

Baltère R., Jermolajeva E.

Daugavpils University, Latvia

**Government-Supported Credit Programmes for Entrepreneurs –
Impact on Regions of Latvia**

Summary

Entrepreneurship in Latvia receives state support under the Latvian National Development Plan 2007-2013, which is the main state medium-term planning document. The programme sets the strategic objective and defines priorities for developing a knowledge-based national economy. These priorities are based on an educated and creative personality, technological excellence, flexibility of industries, and development of science and research. In 2005-2007 Latvia experienced several years long rapid economic growth, the increase of gross domestic product (GDP) was the sharpest in the European Union. Since mid 2007, as the result of global financial crisis, the growth slowed down, and in 2008 it was negative. The tendency remained negative in 2009, too. The Ministry of Economics has elaborated a plan for stabilization of economy that foresees providing of small and middle enterprises (SMEs) that are in need of attracting financial resources, with state support; and effective implementation of this plan will foster stabilization of economy. The Ministry of Economics in cooperation with the Ministry of Finance and members of non-governmental organizations representing business sector have defined concrete measures for raising the economic competitiveness together with shifting 603 million Latvian lats into support of entrepreneurship. Commercial activity support measures include loans, guarantees by the Latvian Guarantee agency (*Latvijas Garantiju Aģentūra*), state guarantees and support instruments, such as risk capital and technology transfer. Lending programmes involving state and the European Union support is a way for the state to stimulate development of national economy of Latvia; credit guarantees give opportunity for entrepreneurs to raise borrowed funds. In situation when all economic sectors experience sharp drop, it is very important to uptake these state funds properly, as well as to precisely define the prior sectors and regions to be supported.

Key words: credit, entrepreneurship, guarantees, state support, grant.

Competitive economy needs developing of an environment favourable for business activity, which ensures growing domestic and foreign investments, and thus creates main

conditions for economic development. Small and middle enterprises form the background of business activity in Latvia. One of conditions for an enterprise to successfully implement its ideas is sufficiency of financial resources. In economic situation when enterprises lack their own resources, it is vital for them to implement their projects using borrowed financial resources. Enterprises need state support for advancing of production development, introduction of innovations, keeping of the existing work places and creation of new ones. The European Union (EU) member states implement various state aid lending programmes on a regular basis. Since Latvia is a member of the EU, entrepreneurs in Latvia also have an opportunity to participate in state aid programmes co-financed by the EU funds – European Social Fund (ESF) and European Regional Development Fund (ERDF). The objective of lending programmes for small and middle enterprises under the ESF and ERDF is to raise their competitiveness, promote business start-ups and establishing of new companies, to educate potential employers, maintain and expand business activity of operating enterprises. The programmes implemented in Latvia are co-financed by the EU funds, the rest of resources to these programmes are allocated by the state budget and the Mortgage Bank (*Hipotēku banka*). Attaining of the aim – facilitation of SMEs functioning – depends on implementation success of these programmes.

An intermediary to implement state aid lending programmes is the Mortgage Bank, which is the only state-owned bank in Latvia experienced in meeting this kind of mission. The Mortgage Bank has implemented several development programmes in the context of which, commissioned by the Government, support for definite groups of entrepreneurs and population was provided – Small and Medium-sized Enterprises Lending Programme, Housing Development Lending Programme, rural development programmes, Lending Programme for Long-term Investments in Agriculture, Non-agricultural Entrepreneurship Development Lending Programme. Programmes implemented by the Mortgage Bank have been successful and have proved that the initial stage of establishing a prosperous enterprise requires state supported attracting of financial resources.

Aim of the research – to evaluate impact of the state aid lending programmes on the national economy of Latvia and business development.

Research objectives:

- 1) To analyze the results of Non-agricultural Entrepreneurship Development Lending Programme (NEDLP) implemented by the Mortgage Bank;
- 2) To evaluate the results of the lending programmes implemented by the Promotional programmes office ALTUM of the Mortgage Bank;
- 3) To analyze the activity of Rural Development Fund and Latvian Guarantee Agency.

Research methods:

- 1) Qualitative research method;
- 2) Method of statistical analysis (data grouping, comparative analysis, calculation of average rates).

Market economy requires constant development of enterprises, implementation of new projects, perfection of goods and services, introduction of innovations. One of the cornerstones of profitable business is sufficiency of financial resources, and the main source of financing entrepreneurial activities nowadays is loans offered by credit institutions. Loans perform several functions in national economy:

- Function of redistribution – ensures redistribution of capital in national economy, shifting it from one sector into another, from one owner to another.
- Economy of circulation expenses – increases the proportion of productive capital, as well as production facility and profit rate.
- Function of national economy control – regulates the movement of capital in national economy and economic processes.

The main indicators characterizing development of national economy are gross domestic product (GDP), employment rate, etc., but for this research it is important to analyze the operation of financial sector in the field of granting loans.

In 2004-2007, national economy of Latvia experienced rapid growth, the GDP increased by 10,9% on average annually, including by 10,0% in 2007. This growth rate was mostly maintained by domestic demand; both private consumption and investments increased substantially. In 2007 the growth rate began to slow down, and in the 2nd quarter of 2008 it became negative. The recession of Latvian economy was largely determined by global financial crisis, which reduced both domestic and foreign demand in Latvia. While global financial problems became more acute, Latvia in 2008 and 2009 plunged deeper into recession. The impact of financial crisis was enhanced by the explicitly unbalanced external sector of Latvia having developed during the years of previous rapid growth. The substantial increase of private demand and investments, being more rapid than general economic growth, was caused largely by considerable inflow of external capital. In 2008, domestic demand reduced sharply. The rapid increase during previous years based on banks' open lending policy. As the result of global financial crisis, the amount of loans offered by banks decreased sharply and banks became cautious about their credit policy¹.

