000	3 500 000	The financial instrument the 'Microcredito Fondo Futuro' primarily targets **individuals up to 35 years old**.
	Sicilia - ESF+ (2021IT05SFPR014) Link	4.1	Loan	898 298	1 283 283	The financial instrument can provide microloans to support business creation and self-employment for **young people, unemployed adult workers (recipients over 35 years of age), the long-term unemployed, unemployed adults or inactive people**.
		4.3	Loan	1 401 424	2 002 034	The financial instrument can be used to provide microloans to support business creation and self-employment for **unemployed women, the long-term unemployed and other disadvantaged female workers.**

Italy	Sardegna - ESF+ (2021IT05SFPR013) Link	4.1	Loan	13 191 150	18 844 500	The financial instrument is an evolution of a similar Fund activated in 2014-2020 and will promote microfinance interventions. These microcredits aim to foster **entrepreneurship, the start-up and development of businesses, including freelance and self-employment.** Based on the result of the ex-ante evaluation, accompanying services, in the form of tutoring, consultancy, training and mentoring, including customised services, may be offered in conjunction with the microcredit.
		4.4	Equity or quasi-equity	10 877 132	15 538 760	The action supports **social enterprises** and the third sector (mainly existing companies), including the case of **worker buyouts**. As an evolution of a similar fund activated in the 2014-2020 programming period targeting the third sector with particular attention to cooperatives, the aim is to promote the social economy in the Region. Quasi-equity is the preferred financing option, but vouchers for specialists and training services will also be considered.
Poland	Social Development - PL - ESF+ (2021PL05SFPR001) Link	4.1	Loan*	97 477 648	114 679 586	The financial instrument will provide preferential loans for people intending to start a business to support **self-employment**. The loans may also be combined with grant support in the form of a partial capital write-off to finance training and advisory support. The refundable support for starting a business is expected to be implemented uniformly throughout the country based on the "First business - Start-up support" programme.
			Grants within a FI operation*	17 634 990	20 747 047	
			Loan**	5 493 763	7 848 233	
			Grants within a FI operation**	993 894	1 419 849	
			Loan***	2 864 715	5 729 430	
			Grants within a FI operation***	518 265	1 036 530	
Romania	Education and Employment – RO – ESF+ (2021RO05SFPR001) Link	4.1	Guarantee*	38 000 000	44 705 882	The interventions foresee support to the **social economy sector** for the development/ innovation/scaling/expansion of social enterprises, including social services and the cultural and creative sectors. Grants will also be provided for assistance, training, consulting, and mentoring to access and use combined financial instruments. These will also include training programmes for staff within these entities and support for the digitization of their activities.
			Grants within a FI operation*	38 000 000	44 705 882	
			Guarantee***	2 000 000	5 000 000	
			Grants within a FI operation***	2 000 000	5 000 000	

* Less developed regions; ** Transition regions; *** Developed regions

Source: own elaboration based on Cohesion Data portal as of 10 April 2024 (available here) and on the 2021-2027 ESF+ Operational Programmes.

Table A.2: 2021-2027 planned financial instruments for education

Member State	Programme name	SO	Type of financial instrument	EU amount	Total amount	Short description
Bulgaria	Education - BG - ESF+ (2021BG05SFPR001) Link	4.5	Guarantee*	2 295 218	2 700 256	Various financial instruments, in the form of guarantees, loans, and equity products, will support the start-up of own businesses and other entrepreneurial activities by **students, PhD students and lecturers in higher education institutions**. The structuring of financial instruments is envisaged to encourage potential target groups to invest in entrepreneurial skills by providing easier access to financial resources, more favourable terms and additional incentives from Programme Education funds.
			Loan*	2 295 218	2 700 256	
			Equity or quasi-equity*	4 590 436	5 400 513	
			Guarantee**	1 031 185	1 473 121	
			Loan**	1 031 185	1 473 121	
			Equity or quasi-equity**	2 062 369	2 946 241	
Malta	Human Resources and Skills – MT – ESF+ (2021MT05SFPR001) Link	4.6	Guarantee	3 000 000	5 000 000	The intervention aims at increasing the participation of students in **high level education** (courses in levels 5-8 and other internationally recognised certificates). Building on the financial instruments utilised in the 2014-2020 programming period (i.e. Further Studies Made Affordable), a combination of a guaranteed soft loan and a grant in the form of an interest rate subsidy is foreseen. Areas of support may include tuition fees, accommodation costs and subsistence expenses, amongst others.
Poland	Pomorze - PL - ERDF/ESF+ (2021PL16FFPR011) Link	4.7	Loan	12 585 972	14 807 026	The financial instrument will be structured as a debt instrument to support **adults** seeking to **improve or confirm their competences and/or obtain qualifications** (including those listed in the Integrated Qualifications Register). Preference will be given to projects developing competences and acquiring qualifications: tailored to the needs of regional Smart Specialization and key industries crucial for the development of specific areas of the voivodeship; focusing on the development of digital competences; in sectors related to the environment, climate, energy, circular economy and bioeconomy.