¹ *Ziņojums par Latvijas tautsaimniecības attīstību*, LR Ekonomikas ministrija, Rīga 2008.gada jūnijs, 9.lpp.

The increase or decrease of GDP directly affects every individual. According to the World Bank data, the highest GDP per 1 inhabitant in 2008 was in Luxemburg – 113 044 US dollars. In Latvia it was 14 997 US dollars in actual prices of 2008 or 13,27% of GDP per 1 inhabitant of Luxemburg.

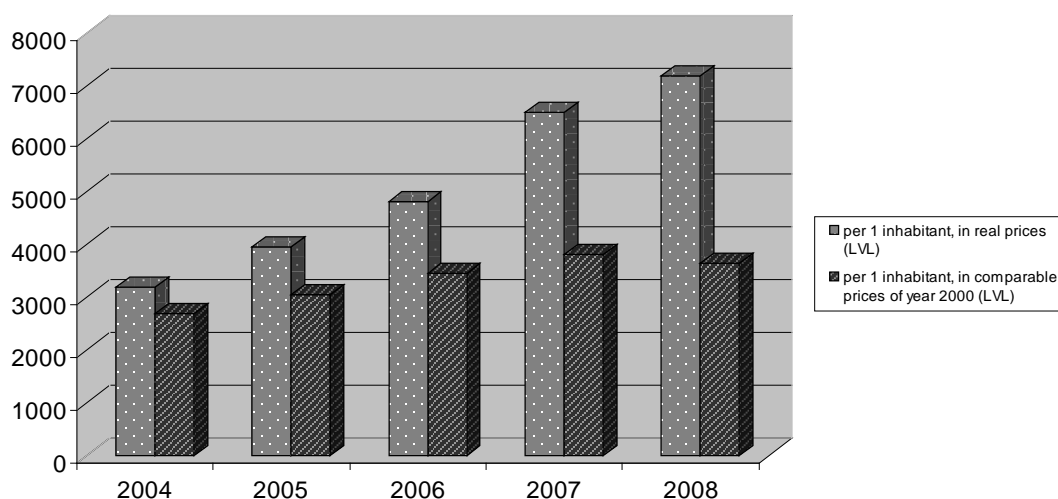


Figure 1. GDP per 1 inhabitant of Latvia in 2004- 2008 (LVL)²

Nevertheless, the sole analysis of GDP index does not precisely describe the overall development of national economy. This index should be viewed together with other economic indicators, e.g. employment. The rapid economic growth in 2004-2007 in Latvia influenced the labour market: employment increased, the unemployment rate diminished and the number of economically active population raised. Due to deteriorated demographics and as a result of other factors – social, economic and political – residents of Latvia reduced in number. In 2004, there were 2 319 203 residents, but in 2008, there were only 2 270 894 of them. Figure 2 displays the proportion of economically active population and the total number of inhabitants in Latvia. The economically active population, in accordance with International Labour Organization methodology, is represented by both males and females offering, in the accounting period, the material assets of their work for production or services.

An indicator of national economy is unemployment rate, expressed as a percentage of able-bodied population. In 2005-2007, the percentage of working population increased by 2,9% on average annually (see Figure 2), but the unemployment rate decreased, it accounted for 10,4% in 2004, but in 2007 – 6%. The sharp economic recession in 2008 had negative

² <http://data.csb.gov.lv/Dialog/Saveshow.asp>

effect on the Latvian labour market³. In the end of 2008, the unemployment rate reached 7%, but in 2009 – 20% already.

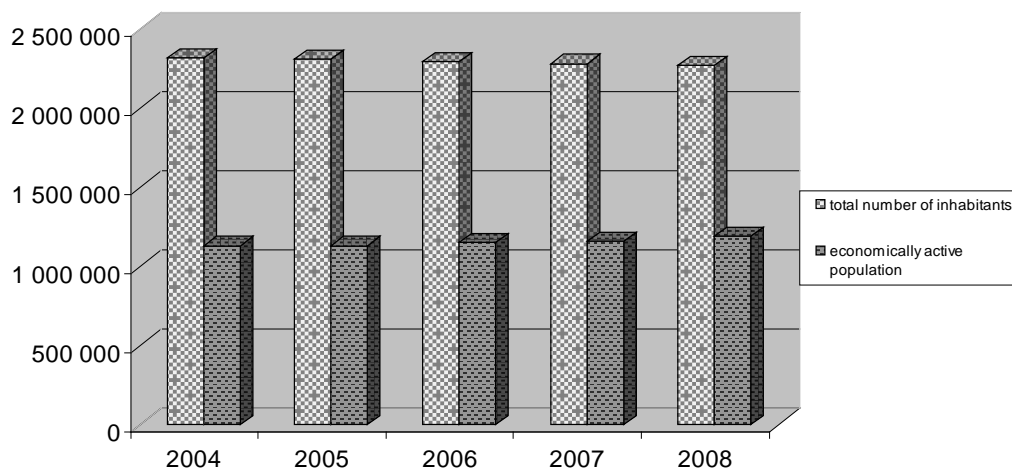


Figure 2. Total number of inhabitants in Latvia and economically active population in 2004-2008

The sharp GDP increase in 2004-2007 was interconnected with the fast increment rate of lending in Latvia. When compared the data on GDP dynamics (Figure 1) and the granted loans' dynamics (Table 1) – similar tendencies can be observed. The amount of loans granted in 2004-2007 increased by 341%, including mortgage loans – by 549%.

³<http://www.em.gov.lv/em/2nd/?cat=137>

Table 1**Types of loans granted in Latvia in 2004-2008 (LVL, thsd.)⁴**

Types of loans	2004	2005	2006	2007	2008
Mortgage loans	1 431 944	2 908 771	5 586 787	7 855 995	8 818 415
Current asset loans (commercial credits)	1 223 539	1 923 855	2 424 261	3 015 193	3 330 654
Industrial loans	838 518	1 230 313	1 428 140	1 989 827	2 167 755
Loans for commodities	193 272	268 589	433 785	616 317	668 949
Other	693 292	628 812	999 882	1 438 793	1 431 983
Total:	4 380 565	6 960 340	10 872 855	14 916 115	16 588 864

Sound national economy requires financial institutions helping to implement promotional programmes for small and middle enterprises. The universal practice shows that state-owned banks – Development banks – are responsible for dealing with these issues, in general. The German Kreditanstalt für Wiederaufbau (KfW) is well-known in Europe. The KfW bank group stimulates global economy. As a confederation and state-owned development bank, it promotes sustainable programmes for improvement of economy, social and ecological programmes. The KfW bank programmes are aimed at funding SME, environmental, housing, infrastructure, education projects and export⁵.

Latvia has the following state aid lending programmes:

- 1) Training, consultations and financial support for business start-ups and self-employment (administrated by the Mortgage Bank);
- 2) Loans for raising the competitive capacity of enterprises (administrated by the Mortgage Bank);
- 3) Guarantees by the Rural Development Fund (*Lauku attīstības fonds*) and Latvian Guarantee Agency.

⁴ http://www.fktk.lv/lv/statistika/kreditiestades/ceturksna_parskati

⁵ Harries, H. KfW-the German Bank with a Public Mission, 1998,56 p.

The Mortgage Bank is an intermediary institution in Latvia that implements special programmes for regional development. It has implemented several promotional programmes, commissioned by the Government, in the framework of which definite groups of entrepreneurs and population were provided with support – Small and Medium-sized Enterprises Lending Programme, Housing Development Lending Programme, rural development programmes. The Lending Programme for Long-term Investments in Agriculture was implemented in 2002, and in January of 2003 the approved Non-agricultural Entrepreneurship Development Lending Programme was launched. The Mortgage Bank, as an intermediary institution, also implements lending programmes for SMEs, co-financed by the state and the European Union.

Due to decrease in number of population working in farming, inhabitants of rural areas are in growing need of finding new occupation without looking for job in cities or abroad. In order to meet those needs and to promote common development, the Cabinet of Ministers approved the Programme on Non-agricultural Entrepreneurship Development Lending on October 14, 2002, the practical implementation of which was launched in 2003 and continued until 2009. The overall objective of the programme was to enhance economic development in rural areas by promoting non-agricultural entrepreneurship, improving infrastructure and perfecting rural landscape for the need of entrepreneurial activity; observing the environmental protection requirements, providing the economically active population with financial support for starting and developing non-agricultural entrepreneurship in rural areas, thus facilitating employment and increasing income, as well as facilitating initiative and activity of rural population. Table 2 shows the planned allocation of NEDLP financial resources and the actual progress during implementation of the programme in 2003-2009.

Table 2**Allocation of NEDLP funds by programme administrators in 2003-2009 (lats)⁶**

Project administrated by	Planned funds	Actual funds
The Mortgage Bank:	5 000 000	3 950 000
for increase of core capital (granting of loans)	2 200 000	2 200 000
for providing with grants	2 800 000	1 750 000
for Rural Development Fund (credit guarantees)	1 400 000	875 000
for Rural Support Service (consulting support)	600 000	375 000
Total	7 000 000	5 200 000

NEDLP loans were granted to projects representing such industries as (except for steel industry and manufacturing of artificial fibre), consumer, tourism, recreational and other services, construction, craft, computer (software and hardware) industry, aquaculture and hunting.

The Mortgage Bank received 321 applications for NEDLP loans and grants, loans covering the sum of LVL 4,685 million, grants – LVL 2,338 million. 254 NEDLP loans and grants were allocated. Total granted loans amounted to LVL 3,958 million, allocated grants – LVL 1,758 million. Figure 3 reflects amount of the claimed and granted loans in regions of Latvia.

⁶ Nelauksaimnieciskās uzņēmējdarbības attīstības programma (2002).-Rīga LR Zemkopības ministrija