Poland	Social Development - PL - ESF+ (2021PL05SFPR001) Link	4.7	Loan*	27 742 316	32 638 019	A financial instrument in the form of loans will be launched to finance the **participation of adults in various forms of education** undertaken on their own initiative, e.g. postgraduate studies, courses, training and other forms of education offered by domestic and foreign entities (except first-, second- and third-cycle studies and uniform master's studies). Loans will be combined with a grant in the form of a write-off of part of the loan capital.
			Grants within a FI operation*	12 553 084	14 768 334	
			Loan**	1 563 535	2 233 621	
			Grants within a FI operation**	707 482	1 010 689	
			Loan***	815 303	1 630 606	
			Grants within a FI operation***	368 916	737 832	
Spain	Aragon - ESF+ Link	4.6	02 Financial instruments: equity or quasi-equity	4 000 000	10 000 000	N/A

* Less developed regions; ** Transition regions; *** Developed regions

Source: own elaboration based on Cohesion Data portal as of 10 April 2024 (available here) and on the 2021-2027 ESF+ Operational Programmes.

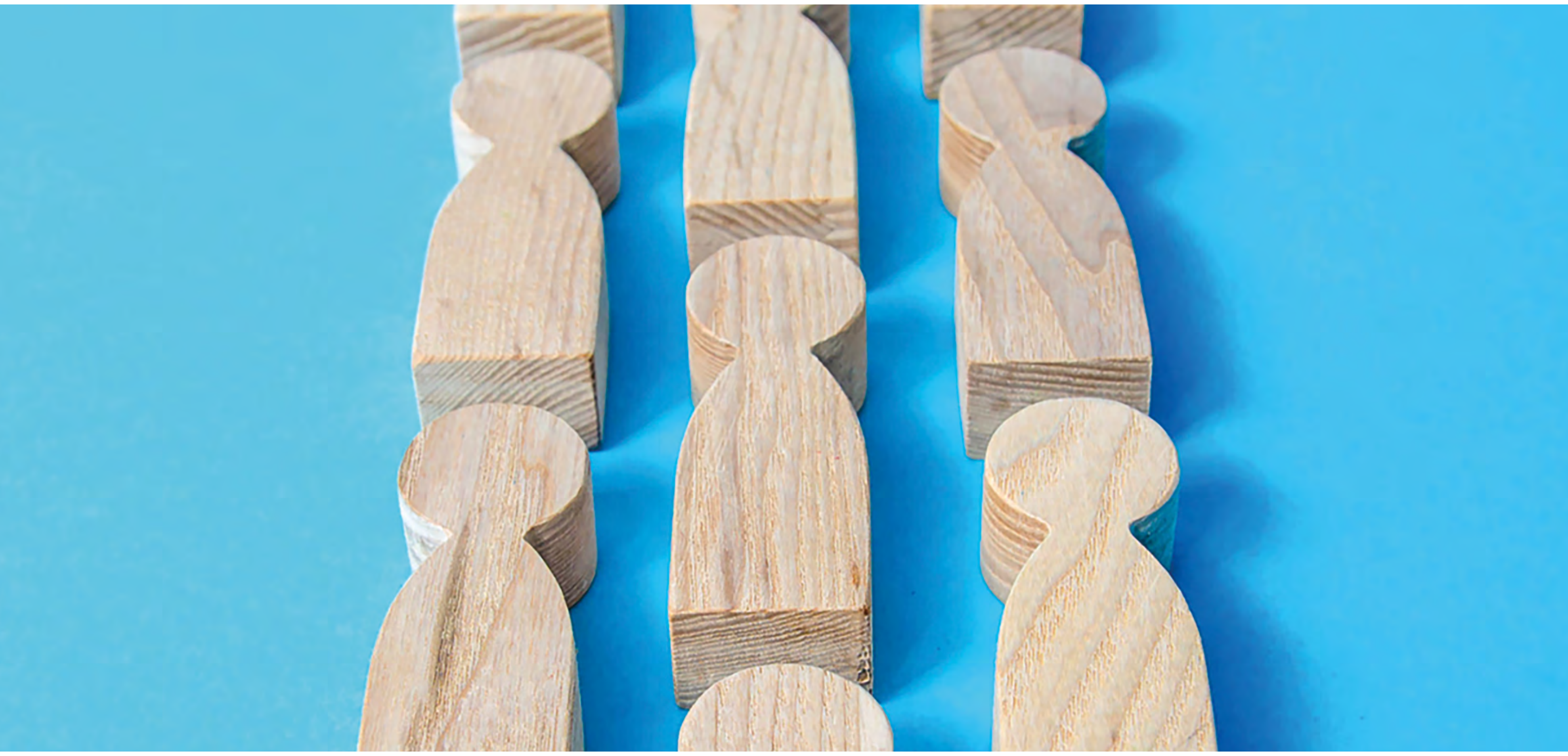
Table A.3: 2021-2027 planned financial instruments for social inclusion