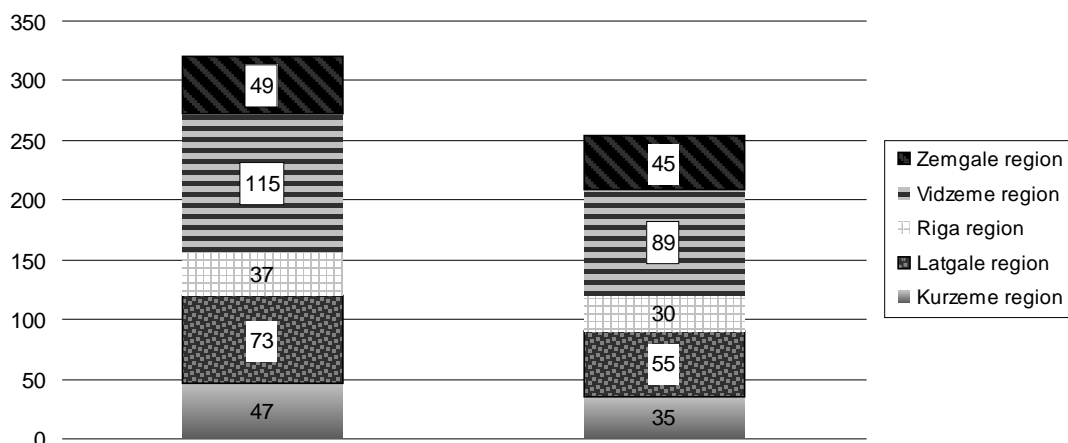


Figure 3. Number of the claimed and granted NEDLP loans and grants⁷

79% of the claimed loans in number were granted during the implementation of NEDLP programme in general, but in Latgale – 75%; in amount – 85% of the claimed in general, but 87% - in Latgale; the allocated grants – 75% of the claimed in general, but 72% - in Latgale. One of the major reasons for refusing loans and grants was insufficient economic grounding for projects.

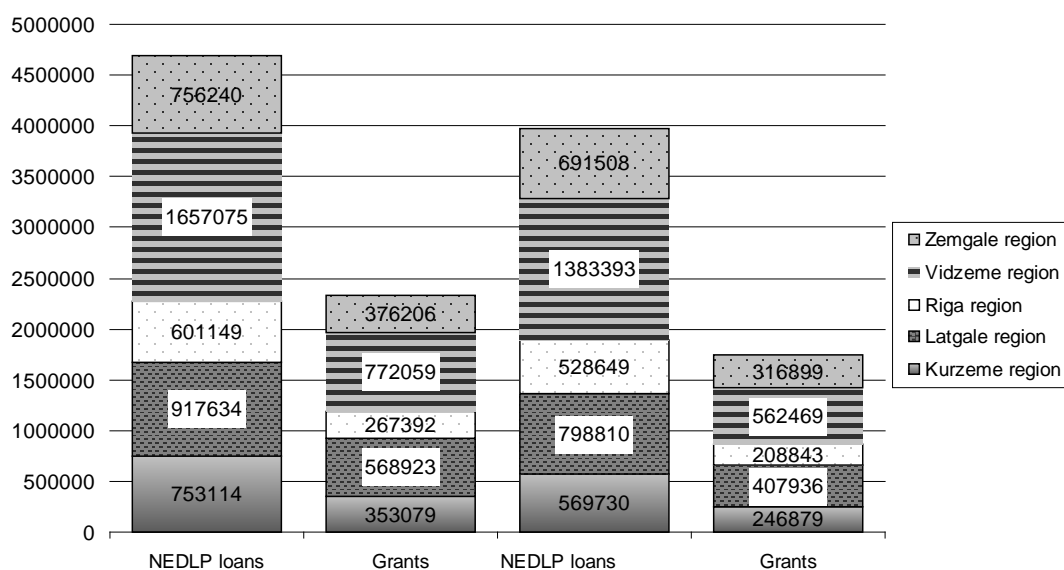


Figure 4. Amount of the claimed and granted NEDLP loans and grants (lats)⁸

⁷ Nelauksaimnieciskās uzņēmējdarbības attīstības programma (2002).-Rīga LR Zemkopības ministrija

⁸ Nelauksaimnieciskās uzņēmējdarbības attīstības programma (2002).-Rīga LR Zemkopības ministrija

The average loan applied for under the NEDLP programme was LVL 14 600, the average granted loan – LVL 15 640. The average grant applied for was LVL 7 280, the average allocated grant – LVL 6 860. Main reasons for not meeting the demands of all the potential NEDLP borrowers were the following:

- 1) Limited funding for state aid payments. The state had assigned LVL 1,75 million for grants, and these appropriations were put to use in a short period of time;
- 2) Totally, 28 NEDLP applications or 8,7% of all the submitted applications were turned down by the Credit committee of the Mortgage Bank. The reason for rejection, in most cases, was mentioned insufficient viability of the project or ineligibility to NEDLP programme requirements;
- 3) The project did not meet the requirements of the Environmental Protection Service (*Vides aizsardzības dienests*);
- 4) During implementation of the programme enterprises ceased claiming for the funding because of starting-up other businesses.

The projects submitted under the programme stood for wide scope of sectors representing non-agricultural entrepreneurship– see Figure 5.

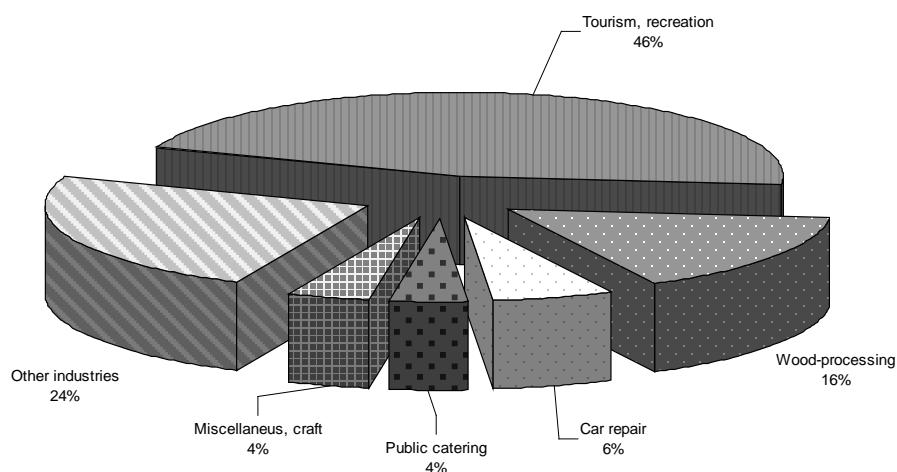


Figure 5. Structure of implemented NEDLP projects by sectors⁹

Almost half of the implemented projects related to rural tourism, the other most significant sector was wood-processing. Other sectors made up 24 per cent of the NEDLP

⁹ VAS „Latvijas Hipotēku un zemes banka” npublicētie materiāli.

structure. Those obtaining NEDLP funding had to submit reports to the Mortgage Bank on their economic activity during next 5 years. The Mortgage Bank employees carried out a regular supervision of the enterprises. Up to January 2009, 230 or 90,55% of the enterprises had met all the requirements and were successfully operating in their selected sectors.

In 2005, the Promotional programmes office ALTUM, a structural unit of the Mortgage Bank, was established. The mission of it was to develop competitive economy, by expanding the scope of financial support opportunities to definite groups of entrepreneurs or population according to the Government-established priorities. ALTUM gives credits to entrepreneurs and provides support of other types under national and European Union promotional programmes. ALTUM was established in order to separate in the Mortgage Bank, according to the EU Commission requirements, the state support functions from the traditional banking services, offered also by other commercial banks of Latvia. Separation of support functions and employees into a separate structural unit ensures that the state support shall not be used for financing commercial activities of the bank. The primary product of ALTUM is subprime loans to projects of good survivability and development prospective, which are not financed by commercial banks due to insufficient mortgage collateral and other project risks. Moreover, commissioned by the Government, ALTUM also implements other promotional programmes, including training and consulting programme for business start-ups and housing guarantees programme.

Rural areas and provincial towns of Latvia where paid-employment opportunity is very limited, require programmes helping people to arrive at a decision to start business and become employers themselves. Potential businessmen need better understanding of market processes, tendency and structure changes, requirements for starting and managing business. Since potential businessmen lack sufficient working capital to cover the expenses of training and consultation on business-essential issues, for instance, on drafting a business plan, completing a credit-application, keeping to accountancy and audit standards, applying of various mechanisms for financing a business, e.g. risk capital and others, there is a considerable amount of abortive attempts to start-up a business among them.

To overcome these obstacles and promote starting of successful commercial activity and self-employment, entrepreneurs need external, determined and proficient help, which is of primary importance during the initial stage of commencing commercial activity or self-employment. Since the training and consultation expenses are relatively high, it is preferable to help to cover these costs. Likewise, the availability of funding for business start-ups and self-employment should be ensured.

In 2006, the national programme “Training, consultations and financial support to business or self-employment start-ups” under the European Social Fund (ESF) was approved, and the Mortgage Bank was chosen a responsible institution for implementing this programme. The purpose of the national programme was to boost economic activities in the country and to raise the employment level. The programme was foreseen to support commencing of a business and it comprised four components:

- 1) trainings;
- 2) loans;
- 3) grants;
- 4) consultations.

Promotional programmes office ALTUM (structural unit of the Mortgage Bank) implemented this project. The specific objective of it was to promote self-employment and increase the number of commercial companies by providing them with training and consultation services, as well as funding in the shape of business start-up loans and grants. The implementation of project was to result in developing of skills and knowledge necessary for commencing a business, establishing of new commercial entities, enhancing of self-employment and, accordingly, boosting the economic growth of separate regions and the country in general.

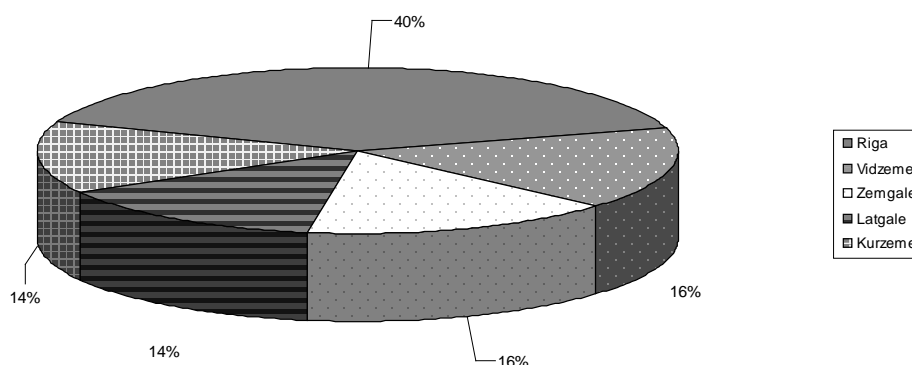


Figure 6. Projects by regions (%) implemented under the training programme¹⁰

Training took place for 50 groups of 20 towns of Latvia in 2006-2008. 998 interested people (there was 1000 planned) were trained in business basics. Training was organized for all regions of Latvia, and it took place both during working hours and beyond them. Consultations during the initial stage of the entrepreneurial activity were also provided.

¹⁰ Mums izdevās. Hipotēku bankas Mārketinga departamenta izdevums, Rīga, 2009,27 lpp

The training, in the context of project, was organized according to regional principle (to cover all 5 planning regions of Latvia), to involve Latvian population in other activities as much as possible.

In conclusion of training, the participants had to draft a business plan for their own business, and these business plan projects were submitted to Promotional programmes office for reviewing. The Mortgage Bank received almost 600 business plans. Most of them – 40% in Riga, 16% in Vidzeme and Zemgale each, 14% in Kurzeme and Latgale each (see Figure 6).