Member State	Programme name	SO	Type of financial instrument	EU amount	Total amount	Short description
Czech Republic	Employment - CZ - ESF+ (2021CZ05SFPR001) Link	4.8	Loan*	6 141 845	7 225 700	The intervention 'S-Enterprise Plus programme' (based on the 2014-2020 experience) offers preferential loans for the financing of investment projects and working capital expenses of **social enterprises supporting disadvantaged people integrating into the labour market**. The programme facilitates start-ups and business development and provides relief for cash flow challenges arising from timing discrepancies between income and expenses. In addition to the preferential loans, the programme also offers advisory services to social enterprises.
			Loan**	5 507 114	7 867 306	
			Loan***	73 326	73 326	
Italy	Calabria - ERDF/ESF+ (2021IT16FFPR003) Link	4.8	Loan	1 319 631	1 885 187	The financial instrument encourages active inclusion and promotes equal opportunities, non-discrimination, and active participation to **improve employability, particularly in disadvantaged groups**. The primary focus is on unemployed workers, women, young people, inactive, people with disabilities, migrants, and disadvantaged people at risk of social exclusion or discrimination.
			Grants within a FI operation	1 319 631	1 885 187	
	Sicilia - ESF+ (2021IT05SFPR014) Link	4.8	Loan	229 157	241 218	N/A
			Loan	392 841	561 201	A microcredit fund will be established to bolster the employability of **individuals particularly at risk of social exclusion** such as people with disabilities, victims of violence and abuse, and those facing discrimination. Third-sector associations will also be among the final recipients.
	Sardegna - ESF+ (2021IT05SFPR013) Link	4.8	Loan	4 303 040	6 147 200	A financial instrument aimed at promoting **Social Impact Investing** in the social economy will be activated, building on a similar instrument from the 2014-2020 programming period. This instrument is expected to comprise loans but will also consider equity or quasi-equity and grants.

Poland	Social Development - PL - ESF+ (2021PL05SFPR001) Link	4.8	Equity or quasi-equity*	5 636 078	6 630 680	The financial instrument aims to support **social economy entities** at different stages of development by addressing their diverse needs. It will offer start-up and development loans in combination with grants, as well as equity or quasi-equity financing for entities with substantial growth potential.
			Loan*	19 463 569	22 898 316	
			Grants within a FI operation*	5 724 579	6 734 799	
			Equity or quasi-equity**	317 645	453 779	
			Loan**	1 096 951	1 567 073	
			Grants within a FI operation**	322 633	460 904	
			Equity or quasi-equity***	165 636	331 272	
			Loan***	572 004	1 144 008	
			Grants within a FI operation***	168 236	336 472	
		4.11	Loan*	9 927 185	11 679 041	The financial instrument will support entrepreneurs in adapting their business activities to increase **accessibility to people with special needs**, thereby ensuring compliance with both national regulation and the European Accessibility Act (EAA), assuming that economic entities are obliged to apply common accessibility principles. For this purpose, preferential loans will be offered with the possibility of partial loan capital cancellation. The instrument will be complemented with grants to finance training and advisory activities enabling entrepreneurs to learn how to align their activities to the provisions of the EAA directive.
			Grants within a FI operation*	2 882 086	3 390 689	
			Loan**	559 488	799 269	
			Grants within a FI operation**	162 432	232 046	
			Loan***	291 744	583 488	
			Grants within a FI operation***	84 700	169 400	

* Less developed regions; ** Transition regions; *** Developed regions

Source: own elaboration based on Cohesion Data portal as of 10 April 2024 (available here) and on the 2021-2027 ESF+ Operational Programmes.



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