Table 3

"Training, consultations and financial support to business or self-employment start-ups", programme results on January 1, 2009¹¹

Type of support	Max amount, LVL	Average amount, LVL	Number of people	Sum, LVL
Grant for commencing a business	2215	2070	296	612 669
Maintenance grant	3700	3700	327	1 209 900
Grant for covering consultancy service expenses	2125	2089	325	679 053
Start-up loans	50 000	17855	327	5 838 520

According to Table 3, almost maximum use was made of the grant for commencing a business – LVL 2020 per 1 enterprise. Average amount of a start-up loan was LVL 17850, i.e. the implemented projects proved to be relatively small.

Skills and knowledge, essential for commencing commercial activity, were acquired and developed during this project; new commercial companies were established as well to enhance the growth of national economy. Those participants who did not establish their own enterprises under the project would also apply their newly acquired competence for starting entrepreneurial activity in future. The established enterprises, on their turn, would develop and grow, increasing the number of work places and turnover.

Specific role is played by the Loan Fund amounting to LVL 5,838 million, which has been set up as a part of the project. The EC Regulation No 448/2004 of 10 March 2004 and

¹¹ ALTUM pārvaldes nepublicētie materiāli.

the Implementation agreement concluded between the Ministry of Economics and the Mortgage Bank under the project state that the operating of the Fund is compulsory until year 2016. The loaned and repaid financial resources will be used only to support small and middle enterprises. Thus, the ESF resources will continue to help the target audience beyond the project¹².

There are a considerable amount of small and middle enterprises in Latvia that require funding, the lending resources, however, are not available in necessary amount due to various conditions. One of the aspects is lack of sufficient experience, funding and credit history of enterprises. Between March, 2006 and October, 2008 „Business start-ups lending programme” was implemented by ALTUM office of the Mortgage Bank. Loans were granted to people starting a business within the framework of the project „Development of Business Commencement Lending System” under the national programme approved by Managing Committee of the European Regional Development Fund (ERDF) in 2005. The programme’s purpose was to grant financial aid to enterprises, the funding being provided by the Government of Latvia, ERDF and the Mortgage Bank. The planned budget reached LVL 21,57 million, but, because of the intense initial activity, the budget was increased up to LVL 24,57 million.

Table 4

Loans granted under the Business Commencement Lending Programme before October 31, 2008¹³

Amount of loan, LVL	Number of projects	% of total	Sum of loan, LVL	Sum of loan, %
1 000- 17 500	112	38,5	1 072 724	4,7
17 501- 50 000	59	20,3	1 819 131	8,0
50 001- 100 000	53	18,2	3 734 365	16,4
100 001- 500 000	62	21,3	12 961 510	56,9
500 001- 700000	5	1,7	3 174 361	14,0
Total	291	100	22 762 093	100

More than every third granted loan (see Table 4), according to the number of projects, was micro-credit – up to LVL 17,5 thsd. However, by percentage, micro-credits in financial terms formed only incomplete 5% of the total amount of granted loans. Most of all - 57% of

¹²http://ec.europa.eu/regional_policy/sources/docoffic/official/regulation/content/lv/02_pdf/00_9_4_expend2_lv.pdf

¹³ ALTUM pārvaldes nepublicētie materiāli.

the granted loans in financial terms fit in the loan category of LVL 100 - 500 thsd. (in total - 62 loans of this kind). In particular cases the sum of granted loans was the maximum allowed or close to it – altogether 5 loans amounting to LVL 500 - 700 thsd. The number and amount of granted loans proved that the target audience of the programme was small enterprises.

Table 5

Description of granted loans by regions of Latvia before October 31, 2008¹⁴

Planning region	Number of projects	%	Sum of the loan, LVL	%	Average sum of the loan, LVL
Riga	127	43,6	10 851 212	47,7	85 466
Vidzeme	57	19,6	2 964 221	13,0	52 004
Kurzeme	30	10,3	2 899 248	12,7	96 642
Zemgale	38	13,1	2 864 500	12,6	75 382
Latgale	39	13,4	3 182 913	14,0	81 613
Total	291	100	22 762 094	100	78 220

A marked leader, according to the number and amount of granted loans, was Riga Planning Region (see Table 5). The indexes of other regions were comparatively similar; only in Vidzeme region the average loan, with a relatively high number of projects, was LVL 52 thsd., i.e. less than on average in the country. The average loan was the largest in Kurzeme region – LVL 97 thsd. These facts are regular, since most of enterprises are situated in Riga region, from the aspect of regional development, though, entrepreneurship should be promoted more in other regions of Latvia.

It was planned to create 1377 new working places by granting 291 loans to start-up projects. Among all planning regions, the largest number of working places – 623 was to be created in Riga region, then Latgale (271 work places), Kurzeme (208), Vidzeme (150), Zemgale (125). See Figure 7 for percentage of working places.

¹⁴ Mums izdevās. Hipotēku bankas Mārketinga departamenta izdevums, Rīga, 2009, 5.lpp

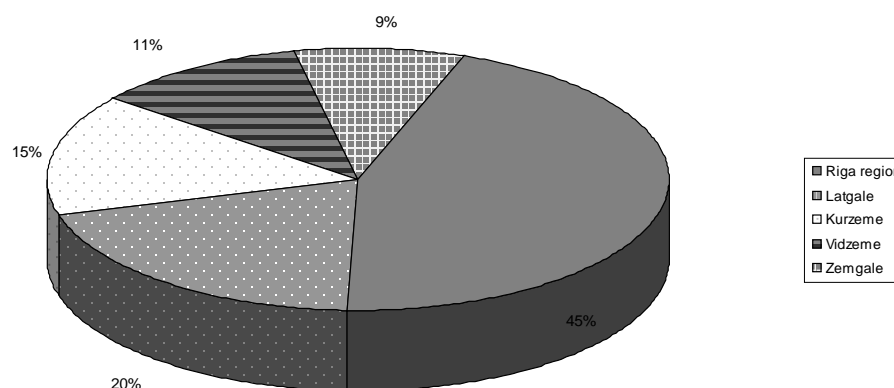


Figure 7. Creation of working places (%) by regions under Business Commencement Lending Programme¹⁵

Most of working places were to be created in manufacturing industry – 545, wholesale trade and retail trade – 262, lodging and catering services – 189, construction – 104.

The implementation of the programme has concluded at the moment (January 2010), but, according to the programme requirements, lending will continue using the repaid-loans resources. Since the borrowers repay loans gradually, the repaid resources are enough for ALTUM to continue crediting in limited amount.

A lending requirement to be met by an enterprise to obtain loans from banks is holding of sufficient collateral, which may be fixed assets, movable property, corporal provisions, debts of debtors, shares etc. The enterprise owners' private pledge is also accepted as collateral. However, there are enterprises lacking it and organizations providing loan guarantees play significant role in solving these problems. In Latvia such organizations are state owned Limited Liability companies „Rural Development Fund” and “Latvian Guarantee agency”.

Rural Development Fund (RDF) was established on October 18, 1994 with the initial aim of granting short-term and long-term loans to rural entrepreneurs. Currently Rural Development Fund issues credit guarantees to rural entrepreneurs for Latvian banks, thus

¹⁵ Mums izdevās. Hipotēku bankas Mārketinga departamenta izdevums, Rīga, 2009. 5.lpp.

facilitating attraction of investment to modernization and raising the effectiveness of the farms¹⁶.

The borrowers actively use the RDF issued guarantees. In 2004-2008, the RDF had issued guarantees to 1233 enterprises, i.e. in 2004 – 427; in 2005 – 337; in 2006 – 205; in 2007 – 135 and in 2008 – 127.

The guarantees issued by the RDF are a solid support to small and middle enterprises for implementation of their projects in rural territories. Banks are active to seize the opportunity of using RDF guarantee as additional collateral. In the result, both entrepreneurs and municipalities where the economic activity takes place become beneficiaries.

Latvian Guarantee agency (LGA) is a state owned Limited Liability company where holder of state shares is Ministry of Economics of Republic of Latvia. Since 2003 LGA enacts tasks defined by state economic policy and backs businesses to attract new investments for further expansion. LGA provides a mechanism how the entrepreneurs can get financial support for innovative business ideas by receiving credit or leasing in commercial banks with the collateral guarantee.¹⁷.

The aim of the guarantee is to assist an entrepreneur in receiving loan resources for commencing commercial activity in case of insufficient own collateral.

Since August 23, 2005 functioned two the state aid programmes „Latvian Guarantee Agency Ltd. State Aid Guarantee Programme” and the national programme under European Union Structural Funds „Development of Guarantee System”, aimed at offering loan and leasing guarantees to entrepreneurs in situations when their own collateral is insufficient for obtaining the necessary loan resources. Closed on December 31, 2008, the programme had issued 359 guarantees amounting to LVL 34,3 million. The issued guarantees provided 275 enterprises with availability of loan resources amounting to LVL 62,9 million.

¹⁶ <http://www.zm.gov.lv>

¹⁷ <http://www.lga.lv>

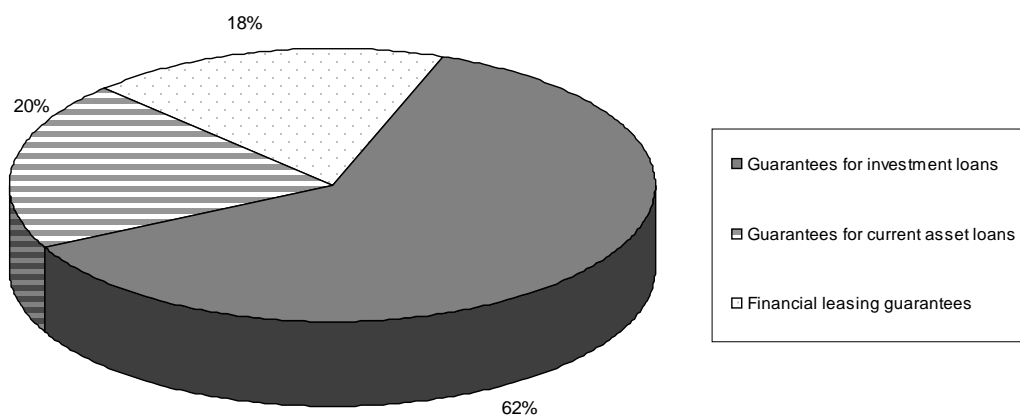


Figure 8. Guarantees issued by the LGA in 2005- 2008 by types of loans¹⁸

Investment loans made up the most part – 62% of the issued loans, 20% were current asset loans and 18% - financial leasing. Since enterprises were active to take the opportunity offered by the LGA to obtain guarantees for investment loans, the guarantee demand grew rapidly in 2008 and reached LVL 20,6 million. In comparison to 2007, the increase was 87%. The most rapid growth by guarantee products was related to guarantees for investment loans. JSC Hansabank (currently JSC Swedbank) was the most active to use guarantee products under the national programme - 23 % of total issued guarantees portfolio. The second most active credit institution was State JSC „Mortgage and Land Bank of Latvia” - 20%, the third was JSC „SEB bank” - 13%¹⁹.

New regulation „On Guarantees for Raising Competitive Capacity of Entrepreneurs” came into effect on March 24, 2009, and under this regulation, the LGA proceeded to issue the programme „Raising Competitive Capacity of Entrepreneurs” guarantees. Support will be provided until December 31, 2010. The total amount of guarantees is forecast EUR 100 million²⁰.

High entrepreneurial efficiency is one of the main conditions for economic advancement of a country. Increased competition, on the side of supply, among manufacturers or service providers makes every enterprise to improve its competitiveness and contribute to improvement of competitive capacity of a country. To ensure further sustainable development

¹⁸ <http://www.lga.lv>

¹⁹ <http://www.lga.lv>

²⁰ http://www.lga.lv/fileadmin/faili/Garantijas_pec_2009/MK_noteikumi.doc

of economy of Latvia and continuous growth of its competitive capacity, pre-conditions for transition from model of employing low-qualification labour force and manufacturing low added value products to innovative (knowledge-based) development growth model need to be favoured. The present economic situation with sharp drop of GDP and increase of unemployment level requires implementation of state aid programmes for enhancement of funding availability to SMEs. Entrepreneurship support measures include lending instruments, guarantees by Latvian Guarantee Agency, state guarantees, risk capital and technology transfer instruments.²¹

The programme „Support to Self-employment and Business Start-ups” was launched in August, 2009. It is co-financed by ESF and will close on June 30, 2013.

The purpose of the programme is to boost economic activities in the country by developing knowledge and skills of business start-ups and providing required financial support to commencing of business. Population of giving age, wishing to start-up a business or self-employment, including a newly established business, and registered in the commercial register not earlier than one year before submitting application are eligible to support from this programme. In line with the approved regulation, the programme is implemented by the Mortgage Bank. The total resources of the programme amount to LVL 23 million, including ESF and the state budget funding – LVL 14 million, the Mortgage Bank co-financing – LVL 9 million. In the context of programme funding LVL 17,5 million are planned for loans, LVL 4 million for grants, trainings and consultations, but LVL 1,5 million to cover administration and management costs.²²

Conclusions and suggestions

The author, as a result of the research, has come to the conclusion that:

- 1) State aid lending programmes help entrepreneurship to develop in rural areas of Latvia and increase the number of small and middle enterprises, and creates new work places;
- 2) The Mortgage Bank, the only fully state-owned bank, is assigned an important part in implementation of SME support programmes. The Mortgage Bank was the first to implement state aid programme, in the context of which SME obtained state support in the shape of grants – NEDLP.

²¹ <http://www.em.gov.lv>

²² <http://www.em.gov.lv>

- 3) NEDLP supported 254 rural enterprises contributing to national economy of Latvia by creating new work places in 2003- 2009. Most of the projects supported by NEDLP were rural tourism projects – 46%, the second most supported sector was wood-processing – 24%.
- 4) ALTUM office of the Mortgage Bank functions as an institution providing support to SME the primary product of ALTUM being subprime loans to projects of good survivability and development prospective, which are not financed by commercial banks due to insufficient mortgage collateral and other project risks. Moreover, commissioned by the Government, ALTUM also implements other promotional programmes, including training and consulting programme for business start-ups and housing guarantees programme.
- 5) The lending programmes funded by the state budget, ESF and ERDF and implemented before 2009 have reached their target-audience – SME. Business start-up lending programme has provided support to 291 entrepreneurs, created 1377 work places.
- 6) ALTUM programmes have mainly been implemented in Riga and Riga region. Training, consultation and financial support for business and self-employment start-ups comprise 40% of the total amount of the programme, but lending programme to people commencing commercial activities – 43,6%.
- 7) RDF guarantees are sound support to small and middle enterprises while implementing their projects in rural areas. Banks actively use RDF guarantees as additional collateral. Beneficiaries, in the result, are both entrepreneurs and municipalities in which the economic activity takes place.
- 8) Enterprises in Latvia have an opportunity to obtain LGA guarantees as additional collateral in case of being granted a loan.
- 9) The Mortgage Bank continues to implement 2 lending programmes funded by the state and the European Union. Loans for improving competitive capacity of enterprises were intended to amount to LVL 210 million. Total funding for support of self-employment and business start-ups – LVL 23 million.

To further encourage population to turn to entrepreneurial activity and support operating commercial companies, the author suggests:

- 1) to set up a system, functioning on a regular basis, for supporting of SME lending in Latvia. The system should comprise 4 components: training, consultations, grants, loans and should be funded by both – state budget and banks. The state should provide training and obtaining of grants; the amount of a grant should cover the expenses of establishing

an enterprise and fixed capital. Population commencing entrepreneurial activity with economically feasible business plans should have access to small loans – up to LVL 10 000 to start implementing their ideas.

2) The NEDLP experience should be applied for developing new state aid programmes. Those entrepreneurs wishing to carry out their economic activity in specially supported areas and diminishing economic imbalance between rural areas and Riga, should receive programme funding. These programmes should not require entrepreneurs' own financing for the projects (at the moment entrepreneurs' own financing is set 10-20% in all state aid programmes); that would help young people to implement their business ideas, since the youth have innovative ways of thinking and energy, but no financial resources for commencing their own business.

3) Micro credit movement, having had good start with support of the Ministry of Agriculture and continuation with different projects implemented by non-governmental organizations, should be promoted.

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